

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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In the matter of the application of :

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

2011-cv-5988 (WHP)

 Petitioners, :

 -against- :

WALNUT PLACE LLC *et al.*, :

 Intervenor-Respondents. :

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**INSTITUTIONAL INVESTORS’ STATEMENT IN SUPPORT OF SETTLEMENT AND
CONSOLIDATED RESPONSE TO SETTLEMENT OBJECTIONS**

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TO THE HONORABLE WILLIAM PAULEY III:

This brief in support of the settlement, and in consolidated response to the various settlement objections discussed below, is filed by BlackRock Financial Management Inc., Kore Advisors, L.P., Maiden Lane, LLC, Maiden Lane II, LLC, Maiden Lane III, LLC, Metropolitan Life Insurance Company, Trust Company of the West and affiliated companies controlled by The TCW Group, Inc., Neuberger Berman Europe Limited, Pacific Investment Management Company LLC, Goldman Sachs Asset Management, L.P., as adviser to its funds and accounts, Teachers Insurance and Annuity Association of America, Invesco Advisers, Inc., Thrivent Financial for Lutherans, Landesbank Baden-Wuerttemberg, LBBW Asset Management (Ireland) plc, Dublin, ING Bank fsb, ING Capital LLC, ING Investment Management LLC, New York Life Investment Management LLC, as investment manager, Nationwide Mutual Insurance Company and its affiliated companies, AEGON USA Investment Management LLC, authorized signatory for Transamerica Life Insurance Company, AEGON Financial Assurance Ireland Limited, Transamerica Life International (Bermuda) Ltd., Monumental Life Insurance Company, Transamerica Advisors Life Insurance Company, AEGON Global Institutional Markets, plc, LIICA Re II, Inc., Pine Falls Re, Inc., Transamerica Financial Life Insurance Company, Stonebridge Life Insurance Company, and Western Reserve Life Assurance Co. of Ohio, Federal Home Loan Bank of Atlanta, Bayerische Landesbank, Prudential Investment Management, Inc., and Western Asset Management Company (collectively, the “Institutional Investors”).

The Institutional Investors support the Trustee’s application to settle repurchase and servicing claims for 530 Countrywide RMBS Trusts (“Trusts”). The Trustee’s decision to settle the claims was reasonable. The settlement is highly beneficial to the Trusts and to the investors in their securities. There is likely no litigation alternative for 341 Trusts at issue in the

settlement, so they will get nothing if the settlement is not approved. For all Trusts, the \$8.5 billion settlement obtains a final resolution with Bank of America, and thus protects them from the risks of a Countrywide bankruptcy. The comprehensive servicing improvements, which will cost Bank of America \$400 million but may spare investors billions of dollars of losses, could not be obtained through contested litigation. The same is true of the defective document indemnity, under which Bank of America has agreed to indemnify the Trusts against 100% of the losses they suffer if the Trusts are unable to liquidate a loan due to unrecorded or incomplete mortgage or title policies.

The overwhelming majority of the thousands of investors who hold Trust securities have chosen *not* to contest the settlement.¹ The interests of this “silent majority” of Certificateholders—none of whom opposes the settlement—should not be ignored. They prefer settlement over: a) litigation to contest the settlement, or b) pursuing litigation of the Trustee’s claims themselves. The interests of these investors, who prefer certainty over *any* form of litigation, are not served by disapproving the settlement.

The 44 objectors in this proceeding are not monolithic in opposition to the settlement. Half of the objectors express *no opposition* to the settlement. Instead, as authorized by Justice Kapnick’s order below, they appeared simply to seek additional information concerning one or more of its terms.² The remaining objectors fall into four categories: a) financial guaranty and monoline insurers who seek only to clarify their rights under the settlement, b) waterfall objections that, necessarily, assume the settlement *will* be approved but seek clarification

¹ The settlement has been widely publicized and was the subject of a world-wide, months long notice program implemented by order of Justice Kapnick in the Supreme Court of New York.

² A chart listing the objections may be found at the beginning of Part III, *infra*.

concerning its distribution, c) objectors who are *litigating* their own, separate claims against BNY Mellon or Bank of America (“Litigation Claimants”), and d) miscellaneous objectors.

Given the requirement that Certificateholders act for the “common benefit” of the Trusts and their Certificateholders, the Litigation Claimants’ objections must be scrutinized carefully to ensure they comply with PSA Section 10.08 and are not a prohibited “individual course of action,” *Batchelder v. Council Grove Water Co.*, 131 N.Y. 42, 46 (1982), that seeks to advance “individual and conflicting pecuniary interests.” *In re Innkeepers USA Trust*, 448 B.R. 131, 144 (Bkcty. S.D.N.Y. 2011). These Litigation Claimants offer only speculation and innuendo in opposing the settlement. Of this group, only one objector, Walnut Place, even proposes to litigate the Trustee’s claims. Walnut’s proposal covers at most three Trusts. It rests on the assumption that an anonymous LLC, formed for the purpose of litigating claims, has the financial wherewithal and staying power to obtain a better result through litigation than the excellent result the Trustee has already obtained through settlement, and it is devoid of any analysis as to whether or how that could be achieved. An anonymous hedge fund’s desire to speculate with the Trustee’s claims in this way does not portend any result, much less a better one, than the highly favorable resolution embodied in the Trustee’s settlement.

The Trustee’s decision to seek court approval through an Article 77 proceeding, which ensured all Certificateholders could and would be heard, is a well and firmly embodied procedure that appears in decades of federal and New York case law, New York statutory law, and the RESTATEMENT (SECOND) OF TRUSTS. The settlement should be approved and the objections to it should be overruled.

I. Overview of the Issues

1. The Trusts exist pursuant to Pooling and Servicing Agreements (PSAs). The PSAs govern the rights and obligations of the Trustee, Certificateholders and the Mortgage

Sellers.³ Under the PSAs, the contract claims resolved in the settlement belong to the Trustee. *See* PSA §§ 2.01(b), 2.04. The Trustee holds those contract claims for the ultimate benefit of the Certificateholders, but the claims do not belong to Certificateholders. The Trustee has the power to pursue the claims, *see* PSA §§ 2.03(c), 2.04, and 3.03⁴; but it is not required to investigate them, *see* PSA § 8.02(iv), or to expend its own funds to do so, *see* PSA § 8.02(vi). These provisions significantly limit the litigation options for the Trustee.

2. The circumstances in which Certificateholders can pursue these claims are also very narrow. The PSAs require Certificateholders to aggregate 25% of the Voting Rights, provide a financial indemnity to the Trustee, and give two consecutive sixty day notice periods. *See* PSA §§ 7.01, 8.01, 8.02 and 10.08; *see also Greenwich Fin. Servs. Distressed Mortg. Fund 3, LLC v. Countrywide Fin. Corp.*, No. 650474/2008, slip op. at 6-7 (Sup. Ct. N.Y. Oct. 7, 2010), attached as Ex. 1 to the Warner Declaration, filed herewith.⁵ Only then can Certificateholders file suit: but they must sue derivatively, on behalf of the Trusts, for the common benefit of Certificateholders. *See* Part II(A), *infra*.

3. The sole issue to be decided here is whether the Trustee's decision to settle the Trustee's claims was reasonable. The PSAs authorize the Trustee to settle disputed claims. *See* PSA §§ 2.01, 2.03(c), 2.04, and 3.03. The Trustee retained five experts to advise it concerning the settlement, so it could make an informed, independent decision whether to accept it. The

³ Unless otherwise indicated, capitalized terms are defined consistently with the PSAs.

⁴ *See also LaSalle Bank, N.A. v. Nomura Asset Capital Corp.*, 180 F.Supp.2d 465, 471 (S.D.N.Y. 2001) (“the plain meaning” of a conveyance of “all right, title, and interest in the mortgages to LaSalle as Trustee . . . ordinarily includes the power to bring suit to protect and maximize the value of the interest thereby granted.”) and *Asset Securitization Corp. v. Orix Capital Mkts., LLC*, 12 A.D.3d 215, 784 N.Y.S.2d 513, 14 (N.Y.A.D. 1st Dep’t. 2004) (under PSA, authority to sue “is committed solely to the trustee of the pooled loans”).

⁵ All subsequent references to Exhibits refer to Exhibits to the Warner Declaration.

Court has questioned whether the Trustee was entitled to rely on experts for this purpose. *See* Tr. of Sept. 1 Hearing at 27:3-5. The PSAs expressly permit the Trustee to do so. *See* PSA § 8.02(ii). In fact, the Trustee's good faith reliance on the opinion of these experts "shall be full and complete authorization and protection in any action taken or suffered or omitted by it hereunder." *Id.* The Second Circuit has recognized that, where an Indenture authorizes a trustee to rely on opinions of counsel, the *correctness* of the underlying opinion is irrelevant: "Nor is the Trustees' good faith put in question merely by virtue of the fact that the opinion relied upon may have been wrong; to so hold would eviscerate the opinion of counsel defense." *Cruden v. Bank of New York*, 957 F.2d 961, 972 (2d Cir. 1992). For this reason alone, the PSAs and applicable law require that the court approve the settlement. *See* Part II(C)(2), *infra*.

4. Even if the court could ignore the plain language of the PSAs, and it cannot, the settlement itself is reasonable. The \$8.5 billion settlement the Trustee asks the court to approve is the second-largest litigation settlement in history, and the largest ever achieved in private litigation. If approved, it will provide the Trusts with a favorable and early resolution of uncertain claims for repurchase of ineligible mortgages. It will substitute a solvent obligor, Bank of America, for the deeply insolvent Countrywide entities who are otherwise liable for the repurchase claims. It effects a complete reform of mortgage servicing, at Bank of America's expense, in a manner that is favorable not only to investors, but to borrowers. Finally, it provides the Trusts with a complete, and automatic, indemnity for losses they suffer as a result of unrecorded mortgages and defective and missing title policies.

5. There are 530 Trusts involved in the settlement. The Institutional Investors hold 25% of the Voting Rights in 189 of these Trusts. If the settlement is not approved, they can and will litigate claims for those Trusts, but they do not believe litigation would achieve a better—or

more certain—result than the settlement the Trustee has in hand. Though they are prepared to litigate, they prefer the settlement. There are 341 other Trusts involved in the settlement. In all but two of those 341 Trusts, no group alleges that they hold 25% of the Voting Rights. In fact, of the over \$40 billion in securities held by the Institutional Investors or by funds and clients they advise, almost \$14 billion are in Trusts where the Institutional Investors lack the required 25% threshold. If the settlement is disapproved, these Trusts will receive no remedy at all. *See* Part II(F), *infra*. Rejection of the settlement would be devastating for these Trusts and their investors. The Court should press the objectors carefully to determine whether they have any plan, at all, to obtain relief for these Trusts if the settlement is disapproved.

6. If the settlement is rejected, the industry-reforming servicing improvements and the document indemnity will also be lost for all of the Trusts. These are affirmative, negotiated remedies. They are not mandated by the PSAs, so they cannot be achieved through contested litigation of prudent servicing claims. Destroying the settlement, and thus the servicing improvements, could cause investors to suffer billions of dollars of additional losses they will likely avoid if the settlement is approved. Borrowers will be hurt too, because the servicing improvements—which provide important protections and incentives for them—will not be implemented fully.

7. Evaluation of any settlement necessarily requires consideration not only of the terms of the proposed settlement but an estimate of the likely outcome of a litigated alternative. It is a truism, and also true, that litigation is inherently uncertain. The inaccurate assertion that there are “billions of dollars in toxic mortgage claims” in the pools does not establish that those claims will succeed if pursued in litigation. Speculative claims that Bank of America is liable as a successor in interest for contracts with the Countrywide Mortgage Sellers do little to assure

investors that years of contested litigation will not end with only an insolvent Countrywide to respond to their claims. The raw assertion that the Trustee's claims "*may* exceed \$150 billion" similarly fails to grapple with the barriers to these claims imposed by the governing agreements. Also left unaddressed are the legal rulings and risks that might render these claims worthless, or at a minimum worth *far* less than the settlement the Trustee has actually achieved.

8. The Institutional Investors are 22 of the world's largest and most reputable investors. They have appeared here to support the settlement because they believe it is reasonable. Their open support for the settlement, and their disclosed efforts to achieve it, were well known to the market and to investors in the Trusts' securities. As the Court has observed, the group grew over time because other investors observed what was happening, believed the Institutional Investors' litigation strategy had merit and wanted to be part of achieving the solution. We submit that the Institutional Investors' group grew for another reason: the market knew these were institutions of sterling reputation. It knew they were not pursuing these claims to obtain an individual advantage: they simply wanted the deals to work, as they were envisioned, for the common benefit of all Certificateholders.

9. The Institutional Investors will receive the *same* benefit under the settlement that will flow to every other, similarly situated investor. None of them has offered to trade approval of this settlement for an individual advantage, whether in litigation or elsewhere. It remains to be seen whether the same is true of the objectors. The reasonableness of the settlement is also evident from another key fact: the vast majority of investors in securities issued by the Trusts, including institutions that hold billions of dollars of certificates, have chosen not to object to the settlement. The court must consider their interests, and those of the Institutional Investors who

want the substantial benefits and certainty conferred by the settlement, in assessing whether to approve the settlement.

10. In the following sections, we provide more detail concerning the reasonableness of the settlement, the feasibility of litigated alternatives, and specific responses to arguments made to date by the objectors. The Institutional Investors, like all other Certificateholders, reserve their right to supplement this brief in support as additional information is disclosed through discovery and litigation of the approval proceedings.

II. The Settlement is Reasonable Given the Terms of the Governing Agreements, the Result Achieved and the Potential Value of the Claims

A. Overview of Contract Provisions and Claims

11. By the summer of 2010, the situation faced by investors in the Trusts' securities had become dire. By virtually *every* measure, Bank of America's home loan servicing was *worse* than that of other firms in the industry. Defaults and delinquencies in the underlying pool of mortgages were mounting. Investors' losses were mounting too. Separately, monoline and private mortgage insurers had filed suit seeking to rescind their insurance coverage on certain Trusts, claiming that they contained high levels of mortgages that were originated in violation of applicable reps and warranties.⁶ Emails released by the Securities and Exchange Commission indicated that Countrywide had originated loans "through our channels with disregard for process [and] compliance with guidelines," even though it knew of a "serious lack of compliance within [its] origination system." *See* Complaint ¶ 49, *SEC v. Mozilo*, No. 09-cv-03994 (C.D.

⁶ "Rep and warranty" is the term used to describe the representations Mortgage Sellers make to the Trusts when they sell a mortgage. The violation of these representations and warranties gives rise to a right, on the part of the Trusts, to demand that the Seller repurchase the mortgage if the defect "materially and adversely affects the interests of Certificateholders in that Mortgage Loan." *See* PSA § 2.03(c).

Cal. June 4, 2009). Faced with mounting losses, a group of institutional investors began to organize to try to compel the Trustee to act.

12. The PSAs *prohibit* Certificateholders from enforcing the Trusts' contracts individually. Instead, they must do so *collectively*, for the good of *all* Certificateholders. *See* PSA § 10.08 (“no one or more Holders of the Certificates shall have any right in any manner whatever . . . to enforce any right under this Agreement, except in the manner provided in this Agreement and for the common benefit of all Certificateholders”). Certificateholders who seek to pursue claims derivatively for the Trusts must also meet a number of technical conditions precedent:

- a. A prior notice of an Event of Default that must be issued by investors holding not less than 25% of the Voting Rights in the Trust. *See* PSA § 7.01;
- b. The Event of Default must remain uncured for a period of sixty days. *Id.*;
- c. The 25% holders must then demand that the Trustee file suit. *See* PSA § 10.08;
- d. The 25% holders must couple their demand with an offer to indemnify the Trustee against all costs and expenses associated with pursuing any investigation or claims. *Id.*; and,
- e. The Trustee must fail to file suit for a period of sixty days, after which any Certificateholder who participated in the Notice of Non-Performance and offered the required indemnity may file suit derivatively on behalf of the Trusts. *Id.*

13. These “no-action” clauses have been rigorously enforced by the courts. As the New York Supreme Court recently observed in enforcing *a substantively identical provision*, under this “broad language,” certificateholders “are barred from bringing [an] action” that does not strictly comply with the provision’s terms. *Greenwich Fin. Servs. Distressed Mortg. Fund 3, LLC*, No. 650474/2008, slip op. at 6-7, attached as Ex. 1. No-action clauses, like the one

contained in Section 10.08, ensure that “the *judgment* of the Trustee concerning whether to resort to the courts is controlling upon all of the bondholders.” *Campbell v. Hudson & Manhattan R.R. Co.*, 277 A.D. 731, 734 (N.Y. App. Div. 1951), *aff’d*, 302 N.Y. 902 (1951).⁷ These clauses “prevent[] individual bondholders from pursuing an individual course of action.” *Batchelder v. Council Grove Water Co.*, 131 N.Y. 42, 46 (1892). No-action clauses also “protect[] against the risk of strike suits,” and against the risk that “a single bondholder or a small group of bondholders . . . might otherwise bring a suit against the issuer that most bondholders would consider not to be in their collective economic interest.” *Feldbaum v. McCrory Corp.*, C.A. No. 11866, 1992 WL 119095, at *6 (Del. Ch. June 1, 1992) (applying New York law). As the New York Supreme Court held in *Greenwich*, certificateholders “agree[] to” the restrictions of a no-action clause “when they purchase[] the certificates.” Slip op. at 7. Courts applying New York law have repeatedly dismissed complaints on the basis of plaintiffs’ failure to comply with no-action clauses.⁸

⁷ Unless noted, all emphasis is added.

⁸ See, e.g., *Peak Partners, LP v. Republic Bank*, 191 F. App’x 118, 126-27 (3d Cir. 2006); *Bankers Ins. Co. v. DLJ Mortg. Capital, Inc.*, 2010 WL 4867533, at *2-*4 (M.D. Fla. Oct. 8, 2010); *Sterling Fed. Bank, F.S.B. v. DLJ Mortg. Capital, Inc.*, 2010 WL 3324705, at *3-*5 (N.D. Ill. Aug. 20, 2010); *Bank of N.Y. v. Battery Park City Auth.*, 251 A.D.2d 211 (1st Dep’t 1998); *Greene v. N.Y. United Hotels, Inc.*, 236 A.D. 647, 648 (1st Dep’t 1932), *aff’d*, 261 N.Y. 698 (1933); *Levy v. Paramount Publix Corp.*, 149 Misc. 129, 133-34 (Sup. Ct. N.Y. Co. 1933), *aff’d*, 241 A.D. 711 (1st Dep’t 1934), *aff’d*, 265 N.Y. 629 (1934); see also *Sutter v. Hudson Coal Co.*, 259 A.D. 1053 (2d Dep’t 1940) (denying plaintiff’s motion for summary judgment); *Schallitz v. Starrett Corp.*, 82 N.Y.S.2d 89, 91 (Sup. Ct. N.Y. Co. 1948) (directing judgment); *Relmar Holding Co. v. Paramount Publix Corp.*, 147 Misc. 824, 825 (Sup. Ct. N.Y. Co. 1932) (denying motion to strike defense), *aff’d*, 237 A.D. 870 (1st Dep’t 1933); *Van Wezel v. McCord Radiator & Mfg. Co.*, 20 N.Y.S.2d 91, 99-100 (N.Y. City Ct. 1939) (granting summary judgment); *McMahan & Co. v. Warehouse Entm’t, Inc.*, 859 F. Supp. 743, 748-79 (S.D.N.Y. 1994) (granting summary judgment), *rev’d in part on other grounds*, 65 F.3d 1044 (2d Cir. 1995); *Victor v. Riklis*, 1992 WL 122911, at *6 (S.D.N.Y. May 15, 1992) (denying leave to amend complaint). Cf. *Beal Sav. Bank v. Sommer*, 8 N.Y.3d 318, 332 (2007) (enforcing contractual provision restricting individual lenders from initiating separate, multiple lawsuits).

14. As a practical matter, no-action provisions *preclude* Certificateholders from pursuing claims on behalf of the Trusts unless they: a) aggregate large numbers of holders and holdings sufficient to satisfy the Voting Rights thresholds and b) prove they have the financial wherewithal to indemnify the Trustee and the Trusts for the expenses associated with lengthy and arduous litigation of servicing and repurchase claims.⁹ *Compare Cruden*, 957 F.2d at 968 (noting that a no-action provision meant that “debenture holders could not bring suit ‘upon or with respect to’ the Indenture” without first complying with requirements of the clause). This important limitation must be considered when the Court assesses whether a litigated alternative is even available for most of the Trusts.

15. The Court has pressed the Trustee to explain why it acted (or failed to act) as it did. The answer lies in the terms of the PSAs. The PSAs significantly limit the Trustee’s obligations to pursue these claims. The term “Trustee” is, in fact, something of a misnomer, at least as it describes BNY Mellon’s role under the PSAs.¹⁰ “The corporate trustee has very little in common with the ordinary trustee The trustee under a corporate indenture has his [or her] rights and duties defined, not by the fiduciary relationship, but exclusively by the terms of the agreement. His [or her] status is more that of a stakeholder than one of a trustee.” *AG Capital Funding Ptnrs., L.P. v. State Street Bank & Trust Co.*, 11 N.Y.3d 46, 896 N.E.2d 61, 866

⁹ With one exception, none of the objecting investors has expressed any willingness to provide the financial indemnity that must be offered before a Certificateholder can compel the Trustee to pursue these claims. The exception, however, is of dubious provenance: an indemnity has allegedly been offered by the anonymously named “Walnut Place LLC,” a hedge fund that has not disclosed its balance sheet. Given the typical lifespan of most hedge fund partnerships, and the fact that it was organized *solely* to pursue litigation claims, Walnut’s unstated resources offer the court (and other investors in the trusts for which it claims the right to act) no assurance that it has the financial wherewithal—or, indeed, the lifespan—to pursue these claims successfully through lengthy litigation.

¹⁰ This “art of the possible” problem is endemic in this case, and must be borne carefully in mind when considering the alternatives to settlement.

N.Y.S.2d 578, 583-84 (N.Y. 2008). Under the PSAs, the Trustee is not required to expend any of its own funds to pursue claims or perform its duties, *see* PSA § 8.02(vi); it is not required to assume any financial risk in the performance of its duties, *see id.*; it is not obligated to investigate any fact unless instructed to do so by the holders of 25% of the Voting Rights, *see id.* at § 8.02(iv); and, it is not under any “obligation to exercise any of the trusts, rights or powers vested in it by this Agreement or to institute, conduct or defend any litigation . . . at the request of the Certificateholders . . . unless such Certificateholders shall have offered to the Trustee reasonable security or indemnity satisfactory to the Trustee against the costs, expenses and liabilities which may be incurred.” *See id.* at §§ 8.02 and 10.08.

16. The Trustee was faced with competing demands from investors about what to do with the Trustee’s claims. The Institutional Investors hold (or advise clients and funds that hold) more than \$40 billion of outstanding securities issued by the Trusts. They believed the settlement was favorable. They wanted the Trustee to accept it. The Walnut Place objectors, in contrast, filed suit on February 23, 2011. *See* Walnut Place Objection, St. Doc. #28 at 2. That action, filed after repeated press releases by the Institutional Investors disclosed ongoing discussions with BNY Mellon and Bank of America, sought relief for only a single trust: CWALT Trust 2006-OA10, in which Walnut Place alleged to hold \$704 million of original face securities.¹¹ *See id.*; *see also* St. Doc. #24, #25, Ex. A, p. 1-2. The Institutional Investors had sizeable holdings in the same trust.¹²

¹¹ Given payments of principal, the outstanding amount of these securities was likely no more than \$500 million.

¹² In April 2011, Walnut Place filed an amended complaint to include an additional Trust, CWALT 2006-OA3, in which it alleged to hold \$110 million of original face securities, and alleged that it had begun to prepare a lawsuit on a third trust, CWALT 2006-OA21. *See* Walnut Place Objection, St. Doc #28 at 2; St. Docs. #24, #25, Ex. A, p. 1-2. The Institutional Investors

17. In the face of these conflicting demands, BNY Mellon *could have* simply settled the claims without seeking court approval. *See* PSA §§ 2.03, 2.04, 3.03; *Redmond v. Commerce Trust Co.*, 144 F.2d 140, 154-55 (8th Cir. 1944). It did not. Instead, BNY Mellon did precisely what the law and the PSAs permitted it to do: it made a judgment about whether the settlement benefitted the Trusts and should be accepted, then it filed suit asking the court to approve the settlement. When it filed suit, the Trustee’s pleading disclosed openly both the settlement and the competing demands of the Walnut Place Plaintiffs. *See* Memorandum of Law in Support of Trustee’s Original Petition, St. Doc. #12, at 13-14.

B. The Trustee’s Common Law Duties Do Not Offer Any Path to a Greater Recovery for the Trusts

18. The Trustee’s common law duty to avoid conflicts of interest does not offer any path to a greater recovery for the Trusts.¹³ Nor do those duties alter the reality that—in the absence of a settlement—claims on behalf of hundreds of Trusts likely will never be pursued.

19. A duty to avoid conflicts of interest cannot possibly be expanded to negate the PSAs’ clear statement that the Trustee is not required to expend its own funds to pursue claims or perform its duties. PSA § 8.02(vi). Even after an Event of Default, when “the indenture trustee’s obligations come more closely to resemble those of an ordinary fiduciary,” *Beck v. Manufacturers Hanover Trust Co.*, 218 A.D.2d 1, 12, 632 N.Y.S.2d 520, 527 (App. Div. 1st Dep’t. 1995), New York law is clear “that this by-now relatively minor change in the legal landscape, if change it is, does not render the indenture irrelevant.” *Id.* As the *Beck* court explained, the terms of the contract still govern and define the Trustee’s obligations post-default:

had holdings in all three of those Trusts. It is as yet unclear how many of Walnut Place’s securities were acquired *after* Walnut Place learned a settlement had been achieved; the Institutional Investors’ holdings predate the settlement.

¹³ *See* Part II(F), *infra*.

“The trustee must in the post-default context act prudently, *but only in the exercise of those rights and powers granted in the indenture*. The scope of the trustee’s obligation then is still circumscribed by the indenture, albeit less narrowly. The Trustee is *not required to act beyond his contractually conferred rights and powers*, but must, as prudence dictates, exercise those singularly conferred prerogatives in order to secure the basic purpose of any trust indenture, the repayment of the underlying obligation.” *Id.* (emphasis added).

20. Two principles thus emerge from *Beck* and the cases that apply it. First, in a post-default world, the Trustee is obligated to exercise those rights it has, prudently. Second, even in a post-default world, the Trustee is not required to act beyond its contractually conferred rights and powers. These principles matter. They have real consequences for the Trusts and their Certificateholders if the settlement is not approved. Under these agreements, the Trustee does not have—and will never have—an obligation to expend its own funds to pursue years of contentious and difficult litigation on behalf of the Trusts.¹⁴ PSA § 8.02(vi). The Trustee does not have, and will never have, an obligation to investigate facts to determine whether an Event of Default has occurred unless 25% of the Certificateholders instruct it to do so. *Id.* at §8.02(iv). Even after an Event of a Default, if the Certificateholders seek to compel the Trustee to take action, they must offer the Trustee an indemnity of the expenses it will incur to do so.¹⁵ Given

¹⁴ No reported case has held that either of the common law duties cited by the Court—the duty to avoid conflicts and the duty to perform ministerial actions competently—would impose on a Trustee the obligation to expend its own funds, in the absence of an indemnity, to pursue claims for a Trust.

¹⁵ *Id.* at §8.02(ix) (Trustee is “under no obligation to exercise any of the trusts, rights or powers vested in it by this Agreement or to institute, conduct or defend any litigation . . . at the request, order or direction of any of the Certificateholders, pursuant to the provisions of this Agreement, unless such Certificateholders shall have offered to the Trustee reasonable security or indemnity satisfactory to the Trustee against the costs, expenses and liabilities which may be incurred therein or thereby”).

the barriers imposed by these agreements, there is reason to question whether the Trustee would ever be obligated to pursue these claims in the future if the settlement were disapproved.

C. The Value and Reasonableness of the Settlement of the Repurchase Claims

21. The issue here is not whether the Trustee's decision to enter into the settlement was right; the issue is whether it was reasonable. *See In re Application of IBJ Schroder Bank & Trust Co.*, Index No. 101530/1998, at 6 (N.Y. Sup. Ct. N.Y. County Aug. 16, 2000) ("the trustee's decision to compromise the . . . action is within the scope of the trustee's powers, is reasonable and prudent, and is entitled to judicial deference"); *In re Stillman*, 107 Misc. 2d 102, 110 (Sur. Ct. N.Y. County 1980); *see also* RESTATEMENT (SECOND) OF TRUSTS § 187 (1959) ("Where discretion is conferred upon the trustee with respect to the exercise of a power, its exercise is not subject to control by the court, except to prevent an abuse by the trustee of his discretion."). As in any decision regarding a settlement, the Trustee was entitled to consider the relative costs, benefits and risks associated with the proposed settlement and with the litigation alternative. A critical set of risks and uncertainties concerns the Trusts' rights to demand the repurchase of ineligible mortgages held in their collateral pools.

1. The Terms that Govern the Repurchase Obligation

22. The Mortgage Sellers' obligation to repurchase defective mortgages is found in Section 2.03 of the PSAs. In pertinent part, it reads as follows:

"Upon discovery by any of the parties hereto of a breach of a representation or warranty with respect to a Mortgage Loan made . . . that materially and adversely affects the interests of the Certificateholders in that Mortgage Loan, the party discovering such breach shall give prompt notice thereof to the other parties. Each Seller hereby covenants that within 90 days of the earlier of its discovery or receipt of a written notice from any party of a breach of any representation or warranty with respect to a Mortgage Loan sold by it . . . shall cure such breach in all material respects, and if such breach is not so cured, shall . . . repurchase the affected Mortgage Loan . . . from the Trustee at the Purchase Price"

23. The “parties” to the agreement are Countrywide Home Loans, Inc. and various “Park” entities (Park Granada, Park Monaco, and/or Park Sienna, all of which were aggregation conduits for Countrywide). Countrywide Home Loans, Inc. is the Mortgage Seller obligated to repurchase defective loans. The other parties are the Depositor, Countrywide Home Loans Servicing, L.P. as Master Servicer, and BNY Mellon as Trustee. The Certificateholders are not parties to the agreements. They thus have no direct rights to demand the repurchase of defective Mortgage Loans. Repurchase claims, if they are pursued, must be pursued by the Trustee (or derivatively, for the common benefit of all Certificateholders, by Certificateholders who have met the conditions precedent).

24. Only the Mortgage Seller, Countrywide Home Loans, Inc., is obligated to repurchase defective mortgage loans. *See* PSA § 2.03(c). Countrywide Financial Corporation, the then-public parent company of Countrywide Home Loans has no obligation, under the PSAs, to repurchase defective mortgage loans. *Id.* It also made no representation or warranty concerning the credit quality or features of the underlying mortgage loans. *Id.* at § 2.03(a).

25. Bank of America, which at the time had no relationship at all with Countrywide, likewise is not a party to any of the PSAs. It therefore made no representation regarding the credit quality of the underlying mortgage loans. It also has no direct contractual obligation to repurchase defective Mortgage Loans. Instead, its sole liability—if it has any—is as the successor in interest to, or as a de facto merger party with, Countrywide Home Loans, Inc.

26. The PSAs require that a defective loan be cured or repurchased. Missing or defective loan documents, liens, endorsements and title policies can often be cured *without* triggering a repurchase obligation. This is authorized by the PSAs, *see* PSA § 2.03(c), and by

law.¹⁶ Thus, an allegedly “toxic” defective mortgage may remain in the pools if the Mortgage Seller can cure the identified defect. Where a defect cannot be cured, the Seller is required to repurchase “that Mortgage Loan” if the defect “materially and adversely affects the interests of the Certificateholders in that Mortgage Loan.” *Id.* The reference to “that Mortgage Loan” creates significant litigation uncertainties the Trustee was entitled to consider in deciding whether to settle the claims. Does this language require loan by loan litigation of thousands of individual loan files?¹⁷ If not, how is a defect as to “that Mortgage Loan” to be proved?¹⁸ The Trustee was also entitled to consider this likelihood of delay, if loan by loan litigation was

¹⁶ See, e.g., UCC §§ 3-203 (right of transferee for value to compel unqualified endorsement), 3-205 (permitting completion of blank endorsements), and 3-309 (permitting proof of existence of a missing note through a *valid* lost note affidavit). See also N.Y. UCC §§ 3-201, 3-204, and 3-804. All fifty states have enacted some version of the UCC. See *Veal v. Am. Home Mortg. Servicing, Inc. (In re Veal)*, 449 B.R. 542, 554 (B.A.P. 9th Cir. 2011). That a lawful cure is permitted does not mean that robo-signing a false document or affidavit is sufficient to constitute a cure. To the contrary, signing false documents or affidavits would be an independent breach of the prudent servicing obligation that exposes the Trusts to liability and additional risks of loss. See also Ex. 2, Bank of America Presentation Regarding Settlement with GSEs, entitled “Addressing Legacy Mortgage Issues,” at p. 4, n.4, Jan. 3, 2011 (noting that GSE claims included “approximately \$832 million of missing document claims in the process of being cured”).

¹⁷ Assuming there are 260 court days per year (52 weeks x 5 days a week) and eight hours of court time in each day, there are only 2,080 hours per year of court time available. There are at least 770,000 loans held as collateral by these Trusts. The Institutional Investors concluded that *at least* 30% of the loans were eligible for repurchase; the Trustee’s expert used a much lower, 14.4% defect rate. Even if one used the Trustee’s calculation, it would mean that 110,880 loans would be the likely subject of repurchase litigation. At a mere thirty minutes per loan, it would take a court—working full time on nothing but repurchase claims—26.6 years to process and decide all of these potential repurchase claims, without considering time for appeal. Even if the cases were spread among a number of courts, and shorter processing and longer trial days were assumed (neither of which is likely realistic), the litigation of these repurchase claims could easily drag on for more than a decade, if not longer.

¹⁸ While one court granted a motion in limine permitting a bond insurer to present sampling evidence on a fraud claim (but left open the question of whether such evidence would be sufficient proof of any element of the claim), we have found no case permitting a trustee to use sampling to demonstrate the breach of a representation or warranty in support of a repurchase claim for an individual mortgage loan or loans.

required, as well as the prospect that years of delay would significantly diminish the value of any ultimate litigation recovery.

27. A separate area of uncertainty surrounds the issue of “material adversity” and when and how it must be demonstrated. The Institutional Investors believe firmly that adversity need be demonstrated only at the time the loan is sold to the securitized trust. Bank of America, however, has made two arguments the Trustee could reasonably consider in assessing the likelihood that litigation would achieve a better result.¹⁹ The first argument concerns adversity: when, if ever, is a loan that is *performing* eligible for repurchase? The Institutional Investors have argued strenuously that performance is *not* a defense to repurchase claims. To cite one extreme example: if a Trust was represented to include loans that were only to prime borrowers, but some loans were made to subprime borrowers, the fact that the subprime borrowers were paying on their loans would not be sufficient to avoid a repurchase claim. This is the logical interpretation of the contract. It also vindicates the expectations of the investors and the contract parties at the time of the securitization.²⁰ There is, however, no reported case even considering whether a performing loan may properly be the subject of a repurchase demand; much less one that concludes a repurchase claim is valid. The second, more familiar argument, concerns “causation”; namely, the assertion that the Mortgage Sellers are not required to repurchase a Mortgage Loan unless the breach of the representation or warranty *caused* the loss that has been suffered on the loan. In this view, losses caused by macro-economic factors such as intervening

¹⁹ Regardless of whether the Trustee agreed with the merit of these arguments, the fact that Bank of America has made them previously in other cases was a clear indication that Bank of America might make them in any litigation of the Trustee’s repurchase claims. The Trustee therefore could reasonably consider the likelihood that it might succeed, or fail, in the argument that only initial adversity—at the time of the securitization—was required to prove a repurchase claim.

²⁰ Put bluntly, if this was not the intent, it is hard to understand why the structure would include a repurchase obligation for the breach of a representation or warranty.

declines in the housing market or the economy, or micro-economic factors such as a borrower's job loss, may be offered as evidence to negate a repurchase claim. The Institutional Investors reject this theory: the repurchase obligation exists because the Trusts are not supposed to be exposed to *any* risks associated with ineligible mortgages, and the mortgages simply aren't supposed to be in the Trusts. Having placed ineligible mortgages in the Trusts, the Sellers—not the Trusts—should bear all subsequent micro- or macro-economic risks associated with them. While the Institutional Investors believe logic and the contracts are firmly on their side in this matter, this too is an issue subject to dispute and uncertainty.²¹

2. Arguments that the Claims “May Exceed \$150 Billion” Ignore the Likelihood that they May Be Worth Far Less.

28. The Trustee faced substantial uncertainty concerning the size of potential repurchase claims. It therefore retained experts to advise it, both with regard to legal issues affecting the likelihood of success on the repurchase claims, and their potential size. The Court has questioned whether the Trustee was entitled to estimate the size of the potential claim in deciding to settle or to retain an expert to assist it in doing so. *See* Tr. of Sept. 1 Hearing, at 27:3-5. The Trustee's reliance on experts for this purpose is not only expressly permitted by the terms of the PSAs, *see* PSA § 8.02(ii), in most circumstances it is conclusive. *Id.* The Trustee's expert concluded the reasonable value of the repurchase claims was between \$8.8 billion and \$11 billion.²² *See* Report of Brian Lin at 7 (“[T]he settlement range of approximately \$8.8 to \$11

²¹ The Trustee retained an independent expert to advise it about these risks. *See* Report of Professor Barry E. Adler. While the Institutional Investors have a different view of this risk, this is an area in which the case law has not yet developed, so the value of a certain recovery that eliminates these risks is higher.

²² The Institutional Investors were not privy to the Trustee's expert reports before they were made public. While we disagree with some of the conclusions drawn by the Trustee's experts, the PSAs expressly permit the Trustee to rely on the opinions of experts in deciding whether to settle or prosecute these claims. *See* PSA § 8.02(ii) (“Except as otherwise provided in §8.01, . . .

billion is reasonable *without applying* any legal haircuts.”) (emphasis added).²³ Based on the data he reviewed, the Trustee’s expert concluded a breach rate of 36%, and a success rate of 40%, for an overall defect rate of 14%, was a reasonable basis on which to estimate the size of the potential repurchase exposure in the Trusts. *Id.* at 8. Those claims, of course, would then have to be proved successfully to yield a recovery.

the Trustee may consult with counsel, financial advisers or accountants of its selection and the advice of any such counsel, financial advisers or accountants and any Opinion of Counsel shall be full and complete authorization and protection in respect of any action taken or suffered or omitted by it hereunder in good faith”). The Trustee’s ability to rely on experts for this purpose is not unique. In the context of derivative claims, for example, courts have held that special litigation committees are entitled to rely on advisors in deciding whether to dismiss such claims. *See, e.g., Lichtenberg v. Zinn*, 260 A.d.2d 741, 744 (N.Y. 3d Dep’t 1999) (affirming SLC’s dismissal of derivative suit; concluding that SLC’s investigation was appropriate because “SLC retained experienced independent counsel and three unaffiliated experts to assist it in evaluating the specific allegations set forth in the complaint, and, further, in reviewing the multitude of documents requested by the SLC”); *Carlton Investments v. TLC Beatrice Int’l Holdings, Inc.*, 1997 WL 305829, at *18 (Del. Ch. 1997) (affirming SLC’s decision to approve proposed settlement of derivative action brought against Delaware corporation, noting that SLC had exercised “a right to justifiably rely on an expert report”). Similarly, courts have held that bankruptcy trustees are entitled to rely on the advice of advisors in deciding whether to settle claims. *See, e.g., JAS Partners, Ltd. v. Boyer*, No. 1:10-CV-303-TLS, 2011 U.S. Dist. LEXIS 42414, at *17-*18 (N.D. Ind. Apr. 19, 2011) (rejecting argument that bankruptcy trustee failed to properly investigate claim where trustee consulted experts in assessing value of claims); *In re Adler*, No. 09-34791-BKC-RBR, Chapter 11, 2010 Bankr. LEXIS 3001, at *10-*11 (Bkcty. S.D. Fla. Sept. 16, 2010) (in finding that trustee acted in good faith in entering into settlement agreement, citing trustee’s familiarity with claims and his extensive work with estate’s counsel and forensic experts in evaluating such claims); *Santos v. Elder (In re Macadam Computer, Inc.)*, No. C 06-4889 SI, 2007 U.S. Dist. LEXIS 49848, at *13-*16 (N.D. Cal. June 28, 2007) (affirming bankruptcy court’s approval of settlement where trustee had hired expert to opine on reasonableness of offer, and after thorough investigation, expert opined that settlement was reasonable); *Desmond v. ASR Acquisition Corp. (In re Desmond)*, Bk. No. 03-13878-MWV, Ch. 7, Adv. No. 04-1107-MWV, Adv. No. 04-1112-MWV, 2006 BNH 20, 2006 Bankr. LEXIS 1021 (Bkcty. D.N.H. 2006) (finding that bankruptcy trustee competently and fairly assessed costs, merits, and possible outcomes in deciding to accept settlement offer, where trustee based estimates on opinions of accounting and lending experts he had hired).

²³ Each of the expert reports has been posted to www.cwrmbssettlement.com.

29. The Institutional Investors, in their separate assessment of the reasonableness of the settlement, estimated that the size of the potential repurchase claims was no more than \$32.3 billion, *before* discounts for litigation risks and delay. This estimate was derived based upon the supported assumption²⁴ that 60% of the loans had breaches of reps and warranties, and that 50% would be successfully repurchased by a solvent obligor.²⁵ The \$8.5 billion settlement thus represents a recovery of roughly 26.3 cents on the dollar for these claims, without the need to overcome legal hurdles such as the burden of proof, loss causation (if applicable), successor liability and losses associated with delay.²⁶

30. In contrast to the Trustee's careful analysis, the claim by Walnut Place that the Trustee's claims "may exceed \$150 billion," *see* Removal Notice at ¶ 13, is unsupported by a citation to any data, expert report or even logic. To be true, this would mean virtually every loan in the Trusts was eligible for repurchase. That extreme claim is not even supported by Walnut's own lawsuit. It also is not supported by the claim of any other objector. Below is a summary of the objectors' allegations concerning rates at which loans in the Trusts allegedly breach reps and warranties:

a. Walnut Place

²⁴ These assumptions were based on data from 150,000 actual loan repurchases on Countrywide originated loans, experience with whole loan repurchases, inquiries to loan review providers and a review of public data concerning loan repurchases.

²⁵ Successor liability, and whether these repurchase claims could be recovered, are discussed in the next section.

²⁶ In contrast, the class action structure advocated by certain objectors typically yields no more than two to seven cents on the dollar. *See* Ellen M. Ryan and Laura E. Simmons, *Securities Class Action Settlements: 2010 Review and Analysis*, Cornerstone Research, at Figure 5; Jordan Milev, Robert Patton, and Svetlana Starykh, *Recent Trends in Securities Class Action Litigation: 2011 Mid-Year Review*, NERA Economic Consulting, at Figure 34 (July 26, 2011).

31. Walnut's initial complaint alleged that CWALT Trust 2006-OA10 held a total of 6,531 loans. Walnut Compl. at ¶ 2. Walnut claimed to have "investigated" 2,166 loans and determined that 1,432 had unspecified but false "representations and warranties." *Id.* This is a breach rate of 66%, not 100%. There is, of course, no guaranty that every repurchase claims on these allegedly ineligible loans would succeed.

b. AIG

32. Objector AIG filed a securities claim asserting that it had investigated 260,000 loans, and determined that 40% of them breached a representation or warranty. *See* Complaint ¶ 126, *American International Group Inc. v. Bank of America Corp.*, Index No. 652199/2011 (N.Y. Sup. Ct. Aug. 8, 2011).

c. FHFA

33. FHFA's Office of Inspector General reported a breach rate of only 15% in a post-mortem forensic review of loans purchased by Freddie Mac. *See* Evaluation of the Federal Housing Finance Agency's Oversight of Freddie Mac's Repurchase Settlement with Bank of America, FHFA Office of Inspector General, at 31 (Sept. 27, 2011).²⁷ This finding is especially noteworthy because the reps and warranties contained in the loans purchased by Freddie Mac are stronger than those contained in the Trusts' contracts.

34. In a separate securities action it filed against Countrywide, FHFA alleged it had conducted a "loan-level" analysis of 86 Countrywide securitizations, involving tens of thousands of loans, to assess compliance with reps and warranties concerning owner occupancy rates and

²⁷ MBIA has a lawsuit alleging breach rates of 90% in an adversely selected population of second lien deals. Only five Trusts in the Settlement involve second lien structures. Because they are different in kind, and because MBIA's review was on an adversely selected loan population, its findings regarding alleged breach rates do not undermine the reasonableness of the estimated exposure calculated by the Trustee's expert.

Loan-to-Value ratios. *See* Complaint, Tables 7 and 8, *FHFA v. Countrywide Financial Corp.*, No.11-cv-06195 (Sup. Ct. NY. Sept. 2, 2011). On average, FHFA alleged that it found 11% of the mortgage loans in the pools breached owner occupancy reps and warranties, 25.6% breached reps and warranties regarding the percentage of loans in the pools with LTV's greater than 80%, and 13.2% breached reps and warranties regarding the percentage of loans in the pools with LTV's greater than 100%, many of which findings were likely on the same loans.²⁸ *Id.* FHFA's findings may well explain why, as the Conservator of Freddie Mac and Fannie Mae, it issued a press release stating that "[FHFA's objection] was filed to obtain any additional pertinent information developed in the matter. [FHFA] is aware of no basis upon which it would raise a substantive objection to the proposed settlement at this time."²⁹

35. The Trustee recognized that the pursuit of repurchase claims could require years. It could yield nothing, something, or a lot. But "a lot" is what the Trustee recovered through the settlement. By any measure, \$8.5 billion is an enormous amount of money. It dwarfs Bank of America's earlier estimate that the *entirety* of its remaining repurchase exposure—across all platforms—faced an upper range of potential loss of between \$7 billion and \$10 billion.³⁰ The settlement compares favorably with the amount received by the GSEs in their separate settlement

²⁸ These findings are far lower than the breach rates the Institutional Investors assumed in their own settlement analysis.

²⁹ *See* Federal Housing Finance Agency Press Release, Aug. 30, 2011, *available at* <http://www.fhfa.gov/webfiles/22570/BofA83011.pdf>.

³⁰ *See* Andrew Frye, *BofA Says \$10 Billion is Top of Buybacks Forecast*, BLOOMBERG NEWS, Jan. 21, 2011, attached as Ex. 3. This "remaining exposure" at the time was estimated to include remaining claims for repurchases by the government sponsored enterprises Fannie Mae and Freddie Mac for their guaranty portfolio, private label repurchase claims such as those held by the Trusts, repurchase claims filed by monoline insurers like MBIA and Ambac, and repurchase claims filed by whole loan buyers.

of repurchase claims with Bank of America, even though the GSE contracts contain stronger contractual reps and warranties than those contained in the Trusts' contracts.

36. The Trustee's filing of the instruction proceeding will permit all interested investors to test the reasonableness of the Trustee's decision to settle these claims. A difference of opinion does not render the Trustee's decision to settle unreasonable. Here, where there was substantial uncertainty concerning the likelihood that claims would be pursued for many Trusts, and where even those claims that might be pursued faced an uncertain legal landscape, the Trustee was entitled to conclude that it preferred an \$8.5 billion "bird in the hand."

37. The Trustee was also entitled to consider whether there was any "bird in the bush" if a settlement was rejected. This was a particular concern given Countrywide's insolvency and the uncertainties concerning whether Bank of America could be held liable as its successor. It is to that issue that we now turn.

3. Successor Liability Risks

38. The successor liability risk here is obvious. Bank of America did not sign any of the PSAs. It never promised to repurchase a single loan. In 2008, Countrywide Financial Corporation (CFC) was merged into a subsidiary of Bank of America in a statutory Delaware merger. CFC did not merge into Bank of America itself. Though Bank of America assumed certain of CFC's corporate debt, it did not overtly assume the repurchase obligations owed by the Mortgage Seller, Countrywide Home Loans, Inc.

39. The case for successor liability or de facto merger is far from clear. A federal court in the Ninth Circuit has dismissed several Countrywide-based claims against Bank of America on separateness grounds, based on facts identical to those alleged by objectors such as

AIG.³¹ That court undertook detailed analyses of the law that should govern the issue of successor liability and de facto merger. The *Maine State Retirement* opinion is particularly comprehensive and makes plain the stark risks the Trustee would face in litigating a successor liability/de facto merger claim.

40. An outlier among the cases that have considered whether Bank of America may be liable as a successor to the Countrywide-affiliated Mortgage Sellers is a case brought by the bond insurer MBIA. In that case, Justice Bransten denied *dismissal* of a claim of de facto merger after she concluded that MBIA had alleged sufficient facts to state such a claim under New York law. The decision does not hold, of course, that Bank of America is liable for Countrywide's liabilities. The court did not provide any basis to conclude that New York law applied to this issue (and other courts considering the matter have concluded it is governed by Delaware, rather than New York, law).

41. The Trustee also sought and obtained advice from a leading corporate and securities professor, and a valuation expert, to assess the risks associated with pursuing a successor liability claim for the Trusts. It was prudent for the Trustee to do so: the issue of successor liability, and the potential to win or lose it, is a huge risk to any prospect of a litigated recovery on the Trustee's claims. The Countrywide-affiliated Mortgage Sellers are deeply insolvent. The financial press is rife with speculation concerning when Bank of America will place them in bankruptcy.

42. The functional insolvency of the Countrywide entities was confirmed by the valuation report from the Trustee's expert, *see* Report of Capstone Valuation Services. The

³¹ *See Maine State Ret. Sys. v. Countrywide Fin. Corp.*, No. 2:10-CV-0302 MRP (MANx), 2011 WL 1765509, at *8-*9 (C.D. Cal. Apr. 20, 2011); *Allstate Ins. Co., et al. v. Countrywide Financial Corp.*, et al., No. 2:11-CV05236-MRP (MANx), slip op. at 43-44 (C.D. Cal. Oct. 21, 2011).

report contains a key finding that neither the court, nor any rational investor, should ignore in evaluating whether to approve the settlement: if the Trusts had to look solely to Countrywide Financial Corporation to satisfy their repurchase claims,³² their *maximum* potential recovery would not exceed \$4.8 billion. *See* Capstone Report at 3. The Trusts have recovered almost twice that amount—\$8.5 billion—by way of this settlement. It was inherently reasonable for the Trustee to settle for twice the likely recovery from Countrywide, given the prospect that successor liability issues might be lost. Settlement is also entirely reasonable given the very real prospect that Bank of America might yet bankrupt Countrywide, leaving the Trusts fighting for what they could get in a Countrywide Bankruptcy.

43. The Trustee was entitled to evaluate these risks and benefits in deciding whether to settle. The opinion of the Trustee's expert, Professor Robert Daines, makes clear that these risks are serious and might be insurmountable. *See* Daines Report at 38 (concluding as to a de facto merger theory: "I think the economic arguments and bulk of the case law favor BAC, but it is possible — though not likely — that the Trustee could succeed on this . . . New York could follow the lead of the recent decision in *MBIA v. Countrywide* and find that de facto merger allegations are plausible enough to survive a motion to dismiss. . . . The potential for a favorable ruling however is muted by the fact that New York law may not even apply," and noting elsewhere that "I do not believe New York law will apply."). It was not unreasonable for the Trustee to conclude that certainty, and the substitution of Bank of America as a solvent obligor, were a better outcome for the Trusts than years of uncertain litigation at the end of which there might be only a bankrupt Countrywide to satisfy the Trustee's claims. Given the risks, the

³² This analysis assumes success on an additional uncertainty; namely, whether the corporate veil could be pierced between Countrywide Financial Corporation and its subsidiary, the Mortgage Seller Countrywide Home Loans Inc.

Trustee's decision to settle might well have been the only truly *prudent* conclusion to be drawn.³³

D. Servicing Improvements and Litigation Risks

44. A key component of the settlement is the near complete transformation of loan servicing that will occur upon the approval of the settlement. This is a matter of keen importance to all investors in the trusts, no matter the tranche in which they hold, because poor loan servicing magnifies investor losses and increases poor outcomes for borrowers. As the chart below demonstrates, at the time of the settlement, Bank of America was by far the worst of the major bank loan servicers. Its consistently poor performance was endemic: regardless of loan type, regardless of activity, Bank of America was at the bottom of nearly every category:

Key Pool Statistics by Servicers – May 2011³⁴

Alt-A	Total Loans/# of Loans 90+ Delinquent	Percentage of Loans 90+ Delinquent	Roll Rate 30 to 60 Days DQ	Roll Rate 60 to 90 Days DQ	Number of Modifications Granted as % of UPB	6 Mo Mod Redefault Rate	Weighted Avg. Mos to Liquidation (last 12)	WA Mos to Liq from Foreclosure
BofA	503,000/56,900	11.3%	43.2%	52.1%	11.2%	12.3%	21	23
JPM Chase	72,000/4,790	6.6%	42.3%	49.1%	7.1%	9.9%	20	19
CitiMortgage	49,000/1,709	3.4%	38.0%	34.6%	16.1%	5.1%	18	19
Wells Fargo	195,593/9,906	5.1%	40.7%	34.6%	15.4%	12.6%	21	19
Option ARM	Total Loans/# of Loans 90+ Delinquent	Percentage of Loans 90+ Delinquent	Roll Rate 30 to 60	Roll Rate 60 to 90	Number of Modifications Granted as % of UPB	6 Month Redefault Rate	Weighted Avg. Mos to Liquidation	
BofA	153,604/36,876	24%	44.3%	57.0%	15.6%	17.2%	24	29
JPM Chase	51,199/4,949	9.6%	40.8%	49.0%	6.3%	11.5%	19	21
Prime	Total Loans/# of Loans 90+ Delinquent	Percentage of Loans 90+ Delinquent	Roll Rate 30 to 60	Roll Rate 60 to 90	Number of Modifications Granted as % of UPB	6 Month Redefault Rate	Weighted Avg. Mos to Liquidation	
BofA	131,568/10,163	7.7%	43.5%	54.3%	5.3%	9.3%	19	21
JPMorgan Chase	105,688/5,582	5.2%	49.2%	53.5%	3.8%	8.2%	17	13

³³ This is particularly true where the majority of Trusts lacked investors ready, willing, and able to fund the Trusts' litigation of these claims and bear the Trusts' substantial litigation risks.

³⁴ Source: RMBS My Final Look as of May 2011 Remittance, using data from CoreLogic Loan Performance, CoreLogic Home Price Index and RMBS 2000-2010 Vintages.

Wells Fargo	184,341/3,947	2.1%	36.1%	44.3%	3.5%	6.8%	15	14
Subprime	Total Loans/# of Loans 90+ Delinquent	Percentage of Loans 90+ Delinquent	Roll Rate 30 to 60	Roll Rate 60 to 90	Number of Modifications Granted as % of UPB	6 Month Redefault Rate	Weighted Avg. Mos to Liquidation	
BofA	426,616/117,472	27.5%	35.9%	42.5%	38.8%	18.9%	27	30
JPMorgan Chase	193,714/25,194	13%	29.4%	40.1%	41.7%	14.7%	23	25
Wells Fargo	155,681/14,391	9.2%	34.4%	33.0%	43.3%	16.5%	24	19

45. Bank of America's poor servicing had real and lasting consequences for investors and borrowers. Its markedly longer time to resolution meant that it advanced more funds, for longer, to pay principal and interest on loans that were hopelessly in default. While on the surface these advances benefitted the trusts, in reality, they magnified collateral losses: every advance creates a super-senior lien that must be satisfied on liquidation, at the expense of holders in loss bearing tranches. Bank of America granted fewer modifications to troubled borrowers, and those it granted failed at a much higher rate, thus exacerbating losses that might have been avoided through competent implementation of an appropriate modification. Bank of America also had much higher rates of delinquencies, and did less to re-convert them to performing loans, than did any other major bank servicer.

46. "Prudent servicing" plainly required a far better level of service than Bank of America was providing, but litigation offered little prospect of improving the situation. Litigation of servicing claims would likely be on a loan by loan basis; i.e., how much of the loss on Loan A could have been avoided through prudent servicing. This was an intractable problem, particularly for long term holders who depend on prudent servicing to minimize losses and maximize performance of their investments. Imprudent servicing was also exceedingly difficult to remedy under the PSAs. Certificateholders cannot compel the Trustee to replace a servicer without: a) amassing 66% of the Voting Rights, b) identifying a replacement subservicer acceptable to the rating agencies, and c) indemnifying the Trustee for any losses reasonably

occasioned by the instruction to replace the servicer. *See* PSA §§ 7.01, 7.02, and 8.02(ix). There are at least 770,000 loans in the Trusts' pools. Even assuming a replacement servicer for such a massive volume of loans could be found, the requirement that Certificateholders must indemnify the Trustee against all losses occasioned by instructed termination and transfer of the Master Servicer was an insurmountable barrier. No investor, much less the fiduciaries who were trying to achieve a better outcome for their investors, could indemnify the Trusts for the risk of loss associated with transferring servicing of \$160 billion in loans.

47. The settlement avoids these problems, because it is a consensual agreement. Though the Trustee had no ability to force Bank of America to transfer loans to subservicing under the contracts,³⁵ by virtue of the settlement, Bank of America has agreed to do so at its own expense. Bank of America has estimated that the costs of implementing these servicing improvements will be roughly \$400 million over and above the settlement payment itself. More important than these cost savings are the potential results. The sub-servicers are specialists. They are incentivized to provide outcomes that are beneficial to both borrowers and investors. Simply in terms of the \$400 million cost to provide it, this benefit is enormous; if it succeeds in returning borrowers to performance through modifications, and otherwise reduces delinquencies, defaults, and loss severities, its value will likely be many times that amount.

48. This is not the only servicing improvement the Trustee has obtained in the settlement. Bank of America has also agreed to benchmark its servicing performance to national servicing standards. *See* Settlement Agreement at ¶ 5(c), attached as Ex. 25. If the settlement is approved, Bank of America will be required to compensate the Trusts, automatically and on a monthly basis, for servicing efforts that fall below the stated benchmarks. Nothing in the

³⁵ PSA § 3.02 (permitting, but not requiring, master servicer to transfer loans to subservicer).

contract requires Bank of America to do this. The Trusts could not have obtained this affirmative, automatic compensation mechanism through contested litigation. They will never be able to recover it if the settlement is not approved.³⁶ An annual, independent compliance review will monitor Bank of America's compliance with this requirement. *See* Settlement Agreement at ¶ 5(f) ("Reporting and Attestation of Compliance with Servicing Improvements"). These important servicing improvements will improve the performance of the Trusts' loans over time. They have substantial value to investors—value that will be destroyed, irretrievably, if the settlement is not approved.

49. The settlement also benefits borrowers. Ultimately, repayment of the securities issued by the Trusts depends upon the ability and willingness of borrowers to make their mortgage payments as and when they are due. The collapse in the American economy coupled with the decline in the housing and job markets has left many borrowers in deep financial distress. Many borrowers could and would benefit from loan modifications. It is widely recognized that principal reductions are one largely unused tool that could help troubled borrowers pay their loans. A positively performing loan, even at a reduced rate, is vastly preferable to having one more property in foreclosure. It is also preferable to ownership of a vacant property, in a depressed real estate market, that deteriorates because no one is there to maintain it. Bank of America (like many other servicers) faced uncertainty in implementing

³⁶ *See, e.g.*, Ex. 4, Amherst Mortgage Insight, "Amherst Analysis: The Bank of America Settlement," June 30, 2011 ("Most interesting, the settlement includes some sizeable steps to improve the servicing on the covered Trusts. Bank of America has agreed to move the servicing of high-risk loans to qualified sub-servicing firms, at Bank of America's expense We applaud this idea, but implementation of the transfer[s] will take time."); *see also* Ex. 5, *BofA to Move High-Risk Countrywide Mortgages to Subservicers*, HOUSING WIRE, July 28, 2011 ("We believe that Bank of America's actions to move the servicing of high-risk loans to qualified sub-servicing firms, at Bank of America's expense, are particularly significant," said Laurie Goodman, an analyst at Amherst Securities.").

significant principal reduction modifications or other innovations such as short sales or “cash for keys” programs because the generic “prudent servicing” mandate in the PSAs did not explicitly authorize them to do so.³⁷

50. The settlement cures this problem: By confirming that principal reductions *are* permissible in the Trusts, the settlement offers hope to tens of thousands of borrowers who might otherwise have been unable to refinance and reduce their payments because their loans were under water.³⁸ By requiring that the servicing of loans for troubled borrowers be transferred to specialty servicers who are incentivized to provide prompt modifications that work over the long term, the settlement increases the likelihood that deserving borrowers’ loans will return to performing status promptly. This outcome is plainly in the interest of borrowers and investors alike. The court should consider whether any feasible alternative exists before it relegates the Trusts to “loan by loan” litigation of prudent servicing claims.

³⁷ The last time Bank of America agreed to implement large scale loan modifications in the Trusts was in connection with the Attorney Generals’ multi-state settlement of predatory lending claims against Countrywide. See March 24, 2010 Press Release of Hon. Martha Coakley, Attorney General of the Commonwealth of Massachusetts (mandating not only loan modifications but “significant principal forgiveness”), available at <http://www.mass.gov/ago/news-and-updates/press-releases/2010/ag-coakley-secures-3-billion-in-loan.html>, and Final Judgment by Consent, C.A.No. 10-1169, *Commonwealth of Massachusetts v. Countrywide Financial Corp., et al.*, in the Superior Court of the Commonwealth of Massachusetts. This agreement precipitated a lawsuit by disgruntled investors who claimed that the Pooling and Servicing Agreements did *not* authorize principal reduction modifications of loans held in the Trusts. See *Greenwich*, No. 650474/2008, attached as Ex. 1.

³⁸ The Institutional Investors are not privy to the ongoing discussions among various Banks, the federal government, and the state Attorneys General. According to a recent Wall Street Journal article, the multi-state discussions with the Attorneys General appear to have been focused on loans in the “held for investment” portfolio of the target banks, rather than on those held in securitized trusts. See Ruth Simon, Nick Timiraos, and Dan Fitzpatrick, *New Mortgage Plan Floated*, WALL ST. J., Oct. 18, 2011, available at <http://online.wsj.com/article/SB10001424052970204346104576637513972299854.html>. While this may change or expand, the certainty that principal reductions *will be* available to borrowers whose loans are held in *these* Trusts removes any doubt and is an important benefit to borrowers.

E. The Document Indemnity

51. The settlement contains another automatic compensation mechanism that will spare the Trusts years of potentially costly and uncertain litigation: the document indemnity. *See* Settlement Agreement at ¶ 6. Recent Consent Judgments issued by the Office of the Controller of the Currency implemented important documentation requirements to protect borrowers against wrongful foreclosure. Those requirements, however, did not address what happened to the Trusts when they were unable to liquidate a loan because the required mortgage and title policies were missing or incomplete.

52. The settlement solves this problem, too. The documentation cure provision in the settlement targets loans where the Trusts' ability to foreclose may be compromised by deficiencies in the recording of the mortgage and where the Trusts' ability to recover insurance proceeds may be compromised by deficiencies in the Trusts' title policies. If the settlement is approved, Bank of America must either cure these deficiencies or, if it does not, and the Trusts cannot liquidate the loan as a first-lien holder as a result of these deficiencies, indemnify the Trusts for 100% of the loss suffered. This automatic remedy is highly beneficial to the Trusts. By imposing an immediate incentive to cure document deficiencies, the settlement will avert many document issues that might arise later. The indemnity for unrecorded mortgages and missing title policies affords the Trusts a certain, 100% recovery and avoids loan-by-loan litigation documentation issues. No provision of the contract could be invoked to achieve this affirmative, comprehensive cure and indemnity obligation through litigation. While individual loans certainly would be subject to repurchase claims if mortgages were unrecorded or title insurance did not exist, the expense and delay of loan by loan litigation is not a better option than an automatic compensation remedy for these defects.

F. What are the Alternatives to Settlement?

53. A key question in any settlement decision is: what is the alternative? That question must be probed carefully, because the PSAs afford Certificateholders few rights and even fewer remedies.

54. All parties agree on one fundamental fact: the claims being settled (or that would have been pursued in litigation in the absence of a settlement) belong to the Trustee. They do not belong to the Certificateholders individually. Section 10.08 of the PSAs expressly denies the Certificateholders any right to “control the operation and management of the Trust Fund, or the obligations of the parties” — and grants to the Trustee the exclusive right to control the trust and litigation on behalf of the trust. The provision goes on to provide, again in clear terms, that Certificateholders do not have the right to sue, but must instead rely on the Trustee: “No Certificateholder shall have any right by virtue or by availing itself of any provisions of this Agreement to institute any suit, action or proceeding in equity or at law upon or under or with respect to this Agreement” PSA § 10.08.

55. There is, therefore, no mechanism under the PSAs by which Certificateholders have any possibility of litigating the Trustee’s claims themselves, particularly over the Trustee’s objection. The PSAs, again, are explicit in providing that the claims belong to the Trustee, not Certificateholders. In this, the Trust structure is not unique. Disgruntled shareholders may not pursue a corporation’s claims themselves; instead, they must meet strict requirements, and proceed derivatively on behalf of the corporation. It would be extraordinary, therefore, to conclude that a party like the Trustee could not control the decision to prosecute—or settle—its own claims simply because a holder of one of its securities objected. This is not the law as it pertains to the highly technical terms of a Pooling and Servicing Agreement.

56. No action provisions are enforced strictly.³⁹ The court must therefore consider the following questions in evaluating the reasonableness of the Trustee's decision to settle and the validity of the objectors' demand for an "opt out" right:

- How can an "opt out" right for Certificateholders be reconciled with the plain language of § 10.08, which vests exclusive control of litigation decisions in the Trustee?
- What plan do the proposed objectors offer to the Trusts if they succeed in destroying the settlement? With few exceptions, none of the objectors has expressed a willingness to fund the litigation of these claims. For many Trusts, there is no identified group of objectors that has aggregated the 25% Voting Rights required to permit them to do so. This issue is important to the Institutional Investors, who have almost \$14 billion in holdings in Trusts included in the settlement where they do not have (and no other objector has claimed to have) 25% of the Voting Rights.
- What certainty do the proposed objectors offer that the Trusts will recover more if the Trustee pursues these claims in litigation? The answer, necessarily, is none. Litigation is inherently uncertain.
- What indemnity do the proposed objectors offer if (on some as yet unrecognized theory) they displace the Trustee's right to control the claims and successfully exclude a Trust from the settlement? The answer, again, is none. No objector has offered to provide an indemnity equal to the risks associated with pursuing litigation over settlement. These risks include: loss of the settlement payment,

³⁹ See ¶13, *supra*.

loss of the funded servicing improvements, loss of the document indemnity and the costs of pursuing the contested litigation.

- What about the rights of investors who want to receive the benefits of the settlement? The PSAs require that the Trustee's claims be pursued for the common benefit of all Certificateholders. The views of those Certificateholders who value certainty over speculation are certainly entitled to deference, given the lack of any articulated plan for, or financial resources to pursue, litigation for most Trusts if the settlement is destroyed.

57. An order rejecting the settlement would also have broad implications for RMBS investors in other trusts created by other issuers. Stated plainly, if a group of well organized, reputable investors cannot gain approval of a settlement that is favorable to the Trusts, why would any other group of investors even try? If a trustee that has taken the extraordinary step of seeking court approval of a favorable settlement is sent packing, what assurance is there that any trustee would feel confident in settling claims later, for different trusts?

58. The law in this area is exceedingly difficult and unfavorable to investors. It imposes few burdens on trustees and interposes multiple barriers to investors' ability to compel trustees to act. This is a fact of life that cannot be ignored: absent this Settlement, it is difficult if not impossible to see how the investors in these Trusts could ever obtain benefits as great as those provided in the settlement. The PSAs present significant hurdles and obstacles to litigation by the Trustee, or the Certificateholders. Those difficulties here are magnified by the fact that no recovery approaching that guaranteed by the settlement could ever be achieved without also piercing the corporate veil and requiring Bank of America to answer for the liabilities of Countrywide—a formidable obstacle all by itself. Given this reality, the court should not lightly

conclude that litigation is a preferable alternative, much less that the outcome of a litigation effort would be better for the Trusts or for RMBS investors as a whole.

III. Response to Objections

59. The objections lodged against the settlement fall into five general categories. *See supra* pp. 2-3. We address each, briefly, below but reserve the right to supplement this response when discovery is concluded. A chart listing the objections appears below:

Objections to The Settlement				
<u>Seek Additional Information</u>	<u>Miscellaneous Objections</u>	<u>Litigation Claimant</u>	<u>Financial Guaranty And Monoline Insurers</u>	<u>Waterfall-Related Objections</u>
American Equity Investment Life Insurance Co., et al. (8/31, St. Doc. #169)	Commonwealth Advisors, Inc. (8/30, St. Doc. #184)	American Fidelity Assurance Co. (8/30, St. Doc. #170)	Ambac Assurance Corporation, et al. (8/30, Doc. #29)	Waterfall Eden Master Fund, Ltd. (8/29, St. Doc. #165)
Ballantyne Re PLC (8/30, St. Doc. #187)	Cranberry Park LLC, et al. (8/2, St. Doc. #90)	American International Group, Inc., et al. (8/10, St. Doc. #131)	CIFG Assurance North America, Inc. (8/24, St. Doc. #155)	Clayhill Investors LLC (8/30, St. Doc. #180)
Blue Mountain Credit Alternatives Master Fund, LP (8/30, St. Doc. #188)	Monarch Debt Recovery Master Fund Ltd, et al. (8/30, St. Doc. #173)	Federal Home Loan Bank (FHLB) of Boston, et al. (7/13, St. Doc. #55)	Syncora Guarantee Inc. (8/30, Doc. #24)	
Federal Deposit Insurance Corporation (8/29, Doc. #3)	TMI Investors, LLC (7/13, St. Doc. #51)	Knights of Columbus (8/20, St. Doc. #141)		
Federal Housing Finance Agency (8/30, Doc. #15)	Triaxx Prime CDO 2006-1, et al. (8/24, St. Doc. #156)	Mary Ellen Iesu, et al. (8/30, Doc. #22)		
First Reliance Standard Life Insurance Co. (8/30, Doc. #33)	United States Debt Recovery VIII, L.P., et al. (8/30, St. Doc. #178)	Policemen's Annuity & Benefit Fund of Chicago, et al. (7/6, St. Doc. #32)		
Good Hill Partners LP (8/29, St. Doc. #167)	Vertical Capital, LLC (8/25) (Ltr.)	Sterling Federal Bank, F.S.B., et al. (8/29, St. Doc. #166)		
Goldman Sachs & Co. Securities Division (8/30, St. Doc. #190)	V Re-REMIC, LLC (7/14, St. Dkt. #61)	The Western and Southern Life Insurance Co., et al. (7/29, St. Doc. #85)		
Liberty View LLC (8/30, Doc. #28)		Walnut Place LLC, et al. (7/5, St. Doc. #28)		
Maine State Retirement System, et al. (8/30, St. Doc. #183)	Attorney General of the State of Delaware (8/10, St. Doc. #129)			
Mortgage Bond Portfolio LLC (8/30, St. Doc. #181)	Attorney General of the State of New York (8/4, St. Doc. #101)			
National Credit Union Administration Board (8/30, Doc. #26)				
Oriental Bank and Trust (8/30, St. Doc. #172)				
Pine River Master Fund Ltd, et al. (8/30, Doc. #7)				
Platinum Underwriters Re, et al. (8/30, Doc. #31)				
Reliance Standard Life Insurance Co. (8/30, Doc. #32)				
RMBS Acquisition Co. LLC (8/29, Doc. #4)				
Safety National Casualty Corporation (8/30, Doc. #35)				
Stone Creek LLC (8/30, St. Doc. #177)				
Sun Life Assurance Co. of Canada (U.S.) (8/30, Doc. #36)				
20	10	9	3	2

A. Standard of Review

60. Each of the Certificateholders became “contractually obligated to speak with one voice,” *In re Innkeepers USA Trust*, 448 B.R. 131, 145 (Bkcty. S.D.N.Y. 2011), when they purchased securities governed by a Pooling and Servicing Agreement. The voice through which they speak, in the absence of compliance with the no action provision, is the voice of the Trustee.⁴⁰ *Id.* No action clauses are “strictly construed,” *Cruden*, 957 F.2d at 968, and are “enforced in a variety of contexts in both state and federal courts.” *McMahan & Co. v. Warehouse Entertainment, Inc.*, 65 F.3d 1044, 1050-51 (2nd Cir. 1995); *see also Teachers Insurance & Annuity Ass’n. v. CRIIMI Mae Svcs. L.P.*, 681 F.Supp.2d 501, 506 (S.D.N.Y. 2010) (no action clauses “are common features of trust indentures” that bar suit by Certificateholders in the absence of compliance with the condition). Claims by certificateholders that fail to comply with these provisions, or that otherwise seek to interfere with the decision of an RMBS trustee or Special Servicer, are routinely dismissed. *See* ¶ 13, *supra*.

61. A key reason no action provisions are enforced is this: “Granting standing to a certificateholder would not only override the terms of the [agreement] and alter the bargained for-terms and risks investors undertook when they bought certificated interests, . . . it would encourage and embolden other certificateholders to hire their own counsel to challenge the special servicer’s authority and to advance their individual and conflicting pecuniary interests.” *Innkeepers*, 448 B.R. at 145. Many of the objectors have filed individual securities claims or

⁴⁰ An alleged conflict on the part of the Trustee does not change this analysis. Instead, as the Second Circuit has recognized, albeit in a different context, the remedy certificateholders have against a conflicted trustee is an independent action for breach of fiduciary duty, *not* disapproval of the settlement. “[A] bankruptcy court’s obligation is to determine whether a settlement is in the best interests of *the estate*, not to ensure that the creditors’ representatives are honoring their fiduciary duties.” *In re Refco, Inc.*, 505 F.3d 109, 119 (2d Cir. 2007) (denying “party in interest” bankruptcy standing to interest holders of a creditor who claimed their representative had breached a fiduciary duty in entering into a settlement) (emphasis original).

securities class actions against Bank of America. Both the PSAs and applicable law strictly prohibit these Certificateholders from using this proceeding—which concerns only the Trustee’s claims—to “advance their individual and conflicting pecuniary interests.” We do not suggest these objectors should not be heard;⁴¹ rather, we submit that the Court should be vigilant to ensure that the individual pecuniary interests of Certificateholders seeking to advance securities claims do not deny the Trusts and their Certificateholders the common benefit of a highly favorable, and otherwise unobtainable, settlement.

B. The Institutional Investors Actions Were Open and Publicized, Not Secret

62. Rhetoric is rarely a substitute for reason. In this case, however, rhetoric—in the form of *ad hominem* attacks—has been employed to distract attention from the many reasons to support approval of the settlement. These attacks are unworthy of those who have made them; they are also inconsistent with the grave and important issues facing the Trusts, the Trustee and the investors in the Trusts’ securities. The Institutional Investors respond to them here.

63. The Institutional Investors were not a secretive or exclusive “clique.”⁴² They began with six like-minded investors⁴³ who sought the right to pursue litigation to redress the

⁴¹ A number of courts have, however, denied standing to certificateholders who seek to interfere with decisions of a trustee or Special Servicer unless the certificateholders have complied with the no action provisions. *See, e.g., Innkeepers*, 448 B.R. at 144-45 citing Summary Order Denying Motion to Intervene, *Bank of America, N.A. v. PCV ST Owner L.P.*, Case No. 10-1178 (S.D.N.Y.) [Doc. #89].

⁴² The Court’s use of this term to describe the Institutional Investors is regrettable. It was also unfounded, even on the limited record then before it. *See, e.g.,* Institutional Investors’ Response Regarding Intervention of AIG at 4-5 (describing press releases); Trustee Response to Walnut Objection at 3-4 (reciting Walnut’s knowledge of settlement discussions and refusal to participate in them).

⁴³ The initial six investors were Blackrock, Kore Capital, MetLife, Neuberger Berman, PIMCO and one other investor who later dropped out. The fact that one investor dropped out demonstrates yet another risk associated with the pursuit of these claims; namely, that a group

repurchase and servicing issues that were ravaging the performance of the Trusts. The PSAs require that this litigation effort proceed through the Trustee, either with or without its cooperation, so these investors contacted the Trustee, first. On June 17, 2010 these investors sent a letter to the Trustee requesting that it meet with them. On August 2, 2010 this meeting occurred at the offices of the Trustee's counsel in New York. By then, the group had expanded to include two additional investors: Freddie Mac and the New York Fed. Nothing in the PSA required the Trustee to give notice to the world that this meeting occurred. The PSA, moreover, expressly contemplates that holders of 25% of the Voting Rights can take certain actions without the consent of other investors, if they meet the other requirements of the contract.

64. The Trustee's initial response was less than helpful. On August 20 the group sent the Trustee a letter instructing it to open an investigation of ineligible mortgages securing over \$26 billion of Countryside-issued RMBS. A few days later, they issued a press release informing the market that this letter had been sent. The press release, a copy of which is attached as Ex. 6, also informed the market that the Institutional Investors "issued their instruction letter *after they met with* senior representatives of the Trustee, and its counsel, on August 2." The public disclosure that a large and organized group of reputable holders was seeking to litigate claims for the Trusts gave other investors hope that litigation of these claims might actually be possible. Other investors thereafter contacted the group and offered to commit their holdings to aggregate Voting Rights, and their balance sheets to fund the indemnity required to pursue the claims. They were welcomed into the group and the group grew.

65. On September 3, BNY Mellon responded to the Institutional Investors' instruction. Citing its indemnity rights and issues related to the calculation of Voting Rights

will initially have 25% of the Voting Rights but will later lose the ability to provide binding instructions to the Trustee, if such instructions were needed.

under the PSAs, BNY Mellon initially resisted the investors' demand that it take action to enforce the agreements. Among the bases on which the Trustee refused to act was its claim that it had not been notified of any Event of Default that would require it to take action.⁴⁴ While unfortunate and unhelpful, BNY Mellon's position was nonetheless grounded in the terms of the PSAs. *See supra* Part II(A).

66. BNY Mellon's response left the investors with no choice. On October 18, 2010, the Institutional Investors issued a Notice of Non-Performance to BNY Mellon, as Trustee, and to BAC Home Loans Servicing, as Master Servicer.⁴⁵ The group issuing the Notice of Non-Performance was markedly larger than the group that sent the initial instruction letter. Its holdings had ballooned to 115 Trusts whose outstanding loans were \$47 billion.

67. The Notice of Non-Performance is noteworthy for an additional reason: it was the first communication sent to BAC Home Loans Servicing (or any other affiliate of Bank of America) concerning the Institutional Investors' intent to pursue the Trusts repurchase and servicing claims through the Trustee. Notice was sent to BAC Home Loan Servicing because notice to the Master Servicer, and the running of a sixty day cure period, were mandatory conditions precedent to the Institutional Investors' ability to file suit and litigate claims. *See* PSA §§ 7.01 and 10.08.

68. Because the issuance of a Notice of Non-Performance might be material to investors in the Trusts' securities, the Institutional Investors issued a press release disclosing they

⁴⁴ BNY Mellon's reluctance to act without the indemnity required by the contract is by no means unique among RMBS Trustees. Deutsche Bank, for example, sent a notice to RMBS investors indicating it was willing to take action to enforce pooling and servicing agreements, "subject to conditions stated in the governing documents." *See* Ex. 7, Oct. 25, 2010 Notice. Other Trustees have taken no action at all, despite widespread evidence of ineligible mortgages in their pools.

⁴⁵ By this time, one investor had dropped out of the group, but another investor—Western Asset Management Company—had joined.

had sent the Notice to BNY Mellon and Bank of America. *See* Ex. 8. This release informed the entire securities market that holders of securities in 115 Trusts had started the running of a clock toward the declaration of an Event of Default. *See* Ex. 9. The Notice of Non-Performance was widely covered in the media.⁴⁶ It was the subject of questions put to Bank of America CEO Brian Moynihan in Bank of America's public earnings call the following Tuesday morning.⁴⁷ The securities markets reacted with alarm: up to that point, Bank of America had indicated it was unable to estimate its repurchase exposure to private label securitizations because no group of investors had organized to pursue these claims.⁴⁸ In the wake of the Notice, Bank of America's stock price dropped by 4.4%.⁴⁹ It has never recovered.⁵⁰

69. With the disclosure that the Institutional Investors group was growing, and was only weeks away from instituting litigation to pursue the Trustee's claims, the group continued to expand. From an original group of six, the group eventually came to include 22 institutions: nine independent investment advisers,⁵¹ seven insurance companies,⁵² two European banks,⁵³

⁴⁶ A compilation of press reports regarding the October 18, 2010 Letter is attached as Ex. 10.

⁴⁷ *See* Nathaniel Popper, *BofA pressured to buy back loans; Separately, the bank reports a \$7.3-billion loss, citing new debit-card fee rules*, LOS ANGELES TIMES, Oct. 20, 2010, Ex. 10 at 71.

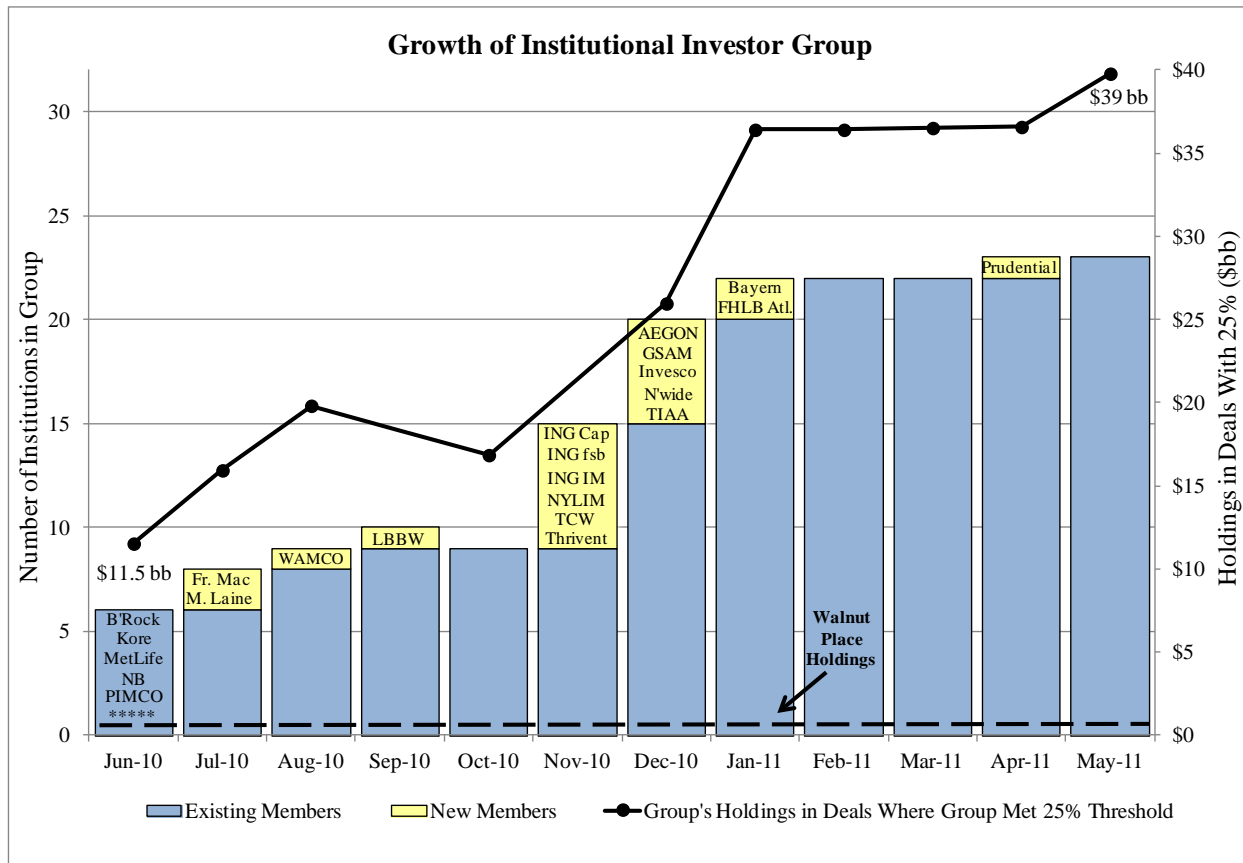
⁴⁸ *See, e.g.*, Bank of America 3Q10 SEC Form 10-Q at 40.

⁴⁹ *See, e.g.*, Alistair Barr, *NY Fed among investors pressuring Bank of America on mortgages*, MARKETWATCH, Oct. 19, 2010, Ex. 10 at 32.

⁵⁰ Though the particular motives of the Institutional Investors are largely irrelevant, these events belie any claim that the Institutional Investors "colluded" with Bank of America regarding the settlement.

⁵¹ The registered investment advisers in the group are a "who's who" of reputable, highly regarded mutual fund, pension fund and separate account advisers: Blackrock, PIMCO, TCW (Trust Company of the West), Western Asset Management (WAMCO), Invesco, Neuberger Berman, Goldman Sachs Asset Management, ING Investment Management LLC, and Prudential Investment Management.

and four other investors and financial institutions.⁵⁴ From original holdings of 25% of 65 deals in June 2010 (in which deals the group held \$11.5 billion), the group expanded to cover 25% of 265 deals by May 2011 (in which deals the group held over \$39 billion). The table below sets out the members of the group, and the size of the holdings involved in their effort, on specific dates relevant to the settlement:



⁵² The insurance company and annuity investors are: MetLife, TIAA-CREF, Nationwide Insurance, New York Life, AEGON Insurance, ING, and Thrivent Financial for Lutherans.

⁵³ The European Banks include Landesbank Baden-Wuerttemberg (LBBW), Bayerische Landesbank (BayernLB) and their affiliates.

⁵⁴ This category includes the New York Fed's Maiden Lane Portfolios, Freddie Mac, the Federal Home Loan Bank of Atlanta and Kore Capital.

70. The demonstrated expansion and openness of the Institutional Investor group is fundamentally *inconsistent* with the suggestion that the Institutional Investors were a preferred or secretive “clique” that excluded other investors from participating in their efforts to obtain a remedy that would benefit all of the Trusts and their investors.⁵⁵ Belated complaints by some Certificateholders that the Trustee failed to “include” them in ongoing settlement discussions also fail to consider these additional facts:

- The Institutional Investors were engaged in discussions with the Trustee because they were able to, and intended to, litigate the Trustee’s claims.
- The Institutional Investor group expanded because it was open to other, like-minded investors willing to bear the risks, costs and burdens associated with contested litigation of the Trustee’s claims.
- With the ostensible exception of Walnut Place, none of the remaining objectors has alleged that they ever *sought* to pursue claims on behalf of the Trusts, or made any demand that the Trustee do so, much less that they informed the Trustee they were willing to put their balance sheets on the line to fund the long term indemnity required to pursue the Trustee’s claims derivatively.
- In contrast, the Institutional Investors were the *only* group of investors who *had* organized themselves for the purpose of litigating the Trustee’s claims. They:
 - amassed the requisite voting rights,
 - possessed the required financial resources to offer a satisfactory indemnity, *and*
 - sent the required notice to trigger the running of the time periods required to permit them to pursue the Trustee’s claims by sending the Notice of Non-Performance.
- Though the Institutional Investors’ activities were the subject of multiple press releases and much media attention,⁵⁶ not a single one of the objectors has alleged it sought to join the Institutional Investors’ group but was rebuffed.

⁵⁵ In contrast to the openness of the Institutional Investors, the objectors’ activities have been far more secretive and opaque. *See infra*, Part III(F).

⁵⁶ *See* ¶72, *infra* (listing press releases and other disclosures).

- None of the objectors has alleged that they made—or were willing to make—any effort to reform and cure mortgage servicing deficiencies for the *common benefit* of all Certificateholders.
- None of the objectors has alleged that they offered the Trustee a plan to improve mortgage servicing so that borrowers would have an easier route to returning their loans to performing status.

71. Some objectors and observers have made the fatuous suggestion that the Trustee was required to “notify” other Certificateholders and “invite them” into the discussions. Nothing in the law or the PSA requires this. Every investor in these certificates understood that a group of holders of 25% of the Voting Rights, willing to provide a robust indemnity, *could* invoke their right to direct the Trustee to act *without* notice to any other Certificateholders. The PSAs do not require investors who do so to thereafter consult with (or obtain the consent of) investors who are bearing none of the risks and who have assumed none of the financial burdens associated with the indemnity. The agreements and the law impose no such requirement on the Trustee, either.

72. To be clear: the Institutional Investors issued regular press releases informing other investors of their activities and advising them that forbearance agreements had been entered tolling claims for some, but not all, of the Trusts. Bank of America also issued press releases and discussed ongoing settlement negotiations in its public filings. In total, the Institutional Investors and Bank of America issued at least 10 press releases or other disclosures informing the market of the ongoing negotiations:

- September 3, 2010, Institutional Investors’ press release announcing the instruction to the Trustee to take action. A copy is attached as Ex. 6.
- On October 18, 2010, counsel for the Institutional Investors sent Bank of America, Countrywide and the Trustee a letter alleging a variety of claims alleging improper handling of mortgages in the trusts. The Institutional Investors

issued a press release regarding the letter, which identified the Trusts to which it applied. A copy of the October 18, 2010 letter is attached as Ex.9, and a copy of the press release is attached as Ex. 8.

- The October 18 letter was reprinted in the New York Times's DealBook and received widespread coverage in the financial press. A compilation of selected articles reporting on the October 18 letter is attached as Ex. 10 (the New York Times's DealBook article is at pp. 35-49).
- Following the October 18 letter, the Institutional Investors' counsel received calls from entities interested in joining the Institutional Investor group. Over time, the group added an additional 14 entities.
- December 15, 2010, Bank of America issued a press release that notified the public of the "constructive dialogue" Bank of America was having with the Trustee and counsel for the Institutional Investors regarding the claims the Institutional Investors had raised, and that the parties had agreed to toll any time periods raised by the October 18, 2010 letter to "continue" that dialogue. A copy of Bank of America's press release, which lists the trusts covered by the tolling agreement, is attached as Ex. 11.
- Bank of America's December 15, 2010 announcement was widely covered in the press, which reported that Bank of America was in settlement talks with a group that had "expanded" and "now includes 17 investors and 167 bond deals." There was additional press coverage of the announcement of continued talks again in early-January 2011, in connection with Bank of America's separate settlement of

certain GSE-repurchase claims. A compilation of selected articles reporting on the release is attached as Ex. 12 (quoted at p. 7).

- On a January 21, 2011 analyst call, Bank of America's then Chief Financial Officer indicated that Bank of America was open to discussions with interested parties: "we always want to talk to everybody in the world to make sure we understand where they stand." This invitation to investors was widely reported in the press. A copy of the transcript from the analyst call is attached as Ex. 13 (quote at p. 11).
- On January 28, 2011, counsel for the Institutional Investors issued a press release stating that the parties had agreed to toll any time periods commenced by the Institutional Investors' October 18, 2010 letter discussing alleged Countrywide defaults, an obvious indication that discussions were ongoing. This press release identifies the trusts covered by the tolling agreement. A copy of the January 28, 2011 press release is attached as Ex. 14.
- On February 2, 2011, Bloomberg reported that the Institutional Investors had agreed to renew "their extensions of any time periods" in the October 18, 2010 letter alleging an Event of Default, and that Bank of America "confirmed that discussions were continuing." A copy of the Bloomberg article is attached as Ex. 15.
- Throughout the winter, newspapers continued to report on the settlement negotiations. For example, a February 15, 2011 article in Debtwire reported that the settlement being negotiated "could bind other CFC [Countrywide Financial Corporation] RMBS investors" and that the parties were "attempting to

encompass all Countrywide RMBS into the deal.” A compilation of this article along with other press reports that appeared at the time is attached as Ex. 16. (the Debtwire article is at pp. 3-5)

- Another article, appearing on February 23, 2011, quoted David Grais, Esq., of Grais & Ellsworth, counsel for objectors now alleging “secrecy”, as stating that an agreement among the negotiating parties “could bind all non-agency mortgage backed securities issued by Countrywide, BofA and potentially Merrill Lynch.” A copy of this article is attached as Ex. 16, p. 6-7.
- On February 25, 2011, Bank of America released its 10-K. In that document, the Bank stated that “BAC Home Loans Servicing, LP and Gibbs & Bruns LLP on behalf of certain investors including those who signed the letter, as well as The Bank of New York Mellon, as trustee, have agreed to a short extension of any time periods commenced by the letter to permit the parties to explore dialogue around the issues raised.” An excerpted copy of Bank of America’s 10-K is attached as Ex. 17.
- On February 28, 2011, a Bloomberg article reported that the amount of debt the Institutional Investor group represented had almost doubled since October and that the number of deals had grown to 225, due to more investors joining the group. Citing the Institutional Investors’ counsel, the article explains that “[t]he investors have only considered a settlement that pays through the mortgage trust, a channel that would serve even the bondholders Patrick doesn’t represent” and that “enough progress” had been made in negotiations “to warrant continued talks.” (Emphasis added.) A copy of the article is attached as Ex. 16, p.8-9.

- On March 31, 2011, counsel for the Institutional Investors again publicly reported that the parties had agreed to toll any time periods commenced by the Institutional Investors' October 18 letter discussing alleged Countrywide defaults. A copy of the press release issued by the Institutional Investors' counsel, which identifies the trusts covered by the tolling agreement, is attached as Ex. 18.
- On May 5, 2011, Bank of America issued its 10-Q for the first quarter 2011. In that document, the Bank stated that “[t]o permit the parties to discuss the issues raised by the letter, BAC Home Loans Servicing, LP and [Gibbs & Bruns LLP] on behalf of certain investors including those who signed the letter, as well as The Bank of New York Mellon, as trustee, have entered into multiple extensions to toll . . . [the time] periods commenced by the letter. We are in discussions with [Gibbs & Bruns], the investors and the trustee regarding the issues raised and more recently the parties have discussed possible concepts for resolution of any potential representations and warranties, servicing or other claims.” An excerpted copy of Bank of America’s 10-Q is attached as Exhibit 19.

73. Not a single one of the objectors has asserted it was unaware of these press releases. Not a single one has alleged that they, in a similarly open and obvious fashion, disclosed their efforts (if, indeed, they made any) to pursue claims for the Trusts. Nor have any objectors alleged that they informed the Institutional Investors, or anyone else, of any of their efforts to negotiate separate settlements with Bank of America and/or BNY Mellon—though such efforts plainly occurred and may indeed be continuing without the Court’s knowledge.

74. The Trustee was entitled to consider the obvious facts that affected the likelihood that one or more investor groups might seek to pursue the Trustee’s claims. The Institutional

Investors were organized. They had retained experienced trial counsel. They were moving forward aggressively, and publicly, to pursue the Trustee's claims. They had notified other investors they were doing so. They presented a credible threat of "hand to hand combat" to achieve a litigated recovery for the Trusts. The Trustee was also entitled to consider that investors who stood on the sidelines, unwilling to provide an indemnity to the Trustee, or those who would later seek a quick recovery for one or two trusts to serve their own interests rather than the common benefit of all Certificateholders, did not pose a credible threat. In these circumstances, it would be *unusual*—and inconsistent with the contract requirements—for BNY Mellon to invite other, unknown Certificateholders to participate in settlement negotiations when they had expressed neither an interest in, nor the willingness to pursue, the Trustee's claims.⁵⁷

C. The Institutional Investors Did Not Seek, Or Obtain, Any Individual Benefit.

75. Though the Institutional Investors were instrumental in forcing Bank of America and BNY Mellon to the negotiating table, they will receive the same benefit under the settlement that any similarly situated investor would receive, no more and no less. The settlement proceeds will flow down the waterfall, in accordance with the contract to which every investor agreed. As a result, pro rata amount of this settlement will likely flow to investors who did *nothing* to pursue the Trustee's claims. Even though they took no risks and invested no time or money, these investors will receive the same benefit as those who did.

76. This "free rider" problem is inherent in the structure of the Pooling and Servicing Agreements. Precisely because the agreements *require* collective action and *preclude* individual

⁵⁷ We address in Part III(F) below the false claims by AIG and Walnut Place that they were excluded from participating in settlement discussions. Whatever communications these entities may have had with BNY Mellon or Bank of America, they never contacted the Institutional Investors to express a desire to join the group or participate with them in efforts to obtain a recovery for the Trusts claims.

benefit at the expense of other Certificateholders, they create barriers to the effective assertion of the Trustee's claims by Certificateholders. Under the PSAs, an investor (or group of investors) that seeks to pursue the Trustee's claims must commit itself to bear 100% of the costs to do so,⁵⁸ even though it will receive only its ratable share of any recovery. In any Trust where an investor holds less than 100% of the certificates, the risk reward ratio is skewed to make it less likely the claims will be pursued, or pursued effectively. That, too, is a factor the Court should consider in assessing whether the objectors' litigation preference actually represents a feasible alternative.

D. The Trustee's Alleged Conflict

77. Eleven of the objectors assert that the settlement process was flawed because the Trustee was conflicted, allegedly because it stood to gain an expanded indemnification upon entering into the settlement. *See, e.g.,* Western & Southern Life Ins. Co. *et al.* Objection, St. Doc. #85 at 3. This is false. The indemnity the Trustee received in the settlement was no more and no less than the indemnity it was *already* entitled to receive under the contract. *Compare* PSA §§ 8.02 and 8.05 (requirement of Master Servicer indemnity) *with* Indemnity Confirmation from Master Servicer at Settlement Agreement Ex. C.

78. Another variant of the "conflict" claim is the contention that the Settlement Agreement indemnified the Trustee for any breach of fiduciary duty arising from entry into the settlement: "[T]he relief sought here appears designed largely to insulate BNYM from fiduciary

⁵⁸ These costs are very high. *See, e.g.,* Ex. 20, Royal Bank of Scotland, *Non-Agency MBS Loan Repurchases: Practical Considerations*, Sept. 17, 2010 (estimating that "without litigation, the cost could range from \$24 million to \$88 million" just to review loan files, make demands and comply with initial cure periods . . ." on the 229,000 loans in the 55 deals then at issue in the Institutional Investors' instruction to BNY Mellon). Extrapolating from that cost, to cover the more than 770,000 loans at issue in the settled trusts, yields a potential out of pocket cost—again exclusive of litigation expense and delay—of between \$42.5 and \$149.6 million. None of the objectors has offered an indemnity sufficient to defray that cost (even assuming they held 25% of all Trusts), much less the years of attorneys' fees that would be incurred to evaluate and prosecute claims on those loans.

claims arising from the settlement.” N.Y.A.G. Objection, St. Doc. #101-4 at 4. This is incorrect. The Settlement Agreement does not release any claim of breach of fiduciary duty against the Trustee. *See* Settlement Agreement at ¶ 9(a) (reciting releases *by* the Trustee but granting none *to* the Trustee). The settlement also does not release any individual tort, fraud or securities claims against either BNY Mellon or Bank of America. *See* Settlement Agreement at ¶¶ 9 and 10. The Trustee is not seeking—and will not obtain—any release of breach of fiduciary duty or fraud claims in the proposed judgment contemplated by the settlement. *Id.* at Ex. B. Nowhere in the Settlement Agreement has the Trustee been indemnified for breaching any fiduciary duty by entering into the settlement. *Id.* Importantly, the PSAs are not amended by the Settlement Agreement, *see* Settlement Agreement at ¶ 21, and they state plainly that “[n]o provision of this Agreement shall be construed to relieve the Trustee from liability for its own negligent action, its own negligent failure to act or its own willful misconduct . . .” PSA § 8.01.

E. The Trustee Is Entitled to Seek an Instruction Concerning Whether to Consummate the Settlement.

79. Certain objectors have argued that the Trustee’s use of an Article 77 Proceeding to seek court approval of the settlement was improper. The Court has also observed that, “Without exception, the often-uncontested proceedings described in these decisions and orders were garden-variety matters of trust administration.” The objectors’ argument, and the Court’s observation, are each incorrect. A leading case recognizing the right of a trustee to seek court approval of a settlement of commercial litigation, in the face of a heated dispute among bondholders in a securitized trust, is a New York case arising under Article 77. *See In re Application of IBJ Schroder*, 271 A.D. at 322.⁵⁹ This case involved substantial litigation, as its

⁵⁹ This decision was attached as Ex. D to the Trustee’s reply brief and was discussed at length in the reply briefs filed by the Trustee and the Institutional Investors in support of their motion to remand. Rather than restate those arguments here, we incorporate them by reference.

procedural history involves an appeal to and decision by the First Department prior to a final decision by the New York Supreme Court approving the Trustee's decision to enter into the settlement.

80. New York and federal case law recognize that seeking an instruction is exactly what a Trustee *should* do when it: a) faces conflicting instructions from beneficiaries about what to do or b) is itself conflicted regarding a given course of action. In *Redmond v. Commerce Trust Co.*, 144 F.2d 140, 154-55 (8th Cir. 1944), the court recognized the propriety of Trustee's decision to seek court approval to consummate a settlement: "Where it is reasonably prudent, in the exercise of good faith sound judgment, to make a contract of compromise, the trustee may do so but, if such compromise is made without proper court approval, the trustee takes the risk of his good faith and sound judgment being attacked successfully by the beneficiaries. If the compromise is made only upon proper court approval, the trustee may safely do so and such is binding upon the beneficiaries." The New York Court of Appeals⁶⁰ recognized that even a self-dealing trustee may proceed with a conflicted transaction, if it does so with court approval. "The rule has long been established that a trustee 'should not be allowed to become a purchaser of trust property, because of the danger in such a case that the interest of the beneficiary might be prejudiced. However, there is little danger of such prejudice if the transaction is subjected to prior judicial scrutiny and given court approval. Accordingly, the rule against self-dealing has not been applied, *and does not apply*, to interdict the purchase of trust property by a trustee where the court, after conducting a full adversary hearing at which all interested parties are represented, approves and authorizes the sale." *In the Matter of Scarborough Properties Corp.*,

⁶⁰ In this removed, state court proceeding which arose under state law, the Court is required to apply the substantive law of New York as established by the New York Court of Appeals.

255 N.E.2d 761, 25 N.Y.2d 553 (N.Y. 1969) (emphasis added and citations omitted). The right of a trustee to conditionally agree to a settlement, subject to court approval of its decision to do so, is so well-settled that it has been incorporated into the RESTATEMENT (SECOND) OF TRUSTS. *See id.* at §292 cmt. d (2010) (“If the trustee is in doubt whether he should compromise or submit to arbitration a claim, he may ask the instruction of the court or he may agree thereto conditionally upon the subsequent approval of the court.”).

81. The Trustee followed this clear law when it filed a proceeding seeking an instruction about whether it should consummate the settlement. The case filed in New York state court, which has now been removed to this court, was one in which all interested parties could be heard. It raises a single issue appropriate for resolution by a court: is the Trustee’s decision to settle reasonable? That the case is now pending in federal court does not change its fundamental nature. It also does not negate the Trustee’s right to obtain that which it is entitled to obtain under governing New York law; namely, an instruction concerning whether it is entitled to proceed with this settlement of disputed claims.

82. The above discussion should put to rest the belated complaints by some Certificateholders that the Trustee failed to include them in settlement discussions. Even if there had been a way to include all Certificateholders in the settlement negotiations, the objectors’ pleadings make clear that no consensus could have been reached. The Trustee would then have had no option but to do exactly what it did: make a good faith decision about whether to settle in the face of competing demands and then seek court approval of its decision.

F. The Settlement Was Not “Clandestine” or “Collusive”

83. AIG and a handful of other objectors have suggested that the Institutional Investors somehow “colluded” with Bank of America in negotiating the settlement. *See, e.g.,*

AIG Objection, St. Doc. #131 at 5-6. This is false. The attack on the Institutional Investors is also beyond absurd when the Court considers the illogical inferences on which it rests.

84. Eight of the Institutional Investors are independent investment advisers. They will receive not a penny of this settlement for themselves; the recovery will go to their clients. These investment advisers are competitors with one another. Many are competitors with Bank of America. The bizarre suggestion that they would abandon their fiduciary and contractual obligations to their clients in an effort to “help” Bank of America is an irrational inference the Court should dismiss out of hand. *See Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007) (explaining that to survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to “state a claim to relief that is *plausible* on its face”); *Ashcroft v. Iqbal*, 556 U.S. 662 (2009) (“A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.”) (citations omitted). The claim of collusions enter the realm of fantasy when it adds to the claimed cabal not only eight independent investment advisers but seven insurance companies, who hold these securities largely to fund policy payments to insurance and pension beneficiaries. Neither the insurance companies nor the investment advisers have a possible motive to take *less* than a fair settlement, anymore than do the other Institutional Investors who appear here to support the settlement.

85. The simple fact is this: these investment advisers and the other Institutional Investors joined together precisely because, in the absence of a decision to cooperate, there was no way to aggregate the Voting Rights required to pursue litigation of the Trustee's claims derivatively, for their clients' benefit. Had they not done so, it is highly likely that none of these

claims would have been pursued at all.⁶¹ Under every potentially applicable pleading standard, these claims of collusion fail as a matter of law.

1. Newly Revealed AIG Documents Refute Its “Clandestine” Negotiation Claim.

86. AIG’s claims that the settlement was “clandestine” or “exclusive,” *see* AIG Objection, St. Doc. #131 at 5-6, are especially baseless in light of recent disclosures in AIG’s securities lawsuit against Bank of America (filed on the same day as its objection to the settlement). Newly filed pleadings in that action *directly refute* AIG’s contention that it was “kept in the dark by BoNY and the Inside Institutional Investors.” *Id.* at 6. *See* Defendants’ Motion to Disqualify Quinn Emmanuel as Counsel For Plaintiffs, Docs. #37, 39, and 42, No. 11-cv-06212 (S.D.N.Y.). In a letter attached as evidence to this motion, Quinn’s disqualification counsel states—on behalf of AIG and its counsel, Quinn Emmanuel—that “in March or April [2011], AIG rejected [Bank of America’s] express request that AIG stop seeking advice from Quinn Emanuel as a condition of allowing AIG access to settlement talks between [Bank of America] and certain institutional investors.” *Id.* at Doc. #42, Ex. F to Dworsky Declaration, p. 4. This letter establishes two facts that refute AIG’s claim of clandestine negotiation. First, by its own admission, AIG knew about the ongoing “settlement talks.” Second, again by its own admission, *if* AIG was excluded from settlement discussions, it was excluded by *Bank of*

⁶¹ Even today, no group of holders has stepped forward to offer to fund the hundreds of millions of dollars in litigation costs necessary to pursue the Trustee’s claims. *Compare* RBS Report re Likely Cost of Litigation. Though Walnut Place has alleged it is willing to pursue claims for three trusts, the Court can have no confidence that an anonymous LLC formed specifically for the purpose of litigation has either the financial wherewithal—or the staying power—to litigate hotly contested claims for years.

America, due to an alleged conflict on the part of AIG's counsel. Neither the Institutional Investors nor the Trustee limited AIG's access to the settlement talks.⁶²

87. The AIG letter should be scrutinized closely by the Court for another reason. In it, AIG acknowledges that it attended a mediation with Bank of America "in July of 2011." *Id.* at 4. The mediation obviously occurred *after* the settlement in this matter was announced on June 29, 2011. See 22 *Institutional Investors in Countrywide-Issued RMBS Announce Global Settlement*, PR NEWswire, June 29, 2011, attached as Ex. 21. AIG's objection was filed on August 8, 2011, less than a month after it was unable to obtain an *individual* settlement with Bank of America in the "July of 2011" mediation. Given the strictures of Section 10.08 of the PSAs, and the prohibition on invoking rights under the agreement to advance "individual and conflicting interests," *Inkeepers*, 448 B.R. at 145, the contents of AIG's letter are cause to question whether AIG's objection is in good faith or seeks the common benefit of all Certificateholders.

88. AIG also questions the attorneys' fee that will be paid to the Institutional Investors' counsel if the settlement is approved. It is normal and customary for counsel to be paid for their work. The fee to be paid is markedly lower than the fees paid to counsel who achieved similar results in complex, high stakes cases.⁶³ The fee is also significantly lower than the contingent fee the Institutional Investors were prepared to instruct the Trustee to accept, if it had become necessary to pursue contested litigation on behalf of the Trusts. When paid, the fee will be in addition to, rather than out of, the settlement payment. That benefits investors in the

⁶² To reiterate, AIG has not alleged that it ever contacted either the Institutional Investors' counsel or counsel for BNY Mellon to ask to participate in the ongoing settlement discussion with Bank of America.

⁶³ See Ex. 22, Cases of Comparable Size and Complexity Ranked by Attorneys' Fee.

Trusts, who will receive a superb settlement at no cost to them or the Trusts. The payment of fees in addition to the settlement amount is also in keeping with Section 2.03 of the PSAs, which permits the Trustee to recover not only the Purchase Price for ineligible mortgages but also “any expenses reasonably incurred by . . . the Trustee in respect of enforcing the remedies for such breach.”

2. Walnut Place Also Knew of Settlement Discussions But Refused to Participate

89. The secrecy allegations in the Walnut Place objection are particularly questionable, since its counsel — the Grais & Ellsworth firm — was provided with personal, first-hand information about ongoing settlement negotiations by both Bank of America and BNY Mellon⁶⁴

90. Walnut Place’s initial allegation was that “BNYM made no effort to inform Walnut Place” of the ongoing settlement negotiations. In response, the Trustee’s counsel submitted a sworn declaration attesting that, to the contrary, on February 2, 2011, counsel for Walnut Place met with counsel for the Trustee, as well as counsel for Bank of America. During this meeting, counsel for the Trustee and counsel for Bank of America each “told counsel for Walnut Place that they were negotiating a settlement, . . . offered to report to Walnut Place on a current and ongoing basis about settlement discussions, [and] invited Walnut Place to provide input on settlement discussions. Walnut Place refused, and instead filed a lawsuit asserting claims against Countrywide, Bank of America and BNY Mellon (as nominal defendant) that are intended to be released by the Settlement.” St. Doc. #43. Simply put, if the settlement

⁶⁴ The Institutional Investors did not participate in these private discussions with Walnut. What follows has been assembled from what has come to light since the settlement was announced.

negotiations took place behind Walnut Place's back, that is because Walnut Place turned its back on those negotiations.

91. Walnut's counsel told newspaper reporters as far back as mid-February that he was evaluating "potential recourse against [BNY Mellon] in case it participates in the settlement." (That news article goes on to report in further detail BNY Mellon's involvement in the Settlement.). *See* Ex. 16, p. 3-5. Furthermore, though Walnut Place claims that it was not informed that the negotiations involved the two Trusts in which Walnut Place holds positions,⁶⁵ that claim is likewise unsupportable. Walnut Place's counsel declared in open court at the August 5, 2011 hearing in the Settlement Court that "*the express purpose*" behind the filing of its February 2011 lawsuit against Countrywide and the Trustee was "*to stop the settlement*" from extinguishing Walnut Place's claims.⁶⁶

3. Knights of Columbus

92. Similar allegations made in the Knights of Columbus objection are equally meritless. The Knights of Columbus claims it was not personally informed by the Trustee of the settlement negotiations in correspondence about its separate lawsuit against the Trustee.⁶⁷ Given the widespread public reports on the settlement negotiations, it is implausible for Knights of Columbus to suggest that it was unaware of the negotiations. In fact, four of the Trusts in which the Knights of Columbus claims to own certificates — CWALT 2005-6CB, CWHL 2005-30,

⁶⁵ Walnut Place Reply at 5 (St. Doc. #49).

⁶⁶ *See* Ex. 23 (Transcript of August 5, 2011 hearing) at 33:20-23.

⁶⁷ *See* Knights of Columbus Objection at 2-3, 7-11 (St. Doc. #141).

CWHL 2004-14, and CWHL 2006-6 — were named in the press releases issued by Bank of America and Gibbs & Bruns regarding the settlement negotiations.⁶⁸

G. Miscellaneous Objections

1. Allocation Issues

93. The proposed settlement allocation, both among the trusts and across the tranches of any individual trust, is the subject of nine objections. In general, these objectors ask why the settlement documents do not specify the amounts that any given trust or tranche will actually receive when the settlement is eventually approved. The Federal Home Loan Banks, for example, complain that “[i]n addition, the Banks need more information about the way in which the settlement fund would be allocated.” FHLB Objection, St. Doc. #55 at 4.

94. These objections are in error. The methodology for allocating the Settlement Payment is described in detail in the Settlement Agreement and described precisely in the Trustee’s filings. *See* Ex. 25 (Settlement Agreement) at ¶ 3(c). Specifically, the Trustee’s independent allocation expert, NERA, will allocate the Settlement Payment among the Covered Trusts according to the amount of net realized and projected losses in each of the trusts. *Id.* at 55. NERA will determine the amount of net losses based on past losses and estimates of future losses (using models to determine the projected performance of the loans in the Covered Trusts and the loss severity on those loans). *Id.* A copy of NERA’s methodology was attached as Exhibit E to the Trustee’s Verified Petition, and is also attached as Ex. 24. The reason an allocation is not available now is simple: the allocation is based on losses of each, individual

⁶⁸ *See* Ex. 8 (October 18, 2010 Gibbs & Bruns LLP press release) (naming CWHL 2005-30); Ex. 11 (December 15, 2010 Bank of America press release) (naming CWALT 2005-6CB and CWHL 2005-30); Ex. 14 (January 28, 2011 Gibbs & Bruns LLP press release) (naming all four trusts); Ex. 18 (March 31, 2011 Gibbs & Bruns LLP press release) (same). The trusts that Knights of Columbus allegedly holds certificates in are listed on Exhibit 1 to the Affirmation of Peter N. Tsapatsaris (St. Doc. #145).

Trust. That figure is constantly evolving and could vary considerably between the time the Settlement Agreement was signed and the date on which the settlement is approved, particularly if the approval process is protracted. The Trustee made a reasonable decision to avoid preventing potentially misleading preliminary calculations that might confuse investors. Equally in error is the suggestion that the settlement does not inform investors how it will be allocated among tranches in a given trust. There was no need to include this in the settlement, because the distribution mechanisms in each PSA already provide for the treatment of “Subsequent Recoveries.” The Settlement Agreement confirms that the payment would flow down the tranches in each Trust in accordance with the existing waterfall in each PSA. *Id.* at ¶ 3(d)(i)-(vi). This was consistent with investors’ expectations and rights under the PSAs.

2. Waterfall Issue

95. A related set of objections concerns the use of the payment waterfall in the Governing Agreements to distribute settlement funds. One such objection complains that “the settlement fund is allocated among investors in accordance with the ‘payment waterfall’ set forth in the Pooling and Servicing Agreements, which may provide some investors with a windfall and may not appropriately compensate others for their actual loss.” *See* Policeman’s Annuity & Benefit Fund of Chicago Objection, St. Doc. #32 at 4; *see also* Clayhill Investors LLC Objection, St. Doc. #180 at 2; The Western & Southern Life Ins. Co. *et al.* Objection, St. Doc. #085 at 3. This form of payment is not an optional or negotiated matter: “[t]hat payment stream is required by the governing agreements, to which all Certificateholders agreed when they purchased trust certificates, and the Trustee is required to follow that agreement when it disburses funds that flow into the trusts.” *See* Mem. of Institutional Investors in Opposition to the Policemen’s Annuity’s Motion to Intervene, St. Doc. #45 at 5. As the New York Supreme Court recently held in a similar context, noteholders “are bound by the agreements that they

made.” *ASR Levensverzekering NV v. Swiss Re Fin. Prods. Corp.*, Index No. 650557/09, slip op. at 7 (N.Y. Sup. Ct. Oct. 11, 2011); *see also Greenwich, supra* and *Innkeepers, supra*. This includes the contract terms establishing the payment waterfall. The use of the waterfall as a distribution mechanism is not only proper, it is required.

3. Former Holders

96. Other objectors claim that former Certificateholders should receive compensation or that initial purchasers should receive greater compensation than secondary-market purchasers. Those contentions seem to miss the point of the settlement entirely. The Settlement Agreement is a settlement of contract-based claims. The contracts provide no entitlements to former Certificateholders; all benefits flowing from the contracts transferred to the Certificateholders that purchased from the former holders. Likewise, the contracts provide no additional entitlements to original purchasers compared to secondary-market purchasers of the certificates. Regardless of when Certificateholders purchased their securities, they purchased the same exact bundle of contract rights under the PSAs. The Settlement treats all contract-right holders the same. There is nothing unreasonable about that.

More fundamentally, none of the allocation objections should bar Final Court Approval of the Settlement, regardless of what the Settlement Court determines is a reasonable allocation within each Covered Trust. The Settlement Agreement specifically provides that changes to the distribution method within each of the Covered Trusts will not constitute material changes to the terms of the Settlement. *See* Ex. 25 (Settlement Agreement) ¶ 3(d)(v). Accordingly, if the Settlement Court determines that a distribution according to the terms of the PSAs is not reasonable, it is free to refashion those distribution provisions accordingly.

4. Rights of Monoline and Financial Guaranty Insurers

97. Two monoline insurers, Syncora Guarantee Inc. and Ambac, and one financial guaranty insurer, CIFG, wrapped certain tranches in certain of the 530 settled Trusts or insured certain losses in one or more Trusts. They have appeared as objectors solely to confirm that the Settlement Agreement does not prejudice their rights to pursue recovery under their own insurance contracts with BOA and CW. The Settlement Agreement fully preserves these separate contract rights. *See id.* at ¶ 10(d) (“To the extent that any third-party guarantor or financial-guaranty provider with respect to any Covered Trust has rights or obligations independent of the rights or obligations of the Investors, the Trustee, or the Covered Trusts, the release and waiver in Paragraph 9 is not intended to and shall not release such rights, or impair or diminish in any respect such obligations or any insurance of indemnity obligation owed by or to any such Person). The agreement thus states plainly that it does not compromise or affect the monolines’ independent contract rights.

5. Homeowners’ Class Action

The final objection is filed by a purported class of homeowners. *See* Mary Ellen Iesu et al. Objection (Doc. #17). It is not cognizable here. The homeowners are neither parties to the PSAs nor holders of certificates issued by the Trusts. They therefore lack standing to appear in this proceeding. Respectfully submitted,

Dated: New York, New York
October 31, 2011

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