

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

In the matter of the application of

THE BANK OF NEW YORK MELLON, (as Trustee under various Pooling and Servicing Agreements and Indenture Trustee under various Indentures), BlackRock Financial Management Inc. (intervenor), Kore Advisors, L.P. (intervenor), Maiden Lane, LLC (intervenor), Maiden Lane II, LLC (intervenor), Maiden Lane III, LLC (intervenor), Metropolitan Life Insurance Company (intervenor), Trust Company of the West and affiliated companies controlled by The TCW Group, Inc. (intervenor), Neuberger Berman Europe Limited (intervenor), Pacific Investment Management Company LLC (intervenor), Goldman Sachs Asset Management, L.P. (intervenor), Teachers Insurance and Annuity Association of America (intervenor), Invesco Advisers, Inc. (intervenor), Thrivent Financial for Lutherans (intervenor), Landesbank Baden-Wuerttemberg (intervenor), LBBW Asset Management (Ireland) plc, Dublin (intervenor), ING Bank fsb (intervenor), ING Capital LLC (intervenor), ING Investment Management LLC (intervenor), New York Life Investment Management LLC (intervenor), Nationwide Mutual Insurance Company and its affiliated companies (intervenor), 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 (intervenor), Federal Home Loan Bank of Atlanta (intervenor), Bayerische Landesbank (intervenor), Prudential Investment Management, Inc. (intervenor), and Western Asset Management Company (intervenor)

Petitioners,

for an order pursuant to CPLR § 7701 seeking judicial instructions and approval of a proposed settlement.

Index No.
651786/2011

Assigned to:
Kapnick, J.

**MEMORANDUM OF THE DELAWARE DEPARTMENT OF JUSTICE IN
SUPPORT OF PETITION TO INTERVENE**

The Bank of New York Mellon (“BNYM”, or the “Trustee”) filed this Article 77 proceeding on June 29, 2011, to obtain judicial approval of a proposed \$8.5 billion settlement of the claims of 530 trusts (the “Covered Trusts”), including a small number of Delaware statutory trusts, for which BNYM serves as trustee or indenture trustee.

The Delaware Department of Justice objects to the approval of the proposed settlement. The claims that would be resolved and released by the proposed settlement

are related to breaches of the governing trust agreements by Countrywide Home Loans, Inc. and related selling entities (collectively “Countrywide”) and BAC Home Loans Servicing, LP, formerly Countrywide Home Loans Servicing, LP, and Bank of America (collectively “BoA”). Countrywide and BoA failed to comply with the standards of conduct governing the creation and administration of the Covered Trusts. These failures allowed for the widespread improper sale and securitization of residential mortgage loans, contributing to the collapse of the market for residential mortgage backed securities (“RMBS”), causing substantial harm to mortgage loan borrowers, investors and the integrity of the securities markets, and precipitating the financial crises in this country and the State of Delaware. The proposed settlement, if approved, would fully and finally resolve the claims of the Covered Trusts, including the Delaware statutory trusts, against Countrywide and BoA. *See* Settlement Agreement at ¶ 9. BNYM seeks to make that resolution binding upon all beneficiaries of the Covered Trusts, whether they are represented in this proceeding or even aware of it. *Id.* at ¶ 9. The proposed settlement may negatively affect the interests of homeowners who are likely to be harmed by the extra-contractual nature of the settlement. In seeking judicial approval of its actions as trustee, BNYM stands to gain from this settlement in that it may effectively extinguish claims that BNYM breached its duties as a New York trustee. Additional relevant facts relating to the background of the proposed settlement are more fully set forth in the Delaware Department of Justice's Amended Petition to Intervene (the “Petition”), filed herewith. *See* Petition at ¶¶ 6-16.

The Delaware Department of Justice intervenes in this proceeding: (i) pursuant to its authority as *parens patriae* to protect the public interest, including the interests of

absent investors and homeowners, as well as the integrity of the marketplace; and (ii) to protect potential state law claims that may be adversely affected if the proposed settlement is approved, including claims for securities fraud and deceptive trade practices, against BNYM, BoA or Countrywide, arising out of the conduct covered by the potential settlement. This is the Delaware Department of Justice's Memorandum of Law in support of his Petition to Intervene pursuant to New York CPLR 401, 1012 and 1013.

ARGUMENT

Interested parties may intervene in an Article 77 proceeding with leave of the Court. CPLR 401. Pursuant to CPLR 1012(a), intervention by a party shall be permitted as a matter of right if “the representation of the person's interest by the parties is or may be inadequate and the person is or may be bound by the judgment.” Intervention is permissible pursuant to CPLR 1013 if “the person's claim or defense and the main action have a common question of law or fact . . . [and] the intervention will [not] unduly delay the determination of the action or prejudice the substantial rights of any party.”

I. THE INTERVENTION OF THE DELAWARE DEPARTMENT OF JUSTICE IS NECESSARY TO PROTECT THE PUBLIC INTEREST

This proceeding, while narrowly characterized by the petitioner as an inquiry into the reasonableness of its conduct in reaching the proposed settlement, will have a significant impact on many different interested parties. The relief sought by BNYM in this proceeding contains broad language¹ suggesting that unrepresented beneficiaries,

¹ BNYM's Proposed Order and Judgment states that it would bind "all Trust Beneficiaries . . . , and any Persons claiming by, through, or on behalf of any of the Trustee, the Trust Beneficiaries, or the Covered Trusts . . . are bound by this Final Order and Judgment", to a finding that "[t]he Trustee acted in good faith . . . " and would "bar[] and enjoin[] [those parties] from instituting, commencing, or prosecuting, any suit, proceeding, or other action asserting against the Trustee any claims arising from or in connection with the

including Delaware investors, “may be bound by the judgment.” CPLR 1012(a)(3). The proposed settlement also contains a sweeping release of claims provision, under which all trust beneficiaries' claims are fully and finally resolved by the terms of the agreement whether or not they are represented in this proceeding. *See* Settlement Agreement at ¶ 9. This settlement will significantly impact homeowners whose mortgage loans are owned by the Covered Trusts. This unrepresented class is comprised of Delaware citizens, New York citizens, and citizens of every other state in the country. The alleged breaches of representations and warranties here did not simply decrease the value of the trust certificates; they had real world consequences on homeowners. These homeowners, many of whom have faced or are now facing foreclosure at the hands of BoA as their mortgage servicer, will be affected by the results of this proceeding. Similarly, property values and the health of our broader economy will also be affected. The Delaware Department of Justice seeks to intervene to protect the interests of Delaware, including absent investors, homeowners and the economic well-being of Delaware citizens.

**A. The Attorney General Has Standing to Intervene Pursuant to his
Parens Patriae Authority**

It is well settled that a state attorney general has *parens patriae* standing in matters involving a quasi-sovereign interest implicating the protection of the safety, health or welfare of its citizens. *Alfred L. Snapp & Son, Inc. v. Puerto Rico*, 458 U.S. 592, 607. As is the case with other state attorneys general, the Delaware Department of Justice has a quasi-sovereign interest in protecting the integrity of the marketplace. *State*

Trustee's entry into the Settlement." (*See* Proposed Final Order and Judgment, Exhibit F to BNYM Petition).

v. 7040 Colonial Road Associates Co., 176 Misc. 2d 367, 374 (Sup. Ct. N.Y. Co. 1998). Similarly, the Delaware Department of Justice has a quasi-sovereign interest in protecting the investing public in Delaware from misleading statements or omissions in the purchase and sale of securities, and in seeking relief on behalf of individual (or institutional) investors who have been the victim of violations of the Delaware Securities Act. *See 6 Del. C. § 7301 (b)* (the Delaware Department of Justice has statutory authority to “remedy any harm caused by securities law violations”).

In fact, a state's interest in an honest marketplace is, in and of itself, a quasi-sovereign interest. *See State of Georgia v. Pennsylvania R. Co.*, 324 U.S. 439, 450-51 (1945) and *New York ex rel. Abrams v. Gen. Motors Corp.*, 547 F. Supp. 703, 705 (S.D.N.Y. 1982). Courts in several states have held that a State has a quasi-sovereign interest, for purposes of establishing *parens patriae* standing, in the economic well-being of its citizens. *See, e.g., Hood v. Microsoft Corp.*, 428 F. Supp.2d 537, 545 (S.D.MI 2006) (“[T]he State has a quasi-sovereign interest in the economic well-being of its citizens, which includes securing the integrity of the marketplace.”); *State of Louisiana v. Borden, Inc.*, 1995 WL 59548, at *2 (E.D.La. Feb. 10, 1995) (same); *State of Maine v. Data General Corp.*, 697 F.Supp 23, at *25 (D. Maine 1988) (“A state's interest in maintaining an honest marketplace is a quasi-sovereign interest, even where the state's action will also benefit individuals”) (citation omitted).

B. Protecting the Interests of Absent Investors and the Integrity of the Marketplace

Here, the Delaware Department of Justice has a quasi-sovereign interest in securing the integrity of the markets and protecting the interests of absent investors. This

interest was recognized by Judge Pauley when he granted the Delaware Department of Justice's motion to intervene when this matter was in the Southern District of New York. *Bank of New York Mellon v. Walnut Place, LLC*, 2011 WL 5843488, at *2 (S.D.N.Y. Nov. 18, 2011). In doing so, Judge Pauley noted that, with respect to the State's quasi-sovereign interest in an honest marketplace, "it is apodictic that the State AGs have *parens patriae* standing to protect citizens from breaches of fiduciary duty and to rectify those breaches." *Bank of New York Mellon v. Walnut Place, LLC*, 2011 WL 5843488, at *2 (S.D.N.Y. Nov. 18, 2011) (citing *People v. H&R Block, Inc.*, 847 N.Y.S.2d 903 (Table), at *8 (Sup. Ct. N.Y. Cnty. July 9, 2007)). BNYM has conceded that as trustee they have an undisputed duty to avoid conflicts of interest. *Bank of New York Mellon v. Walnut Place, LLC*, --- F.Supp.2d ----, 2011 WL 4953907, *9 (S.D.N.Y. 2011). Here, there is evidence to suggest that BNYM negotiated the settlement on behalf of unrepresented certificateholders under a conflict of interest. *See* Petition at ¶ 19.

C. Protecting the Interests of Homeowners and the Economic Well-Being of Delaware Residents

The Delaware Department of Justice also has a quasi-sovereign interest in protecting the interests of absent borrowers who will be significantly affected by this outcome of this proceeding. BNYM itself acknowledges that the prospective servicing changes implemented by the settlement will affect "hundreds of thousands of loans." *See* BNYM Petition at ¶ 10. Undoubtedly, thousands of Delaware homeowners, who have no voice in this settlement, absent the intervention of the Delaware Department of Justice, will be affected by the settlement's servicing provisions. *See* Settlement at ¶ 5. BNYM characterizes the settlement as requiring "meaningful mortgage loan servicing

improvements.” See BNYM Petition at ¶ 1 and ¶¶ 42-47. The proposed settlement’s servicing provisions are vague, permissive and will not necessarily provide value to investors or an incentive for servicers to fully explore loss mitigation options with struggling borrowers. See Petition at ¶ 22. The intervention of the Delaware Department of Justice is vital to ensuring that servicing changes will maximize value for certificateholders, have a positive impact on Delaware homeowners, and thereby stabilize the RMBS and housing markets and our broader economy.

Another way to protect investors, homeowners, and the economic well-being of Delaware residents, would be to align owner and servicer interests in the underlying mortgage loans by enforcing the repurchase provisions in the pooling and servicing agreements (“PSAs”)² that govern the Covered Trusts. Each PSA has a contractual mechanism that requires the repurchase of mortgage loans out of the relevant securitization when, as here, a valid representation and warranty claim has been asserted by the trust. See generally, Trust PSA ¶ 2.03[Ex B to NY Petition]. Using this mechanism honors the terms of the governing contract and has the same economic effect on investors in the trusts.³ At the same time this ensures that borrowers, whose homes may be at risk of foreclosure, avoid being the unintended losers in this settlement and instead obtain the benefits of having their loans putback to an entity that both has an

² According to the BNYM Petition at ¶ 3, “All but seventeen of the trusts are evidenced by separate contracts known as Pooling and Servicing Agreements (the “PSAs”) under which BNY Mellon is the trustee. The remainder are evidenced by indentures and related Sales and Servicing Agreements (“SSAs”) under which BNY Mellon is the indenture trustee.” We refer to the governing agreements collectively as PSAs.

³ The same economic effect could be achieved because the loans could be repurchased at par value as required in the pooling and servicing agreements, while BoA could be receive credit against the settlement amount for the difference between this repurchase price and the actual market value of the repurchased loans.

incentive to service them properly and is subject to defenses in foreclosure for misdeeds associated with origination of the loans.

BoA has financial incentives in its servicing of the loans in the Covered Trusts that are incompatible with maximizing long term loan value. For example, despite its obligation to service the loans in a manner to maximize value for the trusts, BoA also must advance delinquent payments to the trusts. One key way that BoA is able to recover delinquent payments is through foreclosure. *See generally* Trust PSA ¶¶ 3.01, 3.08, 3.11. [Ex B to NY Petition]. Thus, BoA may have an incentive to seek foreclosure even when a possible loan modification is likely to lead to a greater net recovery to the trust. If BoA were to repurchase the loans through the settlement, these skewed incentives would disappear, and BoA, as both owner and servicer, would have an incentive to keep borrowers in their homes through modifications or other means where this maximized the value of the loan over time.

Rather than following the contractual repurchase mechanisms provided for in the governing documents of the securitization as a vehicle to settle the Covered Trusts' claims, the proposed settlement instead calls for an extra-contractual cash payment without any transfer of interests in the mortgage loans. *See* Settlement Agreement at ¶ 3. This may have negative effect on Delaware borrowers who otherwise would be in a much stronger position to stay in their homes if their mortgage loans were repurchased and serviced by BoA. The housing market in Delaware and, thus, the economic well-being of Delaware residents, would also benefit from a situation where the owner of the loan was also responsible for servicing the loan and therefore had a financial incentive to

maximize the value of the loan through loss mitigation, rather than collecting fees associated with instituting a foreclosure proceeding.

II. THE DELAWARE DEPARTMENT OF JUSTICE SHOULD BE ALLOWED TO INTERVENE TO PRESERVE DELAWARE LAW CLAIMS.

While the Delaware Department of Justice has limited information regarding the merits of the settlement, the details of the potential misconduct leading to the proposed settlement are widely reported. The Delaware Department of Justice therefore has a legitimate basis upon which to assume, pending verification through confirmatory discovery, that Delaware's interests may adversely be affected by the proposed settlement.

A. The Delaware Department of Justice's Potential Claims May Be Impaired by a Judgment in This Proceeding

The Delaware Department of Justice has a unique interest in protecting the Delaware interests that potentially are affected by the proposed settlement. Intervention pursuant to CPLR 1012 or 1013 is appropriate because BNYM, Countrywide, or BoA may take the position that the settlement and the facts found by this court, if made binding upon all beneficiaries, precludes the Delaware Department of Justice from pursuing certain claims or remedies for such violations. While the Delaware Department of Justice's potential claims, including any securities fraud, consumer fraud and deceptive trade practices claims, should fall within the definition of "claims not released" in the proposed settlement agreement (§ 10(c)), there is no guarantee that BNYM, Countrywide or BoA would not assert that the Delaware Department of Justice's claims are barred by the terms of the proposed settlement, once approved.

B. Questions Presented by the Delaware Department of Justice's Claims Are Similar to Questions Presented by This Proceeding

Even if the Delaware Department of Justice is not entitled to intervene as a matter of right, the Delaware Department of Justice should be permitted to intervene because the claims that it might assert against BNYM, Countrywide, or BoA on behalf of the relevant Delaware interests share “common questions of law or fact” with this proceeding. CPLR 1013.

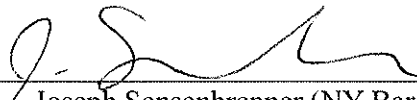
This proceeding will address the question of whether BNYM breached its fiduciary duty in negotiating the settlement and whether the settlement is fair and reasonable. *See* Settlement Ex. B (Proposed Order and Judgment) ¶ (k) (proposing finding that the “[BNYM] acted in good faith, within its discretion, and within the bounds of reasonableness in determining that the Settlement Agreement was in the best interests of the Covered Trusts.”) In addressing these issues, the proceeding necessarily will address the merits and likelihood of success of investors' claims against Countrywide and BoA. Such claims contain common questions of law or fact with the Delaware Department of Justice's potential securities fraud and deceptive trade practices claims. The Delaware Department of Justice's participation would therefore assist the court in ascertaining all of the relevant facts of the proposed settlement.

CONCLUSION

For the foregoing reasons, the Delaware Department of Justice respectfully requests that the Court grant its motion and amend the caption to add it as an intervenor-respondent in this Article 77 proceeding, and award such other and further relief as the Court deems appropriate.

Dated: April 11, 2012

THE DELAWARE DEPARTMENT OF JUSTICE

By: 

Joseph Sensenbrenner (NY Bar No. 4508107)
Assistant Deputy Attorney General
Delaware Department of Justice
820 N. French St.
Wilmington, DE 19801
(302) 577-8600
*Counsel for Proposed Intervenor the State of
Delaware*

Of Counsel:
Gregory C. Strong (DE Bar No. 4664) (Pro Hac Pending)
Deputy Attorney General
Delaware Department of Justice
820 N. French St.
Wilmington, DE 19801
(302) 577-8504
(302) 577-8426 (fax)