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

In the matter of the application of

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

Petitioners,

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

Index No. 651786/2011

Assigned to: Kapnick, J.

JOINT MEMORANDUM OF LAW IN OPPOSITION TO THE PROPOSED SETTLEMENT

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Pursuant to the February 26, 2013 Amended Scheduling Order, the undersigned notify the Trustee and the Court that they object to the proposed settlement and respectfully submit this memorandum in opposition to the proposed settlement.[1] This memorandum also serves as notice to all parties and the Court that the undersigned intend to present evidence and testimony in opposition to the proposed settlement at trial.[2]

INTRODUCTION

The settlement proposed by the Bank of New York Mellon ("BNYM"), the Inside Institutional Investors, and Bank of America (collectively, "settlement proponents") is the result of a conflicted process in which the Trustee placed its interests and the interests of its business partner Bank of America ("BofA") ahead of its certificateholders' interests. By engaging in this self-dealing and unreasonably failing to investigate BofA's massive liability, the Trustee violated its fiduciary duties to all certificateholders. As a consequence, the resulting settlement is a pennies-on-the-dollar bargain for BofA that woefully under compensates certificateholders.

In hopes of limiting the scrutiny that the settlement and the process by which it was reached would receive, the settlement proponents initiated this Article 77 proceeding. Throughout this proceeding, the settlement proponents have persistently attempted to prevent investors in the Covered Trusts from learning how the settlement came about. Though a number

[1] Expert discovery is not yet concluded in this case and there are two pending motions to compel (motion sequence 29 and 31). The undersigned expressly reserve their right to supplement or amend this objection as necessary based on any discovery that occurs in the future, including but not limited to discovery that may be taken after final resolution of the pending motions.

[2] The evidence that will be presented at trial will include, but is not limited to, the testimony and exhibits cited to and submitted with this objection. The undersigned intend to call witnesses and present exhibits at trial and expressly reserve the right to introduce any other relevant evidence, as necessary. Undersigned counsel will consult with the settlement proponents to coordinate the presentation of evidence in a manner efficient for the Court.

of critical questions in this unprecedented proceeding remain unanswered, through the Court's direction much has been learned about both the settlement process and the terms. The information discovered thus far confirms what many sophisticated investors in the Covered Trusts have long suspected—that this proposed settlement and the conflicted process by which it was reached are unworthy of judicial approval. This Court can have no confidence in either the proposed settlement or the process by which it was reached. The undersigned parties therefore request that the Court reject the proposed settlement as it currently stands.

Operating under a settlement-driven mindset from the beginning, BNYM worked in concert with its client BofA and with a select minority of investors to extinguish BofA's staggering liabilities to the Covered Trusts. Despite facing liability for losses expected to exceed $100 billion in 530 separate RMBS trusts, BofA was able to dictate both how the settlement negotiations would proceed and what amount of money it would pay to resolve its exposure. When BofA [redacted], BNYM and the Inside Institutional Investors went along. When BofA wanted to expand the settlement to nearly all Countrywide trusts, BNYM and the Inside Institutional Investors went along. When BofA [redacted], BNYM and the Inside Institutional Investors went along. When BofA retained a trust expert (now BNYM's expert in this proceeding) to brainstorm the Article 77 strategy, the other settlement proponents worked collaboratively with BofA in an attempt to dramatically limit the judicial scrutiny and investor involvement the settlement would face.

The resulting proposed settlement has something uniquely beneficial for all three of the participants. BofA pays only pennies on the dollar for its massive exposure and receives full releases for all certificateholder claims in the Covered Trusts. BNYM satisfies its client, receives full-fledged indemnity protection from BofA for its settlement conduct, payment by BofA of all of its attorneys fees and litigation expenses (including all expert witnesses), and a release of all claims that could be brought against it by its beneficiaries for its conduct in the settlement negotiations. The Inside Institutional Investors receive payment of their attorney's fees by BofA (in the unsupported amount of $85 million) and judicial endorsement of their "settlement without suit" agenda which they hope to offer to other banks with RMBS liability exposure.

Throughout the settlement process, BNYM operated under the mistaken belief that it had no fiduciary duties to its beneficiaries. BNYM was wrong. This Court has found that the Trustee has fiduciary duties. The Trustee's own trust law expert recently conceded under oath that BNYM was subject to fiduciary duties throughout the settlement process. One of those duties is the duty of undivided loyalty, which strictly prohibits self-dealing and dictates that a trustee must refrain from situations in which it is reasonably foreseeable that its conduct may be influenced by considerations other than the beneficiaries' best interest. As a fiduciary, BNYM is also held to the highest standard of care.

Notwithstanding its duty of undivided loyalty to *all* beneficiaries of the 530 Covered Trusts, BNYM repeatedly engaged in self-dealing to protect itself and BofA in the settlement negotiations. When it chose to enter the settlement negotiations, BNYM faced its own substantial liability risk, including losing indemnity rights from BofA and being subject to heightened duties to represent and protect the interests of all certificateholders in the Covered Trusts. Rather than notify its certificateholders of a pending Event of Default and their ultimate right to institute suit against BofA, [redacted]

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[redacted]. Similarly, consistent with its self-dealing throughout the settlement process, BNYM [redacted] tried to obtain a release of all potential claims against it by beneficiaries for all its conduct as Trustee, not limited to its participation in the settlement negotiations.

BNYM's settlement conduct also fell short of its duty of care to the certificateholders. Among other things, the record is now clear that BNYM did nothing to investigate the strength of the claims it could have brought against BofA and which are released by the proposed settlement. Not a single loan file was reviewed during the course of the settlement negotiations, even though the Trustee has a contractual right to demand them from BofA. As a result, the numerous assessments of BofA's exposure are based on nothing more than unsupported assumptions. These assumptions vary widely, with estimates of the losses suffered by the trusts ranging by over $40 billion.

BNYM and the Inside Institutional Investors then accepted a number of BofA discounts off of the potential settlement exposure, including the incorrect and regularly rejected theory that the Trustee would have to prove on a loan-by-loan basis that a breach of the subject representations and warranties caused the loan to default. BNYM also accepted BofA's theory that a large judgment against Countrywide could not be recovered against BofA. This discount was unreasonable for multiple reasons, primarily the Trustee's failure to conduct an investigation as to the underlying facts negating such a claim. Justice Bransten's recent order denying BofA's motion for summary judgment on the issue of successor liability because there are sufficient factual questions to send the question to trial further undercuts the Trustee's rationale for accepting the proposed settlement amount. The Trustee also agreed to release BofA for servicing claim liabilities, document exception liabilities, and loan modification liabilities, all without receiving any value for these releases. Put simply, the settlement number is in no rational way related to the approximately $100 billion in losses to the Covered Trusts or to BofA's liability.

The settlement has been publicly criticized as being a sweetheart deal between two banks and a group of investors with business ties to BofA and a broader agenda different from that of other investors. The conduct of the settlement proponents supports this criticism. [redacted] The settlement proponents claim that litigation would have been too expensive and difficult. In fact, the cost of litigating a lawsuit would be a drop in the bucket compared to the amount at stake and the potential increased recovery to the Covered Trusts. The settlement proponents ignore the ability of the legal system to fashion alternatives to trying multiple complex claims, including the sampling of loan files, partial summary judgment on issues of law, test trials, and formal mediation.

The settlement proponents deny, among other things, that BNYM acted in a self-interested manner, that BNYM failed to conduct an adequate investigation of the underlying claims, and that the settlement amount is unreasonably low. There are numerous factual disputes underlying each of these denials that must be resolved at trial. A trustee who acts in a self-interested manner, or violates its fiduciary duty of care to the certificateholders, or acts unreasonably in agreeing to an unreasonable settlement, is entitled to no deference from the Court. As the Trustee has stated in prior hearings, the Trustee bears the burden of proof that it complied with its duties and is entitled to the broad relief it seeks in the Proposed Final Order and Judgment ("PFOJ").

While a dramatic amount of new information has been developed about the settlement negotiations and its terms since BNYM came to this Court seeking an ex parte order of notice to certificateholders about the proposed settlement—information that wholly contradicts BNYM's initial representations to the Court that the intervenors and objectors had all the information they needed to evaluate the settlement in BNYM's initial voluntary production in the fall of 2011—the settlement proponents continue to withhold critical evidence. The remaining undisclosed information includes:

- what a sampling of the loan files would reveal concerning breach and success rates;
- whether BNYM sought legal advice from its attorneys in order to prevent its beneficiaries from filing claims against it for its role in the settlement process and its general administration of trusts;
- the specifics of legal advice BYNM received from its counsel in its role as fiduciary for the benefit of certificateholders;
- whether any of the Inside Institutional Investors bought their certificates at distressed prices so that the settlement amount would result in a larger return on investment for them than for those who bought earlier, such that the Inside Institutional Investors' interests would not be representative of such other investors;
- the blow-up percentage that would allow BofA and Countrywide to walk away from this deal;
- how the net amount of the settlement will be allocated to any individual trust; and
- how much any individual certificateholder would receive from the proposed settlement.

Much is at stake here. There is widespread conviction among the sophisticated Intervenors that this settlement process was flawed from the beginning. Knowing the conflicted position in which it stood, the Trustee could and should have come to the Court for guidance *before* embarking on the settlement process. Had it done so, the questions of whether notice should have been provided to certificateholders, whether the Trustee had a right to forebear on the Event of Default, whether an Event of Default occurred, whether the Trustee was entitled to additional indemnity, how the interests of the unrepresented certificateholders would be protected, and whether a loan file sampling would be undertaken, could have been addressed before the Trustee went along with a settlement process driven by the liable party and a minority of investors in the 530 trusts. Without the information set forth above, this Court and the outside investors cannot know for certain what settlement amount would be reasonable.

Given the flawed process and resulting unreasonable settlement, this Court should not approve the settlement as it currently stands. The Settlement Agreement contemplates that judicial approval could take until December 31, 2015, to be achieved. This Court has the power and authority to direct the parties to go back to the drawing board, armed with the wealth of information and resources available to them, to engage an experienced mediator who will oversee an open and equitable process for all involved. The undersigned parties stand ready to actively participate in such a process.

BACKGROUND ON THE PROPOSED SETTLEMENT

At its core, the proposed settlement releases claims beneficially owned by certificateholders in the 530 Covered Trusts against BofA/Countrywide in exchange for up to $8.5 billion and certain purported modifications to BofA's servicing practices.[3] The certificateholder claims being released (the "Trust Released Claims") include claims against BofA/Countrywide for (1) widespread breaches of representations and warranties made by

[3] *See* Ex. 1 at §§ 3, 5, 9. All citations to "Ex. ___" in this brief reference the exhibits to the Affirmation of Daniel M. Reilly in Support of this Joint Memorandum of Law in Opposition to the Proposed Settlement, dated May 3, 2013, and filed simultaneously with this brief.

Countrywide when it sold the loans to the trusts, (2) some of the worst servicing in the industry, including a master servicer Event of Default, and (3) incomplete collateral loan files.[4] Although the settlement proponents have consistently blocked efforts to explore the extent of BofA/Countrywide's actual liability for the Trust Released Claims,[5] publicly available information demonstrates the sweeping extent of BofA/Countrywide's misconduct in originating and servicing the mortgage loans in the Covered Trusts.

From 2004 to 2007, Countrywide was the largest mortgage originator in the country.[6] Countrywide usually did not keep the mortgages it originated on its books, however, as its essential business strategy, according to its President and COO David Sambol, was "originating what was salable in the secondary market."[7] Thus, from 2002 through 2005, Countrywide sold or securitized 87% of the $1.5 trillion in mortgages it originated.[8]

By the admission of Countrywide's co-founder and CEO, Angelo Mozillo, the loans Countrywide originated were "toxic."[9] In internal documents, Countrywide classified itself as being at "Considerable Risk" regarding its underwriting practices because "the preventive control over credit risk and fraud was not operating effectively."[10] Countrywide acknowledged that given its practice of "allowing loans with red flags to be funded without evidence of an approved underwriter's review, undesirable loans may result in financial and/or legal ramifications to CFC as well as to investors purchasing these loans."[11] And in 2010, three of

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[4] *Id.* at § 9.
[5] *E.g.* Ex. 2 (Scrivener Dep.) at 12:9-12; 12:20-13:6; 66:6-12; 73:3-77:12; 80:16-81:13; 118:11-25.
[6] Ex. 3 at 105.
[7] *Id.*
[8] *Id.*
[9] *Id.*
[10] Ex. 6 at 4.
[11] *Id.* at 5.

Countrywide's top executives agreed to pay substantial fines to the Securities and Exchange Commission to settle a lawsuit brought by the SEC charging them with knowingly making fraudulent disclosures related to Countrywide's adherence to underwriting guidelines.[12] Countrywide's failure to follow underwriting guidelines and prudent lending practices led to extensive breaches of representations and warranties in loans sold to the Covered Trusts and, ultimately, massive losses to certificateholders.

Bank of America's and Countrywide's servicing practices were similarly defective. Based upon the Inside Institutional Investors' "Key Pool Statistics by Servicers," Bank of America ranked "at the bottom of nearly every category."[13] Tellingly, Bank of America was a party to the "landmark $25 billion agreement" with the Justice Department, the Department of Housing and Urban Development, and 49-state attorneys general "to address mortgage loan servicing and foreclosure abuses" and "resolve violations of federal and state law" related to the servicing of residential mortgages.[14] And in 2010, Countrywide agreed to pay one of the largest judgments ever imposed in a Federal Trade Commission case to settle claims related to its servicing practices.[15] In short, as the Inside Institutional Investors concede, "Bank of America was by far the worst of the major bank loan servicers."[16]

Because of Countrywide and BofA's abysmal origination and servicing practices, investors in the Covered Trusts were suffering massive losses. [redacted]

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[12] *See* Ex. 7.
[13] Ex. 8 at 27.
[14] Ex. 9; Ex. 10, (full document *available at* http://www.justice.gov/opa/documents/bank-of-america-consent-judgement.pdf).
[15] Ex. 11.
[16] Ex. 8 at 27.

When the Trustee received a Notice of Non-Performance from a minority group of investors (the Inside Institutional Investors) on October 18, 2010 that triggered an Event of Default clock, the Trustee replaced prior counsel and retained Mayer Brown [redacted]

In the settlement process that immediately ensued, as described in this objection, BNYM (among other things): attempted to stop the Event of Default clock through a forbearance agreement; failed to give the certificateholders notice of the forbearance or of the settlement negotiations [redacted] failed to look at a single loan file; failed to investigate the scope of Countrywide and BofA's liability or the strength of the underlying claims being settled; [redacted]; allowed the Inside Institutional Investors to negotiate the settlement amount even in the many trusts in which they lacked the requisite 25% voting rights; and relied on facially flawed analyses by its "independent" advisors, paid by BofA, in order to justify the discounted settlement amount. In order to protect against future challenges to the inadequate settlement and the Trustee's unreasonable conduct by certificateholders who were not party to the negotiations, the settlement proponents initiated this Article 77 proceeding to receive judicial blessing of both the settlement process and the settlement's terms. Under the facts in this unique proceeding, such judicial approval is not warranted.

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[17] *See* Ex. 36 (Kravitt Dep.) at 22:18-24:7.
[18] *Id.* at 101:13-115:5.
[19] *Id.*; *see also* Exs. 4, 50, & 51.

STANDARD OF REVIEW

Through this unorthodox Article 77 proceeding, the Trustee has placed squarely before the Court whether the proposed settlement is reasonable[20] and whether the Trustee acted reasonably, consistent with its fiduciary duties to all certificateholders, and in good faith during the negotiations that led to the proposed settlement.[21] Therefore, in reviewing the Trustee's request for approval of the proposed settlement, the Court must determine whether (1) the settlement is fair and reasonable, (2) the Trustee complied with its fiduciary duties during the negotiations that led to the proposed settlement, and (3) the Trustee has met its burden to prove each of the proposed findings it has submitted for Court approval.[22]

BNYM bears the burden of proving that it acted reasonably, complied with its fiduciary duties, and is entitled to the findings it seeks. *See* Bogert's Trusts & Trustees § 560 ("The burden of proving that a discretionary power has been properly used is on the person who is asserting rights resulting from the use of the power, for example, on the trustee claiming the approval of an account which shows that he exercised a power in a certain manner . . . .) (citing *In*

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[20] *E.g.* Doc. No. 1 at 17 ("The Settlement Should Be Approved"); 19 ("The Settlement Is Advantageous to the Trusts and, at the Very Least, Reasonable"); 21 ("The Settlement Payment Is Reasonable"); 30 ("The Servicing Procedures and Improvements Are Reasonable"); *see also* Ex. 1 at Ex. B ¶ n (also found at Doc. No. 7) ("The Settlement Agreement is hereby approved in all respects.").

[21] *E.g.* Ex. 1 at Ex. B ¶ h (also found at Doc. No. 7) ("The Settlement Agreement is the result of factual and legal investigation by the Trustee"); ¶ i ("The Trustee appropriately evaluated the terms, benefits, and consequences of the Settlement and the strengths and weaknesses of the claims being settled."); ¶ j ("The arm's-length negotiations that led to the Settlement Agreement and the Trustee's deliberations appropriately focused on the strengths and weaknesses of the Trust Released Claims, the alternatives available or potentially available to pursue remedies for the benefits of the Trust Beneficiaries, and the terms of the Settlement"); ¶ k ("The Trustee 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."); ¶ l ("The Court hereby approves the actions of the Trustee in entering into the Settlement Agreement in all respects.").

[22] *See id.*

re Jaeck's Will, 42 N.Y.S.2d 514 (Sur. Ct. 1943)).[23] The Court does not owe the Trustee any deference when determining whether BNYM met its burden of establishing that the terms of the settlement are reasonable and that it complied with its fiduciary duties, acted reasonably, and acted in good faith during the settlement negotiations.

While under certain circumstances courts defer to Trustee decision-making, no deference is owed here because (1) BNYM acted unreasonably when it agreed to the terms of the proposed settlement, (2) BNYM operated beyond the express powers conferred to it by the Governing Agreements,[24] (3) BNYM breached its duty of loyalty by acting with conflicts of interest and engaging in self-dealing, and (4) BNYM breached its duty of care. Restatement (Third) Trusts § 87 cmt. b (recognizing that courts do not defer to trustees whose "conduct is [not] reasonable, [is] based on an improper interpretation of the terms of the trust, [or is] otherwise inconsistent with the trustee's fiduciary duties."); *Haynes v. Haynes*, 900 N.Y.S.2d 22, 24 (1st Dep't 2002); *see also In re Stillman*, 107 Misc. 2d 102, 110 (Sur. Ct. 1980).[25]

ARGUMENT

The Court should not approve this settlement. First, the Trustee engaged in self-dealing and conflicted transactions throughout the settlement process. Second, the Trustee acted unreasonably by failing to investigate material facts, by failing to use its leverage to obtain a larger settlement, and by merely rubber stamping a settlement that was negotiated by a minority

[23] *See also* Ex. 12 (Feb. 7, 2013 Hearing Tr.) at 65:14-25 (Trustee's counsel recognizing that BNYM bears the burden of establishing the findings sought in the Proposed Final Order and Judgment).
[24] Ex. 13 (Crosson Dep.) at 97:8-98:5.
[25] *See also* Ex. 14 (Frankel Report (Doc. No. 529)) at 12-14. For purposes of efficiency, the undersigned have attached as exhibits to this objection only the cited portions of the expert reports. Complete copies of the expert reports submitted by Professor Tamar Frankel (Doc. Nos. 529 & 566), Professor John Coates (Doc. Nos. 530 & 567), Professor Adam Levitin (Doc. No. 570), and Dr. Charles D. Cowan (Doc. No. 537 & 568) have previously been provided to the Court and counsel. This objection relies on those reports.

investor group. Finally, the settlement agreement that resulted from this conflicted and unreasonable process is itself unreasonable and unfair to investors because it severely understates BofA's liability to investors in the Covered Trusts.

I. The Court Should Not Approve This Settlement Because The Trustee Violated Its Duty of Undivided Loyalty By Engaging in Self-Dealing, Laboring Under Conflicts of Interest, And Acting to Protect Itself and BofA Throughout the Settlement Negotiations

A. BNYM Owed Certificateholders a Duty of Loyalty at All Times During the Settlement Negotiations

"The most fundamental duty owed by the trustee to the beneficiaries of the trust is the duty of loyalty." *Dabney v. Chase Nat. Bank of City of New York*, 196 F.2d 668, 670 (2d Cir. 1952). "[I]t is elemental that a fiduciary owes a duty of undivided and undiluted loyalty to those whose interests the fiduciary is to protect. This is a sensitive and inflexible rule of fidelity, barring not only blatant self-dealing, but also requiring avoidance of situations in which a fiduciary's personal interest possibly conflicts with the interest of those owed a fiduciary duty." *Birnbaum v. Birnbaum*, 73 N.Y.2d 461, 466 (1989) (quotations, citations omitted); *see also City Bank Farmers Trust Co. v. Cannon*, 291 N.Y. 125, 131 (1943) ("The standard of loyalty in trust relations does not permit a trustee to create or to occupy a position in which he has interests to serve other than the interest of the trust estate."). To comply with the duty of loyalty, "a trustee must refrain, whether in fiduciary or personal dealings with third parties, from transactions in which it is reasonably foreseeable that the trustee's future fiduciary conduct might be influenced by considerations other than the best interests of the beneficiaries." Rest. (Third) of Trusts, § 78 cmt. (b) (2007).

As BNYM's own trust expert recognizes, BNYM was subject to the duty of loyalty throughout the settlement negotiations and was required to protect the certificateholders' interests, not those of BofA.[26] "Every action" that BNYM undertook during the settlement negotiations must have shown "fiduciary loyalty" to the certificateholders.[27] As recently noted by a federal bankruptcy judge in another case concerning BNYM's conduct as Trustee on behalf of bondholders, "once BNYM chose to act as the Bondholders' representative and participate in the settlement negotiations on their behalf, it was obliged to represent the interests of the Bondholders faithfully." *In re Lower Bucks Hospital*, 471 B.R. 419, 453 (E.D. Pa. 2012) ("*In re LBH*"). The *In re LBH* Court characterized BNYM's "argument to the contrary" as "utterly without merit." *Id.*

Here, as explained in detail below, BNYM was concerned throughout the settlement negotiations with its own liability and its protection of BofA, with whom it has important ongoing business relationships. BNYM used its position at the bargaining table to extract benefits for itself and secure its position as BofA's "preferred trustee."[28] BNYM's preoccupation with self-protection and yielding to BofA is evidenced by the record throughout the negotiations. In some cases BNYM was successful in obtaining benefits for itself, in other cases it was not, but BNYM's attempts to use the settlement negotiations for its own benefit tainted both the process and the final decision by creating a "situation[] in which [BNYM's] personal interest conflicts with the interest of those owed a fiduciary duty." *Birnbaum*, 73 N.Y.2d at 466.[29] In any event, this proposed settlement is evidence of BNYM's effective representation of BofA's interests, and does not reflect the actions of a loyal trustee acting in the sole or best interests of it beneficiaries.

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[26] Ex. 15 (Langbein Dep.) at 233:10-16.

[27] *Id.* at 233:17-21.

[28] Ex. 16 (Levitin Report (Doc. No. 570)) at ¶¶ 52-56; Ex. 17 (Fischel Report (Doc. No. 541)) at ¶ 32.

[29] *See also* Ex. 18 (Frankel Rebuttal Report (Doc. No. 566)) at 11-12 ("Provisions that did not make it into the final draft may indicate conflicts just as those that saw the light of day before the Court.").

B. BNYM Faced Substantial Risk When It Chose to Enter Settlement Negotiations

1. The mortgage crisis created risk for BNYM

The meltdown in the mortgage industry created significant uncertainty and potential liability for BNYM. Debra Baker, a senior managing director in BNYM's Corporate Trust division, testified that in the summer of 2008 when the "market downturn" began there was "a lot of activity" within BNYM "around setting up war rooms, we called them at that time, just to make sure we understood any of our exposures."[30] [redacted]

[redacted]

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[30] Ex. 19 (Baker Dep.) at 15:3-16:9.
[31] *Id.* at 34:13-25.
[32] *Id.* at 27:21-24; 32:15-33:2; 34:2-12.
[33] *E.g.* Ex. 20; Ex. 21; Ex. 22; Ex. 23 [redacted]
[34] Ex. 24 (Stanley Dep.) at 39:23-40:7.

[redacted]

[redacted]

BNYM was concerned about its own exposure in the Covered Trusts from the beginning of the mortgage crisis. [redacted]

2. The Inside Institutional Investors' letter writing campaign focused the risk on BNYM as trustee for hundreds of Countrywide trusts

In the summer of 2010, the Inside Institutional Investors began sending letters to the Trustee and its outside counsel at Pillsbury Winthrop Shaw Pittman LLP. These letters, among other things, purported to instruct the Trustee [redacted]

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[35] *E.g.* Ex. 25; Ex. 26; Ex. 27.

[36] Ex. 24 (Stanley Dep.) at 39:5-40:11.

[37] *Id.* at 46:22-51:8.

[38] *Id.* at 52:19-53:9; 57:3-12.

[redacted]

These instruction letters, however, created no risk to the Trustee, and BNYM therefore did not pay them much attention. Instead, BNYM [redacted] by making technical objections to the instruction letters and refusing to take any action.[40]

In October 2010, the Inside Institutional Investors changed their strategy by sending two letters that directly created risk for the Trustee. On October 18, 2010, the investor group sent BofA/Countrywide and the Trustee a detailed Notice of Non-Performance setting forth numerous violations of the PSAs by BofA/Countrywide that, if left unremedied for 60 days, would result in an Event of Default that would subject the Trustee to heightened duties and provide expanded rights to certificateholders.[41] After that shot across the Trustee's bow, the investors then took dead aim at the Trustee. In a letter on October 22, 2010, the Inside Institutional Investors asked the Trustee for evidence of compliance with its own duties under the PSAs to ensure that loans with incomplete mortgage files (which pose risks to investors because they often cannot be foreclosed on) were substituted for loans with complete mortgage files.[42] These were duties of the Trustee itself and failure to comply with those duties would result in direct liability against BNYM.

BNYM clearly understood that it was now facing potential liability. Douglas Chapman, a risk officer for BNYM, [redacted]

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[39] Ex. 28.
[40] Ex. 29.
[41] Ex. 30.
[42] Ex. 31; Ex. 32 § 2.02; Ex. 33 (Chavez Dep.) at 89:2-90:3; 122:10-123:21; Ex. 34 (Bailey Dep.) at 135:2-6 ("a trustee can be liable for breach of contract claims to the extent that it does not fulfill its obligations under the PSA.").

[redacted]

Other BNYM representatives [redacted] In addition, although BNYM did virtually no meaningful investigation of the claims that are being settled (as discussed below in Part II), BNYM [redacted] Early in the negotiations with BofA, BNYM sought to ensure that the settlement would [redacted]

Facing the prospects of heightened duties and direct liability for its own misconduct, BNYM acted in response to these two letters by immediately replacing Pillsbury. BNYM hired Mayer Brown LLP, and specifically, dealmaker Jason Kravitt [redacted] Mr. Kravitt and his firm already had relationships with many of the parties involved in the matter, including BofA, [redacted]

Once the Inside Institutional Investors placed direct pressure on BNYM, and Mayer Brown stepped in, matters moved quickly towards settlement. In the summer of 2010, BNYM took over six weeks to arrange a meeting in New York with the Inside Institutional

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43 Ex. 35 (Chapman Dep.) at 237:14-25.
44 Ex. 34 (Bailey Dep.) at 281:19-282:1; Ex. 35 (Chapman Dep.) at 237:14-25; Ex. 36 (Kravitt Dep.) at 60:20-21.
45 Ex. 34 (Bailey Dep.) at 223:9-224:6; Ex. 33 (Chavez Dep.) at 114:16-24; *id.* at 123:22-124:2.
46 Ex. 37.
47 Ex. 38; Ex. 36 (Kravitt Dep.) at 155:3-156:5; *see also* Ex. 39 [redacted]
48 Ex. 39.

Investors when that group was specifically requesting a meeting.[49] But after receiving Gibbs & Bruns's October 22 letter, Jason Kravitt, Mayer Brown's lead negotiator, [redacted]

C. Facing an Event of Default, the Trustee Sought to Reduce Or Avoid Its Own Risk, at the Expense of the Certificateholders

When an Event of Default occurs, the Trustee is subject to heightened duties and the certificateholders receive additional rights, as BNYM witnesses—though not its counsel in this litigation—have recognized.[51] Specifically, the Trustee is obligated to give notice to all certificateholders of the Event of Default and is held to the standard of a prudent person in the conduct of his own affairs.[52] Certificateholders benefit from receiving notice of an Event of Default and from having a Trustee subject to heightened duties. Certificateholders are also able to demand that the Trustee initiate action against the Master Servicer to cure the Event of Default. If the Trustee fails to take action or otherwise fails to act prudently, the certificateholders can sue the Master Servicer directly.[53]

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[49] Ex. 40; Ex. 41.
[50] Ex. 42.
[51] Ex. 34 (Bailey Dep.) at 136:4-19 ("My general understanding under a PSA is that the trustee is not subject to an enhanced standard of duty unless and until there has been a servicer event of default."); Ex. 36 (Kravitt Dep.) at 201:8-23 [redacted] *cf.* Ex. 12 (Feb. 7, 2013 Hearing Tr.) at 150:12-151:3 (Trustee counsel stating that the duties do not change when an event of default occurs).
[52] Ex. 32 at §§ 7.03; 8.01.
[53] *Id.* at § 10.08.

1. Even though certificateholders would be entitled to expanded rights if an Event of Default occurred, BNYM actively sought to prevent an Event of Default from occurring so that it would not be subject to heightened duties

In December 2010, as the 60-day clock started by the Inside Institutional Investors' October 18 Notice of Non-Performance continued to run, BNYM undertook to ensure that these heightened duties and expanded rights would never take effect. Specifically, BNYM negotiated a "forbearance agreement" with BofA and the Inside Institutional Investors in an attempt to protect both banks from the effects of an Event of Default.[54] The resulting agreement was renewed approximately every two months during the course of the settlement negotiations. The forbearance agreement purports to prevent an Event of Default from occurring, thereby suppressing the Trustee's heightened duties, ensuring valuable certificateholder rights are not triggered, and buying BofA more time to structure a favorable deal without the pressures of mandatory cure obligations and involvement of other certificateholders.

In an early draft of the forbearance agreement, Gibbs & Bruns asserted that the agreement would only prevent their investor group from taking action to initiate a suit against Bank of America, but would not prevent the Event of Default from occurring.[55] Under this formulation, certificateholders would have received notice of the Event of Default from the Trustee,[56] would have received the benefit of having a trustee subject to a

[54] Ex. 43.
[55] Ex. 44 ("Stated differently, we're not *lengthening* the 60 day cure period under Section 7.01. Instead, our clients are simply agreeing to send the 10.08 notice *when they want to send it*, rather than sending it on December 18, the earliest date on which they could otherwise send it.").
[56] Ex. 32 at § 7.03.

higher standard of conduct, and would have been able to avail themselves of their right to sue Bank of America/Countrywide if the Trustee failed to take action.

[redacted]

> [redacted]

[redacted] The parties dispute whether, as a factual matter, an Event of Default occurred and triggered expanded rights for certificateholders.

2. The Trustee intentionally kept some certificateholders in the dark about the negotiations in order to obtain benefits for itself

An Event of Default requires the trustee to give notice of the Event of Default to all certificateholders.[58] This responsibility is consistent with hornbook trust law which recognizes that a trustee's duties change post-default. *See*, *e.g.*, *Beck v. Manufacturers Hanover Trust Co.*, 218 A.D.2d 1, 12 (1st Dep't 1995) ("The reality militating in favor of this revised allocation of responsibility, of course, is that in the aftermath of a default by the obligor, bondholders, particularly those whose bonds represent only a relatively small portion of a large issue, will, as a practical matter, be unable to act effectively to guard

[57] Ex. 45.
[58] Ex. 32 at § 7.03.

against the further impairment of their economic interests, and although those interests may be relatively small when compared to the entire issue, they may nevertheless be, and often are, extremely substantial in the context of the individual bondholder's assets.").

Here, not only did certificateholders never receive notice of an actual or potential Event of Default, BNYM "did not send out a formal notice to certificate holders until the proposed settlement was agreed to."[59] The lack of notice was the result of a conscious decision made by the Trustee to exclude other certificateholders and avoid heightened duties. As Jason Kravitt testified:

> [I]t's very unstable to try to negotiate a large, complicated, time-consuming matter when other parties can interfere because an event happened. Q: Other parties meaning who? A: Any group of certificate holders who want the trustees to do something different or who want to attack the bank based on the event of default.[60]

BNYM's decision not to provide notice here was also a departure from its standard practice. [redacted] Even more mundane topics of trust administration often resulted in certificateholders receiving notice. For example, in September 2010, when the Inside Institutional Investors were requesting that they be appointed on a contingency fee basis to investigate representation and warranty breaches, the Trustee's then-counsel at Pillsbury responded by noting: "The Trustee does not customarily engage counsel on a contingent fee basis and would want, at a minimum, *to*

[59] Ex. 36 (Kravitt Dep.) at 366:20-22.
[60] *Id.* at 187:21-188:5.
[61] Ex. 46 (Griffin Dep.) at 218:6-14.

notice all certificateholders of the proposed engagement to enable them to express any concerns that they might have."[62]

[redacted]

[redacted]

[62] Ex. 29 at 3.
[63] Ex. 47 (Mirvis Dep.) at 69:6-70:4.
[64] *Id.* at 73:9-74:7.
[65] Ex. 48.

[redacted] Less than two weeks after this e-mail, BNYM and BofA entered a signed indemnity agreement (the "December 10 Indemnity").[67] Under the December 10 Indemnity, BofA agreed that "in consideration of the Forbearance Agreement," the "Servicer" would: (1) pay all expenses the Trustee incurred as a result of its participation in the ongoing discussions regarding the Notice of Non-Performance and (2) indemnify the Trustee for all costs or liabilities arising solely out of the Trustee's entry into the Forbearance Agreement.[68]

The settlement proponents' claim that the December 10 Indemnity (and later, the side letter attached to the Settlement Agreement) was simply a "reconfirmation" of what BNYM was already entitled to from BofA is wrong. The Master Servicer has no obligation under the PSAs to indemnify the Trustee for actions taken at the direction of certificateholders.[69] The only reason BNYM engaged in any settlement activity was because of the letter-writing campaign of the Inside Institutional Investors, as described above.[70] [redacted] Further, BNYM's counsel has represented in court that the process leading to the proposed settlement began because the Trustee "received an

[66] Ex. 36 (Kravitt Dep.) at 569:24-570:4.
[67] Ex. 49.
[68] *Id.*
[69] Ex. 32 at § 8.05.
[70] *See also* Ex. 34 (Bailey Dep.) at 235:20-236:20.
[71] Ex. 50; Ex. 51.

instruction" from the Inside Institutional Investors.[72] Under these facts and the plain language of PSA § 8.05, BNYM lost its indemnity from the Master Servicer the moment it began operating at the direction of the Inside Institutional Investors.

Nor did the Trustee have a guaranteed indemnity from the Inside Institutional Investors. In consideration for the Inside Institutional Investors entering the forbearance agreement, BNYM and BofA agreed "that Ms. Patrick's clients will not bear the legal fees, costs and expenses incurred by the Trustee in connection with the Trustee's counsel's participation in the parties' ongoing discussions concerning the October 18 letter."[73] This agreement left BNYM unindemnified for its settlement conduct and therefore exposed to liability for its participation in the settlement negotiations. BofA's agreement to treat the settlement negotiations as falling within the terms of the indemnity therefore provided real and substantial value to BNYM.

[redacted]

The various indemnity agreements gave BofA the opportunity to fund (and therefore control) the entire settlement negotiation process. As of September 2012, BofA had

[72] Ex. 52 (Sept. 21, 2011 Hearing Tr.) at 7:5-24.
[73] Ex. 43; Ex. 5.
[74] Ex. 53.
[75] Ex. 54.

already paid around $10 million in legal fees incurred by the Trustee.[76] BofA has also paid for all the advisors retained by the Trustee to opine on the settlement, [redacted] and is now paying BNYM's litigation experts.[78] When coupled with the $85 million contingent fee that Gibbs & Bruns stands to receive *from BofA*, as well as BofA's agreement to pay their costs,[79] it is now clear that BofA, which is not a party to the litigation, is nevertheless paying *all* of the settlement proponents in this court proceeding.

D. Rather Than Negotiate to Obtain Additional Benefits to the Covered Trusts, BNYM Sought to Obtain for Itself a Broad Release of Claims Against It

Despite BNYM's protestations to the contrary, BNYM was preoccupied throughout the negotiations with obtaining a broad release for itself for claims that could be brought by certificateholders. As early as December 2010, Mr. Kravitt was inquiring of BofA counsel [redacted] There is an issue of fact in dispute between the parties on this point.

[redacted]

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[76] Ex. 36 (Kravitt Dep.) at 537:6-539:14.
[77] *Id.* at 540:4-10; Ex. 55 (Lin Dep.) at 160:5-22.
[78] *E.g.* Ex. 15 (Langbein Dep.) at 138:8-21.
[79] *See* Ex. 1 at Ex. F.
[80] Ex. 37 at BNYM_CW-00270572.

[redacted]

As late as June 23, 2011, just five days before signing the proposed settlement agreement, BNYM was seeking a broad release that would bar certificateholders from asserting any claims against the Trustee for *all* of its conduct as trustee, not just in connection with the proposed settlement.[84] Gibbs & Bruns rejected this provision because there was no "basis in the Settlement for barring claims against the Trustee that are not based on its actions in entering into the Settlement, but rather are based on its pre-settlement conduct."[85]

Gibbs & Bruns also stated "we think *this creates a conflict for the Trustee because it creates the appearance that the Trustee is entering into the Settlement, not because it thinks it benefits the Trusts, but instead because the Trustee wants to obtain a release of other claims for itself.*"[86] [redacted]

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[81] Ex. 56 at 2 ¶ d.
[82] Ex. 57 at 7 ¶ q.
[83] Ex. 58; Ex. 59 at 6 ¶ r.
[84] Ex. 60 at 6 ¶ q.
[85] *Id.*
[86] *Id.* (emphasis added).
[87] Ex. 47 (Mirvis Dep.) at 169:5-10.

[redacted] The mere fact that the Trustee was ultimately stopped from pursuing the release does not absolve the Trustee's conduct any more than a shoplifter is absolved because the security guard stops him before he leaves the store.[89]

Thus, throughout the settlement negotiations and even on the eve of signing the proposed settlement agreement, the Trustee was seeking benefits for itself rather than for certificateholders. In a factually similar matter, the *In re LBH* court rejected BNYM's argument that it could condition its decision to settle the bondholder's dispute with the debtor on achieving a release from bondholder claims for its own conduct: "There is nothing about BNYM's status as the Bondholders' sole authorized representative that justifies acting in any manner *other than in the Bondholders' interests*. . . . [O]nce BNYM chose to act as the Bondholders' representative and participate in the settlement negotiations on their behalf, *it was obliged to represent the interests of the Bondholders faithfully.*" 471 B.R. at 453 (emphasis added). Here, too, BNYM could not put its own interests ahead of certificateholders. Its attempts at doing so constitute a clear-cut case of self-dealing, in violation of its fiduciary duty of loyalty, and further requires the Court to give the resulting settlement close scrutiny.

II. The Court Should Not Approve This Settlement Because The Trustee Acted Unreasonably and Violated its Duty of Care

A. <u>When Participating in Settlement Discussions and Entering the Proposed Settlement, BNYM Was Subject to the Highest Standard of Care</u>

Experts on both sides of this case agree that, at a minimum, the Trustee owes certificateholders a fiduciary duty to act with care.[90] BNYM was subject to the highest

[88] Ex. 15 (Langbein Dep.) at 264:6-15.

[89] Ex. 18 (Frankel Rebuttal Report) at 12 ("Provisions that did not make it to the final draft may indicate conflicts just as those that saw the light of day before the Court.").

standard of care applicable to fiduciaries when engaging in its settlement conduct, for two reasons. First, in undertaking the settlement negotiations BNYM assumed significant powers and engaged in quintessential fiduciary conduct. BNYM's own expert acknowledges this assumption brings with it fiduciary duties. Second, an Event of Default did occur, triggering the prudent person standard found in section 8.01 of the PSAs.

1. BNYM was subject to the duty of prudence and other fiduciary duties by virtue of engaging in its settlement conduct

Despite BNYM's prior assertions that it is not a fiduciary,[91] it is no longer disputed that BNYM was subject to fiduciary duties to the certificateholders when it negotiated and entered the proposed Settlement Agreement.[92] BNYM's own expert acknowledged that BNYM had a fiduciary duty to (among other things): evaluate the strengths and weaknesses of the claims being settled;[93] evaluate the terms, benefits and consequences of the proposed settlement;[94] undertake a legal and factual investigation before entering the Settlement Agreement;[95] and to determine the full extent of Bank of America's liability.[96] The above list does not include all of BNYM's fiduciary duties, and it would "take many

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[90] *See* Ex. 14 (Frankel Report) at 8 ("The Trustee's decision to enter into settlement negotiations is precisely the type of discretionary conduct that subjects trustees to the highest duties. There can be no question that the Trustee owed to the Outsiders fiduciary duties."); *see also* Ex. 15 (Langbein Dep.) at 103:12-104:3; 122:14-124:17.

[91] *See* Doc. No. 263 at 11-16 ("[T]he Trustee is not a fiduciary."); Ex. 62 (Aug. 2, 2012 Hearing Tr.) at 121:19 (Trustee's counsel stating "the Trustee is not a fiduciary").

[92] *See* Ex. 14 (Frankel Report) at 8 ("The Trustee's decision to enter into settlement negotiations is precisely the type of discretionary conduct that subjects trustees to the highest duties. There can be no question that the Trustee owed to the Outsiders fiduciary duties."); *see also* Ex. 15 (Langbein Dep.) at 103:12-104:3; 122:14-124:17.

[93] Ex. 15 (Langbein Dep.) at 122:14-23.

[94] *Id.* at 122:24-123:3.

[95] *Id.* at 100:19-101:18; 123:4-17.

[96] *Id.* at 243:1-7.

years to identify all" of the fiduciary duties BNYM owes the certificateholders.[97] Indeed, all of BNYM's settlement conduct is subject to a fiduciary standard and the fundamental fiduciary duties of loyalty and prudence apply at all times.[98] Thus, both parties' trust experts agree that BNYM was subject to the fiduciary duties of loyalty and prudence during the settlement negotiations.[99]

BNYM's shift in position is significant. The Trustee's prior belief that it did not owe certificateholders any fiduciary duties undercuts any argument that it complied with duties it did not believe it had. BNYM's belief that it was not a fiduciary during the settlement negotiations is itself strong evidence that BNYM violated its duty of care to certificateholders.[100]

2. An Event of Default occurred, thus triggering the prudent person standard of section 8.01

The October 18, 2010 Notice of Non-Performance started a 60-day clock running that, when it expired, resulted in an Event of Default.[101] Under § 7.01(ii) of the PSAs, one way to trigger an Event of Default is for a group of certificateholders to provide notice to the Master Servicer and the Trustee of the Master Servicer's breaches.[102] If those breaches remain unremedied after 60 days, an Event of Default has occurred. Significantly, there is no requirement in the PSAs that the certificateholders have the burden of proving a breach; instead

[97] *Id.* at 103:23-104:3.
[98] *Id.* at 123:11-21; *see also id.* at 165:7-8; 233:17-21.
[99] *E.g.*, Ex. 14 (Frankel Report) at 7 ("[A]t all times, before and after the Event of Default . . . a trustee must avoid conflicts of interest and perform its functions with appropriate care.").
[100] *Id.* at 7 ("In fact, if the trustee presumes that it is strictly a contract party a serious question arises as to whether it even attempted to adhere to its fiduciary duties and whether this posture does not violate its duties.").
[101] *See, e.g.*, Ex. 63 at 49 (recognizing that the notice of non performance "commenced" a "60 day period").
[102] Ex. 32 at § 7.01(ii).

the only requirement is notice. In any event, there is little doubt that the allegations in the Notice of Non-Performance were true. [redacted] Furthermore, the purported "servicing improvements" contained in the proposed settlement agreement provide evidence of the truth of the allegations that the servicing violated the PSAs and led to an Event of Default because many, if not all, of the "improvements" merely bring BofA's servicing up to standards required by the PSAs.[104]

In addition, the conduct of the parties makes clear that they believed an Event of Default had been triggered by the Notice of Non-Performance. In November 2010, Mr. Kravitt e-mailed an economic consulting firm to discuss replacing BofA as master servicer, a step that could be taken if there was an Event of Default.[105] Also, the forbearance agreement itself demonstrates that the parties believed that the 60-day cure period was running and that an Event of Default would occur upon the expiration of the 60th day.

Finally, although the settlement proponents claim the forbearance agreement prevented the 60-day clock from ever running, there is *nothing* in the PSAs that permit such a forbearance agreement, or that permit an amendment to the PSAs without satisfying the requirements of 10.01 (which requires a majority of certificateholders to agree to an amendment of the PSA).[106]

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[103] Ex. 64 (Waterstredt Dep. (MetLife)) at 71:3-87:17; Ex. 65 (Smith Dep. (PIMCO)) at 202:15-221:17; Ex. 66 (Robertson Dep. (BlackRock)) at 106:3-128:18.

[104] Ex. 67 at 3-5 (recognizing that most of the servicing "improvements" in the proposed settlement are designed "[t]o incentivize BofA to service mortgage loans prudently *at industry standard levels*) (emphasis added); Ex. 16 (Levitin Report) at ¶¶ 218-253.

[105] Ex. 69 at BNYM_CW-00276324; Ex. 32 at § 7.02.

10[redacted]. *See, e.g.*, Ex. 15 (Langbein Dep.) at 219:2-19 (entry into forbearance was "not rested on an express term of the instrument" and conceding "there is nothing in [the PSA] that says the Trustee can unilaterally waive the

Nor is there any legal authority supporting the Trustee's assumption that it had the power to purportedly prevent an Event of Default from occurring. [redacted]

Thus, an Event of Default occurred no later than December 17, 2010, and continues uncured through today. Accordingly, the Trustee was subject to the prudent person standard throughout the settlement negotiations, and it is still subject to that standard today.[108]

* * * *

As a result of BNYM's fiduciary status and additionally because of the Event of Default, BNYM's actions must be measured against the standard of whether BNYM used the same degree of care and skill as a prudent person would in the conduct of such person's own affairs.[109] As detailed below, BNYM's settlement conduct was not prudent because (1) BNYM failed to investigate important issues that impacted the rights of investors; (2) BNYM merely rubber stamped the settlement negotiated by the Inside Institutional Investors without making an independent and informed decision; (3) BNYM did not consider how the settlement would impact any of the *individual* 530 Covered Trusts; and

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right of the certificate holders to receive the notice that an event of default has occurred and has gone unremedied"); Ex. 70 (Landau Dep.) at 151:9-24 [redacted]); *see also* Ex. 71 (Lundberg Dep.) at 411:14-24; Ex. 46 (Griffin Dep.) at 148:22-25.

[107] Ex. 70 (Landau Dep.) at 329:23-330:24 [redacted]

[108] Ex. 32 at § 8.01

[109] *Id.*; *see also* Restatement (Third) of Trusts § 90 ("The trustee has a duty to the beneficiaries to . . . manage the funds of the trust as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the trust.").

(4) the Trustee did not believe it had any responsibility to represent absent certificateholders despite the clear terms of the PSAs and hornbook trust law requiring BNYM to act on behalf of all certificateholders. Each of these acts or omissions violated BNYM's duty of care to certificateholders.

B. BNYM Unreasonably Failed to Investigate Critical Issues Throughout the Settlement Process

The duty of care "will ordinarily involve investigation appropriate to the particular action under consideration, and also obtaining relevant information about such matters as the contents and resources of the trust estate and the circumstances and requirements of the trust and its beneficiaries." Restatement (Third) of Trusts § 77 cmt. b. BNYM here breached its duty of due care to all certificateholders by failing to investigate the full nature, scope, and extent of BofA's liability before agreeing to a settlement of that liability.

1. BNYM [redacted] in the October 18, 2010 Notice of Non-Performance

One of the first decisions BNYM made with respect to the settlement negotiations was to enter the forbearance agreement for the unprecedented purpose [redacted] while receiving a comprehensive indemnity from Bank of America in exchange. *See* Section I.C.2, *supra*. Even if this decision did not amount to a conflicted action in violation of the duty of loyalty (which it did), doing so was beyond BNYM's power as Trustee and was unreasonable. [redacted]

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[110] Ex. 45; Ex. 36 (Kravitt Dep.) at 370:18-24; 371:4-16; 545:13-19 [redacted]

[redacted]

The 60-day cure period that the forbearance agreement attempted to stop was triggered by the detailed allegations contained in the Inside Institutional Investors' October 18, 2010 Notice of Non-Performance. Invoking section 7.01(ii) of the PSAs, the Notice of Non-Performance itemized the ways in which the Master Servicer had failed "to observe and perform, in material respects, the covenants and agreements imposed on it by the PSAs."[111] Among other things, the letter detailed that the Master Servicer had: failed to give notice to the other parties of breaches of representations and warranties as required by PSA section 2.03(c); failed to enforce the sellers' repurchase obligations as required by section 2.03; failed in its prudent servicing obligations under section 3.01; failed to foreclose or liquidate defaulted loans as required under section 3.11(a); failed under section 3.11 to require its parent company to bear the costs of loan modifications; and utilized affiliated vendors who overcharged the Covered Trusts for costs and services in violation of section 3.14.[112] The Notice of Non-Performance further gave notice that each of the failures to perform by the Master Servicer were continuing and that each, if they continued for an additional 60 days, would independently constitute an Event of Default.[113]

[redacted]

[111] Ex. 30 at 2.
[112] *Id.* at 2-4.
[113] *Id.* at 4-5; Ex. 65 (Smith Dep. (PIMCO)) at 204:16-205:18.

[redacted] [redacted] [redacted] [redacted] It was manifestly unreasonable for the Trustee to take the unprecedented and unauthorized action of forbearing on an Event of Default. Doing so benefitted the Trustee and Countrywide/BofA but deprived certificateholders of their post-Event of Default rights. Moreover, entering settlement negotiations and ultimately agreeing to the proposed settlement [redacted] is patently unreasonable under the circumstances.

2. BNYM did not investigate the underlying liabilities of Countrywide and BofA that are being settled, including a review of the Countrywide loans

In addition [redacted] BNYM did next to nothing to investigate the strength of the claims against Bank of America and Countrywide that are being settled and released by the proposed settlement. *See* Section III, *infra*. Despite being aware of the allegations concerning the quality of the loans in the Countrywide RMBS,[116] [redacted] As discussed in detail below, as well as in the expert reports of Charles D. Cowan, Ph.D., RRMS Advisors' analysis was woefully inadequate and facially flawed. *See* Section III.B.1, *infra*. BNYM admits that it did not engage in any loan

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[114] *See* Ex. 36 (Kravitt Dep.) at 38:2-18; Ex. 34 (Bailey Dep.) at 217:14-236:20; Ex. 46 (Griffin Dep.) at 170:19-174:21; 194:20-196:3.

[115] Ex. 71 (Lundberg Dep.) at 505:13-19.

[116] *Id.* at 160:5-22; Ex. 13 (Crosson Dep.) at 159:10-163:16.

[117] *See* Ex. 71 (Lundberg Dep.) at 453:4-455:15; 459:2-18; 461:11-16; 482:14-483:11; 490:6-494:2; 495:23-496:8; 505:13-19; Ex. 34 (Bailey Dep.) at 85:17-86:25; 305:13-16; Ex. 13 (Crosson Dep.) at 153:9-155:3; 164:6-10.

file review to evaluate the scope and severity of the representation and warranty breaches in the Covered Trusts,[118] [redacted] Contrary to the settlement proponents' claims, loan file review is a standard and manageable method of measuring the extent of breaches in RMBS trusts. *See* Section III.B.1.a.ii, *infra*. BNYM itself has pursued put-back remedies against a loan seller on the basis of loan file review.[120] Further, BNYM made no attempt to investigate or value servicing and document exception liability, notwithstanding that the Settlement Agreement releases those liabilities.[121]

When Loretta Lundberg was asked to detail the factual investigation the Trustee conducted "in support of this settlement" she responded: "We reviewed the terms of the Settlement Agreement. We consulted with experts on various aspects of the Settlement Agreement. And we had the support of the institutional investors to enter into the Settlement Agreement."[122] When then asked what legal investigation the Trustee conducted, Ms. Lundberg stated that BNYM "consulted with two experts on some legal issues, Professor Gaines [sic] and Professor Adler" as well as consulting with and being guided by Mayer Brown.[123] But these legal experts [redacted] *See* Section II.C.2, *infra*. And to the extent BNYM

[118] *See, e.g.*, Ex. 34 (Bailey Dep.) at 102:8-105:19.
[119] *Id.* at 258:8-19.
[120] Ex. 72.
[121] *See, e.g.*, Ex. 36 (Kravitt Dep.) at 495:2-11; 485:12-486:11.
[122] Ex. 71 (Lundberg Dep.) at 241:19-242:9.
[123] *Id.* at 242:10-243:12.
[124] Ex. 73 at BNYM_CW-00273355.

conducted any legal investigation beyond these reports, BNYM has refused to disclose it on the basis of privilege and consequently it cannot be used to support BNYM's petition.[125]

BNYM representatives testified that [redacted] However, once the Trustee undertook settlement negotiations, it had to do so reasonably, in good faith, and consistent with its fiduciary duties.[127] BNYM's [redacted] was both unreasonable and a violation of its fiduciary duties.[128] Such conduct also contradicts the Trustee's contention that it evaluated the "strengths and weaknesses of the claims being settled."[129]

3. BNYM [redacted] despite having all of its conduct covered by an indemnity

When the Inside Institutional Investors sent their Notice of Non-Performance on October 18, 2010, the investors and the Trustee held a tremendous amount of leverage to pressure BofA to obtain a large settlement or else face a lawsuit from BNYM and the investor group. Instead of maximizing this leverage, BNYM, with the acquiescence of the Inside Institutional Investors, acted to protect itself and its business relationship with BofA by entering a forbearance agreement that purported to stop the Event of Default clock from

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[125] *See, e.g.*, Ex. 71 (Lundberg Dep.) at 242:21-244:9.
[126] *See* Ex. 46 (Griffin Dep.) at 195:22-197:9.
[127] Ex. 14 (Frankel Report) at 9 ("Even if the Trustee had acted within its enumerated powers, the assertion and exercise of this power must be accompanied by the duties of loyalty and care.").
[128] Ex. 15 (Langbein Dep.) at 100:19-101:18; 122:14-124:17; 243:1-7 (acknowledging BNYM's fiduciary duties to evaluate the strengths and weaknesses of the claims being settled; evaluate the terms, benefits and consequences of the proposed settlement; undertake a legal and factual investigation; and determine the full extent of BofA's liability).
[129] Ex. 1 at Ex. B ¶ i (also found at Doc. No. 7).

expiring. [redacted] Rather than focusing on maximizing leverage against BofA, Mr. Kravitt testified that his strategy during the negotiations was to focus on those issues he thought all of the parties would agree on.[131]

[redacted] In fact, a publicly-disclosed e-mail from Ms. Patrick to her clients shows that in the summer of 2010, Gibbs & Bruns was actively seeking to prevent its clients from pursuing a more aggressive strategy.[133] [redacted]

The Trustee [redacted] and embark on a path straight to settlement without conducting any rational or measured risk analysis of the litigation uncertainties BNYM now points to as a justification for settling. [redacted]

BNYM did none of these things.[137]

[130] *See* Ex. 36 (Kravitt Dep.) at 163:13-25; Ex. 34 (Bailey Dep.) at 246:17-247:7; Ex. 24 (Stanley Dep.) at 283:19-284:4.
[131] Ex. 36 (Kravitt Dep.) at 358:8-13.
[132] *E.g.*, Ex. 37; Ex. 71 (Lundberg Dep.) at 134:23-135:6.
[133] *See* Ex. 74, *available at* http://newsandinsight.thomsonreuters.com/uploadedFiles/Reuters_Content/2011/09_-_September/Patrick8.10email.pdf.
[134] Ex. 75.
[135] Ex. 76.
[136] Ex. 77 (Burnaman Dep.) at 113:6-115:24.
[137] Ex. 78 (Coates Report (Doc. No. 530)) at 12-13; Ex. 77 (Burnaman Dep.) at 131:9-25; 134:15-23.

BNYM's failure to use its leverage against BofA or to conduct a meaningful investigation of the liabilities being settled (including through a loan file review) is even more egregious because all the costs of any such investigation would have been covered by others. As a result of the December 10 Indemnity, the Trustee had a full, 100% indemnity from BofA for all of its legal fees and expenses incurred "in connection with . . . ongoing discussions regarding the [Inside Institutional Investors'] October 18 Letter."[138] Additionally, to the extent that BNYM was acting at the instruction of the Inside Institutional Investors, the Inside Institutional Investors were required to indemnify the Trustee.[139] Yet, rather than use this blank check to conduct loan file sampling, hire experts to thoroughly investigate the claims,[140] or otherwise seek to understand the extent of BofA's liability, BNYM sat on the sidelines while the Inside Institutional Investors negotiated a settlement for 530 trusts, most of which they did not hold a 25% interest.

C. <u>The Trustee Merely Rubber Stamped the Settlement Agreement That Was Presented to It by the Inside Institutional Investors</u>

1. BNYM played no role in the negotiation of the settlement amount

In one of the more concrete examples of BNYM failing to represent the certificateholders and acting in violation of its fiduciary duties, BNYM allowed the Inside Institutional Investors to negotiate the most critical settlement term: the amount. Randy Robertson of BlackRock [redacted]

[138] Ex. 49.
[139] Ex. 52 (Sept. 21, 2011 Hearing Tr.) at 7:5-24; Ex. 79 (Patrick Dep.) at 98:25-99:6.
[140] *See, e.g.*, Ex. 80 (Laughlin Dep.) at 193:19-25 ([redacted]

[redacted]

Trustee representatives also confirmed that the Trustee was not meaningfully involved in the negotiations concerning the settlement amount:

- Jason Kravitt, the chief negotiator for BNYM: "I don't know if B of A offered 8.5 and [the Inside Institutional Investors] took it tentatively or Gibbs & Bruns made the offer of 8.5 and B of A accepted it tentatively. I don't know how the last, the final number – I don't know who proposed it and who accepted the final number."[142] Mr. Kravitt also said that BNYM "never stated to the three parties what the Bank of New York's number was that it would be willing to accept."[143]

- Loretta Lundberg, managing director for BNYM's corporate trust division and the individual who signed the verified petition: negotiation of the settlement amount "was largely between the institutional investors and Bank of America." The "final number was communicated" to BNYM only after Bank of America and the Inside Institutional Investors "had reached an agreement."[144]

- Robert Bailey, lead in-house counsel for the Trustee: BNYM did not approve settlement demands made by Gibbs & Bruns.[145] "Q: So if Ms. Patrick and her clients decided to make a settlement offer to settle the claims in the covered trusts, they were doing that on their own? . . . A: To the best of my knowledge, yes."[146] [redacted]

The Trustee's complete lack of involvement in the negotiation of the settlement amount is reflective of BNYM's general passivity during the negotiations, [redacted] evidenced by e-mails from Mr. Kravitt to the

[141] Ex. 66 (Robertson Dep. (BlackRock)) at 285:23-286:5.
[142] Ex. 36 (Kravitt Dep.) at 508:25-509:6.
[143] *Id.* at 511:7-9.
[144] Ex. 71 (Lundberg Dep.) at 229:22-230:13.
[145] Ex. 34 (Bailey Dep.) at 76:15-77:2; 81:11-18.
[146] *Id.* at 77:18-24.
[147] *Id.* at 81:11-18.

other settlement proponents.[148] Such passive conduct is plainly unreasonable from a fiduciary whose beneficiaries would be bound by any settlement and is flatly inconsistent with its fiduciary duty (acknowledged by BNYM's own experts) to maximize recoveries for the certificateholders.[149] This passivity also falls short of what a prudent person would do under the circumstances in the conduct of its own affairs.

2. BNYM controlled and limited the information it provided to its "independent" advisors, and even instructed them as to what result they should reach

The Trustee relies on the opinions it obtained from "independent experts" to justify its entry into the settlement.[150] In reality, [redacted]

[redacted] Unsurprisingly, in light of this clear direction from Trustee

[148] Ex. 81 (Bostrom Dep. (Freddie Mac)) at 260:20-23 [redacted]; *see also* Ex. 82; Ex. 83.
[149] Ex. 15 (Langbein Dep.) at 204:3-206:4; *see also* Ex. 70 (Landau Dep.) at 245:4-246:6.
[150] *E.g.*, Doc. No. 1 at ¶ 61.
[151] Ex. 73 at BNYM_CW-00273355.

counsel, both of the resulting opinions in fact concluded that BofA's arguments were "reasonable."[152]

Not only did the Trustee [redacted] it also severely limited the information available to all of the advisors and told them to rely on BofA's self-interested representations:

- Capstone Valuation Services, retained by BNYM to perform a valuation of Countrywide, accepted key facts from BofA,[153] and simply assumed that BofA paid fair value for Countrywide.[154]

- Professor Robert Daines, retained by BNYM to opine on BofA's successor liability for Countrywide, relied on BofA's assertions without verifying that they were true.[155] He was not provided key merger documents and communications,[156] and while his conclusions depend on whether asset-stripping occurred, [redacted] Finally, Daines did not consider other legal theories of recovery, did not weigh the likelihood of success of any successor liability theory, and did not consider BofA's direct servicing liability or its liability as a successor master servicer under §§ 6.02 & 6.04 of the PSAs.[158]

- In his opinion regarding the settlement amount, Brian Lin [redacted] BNYM also limited the scope of his work to simply comparing the positions of BofA and the Inside Institutional Investors rather than conducting an independent analysis.[162] [redacted]

[152] Ex. 84 (Daines Report (Doc. No. 540)) at Ex. 3 at 7 ("At the very least . . . BAC has a reasonable argument that a successor liability claim would be defeated."); Ex. 85 (Adler Report) at 13 ("[I]t appears to be a reasonable position that a determination of whether a breach materially and adversely affects the interests of Certificateholders should turn on the harm caused by the breach.").
[153] Ex. 86 (Bingham Dep.) at 105:2-12.
[154] Ex. 87 (Capstone Report) at 5.
[155] Ex. 84 (Daines Report) at Ex. 3 at 8 n.3.
[156] Ex. 78 (Coates Report) at 22-24.
[157] Ex. 88 (Daines Dep.) at 156:11-157:19.
[158] Ex. 78 (Coates Report) at 8-11.
[159] Ex. 55 (Lin Dep.) at 95:20-98:14.
[160] *Id.* at 439:24-441:16 [redacted]
[161] *Id.* at 197:16-200:4 [redacted]
[162] *Id.* at 73:22-74:5 ("My task was to arrive [at] a settlement number . . . with the parameter of assume the information [that] was given to me is correct . . . .").

[redacted]

- Professor Barry Adler's opinion regarding loss causation did not weigh the likelihood that BofA's arguments would be accepted by a court.[164] [redacted]

Thus, the Trustee did not seek the *advice* of independent experts, but rather sought opinions that would justify the Trustee's pre-decided conduct—opinions the Trustee secured by limiting the information the advisors received, confining the scope of their work, and giving them assumptions that effectively blocked a meaningful analysis. The Trustee cannot rely on the advice of advisors who are kept ignorant of material facts. *See Lathrop v. Mathers*, 143 A.D. 376, 380 (1st Dep't 1911) ("the record shows that all of the material facts were not stated to counsel, and therefore his advice cannot avail the defendants" of an advice of counsel defense). Furthermore, a trustee's reliance on experts is not a "whitewash" and does not provide a defense that a trustee acted reasonably. *See*, *e.g.*, *Gregg v. Transportation Workers of America Intern.*, 343 F.3d 833, 843 (6th Cir. 2003) (discussing fiduciary duties in the context of ERISA); *see also Donovan v. Cunningham*, 716 F.2d 1455, 1467, 1474 (5th Cir. 1983) ("[A] a pure heart and an empty head are not enough . . . An independent [expert report] is not a magic wand that fiduciaries may simply waive over a transaction to ensure that their responsibilities are fulfilled."). Ultimately, trustees are responsible for making careful and thorough decisions.

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[163] *Id.* at 238:13-239:15.
[164] Ex. 85 (Adler Report) at 12-13.
[165] Ex. 73.

In light of these undisputed facts, the Trustee's reliance on § 8.02(ii) of the PSAs is misplaced. That section permits the Trustee to rely "in good faith" on the "advice of any . . . counsel, financial advisers or accountants."[166] Even assuming that BNYM's advisors were "counsel, financial advisers or accountants," BNYM did not seek or obtain any "advice." By the time the experts issued their opinions, BNYM had already decided what it was going to do and merely sought the cover of conforming opinions. In any event, § 8.02(ii) cannot provide protection here because BNYM did not act in good faith when it confined the advisors' tasks such that their opinions would conform to BNYM's preordained position.

3. BNYM's Trust Committee did not provide a meaningful check on the Trustee's Conduct

BNYM's Structured Finance Corporate Trust Committee, which ultimately made the decision to approve the settlement, was not fully informed, engaged in no serious evaluation of the Settlement Agreement, and did not serve as any meaningful check on the Trustee's settlement process. [redacted]

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[166] Ex. 32 at § 8.02(ii).
[167] *See* Ex. 34 (Bailey Dep.) at 170:8-170:25.
[168] *Id.* at 173:16-17.

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[redacted] Richard Stanley, the Chair of the Trust Committee, testified that he [redacted] never read the advisors' reports.[172]

Compared with the limited information the Trust Committee received, the list of what they did not receive is staggering. [redacted] The Trust Committee also was not told:

- [redacted]
- [redacted]
- [redacted]
- [redacted]
- [redacted]

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[169] Ex. 24 (Stanley Dep.) at 165:1-12; Ex. 13 (Crosson Dep.) at 39:9-16; 40:13-41:25.
[170] *See* Ex. 90; Ex. 19 (Baker Dep.) at 68:1-69:1; 102:13-103:16.
[171] Ex. 34 (Bailey Dep.) at 158:3-159:3; Ex. 71 (Lundberg Dep.) at 212:3-11.
[172] Ex. 24 (Stanley Dep.) at 265:7-22; 226:9-228:6.
[173] Ex. 13 (Crosson Dep.) at 197:17-21.
[174] Ex. 24 (Stanley Dep.) at 225:15-226:5.
[175] Ex. 33 (Chavez Dep.) at 73:21-74:8.
[176] Ex. 34 (Bailey Dep.) at 191:11-15; Ex. 24 (Stanley Dep.) at 236:11-237:4; Ex. 33 (Chavez Dep.) at 180:9-17; Ex. 1 at § 6(a)(i).
[177] Ex. 24 (Stanley Dep.) at 231:17-232:6; Ex. 34 (Bailey Dep.) at 197:25-198:16. [redacted] Ex. 33 (Chavez Dep.) at 72:10-17.

- [redacted]
- [redacted]
- [redacted][181]
- [redacted]
- [redacted]
- [redacted]

The Trust Committee lacked a sufficient factual basis to support its approval of the Settlement Agreement. Ironically, and revealingly, Mr. Stanley [redacted][6]

In short, the Trust Committee had limited information about the settlement and did not conduct any meaningful examination. Rather, the Trust Committee simply served as a rubber stamp to [redacted] approve the settlement.[187]

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[178] Ex. 24 (Stanley Dep.) at 232:7-12; Ex. 34 (Bailey Dep.) at 207:24-208:10.
[179] Ex. 24 (Stanley Dep.) at 232:16-233:3.
[180] *Id.* at 233:4-10; Ex. 34 (Bailey Dep.) at 193:21-194:2.
[181] Ex. 24 (Stanley Dep.) at 233:11-18; Ex. 34 (Bailey Dep.) at 197:6-24.
[182] Ex. 24 (Stanley Dep.) at 235:4-236:10.
[183] *Id.* at 237:16-242:17.
[184] *Id.* at 250:10-252:25.
[185] *Id.* at 184:18-186:17.
[186] *Id.* at 188:5-189:10.
[187] Ex. 13 (Crosson Dep.) at 195:20-197:21.

D. Despite Having 530 Separate Trusteeships, BNYM Negotiated an Aggregate Settlement Without Considering How the Settlement Would Benefit Any Individual Trust

This is a proposed settlement of 530 separate trusts, each governed by a separate agreement and each of which have unique assets.[188] BNYM "owes each trust a separate and distinct duty of care."[189] Because the trusts are competing with one another for a limited amount of settlement funds, a prudent trustee would have to evaluate the settlement on a trust-by-trust basis.[190] [redacted][1] The Trustee's reliance on the Inside Institutional Investors to negotiate a settlement amount for all the trusts makes its lack of prudence particularly problematic because, as discussed below, those investors did not hold the requisite 25% voting rights in 341 of the 530 Covered Trusts.

E. By Its Own Admission, BNYM Did Not Represent the Non-Participating Certificateholders in the Settlement Negotiations

BNYM, as Trustee, also left large segments of the certificateholders in the 530 Covered Trusts unrepresented in the settlement negotiations. This fact is a further indication of BNYM's unreasonable settlement conduct and failure to meet its fiduciary obligations to the certificateholders.

It is undisputed that the Inside Institutional Investors lacked 25% of the voting rights in 341 of the Covered Trusts at the time the parties signed the proposed settlement

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[188] *Id.* at 79:7-80:22.
[189] Ex. 16 (Levitin Report) at ¶ 79; Ex. 13 (Crosson Dep.) at 80:12-15 [redacted]).
[190] Ex. 16 (Levitin Report) at ¶¶ 76-87;*see also id.* ¶ 82 (discussing how the proposed allocation methodology under the settlement is "[a] perfect example of the problems with treating the trusts as an aggregate entity . . .").
[191] *See, e.g.*, Ex. 91 (Buechele Dep.) at 69:3-22.

agreement.[192] The fact that the Inside Institutional Investors did not hold 25% of the voting rights in the majority of the trusts was known to the Trustee before it entered into the settlement.[193] Indeed, before signing the Settlement Agreement, the Trustee was aware that the Inside Institutional Investors had *no* voting rights in many trusts, and that in dozens of others they lacked even 10% of the voting rights.[194] During the course of this litigation, the Inside Institutional Investors have further made clear that they never acted on behalf of any certificateholders other than themselves.[195]

Given that the Inside Institutional Investors did not purport to represent the interests of any certificateholder(s) in the Covered Trusts other than themselves, one might expect that the Trustee would represent the interests of the absent certificateholders.[196] It did not. Bob Bailey, BNYM's in-house counsel who had primary responsibility for overseeing BNYM's participation in the settlement, testified unequivocally that Mayer Brown was *not* hired to represent the absent certificateholders' interests:

> Q: When the trustee hired counsel to represent it in a situation in which the trustee was serving as trustee, did that counsel act on behalf of and for the protection of the certificate holders?
>
> A: No. . . . My understanding is Mayer Brown represented the trustee full stop. *It did not represent the interests of the certificate holders*.[197]

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[192] Ex. 8 at ¶ 5.
[193] Ex. 92.
[194] *Id.*
[195] Doc. No. 250 at 13 ("The Institutional Investors have *never* asserted a derivative claim or otherwise purported to act on behalf of all Certificateholders, the Trustee, or the Covered Trusts.") (emphasis in original).
19[redacted] Ex. 70 (Landau Dep.) at 240:4-242:21; Ex. 15 (Langbein Dep.) at 109:23-112:10. [redacted].
[197] Ex. 34 (Bailey Dep.) at 148:16-149:4 (emphasis added).

Mr. Bailey further testified that [redacted] Mr. Kravitt likewise testified that he did not tell Ms. Patrick he represented absent certificateholders, but rather told her only that "I was representing the Bank of New York Mellon as trustee."[199] The Trustee's failure to represent the interests of the absent certificateholders breached the Trustee's fiduciary duties to those certificateholders.

III. The Court Should Not Approve This Settlement Because The Settlement Is Not Fair and Reasonable

A. The Settlement Agreement Does Not Actually Require BofA to Pay $8.5 Billion

Contrary to the Trustee's representation that the proposed settlement "requires a payment of $8.5 billion,"[200] the Settlement Amount is in fact a cap, not a requirement. The Trustee agreed to two provisions in the Settlement Agreement that allow BofA, at its discretion, to exclude Covered Trusts from the proposed settlement and retain those trusts' allocable share of the $8.5 billion.[201]

The first gives BofA the right to exclude any Covered Trusts in which even one bond is insured by a financial guaranty company, unless that insurer agrees not to pursue any rights it has against BofA.[202] The second provision suggests that BofA has an either unspecified or unfettered right to exclude trusts on some basis other than insurance

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[198] *Id.* at 150:21-151:4.
[199] Ex. 36 (Kravitt Dep.) at 133:11-12; *see also id.* at 373:24-25 ("We had one client, the Bank of New York Mellon as trustee.").
[200] Doc. No. 1 at 1.
[201] Ex. 1 at §§ 3(d)(iv); 4(b).
[202] *Id.* at § 3(d)(iv).

coverage.[203] Nothing in any of the public documents filed by the Trustee identifies the number of trusts that will be excluded or the amount of the $8.5 billion that will be kept by BofA under these provisions. Neither the Court nor the Intervenors know how much of the $8.5 billion will be retained by BofA, in part, because the Trustee has not established the per-trust allocation of the Settlement Amount.[204]

The net effect of these provisions is that BofA can exclude trusts and keep those trusts' allocable share(s) of the $8.5 billion up until the exhaustion of all appeals.[205] Thus, this Court is presented with a request to approve a settlement of which the scope and actual amount remain unknown and is entirely under BofA's control. Moreover, BofA continues to retain the right to withdraw from the settlement completely—*even if and after this Court approves it*—based on a confidential metric that, likewise, remains entirely under BofA's control.[206]

At an absolute minimum, approval of the proposed settlement is premature. The Court should instruct the Trustee (and BofA, if necessary) to disclose: (1) which trusts will be included in the settlement and which will be excluded, (2) the allocable share for each Covered Trust, and (3) whether BofA will seek to exercise its contractual right to withdraw from the Settlement Agreement.

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[203] *Id.* at § 4(b).
[204] *See* Ex. 71 (Lundberg Dep.) at 446:13-447:12; *see also* Ex. 94 (Sabry Dep.) at 67:9-70:12; 132:5-133:13 (testifying that Trustee counsel instructed NERA to stop work on calculating trust level losses, the first step in the Trustee's allocation methodology, when it became apparent that the Article 77 proceeding was not moving along as quickly as the Trustee anticipated).
[205] Ex. 1 at § 3(d)(iv).
[206] *Id.* at § 4(a).

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B. The Settlement Amount is Unreasonably and Unjustifiably Small in Light of the Claims Sought to be Released and the Claim-Related Information Available to the Trustee

Even if BofA pays the entire Settlement Amount, it remains unreasonably and unjustifiably small because: (1) the Trustee accepted a damages analysis that is deeply flawed and significantly understates BofA's repurchase liability, (2) the Trustee further depressed the settlement amount with unjustified litigation discounts, and (3) the Settlement Payment only covers repurchase claims, even though the Settlement Agreement releases BofA from much broader liability.

1. Brian Lin's Damages Analysis, Which is Deeply Flawed, Was Used by the Trustee to Justify the Unreasonably Low Settlement Amount

The $8.5 billion settlement amount is unreasonably low in light of evidence in the record, including data indicating that losses to the Covered Trusts will exceed $100 billion. To justify the pennies-on-the-dollar settlement amount, the Trustee hired Brian Lin of RRMS Advisors, who calculated what he considered to be a reasonable settlement range of $8.8-11 billion.[207] Mr. Lin's report and the analysis therein were unsound on every level. The Trustee accepted Mr. Lin's conclusion without ever reviewing a single loan file, despite the Trustee's contractual right to access loan files.[208] The Trustee's acquiescence to such a small amount, without ever engaging in any meaningful investigation of the Covered Trusts' claims shows the unreasonableness both of the Trustee's approach and the resulting settlement amount. There is nothing about Mr. Lin's approach that can instill confidence that the $8.5 billion proposed settlement amount is reasonable.

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[207] Ex. 68 (Lin Report) at 8.

[208] Ex. 32 at § 3.07.

a. *The Brian Lin Approach*

Mr. Lin received competing data advanced by BofA, on the one hand, and the Inside Institutional Investors, on the other. Mr. Lin made unsupported assumptions about the data and adopted a funnel-like approach to input the data and estimate losses to the Covered Trusts. He then applied assumptions regarding the incidence of breaches of representations and warranties in the Covered Trusts and a so-called "success rate." The result of that approach was a purportedly reasonable settlement range of $8.8-11 billion.

i. In the First Phase of Mr. Lin's Funnel Approach, Mr. Lin Materially Understated the Covered Trusts' Losses

The first part of Brian Lin's funnel purports to calculate the total losses to the Covered Trusts. Brian Lin's estimation of cumulative losses in the Covered Trusts is wrong, opaque, and underinclusive.[209]

Default rates directly impact losses because cumulative losses are the product of default and severity rates.[210] Mr. Lin was presented with default rates for different loan groups from the Inside Institutional Investors.[211] Notwithstanding the back-up data the Inside Institutional Investors sent him and the Trustee's counsel,[212] Mr. Lin understated certain of the default rates. Rather than rely on the Inside Institutional Investors numbers, which were supported by credible industry sources, or use historical information available from BofA or mortgage loan databases such as Intex or LoanPerformance, Mr. Lin relied on

[209] *See generally* Ex. 95 (Cowan Report (Doc. No. 537)).
[210] The default rate represents the percentage of dollars that are bound up in loans that are in default or are likely to go into default in the future. The severity rate is the percentage of those dollars that will be passed on to the trusts as losses after foreclosure and other loss mitigation activity of the servicer. *See id.* at 7.
[211] *See* Ex. 68 (Lin Report) at 1-3; Ex. 96.
[212] *See* Ex. 97.

his own "knowledge" and "belief."[213] Mr. Lin also purportedly relied on "market research," which he defined to include "research reports, news articles, [and] conversations I had with my colleagues."[214] As a consequence, there is no support for Mr. Lin's depressed default rates and subsequent loss estimates.

The second flaw in Mr. Lin's losses analysis runs even deeper because it completely ignores all losses suffered by investors other than those caused by the default of individual mortgage loans. The Trustee assumed—consistent with *BofA's* theory of its repurchase liability—that loan-level default was a condition precedent to repurchase liability.[215] As a result, the breach and success rate assumptions (discussed below) are applied only to the subpopulation of default loans or loans likely to go into default. However, breaches of representations and warranties can result in investor losses even where loans do not go into default.[216] In fact, across the industry, residential mortgage-backed securities have lost significant value.[217] These losses are unaccounted for in Mr. Lin's model.

Because losses were the jumping off point in Mr. Lin's approach, Mr. Lin's errors concerning losses to the Covered Trusts result in the Trustee's deeply flawed estimation of BofA's repurchase liability and its so-called reasonable settlement amount. While Mr. Lin estimated losses at $61.3 to $76.8 billion,[218] the Inside Institutional Investors estimated losses—based on the reliable data Mr. Lin and the Trustee ignored—at $107.8 billion.[219] Even the Trustee's own litigation expert estimated losses to the Covered Trusts at $84.7

[213] Ex. 55 (Lin Dep.) at 302:15-303:19; 268:22-269:6.
[214] *Id.* at 269:7-10.
[215] Doc. No. 1 at ¶ 70; *see also* Ex. 80 (Laughlin Dep.) at 189:8-17.
[216] Ex. 95 (Cowan Report) at 3.
[217] Ex. 98 at 648-52; Ex. 77 (Burnaman Dep.) at 234:9-23.
[218] Ex. 68 (Lin Report) at 8.
[219] Ex. 96 (note that this includes 13 trusts not included in the proposed settlement).

billion,[220] [redacted][redacted] It is thus apparent that Mr. Lin and the Trustee dramatically underestimated losses by as much as more than $ 40 billion.[222] Because the Settlement Amount is calculated based on losses to the Covered Trusts, the wide variance in loss estimations is troubling.

ii. In the Second Phase of Mr. Lin's Funnel Approach Mr. Lin Ignored a Massive Forensic Reunderwriting Analysis of Similar Loans Provided by Freddie Mac, and Instead Blindly Relied on BofA's Irrelevant GSE Experience

Once losses were (mis)calculated, Mr. Lin applied an assumed breach rate of 36%.[223] Mr. Lin's application of a 36% breach rate was a critical error in his approach. This number was allegedly derived from data provided *by BofA* about its experience in wholly distinct repurchase negotiations with Fannie Mae and Freddie Mac (collectively the Government-Sponsored Enterprises or "GSEs").[224]

During the settlement negotiations, the Inside Institutional Investors [redacted]

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[220] Ex. 99 (Burnaman Report) at 5.
[221] Ex. 77 (Burnaman Dep.) at 244:7-249:12; 255:5-257:10.
[222] The Inside Institutional Investors' admittedly reasonable estimate of losses ($107.8 billion), less Mr. Lin's lower bound estimate of losses ($61.3 billion). *See* Ex. 96; Ex. 68 (Lin Report).
[223] According to Mr. Lin, breach rate represents "the percentage of representation[s] & warranties breached for defected loans . . . ." Ex. 68 (Lin Report) at 2.
[224] *Id.* at 4, 8.

[redacted] Freddie Mac's then-General Counsel further testified that the Inside Institutional Investors [redacted]

Additionally, Freddie Mac's conservator, the Federal Housing Finance Agency ("FHFA"), later criticized Freddie Mac's settlement with BofA as methodologically unsound and influenced by business considerations.[228] Additional bases for the inapplicability of the GSE repurchase experience are detailed in Dr. Cowan's expert opinion of March 14, 2013.[229]

In contrast, the Inside Institutional Investors provided the results of actual reunderwriting of 250,000 loans similar to those in the Covered Trusts.[230] After eliminating the higher breach and success ranges in an effort to arrive at an estimate of BofA's repurchase liability, the Inside Institutional Investors reported *a 60% breach rate*.[231]

Despite this evidence, Mr. Lin (and the Trustee) adopted *BofA's* breach rate without verification or further inquiry. Had the Trustee sought to appropriately and

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[225] Ex. 81 (Bostrom Dep. (Freddie Mac)) at 262:8-16 (emphasis added); *see also* Ex. 64(Waterstredt Dep. (MetLife)) at 57:13-17 (acknowledging the different collateral make up of the GSE loans and the Covered Trusts); Ex. 66 (Robertson Dep. (BlackRock)) at 220:4-12.
[226] Ex. 81(Bostrom Dep. (Freddie Mac)) at 263:25-264:5.
[227] *Id.* at 228:12-231:17
[228] Ex. 100.
[229] Ex. 95 (Cowan Report) at 13-15.
[230] Ex. 68 (Lin Report) at 1-3.
[231] Ex. 96 at "Indicative Amount 4."

adequately investigate the Covered Trusts' claims against BofA and identify an accurate breach rate, it could have reviewed—or at least sampled—loan files from the Covered Trusts themselves. Indeed, the Trustee's own expert [redacted]

Loan file review is a generally accepted, common approach to repurchase cases.[233] The Trustee did it in a 2012 case against WMC Mortgage, LLC,[234] and Mr. Lin himself had never tried to establish a breach rate without reviewing the actual loan files.[235] And the Trustee had a contractual right to the loan files and other relevant materials from BofA without cost.[236] While the Trustee opposes loan file review on the grounds of cost, delay, and subjectivity, loan file review is [redacted] The Trustee overstates the delay and cost of loan file review by failing to acknowledge that a statistically significant sample could be comprised of less than 7,000 loans.[238] Despite the wealth of support for loan file review, BNYM unreasonably failed to obtain the files[239] and consequently cannot be said to have adequately investigated the claims against BofA.

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[232] Ex. 77 (Burnaman Dep.) at 280:23-282:18.
[233] Ex. 95 (Cowan Report) at 5.
[234] Ex. 72.
[235] Ex. 55 (Lin Dep.) at 155:16-156:4
[236] Ex. 32 at §§ 3.07 3.13.
[237] Ex. 77 (Burnaman Dep.) at 163:14-184:15.
[238] *See* Ex. 101 (Burnaman Rebuttal Report (Doc. No. 551)) at 3 (stating that Dr. Cowan advocates for an analysis of 50,000 loans, but ignoring the fact that Dr. Cowan also states that a sampling of less than 7,000 loans would yield statistically significant results); *see also* Ex. 77 *(*Burnaman Dep.) at 221:12-222:4; 222:21-223:6 [redacted]
[239] Ex. 46 (Griffin Dep.) at 275:6-276:8.

As set forth in Dr. Cowan's report, in the absence of identifying an actual breach rate based on a review of loan files from the Covered Trusts, the next best source for determining a breach rate is a pool of similar loans, like those the Inside Institutional Investors relied on.[240] That reunderwriting of 250,000 loans revealed a breach rate of 60%. Applying that breach rate to BNYM's litigation expert's loss estimate of $84.7 billion, BofA's repurchase liability is $50.8 billion.[241] Thus if the Trustee had filed a complaint, a $50 billion demand would have been fully justified. Nevertheless the Trustee settled for $8.5 billion. The cumulative effect of the Trustee applying a success rate and the settlement discounts discussed below was a $42.3 billion settlement discount.[242] By any measure, such a massive discount was unreasonable and not in the best interests of the Covered Trusts or the investor-beneficiaries.

The final taper in the Lin funnel is the so-called "success rate," which purports to quantify the percentage of breach loans that will be successfully put back to BofA. There are multiple problems with the way Mr. Lin applied—and the Trustee adopted—a success rate. To begin, BofA, Mr. Lin, and the Inside Institutional Investors do not share a common definition of what the success rate represents. Moreover, to the extent the success rate is intended to represent settlement decision-making in the face of the uncertainties of litigation, its use without analyzing the likelihood of potential outcomes is haphazard at best. Finally, [redacted]

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[240] *See* Ex. 96.

[241] This amount is exclusive of servicing and documentation claims.

[242] Whether and what settlement discount should be applied is a function of the strength of the Trustee's claims, and as set forth in the reports of Dr. Cowan, Professor Coates, and Professor Levitin, the Trustee failed to make a meaningful effort to analyze the strength of its claims, or quantify its probability of success.

[redacted] it was unreasonable for the Trustee to give BofA a 40% discount on its basis. Therefore, there is no basis to apply a success rate in this case. Whether and to what extent BofA must pay for breaches of representations and warranties should be based on evidence of its liability, not unverified and ill-defined assumptions.

The flaws in Mr. Lin's approach cannot be overstated. At every step of the way Mr. Lin made critical assumptions that were unverified and in some instances unsupported. As a result, Mr. Lin's report reflects significantly understated losses, an unreasonably low estimate of BofA's repurchase liability, and an unreasonable settlement range.

b. Because the Flaws in Mr. Lin's Approach Were Readily Apparent on the Face of His Report, the Trustee's Reliance on Mr. Lin's Report is Unreasonable and Unjustified

[redacted] but the Trustee's reliance on Mr. Lin's report is unjustified. First, Mr. Lin issued his report *after* the Settlement Amount had already been agreed to in principle. Thus, while the Trustee insists that Mr. Lin did not know the Settlement Amount, it is evident that the Trustee commissioned Mr. Lin's report not to investigate the Covered Trusts' claims, but to justify an already agreed-upon Settlement Amount.

Second, the flaws in Mr. Lin's report were clear on its face.[245] The Trustee takes the position that the mere *existence* of the report clothes it with authority to act upon it, regardless of its contents. Even now, when the Trustee has hired a litigation expert to review Mr. Lin's work, that expert (Mr. Burnaman) fails to make a meaningful inquiry into the data underlying Mr. Lin's analysis. [redacted]

[243] Ex. 55 (Lin Dep.) at 441:5-442:10; 448:5-449:4.
[244] Ex. 46 (Griffin Dep.) at 67:16-68:8
[245] Ex. 95 (Cowan Report) at 2; 5-15.

[redacted] This is part of the Trustee's pattern of adopting BofA's positions and disregarding countervailing evidence.[249] This loyalty to BofA's metrics flies in the face of the Trustee's fiduciary duties and its contractual obligation to act in good faith towards the certificateholders. Moreover, it reflects a calculated disregard for the best interests of the Covered Trusts and reaffirms that the Trustee never sought to maximize recoveries for the Covered Trusts despite its duty to do so.[250] It does reflect, however, what Professor Levitin describes as the "securitization triangle" and BNYM's motivations to protect BofA and preserve its business relationship.[251]

2. The Trustee Accepted Unjustified Legal Discounts Without Adequate Investigation

After accepting Mr. Lin's unreasonably low settlement range, the Trustee then further discounted the total amount. The Trustee based these discounts on Countrywide/BofA's legal defenses, including a causation defense and a recoverability

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[246] Ex. 77 (Burnaman Dep.) at 40:8-25.
[247] *Id.* at 80:2-81:14.
[248] *Id.* at 47:9-52:21.
[249] *Compare* Ex. 101 (Burnaman Rebuttal Report) at 3 n.6 (relying on an affidavit filed by BofA), *with* Ex. 77 (Burnaman Dep.) at 217:2-219:2 [redacted] *see also* Ex. 68 (Lin Report) at 8 (adopting BofA's breach rate); Ex. 77 (Burnaman Dep.) at 301:3-302:3; 340:6-342:2 ([redacted].
[250] Ex. 15 (Langbein Dep.) at 126:25-127:5; 206:1-4 (testifying the Trustee had a responsibility to act in the best interest of holders and to maximize recovery to the Covered Trusts).
[251] *See* Ex. 16 (Levitin Report) at ¶¶ 38-61.

defense.[252] As a threshold matter, any purported "analysis" conducted by the Trustee's advisors on these topics appears to be yet another post-hoc justification for a settlement number that had already been negotiated.[253] In any event, any discounts related to these two defenses were entirely unjustified and unsupported by any probability weighting that would have allowed the Trustee to actually gauge the likelihood of success in litigating claims against BofA.

a. Material and Adverse Discount

The Trustee unreasonably placed significant weight on BofA/Countrywide's causation defense. BofA/Countrywide took "the position that the Trustee would have to prove . . . that [a] breach caused Certificateholders to suffer a significant loss on the affected loan."[254] The Inside Institutional Investors, on the other hand, argued that "a breach is 'material and adverse' to the interests of Certificateholders if it would have affected their investment decision[.]"[255] Rather than support and develop the investors' legal position, the Trustee hired an advisor, Professor Barry Adler, to opine on whether BofA/Countrywide's causation argument was "reasonable."[256] In essence, the Trustee sought to justify BofA/Countrywide's legal position and in doing so, the Trustee attempted to devalue the Covered Trusts' claims.

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[252] Doc. No. 1 at ¶ 66 ("the Trustee's financial experts calculated a dollar range that could serve as a starting point for assessing the reasonableness of a settlement payment, to which the Trustee would be entitled to apply discounts based on the viability of Countrywide's and Bank of America's legal defenses."); *see also id.* ¶¶ 68-92.
[253] *Compare* Ex. 73 at BNYM_CW-00273355, *with* Ex. 85 at 13 (Adler Report) *and* Ex. 84 (Daines Report) at Ex. 3 at 7.
[254] Doc. No. 1 at ¶ 70.
[255] *Id.* ¶ 71.
[256] *Id.* ¶ 75; Ex. 73 at BNYM_CW-00273355.

As discussed in Dr. Cowan's report,[257] and as set forth in recent judicial opinions issued on this subject,[258] BofA/Countrywide's causation argument is wrong. Trusts suffer harm as a result of breaches even when loans do not experience a payment default. In fact, the loss to investors begins when the loan is made. A loan that contains breaches of representations and warranties generates a much higher risk, such that the loan should never have been made in the first place, or when sold to investors it should have been priced differently.[259] Thus, the investor who acquires loans with breaches of representations and warranties instantly suffers harm. Dr. Cowan's report elaborates on the ways in which breaches adversely affect trusts and investors, including by artificially inflating ratings and bond prices, increasing the risk of loss, depressing the level of confidence in the RMBS market, and overwhelming the protective mechanisms that were supposed to protect RMBS investors.[260] The Trustee ignored those harms—as well as the Inside Institutional Investors' articulation of harms[261]—when it hired Professor Adler to justify BofA/Countrywide's legal position on this issue.[262]

The Trustee committed another sizeable error when it accepted Countrywide/BofA's causation defense "as a compelling reason to discount [Mr. Lin's] settlement range[,]"[263] without accounting for the difference in text among each of the 530

[257] Ex. 95 (Cowan Report) at 3; 25-26.
[258] *See, e.g.*, *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, --- N.Y.S.2d ---, 2013 WL 1296525, at *2 (1st Dep't Apr. 2, 2013); *Assured Guaranty Mun. Corp. v. Flagstar Bank FSB*, 892 F. Supp. 2d 596, 602 (S.D.N.Y. 2012); *Syncora Guarantee Inc. v. EMC Mortgage Corp.*, 874 F. Supp. 2d 328, 334-35 (S.D.N.Y. 2012).
[259] *See* Ex. 77 (Burnaman Dep.) at 155:18-163:13.
[260] *See* Ex. 95 (Cowan Report) at 25-26.
[261] Ex. 64 (Waterstredt Dep. (MetLife)) at 51:20-52:5.
[262] Ex. 73 at BNYM_CW-00273355.
[263] Doc. No. 1 at ¶ 68.

Governing Agreements. As discussed in Professor Levitin's expert report, "many of the PSAs directly contradict the proposition for which the Trustee use[d] [Professor Adler's] report[.]"[264] Specifically, some of the Covered Trusts' PSAs include the following language:

> Any breach of a representation set forth in clauses . . . of Schedule III-A with respect to a Mortgage Loan . . . *shall be deemed to materially and adversely affect the Certificateholders.*[265]

This "deemed to materially and adversely affect" clause eliminates—with respect to at least some of the Covered Trusts—a substantial part of the purported risk related to Countrywide/BofA's causation defense. Despite this significant variance, the Trustee considered the weight of BofA/Countrywide's legal position in the aggregate, rather than on a trust-by-trust basis. Even the Trustee's own counsel acknowledged the danger in that: "It's always dangerous to generalize with regard to RMBS documentation because while it generally follows particular forms, there's lots of variations among the documents."[266] The Trustee should have analyzed the various Governing Agreements to determine the extent to which Countrywide/BofA's causation defense would or would not apply.

Finally, the Trustee actually gave this same discount to BofA as many as three different times in its analysis: (1) by beginning Mr. Lin's calculation of a settlement amount with the subpopulation of loans that had already defaulted or were likely to go into default, (2) by using an additional "success rate" discount that may include causation, and (3) by

[264] Ex. 16 (Levitin Report) at ¶ 144.
[265] *E.g.* Ex. 32; 103; Ex. 105; Ex. 106.
[266] Ex. 36 (Kravitt Dep.) at 77:19-22; *see also* Ex. 71 (Lundberg Dep.) at 116:12-14 ("each PSA is different, so you have to look at each individual PSA.").

further reducing the settlement amount based on BofA's legal defenses, i.e., the difference between Mr. Lin's range and the $8.5 Settlement Amount.

In sum, the Trustee's adoption of BofA's legal defense was wholly unjustified and may have been avoided if the Trustee had hired an advisor to help analyze and bolster arguments that *favor* the Covered Trusts, not justify the adversary's legal position.

b. Recoverability Discount

The Trustee also placed great weight on the issue of recoverability. Specifically, the Trustee concluded—based on a report issued by Capstone—that Countrywide would "be unable to pay any future judgment that exceeds, equals or even approaches the Settlement Payment."[267] It further concluded—based on a report issued by Professor Robert Daines—that "the legal positions of Countrywide and Bank of America are viable," and that there were "significant obstacles to a party seeking to assert successor liability claims, to piece the corporate veil or to apply similar legal theories[.]"[268] In placing such significant weight on BofA/Countrywide's recoverability defense, the Trustee was unreasonable in four respects.

First, just as with the material and adverse discount, the Trustee never performed or commissioned any probability weighting that would have allowed it to make an adequately informed decision about the strength of the Covered Trusts' claims against BofA. As Professor Coates sets forth in his expert report, "[i]n any rational decision analysis, it is important to translate qualitative judgments about likely outcomes of uncertain events into probability weightings."[269] He further states that "[t]his is basic to any economic (indeed, any rational)

[267] Doc. No. 1 at ¶ 81
[268] *Id.* ¶ 91.
[269] Ex. 78 (Coates Report) at 12.

analysis of any uncertain set of events.[270] Even the Trustee's own litigation expert, Phillip Burnaman, concedes that "any prudent comprehensive business decision will include both [qualitative and quantitative considerations.]"[271] Mr. Burnaman appears to be uniquely qualified on this issue because he has experience investing in litigation claims. In that context, he testified that when assessing litigation risk he [redacted] Yet, neither Professor Daines nor the Trustee engaged in such an analysis.[273]

Second, certain critical facts, which directly impact the Trustee's ability to recover against Countrywide and/or BofA, were left entirely uninvestigated.[274] For example, [redacted] Instead, Professor Daines—like Capstone—relied on information provided by BofA, the *adversary.* Even Countrywide's valuation—a most fundamental fact in assessing the likelihood of

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[270] *Id.*
[271] Ex. 99 (Burnaman Report) at 9.
[272] Ex. 77 (Burnaman Dep.) at 110:9-115:24; *see also* Ex. 107 (article Mr. Burnaman relies on regarding litigation risk analysis).
[273] *See* Ex. 77 (Burnaman Dep.) at 130:10-131:25; 142:8-144:5 [redacted]
[274] *See* Ex. 78 (Coates Report) at 14 (stating that "[h]ad the Trustee obtained such statements and/or specific representations as to elements of the Asset-Stripping Transactions that were relevant to the likelihood of success on the fraudulent conveyance, fiduciary duty, contract or direct and successor liability claims, the Trustee would have been able to make an informed judgment about the positions that BAC and CFC were taking in the Settlement discussion. Instead, the Trustee apparently decided to [redacted]
[275] Ex. 88 (Daines Dep.) at 166:2-181:1.

recovery for the Covered Trusts—was left to unverified assumptions based on self-serving statements by BofA.[276]

Third, the Trustee failed to adequately consider other potential sources of recovery, including fraudulent conveyance claims, fiduciary duty claims against entities involved in the Red Oak Merger and the subsequent related transactions, the contractual successor liability of the BofA master servicer based on PSA sections 6.02 and 6.04, and direct liability claims for BofA's post-merger servicing failures.[277]

Fourth, the Trustee was unreasonable in assuming away the applicability of New York law.[278] Professor Coates' expert report notes that "the Trustee would have had a choice as to where to bring an action, on whatever basis, and thus could have brought Claims in New York courts."[279] Moreover, and as detailed in Professor Coates' expert report, there are multiple reasons why New York law might apply, including the fact that the majority of the PSAs are expressly governed by New York law.[280] As Professor Daines noted in his report, there is a potential for a ruling more favorable to the Trustee under New York law.[281]

In any event, Professor Daines' opinion has been effectively rendered moot in light of Justice Bransten's recent ruling in *MBIA Insurance Corp. v. Countrywide Home Loans, Inc.*, Index No. 602825/2008 (Apr. 29, 2013) (attached as Ex. 108). Justice Bransten concluded that New York law applies to the plaintiff's claim regarding BofA's successor liability for Countrywide,

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[276] *See, e.g.,* Ex. 87 (Capstone Report) at 3, 5.
[277] Ex. 78(Coates Report) at 7-11.
[278] Doc. No. 1 at ¶¶ 82-92
[279] Ex. 78 (Coates Report) at 20.
[280] *Id.* at 20-22.
[281] Ex. 84 (Daines Report) at Ex. 3 at 6-7, 38.

thus refuting Professor Daines' position.[282] Not only did the Court refute Professor Daines' opinion with respect to choice of law, it similarly refuted Professor Daines' application of the New York de facto merger doctrine.[283]

At best, the Trustee's failure to adequately consider these issues demonstrates a lack of care on the part of the Trustee. At worst, the Trustee turned a blind eye to its very real chances of recovery against BofA.

c. *Accrued Interest Discount*

The Trustee gave BofA an additional multi-billion dollar discount when it omitted from its damages calculations mention of New York's mandatory pre-judgment interest under CPLR §§ 5001, 5004. Assuming Mr. Lin's lowest possible settlement amount of $8.8, and assuming that the causes of action against BofA did not accrue until the end of the year in which the last securitization was issued (2007), all of which result in the lowest possible estimate of pre-judgment interest, the accrued interest discount is nearly $4 billion.

3. The Settlement Amount Only Includes Payment for BofA's Repurchase Liability, but the Settlement Proponents Ask to Release BofA for Additional Claims

Setting aside the serious flaws in Mr. Lin's approach, the $8.5 billion is still woefully inadequate because it only covers repurchase claims[284] while the Settlement Agreement releases BofA from substantially more liability.[285] The Settlement Agreement releases BofA for servicing claims and document exceptions even though the Trustee never investigated

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[282] Ex. 108 at 8-18.
[283] *Compare id.* at Ex. 3 at 34-37 (characterizing the four factors courts weigh when considering de facto merger claims as "elements" or "tests") *with* Ex. 108 at 19-20 (recognizing that "a finding of de facto merger does not necessarily require the presence of each factor") (internal quotations omitted).
[284] Ex. 71 (Lundberg Dep.) at 337:24-338:8.
[285] Ex. 1 at § 9.

or valued those claims.[286] Indeed, [redacted] the Trustee never engaged any expert to value the Covered Trusts' servicing claims. The Trustee's decision not to value the servicing claims reveals a core problem with the Trustee's overall approach to only negotiate those matters on which the parties agreed.[288] This failure is particularly troubling in light of the fact that the servicing claims are not subject to BofA's successor liability defense because BofA was required to assume Countrywide's servicing-related liabilities as a condition of the BofA-Countrywide merger and BofA is liable for its own servicing-related liability after it assumed the master servicer role.[289]

[redacted] Under the PSAs for approximately 468 of the 530 Covered Trusts, the Master Servicer appears to have an express obligation to repurchase modified mortgage loans.[291] Despite this obligation, the Trustee agreed to release such claims in the Settlement [redacted]

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[286] Ex. 71 (Lundberg Dep.) at 329:14-21.

[287] Ex. 77 (Burnaman Dep.) at 89:23-99:14 [redacted]

[288] Ex. 36 (Kravitt Dep.) at 358:8-13.

[289] Ex. 32 at § 6.04; *see also* Ex. 71 (Lundberg Dep.) at 332:21-334:21.

[290] Ex. 46 (Griffin Dep.) at 291:25-292:6; Ex. 24 (Stanley Dep.) at 253:19-22.

[291] *See* Ex. 32 at § 3.11(b) ("The Master Servicer may agree to a modification of any Mortgage Loan (the "*Modified Mortgage Loan*") if (i) the modification is in lieu of a refinancing and (ii) the Mortgage Rate on the Modified Mortgage Loan is approximately a prevailing market rate for newly-originated mortgage loans having similar terms and (iii) the Master Servicer purchases the Modified Mortgage Loan from the Trust Fund as described below."); *see also* Ex. 109 at § 3.12(a) ("The Master Servicer may agree to a modification of any Mortgage Loan (the "***Modified Mortgage Loan***") if (i) CHL purchases the Modified Mortgage Loan from the Trust Fund immediately following the modification as described below and (ii) the Stated Principal Balance of such Mortgage Loan, when taken together with the aggregate of the Stated Principal Balances of all other Mortgage Loans in the same Loan Group that have been so modified since the Closing Date at the time of those modifications, does not exceed an amount equal to 5% of the aggregate Certificate Principal Balance of the related Certificates.").

[redacted] and without any compensation for the Trusts with respect to such claims.[292] And although the Settlement states that it does not amend the PSAs,[293] it also permits loan modifications without repurchase.[294] In addition, the Trustee negotiated for itself protection in the Settlement against claims that the Trustee breached its duties and obligations to certificateholders by entering into the Settlement.[295] The Trustee's failure to consider and otherwise investigate the value of the loan modification repurchase claims for the benefit of the certificateholders violates the Trustee's obligations to certificateholders of the approximately 468 affected Trusts under the applicable PSAs and is also in direct contradiction of the PFOJ.[296] In this way, as in so many other ways, the Trustee abandoned its fiduciary duty to maximize recoveries for the Covered Trusts in the interests of justifying the BofA settlement.[297]

To the extent the Trustee views the Settlement Agreement's purported servicing improvements as consideration, the Trustee is wrong. The servicing terms in the Settlement Agreement are merely a recitation of BofA's existing duties under prudent servicing standards, the National Mortgage Settlement and other binding agreements, and/or the Governing Agreements. Thus, and as set forth in detail in Professor Levitin's

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[292] *See* Ex. 24 (Stanley Dep.) at 253:19-22 [redacted]

[293] *See* Ex. 1 at § 5(g).

[294] *Id.* § 5(e) (loan modifications undertaken pursuant to the Settlement "shall be deemed to be permissible under the terms of the applicable" PSAs).

[295] *See id.* at Ex. B at 8-9 (also available at Doc. No. 7).

[296] *See*, *e.g.*, *id.* at Ex. B ¶¶ (i), (j), (k) (also available at Doc. No. 7).

[297] *See* Ex.15 (Langbein Dep.) at 126:25-127:5; 206:1-4; 233:10-234:5.

report, the purported servicing improvements under the Settlement Agreement give the Covered Trusts nothing more than that to which they already are entitled.[298]

Also set forth in Professor Levitin's expert report are certain critical details of the Settlement Agreement's purported document cure provisions.[299] Those provisions alter the requirements set forth in the Governing Agreements and actually narrow BofA's contractual obligations. For example, the Settlement Agreement requires BofA to cure *either* the "Mortgage Exceptions," *or* the "Title Policy Exceptions" for any given loan, but not both.[300] In contrast, the PSAs require BofA to cure both.[301] The Settlement Agreement also requires BofA to reimburse the Covered Trusts for uncured document exceptions for non-MERS mortgages if there is a "Mortgage Exception" *and* a "Title Policy Exception" *and* a loss to the Covered Trusts.[302] In contrast, the PSAs only require *either* a "Mortgage Exception" or a Title Exception," and they do not require a loss to the Covered Trust and there is no exclusion for the massive number of loans registered through MERS.[303]

Finally, certain terms in the servicing section of the Settlement Agreement may actually inure to the benefit of BofA and to the detriment of the Covered Trusts. Section 5(i) provides that the Covered Trusts shall bear the costs of "any modification or loss mitigation strategy that may be required or permitted by Law," and "any Advance that is required or permitted by Law," and "any Realized Loss associated with the implementation

[298] Ex. 16 (Levitin Report) at ¶¶ 218-253.
[299] *See id.* ¶¶ 179-186.
[300] Ex. 1 at § 6(b).
[301] Ex. 32 at § 2.02.
[302] *Id.* at § 6(c).
[303] *Id.* at § 2.02.

of such modification or loss mitigation strategy."[304] As explained by Professor Levitin, this means that costs which otherwise would and should be borne by BofA under existing "Law"—a term that includes the National Mortgage Settlement and BofA's other settlements—may now be shifted to the Covered Trusts. This shift of costs could potentially result in a net negative for the Covered Trusts under the proposed Settlement Agreement.[305]

In sum, the Trustee seeks Court approval of a broad release for BofA in exchange for servicing terms that confer no real value to the Covered Trusts and a dollar amount that fails to include any compensation for released liability.

C. The Inside Institutional Investors' Support of the Settlement Provides No Proof of the Settlement's Reasonableness

BNYM's litigation experts point to the support of the Inside Institutional Investors as proof of the substantive fairness of the proposed settlement.[306] This reliance is misplaced. The Inside Institutional Investors' support of the settlement shows nothing more than the fact that those investors determined the $8.5 billion settlement amount and other terms were good *for them*.[307] [redacted]

As discussed in detail by Professor Levitin, there are numerous reasons why the Inside Institutional Investors may not be representative of other certificateholders, including:

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[304] Ex. 1 at § 5(i).
[305] *See* Ex. 16 (Levitin Report) at ¶¶ 254-259.
[306] Ex. 17 (Fischel Report) at ¶¶ 21-26; Ex. 84 (Daines Report) at 6-8; Ex. 110 (Landau Report (Doc. No. 542)) at ¶ 15.
[307] Ex. 16 (Levitin Report) at ¶ 71.
[308] Ex. 65 (Smith Dep. (PIMCO)) at 51:3-55:9.

- The close business relationships between some of the Inside Institutional Investors and BofA;
- The Inside Institutional Investors' equity stakes in BofA; and
- The possibility that the Inside Institutional Investors acquired their securities in the Covered Trusts at distressed prices *after* the market had already collapsed (which would mean the settlement represents a larger return on their investment than it does for investors who paid higher prices at origination).[309]

Further, counsel for the Inside Institutional Investors has previously stated that the settlement strategy employed against Countrywide/BofA here will be or has also been pursued against other banks and servicers.[310] The Inside Institutional Investors' intention of pursuing other banks and servicers for similar settlements may well have influenced their calculation of the settlement amount and terms that would be acceptable to them.

In short, the Trustee has presented no evidence to prove that the Inside Institutional Investors are representative of the other investors in the Covered Trusts and there is no basis for accepting the Inside Institutional Investors' support as substantive proof of the settlement's reasonableness.[311] Nor should BNYM or the Inside Institutional Investors be allowed to offer any explanation of why the Inside Institutional Investors agreed to the settlement. During discovery, Intervenors sought information about when and at what prices the Inside Institutional Investors bought their securities, but they refused to produce this information.[312] Intervenors also asked several of the Inside Institutional Investors about how they evaluated the proposed settlement

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[309] Ex. 16 (Levitin Report) at ¶¶ 62-75.
[310] Ex. 111 at 4.
[311] *See, e.g.*, Ex. 70 (Landau Dep.) at 48:23-49:24; 255:23-256:3; Ex. 15 (Langbein Dep.) at 130:24-131:7 [redacted]
[312] Ex. 112.

and why they agreed to it. The answers were blocked on privilege or "proprietary" grounds.[313] The settlement proponents cannot now rely on the Inside Institutional Investors' support as proof of the settlement's reasonableness when they refused to provide the discovery that would either prove or disprove that position.

CONCLUSION

This Court can have no confidence in the reasonableness of the proposed settlement agreement or in the Trustee's conduct in reaching it. The proposed settlement would release highly valuable claims in exchange for a settlement amount that constitutes nothing more than guesswork without real evidence. The undersigned parties therefore ask this Court that it not approve the proposed settlement as it currently stands.

[313] *See, e.g.,* Ex. 64 (Waterstredt Dep. (MetLife)) at 17:8-17; 80:25-81:22; 112:5-113:9; 142:21-143:5; 157:16-158:16; Ex. 66 (Robertson Dep. (BlackRock)) at 21:19-24:19; 96:23-98:21; 103:15-104:5; 112:12-25; 114:14-22; 141:15-25; 233:13-22; 244:12-245:2; 248:20-249:14; 256:15-257:3; 290:6-16.

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