To be Argued by:
BETH ANN KASWAN

New York County Clerk's Index No. 651786/11

New York Supreme Court

Appellate Division—First Department

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 Continuation of Caption See Inside Cover)

BRIEF FOR RESPONDENTS-RESPONDENTS-CROSS-APPELLANTS THE RETIREMENT BOARD OF THE POLICEMEN'S ANNUITY & BENEFIT FUND OF THE CITY OF CHICAGO AND OTHER MEMBERS OF THE PUBLIC PENSION FUND COMMITTEE, CITY OF GRAND RAPIDS GENERAL RETIREMENT SYSTEM, CITY OF GRAND RAPIDS POLICE AND FIRE RETIREMENT SYSTEM AND THE WESTMORELAND COUNTY EMPLOYEE RETIREMENT SYSTEM

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

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

Petitioner-Appellant-Cross-Respondent,

– and –

BLACKROCK FINANCIAL MANAGEMENT INC., KORE ADVISORS, L.P., MAIDEN LANE, LLC, METROPOLITAN LIFE INSURANCE COMPANY, TRUST COMPANY OF THE WEST and affiliated companies controlled by The TCW Group, Inc., NEUBERGER BERMAN EUROPE LIMITED, PACIFIC INVESTMENT MANAGEMENT COMPANY LLC, GOLDMAN SACHS ASSET MANAGEMENT, L.P., TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA, INVESCO ADVISORS, INC., THRIVENT FINANCIAL FOR LUTHERANS, LANDESBANK BADEN-WUERTTEMBERG, LBBW ASSET MANAGEMENT (IRELAND) PLC, DUBLIN, ING BANK FSB, ING CAPITAL LLC, ING INVESTMENT MANAGEMENT LLC, NATIONWIDE MUTUAL INSURANCE COMPANY and its affiliated companies, AEGON USA INVESTMENT MANAGEMENT LLC, authorized signatory for Transamerica Life Insurance Company, AEGON FINANCIAL ASSURANCE IRELAND LIMITED, TRANSAMERICA LIFE INTERNATIONAL (BERMUDA) LTD., MONUMENTAL LIFE INSURANCE COMPANY, TRANSAMERICA ADVISORS LIFE INSURANCE COMPANY, AEGON GLOBAL INSTITUTIONAL MARKETS, PLC, LIICA RE II, INC., PINE FALLS RE, INC., TRANSAMERICA FINANCIAL LIFE INSURANCE COMPANY, STONEBRIDGE LIFE INSURANCE COMPANY, WESTERN RESERVE LIFE ASSURANCE CO. OF OHIO, FEDERAL HOME LOAN BANK OF ATLANTA, BAYERISCHE LANDESBANK, PRUDENTIAL INVESTMENT MANAGEMENT, INC., and WESTERN ASSET MANAGEMENT COMPANY,

Intervenors-Petitioners-Appellants-Cross-Respondents,

– against –

THE RETIREMENT BOARD OF THE POLICEMEN'S ANNUITY AND BENEFIT FUND OF THE CITY OF CHICAGO, CITY OF GRAND RAPIDS GENERAL RETIREMENT SYSTEM, CITY OF GRAND RAPIDS POLICE AND FIRE RETIREMENT SYSTEM, THE WESTMORELAND COUNTY EMPLOYEE RETIREMENT SYSTEM, TRIAXX PRIME CDO 2006-1, LTD., TRIAXX PRIME CDO 2006-2, LTD., TRIAXX PRIME CDO 2007-1, AMERICAN INTERNATIONAL GROUP, INC., AMERICAN GENERAL ASSURANCE COMPANY, AMERICAN GENERAL LIFE AND ACCIDENT INSURANCE COMPANY, AMERICAN GENERAL LIFE INSURANCE COMPANY, AMERICAN GENERAL LIFE INSURANCE COMPANY OF DELAWARE, AMERICAN HOME ASSURANCE COMPANY, AMERICAN INTERNATIONAL LIFE ASSURANCE COMPANY OF NEW YORK, CHARTIS PROPERTY CASUALTY COMPANY, CHARTIS SELECT INSURANCE COMPANY, COMMERCE AND INDUSTRY INSURANCE COMPANY, FIRST SUNAMERICA LIFE INSURANCE COMPANY, LEXINGTON INSURANCE COMPANY, NATIONAL UNION FIRE

INSURANCE COMPANY OF PITTSBURGH, PA, NEW HAMPSHIRE INSURANCE COMPANY, SUNAMERICA ANNUITY AND LIFE ASSURANCE COMPANY, SUNAMERICA LIFE INSURANCE COMPANY, THE INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA, THE UNITED STATES LIFE INSURANCE COMPANY IN THE CITY OF NEW YORK, THE VARIABLE ANNUITY LIFE INSURANCE COMPANY, WESTERN NATIONAL LIFE INSURANCE, UNITED STATES DEBT RECOVERY VIII, LP, UNITED STATES DEBT RECOVERY X, LP and AMERICAN FIDELITY ASSURANCE COMPANY,

Respondents-Respondents-Cross-Appellants,

– and –

STERLING FEDERAL BANK, F.S.B., BANKERS INSURANCE COMPANY, BANKERS LIFE INSURANCE COMPANY, FIRST COMMUNITY INSURANCE COMPANY, BANKERS SPECIALTY INSURANCE COMPANY, FEDERAL HOME LOAN OF PITTSBURGH, AMICI ASSOCIATES, LP, AMICI FUND INTERNATIONAL LTD., AMICI QUALIFIED ASSOCIATES, CEDAR HILL CAPITAL PARTNERS LLC, CEDAR HILL MORTGAGE FUND GP LLC, CEDAR HILL MORTGAGE OPPORTUNITY MASTER FUND LLP, DECLARATION MANAGEMENT & RESEARCH LLC, DOUBLELINE CAPITAL LP, FIRST BANK, FIRST FINANCIAL OF MARYLAND FEDERAL CREDIT UNION, FIRST NATIONAL BANK & TRUST CO. OF ROCHELLE, ILLINOIS, FIRST NATIONAL BANKING COMPANY, FIRST PENN-PACIFIC LIFE INSURANCE COMPANY, KERNDT BROTHERS SAVINGS BANK, LEA COUNTY STATE BANK, LINCOLN LIFE & ANNUITY COMPANY OF NEW YORK, LINCOLN NATIONAL REINSURANCE COMPANY (BARBADOS) LIMITED, LL FUNDS LLC, MANICHAEAN CAPITAL, LLC, NEXBANK, SSB, PEOPLES INDEPENDENT BANK, RADIAN ASSET ASSURANCE INC., THE COLLECTORS' FUND LP, THE LINCOLN NATIONAL LIFE INSURANCE COMPANY, THOMASTON SAVINGS BANK, VALLEY NATIONAL BANK, MORTGAGE BOND PORTFOLIO LLC, FIRST RELIANCE STANDARD LIFE INSURANCE COMPANY, LIBERTY VIEW, PLATINUM UNDERWRITERS BERMUDA, LTD., PLATINUM UNDERWRITERS REINSURANCE, INC., RELIANCE STANDARD LIFE INSURANCE COMPANY, SAFETY NATIONAL CASUALTY CORPORATION, SUN LIFE INSURANCE COMPANY OF CANADA, CA CORE FIXED INCOME FUND, LLC, CA CORE FIXED INCOME FUND, LTD., CA HIGH YIELD FUND, LLC, CA HIGH YIELD FUND, LTD., STRATEGIC EQUITY FUND, LLC, STRATEGIC EQUITY FUND, LTD., SAND SPRING CAPITAL III MASTER FUND, LLC, CIFG ASSURANCE NORTH AMERICA, INC., BANKERS TRUST COMPANY, PINE RIVER FIXED INCOME MASTER FUND LTD., PINE RIVER MASTER FUND LTD, SILVER SANDS FUND LLC, TWO HARBORS ASSET I LLC, GOOD HILL PARTNERS LP, and BALLANTYNE RE PLACE,

Respondents-Respondents,

– and –

THE KNIGHTS OF COLUMBUS,

Intervenor-Respondent-Respondent.

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Respondents-Appellees-Cross-Appellants, the Retirement Board of the Policemen's Annuity & Benefit Fund of the City of Chicago, the City of Grand Rapids General Retirement System and the City of Grand Rapids Police and Fire Retirement System (collectively, the "Public Funds"), submit this consolidated brief in two capacities. First, as appellees, the Public Funds seek affirmance of those parts of the January 31, 2014 decision (JRA67a-122a)[1] ("Decision") of the court below (the "Article 77 Court") that properly refused to approve the proposed settlement ("Proposed Settlement") on the grounds that The Bank of New York Mellon ("BNYM" or the "Trustee") acted unreasonably in settling loan modification claims without investigating their potential worth or strength – and in releasing all claims and rights of 530 mortgage backed securities ("MBS") trusts and their certificateholders with respect to such claims. However, as appellants, the Public Funds also seek reversal and remand to the extent that the Article 77 Court otherwise purported to (a) approve (in part) the Proposed Settlement and the Trustee's settlement-related conduct or (b) reject any of the Public Funds' objections to the proposed deal.

INTRODUCTION

In an unprecedented action, BNYM, as trustee, has invoked the procedures

[1] This brief uses the following convention citations: "JRA ___" refers to pages of the Joint Record on Appeal; "RTX ___" refers to Respondents' Trial Exhibit #___; and "PTX ___" refers to Petitioners' Trial Exhibit #___.

of Article 77 in an attempt to bind thousands of non-party certificateholders -- and to release their rights to recover massive damages that would dwarf the putative $8.5 billion in proceeds under the Proposed Settlement -- even though BNYM has repeatedly and consistently denied having *any* fiduciary duty to represent these non-parties (including the Public Funds) in this matter, and even though it is undisputed that the counsel (Mayer Brown) that BNYM has relied on throughout was retained to represent *solely* BNYM's own interests. Instead, BNYM has claimed throughout that it has been merely an "indenture trustee," which (absent an "event of default" under the Trusts' governing agreements) had none of the traditional fiduciary obligations to act on behalf of absent certificateholders as a "prudent person" would in the conduct of its own affairs. Indeed, as BNYM's own counsel stated, it is undisputed that BNYM (to minimize its own potential liability) "work[ed] hard" to avoid declaring an "event of default" during the underlying settlement negotiations so it could deny having ever assumed any "prudent person" duties to non-party certificateholders. BNYM has thus defeated its own authority to settle the claims, and fatally undercut the jurisdiction of the Article 77 Court to enter binding relief.

Worse still, BNYM also injected irreconcilable conflicts into the settlement process. In particular, BNYM not only failed to hire counsel to represent the interests of absent certificateholders, but also hired as its *own* counsel Mayer

Brown, which was simultaneously representing Bank of America ("BOA") in other matters. BOA's adversity here was patent, inasmuch as BOA was leading the negotiations for the opposing side in the settlement discussions and would obviously be a defendant if those negotiations broke down -- and BOA, for its part, was willing to grant Mayer Brown only a limited "conflict waiver" that precluded Mayer Brown from suing BOA if a pre-litigation settlement were not reached. BNYM then further compounded its misconduct by failing to give certificateholders notice of Mayer Brown's conflicts, and by failing to obtain certificateholders' consent (or the prior approval of a court) to have a conflicted law firm conduct settlement negotiations on BNYM's behalf in circumstances where that firm could not, did not and was not even retained to fully advocate for the certificateholders to maximize their recoveries. Had this been a typical case where one person seeks to bind others by its actions, such as a class action, derivative suit, or bankruptcy proceeding, it is inconceivable that a court would have found that the type of "representation" BNYM provided here was adequate – yet adequate representation is the very touchstone of due process in any legal proceeding where a party seeks to compromise and release the claims of absent non-parties. *See, e.g.*, *Hansberry v. Lee*, 311 U.S. 32, 40-41 (1940).

Nor can a finding that BNYM acted in "good faith" or "reasonably" otherwise be sustained. For example, BNYM and the Institutional Investors (collectively, the "Settlement Proponents") went along with BOA's position that the "settlement value" of the repurchase claims at issue had to be significantly discounted because the governing agreements for the Trusts contained "no action" clauses that prevented groups of certificateholders -- but not the Trustee -- from suing on behalf of a Trust if they did not own 25% of that Trust's certificates. Indeed, as incredible as it may be, neither BNYM nor its counsel *ever* told BOA (or the Institutional Investors) that, if settlement negotiations collapsed, BNYM would bring suit on behalf of the several hundred Trusts where the Institutional Investors did not have the 25% ownership needed to initiate suit absent the Trustee's cooperation.

Under New York law, "no action" clauses are intended largely to protect trust beneficiaries as a whole by concentrating the Trust's enforcement powers in a single representative and preventing small minority interests from initiating dubious litigation. Here, however, BNYM's inexcusable failure to even threaten to sue as Trustee on behalf of the many Trusts that could not meet the 25% "presentment threshold" (combined with BNYM's failure to issue any Notices of Default) has (1) allowed BOA to get away with reducing the value of the Proposed Settlement by billions of dollars, and (2) also allowed BNYM to effectively coerce many investors into not opposing the Proposed Settlement (inasmuch as BNYM has refused to provide any assurances that it would *ever* sue if the Proposed

Settlement were not approved, thereby putting the beneficiaries of hundreds of Trusts in a none-too-subtle "take the deal or get nothing" position). *See* Institutional Investors' brief (JRA11762-63 (RTX131)) and BNYM's brief (JRA11720-21 (RTX132)) (emphasizing that certificateholders who cannot meet 25% ownership threshold in their Trusts have no alternative for relief apart from the Proposed Settlement.)[2] By refusing to even threaten to sue as Trustee for *all* Trusts to get a better deal -- and by subsequently exploiting the "no action" clauses to effectively coerce support for a tainted settlement that would conveniently limit its own liability for failing to act earlier to take any action on behalf of the Trusts -- BNYM acted both unreasonably and in bad faith.

In addition, throughout the settlement process, BNYM exploited the self-created ambiguities in its status under the Trusts' governing agreements to deny that it had the fiduciary duty of care to investigate the underlying claims, so that there is no basis for finding that, as a substantive matter, the Proposed Settlement is "fair" or "adequate." Indeed, BNYM had strong incentives to *avoid* investigating and quantifying claims that would have only highlighted its own shortcomings and legal exposure for, *inter alia*, having failed to act much earlier. For example, BNYM failed to even request or review critical, readily available evidence that BOA most assuredly did not want to produce, including mortgage

[2] Thus, the Settlement Proponents' reliance on the small number of certificateholders who pursued objections as evidence of widespread support of the Settlement is misplaced.

loan files that could have been used to conduct a "re-underwriting review" (which is typically performed even in repurchase cases with vastly less money at stake). Instead, BNYM's counsel (Mayer Brown) simply hired an advisor to probe BOA's extrapolation from BOA's inapposite experience in settling repurchase claims with various Government Sponsored Entities ("GSEs") to reach the grossly far-fetched conclusion that as few as 14% of the Trusts' mortgage loans breached their "representations and warranties" ("R&Ws) that they had been "prudently" originated, and that they met stated creditworthiness criteria. Moreover, on the "collectability issue" that BNYM's Trust Committee insisted was so critical to its decision to approve the $8.5 billion deal, Mayer Brown simply hired law professors to reach the unremarkable conclusion that the issue of whether BOA (as to which there were no collectability concerns) could escape liability for Countrywide's debts depended on the facts of the case. But such facts could only be determined from evidence that BOA did not want to produce, and that neither BNYM nor its counsel bothered to pursue.

The Article 77 Court addressed the foregoing points only summarily, or not at all. Indeed, instead of fairly weighing and deciding the hotly contested evidence elicited over a nine-week trial, the Court inexplicably adopted an extraordinarily deferential "summary judgment" standard, under which the Court would sustain an objector's challenge on a given issue only where the Trustee offered no evidence to contest it. This was clear error.

The Article 77 Court did not, however, err by refusing to approve the Proposed Settlement's release of $31 billion of repurchase rights for modified loans. As the Article 77 Court correctly found, neither BNYM nor its counsel had quantified, investigated or otherwise evaluated any loan modification claims. In response, the Settlement Proponents argue that such claims were so devoid of merit that they did not warrant consideration, since the Trusts' governing agreements did not require repurchase of loans that were modified to "benefit certificateholders" by mitigating the Trusts' credit losses. But the loan modifications (which reduced principal and/or interest due on the loans), were *not* made in the ordinary course of business to mitigate losses on non-performing loans, *but were made to settle claims by multiple States Attorneys General that the loans had been originated by Countrywide in violation of state predatory lending laws*. As such, the mortgage loans' originator or servicer -- namely Countrywide or BOA -- should plainly incur the losses from the loan modifications, rather than innocent certificateholders who had no role in making any predatory loans.

Moreover, if the loan modification claims are so clearly meritless, BOA could simply sever them from the scope of the proposed release and otherwise seek to proceed (subject to the objector's instant appeals) with the other portions of the Proposed Settlement that the Article 77 Court did not reject. That BOA has not done so is, perhaps, the most telling evidence that BOA understands that it faces substantial exposure on these claims if they are not released.

Accordingly, (1) the Article 77 Court's refusal to approve the Proposed Settlement "in all respects" based on its improper release of loan modification claims (and to otherwise refuse to make all the factual findings contained in Petitioners' Proposed Final Order and Judgment (the "PFOJ") should be affirmed, and (2) the Article 77 Court's findings "approving" other aspects of the Proposed Settlement should be reversed because the entire deal was the product of fatal due process defects (including the Trustee's denial that it owed any fiduciary duties to certificateholders), or reversed and remanded for appropriate analysis under a non-deferential preponderance-of-the-evidence standard.

QUESTIONS PRESENTED

Counterstatement of the Question Presented on Appeal:

(1) Did the Court below err in refusing to approve the Proposed Settlement based on BNYM's failure to pursue claims for the repurchase of $31 billion of modified loans, without investigating their potential worth or merit?

Questions Presented on the Cross Appeal:

(2) Did the Court below err in holding that BNYM had the authority to settle and release absent certificateholders' claims, and that the Court

had the authority to enter binding relief against those certificateholders, where both BNYM and its counsel denied ever representing those certificateholders during the settlement process as their fiduciaries?

(3) Did the Court below err in holding that BNYM acted reasonably, in good faith and without abusing its discretion, and in finding that the Proposed Settlement was "fair" and "adequate" (aside from certain exceptions) where, *inter alia*:

(a) BNYM and its counsel denied having fiduciary duties to certificateholders;

(b) BNYM relied upon conflicted counsel, and did so without notice to or the consent of certificateholders;

(c) BNYM allowed the Trusts' "no action" clauses -- and its own refusal to even threaten to sue BOA on behalf of Trusts where the 25% presentment threshold was not met -- to "justify" a substantial settlement discount at the negotiating table and to thereafter coerce certificateholders' acquiescence in the proposed deal; and

(d) BNYM failed to conduct any investigation of critical, readily available facts relating to liability, damages, and collectability of a judgment?

(4) Did the Court below err in failing to place the burden of proof squarely on the Trustee, and in evaluating the conflicting evidence under an extraordinarily deferential "summary judgment" standard

under which the Trustee was effectively deemed entitled to judgment on each disputed issue as long as there was *any* evidence that might justify the Trustee's conduct?

STATEMENT OF THE CASE

A. Overview of the Settlement

BNYM instituted the Article 77 proceeding to approve what it has referred to as an "historic" $8.5 billion settlement. The Institutional Investors' counsel who actually conducted the price negotiations -- which BNYM and its counsel did not even attend[3] – have touted the deal as the largest private settlement in history. JRA11734 (RTX132 at 5). Though $8.5 billion is facially a large sum, the Proposed Settlement would release *all* repurchase and servicing claims against Countrywide, BOA and their respective affiliates with respect to 530 Covered Trusts that owned *$430 billion* (face amount) of largely toxic Countrywide mortgage loans. To put the resulting liabilities in perspective, the schedule the Institutional Investors prepared for the settlement negotiations shows that by April 2011, as the Settlement was being negotiated, the Trusts had already realized $25 billion in principal losses on their mortgages (due to loans having defaulted and been foreclosed upon at a loss) -- and a breathtaking $72.5 billion of additional

[3] Jason Kravitt unsuccessfully requested that he and his partner, Matthew Ingber, be permitted to attend, because they'd "like to be able to say that we 'watched' the whole thing and it was clearly hard fought arm's length." JRA11669 (RTX90); JRA1471:11-20 (Kravitt).

loans were *at least* 60 days delinquent and thus well on their way to default as well. JRA17336 (PTX 295.2).

For its part, the Trustee "analyzed" conflicting measures of how much of the realized and expected future losses in the 530 Trusts were attributable to defective loans -- *i.e.*, loans that materially breached the R&Ws as to their credit quality that were contained in their governing agreements (or "PSAs") -- without even reviewing a sample of the pertinent loans. However, even BOA's self-serving methodology, which was purportedly derived from an extrapolation of BOA's repurchase experience with Freddie Mac and Fannie Mae (the "GSE's") (JRA6385-90 (PTX 36)) combined with certain additional discounts, estimated its liability at $4 billion. JRA6390 (*Id.* at 5). In contrast, based on data involving the purported re-underwriting of 250,000 unidentified mortgage loans, the Institutional Investors developed "settlement scenarios" of $15-$52 billion. JRA10037 (PTX 604.1); JRA7917 (PTX 444.105). In short, by any measure the potential liabilities at issue were staggering in size -- and warranted a searching factual investigation into the quality of the mortgage loans that were actually included in the Trusts.[4]

Under the terms of the Proposed Settlement, the Settlement was "null and

[4] Although the Article 77 Court granted objectors discovery and conducted a nine-week trial, these steps could not compensate for the failure of the Trustee to come to the negotiating table armed with developed facts to advocate the strengths of the breach of representation and warranty claims. In other words, while the Article 77 Court attempted to compensate for the patently inadequate pre-settlement investigation, it simply was not possible for her to unscramble the eggs.

void" if not finally approved by the Article 77 Court through the issuance of a form of order attached as an exhibit, the PFOJ, which the Article 77 Court ultimately declined to enter. JRA17974 (PTX 1.7); JRA378a, at n.5, JRA80a, JRA365a (Decision at 13). Most of the Proposed Settlement's terms were "severable" – but *not* the terms of the release. JRA18410 (PTX 1.84). Although the Article 77 Court rejected most of the objecting Respondents' challenges, it found that the Trustee had failed to analyze the strength or worth of repurchase claims with respect to $31 billion of modified loans. While contending on this appeal that any loan modification claims are worthless, more telling is BOA's apparent refusal to consent to narrowing the Proposed Settlement's release to conform to the Article 77 Court's opinion, and its apparent insistence that BNYM bring its half of this appeal.

B. BNYM "Works Hard" to Avoid the Responsibilities and Exposure of a "Full-Fledged" Fiduciary, and Refuses to Represent the Certificateholders Who Were Absent from the Negotiations

From the inception of the Covered Trusts until the summer of 2010 when the Institutional Investors' counsel (Gibbs & Bruns) first contacted BNYM:

(1) Countrywide Home Loans ("CHL"), as the "seller" that made the R&Ws, had repurchased *no* mortgage loans for breaching their R&Ws; and

(2) the "master servicer," originally Countrywide Home Loans Servicing LP ("Countrywide Servicing") and then (after BOA acquired Countrywide in the 2008 "triangular merger") a BOA affiliate, did *nothing* to give notice of the breaches or to seek

> repurchase of any mortgage loan. *See, e.g.*, JRA2012:5-14 (Kravitt) ("as of June 2011, at the end of the settlement negotiations, the Master Servicer still had never notified the Trustee of the discovery of even one mortgage loan that violated the representations and warranties").

Moreover, during that same period, BNYM as Trustee had also taken ***no*** steps to "investigate" or give notice of Countrywide's pervasive breaches as "seller," or to trigger the noticing of "Events of Default" under PSA §7.01 based on Countrywide's failure, as "master servicer," to enforce any of the Trusts' resulting repurchase rights. *See, e.g.*, JRA11596 (RTX15.002) (no action taken despite "widespread readily available evidence suggesting that large numbers of mortgages securing the Certificates . . . were sold into the RMBS pools based on false and/or fraudulent representations and warranties"); JRA11601 (RTX16.001) ("[BNYM] informed our clients that it has to date taken no steps to investigate or resolve the allegations made by mortgage insurers"); JRA6710 (PTX108.3) (referencing the Trustee's confirmation that the master servicer "*never* notified it of the discovery of *even one* mortgage that violated applicable representations and warranties") (emphasis in original).[5]

[5] BNYM in its role as Trustee also published monthly reports showing the growing rates of mortgage loan delinquencies and realized losses, and the extent (namely zero) to which any repurchases for R&W violations were made for any Trusts. JRA2485:22-2486:24 (Bailey); JRA12869-902 (RTX1348). In January 2009, Fannie Mae had also advised BNYM that it was in breach of its fiduciary duties by failing to retain experts to investigate and pursue repurchase claims, and that there were likely significantly more defective loans in the Trusts than in the separate Countrywide mortgage pools that the GSEs had purchased. Fannie Mae's January 2009 letter was circulated to, inter alia, BNYM's Robert Bailey and Loretta Lundberg, who both

BNYM's dogged insistence that it had no obligation to protect either the Trusts or certificateholders from mushrooming losses that were plainly due to Countrywide's breaches of R&Ws is epitomized by letters sent by another BNYM law firm (Pillsbury) to Gibbs & Bruns in June and September 2010.[6] In those letters, BNYM averred that it was "entitled to rely, without any independent investigation on its part, on representations and warranties made by other parties, including sellers and originators" -- and that BNYM could therefore disregard contrary evidence from, *inter alia*, numerous governmental proceedings and private lawsuits against Countrywide (including even those actions in which BNYM had been joined as a party) until final decisions in those matters were entered. JRA6676-678 (PTX80); *see also* JRA6697-700 (PTX102). This extreme and illogical interpretation was approved by BNYM's in-house counsel, who confirmed that it reflected BNYM's policy.[7] JRA2424:10-2425:16; 2425:22-

played key roles in BNYM's decision to approve the Proposed Settlement. JRA12863-68 (RTX1342).

[6] In fact, as the Article 77 Court correctly found, the PSAs do indeed give the Trustee the power to enforce the Trust's repurchase rights for breaches of R&Ws for the benefit of certificateholders, JRA90a (Decision at 23). See also JRA6467 (PTX 71.64) (Trustee is required to enforce repurchase rights "to the end that the interests of the Holders of the Certificates may be adequately and effectively protected"). By contrast, as noted below, the PSAs also contain "no action" clauses which erect significant barriers to certificateholders' own ability to enforce these rights. JRA6539 at §10.08 (PTX 71.136).

[7] The position that a trustee can "turn a blind eye" to a raft of credible information evidencing pervasive breaches of representations and warranties in the MBS trust context has been repeatedly rejected by federal courts in which BNYM and other MBS Trustees have been sued. *See, e.g.*, *Retirement Board v. Bank of New York Mellon, 914 F. Supp. 2d 422 (S.D.N.Y. 2012); Policemen's Annuity & Ben. Fund of the City of Chicago v. Bank of America, N.A.*, No. 12-cv-

2427:6 (Bailey).

Thus, it was BNYM's position that it was not required to make any "investigation" of information it was confronted with, unless requested to do so with respect to particular Trusts by certificateholders holding at least 25% of the voting rights for each class of certificates in such Trusts. JRA6697 (PTX 102.1). Such pre-conditions are usually all but impossible to satisfy, as the Trusts typically have multiple tranches with multiple investors, and involved certificates with a total face value of as much as $1 billion. Accordingly, even several years after the mortgage meltdown, only the Trustee was in a position to enforce the repurchase rights of two-thirds of the Trusts here, as even Gibbs & Bruns' Institutional Investors group (which collectively owns $40 billion in certificates) possesses an 25% ownership interest in only 189 of the 530 Covered Trusts. JRA11734-35 (RTX132 at 5, 6).[8]

2865, 2013 WL 5328181 (S.D.N.Y. Sept. 23, 2013); *Oklahoma Police Pension & Ret. Sys. v. U.S. Bank Nat'l Ass'n.*, 291 F.R.D. 47 (S.D.N.Y. 2013); *Bank of New York Mellon Tr. Co., Nat'l Ass'n. v. Morgan Stanley Mortg. Capital, Inc.*, No. 11-cv-0505, slip op., 2013 WL 3146824, at *19 (S.D.N.Y. June 19, 2013) ("A party 'discovers' a breach when it knows or should know that the breach has occurred").

[8] After the Proposed Settlement deal was struck, both the Institutional Investors and BNYM pointedly reminded non-party certificateholders of the overwhelming obstacles to enforcing their rights because as a practical matter only the Trustee had the standing to do it. *See, e.g.*, the Settlement Proponents' respective October 2011 briefs in support of the Settlement (BNYM Br. at JRA11684-722 (RTX131) and Institutional Investors Br. at JRA11723-94 (RTX132)); JRA11735 (RTX132 at 6) ("[O]f the over $40 billion in securities held by the Institutional Investors or by funds and clients they advise, almost $14 billion are in Trusts where the Institutional Investors lack the required 25% threshold. If the settlement is disapproved, these Trusts will receive no remedy at all."); JRA11695, JRA11721 (RTX131 at 7, 33) (stressing the obstacles faced by investors whose holdings were too small to instruct the Trustee, and arguing

The Trustee's position that it was under no obligation to investigate the facts underlying the repurchase claims or to protect the repurchase rights of the Trusts or absent certificateholders – even as it was acting to compromise and release potentially tens of billions of dollars of the Trusts' and the certificateholders' interests in those claims – did not change after the Trustee retained Mayer Brown as its counsel. Instead, in logic reminiscent of *Catch-22*, Mayer Brown's lead attorney, Jason Kravitt, "explained" that (a) unless BNYM gave formal notice of the master servicer's default under PSA §7.01, no "Event of Default" ("EOD") would be triggered, and the Trustee would have no duty to conduct an "investigation" (*i.e.*, to review any individual mortgage loan files), but (b) BNYM would not be able to determine whether an EOD had occurred unless it first conducted an investigation. JRA1991:3-1993:7, JRA1994:5-9 (Kravitt). Thus, despite the clear import of the PSA to impose on the Trustee the duty to give notice of clear master servicer defaults in the first instance (with the alternative of a certificateholder direction as a check), in the Kafkaesque world of BNYM and its counsel BNYM had no responsibility to enforce the Covered Trusts' repurchase rights unless certificateholders holding a 25% ownership interest directed it to do so (and also agreed to indemnify it). JRA2009:22-2010:16 (Kravitt).

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that "[n]one of the objectors suggest any possible route by which investors in the Trusts could obtain any benefit or remedy through a vehicle other than the Settlement – be it litigation or otherwise…" and that, as a practical matter, the only alternative to the deal "is the status quo").

Kravitt did testify that, absent an EOD, BNYM could still choose to be "generous," and exercise its discretion to *negotiate* for the 341 Covered Trusts where the Institutional Investors lacked a 25% ownership interest, even though BNYM had historically refused to act on the Covered Trusts' losses. (As Kravitt added, "[that] [s]ometimes we stand on our rights is not to say that it's not generous not to do that all the time." JRA1634-35 (Kravitt)). But as senior BNYM in-house lawyer Kevin McCarthy testified, even if the Article 77 Court ultimately failed to approve a negotiated settlement, BNYM would *sue* only if certificateholders met the 25% ownership requirements and directed it to do so. JRA5025:2-16 (McCarthy).

For its part, Mayer Brown also denied having fiduciary duties to the Trusts or the certificateholders, and insisted that it represented only BNYM. Thus, as confirmed by Mr. Kravitt -- BNYM's primary representative in the negotiations -- during those negotiations there were *no* lawyers representing the certificateholders in the 341 trusts where the Institutional Investors did not have a 25% interest:

Q: Mayer Brown wasn't representing the certificateholders, correct?

A: Correct.

Q: Ms. Patrick [of Gibbs & Bruns] wasn't representing any certificateholders other than her clients?

A: Correct.

Q: The certificateholders in the trust in which Ms. Patrick had clients

> with 25 percent holdings were not [sic] represented by counsel in these negotiations, correct?

A: Correct.

Q: And the certificateholders in the trusts in which Ms. Patrick didn't have 25 percent were not represented by counsel in these negotiations?

A: Correct.

JRA1655:17-1656:5 (Kravitt). Thus, for example, when Mr. Kravitt signed off on the "Forbearance Agreement" in December 2010 -- by which Gibbs & Bruns agreed to "forbear" from treating its earlier notice as the trigger of an EOD, and in return BOA agreed to toll the statute of limitations for the 115 Trusts in which the Institutional Investors then owned 25% JRA11644-50 (RTX46) -- BNYM took *no* steps to protect the remaining 415 Trusts because "it didn't have an obligation to protect those trusts at that point." JRA1718:2-1719:20 (Kravitt).

By denying that either the Trustee or its counsel owed fiduciary duties to any Trusts or their certificateholders, Mayer Brown also proved to be quite comfortable in deferring to BOA's positions, so long as BOA "indemnified" Mayer Brown's client, BNYM, for any increased exposure that might result. For example, at BOA's suggestion, Kravitt was happy to permit settlement discussions to proceed between BOA and the Institutional Investors alone, without notice to other certificateholders, provided that BNYM was fully indemnified for its exposure for failing to provide such notice. JRA11658 (RTX53); JRA1762:13-1764:19

(Kravitt).

Conversely, Mr. Kravitt agreed that *if* there was an Event of Default, things would have radically changed from what he and BNYM had done. If an EOD occurred such that BNYM had the duties of a fiduciary under PSA §8.01 – *i.e.*, the duty to act as a prudent person would in dealing with its own affairs – *then BNYM would have had to perform "materially" more work*, including "to look more deeply into the short-comings that investors had alleged." JRA2068-69 (Kravitt). "If there were an event of default outstanding . . . then [the Trustee] would consider . . . whether or not to do an investigation." JRA2099:12-17 (Kravitt). But absent an EOD, according to Kravitt, there were no such obligations. JRA1661 (Kravitt). Robert Bailey, the BNYM in-house lawyer most involved in the settlement process, agreed: "The position of the Trustee, as I understood it, in connection with the PSAs, was that unless and until there was a Master Servicer event of default, the Trustee did not assume sort of the prudent person standard." JRA2434:26-2435:4 (Bailey). For this very reason, in December 2010, BNYM and its counsel were "working very hard to avoid an event of default." JRA1733:15-16 (Kravitt); *see also* JRA4988:13-15, JRA5014:25-5015:16 (McCarthy); JRA12984 (RTX1444 at 001) (an Event of Default was not in BNYM's "self interest").

Indeed, as Kravitt privately explained to BNYM's in-house counsel, if Gibbs

& Bruns' earlier letters were interpreted as triggering an EOD, then not only would the Trustee's standard of care change to that of prudent man in the conduct of his own affairs, but, with an EOD, other investors not in the Institutional Investor group (whom Kravitt pejoratively described as "wildmen") could then "jump into the fray." JRA12986-88 (RTX1445); JRA1756:6-1757:19 (Kravitt); JRA5019:10-5020:7 (McCarthy). More specifically, Kravitt fretted that if there was an EOD, any of these "wildmen" would arguably be able to sue without regard to whether they could muster a 25% ownership interest. JRA1740:20-26 (Kravitt). BNYM's McCarthy was also concerned that, if an event of default were deemed to have occurred, a "wildman" might not only sue Countrywide and/or BOA -- and that an EOD would also increase BNYM's liability exposure. JRA5019:22-5021:17 (McCarthy).

Even after a Settlement Agreement was reached releasing hundreds of billions of dollars of certificateholders' claims, BNYM and Mayer Brown had continued to insist that neither the Trustee nor its counsel have ever represented certificateholders as their fiduciary. *See* BNYM Memorandum of Law in Opposition to Motion to Compel Discovery (ECF No. 263), at 11 ("Trustee is not a fiduciary"); JRA1797a at 121:19 (August 2, 2012 Tr.) (BNYM's counsel stating "[BNYM] is not a fiduciary"). Indeed, the Article 77 Court accepted BNYM's position that it was not "a full fledged fiduciary." JRA1835a-36a.

C. BNYM's and Mayer Brown's Disabling Conflicts

1. BNYM's Efforts to Limit Its Own Exposure for Loans With Documentation Defects

BNYM became Trustee for each Trust at its inception. Under the PSAs, one of the Trustee's specific duties was to review each mortgage loan file and prepare "exception" reports identifying any loans whose documentation was deficient. JRA11404 (RTX13-051); JRA5473:6-12 (Levitin). Given the mortgage foreclosure "moratorium" that had been imposed as a result of the widespread documentation problems for the mortgage loans, including for those in the Covered Trusts, BNYM was subject to potentially huge liability if, in preparing the exception reports, it either missed the documentation problems or had identified them without requiring Countrywide to repurchase them. JRA5473:13-22, 5475:24-5476:19 (Levitin).

As Philip Burnaman (one of the Trustee's experts) testified, recently prepared loan level exception reports showed that there were *117,899* mortgage loans with document deficiencies that continued to be included in the Trusts as of June 2011. JRA3011:5-17 (Burnaman).

Mayer Brown, as BNYM's counsel, repeatedly pushed the issue of protecting BNYM from its exposure for the mortgage documentation problems during the settlement negotiations. *See, e.g.*, JRA11659-61 (RTX58) ("List of Settlement Issues," sent by Kravitt to BOA's counsel (but not the Institutional

Investors)). "Will the settlement resolve Trustee certificates issues, such as the recent press over the *Kemp* case and Countrywide and BONY's alleged failure to ensure it had the notes, etc." JRA11661 (RTX58 at 3). Similarly, an April 11, 2011 e-mail sent by Kravitt only to BOA's counsel asked "to speak with you about what the Trustee would like to receive if there's a settlement." JRA15605:19-25 (Ex 34 to Reilly Aff., Bailey Tr. Excerpt at 19444:19-25). In June 2011, Mayer Brown, when proposing release language to be included in the Proposed Settlement, repeatedly attempted to insert language that would bar certificateholders from suing BNYM regarding these documentation problems. JRA11672 (RTX118 at 3); JRA11960 (RTX235). Although this language was ultimately struck from the final version of the Proposed Settlement at the insistence of the Institutional Investors, BNYM effectively obtained some of the protections it had sought through the back door by instead obtaining provisions that changed the servicing remedies under the PSAs with respect to deficient mortgage loan files. JRA2050:19-2052:20, JRA2056:11-19 (Kravitt).

2. Mayer Brown's Undisclosed and Disabling Conflicts of Interest

When BNYM retained Mayer Brown, Mayer Brown represented *BOA* in various other matters. However, BOA's interests were obviously adverse to the Trusts, and BOA would inevitably be sued if negotiations failed. Accordingly, although BOA consented to granting Mayer Brown only a limited conflict waiver that would allow it to advise BNYM as to BNYM's rights and obligations as Trustee, *BOA would not consent to allowing Mayer Brown to sue BOA*. JRA12857-58; JRA1582:19-1583:2 (Kravitt).

Although the Trustee acquiesced in these arrangements, it never provided notice to certificateholders (beyond those in the Institutional Investor group) of its counsel's conflicting relationships with BOA. JRA1593:14-1594:14, JRA1578:12-1579:15 (Kravitt). Nor did BNYM disclose Mayer Brown's conflicts in the form of Notice to certificateholders of the Proposed Settlement that was presented to the Article 77 Court for approval. Instead, Mayer Brown's multiple representations only came to light through the objectors' discovery in this action.

D. BNYM's Failure to Even Threaten to Sue on Behalf of All Trusts Reduced the Proposed Settlement Amount by Billions of Dollars

Throughout the settlement process and the Article 77 proceedings, BNYM viewed itself as having the "power" to sue to enforce the repurchase rights of all 530 Covered Trusts. JRA2031:24-2032:11 (Kravitt). Incredibly, however, Mr. Kravitt, never told BOA or anyone else at the settlement negotiations that BNYM would ever actually sue on behalf of all 530 Trusts. JRA2028:14-20, JRA2032:12-16 (Kravitt). Instead, he testified that when the Proposed Settlement was reached, it remained BNYM's position that it was "not … willing to bring lawsuit without an instruction and indemnity." JRA11304 at 614:22-24 (PTX657). BNYM's Bailey similarly testified that he never told BOA that BNYM would sue for all Trusts if there were no settlement, nor did he authorize anyone to discuss that issue. JRA2465:16-2466:17 (Bailey). While it was purportedly "implied" that, if no settlement were reached, litigation was an "option," BNYM's legal department was never given authority to sue for those Trusts for which the Institutional Investors lacked a 25% ownership interest. JRA2467:17-2468:24 (Bailey). Indeed, as recently as the Settlement Hearing, BNYM continued to assert that it has the right *not* to sue on certificateholders' behalf, and refused to give any assurance that it would sue if the Proposed Settlement blew up. JRA5025:2-16 (McCarthy); JRA3727:15-3728:20 (Fischel).

Meanwhile, it is undisputed that BNYM knew that BOA significantly discounted the amounts it offered in the settlement negotiations based on the many obstacles to bringing suit that certificateholders faced under the PSAs with respect to the majority of the Trusts, inasmuch as even the Institutional Investor group did not satisfy the 25% "ownership threshold" to overcome the PSAs' "no action" clauses for at least 341 Trusts. Indeed, BOA's negotiation presentation noted that "[o]nly parties to the Pooling and Servicing Agreements (PSA) (e.g. the Trustee) can bring such repurchase claims" JRA6347 (PTX 23.7); JRA2016:12-2017:20 (Kravitt), and another BOA presentation slide described how, in assessing its liability exposure, it discounted its overall liability to all the Trusts by roughly 20% (the "presentation haircut") to reflect the fact that there were no certificateholder groups with 25% ownership interests that could overcome the "no action" clauses' bar on direct private suits for most of the Trusts. JRA6389-90 (PTX36 at 4-5); JRA2025:4-2026:3 (Kravitt). Indeed, in its First Quarter 2011 ("1Q2011") Form 10-Q filed with the SEC on May 5, 2011, just *after* negotiations for the $8.5 billion had concluded, BOA publicly reported that it had discounted its expectations of its overall repurchase liabilities (or "range of possible loss") *by $4 billion* because of the difficulty that private investors had in reaching the 25% ownership "presentation threshold," *and because the relevant trustees had not committed to enforce the trusts' repurchase rights*. JRA12165 (RTX350 at 170) ("It is difficult to predict how a trustee may act or how many investors may be able to meet the prerequisite presentation threshold . . . [BOA's] model reflects an adjustment to reduce the range of possible loss for the presentation threshold for all private-label securitizations of approximately $4 billion").[9]

Kent Smith, one of the Institutional Investors that negotiated the $8.5 billion settlement amount, also confirmed that the difficulties in reaching the 25% ownership interest with respect to the majority of Trusts at issue here was a factor that adversely impacted the Settlement Proponents' settlement offer made during the final negotiation session (which Kravitt did not even attend). JRA663:5-15

[9] The $4 billion in BOA's 1Q2011 Form 10-Q was an aggregate number for both Countrywide private-label securitizations ("PLS") and also BOA's non-Countrywide securitizations, for example those involving Merrill Lynch securitizations. Countrywide loans, however, constituted approximately 78.8% of the unpaid principal balance of the total mortgage loan liabilities. JRA6348 (PTX 23.8).

(Smith); JRA1471:11-20 (Kravitt).

E. The Trustee Did Not Perform the Factual Investigation Needed to Effectively Advocate the Strengths of Certificateholders' Claims or to Maximize Their Recoveries

To reasonably determine how many of the mortgage loans in the 530 Covered Trusts needed to be "repurchased" for breaches of R&Ws, and which entities were liable to pay on such claims, required obtaining answers to a number of highly fact-intensive questions.

The R&Ws made in the PSAs about each of the mortgage loans generally included:

(1) that each of the mortgage loans were prudently originated;

(2) that each of the mortgage loans conformed to their applicable underwriting guidelines; and

(3) that the documentation needed to perfect the mortgage loans was included in the mortgage files.

See, e.g., JRA6560-65, ¶¶4, 10, 23, 37 (PTX 71.157-162).

Typically, in "repurchase" cases involving far less money than this matter, the issue of whether the mortgage loans comply with their underwriting standards is determined by identifying a representative loan sample, pulling the origination loan files for the sampled loans, having an expert compare the mortgage loan files to their underwriting criteria, and then extrapolating the results across the remainder of the pool(s) of mortgages at issue. *See, e.g.*, JRA4103:3-23 (Cowan); *Assured Guar. Mun. Corp. v. Flagstar Bank, FSB*, 920 F. Supp. 2d 475 (S.D.N.Y. 2013). Initially, Gibbs & Bruns, on behalf of the Institutional Investors, attempted to proceed that way (JRA13001 (RTX1451 at 002)), but BOA was unwilling to produce any loan files, the Institutional Investors lacked the power to force their production, and BNYM did not demand them. JRA1466:2-5, JRA1468:7-24 (Kravitt); JRA743:5-10 (Laughlin); JRA13004-24 (RTX1454).

To determine whether a sampled loan's documentation was adequate, and to quantify the damages for related deficiencies, requires reviewing the loan's legal file and associated "document exception" schedules. (BNYM already had the latter schedules, as BNYM itself was required to review each loan's legal documentation review at the inception of each Trust). However, neither BNYM nor its consultant (RRMS) ever attempted to quantify BOA's repurchase exposure for servicing deficiencies – doubtless because it would have also quantified BNYM's own exposure for having sat on the Trusts' rights relating to such loans since the Trusts were formed. JRA1831:4-14 (Kravitt). Instead, BNYM conveniently instructed its experts to review only the purported value of proposed forward-looking servicing improvements that the parties had included in the Proposed Settlement. At trial, BNYM relied on its expert, Philip Burnaman, who could have – but did not – quantify the value of the Trust's claims that loans with defective documentation be repurchased, and who instead calculated only the purported value of the Proposed Settlement's "servicing improvement" provisions. JRA2986:19-2987:25 (Burnaman).

Because Countrywide Home Loans ("CHL"), the corporate entity making the R&Ws, was the subject of a "forward triangular merger" in which "substantially all" its assets were transferred to BOA or one of its other affiliates in the second half of 2008, the assessment of how much was available to pay a large judgment was also a critical issue in the settlement negotiations. Indeed, BNYM has argued that Countrywide's "inability to pay" was the most important consideration in approving the Proposed Settlement. JRA5502:25-5503:4 (BNYM closing argument) ("[T]his was an easy decision … the trustee entered into this settlement because [$8.5 billion] is almost double what Countrywide could pay").

However, as the recent summary judgment decision in *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 965 N.Y.S.2d 284, 290-91 (Sup. Ct. 2013) reflects, questions relating to what actually occurred in connection with the 2008 Countrywide/BOA asset transfers -- and their implications for BOA's liability exposure – could be successfully contested where opposing counsel was actually willing to investigate the relevant facts. Indeed, although *MBIA* involved only 15 Countrywide securitizations (compared to the 530 here), Quinn Emanuel, on behalf of MBIA, fought hard to obtain BOA documents and deposed more than 50 current and former Countrywide and BOA directors, officers and others whose testimony was submitted on cross-motions on issues relating to BOA's liability for Countrywide's misconduct.[10] Immediately after the court *denied* BOA's motion for summary judgment on these issues, MBIA obtained a settlement *worth about $9.5 billion* in connection with just the small subset of Trusts at issue in that case. JRA5114:7-14 (Coates).

In contrast, here BNYM conducted *no* factual investigation on any of these issues that would have allowed it to advocate for and otherwise maximize certificateholders' recoveries in settlement negotiations – and it is thus hardly surprising that the Settlement Amount here is so massively inferior to the *MBIA* recovery on a *pro rata* basis. Apart from Brian Lin, BNYM retained its expert advisors only after the settlement negotiations were completed. JRA1857:14-1858:3 (Kravitt). As a general matter, Kravitt was also little more than an observer at the negotiations conducted by Gibbs & Bruns. JRA13352-53 at 17:14-18:5, JRA13393 at 260:17-23 (RTX4142). Indeed, Kravitt did not even attend the final negotiations on the settlement price, even though he had asked to do so, so that Mayer Brown could attest -- apparently without regard to its truth -- that the negotiations were "hard fought" and "arm's-length." JRA1471:11-20, JRA1850:4-1852:4 (Kravitt); JRA11669 (RTX90).

[10] *See MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 27 Misc. 3d 1061, 895 N.Y.S.2d 643 (Sup. Ct. 2010); *MBIA*, ECF 2703, 2947.

Instead of vigorously preparing a highly fact-dependent case on the issue of BOA's liability for Countrywide's repurchase obligations, it was only *after* BOA's and the Institutional Investors' counsel had arrived at the $8.5 billion number that BNYM retained experts (two law professors and two economic advisors) to provide *post-hoc* written opinions based on the meager factual record that had been made available to BNYM at the time of the negotiations. BNYM then provided these "expert" opinions to its Trust Committee as grounds for approving the deal (which it did). JRA7813-922 (PTX 444).

However, the legal opinions that Mayer Brown received *after* the $8.5 billion settlement number was negotiated did nothing to maximize certificateholders' recovery or to provide a meaningful basis on which to quantify the odds of success on reaching BOA's assets (or otherwise gaining its voluntary agreement to pay Countrywide's debts). First, these opinions came too late. Second, they merely confirmed that the successor liability and veil piercing issues were highly fact-dependent conclusions which presumably Mayer Brown's own legal staff could have determined themselves. The type of evidence which MBIA relied upon to make its case -- such as internal e-mails, internal records and deposition testimony that BNYM did not bother to demand from BOA -- thus could not be factored into either Professor Daines' or Mayer Brown's assessment of BOA's exposure.[11] *See, e.g.*, Daines's transmittal letter summarizing his task and conclusions:

> This memo describes in general terms the law of veil-piercing and successor liability in Delaware, New York and California . . . and describes how these laws may apply to a potential case against BAC. This does not constitute legal advice, but gives my general opinions as an academic interested in corporate law and is limited by the available factual record and certain assumptions I make. Both veil piercing and successor liability are fact-intensive legal theories; any ultimate judicial determination may turn on documents or testimony that would be produced at trial that I haven't seen. Much of my understanding comes from review of public filings and transaction documents as well as from discussions with BAC and legacy Countrywide personnel. I have not independently verified the accuracy of any facts discussed or assumed.

JRA7830 (PTX 444.18). Similarly, Professor Adler prepared an "expert opinion" on the issue of how the doctrine of "substantive consolidation" might apply in the event of a bankruptcy filing (JRA7901 (PTX 444.89)), but, in an effort to avoid cross-examination on the report, Mayer Brown asserted that this opinion was not relied upon at all in approving the Settlement. JRA4433:12-4434:20 (Adler).

BNYM's "investigation" of the other merits and damages issues fared no better. For example, RRMS's Lin was asked to analyze the value of repurchase claims based on (1) a one-page worksheet that the Institutional Investors had

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[11] Although Prof. Daines prepared an updated report for the Article 77 hearing, his positions still depended on the assumption that CHL's creditors were not harmed by the 2008 asset transfers, without understanding the facts sufficiently to know whether CHL was insolvent, whether its assets were stripped away for the purpose and with the effect of harming creditors, and whether the consideration paid was diverted to other entities. JRA3376:19-3377:17, JRA3381:16-3382:11, JRA3390:6-3393:7, JRA3393:19-3394:3, JRA3413:26-3414:17 (Daines); JRA4803:19-4804:12, JRA4805:12-4806:26, JRA4874:17-4875:12 (Coates).

produced that contained four settlement "scenarios," at least one of which was based on an analysis of 250,000 mortgage loans (not owned by the Trusts and whose source was unknown), and (2) an analysis that BOA had prepared which extrapolated its past experience in repurchasing mortgage loans sold to GSEs. Pursuant to this latter analysis, BOA concluded that 86% of the hundreds of billions of dollars of loans in the Trusts complied with their loan origination R&Ws -- including that the loans were "prudent" and met their stated creditworthiness criteria -- and that only 14% did not. JRA1248:24-1249:10 (Scrivener); JRA1969:25-1970:16 (Kravitt). Not surprisingly, Lin rejected the Institutional Investors' "breach" and "repurchase" rate percentages since they had not produced any back-up to confirm that the re-underwriting data had even involved Countrywide-originated loans, and accepted those calculated by BOA since he had no meaningful public information to come up with any other assumptions. JRA1963-1965:24 (Kravitt); JRA7917, JRA7922 (PTX 444.105, .110).

Mayer Brown did not ask for the data underlying the Institutional Investors' much higher breach and repurchase rate assumptions (JRA1967:12-16 (Kravitt)), nor did it delve into the assumptions underlying BOA's basic damages methodology -- even though Kravitt himself had earlier suggested that comparing the loans sold to GSEs to loans sold into private trusts was like comparing "sugar cane" to "apples" (*i.e.*, it did not even rise to that of an apples-to-oranges comparison, both of which are at least fruit). JRA11666 (RTX68). Indeed, the earlier January 2009 Fannie Mae letter to BNYM had reported that its analysis showed that 49.8% of its defaulted Countrywide loans contained significant defect exceptions relating to the borrowers' stated income, credit history, occupancy status and/or property values, and that "we estimate that equivalent or even higher levels of troubled loans exist in Countrywide's private label securitizations" (*i.e.*, the Trusts at issue here). JRA12865 (RTX1342-003).

There was also plenty of other publicly available evidence that BNYM could use in negotiations to vigorously attack BOA's dubious assertion that 86% of Countrywide's loans were "prudent," including the summary judgment decision and factual record available from the federal court's electronic docket for the SEC's civil action against former Countrywide CEO Angelo Mozilo. For example, in *S.E.C. v. Mozilo*, No. CV09-3994, 2010 WL 3656068, at *17-18 (C.D. Cal. Sept. 16, 2010), the court cited publicly-filed deposition testimony of Countrywide's former chief risk officer, who had testified how Countrywide had a least-common denominator underwriting policy by which it effectively lowered each of its separate loan underwriting criteria to "match" whatever peer offered the lowest standard for *each* such criteria, such that Countrywide had "the most aggressive [underwriting] guidelines in the industry." Kravitt testified that he was aware of the *Mozilo* action and related discovery materials, but had not read them. JRA1971:17-1973:22 (Kravitt); JRA12908-83 (RTX1391). Nor had he asked BOA to produce any other internal records, such as loan tapes, the underwriting guidelines themselves, audit reports, etc., that would have permitted Mayer Brown to demonstrate that BOA's underlying conclusion that as many as 86% of the mortgage loans were "prudent" or otherwise complied with their underwriting requirements was far-fetched. JRA1955:24-1958:4, JRA1959:25-1962:7 (Kravitt).

Finally, as the Article 77 Court found, and as discussed further immediately below in Argument §I.A, the Trustee conducted *no review at all* of the potential value of any claims relating to the modification of $31 billion of Trust-owned loans.

ARGUMENT

I. The Article 77 Court's Refusal to Approve the Proposed Settlement Based on BNYM's Unreasonable Failure to Investigate Any Loan Modification Claims Should Be Affirmed

A. Relevant Background

Beginning in 2008, the attorneys general ("AGs") of California and several other states sued Countrywide for engaging in predatory mortgage lending practices. BOA (which had acquired Countrywide on July 1, 2008) promptly agreed to settle these claims in October 2008. Although the AGs presumably could have sought to require Countrywide and BOA to pay large fines or make cash restitution to the consumers that they had illegally preyed upon, Countrywide and BOA instead agreed to "pay" for their misdeeds by agreeing to modify the terms of a huge number of mortgages – primarily by reducing the principal amounts due and interest rates payable on them. *See Greenwich Fin. Servs. Distressed Mortg. Fund 3 LLC v. Countrywide Fin. Corp.*, 603 F.3d 23 (2d Cir. 2010) ("*Greenwich II*") (noting the AGs' claims that Countrywide engaged in "deceptive sales practices" and "charged unlawful fees").

However, rather than bear the costs of their misconduct themselves, Countrywide and BOA sought to effectively pass on a huge percentage of the costs of the AG Settlement to the 530 Covered Trusts at issue here, inasmuch as the Trusts -- rather than Countrywide or BOA – owned the loans that were ultimately modified under the AG Settlement. *See* JRA85a (Decision at 18).

Not surprisingly, investors in certain Trusts later sued Countrywide for a declaration that, to the extent that Countrywide reduced any borrowers' principal or interest payments due pursuant to the AG Settlement on any loans owned by the Trusts, Countrywide had to repurchase such loans for 100% of their unpaid principal balance (plus any accrued interest). *See Greenwich Fin. Servs. Distressed Mortg. Fund 3 LLC v. Countrywide Fin. Corp.*, No. 650474/08, 2010 N.Y. Misc. LEXIS 6820, at *2 (N.Y. Sup. Oct. 7, 2010) (Kapnick, J.) ("*Greenwich I*"). The action was initially removed to federal court, and on remand Justice

Kapnick dismissed the claims. The dismissal, however, was based not on the merits, but on its conclusion that the PSAs' "no action" clause (JRA6539 at §10.08 (PTX71.136); JRA11474-75 (RTX13 at 115-16) precluded certificateholders from suing unless they had a 25% ownership stake. *Greenwich I,* at 7-8. Moreover, it is uncontested here that the *Trustee* could bring such claims, irrespective of the "no action" clause.

B. The Proposed Settlement Sought to Improperly Release Valuable Loan Modification Claims for Zero Consideration, and Was Thus Properly Rejected

The court below correctly refused to approve the proposed Settlement's release of the Trusts' rights to have Countrywide or BOA repurchase roughly $31 billion of loans that were modified pursuant to the AG Settlement.

First -- and aside from the additional arguments raised by Triaxx as to why Countrywide was required to repurchase modified loans under PSA §3.11(b) or §3.12(a) (*see* JRA16780-97) – Countrywide, as "seller" of the loans, was unambiguously required to repurchase any loans that breached certain specific representations that no loans in the Trusts violated any state predatory or abusive lending laws -- even if the loans met their "creditworthiness" R&Ws. *See* JRA11489, Schedule III-A at ¶10 (PTX 71.158).

Second, as the Article 77 Court correctly found, BNYM did not quantify or otherwise adequately investigate any loan modification claims. Instead, as the testimony below established:

(1) The Trustee did not undertake any effort to determine the value of any loan modification claims before agreeing to release them (JRA1923:17-1924:10, JRA2172:8-18 (Kravitt); JRA2412:5-11 (Bailey));

(2) The Trustee did not pursue any recovery from BOA or Countrywide for failing to repurchase modified loans, and did not even discuss such claims during negotiations (JRA3195:10-22 (Stanley));

(3) No portion of the $8.5 billion Proposed Settlement amount is compensation for the failure to repurchase modified loans (JRA3195:10-3196:4 (Stanley); JRA972:11-973:2 (Waterstredt)); and

(4) The release of such claims was a benefit to BOA and Countrywide, for which the Trusts received no compensation (JRA1930:11-1931:9 (Kravitt)).

In such circumstances, the Article 77 Court was plainly justified in finding that the Trustee acted unreasonably in agreeing to release all loan modification claims for *nothing* and "without investigating their potential worth or strength." JRA120a (Decision at 53) (citing Trustee's own trust law expert for the proposition that a Trustee may not release a claim without first determining its value); *see also Matter of N.Y. Title & Mortg. Co.*, 257 A.D. 19, 27 (1st Dep't 1939) (before settling and releasing beneficiaries' claims, trustee must "ascertain[] the value of [its beneficiaries'] claims," and noting that the burden of establishing the claims' value is on the trustee); *Matter of Birnbaum v. Birnbaum*, 117 A.D. 2d 409, 416 (4th Dep't 1986) (where fiduciary seeks release from its beneficiary, "there must be proof of full disclosure by the trustee of the facts of the situation and the legal rights of the beneficiary, and there must be adequate consideration paid").

In response, the Settlement Proponents argue that any loan modification claims were so devoid of merit that the Trustee could ignore them in negotiating the Proposed Settlement. Specifically, they primarily assert that the Trusts' governing agreements imposed no obligation to repurchase any loans that were modified "to benefit certificateholders" by mitigating the Trusts' credit losses. However, BNYM and the Institutional Investors simply ignore that Countrywide and BOA agreed to make the loan modifications at issue *to settle predatory lending claims of various States Attorneys General, and resolve Countrywide's and BOA's own liability in connection therewith*, and were *not* made in the ordinary course of business to mitigate losses on non-performing loans "to benefit certificateholders."

Indeed, even if BNYM were correct that BOA had the "better legal argument" on the loan modification claims, that would not support a rational conclusion that claims associated with $31 *billion* of modified loans have *no* value. Claims are routinely settled for highly material sums where both sides agree that the defendant's arguments are "better" than the plaintiff's. For example, a 10% chance of success on a $10 billion claim is still worth $1 billion. But having failed to perform a meaningful "analysis" of the loan modification claims' value, BNYM lacks even a minimal evidentiary foundation for justifying its agreement to release those claims for *nothing.* [12]

Finally, if the Settlement Proponents are correct that these claims are meritless, why file this appeal? BOA and BNYM could, presumably, simply agree to sever those claims from the scope of the proposed release, and to otherwise seek to proceed (subject to the outcome of Respondents' cross-appeals) with the remaining Proposed Settlement terms that the court below approved. That BOA has not done so is telling confirmation that BOA plainly *does* believe that it faces potentially substantial additional exposure on these claims.

Accordingly, the Article 77 Court's rejection of all of the Proposed Settlement's terms relating to loan modification claims should be affirmed.

II. All Remaining Aspects of Proposed Settlement Should Have Been Rejected on Due Process and Other Grounds

No one disputes that, in general, public policy favors settlement of disputes.

However, no principle is more fundamental to the American judicial system than the principle that no entity -- and no court -- can release the claims of non-parties without their consent, except in certain well-defined circumstances that fully comport with the Constitution's standards of Due Process. *See Taylor v. Sturgell*, 553 U.S. 880, 892-93 (2008) ("we have often repeated" the general rule

[12] BNYM also asserts that "many" of the modified loans "would have been subject to overlapping repurchase claims that were already accounted for in the Trustee's valuation of the rep-and-warranty claims." JRA11720-21 (BNYM Br. at 32). However, the Trusts' defect rates were extrapolated from GSE repurchases and, having failed to adequately investigate, BNYM is unable to quantify the extent (if any) to which GSE loans that were repurchased for creditworthiness defects were also modified for having violated state predatory lending laws.

that one cannot be bound by a judgment *in personam* in a proceeding where they were not designated or served as a party), citing *Hansberry*, 311 U.S. at 40; *see also BlackRock Fin. Mgmt. Inc. v. Segregated Account of Ambac Assur. Corp.*, 673 F.3d 169, 177 (2d Cir. 2012) ("[a]s a procedural matter, it is elementary that a court cannot bind a non-party absent special circumstances"). As discussed below, the Proposed Settlement does not meet the criteria of any of those exceptional circumstances, and the Article 77 Court thus lacked the authority to approve it in any respect.

A. Where the Trustee and its Counsel Denied that They Ever Assumed the Fiduciary Duty to Represent Non-Party Certificateholders, the Trustee Lacked the Authority to Release Those Certificateholders' Rights, and the Article 77 Court Lacked the Authority to Enter the Requested Relief[13]

BNYM, in bringing this proceeding, asked the Article 77 Court to make factual findings and enter an order that would release all claims of all certificateholders, the Trustee and the Trusts, whether "direct, derivative, or brought in any other capacity that [they] may now or may hereafter have," against all of the [BOA] Parties and/or Countrywide Parties "arising out of or relating to" the Trusts' mortgage loans' origination or servicing, including any breaches of associated representations and warranties or missing loan-related documentation.

[13] The Decision incorrectly states that no entity disputed the Article 77 Court's jurisdiction below. JRA69a (Decision at 2, n.2). However, the Public Funds' October 29, 2013 brief (JRA16847-61) raised the same arguments as here regarding the Article 77 Court's lack of authority to bind the non-party certificateholders.

JRA6049-50 (PTX 1.33-34). The proposed release also includes any claims against BOA based on successor liability, fraudulent conveyance, veil piercing or similar theories. *Id.* In addition, the Proposed Settlement calls for entry of a bar order that would permanently enjoin the certificateholders from suing on any of the released claims, and from suing BNYM with respect to the Settlement. *See* JRA6049-50 (PTX1.33-.34); JRA6080-82, ¶¶o, p & q (PTX1.64-.66).

State courts may not enjoin a person from prosecuting pending *in personam* claims in federal court (where BNYM has been sued).[14] *See, e.g.*, *Donovan v. City of Dallas*, 377 U.S. 408, 412-13 (1964) ("state courts are completely without power to restrain federal-court proceedings *in personam* actions," and state court injunctions addressed to parties rather than federal courts themselves are equally invalid); *Gen. Atomic Co. v. Felter*, 434 U.S. 12, 17 (1977) ("the rights conferred by Congress to bring . . . actions in federal courts are not subject to abridgement by state-court injunctions."). The Settlement Proponents have therefore pivoted to arguing that the release and factual findings requested by the Trustee will have "res judicata" effect that would bar other actions by certificateholders against BNYM. However, fundamental principles of due process limit the Court's jurisdiction to enter such relief against persons who have not been joined as parties to basically

[14] The Public Funds have sued BNYM for breach of the Trust Indenture Act ("TIA") and under state law for its failure, for years, to sue or otherwise act to enforce the Covered Trusts' repurchase rights. *Retirement Board of the Policemen's Annuity and Benefit Fund of the City of Chicago v. The Bank of New York Mellon*, No. 11-cv-05459 (S.D.N.Y.).

six circumstances. *See Taylor*, 553 U.S. at 892-93 (identifying six exceptions); *see also Briscoe v. City of New Haven*, 654 F.3d 200, 203 (2d Cir. 2011) (citing *Taylor*); *see also Cobalt Multifamily Investors I, LLC v. Shapiro*, No. 06-cv-6468, 2013 WL 5418588, at *3, n.5 (S.D.N.Y. Sept. 27, 2013) (same).

One exception to the Due Process rule against binding non-parties is *Taylor*'s "exception 3," which permits a non-party to be bound "in certain limited circumstances" where they were "adequately represented by someone with the same interests who [wa]s a party" to the suit -- and more particularly in "*properly conducted*" class actions and *suits brought by "trustees,* guardians, *and other fiduciaries.*" *Taylor*, 553 U.S. at 894-95. Defendants may also argue that an Article 77 proceeding falls into *Taylor* "exception 6," which recognizes that "in certain circumstances" a special statutory scheme may "'expressly foreclose[e] successive litigation by nonlitigants … if the scheme is otherwise consistent with due process,'" and giving bankruptcy and probate proceedings as examples. *Id.* at 895, quoting *Martin v. Wilks*, 490 U.S. 755, 762 n.2 (1989).

However, as *Taylor* makes clear, for *any* exception to the rule against binding non-parties to apply:

> *[A]t a minimum*: (1) the interests of the nonparty and her representative are aligned, *see Hansberry*, 311 U.S. at 43, 61 S.Ct. 115; and (2) either the party understood herself to be acting in a representative capacity or the original court took care to protect the interests of the nonparty, *see Richards [v. Jefferson County* 517 U.S.

> 793, 801 (1996)]…. In addition, adequate representation sometimes requires (3) [adequate] notice …

Taylor, 553 U.S. at 900. Significantly, the Supreme Court also emphatically rejected arguments to recognize a more general doctrine of "virtual representation," because doing so would risk authorizing the preclusion of non-parties' claims based merely on "identity of interests and some kind of relationship between parties and non-parties" *without* the kinds of essential procedural safeguards prescribed in *Hansberry*, *Richards* and modern class action practice. *Id.* at 901.

Here, it is undisputed that the Trustee and its counsel, Mayer Brown, have repeatedly denied acting as the non-party certificateholders' fiduciary. *See, e.g.*, JRA1797a (August 2, 2012 Tr. at 121.19) (BNYM "is not a fiduciary"); Jason Kravitt of Mayer Brown retained to represent BNYM "full stop" (JRA2465:10-15 (Bailey); JRA11290 (PTX 657 at 423)). This fact alone dooms the Trustee's request for any requested release, injunction or *res judicata* bar for the Proposed Settlement under *Taylor*. As *Taylor*'s discussion of its "exception 3" makes clear, the exception for "*properly conducted*" class actions and *suits brought by "trustees,* guardians, *and other fiduciaries*" requires the existence of a *bona fide, full-fledged fiduciary* (in addition to the separate requirement that the fiduciary acted "properly'). *Taylor*, 553 U.S. at 894-95. It is, for example, indisputable that class representatives and their counsel in class actions owe unflinching fiduciary duties to represent all absentee class members "*adequately and vigorously*," *Wyly v. Milberg Weiss Bershad & Schulman, LLP*, 12 N.Y. 3d 400, 412 (2009), nor can it be seriously disputed that *Taylor*'s reference to "trustees" was to trustees who had full-fledged "prudent person" fiduciary duties to act to protect their beneficiaries' interests as if they were its own.

Similarly, even if this case falls under *Taylor*'s "exception 6," which permits non-parties to be bound under "special statutory schemes" analogous to bankruptcy or probate mechanisms, such schemes are also structured to insure that those who seek to bind others are themselves bound by concomitant fiduciary duties to protect those other persons' interests. For example, creditor committees and their counsel in bankruptcy proceedings have full-fledged fiduciary duties to entire classes of relevant creditors (*e.g.*, to all unsecured creditors), and not just to the creditors that are committee members. *See, e.g.*, *Woods v. City Nat'l Bk. & Tr. Co. of Chicago*, 312 U.S. 262, 268 (1941) (committee members and counsel are fiduciaries, and citing Justice Cardozo's famous statement in *Meinhard v. Salmon*, 249 N.Y. 458, 464 (1928) that "a trustee is held to something stricter than the morals of the marketplace[;] [n]ot honesty alone, but the punctilio of an honor the most sensitive"). And although BNYM has cited *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1950) for the proposition that state courts have the authority to discharge trustees from future surcharge claims by their beneficiaries upon adequate notice, BNYM ignores the crucial fact that the trustee in *Mullane* did not dispute that it owed traditional fiduciary duties to *all* trust beneficiaries it sought to bind.

BNYM argues that it can invoke its authority to act as a trustee -- and to settle claims and seek judicial action that would bind the certificateholders -- while simultaneously disclaiming the responsibility to fully, adequately and vigorously represent them as their fiduciary. But as *Taylor* makes clear, BNYM's *authority* to release its beneficiaries' rights is no broader than the *duties* that it has actually acknowledged and assumed – *i.e.*, BNYM's view that it could "stand on its rights" to preserve its limited responsibilities as an "indenture trustee" – while simultaneously exercising the indentures' broader powers to sue on (or settle) Trust and certificateholders' claims – is misplaced.

That an indenture trustee's "authority" to bring suit (and thus to settle) is no broader than its duties to do so is illustrated by the Court of Appeals' recent decision in *Quadrant Structured Products Co. Ltd. v. Vertin*, ---N.E. 3d----, 2014 WL 2573378 (N.Y. June 10, 2014). In response to a question certified by the Delaware Supreme Court, the New York Court limited the reach of an indenture's "no action" clause to permit certificateholders to sue third parties, "directly and derivatively" for breach of fiduciary duty, fraudulent transfer and other common law claims (apart from breach of contract), because, where there was no "event of default," the "Trustee was without authorization to act" to bring those claims. *Id.* at *9. If, indeed, as BNYM insists, it has no duty to act because an event of default had not occurred, then the Settlement would be *ultra vires*, and void (or at least voidable) under the New York Estates, Powers and Trust Law ("EPTL") at the insistence of the Trustee's beneficiaries. *Rajamin v. Deutsche Bk. Nat'l Tr. Co.*, ---F.3d----, 2014 WL 2922317 (2d Cir. June 30, 2014) (citing N.Y. EPTL §7-2.4).[15]

B. The Settlement Also Fails on Additional, Independent Grounds Based on Other Aspects of the Trustee's Inadequate and Conflicted Conduct

Typically courts play no role in approving private settlements. Where, however, a court is asked to enter a settlement decree whose terms would release non-parties' claims and otherwise bind them, the invariable rule is that the court may do so only if the settlement "is fair, reasonable and adequate." *In re Masters Mates & Pilots Pension Plan & IRAP Litig.*, 957 F.2d 1020, 1026 (2d Cir. 1992), quoting *Weinberger v. Kenduck*, 698 F.2d 61, 73 (2d Cir. 1982). The Trustee has repeatedly sought to focus solely on the "substantive" fairness of the Proposed Settlement, which looks to whether the settlement consideration falls within an acceptable "range of reasonableness," and argues that its judgment of what is fair

[15] Of course, as held in various actions brought against BNYM and other MBS trustees demonstrate, BNYM had both the authority *and the duty* to sue to enforce the trusts' repurchase rights when confronted with overwhelming evidence of pervasive R&W violations. *See* fn. 6, *supra*; *Oklahoma Police*, 291 F.R.D. at 70. (trustee cannot rely on its own failure to give the triggering notice to escape its broader duties). *Oklahoma Police*, 291 F.R.D. at 70.

should not be second-guessed by the courts as long as the final result is within an acceptable "range."

However, courts have long recognized that any presumption of reasonableness attaches only where the absent parties' interests have been "adequately and vigorously" represented throughout the negotiation (and any related litigation process). *Cf. Wyly*, 12 N.Y. 3d at 412. Accordingly, a settlement will fail the "fair, reasonable and adequate" test unless the court is satisfied that the negotiation process was also *procedurally* fair. At a minimum, a court reviewing a proposed settlement must pay close attention to the negotiating process to ensure that the settlement resulted from arm's-length negotiations and that plaintiffs' counsel have, *inter alia,* engaged in the necessary discovery and otherwise effectively represented the class's interests. *See, e.g.*, *D'Amato v. Deutsche Bk.*, 236 F.3d 78, 85 (2d Cir. 2001); *see also Weinberger*, 698 F.2d at 74 (procedural fairness requires that non-parties whose interests are being compromised have been represented by counsel who "have possessed the experience and ability, and have engaged in the discovery, necessary to effective representation of the class's interests."). That clearly did not occur here. *See* Statement of the Case §E, *supra.* Procedural fairness also requires that the negotiations were free of undue pressure. *County of Suffolk v. Long Island Lighting Co.*, 907 F.2d 1295, 1323 (2d Cir. 1990); *see also In re AOL Time Warner S'holder Deriv. Litig.*, No. 02-cv-6302, 2006 WL

2572114, at *3 (S.D.N.Y. Sept. 6, 2006) (applying same standards in the context of settlement of derivative actions). Moreover, the "procedural" defects have also almost certainly caused the Proposed Settlement amount to be artificially deflated, by billions of dollars, thereby also dooming its ability to pass any test of "substantive" fairness.

1. The Trustee's Failure to Retain *Any* Counsel to Represent Certificateholders' Interests

First, although the Trustee may have hired counsel (Mayer Brown) with "competence and expertise" in the relevant legal areas, it conspicuously failed to retain counsel to represent *certificateholders.* JRA1655:17-1656:5 (Kravitt); JRA11290 (PTX 657 at 423) (Mayer Brown represented only BNYM's interests).

2. The Trustee's, and its Counsel's, Fatal Conflicts of Interest

Mayer Brown, in its opening argument for approval of the Settlement, asked the Court to assess BNYM's potential conflicts of interest in the following limited terms:

(a) Number one, did the Trustee get any money from the Settlement Agreement?

(b) Did the Trustee get any Trust property from the Settlement Agreement?

(c) Did the Trustee get a release of claims in this Settlement Agreement?

(d) Did the Trust get anything in this Settlement Agreement that it wasn't entitled to?

(e) Is there a benefit to the Trustee and a corresponding harm to certificateholders?

JRA147:5-20 (with BNYM answering "no" to each question). By closing arguments, after substantial evidence of both BNYM's and its counsel's conflicts had been entered into evidence, BNYM's counsel put the conflict questions even more narrowly:

(a) Did the trustee get money? No.

(b) Did the trustee get trustee property? No.

(c) And this is key: Is there a benefit to the trustee and a corresponding harm to the certificate holders? No.

JRA5576:5-20; *see also* JRA5579:24-26 (dismissing the objections to Mayer Brown's simultaneous representations of both BNYM and BOA as a theory "that [Mayer Brown] took a bribe and rolled over for [BOA]").

As to BNYM itself, it is indisputable that BNYM (through its counsel) did in fact (a) attempt to include a release in the Proposed Settlement for BNYM's failure to put back loans with defective documentation (JRA11672 (RTX118 at 3); JRA11960 (RTX235); JRA11670-73 (RTX118)) and (b) actually requested an injunction to protect itself from suits by certificateholders in the PFOJ. JRA6081, ¶p (PTX 1.65).

As attorneys, however, Mayer Brown's conflicted representation (and attempts to belittle them) was even more egregious, and is fatal to the Proposed Settlement here. Tellingly, even today Mayer Brown fails to recognize that in negotiating the compromise and release of Certificateholders' rights, *it was obligated to act as the certificateholders' fiduciary,* with the unflagging duty of undivided loyalty to act as their exclusive champion, to obtain and verify key facts and assumptions, and to in all other respects act on their behalf to maximize their recoveries in the negotiations. For, as the Court of Appeals has held, where attorneys for a trustee act to protect the investments of certificateholders, they owe to the certificateholder, "the same undivided loyalty that the trustee owes." *Matter of People [Bond & Mtge. Guar. Co.]*, 303 N.Y. 423 (1952).

Moreover, BNYM and its counsel are simply wrong to suggest that the breach of the fiduciary duty of loyalty turns on a showing of fraud, bad faith or harm to the certificateholders. To the contrary:

> One of the most fundamental duties of a trustee in any case is complete unselfishness and inflexible loyalty to the interests of the beneficiaries of the trust. This duty stems from human frailty when confronted with conflicting interests, evidenced by the centuries-old scriptural passage: "No man can serve two masters."
>
> *The attorneys, concededly in the same position as the trustee, owed an equally high degree of fidelity.... [b]*y *reason of their status as*

> *attorneys for the trustee, [] they were no less fiduciaries than was the trustee himself.*

303 N.Y. at 430 (emphasis added); *see also Matter of Clarke*, 12 N.Y.2d 183, 187 (1962) ("[a]n attorney for a fiduciary has the same duty of undivided loyalty to the *cestui* as the fiduciary himself").

In addition, where a fiduciary is torn by conflicting loyalties, it is no answer that the conflict purportedly did not harm its beneficiaries:

> Finally, we are told that the brokers acted in good faith, that the terms procured were the best obtainable at the moment, and that the wrong, if any, was unaccompanied by damage. This is no sufficient answer by a trustee forgetful of his duty. The law does not stop to inquire whether the contract or transaction was fair or unfair. It stops the inquiry when the relation is disclosed, and sets aside the transaction or refuses to enforce it, at the instance of the party whom the fiduciary undertook to represent, without undertaking to deal with the question of abstract justice in the particular case.

Wendt v. Fischer, 243 N.Y. 439, 443-44 (1926) (Cardozo, J.). Moreover, the evidence of *actual* harm in this case (though not required to reject the Proposed Settlement) is in any event far greater than it was in *Wendt*, for BNYM's failure to even threaten to sue on behalf of Trusts that did not meet the 25% presentment threshold cost the Trusts billions of dollars at the negotiating table, Statement of Case §D above, and its refusal to recognize its responsibilities resulted in the Trustee's acquiescence in key BOA-profferred assumptions and failure to investigate critical liability and damages issues that likely reduced the Trusts' recovery as well. Statement of Case §E. By stark contrast, where MBIA's counsel was faced with the same "collectability" barriers as those raised here, its vigorous discovery and advocacy of its clients' interests resulted in a settlement of $9.5 billion – for just 15 Countrywide trusts. JRA5114:7-14 (Coates).

Mayer Brown's misconduct was all the more egregious because its dual obligations to faithfully represent both certificateholders and BOA was *prima facie* improper under both New York and federal law. In federal court, simultaneous representation of two adverse parties is barred, absent an effective waiver, without regard to whether there is a "substantial relationship" between the matters in which the attorney provides its services. *See Cinema 5, Ltd. v. Cinerama, Inc.*, 528 F.2d 1384, 1386 (2d Cir. 1976) (citing principle that "each represented party is entitled to the attorney's undivided loyalty . . . because no man can serve two masters"). Similarly, in *Matter of Kelly*, 23 N.Y.2d 368 (1968), in addressing the conflicted role of a firm that represented the insureds and the insurance company in unrelated matters, the Court of Appeals noted that the dual representation "could have influenced the effectiveness and vigor with which claims against the carrier were prosecuted," and went on to hold that

> In the exceptional situations where representation may be permissible, despite a potential and sometimes even an actual conflict of interest, the lawyer must, at the very least, *disclose* to all affected parties the nature and extent of the conflict and *obtain their consent* to the continued representation.

Id. at 376 (emphasis added).

Compounding its misconduct, Mayer Brown also agreed to be retained to negotiate a compromise and release of the certificateholders' rights under the terms of a "limited" waiver, insisted upon by BOA, which prohibited it from suing BOA if a settlement was not reached. In so doing, the Trustee's negotiating team agreed to effectively tie their hands throughout the settlement process, because an attorney cannot "negotiate with full efficacy without at least being able to hint at the possibility of litigation." *In re Project Orange Assocs., LLC*, 431 B.R. 363, 375 (S.D.N.Y. 2010).

Here, nobody disclosed to certificateholders that (a) Mayer Brown -- despite being the BNYM's representative at the negotiations -- was simultaneously representing BOA; (b) that Mayer Brown, while obligated *de jure* to represent certificateholders, viewed itself as only the Trustee's counsel; or (c) that BNYM and Mayer Brown, at BOA's urging, had done a deal which precluded Mayer Brown from actually suing BOA if a settlement was not reached. Nor was any effort made to obtain the certificateholders' informed consent to these tainted arrangements. JRA1593:14-1594:14 (Kravitt). With no informed consent of the real parties in interest – but only the tainted "consent" of a self-interested Trustee who itself repeatedly denied having "prudent person" fiduciary obligations to the real parties in interest – the entire settlement process was irretrievably tainted, and no fruits of that process can bind the absent certificateholders as a matter of law.

3. The Trustee's Passive Acquiescence in the "25% Presentment Discount," and Its Failure to Even Threaten to Sue on Behalf of Trusts Where the 25% Presentment Level Was Not Met, Thwarted Certificateholders' Ability to Fairly Maximize Recovery on Their Claims

As Mayer Brown's Kravitt testified, rather than being obligated to maximize certificateholders' recovery from BOA, *et al.*, his role merely required him to take "into consideration the interest of the certificate holders" in the context of his firm's representation *of BNYM*. JRA11294 at 595:6-19 (PTX657). The discussion below is illustrative of just how passive – and prejudicial the Trustee's and its counsel's "consideration" of certificateholders' interests was.

For example, during the negotiation process, BNYM (through another of its counsel, the Pillsbury firm) repeatedly advised the Institutional Investors that BNYM would not bring suit on behalf of any Trusts where there was not a group of certificateholders who could meet the 25% ownership requirement, by tranche, for directing it to act. JRA6697 (PTX 102.1). Even when, at negotiations, BOA (who knew Mayer Brown could not threaten suit because of the limitations of its conflict waiver) told the negotiating parties that it was discounting its negotiating position by 20% because of this barrier to certificateholders' direct enforcement of the Trusts' repurchase rights, what BOA euphemistically referred to as the "presentation threshold," Kravitt sat quietly, telling no one whether BNYM would sue on certificateholders' behalf if negotiations broke down. JRA611:5-614:24

(PTX 657, Kravitt Dep.). Instead, Mayer Brown reaffirmed the Institutional Investors' statement in their brief below in support of the Settlement, that, even with their collective *$40 billion* of holdings, they were impotent to protect the hundreds of trusts where they did not have the 25% ownership interest – including where they owned $14 billion in holdings but less than 25% in particular trusts (and that investors effectively had no choice but to take BOA's deal). JRA11723-93; JRA11684-722 (RTX132; RTX131).

In so doing, Mayer Brown did not merely fail to "maximize" certificateholders' recovery, but (1) gave comfort to BOA to discount its negotiation position by billions of dollars; (2) fostered a belief on the part of the other party to the negotiations, the Institutional Investors, that they were impotent to protect their interests in absence of a settlement (which affected the number they were willing to accept); and (3) then coerced potential objectors to accept an inadequate settlement because they, too, had no alternative – all under circumstances which also would "coincidentally" protect BNYM from having to face the exposure of its own culpable failings to act against BOA and Countrywide years earlier to enforce the Trusts' repurchase rights.

C. Even if the Proposed Settlement Were Not Defective as a Matter of Law, the Decision Must Be Reversed and Remanded Because the Article 77 Court Misapprehended the Relevant Legal Standards

In rendering its decision, the Article 77 Court couched its task as "determin[ing] whether there was any [Trustee] abuse of discretion which would warrant judicial interference with the Trustee's decision to enter into the Settlement." JRA92a (Decision at 25). However, the Court got the standard backwards, as it is black-letter law that the Settlement Proponents bear the burden of proving that the Trustee acted reasonably and is entitled to any requested findings. *See* Bogert's TRUSTS & TRUSTEES §560 (burden of proving that discretionary power was properly used is on person who asserts rights resulting from use of that power, "for example, on the trustee claiming the approval of an account which shows that he exercised a power in a certain manner").

The Court then went on to expressly state that it was applying a "summary judgment" standard under CPLR §409(b), such that "if the papers fail to raise a triable issue of fact, the court is to grant judgment as a matter of law in favor of the appropriate party." JRA92a (Decision at 25). However, for all of the reasons set forth above, it was plain error for the Article 77 Court to grant summary judgment *for Petitioners,* and to effectively draw all factual inferences *against Objectors.*

In short, a review of the Decision shows that (in addition to ignoring Respondents' Due Process arguments) the Article 77 Court misapplied New York law by requiring Respondents to show that there was *no* evidence that supported BNYM's actions, instead of requiring the Trustee to bear *its* burden of proving that

BNYM did not abuse its discretion. *See, e.g.*, JRA94a-95a (Decision at 27-28) (accepting as true Trustee's argument regarding the Mayer Brown conflict waiver); JRA96a-991 (Decision at 29-32) (accepting as true Trustee's argument regarding forbearance and indemnity agreement); JRA801-87a (Decision at 13-20) (accepting as true Trustee's argument regarding its handling of each claim released under the Proposed Settlement – except as to the loan modification claims where the Court found that BNYM had done *nothing* to investigate their potential worth or strength).

Finally, even if the proceedings below were deemed a trial under CPLR §410 (which they were not) and the Decision were deemed to have resolved triable issues of fact (which it does not purport to do), reversal and remand is still warranted because the Decision does not contain the requisite factual findings under CPLR §4213 or provide any analysis or explanation of its result, as required for informed appellate review. In particular, the Decision's one-sentence conclusion that "the Trustee did not abuse its discretion in entering into the Settlement Agreement and did not act in bad faith or outside the bounds of reasonable judgment," (JRA119a-20a (Decision at 52-53)), offers no explanation of how the Court reached that conclusion. Instead, the Decision's purported "Analysis" section, as noted above, simply recites the parties' submissions without analysis. At a minimum, therefore, remand to allow the Court to review the evidence – and under the proper legal standard – is required. *See, e.g.*, *For the People Theatres of N.Y. Inc. v. City of New York*, 84 A.D. 3d 48, 48 (1st Dep't 2011) (remitting case to trial court where it had "failed to state the particular facts on which it based its judgment; rather, it simply detailed the municipality's evidence and arrived at legal conclusions"); *Bowie v. St. Cabrini Home, Inc.*, 906 N.Y.S. 2d 778 (1st Dep't 2009) (twice holding appeal in abeyance pending trial court's issuance of a decision conforming with the specificity requirements of CPLR §4213).

CONCLUSION

For the foregoing reasons, the Judgment below should be affirmed with respect to the loan modification claims, and in all other respects either (a) reversed so as to reject the Proposed Settlement in its entirety as a matter of law, or (b) reversed and remanded for review of its substantive fairness under the correct preponderance of the evidence standard.

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