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

In the matter of the application of

U.S. BANK NATIONAL ASSOCIATION, THE BANK OF NEW YORK MELLON, THE BANK OF NEW YORK MELLON TRUST COMPANY, N.A., WILMINGTON TRUST, NATIONAL ASSOCIATION, LAW DEBENTURE TRUST COMPANY OF NEW YORK, WELLS FARGO BANK, NATIONAL ASSOCIATION, HSBC BANK USA, N.A., and DEUTSCHE BANK NATIONAL TRUST COMPANY (as Trustees under various Pooling and Servicing Agreements and Indenture Trustees under various Indentures),

Petitioners,

for an order, pursuant to CPLR § 7701, seeking judicial instruction.

INDEX NO. 652382/2014

Assigned to: Friedman, J.

NOTICE OF THE NATIONAL CREDIT UNION ADMINISTRATION BOARD AS LIQUIDATING AGENT OF INTENT TO APPEAR AND OBJECT TO THE PROPOSED SETTLEMENT

Pursuant to the Court's October 9, 2014 Order to Show Cause, the National Credit Union Administration Board as Liquidating Agent for U.S. Central Federal Credit Union, Western Corporate Federal Credit Union, Members United Corporate Federal Credit Union, Southwest Corporate Federal Credit Union and Constitution Corporate Federal Credit Union (collectively, the "Liquidating Agents") submits this written notice of its intention to appear and object to the proposed settlement between The Bank Of New York Mellon, The Bank Of New York Mellon Trust Company, N.A., Deutsche Bank National Trust Co., HSBC Bank USA, N.A., Law Debenture Trust Co. Of New York, U.S. Bank, N.A., Wells Fargo Bank, N.A., and

Wilmington Trust, N.A., as trustees ("the Trustees") and JPMorgan Chase & Co. ("JPMorgan"), the sponsor, depositor and/or servicer of the trusts at issue.[1] The Trustees have filed a petition in this Court seeking judicial instructions and approval of the proposed settlement pursuant to Article 77 of the New York Civil Practice Law and Rules.

I. BACKGROUND

A. The Liquidating Agents have an Interest in the Settlement

The National Credit Union Administration ("NCUA") is an independent agency of the Executive Branch of the United States Government that, among other things, charters and regulates federal credit unions and operates and manages the National Credit Union Share Insurance Fund ("NCUSIF") and the Temporary Corporate Credit Union Stabilization Fund ("TCCUSF"). The TCCUSF was created by Congress in 2009 to allow the NCUA to borrow funds from the United States Department of the Treasury ("Treasury Department") to stabilize corporate credit unions under conservatorship or liquidation or corporate credit unions threatened with conservatorship or liquidation. The NCUA must repay all monies borrowed from the Treasury Department for the purposes of the TCCUSF by 2021. The NCUSIF insures the deposits of account holders in all federal credit unions and the majority of state-chartered credit unions.

The NCUA has regulatory authority over state-chartered credit unions that have their deposits insured by the NCUSIF. The NCUA Board manages the NCUA.

[1] The Liquidating Agents are concurrently moving this Court for an Order permitting them to intervene in these proceedings.

See Federal Credit Union Act ("FCU Act"), 12 U.S.C. §§ 1751, 1752a(a). Pursuant to 12 U.S.C. § 1787(a) and (b)(2)(A), the NCUA Board, in specified circumstances and in a distinct capacity, may close an insured credit union and appoint itself the Liquidating Agent for such credit union. As Liquidating Agent, the NCUA Board succeeds to all rights, titles, powers, and privileges of the credit union, its members, accountholders, officers, and directors.

U.S. Central Federal Credit Union, Western Corporate Federal Credit Union, Members United Corporate Federal Credit Union, Southwest Corporate Federal Credit Union and Constitution Corporate Federal Credit Union (collectively "the Credit Unions") purchased certificates in various RMBS at issue in this proposed settlement. In total, the credit unions purchased certificates in 96 of the trusts with an original total par of approximately $6.3 billion. In October 2010, the NCUA Board placed the credit unions into liquidation and appointed itself Liquidating Agent for each of the Credit Unions. Although the Liquidating Agents resecuritized many of the RMBS certificates at issue in 2010 and 2011, they retained various rights and interests associated with the resecuritized certificates due to their role as holders of residual certificates. The Liquidating Agents are also still the registered holders of some of the RMBS at issue. As such, the Liquidating Agents have significant interests in the proposed settlement because they are both direct holders of several certificates at issue and also retain certain rights and interests associated with a much larger number of certificates.

B. The Proposed Settlement

JPMorgan, either directly or through its affiliates, transferred millions of mortgage loans to securitization trusts that JPMorgan sponsored between 2005 and 2007. Through securitization of the loans, JPMorgan was able to sell certificates backed by pools of mortgage loans to investors in the form of RMBS certificates. RMBS are only as good as the loans that back them, and JPMorgan made numerous representations and warranties about the loans backing the RMBS at issue in the agreements governing the transactions. For example, JP Morgan made assurances that the mortgage loans were originated in accordance with applicable underwriting criteria, in addition to other representations about the characteristics of mortgage borrowers and the collateral for the mortgage loans. JPMorgan also promised that the loans would be prudently serviced. If there was a breach of the representations and warranties, JPMorgan agreed to repurchase any loans that did not comply with the representations and warranties.

In August 2014, the Trustees filed a Petition with this Court seeking approval of a $4.5 billion settlement with JPMorgan to resolve hundreds of billions of dollars of claims against JPMorgan for breaches of representations and warranties in the governing documents and servicing issues. The settlement was the product of confidential negotiations between JPMorgan and 21 institutional investors represented by Gibbs & Bruns, LLP. Neither the Liquidating Agents nor many other investors in the RMBS trusts at issue were privy to those discussions.

The Trustees allege the proposed settlement is fair and reasonable and urge this Court to approve it. If approved, the settlement will extinguish any repurchase

and servicing claims against JPMorgan for all certificateholders in all of the 312 accepting trusts.

II. OBJECTIONS

The essential question in this Article 77 proceeding is whether the Trustees acted within "the bounds of a reasonable judgment" by entering into the proposed settlement. *In re Stillman*, 107 Misc.2d 102, 110 (Sup. Ct. N.Y. Cnty. 1980). The Liquidating Agents have reviewed the few publicly available settlement documents and believe the settlement raises several areas of concern.

A. The Trustees Have Not Provided Enough Information About the Proposed Settlement

The Liquidating Agents cannot determine whether the proposed settlement is reasonable without additional information. Although the Trustees produced redacted expert reports that were prepared after the settlement was proposed, the Liquidating Agents need more information to properly evaluate whether the proposed settlement is adequate. For example, the Liquidating Agents need more information about the negotiation of the settlement, the strength of the claims that will be released by the settlement, and the allocation of the settlement funds.

B. The Allocation Formula Is Flawed

The allocation formula in the proposed settlement suffers from at least two serious flaws. First, the allocation formula does not account for the fact that many of the trusts still have viable claims against JPMorgan. In fact, the Fischel Report acknowledges that claims relating to approximately 50% of the trusts would still be timely even after allowing the notice and cure period to run. *See* Fischel Report at

¶124, *et seq*. and Exhibit R1. Some of the timely claims relate to trusts in which the Credit Unions purchased certificates. It is not fair or reasonable to allocate the same amount to trusts whose claims are likely timely as to trusts whose claims are likely time-barred. Yet that is exactly how the proposed settlement is structured.[2]

Second, the proposed settlement provides that when determining the allocation for trusts backed by loans originated by a specific list of originators, the trusts' losses are to be reduced by 90%. *See* RMBS Trust Settlement Agreement as modified on July 29, 2014, Section 3.05. Some of the certificates purchased by the Credit Unions are subject to this so-called 90% "haircut."

The publicly available settlement documents do not adequately explain why the reduction is being proposed for the trusts backed by loans originated by these originators, and no expert has analyzed this issue. And the Trustees have certainly put no evidence in the record justifying that large of a reduction. With no explanation as to why such a large a reduction in the losses (and therefore the dramatically lower allocation based on such losses) is warranted, it is difficult to see how it is fair or reasonable for these trusts to receive an allocation based on a mere 10% of their losses.

[2] Whether the repurchase claims for any particular trust are time barred depends on the facts and governing contract documents specific to that trust. The Liquidating Agents take no position regarding the timeliness of repurchase claims for trusts in which they do not have an interest.

C. The Total Amount of the Proposed Settlement Is Unjustifiably Low

Based on publicly available information, the total amount of the proposed settlement appears unjustifiably low. Numerous reports, settlements, and governmental investigations have revealed that many of the loans JPMorgan sold to the trusts failed to comply with JPMorgan's representations and warranties. As discussed below, JPMorgan has admitted as much in connection with its settlement with the U.S. Department of Justice ("DOJ"). In addition, loan file reviews performed by investors have revealed extremely high breach rates in JPMorgan-issued RMBS. For example, the Federal Finance Housing Agency ("FHFA") filed a complaint against JPMorgan in connection with 103 JPMorgan-issued RMBS, including 57 of the same trusts that are part of the settlement here. FHFA's re-underwriting of loan files in some of those trusts uncovered breach rates between 79% and 98%. *See* Amended Complaint, *FHFA v. JPMorgan Chase & Co., et al.*, No. 11-6188 (S.D.N.Y. June 13 2012), ¶¶ 359-362. Based on this information alone, it is questionable whether $4.5 billion is sufficient in exchange for releasing JPMorgan's repurchase liability for 1.25 million loans in 312 Trusts with an original face value of almost $300 billion and estimated losses of at least $60 billion. In addition to appearing low on its face, there are other indications that the proposed settlement amount may not be adequate.

The settlement amount here, expressed as a percentage of estimated lifetime losses on the loans at issue in the trusts, is below that reached in similar global repurchase settlements with Countrywide Home Loans, Inc., Bank of America and

others,[3] as well as smaller-scale repurchase settlements between various banks and monoline insurers. *See* Fischel Report at ¶33. Here, the settlement amount of $4.5 billion is approximately 7% of the estimated lifetime losses for the 330 trusts. By comparison, the Countrywide global repurchase settlement amount of $8.5 billion was approximately 7.9%-12.5% of the estimated lifetime losses for the trusts at issue there. Similarly the proposed global repurchase settlement of $1.125 billion with Citigroup is approximately 8.3% of estimated lifetime losses for the trusts at issue there. In other litigation, the settlement amounts have ranged from 13% to 74.5% of the estimated lifetime losses. *See* Fischel Report at Ex. F.

The Trustees' expert, Mr. Fischel, admits that the settlement here is lower than nearly every other repurchase settlement. *Id.* at ¶35. Mr. Fischel attempts to defend the fact that the settlement here is "below market" by noting several differences between this case and the others, *id.*, but his attempt falls flat in part because, despite Mr. Fischel's claims to the contrary, the claims at issue here are arguably stronger than those in other global repurchase settlements. For example, much of the uncertainty driving the settlement value down in the Countrywide case (which as noted above is already larger than the proposed settlement) has either been resolved in the trustees' favor or is not even an issue in this settlement.

First, Mr. Fischel asserts that Countrywide did not involve the same concerns regarding the timeliness of the claims at issue. *Id.* at ¶38. As noted above, however, according to Mr. Fischel's own analysis, approximately 50% of the trusts here still

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[3] *In the matter of the application of The Bank of New York Mellon*, Index No. 651786/11 (N.Y. Sup. Ct.)

have timely repurchase claims. *See Id.* at ¶124, *et seq*. and Exhibit R1. It is difficult to justify the low dollar amount of this settlement (in comparison to the potential value of the claims) based on an argument that the claims are subject to a limitations defense when this is only true with respect to about half of the RMBS trusts at issue.

Further, as Mr. Fischel admits, the likelihood of recovery from Countrywide was far less certain, because Countrywide was in dire financial straits and Bank of America's successor liability for Countrywide was far from clear. *Id.* at ¶40. There are no such concerns here because JPMorgan is solvent.

Next, the re-underwriting evidence in this case is more developed and much stronger than in the Countrywide case. According to the Fischel Report, Quinn Emanuel re-underwrote a sampling of the loans at issue here and discovered that between 79% and 98% of the loans examined were defective. *Id.* at ¶26. Fischel also notes that other investors or monoline insurers have conducted loan file reviews for 25 of the RMBS trusts at issue and the breach rate was determined to be 80%. *Id.* at ¶107 and Exhibit Q1.

And unlike Countrywide, JPMorgan has *admitted* to its wrongdoing. Most notably, in November 2013, JPMorgan paid $13 billion to end an investigation by the DOJ and the Attorneys General of several states into the packaging, marketing, sale and issuance of RMBS by JPMorgan, Bear Stearns and Washington Mutual Bank – two entities for which JPMorgan arguably assumed liability. Per the agreed

Statement of Facts annexed to the settlement agreement, JPMorgan admitted the following:

- From 2005-2007, JPMorgan conducted due diligence (largely through third party firms) to confirm that loans being securitized were originated in conformity with the applicable underwriting guidelines and were in compliance with federal and state law. *Id.* at 1-2.
- Through that process, JPMorgan employees were made aware that some of the loans did not comply with underwriting guidelines and did not have adequate compensating factors to justify deviation from the guidelines. *Id.* at 2.
- JPMorgan employees were also made aware of the fact that some of the properties backing the loans had appraisal values higher than the appraisal value indicated by the due diligence testing. *Id.*
- Despite these facts, JPMorgan continued to represent to investors of the RMBS backed by these loans that the loans complied with guidelines. *Id.*
- Despite these facts, JPMorgan also continued to represent to investors of the RMBS backed by these loans that no loan would be included in the pool if JPMorgan had reason to believe the originators' representations and warranties regarding the loans were inaccurate. *Id.*
- The loan pools JPMorgan securitized did include loans not in compliance with the applicable underwriting guidelines. *Id.*

- JPMorgan touted both the originators' underwriting practices and its own due diligence process to investors. *Id.* at 3.
- JPMorgan waived a substantial number of loans into loan pools that the third party due diligence firms had identified as not in compliance with guidelines and lacking sufficient compensating factors. In other words, the loans were securitized and not removed from the pool despite the fact the defects in the loans had not been cured. *Id.* at 3-5.
- JPMorgan had an undisclosed tolerance rate of 15% for faulty appraisals, meaning it would securitize loans so long as the appraised value was not 15% higher than the appraised value of its due diligence valuation firm. *Id.* at 5.
- JPMorgan sometimes denied potential investors' requests for specific information regarding the loans and sometimes provided potential investors with misleading information regarding the specific loans. *Id.* at 6-7.

Mr. Fischel acknowledges both the DOJ settlement and JPMorgan's admitted wrongdoing (Fischel Report at ¶48), but does not seem to realize the impact these admissions would likely have in any repurchase action against JPMorgan.

In short, the differences between the proposed settlement and the Countrywide settlement do not support the low settlement amount here. In fact, the case against JPMorgan is stronger than the Countrywide case, therefore indicating

the settlement here should be higher. There is simply no justification for the unreasonably low settlement amount here.

D. The Trustees' Reliance on Mr. Fischel's Recommendations Was Unjustified

The Trustees relied on Mr. Fischel—an expert paid for by JPMorgan—to determine that the proposed settlement is fair for the accepting trusts. Mr. Fischel performed a trust-by-trust analysis to identify those trusts that could achieve superior results by rejecting the settlement and pursuing separate actions against JPMorgan. He used three factors to determine whether a trust should reject the proposed settlement: (1) whether 15% or more of certificateholders oppose the deal; (2) whether it appears that the recovery in a repurchase action would exceed the settlement recovery based on available information for the trust, including any reunderwriting of loans in the trust; and (3) whether repurchase claims likely would be time-barred or whether recovery on servicing claims would exceed the settlement recovery for the trust. *See* Fischel Report at 17-19.

Mr. Fischel's approach is problematic. For example, factors two and three point to rejection for many trusts, but Mr. Fischel still recommends acceptance based solely on the fact that 15% or more of the certificateholders in those trusts failed to object to the settlement prior to his report. However, Mr. Fischel's numbers certainly under-represent the true number of objecting certificateholders as certificateholders's opinions were never solicited nor were they ever provided with a formal mechanism to register their objections. For those trusts, the trust could recover more money in a repurchase action. In addition, the potential recoveries in a

number of the repurchase actions would be large. For example, for BSMF 2007-AR3, a trust in which the Liquidating Agents have an interest, loan file re-underwriting done in connection with prior litigation showed a breach rate of 98%. Based on this figure, Mr. Fischel estimates that the Trust could potentially recover approximately $684 million in a repurchase action against JPMorgan instead of the approximately $45 million that the trust will receive if the settlement is approved. Fischel Report at Ex. Q1, p. 4. Despite the enormous potential upside to litigation, Mr. Fischel recommends acceptance for this trust. There are numerous other examples of similar problems in Mr. Fischel's report. It is unreasonable for the Trustees to rely on Mr. Fischel's report when litigation appears to be a better option for many of the trusts.

IV. CONCLUSION

Until these issues and objections are adequately addressed, the Liquidating Agents urge the Court to deny approval of the settlement. The Liquidating Agents reserve their rights to modify and/or supplement this objection.

Dated: November 3, 2014

NATIONAL CREDIT UNION ADMINISTRATION BOARD,
as Liquidating Agent of U.S. Central Federal Credit Union, Western Corporate Federal Credit Union, Members United Corporate Federal Credit Union, Southwest Corporate Federal Credit Union, and Constitution Corporate Federal Credit Union

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