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

In the matter of the application of	Index No. 652382/2014
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),	Part 60 Hon. Marcy S. Friedman
Petitioners,	
for an order, pursuant to CPLR § 7701, seeking judicial instruction.	

AMBAC'S STATEMENT OF GROUNDS FOR OBJECTION

Ambac Assurance Corporation and The Segregated Account of Ambac Assurance Corporation (collectively, "Ambac"), by and through their undersigned counsel, respectfully submit this statement of grounds for objection to the proposed settlement entered into by the Petitioner Trustees and JPMorgan Chase & Co. and its affiliates (the "Proposed Settlement").

PRELIMINARY STATEMENT

The Trustees cannot establish that their acceptance of this proposed settlement was reasonable with respect to, at a minimum, the Accepting Trusts for which Ambac provided insurance. The Trustees cannot ignore the vast evidence of Bear Stearns' fraudulent practices and misrepresentations and the staggeringly high incidence of materially defective loans Ambac has uncovered over the past six years in its litigations against JPMorgan concerning securitizations underwritten and sponsored by, respectively, JPMorgan-affiliates Bear Stearns and EMC Mortgage Corporation (with Bear Stearns, "Bear Stearns").

Ambac first sued Bear Stearns in 2008 respect to four Non-Accepting Trusts.[1] In that litigation, Ambac uncovered extensive evidence of a RMBS securitization machine at Bear Stearns that had run amok. Ambac found compelling evidence that Bear Stearns lied about the quality of loans – telling Ambac and investors that the collateral was of investment quality while internally describing that collateral as a "Sack o' [expletive]" – and lied about its due-diligence and quality-control processes – telling Ambac and investors that these processes were in place to ensure the quality of the collateral when in fact they were used by JPMorgan to pocket recoveries for itself at the expense of the trusts. The evidence discovered by Ambac about Bear Stearns's practices in no small part lay the foundation for settlements by JPMorgan with government entities and private plaintiffs totaling tens of billions of dollars.

In the summer of 2011, Ambac began to investigate potential breaches in other Bear Stearns securitizations that were experiencing massive collateral losses and for which Ambac has incurred, or is projected to incur, hundreds of millions of dollars in insurance claims. Based on the evidence uncovered in its first action against Bear Stearns, Ambac notified the trustees of potential breaches of representations and warranties and sought the trustees' assistance in obtaining loan files. In the interim, Ambac performed data analysis on these deals, which demonstrated the existence of widespread breaches of representations and warranties. When Ambac obtained loan files and conducted a forensic re-underwriting of those files, it corroborated its findings of pervasive breaches of representations and warranties – breach rates

[1] *Ambac Assurance Corporation v. EMC Mortgage LLC et al.*, Index No. 650421/2011 (N.Y. Supreme Court) ("*EMC I*"). *See* Ex. 1.

ranging from 60% to 90%. Ambac notified the Trustees for these transactions about these breaching loans and these Trustees in turn requested that JPMorgan repurchase the loans.

In early 2012, Ambac sued JPMorgan for fraud and breach of contract to recover the losses it suffered on these trusts.[2] On October 16, 2014, however, the First Department affirmed the dismissal of Ambac's breach-of-contract claims on the basis of lack of standing. Although Ambac believes that ruling is erroneous, Ambac's sole contractual remedy against JPMorgan is, at least for now, in the hands of the Trustees.

Given the Trustees' knowledge of the evidence of Bear Stearns' fraudulent practices and misrepresentation that Ambac has uncovered and presented to the Trustees, the Trustees simply cannot establish that their acceptance of this proposed settlement with respect to the Accepting Trusts for which Ambac provided insurance was reasonable. If even half of the loans in these Ambac-insured trusts contain material breaches (and all evidence suggests that is a *conservative* assumption), these trusts would recover approximately $1.8 billion, which is $1.5 billion more than the Trustees claim is "reasonable" for these transactions.

And the process employed by the Trustees here is deeply flawed. For one, even the Trustees' own expert, Professor Daniel Fischel, struggles to defend the adequacy of the value of the Proposed Settlement overall. Professor Fischel has no plausible explanation why the proposed "Settlement Payment" here is significantly below other settlements, including the other major omnibus trust settlement (the Countrywide settlement) when the quality of JPMorgan

[2] *Ambac Assurance Corporation et al. v. EMC Mortgage LLC et al.*, Index No. 651013/2012 (N.Y. Supreme Court) ("*EMC2*"). *See* Ex. 2. Ambac asserted fraud and contract claims with respect to six Accepting Trusts: Bear Stearns Mortgage Funding Trust 2006-AR2 ("BSMF 2006-AR2"), Bear Stearns Mortgage Funding Trust 2006-AR4 ("BSMF 2006-AR4"), GreenPoint Mortgage Funding Trust 2006-AR2 ("GPMF 2006-AR2"); GreenPoint Mortgage Funding Trust 2006-AR3 ("GPMF 2006-AR3"); Structured Asset Mortgage Investments II Trust 2006-AR7 ("SAMI 2006-AR7"); Structured Asset Mortgage Investments II Trust 2006-AR8 ("SAMI 2006-AR8"). In addition, Ambac had sought to assert a contract claim with respect to a seventh Accepting Trust, GreenPoint Mortgage Funding Trust 2005-AR5 ("GPMF 2005-AR5"). Finally, Ambac has asserted a fraud claim with respect to Bear Stearns Alt-A Trust 2006-R1 ("BALTA 2006-R1"), which is backed in part by tranches from an eight Accepting Trust, namely BALTA 2006-4.

collateral is *worse* than the Countrywide collateral and when there is no bankruptcy risk, which, was the primary basis for a low recovery in the Countrywide settlement.[3] Although the Trustees may *now* try to justify the Proposed Settlement on the basis that repurchase claims for certain trusts may be time-barred, there is no differentiation in the settlement allocation between trusts whose claims may be time-barred and those whose claims are undoubtedly timely. Moreover, while a decision by the First Department *after this proposed settlement was negotiated – ACE Securities Corp. v. DB Structured Products, Inc.*, 977 N.Y.S.2d 229 (1st Dep't 2013) ("*ACE v. DB Securities*") – might call in to question the timeliness of claims as to some deals, other deals – like the Ambac-insured trusts – are subject to contract language not addressed in *ACE v. DB Securities* that render the repurchase claims timely.[4]

For another, the Trustees' and Institutional Investors' acceptance of the Proposed Settlement smacks of self-serving hypocrisy. For example, while supporting the Trustees' refusal to enforce repurchase obligations here and settle for pennies on the dollar, elsewhere some of these same Institutional Investors are suing these same Trustees for failing to fulfill their prudent-person obligations under the governing agreements and the Trust Indenture Act. As the Institutional Investors correctly point out in other litigations, where Events of Default have long existed under the governing trust documents, the Trustees are required to take action to maximize the recovery for the trusts. The Institutional Investors cannot credibly say there are Events of Default in other transactions, but not in these. Similarly, the Trustees hypocritically suggest they have no independent discretion of any kind to sue to enforce repurchase obligations – they will sue only if a sufficiently large group of investors direct them to do so and agree to

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[3] *See* Expert Report of Daniel R. Fischel, dated July 17, 2014 ("Fischel Report"), at ¶ 40 and n. 56.

[4] The Court of Appeals is currently hearing an appeal of *ACE v. DB Securities*. Even if the Court of Appeals affirms, there are a variety of bases for holding JP Morgan liable for deals that closed more than six years from when this proceeding was instituted (adjusted for any applicable tolling). *See*, *infra*, at 11-12.

fund the litigation – but then exercise independent discretion in agreeing to the Proposed Settlement, even without any direction and indemnity and even for trusts where they know it is a bad deal.

Unlike the Trustees, Ambac has invested substantial resources in investigating and marshalling evidence to support its claims against JPMorgan. It therefore strenuously opposes the Trustees' decision to ignore this evidence and release those well-established claims for pennies on the dollar. The Trustees are not permitted to compromise investors' rights merely because it is the path of least resistance for themselves.

BACKGROUND

A. The Ambac Insured Trusts and JPMorgan's Representations and Warranties

Ambac provided financial guaranty insurance with respect to eight RMBS trusts that are subject to the Proposed Settlement (the "Ambac Insured Trusts"). For each of these transactions, EMC served as Sponsor, while Bear, Stearns & Co. was underwriter and deal manager. Initially, EMC was also the Servicer for BSMF 2006-AR2, BSMF 2006-AR4, GPMF 2005-AR5, and GPMF 2006-AR2, although JPMorgan subsequently transferred EMC's servicing assets to JP Morgan Chase Bank, NA, which currently serves as Servicer.

Petitioner Wells Fargo serves as trustee and Petitioner Law Debenture Trust Company of New York serves as "separate trustee"[5] for BSMF 2006-AR2, BSMF 2006-AR4, GPMF 2005-AR5, GPMF 2006-AR2, GPMF 2006-AR3. Petitioner BNY Mellon serves as trustee for SAMI 2006-AR7 and SAMI 2006-AR8, and Wells Fargo is Master Servicer and/or Securities Administrator for those trusts. Petitioner Wilmington Trust serves as trustee for BALTA 2006-4, certain tranches of which are included in BALTA 2006-R1, which Ambac insured.

[5] Since Wells Fargo is an originator/sponsor in other RMBS transactions, it obtained judicial approval for the appointment of a "separate trustee" in those transactions where it serves as trustee, in an attempt to avoid the conflict of interest present in being required to both enforce and defend repurchases.

Pursuant to Mortgage Loan Purchase Agreements ("MLPAs") and Pooling and Servicing Agreements ("PSAs") for each of the Ambac Insured Trusts, Bear Stearns made numerous representations and warranties concerning the characteristics and credit quality of the loans in the Ambac Insured Trusts.[6] Bear Stearns represented, among other things, that (i) the mortgage loans were originated in accordance with certain specified underwriting guidelines; and (ii) the information set forth in the Prospectus Supplement, made available to investors and Ambac in connection with the sale of certificates, including representations concerning loan-to-value ("LTV") ratios for the mortgage loans and occupancy status of the borrower, was true and correct in all material respects. *See* Ex. 2, §§ 7(xxi) and 8(vii).

The PSAs provide that if the Trustee or the Servicer (or, for certain deals, the Master Servicer and/or Securities Administrator) discovers a breach of one a representation and warranty, it is required to give prompt notice to the other parties. *See* Ex. 3, §2.03(b). Where such a breach materially and adversely affects the interests of Certificateholders, Bear Stearns (and now JPMorgan) is required to repurchase the loan or (if within a certain period of time) replace it with a non-breaching loan. *See* Ex. 4, § 7.[7]

As an inducement for Ambac to provide insurance, Ambac was made a third-party beneficiary of both the MLPAs and the PSAs, including with respect to the representations and warranties from Bear Stearns regarding the mortgage loans.

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[6] The PSA and MLPA for BSMF 2006-AR4 are annexed hereto, respectively, as Exhibits 3 and 4. The transaction documents for the other six Ambac Insured Trusts are substantially the same.

[7] The MLPAs provide that a cause of action against Bear Stearns to enforce its repurchase obligations does not "accrue" until "(i) discovery of such breach by [Bear Stearns] or notice thereof by the patty discovering such breach ***and*** (ii) failure by [Bear Stearns] to cure such breach, purchase such Mortgage Loan or substitute a qualifying Substitute Mortgage Loan. . ." Ex. 2, § 7 (emphasis added). A plain reading of this "Accrual Provision" means that the statute of limitations on a claim to enforce the repurchase obligation does not begin running until Bear Stearns (or its successor) failed to cure the breach and, therefore, that repurchase claims against JPMorgan are clearly timely. *See generally* Expert Report of Hon. Anthony J. Carpinello, dated May 5, 2014 at 3 ("Carpinello Report") ("the process for determining whether a claim is time barred requires the establishment of the date on which the claim 'accrues'. . .") (*citing* CPLR 203(a)).

B. Ambac Suffers Massive Losses

Large percentages (from nearly 60% to more than 80%) of the securitized loans in the loan groups underlying the securities insured by Ambac have defaulted or are severely delinquent, causing massive shortfalls in the cashflows required to pay down the securities and, thereby, requiring Ambac to make significant payments with respect to its insurance policies. With respect to the loan groups for which Ambac provided insurance, the Ambac Insured Trusts have experienced cumulative losses of more than $2.71 billion, resulting in over $500 million in claims that Ambac has paid or is obligated to pay under its policies.

C. Ambac Sues JPMorgan

In 2008, Ambac sued EMC in federal court for breach of contract relating to four Non-Accepting Trusts. During the course of that litigation, it became apparent that not only were there widespread defects in the loans underlying those transactions, but that there was widespread fraud perpetrated by EMC and Bear Stearns. Accordingly, in 2010 Ambac amended its complaint related to the four Non-Accepting Trusts, including by adding fraud claims against Bear Stearns, and when this amendment caused the federal court to lose diversity jurisdiction in 2011, Ambac refiled the case in New York Supreme Court, New York County. In 2012, Ambac filed a second lawsuit against JP Morgan for fraud and breach of contract with respect to the eight Ambac Insured Trusts at issue in this action.

As detailed in Ambac's two complaints, there is powerful and extensive evidence of pervasive malfeasance by Bear Stearns. For example, Ambac uncovered evidence that Bear Stearns systematically abandoned the applicable underwriting guidelines to maximize the volume – and therefore the profits – of Bear Stearns' securitization operation.[8] Bear Stearns conducted sham due diligence on the loans it securitized, directing the third-party diligence

[8] *See generally* Exs. 1 and 2.

vendors it hired to ignore evidence of fraud and other guideline violations to allow defective loans to be included in its securitizations. EMC – which was both the sponsor and servicer for many of the Ambac Insured Trusts – also engaged in a practice in which it would negotiate "bulk settlements" of repurchase claims against loan originators and pocket the proceeds for itself *yet failed to repurchase the same defective loans from the securitization trusts.* An investigation by the SEC revealed that the bulk settlement practice continued even after JPMorgan acquired EMC, and in November 2012, JPMorgan agreed to pay more than $220 million to settle charges brought the SEC.[9]

Prior to initiating the litigation in 2012 related to the Ambac Insured Trusts, Ambac endeavored to obtain loan files, but had considerable difficulty doing so. In the absence of loan files, Ambac commissioned a forensic review based on publicly available data of 5,000 loans with an aggregate principal balance of approximately $2 billion. The forensic review revealed, among other things, that (i) approximately 15% of loan properties that Bear Stearns represented were "owner occupied" were actually second homes or investment properties; (ii) the LTV ratios for 23% of the loans were misrepresented by 10% or more; and (iii) contrary to Bear Stearns's representations that none of the loans had an LTV ratio higher than 100%, more than 8% of the loans had LTV ratios greater than 100%, meaning the loan was greater than the value of the property. Ambac ultimately was able to obtain loan files for a sample of 100 loans in each of six of the eight Ambac Insured Trusts, and re-underwriting review of those files indicated a breach rate of 61% to 90% for the sampled loans.[10] JPMorgan refused to repurchase any of the loans.

Much of the evidence that Ambac has uncovered has been used to support other actions

[9] *See* http://www.sec.gov/litigation/litreleases/2012/lr22533.htm.

[10] *See* Appendix A. Attached as Exhibit 7 are the breach notices that Wells Fargo (in its capacity as Master Servicer) sent with respect to SAMI 2006-AR8 and that Law Debenture sent with respect to BSMF 2006-AR2, BSMF 2006-AR4, GPMF 2005-AR5, GPMF 2006-AR2, and GPMF 2006-AR3.

and settlements against JPMorgan. For example, on November 19, 2013, the United States Department of Justice announced that it entered a $13 billion settlement with JPMorgan (the "DOJ Settlement") with respect to securities issued by many RMBS trusts, including all of the Ambac Insured Trusts. As summarized in the DOJ Settlement, "JPMorgan acknowledged it made serious misrepresentations to the public – including the investing public – about numerous RMBS transactions," and JPMorgan admitted that "JPMorgan employees knew that the loans in question did not comply with those [underwriting] guidelines and were not otherwise appropriate for securitization, but they allowed the loans to be securitized – and those securities to be sold – without disclosing this information to investors." JPMorgan also admitted that it "waived" in loans for securitization that its due diligence vendors identified as non-compliant because, among other reasons, they were "missing documentation."[11]

ARGUMENT

I. THE SETTLEMENT COMPENSATION FOR THE AMBAC INSURED TRUSTS IS INADEQUATE

The Trustees retained Professor Daniel Fischel to evaluate the overall adequacy of the Proposed Settlement. Professor Fischel acknowledges that the value of the Proposed Settlement for investors (and monoline insurers like Ambac) is lower than other comparable settlements.[12] Thus, Professor Fischel concedes that the cash payment *plus* the subservicing protocol are worth only about 7.1% of the Settling Trusts' projected lifetime losses.[13] In comparison, the $8.5 billion Countrywide settlement, which was only partially approved and triggered vigorous investor opposition, reimbursed investors for approximately 10.2 to 17.1% of projected losses.[14] Similarly, the pending Citibank settlement would compensate investors for 8.3% of expected

[11] *See* http://www.justice.gov/opa/pr/2013/November/13-ag-1237.html.
[12] *See* Expert Report of Daniel R. Fischel, dated July 17, 2014, at ¶ 28 and Ex. D ("Fischel Report").
[13] *Id.*, ¶ 95.
[14] *Id.*, ¶ 37.

lifetime losses.[15] Professor Fischel discusses a number of other settlements, virtually all of which provide significantly more value than the Proposed Settlement.[16]

Moreover, the Countrywide settlement was reached without the benefit of meaningful review of loan files to estimate the percentage of loans that violated underwriting guidelines. Here, in contrast, Professor Fischel acknowledges further that there are dozens of settled and pending litigations brought by financial guaranty insurers such as Ambac, RMBS trustees (including several of the Petitioners), and RMBS investors in which the plaintiffs have re-underwritten many thousands of loans in trusts covered by the proposed settlement. Those reviews uniformly demonstrate that extremely high percentages of loans in the trusts did not comply with the represented underwriting guidelines.[17] Indeed, Professor Fischel tested the idea that JPMorgan loans were better than Countrywide and Citigroup, but found the opposite. Thus, evaluated on a global basis, the Proposed Settlement appears to be a great deal for JPMorgan and a very bad deal for investors and Ambac. The inadequacy of the Proposed Settlement with respect to the Ambac Insured Trusts in particular is even more stark.

A. The Potential Recovery From Litigating Repurchase Claims For The Ambac Insured Trusts Dwarfs The Settlement Compensation

Putting aside the timeliness issue (discussed below), the potential recovery from litigating repurchase claims for the Ambac Insured Trusts is significantly higher than the value of the Proposed Settlement, even under Professor Fischel's analysis. Professor Fischel concedes that is the case for every Ambac Insured Trust under at least three of his six valuation methods and for some of the trusts (BSMF 2006-AR2 and GPMF 2005-AR5) under all six methods.[18]

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[15] *Id.*, ¶ 41.

[16] *See generally id.*, Ex. D.

[17] *See, e.g., id.* at ¶ 107 (stating that review of loan files for 25 trusts covered by the Proposed Settlement showed all but one trust with material representation and warranty breach rates greater than 80%)

[18] *See id.*, ¶¶ 106-120, Exs. Q1-Q6. It should be noted that two of Professor Fischel's methods – Loan File Reviews and Outstanding Repurchase Demands – require the cooperation of JPMorgan and the Trustees to make loan files

At this time, Ambac has been able to obtain a sample of 100 loan files for six of the Ambac Insured Trusts and retained a forensic underwriting expert to re-underwrite the loans. Applying Professor Fischel's valuation methodology for repurchase claims – *i.e.*, multiplying the breach rate identified in the loan file review by the total losses for the trust – to the results of that loan file review yields the potential litigation recovery amounts between *eight and twelve times greater* than the value of the Proposed Settlement.[19] *See* Appendix A. Thus, under any reasonable set of assumptions, the litigation value of the repurchase claims for the Ambac Insured Trusts greatly exceeds the value of the compensation offered in the Proposed Settlement.

B. The Trustees Have No Basis To Conclude Repurchase Claims For The Ambac Insured Trusts Are Untimely

Professor Fischel, relying on the analysis of New York law by retired Justice Anthony Carpinello, determined that repurchase claims for SAMI 2006-AR7 and SAMI 2006-AR8 were timely.[20] Given the value of the potential recovery for these trusts, the decision to reject the Proposed Settlement and litigate is obvious. It would be economically irrational not to.

Professor Fischel concluded that repurchase claims for the other Ambac Insured Trusts are untimely, once again relying on Justice Carpinello. However, Justice Carpinello was never asked to consider the timeliness of claims under contracts with an Accrual Provision as in the MLPAs (*see* note 6), and his analysis focused heavily on *ACE v. DB Securities*, Carpinello

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available for review, and such cooperation was not always forthcoming. Despite strenuous efforts over the course of almost a year, Ambac was not able to obtain loan files for BSMF 2006-AR4, GPMF 2006-AR2, SAMI 2006-AR7, and SAMI 2006-AR8 by the time it commenced litigation against JPMorgan. Accordingly, Professor Fischel did not have re-underwriting data for those trusts and so it attributed zero litigation value to those trusts with respect to his Loan File Review method. And without loan files, Ambac also was unable to direct the Trustee to demand repurchase of the breaching loans, so Professor Fischel gave no "credit" to those trusts under the Outstanding Repurchase Demands method.

[19] Although Ambac does not have access to loan files for SAMI 2006-AR7, and therefore lacks re-underwriting data for that trust, there is no reason to believe that the loan pools underwritten during generally the same period under generally the same circumstances will have vastly different breach rates. Moreover, even conservatively assuming only a 50% breach rate for SAMI 2006-AR7, the potential litigation recovery would be approximately $500 million, which would be almost *seven times* the total settlement consideration for the trust ($76,603,299). *See* App. A.5

[20] *Id.*, Ex. R.

Report at 5, in which the transaction agreements at issue did not contain any similar "accrual" language. Indeed, based on the First Department's ruling in *ACE v. DB Securities* that a notice and cure provision in an RMBS pooling and servicing agreement is a substantive condition precedent to suit, 977 N.Y.S.2d at 231, the Accrual Provision in the MLPAs renders the repurchase claims timely under New York law. *See John J. Kassner & Co. v. City of N.Y.*, 46 N.Y.2d 544 (1979) ("as a general rule, when the right to final payment is subject to a condition, the obligation to pay arises and the cause of action accrues, only when the condition has been fulfilled"); *Frigi-Griffin, Inc. v. Leeds*, 383 N.Y.S.2d 339 (1st Dep't 1976) ("when a demand is of a substantive nature . . . the statute runs only after a demand has been refused."); *see also Continental Cas. Co. v. Stronghold Ins. Co., Ltd.*, 77 F.3d 16, 21 (2d Cir. 1996) (same).[21]

Nor did the Trustees or their experts consider other grounds available to the trusts for asserting timely claims against JP Morgan, such as that JP Morgan as Servicer failed to notify deal participants about breaches, as it is contractually obligated to do. *See, e.g., Home Equity Mortg. Trust Series 2006-5 v. DLJ Mortgage Capital, Inc.*, 653787/2012, 2013 N.Y. Misc. LEXIS 4274 (N.Y. Sup. Ct. Sept. 23, 2013).

However, the Court need not resolve in this action when the repurchase claims accrue in light of the Accrual Provision or whether there are other means to assert timely claims. As Justice Kapnick held in the Article 77 proceeding for the BNY Mellon/Countrywide settlement, it is an abuse of discretion for a trustee to settle a claim without sufficient evaluation or expert input. *See Matter of Bank of N.Y. Mellon*, 42 Misc. 3d 1237(A), 2014 N.Y. Misc. LEXIS 1125,

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[21] No New York court has yet construed the Accrual Provision. However, two federal district courts have held repurchase claims to be untimely notwithstanding an Accrual Provision. *Lehman XS Trust, Series 2006-4N ex. rel. U.S. Bank Nat'l Ass'n v. GreenPoint Mortg. Funding*, 991 F. Supp. 2d 472 (S.D.N.Y. 2013); *Deutsche Bank Nat'l Trust Co. v. Quicken Loans Inc.*, 2014 WL 3819356 (S.D.N.Y. Aug. 4, 2014). Those rulings are on appeal to the Second Circuit, and Ambac respectfully submits they were incorrect. Notably, in those actions U.S. Bank and Deutsche Bank – *two of the Petitioners in this action* – have argued that repurchase claims are timely under New York law where the governing contracts have Accrual Provisions. Petitioners can hardly be heard to argue the contrary in this action.

*57-64 (Sup. Ct. Jan 31, 2014). Here, the Trustees have offered no evidence that they even considered these issues, and their failure to do so is dispositive. *Id.*

II. ACCEPTING THE SETTLEMENT FOR THE AMBAC INSURED TRUSTS IS INCONSISTENT WITH THE TRUSTEES' PRUDENT PERSON OBLIGATION

Despite finding that the expected recovery from litigating exceeds the value of the Proposed Settlement for numerous trusts, Professor Fischel nevertheless recommended accepting the Proposed Settlement unless holders of certificates with at least 15% of the Certificates have "expressed opposition" to the Proposed Settlement.[22] The basis for this additional criterion appears to be an assumption that a Trustee is not required to take any action to bring claims on behalf of investors unless holders of 25% of the Certificates direct the Trustee to do so and agree to indemnify the Trustee.[23]

Professor Fischel's assumption ignores the fact that the Trustees are entitled to fund any investigation or litigation of claims for breach of the governing agreements out of the cashflows of the trusts and, in the event such cash flows are insufficient, may recover the balance from the Depositors (which are JPMorgan entities).[24] Thus, the absence of a 25% Certficateholder does not make it "reasonable" for the Trustees to accept the Proposed Settlement if it is a bad deal for investors or insurers like Ambac. Moreover, a Trustee is *required* to take action, and "use the same degree of care and skill in their exercise, as a prudent person would exercise under the circumstances in the conduct of his own affairs" in doing so, under the terms of the governing documents and the federal Trust Indenture Act (the "TIA") where, as here, Events of Default (or, under the TIA, "defaults") have occurred under the terms of the governing documents.[25]

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[22] Fischel Report ¶ 96.
[23] *See id.* ¶¶ 19, 139.
[24] *See* Ex. 2, § 9.05.
[25] *See* Ex. 2, § 9.01(a); *see also* 15 U.S.C. § 77ooo(c).

An Event of Default occurs where, among other things, "the Servicer fails to observe or perform in any material respect any other material covenants and agreements set forth in this Agreement [that] materially affect the rights of Certificateholders."[26] Among other obligations, PSAs require the Servicers to notify the Trustee and Depositor of breaches of representations and warranties.[27] Despite the large number of representation and warranty breaches acknowledged by Professor Fischel, the Servicers here (often affiliates of the Sponsors and Depositors) have systematically failed to give notice of the breaches. The Servicers are also required to service the loans "in accordance with Accepted Servicing Practices [defined as procedures "employed by prudent mortgage servicers" and "in compliance with "all federal, state, and local laws"].[28] Among other things, EMC's practice of entering into bulk settlements of repurchase claims while leaving the defective loans in the trusts clearly violates "prudent" loan servicing.

A significant number of the of the investors that have intervened as Co-Petitioners in the action (including BlackRock, PIMCO, AEGEON, and Prudential Insurance Company) have filed actions against each of the Trustees on behalf of investors in hundreds of RMBS trusts alleging that the Trustees violated their prudent person obligations under the TIA and the governing trust documents by failing to enforce investors' rights with respect to misconduct by RMBS sponsors and servicers (the "BlackRock Actions").[29] The BlackRock Actions allege industry-wide misconduct constituting Events of Default by all major servicers that was known to all Trustees.

[26] *Id.*, §8.01(ii). Although the PSAs also include a notice requirement for triggering an Event of Default, a Trustee cannot avoid the triggering of its prudent person obligation by failing to give notice of a known breach. *See, e.g., Okla. Police Pension & Ret. Sys. v. United States Bank Nat'l Ass'n*, 291 F.R.D. 47, 57 (S.D.N.Y. 2013).
[27] *See* Ex. 1, § 2.03.
[28] *See id.*, § 3.01 and p. 2 (definition of "Accepted Servicing Practices").
[29] *See, e.g.*, Ex. 3 (BlackRock, et al., complaint against BNY Mellon), Ex. 4 (BlackRock, et al., complaint against Wells Fargo). Numerous courts have sustained similar claims against RMBS trustees alleging breaches of their prudent person obligation under the TIA and/or governing trust documents. *See, e.g., Okla. Police Pension & Ret. Sys. v. United States Bank Nat'l Ass'n*, 291 F.R.D. 47 (S.D.N.Y. 2013); *Policemen's Annuity & Benefit Fund of Chi. v. Bank of Am., NA*, 907 F. Supp. 2d 536, 554 (S.D.N.Y. 2013); *Ret. Bd. of the Policemen's Annuity & Benefit Fund v. Bank..*, 914 F. Supp. 2d 422 (S.D.N.Y. 2011); *VNB Reality, Inc. v. U.S. Bank, N.A.*, Civ. No. 2:13-04743 (D.N.J. 2013); *Commerce Bank v. U.S. Bank, N.A.*, Case No. 4:13-cv-00517 (D. Mo. 2013).

Although the BlackRock Actions do not expressly cover the Settling Trusts at issue here, the industry-wide misconduct alleged therein implicates all RMBS trusts, including the Settling Trusts. Thus, Co-Petitioners cannot reasonably dispute the existence of Events of Default for the Accepting Trusts that long pre-dated the Proposed Settlement.

Professor Fischel's recommendations (and, presumably, the Trustees' decisions) are based in significant part on the assumption that no Events of Default have occurred. Therefore, Ambac respectfully submits that the Court cannot determine whether the Trustees have complied with their contractual and statutory duties in accepting the Proposed Settlement (particularly for trusts where the expected value of litigation clearly exceeds the value of the Proposed Settlement) without making a determination as to whether Events of Default exist that trigger the Trustees' prudent person obligation.

Dated: New York, New York
November 3, 2014

WOLLMUTH MAHER & DEUTSCH LLP

By: ______________________________
David H. Wollmuth
Michael C. Ledley
Steven F. Fitzgerald
Ryan A. Kane

500 Fifth Avenue
New York, New York 10110
Tel: (212) 382-3300

Attorneys for Ambac Assurance Company and The Segregated Account of Ambac Assurance Corporation

APPENDIX A

Trust	Breach Rate*	Total Losses**	Potential Litigation Recovery	Total Settlement Value**
BSMF 2006-AR2	85%	$486,603,607	$413,613,065.95	$ 36,755,346
BSMF 2006-AR4	75%	$224,635,789	$168,476,841.75	$ 16,933,329
GPMF 2005-AR5	89%	$336,884,987	$299,827,638.43	$ 25,446,429
GPMF 2006-AR2	89%	$342,855,008	$305,140,957.12	$ 25,897,372
GPMF 2006-AR3	90%	$628,176,647	$565,358,982.30	$ 47,448,991
SAMI 2006-AR7	[50%]***	$1,014,150,193	[$507,075,096.50]	$ 76,603,299
SAMI 2006-AR8	61%	$623,670,604	$380,439,068.44	$ 47,108,629

* Results of Ambac's forensic re-underwriting
** *See* Fischel Report, Exs. Q1-Q4
*** Estimated for illustrative purposes