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), AEGON USA Investment Management, LLC (intervenor), Bayerische Landesbank (intervenor), BlackRock Financial Management, Inc. (intervenor), Cascade Investment, LLC (intervenor), the Federal Home Loan Bank of Atlanta (intervenor), the Federal Home Loan Mortgage Corporation (Freddie Mac) (intervenor), the Federal National Mortgage Association (Fannie Mae) (intervenor), Goldman Sachs Asset Management L.P. (intervenor), Voya Investment Management LLC (f/k/a ING Investment LLC) (intervenor), Invesco Advisers, Inc. (intervenor), Kore Advisors, L.P. (intervenor), Landesbank Baden-Wurttemberg (intervenor), Metropolitan Life Insurance Company (intervenor), Pacific Investment Management Company LLC (intervenor), Sealink Funding Limited (intervenor), Teachers Insurance and Annuity Association of America (intervenor), The Prudential Insurance Company of America (intervenor), the TCW Group, Inc. (intervenor), Thrivent Financial for Lutherans (intervenor), and Western Asset Management Company (intervenor),

Petitioners,

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

Index No. 652382/2014

Part 60

Motion Sequence No. 24

Hon. Marcy S. Friedman

THE QVT FUNDS' REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF THEIR MOTION FOR PARTIAL SUMMARY JUDGMENT

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The QVT Funds respectfully submit this Reply Memorandum of Law, together with the Reply Affirmation of Michael C. Ledley, dated October 14, 2015, in further support of their motion for partial summary judgment.[1]

PRELIMINARY STATEMENT

The QVT Funds are entitled to partial summary judgment rejecting the Proposed Settlement for JPMAC 2006-WMC1 for two reasons. First, U.S. Bank was required to follow the QVT Funds' direction to reject the Proposed Settlement. Second, in the alternative, U.S. Bank abused its discretion by accepting the Proposed Settlement for JPMAC 2006-WMC1 without even investigating or considering the fairness of the Haircut, which is a unique and deeply inequitable component of the Proposed Settlement.

The settlement proponents' argument that U.S. Bank had discretion to ignore the QVT Funds' direction contradicts the plain language of the PSA. U.S. Bank's claim that the direction was invalid because U.S. Bank never received an "offer" of indemnity also fails because the QVT Funds offered to provide a "reasonable indemnity" and U.S. Bank's conduct frustrated the QVT Funds' efforts to negotiate final indemnity terms. U.S. Bank cannot rely on the non-occurrence of a condition that it prevented from occurring.

Alternatively, if U.S. Bank had the power to settle in the face of the QVT Funds' direction, it abused its discretion because U.S. Bank never considered or evaluated the fairness of the Haircut. U.S. Bank also relied on an expert analysis that it knew was based on false or unsupported assumptions. In particular, U.S. Bank's experts did not consider that claims against JPMorgan Chase Bank, N.A., as Servicer, may be timely even though that argument was being advanced on U.S. Bank's own behalf while U.S. Bank evaluated the Proposed Settlement.

[1] Capitalized terms not defined herein have the meanings set forth in The QVT Funds' Memorandum Of Law In Support Of Their Motion For Partial Summary Judgment ("Mov. Br.").

ARGUMENT

I. U.S. BANK WAS REQUIRED TO ACCEPT THE QVT FUNDS' DIRECTION

A. Certificateholders With Requisite Holdings Have The Power To Compel An RMBS Trustee To Reject A Settlement

The PSA provides that the Certificateholders are the beneficial owners of the mortgage loans in the Trust and all claims relating thereto and empowers U.S. Bank, as Trustee, to assert claims "on behalf of the Certificateholders." *See* PSA § 2.01(a) ("The Depositor . . . does hereby . . . convey to the Trustee without recourse ***for the benefit of the Certificateholders*** all the right, title and interest of the Depositor . . . in and to the Mortgage Loans"), § 2.02 ("the Trustee . . . holds or will hold all such assets . . . in trust ***for the exclusive use and benefit of all present and future Certificateholders***"), § 8.02(b) ("any . . . suit, action or proceeding instituted by the Trustee shall be brought in its name ***for the benefit of all the Holders of such Certificates***") (in each case, emphasis added); *see also id.* § 2.03(a)(ii) (stating that repurchase protocol is the sole remedy of "the Trustee on behalf of the Certificateholders").

Because the Certificateholders are the real party in interest with respect to claims arising under the PSA, Section 8.02(a)(iii) unambiguously provides that U.S. Bank is obligated to follow a proper direction from a Certificateholder "to institute, conduct or defend any litigation" of such claims. *Id.* § 8.02(a)(iii). Section 8.02(a)(iii) is conditional, and once the condition (*i.e.*, a direction and offer of reasonable indemnity) is satisfied, the Trustee is obligated to comply with the direction. Mov. Br. at 16-18. Blackletter trust law also recognizes a trustee's duty to act as directed under these circumstances. Mov. Br. at 16-17. None of the settlement proponents dispute this interpretation of Section 8.02(a)(iii) as a matter of basic contract law.

U.S. Bank, JPMorgan, and the Institutional Investors simply ignore the plain language of Section 8.02(a)(iii) and invent a discretionary power on the part of U.S. Bank to ignore a proper

Certificateholder direction.[2] The settlement proponents, however, cite no authority and identify no PSA provision that provides U.S. Bank with such a discretionary power. Instead, the settlement proponents rely on the purported "inherent" power of a trustee to settle claims as well as certain other PSA provisions that do not address the issue at all. All of these arguments run smack into bedrock principles of trust law or well-settled canons of contract interpretation.

First, whatever "inherent" power U.S. Bank may have to settle claims is constrained by the express provisions of the PSA. *See In re IBJ Schroder Bank & Trust Co.*, 706 N.Y.S.2d 114 (1st Dep't 2000) ("the duties and powers of a trustee are defined by the terms of the trust agreement"); *see also* Restatement (Third) of Trusts § 85. The settlement proponents cite no authority to the contrary.

Second, the notion that U.S. Bank has discretion to ignore a proper Certificateholder if it sees fit would write Section 8.02(a)(iii) out of the PSA. One could delete the provision entirely and U.S. Bank still would have discretion to follow a Certificateholder direction, would be exculpated for actions pursuant to that direction, and could insist on an indemnity pursuant to other PSA provisions. *See* PSA § 8.02(a)(iv), § 8.01(iii) (exculpation for actions pursuant to Certificateholder direction), § 8.02(a)(v) (right to demand reasonable indemnity). Therefore, under the settlement proponents' theory, Section 8.02(a)(iii) would serve no purpose at all. A

[2] U.S. Bank says a trustee may "decline to follow a direction and indemnity so long as the trustee does so in good faith and is not negligent." U.S. Bank's Opposition To QVT Funds' Motion For Partial Summary Judgment ("U.S. Bank Br.") at 14-15. JPMorgan says a Certificateholder's power to direct a trustee does not "negate[] the actual language of the PSA that vests any repurchase claims, and the related powers to litigate and to settle, in the Trustee for the benefit of the WMC 1 Trust" (although it never cites any "actual language of the PSA"). JPMorgan's Response To The QVT Funds' Motion For Partial Summary Judgment ("JPM Br.") at 1. The Institutional Investors dispute that a 25% Certificateholder "had the power to divest U.S. Bank of the authority to enter into the Settlement." The Institutional Investors' Opposition to the QVT Funds' Motion for Partial Summary Judgment ("II Br.") at 3.

court may not construe a contract so as to render its provisions meaningless. *See, e.g., Beal Sav. Bank v. Sommer*, 8 N.Y.3d 318, 225 (2007).

Third, the various PSA provisions that the settlement proponents cite do not alter the plain meaning of Section 8.02(a)(iii):

- Section 11.03 is the "no action clause." It authorizes litigation by a 25% Certificateholder when the Trustee fails to follow a proper direction to commence litigation or is otherwise conflicted from doing so. PSA § 11.03. The language quoted by U.S. Bank (U.S. Bank. Br. at 14) prevents a Certificateholder, when litigating in lieu of the Trustee, to agree to a settlement of claims on behalf of all Certificateholders in which it obtains a disproportionate benefit to which it is not entitled under the PSA.[3] It does not prevent a Certificateholder from giving any direction that impacts other Certificateholders. ***Every*** direction to litigate (or to settle) impacts other Certificateholders. If a Certificateholder were prohibited from giving any such direction, once again Section 8.02(a)(iii) would be meaningless. The point of the provision is that a 25% Certificateholder's interests are aligned with other Certificateholders so that it can represent their interests when the Trustee will not. Section 11.03 also reinforces the mandatory nature of Section 8.02(a)(iii) by empowering a 25% Certificateholder to act directly rather than having to sue the Trustee for specific performance for its failure to follow the direction. Section 11.03 and Section 8.02(a)(iii) work hand in glove to make sure the views of the 25% Certificateholder with respect to litigation prevail over the views of the Trustee if there is a conflict.

- Section 8.01(iii) provides that a Trustee shall not be "personally liable" for actions or inactions taken in good faith "***in accordance with the Agreement***" or "***with the consent or at the direction***" of Certificateholders. PSA § 8.01(iii) (emphasis added). The Trustee still must follow the contract. Section 8.01(iii) cannot be read to relieve U.S. Bank of its obligation to follow a Certificateholder direction because it only excuses actions taken "in accordance with" the PSA. Ignoring a proper Certificateholder direction would ***not*** be "in accordance with the Agreement" because it would violate Section 8.02(a)(iii).

[3] Ironically, it appears that the Institutional Investors have negotiated a settlement on behalf of all Certificateholders that provided them with a disproportionate benefit at the expense of other investors. The Institutional Investors negotiated and agreed to the Haircut, pursuant to which investors in the Haircut Trusts receive massively less as a percentage of losses than other Settlement Trusts. [redacted] and therefore the Haircut takes money out of the pocket of investors in the Haircut Trusts (like the QVT Funds) and puts it into the pocket of the Institutional Investors and other investors in the non-Haircut Trusts.

Even if there were an arguable conflict between Section 8.02(a)(iii) and these other provisions – and there is no conflict – the more specific provision must prevail over more general provisions. *See, e.g.*, *Muzak Corp. v. Hotel Taft Corp.*, 1 N.Y.2d 42, 46-47 (1956). Section 8.02(a)(iii) specifically requires U.S. Bank to follow a proper Certificateholder direction in connection with the conduct or defense (or settlement) of litigation. It must therefore prevail over other, more general provisions of the PSA.

Finally, the settlement proponents' argument also ignores the clear intent of Section 8.02(a)(iii) – to provide Certificateholders with large holdings the ability to ensure their rights, and the rights of the other Certificateholders, are properly enforced. Here, it is *Certificateholders'* rights that have been violated by JPMorgan's misconduct and *Certificateholders'* interests that are being compromised for fractions of pennies on the dollar. The suggestion that Certificateholders have no right to protect their interests and direct the Trustee ignores economic reality, the terms of the PSA, and good sense.

In the aftermath of the mortgage crisis, there has been a widespread failure of RMBS Trustees to protect the Certificateholders' rights, as evidenced by the flood of recent actions filed against RMBS Trustees (including several massive actions filed by Blackrock, PIMCO, and other prominent members of the Institutional Investor group). Unless and until RMBS Trustees begin acting as faithful stewards of the Certificateholders' interests, it is essential for the proper functioning of RMBS Trusts and the RMBS market that the law clearly recognize and enforce the principle that the Certificateholders – when they hold the requisite percentage of securities and offer a reasonable indemnity – control the litigation and settlement of claims.

B. U.S. Bank Prevented An Agreement On Indemnity Terms

The QVT Funds clearly held over 25% of the Certificates in JPMAC 2006-WMC1, repeatedly expressed strong objections to the Proposed Settlement (in general) and to the Haircut (in particular), provided express direction to U.S. Bank to reject the Proposed Settlement on behalf of JPMAC 2006-WMC1, and communicated its willingness to provide U.S. Bank with a reasonable indemnity. Facts ¶¶ 28-34, 40, 44. It is also true that the QVT Funds and U.S. Bank never reached an agreement on the terms of the indemnity before U.S. Bank purported to accept the Proposed Settlement. On that basis, U.S. Bank argues that the QVT Funds did not formally "offer" a satisfactory indemnity, and that U.S. Bank had no duty to follow the QVT Funds' direction. This argument ignores that U.S. Bank's conduct prevented the parties from agreeing to indemnity terms, or even engaging in meaningful negotiations, before the August 1, 2014 deadline imposed by JPMorgan for acceptance or rejection of the Proposed Settlement.

U.S. Bank does not contest the legal principle that a party cannot avoid a duty based on the non-occurrence of a necessary condition when the party prevented the satisfaction of that condition. Mov. Br. at 18-19. Instead, U.S. Bank casts the blame on the QVT Funds and contends the QVT Funds are "distorting the record." U.S. Bank Br. at 19. However, the undisputed record shows that U.S. Bank deliberately sought to obstruct the QVT Funds' right to give a direction or, at best, showed no interest in the QVT Funds' concerns and was negligent in its dealings with the QVT Funds.

In particular, the stipulated facts here demonstrate the following:

(i) U.S. Bank completely ignored the QVT Funds' initial letter objecting to the Proposed Settlement because of the Haircut, among other reasons (Facts ¶ 33);

(ii) U.S. Bank invited Certificateholders to request the form of indemnity terms that U.S. Bank would require for a Certificateholder direction and then inexplicably withheld the form of indemnity from the QVT Funds for

over two months, until only three weeks remained before the August 1, 2014 deadline (Facts ¶ 43);

(iii) after the QVT Funds immediately rejected U.S. Bank's indemnity terms and offered to negotiate a "reasonable indemnity," U.S. Bank asked the QVT Funds to ***defer negotiation*** over the indemnity terms until after the Trustees' expert reports were made public (Facts ¶ 45);

(iv) U.S. Bank failed to make the expert reports available to investors until ***nine days*** (seven business days) before the August 1, 2014 deadline (Facts ¶ 48);[4]

(v) U.S. Bank promised to email the QVT Funds when the expert reports were made public but then never sent the promised email (Facts ¶¶ 46, 48);

(vi) when the QVT Funds discovered the expert reports and attempted to engage U.S. Bank again by letter, U.S. Bank ignored that letter until 11:07 p.m. on the eve of the August 1, 2014 deadline (Facts ¶ 63); and

(vii) U.S. Bank never informed the QVT Funds that it was in negotiations with JPMorgan to extend the August 1, 2014 deadline for certain trusts nor took action to extend the deadline for JPMAC 2006-WMC1 so the parties could engage in the negotiations that U.S. Bank had postponed pending publication of the expert reports (Facts ¶ 66).

Whether one concludes from this embarrassing series of events that U.S. Bank was intentionally stalling and running out the clock on the QVT Funds or that it just grossly mismanaged the process is irrelevant. Either way, the QVT Funds' right to direct U.S. Bank should not be prejudiced by U.S. Bank's intentional misconduct or negligence. *See* Mov. Br. at 18-19.

U.S. Bank argues that the QVT Funds could have marked up U.S. Bank's indemnity form or proposed their own form, but that ignores the fact that U.S. Bank said it would negotiate the

[4] There is no reasonable justification for the Trustees' failure to make the expert reports available on a timely basis or to engage in negotiations over indemnity terms. The Trustees had known about the Proposed Settlement since November 2013 (and knew it was being negotiated for long before that). And they repeatedly refused to engage with investors and urged them to wait until the expert reports were published. By dragging their feet until July 22, 2014, the Trustees forced objecting investors to squeeze into seven business days the discussions and negotiations that reasonably required a far longer period of time.

indemnity terms after the expert reports were published. Then, U.S. Bank's failure to notify the QVT Funds by email of the publication of the expert reports as promised cost the QVT Funds another few days. U.S. Bank used up the remaining two days before the August 1, 2014 deadline by sitting on the QVT Funds' July 29 letter and announcing at 11:07 p.m. on the eve of the deadline that it was rejecting the QVT Funds' direction. At that point any further action by the QVT Funds obviously would have been futile.[5]

In any event, the question is not whether, in hindsight, there was some action that the QVT Funds could have taken to overcome U.S. Bank's obstruction. The QVT Funds made clear their intent to give a direction and to negotiate a reasonable indemnity. At the very least, U.S. Bank, as a trustee and contract counterparty, had a duty of good faith and fair dealing to facilitate the QVT Funds' efforts to provide an indemnity and not to frustrate them. The undisputed facts make clear that U.S. Bank's actions frustrated and hindered the QVT Funds' efforts. Therefore, the absence of a formal agreement or binding offer on indemnity terms does not relieve U.S. Bank of its obligation to comply with the QVT Funds' direction. *See In re Bankers Trust Co.*, 450 F.3d 121, 128 n.4 (2d Cir. 2006) ("If the promisor is under a duty to the promisee to do what it can to bring about the realization of the condition, the failure to do so, whether by active or passive steps, would seem to breach that duty and waive the condition."); Restatement (Second)

[5] U.S. Bank argues that there is an issue of fact as to whether the form of indemnity it initially demanded was reasonable. That issue might be material if the parties engaged in negotiations and could not reach agreement. However, U.S. Bank's conduct prevented those negotiations from taking place at all. Whether its initial demand was reasonable is therefore irrelevant. [redacted]

of Contracts § 225 cmt. b (condition "may be excused by prevention or hindrance of its occurrence through a breach of the duty of good faith and fair dealing").

II. U.S. Bank Abused Its Discretion With Respect To JPMAC 2006-WMC1

Even if U.S. Bank had the power and discretion to settle in the face of the QVT Funds' direction, U.S. Bank abused that discretion. The settlement proponents' arguments for delay on this issue have no merit. The Trustees owe separate duties to investors in each trust. U.S. Bank and the other Trustees purported to make their decision with respect to the Proposed Settlement on a trust-by-trust (or, in some cases, loan group-by-loan group) basis. This Court will have to determine whether each Trustee properly exercised its discretion for each trust. Whether U.S. Bank's decision to accept the Proposed Settlement for JPMAC 2006-WMC1 was a proper exercise of its discretion is a discrete issue that, under the circumstances, need not wait for a full hearing on the other 300+ Settlement Trusts. Moreover, the CPLR encourages summary adjudication, to the extent possible, in special proceedings, and "[t]he court may make any orders permitted on a motion for summary judgment." CPLR § 409(b).

A. U.S. Bank Never Considered The Fairness Of The Haircut

U.S. Bank abused its discretion with respect to JPMAC 2006-WMC1 because it failed to undertake any investigation into the reasons for the Haircut and never considered or commissioned any expert advice concerning whether the Haircut was fair and reasonable to JPMAC 2006-WMC1 or the other Haircut Trusts. U.S. Bank relies on Professor Fischel's conclusion that U.S. Bank should accept the Proposed Settlement for JPMAC 2006-WMC1. U.S. Bank Br. at 22-23. This is insufficient. As discussed below, Mr. Fischel's recommendation boils down to the conclusion that something is better than nothing. However, the issue is not merely whether, in a vacuum, it would be reasonable for U.S. Bank to accept 0.8 cents on the dollar for JPMAC 2006-WMC1. The issue is whether it is fair and reasonable to reduce the amount of compensation JPMAC 2006-WMC1 otherwise would have received merely because of the identity of the loan originators. Neither Mr. Fischel nor any other expert has offered an opinion on that, and U.S. Bank never even considered it. A further issue is whether it is fair and reasonable, once JPMorgan put $4.5 billion on the table, to allocate that $4.5 billion in a way that benefitted some trusts and investors disproportionately at the expense of other similarly situated trusts and investors. No consideration was given to that issue either.

Notably, both the Countrywide Settlement at issue in the Article 77 proceeding before Justice Kapnick and the Citigroup Settlement at issue in the other Article 77 proceeding before this Court provided for allocation of the settlement compensation on a *pro rata* basis determined by the amount of losses for each trust. *See* Ledley Reply Aff. Ex. 1 § 3(c) (Countrywide Agreement); *id.* Ex. 2 § 5.04 (Citigroup Agreement). Neither of those settlements arbitrarily reduces the compensation paid to certain trusts, as the Haircut does here.

Given the unique nature of the Haircut, it is striking that no one has stepped forward on this motion – or at any time during this proceeding – to explain and defend it on the merits. On its face, it is fundamentally unfair that investors in the Haircut Trusts receive 0.8 percent of their losses, when other similarly situated investors get nearly ten times more. The Court, sitting as a court of equity, should not give its imprimatur to such inequitable result without at least ***some*** justification. The parties offer none. U.S. Bank has not sufficiently informed itself to be able offer such a justification, in abuse of its discretion. And JPMorgan and the Institutional Investors are shielding their negotiations of the Haircut behind the mediation privilege, so that the Court has no ability to evaluate the issue for itself.

B. Professor Fischel's Recommendation For JPMAC 2006-WMC1 Relied On Unsupported Assumptions

U.S. Bank's reliance on Professor Fischel's recommendation was also an abuse of discretion because Professor Fischel relied on assumptions that U.S. Bank knew were unsupported. Notably, Professor Fischel concluded that the expected value of litigation likely ***exceeded*** the value of the Proposed Settlement for JPMAC 2006-WMC1. Professor Fischel nevertheless recommended acceptance because (i) he presumed that the percentage of investors in JPMAC 2006-WMC1 supporting the Proposed Settlement greatly outweighed the percentage opposing; and (ii) he assumed that all breach of representation-related claims were time barred.

With respect to point (i), Professor Fischel's presumption was incorrect because he did not consider the QVT Funds' holdings, and U.S. Bank was aware of that. *See* Mov. Br. at 22. That much is undisputed.[6] U.S. Bank knew that the actual relative weight of investors opposing the settlement was a factor that, under Professor Fischel's reasoning, actually favored rejection. Moreover, U.S. Bank made no effort to provide Professor Fischel with updated information regarding the Institutional Investors' holdings, [redacted] U.S. Bank is entitled to no deference when it relies on an expert that it knows was misinformed.

With respect to point (ii), Professor Fischel assumed that all released claims (other than servicing claims) with respect to JPMAC 2006-WMC1 were likely time barred, relying on the Justice Carpinello reports. However, there are strong grounds to conclude that claims against

[6] The QVT Funds did not authorize U.S. Bank to disclose their identity to the experts. However, as discussed in the Wollman Affidavit, U.S. Bank's explanation for the request was somewhat cryptic. U.S. Bank never said that its expert would weigh the relative holdings in deciding whether to accept or reject the settlement. Wollman Aff. ¶ 24. If U.S. Bank had made that clear, it would have been very much in the QVT Funds' interest to permit disclosure of their holdings to Professor Fischel and the other experts, and the QVT Funds would have done so. *See id.*

JPMorgan Chase Bank, N.A. ("JPMC Bank"), as Servicer, for failure to give notice of misrepresentations during the administration of the trust are independent of the claims against the JPMorgan seller and depositor entities for breach of representation or breach of the duty to repurchase, and therefore remain timely. U.S. Bank knew of these grounds because, at the same time U.S. Bank was considering the Proposed Settlement, the Securities Administrator for JPMAC 2006-WMC2 was suing JPMC Bank, as Servicer, ***on U.S. Bank's behalf*** and articulating the same arguments in that action (the "WMC2 Litigation"). Ledley Reply Aff. Exs. 3-4.

Justice Carpinello concluded that failure-to-notify claims accrued at the same time as breach of representation claims, but his conclusion appears to be limited to claims against the depositors or sellers who breached the representations in the first place:

> The rule that the six year Statute of Limitations for claims relating to violations of representations and warranties accrues on the date of closing applies regardless of how these claims are denominated; that is regardless of whether they are characterized as a breach of the representations and warranties themselves, or a breach of an obligation to give notice of the breach, or a breach of an obligation to enforce claims for the violations against others, or breach of an obligation to cure the breach or repurchase the loan, or claims for incomplete documentation for the loans, because all such varied denominations for these claims were actionable as of the date of closing of the respective Trusts.

Carpinello Rep. at 7. Justice Carpinello's report does not separately address whether failure to notify claims against ***a Servicer*** accrued at a later time (*e.g.*, when the Servicer discovered the breach) and therefore would still be timely. It appears that Justice Carpinello was not asked to consider that issue. U.S. Bank could not, in good faith, rely on Justice Carpinello's report regarding the availability of claims against JPMC Bank, as Servicer, when that report does not address that issue, of which U.S. Bank was clearly aware. Similarly, U.S. Bank could not, in good faith, rely on Proessor Fischel's recommendation that attributed zero value to the failure to notify claim against JPMC Bank, as Servicer, when the identical claim was being advanced, on U.S. Bank's behalf, in the WMC2 Litigation at exactly the same time.

JPMorgan cites the recent decision of the court in the WMC2 Litigation, which held that the failure to notify claim against JPMC Bank, as Servicer, was "not an independent cause of action" but rather just part of the repurchase protocol. *BNY Mellon v. J.P. WMC Mortgage, LLC*, Index. No. 653831/2013, 2015 N.Y. Misc. LEXIS 3381 (N.Y. Sup. Ct. Sept. 18, 2015) (the "WMC2 Decision"). As the Institutional Investors have repeatedly argued, the issue before the Court is whether U.S. Bank acted reasonably and in good faith based on its knowledge at the time, not in hindsight. Here, U.S. Bank allowed both of its experts to render opinions without even considering the claims and arguments its agent in the WMC2 Litigation was asserting on its behalf. That is neither good faith nor reasonable.

In any event, the QVT Funds respectfully submit that on this point the WMC2 Decision was in error. The court failed to consider the distinction between JPMC Bank, as Servicer, and the separate JPMorgan entities (J.P. Morgan Acceptance Corporation I ("JPMAC I") and J.P. Morgan Mortgage Acquisition Corp. ("JPMMAC"), respectively) that serve as Depositor and Seller. In particular, the Seller in these securitizations made representations and warranties at closing and guaranteed the representations by the mortgage originator (WMC). While it may make sense to conclude that failure to notify claims against the Seller (the responsible repurchase counterparty) and the Depositor (who owned the loans prior to the closing assigns them to the trust via the PSA) are not "independent" of repurchase claims, claims against the Servicer are another matter altogether. JPMC Bank was not appointed servicer until the closing and would not have access to the loans for some time after. Accordingly, it could have discovered the breaches of representation.

More fundamentally, JPMC Bank is a separate corporate entity from the JPMorgan parties making the representations and assuming the repurchase obligations. As Servicer, it also plays a separate and independent role in the securitization in that it administers the loans on a daily basis after the closing. In the ordinary situation the PSA was intended to address (*i.e.*, where there were not massive, systematic breaches of representations by mortgage originators and sellers), the Servicer is the only party likely to discover a breach of representation post-closing. The Servicer's duty to notify therefore plays an essential role in the "checks and balances" built into the PSA post-closing. As Justice Kornreich recognized back in 2013, "[t]his type of 'failure to notify' upends the framework of the MLSA and PSA." *BNY Mellon v. WMC Mortgage LLC,* Index No. 654464/2012, 41 Misc. 3d 1230(A), 981 N.Y.S.2d 633, at *4 n.7 (N.Y. Sup. Ct. Nov. 21, 2013) (the "WMC4 Decision"). Because the Servicer's duty to notify is a pre-requisite for the repurchase protocol, the Servicer's breach of that duty ***must*** be separately actionable.

The Court of Appeals decision in *ACE v. DB* does not change this analysis. In fact, *ACE* expressly distinguishes between "promises of future performance" and remedies for a breach that occurs at closing, and the Servicer's duty to notify is clearly a promise of future performance. *See ACE Secs. Corp. v. DB Structured Prods., Inc.*, 25 N.Y.3d 581 (2015) (distinguishing *Bulova Watch Co. v. Celotex Corp.*, 46 N.Y.2d 606 (1979)).

The court in the WMC2 Litigation also erroneously relied on decisions by this Court that held that failure to notify claims against ***loan sellers*** were not independent of the breach of representation claims against those loan sellers. *See* WMC2 Decision at 8-9 (citing cases). None of the authorities cited in the WMC2 Decision held that claims against mortgage servicers for failure to give notice of misrepresentations after closing of the securitization accrued at the time of the closing. Nor is the reasoning of this Court in the cited decisions extendable to claims against the Servicer.

Ultimately, whether the failure to notify claim against JPMC Bank, as Servicer, is independent of the breach of representation claim against JPMAC, as Seller, is at least colorable. U.S. Bank admitted as much when it allowed its Securities Administrator to advance the claim in the WMC2 Litigation. The Appellate Division (and perhaps the Court of Appeals) likely will resolve the issue definitely in the WMC2 Litigation and the QVT Funds respectfully submit that the failure to notify claim against the Servicer will be deemed timely. Nevertheless, in order to justify rejection of the settlement for JPMAC 2006-WMC1, the claim against JPMC Bank, as Servicer, need not be 100% certain. Even if the likelihood of success were low, it is considerably greater than 0.8% (the percentage of losses paid to JPMAC 2006-WMC1). Therefore, the expected value of the claim against JPMC Bank, as Servicer for JPMAC 2006-WMC1 – *i.e.*, the value of damages times the probability of recovery – is worth much more than the recovery under the Proposed Settlement even today.[7]

CONCLUSION

For the reasons set forth herein and in the QVT Funds' opening memorandum, the QVT Funds respectfully request that the Court grant their Motion for Partial Summary Judgment and reject the Proposed Settlement with respect to JPMAC 2006-WMC1.

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[7] JPMorgan makes certain arguments regarding the repurchase liability of JPMMAC, as Seller. It is not necessary to address those arguments in detail here, but suffice it to say JPMorgan is wrong. The scope of JPMMAC's warranty as Seller was "tantamount to WMC's." *See* WMC4 Decision at *3. Moreover, as to JPMMAC's guaranty, there is no need to exhaust remedies against WMC before proceeding against JPMMAC. The caselaw and the Trustees' expert agree. *Id.*; Schwartz Rep. at 4 (*citing Chem. Bank v. Bruce G. Metzger*, 93 N.Y.2d 296, 302-03 (1999)) ("[u]nder basic guarantee law, the beneficiary can sue the guarantor when the primary obligor does not perform; the beneficiary need not make a formal demand on that obligor").

Dated: New York, New York
October 14, 2015

WOLLMUTH MAHER & DEUTSCH LLP

By: *\/s Michael C. Ledley*
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