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

MEMORANDUM OF LAW IN SUPPORT OF ORDER TO SHOW CAUSE WHY THE FEDERAL HOME LOAN BANK OF BOSTON SHOULD NOT BE ENTITLED TO INTERVENE

Pursuant to the Court's October 9, 2014 Order (Doc. No. 68, ¶ 17), proposed-intervenor the Federal Home Loan Bank of Boston ("FHLB Boston" or the "Bank") submits this memorandum of law in support of its Order to Show Cause Why the Federal Home Loan Bank of Boston Should Not Be Allowed to Intervene pursuant to CPLR 401, 1012, 1013, and 7701.

I. INTRODUCTION

FHLB Boston is a government-sponsored cooperative with a mission to provide wholesale funding to its members in support of housing finance and community and economic development. It principally achieves this mission by making loans to banks, thrift institutions, insurance companies, and credit unions within its district, and by making grants to support affordable housing projects. To help generate the income that supports this mission, the Bank invests in conservative, investment-quality debt issuances.

Petitioners 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 U.S.A., N.A., and Deutsche Bank National Trust Company (collectively, the "Trustees") filed this Article 77 proceeding to seek judicial approval of a proposed $4.5 billion settlement ("JP Morgan Settlement") to resolve the claims of 312 trusts (referred to by the Trustees as the "Accepting Trusts"). Each of the Trustees is a trustee, indenture trustee, successor trustee, and/or separate trustee for residential mortgage loan securitization trusts established and sponsored by JPMorgan Chase & Co. or its affiliates ("JPMorgan"). FHLB Boston owns securities issued by 38 of these trusts, for which it paid $1.8 billion. If approved, the proposed settlement would extinguish certain loan-repurchase and servicing claims that those 38 trusts have against JPMorgan, as well as any claims against the Trustees pertaining to its acceptance of the terms of the JP Morgan Settlement.

Given FHLB Boston's substantial holdings in the 38 trusts, and the material effect that the JPMorgan Settlement may have on the value of those investments, the Bank must carefully evaluate whether the proposed settlement is in the Bank's best interests. However, FHLB Boston is not able to do so based on the information made available by the Trustees and the settlement proponents. Without additional information, FHLB Boston cannot determine, among other things, if the amount of the compensation for representation and warranty breaches and servicing violations, or the way in which the settlement proceeds will be allocated among the Accepting Trusts, is fair and reasonable to FHLB Boston, or whether the Trustees adequately investigated and evaluated the broad array of claims that will be extinguished by the settlement if it is approved. Nor can FHLB Boston determine if the Trustees sought to maximize recoveries for

particular Trusts that the Trustees' own analysis suggested may be better served through individual actions by the Trustees on behalf of the Trusts.

FHLB Boston therefore seeks an order pursuant to CPLR 401, 1012, and 1013 to intervene as a respondent in this proceeding in order to gather the information that it needs to evaluate the proposed settlement, to exercise "the right to examine the trustees, under oath . . . as to any matter relating to their administration of the trust" as provided by CPLR 7701, and generally to protect its interests in this proceeding.

II. BACKGROUND

A. The Proposed Settlement of Repurchase and Servicing Claims for 312 Accepting Trusts, with an Original Face Value of Over Two Hundred and Ninety-Five Billion Dollars

JPMorgan and its affiliates sold millions of mortgage loans to securitization trusts that JPMorgan sponsored. To raise money to pay for the loans, the trusts—established between 2005 and 2007—sold certificates, which are backed by those mortgage loans, to investors all over the world. In order to assure investors that the loans it was selling them were of good quality, JPMorgan made numerous representations and warranties about those loans in contracts known as Pooling and Servicing Agreements ("PSAs"), or in some instances, indentures or Sale and Servicing Agreements ("SSAs") (collectively, the "Governing Agreements"), under which the petitioners are trustees to the Accepting Trusts. For instance, JPMorgan promised that the loans would be serviced in accordance with the customary and usual standards of prudent servicing practices of mortgage loan servicers and consistent with the Governing Agreements. JPMorgan also represented that the loans would be underwritten in all material respects in accordance with certain underwriting guidelines; that the origination, underwriting, and collection practices of the sellers of the loans would be legal, prudent, and customary in the mortgage lending and servicing business; that the loans would conform in all material respects to their descriptions in the

investor disclosure documents; and that the loans would be originated in accordance with all applicable laws. JPMorgan committed to standing behind these representations and warranties by agreeing to repurchase from the trusts loans that did not comply with the representations and warranties.

In a notice dated August 1, 2014, the Trustees announced that they had accepted a proposed settlement agreement on behalf of the Accepting Trusts presented to them by JPMorgan and a group of twenty-one (21) institutional investors (the "Institutional Investors") to resolve claims related to the representation and warranties and servicing guarantees made by JPMorgan. Shortly after the Trustees made the announcement, they filed this Article 77 proceeding on August 3, 2014 to request judicial approval of the proposed settlement. Although the proposed settlement was negotiated by the Institutional Investors and JPMorgan, its effect is not limited to the interests of those investors. Instead, the proposed settlement would extinguish repurchase and servicing claims against JPMorgan for all certificateholders in all Accepting Trusts.

B. FHLB Boston Lacks Information To Fully and Effectively Evaluate the Fairness and Adequacy of the Proposed Settlement

It has been widely reported through, *inter alia*, publicly available information, settlements, and governmental investigations, that many of the loans that JPMorgan sold to the trusts did not comply with JP Morgan's representations and warranties. JPMorgan acknowledged this conduct in the Statement of Facts it provided in connection with its $13 billion settlement with the Department of Justice.[1] Consistent with its "acknowledgement," loan file reviews conducted by investors who have sued JPMorgan suggest extremely high rates of

[1] http://www.justice.gov/iso/opa/resources/943201311191510319906 22.pdf (last visited on October 13, 2014).

loans in JPMorgan issued mortgage-backed securities that did not comply with the originators' stated underwriting guidelines. For example, in a complaint brought by the Federal Finance Housing agency ("FHFA") against JPMorgan with regard to 103 JPMorgan private label mortgage-backed securities backed by loans in (among others) 57 of the Accepting Trusts, the FHFA's loan-file reunderwriting of certain trusts indicated a defect rate between 79% and 98%.[2] JP Morgan paid $4 billion to resolve the FHFA's securities claims, which represented a recovery of 91% of the lifetime losses on the securities. Likewise, JPMorgan's imprudent servicing practices have been the subject of extensive investigation and litigation, including the National Mortgage Settlement, in which JP Morgan agreed to pay over $1 billion, and to provide over $3.7 billion of borrower relief.[3]

In light of this information, whether $4.5 billion is a sufficient payment to resolve all of JPMorgan's liability for representation and warranty breaches and servicing abuses in 312 trusts is an important question that FHLB Boston cannot answer based on the information made public by the Trustees and the Institutional Investors. While the Trustees have made public various expert reports that were prepared after the settlement amount was determined, these reports raise many questions. For example, Dr. Faten Sabry (whose report is heavily redacted) concluded that JP Morgan's total representation and warranty repurchase liability ranged between $1.71 and $4.5 billion (suggesting that JP Morgan agreed to pay between 100% and 260% of its total repurchase liability).[4] Yet, there is ample reason to doubt that JP Morgan's total repurchase

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[2] *See* Amended Complaint, *FHFA v. JPMorgan Chase & Co., et al.*, No. 11-6188 (S.D.N.Y., June 13, 2012) (ECF No. 99) at ¶¶ 359-362.

[3] *See* Consent Judgment, *USA, et al., v. JP Morgan Chase & Co., et al.*, No. 12-361 (D.D.C., April 4, 2012) (ECF No. 10).

[4] Expert Report of Faten Sabry, PhD, National Economic Research Associates, Inc., July 17, 2014 ("Sabry Report").

liability for *1.25 million loans* in *312 Trusts*, with an original face value of *$295.4 billion* and estimated loss of at least *$60 billion*, is as low as Dr. Sabry estimates, particularly in light of the results of loan file reundewriting that has previously been done in other actions for some of the Accepting Trusts. By way of example, if the percentage of loans that failed to comply with stated underwriting guidelines is even a third of the 79-98% that the FHFA determined for some of the Trusts that also are included in this settlement, Dr. Sabry's estimate may be a massive understatement of JP Morgan's total liability.[5]

More questions are raised by the analysis prepared by Daniel Fischel and relied on by the Trustees to conclude that the settlement is fair to all of the Accepting Trusts.[6] Mr. Fischel estimates that the settlement will provide most trusts with approximately 7.6% of the total lifetime losses incurred by the Accepting Trusts – an amount that he recognizes is substantially lower than all but one other prior settlement he identifies in his report. Fischel Report at 21-34, 59. Recognizing that the settlement may not be in the best interests of all trusts subject to it, Mr. Fischel purports to perform a trust by trust analysis in order to identify those trusts that would be "harmed" by the settlement because there is a likelihood that they could achieve superior results by rejecting the settlement and pursuing separate actions against JP Morgan. He identifies three factors that he believes should dictate whether a deal is excluded from the settlement: (1) whether 15% or more of Certificateholders oppose the deal; (2) whether based on available information for the deal, including any loan file reunderwriting of loans in the trust, it appears that the recovery in a repurchase action would exceed the settlement recovery; and (3) whether

[5] Dr. Sabry does not mention the results of the FHFA's loan file re-underwriting in her report, and instead relies only on the LTV and occupancy rate review described in the FHFA's complaint. She does so despite the fact that the core basis of JP Morgan's repurchase liability is the extent to which loans backing the Accepting Trusts failed to satisfy stated underwriting guidelines.

[6] Expert Report of Daniel R. Fischel, Compass Lexecon, July 17, 2014 ("Fischel Report").

repurchase claims likely would be time-barred or where recovery on servicing claims would exceed the settlement recovery for the trust. *See* Fischel Report at 17-19.[7]

This approach to determining whether to exclude trusts from the settlement raises significant questions. For example, there are several trusts for which factors two and three favor rejection, but Mr. Fischel recommends acceptance because 15% or more of investors in those trusts have not opposed the settlement. What this means is that the Trustees are asking the Court to conclude that the settlement is fair for trusts that–according to Mr. Fischel himself– there is a "likelihood" that the trust could recover more money in a repurchase action brought by the trustee– a repurchase action that Mr. Fischel suggests would be timely. Moreover, the potential recoveries in a number of the repurchase actions that the Trustees could bring – again according to Mr. Fischel – could be massive. For example, for BSMF 2007-AR4, a trust in which the FHLB Boston is an investor, Mr. Fischel notes loan file re-underwriting done in connection with prior litigation showing a breach rate of 91%. Based on this figure, Mr. Fischel estimates that the Trust could potentially recover $503 million in a separate action brought by the Trustee against JP Morgan rather than the $38.3 million that will be paid to the trust if the settlement is approved –an over 13x improvement. Fischel Report at Ex. Q1, p.4. Nonetheless, Mr. Fischel recommends acceptance for this trust. This same anomaly appears to exist for numerous other Accepting Trusts.

The fact that investors holding 15% or more of the beneficial ownership have not come forward and demanded exclusion for these trusts does not answer the question whether the

[7] Fischel assumes that the statute of limitations is six-years from when the securitization transaction "closed," absent tolling. However, this is a controversial proposition in its own right, currently under review by the New York Court of Appeals. *ACE Securities Corp. v. DB Structured Products, Inc.*, 23 N.Y.3d 906 (June 14, 2014) (granting leave to appeal).

Trustees' decision to support the settlement for these trusts is reasonable given what the Trustees have learned in their analysis. Before FHLB Boston is in a position to express support for or opposition to the settlement, it needs a far better understanding of the reasons the Trustees believe this settlement is in their best interests.

Likewise, FHLB Boston also is not able to evaluate whether the release of servicing claims against JPMorgan is reasonable. A report prepared by Jeremy Reifsnyder for the Trustees discusses the benefits provided by the servicing improvements (while acknowledging that many of these improvements already are required by the National Mortgage Settlement and the OCC consent order entered into by JP Morgan), and estimates the losses caused by past servicing abuses by determining the extent to which JP Morgan was worse than other servicers.[8] Yet, his analysis appears to assume that the benchmarks he uses were not themselves skewed by abusive servicing practices. Thus, while the analysis may well show how much worse JPMorgan's servicing is compared to other servicers, it does not appear to allow FHLB Boston to determine the total losses to the Trusts caused by abusive servicing practices. Furthermore, there does not appear to be any indication or analysis of what, if anything, is paid to compensate the Trusts for past servicing abuses, as opposed to representation and warranty violations. To the extent that the Trust are not being compensated for servicing-related abuses, then this portion of the settlement provides "injunctive relief" only. While such settlements sometimes occur, this is not often the case where there is a strong liability case against the defendant. Yet, there is no information presented that supports the view that certificateholders would be unable to establish liability and damages for servicing abuses.

[8] Expert Report of Jeremy E. Reifsnyder, Boston Portfolio Advisors, Inc., July 12, 2014.

In short, for these and many other reasons, FHLB Boston lacks information necessary to fully and fairly evaluate whether the settlement is reasonable and in the Bank's best interests. Accordingly, FHLB Boston moves to intervene in these proceedings.

III. ARGUMENT

"As a general matter, intervention should be permitted where the intervenor has a real and substantial interest in the outcome of the proceedings." *Bernstein v. Feiner*, 842 N.Y.S. 2d 556 (App. Div. 2007); *see also Yuppie Puppy Pet Prods., Inc. v. St. Smart Realty, LLC*, 77 A.D.3d 197, 201 (1st Dep't 2010) ("Intervention is liberally allowed by the courts, permitting persons to intervene in actions where they have a bona fide interest in an issue involved in that action."). CPLR 1012(a) permits a party to intervene in an action as of right if (1) "the action involves the disposition or distribution of, or the title or a claim for damages for injury to, property and the person may be affected adversely by the judgment" or if (2) "the representation of the person's interest by the parties is or may be inadequate and the person is or may be bound by the judgment." CPLR 1013 permits a party to intervene with the permission of the Court if "the person's claim or defense and the main action have a common question of law or fact . . . [and] the intervention will [not] unduly delay the determination of the action or prejudice the substantial rights of any party."

Although establishing any of these conditions independently would be sufficient to permit the Bank to intervene, all three are satisfied in this proceeding.

A. This Article 77 proceeding involves claims for damages for injury to property, and FHLB Boston will be affected by the proposed judgment.

FHLB Boston owns securities in 38 of the 312 trusts that are related to the proposed settlement. If approved, the settlement would forever release all claims those trusts have against JPMorgan, and all claims FHLB Boston may have against the Trustees, thereby materially

affecting the value of the Bank's certificates in those trusts. Furthermore, the Order to Show Cause the Trustees obtained from this Court indicates that all "Potentially Interested Persons"—defined in the Affirmation of Robert C. Micheletto as "entities that may have an interest in the subject matter of the Petition" because they are "holders of certificates or notes evidencing various categories of ownership interests in the Accepting Trusts or obligations issued by the Trusts" (Doc. No. 7 at ¶ 4)—may have in an interest in this Article 77 proceeding. FHLB Boston is clearly a Potentially Interested Person as set forth by the Trustees.

Accordingly, there is no dispute that FHLB Boston fits the definition of an interested party that should be permitted to intervene as of right in this proceeding pursuant to CPLR 1012.

B. The Trustees may not be adequately representing the Bank's interests in the Accepting Trusts.

CPLR 1012(a) also permits intervention as of right where "the representation of the person's interest by the parties is or *may be* inadequate and the person is or *may be* bound by the judgment." (Emphasis added). To intervene as adverse parties, the Bank need not show that the Trustees representation will necessarily be inadequate; it is sufficient for the Bank to show that the Trustees may not adequately represent its interests. *Dimond v. District of Columbia*, 792 F.2d 179, 192 (D.C. Cir. 1986). Courts have also held that "[t]ypically, persons seeking intervention need only carry a minimal burden of showing that their interests are inadequately represented by the existing parties." *U.S. v. Union Electric Company*, 64 F.3d 1152, 1168 (8th Cir. 1995).[9]

Although the Trustees are required to protect the interests of all certificateholders, including the Bank, in the trusts that they administer, the Trustees have acknowledged that

[9] CPLR 1012 is modeled after Rule 24 of the Federal Rules of Civil Procedure. Judicial opinions that interpret Rule 24—like those cited here—are thus persuasive authority for this Court.

certificateholders may have conflicting views about the adequacy of the proposed settlement. In fact, the Trustees state that they "recognize that different groups of certificateholders may wish to pursue remedies for the alleged breaches in different ways, creating the potential for disagreements among certificateholders within the same trusts. For example, the Institutional Investors have requested that the Trustees accept the Settlement on behalf of all of the Trusts. Other groups of rcertificateholders have requested that the Trustees not accept the settlement and file (or continue) lawsuits on behalf of particular Trusts." Doc. No. 1 at ¶ 18.

Accordingly, FHLB Boston is concerned that the Trustees may not have adequately protected its interests in evaluating the settlement, and may not do so in this proceeding. Similarly, the Bank cannot know from information now available whether the Institutional Investors have, can, or will protect the interests of the Bank. Indeed, section 2.03(d) of the settlement agreement obligates the Accepting Trustees, JPMorgan and the Institutional Investors to use their reasonable best efforts to obtain Final Court Approval of the Settlement, even if "any Party discovers facts that are additional to, inconsistent with, or different from those which they knew at the time they entered into this Settlement Agreement." Because the proponents of the settlement are bound to support it even if subsequently discovered facts indicate it is unfair, they are not likely to identify ways in which the proposed settlement would adversely affect the interests of FHLB Boston.

In addition, the settlement agreement indicates JPMorgan and the Institutional Investors engaged in "arm's length and good faith negotiations" in entering into the proposed settlement before submitting it to the Trustees. Because the Trustees were not involved in these negotiations despite receiving an instruction from the Institutional Investors on December 15, 2011 to open an investigation into all representation and warranty and servicing claims, the

possibility exists that the Institutional Investors will not adequately protect the Bank's interests. The Governing Agreements also require the Trustees to treat all certificateholders similarly and preclude the Trustees from placing one certificateholder's interests ahead of another. Given that the Settlement was negotiated by 21 Institutional Investors—some of whom purchased significant interests in the securities at issue at distressed prices (in contrast to the Bank)—further information is necessary to evaluate whether the proposed settlement inures to the benefit of all certificateholders fairly and equally.

These are precisely the circumstances that CPLR 1012 was designed to address by permitting parties like FHLB Boston to intervene as of right to protect their own interests.

C. FHLB Boston satisfies the requirements for intervention under CPLR 1013.

Even if the Bank were not permitted as of right to intervene in this proceeding, it nevertheless satisfies the requirements for discretionary intervention under CPLR 1013. The Court has discretion to permit a party to intervene when "the person's claim or defense and the main action have a common question of law or fact." *Id.* In this case, it is particularly appropriate for the Court to exercise its discretion to permit intervention, because "in the absence of the intervenors, there is, as a practical matter, no real adversary proceeding before the court." *In re The Petroleum Research Fund*, 157 N.Y.S.2d 693 (App. Div. 1956). Under Federal Rule of Civil Procedure 24(b)—on which CPLR 1013 is patterned—"intervention is encouraged if the proposed intervenors' claims will add to the Court's understanding of the facts." *Rodriguez v. Debuono*, Case No. 97-0700, 1998 WL 542323, at *3 (S.D.N.Y. Aug. 24, 1998); *see also Commack Self-Service Kosher Meats, Inc. v. Rubin*, 170 F.R.D. 93, 106 (E.D.N.Y. 1996) (intervenors "will bring a different perspective to the case and will contribute relevant factual variations that may assist the court in addressing the constitutional issue raised"). The Bank satisfies all of these conditions for intervention.

Finally, permitting FHLB Boston to intervene in this proceeding will not "unduly delay the determination of the action or prejudice the substantial rights of any party." CPLR 1013. The Bank filed this request to intervene in a timely manner, well in advance of the November 3, 2014 deadline for parties to file a written notice of intention to appear and object. Doc. No. 68 at ¶ 7. The involvement of FHLB Boston will help the Court reach a balanced judgment of the proposed settlement because, unlike the Institutional Investors, it is not contractually bound to support it. And any other interested party that wishes to participate in this proceeding is free to do so. Under these circumstances, substantial rights of the Bank would be prejudiced if it were not allowed to intervene.

IV. CONCLUSION

For the foregoing reasons, FHLB Boston respectfully requests that the Court grant its Order to Show Cause and add it as an intervenor-respondent in this Article 77 proceeding.

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