Ross & Orenstein LLC

M E M O R A N D U M

Date: March 30, 2017
From: Ross & Orenstein LLC
To: HVMLT 2005-10 Certificateholders
Subject: Inadequate HVMLT 2005-10 Proposed Settlement

We write on behalf of Bonitas LLC ("Bonitas"), a certificateholder in HVMLT 2005-10 (the "Trust"), to share our analysis of the Proposed Settlement negotiated by certain certificateholders (the "Initiating Parties"). Bonitas believes that certificateholders ("Holders") in the Trust should not support the Proposed Settlement of the pending litigation, *U.S. Bank Nat'l Ass'n v. Countrywide Home Loans, Inc.*, No. 652388/2011 (N.Y. Sup. Ct. N.Y. Cty) (the "Action").

As a threshold matter, we believe a vote on the Proposed Settlement is inappropriate. There is an existing Event of Default under the PSA, as the memo from counsel for Ambac points out.[1] An Event of Default requires the Trustee to exercise its judgment as a prudent person. A prudent person would not accept a settlement of just 15% of lifetime losses (the estimate of counsel for the Initiating Parties in their memo (the "Keller Rohrback Memo")) in a case as advanced and well-positioned as this one. Bonitas has brought an action against the Trustee on this basis.[2]

Nevertheless, we find it necessary to respond to the Keller Rohrback Memo to ensure that Holders are fully informed.

I. The Action is worth much more than 15% of lifetime losses.

The Keller Rohrback Memo is correct that the Action has been pending for many years and that a lot of money has been spent on it. But the result of that time, effort and expense is that the case is at a highly advanced stage. Fact discovery – the phase of litigation that often is the most time-consuming and arduous – is complete, and expert reunderwriting reports were exchanged last year. According to the Trustee's own pleading, filed just nine months ago, fact discovery and the reports of the Trustee's experts have only confirmed the strength of the Trust's case for over $320 million in damages (an 87% breach rate applied to at least $368 million in collateral losses).

This should not surprise anyone. The heart of the case concerns the practices of Countrywide, a mortgage originator that notoriously (in the words of the Trustee) "ignored its mortgage representations in its pursuit of profit and market share." As the Trustee has also noted,

> Investigations by the [SEC], state attorneys general, the Financial Crisis Inquiry Commission, and the United States Congress have shown Countrywide's failure to abide by the representations and warranties it made in connection with the sale of Loans bound for securitizations, including the Trust.

[1] *See* "Notice of Communication from Counsel Representing Ambac Assurance Corporation and the Segregated Account of Ambac Assurance Corporation" from U.S. Bank, dated March 30, 2017.
[2] *See Bonitas LLC v. U.S. Bank Nat'l Ass'n*, Court File No. 27-CV-17-2229 (Minn. Dist. Ct. Henn. Cty).

Legal developments during the pendency of the Action have also been favorable. For example:

- The court made a ruling that permits the Trustee to present proof on more loans than were specifically identified in breach notices.
- In a related case, the judge presiding over the Action allowed a "successor liability" claim against Bank of America – that is, a claim against Bank of America based on Countrywide's breaches – to proceed, denying Bank of America's motion on that issue.
- The applicable appellate court has held in another case that an RMBS trustee may pursue claims under a provision analogous to this Trust's "No Untrue Statement Warranty" and seek repurchase of *all* loans in the Trust, whether they are individually in breach or not. That decision is on appeal to New York's highest court, and if it is affirmed, the Trustee should have the opportunity to pursue a claim for full repurchase of all loans, subject to the court's discretion.

Ordinarily a lawsuit settles for 15 cents on the dollar when there is some serious weakness or impediment to proceeding. Neither appears to be the case here.

II. The Proposed Settlement is inadequate compared to similar settlements.

The Keller Rohrback Memo repeatedly argues in favor of the Proposed Settlement by comparing it to three settlements that each involved hundreds of RMBS trusts: Countrywide, Citigroup, and JP Morgan Chase & Co. Yet Keller Rohrback has previously described the Countrywide settlement as "a pennies on the dollar giveaway of valuable claims to Bank of America," "negotiated by a minority of certificateholders" with self-interested counsel.[3]

The three bulk settlements are hardly fair comparison points to the Proposed Settlement. In each instance, the vast majority of the trusts involved had not brought litigation at all; there was none of the factual development, specific and thorough expert analysis (including forensic underwriting), or resolution of legal issues that litigation demands. In most instances, the settling trusts had not even asserted claims informally. This is a far cry from the Proposed Settlement, which involves a single trust and a lawsuit that has been through the development and discipline of years of pre-trial litigation.

Moreover, RMBS representation and warranty cases that were not part of mass resolutions have settled at much higher levels. For example:

- *ACE:* in 2016, five actions by Ace Securities Corporation Home Equity Loan Trusts were settled for approximately 25-29% of lifetime losses.
- *GEWMC-2006-1*: in 2015, settled for approximately 22.5% of lifetime losses.
- *SVHE 2006-WF1*: in 2014, settled for 32% of lifetime losses.
- *Assured Guaranty Mun. Corp. v. Flagstar Bank*: in 2013 – after a trial in which a federal

[3] *In re Bank of New York Mellon*, Index No. 651786/2011 (N.Y. Sup. Ct. N.Y. Cty), Doc. 771, at 1, available at: http://www.cwrmbssettlement.com/docs/771.pdf

judge found Flagstar Bank liable for breach of contract – settled for 42.7% of lifetime losses (which was nearly a full recovery of the damages Assured sought at trial).

This is not to say that an outcome at any of these levels would be acceptable in the present case. The point is that comparable settlements, when more appropriate comparables are chosen, do not support the Proposed Settlement but only highlight its inadequacy.

The single example in the Keller Rohrback Memo of a smaller settlement of specific trusts' litigation is the MABS 2006-HE3 and 2007-WMC1 settlement. That case, however, was in a much weaker settlement posture than this one, because (1) although the underlying case had been pending for years, there had been only limited discovery; (2) the trusts had received a series of highly unfavorable rulings from the federal district court on motions to dismiss; and (3) in the *MABS* litigation there was a real threat of potential bankruptcy of the settling defendant. None of those factors exists here, making *MABS* an especially poor comparison.

(*MABS*, however, is instructive in a different respect: the settlement was signed in August 2014, but when the Trustee filed a proceeding to have it approved, the settlement was challenged. The settlement was not paid for over two years. The suggestion in the Keller Rohrback Memo that the Proposed Settlement necessarily "will quickly result in funds being paid to the Trust" should therefore be read with some skepticism.)

III. The negotiations between the Initiating Parties and Countrywide—which excluded the Trustee—do not justify this inadequate settlement.

The Keller Rohrback Memo emphasizes the purportedly "arm's-length" mediation process between the Initiating Parties, Bank of America, and Countrywide. But notably absent from the process was the one party with a duty to Holders: the Trustee, the only party charged with protecting the interests of the Trust as a whole. Moreover, Keller Rohrback itself receives $1,546,362 under the Proposed Settlement (*see* par. 18 of the Trustee's Petition).

Where the Trustee is excluded from the negotiations, and where Holders and their counsel with their own individual interests are conducting the negotiations separately, the process does not necessarily provide a basis for confidence in the outcome.

* * *

Holders should consult their own counsel as to the standards governing the Trustee (and for that matter, as to everything else of a legal nature in this memorandum). But in Bonitas' view, the Trustee has a responsibility to continue to prosecute the Action to a reasonable resolution – whether or not a Holder directs it to do so (and to our knowledge, no Holder has directed that the Trustee *stop* prosecuting the Action). The prudent person standard requires the Trustee to reject the inadequate Proposed Settlement.

Holders also should consult their own counsel as to the impact and appropriateness of providing the release that the Trustee requires as a condition of voting.