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MBS trustee Wells Fargo to funds: If we go down, you're coming with us

(Reuters) - There is something new under the sun in the dwindling days of litigation over flawed mortgage-backed securities.

I've written several times that the last truly unsettled question in MBS litigation is to what extent investors can hold MBS trustees liable for allegedly failing to take action once it became clear the securities didn't live up to contractual promises. Broadly speaking, courts have allowed investors to move ahead to discovery on breach of contract claims against trustees, but have raised obstacles like requiring loan-by-loan re-underwriting and refusing to allow claims based on underlying mortgages peddled by defunct mortgage lenders.

Last week, as Law 360 was the first to report, one of the MBS trustees facing claims by a coalition of big institutional investors did something I haven't seen before: Wells Fargo filed third-party complaints in Manhattan federal court against the investment advisory wings of three of the institutions that have sued the trustee, BlackRock, Pimco and TIAA-CREF.

The suits allege that if Wells Fargo is ultimately socked with a judgment for tort liability in the investors' case, then the investment advisory firms ought to be held responsible for the damages. According to Wells Fargo, BlackRock Advisory, Teachers Advisory and Pacific Investment Management Company had exactly the same access as the MBS trustee to a steady stream of information about the increasing risk of MBS investment and suspicions about the underlying loans. And, unlike the MBS trustee, their job was to assure the quality of investments by their funds. So, Wells Fargo argues, if anyone is to blame for the funds' MBS losses, it's the advisory businesses.

The investment advisers were "players" in the MBS industry, just like MBS trustees, Wells Fargo said. Their own litigation tactic of banding together to force MBS issuers into billion-dollar settlements proves they knew as much as trustees, the complaint said.

The timing of the complaints is interesting. The judge overseeing the investors' case, U.S. District Judge Katharine Failla of Manhattan, partly denied Wells Fargo's motion to dismiss in March. The MBS trustee filed its answer to the plaintiffs' amended complaint on May 12. Two weeks later - with discovery disputes already in full bloom - Wells Fargo filed the complaints seeking contributions for tort damages that may never even be awarded. (Investors also claim the trustee breached its contracts with investors and is liable under the Trustee Indenture Act.)

Investor counsel Blair Nicholas of Bernstein Litowitz Berger & Grossmann declined to provide a statement on Wells Fargo's third-party suits. Trustee counsel Howard Sidman of Jones Day referred my call to the bank, which declined to comment.

---- **Index References** ----

Company: BERNSTEIN LITOWITZ BERGER AND GROSSMANN LLP; BLACKROCK INC; JONES DAY LP; PIMCO FUNDS; Pacific Invt; TIAA CREF FUNDS; WELLS FARGO AND CO

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