# County of Hamilton

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STEVEN E. MARTIN

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Re: The Western and Southern Life Insurance Company, et al. v. The Bank of New York Mellon
Case No. A1302490

Dear Counsel,

I have carefully reviewed the trial transcript, arguments of counsel and the exhibits admitted into evidence. I have weighed the credibility and testimony of each witness. I would like to thank counsel for a well tried case.

The verdict is for the defendant. I have signed the Findings of Fact and Conclusions of Law submitted by the defendant with some changes. I have deleted the section regarding

Countrywide's ability to pay and the section regarding the Article 77 proceeding. I have written separately on those issues. I made other changes as well in original paragraphs 74, 138, 177 and 190. This letter is a supplement to the Findings of Fact and Conclusions of Law and not in substitution of those Findings and Conclusions. Each side will pay their own attorneys. The plaintiffs shall pay the court costs.

As stated above, I have found for the defendant. I find no merit in any of the claims of the plaintiffs. This letter and the Findings of Fact and Conclusions of Law are limited to the facts of this case. Other Pooling and Servicing Agreements (PSAs) and other facts could have led to some different conclusions.

OVERVIEW

The plaintiffs invested in Residential Mortgage Backed Securities (RMBS) for years prior to the economic crisis of 2007-2011. The plaintiffs had a multi-point due diligence process for evaluating these securities. In the case of Countrywide, who put together and sold these securities, the due diligence involved face to face meetings, conference calls, phone calls, research and, after a time, experience gained from doing business with Countrywide. It is only logical that the plaintiffs were very happy with the way Countrywide had handled RMBS or they, and other investors for that matter, would not have bought them.

None of the due diligence done by the plaintiffs on these RMBS purchases had anything to do with who was the trustee. This actually makes sense. The trustee's role and fees in the PSAs that govern these deals is very limited.

In mid-2007, for their own business reasons, the plaintiffs began a new program called the Yield Enhancement Initiative (YEI). Specifically, and relevant to this lawsuit, this program involved purchasing even more RMBS and expanding the list of purchases to include ALT-A and subprime issues. By this time, there were already problems with these securities. Housing prices were down, mortgage default rates were up and as such the price of the securities, particularly the lower quality securities, had dropped thereby making the yields even higher. The plaintiffs documented possible problems in the RMBS market in emails from March and April 2007. They knew there were "storm clouds brewing", to "expect the worst" and that there was considerable thought and evidence that the housing bubble had collapsed. The plaintiff went ahead anyway with their purchase of lower quality RMBS even adopting the YEI to give title to the strategy. It was simply a bad read on the coming crisis. In that the plaintiffs were far from alone. None of the market problems had anything to do with the PSAs in this case. It had everything to do with a market collapse that was historic in nature. The plaintiffs liked to add RMBS to the investment portfolio because the timeline of payments from the RMBS matched up with their annuity and life insurance products.

The testimony in this case has been that the plaintiffs purchased RMBS as part of their YEI even though the plaintiffs knew that they may well have been overexposed in their RMBS investments. They also knew that the underwriters of RMBS had loosened their underwriting standards to keep volume up. Still, as noted above, the plaintiffs thought they were sophisticated

investors capable of managing all of this risk. They felt there was solid value in the ALT-A and subprime markets. Short of the economic tsunami of 2007-2011 they may well have been correct. As Mr. Weston theorized, if housing prices had not dropped, these investments would have performed well. The idea behind the YEI and RMBS investments was to make money. There is no evidence that the plaintiffs in any of their RMBS investments, including the trusts at issue in this case, insisted that a performing loan be taken out of a trust due to document and/or underwriting issues.

As noted above, the plaintiffs knew about the problems in the RMBS markets, but like a lot of people at that time they underestimated how bad it would get. The plaintiffs thought that with a "deft touch" they could pick the best RMBS. The plaintiffs were not expecting the crash that occurred but rather a soft landing. They were hardly alone in their belief however that belief was, in retrospect, erroneous. The plaintiffs thought there might be a correction in the RMBS market. The plaintiffs were simply trying to get the maximum value for and return from their investments. There is nothing in the record that the plaintiffs in any way sought the counsel of the defendant in coming to this decision. The YEI was a program launched by the plaintiffs to serve the best interests of the plaintiffs.

I mention all of the foregoing to say this: At no time during the run up to the economic crisis, or even after, was the trustee in the RMBS deals ever mentioned by the plaintiffs. It was not a factor in the investment decision nor was it part of the internal 2009 post mortem analysis of what went wrong. Internal documents of the plaintiffs created in 2009 and 2010 do not at any time criticize the work of the defendant. In exhibit after exhibit, the plaintiffs internally blamed a bad market, underwriting issues, real estate values, unemployment rates, borrower behavior, etc. for the downturn in the RMBS market. There was simply nothing indicating that the defendant was even remotely a cause of the losses suffered by the plaintiffs. Again, given the limited contractual role of the trustee as outlined in the PSAs, this is not surprising. Further, there is no evidence the defendant had any part in creating the RMBS at issue in this case.

Mr. Hunkler never communicated with the defendant about the RMBS investments of the plaintiffs. He never saw a document blaming the defendant for the losses suffered by the plaintiffs. In his testimony before Congress on RMBS, Mr. Hunkler blamed a bad economy and rampant fraud but did not have a word of critique for the defendant.

Mr. Weston claimed to have read at least some of the PSAs in evidence. Other employees of the plaintiffs who testified at trial still do not have a good grasp on this contract and the defendant's role in it. Since the relationships in this case are governed solely by the contracts at issue, this is a problem for the plaintiffs and why so many of the beliefs of the plaintiffs about the PSAs are not supported by the actual language of the PSAs.

## CAUSATION

The losses suffered by the plaintiffs were real. The evidence in this case is that these losses were caused by the failure of thousands of individuals to make payments on the loans secured by the mortgages at issue in this case. The failure to make payments was caused by an

economic crisis that was historic in its severity and duration. There is no evidence the defendant caused the downturn in the economy or in any way caused people to miss their payments.

There is not a bit of evidence in this case that the people who failed to pay on their loans did so because of document issues or anything else related to the RMBS in which their mortgage was placed. The failure to pay had nothing to do with the Master Servicer or the defendant. There was not a single payment missed because a mortgage or loan file was not complete. There is no credible evidence the Master Servicer failed to service these loans as it was required to do.

The defendant did not in any way underwrite the loans at issue in this case. It did not service the loans nor did it package the RMBS for sale. There is no evidence that the defendant or the Master Servicer for that matter stopped or even slowed a single foreclosure from taking place. This analysis would have had to be done on a loan by loan basis. This analysis has never been done and is not in the record. While Mr. Kontoulis thought the foreclosures at that time took too long, his testimony was simply not credible on that issue. There is no magic number of days a foreclosure case should take to complete. He failed to take into account foreclosure moratoriums, bankruptcy, work-outs or many other things that can delay foreclosure. There is no evidence he even considered the adverse impact on the speed of the judicial system that an unprecedented number of foreclosures would have had. The plaintiffs never complained about or even sought information on a single foreclosure on any mortgage in any trust.

The evidence is also uncontroverted that the plaintiffs never attempted to, on their own or in concert with others, get 25% of the Certificateholders in any given trust to take action. This is referenced in several sections of the PSA. The plaintiffs never offered to indemnify the trustee at any time. The plaintiffs failed in real time to take advantage of the remedy available to them in the PSA. If the plaintiffs wanted additional rights and remedies in the PSA, they should have attempted to negotiate for them. They did not do so. Of course, additional rights and remedies would have involved paying more fees and thus less return for the plaintiffs.

The plaintiffs in their written closing quote language from section 3.01 which is simply not there. Section 3.01 sets forth the obligations of the Master Servicer. The plaintiffs state the trustee is required to protect the interests of the trust fund as it would mortgage loans in its own portfolio. The actual language set forth in Section 3.01 states this obligation belongs to the Master Servicer.

Mr. Milner testified that the trigger for repurchase was not a document defect but a default. This requires a loan by loan analysis. The breach must also involve something that materially and adversely affects the Certificateholders. Thus a document defect without a default would not trigger anything. Specifically such a loan would be kept and the payments received.

The plaintiffs now say that, if the defendant had made disclosure of document issues, the plaintiffs would have walked away from their Countrywide RMBS and halted future investment in Countrywide RMBS. There is no credible testimony or other evidence to support this position. The YEI and the need for it still existed. The plaintiffs had a long history in the RMBS market

and have never abandoned it. This position expressed at trial has no credibility particularly when given years after the fact in an attempt to receive a judgment of over 100 million dollars.

At the end of the case after all the witnesses and exhibits, there is no evidence as to whether the losses of the plaintiffs came from loans with no defects or loans with many defects. Because the evidence is that the documents were irrelevant to whether someone paid their mortgage or not, it is likely defaults came from each group. Because no performing loan was to ever have been substituted or removed in any way from a trust, the plaintiffs have simply failed to prove anything the defendant did or did not do caused them to lose money. There is no evidence that the trusts where the plaintiffs lost money were in any way different in terms of the allegations the plaintiffs have made in this case from the trusts in which the plaintiffs made money.

## SAMPLING

The plaintiffs have used sampling in examining the various files in this matter. They then have attempted to extrapolate from this sampling the damages they seek. The Second Circuit in Ret. Bd of the Policeman's Annuity and Benefit Fund of the City of Chicago U. BNYM (775 F.3d 154 at p. 162) 2014 found "Whether it was obligated to repurchase a given loan requires examining which loans; in which trusts, were in breach of the representations and warranties. And whether a loan's documentation was deficient requires looking at individual loans and documents." I agree with this conclusion as applied to the case at bar.

This case is not one where sampling is in any way appropriate. Countless provisions in the PSAs rely on and presume a loan by loan analysis not sampling. Further, many provisions of the PSAs require not only a breach but a breach that materially and adversely affects the interests of the Certificateholders. This is a loan by loan analysis. Additionally I find that the sampling done by the plaintiffs and then the reliance on that sampling by their experts is, as a matter of credibility, so riddled with holes as to make it unreliable and unusable in this case.

Even if I accepted the sampling protocol used by the plaintiffs, their own experts by their testimony confirm that a loan by loan forensic analysis would be the proper way to proceed. Mr. Kontoulis agreed with Mr. Burnaman that no one would substitute or repurchase a performing loan because of document issues. The object of these investments was to make money. The evidence is that if an investment or loan were making money regardless of mortgage file issues it would not be disturbed. This is in line with the other evidence in this case that document issues had no effect on a loan's performance. To determine if a given loan file or mortgage file has document issues and whether the loan is performing requires a loan by loan review. The PSA confirms this when it speaks of specific loans being repurchased or substituted. There is simply no other way to do this other than loan by loan. This would have had to have been done in real time since things can change. Whether a loan performed depended on the economic condition of those making the payment. Whether or not a loan performed could vary from time to time. If a loan was not performing, the Master Servicer could work to get payments started. Foreclosure is usually a last resort.

The plaintiffs, at least with the trusts in this case, bought so many trusts with so many loans that such a forensic review was, as a practical matter, very difficult. This volume of trusts, and the potential problems associated with it if there was a problem, should have been part of the extensive due diligence the plaintiffs performed before investing but was not. As this Court has seen handling thousands of commercial cases during the worst economic conditions in decades, historic and unprecedented events can expose well hidden issues in contracts and relationships which is what happened here. Nonetheless, the plaintiffs are bound by the contracts they signed.

The protocol used by the plaintiffs for sampling was so flawed as to be without any credibility at all. The defense has thoroughly and convincingly attacked each and every expert put forth by the plaintiffs. I am clearly no fan of sampling because it is not the best evidence. In this matter a specific loan by the loan analysis would have yielded a far better result. The plaintiff never considered that these investments would not perform as other RMBS had in the past. The plaintiffs failed to consider in their due diligence before purchase that a loan by loan analysis might be necessary if there was a problem with the investment. As noted above, they bought so many RMBS with so many loans that such a loan by loan review was difficult. But for the historic economic conditions of 2007-2011, it might not have ever mattered. The burden for the consequences of these investment decisions lies with the plaintiffs and not the defendant.

I write on this to give my thoughts even though I need not decide this issue because the damage theories of the plaintiffs are so full of holes that the case fails on that level. As noted above, to this day, the sampling done by the plaintiffs, even if accepted by this Court, has not established whether the losses in these trusts came from loans with bad underwriting or document deficiencies or from loans that were properly underwritten and had all appropriate documentation and simply did not perform.

## CONTRACT

This case is a matter of contract. These contracts are clear and unambiguous. Obviously the allegation of the plaintiffs is that the defendant breached the contracts between the parties. Essentially the plaintiffs are asking this Court to enforce agreements they wish were in place instead of the contracts they signed.

The parties have stipulated that the PSAs are Exhibits 134 to 164. They have also stipulated the PSAs are valid and binding contracts. The defendant's duties as trustee are contractual in nature and defined by and limited by the contract. The plaintiffs have alleged that the defendant breached the contract in many ways. The defendant was the trustee on all of the trusts at issue. The duties of the trustee are set forth throughout the PSAs but are largely established in Article VIII of the PSAs. The trustee was not a gatekeeper. It was also not a trustee in the common law sense of the word. The trustee had the duties set forth in the contracts and only those duties. It did not have a fiduciary duty to the plaintiffs.

The duties of the trustee are quite limited. If the plaintiffs wanted the trustee to have greater duties, they could have negotiated for that. It would have meant paying much higher fees

thus reducing the return of the plaintiffs on their investment which would have been counter to the goals and objectives of the YEI.

There never was a written notice of an Event of Default received by the trustee. Such a notice would have had to be trust and loan specific. The only party who could cause an Event of Default was the Master Servicer. There is no Event of Default by the Seller, Trustee or any other party. If the plaintiffs wanted the Event of Default to be broader, they should have negotiated for it. Again, this would have required higher trustee fees and less return for the plaintiffs and would have been counter to the YEI and company policy. Another alternative would have been to simply not purchase Countrywide RMBS.

Any Event of Default would have involved the Master Servicer failing to perform in any material respect. The analysis in the PSAs does not stop there. This failure must also materially affect the rights of the Certificateholders. This is not strict liability. It needs to be analyzed on a loan by loan basis. There is simply no other way. It is not evidence of a Master Servicer breach that the investment failed.

Finally even if there was an Event of Default, which there was not, there is little to no evidence in the record as to what a "prudent trustee" would have done in such an event. There is no evidence in the record of what would have benefitted these trusts as a whole given market conditions. For example, it is conceivable if not likely that a blanket program of loan repurchases because of document problems could have harmed some of the trusts. Everyone agrees that no loan would ever but repurchased or substituted because of a document issue. There is no guarantee or evidence that all of the Certificate holders would have viewed the phrase "prudent person" in the same way. Since performing loans, regardless of other issues, were not to be repurchased or substituted, there would have to be a loan by loan analysis. If that analysis were done, it would show how the parties performed with regard to each loan. That analysis, required to prove this case, has never in 9 or 10 years taken place. Again, it simply is not proof of liability or damages to claim, however correctly, that a great deal of money was lost.

## ARTICLE 77

This issue has come up several times. It is my responsibility to explain my decisions. I have previously overruled a Motion to Dismiss filed by the defendant but I have not made myself clear as to the reasons for this. It is largely a moot point since, in any event, I have found the plaintiffs have not proven their case and, based on this, the defendant is entitled to judgment.

As I read the statute and the court case, the defendant secured a great deal of money from Countrywide and its successor Bank of America for bad acts committed by Countrywide. I can find nothing where the defendant has paid for bad acts alleged to have been committed by it.

I have never seen a document releasing the defendant from any liability from its actions as trustee in these trusts. The money in the settlement was paid by Bank of America not the defendant. As noted above, given that I have found that the defendant is entitled to judgment in this case in any and every way this case is analyzed, the Article 77 settlement is a moot point.

## COUNTRYWIDE ABILITY TO PAY

The defendant has claimed that even if the plaintiffs are correct Countrywide had no ability to pay. As noted above and in the Findings of Fact and Conclusions of Law, the theories of the plaintiffs on liability and damages are not credible for a host of reasons.

The defendant has failed to prove that Countrywide had an inability to pay. The testimony of Gene Deetz is credible in same regards and not in others. The financial situation for Countrywide was very fluid during the market collapse as it was for hundreds of companies. To theorize what Countrywide could or could not have done on any given day may be true, however that fact could have changed in a matter of days.

I write to address this issue but it is moot since I have rejected as without merit all of the theories of the plaintiffs on liability and damages.

## DAMAGES

The plaintiffs have not proved by a preponderance of the evidence they are entitled to damages from the defendant. The reasons for this include but are not limited to:

(1) The plaintiffs have failed to prove any case of liability against the defendant
(2) There is no credible evidence that the defendant's actions or inactions caused the plaintiffs to lose the money they did
(3) Using sampling in this case is grossly inappropriate
(4) Even if sampling were appropriate, the sampling methodology done by the plaintiffs is so badly flawed that its results have no credibility

## CONCLUSION

The plaintiffs made a number of investments in RMBS that did well. The trustees in those trusts were not responsible for those successes. The market and the people who made the payments were. The plaintiffs also made a number of investments in RMBS on which they lost a great deal of money. Based on the evidence and the record in the case, the defendant was not in any way responsible for those losses. The market or potentially other entities were responsible for these losses. If the plaintiffs wanted the trustee's duties to be such that they could blame the trustee for a downturn in the economy and thus their losses on these economically sensitive investments, they should have negotiated that into the PSAs somehow.

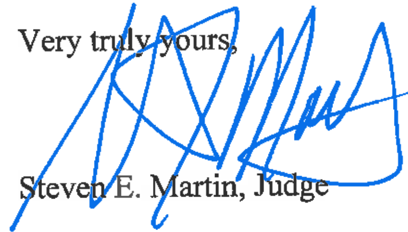
There was never an Event of Default in this matter as that term is defined in the PSA. There was never anything close to an Event of Default. If the plaintiffs wanted Events of Default to include the Seller or Trustee among others, they should have negotiated that into the PSAs which would have required higher fees.

This is a contract case. The plaintiffs, after a due diligence process, chose to invest in these Countrywide RMBS. They signed the PSAs for each trust. I have found no breach of these contracts by the defendant. This case is not unlike hundreds of commercial cases I have seen over the last 9 years. The economic downturn was so sharp, sudden and long-lasting that more

than one contract has been found by one party to have issues in it that were under normal circumstances unforeseeable. These contracts are no exception. These sophisticated plaintiffs have alleged the contracts say what they do not. I am bound by the contracts as written.

Thank you again for a well tried case. Particularly helpful were the thumb drives you each gave me for your closing arguments. The links you gave helped me look at the exhibits and the cases that you referenced which made my job a lot easier. Thank you as well for the hard copies of the exhibits you gave me during the trial. I have reviewed these exhibits extensively during deliberations.

Very truly yours,



Steven E. Martin, Judge