



# Hot Secondary Market Issues: Loan Repurchase Enforcement and Litigation

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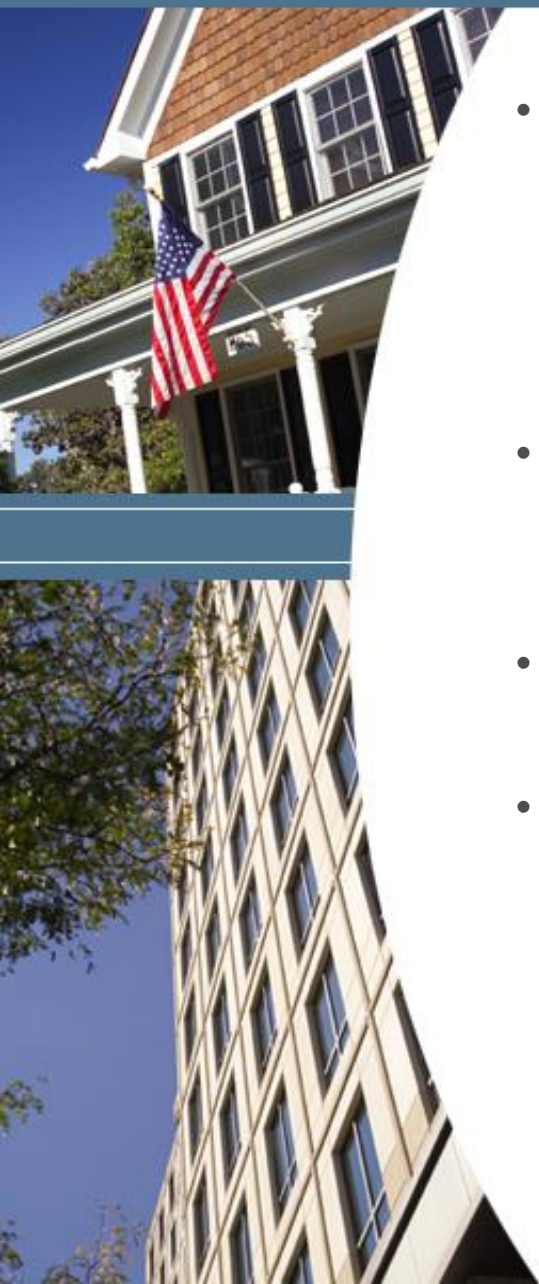


## Repurchase Claims and Investigations by FHFA and GSEs



## FHFA Subpoenas

- FHFA, acting as conservator for Fannie Mae and Freddie Mac, issued 64 subpoenas in July 2010
- Subpoenas issued for the purpose of “assess[ing] whether contractual violations or other breaches have taken place leading to losses for the Enterprises and thus taxpayers.” *FHFA Press Release*, July 12, 2010.
- FHFA has retained a private law firm – signaling an aggressive approach
- Recipients have not been made public, but include servicers, originators, and trustees



- **Broad subpoena power:** statute on which authority is based (Home Economic Recovery Act of 2008) mirrors provisions of Federal Deposit Insurance Act which grant authority to FDIC to investigate claims on behalf of failed banks
- **Subpoenas extremely broad and burdensome:** seek loan files and other information related to hundreds of thousands of loans
- **Negotiations as to scope ongoing:** could end up in litigation if FHFA moves to enforce the subpoena
- **Potential issues:**
  - » Privilege review – takes time and money
  - » Difficulty with asserting burdensomeness argument against private litigants once loan files produced

## GSE Repurchase Demands

- GSEs increasingly aggressive – especially with respect to 2007-08 originations
- Some common issues identified:
  - » Appraisal issues: “retrospective” appraisals conducted and used to challenge property valuation
  - » Stated income: challenges to reasonableness of stated income, often using Salary.com
  - » “Undisclosed liabilities”: borrower entered into transactions just prior to closing that did not appear on the credit report used to underwrite the loan



## Litigation Update

## Overview

- Private (non-agency) repurchase litigation – **still on the upswing**
- Some stats:
  - » Estimated total liability on subprime MBS: \$80.3 billion\*
  - » Estimated total liability on Alt-A MBS: \$67.9 billion\*
  - » Quarterly volume of non-agency MBS repurchases has been between \$60 million and \$100 million since the beginning of 2009
- Most repurchase requests to date dominated by home equity lines of credit, second liens, and first lien deals wrapped by mortgage insurers

\* According to Compass Point Research and Trading

# Loan Repurchase Enforcement and Litigation



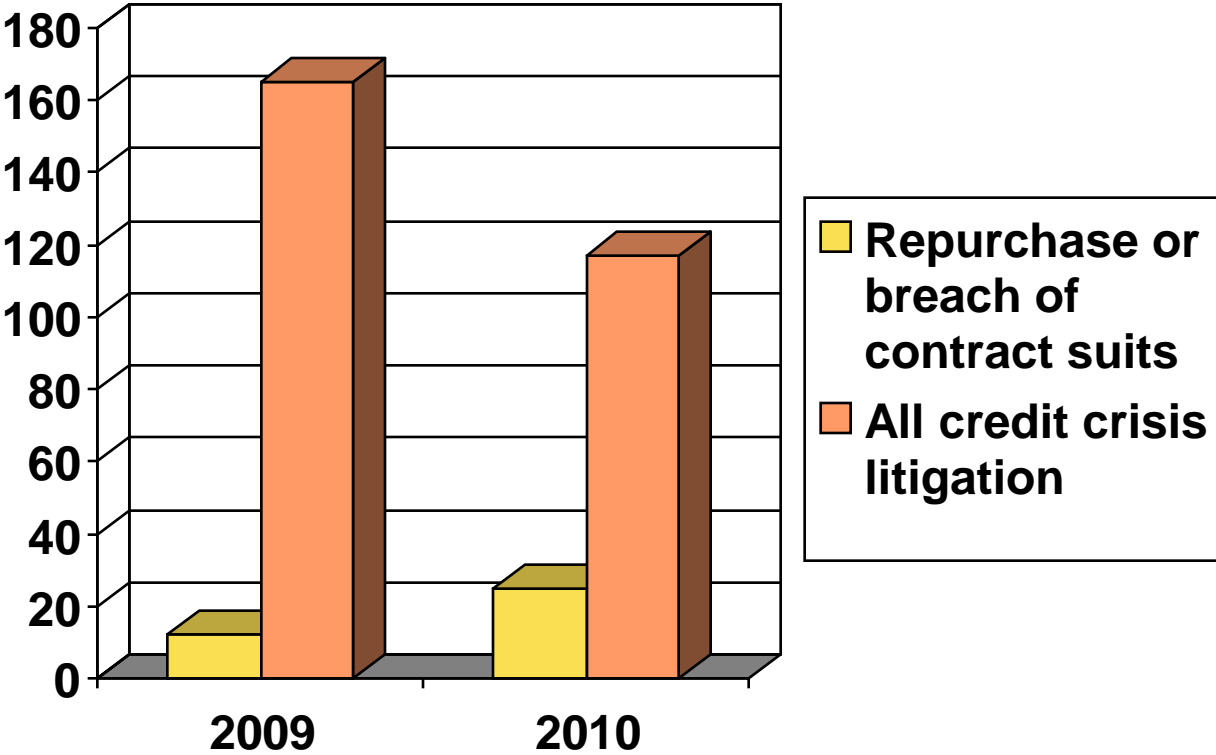
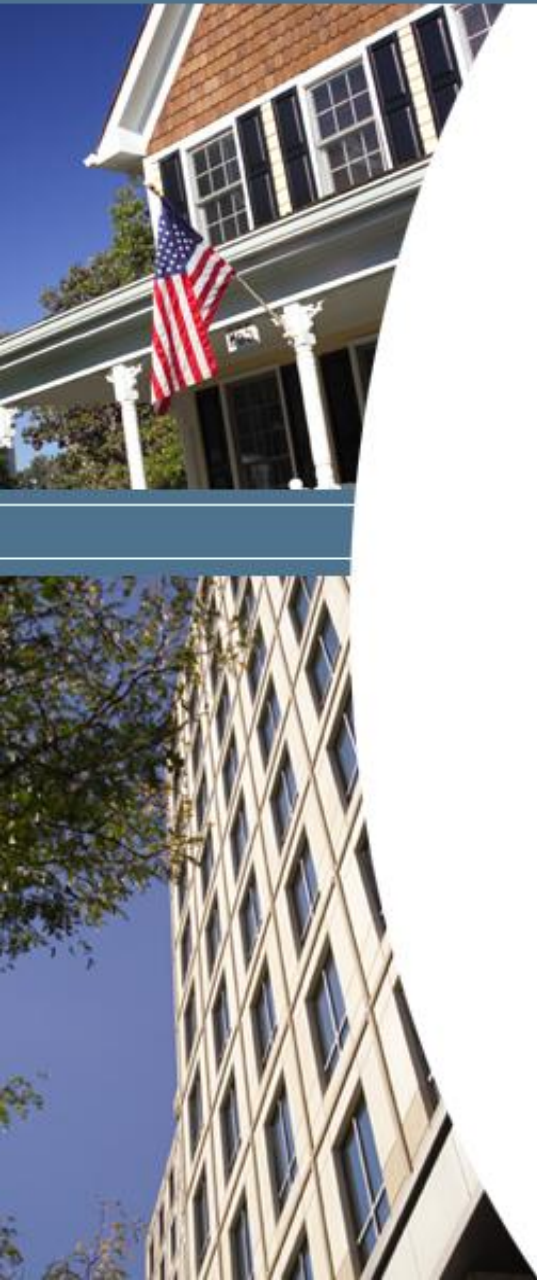
**It's a Jungle out there!** by HAGEN



**If you ask me, the constant fear of litigation is taking all the fun out of life...**

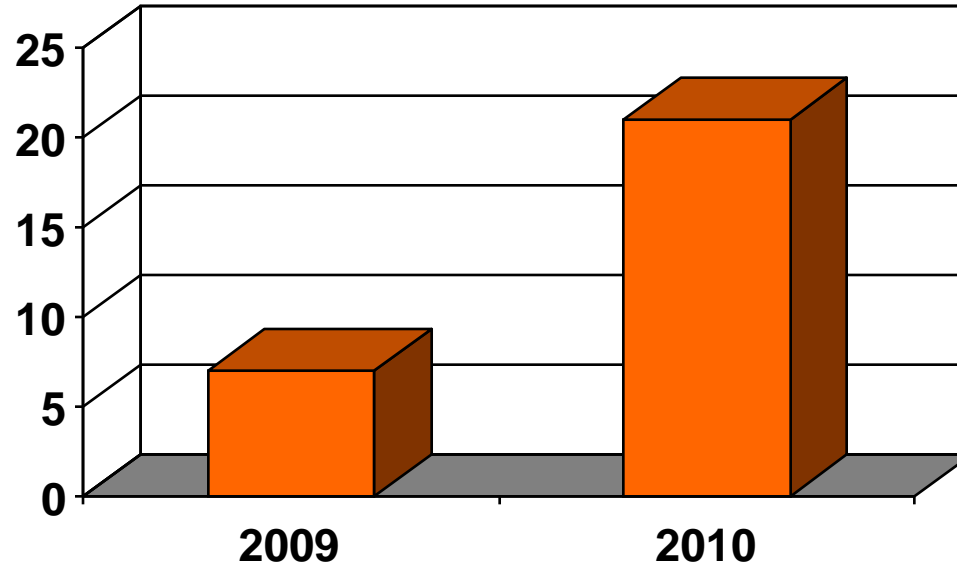
Hagen Cartoons: <http://www.hagencartoons.com>

# Loan Repurchase Enforcement and Litigation



Data compiled by Navigant Consulting

# Loan Repurchase Enforcement and Litigation



- Repurchase suits as percentage of all credit-crisis related litigation

Data compiled by Navigant Consulting

## MBIA v. Countrywide (Sup. Ct. NY) (Bransten, J.)

- » Insurer v. Originator suit
- » **Allegations:** Suit alleges fraud and breach of contract in connection with origination and securitization of mortgage loans (2<sup>nd</sup> liens) which were placed into trusts insured by MBIA
- » **Status:** Motion to dismiss granted in part (negligent misrepresentation claim) and denied in part (fraud, successor liability, breach of implied covenant of good faith and fair dealing); parties have cross-appealed
- » In the meantime, judge will consider arguments on whether to allow the use of statistical sampling

## Syncora v. Countrywide (Sup. Ct. NY) (Bransten, J.)

- » Insurer v. Originator suit
- » **Allegations:** Suit alleges fraud and breach of contract in connection with the origination and securitization of HELOCs and closed-end seconds insured by Syncora.
- » **Status:** Motion to dismiss granted in part and denied in part; appeals pending
- » Discovery is proceeding: Judge Bransten has ordered Countrywide to produce all loan files regarding three securitizations
- » Countrywide has filed counterclaims against Syncora for breach of contract related to its failure to pay claims; Syncora moved to dismiss (briefing is ongoing)



## FHLB Lawsuits

- » Late 2009/Early 2010: the FHLBs of Pittsburgh, Seattle, and San Francisco filed lawsuits against the underwriters of securitizations
- » **Allegations:** Suits allege that the underwriters made inaccurate claims related to the quality of the loans in the securitization prospectus – such as the percentage of high LTV loans, amount of investor properties, or compliance with underwriting guidelines
- » **Status:** Still in early stages; no rulings on dispositive motions yet
- » Combined, these lawsuits seek rescission on about \$25.6 billion in MBS purchases



## Other activity

### » NY Federal Reserve

- Last week, joined PIMCO and BlackRock to send demand letter to Bank of America and Bank of New York Mellon (trustee) seeking repurchase of \$47 billion in Countrywide loans.
- After 60 days, can file lawsuit if no resolution.

## » “Investor Syndicate”

- Investors owning about a third of private-label MBS (approx. \$500 billion worth) have joined together
- The Investor Syndicate has sent letters asking that trustees enforce servicing breaches related to improperly originated loans
- The group now tops the 25% ownership threshold required to force trustees to compel servicers to hand over information (i.e., loan files) or be removed



## Principal Challenges in Loan Repurchase Litigation

- Access to loan files
- Entities playing multiple roles (e.g., originator, servicer, securitizer) in transactions

## What's next?

- » Further and increased intervention by federal and state banking and insurance regulators
- » Continued aggressive action by FHFA and GSEs
  - Need to justify “bailouts” to Congress and public

## What's next?

- » Inevitable large-scale production of borrower loan files
  - Converging on multiple fronts: FHFA subpoenas, private litigation, and possible action by Investor Syndicate
- » Likelihood of settlements increasing
- » But also likely that entities faced with repurchase demands will be more forceful in resisting them -  
- traditional success rate on challenges is around 50% (unclear if that will hold steady)