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SECURITIZED PRODUCTS

### BNY Mellon files an Interpleader action on Countrywide deals

Earlier past week, BNY Mellon as trustee filed an interpleader action seeking judicial instruction on computing the payout for IO bonds in 278 Countrywide deals. **The petition covers 2002-07 vintage prime and Alt-A fixed rate CWALT and CWHL deals and in the near term would affect the deals' callability pending the resolution of the Article 77 process.** Additionally, should the trustee change its current methodology on computing the payout for IO bonds, it could adversely affect valuations on other bonds in the deal.

The dispute on the computation of interest for IO bonds is based on whether the trustee should use the initial interest rate or the current interest rate on mortgages to compute the payout. **The payout on these bonds is backed by any excess interest payment beyond a certain threshold from those mortgages for which the initial interest rate exceeded a specific threshold (also called 'Non-Discount Mortgage Loans'). Due to modifications, the current interest rate is now lower on such Non-Discount Mortgage Loans. For the purpose of computing the payout on IO bonds, the trustee uses the following methodology currently:**

- **A: Compute the UPB of loans which were classified as 'Non-Discount Mortgage Loans' based on their initial mortgage rate**
- **B: Compute the excess of such loans current mortgage rate over a specific threshold (as defined in the PSA), weighted by the current balance.**
- **C: The interest payable to the IO bonds, termed as the 'Class Optimal Interest Distribution Amount' is the product of the above two factors (on a monthly basis) in addition to past unpaid interest.**

In December 2018 a bondholder filed a lawsuit in the NY Federal Court against BNY Mellon as trustee for 156 Countrywide deals over its computation of the payout for IO bonds. According to the bondholder's complaint, the trustee should be using the loan's initial mortgage rate (as opposed to the current mortgage rate) for the purpose of calculating (B) above.

In addition to changing its current methodology, **the bondholder also sought reimbursement for past 'shortfalls' the IO bonds have incurred based on the methodology followed by the trustee.** The bondholder also cited that DBNT as trustee uses the original mortgage rate to compute the payout on IO bonds in deals with similar language in the RAST shelf.

As a result of the lawsuit, the trustee filed the Article 77 petition in the NY State Supreme Court last week seeking a judicial instruction on how the payout should be computed. It also seeks to bar bondholders from asserting any claims on the trustee based on how it has computed the cashflow waterfall.

**Potential impact for bondholders:** As a result of the Article 77 petition and the lawsuit, we expect call activity to decline significantly in these deals. Additionally, as the Article 77 process would affect the valuation of all bonds in the capital structure, we think there would be numerous investors involved in the process and any resolution of a particular deal would depend on whether there are contesting opinions on how the PSA should be interpreted. As a result, the valuations of both the WAC IO and the P&I bonds is likely to be contingent on both the number of contesting bondholders and their respective positions in the Article 77 process.

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##### US Securitized Products

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# Appendix A-1

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