

State of New York Court of Appeals

Summaries of cases before the Court of Appeals are prepared by the Public Information Office for background purposes only. The summaries are based on briefs filed with the Court. For further information contact Gary Spencer at 518-455-7711 or gspencer@nycourts.gov.

To be argued Tuesday, November 17, 2020 (arguments begin at 2 pm)

No. 85 JPMorgan Chase Bank, National Association v Caliguri

No. 86 US Bank National Association v Nelson

These mortgage foreclosure actions hinge on whether the plaintiffs established standing by providing evidence that they were the holder or owner of the mortgage note on which they sought to foreclose, or whether they were required to provide such evidence.

In Case No. 85, JPMorgan Chase Bank brought this action in 2014 to foreclose a \$1 million mortgage on a Suffolk County house owned by Ross Caliguri, alleging he defaulted on the loan. The bank acquired the note in 2008 when it purchased all assets of the originator of the loan, Washington Mutual Bank (WaMu), in a receivership transaction. Caliguri raised affirmative defenses in his answer, including lack of standing, and demanded production of the original note. Chase, which had attached to its complaint copies of the mortgage and the note with a blank endorsement from WaMu, did not comply with the demand to inspect the original note. Supreme Court denied Caliguri's motion to dismiss, finding the bank had established standing, and granted the bank's motion for summary judgment.

The Appellate Division, Second Department affirmed, saying, "JPMorgan Chase demonstrated its prima facie entitlement to judgment as a matter of law by producing the mortgage, the unpaid note, and evidence of default.... In addition, it established its standing by attaching to the summons and complaint a copy of the consolidated note, bearing an endorsement in blank from the original lender.... Contrary to the defendant's contention, 'there is no requirement that an entity in possession of a negotiable instrument that has been endorsed in blank must establish how it came into possession of the instrument in order to be able to enforce it....'" Caliguri argues that Chase failed to establish standing by proving it had actual possession of the original mortgage note. He says the lower courts acted prematurely in granting summary judgment to the bank when he had challenged the bank's standing and his demand for inspection of the original note had not been met.

In Case No. 86, US Bank brought this action in 2009 to foreclose a \$660,000 mortgage on a three-family residence in Brooklyn owned by Kenyatta and Safiya Nelson. US Bank alleged in its complaint that it was "the owner and holder of [the] note and mortgage being foreclosed." In their answers, the Nelsons denied the bank's factual allegations and raised several affirmative defenses, but did not expressly assert that US Bank lacked standing. Supreme Court granted the bank a judgment of foreclosure and sale in 2015.

The Appellate Division, Second Department affirmed on a 3-1 vote, ruling the Nelsons waived any claim that the bank lacked standing to foreclose. It said, "[The] issue of standing is waived absent some affirmative statement on the part of a mortgage foreclosure defendant, which need not invoke magic words or strictly adhere to any ritualistic formulation, but which must clearly, unequivocally, and expressly place the defense of lack of standing in issue by specifically identifying it in the answer or in a pre-answer motion to dismiss. A mere denial of factual allegations will not suffice for this purpose." The dissenter said, "[T]here is no reason to adopt a rule of law that mandates that the defense of lack of standing is waived unless magic words such as 'defense' or 'affirmative defense' appear together with 'lack of standing' in a responsive pleading.... [W]here ... a plaintiff alleges in its complaint that it is the 'owner and holder of [the] note being foreclosed' ..., a denial ... should suffice to put the plaintiff on notice as to the issue of standing."

No. 85 For appellant Caliguri: Jeffrey Herzberg, Hauppauge (631) 761-6558

For respondent JPMorgan Chase: Alan E. Schoenfeld, Manhattan (212) 230-8800

No. 86 For appellant Nelsons: Jared B. Foley, Manhattan (212) 935-3131

For respondent US Bank: Katherine Wellington, Manhattan (212) 918-3000

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No. 84 Matter of Part 60 Put-Back Litigation (Deutsche Bank National Trust Co. v Morgan Stanley Mortgage Capital Holdings, LLC)

Deutsche Bank National Trust Co., acting as trustee of a trust created to hold and securitize 5,337 subprime mortgages, brought this breach of contract action against the sponsor of the securitization, Morgan Stanley Mortgage Capital Holdings, seeking damages for numerous defaults that occurred after the residential mortgage-backed securities (RMBS) were sold to investors. Morgan Stanley acquired the mortgage loans at a bankruptcy auction in 2007, shortly before the housing market collapsed, and conveyed them to an affiliate pursuant to a representations and warranties agreement (RWA) in which it attested to the quality of the loans. The affiliate then conveyed the loans to the trust pursuant to a pooling and servicing agreement (PSA) with Deutsche Bank and others. The RWA provides that, in the event of a breach of any of the warranties, Morgan Stanley must cure or repurchase the affected loans. It also provides that Morgan Stanley's repurchase obligation "constitutes the sole remedy" of any "person or entity with respect to such breach." The PSA contains a similar "sole remedies" clause. Claiming the trust suffered more than \$495 million in damages due to widespread breaches of the warranties, Deutsche Bank sought compensatory and punitive damages. Morgan Stanley argued that compensatory damages were precluded by the sole remedy clauses; Deutsche Bank argued the clauses were unenforceable because Morgan Stanley acted with "gross negligence."

Supreme Court granted Morgan Stanley's motion to dismiss claims for compensatory damages, as precluded by the sole remedy clauses, and punitive damages. It said gross negligence was not established by a 2014 cease and desist order from the Securities and Exchange Commission (SEC), which found Morgan Stanley violated the Securities Act of 1933 by understating to investors the number of delinquent loans in the trust. The court said, "This order does not make findings as to the willful misconduct or gross negligence that would support ... relief from the sole remedy provisions.... Indeed, the SEC order specifically provides ... that the violation of the Securities Act 'may be established by a showing of negligence.'" It dismissed the punitive damages claim because "an independent claim of fraud is not plead; nor does the complaint plead a wrong aimed at the public, generally."

The Appellate Division, First Department reversed and reinstated the claims for compensatory and punitive damages. Citing allegations that an analysis by the trust's insurer found breaches of warranties in all 800 of the loans it sampled and that Morgan Stanley departed from its own underwriting guidelines in various ways, it said "the complaint's allegations of pervasive, knowing breaches of the representations and warranties on multiple grounds as to the quality of loans throughout the pool sufficiently pleaded gross negligence to render the sole remedy clause ... unenforceable." Regarding punitive damages, it said the complaint, which cited SEC findings that Morgan Stanley committed "fraud and deceit" on investors, "sufficiently alleges that defendants' conduct was 'egregious' and 'part of a pattern directed at the public generally...,'" and "plaintiff's allegations of wrongdoing committed against it are sufficient to support a demand for punitive damages at this pleading stage."

For appellant Morgan Stanley: Brian S. Weinstein, Manhattan (212) 450-4000

For respondent Deutsche Bank National Trust: Steven F. Molo, Manhattan (212) 607-8160