

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: CHARLES E. RAMOS  
*Justice*

PART 53

Assured Guaranty Corp.

INDEX NO.

650805/12

- v -

MOTION DATE

EMC Mortgage LLC

MOTION SEQ. NO.

01

MOTION CAL. NO.

The following papers, numbered 1 to \_\_\_\_\_ were read on this motion to/for \_\_\_\_\_

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...  
Answering Affidavits — Exhibits \_\_\_\_\_  
Replying Affidavits \_\_\_\_\_

PAPERS NUMBERED

Cross-Motion:  Yes  No

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Motion is decided in accordance with accompanying Memorandum Decision

Dated: \_\_\_\_\_

CHARLES E. RAMOS

Check one:  FINAL DISPOSITION  NON-FINAL DISPOSITION

Check if appropriate:  DO NOT POST  REFERENCE

SUBMIT ORDER/ JUDG.  SETTLE ORDER/ JUDG.

SUPREME COURT OF THE STATE OF NEW YORK  
COUNTY OF NEW YORK: COMMERCIAL DIVISION

-----X  
ASSURED GUARANTY COPR.,

Plaintiff,

-against-

Index No.  
650805/12

EMC MORTGAGE, LLC (formerly known as EMC  
MORTGAGE CORPORATION), BEAR STEARNS ASSET  
BACKED SECURITIES 1 LLC, J.P. MORGAN SECURITIES  
LLC (formerly known as BEAR, STEARNS & CO. INC.),  
and JPMORGAN CHASE BANK, N.A.,

Defendants.  
-----X

**Charles E. Ramos, J.S.C.:**

Defendants EMC Mortgage, LLC, formerly known as EMC Mortgage Corporation (EMC), Bears Stearns Asset Backed Securities I LLC (BSABS), J.P. Morgan Securities LLC (JPMS), formerly known as Bear, Stearns & Co. Inc. (Bear Stearns & Co., together with EMC, Bear Stearns), and JP Morgan Chase Bank, N.A. (JP Morgan) (together, defendants) move for partial dismissal of the complaint, pursuant to CPLR 3211 (a)(1) and (a)(7).

At oral argument held on these motions, the parties agreed to hold in abeyance that portion of the motion that seeks to dismiss the claim for fraudulent inducement, pending the determination by the First Department of a pending appeal stemming from the May 1, 2012 decision of Justice Sherwood in *CIFG Assurance North America, Inc. v Goldman, Sachs & Co., et al* (652286/11).

## **Background**

The allegations set forth below are taken from the complaint, and are assumed to be true for the purposes of disposition.

Assured, a monoline insurer, provided financial guaranty insurance for residential mortgage-backed securities (RMBS) transactions underwritten by Bear Stearns, and alleges that Bear Stearns grossly misrepresented the risk of the underlying pooled loans.

The transaction at issue in this action, the SACO I Trust 2005-GP1 (SACO Transaction, or Transaction), closed in September 2005, and involved the sale of 6,028 home equity lines of credit (HELOCs) by EMC which were purchased from non-party GreenPoint Mortgage Funding Inc. (Greenpoint). The HELOCs, in turn, were used as collateral for the issuance of \$337 million in debt securities of varying seniority with payments dependent on, or backed by, the cash flow received from the pooled loans. Greenpoint was one of Bear Stearns' largest suppliers of loans, and the sole supplier of the loans in the Saco Trust.

The Transaction was effectuated through a series of interlocking agreements (Operative Documents), including the Mortgage Loan Purchase Agreement (MLPA), the Sale and Servicing Agreement (SSA), and the Insurance & Indemnity Agreement (I&I Agreement).

The MLPA is a sales agreement pursuant to which EMC

transferred and sold HELOCs to the purchaser, another Bear Stearns entity. The SSA provides for the administration and servicing of the HELOCs. Assured is a third party beneficiary under both the MLPA and the SSA.

Under the MLPA and the SSA, EMC made numerous representations and warranties concerning the attributes of the loans and the practices pursuant to which they were originated (Loan Warranties). The MLPA and the SSA also create a repurchase protocol (Repurchase Protocol) pursuant to which the parties to the agreement and Assured, identified thereunder as the Note Insurer, can compel EMC to repurchase HELOCs that breach the Loan Warranties (Repurchase Protocol) (MLPA § 7, 16; SSA § 2.03 [a]).

Both the MLPA and the SSA provide that the Repurchase Protocol is the "sole and exclusive" remedy available for such breaches "hereunder" (MLPA § 7 [uu]; SSA § 2.03).

EMC's commitments to Assured also appear in the Insurance and Indemnity Agreement (I&I Agreement), to which Assured is a direct party. Pursuant to the I&I Agreement, Assured agreed to issue a policy of insurance (Policy) in favor of the Transaction note holders. The I&I Agreement expressly incorporates the Loan Warranties established under the MLPA, including the exclusive remedy with respect to defective and breaching HELOCs, the Repurchase Protocol (I&I Agreement, § 2.02 [k]). The I&I Agreement also confers indemnification and reimbursement rights

to Assured (I&I Agreement, §§ 3.03 [b]; 3.04 [a]).

Beyond the Loan Warranties and indemnification and reimbursement rights, Assured maintains that the I&I Agreement affords it additional warranties and remedies not available to the other securitization participants with respect to the Transaction as a whole, which it refers to as the "transaction warranties" (Transaction Warranties).

#### Tide of Defaults

At some point in late 2007, the loans in the Saco Trust began defaulting at alarming rates. Assured re-underwrote approximately 900 of the HELOCs in the trust and alleges that EMC breached the Loan Warranties with respect to an astounding 88.5% of the loan pool. The majority of the loans in the pool have since defaulted or are seriously delinquent.

Around this time, Bear Stearns itself began aggressively shorting financial guaranty insurers including Assured, and the banks with large exposure to the securities they insured. Nonetheless, it was unable to curb its own exposure to risky mortgages, and in March 2008, Bear Stearns collapsed and was acquired by JP Morgan, with Bear Stearns thereafter merging into and with JP Morgan.

When Assured notified EMC of the 820 breaching loans in the Saco Trust and demanded repurchase under the Repurchase Protocol, EMC, at the direction of JP Morgan, refused to repurchase the

breaching loans identified by Assured. JP Morgan purportedly refused to permit EMC to comply with its obligations under the Repurchase Protocol in order to manipulate its own accounting reserves. Nonetheless, JP Morgan simultaneously asserted against Greenpoint, the originator of the loans, the identical repurchase demands that JP Morgan forced EMC to deny.

The growing tide of defaults in the loan pool in turn caused massive shortfalls in the cash flows required to pay down the securities, requiring Assured to make large payments under the Policy. Assured maintains that its cumulative losses exceed \$75 million, and that it has made more than \$43 million in unreimbursed claims payments.

#### Widespread Fraud

Assured alleges that Bear Stearns and EMC deliberately and knowingly made false statements to Assured to induce its participation in the Transaction, concealed their own knowledge that the loans contained in the Saco Trust were defective, and that the operative documents contain false warranties.

Bear Stearns purportedly acquired loans it knew were defective and sold them at a profit into securitizations before they could default. Bear Stearns purportedly knew that its underwriting due diligence was deficient, did not engage in quality control of its favored loan providers, and did not have protocols to identify and repurchase breaching loans from the

trusts.

Whistleblower testimony from former employees of Watterson Prime, a third-party due diligence firm hired by Bear Stearns to review the loans in the Saco Trust, purportedly affirm that Bear Stearns disregarded loan quality for loan quantity.

Additionally, former Greenpoint employees have come forward and purportedly testified that Greenpoint's management pressured its underwriters to approve loans regardless of quality, and that Greenpoint consistently funded and closed loans in violation of its own underwriter guidelines to maintain its relationship with favored brokers in its network.

#### Assured's Claims

Assured asserts nine causes of action against defendants, including fraudulent inducement against JP Morgan and EMC; breaches of representations and warranties against EMC, BSABS and JP Morgan; breaches of the Repurchase Protocol obligations against EMC, BSABS and JP Morgan, breaches of the I&I Agreement against EMC, BSABS and JP Morgan; indemnification against EMC, BSABS, and JP Morgan; tortious interference with contract against JP Morgan; breach of contract against EMC and BSABS arising out of the asset transfer of EMC to JPMS; and successor liability against JPMS Bank.

## Analysis

### Breach of Contract Claims

Defendants move to dismiss Assured's breach of contract claims that do not arise strictly under the Repurchase Protocol. Defendants argue that limitations on Assured's remedies contained within the MLPA and incorporated in the I&I Agreement bar contract claims which seek remedies beyond the Repurchase Protocol. In support, defendants cite to *Assured Guar. Mun. Corp. v Flagstar Bank, FSB* (2011 WL 5335566, \*11 [SD NY 2011]) (Flagstar Action).

Defendants also seek to dismiss Assured's claims for indemnification and reimbursement of attorney's fees on the ground that the applicable contractual provisions only cover claims brought by third parties against Assured, rather than litigation between the contracting parties.

In opposition, Assured argues that the "sole remedy" language of the MLPA only applies to breaches of the Loan Warranties, whereas its contract claims are premised upon EMC's breaches of Transaction Warranties, which appear in section 2 of the I&I Agreement. According to Assured, defendants' breach of the Transaction Warranties constitute an "event of default" under section 5.10 (a) of the I&I Agreement, which entitles it "in its sole judgment" to pursue "whatever action at law or in equity" available to it (I&I Agreement, § 5.02 [a] [iii]).

The Court rejects Assured's interpretation of the relevant contractual language, which is premised upon a flawed interpretation of the I&I Agreement in isolation to the MLPA. Reading the inter-locking operative documents together, as the Court must, makes it clear that the parties intended to limit Assured's remedies for breach of the representations and warranties relating to the quality and characteristics of the pooled loans to the Repurchase Protocol (see *Brax Capital Group, LLC v WinWin Gaming, Inc.*, 83 AD3d 591 [1<sup>st</sup> Dept 2011] [related set of agreements executed at the same time and related to the same subject matter are contemporaneous writings and must be read together as one]).

Assured, as Note Insurer, is expressly and specifically named in the "sole remedy" provision of the MLPA and the SSA, which states that the "Note Insurer's [Assured] ... sole and exclusive remedy under this Agreement or otherwise respecting a breach of representations or warranties hereunder with respect to the Mortgage Loans" is the Repurchase Protocol.

The Repurchase Protocol is expressly incorporated into the I&I Agreement. Although Assured is a direct party to the I&I Agreement, section 2.02 (k) of the I&I Agreement states that Assured's remedies in the event of a breach of the Loan Warranties is "limited" to the remedy specified in section 7 of the MLPA, which is the Repurchase Protocol:

[The] remedy [Repurchase Protocol] with respect to any defective HELOCs under Section 7 of the [MLPA] **shall be limited to the remedies specified** in the [MLPA] (emphasis added).

Assured argues that its additional claims for breach of contract pertain to a different set of representations and warranties, the Transaction Warranties, and that the Repurchase Protocol was not intended to address pervasive breaches of the type alleged by Assured. To this point, Assured cites to *Syncora Guarantee, Inc. v EMC Mortgage Corp.*, 2011 US Dist LEXIS 31305, \*8 [SD NY 2011], wherein Judge Crotty denied a motion for summary judgment that sought a finding that the repurchase protocol was the exclusive remedy for a monoline insurer's breach of representations claim.

*Syncora Guarantee, Inc. v EMC Mortgage Corp.* is distinguishable, as the section of the MLPA which provided that the repurchase protocol was the "sole and exclusive remedy" under the agreement for breaches of representations and warranties, did not name the note insurer, whereas it specifically named other parties to the transaction. The note insurer was a direct signatory to the I&I Agreement, which did not incorporate any of the limitations on remedies contained within the MLPA. Moreover, the SSA in *Syncora* contained a repurchase protocol that was made exclusive to various parties, but did not name the note insurer. The court determined that, had the sophisticated parties intended the note insurer to be among those excluded from the list of

parties for whom the repurchase protocol is the sole and exclusive remedy, they would have done so in the I&I Agreement (*Id.*).

In contrast, Assured is among the list of parties for whom the Repurchase Protocol is the sole and exclusive remedy in the MLPA and the SSA. Moreover, the I&I Agreement specifically provides that Assured's remedies in the event of a breach of a Loan Warranty is "limited" to the remedy (i.e. the Repurchase Protocol) of the MLPA.

Judge Rakoff reached the same conclusion in the Flagstar Action (2011 WL 5335566 at \*4-5), when he addressed nearly identical contractual language. There, the MLPA, SSA and I&I Agreement established a repurchase protocol as the "sole and exclusive remedy" available to certain parties for breaches of representation and warranties relating to defective loans, and similarly, the note insurer was specifically named therein. The court held that Assured's remedies for breach of representations and warranties relating to defective HELOCs were restricted to enforcement of the repurchase protocol.

Moreover, an examination of the complaint establishes that all of the alleged Transaction Warranties that Assured premises its additional breach of contract claims largely relate to, and overlap with, the Loan Warranties (see Complaint ¶¶ 247-249), which are specifically subject to the Repurchase Protocol under

the MLPA, the SSA and the I&I Agreement.

This Court cannot ignore the language of the parties' agreements that plainly restricts Assured to the remedy of the Repurchase Protocol to enforce EMC's obligations under the Operative Documents (see *Maxine Co. v Brinks's Global Services, USA, Inc.*, 94 AD3d 53, 56 [1<sup>st</sup> Dept 2012] [courts cannot, under the guise of interpretation, rewrite parties' agreements to impose additional terms or relieve parties from the consequences of their bargain]). Consequently, Assured is limited to the remedy of compelling EMC to repurchase defective loans that breach any representations and warranties pertaining to characteristics of the pooled loans.

Indemnification and Reimbursement Claims

Assured seeks indemnification, including past and future insurance payments, resulting from EMC's breaches of the Loan Warranties.

Section 3.04 (a) of the I&I Agreement provides:

[T]he Seller, the Issuer and the Depositor agree, jointly and severally, to pay, and to protect, indemnify and save harmless, the Insurer ... from and against any and all claims, losses ... damages, costs or expenses (...) of any nature arising out of or relating to the breach by the Seller, the Issuer or the Depositor of any of the representations or warranties contained in Section 2.01 or Section 2.05 or arising out of or relating to the transactions contemplated by the Operative Documents" (I&I Agreement, § 3.04 [a]).

The claim for contractual Indemnification against EMC is

dismissed. Section 3.04 (c) of the I&I Agreement plainly limits Assured's indemnity rights to losses that relate solely to third party claims insofar as the provision refers to "actions or proceedings asserted **against**" Assured (emphasis added). Section 3.04 (c) provides:

"If any action or proceeding (...) shall be brought or asserted **against** any Person (individually, an "Indemnified Party" ...) in respect of which the indemnity provided in Section 3.04 (a) ... may be sought from the .... Insurer [Assured] ... hereunder, each such Indemnified Party shall promptly notify the Indemnifying Party" (emphasis added).

Although Assured attempts to characterize its claim as arising out of third party claims, it is plainly seeking coverage for its own losses, i.e. repayment of insurance claims payments that it is pursuing on its own behalf. Such claims are classic first party claims and beyond the contemplation of the indemnification provision, which is subject to strict interpretation (*Hooper Assocs., Ltd. v AGS Computers, Inc.*, 74 NY2d 487, 491 [1989]; *Cahn v Ward Trucking, Inc.*, 101 AD3d 458, 458 [1<sup>st</sup> Dept 2012]).

Moreover, seeking repayment of insurance claims payments that Assured made and/or will make in the future to note holders as a result of purported breaches of the Loan Warranties runs afoul of the Repurchase Protocol, which plainly limits Assured's remedies in the event of a breach (*accord Assured Guar. Mun. Corp. Flagstar Bank, FSB*, 2011 WL 5335566 at \*5).

Assured also seeks reimbursement of its attorneys' fees and

costs incurred in this action under various provisions of the I&I Agreement. In support, Assured cites to a recent decision in the Flagstar Action (Flagstar II), wherein Judge Rakoff permitted the plaintiff-insurer's reimbursement claim to proceed, notwithstanding his earlier dismissal of an indemnification claim, in part, due to the exclusivity of remedies of the repurchase protocol (*Assured Guar. Mun. Corp. v Flagstar Bank, FSB*, \_F Supp 2d\_, 2013 WL 440114, \*40 [SD NY 2013]).

Section 3.03 (b) of the I&I Agreement provides that EMC,

[A]grees to pay the Insurer [Assured] and the Insurer shall be entitled to reimbursement from the Seller [EMC] and shall have full recourse against the Seller for, (I) any payment made under the Policy arising as a result of the Seller's failure to substitute for or deposit an amount in respect of any defective Mortgage Loan as required pursuant to Section 5 of the "MLPA.

Further, section 3.01 (c) of the I&I Agreement provides that EMC,

[A]grees to pay to the Insurer any and all charges, fees, costs and expenses that the Insurer may reasonably pay or incur, including reasonable attorneys' and accountants' fees and expenses, in connection with (I) the enforcement, defense or preservation of any rights in respect of any of the Operative Documents, including defending ... or participating in any litigation ... relating to any of the Operative Documents.

Under the plain import of these provisions, Assured possesses a clear contractual right to recover from EMC its reasonable attorneys' fees and costs incurred in relation to its initial demands under the Repurchase Protocol and its current

claim for breach of this (accord *Assured Guar. Mun. Corp.*, 2013 WL 440114 at \*40). Contrary to defendants' assertion, the reimbursement provision at issue in *Flagstar II* is nearly identical to the one at issue set forth in this action.

*Tortious Interference*

In its seventh claim for tortious interference with contract, Assured alleges that JPMS committed accounting fraud and forced EMC to pursue a bad-faith litigation strategy of denying loan repurchase demands that EMC itself believed to be valid, thereby interfering with EMC's contractual obligation to abide by the Repurchase Protocol by curing, repurchasing, or substituting allegedly defective loans that breached the Loan Warranties.

To plead a claim of tortious interference with contract, a plaintiff must allege the existence of a valid contract, defendant's knowledge thereof, the defendant's intentional procurement of a breach, and damages (*Katzap v Knickerbocker Village, Inc.*, 100 AD3d 423 [1<sup>st</sup> Dept 2012]).

Defendants move to dismiss this claim on the ground that, to the extent that Assured claims that JPMS is directly liable as successor to its alter ego Bear Stearns, a party cannot interfere with its own contract. Further, defendants assert that, even apart from Assured's own alter ego allegations, under New York law, it is privileged to interfere with a related entity's

[EMC's] contract, and to this extent, is protected by the economic interest exception. According to defendants, where the third party's actions were financially motivated, a plaintiff must allege illegal means or malice, which Assured fails to allege with requisite particularity.

First, it is well-settled that a plaintiff is entitled to plead in the alternative (*Lemle v Lemle*, 92 AD3d 494 [1<sup>st</sup> Dept 2012]). To this extent, if JPMS is not an alter ego of its predecessor, Bear Stearns, JMPS would be considered a stranger to the operative documents that were allegedly breached.

Moreover, where the alleged interference is with an existing contract, rather than with a prospective economic relationship, it is not necessary to allege that the defendant used improper means or that its conduct was for the sole purpose of harming the plaintiff (*Carvel Corp. v Noonan*, 3 NY2d 182, 189-90 [2004]; *Shared Communications Services of ESR, Inc. v Goldman Sachs & Co.*, 23 AD3d 162 [1<sup>st</sup> Dept 2005]). Consequently, this Court rejects defendants' assertion that Assured's claim for tortious interference with contract must contain particularized allegations that JPMS acted with illegal means or malice.

Assured's pleadings set forth a cognizable claim for tortious interference with contract against JPMS. Defendants have not established the applicability of the defense of economic justification as a matter of law that would warrant dismissal at

the pleading stage.

In its eighth claim against EMC and BSABS for breach of contract, Assured alleges that EMC transferred assets to JPMS without Assured's consent in violation of the I&I Agreement, and left EMC as a shell without the ability to satisfy its ongoing contractual obligations to Assured.

Defendants argue that this claim is not viable because Assured fails to allege the requisite element of damage. The Court agrees. Damages may not be merely speculative, possible or imaginary, but must be reasonably certain and directly traceable to a breach of contract (*Lloyd v Town of Wheatfield*, 67 NY2d 809 [1986]).

The possibility that EMC was left without the financial ability to satisfy its contractual obligations is uncertain and, at best, premature. Because Assured has failed to allege that it has sustained actual, as opposed to potential, damages flowing from the alleged breach, dismissal of this claim is in order.

Accordingly, it is hereby

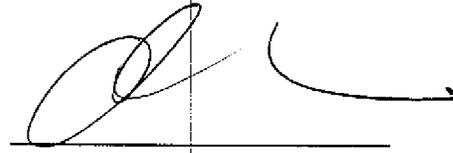
ORDERED that defendants' motion to dismiss is granted, in part, and denied, in part, and the second, fourth, fifth, and sixth causes of action are hereby severed and dismissed; and it is further

ORDERED that defendants are directed to serve an answer within 20 days after service of a copy of this order with notice

of entry.

Dated: April 4, 2013

ENTER:

A handwritten signature in black ink, consisting of a large, stylized initial 'C' followed by a surname that is partially obscured by a vertical line. The signature is written above a horizontal line.

J.S.C.

**HON. CHARLES E. RAMOS**