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

PRESENT: Hon. Doris Ling-Cohan PART 36

Index Number : 600714/2007

DLJ MORTGAGE CAPITAL

VS.

FAIRMONT FUNDING LTD.

SEQUENCE NUMBER : 005

SUMMARY JUDGMENT

INDEX NO. _____

MOTION DATE _____

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

This motion to/for summary judgment

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	1, 2, 3, 4, 5, 6
Answering Affidavits — Exhibits	7
Replying Affidavits	8

Cross-Motion: ☐ Yes ☑ No

Upon the foregoing papers, it is ordered that this motion for summary judgment by plaintiff is granted in accordance with the attached memorandum decision.

FILED
JUL 16 2009
COUNTY CLERK'S OFFICE
NEW YORK

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

Dated: 7/15/09

HON. DORIS LING-COHAN

J.S.C.

Check one: ☑ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☑ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 36

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DLJ MORTGAGE CAPITAL, INC.,

Index No. 600714/07

Plaintiff,

- against -

Motion Seq. No.: 005

FAIRMONT FUNDING, LTD.,

Defendant.

LING-COHAN, J.:

Plaintiff DLJ Mortgage Capital, Inc. moves for summary judgment on liability.

Plaintiff is a purchaser of mortgage loans. Defendant Fairmont Funding, Ltd. is a mortgage lender that originates mortgages. On July 1, 2000, the parties entered into the Seller's Purchase, Warranties and Interim Servicing Agreement (Purchase Agreement), whereby defendant would originate mortgage loans and sell them to plaintiff. On May 1, 2006, they entered into another very similar Purchase Agreement; both agreements will be referred to in the singular.

The Purchase Agreement did not compel plaintiff to buy or defendant to sell any mortgages. Before deciding whether to buy a mortgage from defendant, plaintiff analyzed it and sometimes decided not to buy it. When plaintiff did buy a mortgage, defendant could be compelled to buy it back under certain conditions. In section 3.05 of the Purchase Agreement, defendant agreed to repurchase mortgage loans where the borrower failed to make the mortgage payment due within the first three months of the closing date of the mortgage (early payment default mortages, hereinafter EPDs). Under section 8.01 of the agreement, defendant agreed to

indemnify plaintiff for legal fees and other expenses and losses that arose from defendant's failure to comply with the terms of the agreement.

Between July 2005 and February 2007, plaintiff allegedly repeatedly requested that defendant buy back EPDs and defendant did not. Plaintiff commenced this action seeking to have defendant repurchase EPDs for $19.5 million. Plaintiff moves for summary judgment on liability on the EPDs and for indemnification.

The following account of events derives from defendant's affidavits. According to defendant, the Purchase Agreement was made at a time when the standards for giving mortgages to borrowers was conservative and lenders were more cautious than they were to become in the future. Until 2000, defendant alleges, there were few EPDs, and those few were generally not resolved by repurchase, but in other ways. Defendant was rarely required to repurchase a loan.

In 2000, the mortgage market underwent a radical change. Mortgages became less conservative and more risky. Defendant alleges that mortgage investors, such as plaintiff, liberalized the requirements for giving mortgages by, among other things, no longer requiring down payments, certain kinds of documentation, or unimpaired credit histories. Defendant alleges that plaintiff and other mortgage investors dictated the terms of the mortgages that defendant sold. Plaintiff published detailed guidelines setting forth the terms of the mortgages they would buy, including down payment percentage, length, borrower creditworthiness, documentation, and other provisions. Defendant alleges that the new liberalized standards for giving mortgages became the norm in the market and that an originator not offering them could not remain in business. Defendant changed its mortgages to conform to plaintiff's guidelines.

In 2000, defendant had a net worth of $3 million and no substantial cash reserve. In

2002, the number of EPDs sharply increased, totaling over $2 million by 2003. Defendant explained to plaintiff that it could not repurchase the EPDs because of its limited net worth and the unprecedented volume of EPDs. Plaintiff knew that defendant did not have the cash to buy back the EPDs. Plaintiff began subsidizing defendants' buy backs through the use of special bonuses and incentives.

Plaintiff agreed to accept $480,000 in full settlement of the then extant $2 million worth of EPDs, and paid defendant a bonus large enough to almost extinguish defendants' debt on those EPDs. The settlement is recorded in a July 15, 2003 e-mail from plaintiff to defendant (Defendant's Ex. C). Defendant alleges that the settlement was an incentive for defendant to continue selling mortgages to plaintiff. Plaintiff continued to pursue defendant's business aggressively, despite knowing that defendant could not buy back the EPDs.

By July 2004, the EPDs totaled $2.6 million. On July 30, 2004, the parties entered into a written letter agreement whereby the EPDs would be extinguished by defendant paying a total of $563,238 to plaintiff (Defendant's Ex. D). Plaintiff agreed to pay defendant certain bonuses based upon future volume of mortgages and other factors.

At a meeting on December 20, 2004, by which time the EPDs were worth over $4.5 million, plaintiff complained to defendant about the increasing number of EPDs. Plaintiff told defendant that plaintiff's risk analysis established that the EPD risk on the new mortgage types crafted by plaintiff was nearly the same as the negligible EPD risk for conventional mortgages. Defendant stated that it could not afford to buy back $4.5 million worth of EPDs, given that its net worth was now $5 million, and that plaintiff knew this when it bought the mortgages. Plaintiff agreed that defendant could not repurchase and discussed other ways to resolve the

EPDs. On April 6, 2005, the parties entered into a second letter agreement whereby defendant paid plaintiff $346,830 to resolve the EPDs then outstanding (Ex. E). Plaintiff subsidized this payment in the form of higher payments for future business and bonuses.

In 2005, plaintiff purchased approximately $180 million in mortgages from defendant. The purchases required plaintiff to raise defendant's credit limit. At that time defendant's net worth was still $5 million.

In late 2005, the EPDs reached a value of more than $4.5 million. At a meeting on November 22, 2005, defendant reiterated that it could not repurchase the EPDs and that plaintiff had given up the right to seek repurchases. Plaintiff agreed and, on December 9, 2005, the parties resolved over $2 million in EPDs by a third letter agreement (Defendant's Ex. F). Defendant would pay $266,040 over a period of months, with plaintiff subsidizing the payment. The other $2.5 million in EPDs was resolved by defendant with no expenditure of money.

By January 2006, the EPDs were worth more than $5 million. During the year, the EPDs rose to $15 million. When the parties met in late 2006, defendant learned for the first time that plaintiff had run risk analysis studies which established that the EPD risk was higher for the new types of mortgages than for conventional mortgages, and that plaintiff concealed this information from defendant from 2003 through most of 2006. The parties did not come to any resolutions of the EPDs, which reached $20 million in the following months.

An e-mail dated April 27, 2006, from plaintiff to defendant, seeks not to let "outstanding balances linger and become stale ... balloon and spiral out of control" (Defendant's Ex. R). The e-mail suggests resolving the EPDs and states "[p]lease let me know what you think, as management has agreed to allow this ..." (*id.*).

A September 20, 2006 e-mail from plaintiff to defendant states: "[o]nce again, as always, we are not asking you to buy back all loans, but we need to come to an agreement, plan, and get some semblance of a financial contribution from [defendant] ... in order to keep working forward" (Defendant's Ex. A).

A January 9, 2007 e-mail from plaintiff to defendant announces the attachment of a document containing the "proposed terms of a payment plan to cover all outstanding repurchase obligations" (Defendant's Ex. R). "We have drafted this document taking into consideration our discussion of December and bearing in mind your past success in resolving problem loans. Please review and advise your comments" (*id.*). However, the parties did not reach any agreement.

The mood on Wall Street had changed. Defendant alleges that plaintiff withdrew from the mortgage business in spring 2007 and that it became very anxious about the EPDs. Plaintiff demanded full repurchase and did not offer subsidies. Defendant alleges that, if plaintiff believed it had the right to demand repurchases, plaintiff would have closed defendant's account when it became clear that defendant could not repurchase. Instead, plaintiff continued to aggressively pursue defendant's business despite the increasing numbers of EPDs, and expanded defendant's credit line in order to increase its volume of business with defendant. By these actions, defendant argues that plaintiff waived its right to demand repurchases. Defendant also contends that plaintiff should be estopped from demanding repurchases.

The complaint contains two causes of action, for breach of contract and indemnification. Relevant to the parties' arguments are sections 9.02 and 12.02, respectively, of the Purchase Agreement, which provide that any waivers or amendments to the agreement must be in writing.

Section 12.15 of the Purchase Agreement states that it is the entire understanding between the parties, and that they made no representations, agreements, or promises other than those in the agreement. Each of the three letter agreements resolving EPDs provides that, so long as the letter agreement is complied with, defendant is not obligated to repurchase the loans that are the subject of the agreements. The last section of each letter agreement provides that it is without prejudice to plaintiff's rights and remedies under the Purchase Agreement with regard to any event of default, except as described in the letter agreement, and that it should not be construed as a waiver of those rights and remedies. Each letter agreement states that plaintiff reserves all of the rights and remedies available to it under the Purchase Agreement.

Plaintiff establishes a prima facie case for summary judgment on its breach of contract claim (*see e.g. Alvarez v Prospect Hosp.*, 68 NY2d 320, 325 [1986]). Plaintiff alleges that the Purchase Agreement obligated defendant to repurchase EPDs, that plaintiff demanded defendant repurchase them, and that defendant refused. Defendant seeks to raise issues of fact concerning waiver and estoppel.

A party waives a right under an agreement by voluntarily and intentionally abandoning the enforcement of that right (*General Motors Acceptance Corp. v Clifton-Fine Cent. School Dist.*, 85 NY2d 232, 236 [1995]). "Waiver may be established by affirmative conduct or by failure to act so as to evince an intent not to claim a purported advantage" (*id.*). Waiver of a contract right requires a "clear manifestation of an intent by plaintiff to relinquish her known right" and "mere silence, oversight or thoughtlessness in failing to object" to a breach will not support a finding of waiver (*Courtney-Clarke v Rizzoli Intl. Publs.*, 251 AD2d 13, 13 [1st Dept 1998]).

Although the general rule is that clauses in a written agreement prohibiting oral waivers or modifications will be enforced (*99 Realty Co. v Eikenberry,* 242 AD2d 215, 215 [1st Dept 1997]), there are exceptions. A party to a written agreement may orally waive enforcement of one of its terms despite a provision to the contrary (*Taylor v Blaylock & Partners,* 240 AD2d 289, 290 [1st Dept 1997]). The inclusion of a merger clause in an instrument is no bar to waiver because "'a contractual provision against oral modification may itself be waived'" (*Madison Ave. Leasehold, LLC v Madison Bentley Assoc., LLC,* 30 AD3d 1, 6 [1st Dept], *affd* 8 NY3d 59 [2006], quoting *Rose v Spa Realty Assoc.,* 42 NY2d 338, 343 [1977]). "Such waiver may be evinced by words or conduct, including partial performance" (*Bank Leumi Trust Co. of N.Y. v Block 3102 Corp.,* 180 AD2d 588, 590 [1st Dept 1992]).

On four occasions, plaintiff waived its right under the Purchase Agreement that defendant repurchase the EPDs and made other agreements. The first waiver was memorialized in an e-mail and the others in letter agreements. As shown by the September 2006 and January 2007 e-mails, another agreement was contemplated but unrealized. Each completed letter agreement concerns the EPDs that are the subject of the agreement and expressly does not apply to other EPDs or EPDs in the future. Such agreements demonstrate that plaintiff did not waive the requirement of a writing to waive or modify the Purchase Agreement. Even if the e-mail concerning the first waiver is regarded as an agreement, it was not properly memorialized and was a one-time event. Thereafter, the waivers or modifications were put in writing, as shown by defendant's version of events. Defendant's allegations do not amount to any cogent assertion that plaintiff orally waived the repurchase provision or that plaintiff agreed that it would always waive the repurchase provision. Nor does defendant establish that plaintiff waived its rights

under the letter agreements. Each letter agreement provides that it does not constitute a waiver of plaintiff's rights under the Purchase Agreement.

Waiver is unilateral on the part of the waiving party (*id.*). As waiver does not create a binding agreement; it can be withdrawn, provided that the party whose performance has been waived is given notice of withdrawal (*id.*). In this case, each waiver, by its terms, was a discrete event that did not promise another waiver.

Also militating against defendant's assertion of waiver is the fact that, in May 2006, after several years of plaintiff allegedly waiving the repurchase provision in the first Purchase Agreement, the parties entered into the second Purchase Agreement. The second agreement contains the same repurchase provision as the first agreement made in 2000.

The parties' communications do not raise an issue of fact concerning waiver. The April and September 2006 e-mails, at most, indicate that plaintiff was willing to work out another agreement, similar to the others that resolved some EPDs. An August 30, 2002 memorandum by plaintiff states that defendant does not have the cash to pay off 100% of the buy backs, and suggests establishing a reserve fund for the buy backs (Defendant's Ex. B); this plan, however, was never realized. A February 10, 2004 email by defendant to plaintiff asks about plaintiff's plan to resolve certain EPDs (Defendant's Ex. G). Plaintiff responds to defendant asking for more information about those loans (*id.*). These documents do not indicate a waiver of all repurchases.

Enforcement of a written agreement may also be blocked where a party has orally modified the written agreement, and another party has partly performed that modification (*Rose,* 42 NY2d at 344). The performing party seeks to enforce the oral modification. The doctrine of

estoppel may also serve to block enforcement of a written agreement (*id.* [noting that estoppel is "[a]nalytically distinct" from partial performance]). Estoppel is established where one party to a written contract makes representations that modify the contract and the other party relies to its detriment upon the representations (*id.*). The party making the representations is estopped from enforcing the contract as written (*id.*).

A party arguing that partial performance or estoppel should prevent enforcement of a contract must demonstrate that its actions were "unequivocally referable" to the new, oral agreement or the alleged representations upon which it relied (*id.* at 343-344). It is not enough that the proponent's conduct be consistent with the alleged modification; the conduct must be inconsistent with any other explanation (*Richardson & Lucas, Inc. v New York Athletic Club of City of New York,* 304 AD2d 462, 462 [1st Dept 2003]; *SAA-A, Inc. v Morgan Stanley Dean Witter & Co.,* 281 AD2d 201, 203 [1st Dept 2001]).

In this instance, defendant's conduct of continuing to sell mortgages to plaintiff was consistent with the written Purchase Agreement. Defendant thus cannot establish that it changed its conduct because of an oral modification or representations. Neither partial performance, nor estoppel, are available to block enforcement of the written agreement. It is also noted that defendant fails to clearly allege any detrimental reliance. Defendant states that plaintiff misrepresented the risk of the new mortgages. Defendant does not claim, however, that it was thus induced to originate and sell these mortgages, or that it would not have sold them but for such representations or that it had no way of evaluating the new mortgages by itself (assuming that such allegations would demonstrate detrimental reliance). Defendant also alleges that plaintiff knew that defendant could not afford to repurchase the EPDs. However, the parties'

agreement, which governed their relationship, provided that defendant would repurchase.

Defendant's next objection to the motion is that plaintiff fails to prove that the mortgages that are the subject of this litigation are EPDs. An EPD occurs when the borrower defaults on the first, second, or third mortgage payment. Defendant objects that plaintiff does not sufficiently prove that the defaults happened at the proper time.

Attached to plaintiff's moving affidavits are documents that purportedly show such defaults. The documents, however, do not clearly show when the defaults occurred; more explication of the documents is needed. Nonetheless, for the purposes of summary judgment on liability, plaintiff's allegations are sufficient. Plaintiff shows that there are EPDs and that defendant is obligated to repurchase them. Plaintiff also states that since this action began, it sold some of the EPDs in order to mitigate its damages. Therefore, the final amount of damages will differ from that sought in the complaint. In addition, plaintiff establishes that it is entitled to indemnification for costs and fees resulting from this litigation.

Defendant argues that, since the complaint seeks specific performance, and does not ask for any other kind of damages, the motion should be denied. However, the fact that the complaint prays only for specific performance is no ban to damages (*see Lusker v Tannen,* 90 AD2d 118, 124 [1st Dept 1982]). Also, the complaint clearly contains a cause of action for breach of contract seeking monetary damages. [Exh. S, Exhibits to Memorandum of Law].

Defendant's memorandum of law mentions a cross motion but no notice of motion was filed. As defendant fails to raise any issues of fact regarding plaintiff's entitlement to have the EPDs repurchased, plaintiff's motion for summary judgment on liability is granted.

Accordingly, it is

ORDERED that plaintiff's motion for summary judgment on liability on its causes of action for breach of contract and indemnification is granted; and it is further

ORDERED that the assessment of damages shall be determined by a hearing before a Special Referee, as permitted by CPLR 4317 (b), provided that, within 45 days of entry of this order plaintiff serves a copy of this order with notice of entry, together with a completed Information Sheet, upon the Special Referee Clerk in the Motion Support Office (Room 119), who is directed to place this matter on the calendar of the Special Referee's Part (Part 50 R) for the earliest convenient date; failure to timely comply with this order, will be deemed a waiver of plaintiff's claim, and will warrant a dismissal of this case; and it is further

ORDERED that upon the rendering of the assessment, plaintiff shall recover judgment against defendant in the sum for which the damages are determined by the Special Referee, together with the costs and disbursements of the action to be taxed by the Clerk of the Court, and the Clerk of this Court is directed to enter judgment in favor of plaintiff and against defendant for that sum with interest, and costs of this action as taxed.

Date: 7/15/09

Hon. Doris Ling-Cohan, J.S.C.

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