SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 45

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SYNCORA GUARANTEE INC.,

Plaintiff,

-against-

ALINDA CAPITAL PARTNERS LLC, AMERICAN ROADS LLC, MACQUARIE SECURITIES (USA) INC., and JOHN S. LAXMI,

Defendants.

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**DECISION AND ORDER**

Index No. 651258/2012

Mot. Seq. 006

**HON. ANIL C. SINGH, J.:**

In this action for, *inter alia*, fraud and negligent misrepresentation, Syncora Guarantee Inc. ("Syncora" or "plaintiff"), alleges that Macquarie Capital (USA) Inc. (f/k/a Macquarie Securities (USA) Inc.) ("Macquarie" or "defendant") knowingly misled plaintiff into insuring financing for certain toll road properties through misrepresentations about future traffic projections. Defendant seeks to dismiss plaintiff's amended complaint ("Compl.") pursuant to CPLR §§ 3211(a)(1) and (a)(7) (mot. seq. 006). Plaintiff opposes.

## Facts

Syncora "is a monoline financial guaranty insurance provider that provides credit enhancement for the obligations of debt issuers worldwide." Compl. ¶18. In

exchange for issuing an insurance policy, Syncora receives premiums from the issuer of the obligation. Id. ¶19. In determining whether to issue a policy in any given case, Syncora would consider a number of factors including the credit strength of the issuer, sources of income, type of issue and the available revenue sources and expected revenue amounts. Id. Additionally, Syncora would rely upon information from the structuring banks and issuers in assessing the structure of the proposed debt obligation and the nature and credit quality of the underlying assets. Id. ¶20.

In or around November 2005, Macquarie approached Syncora proposing that Syncora insure a proposed bond issuance in connection with the acquisition and refinancing of regional toll road assets and provide credit protection on interest rate hedging swaps that Macquarie planned to enter into in connection with the bonds. Id. ¶21. Macquarie is a part of the corporate advisory arm of the Macquarie Group. Id. ¶22. In 2006, Macquarie purchased five toll roads through Macquarie Small Cap Roads LLC, which eventually came to be known as American Roads. Id. ¶¶23, 27. Macquarie eventually sold American Roads to Alinda Capital Partners LLC ("Alinda"), a third party investment firm. Id. ¶39.

In order to assure Syncora that American Roads toll assets would provide adequate debt service, Macquarie "procured traffic and revenue forecast reports from its traffic advisor, Maunsell, for each of the facilities in the American Roads' portfolio." Id. ¶32. These projections allegedly showed that the portfolio would

experience increased revenue based upon a projected increase in the amount of traffic on these roads. Id. ¶4. Macquarie also retained Wilbur Smith as an additional consultant in order to perform an audit of Maunsell's work.

Plaintiff asserts that the projections Macquarie provided were grossly misleading and based upon manipulated data in order to misrepresent American Roads revenues to ensure its coverage. Relying on these projections, Syncora issued financial guaranty insurance policies on the bonds, with the bondholders as the ultimate beneficiaries. Id. ¶¶45-46. Additionally, Syncora entered into two financial guaranty insurance policies with Citibank, N.A., insuring American Roads payments on two interest-rate hedging swaps, with Syncora guaranteeing the fixed payments owed by American Roads to its swap counterparty. Id. ¶47.

Relevant to this motion, Syncora collected premiums on this policy from December 2006 through March 2013. See Coyle Aff., Ex. 2, Ex. B. Macquarie contends that Syncora was made aware of the alleged misrepresentation when an article published in The Monthly in July 2007 wrote "about another commentator's 'disquiet at Macquarie's practice of paying [Maunsell] success fees', quoting a former Macquarie employee as describing the practice as 'ridiculous.'" Coyle Aff., Ex. 2, No. 8. Macquarie also alleges that Syncora became aware that Macquarie had made false representations in connection with the policy in mid-2009 and continued to receive nearly $10 million worth of premium payments until March 2013. See

Coyle Aff., Ex. 3, No. 1; Coyle Aff., Ex. 2, Ex. B. According to Macquarie, Syncora learned of the alleged misrepresentation as late as mid-2009 and yet still continued to collect premiums through March 2013.

In 2012, Syncora filed a complaint alleging that Macquarie paid success fees to Maunsell regarding the future revenue projections on the toll roads. Syncora Guarantee Inc. v. Alinda Capital Partners LLC, No. 651258/2012 (Dkt. No. 5). Macquarie's motion to dismiss the complaint was denied. Syncora has collected $42 million in premiums since inception, $10 million after learning of Macquarie's alleged wrongdoing in 2009, $2.5 million worth of premium payments on the American Roads policy after the filing of the summons, and $600,000 four days after Syncora's complaint was filed. See Oral Argument Tr. 4-5. By 2013, American Roads filed for bankruptcy, allegedly based upon their inability to match the projections provided by Macquarie. As a result of this bankruptcy, Syncora is paying the outstanding bonds based upon its guaranty policies.

In March 2016, Syncora filed an amended complaint alleging fraud and negligent misrepresentation seeking rescissory, compensatory and punitive damages on the policy based upon the alleged misrepresentations made by Macquarie. See Compl., pp. 38-41. According to Macquarie, Syncora is estopped from claiming rescissory damages on the basis that after learning of the alleged misrepresentation,

Syncora continued to receive premium payments on the policy thereby waiving their claim for damages.

**Analysis**

On a motion to dismiss a complaint for failure to state a cause of action, all factual allegations must be accepted as truthful, the complaint must be construed in the light most favorable to plaintiffs, and plaintiffs must be given the benefit of all reasonable inferences. Allianz Underwriters Ins. Co. v. Landmark Ins. Co., 13 A.D.3d 172, 174 (1st Dept 2004). The court determines only whether the facts as alleged fit within any cognizable legal theory. Leon v. Martinez, 84 N.Y.2d 83, 87-88 (1994). The court must deny a motion to dismiss, "if, from the pleadings four corners, factual allegations are discerned which, taken together, manifest any cause of action cognizable at law." 511 West 232nd Owners Corp. v. Jennifer Realty Co., 98 N.Y.2d 144, 152 (2002).

"[N]evertheless, allegations consisting of bare legal conclusions, as well as factual claims either inherently incredible or contradicted by documentary evidence, are not entitled to such consideration." Quatrochi v. Citibank, N.A., 210 A.D.2d 53, 53 (1st Dept 1994) (internal citation omitted).

On a motion to dismiss on the ground that defenses are founded upon documentary evidence, the evidence must be unambiguous, authentic, and undeniable. CPLR 3211(a)(1); Fountanetta v. Doe, 73 A.D.3d 78 (2d Dept 2010).

"To succeed on a [CPLR 3211(a)(1)] motion ... a defendant must show that the documentary evidence upon which the motion is predicated resolves all factual issues as a matter of law and definitively disposes of the plaintiff's claim." Ozdemir v. Caithness Corp., 285 A.D.2d 961, 963 (2d Dept 2001), leave to appeal denied 97 N.Y.2d 605. Alternatively, "documentary evidence [must] utterly refute plaintiff's factual allegations, conclusively establishing a defense as a matter of law." Goshen v. Mutual Life Ins. Co. of New York, 98 N.Y.2d 314, 326 (2002).

Macquarie's motion to dismiss plaintiff's first and second causes of action for fraud and negligent misrepresentation is denied except for dismissing the claim for rescissory and punitive damages. Macquarie alleges that Syncora's admission that it accepted premium payments after learning of Macquarie's alleged misrepresentations precludes their fraud and negligent misrepresentation claims, as a matter of law.

Generally, an insurer may waive the right to rescind based upon misrepresentation. However, an insurer that fails to timely rescind upon learning of a misrepresentation sufficient to give it grounds to do so, waives its rights to rescission,

> New York law is crystal clear on this point – when an insurer seeks to rescind a contract...based on misrepresentations by the insured, it must promptly disaffirm the contract upon learning of the misrepresentations – and certainly it may not continue to derive benefit under it.

National Grange Mut. Ins. Co., Inc. v. Judson Const., Inc., 931 F.Supp.2d 373, 382-83 (D. Conn. 2013) quoting GuideOne Specialty Mut. Ins. Co. v. Congregation Adas Yereim, 593 F.Supp.2d 471, 483 (E.D.N.Y. 2009); see also United States Life Ins. Co. in the City of N.Y. v. Blumenfeld, 92 A.D.3d 487 (1st Dept 2012) ("Blumenfeld I").

The First Department clearly holds that "an insurer's failure to rescind a policy promptly after obtaining sufficient knowledge of alleged misrepresentations by an insured constitutes ratification of the policy." Blumenfeld I, 92 A.D.3d at 488. "An insurer's attempt to reserve its rights while accepting premiums is unenforceable for lack of mutuality." Id. at 489; see also Continental Ins. Co. v. Helmsley Enters., 211 A.D.2d 589 (1st Dept 1995).

Accordingly, Syncora cannot seek rescissory damages to alleviate itself of the obligations under the insurance contract based upon the alleged wrongdoing of defendant when it was aware of the wrongdoing at the time that Syncora accepted and continued to derive benefit from the receipt of premiums under the policy. Syncora argues that Macquarie is not the insured, has no policy with Syncora, and has not paid any premiums to Syncora. Additionally, the beneficiary of the bonds was a trustee for the bondholders, and the beneficiary on the swap was the swap counterparty. Therefore, according to Syncora, even if the policy was ratified

through Syncora's acceptance of payments after learning of the breach, there was no ratification as to Macquarie and therefore no 'lack of mutuality' under the case law.

Although reversed on other grounds, this court finds the ruling in Assured Guar. Mun. Corp. v. DLJ Mortg. Capital, Inc., 37 Misc.3d 1212(A) (Sup. Ct. N.Y. Cnty. 2012), persuasive. In DLJ, the court dealt with a similar issue as is presented here. DLJ assembled a pool of residential mortgage loans and transferred them to Credit Suisse First Boston Mortgage Securities Corp. Id. at *1. Credit Suisse then assigned these loans to a trust. Id. Subsequently, these loans were insured. Before each transaction Credit Suisse and DLJ entered into a PSA in which the insurers were third-party beneficiaries, but not signatories. Id. at *2. After certain closings of these loans, there were a large numbers of delinquencies and the insurers brought suit against DLJ for, among other things, rescission. The court held that,

> As a result of [the insurers]' acceptance of premiums after their knowledge of the alleged breach, Plaintiffs are estopped from rescinding the Policies and from obtaining the equivalent of rescission in the form of rescissory damages. It is undisputed that the Insurers are still accepting premiums. Their argument that the rule is inapplicable because the Trusts pay the premiums is not supported by citation to authority...the rule focuses on the insurer's conduct-acceptance of premiums-not on who pays them.

Id. at *7; see also CIFG Assur. N. Am., Inc. v. Bank of Am., N.A., 41 Misc. 3d 1203(A) (Sup. Ct. N.Y. Cnty. 2013) (plaintiff "waived the right to rescind the

policies or recover recessionary damages because it has continued to accept premiums after learning of an event allowing for termination of the policy.").

Here, the focus must be on the insurer's conduct and not whether Macquarie is the insured or a third-party. Plaintiff does not deny that they continued to receive payments on the policy after they learned about the alleged gross misstatements made by Macquarie. As such, Syncora is barred from receiving rescissory damages.

Next, Macquarie alleges that under Section 3105 of the Insurance Law, the only remedy is rescission, and since rescission is unavailable, Syncora is precluded from seeking damages under 3105. The statute at issue states,

> No misrepresentation *shall avoid any contract of insurance or defeat recovery thereunder* unless such misrepresentation was material. No misrepresentation shall be deemed material unless knowledge by the insurer of the facts misrepresented would have led to a refusal by the insurer to make such contract.

Insurance Law §3105(b)(1) (emphasis added).

Macquarie argues that this is a consumer protection statute. See Gluck v. Exec. Risk Indem., Inc., 680 F.Supp.2d 406, 418 (E.D.N.Y. 2010) ("the purpose behind the materiality provision was to stop an insurer from ex post disclaiming an insurance contract, which provide to be a bad deal only in hindsight, by nitpicking the insurance application for minor misrepresentations unrelated to the claim for which coverage was being sought"). However, the First Department is clear that

Section 3105 may indeed apply to monoline insurers seeking non-rescissionary recoveries. The First Department held,

> Although the Insurance Law provides for 'avoiding' an insurance policy (or rescission), it also mentions 'defeating recovery thereunder" which, logically, means something other than rescission. Neither defendants, nor the federal cases on which they rely explain why 'defeating recovery thereunder' cannot refer to the recovery of payments made pursuant to an insurance policy without resort to rescission.

MBIA Ins. Corp. v. Countrywide Home Loans, Inc., 105 A.D.3d 412, 412 (1st Dept 2013); see also Ambac Assur. Corp. v. Countrywide Home Loans, Inc., 2016 WL 7374210, at *15-17 (Sup. Ct. N.Y. Cnty. 2016) (holding that even if rescissory damages are unavailable to a monoline insurer, subsequent damages can be sought pursuant to a claim of material misrepresentation or fraud in the inducement of an insurance contract under Section 3105).

Additionally, Macquarie relies upon the same cases which the First Department in MBIA explicitly states are contradicted by the Southern District. Id. at 412-413 (Defendants rely upon GuideOne Specialty Mut. Ins. Co. v. Congregation Adas Yereim, 593 F.Supp.2d 471 (E.D.N.Y. 2009) and Gluck v. Executive Risk Indem., Inc., 680 F.Supp.2d 406 (E.D.N.Y. 2010) which does not explain why defeating recovery thereunder cannot refer to the recovery of payments made without resort to rescission and are "flatly contradicted by two [cases] from the Southern District of New York (Syncora Guar. Inc. v. EMC Mtge. Corp., 874

F.Supp.2d 328 (S.D.N.Y. 2012)...Assured Guar. Mun. Corp. v. Flagstar Bank, FSB, 892 F.Supp.2d 596 (SD.N.Y. 2012)."). Accordingly, Macquarie's reliance on this line of cases is without merit.

Macquarie responds by stating that MBIA only stands for the proposition that an affirmative claim tantamount to 'defeat recovery thereunder' would be a claim for rescissory damages and points to the lower court's decision in MBIA as evidence that the only claim at issue was one for rescissory and not compensatory damages. However, "the clearest indicator of legislative intent is the statutory text, the starting point in any case of interpretation must always be the language itself, giving effect to the plain meaning thereof." CIFG Assur. North America, Inc. v. J.P. Morgan Securities LLC, 2016 WL 6954098, at *3 (1st Dept 2016) quoting Majewski v. Broadalbin–Perth Cent. School Dist., 91 N.Y.2d 577 (1998). Section 3105 "should be construed in accordance with its common, everyday meaning." CIFG, at *3 quoting Matter of New York Skyline, Inc. v. City of New York, 94 A.D.3d 23, 27 (1st Dept 2012).

The two clauses of Section 3105 are written in the disjunctive. To read the first and second clauses as rescission remedies makes the second clause virtually meaningless. Consequently, the plain language is clear and it unambiguously states that 'defeating recovery thereunder' means something other than rescission, such as recovery of payments without resort to rescission. See also Ambac Assur. Corp. v.

First Franklin Financial Corp., 2015 WL 5578267 (Sup. Ct. N.Y. Cnty. 2015) (Singh, J.) (citing MBIA holding that the recovery of payments made pursuant to an insurance policy without resort to rescission would qualify as a §3105 claim).

Macquarie's reliance on United States Life Ins. Co. in the City of N.Y. v. Blumenfeld, 113 A.D.3d 530 (1st Dept 2014) ("Blumenfeld II") is unavailing. There, the First Department held that all of the claims are dismissed in a suit where "the tort claims and the rescission claim are based on the same allegations, i.e., that plaintiff was harmed by issuing a policy that it would not have issued had defendants not made false representations and/or omissions in the insurance application, and merely seek different relief." Id. at 530. However, the court in Blumenfeld II did not analyze the tort claims in the context of any other First Department precedent in RMBS and CDO litigation brought by monoline insurers alleging, *inter alia*, fraud "informed by" the Insurance Law. See Blumenfeld II, 113 A.D.3d 530; MBIA, 105 A.D.3d 412; see also *supra*. Additionally, no other First Department case has cited Blumenfeld II approvingly, and no other lower court cases have relied upon its reasoning. Upon this backdrop, this court finds that section 3105 of the Insurance Law contemplates an insurer's claim for compensatory damages even where, as here, rescissory damages are unavailable.

It also bears noting that "in order to prove its claims for fraud and [negligent misrepresentation], [a party] must prove all elements of its claims" including loss

causation. Ambac Assurance Corp. v. Countrywide Home Loans, Inc., 2015 WL 6471943 (Sup. Ct. N.Y. Cnty. 2015) quoting MBIA Ins. Corp. v. Countrywide Home Loans, Inc., 34 Misc. 3d 895, 906 (Sup. Ct. N.Y. Cnty. 2012); see also MBIA Inc. Corp. v. Countrywide Home Loans, Inc., 87 A.D.3d 287, 296 (1st Dept 2011). A party "must prove that it was damaged as a direct result of the material misrepresentation." Id. (internal citations omitted); see also 87 A.D.3d at 296 (pleadings for loss causation are sufficient where the pleadings allege that it was foreseeable that they would suffer losses a result of relying upon the alleged misrepresentations.)

Here, Syncora's complaint adequately alleges that Macquarie's misrepresentations were a direct and proximate cause of Syncora's actual losses. See Compl. ¶¶90-98, 100-105 (alleging that for both the negligent misrepresentation and fraud claims, plaintiff relied upon the false information provided to them and was financially harmed by issuing the policy when it otherwise would not have.). Where the "complaint itself pleads a basis for inferring damages", a damages claim is maintainable even where the prayer for relief is defective because it seeks rescissory damages. Id. at *19; see also Ambac Assur. Corp. v. Countrywide Home Loans, Inc., 2016 WL 7374210 (Sup. Ct. N.Y. Cnty. 2016). Therefore, Syncora has adequately pled compensatory damages to survive a motion to dismiss.

Finally, this court grants Macquarie's motion to dismiss plaintiff's claim for punitive damages.[1] To warrant an award of punitive damages, there must be proof of recklessness, or a conscious disregard of the rights of others. Hartford Acc. and Indem. Co. v. Hempstead, 48 N.Y.2d 218 (1979); Zurich Ins. Co. v. Shearson Lehman Hutton, Inc., 193 A.D.2d 1 (1st Dept 1993). The conduct justifying an award of punitive damages must manifest spite or malice, or a fraudulent or evil motive on the part of the defendant, or such a conscious and deliberate disregard of the interests of others that the conduct may be called willful or wanton. Marinaccio v. Clarence, 20 N.Y.3d 506 (2013).

Punitive damages are permitted when the conduct was not simply intentional, but evinced a high degree of moral turpitude and demonstrated such wanton dishonesty as to imply a criminal indifference to civil obligations. Ross v. Louise Wise Services, Inc., 8 N.Y.3d 478 (2007). A showing of conduct aimed at the public is not required in every case in which punitive damages are sought. The Court of Appeals has held that in tort cases such as those involving alleged breaches of fiduciary duty, "harm aimed at the public generally" is not required "so long as the very high threshold of moral culpability is satisfied." Giblin v. Murphy, 73 N.Y.2d

[1] Prior to alleging that punitive damages are warranted, Syncora argues that Macquarie's motion should be denied because it has already been denied by Judge Schweitzer and therefore that Judge's ruling constitutes the law of the case. However, Judge Schweitzer's opinion is silent as to punitive damages. See Decision and Order dated July 1, 2013. Therefore, there is no law of the case as it pertains to punitive damages. See S. Point, Inc. v. Redman, 94 A.D.3d 1086 (2d Dept 2012).

769 (1988); see also Swersky v. Dreyer and Traub, 219 A.D.2d 321 (1st Dept 1996). Thus, "the rule that an award for punitive damages must be limited to conduct directed at the general public applies in breach of contract cases, not tort cases for breach of fiduciary duty." IDT Corp. v. Morgan Stanley Dean Witter & Co., 45 A.D.3d 419 (1st Dept 2007).

Syncora alleges that "Macquarie deliberately and under false pretenses induced Syncora to write insurance on American Roads" and that this is sufficient to state a claim for punitive damages. Opp. Br. at 22. However, even examining Macquarie's conduct without the disputed requirement that the conduct be directed at the general public, Syncora has failed to allege sufficient facts to warrant the denial of the motion to strike punitive damages. There is simply no evidence to suggest that Macquarie's conduct "demonstrated such wanton dishonesty as to imply a criminal indifference to civil obligations." Ross, 8 N.Y.3d 478.

Accordingly, it is hereby

ORDERED that Macquarie's motion to dismiss plaintiff's first cause of action for fraud is denied; and it is further

ORDERED that Macquarie's motion to dismiss plaintiff's second cause of action for negligent misrepresentation is denied; and it is further

ORDERED that Macquarie's motion is granted to the extent of dismissing rescissionary and punitive damages.

Date: February 14, 2017
New York, New York

Anil C. Singh