HSBC Bank USA, N.A. v Merrill Lynch Mtge. Lending, Inc.
2019 NY Slip Op 30358(U)
February 15, 2019
Supreme Court, New York County
Docket Number: 652793/2016
Judge: Marcy Friedman
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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK – PART 60
PRESENT: Hon. Marcy Friedman, J.S.C.

HSBC BANK USA, NATIONAL ASSOCIATION, in its capacity as Trustee of MERRILL LYNCH ALTERNATIVE NOTE ASSET TRUST, SERIES 2007-OAR5,

Plaintiff,

-against-

MERRILL LYNCH MORTGAGE LENDING, INC., BANK OF AMERICA, N.A., and COUNTRYWIDE HOME LOANS, INC.,

Defendants.

DECISION/ORDER
Index No.: 652793/2016

Plaintiff-trustee, HSBC Bank USA, National Association (HSBC), moves for leave to reargue a motion to dismiss and to "clarify" and revise the decision and order by which the motion to dismiss was determined. (NY Slip Op 31110 [U], 2018 WL 2722870 [Sup Ct, New York County June 6, 2018] [prior decision].)[1] The prior decision holds that the trustee's failure to notify claims accrued upon the defendant securitizer's or originator's discovery of material breaches of representations and warranties and failure to provide prompt written notice to the trustee. HSBC contends that the prior decision should be modified to clarify that the trustee's failure to notify claims against defendant originator, Countrywide Home Loans, Inc. (Countrywide), are timely to the extent that they are based on Countrywide's discovery of material breaches or, not and, failure to provide prompt notice to the trustee within the six-year limitations period prior to the assertion of the failure to notify cause of action (accounting for a

[1] The court assumes familiarity with the prior decision, which sets forth the facts in detail.

tolling period under a Tolling Agreement between various parties).[2] (Pl.'s Memo. In Supp., at 3-4.) Put another way, HSBC seeks modification of the prior decision to clarify that the complaint pleads timely failure to notify claims to the extent that either the discovery or the failure to provide prompt notice occurred within the limitations period.

Leave to reargue is granted. Although HSBC's motion requests clarification of the court's prior decision, HSBC contends that the court erroneously applied the standard for accrual of a failure to notify cause of action. Its motion to "clarify" is therefore "properly deemed one to reargue." (See Mendelson v Empire Assocs. Realty Co. Assn., 57 AD3d 413, 413 [1st Dept 2008], lv denied 12 NY3d 707 [2009]; Mordas v Schenkein, 19 AD3d 182, 183 [1st Dept 2005]; accord Macy's Inc. v Martha Stewart Living Omnimedia, Inc., 144 AD3d 453, 454 [1st Dept 2016].)

Upon reargument, the court adheres to its holding that accrual of a failure to notify cause of action requires both the defendant's discovery of breaches and its failure to give prompt written notice of the breaches to the trustee. (2018 WL 2722870, at * 5 [". . . the trustee's failure to notify claims accrued upon the [defendant's] discovery of material breaches of representations and warranties and failure to provide prompt written notice to the trustee"].)

On the prior motion to dismiss, Countrywide argued that HSBC's failure to notify cause of action accrued at the latest on October 1, 2007, prior to the limitations period, at the time it allegedly made its last sale of loans to the sponsor. In support of this contention, Countrywide

[2] As used in this decision, the term limitations period means the limitations period accounting for the Tolling Agreement. A Tolling Agreement, dated October 16, 2013 and in effect through May 18, 2016, tolled HSBC's claims against Countrywide and other defendants, if they were still timely when the parties entered into the Agreement. Thus, claims that had accrued more than six years prior to the date of the Tolling Agreement—i.e., before October 16, 2007—would not benefit from tolling as they were already untimely when the parties entered the Agreement. The parties have not precisely calculated the limitations period as affected by the Tolling Agreement. This calculation must also account for the commencement of the action on May 24, 2016, six days after the expiration of the Tolling Agreement.

cited the allegation of the complaint that Countrywide had knowledge by that date of the falsity of the representations and warranties it made to the sponsor about the loans, as a result of its origination of the loans. (Defs.' Memo. In Supp. Of Prior Motion, at 17-18.) In opposition to the motion to dismiss, HSBC disputed not only that October 1, 2007 was the date of the last sale of the loans, but also that October 1, 2007 was the date as of which Countrywide made its representations and warranties,[3] and therefore the date as of which Countrywide could have had knowledge that such representations and warranties had been breached.[4] (Pl.'s Memo. In Opp. To Prior Motion, at 18-20.) HSBC also argued that notice within two months of discovery of a breach is prompt as a matter of law and that, even assuming that Countrywide made representations and warranties and had knowledge of breaches by October 1, 2007 (i.e., more than six years before the assertion of the failure to notify claim), notice given two months later (i.e., within the six-year limitations period) would still have been prompt. (Id. at 19-20.)

The prior decision held that Countrywide failed to submit evidence sufficient to show that Countrywide did not discover breaches of representations and warranties between October 1,

[3] As set forth more fully in the prior decision, this securitization was effectuated by a series of separate but interrelated governing agreements. These agreements included a Master Mortgage Loan Purchase and Servicing Agreement (MLPSA), dated as of February 1, 2007, between Merrill Lynch Mortgage Lending, Inc. (Merrill or MLML) as Purchaser and Countrywide as Seller and Servicer. Pursuant to the MLPSA, Merrill agreed to purchase, from time to time, groups of mortgage loans originated by Countrywide. (MLPSA §2.) The MLPSA provided that Countrywide's representations and warranties to the sponsor as to each mortgage loan were made "as of the related Closing Date for such Mortgage Loan." (MLPSA § 7.02.) The Closing Date was defined as "[t]he date or dates on which the Purchaser from time to time shall purchase and the Seller from time to time shall sell to the Purchaser, the Mortgage Loans. . . ." (Id., Definitions.) An Assignment, Assumption and Recognition Agreement (AARA) was also "made as of October 1, 2007," between and among Merrill as Assignor, non-party Merrill Lynch Mortgage Investors, Inc. (MLMI) as Depositor/Assignee, and a non-party Countrywide servicing entity. Countrywide as Seller also signed the AARA, although it was not named as a party. Countrywide restated, "as of the date of" the AARA, for the benefit of MLMI, various of the representations and warranties it had made in the MLPSA. (AARA, § 4.)

On the motion to dismiss, the parties disputed, among other things, the date as of which the AARA was effective and whether the representations and warranties were made on the date of the loan sale or the date of the AARA.

[4] As held by the Court of Appeals, "[w]here . . . representations and warranties concern the characteristics of their subject as of the date they are made, they are breached, if at all, on that date." (Ace Secs. Corp. v DB Structured Prods., Inc., 25 NY3d 581, 589 [2015].)

2007 and the closing date of the securitization on October 31, 2007, and therefore that there were no discoveries after October 1 that may benefit from the Tolling Agreement in effect between October 16, 2013 and May 18, 2016. (Prior Decision, 2018 WL 2722870, at * 9.) Further, the prior decision held that the complaint pleaded that Countrywide discovered breaches of representations and warranties through post-closing internal quality control and review processes, and that the trustee's failure to notify cause of action against Countrywide was maintainable based on these allegations as to post-closing discovery. (Id.) It was in this context that the court found that the complaint pleaded a timely cause of action against Countrywide to the extent that it was "based on Countrywide's discovery of [such] breaches, and failure to provide prompt written notice thereof, within the six-year limitations period preceding the assertion of the failure to notify cause of action, accounting for the tolling period." (Id. [emphasis supplied].)

It was not the court's intention to suggest that discovery and provision of notice of the breaches must both occur within the limitations period. Rather, having found that the complaint pleaded timely failure to notify claims based on discovery within the limitations period, the court did not reach HSBC's argument that the complaint also pleaded timely failure to notify claims based on discovery prior to the limitations period and failure to give notice within the limitations period, provided that notice within the limitations period would still have been prompt. In particular, the court did not reach HSBC's argument that even if Countrywide discovered breaches on an October 1, 2007 loan sale date, prior to the closing and prior to the limitations period, the failure to notify claims were also timely to the extent that they were based on Countrywide's failure to give notice up to two months later, within the limitations period.

Nor could the court have determined the timeliness of this claim on the record of the motion to dismiss. The record of the prior motion did not identify the specific dates of the loan sales, and there were factual and legal disputes as to the dates on which Countrywide made its representations and warranties and therefore as to when the breaches of the representations and warranties occurred and Countrywide could have known of such breaches. (See supra, at 3.) In addition, HSBC failed to offer any explanation as to how, if Countrywide made representations on or before October 1 and had knowledge of breaches as of October 1, notice up to two months later could have been considered prompt.

The authority on which HSBC relied on the prior motion, and on which it continues to rely, does not support its contention that notice is prompt as a matter of law if given within two months of the knowledge of the breach. The two cases cited by HSBC in its opposition to the motion addressed the promptness of notice given by a trustee as a condition precedent to suit against a defendant securitizer or loan seller for repurchase of loans, and not, as here, the notice to be provided by the defendant to the trustee. (See Deutsche Alt-A Secs. Mtge. Loan Trust, Series 2006-OA1 v DB Structured Prods., Inc., 958 F Supp 2d 488, 495 [SD NY 2013]; LaSalle Bank N.A. v Lehman Bros. Holdings, Inc., 237 F Supp 2d 618, 637 [D Md 2002] [applying New York law].) HSBC has not discussed the differing purposes for which trustees and the various other parties involved in a securitization are obligated to give notice. Nor has HSBC discussed, or submitted legal authority that addresses, the impact of these differing purposes on the time by which notice must be given in order to be considered prompt and, in the case of a securitizer's or originator's obligation, the time by which the trustee's failure to notify cause of action will accrue if notice is not given.[5]

[5] The additional cases cited by HSBC on the motion to reargue do not remedy the briefing on the motion to dismiss. These cases involved determinations as to what constituted prompt or immediate notice in other contexts in which

In the interest of avoiding confusion, however, the court modifies the prior decision to state explicitly that the prior decision did not reach HSBC's argument that the complaint pleaded timely failure to notify claims based on the defendant securitizer's or originator's discovery of breaches of representations and warranties prior to the limitations period and failure to give notice within the limitations period, provided that notice within the limitations period would still have been prompt. The prior decision therefore does not preclude such a claim in future on a fully developed supporting factual record and on supporting legal authority as to the promptness of such notice.

Also in the interest of avoiding confusion, the court notes that this claim was not at issue in its bellwether decision in the coordinated Part 60 RMBS litigation on the standard for accrual of a failure to notify cause of action. (Federal Housing Finance Agency v Morgan Stanley ABS Capital I Inc., 59 Misc 3d 754, 2018 WL 1187676 [Sup Ct, NY County, Mar. 6, 2018, Nos. 650291/2013, 651959/2013] [FHFA/Morgan Stanley].) The prior decision in the instant action held that the accrual rule for a failure to notify claim set forth by this court in FHFA/Morgan Stanley applied to HSBC's failure to notify claims in this action. (Prior Decision, 2018 WL 2722870, at * 5.) The FHFA/Morgan Stanley decision held that, like other breach of contract claims, the failure to notify claim "does not accrue until the time of the breach," and that "a defendant does not breach its notification obligation until it discovers a breach of representations and warranties and fails to give prompt written notice to the Trustee." (59 Misc 3d, at 771-772.)

The defendant-securitizer in each of the actions decided by FHFA/Morgan Stanley argued that "failure to notify claims are subject to the same statute of limitations as claims for

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the purpose of the notice differed from that in the RMBS context. (Pl.'s Memo. In Supp., at 4, citing e.g. SBK Catalogue Partnership v CBS/Fox Co., 1990 WL 80046, * 9 [SD NY, 86 Civ 1149 (PKL), June 5, 1990] [copyright]; Rand v Underwriters at Lloyd's Subscribing Lloyd's Policy No. DB6/234, 295 F2d 342, 345 [2d Cir 1961], cert denied 368 US 988 [1962] [insurance].)

breaches of representations and warranties, and accrue on the date on which the underlying representations and warranties are made." (Id. at 768.) The Trustee contended that "the earliest [the breach of a notification obligation] could have occurred—and the earliest the statute of limitations could have begun to run—is after [the defendant] discovered the defective loans but failed to notify the Trustee." (Id.) The Trustee further contended that "[u]nder the continuing obligation doctrine, [it] may assert claims for [] persistent failures to notify, regardless of when [the defendant] initially discovered the breaches," because the defendant continued to breach its duty to notify by continuing to fail to provide notice. (Id. at 778, quoting Trustee's Opening Memo. at 20-21; see Trustee's Reply, at 10.)

In FHFA/Morgan Stanley, the parties did not address the meaning of "prompt" notice or its proper interpretation in the RMBS context. The court thus did not consider whether, or to what extent, the time of discovery differed from the time by which prompt notice must be provided. In holding that the Trustee had misconstrued the continuing obligation doctrine, the court stated that "the Trustee's claim for a breach of the notification obligation will be timely only if [the defendant's] discovery occurred within the six-year period before the assertion of the failure to notify causes of action" and that "[c]laims based on defendants' discovery of breaches prior to this six-year period will not be timely." (Id. at 779, 777.) Such statements were made in the context of rejecting the Trustee's apparent contention that, under the continuing obligation doctrine, its failure to notify claims would be timely regardless of when discovery occurred, based on the defendant's ongoing failure to give notice of the discovery. Although these statements appear to equate the time of discovery with accrual of the failure to notify claim, they were not intended to alter the accrual rule articulated earlier in the opinion. Nor should they be read to imply that a claim for failure to notify can accrue before the obligation to provide prompt

notice is breached.

Finally, HSBC seeks leave to reargue the branch of the prior motion for dismissal of certain of HSBC's notice-based claims against defendant Merrill for breaches of representations and warranties. Defendant argued that three of HSBC's pre-action breach notices were not timely served and that HSBC accordingly failed to comply with the condition precedent to suit as to the loans identified in those breach notices. The prior decision dismissed these claims to the extent based on breach notices sent on February 29, March 25, and May 19, 2016, less than the contractually required 90-day period in advance of the commencement of the action. (2018 WL 2722870, at * 10-11.) The prior decision held that the relation back doctrine, as articulated by the Appellate Division in Nomura Home Equity Loan, Inc., Series 2006-FM2 v Nomura Credit & Capital, Inc. (133 AD3d 96 [1st Dept 2015] [Nomura], modified on other grounds 30 NY3d 572 [2017]) and U.S. Bank National Association v GreenPoint Mortgage Funding, Inc. (147 AD3d 79 [1st Dept 2016] [GreenPoint]), did not permit maintenance of the notice-based claims to the extent based on the untimely breach notices. (2018 WL 2722870, at * 10-11.) As explained in the prior decision, although there were two timely pre-suit breach notices, each identified only one loan affected by breaches of representations and warranties. The vast majority of loans affected by breaches were first identified in the untimely notice sent five days before commencement of this action. Moreover, neither of the timely breach notices informed defendant that an investigation of the loans was in process and that further breaches might be discovered. (Id. at * 11.) The prior decision concluded that the timely notices were insufficient to have put defendant on notice of breaches regarding loans that were the subject of the untimely breach notices. (Id.)

In seeking leave to reargue, HSBC contends that the Tolling Agreement to which Merrill,

among others, was a party, provided the "required notice" to support a relation back argument and to support maintenance of the notice-based claims with respect to the loans identified in the three untimely breach notices. (Pl.'s Memo. In Supp., at 6.) HSBC first raised its claim based on the Tolling Agreement at the oral argument of the prior motion, asserting that the standard for application of the relation back doctrine in RMBS actions had been revised by GreenPoint after the briefing of the motion. On the instant motion, defendants address the merits of HSBC's relation back claim based on the Tolling Agreement. (Defs.' Memo. In Opp., at 7-8.) Under these circumstances, and as the prior decision did not discuss the claim, leave to reargue will be granted.

On reargument, the court adheres to its prior decision. As defendants correctly argue, the Tolling Agreement is not a pre-suit notice. Nor does it sufficiently provide notice that an investigation of the loans was being undertaken and might uncover additional defective loans. (Compare Nomura, 133 AD3d at 108; see GreenPoint, 147 AD3d at 88-89.) On the contrary, the Tolling Agreement stated generally that "the Parties believe that it would be mutually beneficial to delay the commencement of any action . . . in order to allow for . . . an opportunity for further investigation, dialogue, and analysis." (Third Whereas Clause.) It thus did not give specific notice of a loan level investigation. Significantly, also, it contained the following disclaimer, which expressly provided that it could not be used to establish liability:

> "The execution of the Tolling Agreement is not, and shall not operate as, an admission or indication of liability, wrongdoing, or responsibility by any Party to any person or entity, and nothing herein shall prejudice or affect any other rights or liabilities of any Party or be used to form the basis of any liability against any Party."

(Tolling Agreement, § 4.)

Moreover, on the date of entry of the Tolling Agreement, October 16, 2013, a timely

breach notice was given regarding only one loan. Approximately 1½ years later, a second timely notice, dated April 8, 2015, was given but, again, regarding only one loan. It was not until approximately 2½ years after entry into the Tolling Agreement and five days before commencement of this action that an untimely notice, dated May 19, 2016, was given regarding 973 loans. (Prior Decision, 2018 WL 2722870, at * 10-11.) The de minimis timely breach notices, even if considered with the Tolling Agreement, cannot be found to support a relation back claim with respect to the loans identified in the untimely breach notices.

It is accordingly hereby ORDERED that the motion of plaintiff HSBC Bank USA, National Association, for leave to reargue is granted to the following extent: Leave to reargue is granted. Upon reargument, the court adheres to its prior decision (NY Slip Op 31110 [U], 2018 WL 2722870 [Sup Ct, New York County June 6, 2018]), except to the extent modified on page 6 of the above decision.

This constitutes the decision and order of the court.

Dated: New York, New York
February 15, 2019

MARCY FRIEDMAN, J.S.C.