SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: Ramos Justice PART 53

Syncora Guarantee Inc.
-v-
EMC Mortgage LLC

INDEX NO. 653519/12
MOTION DATE
MOTION SEQ. NO.

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

Notice of Motion/Order to Show Cause — Affidavits — Exhibits ____ | No(s). ____
Answering Affidavits — Exhibits ____ | No(s). ____
Replying Affidavits ____ | No(s). ____

Upon the foregoing papers, it is ordered that this motion is

Motion is decided in accordance with accompanying Memorandum Decision.

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

Dated: 8/21/2013

CHARLES E. RAMOS, J.S.C.

1. CHECK ONE: ..... ☐ CASE DISPOSED ☐ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: .....MOTION IS: ☐ GRANTED ☐ DENIED ☑ GRANTED IN PART ☐ OTHER
3. CHECK IF APPROPRIATE: ..... ☐ SETTLE ORDER ☐ SUBMIT ORDER
☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

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

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SYNCORA GUARANTEE INC., formerly known as XL CAPITAL ASSURANCE INC.,

Plaintiff,

Index No. 653519/2012

- against -

EMC MORTGAGE LLC (formerly known as EMC Mortgage Corporation), BEAR, STEARNS & CO. INC., CMO HOLDINGS III LTD., J.P. MORGAN SECURITIES LLC (formerly known as BEAR, STEARNS & CO INC.), and JPMORGAN CHASE BANK, N.A.,

Defendants.

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Hon. Charles E. Ramos, J.S.C.

Defendants EMC Mortgage LLC, formerly known as EMC Mortgage Corporation, Bear, Stearns & Co. Inc., J.P. Morgan Securities LLC, and JPMorgan Chase Bank, N.A., (collectively, Defendants) move for partial dismissal of the complaint pursuant to CPLR § 3211(a)(1) and (a)(7).

Background

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

This action arises out of a transaction known as Bear Stearns Structured Products Trust 2007-R5 (the Transaction), which involved the resecuritization of Real Estate Mortgage Investment Conduits (Re-Remics). The Re-Remics consist of previously issued mortgage-backed securities from four pools of residential mortgage loans (RMBS).

To effectuate the Transaction, Bear, Stearns & Co. (Bear Stearns) sold the underlying RMBS to CMO Holdings III Ltd. (CMO)

through an Asset Sale Agreement. CMO then entered into a Fiscal Agency Agreement, appointing the Bank of New York (London Office) (herein "BONY London") as Fiscal Agent, and the Bank of New York (BONY) as Collateral Agent. Bear Stearns then solicited Syncora, a financial insurer, to issue Financial-Guaranty Insurance Policy Number CA03917A (the Policy) pursuant to an Insurance and Indemnity Agreement (the I&I Agreement), dated July 31, 2007.

Inducing Syncora to Issue the Policy

Syncora alleges that Bear Stearns prepared marketing presentations to Syncora concerning its high quality securitization operations, prepared and distributed data tapes containing information pertaining to the individual loans, promoted the AAA ratings secured in the Underlying Transactions, and sent Syncora a Private Placement Memorandum (the PPM) containing additional representations about the loan pool and securitization process.

The data tapes provided to Syncora contained the critical attributes of the underlying loans in the proposed securitization pool, including the combined loan to value ratio for each loan, credit scores for each borrower, and the pay history of each loan. In the agreements, described at length below, Bear Stearns and EMC warranted that the information relating to the underlying loans was true and accurate in all respects. Syncora alleges that Defendants knew this information provided to Syncora was materially false.

Bear Stearns also allegedly misrepresented that its affiliate EMC Mortgage Co. (EMC) conducted a comprehensive background check on all loan originators, weeding out loans that were too risky. Bear Stearns further represented that its quality control department was sufficiently equipped to identify and handle fraud in the underlying loans.

Syncora alleges that these representations were false, and that Bear Stearns made these representations with full knowledge of their falsity, which Syncora relied upon to its detriment.

The Transaction

The Transaction involved a series of interlocking agreements consisting of the I&I Agreement, four Pooling and Service Agreements (PSAs), and four Mortgage Loan Purchase Agreements (MLPAs) (collectively the Operative Documents).

The MLPAs, sales agreements which effectuate the sale of the pool of loans in the Underlying Transactions from EMC to the purchaser, contain representations and warranties by EMC concerning the quality of the loan pool. The MLPAs also imposed a repurchase obligation on EMC in the event of a breach of the representations and warranties or discovery of a defective loan (Repurchase Protocol). Under the Repurchase Protocol, in the event the representations and warranties prove untrue or a defective loan is identified, EMC is obliged to cure by repurchasing the loan from the pool.

The PSAs effectuated the transfer of the trust, containing the pool of loans, from the depositor to the trustee. According to Syncora, the PSAs incorporate by reference EMC's "loan level" representations in the MLPAs, relating to the quality of the loan pool and individual loans.

In July 2007, Syncora entered into the I&I Agreement with EMC, Bear Stearns, CMO, BONY London, and BONY, under which Defendants represented and warranted that information relating to the MLPAs and PSAs, the certificates from the Underlying Transactions, and characteristics concerning the underlying loans and the underwriting practices of EMC were true and accurate. The I&I Agreement provides Syncora with remedies to address breaches of the representations and warranties. The I&I Agreement also incorporates by reference certain provisions of the PSAs and MLPAs, and provides that Syncora is a third-party beneficiary of the Operative Documents with all rights afforded thereunder, with respect to representations and warranties.

The Breaches

According to Syncora, the underlying loans in the trust failed terribly. As of August 25, 2012, only 2,050 of the 18,000 loans initially sold to the trust are current, and 13,684 are in default or have been liquidated. The Transaction has experienced cumulative losses of $111,633,231.75, resulting in Syncora's payment of $94,059,025 in claim payments (net of reimbursements) to the insured note holders. Through an analysis of a

representative sample of the loans (a sample of 258 loans), Syncora discovered that 84.9% of the loans had materially breached one or more of the representations made in the MLPAs.

Syncora alleges that Bear Stearns had full knowledge of the defects of its due diligence protocols as early as November 2005, though the company continued to represent the soundness of those protocols and to adhere to them.

JP Morgan Acquires Bear Stearns

Prior to the collapse of The Bear Stearns Companies Inc. in 2008, Bear Stearns and EMC were wholly owned subsidiaries of The Bear Stearns Companies Inc. Following its collapse, The Bear Stearns Companies Inc. (including its subsidiary EMC) was acquired by JP Morgan Chase (Chase). Bear Stearns was merged into an existing subsidiary of Chase known as JP Morgan Securities (JP Morgan). EMC remains a wholly owned subsidiary of Chase.

Syncora alleges that immediately upon its acquisition of Bear Stearns, JP Morgan implemented a plan of rejecting all of Syncora's demands arising out of the Repurchase Protocol. While assuming EMC's operations, policies, and procedures, Chase directed EMC to refuse all demands to repurchase breaching loans under the Repurchase Protocol, and implemented a moratorium to this effect.

Syncora's Claims

Syncora asserts nine causes of action against Defendants, five of which are at issue on this motion.

Discussion

I. Fraudulent Inducement

Syncora alleges that Defendants fraudulently induced them to enter into the Transaction by misleading them about the quality of the mortgage loans backing the underlying RMBS and the adequacy of its quality controls. Defendants move to dismiss the claim on the ground that Syncora cannot demonstrate justifiable reliance as a matter of law.

In assessing whether a sophisticated plaintiff could justifiably rely upon representations and warranties made as part of a transaction, the Court of Appeals has stated:

> [I]f the facts represented are not matters peculiarly within the party's knowledge, and the other party has the means available to him of knowing, by the exercise of ordinary intelligence, the truth or the real quality of the subject of the representation, he must make use of those means, or he will not be heard to complain that he was induced to enter the transaction by misrepresentations (*DDJ Mgmt., LLC*, 15 NY3d at 154; *see also Centro Empresarial Cempresa S.A. v America Movil, S.A.B. de C.V.*, 17 NY3d 269, 278-79 [2011]).

Nonetheless, the Court went on to state that "where a plaintiff has gone to the trouble to insist on a written representation that certain facts are true, it will often be justified in accepting that representation rather than making its own inquiry," while admonishing that the question of what

constitutes justifiable reliance is fact-intensive (*DDJ Mgt., LLC*, 15 NY3d at 154-56).

The First Department recently reinstated a claim for fraudulent inducement asserted by a monoline insurer against the sponsor of RMBS transactions (*see CIFG Assur. of N. America, Inc.*, 106 AD3d 437 [1st Dept 2013]). Citing to *DDJ Mgmt., LLC* (15 NY3d at 154), the First Department reasoned that where the insurer conducted its own due diligence concerning the underlying loans which were the subject of written representations not demonstrably known to be false when made, there remained a question of fact as to whether the insurer reasonably relied upon the representations.

In support of their motion, Defendants primarily rely on *HSH Nordbank*, in which the First Department dismissed a claim of fraudulent inducement finding that "sophisticated parties have 'a duty to exercise ordinary diligence and conduct an independent appraisal of the risk they [are] assuming'" (*HSH Nordbank AG v UBS AG*, 95 AD3d 185 [1st Dept 2012]).

Although the plaintiff in that case did not obtain written assurances from the defendant as to the accuracy of the information later alleged to be misrepresented, which might limit application to the present claim (*accord Ambac Assur. Corp. v EMC Mortg. LLC*, 39 Misc3d 1240(A) [Sup Ct, NY County 2013, Ramos J.]), Syncora conducted its own due diligence, evidenced by the Credit Committee Memorandum (the CCM). The CCM, which Syncora

prepared prior to issuing the Policy, contained a detailed analysis of the risks associated with the Transaction, and highlights the poor quality and performance of the RMBS loans in the pool. For instance, the CCM states:

> "Since these CES were originated under relaxed underwriting standards in 2006 with close to 100% CLTV and a high percentage of reduced and stated documentation, the performance of the Underlying Bonds, not surprisingly, has been poor, with Class B-3 (BBB-) and Class B-4 (BB+) of two of the Underlying Bonds being put on negative watch by S&P in June" (Cafasso aff 12/7/2012, Exhibit C at 7).

Clearly, such a document demonstrates that, at a minimum, Syncora was on notice as to the riskiness of the Transaction. It cannot now claim that it was justified in relying upon Defendants' misrepresentations. The claim of fraud is dismissed.

II. Punitive Damages

Defendants move to strike the prayer for punitive damages. In light of the dismissal of the fraud cause of action, the complaint does not support Syncora's demand for punitive damages.

III. Indemnification

Syncora seeks indemnification for claims submitted against it under the Policy for the benefit of its security holders, including past and future insurance payments, resulting from EMC's breaches of the warranties and representations.

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

> [E]ach of the Seller and EMC, severally and not jointly, agree to pay, and to protect, indemnify and save harmless, the Insurer and its officers, directors, shareholders, employees, agents and each Person, if any, who controls the Insurer... from and against any and all claims, losses,

> liabilities (including penalties), actions, suits, judgments, demands, damages, costs or expenses... of any nature arising out of or relating to the breach by it, or, with respect to EMC, the Issuer, of any of the representations or warranties... or arising out of or relating to the transactions contemplated by the Operative Documents... (I&I, § 3.04[a]).

"When a party is under no legal duty to indemnify, a contract assuming that obligation must be strictly construed to avoid reading into it a duty which the parties did not intend to be assumed. The promise should not be found unless it can be clearly implied from the language and purpose of the entire agreement and the surrounding facts and circumstances" (*Great Northern Ins. Co. v Interior Const. Corp.*, 7 NY3d 412 [2006]).

Section 3.04(d) of the I&I Agreement states:

> If any action or proceeding... shall be brought or asserted **against** any Person (individually, an "Indemnified Party" and, collectively, the "Indemnified Parties") in respect of which the indemnity provided in Section 3.04(a), (b) or (c) may be sought from EMC or the Seller on the one hand, or the Insurer, on the other (each, an "Indemnifying Party") hereunder, each such Indemnified Party shall promptly notify the Indemnifying Party... (I&I Agreement§ 3.04[d][emphasis added]).

By juxtaposing the language of section 3.04(a) against the language of section 3.04(d), it is clear that the I&I Agreement contemplates indemnity rights for losses that relate solely to third party claims. In contrast, Syncora is actually seeking indemnity for its own losses, which are not cover by the indemnification provision (see *Assured Guar. Mun. Corp. v Flagstar Bank*, 2011 WL 5335566 [SDNY 2011]). As Syncora "did not establish that the agreement's indemnification provision

satisfied the exacting standard of language 'exclusively or unequivocally referable to claims between the parties themselves' as opposed to third-party claims only" (*Gate Five, LLC v Knowles-Carter*, 100 AD3d 416 [1st Dept 2012]), it is dismissed.

IV. Attorneys' Fees

Defendants move to dismiss the claim for attorneys' fees on the ground that, because Syncora is not entitled to indemnification under the I&I Agreement, it is also not entitled to recover its attorneys' fees incurred in this action. A plain reading of the I&I Agreement contradicts this contention, as sections 3.03(b) and 3.03(c) provide limited rights to reimbursement of attorneys' fees pursued independent of Syncora's rights to indemnification.

Section 3.03(b) of the I&I Agreement states:

> Seller agrees to pay to the Insurer, and the Insurer shall be entitled to reimbursement from the Seller and shall have full recourse against the Seller for 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 Underlying Mortgage Loan as required pursuant to the Underlying Pooling and Servicing Agreements... (I&I Agreement § 3.03 [b]).

Furthermore, section 3.03(c) provides:

> EMC agrees 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, monitoring or participating in any litigation or proceeding... relating to any of the Operative Documents, any party to any of the Operative Documents (in its capacity as such a party) or the Transaction or (ii) any amendment, waiver or other action with respect to, or related to, any Operative Document,

whether or not executed or completed (I&I Agreement § 3.03 [c]).

Under the plain import of these provisions, Syncora possesses a clear contractual right to recover from EMC its reasonable attorneys' fees and costs incurred in relation to its demands under the Repurchase Protocol (*accord Assured Guar. Mun. Corp.*, 2013 WL 440114 at *40; *Syncora Guar. Inc. v EMC Mtge. LLC*, 2013 NY Slip Op 50568, 7-8 [Sup Ct, NY County 2013, Ramos J.]). Accordingly, Defendants' motion with respect to the sixth cause of action is denied.

V. Breach of Contract - The Asset Transfer

On or about April 1, 2011, Chase effectuated an inter-company asset sale, whereby EMC transferred to Chase all of its servicing related assets. Syncora alleges that in effectuating the transfer without its consent, EMC breached a provision of the I&I Agreement which prevents the transfer of all or substantially all of its assets without Syncora's consent, which has left EMC without its sole remaining operating asset.

Syncora has failed to allege that it has suffered damage as a result of the asset transfer, and alleges merely speculative harm. "Where a party has failed to come forward with evidence sufficient to demonstrate damages flowing from the breach alleged and relies, instead, on wholly speculative theories of damages, dismissal of the breach of contract claim is in order" (*Lexington 360 Assoc. v First Union Nat. Bank of N.C.*, 234 AD2d 187 [1st Dept 1996]).

Accordingly, the claim for breach of contract arising out of the asset transfer is dismissed.

VI. Tortious Interference with Contract

In support of its claim for tortious interference with contract, Syncora alleges that JP Morgan is interfering with EMC's contractual obligations arising under the Repurchase Protocol by preventing EMC from repurchasing defaulting loans.

In order to state a claim for tortious interference with contract, "the plaintiff must show the existence of its valid contract with a third party, defendant's knowledge of that contract, defendant's intentional and improper procuring of a breach, and damages" (*White Plains Coat & Apron Co., Inc. v Cintas Corp.*, 8 NY3d 422 [2007]).

Syncora alleges that JP Morgan is a continuation of Bear Stearns and assumed the liabilities of that company. To support this allegation, Syncora cites to MLPA § 23 and I&I Agreement § 4.04(a).

MLPA § 23 states, "This agreement shall bind and inure to the benefit of and be enforceable by each of the Mortgage Loan Seller and the Purchaser and their permitted successors and assigns." I&I Agreement § 4.04(a) contains similar language.

Syncora, EMC, Bear Stearns, and CMO are all parties to the I&I Agreement, which incorporates the Repurchase Protocol in the MLPAs and PSAs by reference. The only signatories to the MLPA are EMC and Bear Stearns.

However, to the extent that Syncora alleges that JP Morgan is actually the former Bear Stearns, Syncora, in essence, claims that JP Morgan is interfering with its own contract. "It is well established that only a stranger to a contract, such as a third party, can be liable for tortious interference with a contract" (*Koret, Inc. v Christian Dior, S.A.*, 161 AD2d 156 [1st Dept 1990]). While JP Morgan is not a signatory to the contract, it is an alleged successor to a signatory and to this extent, is not a stranger to the contract capable of tortious interference.

The claim for tortious interference with contact is dismissed.

Accordingly, it is

ORDERED that Defendants' motion to dismiss is granted in part, and denied, in part, and the second, fourth, seventh, and eighth claims are severed and dismissed, and the prayer for punitive damages is struck; and it is further

ORDERED that Defendants are directed to serve an answer to the complaint within twenty days of service of a copy of notice of entry.

Dated: August 21, 2013

ENTER:

J.S.C.