Ownit Mtge. Loan Trust v Merrill Lynch Mtge. Lending, Inc.
2015 NY Slip Op 32303(U)
December 7, 2015
Supreme Court, New York County
Docket Number: 651370/2014
Judge: Marcy S. Friedman

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK – PART 60
PRESENT: Hon. Marcy Friedman, J.S.C.

OWNIT MORTGAGE LOAN TRUST, SERIES 2006-5 (OWNIT 2006-5), by U.S. BANK NATIONAL ASSOCIATION, solely in its capacity as Trustee,

Plaintiff,

– against –

MERRILL LYNCH MORTGAGE LENDING, INC.,

Defendant

DECISION/ORDER
Index No. 651370/2014

OWNIT MORTGAGE LOAN TRUST, SERIES 2006-7 (OWNIT 2006-7), by U.S. BANK NATIONAL ASSOCIATION, solely in its capacity as Trustee,

Plaintiff,

– against –

MERRILL LYNCH MORTGAGE LENDING, INC.,

Defendant

Index No. 651373/2014

SPECIALTY UNDERWRITING & RESIDENTIAL FINANCE TRUST, SERIES 2006-AB3 (SURF 2006-AB3), by U.S. BANK NATIONAL ASSOCIATION, solely in its capacity as Trustee,

Plaintiff,

– against –

MERRILL LYNCH MORTGAGE LENDING, INC. and MERRILL LYNCH MORTGAGE INVESTORS, INC.,

Defendants

Index No. 651371/2014

SPECIALTY UNDERWRITING & RESIDENTIAL FINANCE TRUST, SERIES 2007-AB1 (SURF 2007-AB1), by U.S. BANK NATIONAL ASSOCIATION, solely in its capacity as Trustee,

Plaintiff,

– against –

MERRILL LYNCH MORTGAGE LENDING, INC. and MERRILL LYNCH MORTGAGE INVESTORS, INC.,

Defendants

Index No. 651388/2014

These four breach of contract actions involving residential mortgage backed securities (RMBS) were consolidated on consent solely for the purpose of briefing of motions to dismiss. Plaintiff U.S. Bank National Association is the trustee for the four trusts at issue: Specialty Underwriting & Residential Finance Trust (SURF) Series 2006-AB3; SURF Series 2007-AB1; Ownit Mortgage Loan Trust (Ownit) Series 2006-5; and Ownit Series 2006-7. Merrill Lynch Mortgage Lending, Inc. (Merrill Lending) was the Sponsor of the securitizations and is a named defendant in all four actions. Merrill Lynch Mortgage Investors, Inc. (Merrill Investors) was the Depositor and is named as a defendant only in the two SURF actions. Defendants (collectively Merrill Lynch) move to dismiss, pursuant to CPLR 3211 (a) (1), (a) (5), and (a) (7).

Having been designated by Administrative Order, dated May 23, 2013, to hear all RMBS cases filed after the date of the order, this court has issued numerous decisions on pleading issues raised by motions to dismiss. The issues raised by defendants' motions have largely been decided by this court, and in some instances, by the appellate courts, on substantially similar pleadings involving substantially similar governing agreements. The court will therefore not discuss those issues at length here.

Defendants argue that the complaints fails to state a breach of contract cause of action for repurchase of mortgage loans based on defendants' own discovery of applicable breaches of representations and warranties regarding the loans. Defendants do not dispute that defendants' own discovery of such breaches, as opposed to notice to defendants of the breaches, would give rise to an obligation to repurchase under the repurchase protocols in the governing agreements. They argue, however, that the allegations as to their discovery lack the requisite specificity.

The complaints allege defendants' discovery based on Merrill Lending's due diligence in acquiring loans, and on certain findings in a settlement agreement between the United States

Department of Justice and Bank of America, which had acquired defendants, regarding "tolerances" in Merrill Lynch's due diligence process. (SURF Series 2006-AB3 Compl., ¶¶ 81-90; SURF Series 2007-AB1 Compl., ¶¶ 69-78; Ownit Series 2006-5 Compl., ¶¶ 66-73; Ownit Series 2006-7 Compl., ¶¶ 63-70.) The complaints also plead that substantial percentages of the loans were defective. (SURF Series 2006-AB3 Compl., ¶¶ 51-54 ; SURF Series 2007-AB1 Compl., ¶¶ 39-42; Ownit Series 2006-5 Compl., ¶¶ 39-42; Ownit Series 2006-7 Compl., ¶¶ 39-41.)

These allegations are substantially similar to allegations that this court recently held sufficient to support maintenance of a breach of representations and warranties claim against Merrill Lynch. (See HSBC Bank USA, Natl. Assn., in its capacity as Trustee of Merrill Lynch Alternative Note Asset Trust, Series 2007-A3 v Merrill Lynch Mtge. Lending, Inc., Index No. 652727/14 [Oct. 23, 2015].) These allegations are also of comparable specificity to those which this and numerous other courts have held sufficient to plead discovery of breaches by other securitizers. (See e.g. ACE Secs. Corp., Home Equity Loan Trust Series 2007-ASAP2 v DB Structured Prods., Inc., 2014 WL 4785503, * 5-6 [Aug. 28, 2014] [citing authorities] [ACE 2007-ASAP2]; U.S. Bank Natl. Assn., solely in its capacity as Trustee of the CSMC Asset-Backed Trust 2007-NC1 v DLJ Mtge. Capital, Inc., 2015 WL 298642, * 1 [Jan. 16, 2015].) The allegations at issue as to defendants' discovery are not deficient because the complaints do not specifically identify each of the loans as to which defendants are claimed to have discovered breaches. (See ACE 2007-ASAP2, 2014 WL 4785503, at * 6.) As previously noted, although the pleading of discovery is sufficient, plaintiffs will have the ultimate burden of proving whether or to what extent defendants discovered the breaches. (Id.)

Here also, each of the complaints pleads that at least one timely breach notice was sent to Merrill Lending. (See Nomura Home Equity Loan, Inc., Series 2006-FM2 v Nomura Credit & Capital, Inc., ___ AD3d ___, 2015 WL 5935177, * 8 [1st Dept Oct. 13, 2015] [Nomura] [upholding this court's "refus[al] to dismiss claims relating to loans that plaintiffs failed to mention in their breach notices . . ."].) As to the breach notices in the Ownit actions, the court rejects defendants' claim that the complaints fail to adequately allege that the 2012 notices were served on Merrill Lending, as opposed to Merrill Investors. (See Ownit Series 2006-5 Compl., ¶¶ 74-75; Ownit Series 2006-7 Compl., ¶¶ 71-72.) Moreover, these notices (Exs. 22 and 23 to Weiss Aff. In Supp.), although addressed to Merrill Investors, state on their face that the "Sellers" will be provided "under separate cover" with a schedule of individual loan breaches. Evidentiary matter may be used "to preserve inartfully pleaded, but potentially meritorious, claims" in response to a motion to dismiss. (See Rovello v Orofino Realty Co., 40 NY2d 633, 635-636 [1976] [affidavits].) Whether the notices were in fact given to Merrill Lending is a factual issue that should not be resolved on these motions to dismiss.[1]

Defendants also move to dismiss plaintiffs' claims in the SURF actions against Merrill Investors, on the ground that the complaint does not allege breaches of the specific representations for which this defendant, as Depositor, has a repurchase obligation under the Pooling and Servicing Agreements (PSAs). In both SURF actions, PSA § 2.03 (c) provides that "[w]ithin ninety (90) days of the discovery of a breach of any representation or warranty" that materially affects the value of the related Mortgage Loan, the Depositor or the Sponsor shall

[1] Defendants raise an additional issue as to whether plaintiff in the SURF Series 2007-AB1 action may rely on rescinded notices. The court does not reach this issue with respect to Merrill Lending, as the complaint otherwise adequately pleads Merrill Lending's own discovery of breaches, and there were other timely notices regarding loans at issue in this action. The court does not reach the issue with respect to Merrill Investors because the court holds above (infra at 4-9) that plaintiff does not state a breach of representations and warranties claim against that defendant.

cure, repurchase or, within a specified time period, substitute such Loan.[2] Both SURF PSAs also include § 2.03 (b), which provides:

> "To the extent that any fact, condition or event with respect to a Mortgage Loan constitutes a breach of a representation or warranty of the Sponsor under the Sale Agreement, the only right or remedy of the Trustee or of any Certificateholder shall be the Trustee's right to enforce the obligations of the Sponsor under any applicable representation or warranty made by it. The Trustee acknowledges that the Depositor shall have no obligation or liability with respect to any breach of any representation or warranty with respect to the Mortgage Loans (except as set forth in Section 2.03(a)(v)) under any circumstances."

Section 2.03 (a) (v), in turn, sets forth representations by the Depositor as to good title and claims against the mortgage notes.

The SURF Series 2006-AB3 action, but not the SURF Series 2007-AB1 action, involves transfers of additional loans to the Trust after the closing date of the PSA. The PSA for the 2006-AB3 action includes a section 2.10, which specifically contemplates the conveyance of "subsequent mortgage loans" and provides for additional representations and warranties with respect to quality and characteristics of these loans, including, for example, representations and warranties as to loan-to-value ratios, delinquencies, and compliance with underwriting standards. In section 2 (a) of the Subsequent Transfer Instruments for these loans (Exs. 9 and 10 to Weiss

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[2] PSA § 2.03 (c) provides, more fully, in pertinent part:

> "Upon discovery by any of the Depositor, the Servicer, or the Trustee of a breach of any of representations and warranties set forth in the Sale Agreement [defined as the Mortgage Loan Sale and Assignment Agreement, dated as of September 1, 2006, between the Depositor and the Sponsor] that adversely and materially affects the value of the related Mortgage Loan . . . , the party discovering such breach shall give prompt written notice to the other parties. Within ninety (90) days of the discovery of a breach of any representation or warranty given to the Trustee by the Depositor, the Sponsor and assigned by the Depositor to the Trustee, the Depositor, or the Sponsor shall either (a) cure such breach in all material respects, (b) repurchase such Mortgage Loan or any property acquired in respect thereof from the Trustee at the Purchase Price or (c) within the two year period following the Closing Date, substitute a Replacement Mortgage Loan for the affected Mortgage Loan." (The section continues.)

Aff. In Supp.), made among Merrill Investors as Depositor, U.S. Bank National Association as Trustee and the Servicer, Merrill Investors confirms "that each of the conditions precedent and the representations and warranties set forth in Sections 2.03 and 2.10 of the Pooling and Servicing Agreement are satisfied as of the date hereof with respect to the Subsequent Mortgage Loans."

Citing the language of PSA § 2.03 (c), which provides for cure or repurchase by the Depositor or Sponsor upon discovery of a breach of "any" representation or warranty, plaintiffs argue that this provision renders both defendants liable for a material breach of any representation, whether made by Merrill Lending as Sponsor or Merrill Investors as Depositor. (Ps.' Memo. In Opp. at 22.) Defendants counter that this provision is limited by § 2.03 (b), which imposes the repurchase obligation upon Merrill Investors only for breach of representations specified in § 2.03 (a) (v). (Defs.' Reply Memo. at 13-14.) Plaintiffs do not dispute that the complaint does not allege breach of the § 2.03 (a) (v) representations but, rather, contend that PSA § 2.03 (c) controls or, in the alternative, that §§ 2.03 (b) and (c) are ambiguous and that a triable issue of fact exists as to their meaning. (Ps.' Memo. In Opp. at 22-23.)

Plaintiffs' contention reads § 2.03 (b) out of the PSAs. Under settled principles of contract interpretation, the determination of whether a contract is ambiguous is one of law to be resolved by the court. (Matter of Wallace v 600 Partners Co., 86 NY2d 543, 548 [1995]; W.W.W. Assocs., Inc. v Giancontieri, 77 NY2d 157 [1990].) "All parts of an agreement are to be reconciled, if possible, in order to avoid inconsistency." (National Conversion Corp. v Cedar Bldg. Corp., 23 NY2d 621, 625 [1969].) Thus, "where two seemingly conflicting contract provisions reasonably can be reconciled, a court is required to do so and to give both effect." (HSBC Bank USA v National Equity Corp., 279 AD2d 251, 253 [1st Dept 2001] [internal

quotation marks and citations omitted].) Moreover, "[m]indful of the directive of the Court of Appeals to 'avoid an interpretation that would leave contractual clauses meaningless', [a court must] follow the longstanding rule that, where 'there [is] an inconsistency between a specific provision and a general provision of a contract . . . , the specific provision controls.'" (Matter of TBA Global, LLC [v Fidus Partners, LLC], 132 AD3d 195, 204 [1st Dept 2015] [internal citations omitted].)

Here, PSA §§ 2.03 (b) and (c) can be reasonably reconciled. Section (b) specifically limits the representations for which the Depositor has repurchase obligations. In contrast, section (c) provides, among other things, that the repurchase obligations for which the Sponsor and Depositor are respectively liable arise upon discovery or notice of the material breach, and sets forth the circumstances under which the liable party may cure or substitute loans rather than repurchase them.

This reconciliation of PSA §§ 2.03 (b) and (c) is equally applicable to the PSA for the SURF Series 2006-AB3 Trust. Plaintiffs argue that section (c) must be construed as imposing repurchase obligations upon the Depositor for breach of "any" representation (and not only a PSA § 2.03 [a] [v] representation) because the additional representations that Merrill Investors made in connection with the subsequent loan conveyances to this Trust would otherwise be "unenforceable (and therefore superfluous)." (Ps.' Memo. In Opp. at 24.)

This contention is unpersuasive. Notwithstanding that section 2.10 of this PSA expressly contemplates subsequent loan conveyances and provides for additional representations as to such loans, section 2.03 (b) unequivocally limits Merrill Investors' repurchase obligations to breaches of the section 2.03 (a) (v) representations: "The Trustee acknowledges that the Depositor shall have no obligation or liability with respect to any breach of any representation or warranty with

respect to the Mortgage Loans (except as set forth in Section 2.03(a)(v)) under any circumstances."[3]

Section 2 (b) of the Subsequent Transfer Instruments, in which the Depositor makes the additional representations, expressly provides that "[a]ll terms and conditions of the Pooling and Servicing Agreement are hereby ratified and confirmed," absent a conflict. There is no conflict between the Instruments and the PSA. Although Merrill Investors, as Depositor, made additional representations as to the subsequent loans, the parties to the governing agreements chose to limit the Depositor's repurchase obligation to breaches of section 2.03 (a) (v) representations, and to provide the Trustee with a remedy against the Sponsor for breaches of representations and warranties made by it to the Depositor whose rights the Trustee assumed. Thus, section 2.03 (b) (quoted in full above) provides: "To the extent that any fact, condition or event with respect to a Mortgage Loan constitutes a breach of a representation or warranty of the Sponsor under the Sale Agreement [i.e., the Agreement between the Sponsor and Depositor], the only right or remedy of the Trustee . . . shall be the Trustee's right to enforce the obligations of the Sponsor under any applicable representation or warranty made by it."[4]

As the Appellate Division recently explained in the context of the RMBS litigation, "New York law has long held that contracting parties are generally free to limit their remedies. 'A limitation on liability provision in a contract represents the parties' agreement on the allocation of the risk of economic loss in the event that the contemplated transaction is not fully executed, which the courts should honor.'" (Nomura, 2015 WL 5935177, at * 6, quoting Metropolitan Life

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[3] Mortgage Loans are defined in the PSA to include "any Subsequent Mortgage Loan delivered pursuant to a Subsequent Transfer Instrument."

[4] It is noted that plaintiffs do not argue that Merrill Lending, the Sponsor, did not make representations and warranties comparable to those that plaintiffs would otherwise seek to enforce against Merrill Investors as Depositor.

Ins. Co. v Noble Lowndes Intl., 84 NY2d 430, 436 [1994].) Had these "very sophisticated parties" wished to provide a more extensive repurchase remedy against the Depositor, they could readily have included language in the governing agreements to that effect. (See generally Nomura, 2015 WL 5935177, at * 7.) The court accordingly concludes that the breach of contract claims against Merrill Investors in the SURF actions based on alleged breaches of representations and warranties must be dismissed.

Defendants further seek dismissal of the SURF plaintiffs' claims which allege that defendants breached their obligation upon discovery of material breaches of the loans to provide the Trustee with prompt written notice. As the instant motions were briefed before the Appellate Division's recent decision in Nomura (2015 WL 5935177, at * 7), this branch of the motions will be denied without prejudice to defendants' right to address the scope and import of Nomura on the notice claims in coordinated briefing of the issue in the RMBS put-back actions before this court.

To the extent that the actions seek indemnification, including indemnification for attorney's fees, such claims will be dismissed. Plaintiffs do not cite any provision that would authorize such indemnification and appear to acknowledge that indemnification would be barred under this court's prior decisions. (See Ps.' Memo. In Opp. at 13 n 6.) To the extent that the complaints purport to plead breach of contract claims based on failure to repurchase loans rather than on breaches of representations and warranties, such claims will be dismissed on the authority of Ace Secs. Corp. v DB Structured Prods., Inc. (25 NY3d 581 [2015]). Plaintiffs also represent that they do not seek to pursue independent claims for breach of the repurchase protocols. (Ps.' Memo. In Opp. at 13 n 6.)

OWNIT Series 2006-5 action (Index No. 651370/2014)

It is hereby ORDERED that the motion of defendant Merrill Lynch Mortgage Lending, Inc. is granted to the extent of (1) dismissing with prejudice the sole cause of action for breach of contract only insofar as it pleads a claim for an independent breach of a duty to repurchase defective loans; and (2) dismissing with prejudice the claim for indemnification, including indemnification for attorney's fees.

OWNIT Series 2006-7 action (Index No. 651373/2014)

It is hereby ORDERED that the motion of defendant Merrill Lynch Mortgage Lending, Inc. is granted to the extent of (1) dismissing with prejudice the sole cause of action for breach of contract only insofar as it pleads a claim for an independent breach of a duty to repurchase defective loans; and (2) dismissing with prejudice the claim for indemnification, including indemnification for attorney's fees.

SURF Series 2006-AB3 action (Index No. 651371/2014)

It is hereby ORDERED that defendants' motion is granted to the extent of dismissing with prejudice as against defendant Merrill Lynch Mortgage Investors, Inc. the first cause of action (alleging breaches of representations and warranties and an independent breach of a duty to repurchase defective loans); and it is further

ORDERED that defendants' motion is granted to the extent of (1) dismissing with prejudice the first cause of action as against defendant Merrill Lynch Mortgage Lending, Inc. only insofar as it pleads a claim for an independent breach of a duty to repurchase defective loans; and (2) dismissing with prejudice the claim for indemnification, including indemnification for attorney's fees; and it is further

ORDERED that the branch of the motion for dismissal of the second cause of action (breach of defendants' notice obligations) as against defendants Merrill Lynch Mortgage Investors, Inc. and Merrill Lynch Mortgage Lending, Inc. is denied without prejudice. Defendants may move to dismiss this cause of action in conformity with procedures to be established in the coordinated RMBS put-back actions in Part 60 regarding motions with respect to notice claims. Nothing herein shall be construed as determining the scope or import of the Appellate Division Nomura decision (___AD3d ___, 2015 WL 5935177 [Oct. 13, 2015]) with respect to such claims; and it is further

ORDERED that defendants' motion is granted to the extent of dismissing with prejudice the third cause of action against defendant Merrill Lynch Mortgage Investors, Inc. (alleging breaches of representations and warranties in agreements regarding subsequent loan conveyances).

SURF SERIES 2007-AB1 action (Index No. 651388/2014)

It is hereby ORDERED that defendants' motion is granted to the extent of dismissing with prejudice as against defendant Merrill Lynch Mortgage Investors, Inc. the first cause of action (alleging breaches of representations and warranties and an independent breach of a duty to repurchase defective loans); and it is further

ORDERED that defendants' motion is granted to the extent of (1) dismissing with prejudice the first cause of action as against defendant Merrill Lynch Mortgage Lending, Inc. only insofar as it pleads a claim for an independent breach of a duty to repurchase defective loans; and (2) dismissing with prejudice the claim for indemnification, including indemnification for attorney's fees; and it is further

ORDERED that the branch of the motion for dismissal of the second cause of action (breach of defendants' notice obligations) as against defendants Merrill Lynch Mortgage Investors, Inc. and Merrill Lynch Mortgage Lending, Inc. is denied without prejudice. Defendants may move to dismiss this cause of action in conformity with procedures to be established in the coordinated RMBS put-back actions in Part 60 regarding motions with respect to notice claims. Nothing herein shall be construed as determining the scope or import of the Appellate Division Nomura decision (___AD3d ___, 2015 WL 5935177 [Oct. 13, 2015]) with respect to such claims.

This constitutes the decision and order of the court.

Dated: New York, New York
December 7, 2015

MARCY S. FRIEDMAN, J.S.C.