COURT OF CHANCERY
OF THE
STATE OF DELAWARE

LEO E. STRINE, JR.
CHANCELLOR

New Castle County Courthouse
Wilmington, Delaware 19801

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Kenneth J. Nachbar, Esquire
R. Judson Scaggs, Jr., Esquire
Ryan D. Stottmann, Esquire
Albert J. Carroll, Esquire
Morris, Nichols, Arsht & Tunnell LLP
1201 N. Market St.
Wilmington, DE 19801

Steven J. Fineman, Esquire
Rudolf Koch, Esquire
Richards, Layton & Finger, P.A.
920 N. King St.
Wilmington, DE 19801

***RE: Central Mortgage Company v. Morgan Stanley Mortgage Capital Holdings LLC,* Civil Action No. 5140-CS**

Dear Counsel:

Plaintiff Central Mortgage Company ("Central Mortgage") moves for reargument of a part of my recent opinion in *Central Mortgage Co. v. Morgan Stanley Mortgage Capital Holdings LLC*, in accordance with Court of Chancery Rule 59(f).[1] For the reasons that follow, I deny its motion.

Central Mortgage's motion must be understood in the context of its relationship with Morgan Stanley. That relationship involved Central Mortgage purchasing the right to service a large number of loans that had been packaged together by Morgan Stanley, many of which, so-called Agency Loans, were sold to Fannie Mae and Freddie Mac. Under arrangements with these Agencies, the Agencies could put the ownership of loans

[1] 2012 WL 3201139 (Del. Ch. Aug. 7, 2012) (*Central Mortgage III*).

back to Central Mortgage or Morgan Stanley in certain circumstances. In its Original Complaint and briefing, Central Mortgage sued on only 47 loans and advanced what is fairly termed its "Agency put-back theory," which is that if ownership of a loan was put back by an Agency to Central Mortgage, then Morgan Stanley was obliged to buy the loan back from Central Mortgage. According to this theory, if the Agency put back a loan, Morgan Stanley must necessarily have breached the representations and warranties it had made to Central Mortgage in its contract between them.[2]

But, as I held both earlier this year and in 2010, the Agency put-back theory is wrong, and "the fact that an Agency puts back a loan does not [in itself] give rise to a breach" of contract between Central Mortgage and Morgan Stanley.[3] I explained that, if there was a *contractual* breach by Morgan Stanley, it occurred when the parties entered into the servicing agreement:

> Those claims accrued under Delaware law when Central Mortgage bought the servicing rights. The accuracy of the underlying loan information data is independent of whether the Agencies put back the loans, because if that information was not accurate, it was not accurate from the time the contract was entered, regardless of whether the Agency discovered it or not.[4]

Because an Agency could also require Central Mortgage to repurchase a loan for reasons that have nothing to do with a breach of Morgan Stanley's representations and

[2] Orig. Compl. ¶¶ 1-4, 34-41, 67; Pl.'s Br. in Opp. at 13-15 (Mar. 19, 2010). *See also* Tr. 67:17-70:7 (May 20, 2010).
[3] *Central Mortgage III*, at *9; *see also Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Hldgs. LLC*, 2010 WL 3258620, at *12 (Del. Ch. Aug. 19, 2010) (*Central Mortgage I*).
[4] *Central Mortgage III*, at *20.

warranties to Central Mortgage,[5] Morgan Stanley would not have any fair notice that it might be sued on a loan merely because the Agencies had put it back to Central Mortgage.[6]

In its Original Complaint, Central Mortgage sued on the 47 loans because it had been obliged to repurchase them from the Agencies, and Morgan Stanley had refused to make it whole. It did not sue on any other loans. But, its Original Complaint ominously mentioned that the Agencies had made a preliminary, but not final, decision to put back 140 loans to Central Mortgage – while at the same time admitting that Central Mortgage could not predict how many of these 140 loans the Agencies would ultimately decide to put back, because the Agencies' review process was still underway.[7] When this case came before me on remand, Central Mortgage did not simply proceed on the Original Complaint, or the Original Complaint and 140 additional loans, but sued on an additional 13,000 loans! I ruled that those 13,000 loans were time-barred by the statute of limitations, and that the allegations in the Amended Complaint as to them did not relate back to the time of the Original Complaint under Court of Chancery Rule 15(c).

In this motion for reargument, Central Mortgage claims that I incorrectly dismissed its complaint relating to the 140 loans, out of the 13,000, that it said in the Original Complaint that the Agencies had made a preliminary, but not final, decision to

[5] *Id*. at *21.
[6] *Id.*; *Central Mortgage I*, at *12.
[7] Orig. Compl. ¶¶ 7, 92; *Central Mortgage I*, at *6.

put back. The court will grant a motion for reargument if the moving party shows that the court "misapprehended law or facts that affected the outcome of the decision."[8] But, I did not misapprehend anything.

Central Mortgage argues that its claims on these 140 loans are not time-barred, because they relate back to the time of the Original Complaint. Under Court of Chancery Rule 15(c), an amended pleading relates back to the date of an original pleading when "the claim or defense asserted in the amended pleading arose out of the conduct, transaction or occurrence set forth or attempted to be set forth in the original pleading."[9] The original pleading must give the opposing party "fair notice of the general fact situation out of which the claim or defense arose,"[10] and this notice is the "determinative factor" in the application of Rule 15(c).[11]

But Rule 15(c), by its own terms, cannot apply to this situation. As I held in my ruling in August, each sale of a loan from Morgan Stanley to Central Mortgage was a *separate and independent transaction* for purposes of Rule 15(c).[12] This is because the contracts between Central Mortgage and Morgan Stanley treated each loan distinctly, by requiring Central Mortgage to give notice of the breach of the representations and warranties as to any particular loan before making a claim on that loan. Thus, the

[8] *Ramon v. Ramon*, 963 A.2d 128, 135 (Del. 2008)*; accord Bernstein v. TractManager, Inc.*, 953 A.2d 1003, 1014 (Del. Ch. 2007).
[9] Ct. Ch. R. 15(c)(2).
[10] *Mullen v. Alarmguard of Delmarva, Inc.*, 625 A.2d 258, 264 (Del. 1993).
[11] *Atlantis Plastics Corp. v. Sammons*, 558 A.2d 1062, 1065 (Del. Ch. 1989) (citation omitted).
[12] *Central Mortgage III*, at *18.

breaches of contract alleged by Central Mortgage were "based on different loans and *distinct instances of misrepresentation*."[13] Central Mortgage repeatedly acknowledged this in both its Original and Amended Complaints. Central Mortgage complained of Morgan Stanley's "multiple *independent* breaches of its representations and warranties"[14] and pled that Morgan Stanley had "failed to provide true, complete and accurate information," such as borrower income level or loan-to-value ratio, "[w]ith respect to *each Mortgage Loan*."[15] Central Mortgage even illustrated the separate nature of each of the misrepresentations in exhibits attached to its Original and Amended Complaints, where it documented, line by line for each Agency loan at issue, how it believed Morgan Stanley provided inaccurate or incomplete information in up to 15 different ways.[16] But the Original Complaint addressed only the 47 loans upon which Central Mortgage was then suing, and made only a cursory mention of the other 140 loans.[17] This is because the Original Complaint did not even "attempt to set forth" a claim as to those 140 loans.[18]

[13] *Id*. at *18 & n.154 (emphasis added).
[14] Orig. Compl. ¶ 108; *see also id*. ¶ 98 (complaining of "Morgan Stanley's multiple independent contractual breaches").
[15] Am. Compl. ¶ 92 (emphasis added); *see also id.* ¶¶ 93, 96; Orig. Compl. ¶ 83.
[16] Orig. Compl. Ex. K (showing 10 different ways in which each of the 47 loans were in violation of the agreement); Am. Compl. Ex. G (showing 15 different ways in which each of 226 Agency loans were in violation of the agreement).
[17] Orig. Compl. ¶¶ 7, 92.
[18] Ct. Ch. R. 15(c) ("An amendment of a pleading relates back to the date of the original pleading when … (2) the claim or defense asserted in the amended pleading arose out of the conduct, transaction or occurrence set forth or attempted to be set forth in the original pleading ….").

This sharply contrasts with the Original Complaint's detailed treatment of the 47 loans upon which the Original Complaint focused.[19]

For the same reason, Morgan Stanley did not have "fair notice" that it would be sued on the 140 new loans simply because it was sued on the 47 loans in the Original Complaint. Central Mortgage could have sued on the 140 new loans within the statute of limitations. As I observed, each alleged breach of representations and warranties occurred when Morgan Stanley sold the servicing rights to Central Mortgage, and the claims accrued at this time.[20] But Central Mortgage deliberately chose not to investigate the alleged breaches of representations and warranties in a timely fashion, for its own economic reasons, and instead waited until the Agencies had finally decided to put back the loans.[21] It is hardly notice, let alone "fair notice," under Rule 15(c) for a party to file a complaint mentioning a potential claim that it was expressly not yet making and that thus lacked supporting allegations of fact, but deliberately *not* sue on it, let that never-asserted claim lapse under the statute of limitations, and then bring it *after* the statute of limitations has run and argue that the by-now belatedly asserted claim relates back to the earlier complaint in which it was first mentioned as a future potential claim, but expressly

[19] Orig. Compl. ¶ 5 (stating that Morgan Stanley had refused to repurchase "nearly fifty" put back loans); *id*. ¶ 79 (claiming that Central Mortgage gave Morgan Stanley notice "[f]or every loan that Morgan Stanley has refused to repurchase from, or reimburse, Central Mortgage"); *id*. ¶¶ 82-89 (discussing Morgan Stanley's breaches as to these loans); *id*. ¶¶ 97, 106 (alleging breach of contract and breach of representations and warranties as to these loans); *id*. Ex. K (listing alleged breaches for each of the 47 loans).
[20] *Central Mortgage III*, at *17, *20.
[21] *Id*. at *18.

disclaimed as being brought yet.[22] A new claim cannot fairly "relate back" to an original complaint that said it was *not* asserting that claim. In the precise words of Rule 15(c)(2), claims as to the 140 loans were expressly *not* "attempted to be set forth" in Central Mortgage's Original Complaint.

Even if the Agency put-back theory was correct (which it is not), Central Mortgage's relation back argument would still fail. This is because Morgan Stanley had no notice that it might be sued for a loan just because an Agency had preliminarily decided to put it back to Central Mortgage. Central Mortgage essentially concedes this point in a footnote in its motion for reargument by noting that it has successfully challenged numerous preliminary decisions by the Agencies to put back loans: "By the Original Complaint's filing date, CMC had received and notified Morgan Stanley of 152 preliminary rejections, *47 of which were successfully appealed* and 105 which were finally rejected."[23] Because the Agencies ultimately decided to retain one third of the 140 loans they preliminarily decided should be put back, even under Central Mortgage's erroneous Agency put-back theory Morgan Stanley could not have "fair notice," and Central Mortgage's argument for relation back also fails for that reason.

My decision therefore misapprehended nothing about Central Mortgage's approach to these 140 loans. I specifically addressed its prior admission that it was not

[22] *Cf. Parker v. Breckin*, 620 A.2d 229, 230 (Del. 1993) ("[N]otice of the incident giving rise to the suit, or notice of a potential claim, is not enough to satisfy Rule 15(c).").
[23] Mot. for Rearg. ¶ 1 n.2 (emphasis added).

suing on the 140 loans in the Original Complaint, and its later and blatantly inconsistent attempt to say that the Original Complaint stated a claim as to those same loans:

> Central Mortgage cannot avoid Delaware law and the plain terms of the Master Agreement by pointing to certain ominous allegations in its Original Complaint, such as the one averring that "currently pending are approximately 140 additional Agency repurchases or reimbursement requests related to Morgan Stanley sold loans" …. *To the extent this allegation can be inferred as a threat to plead contract claims related to those "140 additional Agency repurchases" currently pending, it still does not constitute fair notice under Rule 15(c)* because it does not give Morgan Stanley a basis to determine the "general fact situation" giving rise to the claim for breach of representations and warranties *as to those specific 140 Agency Loans* ….[24]

In unvarnished terms, I specifically considered and rejected the notion that Central Mortgage could "come out threatenin'" and say that as to all other loans it bought from Morgan Stanley, it was poking around and would or might sue in the future at its leisure if it wished to do so.[25] That is not *fair* notice under Rule 15(c). The relation back doctrine is grounded in equity, and its purpose is to "ameliorate the harsh result of the strict application of the statute of limitations" when the defendant should have had notice of the claims.[26] Here, Central Mortgage attempts to have claims it consciously chose not to make in its Original Complaint relate back to that complaint. That is inequitable and inconsistent with the plain

[24] *Central Mortgage III*, at *20 (emphasis added) (citations omitted).
[25] *Id*. at *18.
[26] *Garvin v. City of Phila.*, 354 F.3d 215, 220 (3d. Cir. 2003); *see* 6A Charles Alan Wright et al., *Federal Practice and Procedure: Federal Rules of Civil Procedure* § 1496 (3d ed. updated 2012) ("[Federal Rule 15(c)] has its roots in the former federal equity practice ….").

words of Rule 15(c). The Original Complaint makes plain that Central Mortgage was focused on these 140 loans well in advance of the end of the limitations period, but, instead of reading the files carefully, giving timely contractual notice, and suing upon a lack of cure, Central Mortgage slow-walked the claims and brought them to court after the statute of limitations had expired.

Central Mortgage's approach would thus undermine the purpose of the equity-based relation back doctrine *as well as* the statute of limitations. Because Central Mortgage filed a complaint containing vague threats that it might (or might not!) sue on the 140 loans *before* the expiration of the limitations period, it says it should now be able to make claims on those loans *after* the limitations period has run. But our General Assembly has set the statute of limitations at three years as a matter of policy.[27] Central Mortgage purposely delayed suing on these loans until it filed the Amended Complaint, and it would be unfair to Morgan Stanley if the claims were allowed to proceed having been fairly pled for the first time after the statute of limitations period expired.[28]

In sum, Central Mortgage's motion for reargument is an admission that a sophisticated party could have brought claims within the time period the General Assembly established, but chose not to do so. It seeks relief from its own lack of

[27] 10 *Del. C.* § 8106(a).
[28] *See Chaplake Hldgs Ltd. v. Chrysler Corp.*, 766 A.2d 1, 8 (Del. 2001) (explaining that the court should not permit relation back if it prejudices a party) (citing *Hill v. Shelander*, 924 F.2d 1370, 1377 (7th Cir. 1991)).

diligence solely on the grounds that it told the other party that some day when it got around to doing so, it might bring additional future claims. Sanctioning such a theory of Rule 15 would create unhealthy incentives for gamesmanship and delay, and make an already very expensive system of dispute resolution even less cost-effective.

Because I did not misapprehend Central Mortgage's argument or the facts of the case, its motion to reargue is DENIED.

Very truly yours,

/s/ Leo E. Strine, Jr.

Chancellor