

**Home Equity Mtge. Trust Series 2006-5 v DLJ Mtge.  
Capital Inc.**

2013 NY Slip Op 32265(U)

September 18, 2013

Supreme Court, New York County

Docket Number: 653787/2012

Judge: Melvin L. Schweitzer

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SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: MELVIN L. SCHWEITZER
Justice

PART 45

HOME EQUITY MORTGAGE TRUST SERIES 2006-5

INDEX NO. 653787/2012

-v-

MOTION DATE

DLJ MORTGAGE CAPITAL, INC. et al

MOTION SEQ. NO. 002

The following papers, numbered 1 to , were read on this motion to/for
Notice of Motion/Order to Show Cause — Affidavits — Exhibits
Answering Affidavits — Exhibits
Replying Affidavits

Upon the foregoing papers, it is ordered that this motion by defendants to dismiss with respect to the failure to notify cause of action is DENIED;

The motion with respect to dismissal of the indemnification cause of action is GRANTED

Plaintiff is granted leave to amend the complaint all as per the attached Decision and Order

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

Dated: September 16, 2013

MELVIN L. SCHWEITZER

- 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 : PART 45

-----X	
HOME EQUITY MORTGAGE TRUST SERIES 2006-5,	:
By U.S. BANK NATIONAL ASSOCIATION, solely in	:
Its capacity as Trustee,	:
	:
Plaintiff,	:
	:
-against-	:
	:
DLJ MORTGAGE CAPITAL, INC., and SELECT	:
PORTFOLIO SERVICING, INC.,	:
	:
Defendants.	:
-----X	

Index No. 653787/2012  
DECISION AND ORDER  
Motion Sequence No. 002

**MELVIN L. SCHWEITZER, J.:**

Defendants move to dismiss the sixth and seventh causes of action of the complaint against SPS pursuant to CPLR 3211 (a) (1), (3), (5), and (7). Plaintiff brings this action alleging breach of contract (the Pooling and Servicing Agreement) where DLJ failed to cure the breached representations and warranties through the repurchase of relevant loans, as provided for in the agreement, and where SPS failed to inform the other parties to the agreement of the breaches upon its discovery of such misrepresentations. The motion to dismiss the complaint against SPS is granted in part and denied in part.

**Background**

This action is brought by Home Equity Mortgage Trust Series 2006-5 (the Trust) by U.S. Bank National Association (the Trustee) in its capacity as Trustee of the Trust. The Trust is a New York common law trust established pursuant to the Pooling and Servicing Agreement (PSA). The Trustee is a national banking association, organized and existing under the laws of

the United States with its principal place of business in St. Paul, Minnesota and an office in New York County.

DLJ Mortgage Capital, Inc. (DLJ) is a Delaware corporation with its principal place of business in New York, New York. It is a wholly owned subsidiary of Credit Suisse Holdings (USA), Inc., and is primarily engaged in the purchase and sale of mortgage loans. In the underlying transaction of this action, DLJ played the role of Seller for the Trust. Select Portfolio Servicing, Inc. (SPS) is a corporation organized under the laws of Utah with its principal place of business in Salt Lake City, Utah. It, like DLJ, is a wholly owned subsidiary of Credit Suisse Holdings (USA), Inc. SPS acted as Servicer and Master Servicer for the Trust.

The Trust was created in 2006 to hold mortgage loans that DLJ had either previously originated or acquired from third-party originators. The Trust purchased a pool of mortgage loans from DLJ and issued certificates to investors that represent interests in the assets of the Trust. The mortgage loans were initially sold by DLJ to Credit Suisse First Boston Mortgage Securities Corporation (the Depositor) pursuant to an Assignment and Assumption Agreement. The Depositor then conveyed the loans to the Trust and assigned all of its right, title, and interest in the loans to the Trustee for the benefit of the certificateholders pursuant to the PSA.

When the mortgage-backed securities were issued, DLJ made a series of representations to the Trust regarding the characteristics and risk profiles of the underlying loans. Plaintiff alleges that the investors in the Trust did not have access to the origination files of the relevant loans and therefore could only depend on DLJ's representations as to the quality and characteristics of the loans. Specifically, DLJ allegedly made representations that each of the loans had been originated according to underwriting guidelines that were "designed to ensure the quality" of the loans. Section 2.03 of the PSA states that if the representations were later found

to be false, DLJ would repurchase the loans from the Trust. Alleged breaches of such representations are the foundation of this action.

At the instruction of the directing certificateholders, a “Loan File Review” was undertaken in 2012. The review revealed misrepresentations of income and employment, debt-to-income ratios, properties’ owner-occupancy statuses, and combined loan-to-value ratios. Additionally, the directing certificateholders conducted an Automated Valuation Model analysis (AVM), which found additional breaches of DLJ’s representations and warranties.

After discovering the breached representations, the directing certificateholders delivered notices to DLJ that specifically identified breaches based on the AVM investigation. The first notice identified 284 breached loans and was delivered on November 22, 2011. A copy of the first notice was sent to DLJ on December 7, 2011. The second notice identifying 20 loans was sent to DLJ on December 5, 2012 and a copy was sent to DLJ on December 14, 2012. A third notice identifying 235 breaching loans was sent on February 19, 2013 and a copy of the third notice was sent to DLJ on February 27, 2013. Each of the three notices demanded that DLJ repurchase the breaching loans. DLJ responded only to the first notice and refused to repurchase the loans.

Section 2.03 of the PSA requires all parties, including SPS, to “give prompt notice” to the other PSA parties if they discover that DLJ breached a representation or warranty that materially and adversely affects the interests of the certificateholders in any loan. SPS, as a servicer, modified mortgages in certain instances in which borrowers were unable to make loan payments. Plaintiff alleges that the process of loan modification requires SPS to scrutinize the underlying origination files and any supplemental information provided by the borrower to assess the

borrower's ability to pay. It claims that SPS likely became aware of the breached representations through the loan modification process.

Plaintiff also claims that SPS was also responsible for determining whether delinquent loans should be "charged off" and then "released" from the Trust. This process allegedly requires SPS to assess whether a "Significant Net Recovery" would be possible on the severely delinquent loans, which would require SPS to decide whether the borrowers had the current ability to pay. As in the loan modification process, SPS allegedly was required to scrutinize the underlying origination files as well as supplementary information to assess the borrower's ability to pay. Plaintiff claims that this process likely would have caused SPS to become aware of the breached representations.

Plaintiff's first cause of action against SPS is for breach of contract: failure to notify. Section 2.03 (f) requires SPS, as a servicer, to give prompt written notice to the other PSA parties when it discovers that any loans breached DLJ's representations and warranties. Plaintiff alleges that SPS knew that the loans breached DLJ's representations and warranties but failed to notify the Trustee of such breaches. Plaintiff also alleges that SPS's breaches are material and adverse to the value of the loans and the interests of the certificateholders, which resulted in damages to the Trust.

Plaintiff's second cause of action against SPS is for indemnification. Section 8.05 of the PSA requires SPS to indemnify the Trustee for any expense, including attorney's fees and expenses, incurred in connection with any claim or legal action relating to the PSA, to the extent such indemnity relates to the failure of the Servicer to perform its obligations in accordance with the PSA. Plaintiff claims that because SPS failed to perform its obligations under the PSA, part

of which is a reason for this legal action, it must indemnify the Trustee for its expenses incurred in bringing this action.

### Discussion

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); *Fontanetta v Doe*, 73 AD3d 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 definitely disposes of the plaintiff’s claim.” *Ozdemir v Caithness Corp.*, 285 AD2d 961, 963 (3d Dept 2001), *leave to appeal denied* 97 NY2d 605. In other words, “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 NY2d 314, 326 (2002).

On a motion to dismiss for failure to state a cause of action, the court accepts all factual allegations pleaded in plaintiff’s complaint as true, and gives plaintiff the benefit of every favorable inference. CPLR 3211 (a) (7); *Sheila C. v Povich*, 11 AD3d 120 (1st Dept 2004). The court must determine whether “from the [complaint’s] four corners[,] ‘factual allegations are discerned which taken together manifest any cause of action cognizable at law.’” *Gorelik v Mount Sinai Hosp. Ctr.*, 19 AD3d 319 (1st Dept 2005) (quoting *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 (1977)). Vague and conclusory allegations are not sufficient to sustain a cause of action. *Fowler v American Lawyer Media, Inc.*, 306 AD2d 113 (1st Dept 2003).

### Standing

SPS argues that the complaint against it must be dismissed in its entirety because the Trust, as opposed to the Trustee, is the actual plaintiff bringing suit and a Trust does not have the

requisite standing to sue to enforce the PSA. It argues that because the Trustee is not a plaintiff in the action, the Trust cannot assert claims on its behalf. The court finds both arguments unavailing.

SPS claims that the actual plaintiff in this case is the Trust, not the Trustee, and that even if the Trustee were the intended plaintiff, the complaint does not sufficiently reflect that position. It cites a recent decision, *Master Adjustable Rate Mortgages Trust 2006-OA1 (MARM), et al. v. UBS Real Estate Securities, Inc.*, Index No. 651282/2012, in which the court granted the defendants' motion to dismiss for lack of standing without prejudice. Although the court in *MARM* granted the motion, there are several distinctions that can be drawn between that case and the subject action.

First, the *MARM* complaint did not name the trustee in the caption and also lacked specific allegations that the trustee was bringing the action on behalf of the trust. Here, the complaint not only names the Trustee in the caption, but also consistently and repeatedly makes clear that the Trustee is acting on behalf of the Trust.<sup>1</sup> Second, in *MARM*, after finding that the complaint was unclear as to whether the trust or trustee was the actual plaintiff, the court offered the plaintiff three choices: 1) obtain some form of authorization from the trustee indicating approval to continue the litigation on its behalf, 2) commence a special proceeding to compel the trustee to bring suit for the trust, or 3) amend the complaint to include allegations that make clear that the trustee is the actual plaintiff. The court was prepared to grant the plaintiff an opportunity to amend the complaint without dismissing the complaint. Third, the *MARM* complaint also improperly named a certificate holder as a plaintiff. This issue was raised after

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<sup>1</sup> Apart from naming the Trustee in the caption, the complaint also states that the Trust is "acting through the Trustee." Additionally, the causes of action laid out at the end of the complaint specify the Trustee as the source of many relevant actions and allegations.



the court offered the aforementioned choices to the plaintiff. For that reason, in addition to the plaintiff's willingness to file an amended complaint, the court chose to grant the motion to dismiss without prejudice so that the parties could begin anew with a clean slate.

The presence of a certificateholder as an inappropriate plaintiff is not at issue in this action. In *MARM*, but for the presence of that certificate holder, the court was prepared to allow the plaintiff to amend its pleadings to meet the required standard.

SPS also argues that the Trustee should be a stand-alone plaintiff. Not only does SPS offer no evidence to support its claim, but if the Trustee were required to be a stand-alone plaintiff, the proper remedy would not be a dismissal of the complaint, but an amendment to the caption. An amendment would follow our policy of favoring liberal amendments to pleadings. *Am. Home Assur. Co. v Scanlon*, 164 AD2d 751, 752 (1st Dept 1990). The original complaint sufficiently placed the defendants on notice of the subject action and an amendment would not unduly prejudice them in any way. NY CPLR 2001 (providing that the court may permit a mistake or defect to the pleadings may be corrected if a substantial right of a party is not prejudiced).

The original complaint is sufficient in its current form. It is clear to the court that both the Trust and the Trustee are plaintiffs and the challenge to standing is not cause for dismissal. Nevertheless, to ensure the absence of doubt with respect to this matter, the plaintiff is granted leave to amend the complaint to add the Trustee as a stand-alone plaintiff in addition to the Trust. Both the Trust and Trustee are plaintiffs and the challenge to standing is not cause for dismissal. The plaintiff is granted leave to amend the complaint. As the court finds that the complaint contains sufficient allegations to establish the Trustee as the plaintiff, bringing suit on

behalf of the Trust, it is unnecessary to address the defendants' argument that the Trust cannot seek relief on behalf of the nonparty Trustee.

Breach of Contract: Failure to Notify

Plaintiff's first cause of action against SPS, and sixth cause of action in the complaint, is for breach of contract: failure to notify. SPS claims that this cause of action must be dismissed because the plaintiff's allegations that SPS has breached the PSA by failing to inform it of DLJ's breached representations are speculative and conclusory. Section 2.03 (f) of the PSA states in relevant part:

“Upon discovery by any of the parties hereto of a breach of a representation or warranty made pursuant to Section 2.03 (e) that materially and adversely affects the interests of the Certificateholders in any Mortgage Loan, the party discovering such breach shall give prompt notice thereof to the other parties.”<sup>2</sup>

SPS also argues that the plaintiff's allegations that it breached its servicing obligations pursuant to the PSA are based on misunderstandings of what qualifies as servicing obligations. It states that the plaintiff is making unsubstantiated assumptions that when making loan modifications or releasing loans, SPS must have reviewed the “origination files, underwriting guidelines, and deal-specific representations and warranties” relevant to the analysis of whether a material breach of such representations and warranties took place.

The inquiry of whether the duty to notify other parties to the PSA is a servicing obligation is inappropriate to ask at the motion to dismiss stage. On a motion to dismiss for failure to state a cause of action, the court accepts all factual allegations pleaded in plaintiff's complaint as true, and gives plaintiff the benefit of every favorable inference. NY CPLR 3211 (a) (7); *Povich*, 11 AD3d at 120. The plaintiff alleges in the complaint that, upon information

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<sup>2</sup> The referenced representations and warranties from Section 2.03 (e) are those made by the Seller (DLJ) to the Trustee and are detailed in Schedule IV of the PSA.

and belief, when SPS performs its servicing obligations of reviewing the loans, assessing the borrower's ability to pay off the loans, modifying the loans, and releasing the loans, it must also re-underwrite the loans. This process allegedly requires SPS to review the origination files. As the court takes the plaintiff's allegations in the complaint as true, SPS's argument that the alleged underlying understanding of SPS's servicing obligations is incorrect is to no avail.

The plaintiff's allegations in the complaint are also sufficient to survive a motion to dismiss. The complaint not only claims that SPS has breached the PSA by failing to notify the other parties of the discovered breaches, but it also specifies the process by which SPS's obligations under the PSA led it to discover the breached representations.

As the court finds that the complaint is not conclusory, SPS's motion to dismiss the complaint with respect to the cause of action for breach of contract – failure to notify, is denied.

#### Breach of Contract: Indemnification

Plaintiff's second cause of action against SPS, and seventh cause of action in the complaint, is for breach of contract: indemnification. SPS seeks to dismiss this claim on the ground that plaintiff does not allege that SPS has failed to perform its obligations to properly service the loans. SPS also claims that the circumstances of this case fall under the exception to the indemnification provision, which does not mandate indemnification where the costs sought are incurred from actions directed by the certificateholders. Section 8.05 of the PSA states in relevant part:

“The Trustee and any director, officer, employee or agent of the Trustee shall be indemnified by the Depositor and the Servicers, to the extent such indemnity related to the failure of the related Servicer to perform its servicing obligations in accordance with this Agreement . . . other than any loss, liability or expense incurred by reason of willful misfeasance, bad faith or negligence in the performance of any of the Trustee's duties hereunder or incurred by reason of any action of the Trustee taken at the direction of the Certificateholders.”

The PSA is the controlling document in this action and the contractual language specifically provides an exception to the indemnification clause. In circumstances where the certificateholders direct the initiation of the lawsuit, the Trustee does not receive indemnification from the servicer. Here, the plaintiff seeks indemnification for the expenses incurred in bringing the subject action and argues that the exception to the indemnification provision does not apply in this case because the costs for which it seeks indemnification were not necessarily incurred by reason of the certificateholders.

The plaintiff's argument is defeated by language found elsewhere in its own complaint. While the complaint states that "SPS must indemnify the Trustee for its expenses, including attorney's fees and expenses, incurred in bringing this action . . .," it also states that "the Trust, acting through the Trustee (acting, in turn, at the instruction of the Directing Certificateholders), now brings this action for breach of contract, specific performance, and the declaratory judgment to enforce the obligations of DLJ and SPS under the PSA." The Trustee seeks indemnification for the expenses incurred in bringing this action, and the subject action was instigated at the direction of the directing certificateholders – placing these circumstances directly within the scope of the exception to the indemnification provision.

Apart from the provision of the PSA excluding indemnification from SPS in this circumstance, there is another provision that protects the Trustee from the costs associated with actions related to the PSA. Section 10.08 of the PSA outlines criteria that must be met before certificateholders are able to institute a legal proceeding with respect to this agreement. One such requirement concerns indemnification of the incurred costs: "[the certificateholder] shall have offered to the Trustee such reasonable indemnity as it may require against the costs, expenses, and liabilities to be incurred therein or thereby . . . ." The PSA already encompasses

how indemnification must occur in this situation. The only way in which the directing certificateholders are able to instruct the Trustee to bring this action, as alleged in the complaint, is that they are also indemnifying the Trustee for the incurred expenses with relation to this action. The indemnification that the Trustee is seeking from SPS has already been given to it by the certificateholders.

It is clear that the plaintiff seeks indemnification for the costs incurred in bringing the subject action and that the subject action was brought at the direction of the directing certificateholders. These circumstances firmly place this action within the intention of the exception to indemnification from the servicer. Additionally, the plaintiff is already protected from the liabilities incurred as a result of bringing this action. The motion to dismiss is granted with respect to the cause of action seeking indemnification.

#### Damages

SPS seeks to dismiss the plaintiff's claims for consequential and rescissory damages based on its cause of action against SPS for failure to notify. SPS argues that consequential damages are inappropriate because the PSA does not provide for such a remedy. It also argues that rescissory damages are inappropriate because 1) plaintiff is not seeking to rescind the PSA, it is seeking to enforce it, and 2) a recent First Department decision makes rescissory damages legally unavailable.

Consequential damages are rarely awarded to parties. *See Brody Truck Rental, Inc. v Country Wide Ins. Co.*, 277 AD2d 125 (1st Dept 2000). It is permitted only where the contract clearly conveys that the parties intended consequential damages to be part of the recoverable remedies. *Id.* As stated in *Brody Truck Rental*,

“In claims for breach of contract, a party's recovery is ordinarily limited to “general damages which are the natural and probable consequence of the breach[;]” any additional recovery must be premised upon a showing that the unusual or extraordinary damages sought were “ ‘within the contemplation of the parties as the probable result of a breach at the time of or prior to contracting.’”

*Brody Truck Rental*, 277 AD2d at 125 (citing *Kenford Co., Inc. v County of Erie*, 73 N.Y.2d 312, 319).

Section 2.03 of the PSA states that the repurchase protocol is the sole remedy for any breaches of representations or warranties. There is no language in the PSA indicating that consequential damages were within the contemplation of the parties, which is the requirement for an award of such damages. There is no basis for the plaintiff's request for consequential damages.

Like consequential damages, rescission is a “rarely used equitable tool.” *MBIA Ins. Corp. v Countrywide Home Loans, Inc.*, 105 AD3d 412, 413 (1st Dept 2013). Rescissory damages are generally available only where rescission is impracticable and there are no alternative legal remedies. See *MBIA Ins. Corp.*, 105 AD3d at 413 (1st Dept 2013); *Alper v Seavey*, 9 AD3d 263, 264 (1st Dept 2004). Plaintiff's arguments supporting an award of rescissory damages are unavailing because it does not seek rescission and also because there is an available alternative remedy.

Defendants argue that because plaintiff is seeking to enforce the PSA, it cannot simultaneously seek to rescind the same agreement. Despite the plaintiff's adamant averments that it has claimed its rights to rescind the PSA, but is seeking rescissory damages instead because rescission is impracticable, the pleadings show that the plaintiff is not seeking rescission; it seeks enforcement of the PSA. An award of rescissory damages is an alternative remedy in cases where rescission itself is not viable. See *MBIA Ins. Corp.*, 105 AD3d at 413

(holding that granting a motion for summary judgment awarding rescissory damages was inappropriate because rescission was not warranted)<sup>3</sup>. Here, rescission was not sought and therefore rescissory damages are unavailable.

That the plaintiff has an alternative remedy to protect its contractual rights also supports a denial of rescissory damages. As previously discussed, section 2.03 of the PSA offers the repurchase protocol as the sole remedy for any breach of representations or warranties. The agreement itself offers the plaintiff a viable remedy that it is seeking to enforce in this action.

Plaintiff argues that because the sought consequential and rescissory damages are specified as prayers for relief in the complaint, it is currently premature to dismiss them. *Sand Canyon Corp. v Homeward Residential, Inc.*, 36 Misc 3d 1228(A) (Sup. Ct. 2012) (Schweitzer, J.) (“[A] motion to dismiss for failure to state a claim addresses the alleged cause of action and not the remedy sought”). In *Sand Canyon*, the defendant sought to dismiss the plaintiff’s claim for an injunction on the basis that the request was “too vague.” *Id.* The court denied the motion because the court found that the pleadings were adequate with respect to the remedies sought – there was no merit to the defendant’s arguments.

Unlike the cases the plaintiff cites in defense of its position, the adequacy of the pleadings with respect to the sought remedies is not at issue in this action. The arguments supporting an award of either consequential or rescissory damages are meritless. No further analysis or discovery of facts will allow the plaintiff to recover the sought damages, and therefore it is unnecessary to delay the resolution of these issues to a future time. SPS’s motion to dismiss is granted with respect to plaintiff’s request for consequential and rescissory damages.

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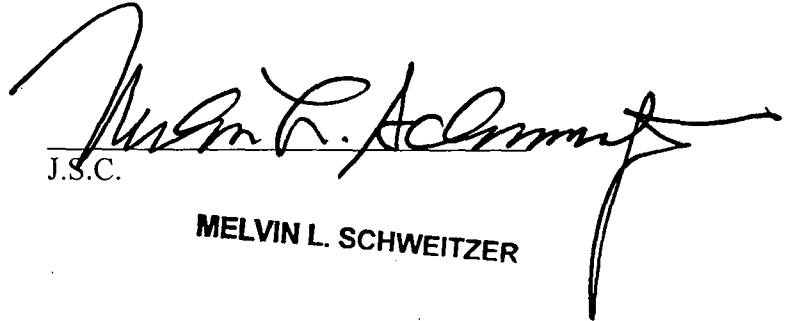
<sup>3</sup> Although the court in *MBIA Ins. Corp.* found that rescissory damages were legally unavailable because the plaintiff had previously given up its right to seek rescission, the court also recognized that the plaintiff did not actually seek rescission. *MBIA Ins. Corp.*, 105 AD3d at 413 (“Plaintiff should not be permitted to utilize this very rarely used equitable tool . . . to reclaim a right it voluntarily contracted away or to obtain relief it never actually requested”).

**Conclusion**

ORDERED that defendants' motion to dismiss is denied with respect to the failure to notify cause of action, granted with respect to the indemnification cause of action, and plaintiff is granted leave to amend the complaint.

Dated: September 18, 2013

ENTER:

  
J.S.C.  
MELVIN L. SCHWEITZER