New York County Clerk's Index No. 650980/12

Supreme Court of the State of New York

APPELLATE DIVISION — FIRST DEPARTMENT

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006,

Plaintiff-Respondent,

—against—

DB STRUCTURED PRODUCTS, INC.,

Defendant-Appellant.

MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE*

GEORGE T. CONWAY III
JEFFREY D. HOSCHANDER
JUSTIN V. RODRIGUEZ
CAITLIN A. DONOVAN
WACHTELL, LIPTON, ROSEN & KATZ
51 West 52nd Street
New York, New York 10019
212-403-1000
gtconway@wlrk.com

Attorneys for Amicus Curiae *the Securities Industry and Financial Markets Association*

SUPREME COURT OF THE STATE OF NEW YORK
APPELLATE DIVISION—FIRST DEPARTMENT

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006, *Plaintiff-Respondent*, — against — DB STRUCTURED PRODUCTS, INC., *Defendant-Appellant.*	Index No.: 650980/2012

NOTICE OF MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE*

PLEASE TAKE NOTICE that upon the annexed affirmation of George T. Conway III, dated September 26, 2013, the Securities Industry and Financial Markets Association, by its attorneys Wachtell, Lipton, Rosen & Katz, will move this Court, at the Supreme Court, Appellate Division, First Department, 27 Madison Avenue, New York, New York 10010, on October 4, 2013 at 10:00 a.m. or as soon thereafter as counsel may be heard, for an order permitting the Securities Industry and Financial Markets Association to serve and file a brief as *amicus curiae*.

Dated: New York, New York
September 26, 2013

WACHTELL, LIPTON, ROSEN & KATZ

By: *George T. Conway III*
George T. Conway III

Jeffrey D. Hoschander
Justin V. Rodriguez
Caitlin A. Donovan
51 West 52nd Street
New York, New York 10019
(212) 403-1000
gtconway@wlrk.com

Attorneys for Amicus Curiae *the Securities Industry and Financial Markets Association*

To:

MARC E. KASOWITZ, ESQ. (mkasowitz@kasowitz.com)
MICHAEL M. FAY, ESQ. (mfay@kasowitz.com)
KASOWITZ, BENSON, TORRES & FRIEDMAN LLP
1633 Broadway
New York, New York 10019
(212) 506-1700

Attorneys for Plaintiff-Respondent

THOMAS C. RICE, ESQ. (trice@stblaw.com)
DAVID J. WOLL, ESQ. (dwoll@stblaw.com)
SIMPSON THACHER & BARTLETT LLP
425 Lexington Avenue
New York, New York 10017
(212) 455-2000

Attorneys for Defendant-Appellant

SUPREME COURT OF THE STATE OF NEW YORK
APPELLATE DIVISION—FIRST DEPARTMENT

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AFFIRMATION OF GEORGE T. CONWAY III IN SUPPORT OF MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE*

GEORGE T. CONWAY III, an attorney duly admitted to practice law before the courts of the State of New York, and not a party to this action, affirms the following to be true under penalty of perjury pursuant to CPLR § 2106:

1. I am a member of the law firm of Wachtell, Lipton, Rosen & Katz, attorneys for *amicus curiae* the Securities Industry and Financial Markets Association ("SIFMA"). I respectfully submit this affirmation in support of SIFMA's motion to file a brief as *amicus curiae* in this appeal. SIFMA has a demonstrated interest in the issues in this matter and can be of special assistance to the Court. A copy of SIFMA's proposed brief is attached hereto as Exhibit A.

2. SIFMA is an organization that brings together the shared interests of hundreds of securities firms, banks and asset managers. Its membership encompasses both sides of the securities industry—those who sell securities (issuers and sponsors) and those who purchase them (institutional investors and asset managers). It champions policies and practices that foster a strong financial industry, investor opportunity, capital formation, job creation and economic growth, and that build trust and confidence in the financial markets. One of SIFMA's important functions is to represent its members' interests in cases addressing issues of widespread concern in the securities and financial markets.

3. This appeal raises just such an issue. It presents for review one of two conflicting rulings from Supreme Court on the application of the relevant statute of limitations to claims of alleged breaches of contractual representations and warranties in issuances of residential mortgage-backed securities, or RMBS. This Court's resolution of this issue will likely have far-reaching, multibillion-dollar implications for the securities and financial industries and SIFMA's members.

4. SIFMA brings an industry-wide perspective, distinct from that of the parties. Accordingly, it seeks leave to file a brief as *amicus curiae* to present its position on the issues raised, to provide the Court with important background on the RMBS marketplace, and to inform the Court of the practical consequences of affirmance or reversal of the ruling below.

5. The appeal in this action is taken from a decision of the Supreme Court, New York County, issued by Justice Shirley W. Kornreich on May 13, 2013,

denying defendant-appellant's motion to dismiss and finding that the statute of limitations does not bar plaintiff-respondent's claims. *See ACE Sec. Corp. Home Equity Loan Trust, Series 2006-SL2* v. *DB Structured Prods., Inc.*, 40 Misc. 3d 562 (Sup. Ct. N.Y. Cnty. 2013). A true and correct copy of the decision is attached hereto as Exhibit B.

6. Three days earlier, Justice O. Peter Sherwood had issued a conflicting decision on the application of the statute of limitations to claims of alleged breaches of representations and warranties in RMBS issuances, granting the defendant's motion to dismiss and finding that the statute of limitations does bar plaintiff's claims. *See Nomura Asset Acceptance Corp., Alternative Loan Trust, Series 2005-S4* v. *Nomura Credit & Capital, Inc.*, 39 Misc. 3d 1226(A), 2013 N.Y. Slip Op. 50743(U) (Sup. Ct. N.Y. Cnty. May 10, 2013).

7. On June 3, 2013, the defendant-appellant in *ACE* served its notice of appeal, a true and correct copy of which is attached hereto as Exhibit C, and on June 20, 2013, plaintiff-appellant in *Nomura* served a Notice of Appeal on defendant-respondent. The defendant-appellant in *ACE* perfected its appeal by filing and serving a brief on July 8, 2013; but the plaintiff-appellant in *Nomura* has yet to perfect its appeal.

8. On July 24, 2013, counsel for defendant-appellant in *ACE* and defendant-respondent in *Nomura* filed a joint motion for coordination of oral argument in the two appeals along with affirmations in support. Those parties asked that the coordinated arguments be held in the November 2013 term, or as soon thereafter as

the Court deemed appropriate.

9. On August 9, 2013, defendant-appellant in *ACE* filed a reply affirmation in further support of the motion for coordination. Annexed to that reply affirmation was an affirmation submitted by me on behalf of SIFMA. In that affirmation, I expressed SIFMA's significant interest in the issues the cases presented, its support for the motion for coordination, its intention to seek leave to file a brief as *amicus curiae* in the appeals, and its belief that a single *amicus* brief addressing *ACE* and *Nomura* together would constitute the most efficient way to provide meaningful assistance to this Court.

10. On September 10, 2013, the Court denied the motion for coordination. *See Nomura Asset Acceptance Corp., Alternative Loan Trust, Series 2005-S4* v. *Nomura Credit & Capital, Inc.*, 2013 N.Y. Slip Op. 84722(U) (1st Dep't Sept. 10, 2013).

11. In light of the Court's decision not to coordinate the *ACE* and *Nomura* appeals, SIFMA seeks leave by this motion to file a brief as *amicus curiae* in the *ACE* appeal. It is our understanding that, as of the date of this affirmation, oral argument on the *ACE* appeal has been adjourned to the November 2013 term.

12. Given SIFMA's perspective as a representative of the financial industry, SIFMA believes that its proposed brief will be of considerable assistance to the Court in resolving this appeal, and respectfully requests that it be considered by the Court. SIFMA believes that it is particularly important that its views be heard here, because the IAS Court's decision is of enormous legal, practical, and finan-

cial significance. Many billions of dollars are at stake in this and in many similar cases, and the decision below contradicts black-letter law that a breach of a representation or warranty is a breach that starts New York's six-year statute of limitations for breach of contract claims. As we show in our brief, the decision below mistakenly uses the parties' agreement that repurchase of a loan would be the "sole remedy" available—clearly meant as a limitation on liability—as a springboard to effectively eliminate a statute of limitations altogether on claims for breach of representations or warranties. Our brief also explains how the decision below undermines any commercial agreement intended to create a remedy that limits liability; threatens New York's longstanding policy of enforcing contracts between sophisticated parties as written; and allows plaintiffs to commence stale and complex loan repurchase litigation that would burden the New York courts for many years to come.

WHEREFORE, on behalf of proposed *amicus curiae* the Securities Industry and Financial Markets Association, I respectfully request that the Court grant SIFMA's motion for leave to file a brief as *amicus curiae*.

Dated: New York, New York
September 26, 2013

George T. Conway III

George T. Conway III

Affirmation of George T. Conway III
in Support of Motion for Leave to File Brief as *Amicus Curiae*

EXHIBIT A

New York County Clerk's Index No. 650980/12

Supreme Court of the State of New York

APPELLATE DIVISION — FIRST DEPARTMENT

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006,

Plaintiff-Respondent,

—against—

DB STRUCTURED PRODUCTS, INC.,

Defendant-Appellant.

BRIEF FOR *AMICUS CURIAE* THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF DEFENDANT-APPELLANT

GEORGE T. CONWAY III
JEFFREY D. HOSCHANDER
JUSTIN V. RODRIGUEZ
CAITLIN A. DONOVAN
WACHTELL, LIPTON, ROSEN & KATZ
51 West 52nd Street
New York, New York 10019
212-403-1000
gtconway@wlrk.com

Attorneys for Amicus Curiae *the Securities Industry and Financial Markets Association*

Printed on Recycled Paper

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STATEMENT OF INTEREST OF *AMICUS CURIAE*

The Securities Industry and Financial Markets Association ("SIFMA") brings together the shared interests of hundreds of securities firms, banks and asset managers. Its membership encompasses both sides of the securities industry—those who sell securities (issuers and sponsors) and those who purchase them (institutional investors and asset managers). SIFMA champions policies and practices that foster a strong financial industry, investor opportunity, capital formation, job creation and economic growth, and that build trust and confidence in the financial markets.

One of SIFMA's important functions is the representation of its members' interests in cases addressing issues of widespread concern in the securities and financial markets. In this regard, although it is judicious in its case selection, SIFMA frequently appears as *amicus curiae* in cases that raise important policy issues that impact the markets represented by SIFMA or otherwise affect common practices in the financial services industry. The fundamental issues of import to the securities and financial markets raised in this appeal make this a paradigm of a case in which SIFMA believes its members should be heard.

This case presents for review one of the two conflicting rulings issued by the Commercial Division within days of each other. Both are on appeal before this Court, and both concern the application of New York's six-year statute of limitations to claims of alleged breaches of contractual representations and warranties in issuances of residential mortgage-backed securities, or RMBS. This appeal will determine whether key contractual terms agreed to by sophisticated parties and crafted to limit remedies available for breaches of representations and warranties will be judicially rewritten to permit litigation in perpetuity. This Court's resolution of this issue will likely have far-reaching, multibillion-dollar implications for the securities and financial industries and SIFMA's members, and more generally, will affect the drafting and enforcement of all manner of complex business contracts under New York law. SIFMA accordingly files this *amicus curiae* brief to present its position on this issue, to provide the Court with important context on the RMBS marketplace, and to inform the Court of the practical consequences of affirmance or reversal of the conflicting rulings below.

PRELIMINARY STATEMENT

This is one of a large number of highly complex cases pending in Supreme Court that involve RMBS repurchase, or put-back, claims. RMBS are securities created out of pools of home mortgages; the mortgages are put into trusts, and investors can freely buy and sell certificates that represent the right to cash flows from the trusts. The publicly disclosed contracts that established those pools and trusts, which include a number of largely standardized terms, contain numerous representations and warranties made by the sellers of the mortgages. Those representations and warranties do not guarantee the performance of the mortgages over time; they only represent and warrant the characteristics that the mortgages had at the time they were initially pooled into the trust and securitized.

The contracts also contain carefully crafted provisions that restrict the remedies available in the event that any of the loans did not comply with the representations and warranties made by the seller at the time those representations and warranties were made. Those remedy provisions expressly and unequivocally establish the "*sole* remedy" for breaches of the representations and warranties: repurchase of the loan determined to have been put into the trust in breach of the representations and warranties, where the breach had a material and adverse effect on the interests of certificateholders in that loan. As a result, RMBS trustees and investors cannot rescind purchase of the investment certificates; nor may they seek damages. Instead, the contracts provide for a limited and *exclusive* repurchase remedy. If, at the time a representation or warranty was made regarding a loan, that loan breached the representation or warranty, and the breach had the requisite material and adverse effect on the interest of certificateholders in that loan, then the seller must repurchase *that loan*.

The operation of these provisions has now assumed great importance, of course, because of the financial crisis whose rumblings began in 2007, roughly six years ago. By the time the crisis peaked in 2008, RMBS prices had tanked. As mortgage delinquencies rose, ratings agencies downgraded the RMBS, and large institutional investors who were restricted from holding low-rated investments were forced to dump their holdings. The buyers in these massive fire sales were principally hedge funds—so-called "vulture funds"—that, to their credit, profited handsomely from following the old Wall Street adage about buying low.

Some of the hedge funds resorted to another strategy to boost their returns. They invested in RMBS put-back litigation. For several years now they have been agitating for trustees to bring repurchase actions like the one now before this Court. As the years have passed, however, the funds recognized that time was running out under the six-year New York statute of limitations governing contracts, CPLR § 213(2). As the six-year anniversary of the contract and securitization at issue here approached, for example, the vulture funds behind this lawsuit warned the trustee about the "Urgent Need for a Tolling Agreement," and about how "it is imperative that the Trustee act expeditiously" because of "potential expiring statute of limitations deadlines."

The funds were right to do so. As we show below, application of the statute of limitations to RMBS securitizations is really very simple. "In New York, a breach of contract cause of action accrues at the time of breach." *Ely-Cruikshank Co.* v. *Bank of Montreal*, 81 N.Y.2d 399, 402 (1993). It runs from the time of breach "'even though the injured party may be ignorant of the existence of the wrong or injury.'" *Id.* at 403 (citation omitted). And the time of breach of a representation or warranty in an RMBS agreement is the date that the representation or warranty is made, because that is the only time at which the seller represents or warrants the condition of the mortgage loans. So if there is a breach of a representation or warranty at all, it has to occur when the representation or warranty is made, and once the sixth anniversary of that date passes, any claims for such a breach are barred. Every court that has addressed this question while actually discussing New York case law has so held.[1]

Except for the IAS Court below. In the order on appeal here, the IAS Court held that the statute of limitations does not run until the RMBS trustee makes a demand for repurchase, and that demand is refused. That holding means that there is effectively *no* statute of limitations. Demand can be made at any time. If, say, in the year 2034 a trustee purports to discover that representations and warranties made in 2006 were untrue, and that the breach of the representations materially and adversely affected the interest of certificateholders, then on the IAS Court's view, the trustee could make a repurchase demand at that time. And whenever the seller refused to repurchase in response to such a request, then, and only then, would the six-year limitations period begin to run—*through the year 2040 or even beyond.*

This is untenable, and unsupportable under the express terms of the contracts and settled principles of New York law. As we show below, the IAS Court's fundamental conceptual error was to treat what the contract repeatedly calls a

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1 *See Nomura Asset Acceptance Corp.* v. *Nomura Credit & Capital, Inc.*, 39 Misc. 3d 1226(A), No. 653541/2011, slip op. 50743(U) (Sup. Ct. N.Y. Cnty. May 10, 2013); *Lehman Bros. Holdings, Inc.* v. *Evergreen Moneysource Mortg. Co.*, 793 F. Supp. 2d 1189 (W.D. Wash. 2011); *Structured Mortg. Trust 1997-2* v. *Daiwa Fin. Corp.*, No. 02 Civ. 3232 (SHS), 2003 WL 548868 (S.D.N.Y. Feb. 25, 2003). The court in *Lehman Brothers Holdings, Inc.* v. *National Bank of Arkansas*, upon which plaintiff relies, did not cite or discuss New York case law on this point. 875 F. Supp. 2d 911, 916-17 (E.D. Ark. 2012). We note that several RMBS cases pending in Supreme Court, such as *Nomura*, raise the issue of whether the representations or warranties about the mortgage loans, made in the governing contract, are made on the date of the contract itself or made on the closing date of the securitization referenced in the contract. *See Nomura*, 39 Misc. 3d 1226(A) at *6-8, slip op. 50743(U) at 7-8. That much more limited issue is not before the Court on this appeal (because, here, the date of the contract and the closing date are the same), and SIFMA takes no position on that issue in this brief.

"breach"—untrue representations and warranties—as something *other* than a breach, and to treat a refusal to comply with a *remedy* as the only independent breach. New York law does not allow this, and for good reason: it would mean that virtually *any* complex business agreement, not just the RMBS agreements at issue here, could breed litigation in perpetuity if it contains representations and warranties along with an exclusive remedy for breaches of those representations and warrenties. To allow such a result would destroy what the Court of Appeals has found to be the Legislature's "primary purpose" in enacting "a limitations period": to provide "fairness to a defendant" by ensuring that a defendant is "'secure in his reasonable expectation that the slate has been wiped clean of ancient obligations.'" *Duffy* v. *Horton Mem'l Hosp.*, 66 N.Y.2d 473, 476 (1985) (citations omitted).

And if affirmed, the decision below would subvert another critical legislative purpose in enacting statutes of limitations: "the need to protect the judicial system from the burden of adjudicating stale and groundless claims." *Id.* at 476-77. Supreme Court is already *flooded* with RMBS repurchase claims: as Justice Sherwood noted in another RMBS case now on appeal to this Court, there are at least "fourteen such cases involving statute of limitations issues currently pending" in the court below, *Nomura Asset Acceptance Corp.*, 39 Misc. 3d at *1 n.1, slip op. 50743(U) at 1 n.1, and obviously many more not raising any limitations question. Given that the financial crisis is now pushing six years on, that litigation flood should be subsiding—*if* the limitations period is properly applied to the contracts as they were written. But if, as happened below, the contracts are distorted and the statute is not applied, the judges of the court below and this Court—not to mention their successors—will bear the burden of stale RMBS put-back cases for many years to come.

BACKGROUND

A. The RMBS contracts—the representations and warranties, and the limited "sole remedy"

Residential mortgage-backed securities, or RMBS, are a creature of private contract. A financial institution, typically called the "sponsor," sells thousands of residential mortgage loans to a trust, usually through an intermediary. The trust next issues securities—"certificates"—that entitle their holders to cash flows generated by the loans in the trust.[2] These residential mortgage-backed securities are then sold to investors. The investors who bought the securities were sophisticated: they were "predominantly institutional and include banks, insurance companies, hedge funds, mutual funds, foreign central banks, and sovereign wealth funds, as well as Fannie Mae and Freddie Mac."[3]

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[2] *See* THOMAS P. LEMKE *ET AL.*, MORTGAGE-BACKED SECURITIES § 1.1 (2011-2012 ed.); *see also, e.g.*, Joint Task Force, Dep't of the Treasury, Office of Federal Housing Enterprise Oversight, and the Securities and Exchange Commission, *Staff Report: Enhancing Disclosure in the Mortgage-Backed Securities Markets*, at 5, 7 (Jan. 2003) ("Joint Task Force Report"), *available at* http://1.usa.gov/16AVxaP. RMBS referred to in this brief without further description are so-called "private-label" or "non-agency," that is, RMBS issued by private financial institutions rather than by the government sponsored enterprises ("GSEs")—the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac")—or the Government National Mortgage Association ("Ginnie Mae"). *See* Joint Task Force Report at 5-6.

[3] Office of Fed. Hous. Enter. Oversight, *A Primer on the Secondary Mortgage Market*, MMN 08-3 at 8 (July 21, 2008), *available at* http://1.usa.gov/18uIydm.

Those investors could freely buy and sell those RMBS certificates. They could do that because the terms of the contracts defining the rights of those certificates were fully disclosed, well-known and often standardized. Those contracts typically included pooling and servicing agreements ("PSAs") and/or mortgage loan purchase agreements ("MLPAs"). These detailed agreements set forth the rights of various parties, including the investors who purchase the RMBS. For public securitizations they are filed, as they were in this case, with the SEC.[4] Anyone with access to the Internet can review these agreements. And there is no doubt that the sophisticated investors who purchased RMBS could easily have done so before they invested.

One common feature of these contracts is the representations and warranties made by the sponsors. Typically an RMBS sponsor makes numerous representations and warranties about the mortgage loans in the securitization pool, and about the real estate securing those loans. Those representations and warranties do not guarantee the loans' future performance; indeed, "in private-label MBS offerings," that is, offerings made by private sellers (as here, and as opposed to government-sponsored entities, such as Fannie Mae and Freddie Mac), "there is seldom an entity that is guaranteeing the payment of the securities."[5] Instead, the representations and warranties only address specific characteristics and qualities of the individual loans and real estate *at the time the representations and warranties*

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[4] *See, e.g.*, Ace Securities Corp., Form 8-K, EX-4.1 (April 25, 2006) (Pooling and Servicing Agreement, ACE Securities Corp. Home Equity Loan Trust, Series 2006-SL2), *available at* http://1.usa.gov/188FBuZ.

[5] *See, e.g.*, Joint Task Force Report at 12.

were made. The representations and warranties are either true or false as to each loan at that time, and if there is a breach of any representation and warranty, it occurs right then and there. For example, defendant DB Structured Products ("DBSP") made representations and warranties that pertain to loan characteristics "*as of the Closing Date*"—such as whether a loan was underwritten in accordance with the originator's guidelines and whether the related property was free of "material damage and waste." R. 296 (MLPA §§ 6, 6(xxiii) & (xxiv); emphasis added).

The representations and warranties are extensive, but there is a trade-off—built into the design of the RMBS offering: a limited and exclusive remedy. Breach of a representation or warranty does not entitle an RMBS investor to rescind their investment purchase, or to seek damages from the seller for any loss of value in their investment.

Those remedies are not available because the contracts say they are not. As reflected by the express language of the contracts, the sponsors make their extensive representations and warranties in exchange for a "*sole remedy*"—the repurchase of the *particular mortgage loan* as to which there is a breach, and even then only if the breach materially and adversely affects the "value of such Mortgage Loan or the interest therein of the Certificateholders." R. 121-122 (PSA § 2.03(a)).[6] The contract at issue here provided that "the obligation of [DBSP] to

[6] Many agreements limit liability to cases involving a breach that materially and adversely affects "the interests of the Certificateholders" in the relevant loan (and do not address the value of the loan). *See, e.g., Walnut Place LLC* v. *Countrywide Home Loans, Inc.*, 35 Misc. 3d

cure or to repurchase . . . shall constitute the sole remedy respecting such . . . breach."[7]

This structure carefully limits the sponsor's exposure. It does not, as the IAS Court erroneously (and inexplicably) held, "function[] as insurance for the Trustee." R. 15. Regardless of the magnitude or number of any breaches, the contracts' "sole remedy" provision makes clear that sponsors do not bear open-ended liability for investors' damages or losses on the portfolio. The remedy for breach is simply and solely to remove individual loans from the trust through repurchase. If a loan breaches the representations and warranties when they were made, and if the breach materially and adversely affected the "value of such Mortgage Loan or the interest therein of the Certificateholders," *that loan* is repurchased and thereby removed.

Under the "sole remedy" provision, the relevant loan is not left in the trust to be subject to claims by others or at some other time.[8] Nor can there be a double gain resulting from a claim on a loan that has been repaid or otherwise removed from the trust. The sole remedy is an elegant—and bargained for—solution to any

1207(A), 951 N.Y.S.2d 84, at *1 n.5 (Sup. Ct. N.Y. Cnty. Mar. 28, 2012), *aff'd*, 96 A.D.3d 684, 948 N.Y.S.2d 580 (1st Dep't 2012).

[7] *See, e.g.*, R. 121-22 (PSA § 2.03(a)) (emphasis added). The governing agreements also typically provide that, as an alternative to repurchase, the sponsor may substitute a replacement loan, but this alternative remedy is only available in the first two years, *see, e.g.*, R. 122-23 (PSA § 2.03(b)), because of federal tax law requirements, *see* 26 U.S.C. § 860G(a)(4)(B)(ii).

[8] For example, in a securitization insured by a "monoline" insurer, if a claim of breach of the representations and warranties is made by the monoline, a remedy other than repurchase could leave the sponsor exposed to additional claims on the same loan and the same breach by the trustee.

problem caused by a breach of a representation and warranty: if there was a breach of a representation or warranty as to a particular loan when it was put into the trust, the contractual repurchase protocol solves the problem, once and for all, without disturbing the rest of the portfolio or the RMBS securities issue as a whole. The repurchase protocol limits and defines the sponsors' own risk. That is consistent with a fundamental structure of "[t]he mortgage securitization process," which is "designed to distribute risk."[9]

In short, under the governing contracts as written, an RMBS sponsor does not represent that homeowners will repay their loans, without fail, for thirty years (or whatever the term of the loan). An RMBS sponsor does not promise to stand guard against the risks of a recession, a decline in housing prices, or an upturn in unemployment. Those risks are borne by investors. Investors who wanted insurance against such risks could purchase insurance "wrapped" RMBS certificates. For those certificates, financial guaranty or "monoline" insurers unconditionally guaranteed the payment of principal and interest. The very existence of such insurers further demonstrates that the repurchase protocol does not, as the IAS Court suggested, "function[] as insurance." R. 15. Instead, under the express terms of the contracts, the repurchase protocol simply and straightforwardly "function[s] as" the sole remedy for breaches of representations and warranties concerning specified characteristics, and only when those breaches cause the requisite material and adverse effect—nothing more, nothing less.

[9] *See, e.g.*, MORTGAGE-BACKED SECURITIES § 1.1.

B. The financial crisis and the vulture-fund RMBS litigation wave

The increase in securitizations during the middle of the last decade, followed by the financial crisis and collapse of the housing market at the end of that decade, has set off a wave of litigation that the court below and this Court now must contend with. Private sponsors issued about $3 trillion in RMBS between 2004 and 2006; securitizations peaked in the spring of 2007, but ground to a complete halt by 2008, and have only recently begun to revive.[10]

When the financial and housing crisis set in, RMBS lost much of their value. And as rating agencies (Moody's and S&P) began downgrading RMBS, "[i]nvestors like banks, pension funds, and insurance companies, who are by rule barred from owning low rated securities, were forced to sell off their downgraded RMBS."[11] Ultimately, "investors fled the multi-trillion dollar market for mortgage-backed securities . . . dropping MBS values . . . to fractions of their former prices."[12]

At that point, hedge funds that speculate in distressed assets and debt stepped in to take advantage of this drastically dislocated market. Seeing an opportunity to buy RMBS on the cheap, they began launching and raising money

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[10] *See* Mark Zandi, *Resurrection of RMBS*, at 1-2 (Moody's Analytics June 2013), *available at* http://bit.ly/1bcPDBr.

[11] U.S. Senate Permanent Subcommittee On Investigations, Wall Street and The Financial Crisis: Anatomy of a Financial Collapse, at 6 (Apr. 13, 2011) (Majority and Minority Staff Report).

[12] Financial Crisis Inquiry Commission, The Financial Crisis Inquiry Report (Jan. 2011) ("FCIC Report"), at 444-45 (Dissenting Statement of Peter J. Wallison), *available at* http://1.usa.gov/1b6KWFG.

for investment vehicles that would, as one vulture fund's press release put it, "provide dedicated exposure to opportunities resulting from the collapse of the housing and related structured products markets."[13] To their credit, they have been wildly successful.[14]

At the same time, however, many of the sophisticated hedge funds began speculating not just in low-priced RMBS, but in RMBS *litigation*. They have bought RMBS with the idea of adding to their profits by hiring lawyers and pursuing repurchase litigation against RMBS sellers and sponsors. "A growing number of [these] hedge funds [have been] scouring the files of securitized home loans, in hopes of reaping rich profits by forcing mortgage-bond issuers to buy back faulty credits."[15] As one industry report described one of the funds behind this case:

> Fir Tree also sees great potential in pursuing putbacks. . . . Last year, the New York firm returned 25%, largely by selling bonds whose values had risen. But it now sees higher returns flowing from efforts to build a team capable of picking apart securitized mortgage pools in search of fraud or other covenant violations before negotiating payouts.[16]

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[13] Press Release, Fir Tree Inc., Fir Tree Closes Mortgage Opportunity Fund (July 9, 2009), *available at* http://prn.to/1boO8ix.

[14] *See* Eric Uhlfelder, *Best 100 Hedge Funds,* BARRON'S (May 18, 2013) ("Top-performing MBS shops occupied four of *Barron's* first 15 spots in our Hedge Fund 100."), *available at* http://on.barrons.com/15A44Lq; Katya Wachtel, *Hedge Fund Scorecard 2012: Mortgage Masters Win, Paulson on Bottom Again,* Reuters Blogs: Unstructured Finance (Jan. 28, 2013) ("Mortgage funds roared home with returns of almost 19 percent last year, trouncing all other hedge fund strategies and beating the S&P 500 stock index."), *available at* http://reut.rs/16gPULK.

[15] Asset-Backed Alert, *MBS 'Putback' Investors Target Big Issuers* (Feb. 24, 2012), *available at* http://bit.ly/14Z088H.

[16] *Id.*

And as part of their speculation-on-litigation strategy, these funds have begun bringing, and directing trustees to bring, untimely claims, such as the claims in this case and the parallel *Nomura* case. But the investors knew their rights, and New York law, when they invested. And they knew in particular that the statute of limitations on breaches of representations and warranties in connection with a securitization would run on the sixth anniversary of the date the representations and warranties were made. The six-year clock was ticking down quickly, in fact, when counsel for the funds behind this lawsuit wrote the trustee about the "Urgent Need for a Tolling Agreement": on January 12, 2012, they beseeched that "it is imperative that the Trustee act expeditiously" because of "potential expiring statute of limitations deadlines." R. 355-59, at 359 (Jan. 12, 2012 Letter from Steven J. Nachtwey at 5).

Even though only the trustee, and not the hedge funds holding the RMBS certificates, could lawfully bring suit, *see Walnut Place, LLC*, 96 A.D.3d at 684, the funds knew that they had to at least try to get *something* on file before the limitations period ran. Thus on March 28, 2006—precisely the sixth anniversary of the contract and securitization at issue in this case—those funds filed a summons, because they knew full well that the statute would run that day. Brief for Defendant-Appellant DBSP ("DBSP Br.") at 12-13. In the other RMBS statute of limitations appeal pending before this Court, *Nomura Asset Acceptance Corp.*, 39 Misc. 3d 1226(A) at *5, slip op. 50743(U) at 7-8, the funds involved there likewise urged the trustee to bring suit, and finally initiated a repurchase action precisely one day before the six-year anniversary of the securitization.[17] They, too, knew the statute was running out.[18]

ARGUMENT

THE STATUTE OF LIMITATIONS RUNS FROM THE DATE OF THE REPRESENTATIONS AND WARRANTIES.

A. Statutes of limitations are "vital to the welfare of society," so vital "that even wrongdoers are entitled to assume that their sins may be forgotten." *Gabelli* v. *SEC*, 133 S. Ct. 1216, 1221 (2013) (internal citations and quotations omitted). "The statutes embody an important policy of giving repose to human affairs," *Flanagan* v. *Mount Eden Gen. Hosp.*, 24 N.Y.2d 427, 429 (1969), and "are 'designed to 'spare the courts from litigation of stale claims.''" *Nussenzweig* v. *diCorcia*, 9 N.Y.3d 184, 188 (2007) (citation omitted). In particular, the Court of Appeals has

> emphasized that the primary purpose of a limitations period is fairness to a defendant. A defendant should "be secure in his reasonable expectation that the slate has been wiped clean of ancient obligations, and he ought not to be called on to resist a claim when the evidence has been lost, memories have faded, and witnesses have disappeared."

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[17] *See also Nomura Asset Acceptance Corp.* v. *Nomura Credit & Capital, Inc.*, 2013 N.Y. slip op. 84722(U) (1st Dep't Sept. 10, 2013) (denying motion for coordination of oral argument).

[18] In that case, however, the funds brought their action more than six years after the date of the contract containing the representations and warranties. *Nomura*, 39 Misc. 3d 1226(A) at *6, slip op. 50743(U) at 8.

Duffy v. *Horton Mem'l Hosp.*, 66 N.Y.2d 473, 476 (1985) (quoting *Flanagan*, 24 N.Y.2d at 429 (citation omitted)); *see also Lyles* v. *State*, 3 N.Y.3d 396, 400 (2004).

Limitations periods, to be sure, can occasionally have "harsh effect," and can "impos[e] hardship on a plaintiff with [an otherwise] meritorious claim." *Zumpano* v. *Quinn*, 6 N.Y.3d 666, 673 (2006). But any such consequences "do not overcome [the] important policy considerations" underlying limitations periods." *Ely-Cruikshank Co.* v. *Bank of Montreal*, 81 N.Y.2d 399, 404 (1993). For statutes of limitations represent "'a *legislative* judgment that . . . occasional hardship . . . is outweighed by the advantage of barring stale claims.'" *Id.* (quoting *Hernandez* v. *N.Y.C. Health & Hosps. Corp.*, 78 N.Y.2d 687, 698 (1st Dep't 1991)). This is a judgment that courts are not free to disregard. And given the passage of time, statutes of limitations will seldom inflict serious hardship upon plaintiffs:

> Statutes of Limitation "are founded upon the general experience of mankind that claims, which are valid, are not usually allowed to remain neglected. The lapse of years without any attempt to enforce a demand creates, therefore, a presumption against its original validity, or that it has ceased to subsist. This presumption is made by these statutes a positive bar."

Flanagan, 24 N.Y.2d at 429 (quoting *Riddlesbarger* v. *Hartford Ins. Co.*, 74 U.S. 386, 390 (1868)).

Indeed, the societal interests animating statutes of limitations are so strong that parties cannot contract around them. A contractual provision adopted at the inception of the contract that is designed as an agreement to extend the statutorily prescribed statute of limitations period or to delay the period in which that limitation is to be computed, is void as against "a societal interest or public policy 'of giving repose to human affairs.'" *John J. Kassner & Co.* v. *City of New York*, 46 N.Y.2d 544, 550-551 (1979) (citations omitted). By statute, an agreement to extend the limitations period, if made prior to accrual, "has no effect." GEN. OBLIG. LAW § 17-103(1), (3).

B. Here, the governing New York statute of limitations is six years—quite a generous amount of time. CPLR § 213(2). And the case law is clear that "[g]enerally, any Statute of Limitations begins to run when a cause of action accrues," and that, "[i]n New York, a breach of contract cause of action accrues at the time of the breach." *Ely-Cruikshank*, 81 N.Y.2d at 402. Under this rule, the limitations period begins to run even if the plaintiff doesn't know about the breach, and even if she has yet to suffer harm from the breach. Thus, "[k]nowledge of the occurrence of the wrong on the part of the plaintiff is not necessary to start the Statute of Limitations running in [a] contract [action]." *Id.* at 403 (quoting *Varga* v. *Credit-Suisse*, 5 A.D.2d 289, 292 (1st Dep't 1958)). The statute "'runs from time of breach though no damage occurs until later,'" *id.* at 402 (quoting 6 WILLISTON, CONTRACTS § 2004, at 5641 (rev. ed. 1938)), "'even though the injured party may be ignorant of the existence of the wrong or injury,'" *id.* at 403 (quoting *Schmidt* v. *Merchants Despatch Transp. Co.*, 270 N.Y. 287, 300 (1936)).

And it is black-letter New York law that a false representation or warranty made at the time of contracting constitutes a contractual breach that immediately starts the limitations clock running. As this Court has expressly held, if a "representation . . . was false when made" in the contract, then "the breach occurred at the time of the execution of the contract," and so that is the time that "'the cause of action accrues and the Statute of Limitations begins to run.'" *W. 90th Owners Corp.* v. *Schlechter*, 137 A.D.2d 456, 458 (1st Dep't 1988) (citation omitted).

The Court of Appeals' holding on the breach-of-warranty claim in *Bulova Watch Co.* v. *Celotex Corp.*, 46 N.Y.2d 606 (1979), illustrates the point nicely. The defendant there had sold some roofing materials to the plaintiff. The plaintiff alleged that the defendant had breached an implied warranty of fitness because the materials were not fit for their intended use. *Id.* at 608-09. The warranty claim "does not hold water," the Court of Appeals held, because "the claim [is] barred by the Statute of Limitations." *Id.* at 609-10. And the reason why the claim was barred was because "the cause of action arose at the time of the sale." *Id.* at 610. The roofing supplies in *Bulova* either were or were not as warranted at the time they were sold. Accordingly, if there was a breach at all, it happened at the time of sale, and the limitations period began to run then.

So too for breaches of RMBS representations and warranties. In the governing agreement, the RMBS sponsor makes representations and warranties that pertain to the characteristics of loans and their collateral at a fixed point in time. DBSP did just that here: it made representations and warranties, in the governing contract, that pertain to loan characteristics "*as of the Closing Date*"—such as whether a loan was underwritten in accordance with the originator's guidelines and whether the related property was free of "material damage and waste." R. 294, 296 (MLPA §§ 6, 6(xxiii) & (xxiv); emphasis added). The representations and warranties were either true or false on the date they were made. And so if there was any breach at all, it happened then.

And that is why—save for the IAS Court below—*every* court that has applied the New York statute of limitations to RMBS representations-and-warranties claims while actually discussing New York law has concluded that the six-year limitations period runs from the date of the representations and warranties. These courts all agree that the limitations period "runs from the time of breach of the Mortgage Representations," and that because "the Mortgage Representations are alleged to have been false when made. . . . [P]laintiff's causes of action, if any, accrued no later than . . . the 'Closing Date.'" *Nomura Asset Acceptance Corp.*, 39 Misc. 3d 1226(A) at *8-9, slip op. 50743(U) at 12-13.[19] They all recognize that "[u]nder New York law, the statute of limitations begins to run from the date of the first alleged breach of a contract"—the date the seller "provided the subject misrepresentations" to the buyer, "the same day that [the buyer] purchased the . . . loan[s]." *Lehman Bros. Holdings, Inc.* v. *Evergreen Moneysource Mortg. Co.*, 793 F. Supp. 2d 1189, 1193-94 (W.D. Wash. 2011) ("*Evergreen*"). They all teach that "[t]he New York Court of Appeals applies an accrual-at-breach rule even when the

[19] The *Nomura* court did not decide "whether the alleged misrepresentations were made for statute of limitations purposes" on the date of the contracts or on the closing date because, whichever date was used, the "plaintiff with standing to sue" filed its complaint "more than six years after Plaintiff's claims for breach of contract accrued." *Nomura*, 39 Misc. 3d 1226(A) at *8-9, slip op. 50743(U) at 13.

breach and injury are not simultaneous," and that as a result, if "the facts warranted in the [securitization] Pooling Agreement were not true when made, the statute of limitations began to run at that time, and expired six years later." *Structured Mortg. Trust 1997-2* v. *Daiwa Fin. Corp.*, No. 02 Civ. 3232 (SHS), 2003 WL 548868, at *2 (S.D.N.Y. Feb. 25, 2003).

C. In concluding otherwise, the IAS Court impermissibly misconstrued both the governing contract and the controlling New York law. In a ruling that should shock any practitioner who drafts contracts under New York law, the IAS Court squarely held that the breach of a representation or warranty is somehow *not* a breach of contract:

> the mere fact that a Representation is false does not mean that DBSP "breached" the PSA. Under the PSA, DBSP has no duty to ensure that the Representations are true. . . . DBSP's obligation is to follow the Repurchase Protocol.

R. 15. The IAS Court held instead that the contractual breach here is the seller's failure to carry out the contractual *remedy*—loan repurchase—for the relevant breach of a representation or warranty: "DBSP commits an independent breach of the PSA each time it fails to abide by and fulfill its obligations under the Repurchase Protocol." As the IAS Court candidly acknowledged, this holding effectively *eliminates* the statute of limitations—because "each breach may begin the running of the statute [of limitations] anew"—and converts "[t]he Representations and the Repurchase Protocol [into] insurance for the Trustee." R. 15, 16.

This badly misreads the contract—indeed, stands it on its head. The seller *does* covenant that the representations and warranties "shall be true and correct in all material respects as of the date as of which they are made," R. 300-01 (MLPA § 8(a)); that is the whole *point* of a seller's representations and warranties in any contract, not just contracts of the sort at issue here. The RMBS pooling and servicing agreement here *expressly states* that a breach of a representation or warranty under the mortgage loan purchase agreement is a breach of the contract. It uses the word "breach" over and over and over again to describe what occurs if a representation or warranty is untrue at closing. *E.g.*, R. 121-23 (PSA § 2.03) (eighteen times). "Courts will not rewrite contracts that have been negotiated between sophisticated, counseled commercial entities." *Flag Wharf, Inc.* v. *Merrill Lynch Capital Corp.*, 40 A.D.3d 506, 507 (1st Dep't 2007). Yet that is exactly what the IAS Court did here, when it held that what the contract repeatedly called a "breach" is not a breach.

The IAS Court got it just as wrong when it held failure to comply with the repurchase protocol to be an independent breach of contract. This holding, as noted, effectively eliminates the statute of limitations period: because the repurchase protocol is triggered by notice from the trustee to the seller, R. 51, the IAS Court's holding "allow[s] [the trustee] to essentially circumvent the statute of limitations by indefinitely deferring" notice, *Evergreen*, 793 F. Supp. 2d at 1194. And the holding eviscerates the rule that "[k]nowledge of the occurrence of the wrong on the part of the plaintiff is not necessary to start the Statute of Limitations running in [a] contract [action]." *Ely-Cruikshank*, 81 N.Y.2d at 402 (quoting *Varga*, 5 A.D.2d at 292).

More to the point, the IAS Court's holding illogically and impermissibly turns the contractual *remedy* into a contractual *breach*. The *remedy* is repurchase, provided that *breach* is shown as well as that the *breach* had the requisite material and adverse effect. As this Court recently recognized, the repurchase mechanism in an RMBS transaction "merely provides for a remedy in the event of a breach." *Walnut Place*, 96 A.D.3d at 684, 685. The repurchase remedy does not and cannot serve as the predicate for an independent breach. This is true, indeed, for any remedy provided for in any contract, not just one involving RMBS. The failure to carry out the remedy cannot itself be an independent breach resetting the limitations period anew—because if it were, there would effectively be no statute of limitations at all. The failure to carry out the remedy may subject the sponsor to suit—but the suit can only be to enforce the remedy, provided that a breach is shown and the other condition of the remedy (material and adverse effect) is demonstrated.

This is exactly the point the Court of Appeals made just last year in *Hahn Automotive Warehouse, Inc.* v. *American Zurich Insurance Co.*, 18 N.Y.3d 765 (2012). Sometime in the 1990s, Zurich acquired the contractual right to bill Hahn for deductibles and various expenses for two insurance policies. It didn't recognize that fact, however, and didn't bill Hahn, until 2005 and 2006. *Id.* at 768-69. The Court of Appeals held that the six-year limitations period had run in the interim: "the statute of limitations . . . was triggered when the party that was owed money had the right to demand payment, not when it actually made the demand." *Id.* at 771. "To hold otherwise would allow [the plaintiff] to extend the statute of limitations indefinitely 'by simply failing to make a demand.'" *Id.* (citations omitted).

Here, to hold otherwise, as did the IAS Court, would accomplish the utterly incongruous: it would take a repurchase protocol unquestionably designed to *limit* the scope of a remedy for contractual breach, and use that limitation on liability to *extend* the duration of that liability, endlessly. As explained above, the repurchase protocol allows the RMBS seller to make a fairly extensive set of representations and warranties about the loans it sells, and does so by carefully circumscribing the remedy to which the seller is exposed in the event of a breach. The repurchase remedy is the "*sole remedy*" available for a breach of representation or warranty, and it is available only when a breach of a representation and warranty causes a material and adverse effect as to a particular loan, and only as to that particular loan. R. 121-22 (PSA § 2.03(a)) (emphasis added); *see* pp. 6-9, above. This sort of "limitation on liability . . . in a contract . . . represents the parties' [a]greement on the allocation of the risk of economic loss" that the Court of Appeals has said "courts should honor." *Metro Life. Ins. Co.* v. *Noble Lowndes Int'l, Inc.*, 84 N.Y.2d 430, 436 (1994). The IAS Court did not honor the agreement on allocation of risk here: it turned "[t]he Representations and the Repurchase Protocol [into] insurance for the Trustee," R. 15, which they were plainly not intended to be.[20]

And nothing in the Court of Appeals' decision in *Bulova* justifies the IAS Court's transformation of the representations, warranties, and repurchase protocol into a form of insurance. As noted above, *Bulova*'s holding on the warranty claim in that case clearly confirms that the statute of limitations on RMBS representations and warranties claims starts running at the time the representations and warranties were made. *See* p. 17, above. Yet the IAS Court apparently relied upon another part of that decision, dealing with a 20-year guaranty bond, to conclude that the RMBS repurchase remedy here "provides for continuing performance over a period of time, [such] that accrual [of the statute of limitations] occurs continuously" and, in effect, perpetually. R. 13 (citing *Bulova* and other cases). In fact, *Bulova*'s guaranty-bond holding actually *refutes* the IAS Court's conclusion.

The "20-Year Guaranty Bonds" issued by the defendants in *Bulova*, 46 N.Y.2d at 608, *did exactly what DBSP did not do* with the RMBS representations and warranties here: they warranted the item being sold *not* just at the time of sale, but continually *after* that. And "the defendants did not merely guarantee the condition or performance of the goods," over the twenty-year period, "but agreed

[20] The IAS Court's conclusion that the repurchase remedy was a form of "insurance" for the Trustee led it improperly to rely on *Continental Casualty Co.* v. *Stronghold Insurance Co.*, 77 F.3d 16 (2d Cir. 1996). R.15 That case deals exclusively with reinsurance and the Court of Appeals has refused to apply it beyond the reinsurance context. *See Hahn*, 18 N.Y.3d at 772 n.5.

to perform a service—to repair the roof." *Id.* at 611-12. So the "bond obligations, as agreements contemplating services, were subject to a six-year statute … running separately for the damages each time a breach of the obligation to repair the bonded roof occurred." *Id.* at 611 (citations omitted). This is the equivalent of not only agreeing to sell a house with a good roof, but of committing to fix the roof if it springs a leak any time after the sale, even if the roof was perfect when the house was sold. Failure to live up to that separate covenant after the sale is a stand-alone breach that gives rise to a separate limitations period. It has nothing to do with any representation about the condition of the roof at the time of sale. But here, as Justice Sherwood rightly put it in the *Nomura* case now pending before this Court:

> the Mortgage Representations are alleged to have been false when made. Those representations did not arise or change over time. If the Mortgage Representations were false when made, they are still false today. If they were true when made, they are still true today. The repurchase obligation in this case is merely a remedy. It is not a duty independent of the Mortgage Representation breach of contract claims. The statute of limitations runs from the time of breach of the Mortgage Representations, not from the time plaintiff elected to make demands for repurchase.

Nomura, slip op. 50743(U), at *9-10. The defendant here, in short, did not give the sort of guaranty addressed in *Bulova*, or issue the sort of "insurance for the Trustee" posited by the IAS Court.

Finally, as noted above, any interpretation of the governing agreements that does not start the statute of limitations at the time of breach contradicts legislative policy. The Legislature has made clear, by statute, that an agreement to extend the limitations period, if made prior to accrual, "has no effect." GEN. OBLIG. LAW

§ 17-103(1), (3); *see also John J. Kassner & Co., Inc.*, 46 N.Y.2d at 551 (1979) ("A contractual provision adopted at the inception of the contract that is designed as an agreement to extend the statutorily prescribed statute of limitations period or to delay the period in which that limitation is to be computed, is void as against a societal interest or public policy 'of giving repose to human affairs.'") (citations omitted). Here, plaintiff's interpretation of the governing agreements would, in effect, toll the statute of limitations until a repurchase demand is refused and thereby extend it beyond the six years dictated by statute.

* * *

In short, there is no contractual or precedential basis for the IAS Court to refuse to consider a breach of representation or warranty to be a breach, to treat a remedy as a breach, to transform a limitation on liability into an expansion of liability, and to effectively eliminate an already-generous statute of limitations altogether. But apart from settled doctrine, the Court should consider the consequences of the ruling below—not just in this case, and not just in RMBS put-back litigation, but in contract cases and commercial matters generally.

The detrimental impact of the IAS Court's decision in this and other RMBS cases is plain. About six years have now passed from the time that the mortgage market began to falter and the first signs of the financial crisis began to appear. Throughout those six years, as noted above, hedge-fund speculators and their attorneys have pored over RMBS offerings, hunting endlessly for possible breach-of-representations-and-warranties claims, in the hope of boosting their investment returns through settlements and judgments. They have had plenty of time to find whatever potential claims they might be able to bring. But the IAS Court, in the apparent belief that these sophisticated parties deserve “insurance” for which they never bargained or paid, rendered a decision that effectively gives them *decades* to commence breach litigation.

That is utterly contrary to established policy of this State, a venerable legislative policy that seeks to “giv[e] repose to human affairs,” *Flanagan*, 24 N.Y.2d at 429, promises “fairness to a defendant,” *Duffy*, 66 N.Y.2d at 476, and serves to wipe “the slate . . . clean of ancient obligations,” *id.* (quoting *Flanagan*, 24 N.Y.2d at 429). And it would entirely undermine another purpose of statutes of limitations: “the need to protect the judicial system from the burden of adjudicating stale and groundless claims.” *Id.* at 476-77. As noted above, the court below is already overburdened with RMBS repurchase cases, including at least fourteen that raise the statute of limitations questions like the one at issue here. *Nomura*, 39 Misc. 3d 1226(A) at *1 n.1, slip op. 50743(U) at 1 n.1. If the statute of limitations is not applied, there will be many more such cases in the decades to come.

The problem with the holding below goes well beyond RMBS litigation. In virtually any complex business contract negotiated in New York today, there are representations and warranties. And there are frequently carefully-crafted provisions specifying and limiting the remedies available for breaches of those representations and warranties. The reasoning of the decision below, if upheld by this Court, would threaten to gut the statute of limitations for claims on countless such contracts. Breaches of representations and warranties would no longer be deemed to occur as of the time they are made; instead, the operative breach triggering the running of the statutory time period would occur when the plaintiff discovers the untrue representation or warranty and seeks to invoke the remedy. That is the equivalent of no statute of limitations at all.

Beyond even that, to uphold the decision below would undermine settled expectations in the law of contracts in a dramatic and most high-profile way. That is no small matter to the State of New York. As the Chief Judge's Task Force on Commercial Litigation in the 21st Century recently observed, "[t]he rule of law [is a] key element" in "helping our State retain its role as the preeminent financial and commercial center of the world," and "in keeping us competitive in today's global economy."[21] New York is a preeminent commercial center in part because parties can rely on dependability and the predictability of its respected law of contracts. And the longstanding, essential principle underlying that dependability and predictability is a straightforward one, a corollary of the rule of law: New York "courts 'may not by construction add or excise terms, nor distort the meaning of those used and thereby make a new contract for the parties under the guise of interpreting the writing.'" *Bailey* v. *Fish & Neave*, 8 N.Y.3d 523, 528 (2007)

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[21] THE CHIEF JUDGE'S TASK FORCE ON COMMERCIAL LITIGATION IN THE 21ST CENTURY, REPORT AND RECOMMENDATIONS TO THE CHIEF JUDGE OF THE STATE OF NEW YORK 1 (2012), *available at* http://bit.ly/16gNUTG.

(citations omitted). Yet that is exactly what the IAS Court did here—and why its order should be reversed.

CONCLUSION

It is respectfully submitted that the order of the IAS Court should be reversed.

Dated: New York, New York
September 26, 2013

WACHTELL, LIPTON, ROSEN & KATZ

By: George T. Conway III
George T. Conway III

Jeffrey D. Hoschander
Justin V. Rodriguez
Caitlin A. Donovan
51 West 52nd Street
New York, New York 10019
(212) 403-1000
gtconway@wlrk.com

Attorneys for Amicus Curiae *the Securities Industry and Financial Markets Association*

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Affirmation of George T. Conway III
in Support of Motion for Leave to File Brief as *Amicus Curiae*

EXHIBIT B

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: JUSTICE SHIRLEY WERNER KORNREICH PART 54
Justice

Index Number : 650980/2012
~~RMBS RECOVERY HOLDINGS 4, LLC~~ Ace
VS.
DB STRUCTURED PRODUCTS, INC.
SEQUENCE NUMBER : 001
DISMISS ACTION

INDEX NO. ______
MOTION DATE 5/7/13
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). 16-18
Answering Affidavits — Exhibits	No(s). 20-28
Replying Affidavits	No(s). 30-31

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

MOTION IS DECIDED IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION AND ORDER.

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

Dated: 5/13/13

SHIRLEY WERNER KORNREICH
J.S.C. , 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: PART 54

---X

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006,

Index No.: 650980/2012

DECISION & ORDER

Plaintiff,

-against-

DB STRUCTURED PRODUCTS, INC.,

Defendant.

---X

SHIRLEY WERNER KORNREICH, J.:

Defendant DB Structured Products, Inc. (DBSP) moves to dismiss the Complaint pursuant to CPLR 3211(a)(1), (3), (7), & (8). Defendant's motion is denied for the reasons that follow.

I. Factual Background & Procedural History

This case concerns DBSP's alleged breach of its contractual obligation to repurchase certain non-conforming loans that were pooled, deposited into a trust, securitized, and sold to investors. Since this action arises from contractual obligations under a trust with a "no-action clause," the Trustee, HSBC Bank USA, National Association, filed the Complaint on behalf of a certificateholder (plaintiff ACE Securities Corp.) (ACE) in the subject trust (Home Equity Loan Trust, Series 2006-SL2) (the Trust). As this decision involves a motion to dismiss, the facts recited are taken from the Complaint.

The loans at issue in this case were purchased by DBSP from at least three originators and then sold to ACE in a Mortgage Loan Purchase Agreement dated March 28, 2006 (the MLPA). Complaint ¶¶ 2-3. Following the usual protocol for creating residential mortgage backed securities, ACE deposited the loans into the Trust. ¶ 4. The loans were securitized through the issuance of over $500 million of certificates pursuant to a Pooling and Servicing Agreement dated as of March 1, 2006 (the PSA). *Id.* In the MLPA, DBSP made over fifty representations and warranties (the Representations) regarding the characteristics and quality of the loans, including those common in many MLPAs (e.g., representations about underwriting guidelines such as the borrower's income and loan-to-value ratio) and those that are somewhat rarer (e.g., a "no-fraud representation").[1] ¶¶ 5-6. Under Section 2.03 of the PSA, DBSP was obligated to cure a breach of a Representation within 60 days of discovery or receipt of notice thereof, or, in the event that such breach could not be cured, DBSP had to repurchase the affected loans within 90 days at a defined Purchase Price. ¶ 26. Both the PSA and the MLPA provide that the Repurchase Protocol is the "sole remedy" with respect to loan losses caused by false Representations.

On March 28, 2012, this action was commenced by two certificateholders (RMBS Recovery Holdings 4, LLC and VP Structured Products, LLC) by filing a Summons with Notice. A single cause of action alleging breach of contract was stated. It is undisputed that these certificate-holders lacked standing to maintain this action under the PSA's no-action clause. They did so, apparently, due to concerns over their claims being time barred, a worry amplified

[1] These representations have been the subject of much litigation involving both investors and monoline insurers. As this decision does not concern substantive disputes over the details of the Representations, the court will not provide further background and assumes familiarity with the recent line of similar cases in this court.

by the Trustee's initial refusal to sue on their behalf. Ultimately, the Trustee was substituted as the plaintiff for the certificate-holders. As discussed *infra*, the manner in which this action was originally commenced, in the end, is not at issue because the relevant statute of limitations did not expire before the substitution.[2]

II. Discussion

On a motion to dismiss, the court must accept as true the facts alleged in the complaint as well as all reasonable inferences that may be gleaned from those facts. *Amaro v Gani Realty Corp.*, 60 AD3d 491 (1st Dept 2009); *Skillgames, L.L.C. v Brody*, 1 AD3d 247, 250 (1st Dept 2003), citing *McGill v Parker*, 179 AD2d 98, 105 (1992); *see also Cron v Harago Fabrics*, 91 NY2d 362, 366 (1998). The court is not permitted to assess the merits of the complaint or any of its factual allegations, but may only determine if, assuming the truth of the facts alleged, the complaint states the elements of a legally cognizable cause of action. *Skillgames*, *id.*, citing *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 (1977). Deficiencies in the complaint may be remedied by affidavits submitted by the plaintiff. *Amaro*, 60 NY3d at 491. "However, factual allegations that do not state a viable cause of action, that consist of bare legal conclusions, or that are inherently incredible or clearly contradicted by documentary evidence are not entitled to such consideration." *Skillgames*, 1 AD3d at 250, citing *Caniglia v Chicago Tribune-New York News Syndicate*, 204 AD2d 233 (1st Dept 1994). Further, where the defendant seeks to dismiss the complaint based upon documentary evidence, the motion will succeed if "the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a

[2] Ergo, the dispute over whether the Summons tolled the stature of limitation is moot.

matter of law." *Goshen v Mutual Life Ins. Co. of N.Y.*, 98 NY2d 314, 326 (2002) (citation omitted); *Leon v Martinez*, 84 NY2d 83, 88 (1994).

A. Statute of Limitations

Pursuant to CPLR 213(2), breach of contract claims are subject to a six year statute of limitations. *Mendelsohn v City of New York*, 89 AD3d 569 (1st Dept 2011). The claim accrues at the time of breach, even if plaintiff does not suffer damages until a later date. *Ely-Cruikshank Co. v Bank of Montreal*, 81 NY2d 399, 402 (1993). "Knowledge of the occurrence of the wrong on the part of the plaintiff is not necessary to start the Statute of Limitations." *Id.* at 403, quoting *Varga v Credit-Suisse*, 5 AD2d 289, 292 (1st Dept 1958). Additionally, CPLR 206(a) provides that "where a demand is necessary to entitle a person to commence an action, the time within which the action must be commenced shall be computed from the time when the right to make the demand is complete." *Parker v Town of Clarkstown*, 217 AD2d 607, 608 (2d Dept 1995). "However, where a contract provides for continuing performance over a period of time, each breach may begin the running of the statute anew such that accrual occurs continuously and plaintiffs may assert claims for damages occurring up to six years prior to filing of the suit." *Airco Alloys Div. v Niagara Mohawk Power Corp.*, 76 AD2d 68, 80 (2d Dept 1980), citing *Bulova Watch Co. v Celotex Corp.*, 46 NY2d 606 (1979); *see also N.Y. Cent. Mut. Fire Ins. Co. v Glider Oil Co.*, 90 AD3d 1638, 1642 (4th Dept 2011) ("Where, as here, a contract provides for a recurring obligation, a claim for damages accrues each time the contract is allegedly breached."); *Beller v William Penn Life Ins. Co. of N.Y.*, 8 AD3d 310, 314 (2d Dept 2004) (same); *Guilbert v Gardner*, 480 F3d 140, 150 (2d Cir 2007) (same).

DBSP argues that plaintiff's claim for breach of the PSA accrued when the contract was executed in 2006. They argue that if the Representations were false, they were false in 2006 since the mortgage loans had already been made. Plaintiff disagrees and argues that their claims did not accrue until DBSP breached its repurchase obligations (which, regardless of the exact date of accrual, would be within six years of the date the Complaint was filed).

In 2003, well before the financial crisis and subsequent flurry of mortgage backed securities litigation, a federal district court dealt with this exact situation. *See Structured Mortg. Trust 1997-2 v Daiwa Finance Corp.*, 2003 WL 548868 (SDNY 2003) (*Daiwa*). In *Daiwa*, the court held that the claim accrued when the PSA was executed because the subject representations "were not true when made" and that the trustee could have made a repurchase demand at that time. *Id.* at *2. Consequently, *Daiwa* held, the statute of limitations runs from the execution of the contract because the claim accrues "when the wrong is committed, and not when the plaintiff discovers it." *Id.*, citing 7B Joseph McLaughlin, Practice Commentaries, CPLR 206 (McKinney's 1990). For the reasons discussed below, this court disagrees with the *Daiwa* holding. CPLR 206(a), the "continuing performance" doctrine, and the nature of the parties' relationship under the PSA militate against *Daiwa*.[3]

Under CPLR 206(a), "'demand is complete' [means] that the Statute of Limitations runs from the time when the party making the demand first becomes *entitled* to make the demand, and not from the time the actual demand is made." *Woodlaurel, Inc. v Wittman*, 199 AD2d 497, 497-

[3] In 2011, another federal court made the same ruling as the *Daiwa* court, though did not cite to *Daiwa*. *See Lehman Bros. Holdings, Inc. v Evergreen Moneysource Mortg. Co.*, 793 F Supp 2d 1189, 1193-94 (WD Wash 2011). This court also considers that case to be a misapplication New York law.

98 (2d Dept 1993) (emphasis added). In Section 2.03, as in other similar PSAs entered into by DBSP, three steps must be followed before the Trustee can sue DBSP for breach of its repurchase obligations: discovery or receipt of notice by the bank, cure, and repurchase. The Trustee is not *entitled* to sue or make a repurchase demand until discovery or notice by the bank occurs and the cure period lapses. It, therefore, follows that DBSP does not breach the PSA and the claim for the breach does not accrue until DBSP fails to timely cure or repurchase a loan.

Though DBSP characterizes a Representation as being "breached" if it is false, in this contract action, the mere fact that a Representation is false does not mean that DBSP "breached" the PSA. Under the PSA, DBSP has no duty to ensure that the Representations are true. Thus, upon discovery or notice of falsity, DBSP's obligation is to follow the Repurchase Protocol. Whatever due diligence DBSP conducted was a matter of its sole discretion. If DBSP knew of or recklessly disregarded signs that the Representations were false, it did so at its own peril because of its potential liability to the Trustee under Section 2.03. In sum, the *only* contractual wrong that DBSP could commit is failure to abide by Section 2.03.

This notion is further reinforced by Section 7(a) of the MLPA, which sets forth that the Trustee's right to enforce DBSP's repurchase obligations "shall not be impaired" by the Trustee's failure to review the loan files or conduct any due diligence on the veracity of the Representations. The whole point of how the MLPA and PSA were structured was to shift the risk of non-complying loans onto DBSP. The Representations and the Repurchase Protocol functioned as insurance for the Trustee and was likely priced accordingly. Consequently, to contend, as the *Daiwa* court and DBSP do, that the Trustee's claims accrued in 2006 because the Trustee could have made a demand at that time utterly belies the parties' relationship and turns the PSA on its head. If this were the case, the contracts, which include specific deadlines for the demand and cure period and involve loans with a 30 year term, could have stated that "repurchase demands can only be made within six years of the PSA's execution." It is highly peculiar that the PSA would leave out an effective 6-year statute of repose if such a limitations period were actually contemplated by the parties. Furthermore, if such a limitations period existed, the Trustee would have an implied duty to conduct constant due diligence on the veracity of the Representations to ensure that lies are ferreted out before the time to make a repurchase demand expires. It is not commercially reasonable to read this obligation into the PSA because it is squarely at odds with Section 7(a) of the MLPA. Instead, DBSP has a "recurring obligation" under the PSA to follow the Repurchase Protocol when it is informed of a problem with a Representation. *See N.Y. Cent. Mut. Fire Ins. Co.,* 90 AD3d at 1642. DBSP commits an independent breach of the PSA each time it fails to abide by and fulfill its obligations under the Repurchase Protocol, and "each breach may begin the running of the statute [of limitations] anew." *Airco Alloys,* 76 AD2d at 80.

It should be noted that the instant case bears a resemblance to reinsurance, where the insurance company is often contractually obligated to make a demand on its reinsurer when it pays out a claim to the underlying insured. The United States Court of Appeals for the Second Circuit, applying New York law, has held that a reinsurer does not breach its obligations to the insurance company until the reinsurer rejects the insurance company's demand. *See Continental Cas. Co. v Stronghold Ins. Co.*, 77 F3d 16 (2d Cir 1996). Though the reinsurer's contractual liability stems from the insurance company's claim payment to the insured, "the reinsurers were not in 'breach' of their contract to indemnify until they rejected the demand." *Id.* at 21.

The statute of limitations began to run when DBSP improperly rejected the Trustee's repurchase demand. Ergo, the breach is the failure to comply with the demand. Of course, plaintiff cannot "put off the running of the Statute of Limitations indefinitely" by waiting an unreasonable time to make the demand. *Id.*, citing *Snyder v Town Insulation, Inc.*, 81 NY2d 429, 435 (1993). Had the Trustee not made its demand in 2012 and instead waited a number of years to file suit, the inquiry might be different. However, not only did the Trustee file suit shortly after making demand, DBSP actually contends (as discussed below) that this action was commenced too quickly. In conclusion, plaintiff's claims did not accrue on the date of the contracts' execution. Hence, the claims are timely.

B. The Repurchase Protocol

The court rejects DBSP's arguments that the Trustee's supposed failure to comply with the Repurchase Protocol's conditions precedent to bring suit precludes its claims. First, the Trustee's alleged failure to wait the requisite time to bring suit is irrelevant given DBSP's repudiation of its repurchase obligations under the PSA. Next, waiting to cure is utterly pointless because the alleged false Representations cannot be cured since most, if not all of the loans, have defaulted. Finally, the Trustee's failure to set forth which of the specific loans are affected by false Representations is not fatal to the Complaint because CPLR 3016(b)'s particularity requirements do not apply to a breach of contract claim. Unlike similar cases, plaintiff does not allege fraud. Nonetheless, given the specificity requirements in Repurchase Protocol, the specific identification of which loans have been affected by false Representations is fair game for interrogatories.

As for DBSP's contention that the PSA's damages calculation prohibits recovery by the Trustee, questions of fact clearly preclude dismissal on this ground. Even if DBSP were correct that Released, Charged Off, and Liquidated Loans are not subject to repurchase, dismissal would still not be warranted because DBSP needs to establish that all of the non-conforming loans fell into these defined categories. Discovery is necessary to make these determinations.

That being said, DBSP's argument that loans in these categories are not subject to repurchase because they are no longer assets of the Trust (or that their defined Purchase Price is now $0) is unconvincing. If DBSP were correct, it would be perversely incentivized to fill the Trust with junk mortgages that would expeditiously default so that they could be Released, Charged Off, or Liquidated before a repurchase claim is made. Indeed, if DBSP learned that loans were non-conforming and played a crafty game of accounting by moving them off the Trust's books to their own to evade their repurchase obligations, such actions would be a breach of the duty of good faith and fair dealing. Consequently, it is to no avail to contend that the non-conforming loans are long gone and the Trustee's repurchase rights have been extinguished by DBSP's actions.

Stepping back, it is worth keeping in mind that DBSP does not bear the risk of loss on all loans that default. Conforming loans, where the Representations are true, will sometimes default for reasons that have nothing to do with borrowers lying or underwriter fraud. If "good" mortgages did not have real default risk, mortgage interest rates would be even lower than their current historically depressed levels. In reality, borrowers will occasionally default due to myriad unexpected circumstances, such as losing their job. In those cases, the Certificateholders bear the risk of loss and their recovery is limited to whatever proceeds can be obtained through foreclosure. In contrast, where, as here, borrowers allegedly defaulted due to the Representations being false, such risk is meant to be borne by DBSP. If, as DBSP contends, the Certificateholders' recovery on misrepresented loans is limited to foreclosure proceeds, the repurchase remedy would be virtually worthless.

Additionally, DBSP's contention that it cannot "repurchase" a loan because the loan technically does not "exist" after foreclosure, misses the point. Foreclosure is not an alternative means of recovery for non-conforming loans; it is a set off to DBSP's obligation to pay back the cost of the loan. The PSA's damages calculation includes foreclosure proceeds because the Repurchase Protocol is a mechanism whereby the Certificateholders can recover the cost of the loan minus the revenue generated (which includes pre-default mortgage payments and foreclosure proceeds).

Nonetheless, DBSP correctly maintains that any recovery under Section 2.03 must be limited to the formula set forth in the PSA. Therefore, if sampling is to be used as a means to calculate damages, the parties must come up with a sampling mechanism that meaningfully reflects the PSA's damages calculation. The parties may not disregard such calculation in an attempt to seek complete rescission of the PSA merely out of frustration that being bound by the strict terms of the contract is laborious and inconvenient. The degree to which bargained for remedies are simple or convoluted is a matter for sophisticated commercial actors to address before the execution of a contract. It is not something to complain about in subsequent litigation. Accordingly, it is

ORDERED that the motion to dismiss the Complaint by defendant DB Structured Products, Inc. is denied; and it is further

ORDERED that the parties are to appear in Part 54, Supreme Court, New York County, 60 Centre Street, Room 228, New York, N.Y., for a preliminary conference on June 4, 2013 at 10:00 in the forenoon.

Dated: May 13, 2013

ENTER:

J.S.C.

Affirmation of George T. Conway III
in Support of Motion for Leave to File Brief as *Amicus Curiae*

EXHIBIT C

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006, *Plaintiff*, -against- DB STRUCTURED PRODUCTS, INC., *Defendant*.	Index No. 650980/2012 IAS Part: 54 Justice Shirley W. Kornreich Motion Sequence No. 001 **NOTICE OF APPEAL**

PLEASE TAKE NOTICE that, pursuant to Sections 5513(a) and 5515 of the New York Civil Practice Law and Rules, Defendant DB Structured Products, Inc. ("DBSP") hereby appeals to the Appellate Division of the Supreme Court of the State of New York, in and for the First Judicial Department, from each and every part of the Order of the Supreme Court, New York County, I.A.S. Part 54 (Shirley Werner Kornreich, J.S.C.) dated May 13, 2013, and duly entered with the Clerk of the Court on May 17, 2013, attached hereto as Exhibit A, which denied DBSP's Motion to Dismiss the Complaint (Mot. Seq. No. 001).

Dated: New York, New York
June 3, 2013

SIMPSON THACHER & BARTLETT LLP

By: /s/ David J. Woll
Thomas C. Rice (trice@stblaw.com)
David J. Woll (dwoll@stblaw.com)

425 Lexington Avenue
New York, NY 10017-3954
Tel: (212) 455-2000
Fax: (212) 455-2502

Attorneys for Defendant-Appellant

To: CLERK OF THE SUPREME COURT,
NEW YORK COUNTY
60 Centre Street
New York, NY 10007

To: Michael Fay, Esq.
Kasowitz, Benson, Torres & Friedman LLP
1633 Broadway
New York, New York 10019

Attorney for Plaintiff-Respondent

EXHIBIT A

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006,

Plaintiff,

-against-

DB STRUCTURED PRODUCTS, INC.,

Defendant.

Index No. 650980/2012
IAS Part: 54
Justice Shirley W. Kornreich

NOTICE OF ENTRY

PLEASE TAKE NOTICE that the attached is a true and correct copy of the memorandum Decision & Order in this action dated May 13, 2013 and duly entered in the Office of the County Clerk of the County of New York on May 14, 2013.

Dated: New York, New York
May 17, 2013

/s/ David J. Woll
Thomas C. Rice
David J. Woll
SIMPSON THACHER & BARTLETT LLP
425 Lexington Avenue
New York, New York 10017
Tel: (212) 455-2000
Fax: (212) 455-2502

Attorneys for Defendant DB Structured Products, Inc.

To: Michael Fay, Esq.
Kasowitz, Benson, Torres & Friedman LLP
1633 Broadway
New York, New York 10019

Attorney for Plaintiffs

Attachment

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: JUSTICE SHIRLEY WERNER KORNREICH PART 54
Justice

Index Number : 650980/2012
~~RMBS RECOVERY HOLDINGS 4, LLC~~ Ace
vs.
DB STRUCTURED PRODUCTS, INC.
SEQUENCE NUMBER : 001
DISMISS ACTION

INDEX NO. ______
MOTION DATE 5/7/13
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). 16-18
Answering Affidavits — Exhibits	No(s). 20-28
Replying Affidavits	No(s). 30-31

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

MOTION IS DECIDED IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION AND ORDER.

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

Dated: 5/13/13

SHIRLEY WERNER KORNREICH
J.S.C. , 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: PART 54

---X

ACE SECURITIES CORP., HOME EQUITY LOAN TRUST, SERIES 2006-SL2, by HSBC BANK USA, NATIONAL ASSOCIATION, solely in its capacity as Trustee pursuant to a Pooling and Servicing Agreement, dated as of March 1, 2006,

Index No.: 650980/2012

DECISION & ORDER

Plaintiff,

-against-

DB STRUCTURED PRODUCTS, INC.,

Defendant.

---X

SHIRLEY WERNER KORNREICH, J.:

Defendant DB Structured Products, Inc. (DBSP) moves to dismiss the Complaint pursuant to CPLR 3211(a)(1), (3), (7), & (8). Defendant's motion is denied for the reasons that follow.

I. Factual Background & Procedural History

This case concerns DBSP's alleged breach of its contractual obligation to repurchase certain non-conforming loans that were pooled, deposited into a trust, securitized, and sold to investors. Since this action arises from contractual obligations under a trust with a "no-action clause," the Trustee, HSBC Bank USA, National Association, filed the Complaint on behalf of a certificateholder (plaintiff ACE Securities Corp.) (ACE) in the subject trust (Home Equity Loan Trust, Series 2006-SL2) (the Trust). As this decision involves a motion to dismiss, the facts recited are taken from the Complaint.

The loans at issue in this case were purchased by DBSP from at least three originators and then sold to ACE in a Mortgage Loan Purchase Agreement dated March 28, 2006 (the MLPA). Complaint ¶¶ 2-3. Following the usual protocol for creating residential mortgage backed securities, ACE deposited the loans into the Trust. ¶ 4. The loans were securitized through the issuance of over $500 million of certificates pursuant to a Pooling and Servicing Agreement dated as of March 1, 2006 (the PSA). *Id.* In the MLPA, DBSP made over fifty representations and warranties (the Representations) regarding the characteristics and quality of the loans, including those common in many MLPAs (e.g., representations about underwriting guidelines such as the borrower's income and loan-to-value ratio) and those that are somewhat rarer (e.g., a "no-fraud representation").[1] ¶¶ 5-6. Under Section 2.03 of the PSA, DBSP was obligated to cure a breach of a Representation within 60 days of discovery or receipt of notice thereof, or, in the event that such breach could not be cured, DBSP had to repurchase the affected loans within 90 days at a defined Purchase Price. ¶ 26. Both the PSA and the MLPA provide that the Repurchase Protocol is the "sole remedy" with respect to loan losses caused by false Representations.

On March 28, 2012, this action was commenced by two certificateholders (RMBS Recovery Holdings 4, LLC and VP Structured Products, LLC) by filing a Summons with Notice. A single cause of action alleging breach of contract was stated. It is undisputed that these certificate-holders lacked standing to maintain this action under the PSA's no-action clause. They did so, apparently, due to concerns over their claims being time barred, a worry amplified

[1] These representations have been the subject of much litigation involving both investors and monoline insurers. As this decision does not concern substantive disputes over the details of the Representations, the court will not provide further background and assumes familiarity with the recent line of similar cases in this court.

by the Trustee's initial refusal to sue on their behalf. Ultimately, the Trustee was substituted as the plaintiff for the certificate-holders. As discussed *infra*, the manner in which this action was originally commenced, in the end, is not at issue because the relevant statute of limitations did not expire before the substitution.[2]

II. Discussion

On a motion to dismiss, the court must accept as true the facts alleged in the complaint as well as all reasonable inferences that may be gleaned from those facts. *Amaro v Gani Realty Corp.*, 60 AD3d 491 (1st Dept 2009); *Skillgames, L.L.C. v Brody*, 1 AD3d 247, 250 (1st Dept 2003), citing *McGill v Parker*, 179 AD2d 98, 105 (1992); *see also Cron v Harago Fabrics*, 91 NY2d 362, 366 (1998). The court is not permitted to assess the merits of the complaint or any of its factual allegations, but may only determine if, assuming the truth of the facts alleged, the complaint states the elements of a legally cognizable cause of action. *Skillgames*, *id.*, citing *Guggenheimer v Ginzburg*, 43 NY2d 268, 275 (1977). Deficiencies in the complaint may be remedied by affidavits submitted by the plaintiff. *Amaro*, 60 NY3d at 491. "However, factual allegations that do not state a viable cause of action, that consist of bare legal conclusions, or that are inherently incredible or clearly contradicted by documentary evidence are not entitled to such consideration." *Skillgames*, 1 AD3d at 250, citing *Caniglia v Chicago Tribune-New York News Syndicate*, 204 AD2d 233 (1st Dept 1994). Further, where the defendant seeks to dismiss the complaint based upon documentary evidence, the motion will succeed if "the documentary evidence utterly refutes plaintiff's factual allegations, conclusively establishing a defense as a

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In 2003, well before the financial crisis and subsequent flurry of mortgage backed securities litigation, a federal district court dealt with this exact situation. *See Structured Mortg. Trust 1997-2 v Daiwa Finance Corp.*, 2003 WL 548868 (SDNY 2003) (*Daiwa*). In *Daiwa*, the court held that the claim accrued when the PSA was executed because the subject representations "were not true when made" and that the trustee could have made a repurchase demand at that time. *Id.* at *2. Consequently, *Daiwa* held, the statute of limitations runs from the execution of the contract because the claim accrues "when the wrong is committed, and not when the plaintiff discovers it." *Id.*, citing 7B Joseph McLaughlin, Practice Commentaries, CPLR 206 (McKinney's 1990). For the reasons discussed below, this court disagrees with the *Daiwa* holding. CPLR 206(a), the "continuing performance" doctrine, and the nature of the parties' relationship under the PSA militate against *Daiwa*.[3]

Under CPLR 206(a), "'demand is complete' [means] that the Statute of Limitations runs from the time when the party making the demand first becomes *entitled* to make the demand, and not from the time the actual demand is made." *Woodlaurel, Inc. v Wittman*, 199 AD2d 497, 497-

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98 (2d Dept 1993) (emphasis added). In Section 2.03, as in other similar PSAs entered into by DBSP, three steps must be followed before the Trustee can sue DBSP for breach of its repurchase obligations: discovery or receipt of notice by the bank, cure, and repurchase. The Trustee is not *entitled* to sue or make a repurchase demand until discovery or notice by the bank occurs and the cure period lapses. It, therefore, follows that DBSP does not breach the PSA and the claim for the breach does not accrue until DBSP fails to timely cure or repurchase a loan.

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The statute of limitations began to run when DBSP improperly rejected the Trustee's repurchase demand. Ergo, the breach is the failure to comply with the demand. Of course, plaintiff cannot "put off the running of the Statute of Limitations indefinitely" by waiting an unreasonable time to make the demand. *Id.*, citing *Snyder v Town Insulation, Inc.*, 81 NY2d 429, 435 (1993). Had the Trustee not made its demand in 2012 and instead waited a number of years to file suit, the inquiry might be different. However, not only did the Trustee file suit shortly after making demand, DBSP actually contends (as discussed below) that this action was commenced too quickly. In conclusion, plaintiff's claims did not accrue on the date of the contracts' execution. Hence, the claims are timely.

B. The Repurchase Protocol

The court rejects DBSP's arguments that the Trustee's supposed failure to comply with the Repurchase Protocol's conditions precedent to bring suit precludes its claims. First, the Trustee's alleged failure to wait the requisite time to bring suit is irrelevant given DBSP's repudiation of its repurchase obligations under the PSA. Next, waiting to cure is utterly pointless because the alleged false Representations cannot be cured since most, if not all of the loans, have defaulted. Finally, the Trustee's failure to set forth which of the specific loans are affected by false Representations is not fatal to the Complaint because CPLR 3016(b)'s particularity requirements do not apply to a breach of contract claim. Unlike similar cases, plaintiff does not allege fraud. Nonetheless, given the specificity requirements in Repurchase Protocol, the specific identification of which loans have been affected by false Representations is fair game for interrogatories.

As for DBSP's contention that the PSA's damages calculation prohibits recovery by the Trustee, questions of fact clearly preclude dismissal on this ground. Even if DBSP were correct that Released, Charged Off, and Liquidated Loans are not subject to repurchase, dismissal would still not be warranted because DBSP needs to establish that all of the non-conforming loans fell into these defined categories. Discovery is necessary to make these determinations.

That being said, DBSP's argument that loans in these categories are not subject to repurchase because they are no longer assets of the Trust (or that their defined Purchase Price is now $0) is unconvincing. If DBSP were correct, it would be perversely incentivized to fill the Trust with junk mortgages that would expeditiously default so that they could be Released, Charged Off, or Liquidated before a repurchase claim is made. Indeed, if DBSP learned that loans were non-conforming and played a crafty game of accounting by moving them off the Trust's books to their own to evade their repurchase obligations, such actions would be a breach of the duty of good faith and fair dealing. Consequently, it is to no avail to contend that the non-conforming loans are long gone and the Trustee's repurchase rights have been extinguished by DBSP's actions.

Stepping back, it is worth keeping in mind that DBSP does not bear the risk of loss on all loans that default. Conforming loans, where the Representations are true, will sometimes default for reasons that have nothing to do with borrowers lying or underwriter fraud. If "good" mortgages did not have real default risk, mortgage interest rates would be even lower than their current historically depressed levels. In reality, borrowers will occasionally default due to myriad unexpected circumstances, such as losing their job. In those cases, the Certificateholders bear the risk of loss and their recovery is limited to whatever proceeds can be obtained through foreclosure. In contrast, where, as here, borrowers allegedly defaulted due to the Representations being false, such risk is meant to be borne by DBSP. If, as DBSP contends, the Certificateholders' recovery on misrepresented loans is limited to foreclosure proceeds, the repurchase remedy would be virtually worthless.

Additionally, DBSP's contention that it cannot "repurchase" a loan because the loan technically does not "exist" after foreclosure, misses the point. Foreclosure is not an alternative means of recovery for non-conforming loans; it is a set off to DBSP's obligation to pay back the cost of the loan. The PSA's damages calculation includes foreclosure proceeds because the Repurchase Protocol is a mechanism whereby the Certificateholders can recover the cost of the loan minus the revenue generated (which includes pre-default mortgage payments and foreclosure proceeds).

Nonetheless, DBSP correctly maintains that any recovery under Section 2.03 must be limited to the formula set forth in the PSA. Therefore, if sampling is to be used as a means to calculate damages, the parties must come up with a sampling mechanism that meaningfully reflects the PSA's damages calculation. The parties may not disregard such calculation in an attempt to seek complete rescission of the PSA merely out of frustration that being bound by the strict terms of the contract is laborious and inconvenient. The degree to which bargained for remedies are simple or convoluted is a matter for sophisticated commercial actors to address before the execution of a contract. It is not something to complain about in subsequent litigation. Accordingly, it is

ORDERED that the motion to dismiss the Complaint by defendant DB Structured Products, Inc. is denied; and it is further

ORDERED that the parties are to appear in Part 54, Supreme Court, New York County, 60 Centre Street, Room 228, New York, N.Y., for a preliminary conference on June 4, 2013 at 10:00 in the forenoon.

Dated: May 13, 2013

ENTER:

J.S.C.