SUPREME COURT OF THE STATE OF NEW YORK
COUNTY NEW YORK

MBIA INSURANCE CORP.,	:	
Plaintiff,	:	
v.	:	Index No. 64676/2012 Honorable Alan D. Scheinkman Commercial Division
J.P. MORGAN SECURITIES LLC (formerly known as BEAR, STEARNS & CO. INC.),	:	Motion Sequence No. 2 (Oral Argument Requested)
Defendant.	:	

DEFENDANT'S MEMORANDUM OF LAW IN SUPPORT OF ITS MOTION FOR SUMMARY JUDGMENT PURSUANT TO CPLR 3212

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Defendant J.P. Morgan Securities LLC ("JPMS") (formerly known as Bear, Stearns & Co. Inc. ("Bear Stearns")) respectfully submits this memorandum of law in support of its motion, pursuant to Rule 3212 of the New York Civil Practice Law and Rules ("CPLR"), for summary judgment in favor of JPMS and against plaintiff MBIA Insurance Corp. ("MBIA") on the Complaint filed in this action by MBIA on September 14, 2012.

PRELIMINARY STATEMENT

This is the second lawsuit brought by MBIA to recover losses it incurred on a residential mortgage-backed securities ("RMBS") transaction known as GMAC Mortgage Corporation Home Equity Loan Trust 2006-HE4 (the "2006-HE4 Securitization"). Two years before filing this lawsuit against Bear Stearns, MBIA filed a very different Complaint (the "GMAC Mortgage Complaint")[1] alleging that it was ***GMAC Mortgage***, the sponsor of the transaction and the originator of the mortgage loans included in the transaction, who fraudulently induced MBIA to issue a financial guaranty policy. MBIA alleged that GMAC Mortgage provided MBIA with false and misleading information concerning the quality of the mortgage loans originated and securitized by GMAC Mortgage in the 2006-HE4 Securitization.

In its GMAC Mortgage Complaint, MBIA did not mention Bear Stearns at all, let alone name Bear Stearns as a defendant or suggest that Bear Stearns also "induced" MBIA to insure the 2006-HE4 Securitization through other purported misrepresentations. Indeed, in its GMAC Mortgage Complaint, MBIA specifically identified the allegedly false and misleading information on which MBIA purportedly relied to its detriment in agreeing to insure the transaction, all of which was allegedly provided to MBIA by GMAC Mortgage and none of which involved Bear Stearns. Yet, when GMAC Mortgage filed for bankruptcy in May 2012,

[1] *See MBIA Insurance Corp. v. GMAC Mortgage, LLC*, No. 600837/2010 (N.Y. Sup. Ct. N.Y. Ctny.).

resulting in a mandatory stay of MBIA's lawsuit against GMAC Mortgage, MBIA's lawyers began searching for a new set of "deep pockets" to sue, and contrived an entirely new theory of fraudulent inducement and reliance against Bear Stearns.

Unlike GMAC Mortgage, Bear Stearns neither sponsored the 2006-HE4 Securitization nor originated any of the mortgage loans included in the transaction and instead served solely as the lead underwriter for the transaction. Ignoring its prior allegations against GMAC Mortgage, MBIA now claims that Bear Stearns is liable for all of MBIA's past and future insurance losses on the 2006-HE4 Securitization because it was really Bear Stearns, not GMAC Mortgage, who induced MBIA to issue its financial guaranty policy for the transaction. But even passing that MBIA's new theory of fraud against Bear Stearns directly conflicts with its earlier theory of fraud against GMAC Mortgage, it is flatly contradicted by the undisputed record evidence, including deposition testimony provided by MBIA's own witnesses.

Contrary to its GMAC Mortgage Complaint, MBIA now alleges that Bear Stearns altered a due diligence report to conceal alleged deficiencies in a large proportion of the loans comprising the collateral pool, and that MBIA read and relied upon that report to issue the policy. Yet the record shows that MBIA ***did not read or review*** the due diligence report until a week ***after*** it issued its financial guaranty policy and closed the 2006-HE4 Securitization. In particular, the record shows that Bear Stearns sent a due diligence report a few hours before the deal closed on September 27, 2006, to two individuals at MBIA: Carl Webb, a Managing Director and head of the new business group, and Lauren Desharnais, who worked for Webb and had certain day-to-day responsibilities for the transaction. Webb testified that he never read the report. Desharnais had no recollection whatsoever of the report, could not say whether she had read or reviewed it prior to the closing of the transaction, and her contemporaneous emails and

travel records—she flew home from Minneapolis to New York on the day of the closing and was on the plane when the due diligence report was sent to her—confirm that she did not review the report until October 3, a week ***after*** closing. Theresa Murray, a Director at MBIA responsible for chairing the Underwriting Committee for the 2006-HE4 Securitization, and the person at MBIA actually responsible for reviewing the report and releasing the insurance policy, likewise testified that she did not even receive the report from Desharnais until October 3, much less review it or any preliminary version prior to early October. In short, MBIA's entire theory of liability against Bear Stearns is predicated on a report that it did not read prior to the closing of the subject transaction. All of these facts are undisputed.

As this Court rightly observed at the very first conference on this case, if MBIA "didn't read the report that they claim is false," then even if the report "has material misrepresentations, replete in its pages… proving on those facts, proving reliance is going to be very difficult." (Ex. A at 20:21-21:8).[2] In fact, under New York law it is not just difficult, it is impossible. With discovery now closed, MBIA cannot present any evidence, much less the required clear and convincing evidence, sufficient to raise a triable issue of fact to allow a reasonable jury to find for it on actual reliance, justifiable reliance, or materiality, each of which is an essential element of its fraud claim. Because MBIA's fraudulent inducement claim cannot survive on this record, JPMS is entitled to summary judgment in its favor.

[2] The exhibits cited herein are exhibits to the accompanying Affirmation of Anastasia A. Angelova in Support of Defendant's Motion for Summary Judgment.

FACTUAL BACKGROUND

A. GMAC Mortgage's 2006-HE4 Securitization

The 2006-HE4 Securitization was an asset-backed securitization sponsored by GMAC Mortgage. (Ex. B ¶¶ 15-16). Bear Stearns was the lead underwriter. (*Id.* ¶¶ 17-18; Ex. C ¶¶ 17-18). MBIA won the right to issue financial guaranty insurance for the securitization through a competitive bid process in September 2006. (Ex. B ¶ 19; Ex. C ¶ 19; Ex. D at 71:14-73:6, 93:11-21). At the time of the transaction, MBIA was a sophisticated and experienced insurer of RMBS securitizations, having participated in numerous such transactions, including a prior securitization sponsored by GMAC Mortgage in 2004 involving the same structure and type of collateral as the 2006-HE4 Securitization. (*Id*. at 53:9-56:2, 88:16-89:4).

MBIA commenced its review and bid process for the 2006-HE4 Securitization on September 14, 2006, and chose to bid for the deal despite having to proceed under a "very tight" time frame with "tight" resources. (Ex. D at 41:2-42:13; Ex. E). Webb testified that MBIA made the bid a "top priority" based on its view that GMAC Mortgage was a "very good originator" and "very strong counterparty." (Ex. D at 44:5-46:12). MBIA "wanted to win" the securitization and sought to be competitive with its bid, charging a lower premium to improve the competitiveness of its bid. (*Id*. at 42:18-43:25, 56:5-60:20, 75:24-76:10, Ex. F).

Murray testified that at the time of the transaction, there was an "enormous amount of pressure" from MBIA's new business unit to close transactions, and the time frame for completing deals was "very quick" due to the "competitive business environment among the monoline insurers." (Ex. G at 18:13-20:17; Ex. H). This pressure created a "horrible work environment" where most decisions were made "outside" of the formal risk process, and where MBIA was "effectively committing at the business stage." (Ex. G at 26:2-28:5; 50:19-51:23). Murray could not recall a single instance in which MBIA voted to approve a transaction at the

bidding stage, but later decided to back out of the bid. (*Id*. at 42:23-43:20).

On September 19, 2006, MBIA approved and sent a Bid Letter to GMAC Mortgage containing its proposal for the 2006-HE4 Securitization. (Ex. D at 73:7-25, 79:18-80:24; Ex. I). Bear Stearns was neither a signatory to nor an addressee of the Bid Letter. (Ex. D at 84:23-85:9, 91:17-92:7; Ex. I). Later that day, GMAC Mortgage informed MBIA that it had "won" the securitization, and MBIA celebrated the announcement as "[g]reat news…!" (Ex. D at 92:8-93:16; Ex. J). MBIA knew it was going to be "very busy," as it had to close in just eight days rather than the more typical time frame of thirty days. (Ex. D at 93:17-95:6; Ex. J). The 2006-HE4 Securitization closed on September 27, 2006. (Ex. B ¶ 40).

B. MBIA's Lawsuit Against GMAC Mortgage

Not long after the 2006-HE4 Securitization closed, the U.S. residential real estate market collapsed and the economy fell into recession. MBIA subsequently suffered losses on the 2006-HE4 Securitization (along with dozens of other RMBS transactions it insured). In its GMAC Mortgage Complaint, filed more than two years before the present Complaint, MBIA alleged that GMAC Mortgage "blatantly violated" numerous contractual representations and warranties in connection with the transaction. (Ex. K ¶¶ 3-7, 46-57). It also alleged that GMAC Mortgage provided MBIA, and MBIA justifiably relied upon the following false and misleading information: (i) loan "tapes" that included data about each borrower's creditworthiness, (ii) schedules setting forth key statistics about the loan pools, (iii) representations and warranties in the transaction documents regarding compliance with underwriting standards and applicable law, and (iv) "shadow ratings" reflecting what credit ratings the transactions would carry without insurance. (*Id*. ¶¶ 3-7, 31-32, 46-69). MBIA further alleged that it had undertaken eight prior GMAC Mortgage-sponsored RMBS securitizations, and that its "longstanding relationship with [GMAC Mortgage] caused MBIA to trust that [GMAC Mortgage] would conduct itself in good

faith." (*Id*. ¶ 56). MBIA asserted claims against GMAC Mortgage for fraud, negligent misrepresentation, and breach of contract. (*Id*. ¶¶ 98-162).

Nowhere in its GMAC Mortgage Complaint did MBIA allege, as it now does, that it also relied on the due diligence report provided by Bear Stearns in deciding to insure the transaction. Indeed, although the GMAC Mortgage Complaint spans 58 pages and 162 paragraphs and carefully details the circumstances of the alleged fraud that supposedly led MBIA to unwittingly insure the transaction, there is not a single reference to Bear Stearns or the due diligence report.

C. MBIA Invents a New Theory of Fraud Against Bear Stearns

Following GMAC Mortgage's bankruptcy, MBIA's counsel invented a new theory of fraud against Bear Stearns. The Complaint in this case alleges that MBIA relied upon the due diligence results provided by Bear Stearns to "test the accuracy" and "assess[] th[e] risks" of the representations and warranties that GMAC Mortgage made to MBIA. (Ex. B ¶¶ 2-3, 24, 26, 35-36). The new Complaint makes no mention of the loan tapes, schedules, or "shadow ratings" that were so central to the GMAC Mortgage Complaint, and describes GMAC Mortgage's "representations and warranties" only as items to be tested and verified through the due diligence provided by Bear Stearns. (*Id*.). The Complaint also alleges that MBIA actually read and reviewed the due diligence report before agreeing to insure the transaction. (*Id*. ¶ 59). The undisputed factual record is to the contrary and confirms that MBIA's lawyers invented a new theory of fraud, untethered to the actual facts, solely to manufacture a lawsuit against Bear Stearns to replace MBIA's derailed lawsuit against GMAC Mortgage.

D. The Undisputed Facts Concerning Due Diligence

1. MBIA's Underwriting Committee Approved the 2006-HE4 Securitization Prior to Receiving the Due Diligence Results

Rather than undertake its own loan-level due diligence, MBIA followed what it viewed as

the "market standard" at the time, which was to have the underwriter (Bear Stearns) contract with a due diligence firm. (Ex. D at 181:8-14). The Bid Letter provides in relevant part, "GMAC Mortgage and Bear Stearns agree to share loan file diligence results with MBIA." (Ex. B ¶ 3; Ex. C ¶ 3; Ex. D at 131:24-132:18; Ex. I). It adds, "To the extent that … the due diligence results prove materially different collateral, our overcollateralization target and fee will change accordingly." (Ex. D at 89:5-91:16; Ex. I). Bear Stearns engaged Mortgage Data Management Corporation ("MDMC") to conduct due diligence. (Ex. B ¶ 3; Ex. C ¶ 3).

On September 25, 2006, two days prior to closing, MBIA's Underwriting Committee voted its conditional approval to issue a policy for the 2006-HE4 Securitization. (Ex. D at 133:18-136:9, 144:11-146:22, 147:16-147:24; Ex. L; Ex. G at 65:4-67:11). One of the closing conditions was "due diligence follow-up." (Ex. D at 151:16-152:5; Ex. L). Murray released the policy in MBIA's system the same day, meaning all work had been completed to her satisfaction and the policy could be signed and sent, even though MBIA's Underwriting Committee had not yet received the due diligence results. (Ex. G at 52:20-55:4, 68:15-76:7; Ex. M; Ex. D at 131:24-133:14, 177:4-180:3). The Underwriting Committee Memorandum made only a passing reference to due diligence results, did not identify due diligence on its list of "major analytical points" supporting pursuit of the 2006-HE4 Securitization, and did not identify Bear Stearns as a "key player" to the transaction. (Ex. D at 111:5-112:2, 122:6-125:8, 131:24-132:4; Ex. N).

2. Three MBIA Employees Received the Due Diligence Results, But None Reviewed Them Prior to Closing

Bear Stearns sent due diligence results to MBIA on September 27, 2006, the day of closing. Robert Durden, a vice president at Bear Stearns, received the due diligence results by email as two spreadsheets from John Mongelluzzo, a member of Bear Stearns' mortgage finance department. Durden combined the spreadsheets and forwarded them by email at approximately

10:00 a.m. EST to Webb and Desharnais. (Ex. O at 22:19-23:11, 85:4-23; Ex. P; Ex. Q at 57:7-10, 63:16-20, 204:14-207:4, 219:10-220:22; Ex. R; Ex. S at 172:4-24). MBIA alleges that Bear Stearns removed approximately 50 columns of information before sending the due diligence report to MBIA, including loan grades identifying deficiencies in the collateral. (Ex. B ¶¶ 4-5, 38, 42-49, 51-57).

It is undisputed that only three MBIA employees ever received the due diligence results: Webb and Desharnais, who received them from Durden on September 27, and Murray, who received them from Desharnais on October 3, a week after the deal closed. (Ex. T at Resp. to Interrog. No. 8; Ex. O at 76:15-77:11, 85:4-23, 117:21-120:3; Ex. P; Ex. U; Ex. V; Ex. G at 107:16-109:5; Ex. Q at 57:7-10, 63:16-20, 204:14-207:4, 219:10-220:22). The record shows that none of them looked at the due diligence results prior to close.

Webb admits that he did not review the results at any time. Webb testified that he "didn't review the results" and could not recall if MBIA even received them prior to closing. (Ex. D at 39:19-40:14, 132:6-133:14).

Murray admits that she did not review the results prior to closing. Webb and Murray confirmed that it was Murray's responsibility to review the due diligence, to confirm that all closing conditions had been met, to sign off on the underwriting, and to determine whether the deal would go forward. (Ex. D at 13:2-16:13; Ex. G at 12:24-15:25, 21:3-25, 65:4-67:11; Ex. L). Murray testified that she completed this responsibility two days earlier, September 25, when she released the insurance policy in MBIA's system ***before*** receiving the due diligence. (Ex. G at 68:15-70:11, 100:16-102:3; Ex. M). She also testified that she did not receive the due diligence results until six days after closing, on October 3. (Ex. T at Resp. to Interrog. No. 8; Ex. O at 76:15-77:11, 117:21-120:3; Ex. U; Ex. V; Ex. G at 107:16-109:5). Thus, it is undisputed that the

person with the responsibility at MBIA for reviewing the due diligence results did not do so until after closing. That leaves Desharnais as the only person who could have even looked at the due diligence results prior to close.

Desharnais has no recollection of reviewing the due diligence results and the evidence confirms that she did not do so until after closing. Desharnais acknowledged that it was not her responsibility to review and sign off on the due diligence results; that was Murray's responsibility as the chair of the Underwriting Committee. (Ex. O at 28:19-30:10). Unlike Murray, Desharnais did not have voting authority on the Underwriting Committee; she was junior to Webb in the new business unit. (Ex. D at 14:14-16:13, 145:9-147:8). Desharnais did not review or rely upon the due diligence results prior to closing. Desharnais has no recollection of receiving the due diligence results, reviewing them, or discussing them with Murray on the day she received them. (*See, e.g.*, Ex. O at 17:4-18:3, 54:2-16, 73:5-74:9, 83:4-84:23, 85:24-86:6, 93:7-93:10, 126:25-127:19, 131:19-24). Desharnais received the due diligence at 10:00 a.m. EST and the deal closed prior to 1:38 p.m. EST that same day. (Ex. O at 74:18-23, 82:7-14, 85:24-86:4; Ex. W). On the day of closing, Desharnais was traveling back to New York from a meeting she and Murray had attended in Minneapolis. (Ex. O at 64:7-12, 73:19-74:4; Ex. X; Ex. Y). Her flight departed Minneapolis at approximately 8:00 a.m. EST and arrived in New York City (LaGuardia) at approximately 10:37 a.m. EST. (Ex. Z at MBIA-JPM-00045100).[3] She then took a car service from the airport to her home in New Rochelle, New York. (Ex. Z at MBIA-JPM-00045098).

Desharnais had no recollection of bringing a laptop with her to Minneapolis, though she

[3] Publicly available flight records indicate that Desharnais' flight departed Minneapolis three minutes early, at 7:57 a.m. EST, and arrived in New York City one minute early, at 10:36 a.m. EST. (Ex. AA). The Court may take judicial notice of matters of public record. *Krause v. Piccozzi*, 106 A.D.3d 1007, 1008 (2d Dep't 2013).

believed she may have had one based on an email she sent before the trip. (Ex. O at 83:4-84:23, 87:15-24). Her travel documents, however, reflect that MBIA was not able to accommodate her request for a laptop. (Ex. BB at MBIA-JPM-00045089). Desharnais acknowledged that any Blackberry or similar smart phone device would not have been suitable to review a large Excel spreadsheet like the due diligence report, and had no idea what she would have done to access her emails with a laptop at that time. (Ex. O at 128:5-130:15). MBIA's network remote log on information indicates that Desharnais attempted to log into MBIA's system on the morning of September 27 at 10:20 a.m., and that she logged out at 10:22 a.m. EST. (Ex. CC at MBIA-JPM-00045108).

Desharnais did nothing with the results until October 3. That day, Desharnais finalized and sent out a pricing memorandum for the 2006-HE4 Securitization that she had originally committed to finish prior to closing. (Ex. O at 50:12-51:6, 52:3-8, 54:21-55:18). Later the same day, Desharnais sent the due diligence results to Murray for the first time, and stated, "I don't see the usual type of reporting except on the last tab." (*Id*. at 117:21-121:19; Ex. V). Murray responded the next day, October 4, that they should get together to discuss the results "maybe some time later today after we have both had a chance to review." (*Id*.).

3. Desharnais Admits That, Had She Reviewed the Due Diligence Results, She Would Have Noticed the Missing Loan Grades

Desharnais described herself as "very experienced" in reviewing due diligence reports, having reviewed them throughout the entire period of her 10- to 15-year career at MBIA as a team leader, and said she "knew what I wanted to find" when she reviewed due diligence results. (Ex. O at 36:2-22). Among other contents, loan grades mattered "very much," and she looked for loan grades, compliance issues and underwriting issues. (*Id*. at 31:24-32:19, 35:6-15; 134:11-135:4). She agreed that, if the loan grades were missing from a due diligence spreadsheet

provided to her, "I would think I would have noticed, yes." (*Id*. at 32:14-33:19). When Desharnais was asked at her deposition to review the due diligence results for the 2006-HE4 Securitization that Durden had transmitted to her on September 27, she immediately noticed that the loan grades were missing from the spreadsheet. (*Id*. at 84:24-89:12; Ex. P).

Webb, Murray, and Desharnais all testified that MBIA could have stopped the closing if it did not get all the information it was entitled to receive under the Bid Letter, and that they could have stopped the closing until they were satisfied with the due diligence. (Ex. D at 36:17-37:23; Ex. O at 112:11-115:10; Ex. G at 29:3-31:18). Desharnais testified that, if she noticed information was missing and had a problem with it, she would stop MBIA from closing. (Ex. O at 112:11-115:10). Yet on September 27, Desharnais took no action whatsoever. Though she is the only MBIA employee who could possibly have reviewed the results prior to closing, and was demonstrably capable of spotting the missing loan grades and halting the closing, her contemporaneous emails reflect that she did nothing with the results until October 3, and even then merely remarked on the absence of "the usual type of reporting[.]" (*Id*. at 117:21-121:19; Ex. V).

4. MBIA Did Not Place Weight on Due Diligence Results in RMBS Transactions with GMAC Mortgage

Desharnais speculated at her deposition that, although she had no specific recollection of reviewing the due diligence results, she "would have" reviewed the due diligence results prior to closing because it was her general "practice" to review due diligence and to discuss it with Murray prior to closing, and because she "would not have let the deal close if those conditions weren't fulfilled." (Ex. O at 39:24-40:3, 82:24-86:4, 121:6-10). Webb similarly testified that the "general practice" at MBIA was that it "would have received" the due diligence results prior to closing, and that the policy "would not have gone out if we didn't have the results." (Ex. D at

39:19-40:5). Desharnais' testimony made clear, however, that she had no "specific knowledge" or "recollection" of reviewing the due diligence results; she just "doubt[ed]" she would have signed off and closed the deal without reviewing the results, based on what she "would have" done in her general "practice." (Ex. O at 70:19-72:6, 82:24-86:7, 121:6-19).

Yet Desharnais also testified that when MBIA was comfortable with its counterparty, as it was with GMAC Mortgage, it was allowable to complete certain tasks after a transaction closed. (*Id*. at 52:3-8; 54:21-55:18, 117:21-120:3; Ex. V). She admitted that this had been done in the 2006-HE4 Securitization, with the pricing memorandum she sent out on October 3 being an example. (*Id*.). And in another case, *MBIA Ins. Corp. v. Countrywide Home Loans, Inc., et al.*, Desharnais admitted that it was not "infrequent" between 2005 and 2007 for MBIA to allow a transaction to close when due diligence had not been completed, because MBIA did not want to "hold up the closing." (Ex. DD at 79:22-81:10).

Murray likewise testified that, due to the intense pressure from MBIA's new business unit to close transactions, securitizations frequently closed and policies issued despite the fact that MBIA was not in possession of all information, including in many instances final due diligence reports. (Ex. G at 19:22-20:12; 21:3-22:12; 24:19-25:21).

ARGUMENT

Under CPLR 3212, a motion for summary judgment "shall be granted" if the papers and proof are sufficient "to warrant the court as a matter of law in directing judgment in favor of any party." CPLR 3212. The party moving for summary judgment must present "sufficient evidence to demonstrate as a matter of law the absence of a material issue of fact." *Tech. Support Servs., Inc. v. Int'l Bus. Machs. Corp.*, No. 02891/2006, 2007 WL 4500382, at *17 (N.Y. Sup. Ct. Westchester Cnty. Dec. 3, 2007) (J. Scheinkman). The burden then shifts to the opponent to "produce sufficient evidence in admissible form to establish the existence of a triable issue of

fact." *Id.* at *17. Summary judgment "is properly granted when the opponent of the motion raises only ***feigned*** issues of fact." *Id.* at *18 (emphasis added). A "sham or frivolous issue will not preclude summary relief." *Kornfeld v. NRX Tech., Inc.*, 93 A.D.2d 772, 773 (1st Dep't 1983), *aff'd*, 62 N.Y.2d 686 (1984).

MBIA must satisfy a demanding legal standard to survive summary judgment on its fraud claim. A claim for common law fraud (or fraud in the inducement) requires a plaintiff to establish: (i) a misrepresentation of material fact; (ii) knowledge by the party making the misrepresentation that it was false when made; (iii) justifiable reliance upon the statement; and (iv) damages. *Orlando v. Kukielka*, 40 A.D.3d 829, 831 (2d Dep't 2007); *Abrahami v. UPC Constr. Co., Inc.*, 224 A.D.2d 231, 232-33 (1st Dep't 1996). Whether at summary judgment or trial, MBIA must present evidence sufficient to satisfy each of these elements by clear and convincing proof. *See Valenti v. Trunfio*, 118 A.D.2d 480, 484 (1st Dep't 1986); *Kleinman v. Blue Ridge Foods, LLC*, No. 9603/2010, 2011 WL 2899428, at *5 (N.Y. Sup. Ct. Kings Cnty. July 7, 2011); *see also Vitolo v. Mentor H/S, Inc.*, 426 F. Supp.2d 28, 37 (E.D.N.Y. 2006). This standard demands "a high order of proof" and forbids the awarding of relief where the evidence is "loose, equivocal, or contradictory." *Abrahami*, 224 A.D.2d at 233 (internal citations omitted). MBIA cannot meet its high order of proof in this case with respect to any of the three elements at issue on this motion: actual reliance, justifiable reliance, or materiality. MBIA did not even look at the allegedly fraudulent due diligence results prior to closing on the 2006-HE4 Securitization, could not have justifiably relied upon the results because the absence of information Bear Stearns supposedly "concealed" was obvious, and did not consider the results at all material to its decision to proceed with issuing a financial guaranty policy. MBIA's fraud claim fails as a matter of law.

I. JPMS IS ENTITLED TO SUMMARY JUDGMENT BECAUSE MBIA CANNOT PRESENT ANY EVIDENCE OF ACTUAL RELIANCE

To meet its burden of proving reliance, MBIA must establish both (i) actual, direct reliance on the alleged misrepresentations or omissions at issue and (ii) that such reliance was justifiable. *See KNK Enters., Inc. v. Harriman Enters., Inc.*, 33 A.D.3d 872, 872 (2d Dep't 2006). With respect to actual reliance, even where an alleged representation is "demonstrably false," summary judgment is nonetheless appropriate where "[n]othing in this record establishes that plaintiffs in fact relied on any misrepresentation by defendants to their detriment." *Vermeer Owners, Inc. v. Guterman*, 78 N.Y.2d 1114, 1116 (1991). That is the case here.

A. There Is No Triable Issue of Fact on Actual Reliance

MBIA cannot show that it actually relied upon Bear Stearns' due diligence results when it closed on the 2006-HE4 Securitization, because the undisputed evidence establishes that nobody at MBIA examined the results until October 3, 2006, six full days after closing. The Underwriting Committee voted to conditionally approve the transaction and Murray released the policy in MBIA's system on September 25, two days prior to closing, without having received the due diligence results. Durden sent the results to Webb and Desharnais on September 27, the morning of closing. Webb admits that he did not look at the results at all. Murray, the person actually responsible for review and sign-off of the due diligence results, admits that she did not even received the results until October 3, and did not review the results or discuss them with Desharnais prior to closing. *See* Factual Background §§ D.1-D.2, *supra*. As Murray testified:

> Q. * * * [I]sn't 2006 HE4 another example of a transaction in which you didn't review the final due diligence until after the policy was issued? * * *
>
> A. It would appear that ***we were looking at the final due diligence after the deal closed*** based on this, yes.

(Ex. G at 108:18-109:5 (emphasis added)).

As for Desharnais, she admits that she has no recollection whatsoever of receiving the due diligence results, reviewing them, or discussing them with Murray prior to close. *See* Factual Background § D.2, *supra*. This total lack of recollection, standing alone, is nearly always fatal to a fraud claim, as fraud cannot be proven by clear and convincing evidence on failed recollections and guesswork. *See Vitolo*, 426 F. Supp.2d at 37 (E.D.N.Y. 2006) (holding that a plaintiff cannot show reliance where he cannot remember what he was told); *Schultz v. Comm'l Programming Unlimited, Inc.*, No. 91 CIV 7924, 1992 WL 396434, at *3 (S.D.N.Y. Dec. 23, 1992) (holding that an individual's vague recollections were insufficient to establish clear and convincing evidence of reliance); *Carter v. Newsday, Inc.*, 528 F. Supp. 1187, 1191 (E.D.N.Y. 1981). "Speculative" or "conclusory" assertions of reliance will not prevent summary judgment under the clear and convincing evidence standard. *Callisto Pharm., Inc. v. Picker*, 74 A.D.3d 545, 545-46 (1st Dep't 2010).

Not only is Desharnais incapable of recalling any facts to demonstrate reliance, but all evidence is to the contrary. Her travel records and data logs reflect that she was traveling from Minneapolis to New York, and then from the airport to her home, for much of the time between Durden's transmittal of the due diligence results and the closing. Her travel records reflect that she did not have a laptop. Her single, two-minute log on attempt that morning coincides almost exactly with the time her plane landed, and Desharnais admits that she could not have reviewed the results on a Blackberry or smart phone. These facts are incompatible with any inference, much less clear and convincing proof, that Desharnais reviewed or relied upon the due diligence results prior to close on the 2006-HE4 Securitization. *See* Factual Background § D.2, *supra*.

Further evidencing Desharnais' failure to review the due diligence results prior to closing is her own inaction that day. Desharnais was very experienced, knew what she wanted to find

when she reviewed due diligence results, and actively looked for loan grades, compliance issues, and underwriting issues. She had little difficulty at her deposition identifying, after only a brief review, the absence of loan grades from Bear Stearns' spreadsheet. Indeed, when Desharnais sent the results to Murray six days later, on October 3, she remarked that they lacked "the usual type of reporting." Yet she did not send a single email or raise a single concern on the day of closing. Not coincidentally, October 3 is also the day that Desharnais completed a pricing memorandum for the 2006-HE4 Securitization that was due prior to closing. There is simply no doubt that Desharnais completed her closing activities, including the pricing memorandum and her review of the due diligence results, six days ***after*** closing on October 3. *See id*. §§ D.2-D.3

MBIA's failure to review or rely upon the due diligence results prior to closing defeats its fraudulent inducement claim as a matter of law. A plaintiff "cannot sustain a cause of action for fraud if defendant's misrepresentation did not form the basis of reliance." *Sec. Investor Prot. Corp. v. BDO Seidman*, 95 N.Y.2d 702, 709 (2001). MBIA cannot have relied on materials it never read prior to closing. *See Singer Co. v. Stott & Davis Motor Express, Inc.*, 79 A.D.2d 227, 232-33 (4th Dep't 1981) (dismissing claims where "[t]here was no showing that [plaintiff] relied on the representation"); *Albion Alliance Mezzanine Fund L.P. v. State Street Bank and Trust Co.*, 797 N.Y.S.2d 699, 705 (N.Y. Sup. Ct. N.Y. Cnty. 2003) (granting summary judgment in part because plaintiffs submitted no evidence that anyone "actually read or relied on" alleged misrepresentations); *Vitolo*, 426 F. Supp.2d at 37 (granting summary judgment where plaintiff failed to present evidence "that he did, in fact, rely on any of the statement or documents to which he draws this Court's attention"); *Gabriel Capital, L.P. v. NatWest Fin., Inc.*, 177 F. Supp.2d 169, 174 (S.D.N.Y. 2001) (holding there could be no reliance on misrepresentations in Offering Memorandum received after plaintiff decided to enter transaction).

Nor can MBIA rely upon mere transmittal of the final report as Bear Stearns' confirmation of the collateral pool. As a matter of law, MBIA cannot meet its burden of proving that it actually relied upon Bear Stearns' purported omission of "significant problems" from its transmittal of a report that MBIA received but never read, any more than it can prove actual reliance upon purported misrepresentations contained in the report. New York has "repeatedly refused to import" a "presumption of reliance for misleading omissions" into common law fraud claims. *Int'l Fund Mgmt. S.A. v. Citigroup Inc.*, 822 F. Supp.2d 368, 387 (S.D.N.Y. 2011). MBIA "must therefore show actual reliance for misrepresentations ***and*** omissions." *Id*. (emphasis in original). *See also Lerner v. Fleet Bank, N.A.*, 459 F.3d 273, 292 (2d Cir. 2006) ("In the absence of an allegation that the plaintiffs actually relied on the banks' omissions, they have not stated a claim for fraudulent concealment."); *Eagle Comtronics, Inc. v. Pico Prods., Inc.*, 270 A.D.2d 832, 833 (4th Dep't 2000) (holding that, to prevail on a fraud cause of action, the plaintiff "had to establish that the alleged misrepresentations or omissions were material and that [plaintiff] actually and justifiably relied on them"). Regardless of what Bear Stearns included or omitted from the due diligence results, the undisputed fact is that MBIA did not look at the results, and thus as a matter of law could not have relied upon any misrepresentation or omission allegedly contained in those results.

B. Desharnais' "General Practice" Testimony Does Not Raise a Triable Issue of Fact With Respect to Actual Reliance

As for Desharnais' conclusory assertions, without any basis in recollection, that she "would have" reviewed the due diligence results because it was her "practice" to do so, that does not raise a triable issue of fact as to actual reliance. Evidence of a practice is admissible to prove conformity with that practice on a specific occasion only "where the proof demonstrates a deliberate and repetitive practice by a person in complete control of the circumstances." *Rivera v.*

Anilesh, 8 N.Y.3d 627, 633-34 (2007) (internal quotes omitted). The Court of Appeals recently clarified that conclusory statements are insufficient to establish evidence of practice; there must be a specific protocol that the witness "repeatedly and invariably used." *Galetta v. Galetta*, 221 N.Y.3d 186, 198 (2013); *see also Halloran v. Virginia Chems. Inc.*, 41 N.Y.2d 386, 393 (1977).

Here, even on its own terms, Desharnais' "practice" testimony is equivocal. She was only able to say that she "doubt[ed]" she would have closed without reviewing the results, even though it was not her responsibility to review and sign off on the due diligence results, while repeatedly admitting her lack of specific knowledge or recollection and offering no description of a typical protocol that she "repeatedly and invariably" followed in reviewing due diligence results. Indeed, both Desharnais and Murray admitted that it was allowable to complete certain tasks after closing when MBIA was comfortable with its counterparty, as it was with GMAC Mortgage, and that securitizations often closed despite the absence of final due diligence reports. *See* Factual Background § D.4, *supra*. In the *MBIA v. Countrywide* litigation, Desharnais admitted that she reviewed due diligence reports ***after*** closing on a "not infrequent" basis, confirming that her supposed "practice" was neither deliberate nor repetitive. *Id*.

Nor does Desharnais' testimony or the documentary evidence establish her "complete control of the circumstances." Desharnais had only a 3.5-hour window to review the due diligence results, and was traveling from Minneapolis to New York and from Laguardia to her home during that time. Her own contemporaneous email record reflects that she did not actually read the results for the first time until October 3, six days after closing. Desharnais' "practice" testimony thus lacks any foundation under the circumstances of this case, and is inadmissible. *See Ferrer v. Harris*, 55 N.Y.2d 285, 294 (1982) (holding evidence inadmissible where plaintiff made no showing of "a persistent habit or regular usage by one in control of the circumstances in

which it is employed"); *Gushlaw v. Roll*, 290 A.D.2d 667, 670 (3d Dep't 2002); *Glusaskas v. John E. Hutchinson, III, M.D., P.C.*, 148 A.D.2d 203, 206 (1st Dep't 1989); *see also Barrer v. Chase Bank, USA, N.A.*, No. 3:06-cv-00415-HA, 2013 WL 665088, at *9 (D. Or. Feb. 21, 2013).

Because MBIA cannot present evidence to raise a triable issue of fact with respect to the threshold element of actual reliance, the Court does not need to go any further in granting summary judgment in favor of JPMS and dismissing MBIA's Complaint. However, as discussed below, the record also establishes that there are no triable issues of fact as to justifiable reliance and materiality.

II. JPMS IS ENTITLED TO SUMMARY JUDGMENT BECAUSE MBIA CANNOT PRESENT ANY EVIDENCE OF JUSTIFIABLE RELIANCE

Summary judgment is equally appropriate where the facts clearly establish a lack of justifiable reliance. *See, e.g., Global Mins. & Metals Corp. v. Holme*, 35 A.D.3d 93, 99-100 (1st Dep't 2006) (affirming summary judgment where facts were "abundantly clear" that plaintiff's alleged reliance was unreasonable); *Tech. Support Servs., Inc.*, 2007 WL 4500382, at *27; *Race v. Goldstar Jewellery, LLC*, No. 2467/09, Decision & Order on Motion Sequence #002, at 16 (N.Y. Sup. Ct. Westchester Cnty. Aug. 17, 2010) (J. Scheinkman). Here, even if MBIA could present sufficient evidence of actual reliance (it cannot), MBIA cannot establish that it justifiably relied on the due diligence report in agreeing to insure the transaction.

A. There Is No Triable Issue of Fact on Justifiable Reliance

Both on October 3, when she sent the due diligence results to Murray, and at her deposition, Desharnais had no difficulty as a "very experienced" underwriter identifying that the results lacked "the usual type of reporting," and, in particular, the loan grades she looked for and which mattered "very much" to her. Yet on the day of closing, Desharnais elected not to seek additional information and chose to proceed with the closing. *See* Factual Background §§ D.2-

D.3, *supra*. That can only mean either that Desharnais did not review the due diligence results, in which case MBIA cannot show actual reliance, *see* Section I.A, *supra*, or that Desharnais reviewed the due diligence results, noted the absence of ordinary reporting and loan grades, and decided to close the transaction anyway, in which case MBIA cannot show justifiable reliance.

New York takes a "contextual view" of justifiable reliance, focusing on "the level of sophistication of the parties, the relationship between them, and the information available at the time of the operative decision." *J.P. Morgan Chase Bank v. Winnick*, 350 F. Supp.2d 393, 406 (S.D.N.Y. 2004). In cases involving a sophisticated party, "[i]f the facts represented are not matters peculiarly within the party's knowledge, and the other party has the means available to him of knowing, by the exercise of ordinary intelligence, the truth or the real quality of the subject of the representation, he must make use of those means, or he will not be heard to complain that he was induced to enter into the transaction by misrepresentations." *DDJ Mgmt., LLC v. Rhone Group L.L.C.*, 15 N.Y.3d 147, 154 (2010) (internal citations omitted); *Big Apple Consulting USA, Inc. v. Belmont Partners, LLC*, No. 23105/07, 2008 WL 4210533, at *3 (N.Y. Sup. Ct. Nassau Cnty. Sept. 15, 2008) (a party cannot establish justifiable reliance where it could have discovered the true nature of the transaction "by ordinary intelligence or with reasonable investigation."); *see also Abbey v. 3F Therapeutics, Inc.*, No. 06 CV 409 (KMW), 2011 WL 651416, at *7-13 (S.D.N.Y. Feb. 22, 2011).

This "duty to investigate" extends to cases in which the plaintiff claims that the defendant has made a "selective disclosure and partial withholding of information relevant to assessing the risks of the subject transactions." *Societe Nationale D'Exploitation Industrielle Des Tabacs Et Allumettes v. Salomon Bros. Int'l*, 268 A.D.2d 373, 374-75 (1st Dep't 2000). Likewise, where a plaintiff voluntarily decides to proceed with a transaction despite knowing that it has not

received full or complete information, its alleged reliance "cannot be considered reasonable or justifiable." *KNK Enters.*, 33 A.D.3d at 872; *see also Centro Empresarial Cempresa S.A. v. America Movil, S.A.B. de C.V.*, 17 N.Y.3d 269, 279 (2011).

Here, MBIA acknowledges that it insured many similar transactions with GMAC Mortgage prior to the 2006-HE4 Securitization, including one in 2004 that followed the same structure. *See* Factual Background § A, *supra*. MBIA also acknowledges that it was "very experienced" in reviewing due diligence results. *Id.* § D.3. All of MBIA's witnesses admit that they did not have to close the deal if they did not get all the information they wanted or were not satisfied with the due diligence. *See id*. Yet MBIA closed anyway. As Murray explained, it was MBIA's competitive business culture that created the pressure to close deals quickly and to commit at the bidding stage. *Id*. § A. In short, MBIA chose to proceed for business reasons; there is no evidence it was deceived or coerced into doing so.

The record shows that Desharnais either did not undertake a reasonable review and investigation of the due diligence results when they were made available to her, or she noted the omissions and elected to proceed anyway. In either event, MBIA's reliance was not justifiable. "Where sophisticated businessmen engaged in major transactions enjoy access to critical information but fail to take advantage of that access, New York courts are particularly disinclined to entertain claims of justifiable reliance." *Grumman Allied Indus., Inc. v. Rohr Indus., Inc.*, 748 F.2d 729, 737 (2d Cir. 1984); *see also ACA Galleries, Inc. v. Kinney*, 928 F. Supp.2d 699, 703 (S.D.N.Y. 2013).

Indeed, a similar fraud claim previously asserted by MBIA against a different RMBS sponsor failed where MBIA had "hints of falsity" yet "fail[ed] to investigate or insert protective language in the contract" as required by its "heightened" duty of inquiry. *MBIA Ins. Corp. v.*

Credit Suisse Secs. (USA) LLC, 927 N.Y.S.2d 517, 533 (N.Y. Sup. Ct. N.Y. Cnty. 2011). *See also ACA Fin. Guaranty Corp. v. Goldman Sachs & Co.*, 967 N.Y.S.2d 1, 3 (1st Dep't 2013) (dismissing fraud claim against investment bank based on alleged misleading statements regarding nonparty hedge fund's intention to invest, where plaintiff "could have, upon further inquiry, uncovered the nonparty hedge fund's actual position, but apparently chose not to"). Here too, MBIA's purported reliance was neither reasonable nor justifiable on this record.

B. The Judicial Admissions in the GMAC Mortgage Complaint Further Confirm the Absence of a Triable Issue of Fact on Justifiable Reliance

Not only are MBIA's allegations of reliance upon the due diligence results from Bear Stearns completely at odds with the proof in this case, they also directly contradict MBIA's allegations in the GMAC Mortgage Complaint. This further supports summary judgment in favor of JPMS. Where a plaintiff presents a new fraud claim alleging justifiable reliance on grounds that "flatly contradict" the plaintiff's own allegations in an earlier action, the new claim cannot survive. *See Morgenthow & Latham v. Bank of New York Co., Inc.*, 305 A.D.2d 74, 75-77 (1st Dep't 2003). The allegations of the GMAC Mortgage Complaint are "informal judicial admissions" by MBIA. *Id*. at 78-79. They make no mention of Bear Stearns, the due diligence report, or any reliance by MBIA upon either in issuing its policy. To the contrary, the GMAC Mortgage Complaint identifies four specific sources upon which MBIA allegedly relied in issuing the policy, all of which came from GMAC Mortgage: loan tapes and data, loan schedules and statistics, representations and warranties, and "shadow ratings." MBIA purportedly relied on these sources based on its relationship with GMAC Mortgage and its reliance upon GMAC Mortgage's "unique and special knowledge for many years." *See* Factual Background § B, *supra*.

MBIA now seeks to replace all of its earlier allegations with a wholesale new theory that it relied instead upon the MDMC due diligence report allegedly altered by Bear Stearns. MBIA's

failure to include any allegations of justifiable reliance upon Bear Stearns and the due diligence results in the GMAC Mortgage Complaint is "irreconcilable" with its belated allegations in this case, and "negate[s] any claim of justifiable reliance" on Bear Stearns' alleged misrepresentations and omissions. *Morgenthow*, 305 A.D.2d at 76-77. This "manifest" inconsistency requires judgment against MBIA on its fraud claim. *Id*. at 78-82. It would be "unseemly, to say the least," to permit MBIA to "renege" on its prior allegations in order to present different theories of reliance in separate actions to pursue incompatible claims of fraud against different defendants for the same alleged injuries. *Matter of Liquidation of Union Indem. Ins. Co.*, 89 N.Y.2d 94, 103 (1996). MBIA cannot now change its theory of justifiable reliance simply because it wishes to pursue a new target after GMAC Mortgage's bankruptcy.

III. MBIA'S FRAUD CLAIM SHOULD BE DISMISSED BECAUSE MBIA CANNOT PRESENT ANY EVIDENCE OF MATERIALITY

Apart from issues of reliance, MBIA also cannot raise a triable issue of fact with respect to materiality. There is simply no evidence that the due diligence results formed any part of MBIA's decision to bid on, enter into, close, and issue a financial guaranty policy for the 2006-HE4 Securitization. To the contrary, the record shows that the due diligence results did not matter to MBIA. A misrepresentation or omission is "material" to the extent that a party "would have acted differently had it been presented with accurate information." *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, No. 602825/08, 2013 WL 1845588, at *5 (N.Y. Sup. Ct. N.Y. Cnty. Apr. 29, 2013) (*citing Geer v. Union Mut. Life Ins. Co.*, 273 N.Y. 261, 270 (1937)); *Horton v. Prudential Ins. Co. of Am.*, 46 A.D.2d 456, 458 (3d Dep't 1975).

The facts of this case are clear that the due diligence results transmitted to MBIA by Bear Stearns were not material to MBIA's decision to issue a financial guaranty policy for the 2006-HE4 Securitization, and that it would not have acted differently if Bear Stearns had provided

other versions of the MDMC spreadsheets. MBIA made the transaction a "top priority" despite the "very tight" time frame and "tight" resources, and lowered its premium to improve the competitiveness of its bid, not because of Bear Stearns' involvement as lead underwriter, but because it viewed GMAC Mortgage as a "very good originator" and "very strong counterparty." *See* Factual Background § A, *supra*. Murray testified that, due to the "enormous amount of pressure" and "competitive business environment among the monoline insurers" at the time, MBIA was "effectively committing at the business stage," and never backed out of a transaction after approving it at the bidding stage, well before receiving the due diligence results. *See id*.

Consistent with this pattern, following MBIA's successful bid, the Underwriting Committee conditionally approved issuance of (and Murray released in MBIA's system) a policy for the 2006-HE4 Securitization two days before closing, without having seen the due diligence results and without requiring a follow-up vote upon receipt of those results. *See* Factual Background § D.1, *supra*. The Underwriting Committee Memorandum did not include due diligence as one of MBIA's "major analytical points" supporting the transaction, and did not identify Bear Stearns as a "key player." *Id*. The Bid Letter itself stated that materially different due diligence results would only affect "our overcollateralization target and fee," not the decision to issue a policy. *Id*. MBIA's allegations are "inherently or flatly contradicted," by the Bid Letter, whose terms render it "impossible to conclude" that MBIA issued its policy based upon Bear Stearns' due diligence. *Perrotti v. Becker, Glyn, Melamed & Muffly LLP*, 82 A.D.3d 495, 498 (1st Dep't 2011); *MBIA v. Credit Suisse*, 927 N.Y.S.2d at 530 (*quoting Stuart Lipsky, P.C. v. Price,* 215 A.D.2d 102 (1st Dep't 1995)). Such a theory is "incredible and strains to the breaking point the credulity of this court." *New York State Urban Dev. Corp. v. Marcus Garvey Brownstone Houses, Inc.*, 98 A.D.2d 767, 770 (2d Dep't 1983) (citation omitted).

Moreover, as discussed above, when Bear Stearns sent the due diligence results to MBIA on the day of closing, Webb and Murray did not so much as glance at them. *See* Factual Background § D.2, *supra*. Murray did not even receive the results until six days after closing, a fact made all the more important because it was Murray who was responsible for signing off on the due diligence, not Desharnais. *Id*. Desharnais also did not look at the results until six days after closing, and in all events did not raise any concerns at the time or afterwards regarding omitted loan grades, compliance, and underwriting information that she had no difficulty identifying when she reviewed the results on October 3 and at her deposition. *See id*. §§ D.2-D.3. These facts preclude any triable issue on the element of materiality, as MBIA has not offered and cannot offer any evidence that it would have acted differently had Bear Stearns disclosed MDMC's due diligence spreadsheets in their entirety. Bear Stearns' alleged misrepresentation of facts that MBIA ***did not consider*** in deciding to issue a financial guaranty policy for the 2006-HE4 Securitization fails the test of materiality. *See MBIA v. Credit Suisse*, 927 N.Y.S.2d at 533 (dismissing MBIA's fraud claim based on alleged pre-contractual misrepresentation of "rigorous due diligence" and "'strict' underwriting" for lack of materiality, because defendant's alleged due diligence conduct and rejection of loans not insured by MBIA "were not material to the Transaction"); *Gabberty v. Pisarz*, 810 N.Y.S.2d 799, 807 (N.Y. Sup. Ct. Nassau Cnty. 2005) (dismissing claims in part because alleged misrepresentations took place "after closing already had occurred," and "therefore were not material" to fraud in the inducement claim).

CONCLUSION

For the foregoing reasons, the Court should grant summary judgment in favor of JPMS and against MBIA, and dismiss MBIA's Complaint in its entirety with prejudice.

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Respectfully submitted,

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