MBIA Insurance Corp. v. Countrywide Home Loans, Inc., et al. Index No. 602825/08

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

MBIA INSURANCE CORPORATION,

Plaintiff,

-against-

COUNTRYWIDE HOME LOANS, INC., COUNTRYWIDE SECURITIES CORP., COUNTRYWIDE FINANCIAL CORP., COUNTRYWIDE HOME LOANS SERVICING, L.P., and BANK OF AMERICA CORP.,

Defendants.

Index No.: 08/602825
IAS Part: 3 (Bransten, J.)

PLAINTIFF'S MEMORANDUM OF LAW IN OPPOSITION TO COUNTRYWIDE'S MOTION FOR SUMMARY JUDGMENT

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Plaintiff MBIA Insurance Corporation ("MBIA" or "Plaintiff") respectfully submits this memorandum of law in opposition to Countrywide's[1] Motion for Summary Judgment.

PRELIMINARY STATEMENT

In the face of overwhelming evidence of its material misrepresentations to MBIA, Countrywide argues, incredibly, that actually it is MBIA that is at fault. But Countrywide's motion is based entirely on misleading snippets of evidence and incorrect assertions of law.[2] The motion should be denied for the reasons set forth in the Argument and summarized here:

First, Countrywide is not entitled to summary judgment on MBIA's fraudulent inducement claim. Countrywide's argument rests on the notion that MBIA supposedly failed to undertake adequate due diligence. The argument is flawed at the outset because Countrywide ignores New York Insurance Law § 3105, which provides that an insurer may obtain rescission or equivalent relief based simply on a showing that the applicant's misrepresentation was material in inducing the insurer to issue the policy. The twin premises of this provision are that an applicant has a duty to make truthful disclosures, and an insurer is entitled to rely upon the representations made (without further due diligence). Even beyond the insurance context, New York common-law authorities hold that a plaintiff often need not engage in any due diligence if he has obtained a representation from the defendant on the very fact due diligence would investigate. As explained in MBIA's affirmative motion for summary judgment, MBIA has established beyond dispute that Countrywide made material misrepresentations in applying for

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[1] "Countrywide" refers to Countrywide Financial Corporation ("CFC"), Countrywide Securities Corporation ("CSC"), Countrywide Home Loans, Inc. ("CHL"), and Countrywide Home Loans Servicing, L.P. ("CHLS"). "Sheth Aff. Ex. __" refers to exhibits to the Affirmation of Manisha M. Sheth in Opposition to Countrywide's Motion for Summary Judgment, dated October 19, 2012. "Holland Aff. Ex. __" refers to exhibits to the Affirmation of Mark Holland in Support of Countrywide's Motion for Summary Judgment, dated September 19, 2012. "CUF" refers to MBIA's Rule 19-a Counterstatement, dated October 19, 2012, In Response To Countrywide's Statement Of Undisputed Facts.

[2] For example, Countrywide leads off its memorandum ("CW Mem.") with a February 2008 quote from MBIA's CFO that sounds superficially supportive of Countrywide's attempt to shift blame from itself to MBIA: "I am afraid we have no one to blame but ourselves." CW Mem. 1. But the impact of this quote immediately falls apart upon examination—the statement was made months before Countrywide gave MBIA the loan files showing that Countrywide had pervasively breached the representations and warranties regarding the loans. *See* Sheth Aff. Ex. 313; CUF ¶ 114.

insurance, and therefore summary judgment on the fraudulent inducement claim, if it is to be granted to either party, should be granted to MBIA. *See* Point I.A, *infra*.

Even if MBIA were required to show due diligence beyond procuring express representations and warranties, it has adduced sufficient evidence not only to withstand summary judgment but to secure summary judgment in its favor on this issue. MBIA went far beyond passive reliance on those representations and warranties: MBIA engaged in industry-standard due diligence by, *inter alia*, evaluating Countrywide to verify its (then-)sterling reputation and running the proposed deals through a series of internal evaluations. Countrywide's warnings of *future* macroeconomic risks did nothing to put MBIA on notice that Countrywide's representations of *present fact* as to specific loans were false, and Countrywide's disclosure of expanded underwriting guidelines did nothing to put MBIA on notice that Countrywide was blatantly violating its new guidelines. Countrywide seeks to poke holes in MBIA's due diligence process, but its assertions are factually insupportable; at most, they raise disputes of fact that preclude summary judgment. *See* Point I.B, *infra*.

Second, Countrywide is not entitled to summary judgment on any aspect of MBIA's claim for breach of the Insurance Agreements. Countrywide begins by arguing that "sole remedy" provisions in the Transaction Documents restrict MBIA to a loan-by-loan repurchase remedy and prevent it from seeking rescissory damages. At the outset, the argument, which Countrywide never mentioned in briefing or oral argument on MBIA's motion for partial summary judgment, is foreclosed by this Court's January 3, 2012 Order on that motion, which held that MBIA could seek rescissory damages. In any event, Countrywide's argument is incorrect because its linchpin, § 2.01(l), limits remedies only as to breach of a specific paragraph of the Insurance Agreements, yet MBIA seeks remedies for breaches of numerous other paragraphs, such as § 2.01(j), that contain no such limitation and that cannot bar MBIA. A federal court rejected this argument in the context of nearly identical provisions, and reasoned further that the loan-by-loan repurchase remedy is impractical in the context of pervasive breaches affecting a majority of loans in the pool. *See* Point II.A, *infra*.

Turning to MBIA's claim for breach of Countrywide's repurchase obligation, Countrywide argues that MBIA may not establish this breach on a pool-wide basis. Again, Countrywide is wrong. Numerous authorities (including this Court's December 22, 2010 Order on sampling) permit MBIA to use sampling to prove its claims for fraud and breach of contract. Additionally, under the Transaction Documents, CHL must repurchase defective loans within 90 days of "becoming aware of" or "discovery" of such loans, with no requirement that CHL await a particularized loan-by-loan demand from MBIA. And there is substantial evidence that Countrywide has known, since at least 2008, that well over a majority of the loans in the pools was defective. Finally, Countrywide should not be heard to insist on a loan-by-loan showing when it has repeatedly frustrated MBIA's prior repurchase requests. *See* Point II.B, *infra*.

Third, Countrywide is not entitled to summary judgment on MBIA's claim for indemnification to the extent the claim is based on Section 3.03 of the Insurance Agreements, which expressly entitles MBIA to recover from Countrywide "reasonable attorneys' and accountants' fees and expenses, in connection with . . . the enforcement by the Insurer of any rights in respect of any of the Transaction Documents, including without limitation, instituting...or participating in any litigation proceeding relating to any of the Transaction Documents." Holland Aff. Exs. 57-71 § 3.03(c). *See* Point III, *infra*.

Fourth, Countrywide is not entitled to summary judgment on MBIA's claim for breach of Countrywide's servicing obligations. Contrary to Countrywide's assertion, MBIA's expert, Mr. Butler, did not render conclusory opinions, but rather reviewed the payment histories and collection notes for hundreds of mortgage loans in finding that Countrywide failed properly to service *over 45%* of the loans in a random sample. In any event Countrywide's argument goes at most to the weight, not the admissibility, of Mr. Butler's testimony. *See* Point IV, *infra*.

Fifth, Countrywide is not entitled to summary judgment on MBIA's prayer for punitive damages. Countrywide's attempt to portray this action as simply a private matter between two companies is belied by the culture of fraud at Countrywide that extended from the reckless origination of ineligible mortgage loans to the off-loading of risks to innocent insurers, investors,

and other third parties based on blatantly false descriptions of the loans. This conduct broadly harmed the public, contributing to the collapse of the housing market and drawing the attention of the SEC and other regulators. On this record of egregious conduct and public harm, the jury should be allowed to determine whether punitive damages are warranted. *See* Point V, *infra.*

SUMMARY COUNTERSTATEMENT OF FACTS[3]

Countrywide's "Statement of Undisputed Facts" ignores and mischaracterizes the factual record, particularly in asserting that MBIA failed justifiably to rely on Countrywide's representations and warranties because MBIA supposedly did not conduct reasonable due diligence. New York law takes seriously representations and warranties made by an applicant to induce an insurer to provide insurance, recognizing that a material misrepresentation by itself supports rescinding the policy or awarding equivalent relief to the insurer. N.Y. Ins. Law §§ 3105(b)(1), 3106(b). Even outside the insurance context, general New York common law, *see, e.g.*, *DDJ Mgmt. LLC v. Rhone Group LLC,* 15 N.Y.3d 147, 153-54 (2010), holds that, "where a plaintiff has gone to the trouble to insist on a written representation that certain facts are true, it will often be justified in accepting that representation rather than making its own inquiry." Finally, even if some additional due diligence were required, the record evidence here demonstrates that MBIA conducted it. At best for Countrywide, there is a factual dispute on justifiable reliance, which renders summary judgment improper.

In this section, MBIA begins with a brief summary of the fraudulent culture at Countrywide and how it injured MBIA. MBIA next summarizes the key facts showing it justifiably relied on Countrywide's representations and warranties. MBIA then responds to Countrywide's misleading snippets of evidence on reliance. MBIA finally summarizes the facts concerning Countrywide's disregard of its repurchase obligations.[4]

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[3] For a fuller factual discussion, MBIA respectfully refers the Court to MBIA's affirmative motion for summary judgment on primary liability ("MBIA SJ Mem.") (filed on September 19, 2012), MBIA's Rule 19-a statement in support of that motion (also filed on September 19), and MBIA's Rule 19-a counterstatement ("CUF") (filed with this memorandum on October 19, 2012) in opposition to Countrywide's motion for summary judgment on primary liability.

[4] MBIA defers to the Argument, *infra*, a discussion of other facts bearing on Countrywide's arguments.

A. Countrywide's "Systemic Fraudulent Activity"

In October 2010, three key Countrywide executives, Angelo Mozilo (Chairman and CEO), David Sambol (COO), and Eric Sieracki (CFO), agreed to pay substantial fines to settle an SEC lawsuit that charged them with knowingly making fraudulent disclosures relating to Countrywide's adherence to underwriting guidelines from 2005 to 2007.[5] This fraud permeated Countrywide and even included efforts to silence the few conscientious Countrywide employees who tried to stop it. For example, after Eileen Foster, who was responsible for oversight of internal and external mortgage fraud investigations, investigated and found "systemic fraudulent activity" at Countrywide, Sheth Aff. Ex. 3, at 164:19-23, she was first asked to downplay the incidents of fraud, *id.* at 115:13-18, 117:19-120:25, and later was fired when she refused to do so. *Id.* at 68:7-69:1; CUF ¶¶ 357, 359-61. As the Department of Labor found, the firing constituted unlawful retaliation against a whistleblower and thus violated the Sarbanes-Oxley Act. Sheth Aff. Ex. 95, at 7-8 (ordering Countrywide to pay Ms. Foster back pay and compensatory damages); CUF ¶¶ 361-63. Other Countrywide employees suffered similar treatment. *See, e.g.*, Sheth Aff. Ex. 5, at 63:11-67:7, 103:14-104:3; CUF ¶¶ 364-65.

This action arises out of an episode of Countrywide's scheme that inflicted substantial injury on MBIA. To induce MBIA to provide insurance for the 15 Securitizations and thus make them more marketable to investors, Countrywide repeatedly misrepresented to MBIA the characteristics and quality of the mortgage loans in the 15 Securitizations. According to MBIA's expert, based on a re-underwriting review of 6,000 randomly selected loans, ***about 96.8% of the loans in the Securitizations, contrary to Countrywide's representations and warranties, contain significant defects***. *See* Sheth Aff. Ex. 80, at 58; Ex. 85, at 37 (97% when sample is extrapolated to the entire population); CUF ¶ 356.

MBIA's expert also re-underwrote the approximately 3,000 loans that had been reviewed by third-party loan file due diligence firms and found numerous misrepresentations, including:

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[5] Sheth Aff. Ex. 180; *id.* Ex. 181; CUF ¶ 366.

- Numerous loans with DTIs and CLTVs well in excess of Countrywide's underwriting guidelines remained in the Securitizations with no defect noted on the third-party reports. Sheth Aff. Ex. 84, at 28-32; CUF ¶ 306.

- Numerous loans with red flags for occupancy or other types of fraud remained in the Securitizations with no defect noted on the third-party reports. Sheth Aff. Ex. 84, at 34-37; CUF ¶ 307.

- Numerous loans with patently unreasonable stated income remained in the Securitizations, with no defect noted on the third-party reports. Sheth Aff. Ex. 84, at 40-43; CUF ¶ 308.

- Numerous loans with unsupported appraised values remained in the Securitizations, with no defect noted on the third-party reports. Sheth Aff. Ex. 84, at 45-50; CUF ¶ 309.

- In many instances, the third-party firms' initial reports noted defects, but those notations were inexplicably deleted before the final reports were given to MBIA.[6]

Thus, Countrywide provided MBIA with loan tapes and third-party reports that largely underestimated the number and severity of the deficiencies in the loans.

B. MBIA's Reasonable Due Diligence

Before discussing MBIA's due diligence and why it was reasonable, it is necessary first to describe Countrywide's affirmative series of detailed loan-level representations and warranties to MBIA, representations and warranties on which Countrywide specifically marketed these deals to Countrywide. These representations and warranties are dispositive because, in the insurance context, an insurer need establish only the applicant's material misrepresentations (and not any justifiable reliance) to obtain rescission or equivalent relief. Similarly, beyond the insurance context, New York common-law authorities recognize that a party who has received a representation from its counterparty often may justifiably rely on it without undertaking further due diligence. For Countrywide now to say that MBIA could place no reliance on the

[6] *See, e.g.*, Sheth Aff. Ex. 84, at 24-27; *compare id.* Ex. 143, at CWMBIA0012994234, *with id.* Ex. 144, at CWMBIA0012994801 (Loan No. [redacted] initially found to be missing hazard insurance, title work, and pre-closing employment verification; results Countrywide provided to MBIA indicate no defects for that loan; Loan No. [redacted] initially found to be missing verbal verification of employment; results Countrywide provided to MBIA indicate no defects for that loan); *compare id.* Ex. 153, at CWMBIA0013196447, *with id.* Ex. 154, at CWMBIA0013207444 (Loan No. [redacted] initially found to have excessive DTI of 60% rather than 21.11%, and missing hazard insurance, title work, income documentation, first lien note, and appraisal; results Countrywide provided to MBIA indicate no defects for that loan); CUF ¶ 310.

representations and warranties is flatly inconsistent both with case law and industry practice. And even if MBIA had been required to perform additional reasonable due diligence, it plainly did so, and at least there is a dispute of fact on the matter.

1. Countrywide's Representations And Warranties

To induce MBIA to provide financial guaranty insurance on the Securitizations, Countrywide made a series of comprehensive representations and warranties relating to the loan pools and individual mortgage loans contained in each of the trusts. *See* MBIA SJ Mem. 6; Holland Aff. Exs. 31-39, § 3.02; *id.* Exs. 40-48, § 2.04; *id.* Exs. 49-54, § 2.03; *id.* Exs. 57-71, § 2.01(l) (incorporating these representations into the Insurance Agreement for MBIA's benefit). The representations and warranties included, for example, that the Mortgage Loan Schedule (also known as the closing loan tape) that reported key data on the individual loans (such as the combined loan-to-value and FICO score) was true and accurate. *See, e.g.*, *id.* Ex. 33, § 3.02(a)(4) ("the Mortgage Loan Schedule is correct in all material respects"); *see also id.* Exs. 31-32, § 3.02(iv) (same); *id.* Exs. 34-39 § 3.04(a)(4) (same); *see id.* Ex. 49-54, § 2.03(b)(7) (similar).

These representations and warranties were absolutely central to these deals. MBIA, through strategic business planning evaluations for the residential mortgage market in 2002 and 2004, had decided to focus its participation in the RMBS sector on top-tier, financially strong issuers with the highest quality collateral, such as Countrywide. Sheth Aff. Ex. 9, at 39:15-40:3; *id.* Exs. 316, 317; *id.* Ex. 10, at 43:7-44:10; *id.* Ex. 15, at 331:3-332:12; CUF ¶¶ 178-85. Countrywide then not only made the representations and warranties for the 15 Securitizations at issue, but affirmatively emphasized them in the offering documents. *See, e.g.*, *id.* Holland Aff. Ex. 6, at S-48 (discussing representations and warranties in the Transaction Documents and repurchase remedy).[7]

[7] Countrywide made similar statements about the high quality of loan production to the investing public. *See, e.g.*, Sheth Aff. Ex. 329, at 11 (A. Mozilo: "There will be no compromise by this company in the over all [sic] quality of the product line."); *id.* Ex. 333, at 19 (A. Mozilo: Countrywide had not "taken any steps to reduce the quality of its underwriting regimen."); CUF ¶¶ 234-46.

Such representations by an insurance applicant are hardly unusual, but when they are materially false, they have consequences. Specifically, Section 3105 of the New York Insurance Law, which informed this Court's partial summary-judgment order dated January 3, 2012, provides that a material misrepresentation by an applicant for insurance avoids the policy. *See* N.Y. Ins. Law § 3105(a)-(b)(1) ("A representation is a statement as to past or present fact, made to the insurer by . . . the applicant for insurance . . . at or before the making of the insurance contract as an inducement to the making thereof. . . . No misrepresentation shall avoid any contract of insurance or defeat recovery thereunder unless such misrepresentation was material."); *see also id.* § 3106(b) (similar for breach of warranty claim). These insurance-law provisions are notable for their focus on the element of materiality at the time the policy was issued, with no suggestion that the insurer need show a causal connection between the misrepresentation and post-closing events, *see MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 34 Misc. 3d 895, 908 (N.Y. Sup. Ct. 2012) (so holding), *and* no mention that the insurer need show that it justifiably relied on the applicant's representations. Even outside the insurance-law context, general common-law authorities hold that a party who procures a representation from his counterparty often may justifiably rely on that representation without performing further due diligence. *See, e.g.*, *DDJ*, 15 N.Y.3d at 153-54 ("where a plaintiff has gone to the trouble to insist on a written representation that certain facts are true, it will often be justified in accepting that representation rather than making its own inquiry").

2. MBIA's Further Due Diligence During The Pre-Closing Period

While MBIA thus would have been entitled simply to rely on Countrywide's representations and warranties without further investigation, MBIA went much further. Consider first the pre-closing period, during which MBIA made numerous reasonable due diligence efforts, all of which were in accord with standard industry practice. *See* Sheth Aff. Ex. 87, at 1-2 (MBIA expert opining, *inter alia*, that "MBIA took reasonable and appropriate steps in conducting the internal review that led to its decision to provide financial guaranty insurance for the Countrywide Securitizations," and that "MBIA's internal review and approval procedures for

the...Securitizations were also consistent with industry custom and practice for a Triple-A rated financial guaranty insurer"); CUF ¶¶ 188-226.

Specifically, MBIA undertook a multi-level internal review of the Securitizations before deciding to issue the insurance policies. MBIA's New Business group received Countrywide's loan tape and anticipated structure and shadow rating of the transaction. *Id.* Ex. 87, at 51-55; *id.* Ex. 26, at 107:9-19; *id.* Ex. 15, at 331:12-333:7, 83:12-84:11; CUF ¶¶ 190-91. As a matter of policy, MBIA pursued only those transactions that received an investment-grade shadow rating and met MBIA's no-loss underwriting rule.[8] The Underwriting Group conducted an assessment of the potential risk of having to pay claims on any transaction MBIA was considering insuring. Sheth Aff. Ex. 87, at 55-60; *id.* Ex. 19, at 27:22-28:2, 143:4-22, 157:19-159:13, 166:4-173:15; *id.* Ex. 20, at 577:3-578:2, 596:3-597:9; *id.* Ex. 28, at 126:15-128:21; *id.* Ex. 33, at 107:11-24; *id.* Ex. 22, at 337:4-13; *id.* Ex. 224; CUF ¶ 201. The Quantitative Group, based on a review of the loan tapes, stratified the loan pool based on specific parameters, so that the Underwriting Group could compare those stratifications to previous Countrywide pools to assess any material differences in the pools, and how those might impact performance projections. Sheth Aff. Ex. 87, at 60-63; *id.* Ex. 19, at 137:2-141:10; CUF ¶¶ 203, 208-09. The Corporate Analytics Group focused on the financial stability and creditworthiness of the issuer of the securities. Sheth Aff. Ex. 87, at 63-65; *id.* Ex. 41, at 32:13-39:15, 41:23-45:8, 50:15-57:20; *id.* Ex. 42, at 141:3-24; CUF ¶ 211. The Servicer Review Team conducted periodic on-site servicer reviews to ensure that Countrywide acted in conformity with industry practices. Sheth Aff. Ex. 87, at 65-68; *id.* Ex. 43, at 48:8-20; *id.* Ex. 303; CUF ¶ 213. And the Insured Portfolio Management Group monitored, *inter alia*, the pool balance, delinquency rates, and transaction performance

[8] *See* Sheth Aff. Ex. 15, at 83:12-84:11; *id.* Ex. 44, at MBIA00176660; *id.* Ex. 87, at 9-15, 54-55; *id.* Ex. 23, at 612:21-613:2; *id.* Ex. 42, at 93:3-94:3, 102; *id.* Ex. 39, at 18:9-16, 36:10-21; *id.* Ex. 40, at 71:20-72:6. Additionally, MBIA assured itself that each of the Securitizations had sufficient loss coverage that MBIA would not have to pay claims until the actual losses exceeded MBIA's "base case" expected loss by four to seven times. *See id.* Ex. 87, at 60-63; *id.* Ex. 165, at MBIA00599809 ("In the event of an economic downturn, this transaction has been structured to withstand 4-5 times expected losses providing ample cushion for deterioration in performance. Further, prime collateral is expected to experience less deterioration in a downturn than subprime collateral due to the nature of the borrower profile."); *see also id.* Exs. 164, 166-175 (similar); CUF ¶¶ 194-99,186, 208-210.

associated with Countrywide securitizations that were part of MBIA's existing portfolio. Sheth Aff. Ex. 87, at 68-70; *id.* Ex. 175, at MBIA00602837-38; *id.* Ex. 39, at 294:7-21; *id.* Ex. 42, at 216:11-21; CUF ¶¶ 215-16.

As part of the above-described internal review, MBIA also considered reports from third-party due-diligence firms retained by CSC to review the loan files.[9] During the relevant period, it was standard practice in the industry for financial guaranty insurers to consider the reviews conducted by third-party due diligence firms commissioned by the issuer, especially one as highly regarded as Countrywide was at the time. *See, e.g.*, Sheth Aff. Ex. 14, at 88:24-89:12 (securitization "industry had gravitated to the point of allowing certain issuers to perform [the due diligence] function," because "it was cost efficient" and "the industry had matured."); *id.* Ex. 15, at 55:10-15 ("By the time MBIA was in the HELOC market, [retention of third party due diligence firm] was done by the bankers and paid for by the bankers."); CUF ¶¶ 227-31. Countrywide's own witnesses and experts have confirmed this industry practice. Sheth Aff. Ex. 10, at 104:2; *id.* Ex. 21, at 71:24-72:1; *id.* Ex. 94, at C-19; *id.* Ex. 13, at 361:3-13. CUF ¶¶ 227-

[9] For some 50% of the Securitizations, MBIA consulted such final reports prior to closing. And for other deals, MBIA consulted initial (if not final) reports prior to closing. Sheth Aff. Ex. 19, 171:6-173:5 (testifying that there were times when deals closed prior to the final due diligence results being received by MBIA, but MBIA would have reviewed at least the preliminary results to ensure there were no adverse trends with which to be concerned); at 271:5-276:20 (testifying that MBIA would look at the initial results for things like systematic issues, so if there was some issue that came up repeatedly MBIA would try to understand what was the problem and how it was resolved); CUF ¶¶ 204, 286, 290, 295-96. In addition to reviewing preliminary due-diligence reports, MBIA reviewed the results from prior transactions. Sheth Aff. Ex. 352, at 121:9-21 (where MBIA did not have final third-party due diligence results from Countrywide prior to closing, they may have considered the results on prior deals and received verbal updates); CUF ¶ 290, 296, 298. Further, MBIA was able to gain comfort with the transaction, in particular from counterparties perceived to be as strong as Countrywide, in light of the representations and warranties that they had received as to the collateral. Sheth Aff. Ex. 19, at 64:15-23 ("So had I thought those conditions were material enough to not do the next transaction. . . then I could have personally withheld my approval. I chose not to do that because I felt that the deals were sound when I underwrote each and every transaction and I approved them."), at 90:16-20 ("I don't feel that I ever approved a transaction that I didn't feel comfortable and I would not have done that. I would not have approved a deal that I thought we were not going to do well with."); *id.* Ex. 28, at 118:2-10 ("the representations and warranties . . . [were] one of the factors that provided comfort" to the risk officer); *id.* Ex. 57, at 668:16-24 (Countrywide was a "large financially secure company[y]" that "could honor reps and warranties if necessary"); *id.* Ex. 10, at 48:15-49:11 ("we absolutely relied on the reps and warranties that were offered up to us because we believed if those reps and warranties were violated, we would be able to recover any claims that we made that should not have occurred."). Thus it was not unreasonable for MBIA to consider third-party due diligence results as one piece of their analysis, even where the final results were provided after closing. *Id.* Ex. 88, at 39-41; CUF ¶¶ 255, 287-300.

28, 230-31.[10] The third-party reports generally reflected pools of high quality loans, as Countrywide employees agreed. *See, e.g.*, Sheth Aff. Ex. 314 ("overall quality of the [2004-I] results are good"); *id.* Ex. 315 ("overall quality of the [2004-P] loans underwritten were good."); CUF ¶255, 287-90. To the extent the reports turned up non-compliant loans (which were then excluded from the pools), those non-compliant loans were extremely small in number (about 183 out of about 3000),[11] and did not suggest that Countrywide had engaged in widespread misrepresentations. *See* Sheth Aff. Ex. 15, at 399:12-400:21 (MBIA reviewed due diligence results for trends and systemic issues in Countrywide's underwriting); *id.* Ex. 19, at 271:5-25 (MBIA underwriter testifying that she reviewed initial results for systemic issues), 41:25-42:5 (MBIA underwriter "would not have approved something" had she not thought it "sound and strong"); *id.* Ex. 87, at 151:23-152:14; CUF ¶¶ 224, 255, 291-96. Had the third-party reports deviated significantly from what was expected, MBIA would have taken appropriate action. *See* Sheth Aff. Ex. 19, at 172:4-10 (MBIA was on lookout for "specific red flags" from loan file reviews that could be a concern to MBIA), 33:10-19, 171:6-173:5; CUF ¶ 299.[12]

Indeed, it warrants emphasis that CSC was the Countrywide entity that arranged for and received the third-party reports. CSC, as an underwriter on the each of the 15 Securitizations,

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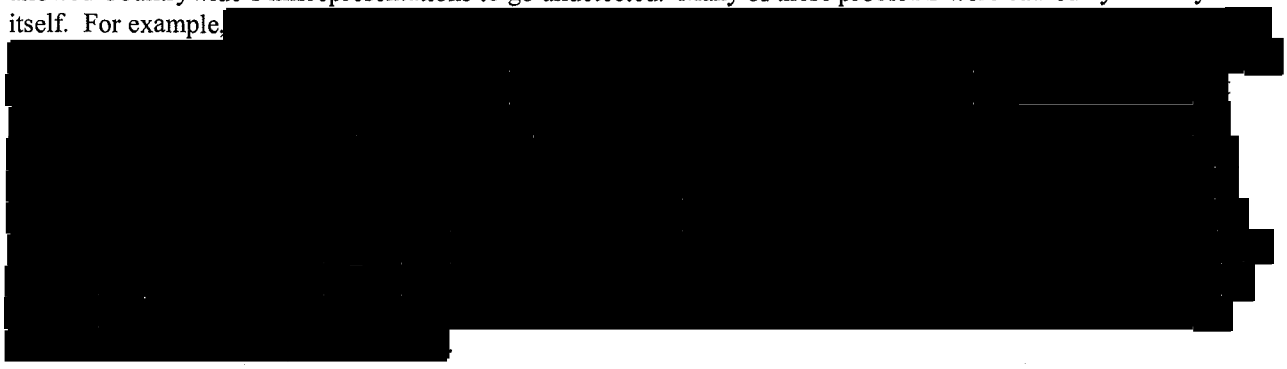
[10] Although MBIA had directly hired due diligence firms until 2002, it no longer needed to do so after 2002, given MBIA's new focus on larger, high quality seller servicers such as Countrywide, and the industry-wide shift discussed above. Sheth Aff. Ex. 23, at 605:8-22; CUF ¶ 232.

[11] Sheth Aff. Ex. 84, at 52; *id.* Ex. 89 (excluding 2005-M kicks); *id.* Exs. 144-152, *id.* Exs. 154-159, *id.* Ex. 161.

[12] Unknown to MBIA prior to closing, there were substantial problems with the third-party due diligence that allowed Countrywide's misrepresentations to go undetected. Many of these problems were caused by Countrywide itself. For example,



see, e.g., Sheth Aff. Ex. 123, at CWMBIA0008744943, CUF ¶¶ 229,[13] was required by the federal securities laws to refrain from making false or misleading statements and to conduct reasonable due diligence toward that goal. *See, e.g.*, *In re WorldCom, Inc. Sec. Litig.*, 346 F. Supp. 2d 628, 662 (S.D.N.Y. 2004) ("Underwriters must exercise a high degree of care in investigation and independent verification of the company's representations. . . . [N]o greater reliance in our self-regulatory system is placed on any single participant in the issuance of securities than upon the underwriter.") (internal cites and quotation marks omitted); *id.* Ex. 79, at 104:8-106:20 (Countrywide expert confirming that RMBS underwriters like CSC perform due diligence of securitization collateral to determine accuracy of what is disclosed in prospectus supplements), 119:15-120:10; CUF ¶¶ 230, 313. CSC, having received all of the third-party reports and not perceived them to require any corrective disclosures, cannot credibly maintain that MBIA's consideration of the reports was deficient in any way.

Finally, at the end of the various Groups' analyses, a consensus-based decision was made by MBIA's Underwriting Committee whether to proceed with the insurance. Sheth Aff. Ex. 19, at 33:10-23; *id.* Ex. 23, at 612:17-613:2; *id.* Ex. 42, at 93:19-94:23, 102:8-11; *id.* Ex. 33, at 336:5-337:3; *id.* Ex. 44, at 52:10-53:25; *id.* Ex. 26, at 302:2-13; CUF ¶¶ 188, 202, 219-20.[14]

3. MBIA's Equally Reasonable Post-Closing Conduct

Again, as an initial matter, MBIA had the assurance of Countrywide's representations and warranties, which at a minimum lowered any due-diligence burden MBIA might otherwise have. But MBIA, having already performed the pre-closing due diligence described above, went further after closing:

First, MBIA monitored the performance of the Securitizations. *See, e.g.*, Sheth Aff. Ex. 175, at MBIA00602837-38; *see id.* Ex. 39, at 294:7-21; *id.* Ex. 42, at 216:11-21; CUF ¶¶ 215-

[13] Sheth Aff. Exs. 124-137.

[14] In reviewing transactions, MBIA's groups had sufficient time and resources to perform their duties, even after personnel was reduced. Sheth Aff. Ex. 19, at 63:25-64:23, 199:10-200:9; *id.* Ex. 41, at 246:20-247:13; *id.* Ex. 33, at 337:4-16; CUF ¶¶ 221-26.

17. But this due diligence did not uncover Countrywide's misrepresentations because the Securitizations were performing as expected until well after the last one had closed. *See* Sheth Aff. Ex. 177, ¶6 (increased delinquencies and defaults in late fall 2007). Other Countrywide transactions in MBIA's portfolio were also performing as expected.[15] The number of sample loans excluded from the pools for the earliest Securitizations was low (*e.g.*, 2004-I, 2004-P, 2005-A, 2005-E, 2005-I),[16] and thus raised no suspicion that there might be substantial misrepresentations as to the loan pools in the later Securitizations.

Second, when MBIA did detect potential problems with loans (well after MBIA had insured the last Countrywide Securitization) and requested the loan files, Countrywide responded by stonewalling. Countrywide often delayed for weeks or longer before responding in piecemeal fashion, and often refused to provide loan files altogether. *See* Sheth Aff. Ex. 311 (unilateral rejections of MBIA's request for loan files associated with paid-in-full loans); *id.* Ex. 312, at CWMBIA0016090933 (Countrywide notification that loan file would not be delivered for 30 days); CUF ¶¶ 267-68.[17]

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[15] *See, e.g.*, Sheth Aff. Ex. 175, at MBIA00724592 (each Countrywide HELOC deal "performing well" after 24-30 months), at MBIA00724593 (showing performance of twenty-seven Countrywide HELOC deals issued before MBIA insured 2004-I); *id.* Ex. 165, at MBIA00599809 (same, at 27-32 months); *id.* Ex. 166, at MBIA00102415 (same, at 33-38 months); *id.* Ex. 167, at MBIA00599898 (same, at 38-43 months); *id.* Ex. 169, at MBIA00108333 (same, at 43-48 months, and noting that 2005 deals were "performing as anticipated"); *id.* Ex. 170, at MBIA00607030 (same, at 46-51 months, and noting that 2005 deals were "performing as anticipated"); *id.* Ex. 171, at MBIA00652502 (each CES pool insured by MBIA "performing well"); *id.* Ex. 172, at MBIA00605054 (same); *id.* Ex. 173, at MBIA00123568 (same); *id.* Ex. 174, at MBIA00116207 (all Countrywide HELOC deals from 2002, 2004, 2005, and 2006 were "performing well").

[16] Sheth Aff. Ex. 144 (only 2 loans excluded from 2004-I), *id.* Ex. 145 (only 4 loans excluded from 2004-P), *id.* Ex 146 (0 loans excluded from 2005-A), *id.* Ex. 147 (only 2 loans excluded from 2005-E), *id.* Ex. 148 (only 3 loans excluded from 2005-I); CUF ¶¶ 255, 287.

[17] Additional prompt post-closing due diligence on several Securitizations would potentially have failed to uncover certain misrepresentations because those Securitizations included a pre-funding provision, whereby a certain amount of funds was expected to be used to purchase additional loans to further populate the pools within approximately 4-5 weeks after the closing of the transaction. *MBIA Ins. Corp. v. GMAC Mortg.*, 30 Misc.3d 856, 863 (N.Y. Sup. Ct. 2010) (denying motion to dismiss fraud claim where mortgage pools not fully populated at time of closing and "faulty loans could be added to the mortgage pools after an investigation."). For CWHEQ 2007-S3, for example, the total principal balance of the transaction was $700,000,100, and the pre-funding amount was $103,872,797. *See* Holland Aff. Ex. 14, at S-34; Sheth Aff. Ex. 46, at 451:5-453:2; *id.* Ex. 51, at 697:19-698:6. Over 1,700 loans were added to the pool for CWHEQ 2007-S3 over one month after the transaction closed (12,909 loans were part of the pool for this Securitization at the time of closing). *Id.* Ex. 327 (email and attached pre-funding population for 2007-S3); *id.* Ex. 328 (email and attached closing population for 2007-S3); CUF ¶¶ 269-70.

C. Countrywide's Assertions Regarding MBIA's Reliance Are Incorrect And At Most Raise Factual Disputes For Trial

As shown above, abundant record evidence affirmatively demonstrates that MBIA justifiably relied on Countrywide's representations and warranties. As to Countrywide's contrary account, MBIA has strong responses to each of Countrywide's assertions. For example:

- Countrywide asserts that MBIA's due diligence became increasingly lax during its consideration of the Securitizations at issue due to competitive pressure from other financial guaranty insurers bidding on the same deals (CW Mem. 8), but Countrywide ignores the substantial evidence that MBIA's controls remained robust throughout. *See, e.g.*, Sheth Aff. Ex. 19, at 43:19-44:6 ("[I]f I thought there was a serious concern or I, myself, felt that we were going to lose money on a transaction, then I would not have gone forward."); CUF ¶¶ 188-226.

- Countrywide quotes a statement by MBIA's then-Chairman Jay Brown concerning the pre-2004 period that MBIA was "'not being paid . . . sufficiently' to warrant the effort and expense of conducting loan file review" (CW Mem. 9), but ignores Mr. Brown's further explanation that MBIA's decision not to undertake that task during the later period relevant here was not dictated by expense, but rather because MBIA was shifting its business to large, stable entities like Countrywide, and industry practice was for the insurer not to conduct loan file review in such deals, *see* Sheth Aff. Ex. 10, at 43:22-44-10 (Because such issuers "had established records of underwriting consistency, ... we felt comfortable that, in dealing with that type of company, we could use a higher caliber ... type due diligence than we would have with a smaller company."); *id.* Ex. 79, at 117:9-118:7 (Countrywide's expert's testimony that in his experience securities underwriters may retain third-party due diligence firms to review loan files); CUF ¶¶ 227-28, 231.

- Countrywide quotes Mr. Brown's observation in 2005 that lenders including Countrywide were using "more relaxed underwriting criteria" (CW Mem. 10), but ignores MBIA lead underwriter Theresa Murray's response that "these buckets/changes still remain relatively minor" and that MBIA "adjust[ed] for them in our loss projection methodology by incorporating in conservative assumptions (relative to actual historic data) as well as by the existing cushion in the [loss coverage] multiple." Sheth Aff. Ex. 319; CUF ¶¶ 271, 273-75.

- Countrywide notes that Mr. Brown in mid-2006 stated his intent to ask MBIA's CEO "to veto any Countrywide deals" and contends that MBIA disregarded Mr. Brown's advice (CW Mem. 10-11). But Countrywide ignores that Mr. Brown's concern was whether MBIA was concentrating too much business with a single mortgage issuer (namely, Countrywide), rather than having particular reservations about doing business with Countrywide as an issuer. *See* Sheth Aff. Ex. 10, at 249:21-250:10; *id.* Ex. 275; *see also id.* Ex. 9, at 184:25-185:7; CUF ¶ 41.

- Countrywide asserts (CW Mem. 14-15, 29) that MBIA should have extrapolated to each Securitization pool the results of the third-party due diligence firms' analysis of samples from the pools (which flagged numerous loans as inconsistent

with Countrywide's representations and warranties), but Countrywide ignores that those samples were both not entirely random (instead consisting in part of "adversely" selected risky loans) and not sufficiently large to support extrapolation to the pools as a whole. *See* Sheth Aff. Ex. 85, at 2; CUF ¶¶ 250-52. Moreover, Countrywide provided MBIA with assurances that Countrywide could obtain any documents the third-party firms indicated were "missing" from the loan files. Sheth Aff. Ex. 15, at 408:9-23; 416:11-25; *see also id.* Ex. 144, at CWMBIA0012994801; CUF ¶ 292. Indeed, it is Countrywide that should have been on notice of the problems in the pool, as it was required under federal securities law to undertake due diligence to ensure that its statements in offering materials are accurate. To the extent a few defective loans were discovered post-closing, MBIA had the right under the Transaction Documents to demand that Countrywide repurchase those loans. *See* Sheth Aff. Ex. 352, at 198:21-199:3 ("if any of these loans didn't match the due diligence or the underwriting criteria, that provided some comfort that . . . they would be taken care of by a repurchase."); *id.* Ex. 19, at 172:16-173:5 (similar); CUF ¶¶ 297, 230, 313, 257-63.

- Countrywide invokes (CW Mem. 28) MBIA's statement in its *JP Morgan* complaint that, had MBIA been aware of third-party due diligence reports in that transaction that approximately one-third of the loans in the sample were not originated in compliance with the lender's underwriting guidelines, MBIA would not have issued a policy; Countrywide argues that MBIA had similar notice here. But Countrywide arrives at its one-third figure here only by artificially inflating the "non-compliant" loans category by including loans that departed from underwriting guidelines but as to which an exception to those guidelines had been made by the lender based on purported compensating factors (*e.g.*, the home might not have been owner-occupied, but the borrower had a very high income). *See* Sheth Aff. Ex. 96, at ¶ 51; CUF ¶ 41; 77.

- Countrywide claims that "for 12 of the 15 Securitizations, MBIA's underwriting committee voted to approve the transaction before it had even received the due diligence results" (CW Mem. 15), but Countrywide's notion of "the due diligence results" is wrong. In fact, for each of the 15 deals, MBIA received and reviewed the amount of due diligence that it deemed necessary to assure itself that the proposed transaction was in line with MBIA's "no loss" underwriting policy, and if it had not, MBIA would not have moved forward with the deal. Sheth Aff. Ex. 19, at 171:6-173:5; *id.* Ex. 14, at 84:15-21; CUF ¶¶ 286-87, 291-92, 295-96, 224-25. Countrywide's assertion is especially disingenuous given its own contemporaneous statements to MBIA that Countrywide had reviewed the third-party due diligence and that it confirmed that the loans had the good quality that Countrywide had represented to MBIA. *See* Sheth Aff. Ex. 142; *id.* Exs. 314-315; CUF ¶¶ 288-90, 292.

- Countrywide claims (CW Mem. 9) that MBIA should have conducted its own review of the loan files before closing, but Countrywide acknowledges MBIA did not have a contractual right to access the files at that time. *See* Countrywide 19-a, ¶ 103 ("MBIA has repeatedly maintained that it had the contractual right to review . . . any loan file *at any time after closing*.") (emphasis added); *see also e.g.*, Holland Aff. Ex. 60, §2.02 (granting MBIA right to request information "during the Term of the Insurance Agreement"); CUF ¶ 264.

- Countrywide asserts (CW Mem. 10) that certain language in the Prospectus Supplements put MBIA on notice of substantial inaccuracies in Countrywide's representations and warranties. In fact, the Prospectus Supplements' supposed

"warnings" are merely *generalized statements* that *some* loans in the pools were originated through Countrywide's Reduced Documentation Program or a reasonable exception to Countrywide's lending guidelines, and that macroeconomic conditions might impact loan performance. *See, e.g.*, Holland Aff. Ex. 1, at S-33-34; *id.* Ex. 12, at S-25; CUF ¶¶ 276-80, 356. They surely did not alert MBIA that 96% of those loans had defects that materially increased the credit risk of the loan. *See* Sheth Aff. Ex. 80, at 55-156. In other words, that Countrywide disclosed (and MBIA committed to insure against) certain risks does not imply that Countrywide disclosed a much different and more problematic set of risks—namely that the characteristics of the loans were markedly worse than Countrywide had represented them to be.[18]

- Countrywide's assertion that the loan tapes it provided to MBIA "allowed MBIA to see for itself that the loan attributes in the collateral pools were becoming increasingly risky over time" (CW Mem. 10) ignores, most obviously, that the loan tapes were themselves beset with numerous misrepresentations regarding key credit characteristics of thousands of loans. *Id.* Ex. 80, at 123-32; CUF ¶¶ 281-82.

- Countrywide's reference (CW Mem. 9) to a lone instance where an insurer (Syncora) requested that Countrywide's chosen third-party due diligence firm review a few additional loans in connection with a single securitization does not undermine MBIA's evidence of industry practice, *see, e.g.*, Sheth Aff. Ex. 14, at 88:24-89:12, and at most highlights a dispute of fact for trial. Nor does it support that MBIA itself could have accessed the loan files before closing. CUF ¶ 58-59.

At bottom, Countrywide's assertions, to the extent they are not rejected outright, at most raise disputes of fact that render summary judgment improper.

D. Countrywide's Repudiation Of Its Repurchase Obligations

The facts concerning Countrywide's disregard for its repurchase obligations are addressed in detail in MBIA's affirmative motion for summary judgment, but MBIA summarizes them here because they bear on certain arguments raised in Countrywide's motion for summary judgment, such as its contention that the Transaction Documents restrict MBIA to a repurchase remedy and prevent MBIA from seeking rescissory damages.

In 2008, after investigating the increased delinquencies and defaults of loans underlying the Securitizations, MBIA attempted to exercise its contractual repurchase rights, demanding that Countrywide repurchase thousands of defective loans from the Securitizations. *See* MBIA SJ Mem. 7. Rather than comply with these legitimate demands, however, Countrywide deliberately frustrated the repurchase remedy by, for example, requiring multiple levels of review for

[18] Moreover, there is evidence that Countrywide knew that many of its representations were false yet never conveyed this knowledge to MBIA in the Prospectus Supplements or elsewhere. Sheth Aff. Ex. 162; *id.* Ex. 163.

repurchase approvals, applying a red-faced standard where only the most egregious loans would be approved for repurchase, and inventing new requirements for repurchase not found in the Transaction Documents. *Id.* at 7-8, 40-43. Countrywide's failure to repurchase *any* of these loans—during a time period when MBIA cumulatively made hundreds of millions of dollars in claims payments under its Policies—finally led MBIA to file this suit in September 2008.[19] It was only after MBIA filed suit that Countrywide agreed to repurchase approximately 600 of the 13,607 loans MBIA had requested, and even these token repurchases were delayed for over a year before Countrywide eventually abandoned the façade of its compliance with the process by revoking the process entirely. *Id.* Countrywide continues to deny MBIA's repurchase requests in bad faith, refusing to repurchase loans even where it recognizes that the repurchase claim is strong. *Id.*

ARGUMENT

Summary judgment will be granted only where no triable issue of fact exists. *Mandelos v. Karavasidis*, 86 N.Y.2d 767, 768-69 (1995). The movant must come forward with evidence "sufficien[t] to warrant the court as a matter of law in directing judgment." CPLR 3212(b); *see Penava Mech. Corp. v. Afgo Mech. Servs., Inc.*, 71 A.D.3d 493, 495-96 (1st Dep't 2010). If the movant offers such proof, "the opposing party must 'show facts sufficient to require a trial of any issue of fact.'" CPLR 3212(b); *see Zuckerman v. City of New York,* 49 N.Y.2d 557, 562 (1980). The court should draw all reasonable inferences in favor of the non-movant (here, MBIA). *See, e.g.*, *Morris v. Lenox Hill Hosp.*, 232 A.D.2d 184, 185 (1st Dep't 1996) ("It is well settled that where the facts permit conflicting inferences to be drawn, summary judgment must be denied."). As shown below, Countrywide's motion should be denied under these standards.

[19] To date, MBIA has made well in excess of $2 billion dollars in claim payments under its Insurance Policies. MBIA Mem. 7.

I. COUNTRYWIDE IS NOT ENTITLED TO SUMMARY JUDGMENT ON MBIA'S FRAUD CLAIM

A. Countrywide Misstates The Reliance Standard In The Insurance Context

This Court's January 3, 2012 Order held "that in [the] insurance context, with MBIA as an insurance company and Countrywide as an applicant for insurance, [MBIA's] claims are informed by New York common law and Insurance Law Sections 3105 and 3106." *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 34 Misc. 3d 895, 906 (Sup. Ct. 2012). Although this Court focused on the causation element and did not have occasion to address the existence or contours of a reliance element, New York Insurance Law § 3105 provides that there is no such element, stating in pertinent part:

> (a) A representation is a statement as to past or present fact, made to the insurer by, or by the authority of, the applicant for insurance or the prospective insured, at or before the making of the insurance contract as an inducement to the making thereof. A misrepresentation is a false representation, and the facts misrepresented are those facts which make the representation false.
>
> (b)(1) No misrepresentation shall avoid any contract of insurance or defeat recovery thereunder unless such misrepresentation was material. No misrepresentation shall be deemed material unless knowledge by the insurer of the facts misrepresented would have led to a refusal by the insurer to make such contract.

In other words, once a misrepresentation is found to be "material" in the sense that "knowledge by the insurer of the facts misrepresented would have led to a refusal by the insurer to make such contract," the insurer may avoid the contract (or obtain equivalent damages) without the need to establish justifiable reliance. Numerous courts interpreting Section 3105 have so held. *See N. Am. Philips Corp. v. Aetna Cas. and Sur., Co.*, C.A. 88C-JA-155, 1995 WL 626044, *2-3 (Del. Super. Ct. Apr. 10, 1995) ("[J]ustifiable reliance has no bearing on the statutory scheme under [N.Y. Insurance Law Section 3105]. It is clear that New York courts have not engrafted an element of justifiable reliance as a precondition to [rescission] of an insurance contract."); *Evanston Ins. Co. v. Biomedical Tissue Servs., Ltd.*, 06-CV-1107, 2007 WL 4180653, at *5-6 (E.D.N.Y. Oct. 22, 2007), *report and recommendation adopted as mod.*, 06-CIV-1107, 2007 WL 4180619 (E.D.N.Y. Nov. 20, 2007) (similar, contrasting New Jersey law). These courts correctly recognize that, under Section 3105, an applicant for insurance has a duty to make

truthful disclosures in its application, and an insurer may rely on those disclosures without further investigation.[20]

Accordingly, because MBIA's fraud claim arises in the context of an application for insurance, MBIA need establish only that it issued the insurance policies for each of the Securitizations on the basis of material misrepresentations by Countrywide. There is ample evidence to support such a finding. Discovery has confirmed MBIA's allegations that Countrywide, in an effort to drive market share, materially misrepresented to MBIA its stated commitment to prudent and customary underwriting by, *inter alia*, approving huge volumes of so-called exception loans that failed to comply with Countrywide's underwriting guidelines and failed to qualify for documented compensating factors offsetting the increased credit risk associated with the exception. CUF ¶¶ 322-40. In addition, Countrywide misrepresented the credit characteristics of the loans to be included in the Securitizations on the loan tapes provided to MBIA and to the ratings agencies. *See* Sheth Aff. Ex. 80, at 123-32; CUF ¶¶ 281-82. Finally, Countrywide falsely represented that the third-party due-diligence firms it retained to conduct loan-level reviews were independent when in fact Countrywide heavily influenced and manipulated the scope of such firms' reviews, and as a result, understated the true number of defects in the loans reviewed. *See generally* Sheth Aff. Ex. 81; CUF ¶¶ 230, 249, 301-13. Had MBIA known of the nature and extent of Countrywide's misrepresentations, it would not have agreed to provide insurance on the Securitizations. *See* Sheth Aff. Ex. 87, at 77-78. This evidence is more than sufficient to find that Countrywide's misrepresentations were material and therefore that MBIA has established its fraud claim.

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[20] Numerous courts have likewise recognized that an insurer who demonstrates that the applicant made material misrepresentations may obtain rescission or equivalent relief without the need to show that the applicant acted with intent. *See, e.g., Precision Auto Accessories, Inc. v. Utica First Ins. Co.*, 52 A.D.3d 1198, 1201 (4th Dep't 2008) ("Insurance Law § 3105(b) does not specify that a misrepresentation must be willful, and '[w]hether or not plaintiff intended to provide inaccurate statements or misrepresentations at the time [it] filled out the application is irrelevant'") (*quoting Curanovic v. New York Cent. Mut. Fire Ins. Co.*, 307 A.D.2d 435, 437 (3d Dep't 2003)) (alterations in original); *Process Plants Corp. v. Ben'l Nat'l Life Ins. Co.*,53 A.D.2d 214, 216 (1st Dep't 1977) (same); *In re Worldcom Inc. Sec. Litig.*, 354 F.Supp.2d 455, 465 (S.D.N.Y. 2005) (same); *Kulikowski v. Roslyn Sav. Bank*, 121 A.D.2d 603, 605 (2d Dep't 1986) (same); *Olympia Mortg. Corp. v. Lloyd's of London*, 2009 N.Y. Misc. LEXIS 5027, at *16 (N.Y. Sup. Ct. Oct. 29, 2009) (same).

Indeed, because, as demonstrated in MBIA's affirmative motion for summary judgment on its claim for breach of the Insurance Agreements, Countrywide indisputably misrepresented the characteristics of over 50% of the mortgage loans in the random samples, *see* MBIA SJ Mem. 2-5, MBIA is entitled to summary judgment on its fraudulent inducement claim as well. *See, e.g.*, *Vinder v. Showbran Leasing & Mgmt., Inc.*, 298 A.D.2d 325, 326 (1st Dep't 2002) ("a court may deny a party's motion for summary judgment and yet search the record to grant summary judgment to the non-moving party on the same issue").

B. Reasonable Jurors Would Find That MBIA Justifiably Relied Under Common-Law Standards

Even if MBIA were required to establish justifiable reliance, it has adduced ample evidence of that score under common-law standards, and Countrywide's arguments to the contrary merely highlight genuine disputes of fact for trial. In determining whether reliance is reasonable, courts consider whether: (i) the plaintiff has "gone to the trouble to insist on a written representation that certain facts are true"; (ii) the "plaintiff has taken reasonable steps to protect itself against deception"; and (iii) the facts represented by defendant are peculiarly within the defendant's knowledge and whether the plaintiff has the means available to know, by the exercise of ordinary intelligence, the truth of the subject of the representation. *DDJ*, 15 N.Y.3d at 153-54. Moreover, a "duty to inquire" into the representations is *not* "necessarily triggered as soon as a plaintiff has the slightest hints of any possibility of falsehood," and a plaintiff "should not be denied recovery merely because hindsight suggests that it might have been possible to detect the fraud when it occurred." *Id.* at 154. As shown below, MBIA has adduced substantial evidence that it justifiably relied on Countrywide's representations, and is well within the standards articulated by the Court of Appeals in *DDJ*.[21]

[21] *See, e.g.*, *DDJ*, 15 N.Y.3d at 155-156 (whether plaintiff was "justified in relying on the warranties they received is a question to be resolved by the trier of fact"); *Brunetti v. Musallam*, 11 A.D.3d 280, 281 (1st Dep't 2004) (where there is a triable issue of fact regarding justifiable reliance, it is "not subject to summary disposition"); *MBIA Ins. Corp. v. GMAC Mortg. LLC*, 914 N.Y.S.2d 604, 608 (N.Y. Sup. Ct. 2010) ("[r]easonable reliance is a fact intensive inquiry, which should be reserved for a trier of fact").

1. MBIA Obtained Comprehensive Representations And Warranties That The Information Provided By Countrywide Was True

As an initial matter, general common-law authorities, like the New York insurance-law provision discussed above, hold that a plaintiff often need not engage in *any* due diligence if he has obtained a representation from the defendant on the very fact that due diligence would investigate. In *DDJ*, the Court of Appeals specifically held that "where a plaintiff has gone to the trouble to insist on a written representation that certain facts are true, it will often be justified in accepting that representation rather than making its own inquiry." 15 N.Y.3d at 153-54 (declining to dismiss fraud claim where plaintiff "obtained representations and warranties to the effect that nothing in the financials was materially misleading"). The Court further noted that it is a rare case that "a plaintiff who did obtain such a representation could not justifiably rely on it." *Id.* at 154. The Second Circuit similarly has held that "[a] 'warranty' . . . is intended precisely to relieve the promisee of any duty to ascertain the fact for himself." *Metro. Coal Co. v. Howard*, 155 F.2d 780, 784 (2d Cir. 1946) (L. Hand, J.); *see also, e.g.*, *Merrill Lynch & Co. v. Allegheny Energy, Inc.*, 500 F.3d 171, 181 (2d Cir. 2007) ("The warranties contained [in the agreement] imposed a duty on Merrill Lynch to provide accurate and adequate facts and entitled Allegheny to rely on them without further investigation or sleuthing.").

Here, the evidence obtained in discovery confirms that MBIA sought and received a series of comprehensive representations and warranties from Countrywide and relied on such representations and warranties in evaluating the risk associated with insuring the Securitizations. *See supra*, at 7; CUF ¶¶ 257-63. These representations and warranties assured MBIA that the information provided by Countrywide about the Securitizations, the underlying mortgage loans, Countrywide's financial condition, and its operations as a whole, including its origination, underwriting, and servicing practices, were true and accurate. *See* Holland Aff. Exs. 57-71 at § 2.01(j). Additionally, MBIA secured a comprehensive array of representations and warranties from Countrywide about the characteristics of the underlying loan pools and of individual loans. *See supra*, at 7.

Under such circumstances, courts have declined to dismiss fraud claims for failure to establish justifiable reliance. *See DDJ*, 15 N.Y.3d at 153-54 (declining to dismiss fraud claim where plaintiff "obtained representations and warranties that nothing in the financials was materially misleading"); *Black v. Chittenden*, 69 N.Y.2d 665, 669 (1986) (reversing grant of summary judgment on fraud claim, relying on fact that the plaintiffs had solicited and received assurances from the defendant regarding the condition of the property); *JP Morgan Chase Bank v. Winnick*, 350 F. Supp. 2d 393, 413 (S.D.N.Y. 2004) (where plaintiff had bargained for a representation and warranty that no event of default had occurred, the issue whether the plaintiff's reliance was reasonable is a factual question inappropriate for summary judgment); *MBIA v. GMAC*, 914 N.Y.S.2d at 609 (declining to dismiss fraud claim where MBIA alleged that, without defendant's representation and warranty as to the accuracy of the loan information and credit scores, MBIA would not have entered into the transaction).

Mountain Creek Acquisition v. Intrawest US Holdings, 96 A.D.3d 633 (1st Dep't 2012) (cited at CW Mem. 20, 21, 26), is inapposite. Although the plaintiff had bargained for and obtained certain express representations and warranties, the contract contained a disclaimer expressly stating that, "in making its decision to enter into this Agreement and to consummate the Transactions, [plaintiff] has relied solely on . . . its own investigation, analysis and evaluation." Sheth Aff Ex. 97, at 14-15. In dismissing the fraud claim, the court ruled that the claim was "barred by the specific disclaimer in the Agreement." *Mountain Creek*, 96 A.D.3d at 634; *see also UST Private Equity v. Salomon Smith Barney*, 733 N.Y.S.2d 385, 386 (1st Dep't 2001) (dismissing fraud claim on basis of express disclaimers that "defendant investment bankers could not guarantee the accuracy or completeness of the information set forth therein, and specifically directed plaintiffs to 'rely upon their own examination'"). Here, by contrast, the Transaction Documents contain no such disclaimers that would bar MBIA's fraud claim.

In addition, Countrywide's claim that MBIA should have reviewed loan files after closing despite obtaining these representations and warranties from Countrywide improperly shifts the burden and costs of performing such loan reviews to MBIA and deprives MBIA of the

benefit of its bargain. Having negotiated and paid for express representations and warranties, there was no reason for MBIA to re-underwrite the loans post-closing to test whether had Countrywide complied with its representations and warranties. Moreover, no performance data suggested any such widespread breach during the early stages of the Securitizations; until the late fall of 2007, the Securitizations performed as expected. *See supra*, at 12-13; CUF ¶¶ 253-54, 271, 273-75. As such, Countrywide's argument that MBIA should have nonetheless conducted loan file reviews despite having obtained comprehensive representations and warranties should be rejected and at most highlights a factual dispute for trial.[22]

2. Reasonable Jurors Would Find That MBIA Undertook Substantial Due Diligence In Connection With Its Decision To Provide Insurance On The Securitizations

In addition to obtaining such representations and warranties, MBIA conducted comprehensive deal-specific due diligence, including: (i) evaluating the structure of each Securitization, (ii) stratifying the pool of loans included in each Securitization and comparing such pools to earlier securitizations, (iii) performing a cash flow analysis of the pool of loans, (iv) analyzing historical performance of similar collateral, including defaults, delinquencies, and pre-payments, and (v) reviewing the results of the loan-level credit and compliance reviews performed by the third-party due-diligence firms retained by Countrywide. *See supra*, at 8-11; CUF ¶¶ 188-226, 286-296, 300. Furthermore, MBIA regularly assessed the financial stability and creditworthiness of Countrywide as the issuer, and MBIA's existing and contemplated future exposure to Countrywide, in setting exposure limits for Countrywide-issued securitizations. Sheth Aff. Ex. 22, at 271:12-16; *id.* Ex. 41, at 32:17-20; CUF ¶¶ 193, 211-12. Finally, MBIA also performed post-closing surveillance on each of the Securitizations and conducted regular

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[22] *CIFG N. Am. Assurance v. Goldman Sachs, Inc.*, Index No. 652286/2011, 2012 WL 1562718 (N.Y. Sup. Ct. May 1, 2012) (cited at CW Mem. 22), is also distinguishable. There, the plaintiff had a *pre*-closing right to review loan files. *See* Sheth Aff. 98, at 7 ("CIFG admits in its Complaint that it made the business decision to conduct *no due diligence on the Loans* prior to the closing of the Securitization (Compl. ¶ 39), even though it had the express contractual right to demand and evaluate any and all of the loan files for the Loans.") (emphasis in original). Here, by contrast, MBIA did not have a *pre-closing* right to obtain the loan files, *see supra*, at 15, and MBIA did engage in reasonable, industry-standard due diligence. Because *CIFG* is inapposite, this Court need not consider whether it is otherwise correct (an appeal is pending).

on-site reviews of Countrywide's servicing practices. *See supra*, at 10; CUF ¶¶ 213-18.[23] There can be no question that such comprehensive and multi-faceted due diligence by MBIA constitutes reasonable efforts to protect itself from deception. At the very least, reasonable jurors would so find.

There is no basis for Countrywide's suggestion (CW Mem. 23-26) that reasonable due diligence required that MBIA engage in its own review of the loan files. In *MBIA Ins. Corp. v. Royal Bank of Canada*, 2010 N.Y. Slip Op. 51490(U), at *17, 33 (N.Y. Sup. Ct. Westchester Cty. Aug. 19, 2010), the court rejected such an argument, finding that MBIA had engaged in other due diligence in accordance with industry standards for financial guarantors on CDOs. Here, MBIA's expert opined that its approach was consistent with industry practice. Sheth Aff. Ex. 88, at 32-41 (MBIA followed industry practice in considering third-party loan file review results); *id.* Ex. 87, at 1-2 (opining, *inter alia*, that "MBIA took reasonable and appropriate steps in conducting the internal review that led to its decision to provide financial guaranty insurance for the Countrywide Securitizations," and that "MBIA's internal review and approval procedures for the...Securitizations were also consistent with industry custom and practice for a Triple-A rated financial guaranty insurer"). Indeed even Countrywide's own expert in this case conceded that he is aware of no MBIA policy or procedure, nor any industry publication discussing industry standards and practices, that imposes upon a monoline insurer such as MBIA any obligation to retain its own third-party loan-level due-diligence firm, separate and apart from the firm retained by the securities underwriter. *Id.* Ex. 13, at 148:20-149:2; 373:22-376:4. Further, he was aware of only one single monoline insurer that retained such third-party firms after 2004, the beginning of the relevant period. *Id.* at 367:24-368:8; CUF ¶ 227-30.

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[23] Countrywide suggests (CW Mem. 7-8) that MBIA dispensed with these processes so as not to lose bids. To the contrary, MBIA's transaction underwriters acted as a check on the New Business group, and MBIA often declined Countrywide's offers when the details of the transaction were not satisfactory to MBIA or when MBIA did not receive the necessary data to prudently underwrite the transaction. CUF ¶¶ 184, 197, 226. In addition, MBIA did not insure any Securitizations unless they complied with its no-loss underwriting policy and had an investment-grade shadow rating. CUF ¶¶ 194-99, 186, 219.

Barneli & Cie SA v. Dutch Book Fund SPC, Ltd., 95 A.D.3d 736 (1st Dep't 2012) (cited at CW Mem. 20-21), is inapposite. The plaintiff, a bank, invested $50 million in defendant, a hedge fund, without conducting its own investigation. *Id.* at 737. Moreover, even though the plaintiff represented in the relevant agreement that it had the requisite knowledge and experience to evaluate the risks of the investment, it admitted in discovery that it in fact lacked the expertise to understand certain algorithms at issue in the investment. *See Barneli & Cie S.A. v Dutch Book Funds, SPC, Ltd.*, 28 Misc. 3d 1232(A), at *9-*10 (N.Y. Sup. Ct. 2010), *rev'd in part*, 95 A.D.3d 736. Here, by contrast, MBIA made no such representation and did conduct a reasonable, industry-standard investigation.

3. Reasonable Jurors Would Find That The Facts Misrepresented By Countrywide Were Peculiarly Within Its Knowledge

Even aside from the ample evidence of Countrywide's extensive representations and warranties and MBIA's reasonable, industry-standard due diligence, summary judgment on MBIA's fraud claim would still be improper because MBIA lacked access to the information necessary to discern the falsity of Countrywide's representations and warranties.

A plaintiff will "not be precluded from claiming reliance on misrepresentations of fact peculiarly within the [defendant's] knowledge." *ACA Fin. Guar. Corp. v. Goldman Sachs, Inc.*, Index No. 650027/11, 2012 WL 1450022, at *10 (N.Y. Sup. Ct. April 23, 2012), *citing Steinhardt Group Inc. v. Citicorp*, 272 A.D.2d 255, 257 (1st Dep't 2000); *see also DDJ*, 15 N.Y.3d at 153-54. Here, Countrywide had peculiar knowledge about the origination, underwriting, and servicing practices applicable to such loans, and the decision to include the loans in the Securitizations by virtue of its role as the originator, seller, sponsor, underwriter, and servicer of the vast majority of the mortgage loans in the Securitizations. *MBIA Ins. Corp. v. Morgan Stanley*, Index. No. 29951/10, 20011 WL 2118336, at *5 (N.Y. Sup. Ct. May 26, 2011). In addition, Countrywide performed various credit, compliance, and fraud reviews of its loans, and thus, had direct, first-hand knowledge of the quality of the loans it was originating and then selling in the secondary market.

In contrast, MBIA was several steps removed from the origination, underwriting, and servicing process, and thus, lacked access to the same information. Indeed, in light of this informational asymmetry, MBIA acted reasonably by securing representations and warranties as to the accuracy of the information provided by Countrywide, and undertaking its own comprehensive due diligence. *See id.* at *5 (sustaining fraudulent inducement claim where defendant "had unique and special knowledge regarding the mortgage loans, particularly the quality of the underwriting of the loans" because it "originated or acquired the mortgage loans to be included in the mortgage pool"); *see also* Sheth Aff. Ex. 90, at ¶¶ 21-22 (because "no guarantor has accompanied the loan through its production history," Countrywide "necessarily ha[s] more information about the loans being sold than those who are insuring the securities for which the loans serve as collateral."); CUF ¶¶ 314-21.[24]

CIFG Assurance v. Goldman Sachs, Index No. 652286/2011, 2012 WL 1562718 (N.Y. Sup. Ct. May 1, 2012) (cited at CW Mem. 22), is not to the contrary. There, the Goldman Sachs defendants did not originate any of the loans in the securitization, and another defendant, M&T Bank, originated 23.09% of the loans. *Id.* at 1-2. Thus, none of the defendants alone possessed unique knowledge about the representations made about all the loans. In contrast, in light of its role at each step of the securitization process, Countrywide here had unique knowledge, "peculiarly" within its possession, of the attributes of the loans as well as its production processes.

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[24] In *HSH Nordbank AG v. UBS AG*, 95 A.D.3d 185 (1st Dep't 2012) (cited at CW Mem. 20), the court dismissed a fraud claim because, *inter alia*, the relevant documents contained "disclaimers...that [plaintiff] was not entering into the deal in reliance on any advice from [defendants]." The court found that the very misrepresentation at issue "was common knowledge among participants in that market," *id.* at 193, and the misrepresentation "could have been ascertained from reviewing market data or *other publicly available information*." *Id.* at 195 (emphasis added). In contrast, no such disclaimer can be found in the Transaction Documents here, and neither the loan files nor any of the information provided by Countrywide to MBIA before closing are common knowledge or publicly available information. *See ACA Fin. Guar. Corp.*, 2012 WL 1450022, at *12 (declining to dismiss fraud claim where information "was not discoverable through any publicly available source of information"); *Morgan Stanley*, 2011 WL 2118336, at *5 (declining to dismiss fraudulent inducement claim where "[n]one of the transaction documents disclaim MBIA's reliance on [the defendant's] pre-contractual representations").

4. The Prospectus Supplements And Due Diligence Results Did Not Trigger A Duty Of Inquiry By MBIA

The Court of Appeals has cautioned against denying recovery to a plaintiff who "has taken reasonable steps to protect itself from deception . . . merely because hindsight suggests that it might have been possible to detect the fraud when it occurred." *DDJ*, 15 N.Y.3d at 154. Despite the Court of Appeals' statements that a "duty to inquire" is not "necessarily triggered as soon as a plaintiff has the slightest hints of any possibility of falsehood," *id.* at 155-56, Countrywide argues (CW Mem. 26-28) that two "hints" should have tipped MBIA off to the fact that Countrywide's representations could not be trusted: (i) the disclaimers in the Prospectus Supplements, and (ii) the results of the third-party due diligence reviews. The argument fails as a matter of law and at most raises a fact dispute.[25]

First, any risk factor noted in the same materials in which Countrywide made its (false) representations and warranties cannot prevent MBIA from justifiably relying on those representations and warranties. Rather, under New York law, a promisee is disabled from justifiably relying on a representation only where he signs a contract that specifically disclaims the representation. *See, e.g.*, *Kwon v. Yun*, 606 F. Supp. 2d 344, 358 (S.D.N.Y. 2009); *Citibank, N.A. v. Plapinger*, 66 N.Y.2d 90, 94-95 (1985) (disclaimer does not defeat claim for fraud in inducement unless it specifically disclaims reliance on very matter as to which plaintiff claims it was defrauded); *Mfrs. Hanover Trust Co. v. Yanakas*, 7 F.3d 310, 316 (2d Cir. 1993) ("[T]he touchstone is specificity."). Here, there were no disclaimers, much less sufficiently specific ones, in the Transaction Documents.

Second, and in any event, although certain of the Prospectus Supplements contained certain disclosures about, *inter alia*, the increasing credit risk of the mortgage loans, Countrywide's expanding underwriting guidelines, and general macroeconomic conditions, those disclosures merely concerned *future* risks. The misconduct at issue is not misrepresentation of

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[25] *MBIA Ins. Corp. v. Credit Suisse*, 33 Misc.3d 1208(A) (N.Y. Sup. Ct. Oct. 7, 2011) (cited at CW Mem. 32), supports MBIA, not Countrywide, insofar as the court ultimately sustained the fraud claim because the "question of reasonable reliance is fact-intensive." *Id.* at *17.

future risks, but misrepresentation of *current* facts concerning the loans, and misrepresentation of Countrywide's compliance with its *current* (if expanded) underwriting guidelines. Had MBIA known of those misrepresentations, it never would have agreed to provide the insurance at all. Sheth Aff. Ex. 87, at 77-78. Hence, reasonable jurors would easily find that the disclosures in the Prospectus Supplements were insufficient to provide MBIA with any "hints" that MBIA should not rely on Countrywide's representations and warranties.[26]

Third, the third-party due-diligence reports likewise did not provide MBIA with any indication that Countrywide was including in the Securitizations large volumes of loans that violated Countrywide's own underwriting guidelines. Rather, those reports showed that only a small number of loans from the sample of loans reviewed for each Securitization were recommended for removal from the Securitization. *See supra* 11; CUF ¶¶ 255, 287. Countrywide's argument (CW Mem. 13-14, 27-28) to the contrary rests on its overstatement of the number of loans supposedly "flagged" as defective; Countrywide now artificially inflates the number of loans supposedly "flagged" as defective, specifically to include loans for which exceptions were warranted based on compensating factors (CW Mem. 12-14, n. 7), when in fact the due diligence results gave MBIA no indication that there was rampant misrepresentation of the credit qualities of the loans in the pool. *See supra* 11, 15; CUF ¶ 58.[27]

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[26] *See Plumbers' Union Local No. 12 Pension Fund v. Nomura Asset Acceptance Corp.*, 632 F.3d 762, 773 (1st Cir. 2011) (warnings in offering materials not sufficient because "saying that exceptions occur when borrowers demonstrate other 'compensating factors' [does not] reveal[] what plaintiffs allege, namely, a wholesale abandonment of underwriting standards"); *Capital Ventures Int'l v. UBS Secs.*, Index No. Civ. 11-11937, Dkt. No. 25, at 9 (D. Mass. Sept. 28, 2012) (same); *In re Morgan Stanley Mortg. Pass-Through Certificates Litig.*, 810 F. Supp. 2d 650, 672 (S.D.N.Y. 2011 (boilerplate disclaimers and disclosures do not disclose the risk of systematic disregard for underwriting standards"); *N.J. Carpenters Vacation Fund v. Royal Bank of Scot.*, 720 F. Supp. 2d 254, 270 (S.D.N.Y. 2010) ("[d]isclosures that described lenient, but nonetheless existing guidelines about risky loan collateral would not lead a reasonable investor to conclude that the mortgage originators could entirely disregard or ignore those loan guidelines"); *In re IndyMac Mortg.-Backed Sec. Litig*, 718 F. Supp. 2d 495, 509 (S.D.N.Y. 2010) ("[d]isclosures regarding the risks stemming from the allegedly abandoned standards do not adequately warn of the risk the standards will be ignored").

[27] Countrywide also relies (CW Mem. 28) on a purported "admission" in a complaint that MBIA filed against J.P. Morgan and its legacy entities, to support its argument that the due-diligence results should have caused MBIA to conduct additional inquiries. As explained *supra*, at 15, the final due-diligence results provided to MBIA here do not show a failure rate anywhere near as high as one-third.

II. COUNTRYWIDE IS NOT ENTITLED TO SUMMARY JUDGMENT ON MBIA'S CLAIM FOR BREACH OF THE INSURANCE AGREEMENTS

Seizing on a contractual provision that is limited by its terms to "this paragraph" (even though MBIA relies on breaches of numerous *other* paragraphs), Countrywide argues that the Transaction Documents limit MBIA to the remedy of repurchase and foreclose its claim for rescissory damages. CW Mem. 15-16. The argument misreads the contractual language, has been rejected by another court construing materially identical language, and is impractical (as that court also found) because it would relegate MBIA to putting back thousands upon thousands of loans one by one. This Court should reject it as well, and indeed has already done so in its January 3, 2012 Order, which recognized MBIA's right to seek rescissory damages if it can establish the elements of its claims for fraud and/or breach of contract. Countrywide's additional argument on the breach of contract claim—that MBIA must establish breaches on a loan-by-loan rather than pool-wide basis—should similarly be rejected.

A. Countrywide's "Sole Remedy" Argument Is Foreclosed By This Court's January 3, 2012 Order And In Any Event Is Incorrect

1. The Argument Is Foreclosed By The January 3, 2012 Order

As an initial matter, this Court has already effectively foreclosed Countrywide's argument that MBIA's sole remedy is a repurchase remedy. In its January 3, 2012 Order on MBIA's motion for partial summary judgment, the Court ruled, *inter alia*, that MBIA "may seek rescissory damages upon proving all elements of its claims for . . . breach of representation and/or warranty." 936 N.Y.S.2d 513, 527 (N.Y. Sup. Ct. 2012). The "law of the case" doctrine provides that, "when an issue is once judicially determined, that should be the end of the matter as far as Judges and courts of co-ordinate jurisdiction are concerned." *Martin v. City of Cohoes*, 37 N.Y.2d 162, 165 (1975). The doctrine "seeks to prevent relitigation of issues of law that have already been determined at an earlier stage of the proceeding." *Brownrigg v. New York City Hous. Auth.*, 29 A.D.3d 721, 722 (2d Dep't 2006). It is especially appropriate to apply the doctrine here because Countrywide failed to argue during the briefing or oral argument leading

to this Court's January 3 Order that rescissory damages were barred by anything in the Transaction Documents.

2. The Argument Is Wrong On The Merits

In any event, Countrywide's argument is wrong on the merits. MBIA's claim for breach of the Insurance Agreements is grounded on breaches of representations, warranties, and covenants contained in at least eight provisions of the Insurance Agreements, *see* Sheth Aff. Ex. 1, at ¶¶ 168-177—not just two, as Countrywide asserts (CW Mem. 32). Most importantly, MBIA alleges that Countrywide breached the warranty in § 2.01(j), which provides:

> Neither the Transaction Documents [including *inter alia* the SSAs, PSAs and Purchase Agreements] nor other material information relating to the Mortgage Loans, the operations of [CHL] (including servicing or origination of loans) or the financial condition of [CHL] or any other information (collectively, the "Documents") . . . furnished to the Insurer by [CHL] contains any statement of a material fact by [CHL] which was untrue or misleading in any material adverse respect when made. [CHL] has [no] knowledge of circumstances that could reasonably be expected to cause a Material Adverse Change with respect to [CHL]. Since the furnishing of the Documents, there has been no change or any development or event involving a prospective change known to [CHL] that would render any of the Documents untrue or misleading in any material respect.

Holland Aff. Ex. 57, § 2.01(j); *see also id.* Exs. 58-71, § 2.01(j) (substantively similar). With one exception, none of the warranties in the Insurance Agreements—including § 2.01(j)—contains any limitation on the remedies available to MBIA for their breach.

The sole exception is § 2.01(l), which incorporates the representations and warranties in the Transaction Documents into the Insurance Agreements, and which states that "[t]he remedy for any breach *of this paragraph* with respect to representations or warranties relating to a Mortgage Loan shall be limited to the remedies specified in the related Transaction Documents." Holland Aff. Ex. 57, § 2.01(l) (emphasis added); *see also id.* Exs. 58-71, § 2.01(l) (substantively similar). Countrywide argues that this limitation, together with the sole remedy provisions in certain sections of the Transaction Documents, limits MBIA to the repurchase remedy for breach of loan representations and warranties. This argument is flawed for at least three separate reasons.

First, the limitation in the last sentence of § 2.01(l) of the Insurance Agreements applies only to breaches "of this paragraph," not to breaches of any other paragraph in § 2.01. None of the other paragraphs—including § 2.01(j)—contains any such limitation. Under the doctrine of *inclusio unius est exclusio alterius*, the omission of this limitation from the other paragraphs is presumed to be intentional. *See, e.g.*, *Two Guys from Harrison-N.Y. v. S.F.R. Realty Assocs.*, 63 N.Y.2d 396, 404 (1984). Accordingly, MBIA's remedies for breach of § 2.01(j) and the other warranties in § 2.01 are not limited to the repurchase remedy. Countrywide suggests in a footnote (CW Mem. 32 n.16) that the limitation in § 2.01(l) is incorporated in § 2.01(j), but that reading is contradicted by § 5.02(b) of the Insurance Agreements, which states that "*[u]nless otherwise expressly provided*, no remedy herein conferred upon or reserved [sic] is intended to be exclusive of any other available remedy, but each remedy shall be cumulative and shall be in addition to other remedies given under the Transaction Documents or existing at law or in equity." Holland Aff. Ex. 57, § 5.02(b); *see also id.* Exs. 58-71, § 5.02(b) (emphasis added). Section 2.01(j) does not "expressly provide" for any limitation on remedies, while the limitation in § 2.01(l) is expressly restricted to any breach "of this paragraph." Thus, § 2.01(j) is not subject to any such limitation.[28]

Indeed, § 5.02(a) of the Insurance Agreements expressly confirms that, in the event that any of Countrywide's loan representations and warranties is materially false (and hence in violation of the warranty in § 2.01(j)), MBIA's remedies will *not* be limited to the repurchase

[28] The restriction of the limitation in § 2.01(l) to "any breach of this paragraph" further distinguishes this case from *Assured Guar. Municipal Corp. v. Flagstar Bank, FSB*, No. 11-CV-2375, 2011 WL 5335566 (S.D.N.Y. Oct. 31, 2011), where the paragraph relied on by Judge Rakoff (§ 2.03(h)) was actually a third-party-beneficiary provision that, not surprisingly, provided that the Insurer was subject to the same limitations as to remedies as the parties and applied this limitation generally, not merely to § 2.03(h). *See id.*, at *4-6; *see also* Sheth Aff. Ex. 107, § 2.03(h). *MASTR Asset Backed Securities Trust 2006-HE3 v. WMC Mortg. Corp.*, 843 F. Supp.2d 996 (D. Minn. 2012), is distinguishable because the claims were brought by a Trustee, not an insurer, who did not benefit from provisions like those contained in the Insurance Agreements. The recent decision granting summary judgment in the same case is distinguishable on the same ground. *See MASTR Asset Backed Securities Trust 2006-HE3 v. WMC Mortg. Corp.*, No. 11-2542, Slip Op. (D. Minn. Oct 1, 2012). *MBIA Ins. Corp. v. Resid'l Funding Co., LLC*, 906 N.Y.S.2d 781, 2009 WL 5178337 (N.Y. Sup. 2009) is simply irrelevant, since the Court did not construe a sole remedy provision, but rather held that MBIA could not circumvent an express-indemnity provision's limits by implying an indemnity right that went beyond those express limits. *Id.* at *7.

protocol unless the affected loan has already been repurchased. Section 5.02(a) provides that, "[u]pon the occurrence of an Event of Default" (defined by § 5.01(a) to occur when, among other things, a representation or warranty under § 2.03 or § 2.04 of the applicable SSA or PSA "shall prove to be untrue or incomplete in any material respect" *and* the affected loan has not been repurchased), MBIA may *either* "[e]xercise any rights and remedies under the Transaction Documents" *or* "take whatever action at law or in equity as may appear necessary or desirable in its judgment to enforce performance and observance of any obligation, agreement or covenant of . . . the Sponsor . . . under the Transaction Documents."[29] Since MBIA's claims for rescissory and compensatory damages seek to enforce CHL's agreements and covenants under the Transaction Documents, these remedies are expressly preserved by § 5.02(b). This preservation of remedies would be nullified if Countrywide's broad interpretation of the sole remedy provisions were upheld. Such a result must be avoided. *See Two Guys from Harrison-N.Y.*, 63 N.Y.2d at 403 ("In construing a contract, one of a court's goals is to avoid an interpretation that would leave contractual clauses meaningless.").

In *Syncora Guarantee, Inc. v. EMC Mortgage Corp.*, No. 09-CV-3106, 2011 WL 1135007 (S.D.N.Y. Mar. 25, 2011), Judge Crotty relied in part on a provision materially identical to § 5.02 in holding that Syncora was not limited by the sole remedy provision. Judge Crotty explained that:

> The Operative Documents grant especially broad rights and remedies to Syncora because, as the financial guarantor under an unconditional and irrevocable insurance policy, it bears the greatest loss if the loans underperform and the other parties break their contractual obligations. The I&I is the primary agreement governing the relationship between Syncora—as insurer of certain securities—and EMC—as their sponsor. The plain language of the I&I reflects the parties' clear intent to provide expansive and inclusive remedies in case of breach, clearly reserving Syncora's right to pursue any available remedy under the I&I, common law, or equity.

Id. at *5. Likewise here, each Insurance Agreement, reflecting the fact that MBIA "bears the greatest loss if the loans underperform and the other parties break their contractual obligations,"

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[29] *See* Holland Aff. Ex. 57 §§ 5.01, 5.02; *see also id.* Exs. 58-71, §§ 5.01, 5.02 (substantively similar).

"clearly reserv[es] [MBIA's] right to pursue any available remedy under the [Insurance Agreement], common law, or equity." Moreover, each Insurance Agreement "plainly makes its remedies cumulative and gives it[s] obligations precedence over any defenses provided by the other [Transaction Documents]." *Id.*

Furthermore, this interpretation of the agreements is consistent with the limited purpose of the repurchase remedy. The repurchase remedy was not intended to address claims based on widespread and pervasive breaches, such as MBIA alleges, but was rather intended as a narrow remedy designed to redress isolated bad mortgages. Again, in *Syncora*, Judge Crotty held:

> The repurchase protocol is a low-powered sanction for bad mortgages that slip through the cracks. It is a narrow remedy ('onesies and twosies') that is appropriate for individualized breaches and designed to facilitate an ongoing information exchange among the parties. This is not what is alleged here.

Id. at *6 n. 4.[30] Judge Crotty held that "[t]he futility of applying an individualized remedy to allegedly widespread misrepresentations is evident in the fact that, of the 1,300 loans actually submitted under the repurchase protocol, EMC has remedied only 20." *Id.* Similarly here, the futility of applying the repurchase remedy to Countrywide's claims is shown by the fact that Countrywide has repurchased only approximately 4.5% of the more than 13,000 loans MBIA has put back.[31] As in *Syncora,* Countrywide cannot reasonably expect the Court to examine each of the almost *400,000* loans at issue to determine whether there has been a breach, with the sole remedy of putting them back one by one. Compounding the impracticality of this remedy is its futility, given Countrywide's repeated refusal to honor its repurchase obligations, *see supra*, at

[30] Similarly, MBIA's expert, Mr. Mason, opined that, "[a]s in any manufacturing process, there is assumed to be a *de minimis* production defect rate associated with underwriting. It is generally assumed that such defects, should they become apparent in the normal course, can be addressed by the repurchase protocol." Sheth Aff. Ex. 90, at ¶ 26. However, "[w]hile Repurchase Damages may be most efficient for idiosyncratic problems with individual loans, this remedy was not designed for a case involving wholesale misrepresentations of loan attributes and wholesale disregard of the loan-production processes, which taints every aspect of the transaction." *Id.* at ¶ 30.

[31] The contrary numbers provided by Countrywide in the affidavit of Shareef Abdou should be disregarded because no documentation whatsoever was produced to support the facts alleged therein. *See Bartee v. D & S Fire Prot. Corp.*, 79 A.D.3d 508 (1st Dep't 2010) (affidavit that was "not based on personal knowledge, and was otherwise conclusory [was] therefore insufficient to satisfy appellant's prima facie burden on the [summary judgment] motion"); *Hoverson v. Herbert Const. Co., Inc.*, 283 A.D.2d 237, 239 (1st Dep't 2001) (vacating grant of summary judgment where "conclusory statement in the affidavit [], unsupported by any documentary evidence or factual detail, is insufficient to establish exhaustion of the policy as a matter of law.").

16 (summarizing facts); *infra,* at 36-39 (explaining why this supports allowing MBIA to prove breach of repurchase obligations on a pool-wide basis), which furnishes yet another reason to reject Countrywide's "sole remedy" argument.

Second, even if all of Countrywide's interpretations of the Transaction Documents were accepted, the Transaction Documents will be void *ab initio* if MBIA establishes that Countrywide made material misrepresentations or materially breached the warranties in the Transaction Documents. *See MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 936 N.Y.S.2d 513, 522 (N.Y. Sup. Ct. 2012). Thus, the sole remedy provisions contained in these agreements, on which Countrywide relies, will also be void and of no effect. *See Olympia Mortgage Corp. v. Lloyd's of London*, 2009 N.Y. Slip Op. 32623U, 2009 N.Y. Misc. LEXIS 5027, at *15-16 (N.Y. Sup. Ct. Kings Cty. Oct. 29, 2009) ("Even if Condition X, P 2 were deemed to be an express waiver by the Insurers of their contractual right to rescind the Bond, such waiver would be ineffective if the Bond were void under *Insurance Law § 3105* from the very beginning."); *Precision Auto Accessories, Inc. v. Utica First Ins. Co.*, 52 A.D.3d 1198, 1201 (4th Dep't 2008) ("when an insurance policy is void ab initio based on material misrepresentations in the application, it is as if the policy never came into existence").[32]

Third, even if Countrywide's reading of § 2.01(l) were otherwise correct, Countrywide ignores that the sole remedy clause in § 2.03 of the PSAs for each of the six CES Securitizations at issue *specifically excludes the Certificate Insurer* (*i.e.*, MBIA). This clause provides that "the obligation under this Agreement of the Sellers to cure, repurchase or replace any Mortgage Loan as to which a breach has occurred and is continuing shall constitute the sole remedy against the Sellers respecting such breach available to *Certificateholders, the Depositor or the Trustee*"—*not* the Certificate Insurer. Holland Aff. Ex. 49, § 2.03(f) (emphasis added); *see also id.* Exs. 50-

[32] Countrywide's cited cases (CW Mem. 34-35) are inapposite because none involved claims, like MBIA's, that the contracts were void *ab initio.* Rather, they involved claims made *pursuant to* the contracts. *See Assured Guar. Municipal Corp. v. Flagstar Bank, FSB,* No. 11-CV-2375, 2011 WL 5335566 (S.D.N.Y. Oct. 31, 2011) (claim for indemnification); *MASTR Asset Backed Securities Trust 2006-HE3 v. WMC Mortg. Corp.*, 843 F. Supp.2d 996 (D. Minn. 2012) (claim for compensatory damages); *MBIA Ins. Corp. v. Residential Funding Co., LLC,* 906 N.Y.S.2d 781, 2009 WL 5178337 (N.Y. Sup. 2009) (claim for equitable or implied indemnification).

54, § 2.03(f). The provision on which Countrywide relies, § 2.01(e)(4) (*see* CW Mem. 33), applies only to Subsequent Mortgage Loans. On their face, then, the sole remedy provisions relating to Initial Mortgage Loans in the CES Securitizations—approximately 35% of the loans in these Securitizations—do not apply to MBIA. *See Assured Guar. Municipal Corp. v. UBS Real Estate Secs., Inc.*, No. 12-CV-1579, Slip Op. at 5 (S.D.N.Y. Aug. 15, 2012) (sole remedy clause "does not appear to apply to Assured," because Assured is not mentioned in the clause).[33]

B. MBIA May Establish that Countrywide Breached Its Repurchase Obligations On A Pool-Wide Basis

Countrywide argues (CW Mem. 36-37) that, to enforce the repurchase obligation, MBIA must provide it with particularized notice, on a loan-by-loan basis, of each defective loan. This is contradicted by (1) the Court's December 22, 2010 Sampling Order and other authorities permitting enforcement of the repurchase remedy on a pool-wide basis; (2) the Transaction Documents, which require repurchase upon Countrywide becoming aware of defective loans; and (3) the fact that MBIA's past repurchase demands have been almost entirely futile.

1. The Court's Sampling Order And Other Authorities Permit Extrapolation From Samples

Countrywide's argument is inconsistent with the Court's December 22, 2010 Order, which permitted MBIA to use statistical sampling to prove its causes of action for fraud *and* breach of contract. The Order specifically noted that MBIA would use sampling to prove its repurchase claim. *See* Dec. 22, 2010 Order at 11-12. The Order thus contemplated that MBIA would seek to prove its repurchase claim on a pool-wide basis rather than individually as to each loan.

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[33] The recent decision in *Assured Guar. Corp. v. DLJ Mortg. Cap., Inc.*, No. 652837/2011 (N.Y. Sup. Oct. 12, 2012), was simply wrong. Not only did it ignore *Assured v. UBS,* even though that decision was cited to by plaintiff, but it attempted to shoehorn the Certificate Insurer into a "sole remedy" provision from which it was specifically excluded by holding that "[t]he Insurers are third-party beneficiaries of the PSAs with all the rights of the Certificateholders." Slip Op. 15. In fact, this holding was directly contradicted by the third-party beneficiary provision, which provided that the Certificate Insurer was a "third-party beneficiary of the Agreement to the same extent as if it were a *party* hereto." The Certificateholders were not parties to the PSAs. Thus, there was no justification for limiting the Certificate Insurer to the same remedies as the Certificateholders.

Countrywide's argument (CW Mem. 36) that allowing MBIA to prove its claim in this fashion would deprive Countrywide of its contractual right to cure such loans was expressly rejected by Judge Rakoff in *Assured v. Flagstar.* There, Flagstar argued, like Countrywide here, "that plaintiff's method of extrapolating from breaches in the sample to the rest of the loans in the transaction does not identify which loans contain breaches and deprives Flagstar of its bargained for right to cure such alleged breaches.'" 2012 WL 4373327, at *9. Judge Rakoff rejected this argument, reasoning that "the cure or repurchase period ends 90 days after defendants learned of the loan breaches . . . and that time period has long since expired." *Id.*; *see also Syncora*, 2011 WL 1135007, at *4, *7 (allowing plaintiff to use sampling). Similarly here, Countrywide has known of the loan breaches for *years*, far longer than the 90 days within which it may cure such loans. *See, e.g.,* Holland Aff. Exs. 40-41, § 2.04(b); *see also id.* Exs. 42-48, § 2.04(d); *id.* Exs. 49-54, § 2.03(f). Countrywide cannot be heard to argue that it was denied its right to cure because it ignored the pervasive breaches which MBIA first brought to its attention more than four years ago, and because it also ignored the substantial evidence of such breaches, which it had in its own possession for an even longer period.

2. The Transaction Documents Provide That Countrywide Must Repurchase Defective Loans Upon "Becoming Aware Of" Such Loans And Need Not Await A Particularized Demand

As noted above, under the Transaction Documents, CHL is required to repurchase defective loans within 90 days of "becoming aware of" or "discovery" of such loans. There is no requirement that CHL receive notice of defective loans *from MBIA* to trigger its repurchase obligation, nor that MBIA make particularized repurchase demands for each such loan. CUF ¶ 118-121.[34] Thus, contrary to Countrywide's argument that MBIA cannot seek repurchase of

[34] Other provisions confirm that Countrywide need *not* receive particularized notice of each defective loan, providing that: "The cure for any breach of a representation and warranty relating to the characteristics of the Mortgage Loans in the related Loan Group in the aggregate shall be a repurchase of or substitution for only the Mortgage Loans necessary to cause the characteristics to comply with the related representation and warranty." *See, e.g.,* Holland Aff. Ex. 46, § 2.04(d); *see also id.* Exs. 40-41, § 2.04(b); *id.* Exs. 42-45, 47-48, § 2.04(d). This provision contemplates the use of repurchase as a pool-wide remedy, based not on defects identified in individual loans but rather on "the characteristics of the [loans] in the aggregate." If identification of defects on a loan-by-loan basis were required, this provision would have no meaning.

any loans other than the loans for which it has provided particularized notice (CW Mem. 36-37), MBIA is entitled to seek repurchase of all defective loans of which Countrywide has become aware—which in practice means all defective loans.[35]

Specifically, Countrywide has been aware since at least 2008, when MBIA filed its original Complaint, that MBIA's reunderwriting review found defects in approximately *90%* of the loans reviewed in the Securitizations. Sheth Aff. Ex. 1349, ¶ 68; *id.* Ex. 1, ¶ 80; CUF ¶ 136. In addition, Countrywide has had possession of the loan files for all of the loans underlying its Securitizations since it originated them, and it has elaborate systems for monitoring the performance and likelihood of delinquency for each of these loans. Sheth Aff. Ex. 20, at 577:3-21. Moreover, Countrywide maintains a "Loan Auditor" database, tracking instances in which Countrywide's Corporate Quality Control found a loan file to be "severely unsatisfactory," Sheth Aff. Ex. 162, and a "FACTS" database, tracking instances in which Countrywide suspected or confirmed fraud in its own origination and underwriting. *Id.* Ex. 163. Thus, while Countrywide may assert that it was not aware of the defects disclosed by the loan files, its access to those files at a minimum would allow reasonable jurors to find that Countrywide can be charged with actual knowledge of the defects those loan files disclose. *See 81 N.Y. Jur. 2d Notice and Notices*, § 4 ("Actual notice is a question of fact, and is open to every species of legitimate evidence which may tend to strengthen or impair the conclusion. Thus, the fact of notice or knowledge need not be established by direct evidence, but may be inferred from circumstances. Where there is conflicting evidence as to whether a person had notice, the issue is one for the jury.").

Even if Countrywide was not *in fact* aware of these defects, it can still be charged with constructive notice, which is also a question of fact. *See Bierzynski v. New York Cent. R.R. Co.*, 31 A.D.2d 294, 297 (4th Dep't 1969), *aff'd sub nom. Bierzynski v. New York Cent. R.R. Co.*, 29 N.Y.2d 804 (1971) ("Constructive notice . . . exists whenever it is shown that reasonable

[35] Countrywide also ignores that MBIA's re-underwriting expert, Mr. Butler, has specifically identified approximately 2,600 additional defective loans in his rebuttal expert report. Sheth Aff. Ex. 84, at 50; CUF ¶ 136.

diligence would have produced actual notice."); *Metro. Life Ins. Co. v. Morris,* 124 A.D.2d 568, 570-71 (2d Dep't 1986) (similar).

3. Even If Particularized Repurchase Requests Could Be Required In The Abstract, They Should Not Be Required Here Because Past Requests Have Been Futile

In *Syncora v. EMC,* Judge Crotty cited futility in support of his decision allowing EMC to seek repurchase on a pool-wide basis:

> The futility of applying an individualized remedy to allegedly widespread misrepresentations is evident in the fact that, of the 1,300 loans actually submitted under the repurchase protocol, EMC has remedied only 20. This .015% success rate does not bode well for the efficiency of employing the repurchase protocol for a generalized claim of breach.

2011 WL 1135007, at *6. Similarly here, Countrywide has repurchased only approximately 4.5% of the more than 13,000 loans MBIA has put back. Countrywide cannot simultaneously require MBIA to provide particularized notice of defects for all loans and then stonewall those notices by repurchasing a mere fraction of these loans—including loans that Countrywide has itself classified as "SUS," or "severely unsatisfactory." Indeed, Countrywide's refusal to comply with its obligations has been so flagrant that it not only mandates denial of Countrywide's motion, but it also constitutes anticipatory breach of these obligations and justifies summary judgment *for MBIA* on this issue. *See* MBIA SJ Mem. 40-44.[36]

III. COUNTRYWIDE IS NOT ENTITLED TO SUMMARY JUDGMENT ON MBIA'S CLAIM FOR INDEMNIFICATION

MBIA does not contest that summary judgment is warranted on MBIA's indemnification claim to the extent it is based on § 3.04 of the Insurance Agreements. To the extent the claim is based on § 3.03, however, it should be sustained. Section 3.03(c) provides:

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[36] Countrywide's argument (CW Mem. 37) that the Court should grant summary judgment on MBIA's repurchase claims relating to loans that are still performing is addressed in MBIA's motion for summary judgment. MBIA SJ Mem. 8-14. MBIA merely notes here that Judge Rakoff's recent decision in *Assured v. Flagstar* further supports MBIA's motion on this point. Judge Rakoff, following *Syncora v. EMC*, held that materially identical repurchase provisions to those here "did not require the plaintiff to show that the breaches caused the loans to default, but only that the breaches 'materially increased' plaintiff's risk of loss." 2012 WL 4373327, at *4.

> [T]he Sponsor agree[s] to pay to the Insurer . . . any and all reasonable charges, fees, costs and expenses that the Insurer may reasonably pay or incur, including, but not limited to, *reasonable attorneys' and accountants' fees and expenses*, in connection with . . . (ii) the *enforcement . . . by the Insurer of any rights in respect of any of the Transaction Documents, including without limitation, instituting . . . or participating in any litigation proceeding . . . relating to any of the Transaction Documents . . .*

Holland Aff. Exs. 57-71, § 3.03(c) (emphasis added). This provision contemplates payment by the "Sponsor" (*i.e.*, CHL) of fees and costs incurred by the "Insurer" (*i.e.*, MBIA) to enforce its "rights in respect of ... the Transaction Documents, including ... [by] instituting ... any litigation proceeding ... relating to any of the Transaction Documents." Plainly, MBIA's action against CHL for breach of its representations and warranties "relat[es] to ... the Transaction Documents." It is therefore "unmistakably clear" that Section 3.03(c) applies. *Hooper Assocs., Ltd. v. AGS Computers, Inc.*, 74 N.Y.2d 487, 492 (1989). Thus, summary judgment is improper.

IV. COUNTRYWIDE IS NOT ENTITLED TO SUMMARY JUDGMENT ON MBIA'S CONTRACT CLAIM FOR BREACH OF CHL'S AND CHLS' SERVICING OBLIGATIONS

MBIA has adduced ample evidence to survive summary judgment on its claim arising from CHL's and CHLS' failure to service the Mortgage Loans in accordance with prudent and customary standards of servicing. *First*, Countrywide unpersuasively accuses MBIA's servicing expert, Mr. Butler, of rendering conclusory opinions. In fact, Mr. Butler and his team reviewed over a million pages of documents, including the payment histories and collection notes for hundreds of mortgage loans in a random sample, before determining that CHL and CHLS failed to service over 45% of the loans in accordance with industry standards. CUF ¶ 168. *Second*, Countrywide's assertion that Mr. Butler ignored certain servicing documents produced in discovery and key contractual provisions goes to the weight of Mr. Butler's testimony, not its admissibility. *Third*, Countrywide's claim that it is liable only for "gross negligence" in the performance of its servicing duties rests on an incorrect reading of the Transaction Documents.

A. There Is Substantial Evidence That CHL and CHLS Breached Their Contractual Servicing Obligations

Countrywide's servicing deficiencies were so severe that Angelo Mozilo, Countrywide's CEO, stated: "I am receiving an enormous amount of complaints from customers who have

become so frustrated with either the complete lack of response or inadequate response from our customer service department as well as from other areas of our servicing division . . . It is clear to me that over the past several years a tolerance for mediocrity and ineptitude has been permitted to creep into our system." Sheth Aff, Ex. 228, at CWMBIA0013052613; *see also id.* Ex. 351 (in March 2012, nation's five largest mortgage servicers, including Bank of America, entered $25 billion agreement to address "mortgage loan servicing and foreclosure abuses"); CUF ¶ 158. These inadequacies permeated the loans in the Securitizations to the point where even Countrywide's purported servicing expert, Barry Bier, conceded that 5% of the loans in the Servicing Sample were serviced in breach of its servicing obligations. *See* CW Mem. 41. This admission is, by itself, sufficient evidence to deny Countrywide's motion for summary judgment on the servicing claims, as even under Countrywide's servicing expert's figures, Countrywide's servicing deficiencies damaged MBIA on approximately $150 million worth of loans in the Securitizations. *See* Affidavit of Dr. Charles D. Cowan in Opp'n to Countrywide's Motion for Summary Judgment.

In addition to Mr. Bier's admission, Mr. Butler's servicing report sets forth the industry standards for servicing second lien mortgages and details numerous servicing violations by Countrywide. *See* Sheth Aff. Exs. 81-83. Mr. Butler concluded that "Countrywide's servicing practices were far below the industry standard of proper servicing on nearly half of the mortgage loans reviewed as part of the servicing review." Sheth Aff. Ex. 81, at 52. Mr. Butler's opinions and findings are based on his experience and substantial evidence produced in discovery, including industry publications, servicing guidelines, servicing files and records, and testimony from Countrywide witnesses. *Id.* Ex. 82 (list of materials relied upon). Countrywide is free to argue to the jury that his opinion should be rejected, but there is simply no basis to grant summary judgment on this record.[37]

[37] Countrywide's cited cases (CW Mem. 41-42) are inapposite because the plaintiffs' experts lacked any support connecting the plaintiff's injury to the defendant's conduct. *See Wright v. New York City Hous. Auth*, 624 N.Y.S.2d 144 (1st Dep't 1995) ("there is no evidence from which to conclude that the deceased, on the night in question, did,

B. Mr. Butler's Inability To Consider Certain Documents Produced By Countrywide In An Unusable Format Goes To The Weight, Not Admissibility, Of His Opinion

Despite the substantial evidence considered by Mr. Butler in reaching his conclusions, Countrywide argues that Mr. Butler's report should be stricken because he did not consider servicing records from Countrywide's subservicing portal. Countrywide's argument is unavailing for three reasons.

First, Countrywide itself is to blame for Mr. Butler's failure to consider the additional documents. The subservicing documents Countrywide contends Mr. Butler failed to consider are thousands of pages of printouts from Countrywide's subservicing website that Countrywide produced to MBIA just weeks before the Butler Servicing Report was initially due. Not only were the printouts frequently illegible, they failed to comply with the E-Discovery Order requiring Countrywide to (i) provide the documents in a text searchable format with identifying metadata and (ii) produce the "native" electronic versions of the documents. *See* Sheth Aff, Ex. 339, at 1-2.[38] These deficiencies prevented Mr. Butler from searching or sorting documents according to a particular loan number. *Id.* Ex. 59, at 693:19-694:15; 696:25-697:4; 705:3-7; 824:5-7; 828:13-21; 842:11-843:18; 846:13-16; *see also* MBIA's Opp'n to Countrywide's Motion to Strike the Expert Servicing Report of Mr. Butler, dated Oct. 19, 2012.

Second, because Countrywide is the summary-judgment movant, Countrywide has the burden of marshalling *affirmative* evidence sufficient to establish that it did not breach its servicing obligations. *See Torres v. Indus. Container*, 305 A.D.2d 136 (1st Dep't 2003) ("appellant must adduce affirmative evidence" that it is not liable). It is not enough for Countrywide to point to gaps in MBIA's proof. *See Torres v. Merrill Lynch Purchasing*, 945 N.Y.S.2d 78, 79 (1st Dep't 2012) (summary judgment was "properly denied because [defendants] merely pointed to gaps in plaintiff's proof instead of carrying their burdens on their

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in fact, take the elevator"); *Robertson v. New York City Hous. Auth.*, 871 N.Y.S.2d 141 (1st Dep't 2009) (plaintiff adduced no evidence that building conditions had caused her injury).

[38] *See also* Sheth Aff, Ex. 340.

motions"). Countrywide has failed to meet its burden because it has not shown that the documents Mr. Butler purportedly failed to consider are material to *every aspect* of his servicing report such that the *entire* report should be excluded. This is particularly true with respect to Mr. Butler's loan-level servicing findings, which detailed, for each loan in the servicing sample, his rationales. *See* Sheth Aff. Ex. 83. Mr. Butler testified that the additional documents are unlikely to affect his overall conclusions. *See id.* Ex. 59, at 951:9-952:22; 705:19-706:3.

Third, and in any event, Mr. Butler's purported failure to review these documents goes to the weight, not the admissibility, of his testimony. *See Schlansky v. Augustus V. Riegel, Inc.*, 9 N.Y.2d 493, 497 (1961) ("the expert's qualifications were established and . . . his lack of further information affected the weight but not the admissibility of his evidence"); *Latour v. Hayner Hoyt Corp.*, 788 N.Y.S.2d 529, 530 (4th Dep't 2004) (similar).[39]

C. The Transaction Documents Do Not Limit CHL's And CHLS' Liability To Only Gross Negligence

The Transaction Documents refute Countrywide's attempt to limit its servicing liability to "gross negligence." Although the SSA could be read to limit Countrywide's liability to gross negligence for lawsuits brought by the Trust, the Owner Trustee, the Transferor, and the Noteholder, there is no such limitation on *MBIA as the Credit Enhancer*. Section 5.03 provides:

> Neither the Master Servicer nor any of its directors, officers, employees, or agents is liable to the *Trust, the Owner Trustee, the Transferor, or the Noteholders* for the Master Servicer's taking any action or refraining from taking any action in good faith pursuant to this Agreement, or for errors in judgment. This provision shall not protect the Master Servicer or any of its directors, officers, employees, or agents against any liability that would otherwise be imposed for misfeasance, bad faith, or gross negligence in the performance of the duties of the Master Servicer or for reckless disregard of the obligations of the Master Servicer.

[39] Just as Countrywide incorrectly criticizes Mr. Butler for not considering certain servicing records, it wrongly asserts that Mr. Butler "failed to consider key contractual provisions governing Countrywide's servicing obligations." (CW Mem. 41). The Transaction Documents require Countrywide to service the loans in accordance with industry practice and that was the focus of Mr. Butler's analysis. *See* Sheth Aff. Ex. 81, at 12-14; *id.* Ex. 59, at 792:23-793:4; CUF ¶ 172.

Holland Aff. Ex. 47, § 5.03 (emphasis added).[40] By contrast many other sections of the SSA contain explicit references to the Credit Enhancer.[41] Accordingly, MBIA need show only that Countrywide was negligent in its performing its servicing duties.

V. COUNTRYWIDE IS NOT ENTITLED TO SUMMARY JUDGMENT ON MBIA'S PRAYER FOR PUNITIVE DAMAGES

This Court should deny Countrywide's motion for summary judgment on MBIA's prayer for punitive damages so that the fact-finder may determine, after trial, whether Countrywide's fraud was sufficiently morally culpable to merit such damages.

Punitive damages are appropriate where "the fraud, aimed at the public generally, is gross and involves high moral culpability." *Walker v. Sheldon*, 10 N.Y.2d 401, 405 (1961); *see also New York Univ. v. Continental Ins. Co.*, 87 N.Y.2d 308, 315-16 (1995) (similar). In such cases, punitive damages deter "those who deliberately and coolly engage in a far-flung fraudulent scheme, systematically conducted for profit." *Walker*, 10 N.Y.2d at 406. "Whether . . . conduct was so reprehensible as to warrant [punitive] damages is a question of fact to be determined at trial." *AT&T Info. Sys., Inc. v. McLean Bus. Servs., Inc.*, 175 A.D.2d 652, 653 (4th Dep't 1991); *MBIA Ins. Corp. v. Morgan Stanley*, Index No. 29951/2010, 2011 WL 2118336 (N.Y. Sup. Ct. Westchester Cnty. May 26, 2011) (same).

Here, ample evidence supports a punitive damages award. *First*, Countrywide's misconduct harmed many victims in addition to MBIA, as shown by the many government investigations and complaints alleging that Countrywide engaged in fraudulent and deceptive

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[40] *See also* Holland Aff. Exs. 41-46, 48, § 5.03; *see also id.* Ex. 49, § 6.03 ("None of the Depositor, the Sellers, the NIM Insurer or the Master Servicer or any of the directors, officers, employees or agents of the Depositor, the Sellers, the NIM Insurer or the Master Servicer shall be under any liability to the Trustee (except as provided in Section 8.05), the Trust Fund or the Certificateholders for any action taken or for refraining from the taking of any action in good faith pursuant to this Agreement, or for errors in judgment"); *see also id.* Exs. 50-54, § 6.03.

[41] *See, e.g.*, Holland Aff. Ex. 47, § 2.01(b)(1) (" The Depositor shall notify the Owner Trustee, the Indenture Trustee, the *Credit Enhancer* . . ."); § 2.03 ("The Master Servicer represents and warrants to the Indenture Trustee and the *Credit Enhancer* that . . ."); § 2.04(f) (noting that a breach of the representations and warranties would obligate the Sponsor to pay "the amount of any loss or expense incurred by the Transferor, the Noteholders, *the Credit Enhancer* . . ."); § 4.01 ("the Master Servicer shall deliver . . . to the Indenture Trustee, the Owner Trustee, the Sponsor, the Depositor, the Paying Agent, the *Credit Enhancer* . . .") (emphasis added in all).

practices that resulted in thousands of borrowers losing their homes through foreclosure,[42] investors losing the value of their investment in securities collateralized by such loans,[43] and insurers such as MBIA paying out billions of dollars in claims.[44] Given Countrywide's position as one of the largest originators in the United States, its massive fraud had a devastating impact on the economy; indeed, its large-scale abandonment of its underwriting standards contributed to the recent financial crisis.[45]

Second, Countrywide's fraudulent misrepresentations to MBIA were made as part of a carefully-orchestrated scheme encompassing much more than the MBIA-Countrywide transactions. The scheme involved originating massive volumes of loans to increase Countrywide's market share and profits, and then off-loading the credit risk associated with such loans through the securitization process. Sheth Aff., Ex. 335. CUF ¶¶ 322-55, 357-59, 364, 366-73. Countrywide deceived and defrauded each market participant at each step in the securitization chain.

Third, Countrywide's misconduct is particularly egregious because it was carried out with the blessing of Countrywide's most senior executives, who knew that the company was originating and approving significant numbers of loans that did not meet its underwriting guidelines and prudent and customary standards of underwriting, and the increased risks associated with these and other high-risk loans. *See, e.g.*, Sheth Aff. Ex. 296 (Mozilo: "I have personally observed a serious lack of compliance within our origination system as it relates to documentation and generally a deteriation [sic] in the quality of loans originated versus the

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[42] *See, e.g.*, Sheth Aff. Ex. 103, at ¶ 159 ("Due to Countrywide's lack of meaningful underwriting guidelines and risk-layering, Countrywide's deceptive sales tactics, Countrywide's high-pressure sales environment, and the complex nature of its Pay Option and Hybrid ARMs, a large number of Countrywide loans have ended in default and foreclosure, or are headed in that direction.").

[43] *See, e.g.*, Sheth Aff. Ex. 106, at ¶ 260 (describing "billions of dollars in damages" from purchase of securities backed by Countrywide mortgages.).

[44] *See, e.g.*, Sheth Aff. Ex. 177 ¶ 8 (stating MBIA has paid out "well in excess of $2 billion in claims"); *id.* Ex. 90, at 15, Table 1 (showing MBIA net losses to date of $3.14 billion).

[45] *See, e.g.*, Sheth Aff. Ex. 178, at 231 (failed mortgage lenders like Countrywide "contributed to the systemic risk that damaged the U.S. banking system, U.S. financial markets, and the U.S. economy as a whole.").

pricing of those loan [sic]."); *see id.* Ex. 63, at 200:20-201:23 ("[W]e're the largest lender in America. So decisions we make, you know, potentially impact a lot of people because we touch a lot of people. . . . [T]he more people you have defaulting in a neighborhood, the worse it is for the rest of the neighborhood."). CUF ¶¶ 323-24, 351.[46] Not only did Countrywide's senior executives actively encourage such fraudulent origination and underwriting practices in an effort to meet the company's stated goal to achieve 30% market share, Sheth Aff. Ex. 103, at ¶20, they squelched any efforts to stop such practices by terminating any employees who tried to put an end to such practices, *see supra*, at 5; CUF ¶¶ 357-65, 341-44, 347-48, 35-51, 355, 366.[47]

CONCLUSION

This Court should deny Countrywide's motion for summary judgment in its entirety.

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Respectfully submitted,

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[46] *Camillo v. Geer*, 185 A.D.2d 192, 193 (1st Dep't 1992) (cited at CW Mem. 43), involved low-level employees.

[47] Countrywide relies on inapposite cases where prayers for punitive damages were dismissed at the pleading stage and where there was no evidence that the defendant, as part of a broader scheme, defrauded and directly harmed the general public by originating risky loans to borrowers who lacked the ability to repay. *See* CW Mem. 42-44 (citing *CIFG Assur. North America, Inc. v. Goldman, Sachs & Co.*, 2012 WL 1562718 (Trial Order, May 1, 2012); *HSH Nordbank AG v. UBS AG*, 941 N.Y.S.2d 59 (1st Dep't 2012); *Mountain Creek Acquisition v. Intrawest US Holdings*, 96 A.D.3d 633 (1st Dep't 2012)).