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

FINANCIAL GUARANTY INSURANCE COMPANY,	Mot. Seq. 001
Plaintiff,	Index No. 652914/2014
- against -	Justice Friedman
MORGAN STANLEY ABS CAPITAL I INC., MORGAN STANLEY MORTGAGE CAPITAL HOLDINGS LLC, MORGAN STANLEY & CO., INC., MORGAN STANLEY, and SAXON MORTGAGE SERVICES, INC.	Part 60
Defendants.	

PLAINTIFF'S MEMORANDUM OF LAW IN OPPOSITION TO MOTION TO DISMISS

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PRELIMINARY STATEMENT

Morgan Stanley's motion to dismiss largely re-treads on issues already resolved by the First Department and this Court, and should be summarily denied.[1] Morgan Stanley's arguments would produce the incredible result that FGIC would ***never*** be entitled to seek damages for Morgan Stanley's breaches and misrepresentations. Morgan Stanley inconsistently asserts that FGIC may not seek damages for claim payments it has yet to make, even though the claim for principal shortfalls is not due to be paid until the maturity date in 2037, ***and*** that FGIC will then be barred from the courthouse by a statute of limitations that runs six years from the 2007 closing. Morgan Stanley's remarkable contention that it is effectively immune from suit is meritless. FGIC's claims are well-pleaded and the case should proceed without delay.

Morgan Stanley's absurd argument—that FGIC's claim for damages can be made only after it pays policy claims—relies on four invalid assertions. First, Morgan Stanley misreads a fragment of the Insurance Agreement to bar FGIC from recovering what it erroneously terms "future damages." But as one would expect, the provision Morgan Stanley cites plainly allows FGIC to sue upon Morgan Stanley's breach. Second, Morgan Stanley construes the First Department's decision in *MBIA v. Countrywide* to preclude an insurer from recovering future claim payments as damages. But the First Department held the opposite. Third, Morgan Stanley claims, based on *Assured v. Flagstar*, that FGIC's damages are too "speculative." But there, Judge Rakoff awarded analogous damages at trial, and did not prematurely deny relief on a motion to dismiss. Fourth, Morgan Stanley misapplies the "out-of-pocket rule." This rule allows damages for the actual harm incurred, which is exactly what FGIC seeks.

Morgan Stanley next asserts that the sole remedy for ***all*** FGIC's contract claims is the

[1] Capitalized terms not otherwise defined herein have the meaning ascribed in the Complaint ("Comp."), dated September 23, 2014, NYSCEF Doc. No. 2. *See, e.g.*, Comp. ¶ 30 n. 3 (defining "Morgan Stanley").

contractual Repurchase Protocol, implying that all such claims are essentially identical. They are not. Unlike the rulings in trustee actions that Morgan Stanley cites, whether the Repurchase Protocol is the "sole remedy" for an insurer's claims turns on the terms of the governing ***insurance agreement***. The Repurchase Protocol, however, is the "sole remedy" for breaches of warranties ***pertaining to individual mortgage loans***; it does not apply to FGIC's other claims, which do not pertain to individual loans and are not remediable by the loan-specific Repurchase Protocol, and for which FGIC is entitled to the alternative remedies afforded by the plain language of the Insurance Agreement and New York Insurance Law.

Finally, Morgan Stanley makes several arguments that appear to be place holders should the Court of Appeals elect to reverse established law. Contrary to numerous rulings, Morgan Stanley asserts that FGIC cannot recover for breaches for which Morgan Stanley had constructive or inquiry notice; that FGIC cannot bring a fraudulent inducement claim based upon misrepresentations incorporated into the contractual warranties; and that FGIC is not entitled to reimbursement of attorneys' fees expressly allowed by the Insurance Agreement. Morgan Stanley's motion should be denied in its entirety.

FACTS

The facts recited herein are drawn from the allegations of the Complaint, which are incorporated by reference and must be taken as true for the purposes of this motion.

A. The Morgan Stanley and New Century "Partnership"

Morgan Stanley is an investment bank that was among the most prolific sponsors of the securitization transactions that led to the 2008 financial crisis. Morgan Stanley's primary source of loans for its securitizations was New Century, a lender now known to have systematically made loans to borrowers who could not afford to pay. (Comp. ¶¶ 33-34, 177-96.) Through its warehouse lending facilities, Morgan Stanley provided billions of dollars to New Century to fund such loans. Morgan Stanley then acquired those loans, sold them into securitization trusts it created, and underwrote the issuance and sale of securities, whose terms it determined, that were backed by the defective loans. (*Id*. ¶ 32.)

In connection with its warehouse lending and securitization, Morgan Stanley conducted due diligence of New Century's origination practices and underwriting guidelines, and the New Century Loans. As the Massachusetts Attorney General concluded in 2010, Morgan Stanley knew from its due diligence that New Century routinely disregarded its own guidelines and made loans to borrowers with no reasonable ability to repay. (*Id*. ¶ 198, n.23.)[2]

B. Morgan Stanley Administers the Disposition of New Century Loans

By early 2007, New Century was engulfed in scandals and criminal investigations. (Comp. ¶ 34.) Seeking to limit its own exposure, in March 2007, Morgan Stanley shut down the credit lines it had extended to New Century. (*Id.*) New Century entered bankruptcy on April 2, 2007. (*Id.*) Morgan Stanley quickly stepped in to act as the administrator of an auction of New Century loans. (*Id*. ¶ 35.) Indeed, pursuant to a stipulated bankruptcy order, Morgan Stanley assembled due diligence materials and data for potential bidders. (*Id.*)

Seeking to recoup some of its losses, and leveraging its unique knowledge, Morgan Stanley submitted, in the auction it administered, a winning bid to acquire the New Century loans for a final round of securitizations. (Comp. ¶ 35.) Morgan Stanley also took over the servicing of the New Century loans, securing full knowledge of, access to and control over the loans. (*Id.* ¶ 36.) Morgan Stanley then sought to securitize the loans. (*Id.* ¶ 37.) Because of the publicity surrounding New Century, however, Morgan Stanley knew it would need financial guaranty insurance to make the transactions marketable. (*Id.* ¶ 38.)

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[2] The Complaint cites the Assurance of Discontinuance, available at http://www.mass.gov/ago/news-and-updates/press-releases/2010/attorney-general-martha-coakley-reaches-102.html.

C. Morgan Stanley Fraudulently Induces FGIC into the Insurance Agreement

Morgan Stanley misrepresented New Century's underwriting and loans, and importantly, Morgan Stanley's business practices and due diligence processes, in order to induce FGIC to participate in the Transaction. Specifically, in the months before closing, Morgan Stanley Vice President Steven Shapiro engaged in multiple discussions with FGIC, representing that Morgan Stanley had conducted extensive due diligence of New Century, its guidelines and its loans in connection with its role as a warehouse lender (Comp. ¶¶ 39, 44); that additional due diligence had been undertaken in connection with the Mortgage Loans acquired through the bankruptcy process (*id.* ¶ 45); and that Morgan Stanley had "cherry-picked" the Mortgage Loans for the proposed securitization, after reviewing approximately 50% of the loans. (*Id.* ¶ 44.)

Morgan Stanley reinforced Mr. Shapiro's representations by furnishing documentation relating to the Mortgage Loans and the represented operations before closing. For example, Morgan Stanley provided mortgage loan tapes and "strats" with detailed data disclosures pertaining to the Mortgage Loans (*id.* ¶¶ 51-55); "shadow ratings" it secured through its disclosures, which purported to show the credit quality of the securities (without insurance coverage) (*id.* ¶¶ 61-63); and draft offering documents describing the New Century guidelines and Morgan Stanley's purported due diligence and business practices (*id*. ¶¶ 56-60.)

Finally, Morgan Stanley agreed to provide warranties attesting to the veracity of its representations and of the information it had furnished concerning the Mortgage Loans, New Century's underwriting, and Morgan Stanley's operations. (*Id*. ¶¶ 42-43.) Morgan Stanley's material representations induced FGIC to enter into the Insurance Agreement, dated June 20, 2007, and to issue to the Trust its irrevocable Policy guaranteeing the payment of amounts due to the holders of Class A Certificates issued in the MSAC 2007-NC4 Transaction. (*Id.* ¶¶ 72, 79.)

D. Morgan Stanley Grants FGIC Two Types of Warranties

Morgan Stanley made two types of warranties. The first type—Loan Warranties—concerned the attributes of each individual Mortgage Loan. (Comp. ¶¶ 80, 90.) Morgan Stanley made the Loan Warranties as Sponsor in the R&W Agreement, and re-conveyed them in its role as Depositor to the Trust. (*Id*. ¶¶ 75-76.) Morgan Stanley restated the Loan Warranties (but not the sole remedy clause) for FGIC's benefit the Insurance Agreement, Section 2.01(n).[3] (*Id*. ¶ 90.)

Separately, Morgan Stanley granted ***only*** to FGIC and ***only*** in the Insurance Agreement certain warranties that concern the transaction as a whole—the Transaction Warranties. (*Id.* ¶ 80.) Significantly, the Transaction Warranties attest that information Morgan Stanley furnished to FGIC before closing and the representations it made in the Offering Documents were not false or misleading. (*Id.* ¶¶ 81-88.) The Transaction Warranties thus encompass Morgan Stanley's representations about its operations, and the practices and protocols it purportedly implemented to ensure the quality of the Mortgage Pool. (*Id.*)

E. Morgan Stanley Grants FGIC Incremental Remedies

In the R&W Agreement, at Section 4(a), Morgan Stanley covenanted to repurchase any Mortgage Loan within 60 days of discovering or receiving notice of a breach (the "Repurchase Protocol"). (Comp. ¶ 94.) Morgan Stanley also granted FGIC in the Insurance Agreement additional covenants and remedies not available to other Transaction participants. <u>First</u>, Morgan Stanley agreed that a breach of a Transaction Warranty that did ***not*** pertain to individual loans would be an Event of Default under Section 5.01(a). (*Id*. ¶ 89.) <u>Second</u>, Morgan Stanley agreed, in Section 5.01(d), that a breach of the Repurchase Protocol—as a covenant made by Morgan Stanley in the Operative Documents— would also be an Event of Default. (Insurance

[3] In addition to being a direct grantee of the Loan Warranties, FGIC is an express third-party beneficiary of the R&W Agreement, as well as the other Operative Documents. (¶ 90, n.10, 11.)

Agreement at 32, Doc. 14.) Third, Morgan Stanley agreed, in section 5.02(a)(iii), that FGIC could redress any Event of Default by taking "whatever action at law or in equity as may appear necessary or desirable in its judgment." (*Id.* at 33). Finally, Morgan Stanley agreed in Section 3.03(d) to reimburse FGIC for "any and all charges, fees, costs and expenses . . . including reasonable ***attorneys' and accountants' fees and expenses***," for any litigation to enforce its rights under the Operative Documents, such as the instant matter. (*Id.* at 24).

F. Morgan Stanley Breaches Its Warranties and Frustrates the Repurchase Protocol

After losses on the Transaction began to mount, FGIC retained consultants to review the Mortgage Loans, finding defects in every one of the approximately 800 non-performing Mortgage Loans they reviewed. (Comp. ¶¶ 95, 106.) FGIC demanded that Morgan Stanley repurchase those breaching loans. (*Id.* ¶ 106.) Similarly, Deutsche Bank and Freddie Mac, as the Trustee and a certificate owner, respectively, gave notice of breaches and demanded repurchase of 441 Mortgage Loans. (*Id.* ¶¶ 108-11.) This evidence of pervasive breaches in the Mortgage Pool belies Morgan Stanley's representations concerning its operations and the protocols it purportedly implemented to ensure the quality of the Mortgage Pool. (*Id.* ¶ 40.)

Equally egregious was Morgan Stanley's failure to comply with the Repurchase Protocol. Of the 1,214 Mortgage Loans submitted for repurchase, Morgan Stanley has repurchased just 6, without legitimate reason for failing to repurchase the remainder. (*Id.* ¶¶ 107, 110.)

As of August 2014, total losses on the Mortgage Loans exceeded $493 million, representing roughly 47% of the original pool balance. (*Id.* ¶ 202.) These losses have caused severe shortfalls in the amounts available to pay holders of Insured Securities, and expected future losses on the Mortgage Loans will cause further increased shortfalls. Under its Policy, FGIC is liable for these existing and expected future shortfalls, which will inevitably result in hundreds of millions of dollars in claims against FGIC. (*Id.* ¶¶ 202-03.)

G. The Trustee Files Suit

On January 23, 2015, the Trustee filed a complaint against Morgan Stanley. The Trustee's claims are generally consistent with and support FGIC's claims.

ARGUMENT

The inquiry on a motion to dismiss is narrow. The court must "accept the facts alleged as true … and determine simply whether the facts alleged fit within any cognizable legal theory." The complaint must be construed "liberally" and the court must accept as true not only "the complaint's material allegations" but also "whatever can be reasonably inferred there from" in favor of the pleader. *P.T. Bank Cent. Asia v. ABN Amro Bank N.V.*, 301 A.D.2d 373, 375-76 (1st Dep't 2003) (internal citations omitted). Morgan Stanley's motion fails under this standard.

I. There is No Basis for Limiting FGIC's Damages Claims at the Pleading Stage

Morgan Stanley inflicted severe harm on FGIC at the close of the Transaction, which was induced by fraud and marked by breaches of warranties, and thereafter by refusing to comply with its repurchase obligations. The harm is readily determinable; hundreds of millions in existing shortfalls will inevitably produce hundreds of millions in claims under FGIC's Policy, and further claims resulting from future shortfalls can be estimated using accepted modeling techniques. *See Assured Guar. Mun. Corp. v. Flagstar Bank, FSB,* 920 F. Supp. 2d 475, 514-515 (S.D.N.Y. 2013). FGIC's damages claims may proceed, particularly at the pleading stage. *Black v. Chittenden*, 69 N.Y.2d 665, 668 (1986) (there is no requirement "that the measure of damages be pleaded, 'so long as there are facts alleged from which damages may properly be inferred'") (internal citations omitted).[4] *See also Wathne Imports, Ltd. v. PRL USA, Inc.*, 101 A.D.3d 83, 89 (1st Dep't 2012) ("Where the existence of damages is certain, and the only uncertainty is as to its amount, the plaintiff will not be denied recovery of substantial damages . . . .").

Disregarding this precedent, Morgan Stanley advances four flawed theories to argue that FGIC improperly seeks what Morgan Stanley terms "future damages." Morgan Stanley misreads the Insurance Agreement to conjure up a limitation on damages where there is none. It interprets two lines of authority—concerning "rescissory damages" and the "out-of-pocket rule"—to preclude damages based upon financial projections, which is not remotely what the decisions hold. And Morgan Stanley argues that FGIC's damages are unduly "speculative" based on cases that both disprove its point and underscore the premature nature of its request.

Laid bare, Morgan Stanley's positions are absurd: it simultaneously asserts that (a) the six-year statute of limitations bars FGIC from suing ***after 2013*** because its claim arose at closing (Mem. of Law in Supp. of Defs.' Mot. to Dismiss Pl's. Compl. ("MS Br.") at 16 n.6.),[5] and (b) FGIC cannot maintain a claim for the bulk of its damages ***before 2037***, when the principal payment is due. Morgan Stanley argues that FGIC's action is both too early and too late, effectively immunizing Morgan Stanley from suit. This reasoning should be rejected.[6]

A. Morgan Stanley Misconstrues the Insurance Agreement

Morgan Stanley begins by misreading the Insurance Agreement to bar suit by FGIC for

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[4] *See also A.S. Rampel, Inc. v. Hyster Co.*, 3 N.Y.2d 369, 383 (1957) ("There is no requirement that the measure of damages be stated in the complaint so long as facts are alleged from which damages may properly be inferred.")

[5] The six year statute of limitations was extended by a tolling agreement to 2014.

[6] Interpreting the agreement to preclude FGIC from having any claim for breach of warranty would be an absurd and commercially unreasonable result. *See Lipper Holdings, LLC v. Trident Holdings, LLC*, 1 A.D.3d 170, 171 (1st Dep't 2003) (citations omitted) ("A contract should not be interpreted to produce a result that is absurd, commercially unreasonable or contrary to the reasonable expectations of the parties.").

"future damages." (MS Br. at 7.) A full reading of the provision, Section 5.02(a)(iii), states that upon an Event of Default, which Morgan Stanley concedes, FGIC may:

> take whatever action at law or in equity as may appear necessary or desirable in its judgment to collect the amounts, if any, ***then due*** under this Insurance Agreement or any other Operative Document or to enforce performance and observance of any obligation, agreement or covenant of the Servicer, the Sponsor or the Depositor under this Insurance Agreement or other Operative Documents.

(Insurance Agreement at 33, NYSCEF Doc. 14 (emphasis added).) Morgan Stanley suggests the term "then due" limits FGIC's recovery to claim payments already made, thus precluding suit before 2037. But the term "then due" plainly refers to amounts *owed by Morgan Stanley* under "any" Operative Document, *e.g.*, the Repurchase Price that Morgan Stanley must pay under the Repurchase Protocol, or damages for Morgan Stanley's breaches of its Transaction Warranties.

The remainder of this provision entitles FGIC to bring suit "to enforce performance and observance of any obligation, agreement or covenant" of Morgan Stanley. This plainly allows FGIC to enforce, *inter alia*, Morgan Stanley's contractual obligation to repurchase breaching loans, regardless of whether, or if, any claim payments are made.

Finally, the Insurance Agreement affords multiple alternative remedies for Morgan Stanley's breaches. In Section 5.02(b), the parties made clear that "no remedy herein conferred or reserved 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 this Insurance Agreement, the other Operative Documents ***or existing at law or in equity***." (emphasis added.) This language affords FGIC the broadest rights to seek recourse, imposing no restriction on damages.

B. Morgan Stanley Misapplies Decisions Addressing Equitable Relief

Finding no valid limitation on FGIC's damages in the Insurance Agreement, Morgan Stanley cites decisions addressing the availability of equitable damages, portraying them as precluding an award of "future" damages. Those are two separate issues. The availability of equitable rescissory damages turns on, *e.g.*, whether there are adequate legal damages. Whether legal damages are properly calculated based on projections, however, is a separate question addressed by a different line of authority (discussed in the following section). Either type of damages may (or may not) involve an analysis of amounts to be paid in the future.

Morgan Stanley contends that the First Department's decision in *MBIA v. Countrywide* bars the recovery of "future damages." (MS Br. at 8.) In fact, that decision addressed whether MBIA could recover equitable rescissory damages. The First Department held that equitable relief tantamount to rescission was unavailable, as MBIA had issued an irrevocable policy. 105 A.D.3d 412, 413 (1st Dep't 2013). But the court clarified that MBIA was entitled to recover its claim payments as legal damages under New York Insurance Law provisions governing material misrepresentations and breach of material warranties—Sections 3105 and 3106. *Id.* at 412. Indeed, the First Department rejected defendants' position that the insurer could not recover claim payments "without resort to rescission." *Id.*

Consistently, on remand, Justice Bransten construed this language as authorizing the recovery of claim payments as a form of compensatory damages. *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, No. 602825/2008, 2013 N.Y. Misc. LEXIS 1818, at *28 (Sup. Ct. N.Y. Cnty. Apr. 29, 2013) ("While rescissory damages are unavailing . . . nothing in the contract language cited above bars other forms of monetary damages, such as compensatory relief.") MBIA thus moved forward with its demand for claim payments.[7]

Also instructive are the two federal cases that the First Department cited in endorsing the

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[7] S*ee also Ins. Co. of N. Am. v. Kaplun*, 274 A.D.2d 293, 298 (2d Dep't 2000) ("An insurance carrier that is precluded from rescinding a policy retroactively due to fraud is not without means of redress. For example, if the insurer is required to pay benefits under the policy to a third party, it may bring an action against its insured to recover such losses.")

recovery of claim payments. First, in *Assured v. Flagstar*, Judge Rakoff awarded the financial guaranty insurer all of its claim payments, without relying on the concept of rescissory damages. *Assured Guar. Mun. Corp. v. Flagstar Bank, FSB*, No. 11 Civ. 2375, 2013 U.S. Dist. LEXIS 57126, at *2-3 (S.D.N.Y. Apr. 15, 2013). The court accepted Assured's expert evidence that, "had Flagstar repurchased the defective loans at issue in this case, Assured would be reimbursed for all claims it has paid in relation to the Trusts—and that there would have been a substantial 'cushion' in each Trust to protect against future claims Assured might have to pay." *Id.* Indeed, the court included ***in compensatory damages*** claim payments that had not been made at the pleading stage, which Morgan Stanley dubs "future" claim payments. *Id.* Second, in *Syncora v. EMC*, Judge Crotty concluded he had authority to award rescissory damages, but ruled that it was premature on summary judgment to decide whether legal damages were adequate to compensate the insurer for claim payments made and to be made. *Syncora Guar. Inc. v. EMC Mortg. Corp.*, 874 F. Supp. 2d 328, 340 (S.D.N.Y. 2012).

Ignoring these leading authorities, Morgan Stanley cites *Assured Guar. Mun. Corp. v. RBS Secs. Inc.*, No. 13 Civ. 2019, 2014 U.S. Dist. LEXIS 63811 (S.D.N.Y. May 8, 2014), incorrectly, for the proposition that future claim payments are never recoverable. In fact, the *Assured v. RBS* decision did not take issue with Justice Bransten's decision after remand in *MBIA v. Countrywide* that future damages may be sought on claims "for breaches of representations and warranties." 2014 U.S. Dist. LEXIS 63811, at *6. Rather, the court distinguished the case before it as one asserting only fraud claims. *Id.* Thus, even accepting the court's ruling, it supports FGIC's contract claims. But as applied to fraud claims, the court erred. As noted above, the governing First Department decision in *MBIA v. Countrywide* allowed recovery of claim payments for both breach of warranty and fraudulent inducement claims.

C. FGIC's Damage Claim is Not Unduly "Speculative"

Faced with controlling authority allowing the recovery of claim payments as legal damages, Morgan Stanley incorrectly asserts that New York law precludes as unduly speculative damages based on projected claim payments. (MS Br. at 8-9.) But Morgan Stanley's first case on this point observed that "[l]oss of future profits as damages"—which are necessarily based on future projections—"***have been permitted*** in New York under long-established and precise rules of law." *Kenford Co. v. Cnty. of Erie*, 67 N.Y.2d 257, 261 (1986) (emphasis added).[8] Indeed, "it is hardly novel in the law for damages to be projected into the future." *Van Wagner Adver. Corp. v. S&M Enter.*, 67 N.Y.2d 186, 194 (1986) (holding that damages should have been extended ***past the time of trial***). *See also Ashland Mgmt. Inc. v. Janien*, 82 N.Y.2d 395 (1993) (upholding damages award based on projections); *Wathne*, 10 A.D.3d 83 (reversing exclusion of expert projections at trial). As these authorities illustrate, it is common for experts to calculate damages based on projections in commercial disputes.[9] Thus, it is premature to determine now that FGIC cannot offer proof of its future claim payments as part of its compensatory damages.

The second case Morgan Stanley cites, *Assured v. Flagstar*, does not support its argument either. As discussed above, Judge Rakoff allowed an analogous claim to proceed to verdict. 2013 U.S. Dist. LEXIS 57126, at *2-3. Morgan Stanley cites the second post-verdict decision in

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[8] Notably, the *Kenford* decision issued ***after verdict***.

[9] The award of "future damages" is well-accepted in personal injury litigation. *See, e.g., Reed v. City of New York*, 304 A.D.2d 1 (1st Dep't 2003) (affirming substantial award of "future damages," including future expenses and lost earnings capacity, which was based on testimony of medical and economic experts). Additionally, CPLR 5041 expressly addresses how "future damages" are incorporated into a judgment after verdict. *See also Tractebel Energy Mktg., Inc. v. AEP Power Mktg., Inc.*, 487 F.3d 89, 112, n.26 (2d Cir. 2007) ("If it is true that projecting profits over twenty years is so absurdly speculative that economists can do no better than fortune tellers, it would have been imprudent for the parties to enter a contract for such a long period in the first place. ***The reality, however, is that long-term contracts are entered into regularly, and a degree of speculation is acceptable in the business community***.") (emphasis added).

that case, in which the court refused to enhance the award to encompass additional future claims. (MS Br. at 9.) What Morgan Stanley omits is that Judge Rakoff declined to do so because the damages model Assured's expert presented did not support such a recovery. 2013 U.S. Dist. LEXIS 57126, at *3. This decision did not address the legal availability of recovery for future claim payments, but rather the sufficiency of the proof presented at trial.

Finally, Morgan Stanley professes concern regarding the impact of a pending suit by the Trustee relating to this same Transaction. (MS Br. at 9.) There are steps that can be taken later in the litigation to avoid double recovery without denying FGIC all recovery.[10] For example, in *Assured v. Flagstar*, the court awarded the insurer damages, but ordered that if recoveries are greater than predicted, "Assured will be responsible for paying this money to Flagstar." 892 F. Supp. 2d 596, 606 (S.D.N.Y. 2012).

D. The "Out-of-Pocket Rule" Does Not Bar FGIC's Claims

Finally, Morgan Stanley argues that the "out-of-pocket rule" bars recovery for claims FGIC "expects it may pay in the future." (MS Br. at 10). That rule is supplanted here by the New York Insurance Law, which allows FGIC to recover its claim payments where a material misrepresentation was made to procure an insurance policy.[11] But regardless of the application

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[10] Morgan Stanley also cites *Ambac Assurance Corp. v. EMC Mortg. LLC*, 121 A.D.3d 514 (1st Dep't 2014), to suggest that it is tolerable for the insurer to have no remedy as long as the trustee does. But that decision rested on a determination that the insurer, which had no separate insurance agreement, lacked standing to sue the transaction sponsor. Morgan Stanley makes no such argument here.

[11] *See* N.Y. Ins. Law § 3105. In confirming the availability of claim payments as damages, the First Department explained, "the motion court was not required to ignore the insurer/insured nature of the relationship . . . in favor of an across the board application of common law." *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 105 A.D.3d at 412. In contrast to the common law, and for sound public policy reasons, New York Insurance Law entitles an insurer to recover its claim payments without proof of "a direct causal link between the misrepresentations . . . and claims made under the policy." *MBIA v. Countrywide*, 34 Misc. 3d 895, 906 (Sup. Ct. N.Y. Cnty. 2012), *modified*, 105 A.D.3d 412 (1st Dep't 2013). The only causation an insurer must prove is that the policy was induced by material misrepresentations (*i.e.*, the insurer would not have issued the policy "or would have issued the policies on different terms had the alleged misrepresentations not been made"). *Id.*

of the Insurance Law, Morgan Stanley misstates the out-of-pocket rule, which does not address the recovery of future payments for harm already incurred. Instead, it distinguishes the recovery of actual pecuniary loss (for fraudulent inducement) from a benefit-of-the-bargain recovery (for breach of contract). As explained in Morgan Stanley's lead case, fraud damages "compensate plaintiffs for what they lost because of the fraud, not for what they might have gained." *Continental Cas. Co. v. PriceWaterhouseCoopers, LLP*, 15 N.Y.3d 264, 271 (2010). That is what FGIC seeks here: its loss from being induced to irrevocably insure securities that were fatally flawed from the start, and have already experienced hundreds of millions of dollars in losses.

In *Continental*, the means of assessing the actual loss depended on the proof presented. *Id.* at 271-72. In that case, the Court assessed the harm from the fraudulently induced investment as the difference between what was paid and received on the date of the investment. *Id.* In doing so, the Court acknowledged its prior ruling in *Hotaling v. A.B. Leach & Co.*, 247 N.Y. 84, 87-88 (1928), wherein it assessed the loss after closing, upon the sale of the fraudulently induced asset. That alternative was utilized in *Hotaling* to ensure plaintiff was not "den[ied] all remedy in action at law for the deceit." *Id.* at 90. As the Court explained, "[v]arying circumstances must logically require variation in the application of that measure of damages." *Id*. at 87-88. Ultimately, the appropriate measure of the actual pecuniary loss depends on the proof at trial, which is what another court held in rejecting Morgan Stanley's identical challenge under the out-of-pocket rule to purported "future damages" sought by another insurer. *See MBIA Ins. Corp. v. Morgan Stanley*, No. 29951/2010, 2011 N.Y. Misc. LEXIS 6827, at *24-25 (Sup. Ct. Westchester Cnty. May 26, 2011) ("Plaintiffs claim for future damages ***cannot be dismissed at this stage of the proceeding***. Upon the trial of the action, Plaintiff will have the burden of establishing its damages by a preponderance of the evidence.”). The same reasoning applies here.[12]

II. FGIC Has Contract Claims that are Not Limited by the “Sole Remedy” Provision

Morgan Stanley argues that the “sole remedy” for ***all*** FGIC’s breach of contract claims is the Repurchase Protocol, as if all six contract claims were identical (they are not). (MS Br. at 10-15.) That circumvention is telling. By its express terms, the sole remedy provision of the R&W Agreement applies only to claims for breach of the Loan Warranties. FGIC’s remaining claims, based on entirely different contracts, with different remedies, are not affected.

A. The Repurchase Protocol Applies Only to Loan Warranty Breaches

While the Repurchase Protocol is the sole remedy under the R&W Agreement for breaches of the Loan Warranties, it does not apply to other breaches. Morgan Stanley (as Sponsor) made the Loan Warranties in Section 2 of the R&W Agreement. (R&W Agreement at 3, NYSCEF Doc. No. 16.) Section 4(c) provides that the Repurchase Protocol, set forth in Section 4(a), is the “sole remedy” for breaches of the Section 2 Loan Warranties:

> It is understood and agreed that the obligation of the Sponsor set forth in Section 4(a) to repurchase for [sic] ***a Mortgage Loan in breach of a representation or warranty contained in Section 2*** constitutes the sole remedy of the Depositor or any other person or entity with respect to such breach.

(*Id*. at 6 (emphasis added).) The Loan Warranties were passed to the Trust in the PSA. Section 2.03(q) of the PSA expressly incorporates the remedial provisions of the R&W Agreement:

> It is understood and agreed by the parties hereto that the obligation of the Depositor under this Agreement or of the Sponsor under the [R&W] Agreement to cure, repurchase or substitute ***any Mortgage Loan as to which a breach of representation and warranty has***

[12] The cases cited by Morgan Stanley are not to the contrary. In *Continental,* plaintiff’s claim was dismissed *after the close of discovery* because it failed to prove direct harm at all, not because payments would materialize in the future. 15 N.Y.3d at 272. In *First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 768-69 (2d Cir. 1994), the court dismissed plaintiff’s RICO claim on the theory that no harm had yet occurred, allowing plaintiff to sue later when its claim became ripe. Here, Morgan Stanley contends that the limitations period began to run at closing in 2007. *See* MS Br. at 16.

> ***occurred*** and is continuing, shall constitute the sole remedies against such Persons respecting such breach . . . .

(Doc. 13 (emphasis added).) The Repurchase Protocol is thus limited to the Section 2 Loan Warranties.

B. Transaction Warranty Breaches Are Governed by Section 5.02

The plain terms of the Insurance Agreement demonstrate that FGIC's remedies for breaches of the Transaction Warranties are not limited to the Repurchase Protocol. The Transaction Warranties are contained only in the Insurance Agreement, not Section 2 of the R&W Agreement. They attested that Morgan Stanley's representations concerning its operations, including due diligence and seller monitoring protocols, were not false or misleading. Those warranties were not loan-specific and, therefore, are not remediable by the loan-specific Repurchase Protocol. *See Ambac Assurance Corp. v. First Franklin Fin. Corp.,* No. 651217/2012, 2013 N.Y. Misc. LEXIS 3092, at *34 (Sup. Ct. N.Y. Cnty., July 18, 2013) (transaction warranty regarding sponsor's "business operation plan" was not subject to the repurchase protocol).

Instead, Morgan Stanley agreed in the Insurance Agreement to alternative remedies for breaches of the Transaction Warranties. Specifically, Section 5.01(a) states that an Event of Default arises upon a breach of a warranty "other than representations and warranties ***relating to the individual Mortgage Loans***." (Doc. 14 (emphasis added).) Thus, the Insurance Agreement distinguishes two different types of warranties: while breaches of the Loan Warranties do not constitute an Event of Default, breaches of the Transaction Warranties do, entitling FGIC to exercise all of its non-exclusive rights and remedies referenced in Section 5.02.[13]

[13] Morgan Stanley's interpretation would fail to give effect to Section 5.01(a) of the Insurance Agreement, rendering a breach of the Transaction Warranties an Event of Default. Thus would contravene "the

Justice Bransten reached this conclusion in *MBIA v. Countrywide* when presented with an analogous argument. 2013 N.Y. Misc. LEXIS 1818, at *27-28. More precisely, the court held that a sole remedy provision applied only to the loan warranties, but not to other warranties set forth separately in the insurance agreement. *Id.* ("MBIA's recovery would not be limited to repurchase.") Justice Ramos likewise held that the sole remedy provision cannot be imported into the insurance agreement to limit the remedies for warranties appearing only in the insurance agreement. *See Syncora Guar. Inc. v. EMC Mortgage, LLC*, 2013 N.Y. Misc. LEXIS 1519, at *6-10. Significantly, in reaching this holding, Justice Ramos distinguished the precedents Morgan Stanley cites in its brief (including his own prior decision) and rejected the arguments Morgan Stanley advances.

For example, Morgan Stanley argues the "sole remedy" provision should be read into the Insurance Agreement under the guise of reading the agreements together. (MS Br. at 13-14.) Faced with that same argument, Justice Ramos ruled that "[t]he fact remains that the parties did not include any language limiting Syncora's remedies under the I&I Agreement, although similarly situated parties did include such limitations in other transactions, such as in *Assured* and *Flagstar*." 2013 N.Y. Misc. LEXIS 1519, at *10. Justice Ramos also rejected the argument, made here, that the sole remedy clause applies because the insurance agreement provides that the insurer's remedies are cumulative "unless otherwise expressly provided." *Id.* at *8-9. As the court held, Morgan Stanley's reading "would effectively rewrite the parties' agreements under the guise of contract interpretation." *Id.* at *9.

C. Breaches of the Repurchase Protocol Are Governed by Section 5.02

Morgan Stanley cites inapposite decisions to argue that FGIC cannot maintain a distinct

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settled rule that a contract is to be construed so as to give effect to each and every part." *FCI Group, Inc. v. City of New York*, 54 A.D.3d 171, 176 (1st Dep't 2008).

claim for breach of the Repurchase Protocol. (MS Br. at 14-15.) These decisions all involved suits by trustees or certificate holders asserting claims under the very same agreements that limited their remedies.[14] None involved a claim based on an insurance agreement granting a separate remedy for breach of a covenant (here, performance of the Repurchase Protocol).

First, Section 2.02(k) of the Insurance Agreement expressly restates Morgan Stanley's covenants set forth in the Operative Documents, including the Repurchase Protocol, without limitation and "for the benefit of the Certificate Insurer." (Doc. 14). Interpreting very similar provisions, Justice Ramos in *Syncora v. EMC* held that those terms incorporate the rights and not limitations for the benefit of the insurer. 2013 N.Y. Misc. LEXIS 1519, at *7-8.

Second, Section 5.01(d) of the Insurance Agreement makes any failure by Morgan Stanley "duly to observe or perform in any material respect any other of the covenants or agreements" in either the Insurance Agreement or the R&W Agreement a separate Event of Default. (Doc. 14.) Accordingly, Morgan Stanley's breach of the Repurchase Protocol (*i.e.*, a covenant) constitutes an Event of Default, which entitles FGIC to exercise all remedies "existing at law or in equity" pursuant to Section 5.02(b). (*Id.* at 33.) Nothing in the Insurance Agreement limits FGIC to a loan repurchase protocol under a sole remedy provision.

D. FGIC's Remaining Claims Are Not Subject to the "Sole Remedy" Provision

Morgan Stanley's motion never specifically addresses FGIC's remaining breach of contract claims, and therefore, FGIC reserves the right to respond if Morgan Stanley does so for

[14] *See ACE Secs. Corp. v. DB Structured Prods., Inc.*, 112 A.D.3d 522 (1st Dep't 2013) (suit initially filed by certificate holders, joined by trustee); *Walnut Place LLC v. Countrywide Home Loans, Inc.*, 96 A.D.3d 684 (1st Dep't 2012) (suit by certificate holders); *Morgan Stanley Mortg. Loan Trust 2006-13ARX v. Morgan Stanley Mortg. Capital Holdings LLC*, No. 653429/2012, 2014 N.Y. Misc. LEXIS 4294 (Sup. Ct. N.Y. Cnty. Sept. 25, 2014) (trustee suit); *Nomura Asset Acceptance Corp. Alt. Loan Trust v. Nomura Credit & Capital, Inc.*, No. 653390/2012, 2014 N.Y. Misc. LEXIS 2905 (Sup. Ct. N.Y. Cnty. June 26, 2014) (trustee suit).

the first time in reply.[15] None of those claims seeks to enforce the Loan Warranties or the R&W Agreement, so none can be constrained by the sole remedy provision.

III. Morgan Stanley's Remaining Arguments Disregard Settled Law

Morgan Stanley concludes by raising a series of arguments that have been rejected by this Court or the First Department. They should be rejected here as well.

A. FGIC's Claims are Not Limited to the Loans Put Back

Morgan Stanley concedes that FGIC timely commenced this action with respect to claims for the repurchase of hundreds of Mortgage Loans. (MS Br. at 5, 16.) Moreover, Morgan Stanley does not dispute that FGIC's allegations are sufficient to allege that Morgan Stanley discovered and had actual, constructive or inquiry notice of pervasive breaches in the Mortgage Pool before the statute of limitations ran. (Comp., *e.g.*, ¶¶ 173-76.) Morgan Stanley nonetheless contends that FGIC may not maintain a claim for Mortgage Loans for which it did not demand repurchase. (MS Br. at 15-16.) To the contrary, this Court repeatedly has held that analogous allegations are sufficient to maintain claims for pervasive breaches in the loan pool. *See, e.g., Morgan Stanley Mortg. Loan Trust 2007-2AX v. Morgan Stanley Mortg. Capital Holdings LLC*, No. 650339/2013, 2014 N.Y. Misc. LEXIS 5079, at *4 (Sup. Ct. N.Y. Cnty. Nov. 24, 2014).

B. FGIC Adequately Pleaded its Fraud Claim

Morgan Stanley makes three meritless arguments against FGIC's fraud claim.

1. FGIC's Fraud Claim Is Not Impermissibly Duplicative

Ignoring controlling precedent, Morgan Stanley asserts that FGIC cannot maintain a fraud claim based on factual representations that were incorporated as warranties into the parties'

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[15] The claims include Claim 3 (for material breach of the Insurance Agreement), Claim 5 (for reimbursement under the Insurance Agreement), Claim 6 (for Saxon's failure to provide prompt notice of breaches of the Loan Warranties, Saxon's breach of its obligation to act as prudent loan servicer, and Saxon's breach of its Side Letter Agreement by failing to notify FGIC of the referral of loans to a subservicer) and Claim 7 (for beaches of warranties made by Saxon and MSAC in the PSA).

agreement. (MS Br. 19-20.) But as the First Department held in allowing a directly analogous claim, a financial guarantor may maintain a fraudulent inducement claim based on the same misrepresentations of present fact that are "also contained in the agreements as warranties and form a basis for the breach of contract claim." *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 87 A.D.3d 287, 293-94 (1st Dep't 2011). *Accord. First Bank of the Americas v. Motor Car Funding, Inc.*, 257 A.D.2d 287, 291-92 (1st Dep't 1999). Such factual statements, made in separate communications before the contract, are "collateral to the contract" and involve "a separate breach of duty." *MBIA*, 87 A.D.2d at 293.[16] *MBIA v. Countrywide* is dispositive.[17]

In urging a different result, Morgan Stanley argues the *MBIA* panel failed to consider decisions said to stand for the proposition that fraudulent inducement and contract claims are impermissibly duplicative if the same damages are sought. (MS Br. at 17-19.) Contrary to Morgan Stanley's suggestion, there is no conflict of authority. ***All*** the cases Morgan Stanley cites for this proposition involve fraud claims properly denied because the plaintiff did ***not*** allege a prior misrepresentation of existing facts collateral to the contract, and attested to by a warranty therein.[18] As the Court of Appeals has held, it is advisable to incorporate pre-contractual

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[16] As in *MBIA*, FGIC alleges that it was induced to participate in the Transaction by Morgan Stanley's pre-contractual provision of: (1) mortgage loan tapes and "strats" describing factual attributes of the Mortgage Loans (Comp. ¶¶ 51-55); (2) offering documents asserting that the Mortgage Loans were originated in compliance with underwriting guidelines and that Morgan Stanley followed loan seller review processes (*Id.* ¶¶ 56-60), and (3) false and misleading "shadow ratings" (*Id*. ¶¶ 61-63.)

[17] Morgan Stanley nonetheless argues the opposite, citing four distinguishable cases that predate *MBIA v. Countrywide*. (MS Br. at 19-20.) Two of these decisions involved a misrepresented intent to perform the contract. *See Hawthorn Group, LLC v. RRE Ventures*, 7 A.D.3d 320 (1st Dep't 2004); *Coppola v. Applied Elec. Corp.*, 288 A.D.2d 41 (1st Dep't 2001). In the other two cases, there were no representations collateral to the contract, as alleged here. *See J.E. Morgan Knitting Mills, Inc. v. Reeves Bros., Inc.*, 243 A.D.2d 422, 423 (1st Dep't 1997); *Pramco III, LLC v. Partners Trust Bank*, No. 2006/021318, 2007 N.Y. Misc. LEXIS 3899, at *1 (Sup. Ct. Monroe Cnty. May 31, 2007).

[18] *See Mosaic Caribe, Ltd. v. AllSettled Group, Inc.*, 117 A.D.3d 421 (1st Dep't 2014); *Chowaiki & Co. Fine Art Ltd. v. Lacher*, 115 A.D.3d 600 (1st Dep't 2014); *Manas v. VMS Assocs., LLC*, 53 A.D.3d 451, 454 (1st Dep't 2008); *Andres v. LeRoy Adventures, Inc.*, 201 A.D.2d 262 (1st Dep't 1994)

representations as warranties to establish justifiable reliance.[19] *DDJ Mgmt., LLC v. Rhone Group LLC*, 15 N.Y.3d 147, 155 (2010) ("[W]here 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.") FGIC having followed this directive by securing warranties as to pre-contractual representations, its fraudulent inducement claim may not be denied because the warranty claim seeks the same recovery. *See MBIA v. Countrywide*, 105 A.D.3d 412 (allowing claim payments as damages under fraud and warranty theories). *See also Jo Ann Homes at Belmore v. Dworetz*, 25 N.Y.2d 112 (1969) (affirming, in relevant part, jury verdict awarding the same amount of damages for both fraud and contract claims).

FGIC's fraudulent inducement claim complies with applicable precedent. The Complaint alleges misrepresentations of existing facts collateral to the Insurance Agreement, analogous to those in *MBIA v. Countrywide*. (Comp. ¶¶ 30-63.) Moreover, refuting the factual predicate of Morgan Stanley's argument, FGIC did allege different damages theories, seeking both to enforce the Repurchase Protocol (a contractual, benefit-of-the-bargain recovery) (*Id.* ¶ 223) and indemnity for the harm incurred from Morgan Stanley's inducement of its Policy (a fraud recovery). (*Id.* ¶ 216).[20] Morgan Stanley's argument thus fails on the law and the facts.

2. FGIC Adequately Pleaded Justifiable Reliance

Morgan Stanley contends that FGIC cannot, as a matter of law, show justifiable reliance on Morgan Stanley's oral representations that it conducted diligence on 50% of the Mortgage

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[19] Indeed, Morgan Stanley complains both that FGIC did include confirming representations in its agreement (MS Br. at 17) and also that it did not (MS Br. at 20-22).

[20] Morgan Stanley argues that the "sole remedy" clause precludes fraud damages. (MS Br. at 19 n.9.). As explained in Section II, this clause applies only to breaches of the Loan Warranties, and the Insurance Agreement expressly reserves FGIC's other remedies. In contrast, the contract in *Mom's Bagels v. Sig Greenebaum Inc.*, 164 A.D.2d 820 (1st Dep't 1990), limited liability for breach of warranty "or otherwise," without a reservation of rights. To the extent FGIC's contractual remedy is limited to loan repurchase, its fraud claim plainly seeks distinct damages.

Loans to ensure their quality. (MS Br. 20-22.) This argument fails for three reasons.

First, under Section 3105 of New York Insurance law, an insurer need not prove reasonable reliance to recover for a material misrepresentation made in the procurement of an insurance agreement. *See MBIA Ins. Corp. v. Countrywide Home Loans*, Inc., 2013 N.Y. Misc. LEXIS 1818, at *9-11, *citing Geer v. Union Mut. Life Ins. Co.*, 273 N.Y. 261 (1937). As the court explained in *MBIA v. Countrywide*:

> Thus, under Geer, and under Section 3105, the inquiry is not whether the information was justifiable but instead whether the insurer might have refused the application had it been aware of the truth of the misrepresentation. . . . Accordingly, the Court finds no justifiable reliance requirement for a fraud claim under Section 3105.

Id. at *10-11. FGIC alleges that Morgan Stanley's representations about its diligence were highly material to FGIC (Comp. ¶ 40) and, had it known the truth, "it would not have agreed to participate in the Transaction and to issue its Policy," which is sufficient. (*Id.* ¶ 50.)

Second, assuming that FGIC must show justifiable reliance, reliance on these oral representations was reasonable because they were inextricably intertwined with the representations incorporated into written warranties. *See DDJ*, 15 N.Y.3d at 154 ("[W]here 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."). Specifically, FGIC alleges, "Mr. Shapiro told FGIC that it was this diligence and selection process that enabled Morgan Stanley to provide FGIC with detailed representations and warranties about the Mortgage Loans and the processes by which they were originated." (Comp. ¶ 47.) Morgan Stanley described its purported diligence in a bankruptcy court stipulation (*id.* ¶ 45) and in the ProSupp. (*Id.* ¶ 86.) Morgan Stanley warranted that these disclosures were not false or misleading in, *inter alia*, the Accuracy of Information Warranty. (*Id.* ¶ 81.) These disclosures were misleading both on their own terms and in light of Morgan Stanley's failure to review 50% of Mortgage Loans.[21] These allegations are sufficient. *DDJ*, 15 N.Y.3d at 155 (citation omitted) ("The question of what constitutes reasonable reliance is always nettlesome because it is so fact-intensive," rendering it inappropriate for decision on the pleadings).

Third, even if it were appropriate to consider Morgan Stanley's oral representations entirely in isolation, FGIC's could properly rely on them because they concerned matters peculiarly within Morgan Stanley's knowledge. Even where there is a disclaimer of reliance, "a purchaser may not be precluded from claiming reliance on any oral misrepresentations if the facts allegedly misrepresented are peculiarly within the seller's knowledge." *Tahini Invs. v. Bobrowksi*, 99 A.D.2d 489, 490 (2d Dep't 1984); *accord Steinhardt Grp., Inc. v. Citicorp*, 272 A.D.2d 255, 257 (1st Dep't 2000). Here, the diligence and selection that Morgan Stanley conducted were peculiarly within Morgan Stanley's knowledge. This distinguishes cases cited by Morgan Stanley. In *HSH Nordbank AG v. UBS AG*, the truth was publicly available and the First Department distinguished *MBIA v. Countrywide*, 87 A.D.3d 287, where the standards Countrywide used to originate mortgage loans "was a matter peculiarly within the knowledge of the defendants." 95 A.D.3d 185, 194-95, 208 n.15 (1st Dep't 2012).[22]

[21] In attempting to distinguish *DDJ*, Morgan Stanley ignores that it, too, involved oral representations. Plaintiffs alleged that before they were provided financial statements (which were the subject of a written warranty), they received "reassuring information" in "several conversations with ARI representatives." *DDJ*, 15 N.Y.3d at 152. Morgan Stanley also contends that FGIC did not perform basic due diligence and did not secure a "prophylactic provision" in the contract. (MS Br. at 22 n.12.) But FGIC conducted diligence by reviewing and assessing the attributes of the Mortgage Loans and modeling the expected performance of the Transaction (Comp. ¶ 53), and secured a prophylactic provision warranting the accuracy of the loan tape, bankruptcy stipulation and other information provided to FGIC in written or electronic form.

[22] *ACA Fin. Guar. Corp. v. Goldman, Sachs & Co.*, 106 A.D.3d 494, 497 (1st Dep't 2013), is inapposite because: (1) the representations "were specifically contradicted by" the offering documents; (2) plaintiff expressly disclaimed reliance; and (3) the matter allegedly misrepresented (the intentions of a third-party hedge fund) "were not peculiarly within defendant's knowledge." *Centro Empresarial Cempressa S.A. v. America Movil. S.A.B.*, 17 N.Y.3d 269, 278-79 (2011), is inapposite because plaintiffs knew that

3. The Complaint Complies with CPLR 3016(b)

Morgan Stanley challenges FGIC's allegations under CPLR 3016(b) (MS Br. at 23), but they satisfy the purpose of 3016(b), which is "to inform a defendant with respect to the incidents complained of." *Sargiss v. Magarelli*, 12 N.Y.3d 527, 530 (2009) (citation omitted).

Contrary to Morgan Stanley's assertions, the Complaint alleges how the representations about its diligence and selection process were made (in conversations with Steven Shapiro) and when (during the first two quarters of 2007). (*See* Comp. ¶¶ 39-40.) No more is required to provide Morgan Stanley sufficient notice of the incidents at issue. Indeed, this Court recently upheld an RMBS fraud complaint that did not identify how the fraudulent statements were published or the particular investors that received them. *People v. Credit Suisse Sec. (USA) LLC*, No. 451802/2012, 2014 N.Y. Misc. LEXIS 5796, at *26-27 (Sup. Ct. N.Y. Cnty. Dec. 24, 2014). The cases Morgan Stanley cites did not dismiss fraud complaints for failing to list the precise dates of communications or the names of particular representatives of the plaintiff to whom representations were made. Instead they concerned basic deficiencies that left the defendant guessing about the incidents complained of.[23] There is no such ambiguity here.

C. FGIC is Entitled to Reimbursement of Attorneys' Fees

Finally, Morgan Stanley seeks to avoid its unambiguous agreement to reimburse FGIC for the cost of this action. (MS Br. at 24.) Section 3.03(d) of the Insurance Agreement clearly

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defendants had not provided them financial information they needed and to which they were entitled before completing the transaction.

[23] *See Summit Solomon & Feldesman v. Lacher*, 212 A.D.2d 487, 487 (1st Dep't 1995) (complaint failed to identify the clients to which defendant's misrepresentations referred); *Mazeh Const. Corp. v. VNB N.Y. Corp.*, No. 500728/2011, 2012 N.Y. Misc. LEXIS 2702, at *13 (Sup. Ct. Kings Cnty. June 11, 2012) (complaint failed to allege which of multiple "lenders" made the misrepresentations or whether they were made directly to the plaintiff); *David v. Simware, Inc.*, No. 602143/1996, 1997 N.Y. Misc. LEXIS 201, at *9 (Sup. Ct. N.Y. Cnty. Mar. 7, 1997) (complaint failed to specify who made the misrepresentations, what was stated, and whether the statements were made directly to the plaintiff).

affords FGIC the right to recover its costs, including "reasonable attorneys' and accountants' fees" in connection with "the enforcement" of its rights under the Insurance Agreement and other Operative Documents (including the R&W Agreement). (Insurance Agreement at 24-25, Doc. 14.) By definition, "the enforcement" of FGIC's rights under the Operative Documents can only be directed to another party to the Operative Documents, making it a "first-party" claim. A separate provision (§ 3.04) provides indemnification for "third party" claims. (*Id.* at 25-28.)

In *Assured v. Flagstar*, Judge Rakoff awarded attorneys' fees and expenses under a nearly identical reimbursement provision. 2013 U.S. Dist. LEXIS 57126, at *4-5. Other Justices have found that insurance agreement reimbursement provisions constitute unmistakably clear promises to pay attorney fees in a suit to enforce the transaction documents. *See Ambac v. First Franklin*, 2013 N.Y. Misc. LEXIS 3092, at *39; *Syncora Guar. Inc. v. EMC Mortg. LLC*, 2013 N.Y. Misc. LEXIS 1519, at *13-14.

This Court applied a similar approach in *HEAT 2006-8 v. DLJ Mortgage Capital, Inc.*, No. 654157/2012, 2014 N.Y. Misc. LEXIS 4380 (Sup. Ct. N.Y. Cnty. Oct. 1, 2014), dismissing a claim for reimbursement of attorney fees not expressly mentioned in the agreement, but not dismissing the claim for reimbursement of the trustee's out-of-pocket expense for "enforcing" the repurchase remedy. This same reasoning supports FGIC's claim.

The only authority cited to the contrary is Justice Bransten's decision in *MBIA v. Countrywide*, 2013 N.Y. Misc. LEXIS 1818, at *43. FGIC respectfully disagrees with this aspect of the decision, which is an outlier, because it failed to differentiate between reimbursement and indemnification, effectively reading the reimbursement provision out of the contract.

CONCLUSION

For all of the foregoing reasons, FGIC respectfully requests that the Court deny Morgan Stanley's motion to dismiss in its entirety.

Dated: January 29, 2015

Respectfully submitted,

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