

**AMBAC Assur. Corp. v Countrywide Home Loans,
Inc.**

2014 NY Slip Op 31615(U)

June 23, 2014

Supreme Court, New York County

Docket Number: 651612/2010

Judge: Eileen Bransten

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART THREE

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AMBAC ASSURANCE CORPORATION and
THE SEGREGATED ACCOUNT OF AMBAC
ASSURANCE CORPORATION,

Plaintiffs,

- *against* -

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

Defendants.

-----X
BRANSTEN, J.

Index No.: 651612/2010
Motion Date: 06/12/2014
Motion Seq. No.: 018, 019

This residential mortgage-backed securities case comes before the Court on motion sequence numbers 018 and 019, which are consolidated herein for disposition.

In motion sequence 018, Defendants Countywide Home Loans, Inc., Countrywide Securities Corp., and Countrywide Financial Corp. (collectively, "Countrywide" or "Defendants") seek an order to confirm that the confidentiality stipulation and order entered in this case ("Confidentiality Order") prohibits disclosure of certain information to unauthorized third parties. In motion sequence 019, Plaintiffs Ambac Assurance Corporation and The Segregated Account of Ambac Assurance Corporation (collectively "Ambac" or "Plaintiffs") seek an order stating that their disclosure of information did not violate the Confidentiality Order. For the reasons stated below, Countrywide's motion sequence 018 is denied, and Ambac's motion sequence 019 is granted.

Background

Ambac alleges that Countrywide fraudulently induced Ambac into insuring twelve residential mortgage-backed securities. Specifically, Ambac asserts that Countrywide made representations and warranties in the securitization transaction documents regarding Countrywide's underwriting practices in issuing mortgage loans to borrowers that comprised the securities. Pertinent to the instant motion, Ambac alleges that Countrywide made certain representations about borrower employment and income levels that were inaccurate.

Ambac alleges that prior to this litigation, it re-underwrote 8,804 loans from the securitizations in an effort to test Countrywide's representations. According to Ambac, the re-underwriting process began with Ambac exercising its contractual rights, based upon the securitization transaction documents, to receive borrower loan files from Countrywide. Once Ambac possessed the loan files, Ambac alleges that it hired several consulting firms to verify whether incomes stated on loan applications were accurate.

To verify Countrywide's underwriting practices, Ambac allegedly used information from borrower loan applications to contact borrowers' employers, or if they were self-employed, their certified public accountants ("CPAs"). Ambac alleges that it only contacted employers or CPAs if the loan files Ambac received from Countrywide contained borrower authorization forms. When Ambac contacted employers and CPAs, Ambac stated that it was not trying to collect a debt and that Ambac did not have a

dispute with the borrower. Ambac provided borrower names, the last five digits of borrower social security numbers and sometimes the borrower authorization form that contained the borrower loan numbers.

Ambac alleges that it discovered that certain borrowers either were not employed at the place listed on their loan application or had inflated their income. When Ambac discovered these purported breaches of Countrywide's stated underwriting practices, Ambac contacted Countrywide, told Countrywide the information it had uncovered, and requested that those loans be repurchased by Countrywide. Ambac provided Countrywide with the results of its re-underwriting process, but Countrywide declined to repurchase the allegedly defective loans.

Ambac commenced the instant litigation on September 28, 2010. Ambac and Countrywide entered into the Confidentiality Order on August 23, 2011, as modified on October 22, 2013. The parties entered into the Confidentiality Order, in part, to protect personal borrower information during the pendency of this action. In the course of discovery, Countrywide turned over borrower loan files to Ambac that contained sensitive borrower information. Ambac used these loan files to continue its re-underwriting process.

Discussion

The Confidentiality Order defines “Confidential Information” as “information identifying individual borrowers,” and prevents disclosure of Confidential Information to “any person except as expressly permitted.” Countrywide argues that the plain language of the Confidentiality Order bars Ambac’s re-underwriting process.¹

Countrywide contends that Ambac disclosed borrower information, in the form of borrower names and loan numbers, to unauthorized third parties. Countrywide posits that Ambac disclosed to employers and CPAs the fact that these employees or clients have Countrywide loans. Countrywide also asserts that one of the firms Ambac hired to conduct the re-underwriting may be creating a negative inference in the mind of employers because its website indicates that it conducts “fraud review.” Countrywide further argues that it could have objected to any Ambac subpoenas, but did not have the right to object to Ambac’s informal discovery process.

Ambac argues that Countrywide knew of Ambac’s re-underwriting process from before this litigation but only now raises this issue. Ambac also argues that Countrywide engaged in the same re-underwriting process during this litigation and that Ambac did not

¹ Although Countrywide initially claimed that Ambac’s actions may have violated federal and state law, Countrywide appears to have abandoned that argument. The pertinent section of the Gramm-Leach-Bliley Act, 15 U.S.C. 6802, permits disclosure of personal information if the disclosure relates to a securitization and if such disclosure would be lawful if made by the Countrywide. Countrywide acknowledges that it had the right to make disclosures here. *See* 15 U.S.C. 6802(c), (e)(1)(C) (“this section shall not prohibit the disclosure of nonpublic personal information . . . in connection with . . . [an] actual securitization”).

“disclose” any information to anyone who did not already have the information. Finally, Ambac argues that Countrywide’s hyper-technical reading of the Confidentiality Order is unavailing because there has been no harm to Countrywide or any borrower.

Countrywide argues that “Ambac’s conduct has been in flagrant violation” of the Confidentiality Order. In Countrywide’s initial papers, Countrywide requests that “Ambac . . . be required to use the subpoena process.” Countrywide contends that the subpoena process “allows courts to weigh evidentiary needs against borrowers’ privacy interests and maximizes the chances that the information obtained will be reliable and maintained as confidential.” In Countrywide’s supplemental submission, it goes further and seeks suppression of all the evidence that Ambac “improperly” obtained and argues that the discovery deadline has passed and it is now too late to use the subpoena process.

There are several reasons why Countrywide’s arguments fail. First, Countrywide did not violate the Confidentiality Order. Second, even if it the complained of conduct did violate the Confidentiality Order, Countrywide has not shown that it or any borrower has suffered any harm as a result. Finally, the relief Countrywide seeks is disproportionate to the claimed harm and is therefore inappropriate. Each of these reasons will be discussed below.

I. *Ambac Did Not Violate the Terms of the Confidentiality Order*

As the Court of Appeals has stated, “there are no statutes and no rules expressly authorizing—or forbidding—ex parte discussions with any nonparty.” *Arons v. Jutkowitz*, 9 N.Y.3d 393, 409 (2007). “Article 31 does not close off these avenues of informal discovery, and relegate litigants to the costlier and more cumbersome formal discovery devices. *Id.* (internal quotation omitted). In *Arons*, the Court of Appeals permitted an attorney to contact a doctor, ex parte, to conduct informal discovery. *Id.* at 401-02. The primary concern was that the non-party must not be “gulled into making an improper disclosure,” so it is important that “attorneys would make their identity and interest known to interviewees and comport themselves ethically.” *Id.* at 410 (citing *Niesing v. Team I*, 76 N.Y.2d 363, 376 (1990)).

Here, Ambac’s sworn affirmation describing the re-underwriting process shows that there were no improper disclosures or communications. Ambac first attempted to verify employment and salary information through internet sources. *See* Affirm. of Robert P. LoBue in Support of Mot. 019 at 2-3. Then, if Ambac was unable to verify the information independently, Ambac proceeded to contact employers or CPAs, but only if the loan files contained borrower authorization forms. *See id.* Ambac stated to employers or CPAs that Ambac did not have a dispute with the borrower and that Ambac was not trying to collect a debt. *See* Affirm. of Robert P. LoBue in Opp. to Mot. 018 at 2. Countrywide does not dispute this description of Ambac’s investigation.

Outside of the Confidentiality Order, Countrywide does not offer any reason that Ambac's actions were improper. Under Countrywide's interpretation, if Ambac requested the loan files contractually outside of this litigation, rather than as document demands within this litigation, Ambac's actions would be proper. Countrywide essentially contends that Ambac contracted away its right to continue the re-underwriting process by entering into the Confidentiality Order.

"A stipulation is an independent contract which is subject to the principles of contract law. . . . A court should construe a stipulation made in open court in accordance with the intent of the parties and the purpose of the stipulation by examining the record as a whole." *Adelsberg v. Amron*, 103 A.D.3d 571, 572 (1st Dep't 2013). "It is well settled that our role in interpreting a contract is to ascertain the intention of the parties at the time they entered into the contract." *Evans v. Famous Music Corp.*, 1 N.Y.3d 452, 458 (2004).

Ambac's re-underwriting process did not violate the terms of the Confidentiality Order. Countrywide undoubtedly knew that Ambac had contacted employers to verify borrower employment and salary. As early as November 17, 2010, Ambac informed Countrywide that Ambac's had contacted borrower employers and that Ambac's investigation would continue. See Affirm. of Robert P. LoBue in Support of Mot. 019, Ex. 4 at 1, 4. Countrywide failed to raise this issue during the negotiation of the Confidentiality Order or for several years thereafter.

Countrywide contends that it only learned about the involvement of one of the firms that Ambac had hired to conduct the investigation during a deposition in a related case in December 2013. Countrywide's contention here misses the point. It is not about the involvement of any single entity, but rather that Ambac's re-underwriting process began before this litigation and before the Confidentiality Order.

Countrywide fails to rebut Ambac's contention that the purpose for requesting loan files was to continue the re-underwriting process, nor does Countrywide offer an alternative reason why Ambac would request the files. *See Adelsberg v. Amron*, 103 A.D.3d 571, 572 (1st Dep't 2013) ("A court should construe a stipulation made in open court in accordance with the intent of the parties and the purpose of the stipulation by examining the record as a whole"). The conduct of the parties prior to entering into the Confidentiality Order shows that Ambac did not tacitly surrender its right to conduct its re-underwriting investigation. Countrywide cannot be heard to complain about a process that it knew was occurring for several years and failed to address.

II. *Countrywide Has Not Shown Any Harm or Prejudice*

Countrywide objects to the "extra-judicial" method that Ambac used because, as described earlier, it does not permit a court "to weigh evidentiary needs against borrowers' privacy interests" and fails to "maximize the chances that the information

obtained will be reliable and maintained as confidential.” However, Countrywide fails to identify any harm or prejudice suffered by either itself or any borrower.

As noted above, the Confidentiality Order “is an independent contract which is subject to the principles of contract law.” *Adelsberg v. Amron*, 103 A.D.3d 571, 572 (1st Dep’t 2013). To state a claim for breach of contract, a party must allege “the existence of a contract, [its] performance . . . breach thereof, and resulting damages.” *Harris v. Seward Park Hous. Corp.*, 79 A.D.3d 425, 426 (1st Dep’t 2010). “In the absence of any allegations of fact showing damage, mere allegations of breach of contract are not sufficient to sustain a complaint, and the pleadings must set forth facts showing the damage upon which the action is based.” *ERE LLP v. Spanierman Gallery, LLC*, 94 A.D.3d 492, 493 (1st Dep’t 2012) (quoting *Gordon v. Dino De Laurentiis Corp.*, 141 A.D.2d 435, 426 (1988)).

It is unclear what harm Countrywide has suffered. Ambac’s contractual rights are not subject to court supervision. The subpoena process, which Countrywide seeks to impose upon Ambac, can also be done without court guidance. Although Countrywide would have been notified of any subpoena Ambac issued to a borrower’s employer or a borrower’s CPA, Countrywide does not articulate how any notice would have changed any aspect of the investigation. This is especially true in light of the fact that the subpoena process championed by Countrywide would disclose precisely the information Countrywide allegedly seeks to protect.

III. *The Remedy Sought by Countrywide is Inappropriate*

Finally, Countrywide's proposed remedy is disproportionate to the alleged harm. Countrywide seeks to preclude Ambac from using its evidence of Countrywide's improper underwriting to support its breach of warranty claims. New York courts do not impose such draconian sanctions absent extreme circumstances. "In light of this State's policy preference for deciding actions on their merits, such a drastic sanction should only be imposed when the party's conduct is willful, contumacious or in bad faith." *Iskowitz v. Forkosh Const. Co., Inc.*, 269 A.D.2d 131, 133 (1st Dep't 2000). Although the *Iskowitz* court was referring to striking a pleading, the remedy Countrywide seeks here is nearly as drastic. Striking Ambac's evidentiary support for its allegations would constitute a severe sanction that would not further New York's policy for deciding actions on their merits.

Further, requiring Ambac to conduct its re-underwriting investigation again would be a waste of resources. Countrywide has failed to identify how subpoenas would be different from what Ambac has already done. Countrywide's proposal would delay resolution of this case without any clear benefit. The Court finds no reason to order such an unnecessary practice.

In sum, Ambac did not violate the terms of Confidentiality Stipulation and Countrywide failed to show any harm that has resulted or propose a proper remedy. Accordingly, Ambac's motion is granted, and Countrywide's motion is denied.

Conclusion

Accordingly, it is hereby

ORDERED that Countrywide's motion sequence 018 is denied; and it is further

ORDERED that Ambac's motion sequence 019 is granted.

This constitutes the decision and order of the Court.

Dated: New York, New York

June 23, 2014

ENTER:

A handwritten signature in black ink, appearing to read "Eileen Bransten", written over a horizontal line.

Hon. Eileen Bransten, J.S.C.