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New York Court of Appeals Affirms Decision on Statute of Limitations for RMBS “Put-Back” Claims

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Recently, the New York Court of Appeals issued a decision that may finally close the door on contractual repurchase claims in connection with residential mortgage-backed securities (“RMBS”) sold years ago. The decision, issued in *ACE Securities Corp. v. DB Structured Products, Inc.*, affirmed a prior ruling by the Appellate Division, First Department, and held that New York’s six-year statute of limitations for alleged breaches of representations and warranties accrues when the representations are made (*i.e.*, the date of the securitization) and not, as the plaintiff-appellant argued, when a sponsor refuses to cure or repurchase the underlying mortgages.¹

Background

As is typical in RMBS transactions, the mortgage loans at issue in *ACE Securities* were purchased by the sponsor, DB Structured Products, Inc. (“DBSP”), and sold to a depositor pursuant to a Mortgage Loan Purchase Agreement (“MLPA”).² The same day, (March 28, 2006), the loans were deposited into a trust (the “Trust”) and securitized through the issuance of certificates.³ In the MLPA, DBSP made various representations and warranties (the “Representations”) concerning the credit quality and characteristics of the loans “as of the Closing Date” of the transaction.⁴ In the event that DBSP breached any of the Representations, the Trust’s sole remedy was to request that DBSP cure or repurchase the non-conforming loan(s).⁵ Specifically, pursuant to the MLPA, DBSP was to be provided with a 60-day period to cure any alleged breach and, if the breach could not be cured, a 90-day period to repurchase the non-conforming loan(s) (the “Repurchase Protocol”).⁶

On March 28, 2012—exactly six years after the closing of the transaction—two certificateholders filed suit against DBSP alleging breaches of the Representations in the MLPA, and failure to buy-back more than \$250 million of mortgage loans in accordance with the agreements. The certificateholders, although they had notified DBSP of the alleged breaches on January 12, 2012, had not provided the requisite 90-day notice, as they filed suit before the 90-day period had run. Subsequently, in September 2012, the Trust sought to substitute itself as plaintiff.⁷

DBSP moved to dismiss the Trust’s complaint as untimely arguing that, if the Representations were false, they were false when made on the closing date of the transaction, *i.e.*, March 28, 2006, and therefore the Trust’s claims were barred by the applicable six-year statute of limitations.⁸ DBSP further argued, among other things, that the certificateholders did not validly commence an action



because they failed to comply with the Repurchase Protocol, namely providing DBSP with 60 days to cure and/or 90 days to repurchase the loans prior to bringing suit.⁹

Procedural History

In May 2013, the New York Supreme Court denied the motion to dismiss, finding plaintiff's claims to be timely. Justice Shirley Werner Kornreich held that DBSP had a "recurring obligation" under the agreements to cure or repurchase non-conforming mortgage loans; when it failed to do so, it committed an independent breach of the RMBS agreements and each breach re-started the running of the statute of limitations.¹⁰ In addition, the Court found that the Trust had satisfied the Repurchase Protocol because the alleged misrepresentations could not be cured, and DBSP had affirmatively denied any obligation to repurchase the loans.¹¹

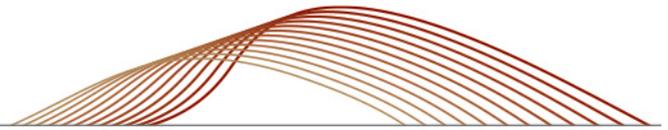
The Appellate Division, First Department, unanimously reversed Judge Kornreich's decision in December 2013, and dismissed the complaint. The First Department found that plaintiff's claims accrued on March 28, 2006, the closing date of the MLPA, "when any breach of the representations and warranties contained therein occurred."¹² Although the certificateholders commenced their action on the last day of the limitations period, March 28, 2012, the certificateholders failed to comply with the Repurchase Protocol—a condition precedent to commencing an action—thereby rendering their suit a nullity.¹³ Separately, the Court found the Trust's September 2012 complaint was time-barred.¹⁴

The Court of Appeals' Decision

On June 11, 2015, the Court of Appeals affirmed the First Department's decision to dismiss the complaint, finding that plaintiff's cause of action did, in fact, accrue at the time the RMBS agreements were executed. Judge Susan Phillips Read, writing for a unanimous court, highlighted the "finality, certainty and predictability" that New York statute of limitations are designed to foster, even when the result may "at times be harsh and manifestly unfair, and creates an obvious injustice."¹⁵ The Court explained that "where, as here, the representations and warranties concern the characteristics of their subject as of the date they are made, they are breached, if at all, on that date"—a holding that is consistent with the result reached by the overwhelming majority of courts in other jurisdictions.¹⁶

The Court of Appeals rejected the notion that DBSP's repurchase obligation was a continuing promise of the loans' future performance—separate from the Representations made in the agreements—that could give rise to an independent cause of action.¹⁷ To the contrary, the Court found the repurchase obligation to be a "remedy" that was necessarily "dependent on" and "derivative of" the Representations, which "did not survive the closing date and were breached, if at all, on that date."¹⁸ The Court also noted the practical reality that DBSP, as sponsor and seller, would not guarantee payments for the life of the transaction because mortgages may default "10 or 20 years after they have been issued for reasons entirely unrelated to the sponsor's representations and warranties."¹⁹

Finally, the Court of Appeals agreed that the Repurchase Protocol was a contractual condition precedent to bringing a lawsuit and, since neither the Trust nor the certificateholders provided DBSP with 60 days to cure and/or 90 days to repurchase, plaintiffs' commencement of the lawsuit on March 28, 2006 (within the six year period) was not valid—*i.e.*, the lawsuit could only be commenced 90 days after notice and since that would violate the statute of limitations, plaintiffs had no valid cause of action.²⁰



Practical Implications

The *ACE Securities* decision makes clear that any new contractual put-back claims governed by New York law, in connection with RMBS sold more than six years ago, are likely foreclosed by the applicable statute of limitations. Although this decision is not binding on other jurisdictions, it should be highly influential to those courts when faced with the same issue, and may finally end the stream of RMBS repurchase litigations.

Separately, parties to any contract—irrespective of whether it involves mortgage-backed securities—must bear in mind the *ACE Securities* decision when crafting remedy provisions similar to the repurchase provisions in RMBS agreements. If, as the Trust argued in *ACE Securities*, the parties intend for the contractual remedies to be independent contractual obligations giving rise to a separate statute of limitations, the contract must be clearly drafted to reflect that intention.²¹



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings New York lawyers:

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¹ 2015 No. 85, at 2 (N.Y. June 11, 2015), available at <http://www.courts.state.ny.us/ctapps/Decisions/2015/Jun15/85opn15-Decision.pdf>.

² *Id.* at 2-3.

³ *Id.* at 3.

⁴ *Id.* at 4.

⁵ *Id.*

⁶ *Id.*

⁷ *Id.* at 6.

⁸ *Id.* at 7.

⁹ *Id.*

¹⁰ *ACE Sec. Corp. v. DB Structured Prod., Inc.*, 40 Misc. 3d 562, 567 (N.Y. Sup. Ct. 2013) (internal quotations and citations omitted).

¹¹ *Id.*

¹² *ACE Sec. Corp. v. DB Structured Prod.*, 112 A.D. 3d 522, 523 (1st Dep't 2013).

¹³ *Id.* at 523.

¹⁴ *Id.*

¹⁵ *ACE Sec. Corp.*, 2015 No. 85, at 2, 9 (internal citation and quotations omitted).

¹⁶ *Id.* at 2; *see also id.* at 13, n.4 (collecting cases).

¹⁷ *Id.* at 2, 10-12.

¹⁸ *Id.* at 12.

¹⁹ *Id.* at 13.

²⁰ *Id.* at 2, 17-18.

²¹ *Id.* at 14; *see also id.* at 11-12.

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