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 The Segregated Account of Ambac Assurance Corporation*

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

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AMBAC ASSURANCE CORPORATION and	:	
THE SEGREGATED ACCOUNT OF AMBAC	:	
ASSURANCE CORPORATION,	:	Index No. 651359/2013
	:	
Plaintiffs,	:	
	:	
- against -	:	<b><u>AMENDED COMPLAINT</u></b>
	:	
NOMURA CREDIT & CAPITAL, INC. and	:	
NOMURA HOLDING AMERICA INC.	:	
	:	
Defendants.	:	

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Plaintiffs Ambac Assurance Corporation ("Ambac") and the Segregated Account of Ambac Assurance Corporation (the "Segregated Account," collectively with Ambac, "Plaintiffs"), for their amended complaint against Defendants Nomura Credit & Capital, Inc. ("NCCI") and Nomura Holding America Inc. ("Nomura Holding," collectively with NCCI, "Defendants"), allege as follows:

**NATURE OF ACTION**

1. This is an action for fraudulent inducement and breach of contract arising from

NCCI's egregious misrepresentations and failure to abide by its contractual obligations concerning the securitization of mortgage loans that were ultimately sold to two residential mortgage-backed securities ("RMBS") trusts: Nomura Asset Acceptance Corporation, Alternative Loan Trust, Series 2007-1 ("NAAC 2007-1") and Nomura Asset Acceptance Corporation, Alternative Loan Trust, Series 2007-3 ("NAAC 2007-3") (together, the "Transactions" or "Trusts").

2. In order to induce Ambac's participation in the Transactions, NCCI made numerous fraudulent misrepresentations directly and indirectly to Ambac *in advance of closing* with respect to (a) the characteristics of the loans pooled for the Transactions, (b) the underwriting guidelines purportedly followed, and (c) the due diligence purportedly conducted to prevent defective mortgage loans from entering the securitizations. NCCI also provided in the agreements *executed in connection with closing* numerous contractual representations and warranties to Ambac regarding the quality of the loans to give Ambac comfort that it could rely on NCCI's various pre-closing representations. NCCI knew—or recklessly disregarded—that these pre-closing representations and contractual warranties, going to the very premise of the securitizations, were false and misleading when made, and NCCI has totally disavowed its obligations under the remedies it agreed to for breaches of those representations and warranties.

3. When representing to Ambac prior to the closing of the Transactions that it conducted rigorous due diligence on the loans that served as collateral for the certificates issued by the Trusts (the "Mortgage Loans"), NCCI failed to disclose that it knowingly and systematically disregarded underwriting standards and ignored unfavorable due diligence results. Indeed, when it was informed by due diligence reports that a substantial percentage of loans in its collateral pools were defective, NCCI nonetheless "waived in" a substantial percentage of

those defective loans and included them in its transactions. According to a report issued by Clayton Holdings, LLC ("Clayton")—a third-party due diligence firm hired by NCCI prior to securitizing the loans in the Transactions—that was publicly disclosed in the January 2011 report by the Financial Crisis Inquiry Commission ("FCIC Report"),<sup>1</sup> NCCI knowingly included in the NAAC 2007-1 Transaction *nearly half* of the loans Clayton had identified as both failing to comply with applicable underwriting guidelines and lacking any compensating factors.

4. In light of these revelations about NCCI's due diligence practices, it is clear that NCCI also knew—or recklessly disregarded—that the detailed loan-level information it provided in advance of closing to Ambac and to investors, that was supposed to contain the true and accurate attributes of the loans proposed for securitization, in fact contained false and misleading data. The due diligence reports from Clayton and others that notified NCCI about defective loans would have demonstrated that certain information contained in the loan files and loan tapes—for example, borrower income, occupancy status, or property value—was false.

5. This conclusion is corroborated by the findings of Ambac's consultant. When the losses on the Transactions began to mount, Ambac, through its counsel, retained a third-party consultant to review the documentation pertaining to the Mortgage Loans. Ambac's consultant has to date reviewed over 1,800 of the Mortgage Loans and has found that, in *over 95%* of them (the "Identified Defective Loans"), one or more of the representations and warranties NCCI made regarding the quality of the loans was false when made. These breaches have materially and adversely affected the value of the Mortgage Loans, and Plaintiffs' interests in those loans. This extraordinarily high breach rate, and the egregious nature of the defects observed in the Mortgage Loans, shows that NCCI knew or recklessly disregarded that the pre-closing

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<sup>1</sup> The FCIC Report is available at [http://fcic-static.law.stanford.edu/cdn\\_media/fcic-reports/fcic\\_final\\_report\\_full.pdf](http://fcic-static.law.stanford.edu/cdn_media/fcic-reports/fcic_final_report_full.pdf) (last visited September 18, 2014).

representations it made concerning the characteristics of the Mortgage Loans and NCCI's underwriting and due diligence protocols were false and misleading when made, and in fact NCCI had abandoned sound underwriting and due diligence practices and knew that the Transactions were filled with loans that failed to meet underwriting standards and were rife with fraud.

6. In addition to misrepresenting the characteristics of the Mortgage Loans and the due diligence practices used to ensure they complied with applicable underwriting standards, NCCI misrepresented the underwriting standards that had been applied to the Mortgage Loans. To induce its participation shortly before closing, NCCI gave Ambac one set of underwriting guidelines, and then, once Ambac's consultant undertook the review described above in order to determine whether the Mortgage Loans complied with those guidelines and the other representations and warranties NCCI made regarding the quality of the loans, NCCI asserted (for the first time) that the guidelines it gave to Ambac in advance of closing did not actually apply, and that its prior representations concerning the applicable guidelines were false.

7. In addition to its pre-closing representations, NCCI made numerous representations concerning the Mortgage Loans in the agreements governing the Transactions. To effectuate the Transactions, NCCI purchased the Mortgage Loans from various mortgage loan originators. NCCI sold the Mortgage Loans to Nomura Asset Acceptance Corporation ("NAAC") pursuant to Mortgage Loan Purchase Agreements ("MLPAs"). NAAC thereafter sold and assigned all of its rights in the Mortgage Loans to the Trusts pursuant to Pooling and Servicing Agreements ("PSAs"). The Trusts then issued certificates (the "Certificates") to investors, backed by the expected cashflows from the Mortgage Loans. Ambac, a financial guaranty insurance company, issued insurance policies (the "Policies") that guaranteed payments

due on certain classes of those certificates (the "Insured Certificates") in the event the underlying loans did not provide sufficient payments of principal and interest.

8. In the MLPAs, NCCI made numerous representations and warranties (the "Mortgage Loan Representations"). The PSAs—to which NCCI was a party and Ambac an express third-party beneficiary—incorporated these Mortgage Loan Representations by reference. NCCI represented, among other things, that each of the loans had been properly underwritten, that the loans were not infected by fraud on the part of any person, and that the borrowers were not in breach of their obligations. NCCI's Mortgage Loan Representations were false on a massive scale. As a result, Ambac has suffered enormous damages and will continue to suffer additional damages.

9. Both the representations made by NCCI in advance of the closing and the Mortgage Loan Representations were critical to Ambac's decision to participate in the Transactions and to issue the Policies. In entering into the Transactions, NCCI assumed the risk that the Mortgage Loans did not conform to the Mortgage Loan Representations, while Ambac assumed the risk that Mortgage Loans that *did* conform to those Mortgage Loan Representations would not perform. In agreeing to provide financial guaranty insurance, Ambac relied on the accuracy of the information NCCI provided to Ambac via the pre-closing representations and the Mortgage Loan Representations to assess the risk of insuring the Transactions.

10. NCCI's motive in misleading Ambac is clear. It sought to obtain Ambac's insurance policies in order to decrease the risk to investors from a shortfall in mortgage loan payments to the Trusts, and thereby make the Insured Certificates more attractive and marketable to those investors. Accordingly, NCCI misleadingly portrayed to Ambac that the Transactions presented manageable, insurable risk. NCCI's false statements enabled it to sell loans to the

Trusts that presented a materially greater risk of default than loans conforming to the Mortgage Loan Representations.

11. In fact, the Mortgage Loans have defaulted at a staggering rate. As of July 2014, approximately half of the loans in the pools for which Ambac provided insurance, measured by original principal balance, have defaulted or become severely delinquent. This has deprived the Trusts of the cashflows necessary to pay down the Certificates. As a direct result of these shortfalls, Plaintiffs have suffered substantial damages. As of June 2014, Plaintiffs have paid over \$100 million in claims under the Policies and have accrued nearly \$90 million in additional claims. Moreover, Plaintiffs estimate that they will suffer tens of millions of dollars in additional claims under the Policies.

12. In addition to incorporating the Mortgage Loan Representations by reference, the PSAs provide Ambac with an expedited remedy for violations of the Mortgage Loan Representations. Specifically, NCCI must cure or repurchase Mortgage Loans as to which it discovers or receives notice of breaches of the Mortgage Loan Representations, where such breaches materially and adversely affect Ambac's interests in the Mortgage Loans. This repurchase remedy (the "Repurchase Protocol") gave Ambac further comfort in agreeing to insure the Insured Certificates, because it provided for an expeditious resolution in the event that a small number of breaching loans were inadvertently included in the Transactions.

13. When Ambac learned of the pervasive breaches of the Mortgage Loan Representations uncovered by its third-party consultant, it notified both NCCI and HSBC Bank, USA, National Association ("HSBC"), as Trustee of the Trusts, and provided detailed and loan-by-loan descriptions of the breaches. HSBC, pursuant to the PSAs, in turn demanded that NCCI comply with its contractual obligation to cure the breaches or repurchase the breaching loans at

the contractually specified repurchase price. To date, *NCCI has refused to repurchase a single loan*, wholly repudiating its obligations under the PSAs.

14. On information and belief, in view of the extremely high breach rate identified by Ambac's consultant, the egregious nature of those breaches, and the revelations about NCCI's due diligence practices, NCCI must have been aware of the Mortgage Loan Representation breaches and of the materially false information about the Mortgage Loans that it provided to Ambac prior to entering into the Transactions (long before its receipt of Ambac's and HSBC's notifications). Since NCCI knew at the outset that many of the Mortgage Loan Representations were false, it has been on notice of the breaches since before the closing dates of the Transactions.

15. NCCI's pre-closing representations, the Mortgage Loan Representations and the Repurchase Protocol were essential to Ambac's decision to issue the Policies. If Ambac had not received the pre-closing representations and the Mortgage Loan Representations or had known, as it now knows, that they were false on such a large scale, it would not have issued the Policies and Plaintiffs would not have incurred enormous damages and would not face tens of millions of dollars in additional claims.

16. On information and belief, Nomura Holding, which shares management and offices with NCCI, exercised and continues to exercise complete domination and control over NCCI, both in general and specifically as to NCCI's conduct before and after the closing of the Transactions. Nomura Holding used its domination and control over NCCI to cause it to knowingly disseminate false information to Ambac to induce Ambac to insure the Transactions and to make false Mortgage Loan Representations. Further, Nomura Holding also intervened in the Repurchase Protocol by causing NCCI to refuse to repurchase any of the loans which it is

contractually obligated to repurchase.

17. Plaintiffs are therefore entitled to relief from NCCI and Nomura Holding for NCCI's fraudulent misrepresentations and omissions and pervasive and material breaches of the parties' agreements, including damages sufficient to put Plaintiffs in the same place they would be in had Ambac never issued the Policies insuring the Transactions.

### **PARTIES**

18. The actual and projected claims under the Policies contributed to the financial deterioration of Ambac, a Wisconsin-domiciled insurer. On March 24, 2010, the Wisconsin Office of the Commissioner of Insurance approved the creation of the Segregated Account pursuant to Wisconsin Statutes § 611.24. That same day, the Wisconsin Circuit Court for Dane County, upon the Verified Petition of the Commissioner of Insurance (the "Commissioner"), placed the Segregated Account into statutory rehabilitation under Wisconsin Statutes §§ 645.31 and 645.32. Pursuant to Wisconsin Statutes § 611.24(3)(e), the Segregated Account is a separate Wisconsin insurer with the legal capacity and authority to sue in its own name and right. Ambac allocated the policies and claims at issue in this action to the Segregated Account pursuant to the Plan of Operation for the Segregated Account attached to the Commissioner's Verified Petition (the "Plan of Operation").

19. The Commissioner is the court-appointed Rehabilitator of the Segregated Account. As Rehabilitator, the Commissioner has the authority to prosecute the claims in this action on behalf of the Segregated Account. Pursuant to Wisconsin Statutes § 645.33(1), the Commissioner has appointed a full-time Special Deputy Commissioner to rehabilitate the Segregated Account.

20. Ambac is a Wisconsin corporation that maintains its principal place of business at

One State Street Plaza, New York, New York 10004. Under the Plan of Operation, Ambac performs specified management services for the Segregated Account and retains the right to receive any cash recoveries relating to the policies and claims that were allocated to the Segregated Account, including the policies and claims at issue in this action.

21. Defendant NCCI is a Delaware corporation with its principal place of business at 2 World Financial Center, New York, New York 10281. NCCI is a wholly owned subsidiary of Nomura Holding.

22. Defendant Nomura Holding is a Delaware corporation with its principal place of business at 2 World Financial Center, New York, New York 10281.

### **JURISDICTION AND VENUE**

23. This Court has jurisdiction over this proceeding pursuant to CPLR §§ 301 and 302 because the Defendants have offices in New York and are licensed to do business in New York. Additionally, NCCI made the relevant representations and warranties, and undertook the relevant obligations, in agreements expressly governed by New York choice-of-law clauses.

24. Venue is proper in this Court pursuant to CPLR § 503(a) and (c) because the Plaintiffs' principal executive offices are in New York County and because Defendants are foreign corporations authorized to transact business in the State of New York with their principal New York offices in New York County.

### **FACTUAL ALLEGATIONS**

#### **A. The NAAC 2007-1 and 2007-3 Transactions**

25. The NAAC 2007-1 and 2007-3 Transactions were effectuated through a series of agreements executed on or about May 10, 2007 and July 10, 2007, respectively. The Mortgage Loans included in the Transactions consist of adjustable-rate, first-lien mortgage loans,

originated by various mortgage lenders.

26. NCCI obtained Ambac's insurance policies for the benefit of the investors in the Insured Certificates issued in the Transactions in order to decrease the risk to those investors from a shortfall in mortgage loan payments to the Trusts, and thereby make the Insured Certificates more attractive and marketable to those investors. The NAAC 2007-1 Trust consisted of two loan "Groups," each of which consisted of a separate, non-overlapping pool of loans. Ambac insured a senior mezzanine class of Certificates (Class II-A-M) backed by the Group II loan pool, which included 2,248 loans with an aggregate principal balance of over \$769 million. Ambac insured all the senior classes of Certificates in the NAAC 2007-3 Transaction, which included 1,240 loans with an aggregate principal balance of over \$389 million.

**B. NCCI Fraudulently Induces Ambac's Participation in the Transactions**

27. In advance of the closing of each of the Transactions, NCCI made myriad false and misleading representations directly and indirectly to Ambac to induce its participation and complete the intended Transaction. From Ambac's perspective, given that its claims-payment obligations under its Policies would be triggered only in the event that payments of principal and interest from loans could not support the requisite payments to Certificate investors, the quality of those loans was paramount. Thus, Ambac sought information about the loans, the practices used in originating them, and NCCI's due diligence and quality control processes. NCCI gave Ambac extensive information on these subjects—but it was all false.

28. *First*, NCCI made disclosures to Ambac concerning its securitization operations and due diligence practices. *Second*, NCCI provided to Ambac, directly and through Bear Stearns, the lead underwriter of the Transactions, mortgage loan "tapes," Offering Documents, and other files that were supposed to contain, for the loans proposed for securitization, the true

and accurate attributes critical to assess the risks associated with the loans. *Third*, NCCI made representations to Ambac concerning the underwriting guidelines that were applicable to the securitized loans.

i. ***NCCI Falsely Represents Its Due Diligence Practices***

29. To induce Ambac to participate in the Transactions, NCCI made a series of false pre-closing representations and omitted material information concerning the due diligence protocols and practices it purportedly had in place to prevent defective mortgage loans from entering the securitizations.

30. For example, prior to the closing of the NAAC 2007-1 Transaction, Mendy Sabo and others at NCCI provided to Ambac, during an April 19, 2007 phone call and an April 24, 2007 meeting, details concerning the due diligence it purportedly performed on the loans proposed for securitization, as well as NCCI's method of finding and approving originators. Specifically, NCCI represented that it (i) conducted "credit and compliance" due diligence reviews on 100% of the Transaction loans that were acquired from its loan-by-loan and mini-bulk loan channels, (ii) reviewed a minimum of 25% of the loans that were acquired from its bulk loan channel, and (iii) tested property values on all loans using Automated Valuation Model ("AVM") reviews. NCCI represented that these due diligence reviews were performed by third parties, including Clayton, Lydian, and American Mortgage Consultants. NCCI also represented that it generally purchased loans from the same originators, and that it also performed due diligence on originators and terminated those that had performance issues.

31. As with the 2007-1 Transaction, prior to the closing of the NAAC 2007-3 Transaction, NCCI represented to Ambac that it (i) conducted "credit and compliance" due diligence reviews on 100% of the Transaction loans that were acquired from its loan-by-loan and

mini-bulk loan channels, (ii) reviewed a minimum of 25% of the loans that were acquired from its bulk loan channel, and (iii) tested property values on all loans using AVM reviews.

32. In addition, on June 26, 2007, Mendy Sabo of NCCI sent Ambac a due diligence "summary" report. This report consisted of a one-page spreadsheet showing that NCCI conducted rigorous due diligence practices, including due diligence reviews of 87% of the loans in the NAAC 2007-3 Transaction. In addition, the report showed that NCCI tested property values on 100% of the loans using AVM reviews, and 7.05% were also subject to a Broker Price Opinion ("BPO") review. The report also gave the same data for the top two originators of the loans in the NAAC 2007-3 Transaction—American Home Mortgage and BrooksAmerica Mortgage—and indicated that NCCI had conducted due diligence for 100% of the BrooksAmerica loans in the Transaction and 54.47% of the American Home Mortgage loans in the Transaction. The diligence summary also showed that NCCI declined to purchase around 11% of the approximately 6,000 loans in the "trades" offered by originators to NCCI from which loans in the NAAC 2007-3 Transaction were selected.

33. These communications, which NCCI intended to provide additional assurances to Ambac regarding the quality of the loans and the integrity of NCCI's protocols, were materially false and misleading. NCCI did not disclose to Ambac that it knowingly and systematically disregarded underwriting standards and ignored unfavorable due diligence results. NCCI did not disclose to Ambac that when it was informed by its due diligence and quality review process that a substantial percentage of the loans in its collateral pools were defective, NCCI nonetheless "waived in" a substantial percentage of those defective loans and included them in its transactions.

34. As described in the January 2011 FCIC Report, securitizers of mortgage loans

such as NCCI often used third-party firms to conduct due diligence on the pools of mortgages that went into the securitizations. FCIC Report at 165-66. One of the major providers of such third-party diligence was Clayton. *Id.* at 166.

35. Firms like Clayton reviewed samples of individual loans in the pools meant for securitization, in order to determine whether the loans met applicable underwriting guidelines. *Id.* Clayton also analyzed whether, to the extent a loan was deficient, there were any "compensating factors." *Id.* "For example, if a loan had a higher loan-to-value ratio than guidelines called for, did another characteristic such as the borrower's higher income mitigate that weakness?" *Id.* Clayton graded the loans on a scale of 1 to 3: loans graded "1" met applicable underwriting guidelines; those graded "2" did not, but had "compensating factors"; and those graded "3" both failed to meet applicable guidelines and had no compensating factors. *Id.* These grades were reported to the financial institutions securitizing the loans. *Id.*

36. According to the FCIC Report, Clayton produced "Trending Reports" summarizing the results of such reviews. *Id.* at 167. One such Trending Report, covering the period between the first quarter of 2006 and the second quarter of 2007, and attached to this Amended Complaint as Exhibit 2 (the "Clayton Report"), summarized results for Clayton's review of loans pooled into five Nomura securitizations, including NAAC 2007-1. The Trending Report (at page 8) shows that Clayton initially rejected 1,188 loans of the 3,366 loans it reviewed in connection with the NAAC 2007-1 Transaction—that is, Clayton graded approximately 35% of the loans it reviewed for the NAAC 2007-1 pool a "3" for failing to comply with applicable underwriting standards and lacking compensating factors. Nevertheless, NCCI "waived" nearly half of those loans—47%—into the NAAC 2007-1 Trust.

37. The Clayton Report—which NCCI had in its possession but never disclosed to

Ambac—shows that, in the NAAC 2007-1 Transaction, NCCI knowingly included nearly half of the loans Clayton had identified as both failing to comply with applicable underwriting guidelines and lacking any compensating factors. The Clayton Report makes clear that NCCI knew at the time they were made that the representations it made to Ambac concerning its due diligence practices were demonstrably false.

38. Furthermore, the extraordinary breach rate that Ambac's consultant found in its review of the over 1,800 loans provides further evidence that NCCI knew or recklessly disregarded that the due diligence it directed was a sham and that the results were false and misleading. Ambac would not have entered into the Transactions had it known that NCCI's disclosures concerning its due diligence practices were false and misleading.

ii. ***NCCI Knowingly Disseminated Materially False and Misleading Mortgage-Loan Tapes and Other Information Concerning the Mortgage Loans***

39. To induce Ambac to participate in the Transactions, NCCI also provided to Bear Stearns, lead underwriter for the Transactions, false and misleading information concerning the mortgage loans proposed for securitization, with the knowledge and intent that Bear Stearns would in turn pass on this false information to Ambac prior to the closing of the Transactions, and that Ambac would rely—and Ambac did rely—upon this information in determining whether to participate in the Transactions.

40. On April 16, 2007, prior to the closing of the 2007-1 Transaction, Matthew Perkins of Bear Stearns sent an e-mail to Ambac stating that "Nomura and Bear Stearns are interested in a proposal from Ambac" to issue insurance policies for the Transaction. His email attached a document that contained numerous fields of information pertaining to the loans in the Transaction. Specifically, the document contained a breakdown of documentation and occupancy types of the loans, as well as weighted average loan-to-value ratios ("LTV") for each

loan (which measured the amount of mortgage debt that encumbers a property against the value of the property), debt-to-income ratios ("DTI") (which compared payments due on a borrower's monthly debts to a borrower's income), and FICO (or credit) scores. The underlying information in this document was provided to Bear Stearns by NCCI, which had acquired the securitized loans and was the sponsor of the Transaction. When providing this information to Bear Stearns, NCCI knew and intended that Bear Stearns would then pass on the information to Ambac in order to induce its participation in the Transaction.

41. In addition, on April 18, 2007, NCCI sent Matthew Perkins (of Bear Stearns) a spreadsheet showing S&P and Moody's ratings levels for the 2007-1 Transaction, which Perkins in turn forwarded to Ambac the same day. On April 18, 2007, Jacquelyn Amato of Bear Stearns sent Ambac information concerning the originators in the Transaction, which she had received "directly from Nomura," as well as "loan tapes" for the Transaction, which detailed information concerning LTV ratios, FICO scores, occupancy statuses, and documentation types. The underlying loan information in the loan tapes was also provided to Bear Stearns by NCCI, and when NCCI provided this information to Bear Stearns, it knew and intended that Bear Stearns would then pass on the information to Ambac in order to induce its participation in the Transaction.

42. Similarly, prior to the closing of the 2007-3 Transaction, NCCI provided information to Bear Stearns concerning the mortgage loans proposed for securitization, with the knowledge and intent that Bear Stearns would in turn provide that information to Ambac. On June 22, 2007, Gregory Rakovsky of Bear Stearns sent Ambac a "loan-level tape" for the Transaction containing detailed information concerning LTV ratios, FICO scores, occupancy statuses, and documentation types. Also on June 22, 2007, Sally Kawana of Bear Stearns sent

Ambac: (i) a document that included weighted average FICO, LTV, and DTI data, as well as information on the occupancy and documentation type of the Transaction loans; (ii) a spreadsheet containing loan-level data; and (iii) a spreadsheet showing rating agency loss coverage levels for the pool. Again, the underlying loan information in the loan tapes and other information Bear Stearns sent to Ambac in advance of closing was provided to Bear Stearns by NCCI, which knew and intended that Bear Stearns would then pass on the information to Ambac in order to induce its participation in the Transaction.

43. Ambac required and relied on the loan tapes and other loan-level information it received as a critical component in deciding whether to provide insurance for the Transactions. Ambac used the data on the tapes as inputs to its risk models, and analyzed the loan metrics, which were central to assessing the risk associated with the loan pools and predicting the expected likelihood and severity of defaults by the borrowers. NCCI knew and intended that Ambac would rely on the veracity of the loan-level information it received to evaluate the Transactions and assess the "market risks" pertaining to the loans.

44. Owner-occupancy statistics were material to Ambac because homeowners who reside in mortgaged properties are less likely to default (which would result in eviction from their homes) than owners who purchase homes as investments or second homes and live elsewhere.

45. Likewise, LTV ratios were material to Ambac because higher LTV ratios are correlated with a higher risk of default. A borrower with a small equity position in a property has less to lose if he or she defaults on the loan. Additionally, the higher the LTV ratio, the greater the likelihood that a foreclosure will result in a loss for the lender. LTV ratio is a common metric for analysts and investors to evaluate the price and risk of mortgage-backed securities.

46. DTI ratios were material to Ambac because the higher the borrower's DTI ratio, the greater the risk that the borrower will have difficulty repaying the loan.

47. In light of the revelations about NCCI's due diligence practices discussed above, it is clear that NCCI fully understood the failings of those controls and, therefore, knew that the loan tapes and other pre-closing loan-level information it provided contained false and misleading data—or recklessly disregarded the veracity of the disclosures. As described above, the Clayton Report—which NCCI had in its possession but never disclosed to Ambac—shows that NCCI knowingly included nearly half of the loans Clayton had identified as both failing to comply with applicable underwriting guidelines and lacking any compensating factors. Although the Clayton Report does not detail the types of defects Clayton found in the 1,188 loans in the NAAC 2007-1 pool it rejected (or in the nearly half of those loans NCCI nonetheless "waived" into the NAAC 2007-1 Trust), Clayton's due-diligence reviews typically involved determinations, for example, that the borrower's income was overstated (which would render the DTI-ratio information NCCI provided false), that the borrower's occupancy status was misrepresented (which would render the occupancy status information NCCI provided false), or that the appraisals of the subject property overstated its value (which would render the LTV-ratio information provided false).

48. Indeed, Ambac's consultant's loan-level reviews of loans in the Transactions described below have confirmed that the loan tapes and other loan-level information provided to Ambac contained materially false and misleading data regarding, among other things, DTI and LTV ratios, and occupancy status.

iii. ***NCCI Knowingly Made Materially False and Misleading Representations and Disclosures in the Offering Documents Used to Market and Sell the Certificates***

49. NCCI marketed the securities issued in its securitizations, including the

Transactions, pursuant to Free Writing Prospectuses ("FWPs"), Prospectuses, and Prospectus Supplements ("ProSupps") (collectively, "Offering Documents"), that were publicly filed with the SEC pursuant to the Securities Act of 1933. As a matter of law, the Offering Documents were required to disclose all material facts concerning the securities offered; not contain any untrue statement of material fact concerning the securities; not omit to disclose any material fact concerning the securities; and not omit to state a material fact necessary to make the statements made therein, in light of the circumstances in which they were made, not misleading.

50. In advance of the closing date of the Transaction, NCCI prepared and sent to Ambac, directly and through its counsel and through Bear Stearns, several drafts of the Offering Documents for the Transactions to induce its participation in the Transaction. The drafts contained false and misleading statements and omissions similar to those made in Offering Documents eventually filed with the SEC.

51. NCCI knew and intended that Ambac and investors would rely on the draft and final Offering Documents in assessing whether to participate in the Transaction. That was the very purpose for which the documents were created and disseminated. Through these disclosures, NCCI deliberately misled investors and induced Ambac to provide financial-guaranty insurance for securitizations plagued by defective loans that did not comport with the characteristics represented in the Offering Documents.

52. The disclosures in the Offering Documents of the risks associated with the Transactions were false and misleading in that they (i) presented false and misleading data metrics pertaining to the securitized loan pools, (ii) provided false and misleading ratings, and (iii) failed to disclose NCCI's complete abdication of its due-diligence and quality-control processes, which it knew resulted in the securitization of pools replete with defective loans.

53. **Loan data:** The Offering Documents contained detailed appendices purporting to represent critical statistical data for stratified segments of the loan pools, including LTV ratios, credit scores, occupancy characteristics, and documentation types. These characteristics were used by Ambac and potential investors to evaluate the risks and expected performance of the underlying loan pools for the securities issued in each Transaction. As discussed below, based on its due diligence and quality control, NCCI knew that these loan characteristics, as disclosed in the Offering Documents, were materially false and misleading in that they significantly understated the credit risk of the securitized loans.

54. **Ratings:** The Offering Documents provided that the Certificates would not be offered unless they received the ratings from Standard & Poor's and Moody's set forth in the ProSupps. Standard & Poor's and Moody's assigned both final ratings and "shadow ratings" for the Transactions. A final rating is an assessment of the risk of the security taking the financial-guaranty insurance policy into consideration, whereas a shadow rating is an assessment of the risk without consideration of the protection afforded by the financial-guaranty policy. For each of the Transactions, the rating agencies assigned final ratings of "AAA" (Standard & Poor's) and "Aaa" (Moody's) to the Certificates that had the benefit of Ambac's Policies. These triple-A final ratings were given in reliance on Ambac's Policies, and Ambac in turn relied on the shadow ratings assigned by the rating agencies for the Transactions in agreeing to issue the Policies. The shadow ratings assigned for the Transactions were materially misleading in that they were fraudulently obtained from the rating agencies on the basis of NCCI's false and misleading representations concerning the characteristics of the securitized loans and NCCI's omissions of material facts regarding its securitization operations and practices. Had NCCI made truthful and complete disclosures to the rating agencies, the shadow ratings would not have been obtained,

and Ambac would not have issued its Policies.

iv. ***NCCI Falsely Represented the Applicable Underwriting Guidelines***

55. NCCI also induced Ambac to participate in the Transactions by falsely representing the underwriting guidelines that applied to the securitized loans.

56. On April 24, 2007, after a meeting where Ambac raised some of its concerns with the NAAC 2007-1 Transaction, Mendy Sabo of NCCI e-mailed Ambac the "latest" version of Nomura's underwriting guidelines. NCCI disclosed no other underwriting guidelines to Ambac. NCCI knew that Ambac was interested in reviewing the guidelines governing the NAAC 2007-1 Transaction and also knew that Ambac would not participate in the Transaction unless the guidelines applied to the Mortgage Loans met minimum underwriting standards. In disclosing only the Nomura guidelines, NCCI intended Ambac to believe—and Ambac reasonably believed—that the Nomura guidelines were the minimum guidelines that applied to loans in the Transactions.

57. NCCI's pre-closing representations concerning the applicable guidelines were false. As discussed in greater detail below, only after Ambac's consultant reunderwrote a substantial number of the Mortgage Loans, at great cost and expense to Ambac, did NCCI assert, for the first time, that the guidelines sent to Ambac shortly before closing did not actually apply to the Transactions.

v. ***NCCI's Knowledge of Misrepresentations, Omissions, and False Information Provided to Ambac***

58. The representations NCCI made concerning the Mortgage Loans and the underwriting and due diligence practices used to originate and securitize them markedly diverged from reality. Ambac's consultant's loan-level reviews of loans in the Transactions described below have confirmed that the loan tapes and other loan-level information provided to Ambac

contained materially false and misleading data regarding, among other things, DTI and LTV ratios and occupancy status.

59. NCCI's motive in misleading Ambac is clear. It sought to obtain Ambac's insurance policies in order to decrease the risk to investors from a shortfall in mortgage loan payments to the Trusts, and thereby make the Insured Certificates more attractive and marketable to those investors. Accordingly, NCCI misleadingly portrayed to Ambac that the Transactions presented manageable, insurable risk.

60. NCCI induced Ambac to participate in the Transactions by failing to disclose, and affirmatively concealing, that it implemented policies and abandoned controls to churn out securitizations that it knew, or recklessly disregarded, were replete with loans that did not conform with the represented attributes, were originated in total disregard of actual or prudent underwriting standards, and were made without regard to borrowers' ability to repay. NCCI knew that the loan tapes and other pre-closing loan-level information it provided to Ambac contained false and misleading data—or recklessly disregarded the veracity of its disclosures.

61. Given its relationship with and history of purchasing loans from the same originators, NCCI knew that large numbers of the mortgage loans it securitized were issued by originators without regard to borrower ability to pay and other basic underwriting standards. In particular, the due diligence it performed gave NCCI all the information it needed to discover the systemic departure from underwriting guidelines.

62. As described above, the vast majority of the loans in the Transactions were subject to routine diligence reports, which told NCCI that the loans frequently failed to meet requisite underwriting guidelines and lacked adequate compensating factors. In particular, the Clayton Report makes clear that NCCI and Nomura Holding knew at the time they consummated

the Transaction—but did not disclose to Ambac—that a significant portion of the loans sold to the NAAC 2007-1 Trust failed to meet the requisite underwriting guidelines.

63. In sum, as a result of its close relationship with originators, its access to the loan files, the due diligence results it received, as well as the extraordinarily high breach rate uncovered by Ambac and the egregious nature of the defects observed in the Mortgage Loans, NCCI was plainly aware that the Transactions were filled with loans that failed to meet underwriting standards and were rife with fraud, and that much of the information in the loan tapes, Offering Documents, and other information NCCI provided to Ambac, directly and through Bear Stearns, was false.

**C. Ambac Reasonably Relied Upon NCCI's Misrepresentations**

64. As particularized in the preceding sections, NCCI knowingly and with the intent to induce reliance thereon made material misrepresentations to Ambac and actively concealed material information pertaining to the Transactions and NCCI's operations. Ambac reasonably relied to its detriment on NCCI's false and misleading representations and omissions. Ambac would not have agreed to participate in the Transactions had it known that NCCI's representations were false and/or omitted critical information that was required to make them not misleading.

65. Ambac's reliance on NCCI's representations was reasonable and consistent with the industry practice and the parties' bargain. As was the general practice and the parties' agreement, Ambac and NCCI assumed risk and undertook due diligence consistent with their respective roles in the Transactions.

66. NCCI and Ambac played very different roles in the Transactions. NCCI acquired all the Mortgage Loans from various originators. NCCI had long-term relationships with many

of these originators and claimed to have thoroughly vetted these originators for the purpose of procuring loans that NCCI knew would constitute the collateral for RMBS sold in the public securities market. Ambac insured certain certificates for which the Mortgage Loans served as collateral. Each party assumed the risks attendant to its respective role.

67. That was a reasoned risk allocation. NCCI was in privity with—and often financed—the originators that sold the loans that it in turn conveyed to the securitization trusts. NCCI dictated the underwriting guidelines, owned the loans and held the loan files, all of which afforded it access to and control over information required to evaluate the loans. To the extent NCCI identified any defect in any loans, it had the right to exclude the loans from any transaction with the entity selling the loans or to demand that the entity repurchase the loans if the defects were discovered after purchase. NCCI thus had the means before the closing of the Transactions to assess the quality of the loans and recourse in the event a defect was discovered.

68. In contrast, Ambac was not in privity with and lacked recourse against the originators, never owned the loans or the loan files, and therefore didn't have the opportunity to review the loans before deciding whether to participate in the Transactions. What Ambac did have, however, were NCCI's numerous representations about the loans. Recognizing the critical importance of these representations, Ambac also insisted, as sophisticated parties typically do, that NCCI reduce many of these representations to enforceable warranties in the parties' written agreements. As explained below, NCCI did so. It therefore made sense for the sophisticated parties to agree that NCCI would bear the loan-origination risk, and that Ambac, relying on the truth of NCCI's representations, would bear the market risk.

69. This risk-allocation arrangement enabled each party to conduct the appropriate

due diligence consistent and commensurate with the risk each party bore. NCCI purported to carefully vet the originators from which it bought the loans and conduct reviews of the loans themselves.

70. Ambac, in turn, (i) secured and evaluated NCCI's pre-closing representations concerning the underwriting and due diligence protocols it purportedly performed, (ii) conducted extensive modeling of its exposure to interest rate and other market variables using the loan data provided by NCCI, and (iii) secured from NCCI its commitment to provide extensive contractual representations and warranties concerning, among other things, the veracity of the mortgage-loan data that NCCI provided and the underwriting practices followed in the origination of the loans.

71. These numerous representations and warranties that NCCI provided, and on which Ambac relied, were the means by which the parties effectuated this reasoned risk allocation, and therefore, were an essential inducement for Ambac to participate in the Transactions.

#### **D. NCCI's Mortgage Loan Representations Concerning the Transaction**

72. As part of both the NAAC 2007-1 and 2007-3 Transactions, NCCI, as Seller, and NAAC, as Purchaser, entered into the MLPAs. In the MLPAs, NCCI agreed to convey all right, title, and interest in the Mortgage Loans to NAAC.

73. In the MLPAs, NCCI made over forty Mortgage Loan Representations, including the following:

- No fraud was committed by any party to any Mortgage Loan, including the borrowers. MLPAs § 8(ii).<sup>2</sup>
- At the time of closing, none of the Mortgage Loans were in default, and there had not been any breach, violation, or event of acceleration under any mortgage securing any Mortgage Loan. MLPAs § 8(xiv).

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<sup>2</sup> The relevant sections of the MLPAs and the PSAs in the NAAC 2007-1 and 2007-3 Transactions are substantively identical.

- The Mortgage Loans were underwritten in accordance with applicable underwriting guidelines. MLPAs § 8(xli).

74. NCCI conveyed the Mortgage Loans to NAAC pursuant to the MLPAs in exchange for cash. NAAC in turn conveyed the Mortgage Loans to the Trusts for the purpose of using the Mortgage Loans as collateral for the Certificates. The Trusts then issued the Certificates, which were offered for sale to investors. In reliance on the pre-closing information conveyed to it by NCCI and the Mortgage Loan Representations, Ambac issued two irrevocable Policies providing insurance for the Insured Certificates: Certificate Guaranty Insurance Policy # AB1078BE for the NAAC 2007-1 Transaction and Certificate Guaranty Insurance Policy # AB1099BE for the NAAC 2007-3 Transaction.

75. The cashflows from the Mortgage Loans, in the form of payments of principal and interest, are used to pay obligations on the Certificates. The purchase of each Certificate is thus the purchase of a right to participate in the cashflows generated by the Mortgage Loans. Because the Mortgage Loans served as the collateral supporting the Certificates, their credit quality was of critical importance to Ambac and the Certificateholders.

76. Shortly after NCCI and NAAC entered into the MLPAs, (i) NAAC, as Depositor, (ii) NCCI, as Seller and Sponsor, (iii) Wells Fargo Bank, National Association, as Master Servicer and Securities Administrator, (iv) GMAC Mortgage, LLC, as Servicer, and (v) HSBC, as Trustee, entered into the PSAs for the NAAC 2007-1 and 2007-3 Transactions, which provided for the creation of the Trusts and the pooling and servicing of the Mortgage Loans for the purpose of selling the Certificates to investors. Ambac is an express third-party beneficiary of both PSAs, which provide that Ambac, as insurer of the Insured Certificates, "is intended to be and shall have all of the rights of a third-party beneficiary under this Agreement." PSAs § 11.13.

77. The PSAs incorporate by reference the Mortgage Loan Representations made in

Section 8 of the MLPAs. PSAs § 2.03(b)(vii) (NCCI represents and warrants that "[t]he representations and warranties set forth in Section 8 of the Mortgage Loan Purchase Agreement are true and correct as of the Closing Date").

78. In addition to Ambac's legal and/or equitable remedies, the PSAs further entitle Ambac, as a third-party beneficiary, to a contractually prescribed, expedited remedy for breaches of the Mortgage Loan Representations made in Section 8 of the MLPAs, to the extent such breaches "materially and adversely affect[] the interests of the Certificateholders or the Certificate Insurer [i.e., Ambac] in any Mortgage Loan." PSAs § 2.03(c). Under that section, which sets forth the Repurchase Protocol, NCCI must cure the breach or repurchase the breaching loan at the contractually specified price within 90 days of discovering or receiving notice of such a breach.<sup>3</sup>

79. The term "repurchase" is and was well understood in the RMBS industry and by the parties involved in the Transactions. "Repurchase" is the mechanism by which a purchaser is made whole for a seller's breach of representations and warranties, irrespective of the loan's status (e.g., current, delinquent, or liquidated). Consistent with this understanding, the custom and practice in the RMBS industry is to refer to the repurchase of liquidated loans as a "make-whole" payment, because these funds make the securitization trust whole for the loss incurred on the liquidated loan. This custom and practice reflects the industry's understanding that the seller of mortgage loans to be securitized bears the entirety of the risk of loss for any breach of the representations and warranties with respect to the loans (subject to the applicable materiality threshold).

80. Recently, in at least two litigations involving different RMBS transactions,

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<sup>3</sup> For the first two years after the closing dates of the Transactions—a period that has now passed—NCCI had a third option, namely to substitute a non-breaching loan for any breaching loan. PSAs § 2.03(c).

Nomura has asserted that it has no obligation to repurchase any mortgage loan that has been liquidated by the servicer via foreclosure or otherwise. This position, created solely for purposes of litigation, is contrary to many years of custom and practice in the mortgage banking industry.

81. Nomura's new-found position is also contrary to its own practices of repurchasing liquidated loans in connection with RMBS transactions. See Amended Complaint ¶ 82, *Nomura Asset Acceptance Corp., Mortg. Pass-Through Certificates, Series 2006-AF2 v. Nomura Credit & Capital, Inc.*, Index No. 652614/2012 (N.Y. Sup. Ct., N.Y. Cnty., Feb. 26, 2013); February 21, 2013 Letter to the Court in *Nomura Asset Acceptance Corp., Alternative Loan Trust, Series 2005-S4 v. Nomura Credit & Capital, Inc.*, Index No. 653541/2011 (N.Y. Sup. Ct., N.Y. Cnty.) (noting that NCCI repurchased millions of dollars of liquidated loans in connection with Nomura Asset Acceptance Corporation Alternative Loan Trust, Series 2007-S2).

82. Furthermore, since May 2012, NAAC has filed ten quarterly ABS-15G reports with the U.S. Securities and Exchange Commission ("S.E.C."). Each of its filings includes a footnote to the column setting forth "Assets That Were Repurchased or Replaced." The footnote makes clear that "Assets That Were Repurchased or Replaced" "may include assets that were previously liquidated, and for which a make-whole payment was made in lieu of repurchase."<sup>4</sup> Moreover, Nomura Holdings, Inc., the parent company of both Nomura Holding and NCCI, disclosed in its June 2012 Form 20-F report to the S.E.C. that its subsidiaries "have agreed to repurchase certain loans (*or to otherwise compensate the issuing trust*) for those claims that the subsidiaries have determined to have merit" (emphasis added).<sup>5</sup>

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<sup>4</sup> The latest such report is available here:  
<http://www.sec.gov/Archives/edgar/data/888874/000089109214006128/e59396ex99-1.htm> (last visited September 5, 2014).

<sup>5</sup> This report is available here:  
<http://www.sec.gov/Archives/edgar/data/1163653/000119312512285775/d308396d20f.htm> (last visited September 5, 2014).

83. The Repurchase Protocol was expected to quickly and efficiently address the inadvertent inclusion in the Trusts of the aberrant non-complying loan. It was, however, not intended to be an alternative to NCCI's truthful description of the loan pool and its due diligence practices or compliance with the extensive Mortgage Loan Representations it made to Ambac. Indeed, the Repurchase Protocol was not intended, and is inadequate, to address the pervasive, systemic fraud and underwriting deficiencies plaguing the loans that Ambac has uncovered. Accordingly, in addition to any relief Plaintiffs are entitled to under the Repurchase Protocol, Plaintiffs are entitled to more global relief to address failings on such a massive scale.

**E. NCCI's Mortgage Loan Representations Allocated Risks Among the Parties**

84. As discussed above, NCCI and Ambac played very different roles in the Transactions. NCCI acquired all the Mortgage Loans from various originators. NCCI had long-term relationships with many of these originators and claimed to have thoroughly vetted these originators for the purpose of procuring loans that NCCI knew would constitute the collateral for RMBS sold in the public securities market. Ambac insured certain certificates for which the Mortgage Loans served as collateral. Each party assumed the risks attendant to its respective role.

85. Ambac obtained NCCI's Mortgage Loan Representations precisely to cover specifically identified risks associated with the Transactions, including, in particular, the risks associated with poorly underwritten loans and loans that involved fraud by borrowers, brokers, appraisers, or anyone else involved in a loan's origination. NCCI assumed, and continues to bear, the risk that those Mortgage Loan Representations would be false, and Ambac assumed and bears the other risks associated with the loans, *on the condition that they conform to NCCI's representations and warranties*. This was the risk allocation that the parties negotiated and it is

this agreement that NCCI has eviscerated.

86. Ambac would not have issued the Policies had it known, as it now knows, that NCCI had materially and pervasively misrepresented the characteristics of the Mortgage Loans and the risks associated with the mortgage loan pools included in the Transactions and breached its Mortgage Loan Representations to such a degree that it deprived Ambac of the benefit of its bargain.

**F. NCCI's Pervasive Fraudulent Misrepresentations and Omissions and Breaches of Its Mortgage Loan Representations Come to Light**

87. There have been an extremely high number of defaults among the Mortgage Loans. As of July 2014, 47.8% in original principal balance of the Group II loans in the NAAC 2007-1 Transaction (the Group Ambac insured) had defaulted or were severely delinquent (that is, delinquent for 60 days or more). As of the same date, 51.6% in original principal balance of the loans in the NAAC 2007-3 Transaction had defaulted or were severely delinquent.

88. In light of the unusually high default rates among the Mortgage Loans, in August 2009, Ambac advised NCCI that it intended to reunderwrite the Mortgage Loans to determine whether they conformed to NCCI's representations and warranties. To confirm that it was using the right guidelines, Ambac asked NCCI to produce the guidelines governing the Mortgage Loans.

89. Instead of responding to Ambac's request in good faith by providing the applicable guidelines or confirming whether the underwriting guidelines previously provided to Ambac prior to closing were the applicable guidelines, NCCI refused to provide any information at all, claiming that Ambac had "no contractual right to obtain such materials."

90. In light of NCCI's refusal to provide any further information, Plaintiffs' counsel

hired a third party to perform a forensic reunderwriting review of 1,038 loans from the NAAC 2007-1 Transaction and 811 loans from the NAAC 2007-3 Transaction, in order to determine whether they complied with the underwriting guidelines provided to Ambac prior to closing and the other Mortgage Loan Representations made by NCCI.

91. Each loan file was analyzed to confirm adherence to the guidelines, including guidelines meant to ensure the completeness of required documentation, such as income, credit, and asset documentation, and the integrity of appraisals.

92. The third party examined the loan files for, among other things, any "red flags" that should have been identified by the loan originator, such as indications that stated income was not reasonable, that borrower employment, income, and/or occupancy were misrepresented, or that debts were not fully disclosed.

93. The results have been staggering. The forensic reunderwriting review revealed that, as of the closing date of the Transactions, 983 of the reviewed Mortgage Loans from the NAAC 2007-1 Transaction (with an original principal balance of approximately \$339 million) and 778 of the reviewed Mortgage Loans from the NAAC 2007-3 Transaction (with an original principal balance of approximately \$255 million) failed to comply with the Mortgage Loan Representations—*a breach rate of approximately 95% for both deals.*

94. The breaches identified evince gross malfeasance, misconduct, and negligence in connection with the origination of the loans that NCCI pooled, reflecting a wholesale abandonment of any attempt to gauge the ability and willingness of borrowers to repay their obligations.

95. For example, the reunderwriting review revealed rampant misrepresentation by borrowers, in violation of Section 8(ii) of the MLPAs. Borrowers systematically misrepresented,

among other things, their incomes, their previously existing debts, the nature of their employment, and their intention to occupy the relevant properties (rather than to use them as investments). Because the individual mortgage documents state that false or misleading statements by borrowers constitute a default under their mortgages, those same misrepresentations also constituted violations of Section 8(xiv) of the MLPAs (the "no default" representation and warranty).

96. The forensic reunderwriting also revealed that the originators systematically failed to originate the Mortgage Loans in accordance with applicable guidelines, in violation of Section 8(xli) of the MLPAs. For example, loans were made to borrowers who did not have the requisite assets, who did not meet the debt-to-income ("DTI") or loan-to-value ("LTV") ratios required by the guidelines, whose credit reports reflected impermissible derogatory credit, or where property appraisals were incomplete or inadequate.

97. Individually and in the aggregate, these and numerous other breaches materially and adversely affected Ambac's interests in the identified loans. Loans that are not properly underwritten to assess the risk of non-payment or the inadequacy of the property as collateral, or the key attributes of which are otherwise misrepresented, are markedly more risky than loans not suffering from such defects. The pervasiveness and egregiousness of these breaches also conclusively demonstrate that the extensive information about the loan pools and securitization practices provided by NCCI in advance of the Transactions' consummation in order to induce Ambac's participation was knowingly (or, at a minimum, recklessly) false and misleading.

#### **G. NCCI's Repudiation of Its Repurchase Obligations**

98. Ambac has attempted to compel NCCI to repurchase or cure the Identified Defective Loans. Between February 2010 and September 2011, Ambac sent twelve notifications

to NCCI and HSBC, the Trustee for both Trusts, informing them of the over 1,700 Identified Defective Loans uncovered by the forensic reunderwriting. Days after receiving each of these notices, HSBC, pursuant to Section 2.03(c) of the PSAs, in turn issued notices to NCCI requesting that it cure the defects or repurchase each of the Identified Defective Loans at the contractually specified repurchase price. The following chart provides more details about the notices, which are collectively attached to this Amended Complaint, in date order, as Exhibit 1.

<b>Transaction</b>	<b>Ambac Notice Letter to Trustee and NCCI</b>	<b>Trustee's Notice to NCCI</b>	<b>Identified Defective Loans</b>
NAAC 2007-1	3/19/2010	3/24/2010	375
NAAC 2007-1	4/21/2011	4/22/2011	100
NAAC 2007-1	5/11/2011	5/27/2011	100
NAAC 2007-1	6/20/2011	7/13/2011	100
NAAC 2007-1	7/20/2011	7/22/2011	100
NAAC 2007-1	9/1/2011	9/14/2011	100
NAAC 2007-1	9/9/2011	9/14/2011	108
NAAC 2007-3	2/3/2010	2/12/2010	383
NAAC 2007-3	4/28/2011	5/12/2011	100
NAAC 2007-3	6/20/2011	7/13/2011	100
NAAC 2007-3	6/27/2011	7/13/2011	100
NAAC 2007-3	7/29/2011	9/14/2011	95

99. For each Identified Defective Loan, Ambac described in detail the relevant defect or defects and identified the specific Mortgage Loan Representation that was breached. HSBC included the same information in its own notices to NCCI.

100. Although the 90-day cure-or-repurchase period under Section 2.03(c) of the PSAs has expired for each of the putback notices, *to date NCCI has refused to repurchase a single Identified Defective Loan.*

101. In communications with Ambac in response to these putback notices, Defendants

asserted, for the first time, that the underwriting guidelines that NCCI had provided to Ambac shortly before closing (the only guidelines NCCI had ever given to Ambac) did *not* apply to the Mortgage Loans, and that its representations in advance of closing concerning the applicable guidelines were false.

102. Defendants' belated assertion is a patent and bad faith attempt to avoid the breach determinations in Ambac's notices. Despite claiming that the previously disclosed guidelines were not applicable, Defendants refused (and still refuse) to provide to Ambac or even identify the guidelines that it now claims apply. Defendants claim that Ambac's request for the applicable guidelines is "unreasonable" because it would involve locating "dozens" of documents.

103. It is evident that NCCI's pre-closing representations that the Nomura Guidelines governed the Transactions were made solely to convey a false assurance regarding NCCI's quality control and scrutiny of the Mortgage Loans it securitized.

104. Defendants claimed that another reason for its refusal to cure or repurchase any of the Identified Defective Loans was that Ambac had not provided it with underlying documentation demonstrating the breaches of the Mortgage Loan Representations. Though it was not required to do so under any of the contracts effectuating the Transactions, Ambac nevertheless provided Defendants with this underlying documentation as a courtesy. NCCI has still not repurchased a single Identified Defective Loan.

105. Given NCCI's abject failure and refusal to comply with its obligations with respect to the Identified Defective Loans, Plaintiffs reasonably anticipate that NCCI will fail to comply with its obligations with respect to any additional defective loans Plaintiffs may identify in the future.

## H. Defendants Are on Notice of Other Defective Loans Pervading Both Trusts

106. The notices Ambac and HSBC sent to NCCI regarding the over 1,700 Identified Defective Loans were more than sufficient to put NCCI on constructive notice of similar pervasive breaches throughout the unsampled loans in the two Transactions. These notices triggered NCCI's repurchase obligations as to any breaching Mortgage Loan in the Trusts, without further notice of loan-by-loan breaches.

107. Furthermore, on information and belief, NCCI and Nomura Holding, based on NCCI's role as the acquirer and securitizer of the Mortgage Loans, *knew* at the time the Transactions closed that loans that did not comply with the Mortgage Loan Representations pervaded the Trusts. Indeed, there is persuasive evidence of this.

108. As described above, the January 2011 FCIC Report discussed a Clayton Trending Report, covering the period between the first quarter of 2006 and the second quarter of 2007 showing that Clayton initially rejected 1,188 loans of the 3,366 loans it reviewed in connection with the NAAC 2007-1 Transaction. Nevertheless, Nomura "waived" *nearly half* of those loans—47%—into the NAAC 2007-1 Trust.

109. Clayton's report makes clear that NCCI and Nomura Holding knew at the time they consummated the transaction—but did not disclose to Ambac—that a significant portion of the loans sold to the NAAC 2007-1 Trust failed to meet the requisite underwriting guidelines. The report, together with the extremely high breach rate identified by Ambac's consultant, provide strong evidence that NCCI and Nomura Holding were likely also aware of the defects plaguing the loans in the NAAC 2007-3 Trust.

110. In other words, it was not necessary for Ambac or HSBC to give NCCI notice of breaches to trigger the Repurchase Protocol. Under the PSAs, NCCI's obligations to cure or

repurchase are also triggered by its *discovery* of breaching loans. PSAs § 2.03(c). Here, the extraordinary breach rate that Ambac's consultant found in its review of the over 1,800 loans and the revelations in the Clayton report regarding NCCI's knowledge of widespread defects in loans included in the NAAC 2007-1 Trust—and its "waiving" of such defective loans into the Trust—show that NCCI had already "discovered" a huge number of breaches when it first sold the Mortgage Loans to the Trusts.

#### **I. NCCI Is a Mere Alter Ego and Instrumentality of Nomura Holding**

111. On information and belief, Nomura Holding operated through several wholly owned subsidiaries that it dominated and controlled in order to profit from the issuance and sale of RMBS. More specifically, Nomura Holding used its domination and control over NCCI and NAAC to induce Ambac to agree to issue financial guaranty insurance policies that it never would have issued had the true quality of the collateral been disclosed, and also used its domination and control over the repurchase process to frustrate NCCI's contractual obligation to repurchase any and all Identified Defective Loans. As a result, Ambac was left to issue policies in connection with transactions whose collateral was materially worse than what had been represented, without recourse to the contractual remedy agreed to by NCCI.

112. Nomura Holding used several wholly owned subsidiaries to effectuate RMBS securitizations, including NCCI and NAAC. At all relevant times, all of these affiliates shared with Nomura Holding the same address (2 World Financial Center in New York City) and substantial overlap in the top tiers of management. Exemplifying this overlapping management, on information and belief, the same person is, or has recently been, the Chief Executive Officer of at least four Nomura affiliates, including Nomura Holding, NCCI, and NAAC.

113. Nomura Holding's wholly owned subsidiaries were mere instrumentalities of

Nomura Holding in the securitization process. NCCI, as in the NAAC 2007-1 and 2007-3 deals, determined the structure of Nomura Holding's securitizations, purchased mortgage loans from originators, determined the distribution of principal and interest for the certificates to be issued by the trusts, and provided data to the credit rating agencies to secure ratings for the certificates. NCCI also selected either NAAC or a similar Nomura Holding affiliate as depositor for the deals, that is, as a special purpose vehicle used to transfer the mortgage loans from NCCI to the trusts. Such depositors were also used to file registration statements with the S.E.C. and to form the certificate-issuing trusts. On some deals, another Nomura Holding affiliate helped structure the securitization and market the certificates.

114. These securitizations were not arm's-length transactions, but instead involved Nomura Holding directing its wholly owned subsidiaries at every step. Nomura Holding profited substantially from this vertically integrated approach to mortgage securitization.

115. As the corporate parent of NCCI and NAAC, Nomura Holding dominated and controlled these subsidiaries in connection with the NAAC 2007-1 and 2007-3 Transactions. On information and belief, at all relevant times, Nomura Holding exercised exclusive and complete domination and control over NCCI and NAAC, both generally and specifically with respect to the Transactions, and used such domination to materially misrepresent the credit quality of the loan pools and NCCI's due diligence practices and to breach the contracts governing the Transactions, by causing NCCI to make false Mortgage Loan Representations and to refuse to comply with the Repurchase Protocol. When NCCI's massive breaches of the Mortgage Loan Representations came to light with Ambac's repurchase demands, the Managing Director and Head of Litigation of Nomura Holding—writing on Nomura Holding letterhead—intervened and rejected every single repurchase demand submitted to NCCI. This concerted scheme to thwart

the Repurchase Protocol has caused and continues to cause grave injury to Ambac. Accordingly, equity requires that Nomura Holding be held accountable and liable for the actions and wrongs of NCCI.

**J. The Harm Suffered by Plaintiffs**

116. Ambac would not have participated in the Transactions and issued the Policies had it known of NCCI's fraud or pervasive breaches of the Mortgage Loan Representations. NCCI's pervasive misrepresentations and breaches, through its inclusion of a massive number of defective mortgage loans in the NAAC 2007-1 and NAAC 2007-3 Transactions, as well as its complete failure to comply with the Repurchase Protocol, go to the very heart of the bargain between the parties. Ambac relied on the detailed information about the Mortgage Loans being securitized in the Transactions and NCCI's due diligence practices and the Mortgage Loan Representations to assess the risk of loss associated with the two Policies it issued. Ambac further relied on NCCI's commitment to cure any breaches of the Mortgage Loan Representations or repurchase any breaching Mortgage Loans as a guarantee that NCCI, and not Ambac, would bear the risk that the Mortgage Loans were not as represented.

117. Contrary to NCCI's pre-contractual and contractual representations, the Trusts were assembled from predominantly poor-quality loans made to non-credit-worthy borrowers that present a materially greater risk of default than loans that conform to such representations. As a direct consequence of these misrepresentations, on day one Ambac's risk of loss was far greater than it would have been had the Mortgage Loans been as represented.

118. As of June 2014, Plaintiffs have received nearly \$200 million in claims on the Transactions. To date, Plaintiffs have paid more than \$63 million of such claims on the NAAC 2007-1 Transaction and more than \$39 million of such claims on the NAAC 2007-3 Transaction,

for a total of over \$102 million in paid claims. In addition, Plaintiffs have accrued over \$26 million of such claims on the NAAC 2007-1 Transaction and almost \$63 million of such claims on the NAAC 2007-3 Transaction. Further, Plaintiffs expect tens of millions of dollars in additional claims under the Policies because additional Mortgage Loans continue to become delinquent and will eventually be liquidated.

119. As discussed above, NCCI's fraudulent statements and material omissions, and the pervasive breaches of NCCI's Mortgage Loan Representations, revealed by Ambac's loan-level reviews and corroborated by the dismal performance of the Transactions, pierce the very heart of the bargain struck by the parties. As only became clear after Ambac's forensic reunderwriting, NCCI did not sell loans with the represented and warranted attributes to the Trusts. Instead, the overwhelming majority of Mortgage Loans did not bear any resemblance to the loans that NCCI represented and warranted it would sell. Contrary to NCCI's representations and warranties, the loans were infected by fraud and other underwriting failures. NCCI induced Ambac to insure each Transaction based upon materially false and misleading information about that Transaction, and, in the case of the 2007-3 Transaction, the preceding one. Ambac never would have issued the Policies or agreed to participate in the Transactions had it known the truth.

120. To place Ambac in the position it would have occupied absent NCCI's fraud and breaches of contract, NCCI and its parent, Nomura Holding, must pay Plaintiffs, at a minimum:

- A. All Policy claims incurred to date; and
- B. All future claims payments Plaintiffs will be obligated to make under the Policies.

#### **FIRST CAUSE OF ACTION**

**(Against NCCI and Nomura Holding, as Alter Ego  
to NCCI, for Fraudulent Inducement)**

121. Plaintiffs reallege and incorporate by reference paragraphs 1 through 120 of this

Amended Complaint.

122. As set forth above, NCCI made materially false statements and omitted material facts with the intent to defraud Ambac in pre-contractual communications between Ambac and NCCI.

123. NCCI, knowingly and with the intent to defraud, delivered to Ambac, directly and through Bear Sterns, materially false and misleading documentation, including loan tapes.

124. Ambac reasonably relied on NCCI's statements and omissions when it issued the Policies.

125. Nomura Holding exercised complete domination and control over NCCI and caused it to fraudulently induce Ambac.

126. As a result of NCCI's statements and omissions, and Nomura Holding's responsibility for that fraudulent inducement, Ambac insured a pool of loans that had a risk profile far greater than NCCI had led Ambac to believe.

127. As a result of NCCI's false and misleading statements and omissions, and Nomura Holding's responsibility for that fraudulent inducement, Plaintiffs have suffered, and will continue to suffer, damages including claims payments under the Policies.

128. Because NCCI committed these acts and omissions maliciously, wantonly, oppressively, and with knowledge that they would affect the general public—which they have—Plaintiffs are entitled to punitive damages.

## **SECOND CAUSE OF ACTION**

**(Against NCCI and Nomura Holding, as Alter Ego to  
NCCI, for Material Breach of the PSAs)**

129. Plaintiffs reallege and incorporate by reference paragraphs 1 through 128 of this Amended Complaint.

130. The PSAs are valid and enforceable contracts that give rise to obligations on the part of NCCI with respect to the Mortgage Loans. Ambac is an express third-party beneficiary to the PSAs.

131. In Section 2.03(b) of the PSAs, NCCI incorporated Mortgage Loan Representations that it made in the MLPAs. In Section 2.03(c) of the PSAs, NCCI agreed to fulfill its obligations under the Repurchase Protocol, namely to cure or repurchase Mortgage Loans that materially breached the Mortgage Loan Representations.

132. NCCI persuaded Ambac to enter into the Transactions and to issue the Policies by making these Mortgage Loan Representations and by agreeing to comply with the Repurchase Protocol.

133. The Mortgage Loan Representations and the Repurchase Protocol were material to Ambac's decision to insure the Insured Certificates. Had Ambac known that the Mortgage Loan Representations were false, and that NCCI would refuse to comply with the Repurchase Protocol, it would not have issued the Policies.

134. NCCI has materially breached its obligations under the PSAs by pervasively breaching the Mortgage Loan Representations and by wholly refusing to comply with, and thereby repudiating, the Repurchase Protocol. These breaches go to the very heart of the bargain Ambac and NCCI entered into.

135. Nomura Holding exercised complete domination and control over NCCI and caused it to materially breach its obligations under the PSAs.

136. As a result of NCCI's breaches, and Nomura Holding's responsibility for those breaches, Plaintiffs have been damaged and will continue to be damaged in an amount to be determined at trial.

137. Plaintiffs are entitled to damages sufficient to place Ambac in the position it would have been in had it never issued the Policies.

### **THIRD CAUSE OF ACTION**

#### **(Against NCCI and Nomura Holding, as Alter Ego to NCCI, for Breach of the Repurchase Protocol)**

138. Plaintiffs reallege and incorporate by reference paragraphs 1 through 137 of this Amended Complaint.

139. NCCI has materially breached its obligations under the Repurchase Protocol by refusing to cure or repurchase any of the Mortgage Loans that materially and adversely breached NCCI's Mortgage Loan Representations.

140. Ambac and HSBC have provided NCCI with notice as to over 1,700 Identified Defective Loans, and HSBC has demanded that NCCI comply with the Repurchase Protocol.

141. On information and belief, NCCI knew or discovered, independent of the notice provided by Ambac and HSBC, that a huge number of the Mortgage Loans breached the Mortgage Loan Representations, thus separately triggering NCCI's obligations under the Repurchase Protocol.

142. Nomura Holding exercised complete domination and control over NCCI and caused it to breach its obligations under the Repurchase Protocol.

143. As a result of NCCI's breaches, and Nomura Holding's responsibility for those breaches, Plaintiffs have been damaged and will continue to be damaged in an amount to be determined at trial.

### **PRAYER FOR RELIEF**

**WHEREFORE**, Plaintiffs respectfully pray for the following relief:

- A. For an award in favor of Plaintiffs and against NCCI and Nomura Holding, jointly and severally, of legal, equitable, and any other present and future damages to be proven at trial, including all claims that have accrued under the Policies to date and all claims due for payment in the future under the Policies, and compensatory, punitive, and consequential damages, including lost profits and business opportunities;
- B. For an order holding Nomura Holding, as NCCI's alter ego, liable to pay in full any award of damages in this case for which NCCI may be liable to Plaintiffs;
- C. For an order compelling NCCI and Nomura Holding, as NCCI's alter ego, to comply with the obligations under the Repurchase Protocol in Section 2.03(c) of the PSAs to cure or repurchase each of the Mortgage Loans in connection with which there is a material breach of any Mortgage Loan Representation;
- D. For an order of prejudgment and postjudgment interest at the maximum legal rate; and
- E. For an order awarding Plaintiffs such other and further relief as the Court deems just and proper.

Dated: New York, New York  
September 22, 2014

Respectfully submitted,

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