MORRISON & FOERSTER LLP
1290 Avenue of the Americas
New York, New York 10104
Telephone: (212) 468-8000
Facsimile: (212) 468-7900
Gary S. Lee
Adam A. Lewis
Norman S. Rosenbaum
Samantha Martin

Counsel for The ResCap Liquidating Trust

UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

Jennifer L. Wilson, Plaintiff, *v.* Residential Capital, LLC, et al. Defendants.	:	Adv. Proc. 12-01936 (MG)
In re RESIDENTIAL CAPITAL, LLC, *et al.*, Debtors	:	Case No. 12-12020 (MG) Chapter 11 Jointly Administered

NOTICE OF FILING OF THE RESCAP LIQUIDATING TRUST'S CORRECTED SUPPLEMENTAL BRIEF IN SUPPORT OF THE DEBTORS' MOTION FOR DISMISSAL OF ADVERSARY PROCEEDING PURSUANT TO BANKRUPTCY RULE 7012(b) AND FRCP 12(b)(1) AND 12(b)(6) OR, IN THE ALTERNATIVE, PERMISSIVE ABSTENTION PURSUANT TO 28 U.S.C. §1334(c)(1

PLEASE TAKE NOTICE THAT on May 29, 2014, the ResCap Liquidating Trust filed the *The ResCap Liquidating Trust's Supplemental Brief in Support of the Debtors' Motion*

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for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP12(b)(1) and 12(b)(6) or, in the Alternative, Permissive Abstention Pursuant to 28 U.S.C. Section 1334 (c)(1) (the "**Supplemental Brief**") [Adv. Proc. Docket No. 54].

PLEASE TAKE FURTHER NOTICE that in connection with the Supplemental Brief, the Debtors hereby submit the *The ResCap Liquidating Trust's Corrected Supplemental Brief in Support of the Debtors' Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP12(b)(1) and 12(b)(6) or, in the Alternative, Permissive Abstention Pursuant to 28 U.S.C. Section 1334 (c)(1)* (the "**Corrected Supplemental Brief**"), a copy of which is annexed hereto as Exhibit 1. Annexed hereto as Exhibit 2 is a blackline of the Corrected Supplemental Brief, reflecting the changes made from the previously filed Supplemental Brief.

Dated: May 29, 2014
New York, New York

/s/ Norman S. Rosenbaum
Gary S. Lee
Adam A. Lewis
Norman S. Rosenbaum
Samantha Martin
MORRISON & FOERSTER LLP
1290 Avenue of the Americas
New York, New York 10104
Telephone: (212) 468-8000
Facsimile: (212) 468-7900

Counsel for The ResCap Liquidating Trust

Exhibit 1

MORRISON & FOERSTER LLP
1290 Avenue of the Americas
New York, New York 10104
Telephone: (212) 468-8000
Facsimile: (212) 468-7900
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THE RESCAP LIQUIDATING TRUST'S CORRECTED SUPPLEMENTAL BRIEF IN SUPPORT OF THE DEBTORS' MOTION FOR DISMISSAL OF ADVERSARY PROCEEDING PURSUANT TO BANKRUPTCY RULE 7012(b) AND FRCP 12(b)(1) AND 12(b)(6) OR, IN THE ALTERNATIVE, PERMISSIVE ABSTENTION PURSUANT TO 28 U.S.C. §1334(c)(1)

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TO THE HONORABLE MARTIN GLENN
UNITED STATES BANKRUPTCY JUDGE:

The Liquidating Trust[1] hereby submits this supplemental brief (the "Supplemental Brief") in support of its Motion to Dismiss pursuant to the Court's instructions at the May 1, 2014 hearing on the Motion to Dismiss (the "Hearing"). Specifically, the Court directed the Liquidating Trust to address three issues with supplemental materials: (1) evidence regarding the chain of title of the Note and Deed of Trust (together, the "Loan Documents") originally issued by Plaintiff in favor of SunTrust Mortgage, Inc., dba Sun America Mortgage; (2) discussion of whether the North Carolina doctrine of preclusion (*res judicata* or collateral estoppel) bars the Plaintiff from making the claims she is making in this Adversary Proceeding; and (3) discussion of whether fraud on the Superior Court regarding the chain of title of the Loan Documents is grounds for setting aside the Order and abrogating the application of the doctrine of preclusion. This Supplemental Brief addresses the second and third issues; contemporaneously, the Liquidating Trust is submitting a separate declaration on the chain of title question.[2] In support of the Supplemental Brief, the Liquidating Trust respectfully represents as follows:

[1] Capitalized terms not defined in this brief will have the meanings ascribed to them in the *Debtors' Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP 12(b)(1) and 12(b)(6) or, In the Alternative, Permissive Abstention Pursuant to 28 U.S.C. §1334(c)(1)* [Docket No. 4] or the *ResCap Liquidating Trust's Reply in Support of the Debtors' Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP 12(b)(1) and 12(b)(6) or, in the Alternative, Permissive Abstention Pursuant to 28 U.S.C. §1334(c)(1)* [Docket No. 38] (the "Reply").

[2] The Court also asked the Liquidating Trust to address three specific cases: *Conklin v. Anthou*, 495 Fed. Appx. 257, 262 (3d Cir. 2012) writ denied, 133 S. Ct. 1729 (2013); *Kelleran v. Andrijevic*, 825F.2d 692, 694 (2d Cir. 1987); and *Johnson v. Laing (In re Laing)*, 945 F.2d 354, 358 (10th Cir. 1991). This Supplemental Brief discusses them in paragraphs 1 n.3, 13 and 15.

PRECLUSION

1. The question the Court posed for the Liquidating Trust was whether the Order of the Superior Court allowing the substitute trustee to foreclose on the Property pursuant to the Loan Documents and Chapter 45 of the North Carolina General Stautes bars the claims that the Plaintiff has made in the Adversary Proceeding against the Debtor Defendants (ResCap and RFC).[3]

2. In deciding whether a state court decision is barred by preclusion, federal courts look to the preclusion law of the subject state. *See, e.g., Migra v. Warrant City Sch. Dist. Bd. Of Educ.*, 465 U.S. 75, 81 (1984); *DiSorbo v. Hoy*, 343 F.3d 172, 182-83 (2d Cir. 1996); *Brumby v. Deutsche Bank Nat'l Trust Co.*, No. 1:09-CV-144, 2010 WL 617368 (M.D.N.C. Feb 17, 2010); *Omernick v. LaRocque*, 406 F. Supp. 1156, 1159 (W.D. Wis.), *aff'd sub nom., Omernick v. Wisconson*, 539 F.2d 715 (7th Cir. 1976); *see also* 28 U.S.C. § 1738 (federal courts must afford state court decisions full faith and credit).

3. Here it is important to remember that the Order is a final judgment under North Carolina law. When a trustee commences a special proceeding to foreclose on a deed of trust in North Carolina, the clerk of court is required to hold a hearing (unless the hearing is waived) to determine if the trustee should be permitted to conduct a foreclosure sale. N.C. Gen. Stat. § 45-21.16(d). At the hearing, the trustee or secured party must establish, among other things, "the

[3] The Court did not ask for further briefing on the related *Rooker-Feldman* issue. But it did ask the Liquidating Trust to discuss Conklin, 495 Fed. Appx. at 262. In *Conklin*, the court held that the loser of a state court foreclosure proceeding could sue various officials related to the proceeding for their alleged misconduct; such a suit did not violate *Rooker-Feldman* if and to the extent that it did not seek to review the judgment of foreclosure as such. Here, *Rooker-Feldman* does apply at least as to paragraph 104i of the Complaint, which asks "[t]hat the defendants take nothing by their foreclosure sale" and paragraph 104j which asks that the Debtor Defendants surrender the Note, if not more broadly. Moreover, unlike in *Conklin*, the Plaintiff is suing defendants who were in no way connected to the foreclosure process.

existence of [i] valid debt of which the party seeking to foreclose is the holder . . .” before it will be allowed to conduct a foreclosure sale. *Id*. § 45-21.16(d). In the special proceeding, the debtor may assert any legal defenses that would establish that the party seeking to foreclose is not the holder of the debt. *Tenney v. Birdsall* (*In re foreclosure of Goforth Props., Inc.),* 432 S.E.2d 855, 859 (N.C. 1993). Under N.C. Gen. Stat. § 45-21.34, the debtor also may file a separate action to assert any legal or equitable defenses that would demonstrate the absence of a valid debt or that the party seeking to foreclose is not the holder of the debt, but the debtor must file such an action and obtain an injunction of the foreclosure sale before the rights of the parties to the sale become fixed. N.C. Gen. Stat. § 45-21.34; *see Goad v. Chase Home Fin., LLC*, 704 S.E.2d 1, 4 N.C. Ct. App. (2010). Those rights ordinarily become fixed when the time for submitting an upset bid expires. N.C. Gen. Stat. § 45-21.29A; see *Goad,* 704 S.E.2d at 5.

4. If the clerk of court finds “the existence of [i] valid debt of which the party seeking to foreclose is the holder” and certain other things, the clerk is required to enter an order authorizing the trustee to conduct a foreclosure sale. N.C. Gen. Stat. § 45-21.16(d). The statutes provide that “[t]he act of the clerk in so finding . . . is a judicial act. . . .” *Id.* at § 45-21.16(d1). A debtor can appeal the clerk’s order for a de novo hearing before a trial judge. *Id.* If, however, the order is not appealed within 10 days of its entry, it becomes final and binding. *See* N.C.R. App. P. 3(c)(1) & (c)(2) (30 days to appeal); *Phil Mech. Constr. Co. v. Haywood*, 325 S.E.2d 1, 3 (N.C. Ct. App. 1985). The Order was entered on January 25, 2010, and the Plaintiff neither appealed it nor sought to enjoin the foreclosure. The time for the Plaintiff to appeal has long since expired. The Order is therefore final.[4]

[4] Whether the Order can be attacked via the fraud on the court doctrine will be the subject of the fraud on the court section of this Supplemental Brief.

A. *Res Judicata*

5. As the Fourth Circuit has held, under North Carolina law, once a final judgment is entered in a prior proceeding, the doctrine of "[r]es judicata, or claim preclusion, bars the relitigation of any claims that were *or could have been* raised in [the] prior proceeding between the same parties [or their privies]". *Sartin v. Macik*, 535 F.3d 284, 287 (4th Cir. 2008) (emphasis added). *Res judicata* is very broad in North Carolina, as in many jurisdictions. It applies "to every point which properly belong to the subject in litigation and which the parties, exercising reasonable diligence, might have brought forward at the time and determined respecting it." *Painter v. Wake Co. Bd. of Educ.*, 217 S.E.2d 650, 655 (N.C. 1975). For an action to be precluded under the doctrine of res judicata (or "claim preclusion") in North Carolina, a prior judgment must have been (1) a judgment on the merits in a prior suit resolving (2) claims by the same parties or their privies, and (3) a subsequent suit based on the same cause of action. *Whitacre P'Ship v. Biosignia, Inc.*, 591 S.E.2d 870, 880 (N.C. 2004). Here, clearly there is a final judgment on the merits in the Superior Court. Thus, only the second and third criteria of *Whitacre* remain to be examined in this matter.

6. Privity is defined in North Carolina as "mutual or successive relationship to the same rights of property. . . . In general, privity involves a person so identified in interest with another that he represents the same legal right." *N.C. ex rel Tucker v. Frinzi*, 474 S.E.2d, 128, 130 (N.C. 1996) (citation omitted) (finding that a state and county in the state were not in privity with each other, even though they were seeking the same outcome with regards to getting someone to pay child support). In *Smith v. Smith*, 431 S.E.2d 196 (N.C. 1993), an ex-wife sued a couple over title to certain property that the defendants got from the ex-husband through the divorce settlement. The defendants were not parties to the divorce or settlement as such. In dismissing entering judgment for the defendants, the Supreme Court of North Carolina held that

the defendants were privies of the ex-husband as to the divorce action for preclusion purposes. *See also Cline v. McCullen*, 557 S.E.2d 588, 591 (N.C. Ct. App. 2001) ("[S]uccessive or mutual [rights in the same property] establishes that the interests of both Tindall and plaintiff are so intertwined that privity exists between them.") Accordingly, the wife was barred from the present suit by *res judicata*. In this Adversary Proceeding, the Debtor Defendants are, on the one hand, the successor to SunTrust Mortgage, Inc., as to the Loan Documents, or the successor's agent, on the other hand.[5] Though not parties to the action in the Superior Court, they are privies.

7. The test for deciding whether the causes of action are identical for claim preclusion purposes is whether the claim presented in the new litigation arises out of the same transaction or series of transactions as the claim resolved by the prior judgment. An action is the same as a prior action when the new claim requests the same relief and raises the same set of material facts. *N.C. ex rel. Tucker v. Frinzi*,474 S.E.2d at 127. The facts of this matter easily satisfy this test as to the Complaints' claims for relief. The first three are for breach of contract and the fourth is for unfair and deceptive trade practices. And all relate in one way or another to whether SunTrust Bank was the holder of the Note and therefore had the right to commence the foreclosure action in the Superior Court. Indeed, as noted in the Motion to Dismiss at page four, one of the findings that the Superior Court had to and did make is the identity of the holder of the Note, which it found to be SunTrust Bank. Those claims for relief, all of which depend in the end on the Plaintiff's assertion that SunTrust Bank lacked title to the Loan Documents when it

[5] An agent is a privy of the principal. *See, e.g., Jones v. First Franklin Loan Servcs.*, No. 3:10-CV-360-FDW-DSG 2011 WL 972518 (W.D.N.C. Mar. 15, 2011).

commenced the foreclosure action, are barred, therefore, by *res judicata* as applied in North Carolina.[6]

B. Collateral Estoppel

8. Applying collateral estoppel forecloses the relitigation of issues of fact or law that are identical to issues which have been actually determined and necessarily decided in prior litigation in which the party against whom [collateral estoppel] is asserted had a full and fair opportunity to litigate.' *Sedlack v. Braswell Servs. Grp., Inc.*, 134 F.3d 219, 224 (4th Cir.1998) (citation omitted). To apply collateral estoppel (also known as issue preclusion) to an issue or fact, the proponent must demonstrate that (1) the issue or fact is identical to the one previously litigated; (2) the issue or fact was actually resolved in the prior proceeding; (3) the issue or fact was critical and necessary to the judgment in the prior proceeding; (4) the judgment in the prior proceeding is final and valid; and (5) the party to be foreclosed by the prior resolution of the issue or fact had a full and fair opportunity to litigate the issue or fact in the prior proceeding. *See id. See also, Kloth v. Microsoft Corp*. (*In re Microsoft Antitrust Lit.),* 355 F.3d 322 (4th Cir. 2004); *Whitacre Partnership v. Biosignia, Inc., supra*.

[6] Notably, the Plaintiff has yet to explain how she was harmed by the foreclosure. She does not deny that she had ceased making payments on the Note well before SunTrust Bank commenced the foreclosure, let alone before it actually occurred. Nor has she specified *how* she was harmed with respect to the conduct at issue (she has not suggested, for example, that she would not have suffered foreclosure by *someone* since she was in default, nor has she indicated that anyone has attempted to impose duplicative liability on her). She also has not quantified her damages. The latter, incidentally, argues against the Adversary Proceedings' being an informal, timely proof of claim. "Courts in the Second Circuit have long recognized the validity of informal proofs of claim. *See In re Lipman* , 65 F.2d 366 (2d Cir.1933); *Nat'l Bank of Westchester v. Wurlitzer Co.*(*In re Gibraltor Amusements, Ltd*.), 315 F.2d 210 (2d Cir.1963); *In re W.T. Grant Co.*, 53 B.R. 417 (Bankr. S.D.N.Y. 1985); *In re Nutri*Bevco, Inc.*, 117 B.R. 771 (Bankr. S.D.N.Y. 1990). In order for a document to constitute an informal proof of claim it must be in writing and filed with the bankruptcy court. *See W.T. Grant*, supra, 53 B.R. at 422. Furthermore, it must set forth the nature *and amount of the claim* and the intent on the part of the claimant to hold the debtor liable. *Id*. at 421; *see also Nutri*Bevco, supra*, 117 B.R. at 789. *In re Float, Inc,*, 163 B.R. 18, 20 (Bankr N.D.N.Y. 1993) (emphasis added).

9. There are two kinds of collateral estoppel, offensive (plaintiff employing against a defendant who previously litigated unsuccessfully against another party) and defensive (defendant employing against a plaintiff who previously litigated unsuccessfully). Courts are stricter when applying offensive collateral estoppel because of concerns for due process. *See In re Microsoft*, 355 F.3d at 326-27. The Debtor Defendants seek to apply collateral estoppel defensively. Thus, there is no heightened standard they must satisfy.

10. In the present case, all five elements of North Carolina collateral estoppel regarding the critical issues of title to the Loan Documents are present. The identity of the holder of the Note was actually litigated through the introduction of evidence by the substitute trustee, the Superior Court found that SunTrust Bank was the holder of the Note, the finding was critical to the Order, as the Order itself establishes, the Order is final and the Plaintiff was duly served with notice of the hearing and able to make an appearance to defend herself (she has never alleged otherwise).

11. Since all of the Plaintiff's claims for relief in the Adversary Proceeding depend on her contention that SunTrust Bank was not the Note's holder, her claims must fail because she is bound by the Superior Court's finding that SunTrust Bank was, in fact, the holder of the Note.

FRAUD ON THE COURT

12. In the MTD Response and at the Hearing, the Plaintiff contends that title to the Loan Documents did not, in fact, rest in SunTrust Bank. This fact was evidenced by a form of the Note that differed from that SunTrust Bank used in the foreclosure action because it had an endorsement to a third party on it.[7] The Plaintiff contends that by representing to the Superior

[7] As noted earlier, the history of the Loan Documents will be the subject of a separate declaration. At this juncture it is worth noting that although the Plaintiff claimed at the Hearing that she only recently learned of the ownership *(cont'd)*

Court that SunTrust Bank did own the Loan Documents, SunTrust Bank committed fraud on the Superior Court that voids the Order, thereby sweeping away with it most of the Debtor Defendants' defenses, including preclusion and *Rooker-Feldman*.

A. The Proper Court

13. As stated in *Kelleran v. Andrijevic*, 825F.2d at 694 (no evidence claim against debtor obtained by fraud on the state court):

> "Congress has specifically required all federal courts to give preclusive effect to state-court judgments whenever the courts of the State from which the judgments emerged would do so...." *Allen v. McCurry,* 449 U.S. 90, 96 (1980) (citing 28 U.S.C. § 1738 (1982)). Bankruptcy courts fall within Congress' mandate. *See, e.g., In re* 27 B.R. 241, 243 (Bankr. E.D.N.Y. 1982).

14. A federal court has no authority to actually set aside a state court action, even when it is alleged that fraud on the court occurred in that action. *See Weisman v. Charles E. Smith Mgmt., Inc.*, 829 F.2d 511, 513 (4th Cir. 1987) ("the proper forum in which to assert that a party has perpetrated a fraud on the court is the court which allegedly was the victim of that fraud"); *Chewning v. Ford Motor Co.*, 35 F. Supp. 2d 487, (D.S.C. 1998) (citing to *Weisman* and holding that fraud on the court, as well as an independent action in equity, must be addressed by the court in which the action occurred); *Wilson v. Comm'r of Internal Revenue*, 309 Fed. Appx. 829 (5th Cir. 2009). As a result, a federal court cannot set aside a judgment for fraud on the

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issue, *see* Transcript of Hearing at 39:4-8, *In re Residential Capital, LLC*, No. 12-12020 (MG) (Bankr. S.D.N.Y.); *see also id.* 33:22-24, that is untrue. A complaint she filed with the North Carolina Commissioner of Banks on October 27, 2010 demonstrates that she knew enough to challenge the foreclosure before it took place on November 15, 2010. (*See* Declaration of Lauren Graham Delehey in Support of the Debtor's Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP 12(b)(1) and 12(b)(6) or, in the Alternative, Permissive Abstention Pursuant to 28 U.S.C. §1334(c)(1), ¶ 16 & Ex. 5 (filed concurrently herewith).) At that point, as the Debtor Defendants will note presently, she still was within the one year limitations period for bringing a motion to vacate the Order for fraud under N. C. R. Civ. P. 60(b)(3), the North Carolina cognate of Fed. R.Civ. P. 60(b)(3).

court or an independent equity action, but must remand the action to the state court that is the subject of the action. *Chewning*. That does not mean that this Court cannot grant the Motion to Dismiss on the ground that, as the Liquidating Trust will argue, it is clear that the Plaintiff cannot succeed in seeking to set aside the Order in North Carolina.

15. However, there is a line of cases holding that a bankruptcy court may refuse to give preclusive effect to a state court judgment obtained by fraud on the court, but each of these cases concerns treatment of a claim *against* the debtor allegedly obtained by fraud on the state court. *See, e.g., In re Laing*, 945 F.2d at 358 (court allows claim against debtor because no fraud on the state court that rendered the underlying judgment; any fraud was intrinsic, not extrinsic in that it was not aimed at court but "related to the events that made up the *subject matter* of [and basis of the claims in] the state court action. . . ."); *Kelleran*, 825 F.2d at 694 (bankruptcy courts must honor state court judgments unless obtained "by collusion or fraud"; exception does not apply to state court default just because of an attorney/client relationship between parties or doubtful claims); *Margolis v. Nazareth Fair Grounds & Farmers Mkt.*, 249 F.2d 221, 223 (2d Cir. 1957) ("Bankruptcy courts are essentially courts of equity endowed with broad equity powers . . . .A bankruptcy court may inquire into the validity of any claim asserted against the bankrupt and may disallow it if it is found to be without lawful existence.") (citation omitted); *In re Mastercraft Record Plating, Inc.*, 32 B.R. 106, 109-110 (S.D.N.Y. 1983) (state court claim obtained by fraud on the court is disallowed because bankruptcy court final arbiter of claims against debtor); *In re Bocker*, 123 B.R. 164, 165 (Bankr. E.D.N.Y. 1991) (claim not obtained by demonstrated fraud consisting of state court plaintiff's misrepresentation of applicable interest rate, so claim allowed by bankruptcy court in debtor's bankruptcy).

16. The preceding materials indicate that this Court cannot look behind the Order for fraud on the court for purposes of *allowing* the claims asserted by the Plaintiff in the Complaint (if they are otherwise cognizable by the Court). However, in the succeeding portion of this Supplemental Brief the Liquidating Trust will analyze whether relief would be available for fraud on the court even if the Court could do so.

B. Fraud on the Court: Standards and Procedures

17. Because North Carolina Rule of Civil Procedure 60(b) is exactly like the Federal Rules of Civil Procedure 60(b)(3) and 60(d)(3), North Carolina state courts have looked to interpretation of the federal rule when interpreting the state rule. *See Henderson v. Wachovia Bank of North Carolina, N.A.*, 551 S.E.2d. 464, 469 (N.C. Ct. App. 2001) (applying the federal standard of fraud on the court to the state rule and determining that negligence on the part of an attorney to not properly communicate with their client did not constitute fraud on the court).

18. The seminal Supreme Court case on the topic is *Hazel-Atlas Glass Co. v. Hartford-Empire Co.*, 322 U.S. 238 (1944), where the court found fraud on the court because of a deliberate scheme to defraud the court of appeals, a scheme that threatened public injury. Courts have interpreted *Hazel* as saying that fraud on the court has been recognized as a "nebulous concept" that "should be construed very narrowly." *Fox ex rel. Fox v. Elk Run Coal Co.*, 739 F.3d 131,136 (4th Cir. 2014). This interpretation has been bolstered by interpretation of Fed. R. Civ. P. Rule 60.

19. Rule 60(b)(3) (whether federal or North Carolina) allows a party up to one year to seek relief from a judgment on grounds that the judgment was procured by fraud, misrepresentation, or misconduct by the opposing party.

20. Fraud on the court is a "nebulous" theory "should be construed very narrowly" lest the doctrine swallow up and render pointless Federal Rule 60(b)(3).. *Great Coastal Express,*

Inc. v. Int'l Bhd. of Teamsters, 675 F.2d 1349, 1356 (4th Cir. 1982). "[T]his doctrine should be invoked only when parties attempt 'the more egregious forms of subversion of the legal process..., those that we cannot necessarily expect to be exposed by the normal adversary process." *Fox ex rel. Fox*, 739 F.3d at 136 (citation omitted). The doctrine is limited to "egregious" situations such "as bribery of a judge or juror, or improper influence exerted on the court by an attorney, in which the integrity of the court and its ability to function impartially is directly impinged." *Great Coastal*, 679 F.2d at 1356. Furthermore, because attorneys are officers of the court, courts have been much more likely to find fraud on the court when an attorney is colluding in the scheme. *See Cleveland Demolition Co. v. Azcon Scrap Corp.*, 827 F.2d 984 (4th Cir. 1987) (finding that mere evidentiary conflicts that do not prove that an attorney was colluding with a witness to present perjured testimony is a conflict to be resolved at trial and does rise to fraud on the court).

21. Courts have held that in order to find fraud on the court, the fraud or misrepresentation must have been intentional. *United States v. MacDonald*, 161 F.3d 4 (4th Cir. 1998) (holding that in order to establish fraud on the court, it must be established that the fraud was material and deliberate); *McMunn v. Mem'l Sloan-Kettering Cancer Ctr.*, 191 F. Supp. 2d 440 (S.D.N.Y. 2002) ("fraud upon the court occurs where a party has acted knowingly in an attempt to hinder the fact finder's fair adjudication of the case and his adversary's defense of the action." (citation omitted)). Fraud on the court must be established by clear and convincing evidence. *E.g., King v. First Am. Investigations, Inc.*, 287 F.3d 91, 95 (2d Cir. 2002).

22. Federal Rule 60(d)(3) and North Carolina Rule 60(b) states that the one year time limitation does not limit a court's power to entertain an independent action to relieve a party

from a judgment, order, or proceeding. This is known as an independent equity action. *E.g.*, *Weisman*, 829 F.2d at 513.

23. The standard for this is (1) a judgment which ought not, in equity and good conscience, to be enforced; (2) a good defense to the alleged cause of action on which the judgment is founded; (3) fraud, accident, or mistake which prevented the defendant in the judgment from obtaining the benefit of this defense, (4) the absence of fault or negligence on the part of the defendant; and (5) the absence of any adequate remedy at law. *Asterbadi v. Leitess*, 176 Fed. Appx. 426, 430 (4th Cir. 2006) (citing *Great Coastal*). For purposes of this analysis, the alleged cause of action is the original cause of action and the defendant is the defendant in the original cause of action. In the Fourth Circuit, courts have held that perjury and false testimony are not grounds for relief in an independent equity action because "they can and should be exposed at trial." *See Great Coastal*, 675 F.2d at 1357. Independent equity actions are only available to prevent "a grave miscarriage of justice." *United States v. Beggerly*, 524 U.S. 38 (1998). Finally, the plaintiff in an independent equity action may not seek damages. *Chewning*, 35 F. Supp. 2d at 489.

24. Furthermore, in the Second Circuit, courts have held that an independent equity action cannot be based on a lack of evidence of the fraud if the evidence could have been discovered earlier with reasonable diligence. *Gottlieb v. S.E.C.*, 310 Fed. Appx. 424 (2d Cir. 2009) (finding that recently discovered evidence is not a sufficient basis). And in *Wolfson v. Wolfson*, No. 03-CIV-0954(RCC) 2004 WL 224508 (S.D.N.Y. Feb 5, 2004) the court found that where the plaintiff knew about the supposed fraud within the year time frame allowed in Fed. R. Civ. P. 60(b)(3) and did nothing, he is in the situation through his own neglect and carelessness and cannot assert an independent equity action.

25. Moreover, "[i]t is well established in North Carolina 'that where a judgment has been entered, relief from that judgment is not available in an independent action upon facts which amount to intrinsic fraud.'" *Hooks v. Eckman*, 587 S.E.2d 352, 354 (N.C. Ct. App. 2003) (quoting *Textile Fabricators, Inc. v. C.R.C. Indus, Inc.*, 259 S.E.2d 570, 572 (N.C. Ct. App. 1979)). Therefore, the ability of a party to maintain a separate action collaterally attacking a final judgment or order due to allegations of fraud or misrepresentations within a prior proceeding depends on whether the basis of the contention is intrinsic or extrinsic fraud. *See Stokley v. Stokley*, 227 S.E.2d 131, 134 (N.C. Ct. App. 1976). The North Carolina Court of Appeals has defined fraud as extrinsic "when it deprives the unsuccessful party of an opportunity to present his case to the court. If an unsuccessful party to an action has been prevented from fully participating therein there has been no true adversary proceeding, and the judgment is open to attack at any time." *Id*. On the contrary,

> "intrinsic fraud occurs when a party (1) has proper notice of an action, (2) has not been prevented from full participation in the action, and (3) has had an opportunity to present his case to the court and to protect himself from any fraud attempted by his adversary. Specifically, intrinsic fraud describes matters that are involved in the determination of a cause on its merits."

Hooks, 587 S.E.2d at 354 (citation omitted); *See also Smith*, 431 S.E.2d at 200. North Carolina courts consider false testimony to be intrinsic fraud. *Hooks*, 587 S.E.2d at 354; *Textile Fabricators, Inc.* at 259 S.E.2d at 571. Therefore, a complaint of intrinsic fraud related to a foreclosure proceeding can only be brought through a N. C. R. Civ. P. 60(b)(3) motion within the special proceeding and within one year of the entry of the clerk's order.

C. The Plaintiff Cannot Obtain Relief for Fraud on the Court

26. As noted earlier, far more than a year has passed since the entry of the Order. Thus, the Plaintiff cannot obtain relief under N. C. R. Civ. P. 60(b)(3) for fraud on the Court.[8]

27. By the same token, because the Plaintiff believed that she discovered that the Note was not held by SunTrust Bank at the time of the foreclosure hearing, as established by her complaint to the North Carolina Banking Commission, she cannot allege tolling of the time limits of N. C. R. Civ. P. 60(b)(3) or assert an independent equity action under N. C. R. Civ. P. 60(b) (or their federal cognates).

28. Furthermore, the fraud the Plaintiff alleges is intrinsic fraud concerning the presentation of evidence to the Superior Court, not extrinsic evidence that prevented the Plaintiff from participating in the proceeding at all. According, for that reason, too, relief under N. C. R. Civ. P. 60(b) is unavailable to the Plaintiff.

29. In addition, the Plaintiff has not alleged either in terms or underlying facts the kind of conduct that amounts to a fraud on the court, let alone a fraud in which the redress is through a N. C. R. Civ. P. 60(b)(3) or (d)(3) equity action. Though the Plaintiff has alleged false testimony, even perjury and false testimony are not grounds for relief in an independent equity action. *Great Coastal*, 675 F.2d at 1357. Nor, for example, has the Plaintiff alleged facts which amount to "'the more egregious forms of subversion of the legal process.., those that we cannot necessarily expect to be exposed by the normal adversary process[ ]", *Elk Run Coal, Co.*,739 F.3d at 136 (citation omitted) a deliberate scheme to defraud the court, *Great Coastal*,675 F.2d at 1364-1365, or "fraud upon the court occurs where a party has acted knowingly in an attempt to

[8] In this and the following paragraphs the result would be the same for the Fed. R. Civ. P. cognates of the respective rules.

hinder the fact finder's fair adjudication of the case and his adversary's defense of the action [ ]"), *McMunn*, 191 F. Supp. 2d at 445 (citation omitted). Indeed, the allegations bespeak not some ominous scheme, but at most ultimately harmless error. After all, what nefarious purpose would that alleged conduct serve? All that activity did was get the Loan Documents and benefits of foreclosure to the right party in the end, however aberrantly. Consonant with the Liquidating Trust's earlier questions about how the Plaintiff was damaged, the Plaintiff has not alleged that someone else later tried to enforce the Loan Documents against her.

30. Finally, in an independent equity action permitted by Federal Rule 60(d)(3) and North Carolina Rule 60(b), the Plaintiff cannot seek damages. Most of her prayer for relief in paragraphs 101-104 seek damages of one kind or another.

CONCLUSION

In sum, the Order is final, claim and issue preclusion apply, the Court lacks the power to allow claims through the fraud on the court doctrine to override a state court judgment against a creditor and in any event the Plaintiff could not prevail on her fraud on the court theory.

Accordingly, for the reasons set forth herein, the Liquidating Trust respectfully request that the Court grant the Motion to Dismiss and grant such other and further relief as it deems just and proper.

Dated: May 29, 2014
New York, New York

/s/ Norman S. Rosenbaum
Gary S. Lee
Adam A. Lewis
Norman S. Rosenbaum
Samantha Martin
MORRISON & FOERSTER LLP
1290 Avenue of the Americas
New York, New York 10104
Telephone: (212) 468-8000
Facsimile: (212) 468-7900

Counsel for The ResCap Liquidating Trust

Exhibit 2

MORRISON & FOERSTER LLP
1290 Avenue of the Americas
New York, New York 10104
Telephone: (212) 468-8000
Facsimile: (212) 468-7900
Gary S. Lee
Adam A. Lewis
Norman S. Rosenbaum
Samantha Martin

Counsel for The ResCap Liquidating Trust

UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

Jennifer L. Wilson, Plaintiff, *v.* Residential Capital, LLC, et al. Defendants.	Adv. Proc. 12-01936 (MG)
In re RESIDENTIAL CAPITAL, LLC, *et al.*, Debtors	Case No. 12-12020 (MG) Chapter 11 Jointly Administered

THE RESCAP LIQUIDATING TRUST'S
CORRECTED SUPPLEMENTAL BRIEF IN SUPPORT OF THE DEBTORS' MOTION FOR DISMISSAL OF ADVERSARY PROCEEDING PURSUANT TO BANKRUPTCY RULE 7012(b) AND FRCP 12(b)(1) AND 12(b)(6) OR, IN THE ALTERNATIVE, PERMISSIVE ABSTENTION PURSUANT TO 28 U.S.C. §1334(c)(1)

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TO THE HONORABLE MARTIN GLENN
UNITED STATES BANKRUPTCY JUDGE:

The Liquidating Trust[1] hereby submits this supplemental brief (the "Supplemental Brief") in support of its Motion to Dismiss pursuant to the Court's instructions at the May 1, 2014 hearing on the Motion to Dismiss (the "Hearing"). Specifically, the Court directed the Liquidating Trust to address three issues with supplemental materials: (1) evidence regarding the chain of title of the Note and Deed of Trust (together, the "Loan Documents") originally issued by Plaintiff in favor of SunTrust Mortgage, Inc., dba Sun America Mortgage; (2) discussion of whether the North Carolina doctrine of preclusion (*res judicata* or collateral estoppel) bars the Plaintiff from making the claims she is making in this Adversary Proceeding; and (3) discussion of whether fraud on the Superior Court regarding the chain of title of the Loan Documents is grounds for setting aside the Order and abrogating the application of the doctrine of preclusion. This Supplemental Brief addresses the second and third issues; contemporaneously, the Liquidating Trust is submitting a separate declaration on the chain of title question.[2] In support of the Supplemental Brief, the Liquidating Trust respectfully represents as follows:

PRECLUSION

1. The question the Court posed for the Liquidating Trust was whether the Order of the Superior Court allowing the substitute trustee to foreclose on the Property pursuant to the

[1] Capitalized terms not defined in this brief will have the meanings ascribed to them in the *Debtors' Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP 12(b)(1) and 12(b)(6) or, In the Alternative, Permissive Abstention Pursuant to 28 U.S.C. §1334(c)(1)* [Docket No. 4] or the *ResCap Liquidating Trust's Reply in Support of the Debtors' Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP 12(b)(1) and 12(b)(6) or, in the Alternative, Permissive Abstention Pursuant to 28 U.S.C. §1334(c)(1)* [Docket No. 38] (the "Reply").

[2] The Court also asked the Liquidating Trust to address three specific cases: *Conklin v. Anthou*, 495 Fed. Appx. 257, 262 (3d Cir. 2012) writ denied, 133 S. Ct. 1729 (2013); *Kelleran v. Andrijevic*, 825F.2d 692, 694 (2d Cir. 1987); and *Johnson v. Laing (In re Laing)*, 945 F.2d 354, 358 (10th Cir. 1991). This Supplemental Brief discusses them in paragraphs 1 n.3, 13 and 15.

Loan Documents and Chapter 45 of the North Carolina General Stautes bars the claims that the Plaintiff has made in the Adversary Proceeding against the Debtor Defendants (ResCap and RFC).[3]

2. In deciding whether a state court decision is barred by preclusion, federal courts look to the preclusion law of the subject state. *See, e.g., Migra v. Warrant City Sch. Dist. Bd. Of Educ.*, 465 U.S. 75, 81 (1984); *DiSorbo v. Hoy*, 343 F.3d 172, 182-83 (2d Cir. 1996); *Brumby v. Deutsche Bank Nat'l Trust Co.*, No. 1:09-CV-144, 2010 WL 617368 (M.D.N.C. Feb 17, 2010); *Omernick v. LaRocque*, 406 F. Supp. 1156, 1159 (W.D. Wis.), *aff'd sub nom., Omernick v. Wisconson*, 539 F.2d 715 (7th Cir. 1976); *see also* 28 U.S.C. § 1738 (federal courts must afford state court decisions full faith and credit).

3. Here it is important to remember that the Order is a final judgment under North Carolina law. When a trustee commences a special proceeding to foreclose on a deed of trust in North Carolina, the clerk of court is required to hold a hearing (unless the hearing is waived) to determine if the trustee should be permitted to conduct a foreclosure sale. N.C. Gen. Stat. § 45-21.16(d). At the hearing, the trustee or secured party must establish, among other things, "the existence of [i] valid debt of which the party seeking to foreclose is the holder . . ." before it will be allowed to conduct a foreclosure sale. *Id*. § 45-21.16(d). In the special proceeding, the debtor may assert any legal defenses that would establish that the party seeking to foreclose is not the holder of the debt. *Tenney v. Birdsall* (*In re foreclosure of Goforth Props., Inc.)*, 432 S.E.2d 855, 859 (N.C. 1993). Under N.C. Gen. Stat. § 45-21.34, the debtor also may file a separate

[3] The Court did not ask for further briefing on the related *Rooker-Feldman* issue. But it did ask the Liquidating Trust to discuss Conklin, 495 Fed. Appx. at 262. In *Conklin*, the court held that the loser of a state court foreclosure proceeding could sue various officials related to the proceeding for their alleged misconduct; such a suit did not violate *Rooker-Feldman* if and to the extent that it did not seek to review the judgment of foreclosure as such. Here, *Rooker-Feldman* does apply at least as to paragraph 104i of the Complaint, which asks "[t]hat the defendants take nothing by their foreclosure sale" and paragraph 104j which asks that the Debtor Defendants surrender the Note, if not more broadly. Moreover, unlike in *Conklin*, the Plaintiff is suing defendants who were in no way connected to the foreclosure process.

action to assert any legal or equitable defenses that would demonstrate the absence of a valid debt or that the party seeking to foreclose is not the holder of the debt, but the debtor must file such an action and obtain an injunction of the foreclosure sale before the rights of the parties to the sale become fixed. N.C. Gen. Stat. § 45-21.34; *see Goad v. Chase Home Fin., LLC*, 704 S.E.2d 1, 4 N.C. Ct. App. (2010). Those rights ordinarily become fixed when the time for submitting an upset bid expires. N.C. Gen. Stat. § 45-21.29A; see *Goad*, 704 S.E.2d at 5.

4. If the clerk of court finds "the existence of [i] valid debt of which the party seeking to foreclose is the holder" and certain other things, the clerk is required to enter an order authorizing the trustee to conduct a foreclosure sale. N.C. Gen. Stat. § 45-21.16(d). The statutes provide that "[t]he act of the clerk in so finding . . . is a judicial act. . . ." *Id.* at § 45-21.16(d1). A debtor can appeal the clerk's order for a de novo hearing before a trial judge. *Id.* If, however, the order is not appealed within 10 days of its entry, it becomes final and binding. *See* N.C.R. App. P. 3(c)(1) & (c)(2) (30 days to appeal); *Phil Mech. Constr. Co. v. Haywood*, 325 S.E.2d 1, 3 (N.C. Ct. App. 1985). The Order was entered on January 25, 2010, and the Plaintiff neither appealed it nor sought to enjoin the foreclosure. The time for the Plaintiff to appeal has long since expired. The Order is therefore final.[4]

A. *Res Judicata*

5. As the Fourth Circuit has held, under North Carolina law, once a final judgment is entered in a prior proceeding, the doctrine of "[r]es judicata, or claim preclusion, bars the relitigation of any claims that were *or could have been* raised in [the] prior proceeding between the same parties [or their privies]". *Sartin v. Macik*, 535 F.3d 284, 287 (4th Cir. 2008) (emphasis added). *Res judicata* is very broad in North Carolina, as in many jurisdictions. It applies "to

[4] Whether the Order can be attacked via the fraud on the court doctrine will be the subject of the fraud on the court section of this Supplemental Brief.

every point which properly belong to the subject in litigation and which the parties, exercising reasonable diligence, might have brought forward at the time and determined respecting it." *Painter v. Wake Co. Bd. of Educ.*, 217 S.E.2d 650, 655 (N.C. 1975). For an action to be precluded under the doctrine of res judicata (or "claim preclusion") in North Carolina, a prior judgment must have been (1) a judgment on the merits in a prior suit resolving (2) claims by the same parties or their privies, and (3) a subsequent suit based on the same cause of action. *Whitacre P'Ship v. Biosignia, Inc.*, 591 S.E.2d 870, 880 (N.C. 2004). Here, clearly there is a final judgment on the merits in the Superior Court. Thus, only the second and third criteria of *Whitacre* remain to be examined in this matter.

6. Privity is defined in North Carolina as "mutual or successive relationship to the same rights of property. . . . In general, privity involves a person so identified in interest with another that he represents the same legal right." *N.C. ex rel Tucker v. Frinzi*, 474 S.E.2d, 128, 130 (N.C. 1996) (citation omitted) (finding that a state and county in the state were not in privity with each other, even though they were seeking the same outcome with regards to getting someone to pay child support). In *Smith v. Smith*, 431 S.E.2d 196 (N.C. 1993), an ex-wife sued a couple over title to certain property that the defendants got from the ex-husband through the divorce settlement. The defendants were not parties to the divorce or settlement as such. In dismissing entering judgment for the defendants, the Supreme Court of North Carolina held that the defendants were privies of the ex-husband as to the divorce action for preclusion purposes. *See also Cline v. McCullen*, 557 S.E.2d 588, 591 (N.C. Ct. App. 2001) ("[S]uccessive or mutual [rights in the same property] establishes that the interests of both Tindall and plaintiff are so intertwined that privity exists between them.") Accordingly, the wife was barred from the present suit by *res judicata*. In this Adversary Proceeding, the Debtor Defendants are, on the

one hand, the successor to SunTrust Mortgage, Inc., as to the Loan Documents, or the successor's agent, on the other hand.[5] Though not parties to the action in the Superior Court, they are privies.

7. The test for deciding whether the causes of action are identical for claim preclusion purposes is whether the claim presented in the new litigation arises out of the same transaction or series of transactions as the claim resolved by the prior judgment. An action is the same as a prior action when the new claim requests the same relief and raises the same set of material facts. ~~*State*~~*N.C. ex rel. Tucker v. Frinzi*,474 S.E.2d at 127. The facts of this matter easily satisfy this test as to the Complaints' claims for relief. The first three are for breach of contract and the fourth is for unfair and deceptive trade practices. And all relate in one way or another to whether SunTrust Bank was the holder of the Note and therefore had the right to commence the foreclosure action in the Superior Court. Indeed, as noted in the Motion to Dismiss at page four, one of the findings that the Superior Court had to and did make is the identity of the holder of the Note, which it found to be SunTrust Bank. Those claims for relief, all of which depend in the end on the Plaintiff's assertion that SunTrust Bank lacked title to the Loan Documents when it commenced the foreclosure action, are barred, therefore, by *res judicata* as applied in North Carolina.[6]

[5] An agent is a privy of the principal. *See, e.g., Jones v. First Franklin Loan Servcs.*, No. 3:10-CV-360-FDW-DSG 2011 WL 972518 (W.D.N.C. Mar. 15, 2011).

[6] Notably, the Plaintiff has yet to explain how she was harmed by the foreclosure. She does not deny that she had ceased making payments on the Note well before SunTrust Bank commenced the foreclosure, let alone before it actually occurred. Nor has she specified *how* she was harmed with respect to the conduct at issue (she has not suggested, for example, that she would not have suffered foreclosure by *someone* since she was in default, nor has she indicated that anyone has attempted to impose duplicative liability on her). She also has not quantified her damages. The latter, incidentally, argues against the Adversary Proceedings' being an informal, timely proof of claim. "Courts in the Second Circuit have long recognized the validity of informal proofs of claim. *See In re Lipman* , 65 F.2d 366 (2d Cir.1933); *Nat'l Bank of Westchester v. Wurlitzer Co.*(*In re Gibraltor Amusements, Ltd.*), 315 F.2d 210 (2d Cir.1963); *In re W.T. Grant Co.*, 53 B.R. 417 (Bankr. S.D.N.Y. 1985); *In re Nutri*Bevco, Inc.*, 117 B.R. 771 (Bankr. S.D.N.Y. 1990). In order for a document to constitute an informal proof of claim it must be in writing and filed with the bankruptcy court. *See W.T. Grant*, supra, 53 B.R. at 422. Furthermore, it must set forth the nature *and amount of the claim* and the intent on the part of the claimant to hold the debtor liable. *Id*. at 421; *see also Nutri*Bevco, supra*, 117 B.R. at 789. *In re Float, Inc,*, 163 B.R. 18, 20 (Bankr N.D.N.Y. 1993) (emphasis added).

B. Collateral Estoppel

8. Applying collateral estoppel forecloses the relitigation of issues of fact or law that are identical to issues which have been actually determined and necessarily decided in prior litigation in which the party against whom [collateral estoppel] is asserted had a full and fair opportunity to litigate.' *Sedlack v. Braswell Servs. Grp., Inc.*, 134 F.3d 219, 224 (4th Cir.1998) (citation omitted). To apply collateral estoppel (also known as issue preclusion) to an issue or fact, the proponent must demonstrate that (1) the issue or fact is identical to the one previously litigated; (2) the issue or fact was actually resolved in the prior proceeding; (3) the issue or fact was critical and necessary to the judgment in the prior proceeding; (4) the judgment in the prior proceeding is final and valid; and (5) the party to be foreclosed by the prior resolution of the issue or fact had a full and fair opportunity to litigate the issue or fact in the prior proceeding. *See id. See also, Kloth v. Microsoft Corp*. (*In re Microsoft Antitrust Lit.),* 355 F.3d 322 (4th Cir. 2004); *Whitacre Partnership v. Biosignia, Inc.*, *supra*.

9. There are two kinds of collateral estoppel, offensive (plaintiff employing against a defendant who previously litigated unsuccessfully against another party) and defensive (defendant employing against a plaintiff who previously litigated unsuccessfully). Courts are stricter when applying offensive collateral estoppel because of concerns for due process. *See In re Microsoft,* 355 F.3d at 326-27. The Debtor Defendants seek to apply collateral estoppel defensively. Thus, there is no heightened standard they must satisfy.

10. In the present case, all five elements of North Carolina collateral estoppel regarding the critical issues of title to the Loan Documents are present. The identity of the holder of the Note was actually litigated through the introduction of evidence by the substitute trustee, the Superior Court found that SunTrust Bank was the holder of the Note, the finding was critical to the Order, as the Order itself establishes, the Order is final and the Plaintiff was duly

served with notice of the hearing and able to make an appearance to defend herself (she has never alleged otherwise).

11. Since all of the Plaintiff's claims for relief in the Adversary Proceeding depend on her contention that SunTrust Bank was not the Note's holder, her claims must fail because she is bound by the Superior Court's finding that SunTrust Bank was, in fact, the holder of the Note.

FRAUD ON THE COURT

12. In the MTD Response and at the Hearing, the Plaintiff contends that title to the Loan Documents did not, in fact, rest in SunTrust Bank. This fact was evidenced by a form of the Note that differed from that SunTrust Bank used in the foreclosure action because it had an endorsement to a third party on it.[7] The Plaintiff contends that by representing to the Superior Court that SunTrust Bank did own the Loan Documents, SunTrust Bank committed fraud on the Superior Court that voids the Order, thereby sweeping away with it most of the Debtor Defendants' defenses, including preclusion and *Rooker-Feldman*.

A. The Proper Court

13. As stated in *Kelleran v. Andrijevic*, 825F.2d at 694 (no evidence claim against debtor obtained by fraud on the state court):

> "Congress has specifically required all federal courts to give preclusive effect to state-court judgments whenever the courts of the State from which the judgments emerged would do so...." *Allen v. McCurry*, 449 U.S. 90, 96 (1980) (citing 28 U.S.C. § 1738 (1982)). Bankruptcy courts fall within Congress' mandate. *See, e.g., In re* 27 B.R. 241, 243 (Bankr. E.D.N.Y. 1982).

[7] As noted earlier, the history of the Loan Documents will be the subject of a separate declaration. At this juncture it is worth noting that although the Plaintiff claimed at the Hearing that she only recently learned of the ownership issue, *see* Transcript of Hearing at 39:4-8, *In re Residential Capital, LLC*, No. 12-12020 (MG) (Bankr. S.D.N.Y.); *see also id.* 33:22-24, that is untrue. A complaint she filed with the North Carolina Commissioner of Banks on October 27, 2010 demonstrates that she knew enough to challenge the foreclosure before it took place on November 15, 2010. (*See* Declaration of Lauren Graham Delehey in Support of the Debtor's Motion for Dismissal of Adversary Proceeding Pursuant to Bankruptcy Rule 7012(b) and FRCP 12(b)(1) and 12(b)(6) or, in the Alternative, Permissive Abstention Pursuant to 28 U.S.C. §1334(c)(1), ¶ 16 & Ex. 5 (filed concurrently herewith).) At that point, as the Debtor Defendants will note presently, she still was within the one year limitations period for bringing a motion to vacate the Order for fraud under N. C. R. Civ. P. 60(b)(3), the North Carolina cognate of Fed. R.Civ. P. 60(b)(3). ⊥

14. A federal court has no authority to actually set aside a state court action, even when it is alleged that fraud on the court occurred in that action. *See Weisman v. Charles E. Smith Mgmt., Inc.*, 829 F.2d 511, 513 (4th Cir. 1987) ("the proper forum in which to assert that a party has perpetrated a fraud on the court is the court which allegedly was the victim of that fraud"); *Chewning v. Ford Motor Co.*, 35 F. Supp. 2d 487, (D.S.C. 1998) (citing to *Weisman* and holding that fraud on the court, as well as an independent action in equity, must be addressed by the court in which the action occurred); *Wilson v. Comm'r of Internal Revenue*, 309 Fed. Appx. 829 (5th Cir. 2009). As a result, a federal court cannot set aside a judgment for fraud on the court or an independent equity action, but must remand the action to the state court that is the subject of the action. *Chewning*. That does not mean that this Court cannot grant the Motion to Dismiss on the ground that, as the Liquidating Trust will argue, it is clear that the Plaintiff cannot succeed in seeking to set aside the Order in North Carolina.

15. However, there is a line of cases holding that a bankruptcy court may refuse to give preclusive effect to a state court judgment obtained by fraud on the court, but each of these cases concerns treatment of a claim *against* the debtor allegedly obtained by fraud on the state court. *See, e.g., In re Laing*, 945 F.2d at 358 (court allows claim against debtor because no fraud on the state court that rendered the underlying judgment; any fraud was intrinsic, not extrinsic in that it was not aimed at court but "related to the events that made up the *subject matter* of [and basis of the claims in] the state court action. . . ."); *Kelleran*, 825 F.2d at 694 (bankruptcy courts must honor state court judgments unless obtained "by collusion or fraud"; exception does not apply to state court default just because of an attorney/client relationship between parties or doubtful claims); *Margolis v. Nazareth Fair Grounds & Farmers Mkt.*, 249 F.2d 221, 223 (2d Cir. 1957) ("Bankruptcy courts are essentially courts of equity endowed with broad equity

powers . . . .A bankruptcy court may inquire into the validity of any claim asserted against the bankrupt and may disallow it if it is found to be without lawful existence.") (citation omitted); *In re Mastercraft Record Plating, Inc.*, 32 B.R. 106, 109-110 (S.D.N.Y. 1983) (state court claim obtained by fraud on the court is disallowed because bankruptcy court final arbiter of claims against debtor); *In re Bocker*, 123 B.R. 164, 165 (Bankr. E.D.N.Y. 1991) (claim not obtained by demonstrated fraud consisting of state court plaintiff's misrepresentation of applicable interest rate, so claim allowed by bankruptcy court in debtor's bankruptcy).

16. The preceding materials indicate that this Court cannot look behind the Order for fraud on the court for purposes of *allowing* the claims asserted by the Plaintiff in the Complaint (if they are otherwise cognizable by the Court). However, in the succeeding portion of this Supplemental Brief the Liquidating Trust will analyze whether relief would be available for fraud on the court even if the Court could do so.

B. Fraud on the Court: Standards and Procedures

17. Because North Carolina Rule of Civil Procedure 60(b) is exactly like the Federal Rules of Civil Procedure 60(b)(3) and 60(d)(3), North Carolina state courts have looked to interpretation of the federal rule when interpreting the state rule. *See Henderson v. Wachovia Bank of North Carolina, N.A.*, 551 S.E.2d. 464, 469 (N.C. Ct. App. 2001) (applying the federal standard of fraud on the court to the state rule and determining that negligence on the part of an attorney to not properly communicate with their client did not constitute fraud on the court).

18. The seminal Supreme Court case on the topic is *Hazel-Atlas Glass Co. v. Hartford-Empire Co.*, 322 U.S. 238 (1944), where the court found fraud on the court because of a deliberate scheme to defraud the court of appeals, a scheme that threatened public injury. Courts have interpreted *Hazel* as saying that fraud on the court has been recognized as a "nebulous concept" that "should be construed very narrowly." *Fox ex rel. Fox v. Elk Run Coal*

Co., 739 F.3d 131,136 (4th Cir. 2014). This interpretation has been bolstered by interpretation of Fed. R. Civ. P. Rule 60.

19. Rule 60(b)(3) (whether federal or North Carolina) allows a party up to one year to seek relief from a judgment on grounds that the judgment was procured by fraud, misrepresentation, or misconduct by the opposing party.

20. Fraud on the court is a "nebulous" theory "should be construed very narrowly" lest the doctrine swallow up and render pointless Federal Rule 60(b)(3).. *Great Coastal Express, Inc. v. Int'l Bhd. of Teamsters*, 675 F.2d 1349, 1356 (4th Cir. 1982). "[T]his doctrine should be invoked only when parties attempt 'the more egregious forms of subversion of the legal process..., those that we cannot necessarily expect to be exposed by the normal adversary process." *Fox ex rel. Fox*, 739 F.3d at 136 (citation omitted). The doctrine is limited to "egregious" situations such "as bribery of a judge or juror, or improper influence exerted on the court by an attorney, in which the integrity of the court and its ability to function impartially is directly impinged." *Great Coastal*, 679 F.2d at 1356. Furthermore, because attorneys are officers of the court, courts have been much more likely to find fraud on the court when an attorney is colluding in the scheme. *See Cleveland Demolition Co. v. Azcon Scrap Corp.*, 827 F.2d 984 (4th Cir. 1987) (finding that mere evidentiary conflicts that do not prove that an attorney was colluding with a witness to present perjured testimony is a conflict to be resolved at trial and does rise to fraud on the court).

21. Courts have held that in order to find fraud on the court, the fraud or misrepresentation must have been intentional. *United States v. MacDonald*, 161 F.3d 4 (4th Cir. 1998) (holding that in order to establish fraud on the court, it must be established that the fraud was material and deliberate); *McMunn v. Mem'l Sloan-Kettering Cancer Ctr.*, 191 F. Supp. 2d

440 (S.D.N.Y. 2002) ("fraud upon the court occurs where a party has acted knowingly in an attempt to hinder the fact finder's fair adjudication of the case and his adversary's defense of the action." (citation omitted)). Fraud on the court must be established by clear and convincing evidence. *E.g., King v. First Am. Investigations, Inc.*, 287 F.3d 91, 95 (2d Cir. 2002).

22. Federal Rule 60(d)(3) and North Carolina Rule 60(b) states that the one year time limitation does not limit a court's power to entertain an independent action to relieve a party from a judgment, order, or proceeding. This is known as an independent equity action. *E.g., Weisman*, 829 F.2d at 513.

23. The standard for this is (1) a judgment which ought not, in equity and good conscience, to be enforced; (2) a good defense to the alleged cause of action on which the judgment is founded; (3) fraud, accident, or mistake which prevented the defendant in the judgment from obtaining the benefit of this defense, (4) the absence of fault or negligence on the part of the defendant; and (5) the absence of any adequate remedy at law. *Asterbadi v. Leitess*, 176 Fed. Appx. 426, 430 (4th Cir. 2006) (citing *Great Coastal*). For purposes of this analysis, the alleged cause of action is the original cause of action and the defendant is the defendant in the original cause of action. In the Fourth Circuit, courts have held that perjury and false testimony are not grounds for relief in an independent equity action because "they can and should be exposed at trial." *See Great Coastal*, 675 F.2d at 1357. Independent equity actions are only available to prevent "a grave miscarriage of justice." *United States v. Beggerly*, 524 U.S. 38 (1998). Finally, the plaintiff in an independent equity action may not seek damages. *Chewning*, 35 F. Supp. 2d at 489.

24. Furthermore, in the Second Circuit, courts have held that an independent equity action cannot be based on a lack of evidence of the fraud if the evidence could have been

discovered earlier with reasonable diligence. *Gottlieb v. S.E.C.*, 310 Fed. Appx. 424 (2d Cir. 2009) (finding that recently discovered evidence is not a sufficient basis). And in *Wolfson v. Wolfson*, No. 03-CIV-0954(RCC) 2004 WL 224508 (S.D.N.Y. Feb 5, 2004) the court found that where the plaintiff knew about the supposed fraud within the year time frame allowed in Fed. R. Civ. P. 60(b)(3) and did nothing, he is in the situation through his own neglect and carelessness and cannot assert an independent equity action.

25. Moreover, "[i]t is well established in North Carolina 'that where a judgment has been entered, relief from that judgment is not available in an independent action upon facts which amount to intrinsic fraud.'" *Hooks v. Eckman*, 587 S.E.2d 352, 354 (N.C. Ct. App. 2003) (quoting *Textile Fabricators, Inc. v. C.R.C. Indus, Inc.*, 259 S.E.2d 570, 572 (N.C. Ct. App. 1979)). Therefore, the ability of a party to maintain a separate action collaterally attacking a final judgment or order due to allegations of fraud or misrepresentations within a prior proceeding depends on whether the basis of the contention is intrinsic or extrinsic fraud. *See Stokley v. Stokley*, 227 S.E.2d 131, 134 (N.C. Ct. App. 1976). The North Carolina Court of Appeals has defined fraud as extrinsic "when it deprives the unsuccessful party of an opportunity to present his case to the court. If an unsuccessful party to an action has been prevented from fully participating therein there has been no true adversary proceeding, and the judgment is open to attack at any time." *Id*. On the contrary,

> "intrinsic fraud occurs when a party (1) has proper notice of an action, (2) has not been prevented from full participation in the action, and (3) has had an opportunity to present his case to the court and to protect himself from any fraud attempted by his adversary. Specifically, intrinsic fraud describes matters that are involved in the determination of a cause on its merits."
>
> *Hooks*, 587 S.E.2d at 354 (citation omitted); *See also Smith*, 431 S.E.2d at 200.

North Carolina courts consider false testimony to be intrinsic fraud. *Hooks*, 587 S.E.2d at 354;

Textile Fabricators, Inc. at 259 S.E.2d at 571. Therefore, a complaint of intrinsic fraud related to a foreclosure proceeding can only be brought through a N. C. R. Civ. P. 60(b)(3) motion within the special proceeding and within one year of the entry of the clerk's order.

C. The Plaintiff Cannot Obtain Relief for Fraud on the Court

26. As noted earlier, far more than a year has passed since the entry of the Order. Thus, the Plaintiff cannot obtain relief under N. C. R. Civ. P. 60(b)(3) for fraud on the Court.[8]

27. By the same token, because the Plaintiff believed that she discovered that the Note was not held by SunTrust Bank at the time of the foreclosure hearing, as established by her complaint to the North Carolina Banking Commission, she cannot allege tolling of the time limits of N. C. R. Civ. P. 60(b)(3) or assert an independent equity action under N. C. R. Civ. P. 60(b) (or their federal cognates).

28. Furthermore, the fraud the Plaintiff alleges is intrinsic fraud concerning the presentation of evidence to the Superior Court, not extrinsic evidence that prevented the Plaintiff from participating in the proceeding at all. According, for that reason, too, relief under N. C. R. Civ. P. 60(b) is unavailable to the Plaintiff.

29. In addition, the Plaintiff has not alleged either in terms or underlying facts the kind of conduct that amounts to a fraud on the court, let alone a fraud in which the redress is through a N. C. R. Civ. P. 60(b)(3) or (d)(3) equity action. Though the Plaintiff has alleged false testimony, even perjury and false testimony are not grounds for relief in an independent equity action. *Great Coastal*, 675 F.2d at 1357. Nor, for example, has the Plaintiff alleged facts which amount to "'the more egregious forms of subversion of the legal process.., those that we cannot necessarily expect to be exposed by the normal adversary process[ ]", *Elk Run Coal, Co.*,739

[8] In this and the following paragraphs the result would be the same for the Fed. R. Civ. P. cognates of the respective rules.

F.3d at 136 (citation omitted) a deliberate scheme to defraud the court, *Great Coastal*,675 F.2d at 1364-1365, or "fraud upon the court occurs where a party has acted knowingly in an attempt to hinder the fact finder's fair adjudication of the case and his adversary's defense of the action [ ]"), *McMunn*, 191 F. Supp. 2d at 445 (citation omitted). Indeed, the allegations bespeak not some ominous scheme, but at most ultimately harmless error. After all, what nefarious purpose would that alleged conduct serve? All that activity did was get the Loan Documents and benefits of foreclosure to the right party in the end, however aberrantly. Consonant with the Liquidating Trust's earlier questions about how the Plaintiff was damaged, the Plaintiff has not alleged that someone else later tried to enforce the Loan Documents against her.

30. Finally, in an independent equity action permitted by Federal Rule 60(d)(3) and North Carolina Rule 60(b), the Plaintiff cannot seek damages. Most of her prayer for relief in paragraphs 101-104 seek damages of one kind or another.

CONCLUSION

In sum, the Order is final, claim and issue preclusion apply, the Court lacks the power to allow claims through the fraud on the court doctrine to override a state court judgment against a creditor and in any event the Plaintiff could not prevail on her fraud on the court theory.

Accordingly, for the reasons set forth herein, the Liquidating Trust respectfully request that the Court grant the Motion to Dismiss and grant such other and further relief as it deems just and proper.

Dated: May 29, 2014
New York, New York

/s/ Norman S. Rosenbaum

Gary S. Lee
Adam A. Lewis
Norman S. Rosenbaum
Samantha Martin
MORRISON & FOERSTER LLP
1290 Avenue of the Americas
New York, New York 10104
Telephone: (212) 468-8000
Facsimile: (212) 468-7900

Counsel for The ResCap Liquidating Trust

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