

HARRY LEE JONES., <i>et al.</i>	*	IN THE
Plaintiffs	*	CIRCUIT COURT
v.	*	FOR
NOVASTAR FINANCIAL, INC., <i>et al.</i>	*	BALTIMORE CITY
Defendants	*	Part 20
	*	Case No. 24-c-04-009317

ORDER

Upon consideration of defendants’ motion to dismiss, motion to dismiss or stay the proceedings due to *forum non conveniens*, plaintiffs’ opposition, and defendants’ reply, arguments of counsel having been heard on April 19, 2005, it is this 4th day of May, 2005, by the Circuit Court for Baltimore City, Part 20,

ORDERED for the reasons set forth in the accompanying memorandum opinion of this date that defendants’ motion to dismiss is **GRANTED**, without prejudice. Plaintiffs are granted leave to amend their complaint within fifteen days of this order. The defendants’ motion to dismiss or stay due to *forum non conveniens* is **DENIED**.

ALBERT J. MATRICCIANI, JR.
Judge

cc: All Counsel (via email)

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MEMORANDUM OPINION

I. Background

NovaStar Financial Inc. (NFI) is a real estate investment company incorporated under Maryland law. NFI is the parent company of NovaStar Home Mortgage Inc. (NHMI), a Delaware mortgage broker business. As NFI’s subsidiary, NHMI seeks to increase securitization of nonconforming loans to serve as collateral to expand NFI’s securities portfolio.

In 1999, NHMI opened Delaware limited liability companies (LLC) nationwide, including Maryland. NHMI recruited mortgage brokers to be branch managers, then formed LLCs with NHMI and branch managers as members. At the LLC’s formation, the branch manager and NHMI entered into a limited liability agreement and a branch support and administration agreement.

In 2003, Harry Lee Jones, Charles E, Mull, Sr., and Pyllis Mull received home loans processed and brokered by the Timothy Brown LLC, an affiliate of NHMI located in Lanham, Maryland. In February 2004, NHMI withdrew as a member of all its LLCs, at which time the LLCs automatically dissolved.

On December 16, 2004, Mr. Jones, and Mr. and Mrs. Mull, as representative plaintiffs,

brought a purported class action against NFI, NHMI, and nine Maryland LLCs.¹ The purported members of the plaintiff class are Maryland residents who received mortgage loans that were “originated, processed and/brokered through LLCs affiliated with Defendants NovaStar Financial, Inc. and NovaStar Home Mortgage, Inc., prior to February, 2004.” (Compl. ¶ 1.) Plaintiffs allege that the unlicensed LLCs brokered a substantial percentage of the loans they originated to NHMI, or one of the NHMI approved investors. Plaintiffs further allege that even though the settlement statements identified NHMI as the recipient of the settlement fees, and the fees were initially paid to NHMI, NHMI paid most of the fees to the unlicensed LLCs. Count I of the complaint alleges that the LLCs operated without a license, in violation of the Maryland Mortgage Lender Law (MMLL). MD. FIN. INST. CODE ANN. §§ 11-501 *et seq.* (Unless noted otherwise, all sections referred to in this opinion will be from the Maryland Financial Institute Article). Count II alleges that the defendants conspired with each other by agreement or understanding to deprive the class members of their statutory rights and money.

On March 1, 2005, defendants filed a motion to dismiss for failure to state a claim and a motion to dismiss or stay the proceedings due to *forum non conveniens*. Plaintiffs filed an opposition on March 15, 2005 and defendants filed a reply on April 1, 2005. A hearing was held on April 19, 2005.

II. Standard of Review

In reviewing a motion to dismiss for failure to state a claim, the Court assumes the truth of all well pleaded allegations and draws all reasonable inferences in the plaintiffs’ favor.

¹ NovaStar/Timothy Brown LLC, NovaStar/Colletti LLC, NovaStar/Frederick Curry LLC, NovaStar/James David Keeny LLC, NovaStar/Joseph F. Morrison/Joseph T. Morrison LLC, NovaStar/Plotnikov LLC, NovaStar/Michael Tumbarello, NovaStar/Patrick Tuttle LLC, NovaStar/Jason E. Williams LLC.

Bennett Heating & Air Conditioning, Inc. v. Nations Bank, 103 Md. App. 749 (1995), *rev'd in part on other grounds*, 342 Md. 169 (1996). Any ambiguity or uncertainty in allegations, however, is construed against the pleader. *Alleco v. Weinberg Foundation*, 340 Md. 175, 193 (1995).

III. Standing

Defendants challenge the named plaintiffs' standing to sue NFI and eight out of the nine LLCs, reasoning that none of these parties were involved with the named plaintiffs' home loans. The Court is persuaded that the named plaintiffs do have to allege injury by every co-conspirator in a class action in order to plead conspiracy properly. The Court finds that plaintiffs have standing only to sue NHMI and the Timothy Brown LLC.

Maryland Rule 2-231 on class actions states:

One or more members of a class may sue or be sued as representative parties on behalf of the class if 1) the class is so numerous that joinder of all members is impracticable, 2) there are questions of law or fact common to the class, 3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and 4) the representative parties will fairly and adequately protect the interests of the class.

Before reaching the requirements listed above, the Court, however, must first determine whether the plaintiffs have "an actual, real and justiciable interest susceptible of protection through litigation." *Mayor and City Council of Ocean City v. Purnell-Jarvis, Ltd.*, 86 Md. App. 390, 403, (1991). If not, class action allegations do not create new claims or remedy a lack of standing under substantive law. *Pollockoff v. Md. Nat'l Bank*, 288 Md. 485, 500 (1980)(stating that "[I]n Maryland civil procedure, the basic building block is the cause of action. Recognition . . . that the class action procedure could be used in appropriate cases at law did not create a new cause of action or claim.); *see also Akerman v. Oryx Communications, Inc.*,

609 F. Supp. 363 (S.D.N.Y. 1984). Representative plaintiffs must have been personally injured by the defendants. It is not enough that injury was suffered by other unidentified members of the class to which the representative plaintiffs belong and whom they purport to represent. *Miller v. Pacific Shore Funding*, 224 F. Supp.2d 977, 996 (D. Md. 2002); *see also Pollockoff*, 288 Md. at 497 (noting in a class action suit that “the fundamental aspect of standing is that it focuses on the party seeking to get his complaint before the court ”)(internal citations and quotations removed).

Here, NFI was not involved in assisting the plaintiffs with their home mortgages. Beyond conspiracy, nothing in the complaint alleges how NFI injured the representative plaintiffs. Likewise, the complaint is void as to the participation of the eight LLCs in the representative plaintiffs' loans. The complaint asserts no injuries caused by the eight LLCs that were personally suffered by the representative plaintiffs. Even in a purported class action, the representative plaintiffs do not have standing to bring an action against NFI and the other eight LLCs, because standing is not created by the possibility that other unidentified members of the class may have been injured by NFI or those eight LLCs.

The plaintiffs assert that they have standing to bring an action against all members of a conspiracy. Besides being the parent company of NHMI, NFI, however, is not connected to the alleged conspiracy. All agreements that purportedly formed the business model which the defendants used to carry out the conspiracy were signed by NHMI, not NFI. Furthermore, NFI is a real estate investment company and the MMLL only applies to mortgage lenders and brokers. Therefore, NFI did not violate the MMLL by failing to obtain a license. §§ 11-501 *et seq.* It is not tied to the other alleged conspirators by any agreement that the plaintiffs can prove.

Additionally, the defendants argue that the eight LLCs should be dismissed as to the conspiracy claim because the complaint fails to plead how the LLCs conspired with each other.

The Court, however, does not believe that is what the complaint intended to plead or actually pleads. The Court believes the complaint alleges that each LLC conspired with NHMI separately to operate without a license and unlawfully to receive settlement fees. Even if the complaint adequately pleads conspiracies between the LLCs and NHMI, there remains the problem of standing. Accordingly, the named plaintiffs have standing only as to the NovaStar/Timothy Brown LLC and NHMI.²

IV. Count I – Violation of MMLL

Defendants seek to dismiss the plaintiffs’ MMLL claim on the basis that Maryland has created no private right of action against unlicensed entities. The Court explains below why this is not the state of law in Maryland, and also why it disagrees that NHMI should be dismissed because at all times NHMI was licensed under the MMLL.

The Financial Institutions Article of the Maryland code states:

Any unlicensed person who is not exempt from licensing under this subtitle who makes or assists a borrower in obtaining a mortgage loan in violation of this subtitle may collect only the principal amount of the loan and may not collect any interest, costs, finders fees, broker fees, or other charges with respect to the loan.”

§ 11-523(b). *Thrasher v. Homecomings Financial Network, Inc.* explained that section 11-523(b) provides an implied right of action against unlicensed persons. 154 Md. App. 77, 84 (2003). While there is no definition for “unlicensed person,” the Court of Special Appeals concluded from the definitions of “license” and “person” that an “unlicensed person” was simply a person who did not have a license to partake in the business of a mortgage lender. *Id.* at 84-85. The Court, however, held that licensed persons do violate the MMLL when they operate

² Unless otherwise noted, the following sections do not discuss the eight LLCs, but only the Timothy Brown LLC.

outside of the place for which they are licensed, but they are not “unlicensed persons” for the purpose of section 11-523(b). §§ 11-505, 11-523(b); *Thrasher*, 154 Md. App. at 85. Although *Thrasher* states in a footnote “a private action was limited to suits against creditors that fail to get a license at all,” it cannot mean the right to private action applies only to creditors. *Thrasher*, 154 Md. App. at 82, n.1 (quoting *Staley v. Americorp Credit Corp., et al.*, 164 F. Supp. 2d 578, 581, n. 2 (D. Md. 2001)). Such a conclusion is contrary to the statute on its face because it clearly states that it applies to persons “who make[] or assist[] a borrower in obtaining a mortgage loan.” § 11-523(b). Clear and unambiguous statutory language needs no further interpretation. *Breitenback v. N.B. Handy Co.*, 366 Md. 467, 473 (2001).

The Court believes that section 11-523(b) applies to the Timothy Brown LLC, even if it is an unlicensed mortgage broker and not an unlicensed creditor. As held in *Thrasher*, an “unlicensed person” is a person who did not have a license to partake in the business of a mortgage lender. *Thrasher*, 154 Md. App. at 84-85. Timothy Brown LLC acted as a “mortgage lender” because it “engage[s] in whole or in part in the business of servicing mortgage loans for others.” § 11-501(j). Because section 11-523(b) is not restricted to creditors, the plaintiffs have a private right of action against the unlicensed person, Timothy Brown LLC.

Finally, while section 11-523(b) does not apply to NHMI because it is undisputed that NHMI is a licensed lender, NHMI may still be a party to the conspiracy claim. The conspiracy claim is addressed in the next section.³

³ Attached to the defendants’ motion to dismiss is a sample employment contract that the defendants allege branch managers signed with NHMI. Defendants argue that because the LLC is an employee of NHMI, section 11-502(b) of MMLL excuses NHMI’s employees from obtaining their own licenses. Section 11-502(b) states “the provisions of this subtitle do not apply to . . . (13) Employees action within the scope of their employment with: (i) a licensed mortgage lender; or (ii) a person who is exempt from licensure of this subtitle.” The Complaint, however, does not mention any employment contracts, and more specifically, it is not clear if the Timothy Brown LLC ever signed an employment contract. Since neither party addressed the employment contract at the hearing, the court finds it unnecessary to address this argument in order to resolve the present motions.

V. Count II – Conspiracy

Defendants seek to dismiss the conspiracy claim for a variety of reasons. Having already addressed some of the argument, the Court will now address arguments not previously discussed: 1) whether the complaint must allege a tort claim as the basis of a conspiracy claim, 2) whether plaintiffs can allege a conspiracy between NHMI and the LLC, and 3) whether the plaintiffs have properly alleged a conspiracy.

Maryland courts have long recognized that conspiracy standing alone is not actionable, but requires an “unlawful act.” *Id.* at 97. An “unlawful act” is not necessarily a criminal act. It could be a tort, a breach of contract, or an actionable wrong. To create an actionable wrong, the legal rights of the plaintiff must be in some way invaded. *Knoche v. Standard Oil Co.*, 138 Md. 278 (1921); *see also Alleco Inc. v. Harry & Jeanette Weinberg Foun., Inc.*, 340 Md. 176 (1994); *Alexander & Alexander v. Evander*, 88 Md. App. 642 (1991). Hence, as long as the legal rights of the plaintiff are violated, an actionable wrong that establishes the basis of a conspiracy claim does not have to be a tort. Here, the plaintiffs allege that their legal rights were violated when the unlicensed LLC conspired with NHMI to deprive them of their legal rights and money. As already discussed, the plaintiffs have a private right of action against unlicensed persons under the MMLL. Therefore, the Court finds that the plaintiffs’ rights to have a licensed mortgage broker process their loans have been invaded and the plaintiffs have alleged an “unlawful act” that can adequately form the basis of a conspiracy claim.

Defendants’ contention that a corporation cannot conspire with itself begs the question here. Under Delaware law, LLCs are regarded as separate legal entities. *See Elf Atochem North America, Inc. v. Jaffari*, 727 A.2d 286, 288 (Del. Supr. 1999). Therefore, it is possible that NHMI, although a member of the LLC, conspired with the LLC, an entity independent of

NHMI.

Lastly, the defendants assert that the plaintiffs failed to plead conspiracy adequately. Conspiracy requires 1) an agreement or understanding between two or more persons, 2) some unlawful or tortious act done in the furtherance of the conspiracy, and 3) actual damages resulting to the plaintiff. *Von Roven v. Lacey*, 262 Md. 94, 98 (1971). The Court first considers whether there was an agreement or understanding between two or more persons. The plaintiffs claim that when NHMI and the branch manager entered into the limited liability agreement and the branch support and administration agreement, the agreements created a business model for conspiracy to engage in mortgage lending activities without a license.

These agreements, however, do not of themselves constitute unlawful or tortious action in furtherance of a conspiracy. It is clear from the agreements that all mortgages were property of NHMI, even though they were brokered by the LLC. The limited liability agreement clearly states that the LLC is to “engage in the business of furnishing branch support and administrative services to NovaStar.” (Defs. Mot. Dismiss Exh. 2 ¶ 1.4.) The branch support and administration agreement then details what the LLC is to provide NovaStar, which includes all “rights under, and interest in, contracts, personal property or equipment leases or agreements . . . owned, used, held for use or employed by the Branch Manager.” (Defs. Mot. Dismiss Exh. 3 ¶ 2.1.) An LLC’s compensation, the branch support fee, is calculated by taking “all fees received by NovaStar for all closed loans brokers to NHMI or any other lenders by NovaStar minus NovaStar’s Fee and Office Expenses.” (Defs. Mot. Dismiss Exh. 3 ¶ 1.1.) Exhibit B, attached to the branch support and administration agreements, lays out NovaStar’s Fee and section 5.1 defines Office Expenses. At all times NHMI had a license to operate as a mortgage lender under the MMLL and its agreement with the LLC clearly states the LLC’s role, to provide branch

services. Even the plaintiffs' complaint states that all brokerage fees were paid to the licensed NHMI, not the LLC. (Compl. ¶¶ 38, 41.) Although the plaintiffs state that the LLC unlawfully received most of the fees, the complaint fails to allege how the written agreements furthered this unlawful purpose. Furthermore, nothing in the agreements mentions licensing. Therefore, the Court cannot accept the plaintiffs' assertions that the agreements themselves created a business model under which the LLC carried out unlawful actions in the furtherance of a conspiracy to operate without a license, in the absence of more specific allegations.

After concluding that there are no unlawful agreements, the Court determines whether there was an understanding between NHMI and the LLC to conspire. Even if the agreements themselves do not indicate a conspiracy, one may exist. The Court, however, does not find in the complaint allegations of an agreement to carry out unlawful actions outside of the limited liability agreement and the branch support and administration agreement. On the contrary, the complaint is confused as to whether the LLC actually agreed with NHMI to operate without a license. On one hand the complaint alleges that LLCs in general paid NHMI a fee to be licensed in each state in which it wanted to operate, but NHMI never licensed the LLCs after receiving the fees. (Compl. ¶¶ 2, 33) On the other hand the complaint makes the allegation that the LLCs were attractive because they allowed loans to originate from all 50 states when it typically cost \$1,700 per state. (Compl. ¶ 31.) The complaint, however, fails to explain why the LLCs would pay NHMI a fee for licensing in different states if the LLCs already permitted loans to originate from all 50 states. Moreover, the complaint does not explain whether the LLC paid for licenses in multiple states, which states, and whether the LLC knew NHMI did not obtain a license for the LLC after receiving the fee. Thus, the Court finds that the plaintiffs failed to plead

adequately the first requirement of conspiracy, that there existed an agreement between two or more persons, and does not find it necessary to consider the remaining two requirements.

VI. Conclusion

The motion to dismiss is granted, without prejudice. Plaintiffs may file an amended complaint within fifteen days of the date of the accompanying order.

VII. Motion to Dismiss or Stay Due to *Forum Non Conveniens*

For the guidance of the parties, the Court would deny the motion to dismiss or stay proceedings based on *forum non conveniens*. While there are three on-going cases involving the same allegations, they do not address Maryland law. The federal cases in the Southern District of Georgia and the Southern District of California involve claims under the federal Real Estate Settlement Procedures Act. The Illinois case involves Illinois law. Although the California case was transferred to Georgia by the multi-district litigation panel on April 26, 2005, the Illinois case remains in Illinois. This case was brought under Maryland law and the alleged injuries were committed in Maryland. The Court believes this state court remains the appropriate jurisdiction to resolve Maryland law and finds that the defendants did not meet their burden of showing that the interests of justice would be served by transferring this action. *Odenton Dev. Co. v. Lamy*, 320 Md. 33, 575 (1990).

ALBERT J. MATRICCIANI, JR.
Judge

cc: All Counsel (via email)

