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Order on Motions for Summary Judgment (ACORN DEVELOPMENT, LLC)

Alice D. Bonner
Superior Court of Fulton County

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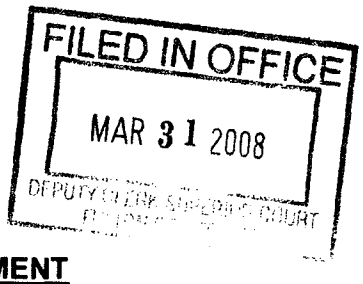
IN THE SUPERIOR COURT OF FULTON COUNTY
STATE OF GEORGIA

ACORN DEVELOPMENT, LLC ROBERT STEWART, AND DENISE STEWART Plaintiffs, v. CJ KELLEY LLC, KELLEY DEVELOPMENT CORPORATION, MORGAN FINANCIAL, LLC, GEORGE O'NEAL, TERESA CURTIS, Defendant,	)	Civil Action No. 2007-CV-135511



ORDER ON MOTIONS FOR SUMMARY JUDGMENT

On January 9, 2008, counsel in the above-styled action appeared before the Court to present oral argument on Plaintiff's Motion for Partial Summary Judgment and the Motion for Summary Judgment of Defendant Morgan Financial, LLC. Upon request and with leave of the Court, Plaintiffs submitted a supplemental brief on February 25, 2008. After reviewing the record of the case, the briefs submitted on the motions, and the arguments presented by counsel, the Court finds as follows:

Factual and Procedural Background:

This case involves a condo conversation investment scheme in The Reserve of Dunwoody Condominiums (the "Reserve"). CJ Kelley, LLC ("CJ Kelley") purchased an apartment complex to be converted into the Reserve. CJ Kelley then sold individual units to investors over market value and pooled the excess money in order to renovate and convert the property into condominiums with the stated purpose of selling the units at a profit.

Plaintiff Acorn Development purchased a total of thirteen units beginning in January 2006. The Stewarts purchased eight units in May 2006. Plaintiffs own their units in fee simple.

To complete the transactions, Plaintiffs signed sales contracts, management agreements, and powers of attorney which gave CJ Kelley the authority to lease the units purchased by investors, to collect rents from them, and to sell the units to third parties. Under the terms of the agreements, CJ Kelley was to be paid a management fee for the services performed on the property.

Joanne Morgan is the principal of Morgan Financial, LLC ("Morgan"), which became the managing member of CJ Kelley sometime between May and July of 2006. On April 5, 2006, CJ Kelley assigned its purchase and sale agreement on the Reserve to Morgan, effective July 15, 2006. Per Morgan's instructions, however, the excess purchase price amounts on units sold in May and June were directed to Morgan's bank accounts. Joanne Morgan, acting for Morgan Financial, first communicated with Plaintiffs and other CJ Kelley investors on July 30, 2006, informing them that, effective July 1, 2006, Morgan had assumed management of CJ Kelley and the Reserve.

Morgan continues to act as the sole Manager-member of CJ Kelley and as the project-manager of the Reserve. Morgan Financial has collected rents on the units, but has not accounted for the proceeds. The parties disagree about whether or not this is allowed under the terms of the management agreements.

George O'Neal was the principal of CJ Kelley and the initial investment solicitor. Neither he nor Ms. Curtis have been served with the Complaint in this matter. Mr. O'Neal has been absent from this proceeding and is alleged by Plaintiffs to be "missing" since June or July of 2006.

CJ Kelley filed an answer in this action, but then filed a bankruptcy petition on December 26, 2007.

Automatic Bankruptcy Stay:

Because CJ Kelley has filed a bankruptcy petition, pursuant to 11 U.S.C. § 362(a), CJ Kelley is entitled to an automatic stay of this proceeding as it relates to the corporation. Harkleroad & Hermance, P.C. v. Stringer, 220 Ga. App. 906, 907 (1996). A stay as to one co-defendant, however, does not automatically stay the proceeding with regard to other codefendants who may be jointly and severably liable to plaintiffs. Paul v. Joseph , 212 Ga. App. 122 (1994). Thus, Plaintiffs' Motion for Summary Judgment with regard to CJ Kelley is stayed pending resolution of the bankruptcy action.

Defendant Morgan's Motion For Summary Judgment:

Members of limited liability corporations are generally not subject to personal liability. See Milk v. Total Pay and HR Solutions, Inc., 280 Ga. App. 449 (2006). Morgan seeks summary judgment on all claims asserted against it because it was acting, and continues to act, solely in its capacity as the Manager-member of CJ Kelley, and therefore, is protected by limited liability. See O.C.G.A. § 14-11-305(b). Exceptions to the general liability prohibition exist where the corporate veil is pierced, in derivative actions, and in some instances of fraud. "An LLC member may be held individually liable if he or she personally participates or cooperates in a tort committed by the LLC or directs it to be done." Milk v. Total Pay and HR Solutions, Inc., 280 Ga. App. 449, 454 (citing BTL COM v. Vachon,, 278 Ga. App. 256, 260(1) (2006)).

Here, Plaintiffs produced the assignments between Morgan and CJ Kelley that indicate a role in the alleged activities beyond that of a mere Member-manager.

Additionally, Plaintiffs introduced a wiring instruction letter directing purchase price proceeds to Morgan's bank account before the purported installment of Morgan as the Member-manager of CJ Kelley. Additionally, Plaintiffs presented the Court with Morgan's 30(b)(6) deposition testimony that Morgan has collected rents, has not accounted for or segregated rents, failed to pay certain mortgage payments, and took a series of actions with regard to the Reserve. These actions—if they are found to be tortious, which is not before the Court at this stage—present questions of fact regarding Morgan's potential liability.

Accordingly, Defendant Morgan's Motion for Summary Judgment is hereby **DENIED**.

Plaintiffs' Motion for Partial Summary Judgment:

Plaintiffs seek summary judgment on its RICO claims against Morgan. Plaintiffs allege that CJ Kelley's offering of the condo conversion investment constituted a sale of unregistered securities in violation of Georgia law, which formed a predicate act under the Georgia RICO statutes. Mosely v. State, 253 Ga. App. 710, 712 (2002). Plaintiffs allege that Morgan's involvement with the securities sale as the assignee under the purchase agreements and, later, as the Manager-member constituted a pattern of racketeering activity which utilized proceeds from a predicate act (e.g., the investment).

Plaintiffs argue that the condo investment qualifies as a "security" because it involves (1) a money investment, (2) a common enterprise, (3) was entered into with an expectation of profit solely derived from the efforts of a third party, and (4) materially restricted the owner's occupancy or rental of his unit. O.C.G.A. § 10-5-2(26); Eberhardt v. Waters, 901 F.2d 1578 (11th Cir. 1990); 1976 Op. Att'y Gen. No. 76-75, p. 129. Such

a security, if sold without proper registration or authorization, is a violation of Georgia's Security Act and may be a predicate act under the RICO statutes.

Under O.C.G.A. § 10-5-2-(26) a "security" includes an investment contract which "holds out the possibility of return on risk capital even though the investor's efforts are necessary to receive such return... [s]uch return is dependent upon essential managerial or sales efforts of the issuer or its affiliates." Id. Under Georgia law, the definition of a "security" is interpreted broadly. Gilbert v. Meason, 137 Ga. App. 1, 3 (1975) ("state security laws are an expression by the General Assembly of a statutory policy affording broad protection to investors and are remedial in nature and should be liberally construed..."); S.E.C. v. W.J. Howey Co., 328 US 293 (1946). Real estate investment contracts will be considered a security if the investor's return is essentially dependent upon the efforts of the syndicator. Fortier v. Ramsey, 136 Ga. App. 203, 205 (1975); Eberhardt v. Waters, 901 F.2d 1578 (11th Cir. 1990).

The Eleventh Circuit in Eberhardt adopted the Supreme Court's test in Howey to determine an investment from a traditional security which looked at three factors: (1) money investment, (2) common enterprise, and (3) expectation of profit solely dependent upon efforts of others. Eberhardt v. Waters 901 F.2d 1578, 1580 - 1581 (11th Cir. 1990). A common enterprise is found where the investors have "no desire to perform the chores necessary for a return, and are attracted to the investment solely by the prospects of a return." Id.

Here, Plaintiffs presented evidence that they invested money into the Reserve by purchasing units in fee simple at a price over market value. They also directed the Court to the management and leasing agreement and powers of attorney to establish that CJ Kelley/Morgan had virtually unfettered control over the property itself and the

profits to be made on the investment. Plaintiffs allege that they have been restricted from accessing their units, but there is some dispute in the record regarding this point. Regardless, the centralized management and aggregation of profits and losses on the individual units restrict Plaintiffs' ability to exercise their ownership rights over their units.

The weight of the evidence supports the finding that the investment in the Reserve constituted a security under O.C.G.A. § 10-5- *et seq.* Such sales, if unregistered, may form the basis of a predicate act under Georgia RICO Act §§16-14-4(a) and 16-14-4(c). See Mosley v. State, 253 Ga. App. 710, 712 (2002).

What is unclear, however, is the distinction between Morgan's independent role in the transaction, if any, and its protected role as a Manager-member of CJ Kelley as it relates to the sale of the Reserve units and their management. The Court has long recognized that that "great caution should be exercised by the court in disregarding the corporate entity." Old Nat. Villages, LLC v. Lenox Pines, LLC, ____ S.E.2d ____, 2008 WL 768097*3 (Ga.App. March 25, 2008) (citing Yukon Partners v. Lodge Keeper Group, 258 Ga.App. 1, 5-6 (2002)). In light of the questions that remain regarding whether or not Morgan should face liability, Plaintiffs' Motion for Summary Judgment is premature and hereby **DENIED**.

SO ORDERED this 31 day of March, 2008.

Alice D. Bonner
ALICE D. BONNER, SENIOR JUDGE
Superior Court of Fulton County
Atlanta Judicial Circuit

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