FOR PUBLICATION

IN THE SUPERIOR COURT
FOR THE
COMMONWEALTH OF THE NORTHERN MARIANA ISLANDS

NORTHERN MARIANAS HOUSING CORPORATION, **Plaintiff, and** **JESSICA CASTRO, et al., and JOSEPH FLORES, et al.,** **Plaintiffs in Intervention,** **vs.** **SSFM INTERNATIONAL, INC., TELESOURCE CNMI, INC., TELEBOND INSURANCE CORPORATION, and JOHN DOE,** **Defendants.**	**CIVIL ACTION NO. 06-0123** **ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT TELESOURCE CNMI, INC.'S MOTION TO DISMISS AND DENYING DEFENDANT TELEBOND INSURANCE CORPORATION'S MOTION TO DISMISS**
JESSICA CASTRO, et al., **Plaintiffs in Intervention,** **vs.** **NORTHERN MARIANAS HOUSING CORPORATION,** **Defendant.**	

This matter came before the Court on April 17, 2007 at 2:30 p.m. in Courtroom 220A on the motion of defendant Telesource, CNMI, Inc. ("Telesource") to dismiss certain claims asserted in the respective complaints of the homeowner plaintiffs in intervention Jessica Castro, et al., ("Castro

Homeowners") and Joseph Flores, et al., ("Flores Homeowners") and on the motion of defendant Telebond Insurance Corporation ("Telebond") to dismiss both complaints on the basis of the plaintiffs' failure to state a cause of action against Telebond. Joseph E. Horey, Esq., appeared on behalf of both Telesource and Telebond to argue in favor of the motions. Appearing in opposition to the motions, the Castro Homeowners were represented by attorneys Edward C. Arriola, Mark K. Smith and Delia S. Lujan, and the Flores Homeowners were represented by Joaquin DLG. Torres, Esq. Plaintiff Northern Marianas Housing Corporation ("NMHC") also appeared at the hearing, represented by counsel Vicente T. Salas and F. Matthew Smith. Defendant SSFM International, Inc., appeared through its counsel Brien Sers Nicholas.

Having considered the arguments of counsel, the materials submitted and the applicable law, the Court hereby issues its written decision to grant in part, and to deny in part the motion of defendant Telesource to dismiss certain claims of the homeowner plaintiffs, and to deny the motion of defendant Telesource to dismiss the homeowners' complaints for the reasons set forth herein.

I. FACTUAL AND PROCEDURAL BACKGROUND

This action arises from various alleged design and construction defects in the Tottotville housing project, also known as the Koblerville Expansion Project, a subdivision of forty-five single-family residences located in Koblerville, Saipan. In the late 1990's, NMHC proposed the construction of a tract of homes for low-to-moderate income families on land that it had acquired for this purpose from the Division of Public Lands, Department of Lands and Natural Resources. Construction began in late 1999 and the project was eventually completed and accepted in early 2002. Between February 1, 2002, and September 25, 2002, NMHC sold all of the improved parcels of the subdivision to individual homeowners by quitclaim deeds. Defendant SSFM International, Inc. ("SSFM"), was the project engineer for the development and served as a consultant to NMHC during construction.

Defendant Telesource served as the general contractor for the construction project and Telebond was the contractor's surety on the construction contract.

Over the next three years, homeowners began to complain to NMHC and to the media about problems with the structures, including roof leakage, rust, termites, inadequate drainage and lack of water pressure. NMHC first undertook to repair some of these problems itself, and then hired a consultant, EFC Engineers & Architects Corp., to inspect the properties and to provide a report on the extent and causes of the problems. In its report of July 26, 2005, the consultant concluded that there were defects in the homes caused by the poor workmanship of the construction contractors and deficiencies in design by the engineers. The homeowners' grievances generated much publicity and even two House Resolutions demanding that NMHC take steps to remedy the situation.[1]

On March 23, 2006, NMHC filed a complaint for damages against defendants SSFM and Telesource for breach of contract, breach of express and implied warranties, violations of the Building Safety Code and the Consumer Protection Act, and also against Telebond on the basis of the performance bond it had issued on the construction contract. SSFM answered with a general denial on May 9, 2006. On May, 15, 2006, Telesource and Telebond filed separate motions to dismiss all causes asserted in the complaint pursuant to Rule 12(b)(6) of the Commonwealth Rules of Civil Procedure. The motions were converted to motions for summary judgment and the Court continued the hearing on the matter until November 6, 2006, after receiving notice that the Tottotville homeowners intended to move to intervene in the action. Motions to intervene were filed by two separate groups of homeowners, respectively, on August 28 and September 30, 2006. These motions were opposed by defendant Telebond. On December 20, 2006, the Court issued a written order (*amended*, April 9, 2007) granting the motions to intervene, dismissing NMHC's claim under the Consumer Protection Act, and denying the defendants' motions for judgment on NMHC's remaining causes of action.

[1] House Resolution No. 14-106 (February 11, 2005) and House Resolution No. 15-34 (March 22, 2006).

On November 29, 2006, plaintiffs in intervention Jessica Castro and other individuals ("Castro Homeowners"), representing the owners of thirty-five of the Tottotville homes, filed their complaint listing a total of twenty-three causes of action variously directed against NMHC, SSFM, Telesource and Telebond. On December 12, 2006, the owners of nine additional homes ("Flores Homeowners") filed a complaint containing eight causes of action and naming as defendants SSFM, Telesource and Telebond. In their complaints, both groups of homeowners seek contractual remedies as alleged third-party beneficiaries of NMHC's contracts with SSFM, Telesource and Telebond, and also seek recovery in tort for the allegedly faulty design and/or construction of their homes. Both groups claim fraud, building code violations, and violations of the Consumer Protection Act by SSFM and Telesource. The Castro Homeowners name NMHC as a defendant in their claims based upon fraud, building code violations and breach of implied warranty, and also assert a claim for strict liability in tort against NMHC, SSFM and Telesource.

On January 30, 2007, Telesource and Telebond filed motions to dismiss certain claims by both groups of homeowners pursuant to Com. R. Civ. P. 12(b)(6). Specifically, Telesource has moved to dismiss the Castro Homeowners' claims against it that are based upon strict liability, fraud, breach of express and implied warranties and the Consumer Protection Act. Telesource moves on the same grounds for the dismissal of the Flores Homeowners' claims for breach of contract, breach of express and implied warranties, negligence, fraud, and for violation of the Consumer Protection Act. Telebond has moved to dismiss all homeowner claims against it on the basis that the homeowners' complaints fail to allege facts that would allow the homeowners to recover as third-party beneficiaries of the performance bond.

II. ANALYSIS

1. The Applicable Standard for a Rule 12(b)(6) motion.

The moving defendants have presented a number of the same issues that were previously raised in connection with their prior motions to dismiss certain claims of NMHC and, with the possible

exception of Telebond, the parties have again included exhibits and arguments on matters extrinsic to the pleadings. Rule 12(b)(6) examines the threshold issue of whether a plaintiff is entitled to present evidence by allowing a defendant to challenge the contents of a complaint. *In re Estate of Roberto*, 2002 MP 23 ¶ 12, 6 N.M.I. 508, 512. When, on a motion to dismiss, matters outside the pleadings are presented to the Court and are not excluded, such motion is treated as one for summary judgment. Com. R. Civ. P. 12(b)(6). *Furuoka v. Dai-Ichi Hotel*, 2002 MP 5 ¶ 17, 6 N.M.I. 378-379. At the hearing on the defendants' motions, the Court indicated that it was inclined to consider the motions under the standard applicable to motions for summary judgment. The parties, however, stipulated to have the motions heard as Rule 12 motions and the Court therefore exercises its discretion to strike and disregard all matters extrinsic to the pleadings and to consider only the legal sufficiency of the complaints. *Cf., Furuoka, supra,* ¶ 19. Accordingly, the Court must determine whether or not the plaintiffs have stated a viable claim for recovery without considering the plaintiffs' conclusions of law, but treating all well-pleaded allegations of fact as true and drawing all reasonable inferences therefrom in favor of the plaintiffs. *In re Adoption of Magofa*, 1 N.M.I. 449, 454 (1990).

2. Telesource's Motion to Dismiss Certain Claims of the Homeowners

Telesource's motion raises fundamental questions of the availability of particular remedies in the context of an action that is brought by the individual purchasers of homes in a multi-home public development against the contractor who built those homes based upon alleged defects in construction. Recent decades have seen an enormous volume of similar cases in the continental United States, resulting in conflicts between various state courts and often changing rules of decision within those jurisdictions as courts have struggled to fit the homeowners' grievances into legally-recognized theories of recovery.[2] While there is local precedent for actions by owners against builders on building

[2] *See, generally, Aas v. Superior Court (William Lyon Company),* 12 P.3d 1125, 1130 (Cal. 2000) (discussing this development and noting that such a case is difficult to characterize "because it arises from the nebulous and troublesome margin between tort and contract law.") The problem arises because home purchasers, although most directly affected by the building contractor's faulty performance, usually lack contractual privity with the contractor and also typically do not

contracts and the Commonwealth is not without legislative and decisional law on the subject of construction defects, the question of the availability of particular remedies to homeowners who are in the position of the plaintiffs in this case has not yet been fully decided in this jurisdiction.

A. Strict Liability for Faulty Home Construction

Telesource raises the fact that strict liability, as it developed in the context of products-liability law, was not traditionally applied to the sale and purchase of improved real property and cites the Restatement. RESTATEMENT (THIRD) OF TORTS: PRODUCT LIABILITY § 19(a) (1998). A full reading of Section 19(a) of the Restatement, however, includes the black-letter statement that items such as "real property… are products when the context of their distribution and use is sufficiently analogous to the distribution and use of tangible personal property that it is appropriate to apply the rules stated in this Restatement," and also the comment that "courts impose strict liability for defects in construction when dwellings are built, even if on-site, on a major scale, as in a large housing project." Id., § 19(a), cmt. e. Admitting this general principle, Telesource maintains that the Castro Homeowners' complaint fails to sufficiently allege the "particular factual context" that would support making the analogy mentioned in the Restatement, and that the strict liability claim should be dismissed for this reason. (Telesource's Mot. to Dismiss, p. 3).

Telesource's position is that homes may only be considered "products" for purposes of strict liability when they are built within "mass-production projects on a truly industrial scale," and that both complaints fail to allege this sort of mass-production. (Telesource's Reply in Supp. of Mot. to Dismiss, p. 3). Telesource relies heavily upon the circumstances underlying the decision in *Schipper v. Levitt & Sons, Inc.*, 207 A.2d 314 (N.J. 1965), a landmark case in which the Supreme Court of New Jersey first extended strict products-liability law to new home construction.

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suffer the type of injury that is compensable in tort. *Id.* The California Legislature reacted to *Aas* by creating a statutory cause of action on behalf of homeowners for construction defects. Cal. Civ. Code §§ 895, *et seq.* (effective Jan. 1, 2003).

To the extent that homes are standardized and built on a mass scale, their construction more closely resembles the mass-production of tangible items of personal property and therefore facilitates the analogy described in Section 19(a) of the Restatement. Some courts have limited their characterization of newly-constructed homes as "products" for purposes of strict liability to only those homes that are "mass-produced," without defining the latter term by any numerical range. *See, e.g.*, *Oliver v. Superior Court*, 211 Cal.App.3d 86, 89 (Cal.App. 1989). Other courts have broadly considered the policy rationale underlying strict products liability to be more determinative, finding that real property improvements constructed by one who is in the business of building such improvements would be considered "products" for the purpose of imposing strict liability with little or no regard for the quantity of improvements or their mode of construction. *See, Chitkin v. Lincoln Nat'l Ins. Co.*, 879 F.Supp. 841, 860-861 (S.D.Cal. 1995)(*citing, Del Mar Beach Club Owner's Assoc., Inc., v. Imperial Contracting*, 123 Cal.App.3d 898, 913 (Cal.App. 1981)); *Board of Educ. of City of Chicago v. A, C and S, Inc.*, 546 N.E.2d 580, 591 (Ill. 1989); *also, Patitucci v. Drelich*, 379 A.2d 297, 298 (N.J.Super. 1977).

The rationale for strict products liability is that the costs of harm caused by defective products are best absorbed by the manufacturer who put the products on the market rather than by the consumers who often have a limited ability to protect themselves. *Greenman v. Yuba Power Products, Inc.*, 377 P.2d 897, 900 (Cal. 1962). Historically, the theory was developed out of the law of implied warranties, which shares the rationale that the manufacturer of a product is in a better position than the consumer to detect and safeguard against the risks posed by defective products. RESTATEMENT (THIRD) OF TORTS: PRODUCT LIABILITY § 1, cmt. a, (1998); *See, also,* Ellen Wertheimer, *The Biter Bit: Unknowable Dangers, The Third Restatement and the Reinstatement of Liability Without Fault*, 70 BROOK. L. REV. 889, 890, n. 2 (Spring 2005) (noting that forty-five states have adopted the Restatement's expression of strict products liability). In a different context, the Commonwealth Supreme Court has held that there exists an implied warranty of habitability on the part of a home builder in favor of the new home's

purchasers that is implied by law in order "to protect new homeowners from shoddy construction work," noting that for new homebuyers, "[t]he harsh rule of *caveat emptor* has no place in today's society." *Reyes v. Ebetuer*, 2 N.M.I. 418, 431 (1992).[3]

The Castro Homeowners allege that Telesource is a commercial builder who constructed forty-five tract homes and related infrastructure within the Tottotville project, which by community standards is "a large housing project" built "on a major scale," and that plaintiffs purchased their homes with limited opportunity to inspect them prior to purchase. REST., *supra*, § 19(a), cmt. e. Plaintiffs allege that Telesource produced, and made commercially available, defective homes that were purchased by the plaintiffs and that these defects actually and proximately caused the plaintiffs harm. Given the rationale for the theory of strict products liability as expressed in the Restatement and accepting the factual allegations of the complaint as true for the purpose of ruling on the present motion, the Court is not prepared to find that the homeowners have inadequately alleged the circumstances from which it may be concluded that their homes are "products" for the purpose of strict liability.

B. The Economic Loss Rule

A more substantive obstacle to the homeowners' tort claims lies in the economic loss rule, raised by Telesource as grounds for dismissal of "Count Sixteen" (Strict Liability) of the Castro Homeowners' complaint and "Count VII" (Negligence) of the Flores Homeowners' complaint.

[3] Because tort liability premised upon a theory of implied warranty has been viewed as a stepping-stone to modern products liability, some jurisdictions have deemed the former theory to be subsumed within the latter, so that a tort plaintiff will generally not be allowed to plead both theories. *See, e.g.*, *Hawkeye Security Ins. Co. v. Ford Motor Co.*, 199 N.W.2d 373, 381 (Iowa 1972); *Thiele v. Faygo Beverage, Inc.*, 489 N.E.2d 562, 584 (Ind.App. 1986). "Count Sixteen" of the Castro Homeowners' complaint is captioned as "strict liability," rather than as "strict *products* liability," and is ambiguous with regard to whether or not the homeowners are seeking a tort recovery on this claim. The Castro Homeowners separately plead breach of implied warranties by Telesource in "Count Nineteen" of their complaint. Based upon the arguments presented in connection with the present motion, and viewing the complaint in a light most favorable to the non-moving plaintiffs, the Court interprets "Count Sixteen" to be based upon a theory of strict liability in tort, and distinguishes it from "Count Nineteen" on this basis.

The economic loss rule prohibits tort recovery based upon a defective product when the product has caused no injury to a person and no damage to some other property. The rule applies equally whether a claim is stated in strict liability or negligence, and received its definitive expression in the unanimous U.S. Supreme Court admiralty opinion *East River Steamship Corp., v. Transamerica Delaval, Inc.*, 476 U.S. 858, 106 S.Ct. 2295, 90 L.Ed 2d 865 (1986) (endorsing California Chief Justice Traynor's rationale for the rule as expressed in *Seely v. White Motor Company*, 403 P.2d 145 (Cal. 1965)). The rule rests upon a straightforward and compelling rationale: someone who purchases a product that fails to meet promised expectations, falls apart or self-destructs, without injuring anyone or harming some other tangible property, already has a remedy in the law of warranty. The duty owed by the manufacturer/seller to the purchaser is determined by the law of contract and defined by their agreement. Allowing a tort action for the mere failure of the product would therefore disrupt the agreed allocation of risks between the parties. *Id.*, 476 U.S. at 872-873.

Despite the apparent simplicity of the rule and the persuasiveness of its rationale, courts have had enormous difficulty applying it to claims by parties in various commercial and consumer contexts. This is especially the case in construction-defect litigation.[4] The parties have taken advantage of the radical differences between jurisdictions on this issue, together with the absence of CNMI authority, to submit persuasive authority strongly supporting their respective positions, but which are ultimately in direct conflict. *Compare, A.C. Excavating v. Yacht Club II Homeowners Assoc., Inc.*, 114 P.3d 862, 866 (Colo. 2005) (rule does not apply to action for negligent home construction) *and*, *Aas v. Superior Court*, *supra*, 12 P.3d at 1138-39 (rule applies to action for negligent home construction).

[4] *See*, Anita Bernstein, *Keep It Simple: An Explanation of the Rule of No Recovery for Pure Economic Loss*, 48 ARIZ. L. REV. (2006) (challenging the Restatement's policy rationale for the rule); *and especially*, Patricia H. Thompson and Christine Dean, *Continued Erosion of the Economic Loss Rule in Construction Litigation By and Against Owners*, 25 CONSTRUCTION LAWYER 36 (2005) (charting the erratic history of the rule and noting the recent reluctance of courts to apply it to homeowners' construction-defect claims).

This Court, however, is constrained by 7 CMC § 3401 to apply the common law rules of decision as they are expressed in the A.L.I.'s Restatements of Law, and the latest version of the Restatement of Torts does supply a "majority position" in the form of its limiting definition of harm:

> § 21. Definition Of "Harm To Persons Or Property": Recovery For Economic Loss
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> For purposes of this Restatement, harm to persons or property includes economic loss if caused by harm to:
>
> (a) the plaintiff's person; or
>
> (b) the person of another when harm to the other interferes with an interest of the plaintiff protected by tort law; or
>
> (c) the plaintiff's property other than the defective product itself.

RESTATEMENT (THIRD) OF TORTS: PRODUCT LIABILITY § 21 (1998).

Comment d to Section 21 of the Restatement (Third) of Torts maintains that a "strong majority" of courts adhere to the strict statement of the rule as expressed in *East River*, and deny recovery in negligence and strict liability when the plaintiff's "harm" does not fit the definition stated in the section. The comment recognizes the minority trend toward narrowing the rule, but expresses that the majority of jurisdictions continue to apply the rule broadly to prohibit tort damages for purely economic harm.

The Castro Homeowners have alleged "personal harm" in the form of a "loss of enjoyment," that they must live in homes that are "unsafe for habitation," and that they essentially must endure "deplorable and substandard" living conditions created by the contractor's negligence. (Complaint of Pls. in Intervention [Castro], ¶¶ 204-205). At the hearing on this motion, the Castro Homeowners conceded that the "majority position" would not recognize these consequences as constituting the type of harm that is compensable in tort. On the other hand, the Flores Homeowners allege that they "have suffered severe emotional distress, severe mental anguish, severe pain and suffering, and severe worries in an amount to be proven at trial." (Summons and Compl. and Demand for Jury Trial [Flores], ¶ 136, p. 44). The Flores Homeowners, however, have not stated facts that would show the intentional infliction of emotional distress, and recovery based upon the negligent infliction of emotional distress

is not available for property damage. *See*, *Charfauros v. Board of Elections*, 1998 MP 16, ¶ 63, 5 N.M.I. 188, 201-202; *also*, *Hocog v. OKP(CNMI) Corporation*, Civ. No. 06-0445 (N.M.I. Super. Ct., Dec. 22, 2006) (Order Partially Granting Defs.' Mot. to Dismiss) (*citing*, RESTATEMENT (SECOND) OF TORTS § 46 (1965)). Based upon the facts as stated in the Homeowners' complaints, the Court must grant Telesource's motion to dismiss "Count Sixteen" (Strict Liability) of the Castro Homeowners' complaint, and "Count VII" (Negligence) of the Flores Homeowners' complaint on the basis that the homeowners have only alleged an economic loss resulting from the condition of their homes.

C. Availability of Claims Under the Consumer Protection Act

The CNMI's Consumer Protection Act provides a cause of action by and on behalf of consumers who have been the victims of specified unfair or deceptive business practices. 4 CMC §§ 5101, *et seq*.[5] It was enacted expressly for the protection of consumers and applies to the sale or marketing of both goods and services. 4 CMC § 5102(a)(1). Although the term "consumer" appears in nearly every section of the Consumer Protection Act, the term is not defined by the Act. The Court has previously determined in this action, however, that the remedies afforded by the Act are intended to protect the party possessing the weaker bargaining strength in a consumer transaction, and that a cause of action under the Consumer Protection Act may not be generally appended to an ordinary commercial contract dispute between parties of relatively equal bargaining power. (Order Granting Mots. To Intervene; Granting in Part and Den. in Part Def. Telesource's Mot. to Dismiss and Den. Def. Telebond's Mot. to Dismiss, December 20, 2006 (*amended*, April 9, 2007), p. 10). The Commonwealth Supreme Court has upheld a homeowner's recovery under the Consumer Protection Act against a builder for misrepresenting the quality of construction that went into the building of a

[5] 4 CMC § 5112(a) states: "*Any person aggrieved* as a result of a violation of this article may bring an action in the Commonwealth Superior Court for such legal or equitable relief as the court may order. In addition to actual damages, the court shall award liquidated damages in an amount equal to the actual damages in cases of willful violations, and shall award costs and reasonable attorney's fees if the plaintiff prevails." (emphasis added). Section 5111 provides that the plaintiff's remedies under the Act are cumulative and non-exclusive of plaintiff's other legal remedies.

house, but noted that there had been no challenge to the general applicability of the Act to the facts in question. *Reyes*, *supra*, 2 N.M.I. at 434, 435.

Telesource maintains that the character of the transactions alleged in the complaints precludes the application of the Consumer Protection Act because Telesource's services and/or products were never advertised or sold to the general public and because the entire Tottotville project, from inception through completion, was carried out under the auspices and direction of NMHC, a government corporation that is exempted from the Act. 4 CMC § 5106(a).[6] Section 5105 of the Act proscribes enumerated practices "in the conduct of any trade or commerce," and section 5104(b) defines "trade" and "commerce" as "the sale, advertising, offering for sale, contracting for sale, exchange, distribution for consideration, or solicitation for purchase to the general public of any goods or other property, real, personal, or tangible[sic], or of any service…." Telesource argues that it contracted to build the residences in response to a proposal from NMHC, and that the plaintiffs are a discrete group of homebuyers who purchased their homes directly from NMHC, so that Telesource cannot be found to have offered, advertised, or sold any goods or services "to the general public." 4 CMC § 5104(b).

Like the consumer protection laws of nearly every state, the CNMI's Consumer Protection Act was modeled on the Federal Trade Commission Act (15 U.S.C. § 45(a)), but provides for broader protection to the public through its general scope and available remedies. (See, 33 TTC § 351; *amended by* PL 6-46, § 1, *modified*). Unlike the comparable statutes found in a majority of the states, the CNMI's Consumer Protection Act does not require a plaintiff to show actual harm to a consumer in order to prove a violation of the Act. 4 CMC § 5108. Rather, it is enough for the plaintiff to show more probably than not that the defendant's practices are prohibited by the Act with respect to a "hypothetical consumer." *Isla Financial Services v. Sablan*, 2001 MP 21 ¶ 24, 6 N.M.I. 338, 342. The Commonwealth Supreme Court affirmed the applicability of the Act to a single telephonic solicitation

[6] 4 CMC § 5106 "Exemptions" states in part: "Nothing in this article shall apply to: (a) Actions or transactions carried out by the Commonwealth government, any branch thereof or any other governmental agency…."

between the Vice President and General Manager of a financial services company and the surviving daughter of the company's deceased client, even though the solicitation was personally targeted and in no way addressed to the general public. *Id*., ¶ 7, ¶ 25. Unlike Telesource, however, the defendant in *Isla Financial Services* did not contest the finding that it was involved in "trade or commerce" as these terms are defined by Section 5104(b) of the Act. *Id.*, ¶ 23.

The comparable statutes and related decisional law from other jurisdictions reveal a tension between the public policy supporting broad protections on behalf of the consuming public and the need to prevent an over-inclusiveness that would transform every breach of commercial obligation into a statutory violation.[7] In support of its position, Telesource cites decisions representing a restrictive application of consumer protection statutes. *Eg*., *Teller v. Bill Hayes, Ltd.*, 213 A.D.2d 141, 145, 630 N.Y.S.2d 769, 772 (App. Div. 1995) (fraudulent conduct by home repair contractor not shown to have "potential impact on consumers at large"); *Zeeman v. Black*, 273 S.E.2d 910, 914-915 (Ga.App. 1980) (isolated sale of home does not impact "consumer marketplace"), *citing*, *State v. Meridith Chevrolet, Inc.*, 244 S.E.2d 15, 18 (seller of used automobiles who rolled back odometers on the vehicles before selling them to a retail auto dealer could not be liable under Georgia's consumer protection statute because sale from wholesaler to retailer was not a "consumer transaction"). The Court notes that these decisions were first cited by Telesource in its 25-page reply brief to the plaintiffs' opposition to the present motion and, although no procedural objection was raised, plaintiffs have not been afforded the opportunity to file a written response prior to their oral arguments at the hearing.[8]

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[7] *See*, Jeff Sovern, *Private Actions Under the Deceptive Trade Practices Acts: Reconsidering the FTC Act as Rule Model*, 52 OHIO ST. L. J. 437 (1991); *and* Anthony Paul Dunbar, *Consumer Protection: The Practical Effectiveness of State Deceptive Trade Practices Legislation*, 59 TUL. L. REV. 427 (Dec. 1984).

[8] Plaintiffs did not request an opportunity to file supplemental memoranda in response to the additional matters raised in the plaintiff's reply memorandum, but were allowed to extensively address such matters at the lengthy hearing on the defendants' motions to dismiss. In the interest of fairly deciding the material issues raised with respect to the pending motions, the Court has considered all of the cited authorities and legal arguments actually presented without regard to the procedural irregularity, even though assuming this burden inevitably delays to some extent the final ruling on the matter.

The history of the Consumer Protection Act and the various forms it has taken in other jurisdictions may illuminate the issues involved, but the Court's interpretation of the CNMI's Consumer Protection Act must be guided in the first instance by the plain meaning of the words used therein, as understood from the context of the whole statute, so that its application of the statute will ultimately give effect to the clearly expressed intent of the legislature. *Commonwealth Ports Authority v. Hakubotan Saipan Ent., Inc.*, 2 N.M.I. 212, 222-224 (1991). As noted, Section 5102 of the Act clearly expresses the legislature's intent to protect consumers from abusive commercial practices, but also clearly expresses its finding that merchants themselves may be included within the class of consumers to be benefited, and that one of the Act's purposes is to "[r]equire or restrict commercial practices in order to further an orderly market environment." 4 CMC § 5102(a)(5), (b)(3). Although "commercial practices" are not defined by the statute, a "business practice" is defined as "any conduct carried out in a business context, whether an isolated act or a continuing series of related acts." 4 CMC § 5104(a).[9] Section 5123(a) provides that "In interpreting this article, the courts of the Commonwealth shall construe any ambiguity in any provision of this article, or in any regulation or order issued under this article, *or in any implied or express warranty covered by this article, or any similar ambiguity, in favor of the consumer*." (emphasis added). Given this directive from the legislature and in light of the broadly stated purpose of the Act, the Court may not supply an interpretation of terms such as "commercial practices" or of "general public" that serves to restrict the applicability of the Act, unless the legislature's intention to provide such a restriction is manifestly apparent in the statutory text. *Bank of Saipan v. Superior Court (Att'ys Liab. Assurance Soc'y, Inc.)*, 2001 MP 5 ¶¶ 17-23, 6 N.M.I. 242, 248.

Telesource's argument that it is beyond the reach of the consumer protection laws because it does not solicit, or provide services to, the public at large would require the Court to adopt an unwarranted and overly restrictive interpretation of the Consumer Protection Act. Telesource certainly

[9] "Business practice" does not appear in any other section of the Consumer Protection Act.

holds itself out to be a competent construction contractor and responded to NMHC's request for proposals to build forty-five homes for sale to low and moderate income families by warranting that its services would be of a particular quality fit for the ultimate purchasers. Although the CNMI's Consumer Protection Act defines "trade or commerce" as encompassing a broad range of marketing and sales to "the general public," to construe "the general public" as meaning no less than the *entire* public, thereby excluding any identifiable sub-market, would frustrate the purpose of the Act and lead to unconscionable results. Many items commonly regarded as consumer products and services are not available or even offered to the entire public at large, and the ability to redefine sub-classes of consumers so as to exclude them from the "general public" appears limitless. No provisions of the Act support this limitation, nor would it be consonant with the purpose of the Act to allow a business to shield itself from liability for its illegal practices by passing its representations, goods, or services through a retailer or middleman. *Cf.*, *Zeeman v. Black*, *supra*, 273 S.E.2d at 915-916.[10]

Telesource further distinguishes its role in the Tottotville development on the basis that the "middleman" to whom its services were rendered was NMHC, a public entity that is itself exempted from liability under the Consumer Protection Act. 4 CMC § 5106(a). Telesource argues that it cannot

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[10] *Zeeman* and *Merideth Chevrolet*, *supra*, relied upon a definition of "consumer transaction" in the Georgia statute as "…the sale, lease, or rental of goods, services, or property, real or personal, primarily for personal, family, or household purposes." Ga. Code Ann. § 106-1202(g). This definition was derived from the *Magnusson-Moss Warranty-Fed. Trade Comm. Improvement Act*, 15 U.S.C. § 2301 and incorporated into the Model Uniform Deceptive Trade Practices Act (Nat. Conf. of Comm.'s on Uniform State Laws & ABA, 1966). Although the Model Act was a source of some of the "unlawful acts or practices" listed in the CNMI's statute, the definition of "consumer transaction" was not adopted. *See*, CNMI Law Revision Comment to 4 CMC § 5105. Section 5105 also contains the statement that it prohibits "deceptive acts or practices in the conduct of any trade or commerce," which is identical to the Model Act. The Georgia Legislature departed from the Model Act by adding "consumer" to the statement, so that it reads "…in the conduct of consumer transactions and consumer acts or practices in trade or commerce." Ga. Code Ann. § 106-1203(a). The court in *Merideth Chevrolet* relied upon this deviation as evidence of a legislative intent to strictly limit the scope of the statute to transactions wholly within the "consumer marketplace," with the result that fraudulent advertising in a medium "reasonably restricted" to merchants would not implicate the statute, "even though the product so advertised were eventually to reach the hands of consumers." *State v. Meridith Chevrolet, Inc.*, 244 S.E.2d at 18. Even though a commercial seller's turning back of a car's odometer may be a paradigmatic example of a "deceptive business practice," the Georgia Court of Appeals was led by its restrictive view of the "consumer marketplace" to conclude that the consumer plaintiff *actually harmed* by the deceptive practice had no cause of action under Georgia's consumer protection statute against either the wholesaler or the retailer who *benefited* from the practice. *Id*. No part of the CNMI's Consumer Protection Act evidences a similar legislative intent to limit its protection of individuals harmed by unfair business practices and the Court is disinclined to adopt any definitions of statutory terms that would have this result.

be liable under the Act because it contracted directly with NMHC who, pursuant to its statutory authority, supervised and directed Telesource's performance on what is essentially a government project. In this context, Telesource maintains that its activities are inseparable from the public purpose of the development and that it essentially shares a form of derivative immunity from an action based upon the Consumer Protection Act. *Boyle v. United Technologies Corp.*, 487 U.S. 500, 512-513, 108 S.Ct. 2510, 2518-19, 101 L.Ed.2d 442 (1988); *Yearsley v. W.A. Ross Const. Co.*, 309 U.S. 18, 19-20, 60 S.Ct. 413, 414, 84 L.Ed. 554 (1940); *U.S. ex rel. Ali v. Daniel, Mann, Johnson & Mendenhall*, 355 F.3d 1140, 1146-47 (9th Cir. 2004).

Strictly speaking, NMHC does not enjoy governmental immunity when it contracts to build and sell houses. 7 CMC § 2251(b). The legislature has foreclosed contention on this subject by expressly *exempting* government entities from the Consumer Protection Act. 4 CMC § 5106(a). Analytically, therefore, the provision that CNMI government entities may not be sued under the Act is best interpreted as a statutory exemption, rather than according to general principles of governmental immunity. The CPA's exemption at Section 5106(a) is broadly stated, but its clear purpose is to protect the *government* from consumer protection claims based upon the government's activities.[11] Viewing the exemption literally and in isolation from the remainder of the statute, Telesource suggests that because it states that "[n]othing in this article shall apply to… transactions carried out by the Commonwealth government," it follows that a consumer may not state a claim under the Consumer Protection Act for unfair business practices if such practices occurred in connection with the business' execution or performance of a "transaction" with the government. (Telesource's Mot. to Dismiss, p. 9).

Under this interpretation of the exemption at Section 5106(a), no matter how directly or how grievously the business' illegal practices harmed the consumer, the consumer would be foreclosed from any statutory remedy against the business because of the presence of a government transaction. It necessarily follows that, even with respect to commercial transactions in which it is no different than

[11] *Supra*, note 6.

any other consumer, a government agency would never be allowed to state a claim under the Consumer Protection Act.[12] The defendant's proffered interpretation does not represent a fair reading of Section 5106(a). The broad language of the exemption indicates the legislature's intention to provide complete and unequivocal protection to the government from consumer protection claims arising from the government's performance of its executive functions. The following subsection (b) uses *identical* language to exempt persons in the communications media who unknowingly publish false or deceptive advertisements (apparently, in defendant's view, protecting the false advertiser from liability because it is a party to the "transaction" with the publisher). 4 CMC § 5106(b). Nothing in the government exemption of Section 5106(a) indicates an intention to exempt *other* parties to whom the Act would otherwise apply, and the legislature could easily have included such a provision if that were its purpose. The statutory exemption at Section 5106(a), therefore, provides no basis for dismissing the homeowners' consumer protection claims against Telesource.

Nevertheless, the "government contractor" defense may still operate to shield a contractor from liability for conduct in conformance with directions from the government or its authorized bodies. *Boyle*, *supra*, 487 U.S. at 513; *Cf.*, *Richardson v. McKnight*, 521 U.S. 399, 412, 117 S.Ct. 2100, 2108, 138 L.Ed.2d 540 (1997). Such a defense, however, is not established by the mere fact that a defendant is involved in a government contract or public project, but rests upon proof of a number of factual issues relative to the defendant's alleged conduct. Some courts have found that contractors employed

[12] The Court previously dismissed NMHC's consumer protection claim against Telesource on the basis that the allegations contained in NMHC's complaint established no more than an ordinary commercial contract dispute between parties of relatively equal bargaining power; i.e., that the circumstances alleged did not show that NMHC was a consumer entitled to the protection of the CNMI's Consumer Protection Act (Order Granting Mots. To Intervene; Granting in Part and Den. in Part Def. Telesource's Mot. to Dismiss and Den. Def. Telebond's Mot. to Dismiss, December 20, 2006 (*amended*, April 9, 2007), p. 10). Although the Court believes that its ruling was clear on this issue, both Telesource and NMHC have subsequently advanced arguments that suggest a misunderstanding of the basis of the Court's ruling. To be clear: the Consumer Protection Act does not state, and the Court's Order of December 20, 2006, does not imply, that a public entity may *never* be entitled to protection under the Act. No consumer is excluded from the benefits of the Act based upon their *legal status*. *See*, 4 CMC § 5102(a)(5) ("In addition to the general public, merchants themselves, especially small business people, are consumers…."); § 5104(d) ("person" includes "natural persons, corporations, firms, partnerships, joint stock companies, and associations or other organizations…."). But likewise, it should be painfully obvious that pleading one's legal status or capacity is not sufficient to state a claim for relief under the statute or under any other law whatsoever.

by the government on public projects may be liable under consumer protection or unfair competition statutes. *In re World Trade Center Disaster Site Litigation*, 456 F.Supp.2d 520, 563 (S.D.N.Y. 2006); *Ramapo Brae Condo. Ass'n, Inc. v. Bergen County Housing Authority*, 746 A.2d 519, 579 (N.J.Super.A.D. 2000). Telesource has not shown that this defense is established by the pleadings.

D. The Statute of Limitation on Actions Under the Consumer Protection Act

The Castro Homeowners filed their complaint on November 28, 2006, and the Flores Homeowners filed their complaint on December 12, 2006. Telesource obtained a certificate of completion for the development on June 19, 2002. The complaints allege that the homeowners began moving in between spring and late fall of 2002, but are imprecise as to exactly when any material defects were discovered.

Telesource argues that the homeowners' claims under the Consumer Protection Act should be dismissed because, from the face of the complaints, they were filed beyond the four-year limitation period set forth in the Act. 4 C.M.C. § 5110. The homeowners contend that the accrual of their causes of action under the Act should be delayed until the point at which they were reasonably on notice of the existence of their statutory causes of action; i.e., either upon the discovery of latent defects in their homes reasonably attributable to the defendant's violations, or upon ascertaining the defendant's liability from the facts disclosed in the July 26, 2005 report from EFC Engineers & Architects Corp., or even from the facts alleged within NMHC's complaint of March 23, 2006. (Complaint of Pls. in Intervention [Castro], ¶ 267; Summons and Compl. and Demand for Jury Trial [Flores], ¶ 113). Alternatively, plaintiffs allege that Telesource's false promises to address their problems, including a supplemental warranty issued to NMHC on January 10, 2003, represented an on-going pattern of deceptive practices or constituted "fraudulent concealment" of their causes of action sufficient to toll the limitation period or to estopp Telesource from asserting the limitation as a defense. 7 CMC § 2509.

Telesource cites several decisions from two California federal courts and one state appellate court interpreting a similar provision and ruling that the limitation period may not be extended by

application of the "delayed discovery rule." *See, e.g., Stutz Motor Car of America, v. Reebock International, Ltd.*, 909 F.Supp. 1353, 1363 (C.D.Cal. 1995); *Snapp & Assoc. Ins. Services, Inc. v. Malcolm Bruce Burlingame Robertson*, 96 Cal.App.4th 884, 891 (2002). Telesource alternatively argues that the complaints admit that the homeowners were on notice that there were defects in the homes shortly after they moved in, so that the basis of their CPA claims were "reasonably discoverable" more than four years prior to this action (before 11/28/02 and 12/12/02).

The case law cited by Telesource does not represent the rule in California, nor does it appear to represent a majority approach to construing the limitations on state consumer protection actions. *Grisham v. Philip Morris U.S.A., Inc.*, 151 P.3d 1151, 1157, n.7 (Cal. 2007); *Miller v. Dickenson*, 677 S.W.2d 253 (Tex. 1984). If the defendant's unlawful business practices resulted in latent construction defects and delayed discovery by the consumer, it is difficult to find a rationale for not tolling the limitation period on the statutory claim. Telesource argues that because 4 CMC § 5108 eliminates the need for a plaintiff to show "harm to a consumer," the cause of action is complete and therefore accrues when the unlawful practice occurs. With no requirement of actual damages, it is argued that delayed discovery of damages may not be used as a basis for extending the limitation period. (Telesource's Reply in Supp. of Mot. to Dismiss, pp. 12-13).

This argument is unpersuasive. The four-year limitation period provided by Section 5110 begins to run when the cause of action "accrues." The statute gives no specific guidance with respect to when a private plaintiff's cause of action under Section 5112(a) accrues. Section 5107(a), however, provides that the Attorney General may bring a civil action when the Attorney General "*has reason to believe* that any person is using, *has used*, or is about to use any method, act or practice declared in 4 CMC § 5105 to be unlawful…." (emphasis added). Thus, the discovery of a violation of the Act is incorporated as a constituent element of a consumer protection action brought by the Attorney General. There is no apparent reason for the Court to supply a different rule for the private plaintiff. Interpreting the Act in accordance with Sections 5102 and 5123(a), the Court concludes that the limitation period

on the plaintiffs' statutory causes of action commenced at the point the plaintiffs discovered, or reasonably should have discovered, that they were victims of the defendant's prohibited practices.

Telesource's affirmative defense of the statute of limitations must be unequivocally established from the pleadings in order to be grounds for dismissal under Rule 12(b)(6). *In re Estate of Roberto*, *supra*, 2002 MP 23 ¶ 12, 6 N.M.I. at 512. The pleadings and the exhibits attached to the pleadings in this action do not suffice to show that the Homeowners' consumer protection claims are barred by 4 CMC § 5110.

E. The Homeowners' Status as Third-Party Beneficiaries of NMHC's Contracts

In ruling on the sufficiency of the complaint, a court must disregard the plaintiff's legal conclusions, but a motion to dismiss must be denied if the facts alleged support any cause of action. *Sablan v. Tenorio*, 4 N.M.I. 351, 355 (1996). The Homeowners' standing as third-party beneficiaries of the construction contracts depends entirely upon the intentions of the contracting parties or the reasonable reliance by the third party upon the contracting parties' objective manifestation of intent. RESTATEMENT (SECOND) OF CONTRACTS § 302, cmt. d, (1981). Both the intention of the contracting parties, and any reasonable reliance by the third party, are inherently factual questions, but may be determined as a matter of law if the terms of the agreement appear in an integrated writing and the dispositive facts are incorporated into the pleading. *Riley v. Pub. Sch. Sys.*, 4 N.M.I. 85, 88 (1994).

Telebond and Telesource challenge both complaints on the basis that the homeowner plaintiffs have failed to plead facts that would establish their right as third-party beneficiaries to enforce defendants' contracts with NMHC. The moving defendants have stipulated that their arguments are the same on this motion and that a resolution of the issue will be dispositive with respect to Telebond's entire motion. Defendants argue from the premise that the only third-party beneficiaries with enforceable contract rights are either "creditor beneficiaries" or "donee beneficiaries," the remaining category being "incidental beneficiaries" who have no enforceable rights under the contract. Since the Homeowners are not exactly "creditors" and did not exactly receive a "gift," defendants maintain that

they must be "incidental beneficiaries" with no rights under the contract. Defendants cite *Aplus Co., v. Niizeki Intl. Saipan Co., Ltd.*, 2006 MP 13 ¶¶ 13-14 in support of their argument.

The Court notes at the outset that the Restatement Second of Torts eliminated the terminology of "donee" and "creditor" beneficiaries that had appeared in the First Restatement for the *express reason* that the formalism engendered by these terms could be misleading. In its stead, the Second Restatement has established that the only meaningful distinction in this regard is between "intended" and "incidental" third-party beneficiaries. RESTATEMENT (SECOND) OF CONTRACTS, Intro. Note to Chapter 14, Contract Beneficiaries (1981) (*See, also,* Id., Reporter's Note to § 302).

The Commonwealth Supreme Court in *Aplus* followed the Restatement Second by avoiding the "donee"/"creditor" terminology and applied the modern test to determine whether a third party is an "intended beneficiary" of a contract; i.e., where "(1) The parties have not agreed otherwise, (2) recognition of a right to performance is appropriate to effectuate the intention of the parties; and (3) the circumstances indicate that either the performance of the promise will satisfy an obligation or discharge a duty owed by the promisee to the beneficiary or the promisee intends to give the beneficiary the benefit of the promised performance." *Aplus Co., v. Niizeki Intl. Saipan Co., Ltd.*, 2006 MP 13 ¶ 14. Although factor (3) appears to preserve the "donee"/"creditor" dichotomy, comments c and d and the reporter's note to section 302 explain that the second prong is not restricted to cases where there is an intent "to make a gift," but that third-party rights may arise when the promisee receives some consideration from the beneficiary, when the contracting parties intend that their contract will "confer a right" on the beneficiary, and even when the beneficiary reasonably relies upon the manifestation that such a right has been conferred.[13]

The Court in *Aplus* also approvingly cited an opinion in which the Pennsylvania Supreme Court upheld the determination that a group of homeowners were third-party beneficiaries of a contract

[13] *See*, Melvin Aron Eisenberg, *Third-Party Beneficiaries*, 92 COLUM. L. REV. 1358 (1992) (criticizing the retention of § 302(3) in the final version of the Second Restatement).

between a subdivision developer and an architect to provide and enforce restrictive covenants on the lots, even though the contract did not identify the prospective homeowners or expressly state an intention to benefit them directly, because the circumstances indicated that it was within the contemplation of the contracting parties that the homeowners would reap the benefit of the covenants and, after the sale of the lots, only the homeowners would suffer damages as a result of the failure to perform the contract. *Scarpitti v. Weborg*, 609 A.2d 147 (Pa. 1992) (*cited at* 2006 MP 13 ¶ 16).[14]

The responding plaintiffs in this action have alleged that they are members of a defined class of homeowners for whose benefit NMHC undertook the development of the Tottotville project, which included NMHC's contract with Telesource and Telebond's guarantee of Telesource's performance. The facts alleged support the inference that the contracting parties intended to confer a benefit upon the homeowners and that the homeowners' right to enforce their agreements would serve to effectuate the purpose of their contracts. It is the intention of the contract promisee at the time of the agreement that is most determinative of whether or not third-party rights are created by the contract. RESTATEMENT (SECOND) OF CONTRACTS § 304, cmts. d, e (1981). In this regard, it is noted that NMHC has averred in its complaint that its efforts in developing the Tottotville project were "for the benefit of… those homeowners who intended to and would eventually reside therein." (Complaint and Demand for Jury

[14] Other notable case law recognizing third-party rights to enforce construction contracts include: *Shillman v. Hobstetter*, 241 A.2d 570, 575 (Md.App. 1968) (applying Restatement (First) of Contracts—homeowners were donee beneficiaries of provision in contract between minority shareholders of developer and FHA lender that provided for return of homeowners' deposits if developer failed to complete the project); *Tudor Dev. Group, Inc. v. U.S. Fidelity & Guaranty Co.* 692 F.Supp. 461, 463 (M.D. Penn. 1988) (surety liable for any implied warranties applicable to its principal on construction contract); *Tarin's Inc. v. Tinley*, 3 P.3d 680, 686 (N.M.App. 1999) (although general rule is that a building owner is not a third-party beneficiary of the builder's contract with a sub-contractor, it is error to dismiss on that basis if facts could be proved to indicate a contrary intention). *Green Mountain Power Corp., v. General Electric Corp.*, 496 F.Supp. 169, 173 (D.C.Vt. 1980) (contention that minority shareholder and customer of power company was an intended third-party beneficiary of contract between power company and repair contractor was "doubtful," but question of "intent to benefit" precluded summary judgment); and *Jabco, Inc., v. Bob Smith Construction*, 556 F.Supp. 27, 28 (E.D.Tenn. 1981) (contractor's claim to be a third-party beneficiary of municipality's promise pursuant to a construction contract to obtain an appropriate type of insurance depended upon "the factual issue of intent" and could not be determined as a matter of law).

Trial [NMHC], ¶ 8). The Court finds that the factual allegations of each complaint are sufficient to state causes of action against the moving defendants for breach of warranty and breach of contract based upon the homeowners' status as third-party beneficiaries of the construction contract and performance bond and that these claims may not be dismissed pursuant to Com. R. Civ. P. 12(b)(6).

F. Adequacy of the Homeowners' Pleading With Respect to Fraud.

Fraud requires a representation in which the maker (1) knows or believes that the matter is not as he represents it to be, (2) does not have the confidence in the accuracy of his representation that he states or implies, or (3) knows that he does not have the basis for his representation that he states or implies. *Benavente v. Marianas Pub. Land Corp.*, 2000 MP 13, ¶ 40, 6 N.M.I. 136, 145. To state an action for fraud, a plaintiff must allege that the fraudulent representation was material and that the plaintiff's reasonable reliance upon the truth of the representation actually and proximately caused the plaintiff to suffer damages. *Del Rosario v. Camacho*, 2001 MP 3, ¶ 79, 6 N.M.I. 213, 228-229; RESTATEMENT (SECOND) OF TORTS § 525 (1977). Furthermore, in a complaint alleging fraud, "the circumstances constituting fraud… shall be stated with particularity. Malice, intent, knowledge, and other conditions of the mind of a person may be averred generally." Com. R. Civ. Proc. 9(b).

The Castro Homeowners claim fraud against Telesource in "Count Seventeen" and in "Count Twenty" of their complaint. The Flores Homeowners claim fraud against Telesource in "Count VIII" of their complaint. In "Count Seventeen," the Castro Homeowners allege that Telesource "caused to be issued" Certificates of Occupancy for their houses on June 19, 2002, certifying that the homes were "Architect reviewed" and fit for occupancy, built in accordance with specifications, safety code, etc., when Telesource in fact knew that the homes were unfit and not in compliance, and when the project would not be accepted as complete for another five months, and that the Homeowners relied upon the representations made in the Certificates of Occupancy by forbearing from "acting to safeguard their interests." In "Count Twenty," the Castro Homeowners allege that Telesource's supplemental representations to NMHC that it would remedy the defects was a false promise made without the

present intention to perform the promise, and offered only to lull the plaintiffs into foregoing any action to enforce their rights against Telesource. The Homeowners allege additional damages from structural deterioration due to the delay. In "Count VIII" of the Flores Homeowners' complaint, the allegations are materially the same as those made in "Count Seventeen" of the Castro Homeowners' complaint, but without reference to the Certificates of Occupancy and with the allegation that plaintiffs relied upon Telesource's misrepresentations of quality by purchasing their homes.

Telesource argues that all of these claims should be dismissed because they are not stated with the degree of particularity required by Com. R. Civ. Proc. 9(b) or do not make out a legal claim of fraud. With regard to "Count Twenty" of the Castro Homeowners' complaint, Telesource argues that "A claim for fraud cannot arise out of a promise of future action, even if the promise is made and broken." (Telesource's Mot. to Dismiss, p. 11). Telesource also argues that the remaining allegations of fraud, based upon Telesource's alleged misrepresentations as to quality, lack particularity because they do not specify the false statements, are imprecise as to the time the representations were made, and do not state clearly that Telesource communicated false statements directly to the Homeowners. (Telesource's Mot. to Dismiss, pp. 12-13).

Although a "promise" or "prediction," *by itself*, is not a false statement of fact, either may be used to perpetrate a deception that is actionable as fraud. *Cf., Benavente, supra*, 2000 MP 13, ¶ 43 ("mere broken promises" are not actionable as fraud). A promise made without the present intention to perform the promise is a misrepresentation *of fact* that may serve as a basis for fraud. RESTATEMENT (SECOND) OF TORTS § 530 (1977). The Restatement also makes clear that a "representation" may consist of actions as well as statements (REST. § 525) and that there is no requirement of a direct communication to the plaintiff, only that the plaintiff be one of a class of recipients whom the defendant could reasonably expect to rely upon the representation (REST. §§ 531, 533). Plaintiffs allege that Telesource promised NMHC that it would repair construction defects, that these representations were "for the benefit of Homeowners" and "knowingly false when made," that

Telesource "knew or should have known" that the homeowners would rely upon its misrepresentation of its intention to effect repairs, and that the homeowners did in fact rely upon these representations to their detriment. (Complaint of Pls. in Intervention [Castro], ¶¶ 249-255). These allegations describe a fraudulent misrepresentation that is actionable by the plaintiffs under the cited sections of the Restatement. The defendant's argument that a claim for fraud cannot arise from a false promise of future action does not accord with the position of the Restatement. REST., § 530. Defendant's motion to dismiss plaintiffs' "Count Twenty" (Fraud) on this point of law is therefore denied.

To adequately describe the circumstances giving rise to a claim of fraud, it is generally held that a plaintiff must state the "time, place, and nature of the misleading statements, misrepresentations, or specific acts of fraud." *Kaplan v. Rose,* 49 F.3d 1363, 1370 (9th Cir. 1994). The plaintiff's allegations "must be specific enough to give defendants notice of the particular misconduct… so that they can defend against the charge and not just deny that they have done anything wrong." *Vess v. Ciba-Geigy Corp., U.S.A.*, 317 F.3d 1097, 1106 (9th Cir. 2003). The accepted rationale for requiring a heightened pleading standard involves both notice and deterrence: fraud can easily be alleged regarding such a broad range of activity that a defendant may require more details in order to respond, and unfounded claims of fraud may be used as an improper litigation device and may harm the defendant's reputation and goodwill. *In re Initial Public Offering Securities Litigation,* 241 F.Supp.2d 281, 325-328 (S.D.N.Y. 2003) (*citing,* 5A CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE §1296, §1297 (3d. 1995)).

On a motion to dismiss, the requirements of Rule 9(b) must be reconciled with the notice pleading standard of Rule 8. *See,* Com. R. Civ. P. 8(f); *Zatkin v. Primuth,* 551 F.Supp. 39, 42 (S.D.Cal. 1982) ("The Ninth Circuit has consistently taken the approach of reading the two rules in conjunction."); *See also, Daisley v. Riss Bank, N.A.*, 372 F.Supp.2d 61, 78-79 (D.D.C. 2005); WRIGHT & MILLER, *supra,* § 1241. The need to state the "circumstances" with "particularity" does not revive a code-pleading standard or require the pleading of evidentiary facts, but rather the pleading "is

sufficient under Rule 9(b) if it identifies the circumstances surrounding the fraud so that the defendant can prepare an adequate answer from the allegations." *Wool v. Tandem Computers, Inc.*, 818 F.2d 1433, 1439-40 (9th Cir. 1987) (*quoting*, *Semegen v. Weidner*, 780 F.2d 727, 735 (9th Cir. 1985)). The degree of particularity that is required depends upon the circumstances of each case, including the relationship of the parties and any knowledge that an opposing party may possess of matters under its control. *Id.*, at 1440.

Applying these rules to the challenged pleadings, the Court agrees with Telesource that "Count Seventeen" of the Castro Homeowners' complaint fails to meet the pleading standard of Com. R. Civ. P. 9(b). Plaintiffs appear to be alleging that the Certificates of Occupancy issued by a building safety official are evidence of Telesource's assurances of contract conformance and quality to NMHC, that the fact that these certificates pre-dated the Certificate of Completion for the project prove the falsity of these representations, and that the homeowners relied to their detriment upon the *certificates* that incorporated and re-communicated Telesource's misrepresentations, all as Telesource intended. (Complaint of Pls. in Intervention [Castro], ¶¶ 210-212). Even such a construction, however, requires speculation based upon the literal statements in the pleading and therefore departs from the standard of Rule 9(b). The two kinds of certificates described in the complaint appear to have independent purposes and their comparison does not obviously reveal a falsehood. Plaintiffs do not actually describe any misrepresentation by the defendant, only that it "caused and permitted" the certificates to issue, and that the Certificates of Occupancy "were false and fraudulent *in that* they predated by more than five (5) months the Certificate of Completion." (Id. ¶ 210, emphasis added). The only reliance upon the "false and fraudulent certificates" alleged by the plaintiffs is that they "forbore from acting to safeguard their interest." (Id. ¶ 212) These allegations do not describe circumstances in which the elements of fraud are apparent. The defendant's motion to dismiss the Castro Homeowners' "Count Seventeen" (Fraud) is therefore granted.

"Count VIII" of the Flores Homeowners' complaint is also less than ideal in its depiction of the circumstances underlying their claim of fraud against Telesource. Plaintiffs allege that in "the Spring of 2002," the defendant knowingly misrepresented to NMHC that the project was complete and in conformance with the construction contract and building codes. (Summons and Compl. and Demand for Jury Trial [Flores], ¶¶144-145). The defendant is alleged to have made this false representation with the knowledge and intent that the homeowners would be deceived by the misrepresentation so that the homeowners would purchase the homes, that this occurred, and that the homeowners reasonably relied upon this misrepresentation to their detriment by purchasing defective homes that caused them to suffer damages. (Id., ¶¶ 146-147). Telesource objects that the pleading fails to specify the precise timing and circumstances of its alleged misrepresentation to NMHC, and also fails to expressly state that NMHC re-communicated this misrepresentation to the plaintiffs.

As explained above, the pleading rules do not require the plaintiffs to prove a prima facie case against the defendant, and the particularity required by Rule 9(b) in order to give sufficient notice to a defendant is dependant upon the context established by the entire pleadings. *Federal Savings & Loan Ins. Corp. v. Shearson-American Exp., Inc.*, 658 F.Supp. 1331, 1336-37 (D.Puerto Rico 1987); *Daisley v. Riggs Bank*, *supra*, 372 F.Supp.2d at 79 (*citing*, *Towers Fin. Corp. v. Solomon*, 126 F.R.D. 531, 535 (N.D.Ill. 1989)). A sufficient statement of fraud may be made in a single sentence. *In re Initial Public Offering Securities Litigation*, 241 F.Supp.2d at 327 (noting that Fed. R. Civ. P. App. Form 13 alleges fraud). The complaint alleges a number of instances of the defendant's knowing non-conformance with contract requirements and building standards, and the defendant cannot legitimately claim prejudice from not knowing precisely when, or whether, its officers certified that its work was sufficient and complete. *Wool v. Tandem Computers, Inc.*, *supra*, 818 F.2d at 1439.

Although Paragraph 146 of the Flores Homeowners' complaint alleges that Telesource misrepresented facts to NMHC with the intent to deceive the homeowners and to induce the homeowners to rely upon its misrepresentation, and Paragraph 147 alleges that the homeowners did

rely upon Telesource's misrepresentation, Telesource also moves to dismiss on the basis that the plaintiffs have neglected to state the "necessary element" that NMHC relayed Telesource's misrepresentation to the homeowners or to particularly describe the contents of this secondary communication. (Telesource's Mot. to Dismiss, p. 13). On this point, the Court notes that while the plaintiff's "reliance" is a necessary element of an action for fraud, a verbatim "re-communication" or "republication" is not. RESTATEMENT (SECOND) OF TORTS § 531 (1977). Under the Restatement's principle of "indirect misrepresentation," liability attaches to the defendant for its original misrepresentation to a third party if the defendant reasonably expects to thereby induce the plaintiff and the third party to enter into a transaction and the transaction actually and proximately causes loss to the plaintiff. REST. § 533. In *Committee on Children's Television, Inc., v. General Foods Corp.*, 673 P.2d 660 (Cal. 1983), the California Supreme Court applied Section 533 of the Restatement (Second) of Torts to a common law fraud claim to hold that children targeted by fraudulent advertising were not required to repeat the contents of the false ads to their parents who purchased the products, stating "Repetition, however, should not be a prerequisite to liability; it should be sufficient that defendant makes a misrepresentation to one group intending to influence the behavior of the ultimate purchaser, and that he succeeds in this plan."). *Id.*, at 674 (Broussard, J.), *citing*, *Varwig v. Anderson-Behel Porsche/Audi, Inc.*, 74 Cal.App.3d 578, 581 (1977) ("[defendant's] misrepresentation to [third-party] was *in law* an indirect misrepresentation to plaintiff") (emphasis added).

Given the totality of the pleadings in this action, and in light of the Restatement principles discussed above, the Court considers it a useless exercise in formalism to require the plaintiffs to re-plead in order to include a sentence more precisely specifying a causal link that is otherwise implicit in the circumstances properly alleged. Plaintiffs have described the circumstances underlying their claim of fraud with sufficient particularity to give fair and adequate notice to the defendant. *Vess v. Ciba-Geigy Corp., U.S.A., supra*, 317 F.3d at 1106. Accordingly, defendant Telesource's motion to dismiss plaintiffs' "Count VIII" (Fraud) is denied.

III. CONCLUSION

For the reasons detailed above, defendant Telesource's motion to dismiss "Count Sixteen" (Strict Liability) of the Castro Homeowners' complaint and "Count VII" (Negligence) of the Flores Homeowners' complaint is GRANTED.

Telesource's motion to dismiss "Count Seventeen" (Fraud) of the Castro Homeowners' complaint is GRANTED, with leave for the Plaintiffs to amend the complaint.

Telesource's motion to dismiss is DENIED with respect to the remaining causes of action stated in the complaints of the plaintiff homeowners.

Telebond's motion to dismiss "Count Twenty-three" ("Claim for Insurance Bond and Policy") of the Castro Homeowners' complaint and "Count VI" ("Insurance Bonds and Policies") of the Flores Homeowners' complaint is DENIED.

SO ORDERED this 5th day of June, 2007.

/S.
RAMONA V. MANGLOÑA, Associate Judge