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S.C. SUPREME COURT

THE STATE OF SOUTH CAROLINA

In The Supreme Court

APPEAL FROM FAIRFIELD COUNTY

Court of Common Pleas

Carol A. Tolen, Special Referee

Trial Court Case No. 2012-CP-20-00132

Appellate Case No. 2021 -- 000149

ArrowPointe Federal Credit Union . . . . . Respondent,

v.

Jimmy Eugene Bailey; Laura Jean Bailey; and U.S. Bank National Association not in its individual capacity but solely in its capacity as Indenture Trustee for WVUE 2015-1 . . . . . .Defendants,

Of which U.S. Bank National Association not in it individual capacity but solely in its capacity as Indenture Trustee for WVUE 2015-1 is the Appellant.

RESPONDENT'S RETURN TO APPELLANT'S PETITION FOR REHEARING

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STANDARD OF REVIEW

When entertaining a Petition for Rehearing, the Court's standard of review is to determine whether a point has been overlooked or misunderstood by the Court. Rule 221(a), SCAR. Not all points are created equal. Some points made by the Court in its Opinion are crucial to the holding of the case, while other points are dicta. "The purpose of a petition for rehearing is not to present points which lawyers for the losing parties have overlooked or misapprehended, nor is it the purpose of the petition for rehearing to have the case tried in the appellate court a second time." Herron v. Century BMW, 395 S.C. 461, 466, 719 S.E.2d 640, 643 (2011); Kennedy v. S.C. Retirement Sys., 349 S.C. 531, 532, 564 S.E.2d 322, 322 (2001) (quoting Jean H. Toal, Appellate Practice in South Carolina 309 (1999)).

A. The Opinion does not vacate existing equitable subrogation case law.

This Court's Order entered in this case on January 11, 2023 ("Opinion" or "Decision") does not need reconsideration or a rehearing. The Court correctly found that, absent compelling reason, South Carolina's legislature is the proper entity to address additional exceptions to the recording statute. This Court has previously made it clear that replacement mortgage theory is a separate and distinct theory than the doctrine of equitable subrogation. Matrix Financial Serv. Corp. v. Frazer, 394 S.C. 134, 714 S.E.2d 532 (2011); Dedes v. Strickland, 307 S.C. 155, 414 S.E.2d 134 (1992). Therefore, the holding found in this Decision could not possibly be a departure from the equitable subrogation doctrine. The decision gives much needed guidance to practitioners regarding the priority of a refinancing mortgage lender.

The Opinion in no way vacates existing equitable subrogation case law. Equitable subrogation is still in effect. Nowhere in Appellant's Petition for Rehearing is there a citation to

the part of the Opinion that struck down equitable subrogation. In fact, Footnote 1 of the Opinion lists all five elements of the well-settled doctrine of equitable subrogation.

> This doctrine states a party may be equitably subrogated to the rights of an earlier creditor if the party demonstrates: (1) he has paid the debt; (2) he was not a volunteer but had a direct interest in the discharge of the debt or lien; (3) he was secondarily liable for the debt or for the discharge of the lien; (4) no injustice would be done by the allowance of equitable subrogation; and (5) he did not have actual notice of the prior lien. Indep. Nat'l Bank v. Buncombe Prof'l Park, LLC, 411 S.C. 605, 608, 769 S.E.2d 663, 665 (2015). Id.

The Opinion notes that both equitable subrogation and replacement mortgage are exceptions to the race-notice statute; however, the Court clearly declines to adopt replacement mortgage for multiple reasons, any of which is sufficient to reject the adoption of the theory. The reasons given are fairly clear and easy to understand: it really is important to properly search title, adopting replacement mortgage would lead to avoidable litigation about what constitutes material prejudice dealt to intervening lienholders, and subrogation line of cases developed to address situations where the creditors were being replaced. The removal of any one of the reasons could not and should not change the ultimate holding in the case. The Court's point is well-made that the equitable subrogation line of cases was adopted when one creditor pays off an existing obligation and becomes the new creditor. This is the history of the doctrine. Enterprise Bank v. Federal Land Bank, 139 S.C. 397, 138 S.E. 146 (1927), United Carolina Bank v. Caropop, 316 S.C. 1, 446 S.E.2d 415 (1994), Meaders Brothers v. Skelton, 234 S.C. 134, 107 S.E.2d 1 (1959), Sutton v. Sutton, 26 S.C. 33 (1886), and Norton v. Sitton, 11 S.C. 593 (1867).

Relative to other states, South Carolina is known to protect the public by requiring stringent standards for real estate practitioners, and the Opinion is an extension of this overarching concern. That is the main idea. State v. Buyers Serv. Co., 292 S.C. 426, 357 S.E.2d 15 (1987); Wachovia Bank v. Coffey, 389 S.C. 68, 698 S.E.2d 244 (Ct. App. 2010); Doe v. McMaster, 355 S.C. 306,

585 S.E.2d 773 (2003). Any statement in the Opinion about the release or lack of release of an existing mortgage when equitable subrogation is used is not consequential to the result reached. It is dicta, which even if deleted, would not change the overall holding.

In the Opinion, this Court noted, "[w]hile the replacement mortgage doctrine provides the intervening lienholder with some relief 'to the extent that any change in the terms of the mortgage or the obligation it secures is materially prejudicial to' the intervening lienholder, we conclude the replacement mortgage doctrine invites needless litigation that could be avoided by a simple examination of the title to the real property." [Op. at 175.] The Court will use its power judiciously and will recognize a corollary to the race-notice statute such as equitable subrogation, only when there is a compelling equitable reason to do so, such compelling reason being absent in this case.

When a refinance is conducted, the original mortgage is paid off, the original mortgage is satisfied of record, and a new mortgage is recorded. Sometimes this sequence of events occurs when equitable subrogation is applied, but sometimes these events do not occur in an equitable subrogation case. The holding of Independence National Bank vs. Buncombe is that "an agent's actual knowledge imputes only constructive knowledge to his principal. . . ." Indep. Nat'l Bank v. Buncombe Prof'l Park, LLC, 411 S.C. 605, 608, 769 S.E.2d 663, 665 (2015). Independence National Bank is not vacated by this Court's Opinion. The principals of agency espoused in the case remain undisturbed by this Opinion. The elements of equitable subrogation have not been changed.

The facts of Independence National Bank case are distinguishable from the facts in the instant matter. Independence National Bank gave a mortgage to Buncombe Professional Park, LLC, whose sole member was David DeCarlis. DeCarlis held the intervening mortgage given to the LLC. The closing attorney erroneously failed to release the intervening mortgage with the

closing of the refinanced loan, so the borrower in the refinanced mortgage was the lender in the intervening mortgage. The fact that the holder of the intervening mortgage is one of the borrowers in the refinance mortgage made all the difference. And of course, the biggest distinction is that Independence National Bank proceeded under equitable subrogation, rather than replacement mortgage. It was not paying off its own mortgage, so equitable subrogation was available to it. Matrix and Dedes make it clear that equitable subrogation is not available to a lender when it refinances its own debt. Matrix Financial Serv. Corp. v. Frazer, 394 S.C. 134, 714 S.E.2d 532 (2011); Dedes v. Strickland, 307 S.C. 155, 414 S.E.2d 134 (1992).

Appellant seeks to cobble together parts of equitable subrogation and parts of replacement mortgage to end up in a scenario where it is not responsible for its own missing or inadequate title search. Appellant cannot go forward under an equitable subrogation theory, because it cannot meet the fourth standard "(4) no injustice would be done by the allowance of equitable subrogation." Indep. Nat'l Bank v. Buncombe Prof'l Park, LLC, 411 S.C. 605, 608, 769 S.E.2d 663, 665 (2015). Also, the Appellant cannot proceed under equitable subrogation because of the Matrix and Dedes cases. A lender cannot be subrogated to itself. Subrogation is stepping into the shoes of another. Dedes v. Strickland, 307 S.C. 155, 414 S.E.2d 134 (1992).

Equitable subrogation is set up to protect a third party who pays off the original debt and as a result should have the same lien priority as the original lender. The terms are the same, as demonstrated by the "no injustice" element of the doctrine. Replacement mortgage, on the other hand, involves the same parties as the original debt, so there is no "substitution" of interests. Equity is utilized with equitable subrogation to place the new lender in the shoes of the original lender. Conversely, equity is not required when an original lender refinances its own debt.

The Opinion correctly notes that whether to provide the original lender any protections from the race notice statute is best left to the South Carolina General Assembly.

This Court has never been compelled to adopt the same laws as other jurisdictions, such decisions being up to the discretion of this Court. The record lacks case law to demonstrate that the Court is the first to openly reject the theory of replacement mortgage, though even if true is not sufficient cause to adopt the theory. The Court should not be bullied into adopting legal theories based on non-precedential opinions. How other states handle this issue is interesting but not binding, and since other states have different statutes and development of their own case law, it is not instructive either.

The question the Appellant poses is that if equitable subrogation is available in South Carolina, why is replacement mortgage not available? The Court's answer is that there is no need for it. The Court's answer does not disturb or abrogate the elements of equitable subrogation.

The Court's main concern in this case is not whether or not the original mortgage is satisfied when equitable subrogation is used. The observation is not necessary to resolve the case. The chief concern is the complete lack of necessity to adopt the replacement mortgage theory when lenders can bypass the favor or indulgence by doing their job as espoused time and again the Buyers Services line of cases.

B. The Court's statement regarding the "no injustice" element of equitable subrogation is an accurate observation.

Appellant complains about the Court's interpretation of element four of equitable subrogation, which is "(4) no injustice would be done by the allowance of equitable subrogation." Putting aside the fact that this element is quoted verbatim in the Opinion with approval, Appellant

specifically argues that it is improper to categorize this element as requiring that "the junior mortgagee has not lost anything at all." App. Petition Rehearing, Page 6. As support for Appellant's contention that the Court's has misunderstood a point, Appellant offers Meadors v. Skelton, 107 S.E.2d 1, 234 S.C. 134 (1959). This opinion does not expound on element four of equitable subrogation at all.

The only other case enjoying favorable treatment that cites to Meadors is Dodge City of Spartanburg, Inc. vs. Jones, 317, S.C. 491, 454 S.E.2d 918 (Ct. App. 1994). In the Dodge City case, there was a first and a second mortgage, both totaling $28,224.08 when given. The mortgage lender that was allowed to exert equitable subrogation gave a mortgage in the amount of $19,274.15. When the third mortgage was made, the balance on the first and second mortgages was $14,095.51. The court ultimately gave the third mortgage lender priority under equitable subrogation to the tune of $11,437.63. True, ratios were used to calculate the portion of the third mortgage that injured the intervening lienholder (in this case, a judgment lien). However, the end result is that the junior mortgagee had not lost anything at all, which is the unproblematic language used by the Court in the Opinion.

C. Recognizing replacement mortgage theory would cause more litigation than it would avoid.

Appellant contends that recognizing the replacement mortgage theory would cause less harm than adopting the theory. Appellant's Petition for Rehearing, Page 7. This is an example of the Appellant's misapprehension, not the Court's misapprehension. Appellant's discussion about forfeitures is an example of an attempt to re-argue the case, which is not the purpose of Rule 221 SCAR. Herron v. Century BMW, 395 S.C. 461, 466, 719 S.E.2d 640, 643 (2011).

The record shows only that the Baileys were charged for a title search. [App. 512, line 1103.] The record does not show that a title search was performed, and there is certainly nothing in the record to indicate what the Appellant deems to constitute a title search, nor does it indicate the quality of the title search. The fact remains that ArrowPoint's recorded mortgage was missed, either by failure to look or by carelessness in the looking.

Appellant also complains that it was just acting on the advice of counsel in its actions to close the refinanced loan. Again, this is another example of Appellant's misunderstanding, not the Court's misunderstanding.

D. The Decision creates certainty for practitioners moving forward.

Appellant claims that the Opinion leaves practitioners and lenders without clear guidance. This is patently illogical. The Opinion clearly rejects replacement mortgage theory in South Carolina, which gives practitioners the information we need to properly close refinance mortgage loans. It also provides practitioners the information we need to settle future disputes between competing mortgage creditors. The holding is reached because the legislature would be the proper entity to address it, because lenders ought to competently search title when refinancing their own loans, and because adoption of replacement mortgage theory would result in less certainty for practitioners and more litigation over what constitutes material prejudice to intervening lienholders. Any other reading of the Opinion is a pedantic interpretation.

CONCLUSION

The holding in this Opinion did not destroy well-established elements of equitable subrogation. The Court's comments about prejudice done to an intervening lienholder when considering equitable subrogation do not undermine the fourth element of equitable subrogation.

The Court accurately determined replacement mortgage theory would result in less certainty and more litigation among competing creditors. A rehearing is not warranted, as Appellant has not met its burden of showing that the Court missed a crucial point or misunderstood a crucial point. Appellant has cherry-picked a few phrases out of context in an attempt to obtain a rehearing, but ultimately these phrases were misapprehended by Appellant.

Respectfully submitted,

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