THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM HORRY COUNTY
Court of Common Pleas

John M. Milling, Special Referee

Case No: 2013-001291

Harleysville Group Insurance, a Pennsylvania Corporation, Appellant/Respondent

v.

Heritage Communities, Inc., A South Carolina Corporation; Heritage Riverwalk, A South Carolina Corporation; Buildstar Corporation, A South Carolina Corporation, Riverwalk at Arrowhead Country Club Horizontal Property Regime, Riverwalk at Arrowhead Property Owners Association, Inc., A South Carolina Corporation, National Surety Corp., and Tony L. Pope and Lynn Pope Individually and Representing as a Class All Unit Owners at Riverwalk at Arrowhead Country Club Horizontal Property Regime, Defendants,

Of whom Heritage Communities, Inc., a South Carolina Corporation; Heritage Riverwalk, a South Carolina Corporation; Buildstar Corporation, a South Carolina Corporation; National Surety Corp., And Tony L. Pope and Lynn Pope, individually and representing as a class all unit owners at Riverwalk at Arrowhead Country Club Horizontal Property Regime are Respondents,

And Riverwalk at Arrowhead Country Club Horizontal Property Regime; Riverwalk at Arrowhead Country Club Property Owners Association, Inc. are Respondents/Appellants.

INITIAL BRIEF OF RESPONDENTS/APPELLANTS

John P. Henry
Philip C. Thompson
Thompson & Henry, P.A.
1300 Second Avenue, 3rd Floor
Post Office Box 1740 (zip: 29528)
Conway, South Carolina 29526
(843)248-5741

Attorneys for
Respondents/Appellants Riverwalk at Arrowhead Country Club Horizontal Property Regime and Riverwalk at Arrowhead Country Club Property Owners Association, Inc.

Table of Contents

Table of Authorities

Cases

Statutes

Other Authorities

Rules

Statement of Issues

I. Did the Trial Judge err in applying TOR to the general unallocated verdict, especially in light of the fact that in order to do so the Trial Judge had to enter into speculation as to the type of damages and the amount of progressive damages allocated by the jury?

II. Did the Trial Judge err when he determined that it was improper to allocate the general verdict into covered damages and uncovered damages and thus the entire verdict was covered, and then applied TOR to the general verdict?

III. Did the Trial Judge err when he applied TOR to the general verdict even after he had ruled that Harleysville failed to properly reserve its right to contest coverage?

IV. Did the Trial Judge err in finding the ending date for TOR purposes to be April 30, 2004, since the jury found breach of fiduciary duty occurred on May 29, 2002, and it is not possible to determine if the jury awarded any continuing deterioration (progressive) damages after that date? And did the Trial Judge err in setting the ending date at April 30, 2004, when a damage estimate submitted to the jury was based on a 2003 scope of work?

Statement of the Case

This cross appeal is from a declaratory judgment action filed October 14, 2009, by Harleysville Group Insurance ("Harleysville") pursuant to South Carolina Code 1976 § 15-53-10, et seq., seeking a declaration relative to certain coverage issues involving two general unallocated verdicts. These verdicts were awarded to the Riverwalk at Arrowhead Property Owners Association, Inc. ("POA") and a consolidated putative class action ("Pope Class Action"). The consolidated Pope Class verdict is not the subject of this cross appeal.[1] The verdict awarded to the POA was a general unallocated verdict in the amount of Four Million Two Hundred Fifty Thousand ($4,250,000.00) Dollars actual damages and punitive damages of Two Hundred Fifty Thousand ($250,000.00) Dollars. (Verdict Form Tr. Ex. 25) The punitive damages are not the subject of this cross appeal.[2]

In its complaint, Harleysville asked the Court to find that certain exclusions excluded coverage for the POA verdict. (Comp. filed October 14, 2009, p. 5-7) In the alternative, Harleysville asked the Court if it found any of the POA's claims were covered under its policies, that the Court "perform an accounting" to determine which part of the general verdict constituted covered damages. (Comp. filed October 14, 2009, p. 8-11) Harleysville then asked the Court to apply "Time-on-the-Risk" ("TOR") to that part of the general verdict found to be covered. (Comp. filed October 14, 2009, p. 8-11) Harleysville also contended that punitive damages were not covered. (Comp. filed October 14, 2009, pp. 11-12)

[1] The Trial Judge did not apply "Time-on-the-Risk" to the Pope Class verdict.
[2] The Trial Judge did not apply "Time-on-the-Risk" to the punitive damages.

On November 6, 2009, the POA timely filed its Amended Answer and Counterclaim denying the allegations of the Complaint; denying that TOR could be applied to the general verdict; alleging that under the *Newman* case (discussed infra.) that the entire general verdict was covered by the Harleysville policies because of Harleysville's failure to seek an allocated verdict and asked the Court to find the full amount of the verdict covered under the Harleysville policies. (Amended Answer and Counterclaim filed November 6, 2009, p. 5)

The Riverwalk POA case, Pope Class Action and a companion case, Magnolia North[3], were consolidated and were referred to the Honorable John M. Milling as special referee directing him to dispose of the cases with finality. (Order dated October 21, 2010) A trial of the case was held on August 3, 2010. Because of the pending *Crossman* decision (discussed infra) the parties agreed to hold the case open until a final decision on *Crossman* was reached by The Supreme Court. The *Crossman* decision was finalized on August 22, 2011. Judge Milling reopened the hearing on December 9, 2011 and the testimony was concluded. After taking testimony, Judge Milling issued his order on February 28, 2013 finding, inter alia, covered claims were submitted to the jury; the exclusions did not apply to exclude coverage of those claims; it would not be appropriate to attempt an allocation of the general verdict because Harleysville did not intervene or otherwise attempt to have the Trial Court allocate the verdict; Harleysville did not effectively reserve its rights to contest coverage; punitive damages were covered; and the general verdict was covered but TOR was to be applied to the general verdict reducing the availability of coverage for actual damages under the Harleysville policies from

[3] The Magnolia North Property Owners case involves the same issues addressed in this cross appeal but is the subject of a separate appeal.

$3,228,678.36[4] to 1,794,499.43. (Order filed November 28, 2013) The POA timely filed a Motion to Alter or Amend his Order on March 20, 2013, contesting application of TOR on numerous grounds. (Motion filed March 20, 2013) Harleysville also filed a Motion to Alter, Amend or Vacate the Order on numerous grounds. (Motion filed March 21, 2013) Both Motions were denied. (Order of Judge Milling dated April 24, 2013) Harleysville filed a Notice of Appeal on May 20, 2013, and the POA filed a cross appeal on May 23, 2013.

[4] The Trial Judge in the underlying action granted a set-off for settlement payments made by subcontractors reducing actual damages from $4,250,000.00 to $3,228,678.36.

Statement of Facts

The judgment which is the subject of this cross appeal arose out of a construction defect action filed by the POA against Heritage Communities, Inc., the overall developer, Heritage Riverwalk Inc., the site specific developer and Buildstar Corporation, the general contractor ("Harleysville Insureds"). The Harleysville Insureds developed, constructed and sold the Riverwalk Condominiums which consisted of 19 buildings and 228 condominiums. All of the work was performed by subcontractors. (Tr. pp. 190-191) Each of the Harleysville Insureds purchased numerous commercial and excess standard ISO (Insurance Services Organization) general liability policies ("CGL") from Harleysville. (Tr. Ex. 12) Harleysville Insureds only purchased CGL policies from Harleysville. Pursuant to the terms of its policies, Harleysville hired attorneys to represent the Harleysville Insureds. These attorneys were hired on a regular basis by Harleysville. (Tr. p. 187) Harleysville sent reservation-of-rights letters to the developers but failed to send a reservation-of-rights letter to the general contractor, Buildstar. Harleysville controlled the defense and attended the trial with its coverage counsel. (Tr. p. 189) Harleysville had an agreement with its insureds that coverage issues would be decided in a subsequent action. (Tr. pp. 208-209)

The Pope Class Action was consolidated with the POA action and a jury trial commenced on January 5, 2009, and concluded with general jury verdicts in favor of the POA and Pope Class on January 15, 2009. ("underlying action") (Tr. Ex. 25) The Pope Class Action verdict is not the subject of this cross appeal. These verdicts were upheld by

the Court of Appeals. *Pope v. Heritage Communities, Inc., 395 S.C. 404, 717 S.E.2d 765 (2011)* A petition for rehearing was filed with the Court of Appeals which was denied and a Writ of Certiorari was filed with the Supreme Court which is now pending.

In the underlying POA action, the POA alleged negligence and breach of fiduciary duty and sought damages for construction defects and progressive property damage in the construction of the Riverwalk Condominiums. The claims were for both defective construction and for water intrusion damages resulting from the defective construction. (POA Fourth Amended Complaint, Tr. Ex. 4) The POA also submitted to the jury as damages the expenditures it had made over the years in an attempt to mitigate water intrusion damages and to make the buildings safe (Un. Tr. Ex. 11; pp. 438-439) Various repair estimates were submitted to the jury by both the POA and the Harleysville Insureds. The POA alleged numerous causes of action but only breach of fiduciary duty and negligence went to the jury. (Tr. Ex. 25) Both the POA and defense counsel hired by Harleysville consented to the form of the verdict. (Un. Tr., pp. 1726-1727) Although Harleysville's construction defects litigation specialist, Lee Wright, along with Harleysville's coverage counsel attended the trial and had discussions with defense counsel (Tr. p. 189), (who were lawyers regularly hired by Harleysville to defend its insureds) (Tr. p. 187) no attempt was made to intervene or to seek an allocated verdict, and in fact, Harleysville made a conscious decision not to intervene. (Tr. p. 188) Harleysville candidly admits that there is no way now to determine how the jury allocated damages. (Tr. Ex. 11, Wright depo. p. 85; Tr. Ex. 11, Tormay depo. p. 28) Harleysville did not advise the Harleysville Insureds that it had a conflict of interest or the devastating

consequences a general verdict may engender. (Tr. p. 182) Harleysville never discussed the need for an allocated verdict with its insureds (Tr. pp. 188-89)

On January 15, 2009, the jury returned its general verdict finding the Harleysville Insureds were negligent and breached their fiduciary duty to the POA. The jury awarded the POA Four Million Two Hundred Fifty Thousand ($4,250,000.00) Dollars actual damages and punitive damages of Two Hundred Fifty Thousand ($250,000.00) Dollars. (Tr. Ex. 25) Pursuant to post trial motions, the Court granted a set-off. (Order dated April 10, 2009)

In this declaratory judgment action, Harleysville asked the Court to allow it to re-litigate the damages awarded by the jury by doing a complete new estimate of damages and then using the new estimate to determine what part of the POA general verdict may have constituted covered ("progressive property damage") damages. Harleysville contended that this could be done by taking the percentage of the new estimate that represented "covered" damages and multiplying that percentage times the POA general verdict to arrive at the amount of covered ("progressive") damages that may have been included in the general verdict. (Tr. p. 250) The "new estimate" had no relationship to the estimates provided to the jury in the underlying trial. (Tr. p. 262) Harleysville's expert in fact never even looked at any estimate submitted to the jury. (Tr. p. 262)

The POA objected to this attempt by Harleysville to re-litigate damages in an attempt to go behind or parse the verdict. (Tr. pp. 217-219) The POA took the position that the new estimate was not relevant (Tr. pp. 217-219) and that there was no basis in the law to go behind the general verdict to guess at what the jury had in their minds when

they delivered their verdict. (Tr. pp. 217-219) The Trial Judge sustained the POA's objection but allowed Harleysville to proffer the evidence. (Tr. pp. 233-234)

At the time of the initial hearing of this case on August 3, 2010, the *Crossman* decision discussed infra, had not been finalized and the parties agreed to hold the case open until the *Crossman* case, which had as the main issue "Time-on-the-Risk", was concluded. After the *Crossman* decision was finalized, this case was reopened on December 9, 2011, to receive testimony relative to the application of TOR. The POA renewed its objection to any testimony which attempted to form a basis to apply TOR or parse the general verdict. (Tr. December 9, 2011, pp. 5-12) The Trial Judge issued his Order dated February 28, 2010, finding, inter alia, that it was appropriate to apply TOR to the POA general verdict. The Trial Judge cited no legal authority for applying TOR to a general unallocated verdict[5]. The POA filed a Motion to Alter or Amend, (Motion to Alter or Amend filed March 20, 2013) asking the Trial Judge to eliminate from his Order the application of TOR to the general verdict on numerous grounds which he declined and this cross appeal followed.

[5] Although the Trial Judge based his ruling on the *Crossman* decision, the *Crossman* parties stipulated that all damages were progressive damages. Id. at p. 46.

Argument

I. Did the Trial Judge err in applying TOR to the general unallocated verdict, especially in light of the fact that in order to do so the Trial Judge had to enter into speculation as to the type of damages and the amount of progressive damages allocated by the jury.

Pro-rata, "Time-on-the-Risk" ("TOR") claims usually arise in environmental cases involving long term environmental contamination where a policy holder sues one of its CGL insurers that provided coverage for the risk (was "on the risk") for only a portion of the time during which the contamination took place. These disputes involve "long-tail" claims. *Boston Gas Company v. Century Indemnity Company, 454 Mass. 337, 910 N.E.2d 290 (2009)* In the recent case of *Crossman Communities of North Carolina, Inc., et. al., v. Harleysville Mutual Insurance Company, 395 S.C. 40, 717 S.E.2d 589 (2011)* ("Crossman") the Supreme Court adopted the pro-rata, TOR method to allocate loss among successive insurers where property damages are progressive, such as water intrusion damages occurring over different policy periods. TOR limits coverage to damages occurring during the policy period which may require the insured to absorb any loss during any periods he did not have insurance. The TOR application only applies to "progressive damages" occurring during more than one policy period. *Crossman* Therefore, the first inquiry by the Court must be the amount of progressive damages. The amount of progressive damages in the underlying POA verdict is impossible to determine since it is a general unallocated verdict. (Tr. Ex. 25)

In this declaratory judgment action, the Trial Judge held that the general verdict in the underlying action was covered by Harleysville's policies since Harleysville failed to seek or obtain an allocated verdict; covered claims were submitted to the jury; and there

were no exclusions that would preclude coverage of those claims. *Owners Ins. Co. v. Clayton, 364 S.C. 555, 614 S.E.2d 611 (2005)* (where a covered claim and a non-covered claims are submitted to the jury and a general verdict is rendered, the entire verdict is covered.); see also *Newman*, infra. During oral arguments counsel for Harleysville conceded that covered claims were submitted to the jury. (Tr. April 19, 2013, p. 11, pp. 77-78) Notwithstanding, the Trial Judge determined that pursuant to the recent *Crossman* decision there were uninsured periods of progressive damages and using the Time-on-the-Risk ("TOR") analysis substantially reduced the amount of insurance coverage available under the Harleysville policies to pay the actual damages awarded to the POA.[6] This ruling is inconsistent and in err. In the underlying POA case, progressive damages, non-progressive damages and other types of damages were submitted to the jury which rendered a general verdict. (Un. Tr. pp. 438-439, 879-914) By applying TOR, the Judge in effect ruled that a portion of the general verdict is not covered by the Harleysville policies. In this case, he cannot find both. TOR determines if a part or all of "progressive property damages" are covered damages. To apply TOR to the verdict, the Trial Judge necessarily had to know: a) the jury allocated damages to progressive damages; b) the amount so allocated; and c) if the progressive damages so awarded were for periods outside the coverage of the Harleysville policies. The Trial Judge had none of this information upon which to base the application of TOR. *Krock v. Chroust, 300 Pa. Super. 108, 478 A.2d 1376 (1984)* (In light of the complete lack of information about the intent of the jury, it was error for the Trial Court to grant appellants motion to mold the verdict. It is beyond peradventure that the Trial Judge has the power to mold a jury's

[6] The Trial Judge reduced the actual damages available for coverage by applying TOR from $3,288,678.36 to $1,794,499.43. (Order February 28, 2013, p. 47)

verdict). Once the Trial Judge declared the general verdict to be covered, he had no basis to apply TOR to exclude part of the general verdict. The Court was misguided in its ruling.

In its complaint Harleysville asked the Court to "conduct an accounting" of the general verdict to determine what part of the general verdict was covered and then apply TOR to that part of the verdict the Court concluded were covered damages; recognition that the Court can only apply TOR to progressive property damages. (Harleysville's Comp. p. 9) Nowhere in its pleadings did Harleysville ask the Court to apply TOR to the entire general verdict. The Court was clearly in err in applying TOR to the POA general verdict even if Harleysville had asked for such relief since TOR only applies to "progressive property damages" and Harleysville concedes it is now impossible to determine how the jury allocated damages. (Tr. Ex. 11, Wright depo. p. 85; Tr. Ex. 11, Tormey depo. p. 28)

In *Crossman*, the Court was asked to decide the proper method of allocating loss caused by progressive damages [7] over successive policy periods. The parties stipulated in *Crossman* that all of the damages under consideration were "progressive damages". Id. at p. 46. *Crossman* makes it clear that TOR only applies to property damages that occur progressively over successive periods and is a method to allocate coverage for progressive damages among successive policy periods and uninsured periods. In the typical "occurrence" covered by a liability policy, there is usually an event with something akin to a car accident. "Losses of this nature are relatively easy to identify

[7] The Court defines a progressive injury in Crossman as "a progressive injury is an injury that results from an event or set of conditions that occurs repeatedly or continuously overtime such as long term exposure to asbestos fibers or the continual intrusion of water into a building."

because damages are both immediate and finite, and can be measured quite simply against the limits of the policy or policies in effect on the date of the accident." *William R. Hickman & Mary R. DeYoung, Allocation of Environmental Cleanup Liability Between Successive Insurers, 17 N. Ky. L. Rev. 291, 292 (1990)* In contrast, progressive damages occur over an extended period of time, such as bodily injury claims for toxic exposures and property damage claims for environmental contamination. The *Crossman* court held that progressive damages may also occur from water intrusion resulting from defective construction. *Crossman* made it clear that TOR is the appropriate method of allocating coverage only in a "progressive property damage" case. Id. at p. 64-65. Therefore, in order to apply TOR the Trial Court had to necessarily know what amount the jury allocated to progressive property damages. This is not possible since the POA verdict was a general verdict.

Harleysville has not sought application of TOR to the entire general verdict either in its pleadings or at trial. Harleysville conceded at oral arguments on the motions to alter or amend that the POA verdict included covered as well as uncovered claims. (Tr. April 19, 2013, p. 11, pp. 77-78) Had Harleysville sought the application of TOR to the entire general verdict, there would have been no reason for Harleysville to seek to introduce testimony in an attempt to allocate the general verdict. The Court therefore clearly erred in applying TOR to the POA general verdict rendered by a jury that considered numerous types of damages. (Un. Tr. pp. 438-439, 879-933)

Applying TOR to the general verdict may be reducing damages the jury did not award. *State v. Dasher, 278 S.C. 395, 297 S.E.2d 414 (1982)* (a Trial Judge may not invade the province of a jury or substitute his verdict for theirs). This is illustrated by the

fact that the POA asked the jury to return a verdict in excess of Nine Million Five Hundred Thousand ($9,500,000.00) Dollars. (Un. Tr. p. 1769) Instead, the jury returned a verdict of Four Million Two Hundred Fifty Thousand ($4,250,000.00) Dollars, less than half of the asked for relief. The Trial Judge charged the jury that the POA had the duty to mitigate damages. (Un. Tr. pp. 1819-1820) Who is to say that the jury did not reduce the POA's demand for failure to mitigate damages thus eliminating or substantially reducing "progressive property damages"? Or who is to say that the jury (which found a breach of fiduciary duty which had to occur upon turnover of the common elements to the POA) found the POA should not be paid for any continuing damages after turnover. *Concerned Dunes West Residents v. Georgia Pacific Corporation, 349 S.C. 251, 562 S.E.2d 633 (2002)* (developer who breaches fiduciary duty by turning common elements which are in disrepair over to the homeowners is liable for all damages flowing from the breach "including damages for continued deterioration of these areas". Id. at p. 260). The "continued deterioration" is tantamount to "progressive damages". In applying TOR, the Trial Judge speculated that the jury awarded some measure of damages for "progressive property damages", an assumption he erred in making. *Armstrong v. Collins, 366 S.C. 204, 621 S.E.2d 368 (Ct. App. 2005)* (Court cannot speculate how the jury allocated damages); *Jenkins v. Few, 391 S.C. 209, 705 S.E.2d 457 (2012)* (because the verdict was a general verdict, Court will not speculate on how the jury allocated damages); *State v. Williams, 166 S.C. 63, 164 S.E. 415 (1932)* (The Trial Judge is not a juror).

II. Did the Trial Judge err when he determined that there was no method to allocate the general verdict into covered damages and uncovered damages and thus the entire verdict was covered and then applied TOR to the general verdict?

Courts have long recognized the sanctity of a general verdict. *Midwest Underground Storage, Inc. v. Porter, 717 F.2d 493 (C.A. 10, Kan. 1983)* (general verdicts have "traditional sanctity" and will not be upset on the basis of speculation as to the manner in which the jurors arrived at it.) Nowhere could this writer find in the annals of South Carolina jurisprudence where the appellant court allowed the post trial dissection of a general verdict. *State v. Mitchell, 399 S.C. 410, 731 S.E.2d 889 (2012)* (A Trial Judge may not substitute his own judgment for that of the jury.) Judge Milling cites many examples in his Order where the South Carolina Appellate Courts refused to speculate as to what the jury had in its mind when it reached its verdict. (Order of Judge Milling, February 28, 2013, p. 32) For example, in *Moore v. Moore, 360 S.C. 241, 599 S.E.2d 467 (S.C. App. 2004)*, the Court held "since the jury returned a general verdict and appellant did not request the trial court to submit a special verdict form to determine the type of damages rendered by the jury, the court cannot speculate as to what portion of the award the jury attributed to lost profits as opposed to other tort damages". Id. at p. 257 Harleysville controlled the defense and by making the decision not to intervene or otherwise seek a special verdict or special interrogatories prejudiced the rights of its insureds and the POA. Harleysville now asks the Court to speculate as to what part of the jury's verdict represents damages occurring outside (uncovered) policy periods. This very issue was addressed in *Auto-Owners Insurance Co. v. Newman, 385 S.C. 187, 684 S.E.2d 541 (2009)* ("Newman"). *Newman* was a declaratory judgment action to determine if an arbitrator's award in a defective house construction case was covered by the Auto-Owners policy. In *Newman,* various claims had been submitted to the arbitrator. The arbitrator issued a general award and did not allocate damages among the various claims.

Auto-Owners employed attorneys to represent its insureds in the underlying arbitration but did not ask for any allocation of the arbitrator's award. The *Newman* Court held that part of the damages submitted to the arbitrator were covered and a part not. The Court held that because the arbitrator issued a general award, Auto-Owners would be liable for the entire award. The Court said:

> "Nevertheless, it is not possible from the record before this Court to determine what portion of the arbitrator's itemized list of damages may be attributed to the removal and replacement of the defective stucco, and it is not the purpose of this declaratory judgment action to re-litigate the issue of damages. Auto-Owners had an opportunity to raise this matter [allocation of damages between covered and non-covered damages] when the issue of damages was litigated before the arbitrator, who issued a final, binding award on the merits. FN5 (citation omitted). *Id.* at p. 198.

> FN5. Auto-Owners represented Trinity in binding arbitration, made mandatory by the terms of the insurance contract. Auto-Owners did so with a reservation of rights and an understanding that the coverage issue would be reserved for judicial consideration in a separate proceeding. When the arbitrator determined damages, Auto-Owners did not seek review or otherwise contest the damages award. *Id.* at p.198

The Supreme Court has consistently applied this reasoning. In *Owners Insurance Company v. Clayton, supra*, ("Owners") the Court had before it a Summary Judgment granted by the Circuit Court on an insurance policy coverage question. The Circuit Court had ruled that Lands Inn was entitled to indemnification of a One Million Two Hundred Thousand ($1,200,000.00) Dollar verdict in Clayton's favor. Owners had defended its insureds under a full reservation-of-rights. The case had been submitted to the jury on three (3) causes of action: malicious prosecution, slander and negligence. Owners contended that the "Employment-Related-Practices Exclusion" ("ERP") should exclude coverage of the general verdict. The Court stated that the inquiry was whether the

claimed defamation related to Clayton's employment. The Court found that one of the acts of defamation presented at trial was not related to Clayton's employment and therefore was not excluded. The Court therefore had before it this question: Where several claims are submitted to the jury, some covered by the policy and some excluded, what is the answer to the coverage question when there is a general verdict? The Court held that since there was a general verdict and one of the claims was covered, the insurance carrier, in this case Owners, must pay the entire verdict. The case sub judice is no different. The Trial Judge found that covered claims were submitted to the jury and the general verdict was covered. The Trial Judge erred when he then reduced coverage by applying TOR. This is no different than if the Trial Judge in *Owners* had ruled that since there were two non-covered claims and one covered claim submitted to the jury he would reduce coverage by 2/3 to give Owners credit for the two uncovered claims. This in spite of the fact that in this case, as in *Owners*, the general verdict makes it impossible to determine how the jury arrived at its verdict. Since Harleysville controlled the defense, Harleysville should suffer the consequences of its failure to seek an allocated verdict. See also *Automax Hyundai South, LLC v. Zurich American Insurance Company, 2013 WL 3198603 (U.S. Ct. App. C.A. 10)*, (Citing *Owners Insurance Company v. Clayton, supra*, holding that where covered claims and uncovered claims are submitted to the jury and there is no way to determine how the jury allocated damages because a general verdict is rendered, the insurer who is in charge of the defense has an obligation to seek an allocated verdict and failure to do so requires the carrier to pay the entire verdict.) Finding that there were covered claims submitted to the jury in this case means the entire verdict must be paid by Harleysville.

In the underlying case, Harleysville defended its insureds as it was required to do under the terms of its policies. By assuming and controlling the defense of its insureds, it took upon itself certain duties. As the Trial Court pointed out (Order of Judge Milling February 28, 2013, p. 34) one of those duties is not to prejudice the insureds' rights by failing to request a special verdict or special interrogatories in order to clarify which damages are covered. *Magnum Foods, Inc. v. Continental Gas Co., 36 F. 3d 1491 (10th Cir. Ok. 1994)* In this case, Harleysville controlled the defense, had its "construction litigation specialist" attend the trial with coverage counsel, conferred with defense counsel during the trial and never suggested or discussed the need for an allocated verdict. (Tr. pp. 182-189) Harleysville completely ignored its obligations to protect its insureds. *Butterfield v. Giuntoli, et. al., 448 Pa. Super. 1, 670 A.2d 646, 658 (1995)* (holding that insurer had the opportunity and obligation to request specific interrogatories allocating damages between covered and uncovered claims where insurers attorney attended the trial, was in constant contact with defense counsel, and sat in chambers conferences). Harleysville could have avoided the very issue which is now being litigated ten (10) years after the underlying case was filed. The insurer is in the best position to see to it that damages are allocated. (*Magnum Foods*, Id. at pp. 1498-1499) The Trial Court in its Order correctly pointed out that the lack of an allocated verdict has dire consequences not only to the insureds, but also to the injured parties who stand in the shoes of the insured. (Order pp. 34-35) These consequences cannot be eliminated by the Trial Judge; the entire verdict is covered. *Newman*, supra.

The *Newman* holding has been followed in other jurisdictions. For example, in *Pharmacists Mutual Insurance Co. v. Mayer, 187 Vt. 323, 993 A.2d 413 (2010),*

Pharmacists filed a declaratory judgment action to determine its obligation for coverage of a verdict for defamation under the *Pharmacists'* policy. Certain defamatory statements were covered and some not. The verdict did not differentiate on what basis the jury found defamation. The court first pointed out that in order to escape coverage, *Pharmacists* had the burden of showing that the verdict sought to be paid was entirely excluded from coverage. *Pharmacists* had determined in the underlying trial that it had a conflict and allowed its insured to select independent counsel to be paid by *Pharmacists*. The Court's discussion mirrors the underlying problem that Harleysville has created in this case:

> In the absence of special interrogatories it is impossible, of course, to reliably allocate the defamation damages, but the problem could and should have been avoided. While Pharmacists did not control the litigation having perceived a conflict and deferred to independent counsel it nevertheless continued to monitor the *Cooper* trial though its "litigation specialist" and remained in regular contact with defense counsel. Indeed, Pharmacists remained the most informed party concerning coverage issues and the potential difficulties of parsing a general verdict as between covered and uncovered claims. Therefore, to protect its interests and meet its burden it was incumbent upon Pharmacists to notify the trial court and the parties of the potential apportionment issue and of the need for special interrogatories allocating damages, to seek permission if necessary to attend the charge conference to propose such interrogatories, or even to intervene in the litigation if all else failed.

The Court went on to hold that the fact that the insured hired separate counsel did not obviate or lesson *Pharmacists*' duty to seek an allocated verdict citing *Duke v. Hoch, 468 F.2d 973, 979 (5th Cir. 1972).* In this case, Harleysville attended the trial along with its coverage counsel (Tr. p. 189); conferred with defense counsel (Tr. p. 188); and yet made a conscious decision not to intervene or take any action to seek an allocated verdict. (Tr. p. 182-183) Harleysville clearly knew the problems they and their insured would

have with an unallocated verdict yet sat on their hands and took no action, relying on their mistaken belief that there was no coverage.

Allowing a Trial Court to apply TOR to a general unallocated verdict as in the case at bar, could have devastating consequences to insureds who are at the mercy of their carrier. Were Harleysville allowed to assume the defense of its insureds and then determine whether or not to seek an allocated verdict, Harleysville would put itself in a position of saying to their insureds, "Heads I win, tails you lose". *Tyger River Pine Co., v. Maryland Cas. Co., 170 S.C. 286, 170 S.E. 346 (1933)* If it were advantageous to the insurance carrier to seek an allocated verdict it would, and if not, it could refrain from doing so. This would place the burden on the insured or the injured party to engage in more protracted litigation as is the present case. It puts the Court in a guessing game sending it down the path of unguided speculation. Harleysville made a conscious decision not to intervene and should not be allowed to benefit from its conscious failure to protect the rights of its insured and ergo these claimants by allowing Harleysville to re-litigate damages. Harleysville seeks the Court's aid to extricate it from its own failure to protect its rights and those of its insureds. Harleysville failed to avail itself of the procedure (intervening or submission of special verdict or interrogatories) that the legislature provided under SCRCP 24 and the Court should not extricate Harleysville from its misguided decision. *McCloud v. Toy Reigels Chemicals, 20 Cal. App. 3d 928, 97 Cal. Rptr. 910 (Cal. App. 3d Dist. 1971)* (A party should have but one chance to have a jury's fact finding pinpointed. They should not be permitted to drag out litigation through the Appellate Courts by turning their backs on safeguards [intervening] afforded by the legislature thereby placing the Court in a guessing game.) Allowing an insurance carrier

who opts not to seek an allocated verdict to later attempt to allocate damages is not only prejudicial to its insured, but also requires more litigation of issues that could have been resolved in one trial.

The Trial Judge should have ruled as the *Newman* Court did, that Harleysville's failure to intervene or otherwise seek an allocated verdict when it had the opportunity and obligation meant that Harleysville must pay the entire verdict without TOR reduction.

III. Did the Trial Judge err when he applied TOR to the general verdict even after he had ruled that Harleysville failed to properly reserve its right to contest coverage?

The Trial Judge also found that the reservation-of-rights letters that Harleysville sent to the Harleysville Insureds were not sufficient to allow Harleysville to contest coverage. These findings by the Trial Judge should preclude Harleysville from contesting coverage for any reason including that progressive damages occurred outside the policy period. The requirement of the carrier to properly explain to its insureds that there is a conflict of interest and it is reserving its right to contest coverage is so that the insured can make an informed decision as to whether they should take some action to protect their interests. *Alan G. Windt, Insurance Claims and Disputes: Representation of Insurance Companies Insureds § 2.14 (5th Ed. 2007)* Failure to properly reserve its rights to contest coverage while undertaking and controlling the defense precludes the insurer from asserting policy defenses. *North River Ins. Co. v. Huff, 628 F. Supp 1129, 1134 (D. Kan. 1985)* In this case the reservation-of-rights letters failed to communicate to its insureds that it was contesting coverage because a part of the damages occurred outside the policy period. Since the Trial Judge held that the reservation-of-rights letters were

inadequate, the Court should have determined that Harleysville could not contest coverage of any part of the verdict.

IV. Did the Trial Judge err in finding the ending date for TOR purposes to be April 30, 2004, since the jury found breach of fiduciary duty which occurred on May 29, 2002, and it not possible to determine if the jury awarded any continuing deterioration (progressive) damages after that date? And did the Trial Judge err in setting the ending date at April 30, 2004 when a damage estimate submitted to the jury was based on a 2003 scope of work?

As noted above, in addition to the negligence cause of action, a breach of fiduciary duty cause of action was submitted to the jury and the jury found that the Defendants breached their fiduciary duty. A developer that has controlled the Association and has developed the project has a fiduciary duty to the Property Owners Association to transfer the common areas in good repair or to provide funds to bring the common areas up to a standard of reasonably good repair. If the developer fails in their duty, the developer is liable to the POA for all damages proximately flowing from the breach, including damages for the continued deterioration of the areas. *Concerned Dunes West Residents Inc. v. Georgia-Pacific Corporation, et. al., supra.* In the Riverwalk Condominium project, the developers turned the common areas over to the Association on May 29, 2002. (Un. Tr. Ex. 8) Who is to say that the jury awarded damages at the time the common areas were turned over to the Association on May 29, 2002 and awarded no damages occurring after that date? Maybe the jury determined that the POA did not mitigate damages and therefore did not allocate damages to progressive damages after a certain date. The jury was charged relative to the POA's obligation to mitigate damages. (Un. Tr. pp. 1819-1820) This points up the Court's error in applying TOR when there is

no way of knowing what damages the jury awarded and whether or not they awarded continuing damages after the breach of fiduciary duty. Application of TOR could well be a reduction of damages that have already been eliminated by the jury. The Trial Judge did exactly what it would not allow Harleysville to do, ie., speculate as to how the jury allocated damages. This is clearly pointed out by the fact that the jury only awarded the POA approximately one half (1/2) of the requested damages. Harleysville conceded that there is no way to now determine how the jury allocated damages and it was err for the Trial Judge to apply TOR in this case.

Conclusion

The Trial Judge erred in finding that TOR can be applied to a general unallocated verdict and this Court should reverse and find that the entire verdict is covered by the Harleysville policies. In the event the Court finds that TOR should be applied to the general verdict, the Court should determine September 9, 2002 as the ending date to recalculate TOR reduction.

[SIGNATURE PAGE ATTACHED]

THOMPSON & HENRY, P.A.

By: _____

John P. Henry
Philip C. Thompson
Thompson & Henry, P.A.
1300 Second Avenue, 3rd Floor
Post Office Box 1740 (zip: 29528)
Conway, South Carolina 29526
(843)248-5741

Attorneys for Respondents/Appellants Riverwalk at Arrowhead Country Club Horizontal Property Regime and Riverwalk at Arrowhead Country Club Property Owners Association, Inc.

Conway, South Carolina

August 14, 2013

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM HORRY COUNTY
Court of Common Pleas

John M. Milling, Special Referee

Case No: 2013-001291

Harleysville Group Insurance, a Pennsylvania Corporation,.....Appellant/Respondent

v.

Heritage Communities, Inc., A South Carolina Corporation; Heritage Riverwalk, A South Carolina Corporation; Buildstar Corporation, A South Carolina Corporation, Riverwalk at Arrowhead Country Club Horizontal Property Regime, Riverwalk at Arrowhead Property Owners Association, Inc., A South Carolina Corporation, National Surety Corp., and Tony L. Pope and Lynn Pope Individually and Representing as a Class All Unit Owners at Riverwalk at Arrowhead Country Club Horizontal Property Regime,.....Defendants

Of whom Heritage Communities, Inc., a South Carolina Corporation; Heritage Riverwalk, a South Carolina Corporation; Buildstar Corporation, a South Carolina Corporation; National Surety Corp., And Tony L. Pope and Lynn Pope, individually and representing as a class all unit owners at Riverwalk at Arrowhead Country Club Horizontal Property Regime are.....Respondents

And Riverwalk at Arrowhead Country Club Horizontal Property Regime; Riverwalk at Arrowhead Country Club Property Owners Association, Inc. are.....Respondents/Appellants.

RESPONDENTS/APPELLANTS DESIGNATION OF MATTER FOR THE RECORD ON APPEAL

Pursuant to Rule 209, SCACR, Respondents/Appellants Riverwalk at Arrowhead Country Club Horizontal Property Regime and Riverwalk at Arrowhead Country Club Property Owners' Association, Inc. ("Respondents/Appellants") designate the following material for inclusion in the record on appeal. Undersigned counsel certifies, pursuant to Rule 209(c), SCACR, that the designation contains no matter which is irrelevant to the appeal:

ORDERS

1. Order appointing John M. Milling as special referee dated October 21, 2010.
2. Order of John M. Milling, special referee dated February 28, 2013.
3. Order of John M. Milling, Special Referee, denying relief requested in Respondents/Appellants and Appellants/Respondents motions to Alter, Amend or Vacate the February 28, 2013 Order.
4. Underlying Order in re post trial motions dated April 10, 2009.

VERDICT FORM

1. Tr. Ex. 25 Verdict Form from the underlying trial dated January 15, 2009.

PLEADINGS

1. Declaratory Judgment Complaint filed by Harleysville October 14, 2009
2. Amended Answer and Counterclaim filed by POA November 6, 2009.
3. Harleysville's Reply to Amended Counterclaim dated November 23, 2008.
4. Ex. 4 underlying Fourth Amended Complaint filed August 3, 2006.

TRANSCRIPTS

1. Trial Transcript dated December 13-14, 2010, pages: 18, 26, 95, 98, 99, 101, 103, 111, 118, 120, 130, 138-139, 166-167, 178-191, 204, 208-209, 216, 219, 233-235, 250-267, 262
2. Trial Transcript dated December 9, 2011.
3. Trial Transcript dated April 19, 2013.
4. Underlying Trial Transcript, pages: 438-439; 879-993; 1726-1727; 1769; 1819-1820
5. Wright Deposition August 3, 2010, pages: 9; 11; 13-33; 44; 48; 80-87.
6. Tormey Deposition October 19, 2010, pages: 6; 7; 9; 10; 17; 22-30; 32.

EXHIBITS/DOCUMENTS

1. Tr. Ex. 15 Reservation-of-Rights letters.
2. Tr. Ex. 14 Discovery responses by Harleysville.
3. Tr. Ex. 17 Chart of Harleysville's policies.
4. Tr. Ex. 19 Harleysville policy common forms.
5. Tr. Ex. 12 Notebook of Harleysville's policies.
6. Harleysville's Amended Answers to Defendant's Requests for Admissions dated October 1, 2010.
7. Harleysville's Amended Answers to Interrogatories dated October 15, 2010.
8. Underlying Tr. Ex. 8.

MOTIONS

1. POA Motion to Alter or Amend filed March 20, 2013.

2. Harleysville's Motion to Alter or Amend or Vacate filed March 21, 2013.

THOMPSON & HENRY, P.A.

By: _____

John P. Henry
Philip C. Thompson
Thompson & Henry, P.A.
1300 Second Avenue, 3rd Floor
Post Office Box 1740 (zip: 29528)
Conway, South Carolina 29526
(843)248-5741

Attorneys for Respondents/Appellants Riverwalk at Arrowhead Country Club Horizontal Property Regime and Riverwalk at Arrowhead Country Club Property Owners Association, Inc.

August 14, 2013

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM HORRY COUNTY
Court of Common Pleas

John M. Milling, Special Referee

Case No: 2013-001291

Harleysville Group Insurance, a Pennsylvania Corporation,.....Appellant/Respondent

v.

Heritage Communities, Inc., A South Carolina Corporation; Heritage Riverwalk, A South Carolina Corporation; Buildstar Corporation, A South Carolina Corporation, Riverwalk at Arrowhead Country Club Horizontal Property Regime, Riverwalk at Arrowhead Property Owners Association, Inc., A South Carolina Corporation, National Surety Corp., and Tony L. Pope and Lynn Pope Individually and Representing as a Class All Unit Owners at Riverwalk at Arrowhead Country Club Horizontal Property Regime,.....Defendants

Of whom Heritage Communities, Inc., a South Carolina Corporation; Heritage Riverwalk, a South Carolina Corporation; Buildstar Corporation, a South Carolina Corporation; National Surety Corp., And Tony L. Pope and Lynn Pope, individually and representing as a class all unit owners at Riverwalk at Arrowhead Country Club Horizontal Property Regime are.....Respondents

And Riverwalk at Arrowhead Country Club Horizontal Property Regime; Riverwalk at Arrowhead Country Club Property Owners Association, Inc. are.....Respondents/Appellants.

PROOF OF SERVICE

I, the undersigned legal assistant for John P. Henry of Thompson & Henry, P.A., attorneys for Respondents/Appellants, do hereby certify that I have served all counsel in this action with a copy of the documents(s) hereinbelow specified by mailing a copy of same by United States Mail, postage prepaid, to the following address(es) this 15th day of August, 2013:

Pleading(s): Initial Brief of Respondents/Appellants; and
Respondents/Appellants Designation of Matter

Counsel Served:

Robert C. Calamari, Esquire
Nelson, Mullins
3751 Robert M. Grissom Parkway
Myrtle Beach, South Carolina, 29577

C. Mitchell Brown, Esquire
Nelson, Mullins
1320 Main Street, 17th Floor
Post Office Box 11070 (29211)
Columbia, SC 29201

Laura J. Evans, Esquire
Smith Moore Leatherwood, LLP
25 Calhoun Street, Suite 250
Charleston, South Carolina 29401

Karin McCarthy, Esquire
Rivkin-Radler
Long Island- 926 RXR Plaza
Uniondale, New York 11556-0926

Stephanie Hall

Stephanie Hall

Conway, South Carolina