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. 2009-CP-26-11862
Appellate Case No. 2013-001291

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

v.

Heritage Communities, Inc., a South Carolina corporation; Heritage Magnolia North, Inc., a South Carolina corporation; Buildstar Corp., a South Carolina corporation; Magnolia North Horizontal Property Regime; Magnolia North Property Owners Assoc., Inc., a South Carolina corporation; and National Surety Corp., ... Defendants,

Of whom Heritage Communities, Inc., a South Carolina corporation; Heritage Magnolia North, Inc., a South Carolina corporation; Buildstar Corp., a South Carolina corporation; and National Surety Corp. are..... Respondents,

And Magnolia North Horizontal Property Regime and Magnolia North Property Owners Assoc., Inc., a South Carolina corporation are..... Respondents/Appellants.

INITIAL REPLY BRIEF OF APPELLANT/RESPONDENT

NELSON MULLINS RILEY & SCARBOROUGH, LLP

C. Mitchell Brown
William C. Wood, Jr.
A. Mattison Bogan
Miles E. Coleman
Post Office Box 11070
Columbia, SC 29211
(803) 799-2000

Robert C. Calamari
Post Office Box 3939
Myrtle Beach, SC 29577
(843) 448-3500

Attorneys for Appellant/Respondent

Table of Contents

Table of Authorities

Cases

Statutes

Rules

Harleysville Group Insurance ("Harleysville") hereby replies to the brief of Respondents/Appellants Magnolia North Horizontal Property Regime and Magnolia North Property Owners Assoc., Inc. (collectively "the property owners' association" or "the association").

Argument

I. The Special Referee erred by denying Harleysville's request to allocate the underlying damages into categories of covered and non-covered damages.

As explained in Harleysville's opening brief, the Special Referee improperly denied Harleysville's request to perform the *Crossmann* analysis of dividing and categorizing the underlying verdict amount into (1) the costs of repairing the defect, which are not covered damages, and (2) the costs of repairing the damage resulting from the defective work, which may be covered. *See* Harleysville's Opening Brief at 4-14. As explained below, the counterarguments raised in the association's Response brief do not justify the Special Referee's error nor do they rebut Harleysville's arguments in favor of allocation.

A. An allocation is not a "re-litigation" of any issue.

As explained in Harleysville's opening brief, its request in this coverage action to allocate the underlying damages would not "re-litigate" the issue of damages. *See id.* at 5-8. Rather, allocation merely determines what portion of that amount should be paid by Harleysville and what portion should be paid by its insureds. Because this question—which is an issue between the insurer and the insured—was not previously litigated, its resolution now is not a "re-litigation."

The association does not dispute this. Rather, it argues that Harleysville "had a duty to its insured to seek" an allocated verdict in the underlying action. *See* Association's Response Brief at 13. The association cites no South Carolina authority establishing such a duty.[1] Even assuming *arguendo* that such a duty exists, Harleysville satisfied that duty by discussing the coverage issues with its insureds and mutually agreeing to resolve those issues in a subsequent coverage action. (Trial Tr. of Dec. 13-14, 2010 at 113, 182, 209; *see also* Association's Response Brief at 4 ("Harleysville had an agreement with its insureds that they would resolve coverage issues in a subsequent judicial proceeding.") (citing Trial Tr. of Dec. 13-14, 2010 at 185).)

Furthermore, the failure of an insurer to inform its insured of the wisdom of requesting an allocated verdict should not result in the inability to conduct a subsequent allocation of an underlying general verdict. *See Remodeling Dimensions, Inc. v. Integrity Mut. Ins. Co.*, 819 N.W.2d 602, 618 (Minn. 2012) (noting that where the insurer fails to inform its insured of the benefits of a special verdict, the insurer may bring a subsequent coverage action where "both parties may present evidence and the district court must, as best it can, establish the allocation the arbitrator would have made if allocation had been requested").

B. At the time of the underlying trial, there was no need or possibility for Harleysville to intervene and seek an allocated verdict.

As explained in Harleysville's opening brief, under the law in force at the time of the underlying trial, Harleysville had neither the opportunity nor the incentive to

[1] The sole South Carolina case the association cites for this supposed duty—*Armitage v. Seabord Airline Ry. Co.*, 166 S.C. 21, 164 S.E.2d 169 (1932)—has nothing to do with insurance coverage or the allocation of damages into covered and non-covered amounts.

intervene and request a special verdict form.[2] *See* Harleysville's Opening Brief at 8-11. In its Response Brief, the association does not dispute this. Rather, it merely asserts that Harleysville should have foreseen a future change in the law and sought to stay the underlying cases until any change in the law occurred, or that Harleysville should have filed its declaratory judgment action sooner. *See* Association's Response Brief at 14-15.

These assertions do not alter the fact that at the time of the underlying trial, the law as pronounced was that every dollar of construction defect damages triggered indemnity obligations under a standard CGL policy, and thus there was no reason for an insurer to seek an allocation in a liability trial against its insureds. Even if Harleysville had foreseen the future possible ability of an insurer to seek intervention, case law from other jurisdictions indicates that an insurer is rarely required to intervene, because a subsequent coverage action is a much simpler solution. *See*, *e.g.*, *Buckley v. Orem*, 730 P.2d 1037, 1043 (Idaho Ct. App., 1986) ("We believe that requiring intervention by an insurance company in the primary action as a prerequisite to allowing the company to assert its clearly stated policy limits is a costly solution to an easily correctable problem. Intervention, with its added litigation expense, with its tendency to protract, to divert and to complicate the injury action, would certainly occur in more cases than necessary."); *id.* at 1043 n.5 ("At least one authority discourages intervention of insurance companies in the injury trial for a variety of

[2] The association claims to be confused by Harleysville's statement that there was no "opportunity" to intervene, noting that no one prevented Harleysville from filing a motion to intervene. *See* Association's Response Brief at 14. While nothing prevented Harleysville from filing a motion to intervene, there was no opportunity to *meaningfully* intervene—*i.e.*, to intervene and request a special verdict allocating the damages—because under the law then in force there was no coverage distinction between shoddy workmanship and the resulting damages, thus the allocation categories were unnecessary and meaningless. *See* Harleysville's Opening Brief at 8.

reasons.") (citation omitted). Because allocation was not known to be needed or possible at the time of the underlying Magnolia North trial, the appropriate time for allocation was in the subsequent coverage action.

C. South Carolina precedent does not preclude allocation of an underlying general verdict.

As explained in Harleysville's prior briefs, neither *Auto-Owners Ins. Co. v. Newman*, 385 S.C. 187, 684 S.E.2d 541 (2009) nor *Owners Ins. Co. v. Clayton*, 364 S.C. 555, 614 S.E.2d 611 (2005) prevent an insurer and insured from relying on a subsequent coverage action to allocate an underlying verdict into categories of covered and non-covered damages. *See* Harleysville's Opening Brief at 11-12; Harleysville's Response Brief at 11-12. Harleysville will not here repeat its prior arguments explaining and distinguishing *Newman* and *Clayton*. However, several of the association's other arguments warrant reply.

First, the association argues that the only evidence that may be used to allocate the underlying verdict is the record from the underlying trial and that no new evidence or analysis may be introduced in the coverage action. *See* Association's Response Brief at 10 (quoting Allan D. Windt, *Representations of Insurance Companies and Insureds* § 6:26); *id.* at 20. This is incorrect. The association cites no case law in support of this argument and quotes a treatise section that discusses a different issue.[3] Indeed, the

[3] The treatise excerpt quoted by the association discusses what evidence is permissible to determine whether any covered claim was submitted to the jury *See* Windt, § 6:26 ("The preceding discussion relates to the issues that are presented when there is a dispute as to whether a judgment was entered on grounds that would give rise to coverage. Such disputes can be resolved by analyzing what was proved in the underlying action. A more difficult problem is presented when the parties agree that the judgment represents both covered and noncovered items, and there is a dispute as to how to allocate the judgment between the two.").

treatise notes that in the situation presented here—where the judgment includes both covered and non-covered claims[4]—there is a different and "more difficult problem" in determining "how to allocate the judgment between the two." Windt, § 6:26.[5] Courts addressing this issue have held that an insurer *may* present new evidence in a coverage dispute to properly allocate an underlying general verdict. *See Duke v. Hoch*, 468 F.2d 973, 984 (5th Cir. 1972) ("[T]he court will face the issue of attempting retrospectively to allocate the damages awarded. . . . The primary source of evidence will be, of course, the transcript of the merits trial, containing the evidence on which the jury based its verdict. . . . . If it is impossible for the court to make a meaningful allocation based on only the transcript, [the judgment holder] should have the right to adduce additional evidence and [the insurer] to present evidence in rebuttal); *Remodeling Dimensions, Inc. v. Integrity Mut. Ins. Co.*, 819 N.W.2d 602, 618 n.4 (Minn. 2012) (noting that in a coverage action to allocate an underlying award, "[t]he primary source of evidence will be the transcript of the arbitration proceeding and the evidence before the arbitrator, but if it is impossible for the district court to make a meaningful allocation based solely on the arbitration record, the parties should have the right to adduce additional evidence"); *Allstate Ins. Co. v. Keltner*, 842 N.E.2d 879, 883 (Ind. Ct. App. 2006) (noting that the allocation of an underlying general verdict "might be

[4] Here, all—including the Special Referee—agree the underlying verdict includes both covered and non-covered damages. (*See* Post-Trial Hearing Tr. of April 9, 2013 at 89.)

[5] In quoting from this section of the treatise, the association apparently overlooks its statement that "[i]f, as is normally the case, the insured has the burden of allocating the judgment, *there will be no coverage*." Windt, § 6:26 (emphasis added; citations omitted). Indeed, the treatise supports Harleysville's argument that allocation is an appropriate issue for a coverage dispute. *Id.* at § 6:27 ("Whether the grounds on which a judgment against the insured was entered were within the policy coverage should always be a contestable issue.") (citation omitted).

determined by examining the evidence and argument of counsel presented during the underlying trial or by the presentation of additional evidence"); *Buckley v. Orem*, 730 P.2d 1037, 1043 (Idaho Ct. App., 1986) (remanding coverage action for taking of new evidence to allocate underlying general verdict).

Second, the association claims there are no South Carolina cases in which a litigant was permitted to allocate an underlying general verdict. *See* Association's Response Brief at 11. Although South Carolina's appellate courts have not previously confronted the precise issue presented in this appeal, they have recognized a court's ability to analyze and reform a jury's general verdict to bring it into compliance with the law. *See Chastain v. AnMed Health Foundation*, 388 S.C. 170, 694 S.E.2d 541 (2010) (affirming trial court's post-verdict ruling that, because it was impossible to determine from the general verdict how many negligent occurrences the jury had found, the damages award should be reduced to the amount appropriate for one occurrence). Similarly, our courts have recognized a trial court's ability to allocate an underlying settlement between various claims. *See Smith v. Widener*, 397 S.C. 468, 473, 724 S.E.2d 188, 191 (Ct. App. 2012) (holding that where a prior settlement involves two claims, one of which is later tried to a verdict, "the circuit court must make the factual determination of how to allocate the settlement between the two claims" and thus determine how much of a setoff to apply to the verdict); *Rutland v. S.C. Dept. of Transp.*, 400 S.C. 209, 734 S.E.2d 142 (2012) (affirming trial court's allocation of underlying settlement in a different way than the settling parties had agreed the amount should be allocated). In sum, neither South Carolina precedent nor persuasive authority

from other jurisdictions prevents a trial court in a coverage action from allocating an underlying general verdict on the basis of new evidence and arguments.

D. Other jurisdictions permit allocation of an underlying general verdict.

As explained in Harleysville's prior briefing, other jurisdictions permit the allocation of an underlying verdict into categories of covered and non-covered damages. *See* Harleysville's Opening Brief at 12-14; *see also Duke v. Hoch*, 468 F.2d 973 (5th Cir. 1972); *Remodeling Dimensions, Inc. v. Integrity Mut. Ins. Co.*, 819 N.W.2d 602, 618 (Minn. 2012); *Allstate Ins. Co. v. Keltner*, 842 N.E.2d 879, 883 (Ind. Ct. App. 2006); *Donna C. v. Kalamaras*, 485 A.2d 222, 224 (Me. 1984).

A federal district court recently allocated an underlying amount in a coverage action strikingly similar to this one. *See Crossmann Communities of N.C., Inc. v. Harleysville Mut. Ins. Co.*, No. 4:09-CV-1379-RBH, 2013 U.S. Dist. Lexis 138941 (D.S.C. Sept. 27, 2013). In that case, the total underlying settlement between the homeowners' association and the underlying defendants included both covered and non-covered damages. *Id.* at *37 ("The total settlement paid by Beazer to True Blue was $3,336,800, which included both covered and non-covered damages."). To determine what portion of this settlement was covered by Harleysville's policies, the trial court in the coverage action accepted expert testimony from both Harleysville and the insured builder. *Id.* at *40. The builder's estimate of the cost of repair included the cost to repair defective work (*i.e.*, non-covered damages) and the resulting damage to non-defective work (*i.e.*, covered damages). *Id.* at 41-42 (noting that the insured's expert "admitted that some of his estimate includes the cost to repair defective work rather than resulting damages"). Harleysville's expert, in contrast, estimated a cost of repair

that included only the "cost to repair the resulting damages," *i.e.*, the covered damages. *Id.* at 41. Based on these estimates, the trial court determined the amount for which Harleysville was responsible—an amount that included only the covered cost to repair resulting damages, not the defective work itself. *Id.* at 42-43. Here, the Special Referee should have similarly relied on expert testimony proffered in the coverage action to allocate the underlying verdict.

Other jurisdictions permit an allocation in circumstances like those presented here, and the association fails to effectively distinguish these cases. For example, the association argues that *Duke v. Hoch* is distinguishable because in *Duke* the insurer could prove the underlying verdict included non-covered damages. *See* Association's Response Brief at 18-19. This is no distinction. There is no dispute here that the underlying verdict included non-covered damages. *See* Post-Trial Hearing Tr. of April 9, 2013 at 89; *see also* Association's Opening Brief at 11 ("Harleysville conceded at oral arguments on the motions to alter or amend that the POA verdict included covered as well as uncovered claims.") (citing Post-Trial Hearing Tr. of 4/9/13 at 11, 77-78)).

Similarly, the association tries to distinguish other cases allocating an underlying general verdict by arguing that the facts of those cases "are vastly different." *See* Association's Response Brief at 20-21. However, the only difference the association can identify is that in those cases the insurer had moved unsuccessfully to intervene in the underlying suit. *Id.* This is a distinction without a difference. An unsuccessful motion to intervene changes none of those cases' relevant procedural facts or the courts' reasoning and holdings. This Court should follow the lead of other jurisdictions and allow a coverage action to determine an insurer's responsibility for an underlying

verdict by allocating that verdict into categories of covered and non-covered damages. This should be done in all cases where it is clear, as it is here, that the underlying verdict contains both covered and non-covered damages.

II. The "time on risk" formula applies to the underlying damages award, but the Special Referee erred in his application of that formula.

As explained in Harleysville's opening brief, the Special Referee correctly determined that *Crossmann's* "time on risk" formula applied, though he erred in several aspects of applying the formula. *See* Harleysville's Opening Brief at 14-21. The question of whether "time on risk" applies is separate from the question of allocation. Harleysville's Response Brief at 8-13. The association nevertheless continues to argue that the Special Referee erred by applying "time on risk" to a general verdict because to do so would be speculative and unprecedented in any jurisdiction. *See* Association's Response Brief at 22-24.[6] As explained below, the association is incorrect.

A. Application of "time on risk" is not speculative because all *of the underlying causes of action were premised on progressive physical damage.*

"Time on risk" applies to all covered damages here because *all* of the causes of action alleged by the association in the underlying suit were based on progressive damages. In the underlying liability action, the association brought four causes of action: negligence, breach of express warranties, breach of implied warranties, and breach of fiduciary duty. *See* Mag. North Eighth Amend. Compl. at ¶¶ 8-28. *Each* of these causes of action was expressly premised on progressive physical damages. *See id.*

[6] In addition, the association erroneously argues that the Special Referee did not err by calculating Harleysville's period of coverage based on an incorrect policy that was never in force. *See* Association's Response Brief at 24-25. The incorrect policy date, however, is not an issue in this suit. Rather, it is an issue in the companion case involving the Riverwalk at Arrowhead Country Club complex.

at ¶¶ 10, 15, 19, 25, and 26.[7] Indeed, the property owners' association concedes that a developer's breach of fiduciary duty that causes continued deterioration "is tantamount to 'progressive damages.'" *See* Association's Opening Brief at 12 (citing *Concerned Dunes West Residents v. Georgia Pac. Corp.*, 349 S.C. 251, 562 S.E.2d 633 (2002)). Because each of the association's underlying claims was based on progressive damages, there is no speculation in determining that "time on risk" applies to the entire underlying verdict.

B. Other jurisdictions apply the "time on risk" formula to underlying unallocated amounts.

The association argues there is no legal authority "authorizing application of TOR to a general verdict containing numerous types of damages and causes of action." Association's Response Brief at 24. The association is incorrect. Courts of other jurisdictions have applied "time on risk" to underlying unallocated amounts that include a variety of claims and damages. *See, e.g., Penn. Nat'l Mut. Cas. Ins. Co. v. Roberts*, 668 F.3d 106 (4th Cir. 2012) (applying "time on risk" to determine insurer's coverage responsibility for underlying verdict that included claims of unfair trade practices and negligence resulting in progressive damages from lead poisoning); *City of Sterling Heights v. United Nat'l Ins. Co.*, 319 Fed. Appx. 357 (6th Cir. 2009) (affirming use of

[7] Paragraph 10 asserts a claim for negligence based on allegation that "the buildings have been continuously and repeatedly exposed to leaks causing moisture infiltration." Paragraph 15 asserts a claim for breach of express warranties with the sole alleged damages being the same "as set forth in hereinabove," *i.e.*, the progressive damages alleged in paragraph 10. Similarly, paragraph 19 asserts a claim for breach of implied warranties with the sole alleged damages being the same "as set forth in hereinabove," *i.e.*, the progressive damages alleged in paragraph 10. Finally, paragraph 25 asserts the insureds breached their fiduciary duty by building with substandard and inappropriate materials and in turning over the buildings and common areas in deteriorated condition, and paragraph 26 alleges the damages that resulted were the same "as set forth in hereinabove," *i.e.*, the progressive damages alleged in paragraph 10.

"time on risk" formula to determine insurer's coverage liability for an underlying, unallocated settlement of claims for defamation, interference with contract, and violation of due process and equal protection rights). Because the underlying verdict here could be entirely based on progressive damages, it is appropriate to apply "time on risk" to the entire amount.

C. The Special Referee erred by failing to apply "time on risk" on a per-building basis.

As explained in Harleysville's opening brief, the Special Referee erred in his "time on risk" calculation by using a single starting date for damages to all 21 buildings, despite the fact that many of the buildings had not yet been built on the date when the damages supposedly began to occur. *See* Harleysville's Opening Brief at 16-18. The Special Referee should instead have applied his calculation on a per-building basis. A federal district court in the District of South Carolina recently applied a per-building "time on risk" calculation in a coverage action strikingly similar to this one. *See Crossmann Communities of N.C., Inc. v. Harleysville Mut. Ins. Co.*, No. 4:09-CV-1379-RBH, 2013 U.S. Dist. Lexis 138941, *57-58 (D.S.C. Sept. 27, 2013). The association does not dispute the accuracy or reasonableness of a per-building calculation. Accordingly, this Court should adopt the per-building formula set out in Harleysville's prior briefing and reduce the damages accordingly.[8]

III. The "time on risk" calculation applies to the underlying punitive damages.

In its prior briefing, Harleysville explained that, even assuming Harleysville's policies cover punitive damages, the Special Referee erred by refusing to apply the

[8] *See also* part XI, *infra*, explaining with specificity the way in which Harleysville requests this Court correct the amount for which Harleysville is responsible.

"time on risk" analysis to the underlying punitive damage award. *See* Harleysville's Opening Brief at 18-21. In response, the association seeks to analogize to contributory negligence, arguing that because a plaintiff's comparative negligence does not reduce a punitive damage award, neither should "time on risk." *See* Association's Response Brief at 26. This supposed analogy, however, fails to acknowledge the significant differences between "time on risk" and contributory negligence, such as the fact that "time on risk" does not reduce the association's punitive damages but merely determines what portion of that award Harleysville is responsible to pay.

IV. Harleysville's policies do not cover the underlying punitive damages.

As explained in Harleysville's prior briefing, Harleysville's policies cover only damages the insured is legally obligated to pay arising from bodily injury or property damage caused by an "occurrence," *i.e.*, an *accident*. Harleysville's Opening Brief at 21-23; *see also Auto-Owners Ins. Co. v. Rhodes*, 405 S.C. 584, __, 748 S.E.2d 781, 789-90 (2013) (defining an "occurrence" in a CGL policy to be an "accident," *i.e.*, an "unexpected happening or event, which occurs by chance") (citing *Green v. United Ins. Co. of Am.*, 254 S.C. 202, 206, 174 S.E.2d 400, 402 (1970)).

Punitive damages, as a matter of law, cannot be awarded for mere accidental conduct. *See Atkinson v. Orkin Exterminating Co., Inc.*, 361 S.C. 156, 167, 604 S.E.2d 385, 391 (2004) (noting that punitive damages may be warranted where the harm is the result of "intentional malice, trickery, or deceit" but not where the wrongdoing was a "mere accident") (quoting *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 419 (2003)); *Lengel v. Tom Jenkins Realty, Inc.*, 286 S.C.

515, 519-20, 334 S.E.2d 834, 837 (Ct. App. 1985) ("A plaintiff is entitled to recover punitive damages if the act complained of is determined to be willful, wanton or reckless. . . . *Punitive damages are not awarded for mere negligence.*") (emphasis added) (quotation marks and citations omitted).

Furthermore, the underlying jury instructions here make clear that the punitive damages were not awarded for merely accidental conduct. *See* Underlying Magnolia North trial Tr. at 1292-1302 (charging the jury that punitive damages could be assessed to punish Harleysville's insureds for wrongdoing that was a "conscious failure" and involved a "present consciousness of wrongdoing"). Because punitive damages—as a matter of law and in light of the underlying jury instructions—cannot be and were not awarded for mere accidental conduct, Harleysville's policies do not cover the punitive damages assessed against its insureds.

In response, the association relies on cases that are distinguishable in significant respects. *See* Association's Response Brief at 29 (citing *Carroway v. Johnson*, 245 S.C. 200, 139 S.E.2d 908 (1965) and *S.C. State Budget & Control Bd. v. Prince*, 304 S.C. 241, 403 S.E.2d 643 (1991)). *Carroway* is inapposite because it involved automobile insurance, which by statute is required to cover punitive damages. *See* S.C. Code Ann. §§ 38-77-140 (requiring coverage for "damages") and 38-77-30(4) (defining "damages" to include punitive damages). Similarly, *Prince* is inapposite because the policy expressly covered intentional torts including the underlying defamation. In addition, *Prince*, like the other case cited by the association—*State Farm Fire & Cas. Co. v. Martinez*, 995 P.2d 890 (Kan. Ct. App. 2000)—involved policies with broader language than Harleysville's policies. Specifically, the policies in *Prince* and *Martinez* covered

"all sums" the insured was obligated to pay as damages. Here, in contrast, Harleysville's policies cover only those sums the insured is liable to pay arising from an *accident*. Furthermore, *Martinez* analyzed whether the policy covered a statutory fine imposed as civil penalties on the insured, not the question of whether punitive damages were covered.[9] Thus, the cases relied upon by the association are unpersuasive.

Next, the association argues that because punitive damages may be awarded for less than intentional conduct, they must be covered by the policy. *See* Association's Response Brief at 28-30. The association's argument rests on the premise that punitive damages may be imposed not only for intentional conduct but also for reckless, willful, wanton, or grossly negligent conduct. *Id.* (citing *Penn. Thresherman & Farmers' Mut. Cas. Ins. Co. v. Thornton*, 244 F.2d 823 (4th Cir. 1957)). From this premise, however, the association leaps to the unsupported conclusion that punitive damages must be covered by Harleysville's policies. The association's argument fails for two simple reasons: (1) Harleysville's policies cover only those sums arising from accidents and (2) no authority—including *Thornton*—permits the imposition of punitive damages for merely negligent conduct.

---

[9] Incidentally, in contrast to the *Martinez* court's holding, most courts have held that insurance policies do *not* cover civil penalties. *See, e.g., Travelers Ins. v. Waltham Indus. Labs.*, 883 F.2d 1092 (1st Cir. 1989) (finding no coverage for civil penalties); *Township of Gloucester v. Maryland Cas. Co.*, 686 F. Supp. 394, 401-02 (D.N.J. 1987) (holding fines and civil penalties did not constitute "damages" under CGL policy); *A.Y. McDonald Industries v. INA*, 475 N.W.2d 607, 626 (Iowa 1991) ("We hold that the term 'damages' under the CGL policies does not include the civil penalty imposed."); *Drexel Group v. Vigilant Ins.*, 595 N.Y.S.2d 999, 1009 (N.Y. Supr. Ct. 1993) (finding "the sting of criminal penalties is not to be soothed by permitting its payment out of an insurance pool rather than directly by the wrongdoer"); *see also Washington Cnty. Unified Sewerage Agency v. First State Ins. Co.*, No. 94-36277, 1996 U.S. App. Lexis 8503, * 5-6 (9th Cir. March 28, 1996) (predicting that Oregon courts would follow the "sensible line of authority" holding that civil penalties are not covered by insurance policies).

Here, in light of the jury charge in the underlying case regarding punitive damages, the jury necessarily found and sought to punish Harleysville's insureds for wrongdoing that, in the words of the jury charge, was a "conscious failure" and involved a "present consciousness of wrongdoing." *See* Underlying Magnolia North trial Tr. at 1292-1302; *see also Pope v. Heritage Comms., Inc.*, 395 S.C. 404, 436, 717 S.E.2d 765, 782 (Ct. App. 2011) (*certiorari* pending) (holding that the Heritage entities had knowingly sold the condominiums with construction deficiencies). Because the punitive damages could not and did not arise from an "accident" as required by the express terms of the policies' insuring agreements, they are not covered.

V. The underlying damages—both actual and punitive—are excluded from coverage by the policies' "expected or intended" exclusions.

As explained in Harleysville's prior briefing, the Special Referee erred by ruling that the underlying damages are covered despite the "expected or intended" exclusions in each of the CGL policies. *See* Harleysville's Opening Brief at 23-33. In response, the association argues that Harleysville cannot prove that the insureds expected or intended their acts and the resulting damage. *See* Association's Response Brief at 31-38. As explained below, however, the association's argument fails to account for the exclusion's breadth and the evidence of the insureds' intent and expectations.

A. The actual damages were expected or intended.

The essence of the association's argument on this issue is fairly simple. It argues that because there is evidence the insureds did not intend the damages resulting from their acts, this Court cannot disturb the Special Referee's ruling that the exclusion does not apply. *See* Association's Response Brief at 35-38. The association's argument,

however, suffers from two fatal defects. First, contrary to the association's assertion, the evidence and testimony from the underlying trial indicated the insureds *did* expect or intend their actions and resulting damages.[10] Second, even if the evidence was unclear as to the insureds' *intent,* the evidence was clear that the insureds would have reasonably *expected* the damage that resulted from their shoddy workmanship.

Although the policy excludes *expected* or intended acts and damages, the association's argument focuses on the insureds' intent. *See* Association's Response Brief at 31,[11] 36,[12] and 38[13]; *see also* Mag. North Order at 19-22.[14] The distinction

---

[10] For example, the insureds knew they were using materials and practices that had previously caused damages at their prior developments, but persisted with these practices at Magnolia North. (*See* Underlying Mag. North Trial Tr. at 846-49, 852-89; Tr. of video dep. of Gwyn Hardister of April 15, 2009.) Indeed, the association's closing argument in the underlying trial argued forcefully that there was evidence of intent or expectation of damages—exactly the opposite of what it argues now:

> As you saw in the video we played of Gwyn Hardister's deposition . . . he said before we ever started Magnolia North we were having deck leaks and we were having window leaks and they, they ignored that. They just flat ignored that.
>
> * * *
>
> They knew they were having water intrusion problems at the other developments. They knew that they had deck problems. They knew that they had window problems. They knew that they were using products that was [sic] not specified by the architect. They knew that they were using cheaper products than what he had specified. And what did they do, they kept on using those same products.

Underlying Magnolia North Trial Tr. at 1216-17. The association has made a similar reversal by now relying on Mr. Hardister's testimony at the underlying trial to argue that the insureds were unaware of their shoddy practices and the substantial likelihood of resulting damage. *See* Association's Brief at 36.

[11] The association points to testimony in the coverage action from Lee Wright, Harleysville's construction litigation manager, who stated he had no evidence the insureds "'consciously *intended* to create a situation that water damage would occur.'" Association's Response Brief at 31 n.12 (citing hearing Tr. of December 13-14, 2010 at 191-92) (emphasis added).

[12] The association relies on the underlying testimony of Gwyn Hardister, president of the developer, who claimed he had "little knowledge" of the leaky windows and did not knowingly use and install substandard products. Association's Response Brief at 36.

between these terms is significant. The association incorrectly states that "expected" and "intended" are synonymous. *See* Association's Response Brief at 31. The sole case the association cites involved a different exclusion, and in any event, does not hold that the two terms are synonymous. In *S.C. Farm Bureau Mut. Ins. Co. v. Dawsey*, 371 S.C. 353, 355, 638 S.E.2d 103, 104 (Ct. App. 2006), the insured had fired shots at his sons' car tires. One of the shots ricocheted and injured the son. The insurer filed a declaratory judgment action against the father and the son to determine coverage. The trial court held that the "intentional acts" exclusion, which excluded coverage for any injury caused by an intentional act, regardless of whether the resulting injury was expected or unexpected, applied and barred coverage.[15] On appeal, the son sought to distinguish between an intentional act causing an *unexpected* result and an intentional act causing an *unintentional* result, arguing that the latter should be covered. The Court of Appeals rejected this argument because under the facts of the case, the distinction made no difference and the son had admitted "that the terms "intend' and 'expect' are 'often defined synonymously.'" *Id.* at 357, 638 S.E.2d at 105.

---

[13] The association notes the Special Referee found that the insureds installation of windows it knew had moisture intrusion problems "was *unintended* by the Harleysville insureds." Association's Response Brief at 38 (citing Special Referee's Order at 9) (emphasis added).

[14] The Special Referee relied on Lee Wright's testimony "that he had no evidence that the insureds 'consciously *intended* to create a situation that water damage would occur.'" Mag. North Order at 19 (emphasis added). Similarly, the Special Referee relied on Mr. Hardister's testimony "that Heritage had no *intent* to harm the homeowners." *Id.* at 20 (emphasis added). Likewise, the Special Referee erroneously stated "[i]t is the *intent*, not the foreseeability that determines the application of exclusion 'a'" and that "there is nothing in the record that indicates the insureds *intended* to injure the plaintiffs or *intended* its subcontractors to perform negligently." *Id.* at 21-22 (emphasis added).

[15] Specifically, the clause excluded coverage for injury "'resulting from intentional acts or directions of you or any insured. The expected or unexpected results or (sic) these acts or directions are not covered.'" *Dawsey*, 371 S.C. at 355, 638 S.E.2d at 104.

In contrast, courts specifically considering the "expected or intended" exclusion have recognized the term "expected" is broader than the term "intended," and that an "expected or intended" exclusion is broader than the type of exclusion at issue in *Dawsey*. *See Mut. Serv. Cas. Ins. Co. v. Country Life Ins. Co.*, 859 F.2d 548, 552 (7th Cir. 1988) ("[E]ven where the damages are not accomplished by design or plan (not intended), they may be of such a nature that they should have been reasonably anticipated (expected) by the insured. [] This Court recently noted that an exclusion for 'intended' or 'expected' damages would be significantly broader than an exclusion for damages caused intentionally by or at the direction of the insured.") (citations and internal quotation marks omitted); *Allstate Ins. Co. v. Lahoud*, 605 S.E.2d 180, 183 (N.C. Ct. App. 2004) (noting an "expected or intended" exclusion is broader than an exclusion of only "intentional" acts); *Auto-Owners Ins. Co. v. Harrington*, 565 N.W.2d 839, 842 (Mich. 1997) ("In this case, the policy's use of the word 'expected' broadens the scope of the exclusion because 'expected' injuries are the 'natural, foreseeable, expected, and anticipated result of an intentional act.'") (citation omitted).

Here, even if it were unclear whether the insureds *intended* to cause damage, there can be no question that they *expected* the damages that occurred. *See* Underlying Mag. North Trial Tr. at 887 (Transcript of video deposition of Gwyn Hardister of April 15, 2009) (testimony of Mr. Hardister that "*before* they started Magnolia North," the developer had received complaints of water intrusion and window leaks at its prior condominium complexes containing construction defects "practically identical" to the construction practices that were later used at Magnolia North); Underlying Riverwalk Trial Tr. at 846-49, 852-89 (evidence from a similar, nearly contemporaneous suit that

during the construction of Magnolia North a representative from Betterbilt windows met with insureds and explained the insureds' window installation practices were causing the water intrusion problems and if those installation practice continued, the windows would leak and cause damages). Where an insured has advance notice of an issue, the insured "necessarily anticipated or expected any damage" that subsequently occurs. *Dunes W. Residential Props. v. Essex Ins. Co.*, No. 06-2020, 2007 U.S. App. Lexis 29931 (4th Cir. Dec. 28, 2007) (applying South Carolina law).

These damages were the natural, foreseeable, expected, results of their conduct. The association argues it is irrelevant whether the wrongdoer foresaw or should have foreseen the results of his acts. *See* Association's Response Brief at 31-32. Although South Carolina courts have not previously considered whether a foreseen or foreseeable injury is "expected,"[16] other courts analyzing this exclusion have expressly held that it applies where the damage was foreseeable or foreseen. *See* Harleysville's Opening

---

[16] Contrary to the association's assertion, the Court in *Auto-Owners Ins. Co. v. Newman* did not reject a foreseeability test. *See* Association's Response Brief at 31. Rather, *Newman* simply held that in the absence of any evidence the insured expected the damages, the "expected or intended" exclusion did not apply. *Newman*, 385 S.C. 187, 197, 684 S.E.2d 541, 546 (2009). The association fails to note *Newman's* only mention of foreseeability is when it cited with approval a case from Tennessee, which holds that a court *should* consider foreseeability to determine coverage under a CGL policy. *Id.* at 194, 684 S.E.2d at 545 (citing *Travelers Indem. Co. of Am. v. Moore & Assocs.*, 216 S.W.3d 302, 309 (Tenn. 2007)).

Similarly, the association is incorrect when it says South Carolina courts have long rejected foreseeability as the test for determining whether an "expected or intended" exclusion applied. *See* Association's Response Brief at 32. The sole case cited by the association—*Stevenson v. Conn. Gen. Life Ins. Co.*, 265 S.C. 348, 218 S.E.2d 427 (1975)—does not involve an "expected or intended" exclusion. Rather, it involved the question of whether burns suffered by the insured were covered at all by the policy despite the fact that a reasonable man might have foreseen that walking barefoot on a hot surface could lead to injury. The *Stevenson* Court held that the appropriate question is not whether an objective man might have foreseen the injury, but whether *the insured* foresaw or expected the injury. *Stevenson*, 265 S.C. at 353-54, 218 S.E.2d at 430 (holding that the question of whether an injury was an accident was "not to be determined in terms of whether it was reasonably foreseeable, but in terms of whether it occurred with his intent or volition; *whether it was an event which he actually expected or anticipated* as a result of walking on the boat deck") (emphasis added).

Brief at 28 n.29 (compiling cases); *see also Auto-Owners Ins. Co. v. Harrington*, 565 N.W.2d 839, 842 (Mich. 1997) (noting that "'expected' injuries are the 'natural, foreseeable, expected, and anticipated result of an intentional act.'") (citation omitted).

B. The punitive damages were, by definition, awarded for conduct that was expected or intended.

As previously explained by Harleysville, the punitive damages awarded by the underlying jury—as a matter of law and in light of the underlying jury charge—were necessarily premised on the jury's finding that Harleysville's insureds engaged in conscious wrongdoing. *See* Harleysville's Opening Brief at 31-32. The association's argument in response is easily put to rest. The association argues that punitive damages may be awarded not only for intentional wrongdoing but also for reckless conduct. *See* Association's Response Brief at 41.[17] The association's argument, however, fails to recognize that, as a matter of law, conduct that is sufficiently reckless to warrant punitive damages necessarily contains an element of intent. *Carter v. R.L. Jordan Oil Co., Inc.*, 301 S.C. 84, 86, 390 S.E.2d 367, 368 (Ct. App. 1990) ("'Conduct is wilful, wanton, or reckless *when it is committed with a deliberate intention* under such circumstances that a person of ordinary prudence would be conscious of it as an invasion of another's rights. *It is the present consciousness of wrongdoing that justifies the assessment of punitive damages* against the tortfeasor'") (quoting *Cohen v. Allendale Coca-Cola Bottling Co.*, 291 S.C. 35, 351 S.E.2d 897 (Ct. App. 1986)) (emphasis added); *Bussey v. Charleston & W. Carolina R. Co.*, 75 S.C. 116, 129, 55

[17] In addition, the association asserts that nothing in the policy excludes punitive damages and that Mr. Wright supposedly conceded that punitive damages may be covered. *See* Association's Response Brief at 41. This assertion is correct only insofar as the policy has no exclusion that expressly excludes punitive damages and insofar as Mr. Wright stated there was no such explicit exclusion.

S.E. 163, 167 (1906) (noting that recklessness warranting punitive damages "*is the equivalent of willfulness or intentional wrong.*") (citation omitted; emphasis added).

Indeed, even the case the association cites notes that conduct warranting punitive damages must be so reckless as to take the nature of a willful act. *Anderson v. Atl. Coast Line R. Co.*, 179 S.C. 367, 184 S.E. 164, 166 (1936) ("[N]egligence may be so gross as to amount to recklessness, but, when it does, *it ceases to be mere negligence, and assumes very much the nature of willfulness.*") (emphasis added).

VI. Coverage of the underlying damages is barred by the policies' "faulty work" exclusion.

In its opening brief, Harleysville explained that the Special Referee erred when he ruled that the underlying damages are covered despite the fact that each policy contains an exclusion "j(5)" for damage to any piece of real property on which the insured or its subcontractors performed operations which resulted in damage to that property. *See* Harleysville's Opening Brief at 33-35. In response, the association cites a recent opinion in which our Supreme Court held "that the temporal limits of the exclusion are coterminous with the performance of the acts." *Bennett & Bennett Const., Inc. v. Auto Owners Ins. Co.*, 405 S.C. 1, 747 S.E.2d 426 (2013). The Supreme Court's ruling in *Bennett* largely forecloses portions of Harleysville's prior argument regarding exclusion j(5). Nevertheless, the interpretation of the exclusion adopted in *Bennett* highlights the internal inconsistency of the Special Referee's ruling in this regard.

Specifically, when discussing "time on risk," the Special Referee found that the progressive damages began to occur on *all* the buildings 30 days after the certificate of

occupancy was issued on the *first* building completed by Harleysville's insureds. Mag. North Order at 42-43. At the time of the first certificate of occupancy, however, the vast majority of the other buildings in the complex were still being built.[18] Accordingly, the Special Referee ruled that damages were occurring to buildings during the time in which the insureds or their subcontractors were performing work. If this is correct, then under *Bennett* the majority of the underlying damages are barred by exclusion j(5).

The association cannot have it both ways, arguing one thing when discussing "time on risk" and arguing the opposite when discussing exclusion j(5). Either all damages began on a single date before most of the buildings were built (in fact not possible), or the damages to each building began on a date specific to that building's completion. If the former is correct, then the Special Referee erred by failing to rule that exclusion j(5) excludes coverage for the majority of the damages. Alternatively, if latter is correct, then the Special Referee erred by failing to apply "time on risk" on a per building basis.

VII. The Special Referee made improper and prejudicial findings of fact.

In its opening brief, Harleysville explained that the Special Referee erred in his findings regarding Harleysville's reservation of the right to contest coverage, Harleysville's decision to forgo a needless and futile attempt to intervene in the underlying suit, and Harleysville's correct interpretation of the then existing law

[18] The Special Referee determined that damages began to occur on January 10, 1998. Mag. North Order at 42-43. Of the 21 buildings at the Magnolia North complex, 15 of them were not completed until September 17, 1999. *See* "Magnolia North Data" attached to Harleysville's proposed order submitted to the Special Referee. Accordingly, the Special Referee in effect ruled that in 15 of 21 buildings, the damages were occurring during their construction.

regarding allocation. *See* Harleysville's Opening Brief at 36-42. The only assertions raised by the association that warrant response are briefly rebutted below.

First, the association asserts that the Special Referee's erroneous findings regarding Harleysville's reservation of rights were not prejudicial. *See* Association's Response Brief at 44. The prejudice of the erroneous findings was that the Special Referee concluded "that Harleysville's actions constitute an implied waiver of Harleysville's right to contest coverage in this action." Mag. North Order at 41 (citation omitted). In addition, the prejudice is evident by the fact that the association relies on the supposed inadequacy of Harleysville's reservations of rights to argue that the verdict is not subject to allocation. *See* Association's Response Brief at 55.

Next, the association asserts the Special Referee's finding that Harleysville failed to reserve its rights cannot be disturbed if that finding is supported by any evidence, and that Harleysville's failure to produce a letter sent to one insured constitutes such evidence. *See* Association's Response Brief at 45-46. However, the problem with the Special Referee's finding was that it was *contradicted* by the evidence and was incorrect as a matter of law. *See* Harleysville's Opening Brief at 37-39 (explaining that Harleysville repeatedly and clearly explained to its insureds Harleysville's reservation of its rights).[19]

In addition, the association asserts that the contents of Harleysville's reservation of rights letters were insufficient and that Harleysville should have intervened in the underlying suit. *See* Association's Response Brief at 46-50. The legal and factual

[19] Even assuming *arguendo* the absence of the letter creates an evidentiary inference that it never existed, Harleysville's oral reservation of rights was sufficient and effective. *See* Harleysville's Opening Brief at 49 n.36 and accompanying text (compiling cases).

sufficiency of Harleysville's letters is thoroughly established in Harleysville's prior briefing and need not be repeated here, *see* Harleysville's Opening Brief at 47-56, as has the futility and needlessness of intervention, *see id.* at 8-11; *see also supra* at 3-4.

VIII. The Special Referee erred by excluding relevant, admissible evidence and testimony.

Harleysville explained in its opening brief that the Special Referee made numerous evidentiary rulings. *See* Harleysville's Opening Brief at 42-47. In response the association argues the Special Referee's rulings were correct. Several of the association's arguments merit reply and are easily rebutted.

First, the association wrongly asserts "Harleysville conceded that there is no method to determine how the jury allocated damages." Association's Response Brief at 50 n.19. Harleysville made no such concession. Rather, it repeatedly argued to the Special Referee and this Court that it is possible to accurately allocate the underlying damages. *See* Harleysville's Pre-Trial Brief at 20-36; Trial Tr., December 13-14, 2010, at 235-53; Harleysville's Motion for Judgment and Directed Verdict at 3; Harleysville's proposed Order at 23-30; Harleysville's Motion to Vacate, Alter, or Amend at 5; Harleysville's Opening Brief at 5-18. The fact that a lay witness stated in a deposition that he was personally unsure how the underlying jury awarded damages is hardly a concession of this issue of law and legal theory. *See Linder v. Ins. Claims Consultants, Inc.*, 348 S.C. 477, 489, 560 S.E.2d 612, 618-19 (2002) (recognizing that lay persons like insurance employees are not expected to understand or decide issues of abstract legal principles or trial strategy) (citing *Dauphin Cnty. Bar Ass'n v. Mazzacaro*, 351 A.2d 229, 233-34 (Pa. 1976)).

Second, the association states Harleysville was not prejudiced by the Special Referee's ruling excluding testimony that Harleysville met with its insureds to discuss its coverage concerns and to reserve the right to contest coverage in a subsequent action. *See* Association's Response Brief at 51 ("Harleysville failed to point out any prejudice resulting from this ruling.") (citation omitted). The prejudice of these rulings is that in conjunction with the Special Referee's erroneous legal analysis, *see* Part IX, *infra*, they led the Special Referee to incorrectly conclude that Harleysville failed to reserve its right to contest coverage. *See* Mag. North Order at 41.

Third, the association states that it was harmless error for the Special Referee to exclude testimony of Harleysville's discussions and agreement with its insured prior to the underlying trials to defer resolution of the coverage dispute until after trial. See Association's Response Brief at 52. Specifically, the association asserts this error was harmless because the "same testimony was allowed on cross examination." *Id.* This is incorrect because the testimony allowed on cross examination was not the same. The testimony excluded by the Special Referee described meetings that occurred *before* the underlying trial. (*See* Trial Tr. of December 13-14, 2010 at 113 (noting that in discussion with the insureds, "the idea was to go into the trials in lockstep" together and defer coverage dispute until later).) The testimony later elicited on cross-examination describes discussions after the lawsuit in which Harleysville reiterated its position there was no coverage. (*See id.* at 180.) This error was not harmless. As noted above, this erroneous ruling, in conjunction with the Special Referee's erroneous legal analysis, *see* Part IX, *infra*, led the Special Referee to incorrectly conclude that Harleysville failed to reserve its right to contest coverage. *See* Mag. North Order at 41.

IX. Harleysville adequately reserved its right to contest coverage.

In its opening brief, Harleysville explained that the Special Referee incorrectly ruled that Harleysville failed to reserve its right to contest coverage. *See* Harleysville's Opening Brief at 47-58. In response, the association concedes that the "real issue" is not whether every insured received a reservation of rights letter but argues that Harleysville, in its oral or written reservations of rights, was obliged to advise its insureds of a conflict of interest and the supposed need for an allocated verdict. *See* Association's Response Brief at 54. South Carolina's courts have never mandated the contents of a reservation of rights letter or conversation, but other jurisdictions to consider this question have *not* required that an insurer's reservation of rights inform the insured of any supposed conflict of interest. *See* Harleysville's Opening Brief at 51-52 (compiling authorities). Indeed, the very existence of a reservation of rights letter implicitly notifies the insured of any conflict. *Britt v. Cambridge Mut. Fire Ins. Co.*, 717 S.W.2d 476, 481 (Tex. Ct. App. 1986). As to the allocated verdict, as explained repeatedly in Harleysville's prior briefing, there was no need for Harleysville to advise its insureds they should request an allocated verdict because, *inter alia*, at that time, under South Carolina law, *all* the underlying damages were covered.

In addition, the association argues that a stranger to the insurance contract, such as the association, may raise and rely on supposed deficiencies in the insurer's dealings with its insureds. *See* Association's Response Brief at 55-56. The association relies on a significantly distinguishable case—*Canadian Ins. Co. of Canada v. Rusty's Island Chip Co.*, 36 Cal. App. 4th 491 (Cal. Ct. App. 1995)—for the proposition that a party

injured by an insured has standing to litigate coverage issues such as an insurer's reservation of rights. The critical difference between that case and the case at bar, however, is that in *Canadian*, the court's holding was expressly premised on the fact that a California statute made the underlying injured party a third party beneficiary of the insurance contract between the insurer and the insured, and thereby permitted the injured party to enforce those promises made for his benefit. *Canadian*, 36 Cal. App. 4th at 497 (relying on Cal. Ins. Code § 11580 (b)(2)). In contrast to this California statute, South Carolina's courts have stated that an injured person is a stranger to the insurance contract and has no right to enforce it or rely on its breach. *See, e.g., Auto-Owners Ins. Co. v. Rhodes*, 405 S.C. 584, 598, 748 S.E.2d 781, 788 (2013) (citing *Young v. Smith*, 168 S.C. 362, 167 S.E. 669 (1933) for the proposition that "no privity of contract exists between an insurance company and a third party who may benefit from indemnification unless the insurance contract specifically lists the third party as a beneficiary"); *Trancik v. USAA Ins. Co.*, 354 S.C. 594, 554-55, 581 S.E.2d 858, 861 (Ct. App. 2003) (holding an injured party "does not have a contractual relationship with the insurer and cannot maintain an action against the insurer for breach of the insurance contract"); *see also* Harleysville's Opening Brief at 57-58 (compiling cases).

X. The Special Referee erred by refusing to consider Harleysville's Motion for Judgment.

The Special Referee denied its motion for judgment based on his erroneous belief that motions for judgment are inapplicable in a non-jury setting. *See* Harleysville's Opening Brief at 58-59. In response, the Association does not dispute that Harleysville is correct regarding the applicability of motions for judgment in a

bench trial pursuant to Rule 41, SCRCP. Rather, the association merely argues that the Special Referee's erroneous denial of the motion should be excused because Harleysville's Motion for Judgment was inadvertently titled as a Rule 50 or 56 motion rather than as a motion pursuant to Rule 41. *See* Association's Response Brief at 56-57. The association's argument places form over substance and ignores the fact that courts should and do apply the proper law to an incorrectly captioned motion. *See*, *e.g.*, *Ducworth v. Neely*, 319 S.C. 158 n.1, 459 S.E.2d 896 n.1 (Ct. App. 1995) (noting that an incorrectly captioned motion was actually a motion pursuant to Rule 41(b), SCRCP, and therefore reviewing it as such).

XI. This Court should recompute the damages amount for which Harleysville is responsible by applying the correct law.

Assuming some of the the underlying damages are covered and not excluded by the policies, this Court should apply the proper law regarding allocation and "time on risk" and should thus recompute the amount for which Harleysville is responsible. In the underlying trial, the association was awarded a verdict of $6,968,936.85.[20] *See* Mag. North Order at 3. According to the Special Referee, Harleysville is responsible for $2,766,954. After correcting the Special Referee's errors, several options for this Court's recalculation of damages are explained below. The below options assume the exclusion-based arguments of Harleysville are not adopted by this Court. Should they be, which Harleysville urges, this Court can easily adjust the judgment accordingly.

First, after allocating the actual damages, applying "time on risk" to the covered actual damages on a per-building basis, and applying "time on risk" to the underlying

[20] This amount includes actual damages, after set off, of $4,968,936.85 and punitive damages of $2,000,000. Mag. North Order at 3.

punitive damages, Harleysville would be liable for **$1,157,244.45**. This result is calculated as follows. As explained in the bench trial, only 32.93% of the underlying actual damages are covered, *see* Harleysville's Opening Brief at 4-5, bringing the covered amount of actual damages to $1,609,438.65. When this amount is subject to a per-building "time on risk" formula, it is reduced to $446,044.45:

Bld.	"Start date" (CO + 30)[21]	Days of coverage[22]	Days of damages[23]	Multiplier[24]	Damage per building[25]	Covered damages
1	1/10/1999	691	1943	.3556	$76,639.94	$27,253.16
2	1/10/1999	691	1943	.3556	$76,639.94	$27,253.16
3	1/17/1999	684	1936	.3533	$76,639.94	$27,076.89
4	1/15/1999	682	1938	.3519	$76,639.94	$26,969.59
5	1/22/1999	679	1931	.3516	$76,639.94	$26,946.60
6	2/22/1999	648	1900	.3411	$76,639.94	$26,141.88
7	10/17/1999	411	1663	.2471	$76,639.94	$18,937.73
8	3/19/1999	623	1875	.3323	$76,639.94	$25,467.45
9	5/1/1999	580	1832	.3166	$76,639.94	$24,264.21
10	6/12/1999	538	1790	.3006	$76,639.94	$23,037.97
11	12/4/1999	363	1615	.2248	$76,639.94	$17,228.66
12	12/5/1999	362	1614	.2243	$76,639.94	$17,190.34
13	11/8/1999	389	1641	.2371	$76,639.94	$18,171.33
14	12/22/1999	345	1597	.2160	$76,639.94	$16,554.23
15	1/29/2000	307	1559	.1969	$76,639.94	$15,090.40
16	1/23/2000	313	1565	.2000	$76,639.94	$15,327.99
17	2/14/1999	656	1908	.3438	$76,639.94	$26,348.81
18	1/29/2000	307	1559	.1969	$76,639.94	$15,090.40

[21] These dates are taken from Harleysville's chart "Magnolia North Data," an attachment to its proposed order. Although that chart lists data for all 23 buildings at Magnolia North, Harleysville's insureds built only 21 of them. (*See* Trial Tr. of Dec. 13-14, 2010 at 93.)

[22] The Special Referee ruled that the applicable insurance policies expired on November 30, 2000. (*See* Magnolia North Order at 43.) Accordingly, each building was covered from its "start date" through November 30, 2000.

[23] The Special Referee ruled that the water damage at Magnolia North effectively concluded on May 5, 2004. (*See* Magnolia North Order at 43-44.) Accordingly, the damages to each building occurred between its "start date" and May 5, 2004.

[24] The multiplier is calculated by dividing the days of coverage by the days of damages. It reflects the portion of time Harleysville's policies were in effect during the period of time in which the damages were occurring.

[25] The actual damages, after set-off, not including punitive damages and loss of use damages, and after allocation are $1,609,438.65. Divided among the 21 buildings at Magnolia North, the actual damages amount to $76,639.94 per building.

19	7/29/1999	491	1743	.2817	$76,639.94	$21,589.47
20	1/30/2000	306	1558	.1964	$76,639.94	$15,052.08
21	1/30/2000	306	1558	.1964	$76,639.94	$15,052.08
					Total:	**$446,044.45**

The Court would then apply "time on risk" to the underlying punitive damages, yielding a punitive damage amount of $711,200.[26] Taken together, as noted above, after allocating and applying per-building "time on risk" to the actual damages and applying "time on risk" to the punitive damages, Harleysville is responsible for $1,157,244.45.

Even if this Court declines to allocate the underlying damages, the per-building "time on risk" calculation reduces the underlying actual damages award to $1,377,105.41, *see* Harleysville's Opening Brief at 17, and the application of "time on risk" to the punitive damages reduces that amount to $711,200, *see* note 28, *supra* and accompanying text. Accordingly, Harleysville would be responsible for **$2,088,305.41**.

Finally, even if allocation is not warranted and "time on risk" is not applied per-building or to punitive damages, the remaining aspects of the Special Referee's "time on risk" calculation—*i.e.*, that it applies to the covered damages and his chosen "end date" of damages—are correct, and the association is not entitled to the inflated amount it seeks in its cross-appeal. *See generally* Harleysville's Response Brief (refuting the association's arguments on appeal seeking to enlarge the amount of its recovery).

Conclusion

For the foregoing reasons, this Court should reverse the judgment of the Special Referee in the various respects noted herein and either eliminate or reduce the amount

[26] The longest time period of Harleysville's coverage was for the first building built, where Harleysville covered 691 of the 1943 days in which damage occurred. *See* Magnolia North Order at 43. Accordingly, Harleysville's "time on risk" is calculated by multiplying the damage amount by .3556.

of Harleysville's liability in accordance with its holdings or alternatively remand for further proceedings consistent with such an opinion.

NELSON MULLINS RILEY & SCARBOROUGH LLP

By: _____

C. Mitchell Brown
SC Bar No. 012872
E-Mail: mitch.brown@nelsonmullins.com
William C. Wood, Jr.
SC Bar No. 015111
E-Mail: bill.wood@nelsonmullins.com
A. Mattison Bogan
SC Bar No. 72629
E-Mail: matt.bogan@nelsonmullins.com
Miles E. Coleman
SC Bar No. 78264
E-Mail: miles.coleman@nelsonmullins.com
1320 Main Street / 17th Floor
Post Office Box 11070 (29211-1070)
Columbia, SC 29201
(803) 799-2000

Robert C. Calamari
SC Bar No. 064985
E-Mail: bob.calamari@nelsonmullins.com
3751 Robert M. Grissom Parkway / Suite 300
Post Office Box 3939 (29578-3939)
Myrtle Beach, SC 29577-3165
(843) 448-3500

Attorneys for Appellant

Columbia, South Carolina
January 30, 2014

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. 2009-CP-26-11862
Appellate Case No. 2013-001281

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

v.

Heritage Communities, Inc., a South Carolina corporation; Heritage Magnolia North, Inc., a South Carolina corporation; Buildstar Corporation, a South Carolina corporation; Magnolia North Horizontal Property Regime; Magnolia North Property Owners Association, Inc., a South Carolina corporation, and National Surety Corp.,..... Defendants.

Of whom Heritage Communities, Inc., a South Carolina corporation; Heritage Magnolia North, Inc., a South Carolina corporation; and National Surety Corp. are ..... Respondents,

And Magnolia North Horizontal Property Regime and Magnolia North Property Owners Assoc., Inc., a South Carolina corporation are ..... Respondents/Appellants.

PROOF OF SERVICE

I, the undersigned Administrative Assistant of the law offices of Nelson Mullins Riley & Scarborough LLP, attorneys for Appellant, do hereby certify that I have served all counsel in this action with a copy of the pleading(s) hereinbelow specified by mailing a copy of the same by United States Mail, postage prepaid, to the following address(es):

Pleadings:

Initial Reply Brief of Appellant/Respondent

Counsel Served:

John P. Henry, Esquire
Philip C. Thompson, Esquire
Thompson & Henry
1300 Second Avenue, 3rd Floor
Conway, SC 29528

Laura Johnson Evans, Esquire
Smith Moore Leatherwood, LLP
25 Calhoun Street, Suite 250
Charleston, SC 29401

Karin McCarthy, Esquire
Rivkin Radler
926 RXR Plaza
Uniondale, NY 11556

Lisa P. Whitehurst
Lisa P. Whitehurst
Administrative Assistant

January 30, 2014