THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

Mikell R. Scarborough, Master in Equity

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SC Court of Appeals

Case No. 2016-CP-10-1143
[Appellate Case No. 2016-002308]

Palmetto Construction Group, LLC — Respondent

v.

Restoration Specialists, LLC,
Reuben Mark Ward, and
Lynnette Pennington Ward — Appellants

REPLY BRIEF OF APPELLANTS

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I. BECAUSE GOOD CAUSE EXISTS FOR RELIEF FROM THE ENTRY OF DEFAULT, THE COURT ERRED WHEN IT DENIED APPELLANTS' MOTION TO SET ASIDE ENTRY OF DEFAULT.[1]

[1] Respondent continues to cite facts in its Pleadings and Motions without "references to the transcript, pleadings, orders, exhibits or other materials which may be properly included in the Record on Appeal". (SCRAP 208(B)(4). Accordingly, Appellants contend that facts presented without citation should not be considered in the Court of Appeal's analysis of this appeal.

(A): The Master's Orders Denying Appellants' Motions To Stay And To Compel Arbitration Are Immediately Appealable.

The Appellants have appealed the Master's Orders dated July 14, 2016 and October 28, 2016. The Master's July 14, 2016 Order ruled, in part, that "Defendants' motion to stay and to compel arbitration is denied as Defendant is in Default." The Master's October 28, 2016 Order ruled that "the affirmative defense of arbitration has been waived and Defendant's Motion to Stay and Compel filed July 11, 2016 was not properly made." As such, both orders refuse to stay this action and deny Appellants' application and rights to compel arbitration. The Master's orders refusing to stay this litigation and denying Appellants' application and rights to compel arbitration are immediately appealable under both federal and state law.

Under federal law, an order that favors litigation over arbitration—whether it refuses to stay the litigation in deference to arbitration or refuses to compel arbitration—is immediately appealable, even if interlocutory in nature. *See* 9 U.S.C. §16(a)(1); *Stedor Enter., Ltd. v. Armtex, Inc.*, 947 F. 2d 727 (4th Cir. 1991). Likewise, under state law an order denying an application to compel arbitration is immediately appealable. S.C. Code Ann. §15-48-200(a)(1); *Cape Romain Contractors, Inc. v. Wando E, LLC,* 405 S.C. 115, 747 S.E. 2d (2013); *Towles v. United Healthcare Corp.*, S.C. 29, 524 S.E. 2d 839 (Ct. App. 1999). Also, an order finding that a party waived its right to compel arbitration is immediately appealable. *Liberty Builders, Inc. v. Horton*, 336 S.C. 658, 521 S.E. 2d 749 (Ct. App. 1999).

The Court of Appeals expressly affirmed these principles allowing for immediate appeal of the Master's orders in its previous order denying Respondent's motion to dismiss. (R.p. 8). In addition, the Master's orders are immediately appealable in that they deny the Appellants the right to arbitration and, therefore, affect a substantial right of the Appellants. An order denying a party a mode of trial to which he is entitled is immediately appealable. S.C. Code Ann. §14-3-330 (2); *Lester v. Dawson*, 327 S.C. 263, 491 S.E. 2d 240 (1997); *Widdicombe v. Tucker-Cales*, 366 S.C. 75; 620 S.E. 2d 333 (Ct. App. 2005). Such orders must be appealed immediately

and cannot be challenged in an appeal from final judgment. *Id.*

(B): The Master's Orders Denying Appellants' Application To Compel Arbitration Are Immediately Appealable And, Therefore, The Master's Entire Orders Should Be Considered On Appeal.

Where there is a single order that is appealable in part, the entire order should be considered upon the appeal. *See Rice Hope Plantation v. South Carolina Pub. Serv. Auth.*, 216 S.C. 500, 59 S.E. 2d 132 (1950); overruled on other grounds, *Mcall v. Batson*, 285 S.C. 243, 329 S.E. 2d 741 (1985).

Ordinarily, an order denying a motion to lift entry of default is interlocutory and not immediately appealable. *Thynes v. Lloyd*, 294 S.C. 152, 363 S.E. 2d (Ct. App. 1987). An order that is not immediately appealable, however, will be considered if there is another appealable issue before the court. *Cox v. Woodmen of the World Ins. Co.*, 347 S.C. 460, 556 S.E. 2d 397 (Ct. App. 2001). In the present case, the appealable issues of the Master's refusal to stay this action and the denial of Appellants' applications and rights to compel arbitration is squarely before this court. Therefore, the entire orders of the Master, including the Master's denial of Appellants' Motion to Lift Entry of Default, should be considered upon appeal. *Id.* Furthermore, a decision by the Court of Appeals on the Master's entire orders will best serve the interests of judicial economy and eliminate the inevitable additional appeals which would arise from a piecemeal appellate review of the Master's orders. *See Laffitte v. Bridgestone Corp.*, 381 S.C. 460, 674 S.E. 2d 154 (2009); *Southern Bell Tel. and Tel. Co. v. Hamm*, 306 S.C. 70, 409 S.E. 2d 775 (11991); *Widdicombe v. Tucker-Cales,* 366 S.C. 75, 620 S.E. 2d 333 (Ct. App. 2005); *Pruitt v. Bowers*, 330 S.C. 483, 499 S.E. 2d 250 (Ct. App. 1998).

(C): The Master Had Jurisdiction To Enter An Order On Appellants' Rule 59(e) Motion.

The Respondent asserts that the Master had no jurisdiction to enter an order on Appellants' Rule 59(e) motion and that Appellants' appeal constitutes a "misuse of process." Brief of Respondent, Section V.A.1. The record refutes Respondent's statement.

The Appellants requested and the Master initially agreed to hear Appellants' Rule 59(e), SCRCP motion prior to the damages hearing. Brief of Appellants, Statement of the Case (p. 8, line 15 – p. 9, line 7). The Master reversed his decision to hear Appellants' Rule 59(e) motion first ***only*** after Respondent notified the Master of its preference to proceed with the damages hearing prior to any hearing on the Rule 59(e) motion. *Id.* The Master's decision to proceed with the damages hearing before hearing the Rule 59(e) motion effectively denied this motion as proceeding with the damages hearing would severely prejudice, and potentially force a waiver of Appellants' rights to arbitration and foreclose any appeal therefrom. Therefore, subject to, without waiving and fully reserving their rights to arbitration, the Appellants served and filed a notice of appeal from the Master's "effective" denial of Appellants' Rule 59(e) motion on September 30, 2016. (R.pp. 496-500; R.p. 7).

Thereafter, in ruling on the Respondent's motion to dismiss the appeal, the Court of Appeals held that "because the master discussed the Rule 59(e) motion during the [October 4, 2016] hearing, accepted memoranda regarding the motion, and allowed the parties to proffer information relating to the motion, it appears the master intends to issue a final, written order on the Rule 59(e) motion." (R.p. 7, lines 2-6). Accordingly, the Court of Appeals expressly acknowledged the Master's jurisdiction over Appellants' Rule 59(e) motion and dismissed the initial appeal **without prejudice**. In its Order, the Court of Appeals further affirmed Appellants' right to appeal within ten days after the Master's order disposing of the Rule 59(e) motion. (R. p. 7, lines 7-12). Indeed, the Master did issue his written order denying Appellants' Rule 59(e) motion and Appellants timely appealed consistent with the Order of the Court of Appeals and the South Carolina Appellate Court Rules. The Appellants good faith compliance with the appellate court's order and rules and non-wavering assertion of their right to arbitration do not constitute a misuse of process.

(D): The Appellants Are Entitled to Mandatory Mediation/Arbitration Of This Matter and Have Meritorious Defenses To The Plaintiff's Lawsuit.

The Appellants are entitled to the substantial right to mediation/arbitration of the claims in Respondent's lawsuit for the reasons set forth in the Brief of Appellants, Arguments Section II. In addition, the Appellants have asserted the further substantive defenses to Respondent's claims discussed below:

(1): **Overpayment to PCG**: Respondent admits by footnote 1 in Section V.C.2.b. of its Brief that Appellants' claim of overpayment is a meritorious defense when they indicate it is a set-off that is a proper subject of a damages hearing.

Respondent has relied on documents it prepared for use at the damages hearing to support its claim that it is owed $184,858.69. (Brief of Respondent, Section V.C.2.b.). Appellants maintain that these documents are not properly in the record on the grounds set forth in Appellants' Motion to Exclude and Strike. (R.pp. 377-394; R.pp. 395-457). Reviewing the document prepared by Respondent that makes this calculation, Respondent has apparently relied on all project costs it incurred that are listed in its "Job Cost and Billing Detail" report which is attached thereto. (Brief of Respondent, Section V.C.2.b.). Accordingly, Respondent is treating the Subcontract as a "cost plus" subcontract rather than a firm fixed price subcontract. However, by the express terms of §10.1 of the Subcontract, this is a firm fixed price contract; specifically, "The Contractor shall pay the Subcontractor in current funds for performance of the Subcontract the Subcontract Sum of One million eighty two thousand three hundred forty two dollars and 10/100, ($1,082.342.10)..." (R.p. 27, lines 18-19). There were no modifications to the Subcontract. Appellants agree that payments in the amount of $1,096,569.19 have been made; accordingly, Respondent has been overpaid by $14,227.09.

(2): **No Profit Sharing:** Regardless of what Respondent indicates may have been contemplated by the Teaming Agreement, per its express language, which both Appellants and Respondent quote in their initial briefs, the Teaming Agreement did not allow profit sharing.

Concerning the allegation that the Subcontract contains a profit sharing agreement, the original

Complaint in this case did not include the attachment that Respondent is now relying upon. Further, no other documents in the record at the time of submission of the Motion to Lift Entry of Default or at the time of submission of the Motion to Stay and Compel Arbitration which are the subject matter of this appeal included the document that Respondent is relying upon concerning profit sharing. The Appellants' position opposing the admission of documents in the possession of Respondent during the October 4, 2016 hearing (including the attachment to the Subcontract that mentions profit-sharing) into the record on appeal remains unchanged from that stated in Appellant's Motion to Exclude and Strike.

Assuming, *arguendo*, that the alleged attachment to the subcontract is in the record and that profits are to be shared, that document expressly indicates that profits are "projected" and "to be determined". Appellants have indicated that the project remains active with major rework and warranty work continuing, some directly attributable to Respondent. (R.p. 475, Tr. p. 30, line 21 – p. 31 line 6); accordingly, a set-off is due for those expenses, and profits, if any, cannot yet be determined. Respondent has also breached various terms of the subcontract related to overhead and supervision which has resulted in additional expense to Appellant Restoration Specialists for which they seek a set-off.

Finally, Respondent admits by footnote 2 in Section V.C.2.c. of its Brief that Appellants' position related to profit sharing is a meritorious defense when they indicate it is a set-off that is a proper subject of a damages hearing.

(3): **Merit of Subcontractors' Claims:** Appellants have and still contend that the surety, Hanover, has overpaid many bond claimants, failed to notify Appellant Restoration Specialists of the majority of the claims, failed to provide Affidavits of Claims for all but one claim, and failed to allow Appellants to participate in claim review prior to payments being made. (R.p. 475, Tr. p. 30, lines 10-21). In fact, Appellants contend that more than half of the payments made by Hanover exceeded what is due those claimants.

Respondent alleges that "this is not a defense to [Respondent's] claim' and that "Appellants had no defenses to the subcontractors' claims". Both of these statements are patently untrue. Per the express language of Respondent's Complaint under its cause of action for "Breach of Agreements", it alleges that, "[a]s a consequence of [Appellant Restoration Specialists'] default under its agreements with [Respondent] Palmetto and other subcontractors [for failure to pay], [Respondent] Palmetto has been damaged..." Respondent is attempting to sue Appellant Restoration Specialists for nonpayment under subcontracts with others. Clearly, overpayment of those subcontractors by Hanover is a defense to that allegation. Concerning the statement that "Appellants had no defenses to the subcontractors' claims", Respondent has cited an email chain related to a **single** claimant to support that premise, and has ignored Appellant Restoration Specialists' continued position that more than half of the claimants have been overpaid.

(4): **VA Final Payment:** Respondent continues to treat this project as complete and tries to singularly rationalize why each defense is not valid without consideration of that defense in concert with others. Here, Respondent computes numbers it believes shows that monies received under the contract "should have been more than enough to pay all the subcontractors in full and produce a profit of $226,092.67." [By footnote 4, they allege to have computed the project profit to total $443,460.91. (Brief of Respondent, Footnote 4.)] Here, Respondent has failed to consider, *inter alia*, that: (1) substantial rework and warranty work is ongoing, including rework attributable to Respondent's defective work, (2) Appellant Restoration Specialists has claimed set-offs for Respondent's breach of contract, (3) profitability cannot be considered until the project work is complete, and (4) that pursuant to the express terms of paragraph 20 of the indemnity agreement, the indemnitors waived and subordinated all rights of indemnity, subrogation, and contribution each against the other until all obligations to the Surety have been first satisfied in full. (Items 1, 2 and 3 were all discussed in the paragraphs above.)

(5): **Waiver of Consequential Loss:** Respondent has alleged breach of contract against Appellant Restoration Specialists for alleged breach of its subcontract with Respondent as well as subcontracts with other subcontractors. Insomuch as Respondent has no privity related to subcontracts between Appellant Restoration Specialists and its other subcontractors, Respondent cannot claim that these are purely contract damages. Respondent has now, in its initial brief, alleged breach of the indemnity agreement for the **first time**, something that was not alleged in its original complaint.

Respondent also ignores paragraph 20 of the Indemnity Agreement which indicates that the indemnitors waive and subordinate all rights of indemnity, subrogation, and contribution against each other until all obligations to the Surety have been first satisfied in full. Article 9 of the Teaming Agreement cited in Section V.C.2.f. of Respondent's Brief indeed applies to any damages claimed by Respondent other than those alleged that are related to its subcontract with Appellant Restoration Specialists.

The existence of any one of the above-enumerated defenses satisfies the meritorious defense element of Rule 55(c), SCRCP.

II. BECAUSE THE CONTRACT CONTAINS MANDATORY MEDIATION/ARBITRATION PROVISIONS AND THE APPELLANTS HAVE NOT DEFAULTED UPON NOR WAIVED THEIR RIGHTS TO MEDIATION/ARBITRATION, THE COURT ERRED WHEN IT FAILED TO STAY THIS ACTION AND COMPEL MEDIATION/ARBITRATION.

(A): The Respondent's Claims Against the Ward Appellants Relate To and Are Intertwined With The Subcontract And, Therefore, Are Subject To Arbitration.

The Respondent asserts that its claims against the Ward Appellants are not intertwined or interwoven with the Subcontract between Appellant Restoration Specialists and Respondent and are not subject to arbitration. The Respondent's assertion is expressly refuted by the language of the alternative dispute resolution provisions in the Subcontract Agreement. Section 6.1.1 and 6.2 of the Subcontract read as follows:

"**[a]ny claim arising out of or related to this Subcontract, except those waived in this**

Subcontract, shall be subject to mediation as a condition precedent to binding dispute resolution (emphasis added)." Section 6.1.1.

"**any claim subject to but not resolved by mediation shall be resolved by binding arbitration (emphasis added)"** pursuant to Section 6.3 of the agreement. Section 6.2.

These are not narrow arbitration clauses requiring only the arbitration of claims arising under the Subcontract. *See Prima Paint Corp. v. Flood & Conklin Mfg. Co.,* 388 U.S. 395, 87 S.Ct. 1801, 18 L.Ed. 2d 1270 (1967); *American Recovery Corp. v. Computerized Thermal Imaging, Inc.,* 96 F. 3d 88 (4th Cir. 1996). In contrast, these are broad arbitration provisions not limiting arbitration to the literal interpretation or performance of the contract, but embrace disputes having a relationship to the contract regardless of the label attached to the dispute. *See Id.* Respondent's own statements and allegations clearly assert actions by the Ward Appellants which relate to and are intertwined with the Subcontract and which Respondent alleges give rise to liability on the part of the Ward Appellants. While Appellants would dispute many of these allegations, the summary below is a sampling of Respondent's own statements and allegations contradicting Respondent's assertion that the claims against the Ward Appellants are not intertwined and, thus not arbitrable:

(1): Mr. Ward of Restoration Specialists approached PCG about working on the VA project as a concrete subcontractor, as well as in a supervisory capacity. Further, Mr. Ward indicated that Restoration Specialists was unable to secure the sizable bond the VA Project required, and asked that PCG obtain the bond from its surety, Hanover. PCG agreed and a subcontract was entered into between Restoration Specialists and PCG dated September 10, 2014. (Subcontract) (Initial Brief of Respondent, p. 3, lines 15-20);

(2): Per the subcontract agreement between Restoration Specialists and PCG, PCG agreed to aid Restoration Specialists in obtaining the bond. (Initial Brief of Respondent, p. 3, lines 20-22 & p. 4, lines 1-2).

(3): PCG's surety, Hanover, did issue the payment and performance bond for the project, Bond No. 9000-0045. (Bond). However, Hanover required that both PCG and Restoration Specialists, as well as their respective principals and their spouses sign an indemnity agreement, requiring them to indemnify Hanover for any sums it expends in paying claims made on the bond. (Indemnity Agreement). (Initial Brief of Respondent, p. 4, lines 5-9).

(4): Claims have been made by other subcontractors upon the Payment Bond and as a consequence subcontractors are making claims against Palmetto and its surety. Palmetto, Restoration, and individually, Mr. Ward and Mrs. Ward, all signed an indemnity agreement

with a surety in relation to a Payment Bond for this project (Exhibit C). Accordingly, Restoration, Mr. Ward and Mrs. Ward must indemnify the surety and Plaintiffs to the extent that they are required to pay. (R.p. 13, lines 12-17).

(5): Mr. Ward represented that he would manage this project and that all monies from the project would be used to pay for material and work supplied to or performed on the project. Mr. Ward has a pecuniary interest in the project. The representations of Mr. Ward were material and were relied upon by Palmetto. Mr. Ward intended and induced Palmetto to rely upon his representations. Mr. Ward is personally liable for his own tortious conduct. Palmetto's justifiable reliance upon Mr. Ward has damaged Palmetto. (R.p. 14, lines 6-12).

(6): All Defendants are contractually bound to pay funds if there are claims on the surety bond. There are claims on the surety bond. (R.p. 15, lines 4-5).

(7): Hanover made a demand under its indemnity agreement and upon the VA for the contract balance but by this time Mr. Ward had collected all but $90,000 of the $8.1 Million contract. (Initial Brief of Respondent, p. 4, lines 17-19).

(8): PCG sued all Appellants for actual and constructive fraud and negligent misrepresentation regarding the Appellants' misappropriation of funds paid to them by the VA, which resulted in over $1.4 Million in claims by subcontractors on the payment bond. (Initial Brief of Respondent, p. 5, lines 2-5).

As a whole, these disputed allegations clearly establish that the parties' dealings, the subcontract, the indemnity agreement and Respondent's claims against the Ward Appellants arising therefrom are all related to and intertwined with the subcontract as part and parcel of the VA Project.

In addition to asserting these allegations, the Respondent filed a Motion to Stay and Compel mediation/arbitration at the commencement of suit. The Respondent did not carve out the claims against the Ward Appellants as being independent of the Subcontract and not subject to arbitration. To the absolute contrary, the Respondent demanded that **all claims in this action, including Respondent's claims against the Ward Appellants, be stayed and compelled to mediation, and if necessary, to arbitration.**

Based on the above, as well as the additional authorities cited in Section II. (C) of the Brief of Appellants, all of the Appellants, including the Ward Appellants, have standing to enforce the mandatory mediation/arbitration provisions. Accordingly, all of the Appellants, including the Ward Appellants, are entitled to an order compelling mediation/arbitration of the Respondent's

claims in this action.

(B): The Defendants Have Not Defaulted Upon Nor Waived Their Right To Mediation/Arbitration Under The Mandatory Alternative Dispute Resolution Provisions Of The Contract And Applicable Law.

(1): The Master's Ruling That The Right To Arbitration Is An Affirmative Defense Which Has Been Waived By Appellants Constitutes An Error Of Law And Should Be Reversed.

Respondent asserts that arbitration is an affirmative defense that is waived if not pled. Respondent first cites Rule 8(c) SCRCP in support of this proposition. As briefed in the Brief of Appellants, the specific defense of "arbitration and award" contained in Rule 8(c) does not apply in this case. Brief of Appellants, Section II.(E)(1).

Likewise, the umbrella provision requiring the affirmative pleading of any other matter constituting an avoidance does not apply. In order to constitute an avoidance, the matter pled must assert facts and arguments that, if true, will defeat the plaintiff's claim, even if all the allegations in the complaint are true. *Black's Law Dictionary* 482 (9th ed. 2009). The right to arbitration as a mode of trial is certainly a substantial right of a party to litigation. Consequently, the denial of the right to arbitration is immediately appealable and must be immediately appealed by the aggrieved party. However, pleading a right to arbitration under an arbitration agreement does not constitute the assertion of facts and arguments that, if true, will defeat the plaintiff's claim, even if the allegations in the complaint are true. Therefore, the right to arbitration under an arbitration agreement does not constitute an affirmative defense under the umbrella provision of Rule 8(c).

The Respondent next asserts that South Carolina and federal courts have consistently held that arbitration is an affirmative defense that is waived if not pled. The Brief of Appellants addresses the majority of the cases cited by Respondent in arguing this proposition. A review of the remaining cases cited by Respondent establishes that these cases are distinguishable and inapposite to the arbitration issues before this court:

(1): *General Star Nat'l Ins. Cp. v. Administratia Asigurarilor de Stat*, 289 F. 3d 434 (6th Cir. 2002) – This is an opinion issued by the United States Court of Appeals, Sixth Circuit on appeal from the United States District for the Southern District of Ohio. The court applied Sixth Circuit federal law in finding that the Defendant waived its right to arbitration due to its extreme delay in asserting the right to arbitrate and the prejudice incurred by the Plaintiff. *Id.* Specifically, the Defendant did not assert its right to arbitration until 17 months after receiving notice of the lawsuit and 1 year after the entry of default judgment. The Plaintiff incurred the costs of the action for 17 months **before** the Defendant filed its application for arbitration. *Id.* The extreme delay and actual prejudice demonstrated during the period before Defendant applied for arbitration in *General Star Nat'l Ins. Cp.* are in stark contrast to the short delay and lack of prejudice in the present case.[2] See Initial Brief of Appellants, Sections I.(E) and (G) and II.(E)(3).

(2): *Johnson Associates Corp. v. HL Operating Corp.*, 680 F. 3d 713 (6th Cir. 2012) – This is another distinguishable Sixth Circuit case in which the court states the Sixth Circuit standard for waiver of an agreement to arbitrate as follows: "A party may waive an agreement to arbitrate by engaging in two courses of conduct: (1) taking actions that are completely inconsistent with any reliance on an arbitration agreement; and (2) delaying its assertion to such an extent that the opposing party incurs actual prejudice." *Id*, at 717 (6th Cir. 2012).

As an initial matter, the *Johnson* Court expressly rejected the "substantial invocation of the litigation process" analysis relied on by Defendant in light of the "completely inconsistent" actions test employed in the Sixth Circuit. *Id*, at 718 (6th Cir. 2012). The "substantial invocation of the litigation process" standard rejected by the *Johnson* Court is similar to the waiver

[2] Appellants addressed Respondent's original claims of prejudice in their Brief of Appellants, Section I.(G). Respondent's Final Brief alleges three new prejudices, specifically, 1) it is nearing bankruptcy, 2) it now has incurred legal fees related to this appeal, and 3) the first appeal of Appellants related to this case was dismissed. All of these allegations are unsworn assertions by Respondent's counsel, lack legal citation and fail to satisfy the standards for legal prejudice in South Carolina.

standard applied in the state and federal courts in South Carolina. Thus, the first element of the Sixth Circuit waiver standard is distinguishable from the South Carolina standard. Secondly, in analyzing the prejudice element of the Sixth Circuit standard of waiver, the *Johnson* Court found the Plaintiff had suffered actual prejudice based on the totality of the following facts:

(a): Defendant delayed 8 months from the date suit commenced before asserting the right to arbitration; (b): Defendant filed an answer and counterclaim; (c): the parties engaged in court case management and judicial settlement conferences, held settlement discussions, and exchanged multiple settlement offers with the assistance of a magistrate judge before the filing of Defendant's motion for arbitration; (d): the defendant, both unilaterally and jointly with plaintiffs, filed multiple motions to continue trial, extend discovery and modify the case management order prior to filing its motion for arbitration; (e) the defendant served plaintiff with interrogatories, requests to produce and requests for admission and noticed 8 depositions prior to filing its motion for arbitration; (f) the plaintiffs served defendant with discovery requests prior to the filing of defendant's motion for arbitration; (g): the plaintiffs served defendant with discovery responses (including 1151 pages of responsive documents and a 4.11 gigabyte hard-drive containing responsive information) prior to the filing of defendant's motion for arbitration; (h) defendant served discovery responses on plaintiffs and continued to seek discovery from plaintiffs while defendant's motion to compel arbitration remained pending. Clearly, the *Johnson* defendant's delay and involvement in the litigation process prior to asserting a right to arbitration are totally distinguishable from the actions of the Appellants herein. *See* Brief of Appellants, Sections I.(E) and (G) and II.(E)(3).

Thirdly, the *Johnson* Court's reliance on the defense of arbitration in a defendant's answer as providing notice to a plaintiff of the defendant's desire to arbitrate is irrelevant to the present case. The *Johnson* plaintiff did not move for arbitration and their first notice of any arbitration issue was by way of the defendant's motion to compel arbitration filed 8 months after commencement of suit. In the present case, the Respondent was already on notice of the arbitration agreement at the time it commenced suit as it filed its very own Motion to Stay and Compel mediation/arbitration at the time it commenced suit. Accordingly, it certainly had notice of the arbitration agreement and cannot be prejudiced by Appellants application for arbitration.

(3): *Doubleday & Company, Inc. v. Curtis*, 763 F. 2d 495 (2nd Cir. 1985) – This is a federal opinion issued by the United States Court of Appeals, Second Circuit on appeal from the United States District Court for the Southern District of New York. The *Doubleday* case arises out of

a book publishing dispute, applies federal procedural law and New York substantive law, and involves the affirmative defense of waiver. This case does not in any way involve issues of arbitration.

(4): *American Recovery Corp. v. Computerized Thermal Imaging, Inc.*, 96 F. 3d (4th Cir. 1996) – This is a federal opinion issued by the United States Court of Appeals, Fourth Circuit on appeal from the United States District Court for the Eastern District of Virginia. The *American Recovery* Court held that the Plaintiff's claims against the defendant were arbitrable inasmuch as:

(a): Plaintiff's claims related to the parties' agreement containing the arbitration provision and (b): Plaintiff failed to carry its burden of proving that defendant's actions constituted a default of its right to arbitrate under the Federal Arbitration Act.

The *American Recovery* opinion establishes that a party's failure to raise arbitration as an affirmative defense alone is insufficient to waive the right of arbitration in the Fourth Circuit. *Id.* Instead, it requires sufficient delay and significant utilization of the litigation machinery by the party asserting the right to arbitration and legally sufficient prejudice to the opposing party to constitute waiver/default of a right to arbitration. *Id.*

(2): Applying The Proper Legal Standard To The Facts Of This Case Establishes Appellants Have Not Waived Nor Defaulted Upon Their Right To Mandatory Mediation/Arbitration.

The proper legal standards are set forth in the Brief of Appellants, Section II.(E)(2). Respondent attempts to argue against these standards by alleging that Appellants waived any rights to arbitration by participating in litigation in the lower court. Brief of Respondent, Section V.D.4. The record belies the merits of this assertion, however, as Appellants' limited activities in the lower court do not rise to the level necessary to constitute a waiver of the right to arbitration. Brief of Appellants, Section II.(E)(3).

Respondent also argues that Appellants have waived any rights to arbitration by committing acts inconsistent with their arbitration rights. As legal precedent for this argument, Respondent

cites *Brown v. Dillard's, Inc.*, 430 F.3d 1004 (9th Cir. 2005) and *DeLage Linden Fin. Services, Inc. v. Raynes, McCarty, Binder, Ross and* Mundy, 51 Pa. D. & C. 4th 57 (Pa. Com. Pl. 2001). The Respondent cites *Brown* for the proposition that a party who is in material breach of an arbitration agreement (e.g., by refusing to arbitrate) is in default of that right and cannot compel arbitration. The *Brown* case, however, is distinguishable both on a legal and factual basis. In *Brown*, the plaintiff was an employee of Dillard's department store until she was fired from her job. The plaintiff filed a pre-litigation notice of intent to arbitrate a wrongful termination claim under Dillard's Fairness in Action Program. Dillard's refused to participate in the pre-suit arbitration proceedings. After Dillard's refused to arbitrate her claim, the plaintiff filed suit in state court for wrongful termination. At that point, Dillard's decided it wanted to arbitrate plaintiff's claim. Therefore, Dillard's removed plaintiff's suit to federal court and moved to compel arbitration. Based on these facts, the Ninth Circuit held that:

> "when an employer enters into an arbitration agreement with its employees, it must itself participate in properly initiated arbitration proceedings or forego its right to compel arbitration. That is, we hold that Dillard's cannot compel Brown to honor an arbitration agreement of which it is itself in material breach." *Id* at 1006.

The facts and legal holdings in the *Brown* case are clearly distinguishable and inapposite to the present case.

Likewise, the *DeLage* case is equally distinguishable and non-dispositive of the arbitration issues on appeal before this court. The *DeLage* order is not an appellate decision. The opinion is a trial court order issued by the Court of Common Pleas of Pennsylvania, Philadelphia County. First, the *DeLage* case is a Pennsylvania case distinguishable on the same grounds as the previous Pennsylvania cases reviewed in Section II.B. of Appellants' Initial Reply Brief herein. Secondly, in *DeLage*, neither the plaintiff nor third party defendant asserted the right to arbitration. The third-party defendant, Sharp, also never raised an arbitration defense by way of preliminary objections or in answer and new matter. *Id* at 3. Instead, Sharp engaged in the judicial process and served discovery upon third party plaintiff, IKON, which IKON responded

to. *Id.* It was only when IKON served discovery on Sharp that Sharp first objected to the trial court's jurisdiction some two and a half months later.

The Respondent makes the following factual assertions for its argument that Appellants waived their rights to arbitration by acting inconsistently therewith:

(a): No motion or request was made by Appellants to invoke the arbitration provision in Appellants motion for continuance or motion to be relieved from default filed before the June 6, 2016 court hearing. Initial Brief of Respondent, p. 5, lines 15-18.

(b): The Appellants did not raise the issue of arbitration at the June 6, 2016 court hearing. Initial Brief of Respondent, p. 5, lines 20-21.

(c): It was only after the Court indicated that the motion to be relieved from default may not be granted that Appellants moved to compel arbitration. Initial Brief of Respondent, p. 23, lines 12-14.

(d): Appellants only sought to compel arbitration after they were unsuccessful before the Master. Initial Brief of Respondent, p. 29, lines 2-3.

(e): Appellants ignored Respondent's pleadings and failed to respond and consent to Respondent's motion to stay and compel arbitration, thereby refusing to arbitrate. Initial Brief of Respondent, p. 24, lines 13-15.

The Respondent's assertions are manifestly incorrect, grossly distort the record, and cannot serve as the basis for a finding of waiver.

The Respondent's Summons and Complaint contains no allegations whatsoever concerning the application of mandatory mediation/arbitration provisions to the Respondent's claims. Therefore, the Appellants' failure to timely respond to these pleadings due to an unintentional and good faith misunderstanding does not constitute a refusal to arbitrate.

The Respondent's Motion to Stay and Compel did contain such allegations and expressly demanded a stay of the lawsuit and submission of Respondent's claims to mandatory mediation/arbitration. Appellants were justified in relying on Respondent's assertion that it was moving the court for an order staying the matter and compelling mandatory mediation/arbitration.

Furthermore, the South Carolina Rules of Civil Procedure did not require a responsive pleading

to Respondent's Motion to Stay and Compel. As such, the Appellants were fully within their rights: (a): simply not to contest the Respondent's Motion to Stay and Compel and await the court's order compelling arbitration or (b): to appear and state their position on mediation/arbitration at the hearing on Respondent's motion. The Appellants, however, never received the opportunity for hearing to which they were entitled due to the administrative "closure" of Respondent's motion and the Master's adjudication of the motion on that basis. Accordingly, the Appellants' failure to respond to Respondent's Motion to Stay and Compel does not constitute a refusal to arbitrate.

As the record reflects, the Appellants were unaware of the default status of the case and the scheduling of the damages hearing until they received the damages hearing notice on June 2, 2016. (R.pp. 72-73). Appellants immediately retained legal counsel on June 3, 2016. (*Id).* Appellants' counsel immediately filed a Motion for Continuance of the damages hearing and a Motion to Set Aside Entry of Default on June 3, 2016 citing the mandatory mediation/arbitration provisions and Respondent's Motion to Stay and Compel mediation/arbitration as one of Appellants' grounds for relief. (R.pp. 77-81; R.pp. 82-87). The Appellants understood that Respondent's Motion to Stay and Compel mediation/arbitration remained pending for decision by the court at this time. (R.p. 79, line 18 – p. 80, line 2).

The Appellants' counsel next raised and again put the court on notice of the application of the contractual mandatory mediation/arbitration provisions at the June 6, 2016 court hearing. (R. p. 465, Tr. p. 8, lines 4-8). The Master expressly acknowledged Appellants' counsel's comments and the existence of the mandatory mediation/arbitration provision. (R.p. 466, Tr. p. 12, lines 10-17). In fact, Respondent acknowledged mediation was required and requested the Court's assistance during that hearing, "if we need to go to mediation. (R.p. 465, Tr. p. 7, lines 4 – 9.)

Thereafter, the Appellants again asserted their right to arbitration and joined in Respondent's

Motion to Stay and Compel by virtue of Appellants' Motion to Stay and to Compel mediation/arbitration filed July 11, 2106. (R.pp. 88-93).

The parties reconvened before the Master on July 14, 2016. Appellants also filed a memorandum in support of Appellants' Motion to Lift Entry of Default that date. (R.pp. 94-124). Appellants' supporting memorandum included their continuing invocation of the right to arbitration, coupled with their demand for stay of this action and submission of the matter to mandatory mediation/arbitration. (R.p. 97, lines 15-20; R.pp. 94-124).

Finally, the Appellants timely filed a Motion to and to Alter and Amend the Master's orders pursuant to SCRCP 59(e) again demanding that this action be stayed and compelled to mandatory mediation/arbitration. (R.pp. 125-129).

The Appellants actions described above show the Appellants' vigorous efforts to assert their right to mandatory mediation/arbitration early, often and continuously in the lower court. Appellants' actions were absolutely consistent with their right to arbitration and do not constitute a refusal or waiver of the right to arbitrate.

(3): The Entry Of Default Does Not Constitute A Default Or Waiver Of Appellants' Right To Mandatory Mediation/Arbitration.

The Respondent asserts that the Appellants have waived their right to compel arbitration by virtue of the entry of default in this case. The Brief of Appellants addresses the majority of the cases cited by Respondent in arguing this proposition. A review below of the remaining cases cited in Respondent's Brief establishes that these cases are distinguishable and inapposite to the arbitration issues before this court:

(1): *Bland v. Green Acres Group, L.L.C.*, 12 So. 3d 822 (Fla. App. 2009) – This is a Florida case applying Florida waiver of arbitration standards, not the state or federal law standards applied in South Carolina. The legal standards and factual circumstances involved in the *Bland* case are significantly different than those in the present case. Even so, the *Bland* Court looked to the totality of the circumstances, not just the entry of default to determine the issue of waiver.

In the *Bland* case, the plaintiff sued the defendant for breach of contract in March 2005, but then dismissed its case without prejudice in August 2007. The plaintiff refiled its case in August 2007 and the court entered default in October 2007. In December 2007, the plaintiff moved for default final judgment. Unlike in the present case, the *Bland* plaintiff did not at any time during these two lawsuits file a motion to compel arbitration. On July 29, 2008, defendant served a Motion to Stay and to Compel Arbitration asking, for the first time, that the dispute be resolved in arbitration. On August 8, 2008, the trial court denied the motion to compel arbitration, finding that defendant had waived the contract's arbitration clause. The *Bland* Court ruled that a finding of waiver may be predicated on both pre- and post-suit actions in tandem. *Id* at 825. Applying this standard to the facts of the case, the *Bland* Court then reviewed the pre and post-suit filing actions of the defendant to determine if his actions were sufficient to waive arbitration. The *Bland* Court found that:

> "the trial court heard evidence that [defendant] knew of the 2005 suit no later than March of 2006; actively avoided service; never sought to trigger the mediation pre-condition to arbitration; never made a demand to arbitrate under Fla. Stat. § 684.22(1); waited eleven months after learning suit had been refiled and over seven months after appearing to seek to compel arbitration; and engaged in settlement negotiations for years without raising the arbitration clause." *Id* at 825.

The *Bland* Court determined that the above actions were sufficient to waive arbitration. *Id.* In doing so, the *Bland* Court looked beyond the singular fact of the entry of default and found that the totality of defendant's actions constituted waiver of the right to arbitration. Clearly, the legal standards and facts dispositive of the *Bland* case are distinguishable from the present case. *See* Brief of Appellants.

(2): *Bojadzijev v. Roanoke Technology Corp.*, 997 So. 2d 1251 (Fla. App. 2009) - Like the *Bland* case, this is a Florida case applying Florida waiver of arbitration standards, not the state or federal law standards applied in South Carolina. Again, the legal standards and factual circumstances involved in the *Bojadzijev* case are distinguishable from the present case. And again, even so, the *Bojadzijev* Court looked to the totality of the circumstances to find waiver.

In *Bojadzijev*, the plaintiff filed a breach of contract action against the defendant and did not at any time during the lawsuit file a motion to compel arbitration. After obtaining an entry of default against defendant, the plaintiff filed a motion for default final judgment in excess of six million dollars. A hearing was held on plaintiff's motion and the trial court entered a default final judgment for the full amount of damages sought. Months later, the defendant filed a motion to be relieved from default judgment which the trial court denied. The *Bojadzijev* Court upheld the trial court and affirmed the default judgment. The distinguishing elements of the *Bojadzijev* case are numerous and significant; namely:

(1): The *Bojadzijev* plaintiff never filed a motion to compel arbitration – In the present case, the Respondent did file such a motion with the trial court, was on full notice of the arbitration agreement and expressly requested arbitration. Furthermore, Appellants relied upon and joined in Respondent's motion but were deprived of the opportunity to be heard on that motion due to the Clerk's administrative "closure" of this motion and the Master's "adjudication" of this motion on that basis; (2): In *Bojadzijev*, a default judgment had been entered and the court applied the Florida equivalent of the higher Rule 60, SCRCP "excusable neglect" standard – In the present case, there is no default judgment – instead, there is an entry of default subject to the lower "good cause" standard (3): The *Bojadzijev* defendant did not file a motion to compel arbitration until "months" after a default judgment had been entered.The *Bojadzijev* Court found that, by doing so, the defendant acted inconsistently with any arbitration right and failed to raise the arbitration issue in a timely motion to compel arbitration – In the present case, the Appellants filed timely motions to lift the entry of default and applications for arbitration pursuant to state and federal law applicable in South Carolina. *See* Brief of Appellants, Sections I.(E) and (G) and II.(E)(3).

(3): *Samuel J. Marrance General Contracting Co., Inc. v. Amerimar Cherry Hill Associates Ltd. Partnership*, 416 Pa. Super. 45, 610 A. 2d 499 (Pa. Super., 1992) *citing Foster v. Philadelphia Manufacturers*, 140 Pa. Cmwith 186, 592 A. 2d 131 (1991) – These are Pennsylvania cases applying Pennsylvania waiver of arbitration standards, not the state or federal law standards applied in South Carolina. These cases do not involve defendants held in default. The legal standards and factual circumstances involved in these cases are significantly different than those on appeal before this Court. Also, the defendants in these cases had not been held in default by the lower court.

In the *Foster* case the trial court had not entered default against the defendant. Furthermore,

the *Foster* Court actually upheld the defendant's right to arbitration, dismissed the Plaintiff's complaint and referred the matter to arbitration.

In the *Samuel J. Marrance* case the lower court had not entered default against the defendant. The *Samuel J. Marrance* Court articulated the Pennsylvania waiver standard as follows:

"[w]aiver may be established [in Pennsylvania] by a party's express declaration or by a party's undisputed acts or language so inconsistent with a purpose to stand on the contract provisions as to leave no opportunity for a reasonable inference to the contrary. See 17A Am.Jur.2d, Contracts §656." *Id* at 501.

Applying this waiver standard the *Samuel J. Marrance* Court looked to the totality of the circumstances, not just the defendant's failure to plead arbitration as an affirmative defense to determine waiver. Based on the following facts, the *Samuel J. Marrance* Court held that defendant's conduct constituted waiver:

(a): defendant chose not to file a petition to compel arbitration; (b): defendant elected not to assert arbitration as an affirmative defense either in preliminary objections or in new matter as required by Pennsylvania Rule of Civil Procedures 1030 and 1032; (c): defendant filed pretrial motions for improper venue and forum non-conveniens; (d): defendant's venue motions unequivocally established a willingness on defendant's part to litigate the case without arbitration in another jurisdiction; (d): defendant waited until it had received an adverse lower court ruling on its venue motions before invoking and seeking to enforce the arbitration provision of the contract; and (e): defendant initiated other proceedings in different jurisdictions regarding matters related to the contract.

The *Samuel J. Marrance* Court held that the above facts constituted waiver of defendant's right to arbitration. The court's holding established that the singular fact of the failure to plead arbitration as an affirmative defense was not dispositive. Instead, it was the totality of the defendant's actions that "amounted" to waiver in the eyes of the *Samuel J. Marrance* Court. *Id* at 501. Clearly, the legal standards and facts dispositive of the *Samuel J. Marrance* case are distinguishable from the present case. *See* Brief of Appellants.

(4): *Sigma Motors, Inc. v. Klien*, CA-CV 07-0831, 2008 WL 4853611 (Ariz. App. 1st Div. Nov. 6, 2008) – This is an Arizona case containing the Court of Appeals of Arizona specific legal precedent disclaimer notice. The notice states: "THIS DECISION DOES NOT CREATE LEGAL PRECEDENT AND MAY NOT BE CITED EXCEPT AS AUTHORIZED BY

APPLICABLE RULES." *Id* at 1. In addition to lacking precedential value on the issue of waiver in Arizona, much less South Carolina, the *Sigma Motors* opinion is distinguishable from the present case for the following reasons:

(a): The quotation the Respondent attributes to the Court of Appeals of Arizona is, in fact, the statement of the Arizona trial court from which the appeal was taken; (b): The case involved a default judgment governed by Rule 60 "excusable neglect" standards not simply Rule 55(c) "good cause" standards; (c): The *Sigma Motors* Court specifically stated in its opinion that it did not address "whether the [defendants] waived their right to arbitration." *Id* at 5.

(5): *Olde Discount Corp v. RCK Corp.*, Inc., 110 F.3d 69, 1997 WL 133239 (9th Cir. 1997). – This is a United States Court of Appeals, Ninth Circuit decision containing the Court of Appeals specific legal precedent disclaimer notice. The notice states that this opinion is not suitable for publication, is not precedential and may not be cited to or by the courts of the Ninth Circuit except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel. *Id* at 1. In addition to lacking precedential value on the issue of waiver in the Ninth Circuit, much less South Carolina or the Fourth Circuit, the *Olde Discount Corp.* opinion is distinguishable from the present case for the following reasons:

(a): The *Olde Discount Corp.* case is a securities fraud action – such actions are not subject to arbitration under federal securities laws; (b): The legal authority for the quotation relied upon by Respondent (i.e., *Conover v. Dean Witter Reynolds, Inc.*, 837 F.2d 867, 868 (9th Cir. 1988) is a comparative citation (Cf.) case in which the Dean Witter defendant waited almost 2 years from the date suit was filed to move for arbitration; (c): the court found that the default was due to defendant's own culpable conduct in refusing to accept personal service of the summons and complaint; (d): the plaintiff did not file a motion to compel arbitration; (e): the brief decision indicates that defendant first raised the issue of arbitration on appeal.

(6): *Cho Yang Shipping Co., Ltd. V. American Freight Lines, Ltd.*, No 94 Civ. 0347, 1994 WL 577006 (S.D.N.Y. Oct. 19, 1994) – This is a United States District, S.D. New York decision. The *Cho Yang Shipping* opinion does not apply the state or federal waiver standards applied in South Carolina. In addition, the *Cho Yang Shipping* decision is distinguishable from the present case for the following reasons:

(a): the plaintiff did not file a motion to compel arbitration; (b): the defendant did not file a motion to compel arbitration; (c): the defendant first raised the issue of arbitration as a challenge to the court's jurisdiction on appeal; (d): the *Cho Yang Shipping* case involved a default

judgment governed by Rule 60 standards not simply Rule 55(c) "good cause" standards. *Id.* Based on the above authorities, the entry of default against Appellants herein does not constitute a waive or default of Appellants' right to mandatory mediation/arbitration of the parties' disputes. In light of the applicable and well established standards discussed throughout the Brief of Appellants, the Court should reverse the Master's ruling, stay this action and compel the parties to mediate, and if necessary, arbitrate their disputes pursuant to their contractual agreement.

CONCLUSION

For the reasons stated above, this Court should reverse the rulings of the circuit court, lift the entry of default, stay this action and compel mandatory mediation/arbitration pursuant to the contractual agreement of the parties.

Respectfully submitted,

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September 26, 2017
Charleston, South Carolina

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

RECEIVED
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SC Court of Appeals

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

Mikell R. Scarborough, Master in Equity

Case No. 2016-CP-10-1143
[Appellate Case No. 2016-002308]

Palmetto Construction Group, LLC — Respondent

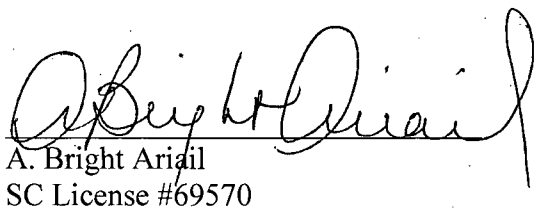
v.

Restoration Specialists, LLC,
Reuben Mark Ward, and
Lynnette Pennington Ward — Appellants

CERTIFICATE OF COUNSEL

The undersigned certified that this Final Reply Brief complies with Rule 211(b), SCACR.

September 26, 2017



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