THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM GEORGETOWN COUNTY
Court of Common Pleas
The Honorable Joe M. Crosby, Master-In-Equity

Case No. 2011-CP-22-0180
Appellate Case No. 2013-001447

Kennedy Funding, Inc. as predecessor-in-interest, and BNP Paribas.....Respondents,

v.

Pawleys Island North, LLC, Will Darwin Wheeler, Peggy Wheeler-Cribb, and J. Mars Sapp, Defendants,
of whom Pawleys Island North, LLC, Will Darwin Wheeler and Peggy Wheeler-Cribb are Respondents and

J. Mars Sapp is the .....Appellant.

REPLY BRIEF OF APPELLANT

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I. INTRODUCTION

This Court's Ultimate Decision. In this appeal the court will determine if a judgment creditor should be left with no remedy after his insolvent debtor fraudulently transferred unencumbered property to a fraudulent grantee which gave a mortgage on the property for new indebtedness to a lender who had knowledge of both the judgment creditor's claim, and the facts of the fraudulent transfer.

Appellant Sapp leased a commercial building in Surfside Beach to Wheeler's company in 1994. Wheeler guaranteed the lease. When the lease went into default, Sapp had the occupants evicted in the Magistrate's Court in 2008. On September 30, 2008 Sapp then sued Wheeler's company and Wheeler in the Court of Common Pleas for Georgetown County where Wheeler resides. The case was tried for three days resulting in a jury verdict for Sapp on June 4, 2010 (R. p. 713, line 1-p. 717, line 20; and Sapp's Exs 2–5, R. pp. 756–785).

After the verdict, Sapp sent a judgment execution to the Georgetown County Sheriff (Sapp Ex. 6, R. pp. 786, 787). The Sheriff returned the execution *nulla bona*, stating:

> Date: 4/11/11
> This is to certify that I am unable to find personal or real property to satisfy the within execution. I hereby Nulla Bona this execution.
> /s
> A. Lane Cribb
> Georgetown County, SC

While Sapp's suit was pending against Wheeler, Kennedy Funding assumed the risk of making a new non-purchase money loan, secured by the unencumbered Lot 3 and a partially encumbered Lot 4, when Kennedy had knowledge of the fraudulent transfer. Every lawyer and party involved in the transaction from Kennedy Funding and its two outside attorney firms and in-house counsel, to Wheeler, Wheeler-Cribb, and Pawleys and their attorney, knew that the Property with a value of $1,920,000 was being quitclaimed by Wheeler for no consideration,

knew that Wheeler had personally guaranteed a commercial lease which went into default, and knew that Wheeler was being sued by Sapp on the guaranty.

Sapp has taken all necessary and reasonable steps to secure and collect his judgment. He filed suit, his case came to trial in due course, and he secured a jury verdict on which judgment was entered. Despite following all the procedural rules of the court where it took 20 months to get to trial, prevailing on appeal, diligently searching for assets, and executing on his judgment, if the Kennedy mortgage has priority over Sapp's judgment lien, Sapp has no means of collecting his judgment against Wheeler.

Neither the applicable case law nor the equities of this case leave Sapp without a remedy. The fraudulently transferred property should be ordered sold in satisfaction of Sapp's judgment.

Respondents' Briefs and Facts. There are two sets of Respondents in this appeal: the first set includes Respondents Will D. Wheeler, Peggy Wheeler-Cribb, and Pawleys Island North, LLC. The second set of Respondents includes Kennedy Funding, Inc. and BNP Parabis. Each set of Respondents filed a Respondent's brief and this Reply Brief is Appellant Sapp's reply to both briefs.

The facts of this appeal are set forth in the Statement of the Case and Statement of Facts of Appellant Sapp's Brief. This brief introduction clarifies any additional facts included in Respondents' briefs. Defined terms in this brief are set forth in Appellant Sapp's Brief.

As to Sapp's motion to stay the sale of the property (Kennedy's Initial Brief, p. 4), a telephone hearing was conducted where the Master erroneously set the bond required to stay the sale, but the Master never entered a written order.[1] The Master stated he would file a written

[1] The Master set the bond at $1,825,935.53, the amount of the debt owed Kennedy by Pawleys and the Guarantors. To the extent that a bond was required to stay the sale, it should have been set in accordance with S.C. Code Ann. § 18-9-170 (1976). For unimproved land like that

order on Sapp's motion to stay the sale, and requested a proposed order from Kennedy's counsel which was provided. Kennedy and BNP proceeded with a foreclosure sale on August 5, 2013. Regardless, Sapp could not post a bond of over $1.8 million and he seeks to protect his interest in the property by the filing of a *lis pendens*. *See, Lebovitz v. Mudd,* 293 S.C. 49, 358 S.E.2d 698 (1987), holding that the filing of a *lis pendens* is proper pending appeal in a fraudulent conveyance case.

Prior to filing suit against Wheeler in September 2008, and prior to executing on his judgment, Sapp conducted a search of Wheeler's assets. He discovered that Wheeler owned four parcels of real property which are contiguous lots at Pawleys Island. Lots 1 and 2 were subject to existing mortgages, and they are in foreclosure. *Citibank v. Will D. Wheeler et al.,* 2012-CP-22-321. Prior to the Sapp/Wheeler Litigation, Lot 3 was not encumbered by any mortgage or judgment lien, and Lot 4 was encumbered by a $300,000.00 mortgage to First South Bank. While the Sapp/Wheeler Litigation was pending Wheeler fraudulently conveyed by quitclaim deed Lots 3 and 4 (the Property), and the fraudulent grantee Pawleys Island North, LLC ("Pawleys") gave Kennedy a mortgage on the Property. Prior to this loan and mortgage, there was no existing relationship between Wheeler and Pawleys with Kennedy, nor was there any indebtedness owed by Wheeler or Pawleys to Kennedy. Sapp did not locate any other property in his asset search on which to execute in Georgetown County, a fact confirmed by the *nulla bona* return of the execution (R. p. 719, line 1–p. 721, line 2; p. 724, line 21–p. 726, line 15).

To the extent that there might have been equity in the Property immediately after the Kennedy loan and mortgage transaction, there is none now with Kennedy's addition of interest at

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involved in this appeal, the statute requires a bond be set in relation to taxes on the property and interest on the debt, not the full amount of the debt.

25% and attorney's fees. In fact, after the foreclosure sale, a deficiency judgment of $352,790.61 was entered against Pawleys and the Guarantors.

II. STANDARD OF REVIEW

An action to establish lien priorities regarding property that is subject to a mortgage is an action in equity, as is an action to foreclose a mortgage. The appellate court's standard of review in equitable matters is its own view of the preponderance of the evidence. *Independence National Bank v. Buncombe Professional Park, LLC*, 402 S.C. 514, 741 S.E.2d 572 (Ct. App. 2013). Likewise, an action to set aside a conveyance under the Statute of Elizabeth is an equitable action. Sapp's initial burden was to prove a fraudulent conveyance by clear and convincing evidence, and a *de novo* standard of review applies.[2] *Oskin v. Johnson*, 400 S.C. 390, 735 S.E.2d 459 (2012). "An action to set aside a conveyance under the Statute of Elizabeth is an equitable action, and a de novo standard of review applies." *Id.* at 397, 735 S.E.2d at 463.

III. ARGUMENT

Respondents Kennedy and BNP misapprehend Sapp's brief and arguments, make inexplicable legal conclusions[3], and even assert the "parade of horribles" that mortgage lending in South Carolina would be eliminated if Sapp's arguments are upheld.

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[2] Respondents Kennedy and BNP incorrectly assert that Sapp contended that a preponderance of the evidence standard applies.

[3] For example, at pages 11–12 of their brief, they state that "This transaction [the loan and mortgage between Kennedy and Pawleys] cannot be set aside under the Statute of Elizabeth because no conveyance occurred." The statutory language and the case law make it clear that mortgages are subject to attack under the Statute of Elizabeth. *See, e.g., South Carolina Nat. Bank v. Halter*, 293 S.C. 121, 359 S.E.2d 74 (Ct. App. 1987). At page 26 of its brief, Kennedy incorrectly states that it made a purchase money mortgage to Pawleys. A purchase money mortgage is recognized where a purchaser of land, contemporaneous with the acquisition of the legal title or afterward, but as a part of the same transaction, executes a mortgage to secure the purchase money. *Hursey v. Hursey,* 284 S.C. 323, 327, 326 S.E.2d 178, 180 (Ct. App. 1985). Pawleys did not secure purchase money for the acquisition of the Property or either of the Lots. The property was transferred by quitclaim deed from Wheeler to Pawleys for "the sum of FIVE

A. The conveyance of the Property by Wheeler to Pawleys for "the sum of FIVE AND NO/100 DOLLARS ($5.00) and no other consideration" is a fraudulent conveyance.

In their Argument I, their lead argument, Kennedy and BNP (collectively "Kennedy" unless noted otherwise) inaccurately assert that Sapp argues that (1) the mortgage given to Kennedy should be set aside as fraudulent because it is not supported by consideration, or (2) there is no evidence Kennedy intended to defraud Sapp (Kennedy's Initial Brief, p. 11).

Kennedy misapprehends Sapp's argument so much that Kennedy's lead argument is really not responsive to Sapp's argument. Kennedy asserts that Sapp conflates a mortgage and a sales transaction, when, in fact, they are the ones who do just that, most likely to deflect attention from Wheeler's fraud. Without reference to the Kennedy mortgage transaction whatsoever, other than the fact the mortgage was recorded, Sapp clearly and convincingly sets forth at pages 8–17 of Appellant's Brief (Argument A), that the conveyance from Wheeler to Pawleys is fraudulent. Wheeler's fraudulent conveyance cannot stand on its own merit regardless of the Kennedy loan and mortgage transaction. In fact, assuming that the Kennedy mortgage was not on the Property, could anyone seriously argue that the transfer from Wheeler to Pawleys was not fraudulent? The Kennedy loan and mortgage are irrelevant to the fact that Wheeler fraudulently transferred the Property to Pawleys. The effect of that fraudulent conveyance and how Sapp's claim to the Property takes priority over the Kennedy mortgage are then explored beginning at page 18 in Arguments B and C of Appellant's Brief.

Examining the Wheeler transfer to Pawleys, it is fraudulent and should be set aside. Conveyances shall be set aside as fraudulent under the Statute of Elizabeth under two conditions:

AND NO/100 DOLLARS ($5.00) and no other consideration to the Grantor." Some loan proceeds were applied to pay off the First South mortgage, but the proceeds were not applied to purchase any of the Property from Wheeler. At page 19 of its brief, Kennedy classifies Wheeler's Answer to the Sapp's Cross-claim as evidence.

> First, where the transfer is made with the actual intent of defrauding his creditors where the intent is imputable to the grantee, even though there is a valuable consideration; and, second, where a transfer is made without actual intent to defraud the grantor's creditors, but without consideration.

Coleman v. Daniel, 261 S.C. 198, 208, 199 S.E.2d 74, 79 (1973).

1. Wheeler intended to defraud Sapp.

The evidence at trial clearly and convincingly established multiple badges of fraud by Wheeler which he failed to rebut.

> The idea of a badge of fraud is, that it furnishes a legal presumption of a fraudulent intention, which supersedes inquiry into the actual intention; and every badge of fraud is therefore evidence of a legal fraud, or fraud per se. It does not change the essential character of the presumption, that sometimes it may be rebutted, and sometimes not; for, until it is rebutted, the presumption remains, and whether rebutted or not, presents a question for the determination of the court, and not of the jury.

Dinkins v. Robbins, 200 S.C. 475, 21 S.E.2d 10, 16 (1942).

Some of the un-rebutted badges of fraud include: Wheeler's indebtedness to Sapp at the time of the transfer, the failure or lack of consideration for the transfer[4], the intra-family transfer (*Windsor Properties v. Dolphin Head Const. Co., Inc.*, 331 S.C. 466, 498 S.E.2d 858 (1998)), the filed and pending Sapp/Wheeler Litigation, the insolvency of Wheeler as a result of the transfer[5], and despite the formality of the limited liability company, Wheeler's retained use, possession, and development rights to the Property with his 99% interest in the company. These badges of fraud furnish "a legal presumption of fraudulent intention" and unless rebutted, which they were not, should not even create a question of fact. *Dinkins*.

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[4] Discussed more fully at Argument A.3, below.

[5] Discussed more fully at Argument A.4, below.

2. The fraudulent intent is imputable to Pawleys.

The badges of fraud created a presumption of fraud. It was incumbent then upon Wheeler and Pawleys to rebut that presumption. As a 99% owner of Pawleys, Wheeler's fraudulent intent is mirrored by and imputable to Pawleys. Wheeler's intent is imputable to the company in which he held a 99% interest, a fact never contradicted by Wheeler, Wheeler-Cribb, Pawleys, Kennedy or BNP. In fact, Kennedy acknowledges this legal conclusion in its brief when discussing *Coleman v. Daniel.*

> The property was, in essence, being held in the daughter and son-in-law's name for their father's perpetual use. Under these facts, the Court found the daughter and son-in-law's failure to inquire as to their father's indebtedness to plaintiff Coleman resulted in the knowledge of the debt imputed to them and voided the transfer as a fraudulent conveyance.

Kennedy's Initial Brief, pp. 12, 13.

Coleman holds:

> Actual knowledge of, or participation in, the debtor's fraudulent intention on the part of the transferee need not be established in order to justify a conclusion that the transaction was illegal. The transaction is subject to attack if at the time of the transfer the transferee had notice of circumstances which would arouse the suspicion of an ordinarily prudent man and cause him to make inquiry as to the purpose for which the transfer was being made, which would disclose the fraudulent intent of the maker.

261 S.C. at 201, 199 S.E.2d at 80.

Here, the Property was being held in Pawleys' name for Wheeler's continued development thereof, and Pawleys had actual knowledge of Wheeler's indebtedness to Sapp from its 99% member, Wheeler. The transferee, Pawleys, not only had notice of circumstances which would arouse suspicion of an ordinarily prudent person and cause it to make inquiry, but every lawyer and party involved in the overall transaction, including the transferee Pawleys, knew that the Property was being quitclaimed, knew that Wheeler was being sued by Sapp, knew

that Wheeler had personally guaranteed a lease which was in default, and knew that property valued at $1,920,000 was being conveyed for $5.00 and no other consideration. If ignorance did not save the fraudulent grantees in *Coleman*, certainly Pawleys' knowledge of the facts surrounding the conveyance would arouse suspicion, and requires the same conclusion – that Wheeler's intent is imputable to Pawleys.

3. Wheeler received no consideration for the transfer.

Despite Respondents' contentions to the contrary, Wheeler chose the quitclaim deed language of $5.00 and "**no other consideration**." Respondents now wish to unravel Wheeler's intentional use of this specific and unambiguous language, and contrive an argument of so-called consideration by referring to Wheeler's statement used to avoid paying deed stamps. They argue that Wheeler increased his interest in Pawleys by conveying the Property. Respondents' argument fails for at least three reasons.

a. The Court should have given effect to the deed language. Respondents argue that the court can ignore the deed and consider extrinsic evidence of consideration. In the absence of testimony from Wheeler or Pawleys, the best evidence of the consideration is the specific and unambiguous statement that there was NO CONSIDERATION other than a nominal $5.00 for the transfer. The deed did not state that the consideration was for an interest or increased interest in a business. It did not state that consideration was the assumption of any debt (which did not occur anyway). The deed stated the actual consideration, $5.00 and "no other." "The rule is that the intention of the parties is to be ascertained by considering all the provisions of the deed, as well as the situation of the parties, and then to give effect to such intention, if practicable, when not contrary to law." *First Carolinas Joint Stock Land Bank of*

Columbia v. Ford, 177 S.C. 40, 180 S.E. 562, 565 (1935). The deed reflects no other consideration, is the best evidence, and is conclusive on the subject.

b. The transfer did not increase the value of Wheeler's membership interest in Pawleys. Wheeler already had 100% interest in the property at its full value. Respondents' argument misses the point that the membership interest could be worth no more that the interest Wheeler already had so Wheeler received no benefit for the transfer. In fact, Wheeler lost value by the transfer and contemporaneous loan transaction. Respondents' argument fails to address that the Property was mortgaged for all obligations owed to Kennedy which subsequent events have shown those obligations to exceed the value of the property, so there was no increase in value of the membership interest. In short, Wheeler simply gave away the Property in exchange for nothing.

c. The transfer did not increase Wheeler's membership interest in Pawleys. The transfer of the Property to Pawleys did not increase Wheeler's membership interest in the limited liability company. Wheeler's interest in Pawleys was established on March 4, two months before he transferred the Property to Pawleys (See Pawley's Island North Operating Agreement, Kennedy Ex. 1, R. pp. 410–437, with Wheeler's interest set forth at p. 436).

4. The transfer by Wheeler to Pawleys rendered him insolvent.

Respondent Kennedy argues that the "borrower [Pawleys] was not insolvent when the loan was executed" (Kennedy's Initial Brief, p. 13), that Pawleys (and Wheeler via his 99% interest in Pawleys) had cash and equity of $1,357,438.50 when Kennedy made the loan (*Id.*, p. 16), that Wheeler's distributional interest in Pawleys could pay the Sapp debt at the time of closing (*Id.*, p. 20), and that Sapp failed to investigate Wheeler's assets in other jurisdictions.

These arguments are addressed below, and each fails on the clear and convincing facts of the case and the law.

The argument of Pawleys' solvency is irrelevant as Sapp's claim is against Wheeler, and even it is relevant, Pawleys was not solvent. Further, the test is not whether Wheeler was insolvent at the time of the transfer, but also whether he was insolvent at the time Sapp tried to collect the debt.

Despite arguing that Pawleys is a separate and distinct entity from Wheeler (*Id.*, pp. 18, 19), Kennedy argues that the alleged solvency of Pawleys gives Sapp a remedy even though at the time Kennedy alleges Pawleys was solvent, the time of the Kennedy loan, Sapp's claim had not been reduced to a final judgment. In fact, Kennedy commenced its foreclosure action a month before Judge Cooper issued his order on post trial motions in the Sapp/Wheeler Litigation and two months before the Georgetown Sheriff issued the *nulla bona* return. Kennedy chooses to ignore these facts and fails to set forth how or when Sapp should have collected his judgment from Pawleys when Pawleys had no cash and was in foreclosure when the final trial court order was issued in the Sapp/Wheeler litigation.

Even if Pawleys' solvency is relevant, the Property was mortgaged for all of Pawleys' obligations to Kennedy (Plaintiff's Ex. 1, R. p. 283). As now seen, that mortgage lien was over $1.8 million dollars plus accruing interest. Thus, upon closing the loan, which was contemporaneous with the quitclaim deed from Wheeler, Pawleys was not solvent. By conveying and encumbering the Property with new debt, Wheeler put the Property beyond the reach of Sapp. Pawleys only business was to develop and sell the Property (Plaintiff's Ex. 1, R. p. 400 at para. 9.0). It had no other means of becoming solvent. It was precluded by Kennedy

from acquiring other property (Plaintiff's Ex. 1, R. pp. 438, 440 at para. 13.5(ii)). Thus, the only way for Pawleys to ever be solvent was to sell Lots 3 and 4, which it never did.

Assuming *arguendo* that Pawleys alleged solvency is relevant and that Pawleys was solvent at the time of closing, Respondents' argument fails because Pawleys was not solvent in the final analysis for Sapp to collect Wheeler's debt in full.

> Where a conveyance is made without an actual intent to defraud but without consideration, it is said that the conveyance will stand if the grantor reserves a sufficient amount of property to pay his creditors. *Penning v. Reid* et al., 167 S.C. 263, 283, 284, 166 S.E. 139, 146.
> But this means a sufficient amount of property not merely at the time of the transfer, but *an amount from which in the final analysis the creditors are able to collect their indebtedness in full*. The court in the *Reid* case said:
> "No rule is more clearly imbedded in the law of this state, than that a debtor must be just before he is generous. 'The law will not permit one who is indebted at the time to give his property away, provided such gift proves prejudicial to the interest of existing creditors. The motive which prompts the donor to make the gift is wholly immaterial. If the donor is indebted at the time, and the event proves that it is necessary to resort to the property attempted to be conveyed away by a voluntary deed for the purpose of paying such indebtedness, the voluntary conveyance will be set aside, and the property subjected to the payment of such indebtedness upon the ground that it would otherwise operate as a legal fraud upon the rights of creditors, even though it might be perfectly clear that the transaction was free from any trace of moral fraud. *Citations omitted.*
> *If in the final event the property of the debtor is not sufficient to pay his debts existing at the time of his voluntary conveyance, then such conveyance is null and void as to such debts*." (emphasis added)

Gardner v. Kirven, 184 S.C. 37, 191 S.E. 814, 816-17 (1937).

Respondents further argue that Sapp failed to prove that Wheeler was insolvent. They argue that Sapp did not check assets in Horry County. Sapp performed a reasonable and prudent asset search in Georgetown County where the judgment debtor resided. There is no evidence from any respondent that Wheeler owns any property in other locales from which the debt could be paid. Further executions require the Sheriff to satisfy a judgment out of the judgment debtor's

personal and real property. S.C. Code Ann. § 15-39-80 (1976). In carrying out his statutory duty, the Sheriff could not locate any property to satisfy Sapp's judgment or any part of it.

By itself, the *nulla bona* return by the Sheriff is sufficient evidence of insolvency to set aside a conveyance as a fraud on a judgment creditor. *Bates v. Cobb,* 29 S.C. 395, 7 S.E. 743 (1888). When combined with Sapp's attempt to locate other assets, the instant foreclosure by Kennedy, the pending foreclosure on lots 1 and 2, and Wheeler's failure to offer any evidence of his ability to pay the debt, much less any part of it, clearly and convincingly Wheeler has insufficient property to pay the judgment. Sapp proved Wheeler's insolvency. If Wheeler was solvent, Sapp would not be engaged in this lengthy, costly litigation with Kennedy.

B. Respondents fail to distinguish *Coleman v. Daniel.*

In its lead argument Kennedy makes several specious arguments and confounding factual assertions at pages 12 and 13 of its brief while unsuccessfully trying to distinguish *Coleman v. Daniel.* These arguments and statements are restated, and then examined in light of the actual facts in the record.

> Appellant presents an absurd argument that would eliminate cash-out, home equity, second mortgage and most primary mortgage lending in South Carolina, because no prudent lender ever loans 100% of the value of the collateral.

Kennedy's Initial Brief, p. 12.

Kennedy's "Chicken Little" argument does not hold water. Any lender with knowledge of a fraudulent conveyance or with knowledge that his borrower is being sued assumes the risk that the loan transaction could be unwound - that a creditor like Sapp whose claim is known to the lender, could take priority when a mortgage is taken on fraudulently conveyed property. This is exactly what occurred in *Coleman v. Daniel* in 1973, yet mortgage lending has survived in

South Carolina for the last 40 years. This is exactly what happened in *Rilling v. Schultz* over a century ago in Texas, but mortgage lending survives there as well.

Kennedy then states:

> This case does not involve any of the key facts which supported a fraudulent conveyance finding in *Coleman*. First, this was an arms-length loan transaction between a lender based in New Jersey and a South Carolina limited liability company with no prior relationship. (Kevin Wolfer Depo. Tr. 13: 22-25, 14:1-10: R.___). Second, no property was sold or transferred to Kennedy. Third, the borrower was not insolvent when the loan was executed, but retained over 1.3 million in cash and equity from this transaction alone. Fourth, the borrower was not living on the Property when the transaction closed. (Plaintiff's Trial Exhibit No. 1, R. ____). Finally, the borrower did not retain, via secret agreement, perpetual use of the Property rent free. The only reasonable conclusion to draw from the amount Kennedy loaned is that it was a conservative and prudent lender. Sapp's argument that a 50% loan to value ratio was grossly inadequate is not supported by *Coleman* or any other South Carolina case.

Kennedy's Initial Brief, p. 13. Despite Kennedy's attempt to distance Respondents from the facts of *Coleman*, this case involves all of the "key facts" recited by Kennedy in the above quote.

- Kennedy argues it entered into an arm's length transaction with Pawleys, the grantee. There was an arm's length loan transaction by New Lender with the fraudulent grantees in *Coleman*.
- Kennedy argues that no property was sold or transferred to it. No property was sold or transferred to New Lender in *Coleman*.
- Kennedy argues that the borrower was not insolvent when the loan was executed. The borrower in *Coleman*, like the borrower in this case, was the fraudulent grantee. The borrower in *Coleman* also was not insolvent when it borrowed $32,000.00 from New Lender as the borrower was the owner of record of property worth at least $85,000.00. Further, Kennedy's argument misses the

point because the fraudulent grantee's solvency is irrelevant. The test is whether Wheeler, the fraudulent grantor, is solvent so he can pay his creditors. In most fraudulent conveyance situations the fraudulent grantee pays nothing to the debtor/fraudulent grantor, and takes unencumbered property, or property with significant equity; therefore, the fraudulent grantee/borrower should be solvent. That's the point of making the fraudulent conveyance – to shield a valuable asset from one's creditors.

- Kennedy argues that the borrower in *Coleman* was not living on the property when the transaction closed. Likewise, Pawleys was not living on the Property. Thus, Kennedy does not distinguish *Coleman* or distance itself from the *Coleman* facts on this argument, either. However, Wheeler, as the fraudulent grantor, did retain a 99% development interest in the raw land he conveyed, just as the fraudulent grantor in *Coleman* retained the ability to use his property.
- Kennedy argues that the borrower did not retain perpetual use of the property in secret rent free. That is exactly what Pawleys did. It secured all rights to the property vis-a-vis its fraudulent grantor, but subject to the claims of the defrauded creditor. Wheeler's transaction is structured no differently than the transaction in *Coleman*. If Kennedy is attempting to argue that the fraudulent grantor in *Coleman* retained use of the property in secret, in fact, Wheeler as a 99% owner of Pawleys, retained use of the property in the company's operating agreement, a non-public document.

No respondent has distinguished the *Coleman* facts from the facts of this case. This Court should follow *Coleman's* precedent and order the Property be sold in satisfaction of Sapp's judgment against Wheeler.

C. A mortgage given by a fraudulent grantee and taken for new debt is void as to an existing creditor of a fraudulent grantor under *Coleman v. Daniel* and *Rilling v. Schultz.*

Rilling v. Schultze, 95 Tex. 352, 67 S.W. 401 (1902), holds that a mortgage executed by a fraudulent grantee is invalid as to creditors of the fraudulent grantor existing at the time of the fraudulent conveyance when the mortgagee had notice of the fraud. Because Rilling (the lender) had notice of the fraud in the conveyance from Schultze, Jr. (the fraudulent grantor) to his father (the fraudulent grantee), Rilling was not a bona fide purchaser from the fraudulent grantee (Sr.). The Texas Supreme Court determined that the debt owed to Rilling (Kennedy) consisted largely of debt which arose subsequent to the indebtedness owed by Schultze, Jr. (Wheeler) to Caroline Schultz (Sapp) arose, and found Rilling's mortgage to be invalid as to Caroline Schultz as to all new debt created when the mortgage was given. Following *Rilling*, this court should find that the Kennedy mortgage is invalid as to Sapp as to all indebtedness created when the Kennedy mortgage was executed.

Kennedy seeks to distinguish *Rilling* at page 16 of its brief by stating that *Rilling* "involved a father and son conspiring to keep property out of the hands of the son's ex-wife by transferring it to an individual who knew the circumstances of the divorce." Note that the *Rilling* court deemed the deed to be a mortgage; therefore, we have the same facts present in this case - a mother and son combining to keep the Property out of Sapp's hands by mortgaging it to Kennedy which knew the circumstances of Wheeler's indebtedness to Sapp. The underlying facts of *Rilling* are legally indistinguishable from the facts of the case before this court.

Likewise, in *Coleman v. Daniel*, the South Carolina Supreme Court held that a conveyance was fraudulent and void as to the creditor (Coleman). It held that the property was subject to Coleman's judgments and that Coleman could seek an order of the lower court for sale of the property in satisfaction of his judgments. Justice Bussey advocated that Coleman should only be paid to the extent that the sales price exceeded the consideration actually paid or assumed by the fraudulent grantees. The four justice majority refused to adopt Justice Bussey's analysis, thus voiding New Lender's mortgage as to Coleman. As discussed above, at Argument B, Kennedy has failed to legally distinguish *Coleman* from the facts of this case.

Kennedy relies heavily on *Oskin v. Johnson,* 400 S.C. 390, 735 S.E.2d (2012). *Oskin* has nothing in common with the facts of this case and is easily distinguishable from *Rilling* and *Coleman*. While suit was pending against him by Oskin for breach of contract, Johnson jointly purchased a beach home with his uncle. Johnson and his uncle co-signed a $3.5 million note in favor of SCB&T for purchase money financing. SCB&T duly recorded its mortgage on the home. The note had a two year balloon payment. There was also a second mortgage recorded on the home in favor of Ameris Bank for $500,000. Johnson was unable to pay his share of the SCB&T loan when it came due leaving his uncle with liability for the full SCB&T debt on a home which was then appraised at approximately $2.5 million. Uncle's wife formed a limited liability company which borrowed money from Wachovia and paid SCB&T $3.5 million, plus Uncle paid SCB&T another $44,000 which was due on the note. SCB&T received full consideration for the note, and assigned the note and mortgage to the uncle's wife's limited liability company.

Oskin sued claiming that the assignment of the note and mortgage by SCB&T was a fraudulent conveyance. Neither Johnson nor his uncle had conveyed any interest in the home, as

opposed to Wheeler who quitclaimed his interest in the Property. The South Carolina Supreme Court held that the Statute of Elizabeth is concerned with the intent of a grantor who conveys an interest in land. In *Oskin*, SCB&T assigned a note for valuable consideration. It took what it was due when the purchase money note was paid in full. There was no evidence that SCB&T intended to defraud anyone. It simply received payment for its purchase money loan.

Further, given the value of the property compared to the purchase money mortgage, Oskin would not have been damaged by the assignment. Oskin was the third lien creditor in line behind the $3.5 million SCB&T mortgage and a $500,000 mortgage to Ameris Bank. Oskin did not challenge the validity of either mortgage, just the assignment of the mortgage by SCB&T. Even excluding the $500,000 second mortgage, the value of the home was upside down compared to the SCB&T loan by approximately $1.0 million more than the property was worth. Had the SCB&T note not been paid, SCB&T could have foreclosed, and Oskin would not have received anything. Comparing *Oskin* to the facts of this case, Lot 4 was encumbered by a note for 34% of its value. Lot 3 had no liens on it and was appraised for $1,020,000. Although Oskin could not show any damage by the assignment of the SCB&T note, Sapp was clearly damaged by Wheeler making a fraudulent conveyance and by the fraudulent grantee giving a non-purchase money mortgage on the Property to a lender which had full knowledge of the facts.

It is said that equity will not suffer a wrong without a remedy, and that he who seeks equity must do equity. If the Master's order is affirmed: this court will sanction Wheeler's transfer of essentially unencumbered property for no consideration when he was indebted to Sapp; this court will sanction Kennedy's inequitable conduct of making a new loan to a fraudulent grantee secured by a mortgage on fraudulently conveyed property when Kennedy had actual knowledge of the facts; and this court will leave Sapp, an innocent party who has done all

he can to secure a just remedy and result, with no remedy. Following *Coleman* and *Rilling,* and given that *Oskin* has no application to the facts of this case, this Court should order the Property to be sold in satisfaction of Sapp's judgment.

D. The Recording Statute does not assist Kennedy in the face of a void transfer of the Property.

Respondent Kennedy argues that the recording statute, S.C. Code Ann. § 30-7-10 (1976), gives Kennedy a superior lien over Sapp because the mortgage was filed fourteen months before Sapp secured judgment against Wheeler (Kennedy's Initial Brief, p. 25). Although Kennedy cites no case in which the recording act can be used to uphold a fraudulent transfer, Kennedy relies upon *Atlas Supply Co. v. Davis*, 273 S.C. 392, 256 S.E.2d 859 (1979), and speculates that Kennedy obtained no advantage in lending to Pawleys versus lending to Wheeler directly. Kennedy incorrectly argues that it holds a purchase money mortgage (Kennedy's Initial Brief, p. 26).[6] None of these arguments are persuasive.

The argument that the recording statute and equity "dictate Respondent's lien is superior" would nullify the Statute of Elizabeth and South Carolina precedent. South Carolina Courts recognize that the recording statute is inapplicable when property is fraudulently conveyed. If the recording statute did apply, a creditor who secures his judgment after the conveyance would never have a remedy. Like this case, a fraudulent conveyance often occurs where a debtor conveys his property, a deed is recorded for the conveyance, and a creditor then secures judgment. The creditor then discovers that the debtor has transferred his property for no consideration. *See, e.g., Lebovitz v. Mudd; Albertson v. Robinson*, 371 S.C. 311, 638 S.E.2d 81 (Ct. App. 2006); and *Coleman v. Daniel.* If the recording statute applied in these circumstances,

[6] See footnote 3, *supra.*

the fraudulent grantee could simply argue that the recording of the deed trumps the fraudulent transfer, thus nullifying the Statute of Elizabeth, S.C. Code Ann. § 27-23-10 (1976).

South Carolina precedent does not support Kennedy's argument that the recording statute gives its mortgage priority over Sapp's lien. In *Leasing Enterprises, Inc. v. Livingston*, a judgment creditor ("LEI") brought an action to attack a conveyance of real property from a judgment debtor ("Livingston") to his mother. 294 S.C. 204, 363 S.E.2d 410 (Ct. App. 1987). LEI obtained a money judgment against Livingston in California in November 1981. *Id.* at 206, S.E.2d at 411. In April 1983, Livingston quitclaimed his one-half (1/2) interest in approximately thirty-seven (37) acres of land in Oconee County, South Carolina to his mother Margaret Schlee for the stated consideration of love and affection. *Id.* In December 1984, LEI recorded its domesticated judgment against Livingston in Oconee County. *Id.* LEI filed suit and alleged the quitclaim deed from Livingston to Schlee constituted a fraudulent conveyance and that the deed was not validly recorded under the South Carolina recording statute. *Id.* The Court stated,

> Section 30-7-10, Code of Laws of South Carolina, 1976, is the recording statute. If this deed was acceptable for recording, Leasing's judgment would not have priority over Schlee under the current recording statute unless Leasing shows the deed is a fraudulent conveyance.

Id. at 207, S.E.2d at 411. The Court further stated,

> Our reading of the current statute indicates the recording act is a race-notice act which will provide protection to the subsequent purchaser or creditor provided he records first. Therefore, even though Leasing had no actual or constructive notice of the deed between Livingston and Schlee when the Lease Purchase agreement was made and was a subsequent creditor of Livingston, it has no protection under the recording statute unless either the deed from Livingston to Schlee was not valid for recording thereby causing Schlee to lose her filing priority or Leasing can demonstrate a fraudulent conveyance.

Id. at 208, S.E.2d at 412. Thus, even if the deed to Schlee could have been validly recorded prior to LEI's domesticated judgment, LEI still had priority under the recording statute if LEI proved the deed to Schlee was a fraudulent conveyance.

In *Coleman v. Daniel*, the recording statute was also inapplicable. In *Coleman*, the debtor/fraudulent grantor executed notes payable to Coleman in 1962 and on October 14, 1964. Twelve days later, on October 26, 1964, the property in question was fraudulently conveyed to the debtor's married daughter and son-in-law (the Daniels). Twenty-three days later, on November 23, 1964, the fraudulent grantees borrowed $32,000 from New Lender which recorded a mortgage on the fraudulently conveyed property. Eighteen months later, on May 30, 1996, Coleman obtained a judgment against the debtor/fraudulent grantor. Over Justice Bussey's dissent that New Lender should be paid first from the sale of the property, the Supreme Court held that the deed for the fraudulently conveyed property was void as to Coleman and that the property be sold in satisfaction Coleman's judgment.

Under both *Leasing Enterprises* and *Coleman*, the recording act is inapplicable and Kennedy's argument fails.

Kennedy's reliance on *Atlas Supply Co. v. Davis*, 273 S.C. 392, 256 S.E.2d 859 (1979) is also misplaced. First, there was no fraudulent conveyance issue in *Atlas*. Second, Kennedy knew of Sapp's claim, a fact not present in *Atlas*. Kennedy cites *Epps v. McCallum Realty*, 129 S.C. 481, 138 S.E. 297 (1927), for the proposition that the purpose of the recording statute is to protect subsequent creditors without notice. In fact, Kennedy had notice of Sapp's claim, but elected to proceed with its loan transaction regardless. It is this notice which precludes Kennedy from being a bona fide purchaser for value.[7]

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[7] The term good faith purchaser for value includes the concept of lack of notice. *See, e.g., Messervy v. Barelli*, 11 S.C. Eq. (2 Hill Eq.) 576 (1837) and *Brunson v. Sports*, 239 S.C. 58, 121 S.E.2d 294 (1961). In *Messervy*, a mortgage was deemed subordinate to the rights of the grantee's wards where the mortgagee took the mortgage with notice of the wards' claims against the mortgagor. Similarly, in *Brunson*, Dukes took a deed to property from West. The property was subject to an unrecorded trust. Dukes had notice of the unrecorded trust. The Supreme Court stated, "The law is well settled that actual notice of an outstanding equity will cut off the

Even if this court were to find *Atlas Supply* applicable, the equities of this case significantly favor Sapp, and the Kennedy mortgage should be subordinated to Sapp's lien. *See Regions Bank v. Wingard Properties, Inc.*, 394 S.C. 241, 715 S.E.2d 348 (Ct. App. 2011). In *Regions*, Regions Bank made a $7,000,000 construction loan to Wingard secured by a recorded mortgage on three lots, one of which was lot 38. At the time of the loan and mortgage, Regions knew that Covington had given Wingard a $276,700 down payment for a residential home purchase agreement on lot 38. There was no public recording of the residential home purchase agreement and Covington's interest in lot 38. Relying heavily on Regions' knowledge of the down payment, this court found that Covington's unrecorded interest in the property had priority over Regions' recorded mortgage. This court refused to give Regions priority under the recording statute, but looked to the equities of the case to give Covington priority.

> Here, Covington's equitable interest is not defeated by Regions Bank's mortgage because Covington entered into his purchase contract before Regions Bank filed its mortgage with the register of deeds and Regions Bank was aware of this interest. *See* S.C.Code Ann. § 30–7–10 ("[A]ll mortgages ... are valid so as to affect the rights of subsequent creditors (whether lien creditors or simple contract creditors), or purchasers for valuable consideration without notice...."). The intervention of equity does not impugn the integrity of the recording statute in this case. *See Crystal Ice Co.,* 273 S.C. at 308, 257 S.E.2d at 497 (finding a first-to-file mortgage holder not entitled to the protection of the recording statute where that mortgage holder had knowledge of the existence of a prior purchase money mortgage). The trial court was presented with the question of whether equity should intervene only as between Regions Bank and Covington, not any other person or creditor potentially impacted by the recording statute. The trial court appropriately looked at the substance of the issue, namely Regions Bank's knowledge of Covington's prior interest, over Covington's failure to ensure that his down payment was received by Wingard prior to closing. In fact, Regions

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defense of bona fide purchaser." *Brunson*, 239 S.C. at 68, 121 S.E.2d at 299. The court further stated that even if Dukes secured from reputable counsel an opinion that his paper title was good, that the property was impressed with a trust in favor of the respondents. Kennedy knew that Sapp was subject to a pending legal action asserting a claim of over $500,000.00. It stopped investigating the fraudulent nature of the transaction because it secured an attorney's opinion and title insurance. Based on Kennedy's notice of Sapp's claim, and even with an opinion of counsel, Kennedy cannot be a bona fide purchaser (Appellant's Brief, pp. 22–23).

> Bank would not have given Wingard a construction loan if Wingard had not already sold the lot to a purchaser. Therefore, just as equity was allowed to intervene in *San–A–Bel* and *Crystal Ice,* we conclude the record herein supports the trial court's award to Covington of priority on his equitable lien over Regions Bank's mortgage.

Regions Bank v. Wingard Properties, Inc., 394 S.C. 241, 255-56, 715 S.E.2d 348, 356 (Ct. App. 2011).

Thus, even if the recording statute was applicable, Kennedy's loan with full knowledge of the Sapp/Wheeler Litigation and the fraudulent conveyance require that the mortgage at least be subordinated to Sapp's lien under the analysis in *Regions Bank.*

In further support of its argument on the recording statute, Kennedy claims the "folly in Sapp's entire appeal" is that Kennedy obtained no advantage in lending to Pawleys versus lending to Wheeler directly, and if it had loaned to Wheeler, its lien would have been superior to Sapp's judgment. Kennedy's argument is no more credible than its CEO testifying under oath that he would not know if the transfer to Pawleys of the unencumbered Lot 3 and the Kennedy mortgage would make it more difficult for Sapp to satisfy a claim out of Lot 3.

Kennedy argues that it could have made the loan directly to Wheeler, but this is contradicted by Kennedy's testimony. Kennedy required that the loan be made to Pawleys (Wolfer Deposition 2, R. p. 653, lines 4–9). No title insurer would have issued a lender's mortgage policy on a loan to Wheeler without excepting to the Sapp/Wheeler litigation. Kennedy and Wheeler needed the Property transferred to a third party to secure title insurance. Kennedy and Wheeler structured the transaction to insulate the Property from Sapp since Kennedy was not relying on any income from the borrower or guarantors to repay the loan. The sole source of payment was the sale of the Property. In order to make the loan, the Property needed to be taken out of Wheeler's name. There was no other reason to form Pawleys. Wheeler and his mother put the Property into a limited liability company formed by Wheeler-

Cribb, but in which Wheeler held a 99% interest, secretly retaining his interest in the Property. Not only was Kennedy able to secure title insurance by making the loan to Pawleys, but Kennedy gained further advantage by forcing Sapp to pursue a claim for a fraudulent conveyance which he would not need to do if the property remained in Wheeler's name.

The alleged "folly of Sapp's entire appeal" is, also, not based on the facts of this case. Kennedy did not make a loan to Wheeler, did not take a mortgage from Wheeler, and refused to make a loan to Wheeler. Instead, on March 4, 2009, Wheeler-Cribb formed Pawleys, and Wheeler made himself a 99% member. About two months later, while the Sapp/Wheeler Litigation was pending Wheeler transferred the Property to Pawleys for "$5.00 and no other consideration" and tried to give a mortgage on the Property to a creditor who was fully aware of the nature of the fraudulent conveyance. This appeal should be decided on the facts of this case and not Kennedy's conjecture about a loan that was never made, a loan that could not stand legal scrutiny.

Undercutting Kennedy's argument is that Sapp was named as a defendant by Kennedy in this case. Sapp did not intervene. Kennedy's attorneys understood Sapp's claim against Wheeler and the Property prior to the loan transaction when they three times asked Wheeler's attorney for an explanation of the Sapp/Wheeler Litigation, and Kennedy joined Sapp as a party to this case when they knew Kennedy could not pass clear title after a foreclosure sale if Sapp's interest was not adjudicated. There would be no reason for Kennedy to join Sapp as a party in the foreclosure if he had no interest in the property as Kennedy now argues.

Even if Kennedy had made a loan directly to Wheeler, it would not stand under the law. For such a mortgage to stand, it must be made for existing debt, and the transaction must be bona fide. *See South Carolina National Bank v. Halter*, 293 S.C. 121, 359 S.E.2d 74 (Ct. App. 1987),

Lenhardt v. Ponder, 64 S.C. 354, 42 S.E. 169 (1902), and *Magovern v. Richard*, 27 S.C. 286, 3 S.E. 340 (1887). In these cases mortgages were upheld in the face of a fraudulent conveyance attack but only because the mortgagor was already indebted to the mortgagee when the mortgage was executed. Based on the existing debts owed by the mortgagors, each court found the mortgage conveyance to be supported by valuable consideration. In the case before this court there was no debt owed to Kennedy until the loan closed; therefore, a loan to either Wheeler or Pawleys would be subject to Sapp's judgment.

In addition, the transaction was not bona fide. In, *McElwee v. Kennedy*, 56 S. C. 154, 34 S. E. 86 (1899), the court upheld a conveyance from a husband to a wife based on debts owed by the husband to the wife. The court further addressed the bona fides of the transaction stating:

> To annul for fraud a deed based upon a valuable consideration, it must not only be shown that the grantor intended thereby to hinder, delay, or defraud, creditors, but it must also appear that the grantee participated in such fraudulent purpose. Even if we were to assume that there is evidence of mala fides in the grantor, yet if the sole purpose of the grantee was to secure her claims, having no intent to hinder, delay, or defeat other creditors, her title cannot be affected by the mala fides of the grantor. The evidence fails utterly to show any intent on the part of the grantee to defraud her husband's creditors, and merely shows a purpose to secure her own bona fide claims. Conceding the insolvency of the firm of which the grantor was a member, it does not appear that the grantee was aware of it; and, if she was aware of it, that would not show fraud in her, since a bona fide creditor has the right to obtain a transfer of property from an insolvent debtor, at a fair price, for the sole purpose of securing or paying the debt.

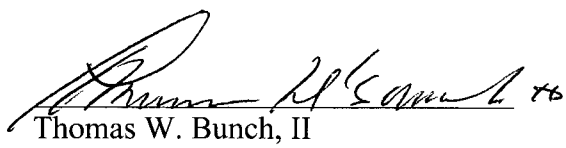
Although *McElwee* involves a deed, the bona fide/mala fide concept remains the same. Here, Wheeler's and Pawley's mala fides are established by the badges of fraud, and their failure to rebut those badges. Kennedy did not seek to "secure her bona fide claims" since no such claims existed. Kennedy "was aware" of the claims against Wheeler and his insolvency since it was only looking to the sale of the Property for payment of the debt. Kennedy did not take its mortgage for a fair price. The mortgage of an unencumbered lot and the entire Property which

was valued at $1,920,000 for a $774,000 loan was not a fair price. The consideration was grossly inadequate. By its mala fides and with no existing lending relationship with Wheeler or Pawleys, Kennedy and Pawleys put the Property beyond Sapp's reach when they had actual knowledge of Sapp's claims. Kennedy's argument that it gained no advantage by lending to Pawleys fails, as a loan to Wheeler would also fail because there was no previous obligation to support the loan and Kennedy's mala fides has been proved. Just as in *Coleman v. Daniel*, the Property should be sold to satisfy Sapp's judgment.

V. CONCLUSION

This court should reverse the Master's Order on Summary Judgment and the final Order and Judgment. Based on a *de novo* review of the record, it is clear and convincing that Wheeler fraudulently conveyed the Property to Pawleys, that the mortgage given by Pawleys to Kennedy is not valid as to Sapp, and that the Property should be sold in satisfaction of Wheeler's debt owed to Sapp. Alternatively, the mortgage of the previously unencumbered lot 3 should be set aside and that lot should be sold in satisfaction Sapp's claim.

Respectfully submitted,



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December 13, 2013

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM GEORGETOWN COUNTY
Court of Common Pleas
The Honorable Joe M. Crosby, Master-In-Equity

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Appellate Case No. 2013-001447

Kennedy Funding, Inc. as predecessor-in-interest, and BNP Paribas.....Respondents,

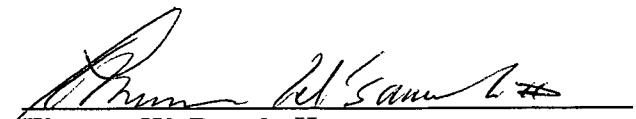
v.

Pawleys Island North, LLC, Will Darwin Wheeler, Peggy Wheeler-Cribb, and J. Mars Sapp, Defendants,
of whom Pawleys Island North, LLC, Will Darwin Wheeler and Peggy Wheeler-Cribb are Respondents and

J. Mars Sapp is the .....Appellant.

CERTIFICATE OF COUNSEL

The undersigned hereby certifies that this Final Reply Brief of Appellant complies with Rule 211(b), SCACR.



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PROOF OF SERVICE

I certify that I have served Appellant's Final Reply Brief on opposing counsel by depositing a copy of it in the United States Mail, postage prepaid, on **December 13, 2013** addressed as follows:

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