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SC Court of Appeals

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-22-00180
Appellate Case No. 2013-001447

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

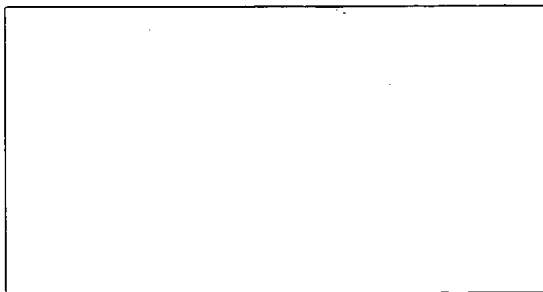
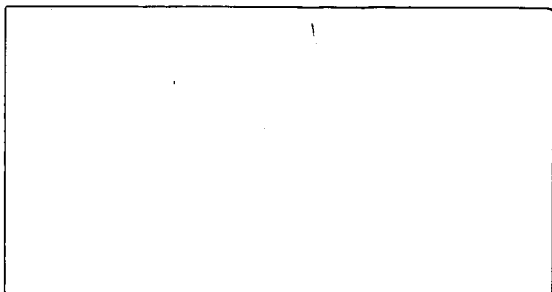
v.

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.

SUPPLEMENTAL BRIEF OF APPELLANT ON REMANDED ISSUE

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- a. Under the Statute of Elizabeth and the same material facts as the case now before this Court, the South Carolina Supreme Court held in Coleman v. Daniel that the fraudulently transferred property should be sold in satisfaction of the judgment creditor’s lien.
b. Kennedy’s knowledge of the facts constituting the fraudulent transfer and Kennedy’s conduct in actually requiring the transfer are even more compelling than the facts present in Coleman, and in this equity case the Court should adjudge Kennedy’s mortgage void as to Sapp, thus subordinate to Sapp’s judgment lien.
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INTRODUCTION

Appellant J. Mars Sapp respectfully submits this supplemental brief on the question remanded by the Opinion of the Supreme Court filed 11 May 2016. In light of space limitations, repetition of arguments and citations included in the previously filed briefs of Appellant has been minimized. In case this Court may find some of Respondent's previous arguments relevant to the question presented on remand, appellant also presents an appendix to this brief addressing some of those arguments in summary fashion.

This supplemental brief will set forth the extraordinary facts affecting the remanded question and focus on the following points: the effect of the Statute of Elizabeth on the fraudulent conveyance; the resultant effect on the fraudulent grantee's inability to impair the defrauded creditor's interests; the holding under the same material facts in *Coleman v. Daniel*; and the extraordinary factors in favor of Appellant, beyond those which were present in *Coleman*. Finally, the supplemental brief will demonstrate how a ruling in favor of the appellant would not affect customary lending practices in South Carolina.

STATEMENT OF ISSUE ON APPEAL

WHERE THE GRANTEE IN A FRAUDULENT CONVEYANCE TAKES A VOID TITLE VIS-À-VIS AN EXISTING CREDITOR, IS A PURPORTED MORTGAGE FROM THE FRAUDULENT GRANTEE, TO A LENDER WHO KNOWS OF THE CREDITOR'S CLAIM AND INSTIGATES THE FRAUDULENT CONVEYANCE, VOID AS TO THE RIGHTS OF THAT CREDITOR, SO THAT THE CREDITOR'S JUDGMENT LIEN IS SUPERIOR TO THE MORTGAGE?

STATEMENT OF THE CASE

In 2015-UP-138 (the "Decision"), this Court reversed the lower court, in part, by holding that the transfer for \$5.00 was indeed fraudulent as to two lots at Pawleys Island (the "Property") conveyed from Will Darwin Wheeler to Wheeler's family-owned limited liability company, Pawleys Island North, LLC ("Pawleys"). No exception has been taken

by any party to this holding. The Decision also held that the subsequent mortgage from Pawleys to Kennedy Funding, Inc. (“Kennedy”) was not itself a fraudulent conveyance, and it was upon this finding that the panel of this Court determined that Kennedy’s mortgage had priority over Sapp’s judgment.

Appellant petitioned the Supreme Court for a writ of certiorari, contending that, even if the mortgage from Pawleys to Kennedy was not itself fraudulent, such a finding was not determinative of priority because Sapp had contended, as an alternative basis for relief, that the previous fraudulent transfer from Wheeler to Pawleys rendered the mortgage void as to Sapp, a defrauded creditor under the Statute of Elizabeth, S.C. Code Ann. § 27-23-10(A) (2007). The Supreme Court granted the petition for certiorari and remanded to this Court to decide the question whether the fraudulent conveyance from Wheeler to Pawleys rendered the subsequent mortgage from Pawleys to Kennedy void as to the interest of Sapp, rendering Sapp’s lien superior to Kennedy’s mortgage. 2015-MO-061.

A history of the litigation up to the time of the appeal, with dates and references, is reflected at pages 2-4 of the Brief of Appellant filed December 13, 2013.

STATEMENT OF FACTS

Sapp sued Wheeler in September 2008 to collect an unpaid debt. (R. 759). While the Sapp suit against Wheeler was awaiting trial, on 28 April 2009, Wheeler quitclaimed the Property to Pawleys for “five dollars and no other consideration.” (R. p. 750). Kennedy then made a non-purchase money loan to Pawleys, taking a mortgage on the fraudulently conveyed property as security for the loan.

The following facts appear uncontroverted in the record: Prior to the conveyance of the Property and prior to closing the loan, Kennedy knew of Sapp’s pending suit against

Wheeler. Kennedy knew Wheeler owned the Property solely in his name. Kennedy knew Wheeler was the 99% owner of Pawleys. See pages 5 and 6 of Appellants Brief filed December 13, 2013 for record references of the foregoing facts. As a condition of closing the mortgage loan, Kennedy required the conveyance of the Property from Wheeler to Pawleys (R. p. 653, ll. 4-9, Deposition of Kennedy's President). This is the conveyance which this Court determined to be fraudulent in 2015-UP-138.

Kennedy twice asked Wheeler's counsel for an explanation of the litigation, but got none. Ultimately, Kennedy decided that Sapp's pending collection suit on the debt owed by Wheeler did not matter as long as Kennedy obtained a title opinion on the Property and title insurance. See page 6 of Appellants Brief for record references. After a jury trial in June 2010, Sapp secured his money judgment against Wheeler. Because of the fraudulent conveyance and Kennedy's taking the mortgage with full knowledge of the facts giving rise to the fraudulent conveyance, Sapp's judgment has proven uncollectible.

A summary chart of the above facts follows:

Date	Transaction
September 2008	Sapp sues Wheeler to collect a debt.
Prior to 28 April 2009	Wheeler negotiates to borrow from Kennedy. Kennedy learns of the Sapp suit against Wheeler to collect a debt. As a condition of the loan, Kennedy requires that Wheeler convey the Property out of his name.
28 April 2009	Wheeler transfers the Property to Pawleys by quitclaim deed for \$5.00.
30 April 2009	Loan closing/mortgage transaction between Kennedy and Pawleys.
June 2010	Jury awards Sapp judgment against Wheeler.
April 2011	Unable to locate property to satisfy Sapp's judgment, Georgetown County Sheriff returns execution, <i>nulla bona</i> .

ARGUMENT

WHEELER'S FRAUDULENT CONVEYANCE OF THE PROPERTY TO PAWLEY'S WAS UTTERLY VOID AS TO SAPP; THEREFORE, PAWLEY'S SUBSEQUENT ATTEMPT TO ENCUMBER THE PROPERTY WITH A MORTGAGE TO A LENDER (KENNEDY) WHICH HAD KNOWLEDGE OF THE "BADGES OF FRAUD" AND REQUIRED THE CONVEYANCE WAS ALSO VOID AS TO SAPP, AND SAPP'S JUDGMENT LIEN IS SUPERIOR TO THE MORTGAGE.

- a. Under the Statute of Elizabeth and the same material facts as the case now before this Court, the South Carolina Supreme Court held in *Coleman v. Daniel* that the fraudulently transferred property should be sold in satisfaction of the judgment creditor's lien.**

As relevant and as enacted in South Carolina, the Statute of Elizabeth provides:

Every . . . conveyance of lands . . . for any intent or purpose to . . . defraud creditors . . . of their just and lawful actions, suits, debts . . . must be deemed and taken (only as against that person . . . whose actions, suits, debts, . . . by guileful, covinous, or fraudulent devices and practices are . . . defrauded) to be clearly and utterly void, frustrate and of no effect

S.C. Code Ann. § 27-23-10(A) (Rev. 2007).

It having been determined that Wheeler's transfer of the Property to Pawleys was fraudulent, the transfer is "utterly void, frustrate and of no effect" as to Sapp, the defrauded creditor. "A fraudulent conveyance is no conveyance at all, but a mere nullity, the title remaining all the while in the debtor, and subject to all legal liens, as if the fraudulent deed never existed. *Turner v. Washington Realty Co.*, 126 S.C. 378, 403, 120 S.E. 371, 379 (1923). Because Pawleys' ownership of the Property is void as to Sapp, any lien Pawleys attempted to give on the Property is ineffective as to Sapp's judgment lien on the Property. In *Coleman v. Daniel*, 261 S.C. 198, 199 S.E.2d 74 (1973), under the same material facts as present in this case, the South Carolina Supreme Court held that fraudulently conveyed

property would be sold to satisfy a defrauded creditor's judgment lien.

In *Coleman*, Linzie Rogers incurred debt to Coleman in 1962 and on October 14, 1964 by the execution of two notes. After Rogers executed the notes in Coleman's favor, Rogers fraudulently conveyed his property to the Daniels, just as Wheeler became indebted to Sapp then fraudulently conveyed the Property to Pawleys. Like Pawleys did in this case with Kennedy, the fraudulent grantees (the Daniels) then borrowed \$32,000 from an unidentified financial institution, which is referred to herein as "New Lender." New Lender paid off an existing \$29,000 mortgage on the fraudulently conveyed property which had a value of at least \$85,000, and New Lender recorded its non-purchase money mortgage executed by the fraudulent grantees. After the execution and recording of New Lender's mortgage from the fraudulent grantees (Daniels') in November 1964, Coleman secured judgments in 1966 against the Daniels' fraudulent grantor, Rogers. Under the same material fact pattern as present in this case, because the conveyance to the Daniels' was void as to Coleman, the South Carolina Supreme Court directed that the fraudulently conveyed property be sold in satisfaction of Coleman's judgment lien, even though the judgment lien was recorded after the mortgage.

The deed from Linzie Rogers to Annie Margaret Rogers Daniel and James D. Daniel, II, dated October 26, 1964, is void as to Coleman and the property described in the deed is therefore subject to the lien of Coleman's judgments. Coleman may seek an order of the lower court for sale of the property in satisfaction of his judgments unless the amounts due him be sooner paid.

Coleman, 261 S.C. at 211, 199 S.E.2d at 80.

- b. Kennedy's knowledge of the facts constituting the fraudulent transfer and Kennedy's conduct in actually requiring the transfer are even more compelling than the facts present in *Coleman*, and in this equity case the Court should adjudge Kennedy's mortgage void as to Sapp, thus**

subordinate to Sapp's judgment lien.

While the material facts of the within case are substantially the same as *Coleman*, the equities favoring the rights of the good faith judgment creditor (Sapp) are dramatically stronger in the present case than they were in *Coleman*, the lender Kennedy having had knowledge of the badges of fraud constituting the fraudulent conveyance and having actually required the fraudulent transfer as a condition of making the loan. Kennedy had extensive self-interested motivation for being so deeply involved: it was going to either be paid the \$775,000 it advanced and collect its 25% interest, or foreclose and own beachfront property at Pawley's Island valued at almost \$2 million.

One of Kennedy's main contentions (as taken from its brief in 2014 to this Court), the one that is supposed to illuminate the "folly in Sapp's entire appeal," is that Kennedy obtained no advantage from the fraudulent transfer to Pawleys, since if it had made the loan to and received the mortgage directly from Wheeler, the mortgage would have been superior to Sapp's judgment. But this argument, while purely hypothetical, is also incorrect.

First, 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 cited cases, mortgages were upheld in the face of a fraudulent conveyance attack but only because, unlike the facts present in this case, the mortgagor was already indebted to the mortgagee when the

mortgage was executed. In the case before this court there was no debt owed to Kennedy until the loan closed; therefore, a loan to Wheeler would be subject to Sapp's judgment.

Second, under equitable principals applied in foreclosure cases before this Court, Kennedy is not entitled to priority over the innocent, but defrauded creditor, Sapp. Given Kennedy's actual knowledge of Wheeler's indebtedness to Sapp and of Sapp's legal action for collection of that debt, even a hypothetical mortgage directly from Wheeler to Kennedy would be subordinate to Sapp's later-recorded judgment under equitable principals. *See, Regions Bank v. Wingard Properties, Inc.*, 394 S.C. 241, 715 S.E.2d 348 (Ct. App. 2011) (and cases cited therein). In *Regions*, the bank made a loan to Wingard secured by a mortgage. Bank brought a foreclosure action. When bank took the mortgage, bank knew that Covington had made a down payment to Wingard to purchase one of the lots covered by the mortgage. Covington's interest was not recorded. In light of bank's knowledge of the down payment, this Court held that Covington's unrecorded interest in the property must be given priority over Regions Bank's recorded mortgage, through the "intervention of equity." *Id.*, 394 S.C. 241, 255-56, 715 S.E.2d 348, 356.

The equities in this case favor the defrauded creditor Mars Sapp even more so than they did the defrauded creditor in *Coleman* where the court did not allude to any misconduct by New Lender but still provided a remedy for the defrauded creditor. In this equitable foreclosure action, Kennedy's mortgage is and should be void as to Sapp, the mortgage having been taken from the fraudulent grantee at Kennedy's instigation and with Kennedy's undeniable knowledge of the badges of fraud.

c. A holding in favor of the defrauded creditor Sapp will not affect customary lending practices in this State.

Respondent had argued in its original brief at page 12 (filed January 6, 2014), that Sapp's position would severely affect mortgage lending in South Carolina. Such a cry is hollow and specious. Kennedy was so deeply involved in the legal fraud underlying the conveyance in question, that a decision by this Court protecting Sapp, an innocent creditor, can neither affect customary lending practices nor hamper ethical lenders. Kennedy was well aware of Sapp's pending suit. The mere existence of the debt - which in this instance was a matter of public record known to Kennedy - gives rise to Sapp's right to invoke the Statute of Elizabeth. *See, Matthews v. Montgomery*, 193 S.C. 118, 133 7 S.E.2d 841, 848 (1940). Yet, Kennedy sought no explanation from Sapp or protection from Sapp, as it should have done. *See, Horry County v. Ray*, 382 S.C. 76, 674 S.E.2d 519 (finding that one simply on "inquiry notice" should direct its inquiry to the defrauded party). Had Kennedy inquired of Sapp, instead of relying on Wheeler's attorney for advice, the last five plus years of litigation among these parties would have been avoided. Instead, to insulate itself from Sapp's ultimate judgment, Kennedy required the transfer of Property from Wheeler who, by virtue of the holding of the fraudulent conveyance, purposefully defrauded Sapp, Wheeler's innocent creditor. The facts of this case combined with Kennedy's complicity (or at best plausible deniability) would affect only a lender who fails to make inquiry of a creditor in a pending suit, or may be further limited to a lender who is complicit in a borrower's fraud. A decision in favor of Sapp would render a lender's non-purchase money mortgage void only where the lender has notice of a creditor's claim whose suit is pending, or where this Court on its *de novo* review finds the lender's conduct

so inequitable that the Court in this equitable proceeding invokes equity to void the mortgage, or subordinate it to an innocent and defrauded creditor.

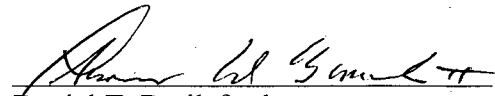
CONCLUSION

This case began in a court of equity, and it has been said, "The law follows justice." The Statute of Elizabeth and the host of South Carolina cases invoking it, including *Coleman v. Daniel*, recognize that justice favors the payment of honest debts, and that sham conveyances to avoid them will not be tolerated and are void as to existing creditors. The Supreme Court faithfully applied that principle in the case of *Coleman v. Daniel*, although to do so required choosing between the interests of two innocent parties. There is no such requirement here. This is an aggravated case of conveyance fraud in which the subsequent mortgagee, Kennedy, actually required the fraudulent conveyance as a precondition of the loan. And yet the lower court did not apply *Coleman*. Rather, it rewarded a lender who had instigated the fraudulent conveyance of the mortgaged Property, it protected the fraudulent grantor who had guaranteed the loan, and, thus, it denied justice to the only innocent party in the dispute.

It is respectfully requested that the lower court's Final Order and Judgment be reversed, that Sapp's judgment against Wheeler be adjudged a first lien on the Property, that the property be sold in satisfaction of Sapp's judgment, and that the case be remanded to the Master for the issuance of such orders and proceedings as are necessary to accomplish the above.

Signature on following page

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Daniel T. Brailsford", is written over a horizontal line.

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APPENDIX TO APPELLANT'S BRIEF ON REMAND
(SUMMARY OF RESPONSES TO SELECTED ISSUES)

- A. **That Kennedy was a good faith purchaser for value.** Kennedy had actual knowledge of the prior fraudulent conveyance and could not possibly have been a good faith purchaser for value without notice. To qualify for such defense, Kennedy must: (1) not have had notice of the debt to Sapp and the pending lawsuit before paying the purchase price (but it did); (2) not have had notice before acquiring the mortgage (but it did); and therefore (3) have purchased “bona fide without notice” (but it did not). *Kirton v. Howard*, 137 S.C. 11, 134 S.E. 859, 868 (1926) (lack of notice is a clear element of “good faith purchaser for value.”)
- B. **That Kennedy was entitled to priority under *Atlas Supply Co. v. Davis*, 273 S.C. 392, 256 S.E.2d 859 (1979).** *Atlas Supply* concerns a lien priority question under the Recording Act, S.C. Code Ann. 30-7-10 (1976). Sapp’s claim is not based upon the Recording Act, but rather on the Statute of Elizabeth which declares a fraudulent conveyance void as to a defrauded creditor. Though Sapp’s judgment was entered after the recording of the mortgage, Sapp’s interest in the Property dated back to the inception of the debt, and Sapp’s later procured judgment had priority over Kennedy’s interest in the Property. *See, e.g., Matthews v. Montgomery*, 193 S.C. 118, 7 S.E.2d 841 (1940) (judgment creditor stated a cause of action to set aside deed procured by downstream purchaser from a fraudulent grantee where downstream purchaser was on notice of the fraudulent transfer which led to his title). *See also Leasing Enterprises, Inc. v. Livingston*, 294 S.C. 204, 363 S.E.2d 410 (Ct. App. 1987.) (A judgment creditor, Leasing,

would not have priority over a prior recorded deed, “**unless Leasing shows the deed is a fraudulent conveyance.**”) *Id.* At 208, S.E.2d at 412. (emphasis added)

C. **That Sapp did not file a *Lis Pendens*.** The filing of a *lis pendens* is not appropriate for an action simply seeking money damages. *Carolina Park Associates, LLC v. Marino*, 400 S.C. 1, 732 S.E.2d 876 (2012). Moreover, the filing of a *lis pendens* -- even in a proper case -- is designed to put parties on notice. Here, Kennedy had extensive notice decided to make the loan despite its actual knowledge of Sapp’s pending collection action against Wheeler.

D. **Kennedy relied on Pawleys’ counsel’s opinion letter.** The opinion expressed by Pawleys’ counsel in the letter was clearly wrong, as shown by Kennedy’s having later included Sapp in the foreclosure action out of which this appeal arises. Moreover, even if the opinion was correct based on an examination of the property records, Kennedy would have had no right to rely upon that opinion when Kennedy had actual notice of Sapp’s outstanding equity in the Property. *Brunson v. Sports*, 239 S.C. 58, 121 S.E.2d 294 (1961)

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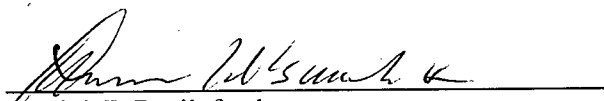
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J. Mars Sapp is theAppellant.

CERTIFICATE OF COUNSEL

The undersigned hereby certifies that this Supplemental Brief of Appellant on Remanded
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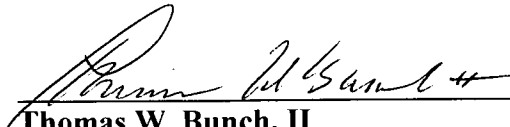
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