THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

The Honorable Stephanie P. McDonald, Circuit Court Judge

Op. No. 5588 (S.C. Ct. App. refiled February 27, 2019)

Case No. 2010-CP-10-10490
Appellate Case No. 2015-001590

Brad J. Walbeck and Lea Ann Adkins, Both Individually and Derivatively on Behalf of The I'On Assembly, Inc.; and I'On Assembly, Inc.,

Petitioners-Respondents,

v.

The I'On Company, LLC, The I'On Club, LLC, The I'On Group, LLC f/k/a Civitas, LLC, and I'On Realty, LLC,

Respondents-Petitioners.

REPLY TO PETITIONERS-RESPONDENTS' RETURN TO PETITION FOR WRIT OF CERTIORARI

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INDEX

Pursuant to Rule 242(g), SCACR, Respondents-Petitioners ("Defendants") submit this Reply to Petitioners-Respondents' ("Plaintiffs") Return to Defendants' Petition for Writ of Certiorari.[1]

The Court of Appeals denied cross-motions for rehearing on May 22, 2019. Defendants filed their petition on June 21, 2019, and Plaintiffs filed a return on July 22, 2019. After extending its deadline, Plaintiffs filed their own petition on July 11, 2019. As a result, there are cross-petitions for certiorari pending.

ARGUMENT

This Reply addresses Plaintiffs' response to the issues actually raised in Defendants' petition. In large part, Plaintiffs use their return to advance arguments raised in their own petition related to entirely different issues.[2] These arguments have very little to do with the Court of Appeals' expansion of a developer's fiduciary duty or the application of the two-issue rule to the 2000 Recreational Easement—the only two issues raised in Defendants' petition.

As a preliminary matter, one factual misstatement by Plaintiffs is worth highlighting. Throughout its return, Plaintiffs conveniently adopt the term "Commons" to encompass all of the property allegedly promised to the Assembly in the 1998 Property Report: the Creekside Park, Community Dock, "and the Dock's associated parking and boat ramp on two civic lots known as CV5 and CV6." (Return p. 2, n. 4.) The use of this collective label seeks to skirt the plain language of the Property Report and the testimony at trial. Neither Adkins nor Walbeck testified that the

[1] "Defendants" are The I'On Company, LLC, The I'On Club, LLC, The I'On Group, LLC, and I'On Realty, LLC. "Plaintiffs" are Brad Walbeck and Lea Ann Adkins, individually and derivatively on behalf of The I'On Assembly, and The I'On Assembly.

[2] Many factual arguments included in Plaintiffs' return are easily refuted by the lengthy discussion related to the statute of limitations. (App. pp. 147-155.) Defendants will address all arguments in Plaintiffs' petition in the Defendants' return.

Assembly had been promised the Creek Club facility, a boat ramp, a staging dock, or a parking lot. (R. pp. 891:16-19; 976:22-977:2; 977:20-978:17.) Defendants' only obligation to convey any amenity to the Assembly arose from the 1998 Property Report, which stated a "Community Dock" and a "Creekside Park" would be conveyed to the Assembly. (R. pp. 3022-3023.) Plaintiffs seek to distract the Court from this plain truth.

Defendants prevailed on every major substantive issue at the Court of Appeals. Accordingly, if this Court does not grant Plaintiffs' petition, Defendants do not seek review of the Court of Appeals' opinion because the issues raised in Defendants' petition would not be revisited in the context of a new trial. If the Court grants Plaintiffs' petition, the issues raised by Defendants are intertwined with the issues raised by Plaintiffs and are proper for certiorari.

As to the Court of Appeals' discussion of the scope of fiduciary duty owed by a developer to a homeowners' association, the issue is both arguably novel and in conflict with previous decisions of the Court. The Court of Appeals misapplied the two-issue rule to the validity of the Recreational Easement and, as a result, declined to address the novel issue of whether the after-acquired title doctrine applies to servitudes. (App. p. 24.)[3] The requirements of certiorari are satisfied. *See* SCACR, Rule 242.

I. THEORETICAL CONTROL DOES NOT CREATE A FIDUCIARY DUTY AS A MATTER OF LAW.

The Court of Appeals suggests that a developer's fiduciary duty is infinite in duration and indefinite in scope. The extrapolation of the Court of Appeals' discussion by Plaintiffs illustrates the fundamental problem for which Defendants seek clarification:

[3] Defendants cite to the Appendix and Record submitted with their petition on June 21, 2019.

> The only requirement for this [fiduciary] relationship to exist is that the HOA "trusted" Developers or that Developers were in a "superior" position, and during this trust or superiority period, Developers are obligated to act in the HOA's interest in all matters.

(Return p. 14.)

If the Court of Appeals' discussion can be fairly characterized this way, South Carolina law now eliminates a developer's business judgment and subjects a developer who contemplates *any* business decision that relates to a pending or ongoing development project to an impractical standard never before required by South Carolina law.

1. Appropriate limitations on the scope of the developer fiduciary duty were announced in *Goddard* and *Concerned Dunes West.*

The limited nature of the fiduciary relationship between a developer and a homeowners association is plainly supported by South Carolina law. While Plaintiffs do not misquote general law defining "fiduciary duty" or "fiduciary relationship," the *meaning* of those terms is not the issue before the Court. (Return pp. 12-14.) The issue raised in Defendants' petition is consideration of when such fiduciary duty is owed and whether that fiduciary relationship will be expanded beyond the limited circumstances the law has recognized. It is this issue that Defendants ask the Court to review.

Our courts have been clear that a developer has a fiduciary duty to bring about a viable homeowners association. *Goddard v. Fairways Development General P'ship*, 310 S.C. 408, 415, 426 S.E.2d 828, 832 (Ct. App. 1993). Like a promoter of a corporation, a developer "should be expected to use good judgment and act in utmost good faith to complete the formation of their organizations." *Id.* at 415, 426 S.E.2d at 832. A developer's fiduciary obligation is satisfied when a functional organization has been created.

Any further fiduciary obligation is triggered if the developer conveys common areas to the homeowners association. *Concerned Dunes West Residents, Inc. v. Georgia-Pacific Corp.*, 349 S.C. 251, 257, 562 S.E.2d 633, 637 (2002) (holding failure to turn over common areas in good repair "subjects the developer to liability for bringing the common areas up to standard"); *Goddard*, 310 S.C. at 415, 426 S.E.2d at 832 ("It seems unfair to villa owners for the Developer to burden them with substandard or deteriorated common areas that required an immediate expenditure of funds to bring them up to standard without a plan or reserve fund to cover the expenditures").

Outside of the circumstances discussed in *Goddard* and *Concerned Dunes West*, a developer is not in a position of continual confidence or in an ongoing "special relationship" with a homeowners association. Every single case cited in Plaintiffs' lengthy footnote *limits* consideration of when a fiduciary duty is owed by a developer to the time period when either the homeowners association was not yet formed or when common areas were turned over without financial reserves to provide for their maintenance. None of these cases—spanning from California to Illinois—stands for the proposition that once a developer is a fiduciary, it is always a fiduciary and must, in all circumstances, place the homeowners associations' interests above its own.[4] (Return pp. 13-14, n. 17.)

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[4] *See Seven Bridges Courts Ass'n v. Seven Bridges Dev., Inc.*, 306 Ill.App.3d 697, 706, 714 N.E.2d 601, 607 (1990) (finding "there was a fiduciary relationship between [townhome owners association] and [developer]" until the day unit owners took control of the association board); *Maercker Point Villas Condo. Ass'n v. Szymski*, 275 Ill. App. 3d 481, 485 (1995) ("By leaving plaintiff underfunded, [the developer] violated his fiduciary duty to plaintiff."); *Board of Managers of Weathersfield Condo. Ass'n v. Schaumburg Ltd. P'ship*, 307 Ill.App.3d 614, 617 (1999) (addressing allegations of inadequate capital reserves and maintenance at time of board turnover); *Orange Grove Terrace Owners Assn. v. Bryant Properties, Inc.*, 176 Cal. App. 3d 1217, 1223, (Ct. App. 1986) (holding that plaintiff had a cause of action against developer for negligent acts prior to the formation of the homeowners association); *Raven's Cove Townhomes, Inc. v. Knuppe Dev. Co.*, 114 Cal.App.3d 783, 800-01 (Ct. App. 1981) (analogizing the fiduciary duty of

2. The extension of a developer's fiduciary relationship with a homeowners association is altered by whether or not it is exercising retained rights.

The Court of Appeals appropriately determined that the trial court erred in ruling that Defendants had a fiduciary duty to convey amenity property to the Assembly. (App. pp. 12-17.) Beyond that correct ruling, this Court should clarify that any fiduciary duty owed by a developer to a homeowners association is not triggered merely as the result of theoretical control that exists as the result of retained—but unused—rights on behalf of a developer.

The events that gave rise to Plaintiffs' claims occurred many years after the Assembly was formed and control of the Assembly board was handed over to the homeowners. Beyond the circumstances recognized in *Goddard* and *Concerned Dunes West*, there would be no reason for either Plaintiffs or Defendants to believe that Plaintiffs continued to place any special confidence or trust in Defendants. Most business relationships are simply not fiduciary in nature. In *Burwell v. South Carolina National Bank*, the Court explained:

> As a general rule, mere respect for another's judgment or trust in his character is usually not sufficient to establish such a [fiduciary] relationship. The facts and circumstances must indicate that one reposing the trust has foundation for his belief that the one giving advice or presenting arguments is acting not in his own behalf, but in the interests of the other party.

288 S.C. 34, 41, 340 S.E.2d 786, 790 (1986).

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a developer to bring about a viable property owners' association to the that of a corporate promoters to shareholders); *Richard Gill Co. v. Jackson's Landing Owners' Ass'n,* 758 S.W.2d 921, 924-25 (Tex. App. 1988) (discussing developer's fiduciary duty to collect assessments and manage books until homeowners association handed over to owners); *Laurel Road Homeowners' Ass'n, Inc. v. Freas,* 191 A.3d 938, 941 (Pa. Cmwlth. 2018) (analyzing developer's malfeasance "during the period when they solely and exclusively developed the planned community and controlled the [a]ssociation"); *Innermiages, Inc. v. Newman,* 2019 WL 1380096 at *1 (Tenn. App. 2019) (holding the developer is liable for failing to honor obligations under restrictive covenants).

If, as the Court of Appeals states, the fiduciary duty exists as the result of Defendants' retained rights, it can only be owed if those retained rights are utilized to exert control over the homeowners association. The existence of theoretical control over board decisions does not extend a developer's fiduciary relationship beyond the relationship recognized in *Goddard* and *Concerned Dunes West*. Or, if the retention of limited rights by a developer extends a fiduciary relationship, the corresponding duty arises only when the developer exercises the right and only concerning the subject matter over which the developer exercises such control.

Plaintiffs misunderstand the application of the "bank cases" to the issue presented here. (Return p. 20.) The question is not whether there was a breach of a known fiduciary duty; the question is whether a fiduciary relationship existed between Defendants and Plaintiffs at the time of events that gave rise to this litigation—a time when any "control" was theoretical. These cases serve as examples of how South Carolina courts have previously grappled with the notion that a party can be fiduciary in one, limited context, but not another. *See Regions Bank v. Schmauch*, 354 S.C. 648, 671, 582 S.E.2d 432, 444 (Ct. App. 2003) ("a bank may be held to a fiduciary duty if it undertakes to advise a depositor as part of services the bank offers"); *Burwell v. South Carolina Nat'l Bank*, 288 S.C. 34, 40, 340 S.E.2d 786, 790 (1986) (finding no fiduciary duty existed between a customer and a bank "for the purpose of [the] transaction in dispute"); *Nat'l Loan & Exch. Bank v. New York Life Ins. Co.*, 149 S.C. 378, 147 S.E. 322, 323 (1929) (same).

3. Defendants have not exercised retained rights to control the Assembly.

Defendants have not exercised any retained rights to control the Assembly. Any "control" over the Assembly is and has been theoretical.

Plaintiffs identify several provisions in I'On's Covenants that they claim "give [Developers] *de facto* control and absolute power over the HOA . . . ." (Return p. 15.) That

statement is simply untrue. The *only* provision that has been called upon by Defendants since control was turned over to the I'On homeowners in 2005—the appointment of Chad Besenfelder to the Assembly Board in 2014—demonstrates how little "control" Defendants had.[5] The Assembly prohibited Besenfelder from participating in decisions involving the developer. (App. p. 15, n. 7.)

Plaintiffs also reference the attendance by I'On company representatives at Assembly meetings over the years. (Return p. 19.) No argument was made that the presence of Defendants at various Assembly meetings over the years had any impact or influence on the Assembly's operations. The Assembly Board refused to allow these representatives to participate in Board discussions and votes when the Assembly decided against it. (R. p. 1345:2-15.) There has simply been no control exercised by Defendants to prohibit, stall or impede the functioning of the Assembly.[6]

Plaintiffs also rely on the testimony of Deborah Bedell, the President of the Assembly Board at the time of trial, as evidence of control. (Return at 18-19.) Bedell testified that she spoke with many former Board members and did not personally believe that Developers controlled the Board. Bedell conceded that she is aware of no decision of the Board that Developers' "veto power" impacted. (R. pp. 1303:9-25; 1304:5-9; 1346:17-1347:5; 1426:23-1427:3.)

If the Court determines that a review of the fiduciary duty issue is warranted at the request of Plaintiffs, the Court should clarify the law of developer fiduciary duty as to scope and duration.

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[5] Plaintiffs concede and the trial court found that control of the Assembly was turned over to the I'On homeowners by December of 2005. (App. p. 199; R. pp. 33; 791:20-792:8; 3429-3431, 3475-3477.)

[6] Plaintiffs recount "acts and omissions" that purport to demonstrate Defendants' control over the Assembly. (Return pp. 19-20.) The selection of these particular "acts and omissions" ignores the repeated and countless notice Plaintiffs received that they would not receive the "Commons" for free for years prior to filing suit.

II. THE TWO-ISSUE RULE DOES NOT APPLY TO DEFENDANTS' CHALLENGE TO THE TRIAL COURT'S RULINGS AS TO THE RECREATIONAL EASEMENT.

The Court of Appeals misapplied the two-issue rule. The merits of the validity of the 2000 Recreational Easement pose a novel and important question as to whether the after-acquired title doctrine applies to servitudes. The Court of Appeals declined to address the merits because this Court has not previously addressed "this precise issue." (App. p. 24.) This Court should reject the "gotcha' game"[7] employed by the Court of Appeals to summarily dispose of this issue and address the trial court's rulings as to the Recreational Easement.

Whether the execution of the 2000 Recreational Easement was an arms-length transaction was simply not a significant—or even minor—factor in the trial court's ruling. A cursory review of the trial court's eight-page order demonstrates only two passing references to "arms-length transaction": 1) it is included as one of two items that "gives [the] court pause" in an introductory clause to a statement regarding equitable concerns; and 2) it is listed in the concluding paragraph of the order. (R. pp. 70-78.) There was neither any factual discussion of what the trial court meant by "arms-length transaction" nor any legal analysis of this term. *Id.* Defendants addressed the trial court's "equitable concerns" at length in discussing the after-acquired title doctrine. (App. pp. 155-160.)

The HOA is correct that Defendants did not challenge the termination of the Recreational Easement in 2014 when the Assembly acquired the Creek Club and the boating facilities in a partial settlement. However, Defendants have consistently challenged the trial court's ruling as to the

[7] *See Atl. Coast Builders & Contractors, LLC v. Lewis*, 398 S.C. 323, 333, 730 S.E.2d 282, 287 (2012) (Toal, C.J., dissenting).

validity of the Recreational Easement *prior* to the Assembly's acquisition because it affects Plaintiffs' claim of damages. (App. pp. 155-56.)

The Court should grant certiorari to rule that the after-acquired title doctrine applies to servitudes and determine that the 2000 Recreational Easement was valid and perpetual.

CONCLUSION

For the reasons and under the circumstances discussed above, this Court should grant certiorari and reverse the Court of Appeals. All other arguments in Plaintiffs' return that address issues raised in Plaintiffs' petition will be addressed in Defendants' return to that petition.

Respectfully submitted,

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July 31, 2019
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CERTIFICATE OF SERVICE

I, Pamela Jones, Paralegal at Duffy & Young, LLC, certify that I have served the **REPLY TO PETITIONERS-RESPONDENTS' RETURN TO PETITION FOR WRIT OF CERTIORARI** on Petitioners-Respondents' on July 31, 2019 by U.S. First Class mail to their attorneys of record as shown below:

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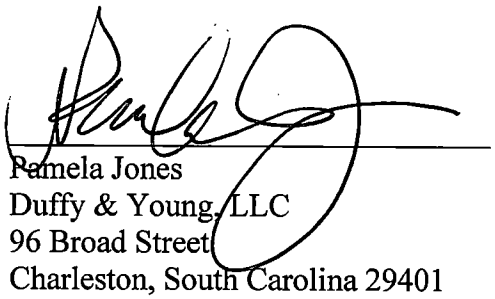

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