THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM YORK COUNTY
Court of Common Pleas

S. Jackson Kimball, Special Circuit Court Judge

Appellate Case No. 2016-002317

Lloyd C. (Chad) Whitmire ..... Respondent,

v.

Johnny C. (Carl) Hawkensen and
The Commons at Fort Mill, LLC, ... Appellants.

FINAL BRIEF OF APPELLANTS

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STATEMENT OF THE CASE

This action was commenced on August 19, 2016, with the Respondent's filing of a summons and complaint naming as defendants the Appellants herein, Johnny C. Hawkensen and The Commons at Fort Mill, LLC. (R. pp. 16, 17). In the Complaint, Respondent asserted nine separate causes of action, all based on his membership in and the operation of the appellant limited liability company.[1]

Contemporaneously with the Summons and Complaint, Respondent filed a Motion to Appoint Receiver (R. p. 116) and a supporting Affidavit of Lloyd C. Whitmire. (R. p. 143). On September 6, 2016, Appellants filed a Motion to

[1] Specifically, Respondent asserted claims for (1) breach of duty of loyalty, (2) breach of duty of care, (3) breach of contract, (4) breach of contract accompanied by fraudulent act, (5) gross negligence, (6) unfair trade practices, (7) declaratory judgment regarding percentage ownership interest, (8) reformation of organizational chart, and (9) dissociation.

Compel Arbitration (R. p. 120) and, attached as an exhibit, a copy of the limited liability company's Operating Agreement. On September 13, 2016, Appellants filed several affidavits in opposition to Repondent's motion for appointment of a receiver. (R. pp. 151, 154, 159, 161).

On September 15, 2016, the circuit court heard arguments on both pending motions and instructed counsel for Respondent to submit proposed orders. On September 30, 2016, the circuit court entered an order denying Respondent's motion for appointment of a receiver but requiring Appellants to produce certain financial records. (R. p. 1). On October 3, 2016, expressly reserving the right to pursue arbitration, Appellants filed their Answer and Counterclaims. (R. p. 18) On October 6, 2016, the circuit court entered a second order, this time denying Appellants' motion to compel arbitration. (R. p. 6).

Appellants subsequently moved for the circuit court to reconsider both rulings, with a motion to reconsider the order denying appointment of a receiver filed on October 11, 2016, (R. p. 136) and a motion to reconsider the order denying arbitration filed on October 14, 2016. (R. p. 139). Although the circuit court denied Respondent's request for a receivership, it also ordered ongoing production of financial statements and left open the possibility of future judicial reconsideration of the receivership issue. Accordingly, Appellants requested reconsideration of the rulings in the receivership order on the ground that, since the underlying dispute is subject to arbitration as argued by the Appellants, the circuit court lacked jurisdiction to order any such relief.

The Appellants' motions to reconsider the two prior orders came before

the circuit court for a hearing on October 31, 2016, and, on November 1, 2016, the circuit court entered a Form 4 order denying the motions. (R. p. 14). Appellants' Notice of Appeal was served on November 14, 2016, and then timely filed, commencing this appeal.

FACTS

This litigation is based on a dispute between Respondent Chad Whitmire and Appellant Carl Hawkensen over their relative membership interests in The Commons at Fort Mill, LLC ("the Company"), also an Appellant. Hawkensen and the Respondent maintained a business relationship for a number of years, involving a succession of entities and, at times, other investors not party to this matter. (R. p. 18, ¶ 6). In October 2014, Respondent and Hawkensen formed the Company, a manager-managed limited liability company. (R. p. 20, ¶ 23; R. pp. 149 – 50). The three members of the Company were Hawkensen, Respondent, and another entity called Blue Wave Management, Inc., of which Hawkensen and Respondent were the only two shareholders. (R. p. 123). Shortly after forming, the company took title to and assumed operation of a 144-unit apartment complex in Fort Mill. (R. p. 20, ¶ 24).

On October 28, 2014, Respondent and Hawkensen executed an operating agreement for the company. (R. p. 123). At the top of the first page of the Operating Agreement, it is stated that "THE TERMS AND CONDITIONS OF THIS OPERATING AGREEMENT ARE SUBJECT TO BINDING ARBITRATION PURSUANT TO S.C. CODE ANN. 15-48-10, ET SEQ." (R. p. 123). In December 2014, in connection with an $11 million loan closing to finance the Company's

acquisition of the apartment complex, Respondent and Hawkensen signed an organizational chart. The organizational chart reflected Respondent's ownership interest in the Company at thirteen (13%) percent and Hawkensen's interest of at least eighty-six (86%) percent[2]. (R. p. 21, ¶¶ 28, 32; R. p. 42, ¶ 131; R. pp. 151 – 52, ¶ 4; R. p. 187).

Many months later, a disagreement developed when Respondent asserted that he owned a greater percentage interest in the Company than indicated in the organizational chart. Respondent asserts that he and Hawkensen each own equal fifty (50%) percent interests. (R. p. 20, ¶¶ 26 - 27). Hawkensen, on the other hand, asserts that Respondent owns a minority interest of thirteen (13%) percent. (R. p. 42, ¶ 131). Under the governing terms of the Operating Agreement, the relative extent of Respondent's ownership in the Company is determinative of his distributional interest and of his power to influence management of the entity's business activities. (R. p. 125, Art. II, Sec. 8; R. p. 127, Art IV, Sec. 1).

In late July or early August 2016, Respondent dissociated from the Company, (R. p. 31, ¶ 94; R. p. 38, ¶ 94), and shortly thereafter initiated the civil action underlying this appeal.

ARGUMENT

"Arbitrability determinations are subject to *de novo* review." Bradley v. Brentwood Homes, Inc., 398 S.C. 447, 453, 730 S.E.2d 312, 315 (2012) (quoting

[2] Repondent alleged that the organizational chart attributed 87% ownership to Hawkensen. (R. p. 31, ¶ 32). Hawkensen alleged that the organizational chart attributed 86% ownership to Hawkensen and 1% ownership to Blue Wave Management, Inc. (R. p. 42, ¶ 131).

Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 22, 644 S.E.2d 663, 667 (2007). "Nevertheless, a circuit court's factual findings will not be reversed on appeal if any evidence reasonably supports the findings." Id. However, '[t]he construction of a written instrument is, in the first instance, a question of law for the court." Campbell v. Bi-Lo, Inc., 301 S.C. 448, 451, 392 S.E.2d 477, 479 (Ct. App. 1990). "Interpretation of an unambiguous agreement is for the court." Pearson v. Church of God, 325 S.C. 45, 54, 478 S.E.2d 849, 853 (1996). Likewise, "[t]he issue of interpretation of a statute is a question of law for the Court." Hopper v. Terry Hunt Const., 383 S.C. 310, 314, 680 S.E.2d 1, 3 (2009). On appeal, questions of law are subject to *de novo* review. State v. Adams, 409 S.C. 641, 647, 763 S.E.2d 341, 344 (2014).

"[T]he party resisting arbitration bears the burden of proving that the claims at issue are unsuitable for arbitration." Wilson v. Willis, 416 S.C. 395, 408–09, 786 S.E.2d 571, 578 (Ct. App. 2016), reh'g denied (June 24, 2016).

I. The circuit court erred in holding that the operating agreement does not include an arbitration clause

The circuit court's denial of Appellants' motion to compel arbitration was based on its incorrect conclusion that the Operating Agreement language regarding binding arbitration was insufficient to create an agreement to arbitrate pursuant to the South Carolina Uniform Arbitration Act ("SCUAA"). S.C. Code § 15-48-10, et seq. Specifically, the circuit court held in its order denying Appellants' motion that, under Section 15-48-10, "[i]t is clear that an 'agreement' to arbitrate and a 'notice' of arbitration are separate and distinct requirements, both of which must exist before arbitration may be compelled . . . . [T]he mere

presence of a notice, without a specific agreement to arbitrate, is insufficient." (R. p. 11). This conclusion misreads the parties' contract and the applicable statute, and fails to account for relevant case law demonstrating the well-established public policy in favor or arbitration.

"The policy of the United States and South Carolina is to favor arbitration of disputes." Zabinski v. Bright Acres Associates, 346 S.C. 580, 596, 553 S.E.2d 110, 118 (2001). "Courts should apply ordinary state-law principles that govern the formation of contracts in determining whether an agreement to arbitrate exists." The Hous. Auth. of City of Columbia v. Cornerstone Hous., LLC, 356 S.C. 328, 335, 588 S.E.2d 617, 621 (Ct. App. 2003).

"The cardinal rule of contract interpretation is to ascertain and give legal effect to the parties' intentions as determined by the contract language." Maybank v. BB&T Corp., 416 S.C. 541, 787 S.E.2d 498, 516 (2016), reh'g denied (July 13, 2016). "When the contract's language is clear and unambiguous, the language alone determines its force and effect." Id. "Whether enforcing an agreement to arbitrate or construing an arbitration clause, courts and arbitrators must give effect to the contractual rights and expectations of the parties. In this endeavor, as with any other contract, the parties' intentions control." Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp., 559 U.S. 662, 682 (2010) (internal citations omitted).

a. The plain language of the operating agreement includes a broadly worded arbitration provision

In the case at hand, the agreement provided that "THE TERMS AND CONDITIONS OF THIS OPERATING AGREEMENT ARE SUBJECT TO

BINDING ARBITRATION PURSUANT TO S.C. CODE ANN. 15-48-10, ET SEQ."

This language clearly constitutes "a provision in a written contract to submit to arbitration any controversy thereafter arising between the parties." § 15-48-10(a). While contracts sometimes contain arbitration clauses of greater length and detail, nothing in the relevant statute or case law requires anything beyond a succinct expression of the parties' intent to subject the agreement to dispute resolution by way of arbitration.

The Court of Appeals has explicitly recognized that a concise statement of intent to arbitrate is sufficient to create an agreement. In an opinion analyzing a construction dispute involving two successive contracts, the Court of Appeals held that

> [B]oth contracts contained broadly worded arbitration agreements. The first contract stated, **"This contract is subject to arbitration under S.C.Code ANN 15-48-10, ET SEQ."** The second contract stated, **"This contract is subject to binding arbitration under the Commercial Arbitration Rules of the American Arbitration Association."**

The Hous. Auth. at 337, 588 S.E.2d at 622 (emphasis added). The Court again emphasized that "[e]ach contract contained an arbitration provision that covered disputes arising between [the parties]", Id. at 335-36, 588 S.E.2d at 621, and that "[r]eading the two contracts in this case together, it is evident the parties agreed that any dispute arising after the signing of the first contract was to be arbitrated." Id. The concise language under consideration in Hous. Auth. is virtually identical to the language in the Operating Agreement in the case at hand.

Furthermore, the Court of Appeals has held that a provision stating that disputes are "subject to" an arbitration statute providing procedural terms is

sufficient to constitute an agreement to arbitrate, even in the absence of specific terms as to "how an arbitrator is chosen; what discovery rules apply; how arbitration fees are allocated; and how arbitration is initiated." York v. Dodgeland of Columbia, Inc., 406 S.C. 67, 82, 749 S.E.2d 139, 146 (Ct. App. 2013) (applying Federal Arbitration Act, 9 U.S.C.A. § 1, et seq.) "[A] party who signed a contract is deemed to have read and understood 'the effect' of the contract . . . and the ordinary meaning of 'subject to,' [is] that all disputes within the scope of the provision must be arbitrated." Id. at 81, 749 S.E.2d at 146. The SCUAA includes specific default provisions on a broad range of procedural issues. See, e.g., §§ 15-48-50, -80.

If, for example, the Operating Agreement contained nothing more than a notice stating that, "this agreement contains an arbitration provision," or words to that affect, such a provision might arguably be interpreted as falling short of a binding agreement to arbitrate. However, this is clearly distinguishable from the actual provision at issue in this case, which provides that the agreement is in fact "SUBJECT TO BINDING ARBITRATION". (R. p. 123).

Returning to the fundamental issue of the parties' intent in executing the Operating Agreement, it is hard to imagine that the Respondent intended anything other than to submit disputes to arbitration when he signed an agreement stating at the top of the first page, in bold, underlined, all-capital font, that the agreement is subject to binding arbitration. This provision also satisfies the notice requirement in the SCUAA, which is intended precisely to ensure that parties are aware they are consenting to arbitration. The Respondent is legally

bound as though he had read the language of the Operating Agreement, York, supra, and the law requires that his intent be determined from the plain language of the agreement he not only signed, but initialed on the very page where the arbitration agreement appears. (R. p. 123).

b. Section 15-48-10 does not require that an arbitration provision be separate from the statutory arbitration notice

Furthermore, the circuit court's order declining to compel arbitration appears to rely on a conclusion that, because the SCUAA makes separate reference to both (1) "a provision in a written contract to submit to arbitration" and (2) a "[n]otice that a contract is subject to arbitration", § 15-48-10(a), a single provision cannot serve as both the agreement and the notice. The statute simply does not contain any such arbitrary technicality.

While contracts often do contain separate notice and "dispute resolution" provisions for practical reasons or formatting purposes, such as the parties' desire to include more detailed arbitration terms or to utilize a tidy cover page without any substantive provisions, that merely highlights the fact that contracting parties are likewise free to instead employ the efficiency of a one-line, front page arbitration provision and notice. Neither the SCUAA nor any recognized principle of statutory interpretation empowers the circuit court to retroactively make this drafting decision on the parties' behalf. See, e.g., MailSource, LLC v. M.A. Bailey & Assocs., 356 S.C. 363, 369, 588 S.E.2d 635, 639 (Ct. App. 2003) ("re-writ[ing] the parties' contract [is] a service the courts of South Carolina do not perform.").

The purpose of the notice requirement in § 15-48-10, as is self-evident from the language of the statute and the very existence of the requirement, is to ensure that parties are aware that important rights are affected by an arbitration clause which may be buried deep in the fine print. The technical requirement that arbitration notice be in capitalized, underlined language on the first page of the contract, far from arbitrary even though strictly enforced by the courts, serves to ensure that a party to a contract does not unknowingly waive the right to judicial dispute resolution.

The notice requirement also provides the courts with a bright-line rule for determination of the otherwise difficult question of whether a party should be able avoid application of an arbitration provision based on alleged lack of notice. Soil Remediation Co., 323 S.C. at 457, 476 S.E.2d at 151. On the other hand, the circuit court's ruling that a properly drafted notice cannot also function as an enforceable arbitration provision does nothing other than to judicially insert an arbitrary technicality, serving no purpose except frustration of the clearly stated intentions of the parties and the public policy in favor of arbitration.

II. The circuit court erred in holding that the arbitration language in the Operating Agreement does not cover the parties' dispute

The parties have unambiguously agreed to submit the types of disputes at issue in this litigation to arbitration. As set forth below, each of the Respondent's claims are based on and require specific reference to and application of the terms and conditions of the parties' Operating Agreement. The plain language of the contract demonstrates the parties' clear intention to subject disputes over the

operation of the LLC to arbitration. Each of the Plaintiff's claims is clearly based on allegations about the operation and management of the Company. In essence, each of the Respondent's causes of action is an attempt to enforce some provision of the Operating Agreement or to seek relief regarding issues that are specifically governed by it.

"The operating agreement is the essential contract that governs the affairs of a limited liability company." S.C. Code Ann. § 33-44-103, *cmt.* The S.C. Supreme Court has recognized that courts may only discern parameters governing members' operation and management of an LLC by reference to the terms and conditions of the operating agreement. Dutch Fork Dev. Grp. II, LLC v. SEL Properties, LLC, 406 S.C. 596, 606, 753 S.E.2d 840, 845 (2012). "The operating agreement governs: (1) relations among the members as members and between the members and the limited liability company; (2) *the rights and duties of a person in the capacity of manager;* (3) the activities of the company and the conduct of those activities; and (4) the means and conditions for amending the operating agreement." Id. at 606, 753 S.E.2d at 845 fn. 6 (quoting 51 Am.Jur.2d *Limited Liability Companies* § 4 (2011)) (emphasis in original).

The circuit court held that the Respondent's claims are beyond the scope of the arbitration language in the Operating Agreement. The heart of the circuit court's analysis on this issues is the finding that "[Respondents'] claims do not turn upon the 'terms and conditions' of the Operating Agreement. (R. p. 12). The circuit court held that, if the parties had intended broad arbitration language to cover the claims asserted in this matter, they could have included a provision

requiring that "'any and all disputes' between them be arbitrated." (R. p. 12). This analysis directly contradicts clear South Carolina law.

"The heavy presumption of arbitrability requires that[,] when the scope of the arbitration clause is open to question, a court must decide the question in favor of arbitration." Wilson, 416 S.C. at 413, 786 S.E.2d at 580. Beyond the initial question of the existence of an enforceable agreement, discussed above, "[t]o decide whether an arbitration agreement encompasses a dispute, a court must determine whether the factual allegations underlying the claim are within the scope of the broad arbitration clause, regardless of the label assigned to the claim. Any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." Zabinski at 597, 553 S.E.2d at 118 (internal citations omitted).

> [U]nless the court can say with positive assurance that the arbitration clause is **not susceptible to an interpretation that covers the dispute**, arbitration should be ordered. A motion to compel arbitration made pursuant to an arbitration clause in a written contract should only be denied where the clause is not susceptible to **any interpretation** which would cover the asserted dispute.

Id. at 597, 553 S.E.2d at 118–19 (emphasis added).

The order denying arbitration acknowledged that "[t]his lawsuit arises from, among other things, the parties' dispute over their relative membership interests[.]" (R. p. 8). While the liberal standard for enforcement of the arbitration clause requires consideration only of whether "the clause is not susceptible to any interpretation which would cover the asserted dispute", Zabinski, supra, in this case it is difficult to conceive of any interpretation of the clause that would *not* encompass the Plaintiff's claims.

a. The arbitration provision is susceptible to interpretation that would cover the asserted disputes

The plain language of the broad arbitration provision makes it clear that the Respondent's claims are incapable of resolution without application of the "terms and conditions" of the Operating Agreement and are therefore subject to arbitration. The language of the arbitration provision did not limit its applicability by, for example, stating that arbitration would only apply to disputes over *interpretation* of the Operating Agreement. At a minimum, under South Carolina's liberal standard for arbitrability, the parties' arbitration agreement is susceptible to an interpretation that would cover the asserted disputes. Zabinski at 597, 553 S.E.2d at 118-19.

i. Breach of Duty of Loyalty and Duty of Care

Respondent's first and second causes of action, asserted against Hawkensen individually for breach of duty of loyalty and breach of duty of care, are only actionable to the extent that Hawkensen has been or has acted in the capacity of a manager of the company[3]. § 33-44-409(h). The LLC statute provides that the duty of loyalty of a party acting in a management capacity is limited, in relevant part, to the following:

> (1) to account to the company and to hold as trustee for it any property, profit, or benefit derived by the member in the conduct or winding up of the company's business or derived from a use by the member of the company's property, including the appropriation of a company's opportunity; [and] (2) to refrain from dealing with the company in the conduct or winding up of the company's business as or on behalf of a party having an interest adverse to the company

[3] The Operating Agreement provides that "[t]he initial manager shall be Blue Wave Management, Inc." (R. p. 126, Art 3, Sec. 1).

§ 33-44-409(b). Likewise, an acting manager's duty of care is "limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." § 33-44-409(c).

Respondent alleges that Hawkensen breached the duties of loyalty and care through a number of instances of use and management of Company property and funds. (R. p. 21 – 22, ¶ 35; R. pp. 24 – 25, ¶¶ 47, 52). Crucially, the Operating Agreement contains, among numerous other provisions relevant to these allegations, detailed provisions governing the Company manager's responsibilities, powers, authority to transfer Company property, and compensation. (R. pp. 125 – 26, Art. 3).

Accordingly, to the extent that Hawkensen did assume any duties of loyalty and care by acting in a management capacity as alleged, determination of any breach of duty requires primary and continuous reference to the governing provisions of the Operating Agreement. Notably, with regard to the duty of care, it appears impossible to determine whether a manager has engaged in tortious conduct without specific reference to what the governing agreement authorizes and forbids the manager to do. These causes of action are based on and inextricably tied to the terms and conditions of the Operating Agreement.

ii. Breach of Contract and Breach of Contract Accompanied by Fraudulent Act

Respondent's third and fourth causes of action, asserted against Hawkensen individually for breach of contract and breach of contract accompanied by fraudulent act, attempt to hypothetically rewind the clock to a point in time when Hawkensen and Respondent had agreed upon, but not yet

executed, a plan to form the Company and convey to it business operations and assets formerly held by other entities. Respondent does not plead his breach of contract theory on the basis of the Operating Agreement, but instead asserts that it is this prior agreement to organize the Company in a particular way that Hawkensen has breached. (R. p. 26, ¶¶ 57 – 60). This ambitious reframing of the dispute does not change the fact that these causes of action, however named, are in reality based on a disagreement as to percentage ownership of the Company.

By the Respondent's own pleading, Hawkensen's alleged "breach of contract" occurred, in its entirety, "when he failed to honor his agreement with [Respondent] and refused to treat [Respondent] as an equal and bona fide member of the Company." (R. p. 26, ¶ 60). The alleged "agreement with [Respondent]" at issue was "that their ownership interests in the Company would be identical to their prior interests in [a predecessor entity], with each member holding an equal (50% +/-) interest in the Company." (R. p. 26, ¶ 58). The purported "fraudulent acts" alleged by Respondent involve (1) inequitable membership distributions, (2) "self-dealing and fraudulent transactions with the Company," and (3) asserting that Respondent possesses only a minority interest in the Company. (R. p. 26, ¶ 63).

The Operating Agreement contains, among other relevant provisions, specific and detailed clauses governing "Certificates of membership interests", "Transfer of member's interests", "Capital account[s]", "Profits and losses", "Distributions", and "Dissolution and Liquidation." (R. p. 123 - 29, Art. I, IV, VI).

The actual claim asserted by the two causes of action designated by Respondent as "breach of contract" is a request for relief due to a disagreement about the percentage of Respondent's membership interest. This is a claim for relief based on, and requiring reference to and application of, the terms and conditions of the Operating Agreement governing ownership and management of the Company.

Finally, any prior agreement to organize the Company was merged and extinguished when the Company was formed and the Operating Agreement was enacted, and therefore as a matter of law cannot be the subject of the current dispute. Although Respondent attempts in his pleadings to characterize this in part as a dispute about a prior agreement with Hawkensen to organize the Company with equal membership interests, the only logical interpretation of the Complaint as a whole is that Respondent alleges:

(1) Following a series of disputes with fellow members of prior business entities, Respondent and Hawkensen decided to resolve the disputes and move forward by buying the interest of the other members and to organize the Company for the purpose of carrying on a going business concern, (R. pp. 19 – 20, ¶¶ 20 – 23);

(2) Respondent and Hawkensen agreed to set up the Company with equal ownership interests, (R. p. 26, ¶ 58);

(3) Respondent and Hawkensen did in fact organize the Company with equal ownership interests and, therefore, Respondent does have an interest of approximately 50%, (R. p. 26, ¶ 59); and

(4) Hawkensen now refuses to recognize or allow Respondent the benefit of his full membership interest. (R. p. 26, ¶ 60).

In other words, Respondent's allegation is that he and Hawkensen did in fact execute the alleged prior agreement to set up an equally owned limited liability company. It follows that, when the Company was formed and organized, any prior agreement was merged into the operating agreement and extinguished. 30 S.C. Jur. Contracts § 73 ("Upon the execution of a valid substituted agreement, the original agreement becomes merged into it and is extinguished."). Accordingly, the rights of the parties with respect to ownership interests in the Company are governed by the Operating Agreement, and not by any prior agreements.

iii. Gross Negligence

Respondent's fifth cause of action, asserted against Hawkensen individually, is for negligence and gross negligence. While Respondent baldly alleged, without any further explanation, that Hawkensen's purported duty of care towards Respondent "arose independently of Hawkensen's and [Respondent]'s membership in the Company," (R. p. 27, ¶ 67), the more detailed allegations of what Hawkensen supposedly did to *breach* this duty make it clear beyond doubt that Respondent objects specifically to the supposed mismanagement, use and disposal of Company property and funds, and to nothing else whatsoever (and certainly not to any conduct outside the scope of management of the Company).

Furthermore, returning to the question of the source of Hawkensen's alleged duty of care, the LLC statute specifies that any duty of care would only

apply to management activity and would be "limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." § 33-44-409(c), -(h)(1). Once again, analysis of any such tortious conduct requires specific reference to what the Operating Agreement authorizes and forbids the manager to do.

iv. Unfair Trade Practices

Respondent's sixth cause of action, also asserted against Hawkensen individually, is for unfair trade practices. Specifically, Respondent alleges in his pleadings that Hawkensen engaged in unfair and deceptive conduct by inducing Respondent to sign an organizational chart showing purportedly inaccurate ownership interests in order to obtain a loan for the Company; by asserting that Respondent possesses only a minority interest in the Company; by denying Respondent access to Company records and accounts; and by disbursing and withholding distributions inequitably. (R. p. 21, ¶ 28; R. p. 28, ¶ 73). As referenced above in the discussion of the breach of contract claims, the Operating Agreement includes specific provisions governing all of these issues. (*See also* Operating Agreement Art. V ("Financial Statements and Books") (R. p. 128). Accordingly, this cause of action as well is based on and inextricably tied to the terms and conditions of the Operating Agreement.

v. Declaratory Judgment and Reformation of Organizational Chart

Respondent's seventh and eighth causes of action, asserted against both Appellants, are for declaratory judgment and "Reformation of Organizational Chart." Specifically, Respondent seeks "declaratory judgment that his ownership

interest in the Company is equal to the ownership interest of Hawkensen, with each holding an equal 50% +/- interest in the Company", (R. p. 30, ¶ 87), and reformation of an organizational chart to reflect equal ownership. (R. p. 31, ¶ 90). Once again, the dispute over percentage membership interests is based upon and cannot be resolved without reference to and application of the Operating Agreement, which includes detailed provisions governing the creation and benefits of such interests in proportion to member contributions. The Operating Agreement specifically provides, for example, that "[t]he company shall have the power to issue certificates of membership interest . . . The denominations of the certificates shall correspond to the amount of capital contributed by the member to the company." (R. p. 123, Art. I, Sec. 1. *See also* R. p. 127, Art. IV, Sec. 1 ("Capital Account")).

vi. Dissociation

Finally, Respondent's ninth cause of action is for dissociation. Specifically, Respondent seeks a determination of the value of his distributional interest in the Company and an order requiring the Company to purchase his interest at fair value. The Operating Agreement contains specific, detailed provisions governing determination of the proportional value and accessibility of distributional interests and the effect of a member's resignation. (R. pp. 127 – 29, Art. IV, VI). As with the other claims, this cause of action can only be addressed by reference to and application of the terms and conditions of the Operating Agreement.

b. A "significant relationship" exists between Respondent's claims and the Operating Agreement

"[E]ven if the court finds that a claim is outside the scope of the arbitration clause, the clause may still apply." Wilson, 416 S.C. at 413–14, 786 S.E.2d at 580 (quoting Partain v. Upstate Auto. Grp., 386 S.C. 488, 492, 689 S.E.2d 602, 604 (2010)). Specifically, "a broadly-worded arbitration clause applies to disputes that do not arise under the governing contract when a 'significant relationship' exists between the asserted claims and the contract in which the arbitration clause is contained." Zabinski, 346 S.C. at 598, 553 S.E.2d at 119.

Our state Supreme Court has recognized that the "significant relationship" standard, rephrased, requires that "broad arbitration clauses encompass all claims that 'touch matters' covered by the contract or agreement." Landers v. Fed. Deposit Ins. Corp., 402 S.C. 100, 116, 739 S.E.2d 209, 217 (2013). The Court of Appeals has held that arbitration provisions virtually identical to the language in the Repondent and Appellants' operating agreement were "broadly worded arbitration agreements." The Hous. Auth., 356 S.C. at 337, 588 S.E.2d at 622.

In Landers, the S.C. Supreme Court considered whether an employment contact arbitration clause required arbitration of a former bank employee's claim against the bank's chief executive officer for employment related defamation. 402 S.C. at 112, 739 S.E.2d at 215. The Court held that the tort claim did bear a significant relationship to the contract, because "[t]he perceived inability to perform one's *job* certainly relates to an *employment* contract." Id. (emphasis in original). The Court noted a "clear nexus between [the] claims and the

employment contract sufficient to establish a significant relationship to the employment agreement." Id. at 103, 739 S.E.2d at 210.

In the case at hand, for the same reasons detailed in the discussion above of each of the Respondent's causes of action, it is clear that all of the asserted claims have a clear nexus with and touch upon the terms and conditions of the Operating Agreement, and therefore have a significant relationship with the terms of the parties' governing agreement. The Respondent's claims simply cannot be decided without reference to and application of the terms and conditions of the Operating Agreement. Accordingly, even if the Court finds that the arbitration provision is not susceptible to any interpretation that would cover the asserted claims, the provision is nonetheless binding here because of the "significant relationship" between the Operating Agreement and the Respondent's claims all requiring reference to and application of the agreement.

III. The circuit court erred in holding that the parties' dispute does not involve interstate commerce and therefore trigger application of the Federal Arbitration Act

The circuit court further erred in holding that the Operating Agreement and the business operation governed by the Operating Agreement do not touch on interstate commerce. Accordingly, even assuming for the sake of argument that the arbitration agreement in this case were somehow technically deficient under the SCUAA, the agreement would nonetheless be enforceable under the Federal Arbitration Act ("FAA"). 9 U.S.C. §1, et seq.

The FAA applies where an arbitration provision is included in a contract "evidencing a transaction involving [interstate] commerce". 9 U.S.C.A. § 2. "The

terms 'involving commerce' amount to the functional equivalent of 'affecting commerce' and signal an intent to exercise Congress' commerce clause power to the full." Towles v. United HealthCare Corp., 338 S.C. 29, 36, 524 S.E.2d 839, 843 (Ct. App. 1999) (quoting Allied–Bruce Terminix Co. v. Dobson, 513 U.S. 265, 277 (1995)). "The phrase 'evidencing a transaction' only requires 'that the 'transaction' in fact 'involv[e]' interstate commerce, even if the parties did not contemplate an interstate commerce connection.'" Id. "To ascertain whether a transaction involves commerce within the meaning of the FAA, the court must examine the agreement, the complaint, and the surrounding facts." Id.

The S.C. Supreme Court has held that a dispute over a contract with an agreement to submit to "ARBITRATION PURSUANT TO SECTION 15–48–10, CODE OF LAWS OF SOUTH CAROLINA (1976)", although technically deficient under the strict terms of the South Carolina statute, was nonetheless subject to arbitration under the FAA. Soil Remediation Co., 323 S.C. at 456, 476 S.E.2d at 150 (finding the quoted language deficient because it was not underlined). As the Court explained in a later opinion discussing Soil Remediation Co., "[s]tate law was therefore preempted *to the extent it would have invalidated the arbitration agreement.*" Munoz v. Green Tree Fin. Corp., 343 S.C. 531, 539, 542 S.E.2d 360, 363 fn.2 (2001) (emphasis in original).

This case involves interstate commerce because it is undisputed that while Appellants are residents of South Carolina, Respondent is a resident of North Carolina. (R. p. 17, ¶ 1 – 3). Furthermore, the Company financed the purchase of its primary asset, the apartment complex in Fort Mill, using proceeds

of an $11 million loan provided by a Delaware limited partnership operating out of New York. (R. p. 186; R. p. 151, ¶ 3). The S.C. Supreme Court has recognized that a business operation involving out-of-state investors implicates interstate commerce. Zabinski, 346 S.C. at 595, 553 S.E.2d at 118.

Additionally, one of the many disputed issues between the parties is the ownership of a tract of real property located in Mooresville, North Carolina. (R. p. 40, ¶ 107; R. p. 44, ¶ 146; R. p. 153, ¶ 14). Specifically, the Appellants allege that Company funds were used to purchase the property and that the Company has either a legal or an equitable ownership interest in the property. The Appellants seek imposition of a resulting trust on that basis.[4] (R. p. 44, ¶ 147). Resolution of this aspect of the dispute directly implicates and requires reference to provisions of the Operating Agreement relating to, among other issues, the value of member's capital accounts based on the fair market value of Company property and loans from the Company to members. (R. p. 127, Art. IV, Sec. 1(a) and 3).

Courts have made it clear that this disputes over this type of multi-state property ownership affects interstate commerce. Cohoon v. Ziman, 298 S.E.2d 729, 731 (N.C. App. 1983) (agreement affected interstate commerce where partners were residents of North Carolina and South Carolina and partnership engaged in real estate transactions in both states). See also Snyder v. Smith, 736 F.2d 409, 418 (7th Cir. 1984) (Illinois partnership's ownership of Texas real estate affected interstate commerce) (overruled on other grounds by Felzen v.

[4] The Respondent's Answer to Counterclaim was not filed until after the October 31, 2016, hearing, and was not part of the record before the circuit court.

Andreas, 134 F.3d 873 (7th Cir. 1998)); Pioneer Properties, Inc. v. Martin, 557 F. Supp. 1354, 1364 (D. Kan. 1983) (Kansas citizen's investment in Canadian real estate affected interstate commerce).

Finally, although the arbitration agreement in this matter is enforceable under the FAA, the parties' agreement to submit to arbitration pursuant to the provisions of the SCUAA is still binding. In other words, arbitration of this matter is subject to the rules and procedures set forth in the South Carolina arbitration statute. While the FAA preempts state laws purporting to invalidate agreements to arbitrate matters of interstate commerce, "it does not follow that the FAA prevents the enforcement of agreements to arbitrate under different rules than those set forth in the Act itself." Volt Info. Scis., Inc. v. Bd. of Trustees of Leland Stanford Junior Univ., 489 U.S. 468, 479 (1989). "[P]arties are free to enter into a contract providing for arbitration under rules established by state law rather than under rules established by the FAA." Munoz at 539, 542 S.E.2d at 363 fn.2.

Accordingly, because the dispute in this matter involves interstate commerce, the Operating Agreement provision providing for arbitration pursuant to the procedures of SCUAA is enforceable under the FAA even if the arbitration provision is for some reason technically deficient under the state statute.

IV. The circuit court erred by asserting jurisdiction over the Respondent's motion for appointment of a receiver and injunctive relief

The circuit court also erred in holding that it had jurisdiction to rule on the Respondent's motion for appointment of a receiver and then issuing an order requiring the Appellants to provide Respondent monthly bank statements and

profit and loss statements during the pendency of the action, with specific leave granted to Respondent to renew his request for a receivership if deemed necessary. (R. p. 5). Admittedly, counsel for Appellants stated at the first hearing that Appellants did not object to voluntarily providing financial statements to Respondent. However, Appellants did not waive their objection to the jurisdiction of the circuit court to *order* such production when the case is rightfully subject to arbitration. (R. p. 81, ln. 3 – 7; R. p. 99, ln. 17 through R. p. 100, ln. 25). *See also* Johnson v. S.C. Dep't of Prob., Parole, & Pardon Servs., 372 S.C. 279, 284, 641 S.E.2d 895, 897 (2007) (objection to lack of subject matter jurisdiction may not be waived). Of most concern to Appellants is the circuit court's purported retention of jurisdiction to award equitable relief with regard to Company financial management.

While the circuit court denied the Respondent's request for appointment of a receiver, and to that extent ruled in favor of Appellants in the order that Appellants now appeal, this issue is justiciable because the order (1) constitutes an assertion of ongoing jurisdiction over the parties' dispute; (2) specifically grants leave to Respondent "to renew the motions should further discovery reveal that the Company's property, or its rents and profits, are in danger of being lost or materially injured during the pendency of this case," (R. p. 5); and (3) imposes on Appellants an ongoing requirement for production of Company financial records. See Peoples Fed. Sav. & Loan Ass'n of S.C. v. Res. Planning Corp., 358 S.C. 460, 477, 596 S.E.2d 51, 60 (2004) ("A justiciable controversy is a real and substantial controversy which is ripe and appropriate for judicial

determination, as distinguished from a contingent, hypothetical or abstract dispute."); Collins Music Co. v. IGT, 365 S.C. 544, 549, 619 S.E.2d 1, 3 (Ct. App. 2005) (applying mootness doctrine exception where "the decision by the trial court can affect future events or have collateral consequences to the parties").

In the event that the Court of Appeals reverses the circuit court's ruling on the motion to compel arbitration, the Appellants do not want to have waived their objection to the circuit court's assertion of jurisdiction over matters of receivership and injunctive relief, or be required to initiate a second appeal if the circuit court again asserts jurisdiction.

a. The circuit court lacks subject matter jurisdiction to award equitable relief in an action subject to arbitration

Because this dispute is subject to binding arbitration, the circuit court does not have jurisdiction over matters of even temporary equitable relief. South Carolina's eventual embrace of arbitration was a reversal of prior law holding that "general arbitration agreements which oust the South Carolina circuit court from jurisdiction are unenforceable as against public policy." Episcopal Hous. Corp. v. Fed. Ins. Co., 269 S.C. 631, 636, 239 S.E.2d 647, 649 (1977). Where a broad arbitration provision is in place and does not specifically reserve to the circuit court jurisdiction over requests for temporary equitable relief such as appointment of a receiver, there is no basis for the circuit court to retain such split jurisdiction.

Undeniably, the circuit court does have jurisdiction over the initial question of whether the parties have agreed to arbitrate. "[A] gateway dispute about whether the parties are bound by a given arbitration clause raises a 'question of

arbitrability' for a court to decide. . . . Similarly, a disagreement about whether an arbitration clause in a concededly binding contract applies to a particular type of controversy is for the court." Howsam v. Dean Witter Reynolds, Inc., 537 U.S. 79, 84 (2002) (internal citations omitted). See also Zabinski, 346 S.C. at 596, 553 S.E.2d at 118.

However, when a binding arbitration clause governs the controversy, the authority of the circuit court extends no further than those "gateway" arbitrability questions unless the parties have agreed otherwise. "Thus 'procedural' questions which grow out of the dispute and bear on its final disposition" are presumptively *not* for the judge, but for an arbitrator, to decide." Howsam at 84. In the case on appeal, the circuit court has stepped beyond the initial gateway questions of arbitrability and waded into consideration and determination of the substantive rights of the litigants. For example, a receiver may not be appointed in the first place "unless there is the strongest reason to believe that the plaintiff is entitled to the relief demanded in his complaint." Pelzer v. Hughes, 27 S.C. 408, 3 S.E. 781, 785 (1887) (discussing prior S.C. Code section with language identical to current § 15-65-10(1)). See also Zabinski at 596, 553 S.E.2d at 118 ("[I]n deciding whether the parties have agreed to submit a particular grievance to arbitration, a court is not to rule on the potential merits of the underlying claims.").

Furthermore, judicial appointment of a receivership pending arbitration of a dispute by necessity implies ongoing circuit court involvement even after it has been divested of jurisdiction. "When a case is sent to arbitration, the circuit court is divested of jurisdiction over the case." Steinmetz v. Am. Media Servs., LLC,

393 S.C. 72, 74, 709 S.E.2d 708, 709 (Ct. App. 2011). "Arbitration is not litigation carried on by other means, but is an alternative means for resolving disputes without the cost and delay of a lawsuit. Judicial review of an arbitration award is limited in scope, and any attempt to convert arbitration into a trial-like judicial proceeding is looked upon with disfavor." Lauro v. Visnapuu, 351 S.C. 507, 516, 570 S.E.2d 551, 555 (Ct. App. 2002). "In bilateral arbitration, parties forgo the procedural rigor and appellate review of the courts in order to realize the benefits of private dispute resolution: lower costs, greater efficiency and speed, and the ability to choose expert adjudicators to resolve specialized disputes." Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp., 559 U.S. 662, 685 (2010). "Any action or proceeding involving an issue subject to arbitration shall be stayed if an order for arbitration . . . has been made." S.C. Code Ann. § 15-48-20(d).

The retention of jurisdiction to grant temporary equitable relief, and in particular the drastic remedy of receivership, would keep the circuit court deeply and continuously involved in resolution of a dispute submitted to arbitration. "A receiver represents the Court appointing him; he is an officer of the Court and is the agency through which the Court acts. . . . He is subject only to the Court's direction." Kirven v. Lawrence, 244 S.C. 572, 580, 137 S.E.2d 764, 768 (1964). Appointment of a receiver "is a stronger measure than that of injunction, in that the effect is to transfer the custody of the property in controversy from a litigant to a third party, under the direction of the court, during the litigation." Pelzer at 784–85. Accordingly, ongoing judicial control of the parties' business affairs pending arbitration would not only thwart the contractually memorialized intent of the

parties to resolve disputes without substantive judicial involvement, but would constitute an impermissible exercise of jurisdiction legally divested upon submission of the case to arbitration. See Steinmetz, supra.

The question of whether an *arbitrator* has authority to appoint a receiver, posed by the circuit court at the hearing in this matter, (R. p. 55, 10 ln. 3 – 8), is ultimately only of academic interest to the issue on appeal. Even if the arbitrator does not have authority to appoint a receiver, it does not follow that on that basis the circuit court does retain jurisdiction to do so. To the extent that a party agreeing to arbitration might therefore altogether forego the right to seek the equitable relief of receivership, this is no more inequitable than the fact that the party has given up, in exchange for the efficiency and other benefits of arbitration, the right to a trial by jury. These are simply the issues that a party to a contract must consider and weigh before agreeing to a binding arbitration provision.

In arguing for appointment of a receiver, counsel for Respondent cited to federal authority for the proposition that "where a dispute is subject to mandatory arbitration under the Federal Arbitration Act, a district court has the discretion to grant a preliminary injunction to preserve the status quo pending the arbitration of the parties' dispute if the enjoined conduct would render that process a 'hollow formality.'" Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bradley, 756 F.2d 1048, 1053 (4th Cir. 1985). The Merrill Lynch opinion is inapplicable to the issues on appeal for several reasons. First, the Fourth Circuit's ruling of the jurisdiction of federal district courts does not affect the prerogative of South Carolina to

determine the jurisdiction of its own circuit courts. Accordingly, the ruling does not supersede the effect of clear South Carolina case law holding that the circuit court is divested of jurisdiction upon submission of a dispute to arbitration. Steinmetz at 74, 709 S.E.2d at 709.

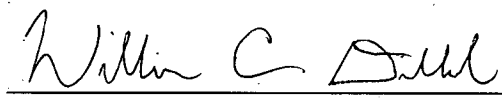
Second, while the Merrill Lynch opinion is based specifically on the Federal Arbitration Act, the agreement at issue in this matter specifies that arbitration is to be governed by the South Carolina Uniform Arbitration Act. The South Carolina statute provides for only minimal participation by the circuit court, such as confirming or modifying arbitration awards based on specific criteria, § 15-48-120, et seq., and does not provide for judicial imposition and enforcement of drastic injunctive relief or receivership. Third, while Merril Lynch refers specifically to authority to issue a preliminary injunction, there is no basis to conclude that its holding should be extended to the even more drastic remedy of receivership, "a stronger measure than that of injunction". Pelzer, 27 S.C. 408, 3 S.E. at 784–85. Whereas the language of Merrill Lynch justifies its holding on the need to preserve the status quo, appointment of a receiver in fact disturbs the status quo by seizing and transferring custody of the relevant property and business affairs.

Accordingly, the circuit court lacked jurisdiction to rule on the merits of the Respondent's motion for appointment of a receiver, and likewise lacked jurisdiction to order Appellants to continuously produce financial records.

CONCLUSION

For the foregoing reasons, the Appellants respectfully submit that the Court of Appeals should reverse the circuit court's order denying Appellants' Motion to Compel Arbitration, should reverse the circuit court's order denying appointment of a receiver to the extent that the order asserted continuous jurisdiction and imposed a requirement for production of financial statements, and should remand this matter for entry of an order compelling arbitration of the parties' dispute.

Respectfully submitted,



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June 7, 2017

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM YORK COUNTY
Court of Common Pleas

S. Jackson Kimball, Special Circuit Court Judge

Appellate Case No. 2016-002317

Lloyd C. (Chad) Whitmire ..... Respondent,

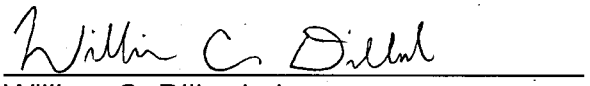
v.

Johnny C. (Carl) Hawkensen and
The Commons at Fort Mill, LLC, ... Appellants.

CERTIFICATE OF COUNSEL

I certify that this Final Brief of Appellants complies with Rule 211(b), SCACR.

June 7, 2017



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