

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM RICHLAND COUNTY
Court of Common Pleas

Robert E. Hood, Circuit Judge

Appellate Case No. 2019-000719

Carrington Mortgage Services, LLC,.....Respondent,

v.

Paul R. Watson,.....Appellant.

INITIAL BRIEF OF APPELLANT

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STATEMENT OF ISSUES

- I. Did the lower court err in striking Appellant's jury demand on legal counterclaims asserted in response to Respondent's mortgage foreclosure and reformation claims, especially where the claims arose out of Respondent's breach of the mortgage contract and where success on the claims would prove the grounds of Appellant's affirmative defenses to Respondent's claims?

STATEMENT OF THE CASE

The Respondent, Carrington Mortgage Services, LLC (hereinafter “Carrington”) brought this action for mortgage foreclosure and reformation of a mortgage against the Appellant, Paul R. Watson (hereinafter “Watson”). (R. pp. ____; complaint pp. 1-4.) Watson answered, asserting affirmative defenses of Carrington’s breach of the mortgage and unclean hands, both arising out of Carrington taking possession of Watson’s property and locking him out of it without permission and without the law or provisions of the mortgage providing Carrington with any right to do so. (R. pp. ____; answer and counterclaim pp. 3-4.) Watson also pled counterclaims for breach of the mortgage contract, trespass, forcible entry and detainer under S.C. Code Ann. §§ 15-67-410 through -470, violation of the South Carolina Unfair Trade Practices Act, S.C. Code Ann. § 39-5-10, *et seq.*, and interference with contract and prospective contract, all based on the same conduct that gave rise to the affirmative defenses. (R. pp. ____; answer and counterclaim pp. 5-7.) Watson demanded a jury trial. (R. pp. ____; answer and counterclaim p. 1.)

Carrington served a reply to the answer and counterclaim and, later, moved to strike Watson’s jury demand. (R. pp. ____; reply; motion to strike.) The motion was heard, taken under advisement, and then granted. (R. pp. ____; order granting motion to strike; transcript.) The circuit judge acknowledged that Carrington conceded that Watson’s counterclaims were legal, but he agreed with Carrington’s assessment of them as permissive, rather than compulsory, counterclaims. (R. pp. ____; order granting motion to strike pp. 2-3.)

Watson moved for reconsideration of that order. (R. pp. ____; motion to reconsider.) The circuit court denied that motion, without a hearing, by a Form 4 order. (R. pp. ____; order denying motion to reconsider.) This appeal followed.

STANDARD OF REVIEW

“Whether a party is entitled to a jury trial is a question of law.” Verenes v. Alvanos, 387 S.C. 11, 15, 690 S.E.2d 771, 772 (2010). “An appellate court may decide questions of law with no particular deference to the [lower] court.” Id. at 15.

ARGUMENT

I. The law in South Carolina about what makes a counterclaim compulsory.

“A pleading *shall* state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party’s claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction.” Rule 13(a), SCRPC (emphasis added). Such claims are usually referred to as compulsory counterclaims. “A pleading *may* state as a counterclaim any claim against an opposing party not arising out of the transaction or occurrence that is the subject matter of the opposing party’s claim.” Rule 13(b), SCRPC (emphasis added). Such claims are usually referred to as permissive counterclaims.

Compulsory, at-law counterclaims made by a defendant in a case in which the plaintiff has asserted only causes of action that sound in equity must be tried by a jury if a jury demand has been made on the claim. Wachovia Bank, N.A. v. Blackburn, 407 S.C. 321, 330, 755 S.E.2d 437, 441 (2014); Johnson v. S.C. Nat. Bank, 292 S.C. 51, 54-56, 354 S.E.2d 895 (1987). Conversely, a defendant waives his right to a jury trial

if he asserts a legal but permissive counterclaim where the plaintiff's complaint pleads only equitable causes of action. Blackburn, 407 S.C. at 330; Johnson, 292 S.C. at 54-56.

What is more difficult in many cases than it seems in the abstract is determining whether a counterclaim is compulsory or permissive. This court has held in this context that “[t]he right of trial by jury is highly favored, and waivers of the right are always strictly construed and not lightly inferred or extended by implication.” Keels v. Pierce, 15 S.C. 339, 342, 433 S.E.2d 902, 904 (Ct. App. 1993); accord Broome v. Watts, 319 S.C. 337, 340, 461 S.E.2d 46 (1995) (same principle, different context); North Charleston Joint Venture v. Kitchens of Island Fudge Shoppe, Inc., 307 S.C. 533, 535, 416 S.E.2d 637 (1992) (same principle, different context); Beach Co. v. Twillman, Ltd., 351 S.C. 56, 64, 566 S.E.2d 863 (Ct. App. 2002) (same principle, different context).

Our Supreme Court has developed a test to determine what “arises out of the transaction or occurrence that is the subject matter of the opposing party’s claim” and is, thus, a compulsory counterclaim. Rule 13(a), SCRPC. In N.C. Fed. Sav. & Loan Ass’n v. DAV Corp., 298 S.C. 514, 518, 381 S.E.2d 903, 905 (1989), a foreclosure action with counterclaims, the Supreme Court adopted the “logical relationship” test for determining whether a counterclaim is compulsory. The Court held that most of DAV’s counterclaims were compulsory because “there [was] a logical relationship between the enforceability of the note which [was] the subject of the foreclosure action and the validity of the purported oral agreement which, if performed, would have avoided default on the note[.]” Id. The Court made clear the reason for doing so: of the four tests considered by the Court for whether a counterclaim is compulsory, the

Court settled on the “logical relationship test,” which is “by far the most widely accepted because of its flexibility.” Id.

In the DAV case, the plaintiff’s claim was for foreclosure of a mortgage, and the Court’s described of DAV’s counterclaims as follows:

- 1) breach of a subsequent oral contract to arrange additional financing for interest payments and construction costs;
- 2) breach of the joint venture agreement as parent company of joint venturer NCF by bringing the foreclosure action;
- 3) breach of fiduciary duty to co-joint venturers;
- 4) wrongful dissolution of the joint venture by failing to voluntarily refrain from foreclosure as agreed;
- 5) violation of the Unfair Trade Practices Act by breaching the oral agreement;
- 6) breach of two subsequent oral contracts to purchase DAV’s interest in the joint venture.

Id. at 517.

The Court held that all but the sixth counterclaim on this list was compulsory. Id. at 518. The logical relationship that each of those counterclaims had to the plaintiff’s foreclosure claim was that each counterclaim arose out of the parties’ relationship that was the subject of the foreclosure claim, dealt with the manner in which the loan was administered, or both. Id.

In Carolina First Bank v. BADD, L.L.C., our Supreme Court, citing the rule that a counterclaim is compulsory if it has a “logical relationship” to the transaction or occurrence subject of the opposing party’s claim, held that a counterclaim is compulsory in a foreclosure action if it arises out of the execution of the documents that form the basis of the plaintiff’s claim or affects the enforceability of the plaintiff’s

claim. 414 S.C. 289, 295, 296, 778 S.E.2d 106, 109, 110 (2015). The Court there found that the counterclaims were not compulsory where they both assumed the enforceability of the guaranty agreements subject of the plaintiff's claim and did not arise from the events of the execution of the guaranty documents. Id. at 296. The Court stated that the claims did "not arise out of the underlying transaction or occurrence because [they do] not affect the execution or enforceability of the guaranty agreements." Id.

Only one reported case since BADD has discussed that decision in the context of whether a counterclaim is compulsory. In S.C. Community Bank v. Salon Proz, LLC, 420 S.C. 89, 97, 800 S.E.2d 488, 492 (Ct. App. 2017), this court determined a claim for violation of the South Carolina Unfair Trade Practices Act, S.C. Code Ann. § 39-5-10, *et seq.*, was compulsory, citing BADD as authority.

For example, the UTPA claim is an action at law seeking treble damages. The substance of Salon's UTPA claim alleges Bank "engaged in a pattern of reneging upon promises to modify or otherwise restructure loans, including, but [not] limited to, the loan subject of this case." Were this allegation true, it could affect the loan's enforceability. Cf. BADD, 414 S.C. at 296, 778 S.E.2d at 109 (holding a counterclaim was permissive when its allegations, if true, would not have rendered the guaranty agreements unenforceable). Therefore, we find the UTPA claim was both legal and compulsory. See N.C. Fed. Sav. & Loan Ass'n v. DAV Corp., 298 S.C. 514, 518-19, 381 S.E.2d 903, 904-05 (1989) (holding a counterclaim alleging violation of the UTPA by breach of an oral agreement was both legal and compulsory).

Salon Proz, 420 S.C. at 97.

DAV Corp., BADD, and Salon Proz may be boiled down to this: there are at least two recognized ways a counterclaim may be compulsory. If a counterclaim arises

out of the same set of facts as the plaintiff's claim, it is compulsory. BADD, 414 S.C. at 295, 296; DAV Corp., 298 S.C. at 518-19; Salon Proz, 420 S.C. at 97. If success on a counterclaim could affect the enforceability of the plaintiff's claim, it is compulsory. BADD, 414 S.C. at 295, 296; DAV Corp., 298 S.C. at 518-19; Salon Proz, 420 S.C. at 97.

II. Watson's counterclaims are compulsory because they arise out of the same transaction or occurrence that forms the basis of Carrington's claims.

In invading Watson's property and locking him out of it, Carrington violated the terms of its mortgage agreement with Watson. (R. pp. ____; complaint – mortgage exh. p. 2, ¶ 5.) The mortgage only provides for one instance in which the mortgagee is allowed to enter the property while the mortgage relationship continues. (R. pp. ____; complaint – mortgage exh. p. 2, ¶ 5.) That is when the mortgaged property has been abandoned, in which case the mortgagee “may take reasonable action to protect and preserve such vacant or abandoned property.” (R. pp. ____; complaint – mortgage exh. p. 2, ¶ 5.) As Watson's answer and counterclaim notes, he never abandoned the property and was actively trying to sell it when Carrington took possession of it. (R. pp. ____; answer and counterclaim pp. 3, 7.) His counterclaims arise out of Carrington's actions in violation of the terms of the mortgage Carrington seeks to foreclose. (R. pp. ____; complaint – mortgage exh. p. 2, ¶ 5.; answer and counterclaim pp. 3, 7.)

Carrington's position below was that claims that arise out of its breach of the same mortgage it is trying to enforce against Watson are not compulsory claims. This position was adopted by the lower court. (R. pp. ____; order granting motion to strike

pp. 2-3.) This position is inconsistent with DAV Corp. and Salon Proz. The Supreme Court in DAV Corp. found counterclaims that arose out of the parties' relationship that was the subject of the foreclosure claim, dealt with the manner in which the loan was administered, or both to be compulsory counterclaims. 298 S.C. at 517-19. Salon Proz similarly dealt with a counterclaim, determined to be compulsory, that arose out of the parties' lender-borrower relationship and the way the loan was administered. 420 S.C. at 97.

Here, Watson's counterclaims arise out of the parties' mortgagor-mortgagee relationship – even from the same fundamental document establishing that relationship – and the manner in which the loan was administered. (R. pp. ____; transcript p. 9 ln. 4-6.) They more “arise[] out of the transaction or occurrence that is the subject matter of the opposing party's claim[,]” Rule 13(a), SCRCF, than did the counterclaims deemed compulsory in DAV Corp., 298 S.C. at 517-19, and Salon Proz, 420 S.C. at 97. Watson's counterclaims are compulsory counterclaims.

III. Watson's counterclaims are compulsory because they have the potential to defeat Carrington's claims.

The lower court's analysis of whether Watson's counterclaims are compulsory is as follows:

Defendant is not entitled to a jury trial on his counterclaims because Plaintiff's ability to enforce the note and mortgage would not be affected by Defendant's success on the counterclaims. “Generally, the party seeking foreclosure has the burden of establishing the existence of the debt and the mortgagor's default on that debt.” U.S. Bank Trust Nat'l Ass'n v. Bell, 385 S.C. 364, 374-75, 684 S.E.2d 199, 205 (Ct. App. 2009). Defendant's counterclaims pertain to alleged actions by Plaintiff in securing the property many years after the note and mortgage were executed. The resolution of the

counterclaims would not affect the existence of a debt or Defendant's default on that debt. The counterclaims do not affect the enforceability of the note and mortgage.

(R. pp. ____; order granting motion to strike p. 3.)

If Watson succeeds on his counterclaims, however, he will have established a set of facts that proves the basis of his affirmative defenses – breach of the mortgage by Carrington and Carrington's unclean hands. (R. pp. ____; answer and counterclaim pp. 3-7.) Accordingly, his success on the counterclaims may well affect Carrington's right to prevail on its claims in this case. (R. pp. ____; transcript p. 9 ln. 17 through p. 10 ln. 1.) Instructive in this regard is this court's summary of what must be shown in mortgage foreclosure actions:

Generally, the party seeking foreclosure has the burden of establishing the existence of the debt and the mortgagor's default on that debt. Once the debt and default have been established, the mortgagor has the burden of establishing a defense to foreclosure such as lack of consideration, payment, or accord and satisfaction.

U.S. Bank. Natl. Assn. v. Bell, 385 S.C. 364, 684 S.E.2d 199, 205 (Ct. App. 2009)
(footnote omitted).

Bell never purported to give an exhaustive, exclusive list of affirmative defenses to mortgage foreclosure. See id. Like the defenses listed in Bell, Watson's affirmative defenses of breach of the mortgage by Carrington and Carrington's unclean hands have the potential to defeat Carrington's mortgage foreclosure and reformation claims.

If Watson proves his defense that Carrington breached the mortgage contract by entering his property and taking possession of it even though he had not abandoned

it, that could result in Carrington losing the case on its foreclosure claim. (R. pp. ____: transcript p. 9 ln. 19-22.) Notes and mortgages are contractual documents. See Saro Investments v. Ocean Holiday Partnership, 314 S.C. 116, 122, 441 S.E.2d 835 (Ct. App. 1994) (construing mortgage transaction in accordance with “settled principles of contract law”). Where there has been a material breach of a contract by a party seeking its enforcement, “equity will not enforce the contract against him.” Masonic Temple, Inc. v. Ebert, 199 S.C. 5, 18 S.E.2d 584, 591 (1942).

If Watson proves his unclean hands defense arising out of those same facts, he will have, similarly, proven a defense that has the potential to defeat Carrington’s equitable claims in this case, as “the Court of Equity will refuse to lend its aid to one who has been guilty of inequitable conduct in the subject matter.” Id.; accord Arnold v. City of Spartanburg, 201 S.C. 523, 23 S.E.2d 735, 738 (1943).

The same facts that underlie these defenses form the basis of Watson’s counterclaims. (R. pp. ____; answer and counterclaim pp. 3-7.) If Watson’s counterclaims are tried to a jury, as they should be, “[t]he court may then determine the equitable claims, but the jury’s determination of common factual issues shall be binding upon the court.” Blackburn, 407 S.C. at 330. Accordingly, victory for Watson on any of his counterclaims would necessarily determine that the facts exist that form the basis of his affirmative defenses to Carrington’s claims. (R. pp. ____: transcript p. 9 ln. 17 through p. 10 ln. 2.) That is the essence of a compulsory counterclaim.

Further, to be compulsory, there is no requirement of Watson’s counterclaims that they *of necessity* would bar Carrington’s claim if they succeed. The lower court appeared to adopt such an unduly narrow interpretation of the law in this area. (R. pp.

__ order granting motion to strike pp. 2-3.) This court in Salon Proz held a counterclaim was compulsory where “it *could* affect the loan’s enforceability.” 420 S.C. at 97 (emphasis added). Neither that decision nor any reported decision of any South Carolina appellate court has held that, to be compulsory, a counterclaim must necessarily and always bar the plaintiff’s claim if successful.

There are also cases beyond the DAV Corp.-BADD-Salon Proz trinity that reveal the compulsory counterclaim rule is not as narrow as perceived by the lower court. In Jaynes v. County of Fairfield, the Jaynes were defendants in an earlier road-closing action brought by Fairfield County that concerned, *inter alia*, whether a road was public property – a case that Fairfield County lost. 303 S.C. at 435-36, 438 & n. 1. This court held that the Jaynes’ later inverse condemnation action against the county about that road was barred by res judicata, since the claims were about the same road and bore a logical relationship to one another. Id. The claims arose out of a common matter: the road and who owned it. Id.

In First-Citizens Bank & Trust Co. v. Hucks, a case in which the compulsory or permissive nature of a counterclaim was put in issue by a jury demand on the counterclaim, the Supreme Court’s analysis was as follows:

In the instant case, the trustee’s equity action seeks a declaration of rights arising in the administration of a trust. The legal counterclaim alleges that the trustee has breached its contractual agreement and fiduciary duty. We find that there is a logical relationship between the counterclaim and the claim. Hence the counterclaim is compulsory, and appellants are entitled to a jury trial on their counterclaim.

305 S.C. 296, 298, 408 S.E.2d 222, 223 (1991). Again, the claims arose out of a common matter or set of transactions: the trust and its administration. Id.

The purpose of the compulsory counterclaim rule is “to prevent multiplicity of actions and to achieve resolution in a single lawsuit of all disputes arising out of common matters.” Beach Co., 351 S.C. at 62. If the scope of what is a compulsory counterclaim were instead limited to a counterclaim that would of necessity preclude success on the opposing claim, Jaynes and Hucks could not have been decided in the way that they were. Hucks, 305 S.C. at 298; Jaynes, 303 S.C. at 435-36, 438 & n. 1.

In addition to arising out of a common transaction or occurrence – the mortgage and the administration of the loan – Watson’s counterclaims are compulsory because they do have the potential to prevent Carrington from prevailing on its claims.

IV. If there is doubt or the question is close, counterclaims are to be treated as compulsory, to avoid depriving a party of his right to a jury trial.

“The right of trial by jury is highly favored, and waivers of the right are always strictly construed and not lightly inferred or extended by implication.” Keels, 15 S.C. at 342; accord Broome, 319 S.C. at 340; N. Charleston Jt. Venture, 307 S.C. at 535; Beach Co., 351 S.C. at 64.

When the Supreme Court had occasion to rein in the “main purpose” rule in an effort to keep that body of jurisprudence from heading in a dangerous direction, it stated as follows:

We are concerned that, as courts have sought to ascertain the “main purpose” of lawsuits, the pendulum appears to have swung with steadied progress toward decisions tending to place within the sole purview of the equity judge issues properly triable only by jury.

Floyd v. Floyd, 306 S.C. 378, 380, 412 S.E.2d 397, 399 (1991). The concern expressed by this Court in Floyd was that courts “not deprive litigants of the right to a jury trial where appropriate.” Id.

The touchstone of the logical relationship test of whether a counterclaim is compulsory or permissive is its *breadth* – flexible breadth, but breadth nonetheless. Among the reasons for this breadth and flexibility is the concern the Supreme Court has expressed in cases where both legal and equitable claims were present that “caution should be taken to assure that, under the circumstances of the case, a joint trial will not deprive a party of his right to a full jury trial of legal issues.” Johnson, 292 S.C. at 55.

Further, a broad but flexible conception of the compulsory/permissive counterclaim distinction, geared toward preserving the jury trial right, especially in a case of doubt, dovetails neatly with the purpose behind the requirement of Rule 13(a), SCRPC, that compulsory counterclaims a defendant has against a plaintiff must be asserted in the same suit. Rule 13(a)’s purpose is “to prevent multiplicity of actions and to achieve resolution in a single lawsuit of all disputes arising out of common matters.” Beach Co., 351 S.C. at 62. The idea is to have everything about a given matter between the same parties decided in the same case. Id.

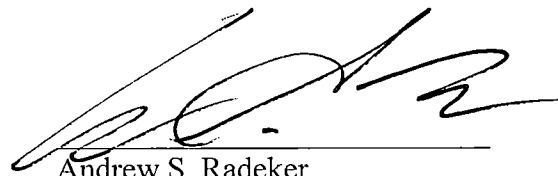
A counterclaim is compulsory “if it arises out of the same transaction or occurrence as the opposing party’s claim[.]” which is ascertained by determining whether there is “*any* logical relationship between the claim and the counterclaim[.]” DAV Corp., 298 S.C. at 517, 518 (emphasis added). Too narrow a construction of the logical relationship test has the effect of doing away with the very flexibility that was the reason for the Supreme Court’s choice of the logical relationship test. Id. at 518.

Accordingly, if this court reckons the question is close or is in doubt about whether Watson's counterclaims are compulsory, this court should take the side of protecting Watson's constitutional right to trial by jury. Johnson, 292 S.C. at 55.

CONCLUSION

This court should reverse the lower court's decision to grant Carrington's motion to strike Watson's jury demand and should remand this case for trial, with Watson's counterclaims to be tried by a jury.

Respectfully submitted,



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October 21, 2019

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM RICHLAND COUNTY
Court of Common Pleas

Robert E. Hood, Circuit Judge

Appellate Case No. 2019-000719

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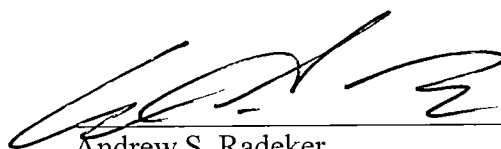
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v.

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I certify that I served the foregoing initial brief of appellant in this case by depositing a copy of it on the date shown below in the United States Mail, postage prepaid, addressed as follows:

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**Re: Carrington Mortgage Services, LLC v. Paul R. Watson
Appellate Case No. 2019-000719**

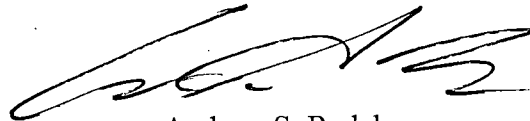
Dear Ms. Kitchings:

Enclosed herewith for filing are an original and one copy of the appellant's initial brief, designation of matter for inclusion in record on appeal, and motion for extension out of time. Also enclosed is this firm's check in the amount of \$50.00 as the fee for the motion.

Kindly file these materials and return a file-stamped copy thereof to this office in the stamped and addressed envelope enclosed. Thank you for your attention to this matter. Of course, if you or your staff have any questions or concerns, please do not hesitate to contact me.

With kind regards, I am,

Very truly yours,
HARRISON, RADEKER & SMITH, P.A.



Andrew S. Radeker

ASR/

Enclosures

cc: Peter M. Balthazor, Esq.

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