THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM HORRY COUNTY
Court of Common Pleas

Clifton Newman, Circuit Court Judge

Appellate Case No. 2019-001053

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S.C. SUPREME COURT

Ex. Parte: Hartford Fire Insurance Company, Hartford Casualty Insurance Company, American Empire Surplus Lines Insurance Company, BITCO General Insurance Corporation, Clarendon National Insurance Company, Harleysville Insurance Company n/k/a Nationwide Insurance Company, Selective Insurance Company, Crum & Forster Specialty Insurance Company, and First Mercury Insurance Company, ... Appellants

In Re:

The Havens Condominium Association, ... Plaintiff,

v.

Centex Homes, et al., ... Defendants,

The River Crossing Condominium Association, and Vincent J. Tamburro, on behalf of himself and others similarly situated ..... Plaintiffs

v.

Centex Homes, et al., ... Defendants,

The Tanglewood Condominium Association ..... Plaintiff,

v.

Centex Homes, a Nevada General Partnership, et al., ... Defendants,

The Woodlands Condominium Association ..... Plaintiff,

v.

Centex Homes, a Nevada General Partnership, et al., ... Defendants,

Of Which, The Havens Condominium Association, The River Crossing Condominium Association, Vincent J. Tamburro, The Tanglewood Condominium Association, The Woodlands Condominium Association, and Centex Homes, a Nevada General Partnership, are the ..... Respondents.

Initial Brief by Appellants American Empire Surplus Lines Insurance Company, BITCO General Insurance Corporation, Clarendon National Insurance Company, Harleysville Insurance Company n/k/a Nationwide Insurance Company, Selective Insurance Company, Crum & Forster Specialty Insurance Company, and First Mercury Insurance Company

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Robert C. Calamari
Matthew A. Abee
Patrick F. O'Dea
Nelson Mullins Riley & Scarborough LLP
1320 Main Street, 17th Floor
Columbia, SC 29201
(803) 799-2000

Attorneys for Harleysville Insurance Company n/k/a Nationwide Insurance Company and Selective Insurance Company

Clayton B. McCullough
Ross A. Appel
McCullough Khan, LLC
359 King Street, Suite 200
Charleston, SC 29401
(843) 937-0400

Attorney for American Empire Surplus Lines Insurance Company

Lawrence M. Hunter, Jr
Hunter & Foster, PA
Post Office Box 10309
Greenville, SC 29603
(864) 242-2111

Attorney for BITCO General Insurance Corporation

Neil S. Haldrup
Thomas B. Boger
Wall Templeton & Haldrup, P.A.
Post Office Box 1200
Charleston, SC 29402
(843) 329-9500

Attorneys for Clarendon National Insurance Company, Successor by Merger to Clarendon America Insurance Company

John S. Wilkerson, III
R. Hawthorne Barrett
Turner Padget Graham & Laney, P.A.
P.O. Box 22129
Charleston, SC 29413
(843) 576-2801

Attorneys for Crum & Forster Specialty Insurance Company and First Mercury Insurance Company

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Statement of the Issues on Appeal

Under *Sims v. Nationwide Mutual Insurance Company*, an insurer is not precluded from denying coverage regardless of any ruling in an underlying liability action if the insurer was unable to raise its defense to coverage in the liability action due to a conflict of interest with its insured. Notwithstanding *Sims*, the Court's rulings in *Auto Owners Insurance Company, Inc. v. Newman* and *Harleysville Group Insurance v. Heritage Communities, Inc.*, state that an insurer under a commercial general liability policy loses its ability in a coverage action to seek a court's review of a verdict in an underlying construction defect action if the insurer fails to seek intervention and the record does not include an allocation between covered and non-covered types of damages in the general verdict.

As a result of the conflict between *Sims*, *Newman*, and *Harleysville*, an insurer in South Carolina must seek intervention in the liability action to request that the jury consider special interrogatories or a special verdict form in order to allocate damages. If intervention is denied, an insurer's ability to seek review of its duty to indemnify only portions of the general verdict is impaired or impeded.

The questions presented are:

I. Whether the trial court erred by denying insurers' motions to intervene to request special interrogatories allocating the jury's damages between covered and non-covered damages?

II. Whether *Newman* and *Harleysville* conflicts with other opinions from the Court and should be modified to allow parties to allocate damages in a separate declaratory judgment action rather than requiring intervention in the underlying liability action?

Statement of the Case

This is a consolidated appeal from a trial court's denial of nine insurance companies' motions to intervene in four construction defect actions involving their insured-contractors.[1] The Insurers moved to intervene in the construction defect action to request the trial court interpose special interrogatories to the jury. They did so in response to this Court's precedent in *Auto Owners Ins. Co. v. Newman*, 385 S.C. 187, 198, 684 S.E.2d 541, 547 (2009), and *Harleysville Grp. Ins. v. Heritage Communities, Inc.*, 420 S.C. 321, 343–44, 803 S.E.2d 288, 300–01 (2017). The Insurers sought intervention to avoid the possibility of forfeiting their right to seek allocation between covered and non-covered damages under the commercial general liability ("CGL") policies they issued in a subsequent coverage action as contemplated by *Sims v. Nationwide Mut. Ins. Co.*, 247 S.C. 82, 83, 145 S.E2d 523, 523 (1965).

A. The Underlying Construction Defect Actions

The Havens Condominium Association, The River Crossing Condominium Association, The Tanglewood Condominium Association, and The Woodlands Condominium Association (collectively, the "Condominium Associations") are South Carolina horizontal property regimes comprised of numerous different condominium unit owners in Myrtle Beach, South Carolina. (R. at __; Compl.) The Condominium Associations, along with Plaintiff Vincent Tamburro (individually and in a representative capacity), allege that as a result of defects and deficiencies in their condominium units, they will be required to expend large sums of money to repair,

[1] Nine insurance companies appealed the trial court's order denying their motions to intervene. Seven of the insurers join this brief: American Empire Surplus Lines Insurance Company, BITCO General Insurance Corporation, Clarendon National Insurance Company, Successor by Merger to Clarendon America Insurance Company, Harleysville Insurance Company n/k/a Nationwide Insurance Company, Selective Insurance Company, Crum & Forster Specialty Insurance Company, and First Mercury Insurance Company (collectively, the "Insurers"). Hartford Fire Insurance Company and Hartford Casualty Insurance Company separately brief the issues raised on appeal.

correct, and replace various parts and components of the condominiums and surrounding buildings. (R. at __; Compl.)

Because of these damages, the Condominium Associations filed four separate construction defect actions against Centex Homes and various related entities, contractors, and subcontractors in 2015. (R. at __; Compl., Jan. 13, 2015.)[2] The Condominium Associations seek damages for alleged construction defects and consequential damage arising out of the construction of the condominium units. (*Id.*; R. at __; Am. Compl., Feb. 13, 2015.) Plaintiffs allege negligence, gross negligence, carelessness, recklessness, willfulness, and wantonness; breach of warranty of habitability, breach of warranty against latent defects, breach of warranty of workmanlike services, breach of warranty for fitness for a particular purpose, breach of warranty of merchantability and serviceability, breach of express warranty; unfair trade practices; breach of fiduciary duty; and reformation. (*Id.*)

Centex filed cross-claims and third-party claims for indemnity, negligence, breach of warranty, and breach of contract against various subcontractors, including those insured by the Insurers. (R. at __; Ans. Am. Compl., Cross-Claims, and Third-Party Compl., Feb. 27, 2015)

B. The Insurance Policies and Reservations of Rights

The Insurers issued primary CGL insurance policies to numerous contractors and subcontractors involved in the construction defect cases for various policy periods. (R. at __; Mot. Intervene.) The applicable policies contain detailed terms, conditions, and exclusions controlling whether and to what extent the insured-contractors are to be indemnified for damages

[2] These lawsuits were: (1) *The Havens Condominium Association v. Centex Homes, et al.*, Case No. 2015-CP-26-00118; (2) *The River Crossing Condominium Association, et al. v. Centex Homes, et al.*, Case No. 2015-CP-26-00279; (3) *The Tanglewood Condominium Association v. Centex Homes, et al.*, Case No. 2015-CP-26-02718; and (4) *The Woodlands Condominium Association v. Centex Homes, et al.*, Case No. 2015-CP-26-04514.

awarded against them. Generally, the policies provide indemnity only for "property damage" arising within a policy period from an "occurrence" as defined in the policy. There is no coverage for economic losses, or for the costs of repairing or replacing the insured-contractors' defective work.

The Insurers received notice of claims asserted against the insured-contractors at various times after the filing of the complaint. The Insurers agreed to participate in the defense of their insured-contractors subject to full and complete reservation of their rights. *See Harleysville*, 420 S.C. at 341, 803 S.E. 2d at 299.[3]

C. Procedural Posture and the Trial Court's Order Denying Intervention

The Condominium Associations filed their four lawsuits in 2015. (R. at __; Compl., Jan. 13, 2015.) In December 2017, the Insurers began filing their motions to intervene in the construction defect actions. (R. at __–__; Mot. Intervene.) The motions sought intervention under the Court's opinion in *Harleysville* and Rule 24, SCRCP, for the limited purpose of requesting that the trial court send special interrogatories or a special verdict form to the jury in the construction defect actions so as to identify the amount and types of damages potentially covered by insurance. The Insurers moved to intervene to avoid the prejudice to the Insurers that could result from a general verdict entered against their insured-contractors. (*Id.*)

The trial court held a hearing on the motions to intervene on April 25, 2019. (R. at __; Hr'g. Tr. 7:19–23, 12:8–13, 15:13–16, Apr. 25, 2019.) The Insurers adopted each other's arguments on the motions at the hearing. (*Id.*) To clarify the record before the trial court at the hearing, the parties entered into a Stipulation and Agreed Record for the hearing. (R. at __; Stipulation at 8–10; R. at __; Hr'g. Tr. at 15:13–21.)

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[3] At least one coverage action is currently pending involving some of the parties to the underlying construction defect action. (R. at __; Order at 6.)

The Court denied the motion in the four construction defect actions on June 21, 2019. (R. at __; Order.) To support its decision to deny intervention, the trial court concluded that the Court's "recent decision in *Harleysville Grp. Ins. v. Heritage Communities, Inc.*, 420 S.C. 321, 803 S.E.2d 288 (2017) does not mandate that the Insurers have a right to intervene to ask special interrogatories or request special verdict forms." (R. at __; Order at 6.) It also concluded that the Insurers failed to establish standing and the elements required by Rule 24, SCRCP. (*Id.*)

The Insurers timely served and filed their notices of appeal in June, 2019. (R. at __–__; Notices of Appeal.) Following the Insurers' appeals, the trial court denied a motion to stay the four underlying actions pending appeal. (R. at __; Order, Sep. 9, 2019.) As of the filing of the Insurers' initial brief in December 2019, the construction defect actions have not been tried. (R. at __.) Trial is expected in the first of the four actions in February 2020 at the earliest. (*Id.*)

Standard of Review

"The decision to grant or deny a motion to . . . intervene in an action pursuant to Rule 24, SCRCP, lies within the sound discretion of the trial court." *Ex Parte Gov't Employee's Ins. Co.*, 373 S.C. 132, 135, 644 S.E.2d 699, 701 (2007). "An abuse of discretion occurs when the ruling is based on an error of law or a factual conclusion without evidentiary support." *Historic Charleston Holdings, LLC v. Mallon*, 381 S.C. 417, 434, 673 S.E.2d 448, 457 (2009) (citing *Patel v. Patel*, 359 S.C. 515, 529, 599 S.E.2d 114, 121 (2004)). Questions of law underlying review of a motion to intervene are reviewed *de novo*. *Hoyler v. State*, Op. No 5676 (S.C. Ct. App. filed Aug. 7, 2019) (Shearouse Adv. Sh. No. 32 at 110).

Argument

An insurer generally has two duties: the duty to defend the insured against covered claims and the duty to indemnify, i.e., to pay covered damages awarded against the insured in favor of

the plaintiff. *Sloan Const. Co. v. Cent. Nat. Ins. Co. of Omaha*, 269 S.C. 183, 186, 236 S.E.2d 818, 820 (1977). The duty to defend is determined by the claims raised in the lawsuit against the insured. *See Liberty Life Ins. Co. v. Commercial Union Ins. Co.*, 857 F.2d 945, 950 (4th Cir. 1988) (applying South Carolina law). The duty to indemnify is independent of the duty to defend; it is limited to those losses covered by the insurance policy and is not controlled by the claims made in the complaint. *See B.L.G. Enters.. Inc. v. First Fin. Ins. Co.*, 334 S.C. 529, 535, 514 S.E.2d 327, 330 (1999). An insurer balances these two duties by retaining defense counsel whose loyalty is to the insured, while still reserving rights as to coverage issues. *Sentry Select Ins. Co. v. Maybank Law Firm, LLC*, 426 S.C. 154, 160, 826 S.E.2d 270, 273 (2019) (holding that retained counsel represented the insured, not the insurer).

When litigation involving the insured ensues, two separate questions often arise: (1) whether the insured is liable to the plaintiff, a question normally answered in an underlying tort action; and (2) whether insurance coverage for any judgment against the insured-defendant exists under the policy, a question normally answered in a subsequent declaratory judgment action based on the insurance contract. *See Sims v. Nationwide Mut. Ins. Co.*, 247 S.C. 82, 83, 145 S.E2d 523, 523 (1965). An insurer with potential coverage is not a party to the first dispute, *see Major v. Nat'l Indem. Co.*, 267 S.C. 517, 520, 229 S.E.2d 849, 850 (1976), and issues regarding the availability of insurance are not considered by the jury to avoid prejudicing the verdict, *see Bartell v. Willis Constr. Co.*, 259 S.C. 20, 24, 190 S.E.2d 461, 463 (1972); Rule 411, SCRE.

When there are no coverage issues, the parties to the underlying liability case are not concerned with preserving information about the verdict in the underlying tort case necessary to allocate across available coverages or policies. Not so in construction defect cases. Such cases often involve claims in the underlying liability action that are covered by the applicable CGL

policy, and those that are not covered. Traditional CGL policies do not cover the defective construction itself, but property damage caused by the defective construction. *Newman*, 385 S.C. at 197–98, 684 S.E.2d at 546; *Bennett & Bennett Constr., Inc. v. Auto Owners Ins. Co.*, 405 S.C. 1, 8, 747 S.E.2d 426, 430 (2013); *Crossmann Cmties. of N.C., Inc. v. Harleysville Mut. Ins. Co.*, 395 S.C. 40, 50, 717 S.E.2d 589, 594 (2011). The policy also does not cover repairs or replacement of defective work or work that does not comply with any applicable construction contract. *Crossmann*, 395 S.C. at 50, 717 S.E.2d at 594 (holding that coverage is not afforded for costs of removing defective work, even where it is incidental to repairing damaged property). This distinction is grounded in the public policy of preventing insureds from being indemnified for their own intentional or unlawful acts. *Hendrix v. Employers Mut. Liab. Ins. Co. of Wis.*, 78 F. Supp. 84, 87 (E.D.S.C. 1951).

Most construction defect actions involve mixed claims—those for damages caused by the defective work and for amounts required to cover repairs of that work. *See Harleysville*, 420 S.C. at 335, 803 S.E.2d at 296 (distinguishing between covered and non-covered claims under CGL policy). As a result, issues regularly arise as to how to determine which amounts awarded by a jury in a liability action apply to the two distinct categories of damages.

South Carolina precedent states that the burden is on an insured—not its insurer—to establish coverage. *Gamble v. Travelers Ins. Co.*, 251 S.C. 98, 103, 160 S.E. 2d 523, 525 (1968). *Newman* and *Harleysville* have shifted this burden from the insured to its insurer, at least in cases when a factfinder in the liability action renders a general verdict and the insurer does not attempt to intervene. *See Newman*, 385 S.C. at 198, 684 S.E.2d at 547; *Harleysville*, 420 S.C. at 343–44, 803 S.E.2d at 300–01. In such circumstances, an insurer is bound by the verdict even though it was not a party to the case in which the verdict was issued, and even though the insurer had no

ability to develop the record underlying the verdict because of a conflict of interest. *See Sims*, 247 S.C. at 83, 145 S.E2d at 523; *Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273. Failure to seek intervention to prove allocation in the liability action comes with a harsh result; the insurer's ability to contest its duty to indemnify for non-covered damages is severely impeded.

In the wake of the Court's shift of the burden to prove covered damages from the insured, the Insurers did what the Court suggested—they moved to intervene solely for the purpose of requesting that special interrogatories or a special verdict form be submitted to the jury in the construction defect action. Despite the Court's precedent in *Newman* and *Harleysville*, however, the trial court denied intervention. Doing so was in error.

The Court should reverse the trial court's denial of the Insurers' motions to intervene and remand the action with instructions that the Insurers be permitted to intervene so they may propose special interrogatories or a special verdict form to be submitted to the jury in the underlying construction defect action. In so ruling, the Court should also modify its opinions in *Newman* and *Harleysville*, resolving the opinions' conflict with the Court's prior precedent. *See Sims*, 247 S.C. at 83, 145 S.E.2d at 523 (establishing exception to general rule preclusive effect of liability verdict where insurer's assertion of a defense to coverage would have prejudiced the insured and created a conflict); *Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273 (holding that retained defense counsel represents the insured, not the insurer's, interests). When resolving this conflict, the Court should reiterate that *Sims* permits allocation of an underlying general verdict between covered and non-covered damages in a subsequent lawsuit regarding coverage issues.

I. The trial court erred in applying recent precedent and denying the Insurers' motions to intervene.

To support its decision to deny intervention, the trial court concluded that the Court's "recent decision in *Harleysville* . . . does not mandate that the Insurers have a right to intervene

to ask special interrogatories or request special verdict forms." (R. at __; Order at 6.) The trial court misunderstands the practical effect of the Court's precedent in *Harleysville*, and how it is an extension of the Court's opinion in *Newman*. The Court also erred by using that precedent to support its decision to deny intervention by the Insurers.

A. *Newman* and *Harleysville* require intervention to preserve the right to later seek allocation between covered and non-covered damages.

In *Newman*, the insurer of a builder sought a declaratory judgment that it did not have to indemnify a builder for non-covered damages under its CGL policy. *Newman*, 385 S.C. 187, 190, 684 S.E.2d 541, 542 (2009). The insurer argued that portions of an earlier arbitration award issued against the builder included amounts for replacing and repairing defective stucco, a damage that was not covered by the policy. *Id.* at 197, 684 S.E.2d 546. The Court initially agreed. *Id.* at 198, 684 S.E.2d at 546–47. It held that the CGL policy's terms "unambiguously prohibit[ed] recovery for the cost of removing and replacing the defective stucco—even when the replacement of the defective work may be incidental to the repair of property damage covered by the policy," and that "any amount in the arbitrator's allowance allotted to the removal and replacement of the defective stucco is not covered under the CGL policy." *Id.*

Nevertheless, the Court affirmed the trial court's order and required the insurer to indemnify the builder for the non-covered repair and replacement damages because it was "not possible from the record before this Court to determine what portion of the arbitrator's itemized list of damages may be attributed to the removal and replacement of the defective stucco, and it is not the purpose of this declaratory judgment action to re-litigate the issue of damages." *Id.* at 198, 684 S.E.2d at 547. Although recognizing that the insurer defended its insured "with a reservation of rights and an understanding that the coverage issue would be reserved for judicial consideration in a separate proceeding," the Court held the insurer responsible for the entire

damages award because when "the arbitrator determined damages, [the insurer] did not seek review of or otherwise contest the damages award." *Id.* at 198 n.5, 684 S.E.2d at 547 n.5. The Court determined that the insurer must face the consequences for this gap in the record because the insurer "had an opportunity to raise this matter when the issue of damages was litigated before the arbitrator, who issued a final, binding award on the merits." *Id.*

Eight years after *Newman*, the Court issued its substituted and refiled opinion in *Harleysville*. There, the insurer under a CGL policy brought a declaratory judgment action after the jury issued a verdict for the plaintiff in the construction defect action against its insured. *Harleysville*, 420 S.C. at 331, 803 S.E.2d at 294. The insurer sought a declaration that it was not required to pay the full amount of the general verdict because it included damages for the cost to repair faulty workmanship (a damage not covered as "property damage" under the policy) and the cost to repair resulting damage to otherwise non-defective components (a potentially covered "property damage"). *Id.* at 335, 803 S.E.2d at 296.

The trial court rejected the insurer's coverage arguments. It concluded that the insurer "made a conscious decision not to intervene in the underlying action[s] and took no action to seek an allocated verdict by informing the trial court of the need for an allocated verdict or by submitting special interrogatories for the Court's consideration for submission to the jury." (*See* Record on Appeal at 37, 86, *Harleysville Group Ins. v. Heritage Communities, Inc.*, No. 2013-001281.)[4] It then concluded that the insurer's "failure to intervene or otherwise seek an allocated verdict cannot now be used to prejudice the rights of its insureds or the rights of the claimants who step into the shoes of the insureds." (*Id.* at 58, 107.) Even though the trial court

[4] A court may "take judicial notice of its own records, files and proceedings for all proper purposes including facts established in its records." *Freeman v. McBee*, 280 S.C. 490, 494, 313 S.E.2d 325, 327 (Ct. App. 1984); *accord Wise v. Wise*, 394 S.C. 591, 601, 716 S.E.2d 117, 122 (Ct. App. 2011).

acknowledged that the verdict included damages not covered by the insurance policy, the trial court did not allow the insurer to "relitigate" the issues decided in the underlying liability action, suggesting that the court was applying issue preclusion against the insurer even though it was not a party to the liability action. (*Id.* at 54–55, 59.)

On appeal, this Court affirmed, rejecting the insurer's attempt to allocate between covered and non-covered damages. *Harleysville*, 420 S.C. at 343–44, 803 S.E.2d at 300–01. The Court first held that the insurer's reservation of rights "letters were not sufficiently specific to put [its insured] on notice of [the insurer's] specific defenses, particularly as to the need for an allocated verdict." *Id.* at 342, 803 S.E.2d at 299.[5] The Court further stated that the "'right to control the litigation carries with it certain duties,' including 'the duty not to prejudice the insured's rights by failing to request special interrogatories or a special verdict in order to clarify coverage of damages.'" *Harleysville*, 420 S.C. at 341, 803 S.E.2d at 299 (quoting *Magnum Foods, Inc. v. Cont'l Cas. Co.*, 36 F.3d 1491, 1498 (10th Cir. 1994)).

The Court also affirmed the trial court's refusal to allocate based on its finding that it had "no basis upon which to make a logical assessment of the jury's purpose when it awarded the general verdict' . . . ." *Id.* The Court's ruling prohibiting allocation of the verdict because of the lack of information in the record was "[i]n addition to" to its ruling prohibiting the allocation because of the deficient reservation of rights letters. *Id.* at 343 n.11, 803 S.E.2d at 300 n.11. To support its additional holding, the Court cited *Newman*: "there was insufficient evidence in the record to allow the Court to determine which costs were solely attributable to the non-covered

[5] There is no such allegation here that the insured-contractors are not on notice under specific reservation of rights letters. And even if the insured-contractors were not given specific notice, it cannot be said that they do not know of the need to seek an allocated verdict following the Insurers' motions to intervene, the briefing and argument below, and this appeal. Because the construction defect actions have not yet been tried, the insured-contractors must still seek an allocated verdict, regardless of the outcome of this appeal.

faulty workmanship and finding that the insurer's duty to indemnify therefore covered the entire award." *Id.* The Court emphasized that prohibiting allocation was proper "particularly when the dilemma now confronting [the insurer] is of its own making." *Id.* (quoting *Newman*, 385 S.C. at 198, 684 S.E.2d at 547).

Harleysville relied on an opinion from the United States Court of Appeals for the Fifth Circuit, which applied Florida law. *Harleysville*, 420 S.C. at 341, 803 S.E.2d at 299 (citing *Duke v. Hoch*, 468 F.2d 973, 377 (1972)). While the Court appeared to accept the outcome reached in *Duke*, it did not also adopt its reasoning and the presumption under Florida law on which the Fifth Circuit's opinion turns. This is likely because Florida law's burden for allocating damages is completely different from South Carolina's burden under *Newman* and *Harleysville*.

Florida law applies a burden-shifting mechanism. Once the insurer initially establishes that some damages are not covered, the burden is on the insured to provide an allocation of damages in the underlying construction defect action in order to be entitled to any coverage at all. In *Duke*, the Fifth Circuit explained:

> Once [the insurer] established that part of the liability represented by the judgment was for noncovered acts, the burden became [the insured's] to prove the precise portion of the unallocated verdict representative of acts for which [the insurer] is responsible. . . . .
>
> There was no evidence or proof of any kind as to how the jury's verdict should be divided, and it necessarily follows that the, party having the burden of proof on this matter has not met its burden. If the burden of proof is placed upon the [judgment creditor], this automatically makes the decision in favor of the [judgment creditor]; whereas, if the burden is on the [insurer], the decision automatically goes to the [insurer].

Duke, 468 F.2d at 377.

The requirements that the insurer notify the insured of a potential conflict of interest and of the need for an allocated verdict flow from this presumption. *Id.* If the insurer is allowed to

use its control of the defense to direct defense counsel not to request an allocated verdict, the insurer would always defeat coverage because the insured could never establish that at least some of the damages are covered. The requisite warnings in reservation of rights letters are designed to protect insureds from that harsh result. *Id.* at 977–79 (holding that the insurer's failure to properly warn the insured relieved the insured of this burden of proof).

Newman and *Harleysville* created the opposite presumption from the presumption that exists under Florida law. By refusing to permit allocation, the Court's presumption is now always *against* the insurer: If the record does not contain an allocation of the verdict between covered and non-covered damages, then courts must presume that *all* of the damages are for covered risks notwithstanding the insured's burden of proving that coverage exists. *Compare Newman*, 385 S.C. at 198, 684 S.E.2d at 547 and *Harleysville,* 420 S.C. at 343 n.11, 803 S.E.2d at 300 n.11, *with Gamble v. Travelers Ins. Co.*, 251 S.C. 98, 103, 160 S.E. 2d 523, 525 (1968) (holding that insured has burden of proving coverage) and *UFP Eastern Division, Inc. v. Selective Ins. Co.*, 2017 WL 499083, *5 (D.S.C. Feb. 6, 2017) (same). *Newman* and *Harleysville,* therefore, require the insurer to take additional action to preserve evidence about the verdict for a court in a subsequent coverage action to allocate a general verdict between covered and non-covered damages. *Newman*, 385 S.C. at 198, 684 S.E.2d at 547; *Harleysville,* 420 S.C. at 343 n.11, 803 S.E.2d at 300 n.11.

Newman and *Harleysville* do not explain how an insurer may protect its interests in the subsequent coverage action. The opinions, however, do hold an insurer's failure to "request a special verdict or special interrogatories" in the underlying liability action forecloses the ability to allocate between covered and non-covered damages in the subsequent coverage action. *Harleysville*, 420 S.C. at 341, 803 S.E.2d at 299 (citing *Magnum Foods, Inc. v. Cont'l Cas. Co.*,

36 F.3d 1491, 1498 (10th Cir. 1994); *Duke v. Hoch*, 468 F.2d 973, 979 (5th Cir. 1972)). The Court does not explain "how [the insurer] could . . . intervene[] . . . and assert[] a defense against coverage without creating an impermissible conflict of interest in violation of established South Carolina law." *Id.* at 363, 803 S.E.2d at 311 (Pleicones, Acting Justice, dissenting)

Following *Newman* and *Harleysville*, insurers move to intervene in construction defect actions for the limited purpose of requesting special interrogatories or a special verdict form. (R. at __; Hartford's Mem. Supp. Mot. Intervene at 3 n.2.) This has garnered mixed results. *See, e.g.*, *Order Granting Mot. Intervene, Ingram, et al. v. Lauderdale Bay Devs.. LLC*, Case. No. 2017-CP-26-02854 (Horry Ct. Comm. Pleas filed Oct. 18, 2018). The change in the burden of proof by *Newman* and *Harleysville* has also resulted in several appeals, including this one. *See Ex Parte: Hartford Fire Ins. Co.*, Appellate Case No. 2017-002146; *Ex Parte: Nationwide Mut. Fire Ins. Co.*, Appellate Case No. 2017-000202; *Ex Parte: Builders Mut. Ins. Co.*, Appellate Case No. 2019-000238; *Stoneledge at Lake Keowee Owners Ass'n, Inc. v. Cincinnati Ins. Co.*, Case No. 19-2009 (4th Cir.) (appealing trial court's refusal to permit allocation in coverage action, *Stoneledge at Lake Keowee Owners Ass'n, Inc. v. Cincinnati Ins. Co.*, No. 8:14-CV-01906-BHH, 2018 WL 4689135 (D.S.C. Sept. 28, 2018)). These motions to intervene and the conflicting orders and appeals evidence that many interpret *Newman* and *Harleysville* to require intervention in construction defect actions to protect the record.

B. The trial court erred in denying the Insurers' motions to intervene.

The trial court denied the Insurers' motions to intervene by concluding that they lacked standing and failed to meet the requirements of Rule 24, SCRCP. (R. at __; Order at 5–6.) Because *Newman* and *Harleysville* require intervention, the Court erred in denying the motions.

"Generally, the rules of intervention should be liberally construed where judicial economy will be promoted by declaring the rights of all affected parties." *Cooper v. S.C. Dep't. Soc. Servs.*, Op. No. 27927 (S.C. Sup. Ct. filed Nov. 6, 2019) (Shearouse Adv. Sh. No. 43 at 23) (quoting *Ex Parte Gov't Emp.'s Ins. Co. v. Goethe*, 373 S.C. 132, 138, 644 S.E.2d 699, 702 (2007); *Berkeley Elec. Co-op., Inc. v. Town of Mt. Pleasant*, 302 S.C. 186, 189, 394 S.E.2d 712, 714 (1990) (interpreting Rule 24, SCRCP "to permit liberal intervention . . . ."). Accordingly, a court "should consider the practical implications of a decision denying or allowing intervention." *Ex parte Gov't Emp.'s Ins. Co.*, 373 S.C. at 138, 644 S.E.2d at 702. "However, a party must have standing to intervene in an action pursuant to Rule 24, SCRCP." *Id.* "A party has standing if the party has a personal stake in the subject matter of a lawsuit and is a 'real party in interest.'" *Id.* (quoting *Bailey v. Bailey*, 312 S.C. 454, 458, 441 S.E.2d 325, 327 (1994)). "A real party in interest . . . is one who has a real, actual, material or substantial interest in the subject matter of the action, as distinguished from one who has only a nominal, formal, or technical interest in, or connection with, the action." *Id.* (quoting *Bailey*, 312 S.C. at 458, 441 S.E.2d at 327).

As is relevant here, a party may intervene as of right

> when the applicant claims an interest relating to the property or transaction which is the subject of the action and he is so situated that the disposition of the action may as a practical matter impair or impede his ability to protect that interest, unless the applicant's interest is adequately represented by existing parties.

Rule 24(a), SCRCP. A party may also intervene under Rule 24(b), SCRCP, when its "claim or defense and the main action have a question of law or fact in common." Rule 24(b)(2), SCRCP. "To warrant intervention under Rule 24(b) an applicant should ordinarily show he is charged with a public duty requiring him to intervene, or he has a claim or defense involving a question

of law or fact in common with the main action." *S.C. Tax Comm'n v. Union Cnty. Treasurer*, 295 S.C. 257, 262, 368 S.E.2d 72, 75 (Ct. App. 1988).

To intervene as a matter of right, an intervening party must: (1) establish timely application; (2) assert an interest relating to the property or transaction which is the subject of the action; (3) demonstrate that it is in a position such that without intervention, disposition of the action may impair or impede its ability to protect that interest; and (4) demonstrate that its interest is inadequately represented by other parties. *Berkeley Elec. Co-op.*, 302 S.C. at 189, 394 S.E.2d at 714. Whether the proposed intervenor's interest warrants intervention "must be determined in relation to the overall subject matter of the action and not in relation to the particular issue that is before the Court." *Id.* at 190, 394 S.E.2d at 714. Additionally, the test "further requires that the prospective intervenor demonstrate that without its intervention, the disposition of the case *may* impair or impede its ability to protect its interest." *Id.* at 190, 394 S.E.2d at 715 (emphasis added). "To meet that requirement, a party need not prove that it would be bound in a res judicata sense by the judgment, only that it would have difficulty adequately protecting its interests if not allowed to intervene." *Id.*

The burden for showing that the interests of the proposed intervenor will not be adequately represented by the existing parties is "minimal," so the intervenor "need only show that the representation of his interests 'may be' inadequate." *Id.* at 191, 394 S.E.2d at 715 (quoting *Trbovich v. United Mine Workers of Am.*, 404 U.S. 528 (1972)). Courts analyze:

> (1) whether the existing parties will undoubtedly make all of the intervenor's arguments;
>
> (2) whether the existing parties are capable and willing to make such arguments; and
>
> (3) whether the intervenor offers different knowledge, experience, or perspective on the proceedings that would otherwise be absent.

Id. As a number of courts have explained, "where a proposed intervenor's interest will be prejudiced if it does not participate in the main action, the mere availability of alternative forums is not sufficient to justify denial of a motion to intervene." *Commodity Futures Trading Comm'n v. Heritage Capital Advisory Servs., Ltd.*, 736 F.2d 384, 387 (7th Cir. 1984); *accord W. Energy Alliance v. Zinke*, 877 F.3d 1157, 1167–68 (10th Cir. 2017).

Here, the trial court abused its discretion when it determined that the Insurers lacked standing to intervene. (R. at __; Order at 5.) The trial court's determination that the Insurers lacked standing because they do not "have an interest in the [Condominium project] that is the subject of," the construction defect lawsuits is controlled by an error of law—it is an application of the narrow view of intervention established under the statutory precursor to the South Carolina Rules of Civil Procedure. *See* James F. Flanagan, *South Carolina Civil Procedure* at 200 (3d ed. 2010) ("Intervention under the prior statute was restricted, and discretionary with the court, and limited to actions for the recovery of real or personal property.") (citing S.C. Code Ann. § 15-5-200 (repealed)). As the Court confirmed as recently as November, intervention under current practice must be more liberally granted. *Cooper*, Op. No. 27927 (S.C. Sup. Ct. filed Nov. 6, 2019) (Shearouse Adv. Sh. No. 43 at 23) (reversing trial court's refusal to permit intervention).

Under this more liberal standard, the Insurers have a "real, actual, material or substantial interest" in the construction defect action: their ability to determine whether any portion of a potential judgment is a covered or non-covered damage. *Ex parte Gov't Emp.'s Ins. Co.*, 373 S.C. at 138, 644 S.E.2d at702. This can hardly be said to be "nominal, formal, or technical," because South Carolina courts have interpreted the failure to intervene as creating a presumption that all damages are covered by the applicable CGL policy. *See Harleysville*, 420 S.C. at 343–44, 803 S.E.2d at 300–01. This is more than merely having "a monetary interest in the outcome

of the case," as the trial court explained—it is the ability of the Insurers to even be heard on the issue *at all*. (R. at __; Order at 6.)

Second, the trial court abused its discretion when it determined that the Insurers had not satisfied Rule 24's requirements. (R. at __; Order at 5.) The Insurers satisfy each of the four prongs necessary for intervention as of right.[6] *Berkeley Elec. Co-op.*, 302 S.C. at 189, 394 S.E.2d at 714. Specifically, if the jury does not allocate between covered and non-covered damages, the Insurers will be forced to pay the entirety of any general verdict. *See Harleysville*, 420 S.C. at 341, 803 S.E.2d at 299 (explaining that the ability to control the defense imposes "the duty not to prejudice the insured's rights by failing to request special interrogatories or a special verdict in order to clarify coverage of damages.") (quoting *Magnum Foods, Inc. v. Cont'l Cas. Co.*, 36 F.3d 1491, 1498 (10th Cir. 1994)). The Insurers are in a position following *Newman* and *Harleysville* that, without intervention, their ability to seek allocation of any damages would not only be impaired or impeded, but would be lost altogether.

That interest is not protected by the remaining parties. Indeed, the exact opposite position is represented by the parties if the Insurers are not permitted to intervene—the insured-contractors benefit from all damages being covered by insurance, as do the plaintiffs seeking to collect on any eventual judgment. This is evidenced by the memoranda in opposition filed by Centex Homes and the Condominium Associations. (R. at __.) In light of this opposition to the Insurers' motions, the existing parties will almost certainly not "make all of the intervenor's arguments," and are not "capable and willing to make such arguments." *See Berkeley Elec. Co-*

[6] Because permissive intervention is more relaxed, the Insurers only analyze the trial court's error in failing to permit them to intervene as of right. The Court should reverse under either standard, though. *S.C. Tax Comm'n*, 295 S.C. at 262, 368 S.E.2d at 75 (Ct. App. 1988)

op., 302 S.C. at 189, 394 S.E.2d at 715. The Insurers would offer a different knowledge, experience, and perspective on the proceedings that would otherwise be absent.

Additionally, the Insurers timely moved to intervene within the timeframe contemplated by *Harleysville*. Before they filed their motions, they had no direct interest in the case, aside from providing counsel to represent their insured-contractors' interests. Once it became apparent that the four cases would proceed to trial, the Insurers' interest in obtaining an allocated verdict arose. Thus, the Insurers satisfy all of Rule 24's requirements.

This case is similar to *Berkeley Elec. Co-op., Inc. v. Town of Mt. Pleasant* in which the Court reversed the trial court's denial of a motion to intervene. 302 S.C. at 188, 394 S.E.2d at 713. That case involved a dispute between Berkeley Electric Cooperative and the Town of Mount Pleasant regarding the applicability of a franchise agreement to the extension of service to a newly annexed subdivision. *Id.* South Carolina Electric and Gas ("SCE&G") moved to intervene, asserting it had a right to serve this area, but the trial court denied the motion. *See id.* at 189, 394 S.E.2d at 714. The Supreme Court reversed and concluded that SCE&G should have been allowed to intervene, noting that SCE&G had a financial interest in the dispute, as an adverse ruling would destroy any investments it made under the belief that it was the rightful supplier of electricity to the new subdivision. *Id.* at 190, 394 S.E.2d at 715. As the Court explained, a party need only demonstrate that disposition of the case *may* impair or impede its ability to protect its interests, not that it would be bound to the judgment under res judicata. *Id.*

Like SCE&G, the Insurers need only show that they "would have difficulty adequately protecting [their] interests if not allowed to intervene." *Id.* And like the ruling prohibiting SCE&G to intervene, the trial court's ruling prohibiting the Insurers to intervene, "as a practical matter," would not only impair their ability to protect their rights under the insurance policies,

but would prevent them from exercising those rights altogether. *Id.* at 191, 394 S.E.2d at 715. It would be very difficult for the Insurers to collaterally attack an adverse verdict given the Court's holdings in *Newman* and *Harleysville*. *Id.*

Thus, the trial court incorrectly applied *Harleysville* and erred by concluding that the Insurers lacked standing and could not satisfy Rule 24, SCRCP. As a result, the trial court abused its discretion by refusing to permit the Insurers to intervene. The Court should reverse.

C. Requiring intervention in theory but refusing intervention in practice denies the Insurers due process.

If South Carolina courts do not permit intervention by insurers in construction defect actions while still holding that the judgments in those actions have preclusive effect *against the insurers* in coverage actions, insurers' due process rights will continue to be violated just as the Insurers' due process rights were violated here. Without intervention, the Insurers have no opportunity to be heard regarding allocation between covered and non-covered damages.

While an insurer may control the defense in the liability action, this right is limited by the duties the insurer and the attorney it retains to defend the insured both owe to the insured. This Court has recently explained that, notwithstanding the special relationship between an insurer, the insured, and the insured's defense counsel, the defense counsel's obligations are to the insured. *See Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273. The defense counsel cannot protect the interests of the insurer if those interest diverge from the interests of the insured. *Id.* If the defense counsel acts in the insurer's best interests, it creates an impermissible conflict between himself and his client. *See Harleysville*, 420 S.C. at 363, 803 S.E.2d at 311 (Pleicones, A.J., dissenting) (citing *Sims* after commenting that "there is no suggestion how Harleysville could have intervened in these lawsuits and asserted a defense against coverage without creating an impermissible conflict of interest in violation of established South Carolina law.").

In construction defect cases, such a conflict is likely to arise if the insurer attempts to control the defense's submission of special interrogatories or a special verdict form to the jury. In that situation, the insured's interests are best served by all of the damages being covered; the insurer's interests are best served by none of the damages being covered. *Crossmann*, 395 S.C. at 50, 717 S.E.2d at 594. As a result, if *Newman* and *Harleysville* continue to mean that an insurer cannot later seek allocation of a general verdict without special interrogatories being answered by the jury in the liability action, then defense counsel must argue against submission of special interrogatories. *Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273. The same is true for a special verdict form. This limitation on defense counsel exists because, under the Court's current precedent, a *de facto* presumption that all damages are covered arises against the insurer if it fails to seek intervention and the general verdict is not allocated by the jury in the liability action. *Harleysville*, 420 S.C. at 343 n.11, 803 S.E.2d at 300 n.11. Were defense counsel to request special interrogatories, he would be providing the insurer with a way to rebut that presumption through the jury's allocation between covered and non-covered damages. That would prejudice defense counsel's only client, the insured. *Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273. It would also cause defense counsel to impermissibly divide his loyalties between the insurer and the insured contrary to his ethical duties. *Id.* (citing Rules 1.8(f) and 5.4(c), RPC, Rule 407, SCACR).

Therefore, under the Court's reasoning in *Newman* and *Harleysville*, there is no other way for a court to allocate damages than for an insurer to seek intervention and request that special interrogatories or a special verdict form allocating damages be submitted to the jury in the liability action. When the court denies intervention, then the insurer has no opportunity to be heard on the issue of the proper allocation of damages based on *Newman* and *Harleysville*. This

violates the insurer's right to any process, much less due process. *B.L.G.*, 334 S.C. at 535, 514 S.E.2d at 330 (holding that liability insurers "have the right to limit their liability and to impose conditions on their obligations provided they are not in contravention of public policy or a statutory prohibition.").

Employing the preclusive effect of the liability judgment as a way to allocate damages makes little sense. First, the liability action and the coverage action aim to answer different questions. The construction defect action generally asks whether a contractor violated applicable building codes, deviated from industry standards, or constructed housing that posed a serious risk of physical harm. *Kennedy v. Columbia Lumber & Mfg. Co. Inc.*, 299 S.C. 335, 347, 384 S.E.2d 730, 738 (1989). Indeed, the availability of insurance is not disclosed to the jury in the liability action. *See Bartell*, 259 S.C. at 24, 190 S.E.2d at.463; Rule 411, SCRE. On the other hand, the question of whether a particular claim is covered under a policy of insurance turns on the separate matter of interpretation of the insurance contract between the contractor and the insurer. *B.L.G. Enters., Inc. v. First Fin. Ins. Co.,* 334 S.C. 529, 535, 514 S.E.2d 327, 330 (1999).

Although both questions can involve issues of both law and fact, liability in the underlying tort action primarily presents a question of fact for the jury, while interpretation of insurance contracts primarily presents an issue of law for the court. *Bennett & Bennett Constr., Inc. v. Auto Owners Ins. Co.*, 405 S.C. 1, 4, 747 S.E.2d 426, 427 (2013). Because these are different questions, the damages judgment in the liability action should not preclude an insurer from allocating the total amount of the awarded judgment between covered and non-covered damages in a later coverage action. *See S.C. Prop. & Cas. Ins. Guar. Ass'n v. Wal-Mart Stores, Inc.*, 304 S.C. 210, 213, 403 S.E.2d 625, 627 (1991) (applying preclusive effect to issues actually litigated and essential to the judgment); *Sims*, 247 S.C. at 86–87, 145 S.E.2d at 525.

Second and more fundamentally, the damages judgment cannot have preclusive effect *against the insurer* in the subsequent coverage action because the insurer is not a party to the liability action. *See Major*, 267 S.C. at 520, 229 S.E.2d at 850. While an insurer may have a contractual relationship with the insured by virtue of the policy, that contractual privity is insufficient to trigger the preclusive doctrines because the interests of the insured and the insurer are only aligned on issues of liability, not issues of coverage. *See Normandy Corp. v. S.C. Dep't of Transp.*, 386 S.C. 393, 410 n.12, 688 S.E.2d 136, 145 n.12 (Ct. App. 2009) (explaining that issue preclusion may be applied where parties are in privity). "The term 'privy,' when applied to a judgment or decree, means one so identified in interest with another that he represents the same legal right. One in privity is one whose legal interests were litigated in the former proceeding." *Richburg v. Baughman*, 290 S.C. 431, 434, 351 S.E.2d 164, 166 (1986).

As *Sentry Select* confirms, the relationship between the insured and the insurer generally does not permit the insurer to control the defense where the interest of the two conflict. *See Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273. Where the insured and the insurer's interests diverge, the 'insurer's ability to control the defense is diminished to the extent it must be effectuated through retained counsel for the insured. *Id.* ("[T]he loyalties of the attorney may not be divided. . . . We do not recognize what the dissent calls the 'dual attorney-client relationship.'"). The retained defense counsel in such a conflict must act for the insured, and not as an agent for the insurer. *See Myatt v. RHBT Fin. Corp.*, 370 S.C. 391, 395, 635 S.E.2d 545, 547 (Ct. App. 2006) (confirming existence of adverse interest exception to agency whereby an agent may not act on behalf of a principle if the agent is acting against the principal's interest). This conflict destroys any privity between the insured and the insurer in the liability action, so

the damages judgment cannot have preclusive effect *against the insurer* in the subsequent coverage action.

Preclusion rules assume that the adversarial process will ascertain the truth of contested matters. *See Restatement (First) of Judgments* § 82 ("The rules of res judicata are based upon an adversary system of procedure which exists for the purpose of giving an opportunity to persons to litigate claims against each other."); *cf. Nance v. Ozmint*, 367 S.C. 547, 551, 626 S.E.2d 878, 880 (2006). Without intervention by the insurer, the adversarial process is lacking, leaving the insurer with no ability to contest a judgment in the liability or coverage actions. This fundamentally violates the insurer's right to due process because it allows the court in the liability action to issue a judgment binding the insured as a non-party that has been afforded no opportunity to be heard as required by due process. *See Langford v. McLeod*, 269 S.C. 466, 474, 238 S.E.2d 161, 164 (1977) (explaining that courts cannot bind non-parties).

Therefore, the Court should reverse to afford the Insurers the due process to which they are entitled.

II. The Court should modify *Newman* and *Harleysville* because they conflict with this Court's prior precedent and intervention is unworkable in practice.

The trial court denied the Insurers' motions to intervene by reasoning, in part, that the "Insurers can satisfactorily protect any purported interests they may have in a separate declaratory judgment action . . ." (R. at __; Order at 6.) Relying on *Sims v. Nationwide Mut. Ins. Co.*, 247 S.C. 82, 145 S.E2d 523 (1965), the trial court also ruled that South Carolina "requires a separate action" to determine insurance coverage issues "to avoid an impermissible conflict" in the underlying liability action. (*Id.*)

The trial court's ruling in reliance on *Sims* is only partially correct. The Court's orders in *Newman* and *Harleysville* changed the landscape for insurers attempting to protect their right to

allocate a general verdict between covered and non-covered damages. Though the two cases did not expressly state that they were overruling prior precedent, *see Sims*, 247 S.C. at 83, 145 S.E2d at 523, the cases implemented a procedure differing from prior practice. That new procedure—intervention and requesting special interrogatories to protect the record for a subsequent coverage action—is unworkable and conflicts with this Court's precedent. *See Sims*, 247 S.C. at 83, 145 S.E2d at 523; *Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273. Accordingly, the Court should modify its decisions in *Newman* and *Harleysville* to resolve this conflict.

A. *Newman* and *Harleysville* conflict with *Sims*' familiar limitations on the application of issue preclusion in future coverage actions.

The Court first addressed the effect a judgment in a liability action would have on an insurer in a subsequent coverage action in *Sims v. Nationwide Mut. Ins. Co.*, 247 S.C. 82, 83, 145 S.E2d 523, 523 (1965). There, an insurer refused coverage under an automobile liability policy on the grounds that its insured intentionally caused the accident. Because of the intentional action, the insurer refused to defend or indemnify the insured, which resulted in a damages verdict against the insured in the underlying tort action. *Id.* at 84, 145 S.E.2d at 523. In the subsequent coverage action, the trial court refused to permit the insurer to introduce evidence showing that the insured had acted intentionally because of the supposed preclusive effect of the underlying verdict in the liability action on the coverage action. *Id.* at 84, 145 S.E.2d at 524.

On appeal, the Court first recognized the general principle that "where an indemnitor has notice of and opportunity to defend an action against the indemnitee, he is bound by material facts established against the indemnitee whether he appeared in defense of the action or not." *Id.* at 86, 145 S.E.2d at 524–25. The Court, however, held that the underlying tort verdict could not preclude the insurer from arguing that its insured intentionally caused the accident. *Id.* at 86, 145 S.E.2d at 525. In so doing, the Court adopted the "unassailable" logic of an exception for

conflicts of interest, explaining that it was obvious that "the binding effect of a judgment against the insured does not extend to matters outside the scope of the insurance contract, and that the Insurance Company is neither obligated to defend nor bound by the findings of the court if the claim against the insured is not covered by the policy." *Id.* at 86–87, 145 S.E.2d at 525 (citing *Restatement (First) of Judgments* § 107(a)). The Court explained that a contrary holding would "estop the Insurance Company by the acts of parties in a transaction in which it has no concern and over which it has no control, and . . . deprive it of its day in court to show that the transaction is foreign to the contract of insurance." *Id.* Thus, the Court held that preclusion rules meant that the underlying judgment "is binding only as to issues relevant to the proceeding" and that the judgment "does not decide issues as to the existence and extent of the duty to indemnify . . . ." *Id.* (quoting *Farm Bur. Mut. Auto. Ins. Co. v. Hammer*, 177 F.2d 793, 799–800 (4th Cir. 1949)). Those questions, the Court held, were proper for "a subsequent action" where the insurer "may show that the circumstances under which he was required to give indemnity do not exist." *Id.*

Under *Sims*, liability actions and coverage actions proceed on two separate tracks. *Id.* In the construction defect context, the plaintiffs in the liability action must prove that the building was defectively constructed by the insured-contractor resulting in damages. *See Kennedy v. Columbia Lumber & Mfg. Co. Inc.*, 299 S.C. 335, 347, 384 S.E.2d 730, 738 (1989); *Bennett & Bennett Constr., Inc. v. Auto Owners Ins. Co.*, 405 S.C. 1, 4, 747 S.E.2d 426, 427 (2013). In the coverage action, the insurer seeks to demonstrate that its insurance contract with the insured-contractor does not cover all or certain portions of the damages awarded. *See B.L.G. Enters., Inc. v. First Fin. Ins. Co.*, 334 S.C. 529, 535, 514 S.E.2d 327, 330 (1999). The insurer is generally bound by the total amount of the judgment in the tort action and may be bound by factual findings made in the tort action upon issues in which the interests of the insured

contractor and the insurer were sufficiently aligned. *Sims*, 247 S.C. at 86–87, 145 S.E.2d at 525. If the interests of the insurer and insured diverge, however, no preclusion applies to limit the insurer's ability to contest coverage. *Id.*

Sims has been the law of the State for over fifty years. Yet in *Newman*, the Court ruled that "it is not the purpose of this declaratory judgment action to relitigate the issue of damages." *Newman*, 385 S.C. at 198, 648 S.E.2d at 547. This statement appears to depart from the exception recognized in *Sims* whereby the insurer may litigate—for the first time—the issues necessary to establish or deny coverage when a conflict of interest prohibited it from doing so during the underlying liability action. *Id.* at 86–87, 145 S.E.2d at 525. *Newman*, though, does not cite *Sims*, nor explain its departure from that prior precedent.

The Court's ruling in *Harleysville* also conflicts with *Sims*. As explained above, *Harleysville* requires an insurer to seek intervention in a construction defect proceeding to avoid the entry of a general verdict that fails to allocate between covered and non-covered damages. *Harleysville*, 420 S.C. at 343–44, 803 S.E.2d at 300–01. In so doing, *Harleysville* creates a presumption of coverage in favor of the insured if the insurer fails to seek intervention to secure responses to special interrogatories. *Id.*; *cf. Duke v. Hoch*, 468 F.2d 973, 984 (5th Cir. 1972) (explaining opposite presumption under Florida law).

In light of the presumption created by *Harleysville*, it is only the insurer that has an interest in an allocated verdict, not the insured. Thus, it is in the best interest of the insured-contractor to oppose any request for an allocated verdict. This, in turn, requires the defense counsel retained for the insured to argue against an allocated verdict. Otherwise, an impermissible conflict of interest arises in which the defense counsel must refuse to seek

allocation as requested by the insurer. *See Sentry Select*, 426 S.C. at 160, 826 S.E.2d at 273 (2019) (citing Rules 1.8(f) and 5.4(c), RPC, Rule 407, SCACR).

This puts *Newman* and *Harleysville* in conflict with *Sims*, especially in light of this Court's recent opinion in *Sentry Select*. The Court should, therefore, modify *Newman* and *Harleysville* to explain whether the exception in *Sims* has been abrogated. If *Sims* remains good law, then the Court should modify its opinions in *Newman* and *Harleysville* to address the practical effect those opinions have had on insurers attempting to preserve their contractual right to allocate between covered and non-covered damages in construction defect actions.[7]

B. Returning to *Sims* avoids confusion and the opportunity for conflict created if an insurer is required to intervene to protect the record.

As the dissent in *Harleysville* explained, the Court has offered no guidance to insurers in how they can properly protect the record to preserve their right to contest coverage in a subsequent action. *Harleysville*, 420 S.C. at 363, 803 S.E.2d at 311 (Pleicones, A.J., dissenting) (citing *Sims* after commenting that "there is no suggestion how Harleysville could have intervened in these lawsuits and asserted a defense against coverage without creating an impermissible conflict of interest in violation of established South Carolina law."). Attempting to protect the record by seeking intervention has created inconsistent results and has proven unworkable given the potential for conflicts.

This is why courts from other jurisdictions permit the issue of allocation to be determined in a subsequent action. Those courts have recognized, like *Sims*, that an underlying verdict is not preclusive relating to issues of covered versus non-covered damages, and that subsequent

[7] The Court's deferential adherence to its opinions in *Newman* and *Harleysville* should not deter it from clarifying whether that precedent requires intervention and special interrogatories here. "It is well-established that [the Court] need not blindly adhere to established precedent." *Proctor v. Whitlark & Whitlark, Inc.*, 414 S.C. 318, 332, 778 S.E.2d 888, 895 (2015).

declaratory judgment litigation is permissible. Those courts permitting allocation of a general verdict analyze the actions of the insurer and insured in the liability action to determine which party has the burden of proving allocation in the coverage action. The courts then use the parties' actions to determine whether additional evidence and testimony is necessary to allocate the verdict from the liability action. The courts do not reach the same harsh result reached by the Court in *Newman* and *Harleysville*, whereby an insurer is left with no ability to argue issues of coverage or allocation in the subsequent action *at all*. The courts from other jurisdictions instead allocate the burden of proof differently—they stop short of precluding a party from litigating the issue altogether. In resolving the conflict amongst its precedent in *Sims*, *Newman*, *Harleysville*, and *Sentry Select*, the Court should follow the courts that have addressed the issue by allocating the burden of proof based on the parties' actions in the liability action in lieu of prohibiting a party (or non-party) from arguing allocation altogether under issue preclusion principles.

For example, if an insurer under Florida law succeeds in showing that "the judgment includes elements for which an insurer is liable and also elements beyond the coverage of the policy, the burden of apportioning or allocating these damages is on the party seeking to recover from the insurer." *Arnett v. Mid-Continent Cas. Co.*, No. 8:08-cv-2373, 2010 WL 2821981, at *5 (M.D. Fla. July 16, 2010). In *Arnett*, the parties contended that apportionment was impossible in light of the underlying general verdict. *Id.* The court explained, however, that an insured under Florida law would be relieved of its burden if the insurer failed to advise the insured of the availability of a special verdict and the divergence of interest between the insurer and insured regarding obtaining an allocation. *Id.* at *5–6. The court noted that obtaining an allocated verdict is in the insured's interest because the "inevitable consequence of a general verdict is a 'catastrophic total loss of coverage.'" *Id.* Contrast this with the insurer, which has

an interest under Florida law in using a general verdict form "when an action involves elements of both covered and non-covered damages." *Id.*

In *Arnett*, the record did not contain any evidence suggesting that such a disclosure was made to the insured. *Id.* at *6. Therefore, the insured was relieved of the "impossible burden" of proving the precise amount awarded for covered damages. *Id.* The declaratory judgment court was then tasked with determining "as best [it] can the allocation which the jury would have made had it been tendered the opportunity to do so." *Id.* (quoting *Duke v. Hoch*, 468 F.2d 973, 984 (5th Cir. 1972)). The court noted that the underlying trial record did not permit a meaningful allocation. *Id.* But instead of merely deciding that the general verdict had preclusive effect, prohibiting either party from presenting additional evidence regarding allocation, the court did just the opposite—it determined that allocation would be resolved at trial in the declaratory action. *Id.*; *see also Mid-Continent Cas. Co. v. C-D Jones & Co. Inc.*, No. 3:09-cv-565, 2013 WL 12081104, at *5 (N.D. Fla. Aug. 6, 2013) (under similar facts, noting that the trier of fact in the coverage action would "determine what allocation the jury would have made if it had been given an opportunity to do so" based on the trial record, but the insureds would be permitted to present additional expert evidence, to which the insurers could present rebuttal evidence).

The Tenth Circuit reached a similar result in *Automax Hyundai S., L.L.C. v. Zurich Am. Ins. Co.*, 720 F.3d 798 (10th Cir. 2013). As the *Automax* court explained, where there is a general verdict in an underlying liability action possibly consisting of covered and non-covered claims, the question "becomes "who bears the burden for allocating the judgment between the covered and noncovered claims." *Id.* at 807 (quoting Allan D. Windt, *Ins. Claims & Disputes* § 6:27 (2013)). Where both covered and non-covered causes of action are alleged, the insurer, if it is controlling the insured's defense, "must request a special verdict to disentangle the facts

relevant to its indemnification of the insured." *Id.* In other words, "'damages are presumed to be covered' unless the insurer can demonstrate an appropriate allocation." *Id.* (quoting *Magnum Foods, Inc. v. Cont'l Cas. Co.*, 36 F.3d 1491, 1498 (10th Cir. 1994)). If the insurer fails to request a special verdict or fails to provide a defense at all, the insurer would bear the burden of allocation in a subsequent action. *Id.* However, the insurer can shift the burden to the insured by informing the insured that it would be in its best interest to request a special verdict. *Id.* at 807 n.2. The *Automax* court found that when the insurer fails to obtain a special verdict or wrongfully refuses to defend and a general verdict is rendered, the insurer should still have the opportunity to satisfy its burden in a subsequent declaratory action. *See id.* at 809–10.

The Southern District of New York also handled the placement of the burden of proving allocation in the same way. In *Uvino v. Harleysville Worcester Ins. Co.*, No. 13-cv-4004, 2015 WL 925940, at *7–8 (S.D.N.Y. Mar. 4, 2015), the insurer moved to intervene for the purpose of requesting special interrogatories to avoid a coverage allocation dispute and "therefore made known [to the insured] both the availability of the interrogatories and the parties' divergence of interests." *Id.* Thus, the insurer complied with its responsibilities to its insured such that the burden of proving allocation would remain with the insured. *Id.* However, the court found that the insurer was not entitled to summary judgment in the coverage action due to a genuine issue of fact, and noted that the insureds could proceed to trial on the issue of allocation, "at which they can attempt to show what portion of the general verdict returned by the jury, if any, is attributable to covered claims." *Id.*

Similarly, in Texas, a federal district court also permitted allocation in a subsequent coverage action notwithstanding the issuance of a general verdict. *Soc'y of Professionals in Dispute Resolution, Inc. v. Mt. Airy Ins. Co.*, No. 3:97-CV-0071, 1997 WL 711446, at *7–8

(N.D. Tex. Nov. 7, 1997). There, the court noted that apportionment most frequently becomes an issue where the insurer breaches its duty to defend. *Id.* at *7. The court explained that although prior cases found that an insurer is bound by the judgment where it refuses to defend, they also acknowledge that "the insurer does not necessarily owe the insured a duty to pay all damages assessed." *Id.* Rather, the damages in a judgment or settlement of the underlying lawsuit "must be apportioned between claims covered by the policy and those that are not." *Id.* The insured bears the burden under Texas law of apportioning damages between coverage and non-coverage. *Id.* Because the court could not determine the issue of apportionment as a matter of law based on a lack of disputed facts, the Court determined that the issue would be tried even though the insurer had previously breached its duty to defend. *Id.* at *8.

All of these cases support that allocation of a general verdict rendered in an underlying liability action may be made between covered and non-covered claims in a subsequent declaratory judgment action. Such a procedure would be consistent with *Sims.* Such a procedure would also avoid the types of conflicts inherent in requiring special verdicts to allocate the liability when such an allocation would not be in the insured's best interests. *See Sentry Select,* 426 S.C. at 160, 826 S.E.2d at 273. When an insurer is not a party to a liability action against its insured, and a verdict is rendered that relates to both covered and non-covered claims, the insurer should have the right to obtain allocation of the verdict. Otherwise the scope of coverage is impermissibly expanded beyond what the parties contemplated at the time of contract. *S.C. Farm Bureau Mut. Ins. Co. v. Wilson,* 344 S.C. 525, 530, 544 S.E.2d 848, 850 (Ct. App. 2001) ("[I]f the intention of the parties is clear, courts have no authority to torture the meaning of policy language to extend coverage that was never intended by the parties."); *Alverson v. Minn.*

Mut. Life Ins. Co., 287 S.C. 432, 434, 339 S.E.2d 140, 142 (Ct. App. 1985) ("Waiver cannot create coverage and cannot bring into existence something not covered in the policy.").

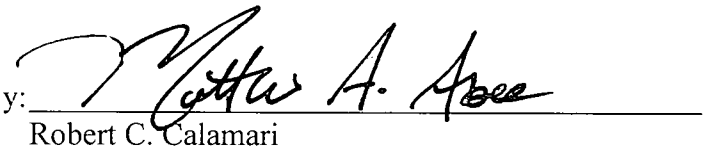
Conclusion

Here, the Insurers attempted to protect their rights to later contest coverage by intervening and to request that the trial court interpose special interrogatories or a special verdict form to the jury. They did so to avoid the possibility of forfeiting their right to an allocated verdict. The trial court erred in denying their motions to intervene because the Insurers ability to obtain allocation between damages covered by their policies and those that are not covered will now be impaired or impeded. *See Newman*, 385 S.C. at 198, 684 S.E.2d at 547; *Harleysville*, 420 S.C. at 343–44, 803 S.E.2d at 300–01. Thus, the Court should reverse.

In so doing, the Court should modify *Newman* and *Harleysville*, resolving the conflict that those cases present with *Sims* and the Court's more recent opinion in *Sentry Select*. The Court should instead adopt a procedure for permitting allocation of covered and non-covered damages in a subsequent coverage action by properly allocating the burden of proof based on the parties' actions in the underlying liability action. Doing so will not only provide clarity to the bench and bar, but will also protect the due process rights of the Insurers.

[Signature on following page.]

NELSON MULLINS RILEY & SCARBOROUGH LLP

By: 

Robert C. Calamari
SC Bar No. 064985
E-Mail: bob.calamari@nelsonmullins.com
Matthew A. Abee
SC Bar No. 101100
E-Mail: matt.abee@nelsonmullins.com
Patrick F. O'Dea
SC Bar No. 004262
E-Mail: patrick.odea@nelsonmullins.com
1320 Main Street / 17th Floor
Post Office Box 11070 (29211-1070)
Columbia, SC 29201
(803) 799-2000

Attorneys for Harleysville Insurance Company n/k/a Nationwide Insurance Company and Selective Insurance Company

Columbia, South Carolina
December 4, 2019

MCCULLOUGH KHAN, LLC

Clayton B. McCullough
SC Bar No. 13722
Email: clay@mklawsc.com
Ross A. Appel
SC Bar No. 79149
Email: ross@mklawsc.com
359 King Street, Suite 200
Charleston, SC 29401
(843) 937-0400

Attorney for American Empire Surplus Lines Insurance Company

HUNTER & FOSTER, PA

Lawrence M. Hunter, Jr.
SC Bar No. 11808
Email: Lawrence@HunterFoster.com
Post Office Box 10309
Greenville, South Carolina 29603
(864) 242-2111

Attorney for BITCO General Insurance Corporation

WALL TEMPLETON & HALDRUP, P.A.
Neil S. Haldrup
SC Bar No. 13017
Email: Neil.Haldrup@WallTempleton.com
Thomas B. Boger
SC Bar No. 81228
Email: Tommy.Boger@WallTempleton.com
Post Office Box 1200
Charleston, South Carolina 29402
(843) 329-9500

Attorneys for Clarendon National Insurance Company, Successor by Merger to Clarendon America Insurance Company

TURNER PADGET GRAHAM & LANEY, P.A.
John S. Wilkerson, III
SC Bar No. 6105
Email: jwilkerson@turnerpadget.com
P.O. Box 22129
Charleston, South Carolina 29413
(843) 576-2801

R. Hawthorne Barrett
SC Bar No. 16973
Email: tbarrett@turnerpadget.com
PO Box 1473
Columbia, SC 29202
(803) 227-4219

Attorneys for Crum & Forster Specialty Insurance Company and First Mercury Insurance Company

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM HORRY COUNTY
Court of Common Pleas

Clifton Newman, Circuit Court Judge

Appellate Case No. 2019-001053

Ex. Parte: Hartford Fire Insurance Company, Hartford Casualty Insurance Company, American Empire Surplus Lines Insurance Company, BITCO General Insurance Corporation, Clarendon National Insurance Company, Harleysville Insurance Company n/k/a Nationwide Insurance Company, Selective Insurance Company, Crum & Forster Specialty Insurance Company, and First Mercury Insurance Company, ... Appellants

In Re:

The Havens Condominium Association, ... Plaintiff,

v.

Centex Homes, et al., ... Defendants,

The River Crossing Condominium Association, and Vincent J. Tamburro, on behalf of himself and others similarly situated ..... Plaintiffs

v.

Centex Homes, et al., ... Defendants,

The Tanglewood Condominium Association ..... Plaintiff,

v.

Centex Homes, a Nevada General Partnership, et al., ... Defendants,

The Woodlands Condominium Association ..... Plaintiff,

v.

Centex Homes, a Nevada General Partnership, et al., ... Defendants,

Of Which, The Havens Condominium Association, The River Crossing Condominium Association, Vincent J. Tamburro, The Tanglewood Condominium Association, The Woodlands Condominium Association, and Centex Homes, a Nevada General Partnership, are the ..... Respondents.

Proof of Service

I, the undersigned Administrative Assistant of the law offices of Nelson Mullins Riley & Scarborough LLP, attorneys for Harleysville Insurance Company n/k/a Nationwide Insurance Company and Selective Insurance Company, certify that I have served all counsel in this action with a copy of the document(s) set forth below by mailing a copy by United States Mail, postage prepaid, to the following address(es):

Pleadings: **Initial Brief by Appellants American Empire Surplus Lines Insurance Company, BITCO General Insurance Corporation, Clarendon National Insurance Company, Harleysville Insurance Company n/k/a Nationwide Insurance Company, Selective Insurance Company, Crum & Forster Specialty Insurance Company, and First Mercury Insurance Company**

Counsel Served:

Mark Steven Barrow, Esquire
Christy Elizabeth Mahon, Esquire
Sweeny, Wingate & Barrow, P.A.
PO Box 12129
Columbia, SC 29211

Steven M. Klepper, Esquire
Kramon & Graham PA
One South Street, Suite 2600
Baltimore, MD 21202

Clayton B. McCullough, Esquire
Ross A. Appel, Esquire
McCullough Khan, LLC
359 King Street, Suite 200
Charleston, SC 29401

Lawrence M. Hunter, Jr., Esquire
Hunter & Foster, PA
PO Box 10309
Greenville, SC 29603

John W. Wilkerson, III, Esquire
Turner Padget Graham & Laney, P.A.
PO Box 22129
Charleston, SC 29413
Neil S. Haldrup, Esquire

Thomas B. Boger, Esquire
Wall Templeton & Haldrup, P.A.
PO Box 1200
Charleston, SC 29402

R. Hawthorne Barrett, Esquire
Turner Padget Graham & Laney, P.A.
PO Box 1473
Columbia, SC 29202

Phillip Ward Segui, Jr., Esquire
Mary Abigail Young, Esquire
Segui Law Firm
864 Lowcountry Blvd., Suite A
Mt. Pleasant, SC 29464

John T. Chakeris, Esquire
Chakeris Law firm
231 Calhoun Street
Charleston, SC 29401

Shaun W. Cranford, Esquire
Cranford Law Firm
PO Box 50684
Columbia, SC 29250

Thomas C. Hildebrand, Jr., Esquire
William Green DesChamps, IV, Esquire
Parker Poe Adams & Bernstein, LLP
200 Meeting Street, Suite 301
Charleston, SC 29401

Laura Figueroa Locklair, Esquire
Boyle, Leonard & Anderson, P.A.
28 Hasell Street
Charleston, SC 29401-3156

Kim Smith

Kim Smith, Administrative Assistant

December 4, 2019