THE STATE OF SOUTH CAROLINA
In the Supreme Court

RECEIVED

May 28 2020

S.C. SUPREME COURT

APPEAL FROM CHARLESTON COUNTY
Court of Common Pleas

Jennifer B. McCoy, Circuit Court Judge

Case No. 2015-CP-10-00955
Appellate Case No. 2019-000238

Ex Parte:

Builders Mutual Insurance Company and Nationwide Mutual Insurance Company, ... Appellants,

In Re:

Palmetto Pointe at Peas Island Condominium Property Owners Association, Inc., and Jack Love, Individually, and on behalf of all others similarly situated, ...Plaintiffs,

v.

Island Pointe, LLC; Leonard T. Brown; Complete Building Corporation; Tri-County Roofing, Inc.; Creekside, Inc.; American Residential Services, LLC d/b/a Rescue Rooter Charleston; Andersen Windows, Inc.; Atlantic Building Construction Services, Inc. n/k/a Atlantic Construction Services, Inc.; Christopher N. Union; Builder Services Group, Inc. d/b/a Gale Contractor Services; Novus Architects, Inc. f/k/a SGM Architects, Inc.; Tallent and Sons, Inc.; W C Services, Inc., CRG Engineering, Inc.; CertainTeed Corporation; Kelly Flooring Products, Inc. d/b/a Carpet Baggers and John Doe 1-60, ... Defendants,

Tri-County Roofing, Inc., ...Third-Party Plaintiff,

v.

Cornerstone Construction and Mark Malloy d/b/a Cornerstone Construction; Gutter Works, Inc. and Michael L. Segars d/b/a Gutter Works; Mr. Gutter; Litchfield Seamless Gutters & Windows, LLC and Thomas Litchfield d/b/a Litchfield Seamless Gutter; Miracle Siding, LLC and Wilson Lucas Sales d/b/a Miracle Siding, LLC; Mark Palpoint a/k/a Micah Palpoint; Elroy Alonzo Vasquez; and Chris a/k/a John Doe 61, ...Third-Party Defendants.

and

Complete Building Corporation, Inc., ...Third-Party Plaintiff,

v.

Alderman Construction; Stanley's Vinyl Fence Designs; Cohen's Drywall; and Mosley Concrete, ...Third-Party Defendants,

Of Whom Palmetto Pointe at Peas Island Condominium Property Owners Association, Inc. and Jack Love, Individually, and on behalf of all others similarly situated, and Tri-County Roofing, Inc., Stanley's Vinyl Fence Designs, and WC Services, Inc., ...Respondents.

RESPONDENTS' PETITION FOR REHEARING

Justin O'Toole Lucey, Esquire
SC Bar No.: 15438
Anna S. McCann, Esquire
SC Bar No.: 102314
Justin O'Toole Lucey, P.A.
415 Mill Street
Mount Pleasant, South Carolina 29201
Telephone: 843.849.8400
E-Mail: jlucey@lucey-law.com
amccann@lucey-law.com

Attorneys for the Respondents Palmetto Pointe at Peas Island Condominium Property Owners Association, Inc. and Jack Love, Individually, and on behalf of all others similarly situated

PETITION FOR REHEARING

Pursuant to Rules 221 and 240 of the South Carolina Rules of Appellate Procedure ("SCACR"), Respondents[1] respectfully file this Petition for Rehearing of this Court's Opinion filed May 13, 2020 (Shearhouse Adv. Sh. No. 19 at 48, Opinion No. 27970) ("Opinion"). Respondents seek a limited rehearing to clarify certain conflicting points of law and procedure contained in the Court's Opinion.

CLARIFICATION SOUGHT

I. Did the Court err 1) in making the trial transcript primary, without limitation; and 2) in making the admission of additional evidence discretionary in a declaratory judgment action?

STANDARD OF REVIEW

Rule 221, SCACR, authorizes a party who believes the Court overlooked or misapprehended points of law or fact to petition for rehearing. *Arnold v. Carolina Power & Light Co.*, 168 S.C. 163, 167 S.E.2d 234 (1933). "The purpose of such a petition is to aid the court in deciding correctly a case heard by it" and a properly drawn rehearing petition must state "the points … overlooked or misapprehended by the court." *Id.* at 172-73; *Kennedy v. S.C. Retirement System*, 349 S.C. 531, 532, 564 S.E.2d 322, 322 (2001).

ARGUMENT

I. All Parties to a Declaratory Judgment Action Must Have the Right to Fully and Fairly Litigate Coverage Issues

This Court's holding that "[t]he primary source of evidence in the declaratory judgment action should be the transcript of the merits hearing"[2] and only allowing additional evidence at the

[1] The "Respondents" are: Palmetto Pointe at Peas Island Condominium Property Owners Association, Inc. and Jack Love, Individually, and on behalf of all others similarly situated.
[2] (Opinion, pp. 61-2).

court's "discretion"[3] is erroneous because (1) it would unduly prejudice *all* parties to a declaratory judgment action, and (2) introducing "discretion" into the framework without caveat conflicts with this Court's own Opinion and established South Carolina precedent. The transcript of the merits hearing should be primary (and binding) as to the matters fully and fairly litigated therein, such as liability and amount of damages, and should otherwise simply provide a contextual background for the insurance coverage litigation.

Respondents respectfully request that the Court modify its holding as follows:

> The transcript of the merits hearing will be the primary source of evidence *concerning matters litigated therein*; it will *not* be primary as to issues not litigated in and not necessary to the resolution of the underlying trial, e.g., policy interpretation, proof of consequential damages, and questions of coverage, and additional evidence will typically be admitted on these latter issues.

While this distinction may seem minute, rendering a party's ability to introduce additional evidence relevant to questions of coverage in a declaratory judgment proceeding "discretionary" may lead to the very result this Court sought to avoid in precluding an insurer's ability to intervene – creating an indirect requirement that the parties force their coverage evidence into the trial of the underlying litigation to make sure it is part of the "primary evidence," rather than taking the risk that the subsequent court's discretion will be favorable.

a. Allowing Additional Evidence on Coverage Matters Only at The Court's Discretion Would Result in Prejudice to All Parties

This Court firmly, and correctly, held that allowing an insurer to intervene in an underlying construction defect action would result in prejudice to the original parties, i.e., the injured plaintiff Association ("Association")[4] and the insured. (Opinion, p. 54). The prejudice to the insured stems

[3] (*Id.*).

[4] Respondent will interchangeably use the terms "Association", "Underlying Plaintiff", and "Injured Plaintiff" herein, as dictated by context, each meaning the Plaintiff in the underlying action.

from the conflict of interest which intervention would create for the insureds' counsel "to essentially concede[] liability so as to focus instead on damages." (*Id.* at 56). The prejudice to the Association would effectively force on it a "heightened burden to itemize damages into insurer-defined categories which the Association may not have intended to present to the jury." (*Id.* at 55).

After recognizing the prejudice which would result from allowing an insurer to intervene, this Court moved on to the mechanism by which a subsequent declaratory judgment action should be tried. (*Id.* at 59). There, it discussed the prejudice which would result to the insurer if it were bound by factual determinations made in the underlying merits trial. (*Id*.). The premise that an insurer cannot be bound by factual determinations in the underlying action because of the inherent conflict of interest between its indemnification obligations and its obligation to defend was established in *Sims* and is reestablished by this Court in the instant Opinion: "[T]he indemnitor has a right to its day in court on whether the indemnitee's liability is within the scope of the indemnity obligation." (Opinion, p. 60).

> In *Sims*, the Court explained that, generally, "where an insurance company has notice and [an] opportunity to defend an action against its insured, the company is bound by pertinent material facts established against its insured, whether it appears in the defense of the action or not." 247 S.C. at 84–85, 145 S.E.2d at 524. However, the Court reasoned that rule could not apply in situations where the insurance company had a conflict of interest with its insured, such as when the company claimed the acts being sued over were partially or wholly outside the scope of the applicable insurance policy. *Id.* at 85–89, 145 S.E.2d at 524–26 (explaining the underlying purpose of the general rule is to obviate the delay and expense of two trials upon the same issue between parties whose interests are identical; and when a conflict of interest causes the parties' interests to diverge, "the judgment against the [insured] does not decide issues as to the existence and extent of the duty to indemnify," such that "in a subsequent action the [insurance company] may show that the circumstances under which [it] was required to give indemnity do not exist" (quoting *Farm Bureau Mut. Auto. Ins. Co. v. Hammer*, 177 F.2d 793, 799–801 (4th Cir. 1949) (citing the predecessor to the modern Restatement (Second) of Judgments § 58 (2020)))).
>
> As further explained in section 58 of the Restatement (Second) of Judgments:

> [T]he indemnitor has a right to its day in court on whether the indemnitee's liability is within the scope of the indemnity obligation....
>
> ... [A]n indemnitor who has an independent duty to defend the indemnitee in effect has two legal capacities with regard to the indemnitee. In his capacity as insurer against the indemnitee's risk of being sued on claims that "might be found to be" within the indemnity obligation, the indemnitor has a responsibility to provide counsel and supporting assistance to defend the indemnitee without regard to the indemnitor's interests .... In his capacity as indemnitor, he has a responsibility to indemnify for such liability as may be within the indemnity obligation. In the latter capacity, he should not be bound by determinations in an action in which he participated in the former capacity if there is a conflict of interest between the two.

(Opinion, pp. 59-60) (some internal citations omitted).

Allowing the introduction of additional evidence on coverage issues *only* at the *discretion* of the trial court cannot be squared with an indemnitor having the "right to its day in court" as to its indemnity obligation, nor can it be squared with an insured (and injured plaintiff) having the same right. This Court said as much earlier in the Opinion: "Insureds and the Insurers are not precluded from introducing evidence as to which damages are covered (or excluded from coverage) by the CGL policies." (Opinion, p. 60). The Association (as well as the insured and insurer)[5] must also have the unqualified *right* to litigate issues relevant to coverage which were not litigated previously.[6] To hold otherwise would deny a fair day in court to all parties involved, and would essentially allow the insurer to reap the benefits of collateral estoppel and issue preclusion without meeting the essentials of those legal theories, especially that the issue was "directly determined in the prior action" and the issue was "necessary to support the prior

[5] Arguably, this error is more prejudicial to the insured as the Opinion elsewhere indicates that insurers have a right to re-litigate matters in which there was a conflict of interest, thereby potentially tempering the discretion in favor of insurers.

[6] *Amerisure Ins. Co. v. Auchter Co.*, No. 3:16-CV-407-J-39JRK, 2017 WL 4862194, at *13 (M.D. Fla. Sept. 27, 2017) ("Where coverage issues were not litigated or determined by judgment in the underlying state court action, **the parties are not estopped** from litigating coverage issues in a subsequent lawsuit regarding an insurer's indemnity obligations.")(emphasis added).

judgment." *Carolina Renewal, Inc. v. S.C. Dep't of Transp.*, 385 S.C. 550, 554, 684 S.E.2d 779, 782 (Ct. App. 2009).[7]

Respondent suggests that the proper framework for adducing evidence in a coverage-focused declaratory judgment action following an underlying trial on the merits is that the transcript of the underlying trial will be the primary evidence *as to those matters litigated therein*, but it will not be primary as to issues *not* litigated therein, e.g., additional facts or expert testimony relevant to policy interpretation and coverage.

b. Allowing the Discretionary Introduction of Additional Evidence Regarding Issues of Coverage Conflicts in Practice with the Court's Opinion

In holding that the transcript of the merits hearing will be the "primary" source of evidence in a coverage-focused declaratory judgment action and by introducing unbridled discretion into the declaratory judgment framework, the Court is *still* essentially asking the Association (and any

[7] Other jurisdictions echo similar concerns. *See e.g., Nationwide Mut. Ins. Co. v. Pasiak*, 327 Conn. 225, 266–67, 173 A.3d 888, 911 (2017) (""[F]acts pertaining to insurance coverage may have no relevance to the issues of liability and damages that the trier of fact must decide in the underlying action.") *see also Swicegood ex rel. Swicegood v. Med. Protective Co.*, No. CIV.A.3:95-CV-0335-D, 2003 WL 22234928, at *14 (N.D. Tex. Sept. 19, 2003) ("The court predicts that the Texas Supreme Court will hold that new evidence can be introduced at a coverage trial when the proof is necessary to resolve a controlling coverage question that was not conclusively decided in the indemnity suit. By "not conclusively decided" the court means the issue was not determined in a way that binds all affected parties in the coverage case (e.g., via **collateral estoppel**). An undecided issue could include one that the parties in the indemnity case had no reason to litigate, e.g., an exclusion from coverage, where the burden of proof would be on a non-party insurer.") (emphasis added); *Chenkus v. Dickson*, Docket No. 282007, 1990 WL 283216, *1 (Conn. Super. September 7, 1990) (noting that, because case pertains to negligent and intentional assault, it had nothing to do with whether those acts are covered under contract of insurance); *Wear v. Farmers Ins. Co. of Washington*, 49 Wash. App. 655, 661, 745 P.2d 526, 529 (1987) ("Therefore, the jury's interrogatories and the verdict in the liability trial are irrelevant to the determination of Wear's intent and the existence of coverage under the Wears' policy. How, then, is the issue of the insured's intent to be determined? It can only be determined at a hearing at which the trial court **takes evidence on the coverage issue**.").

underlying injured plaintiff in similar circumstances) to tailor its evidence and testimony to coverage issues. This is unworkable for the same reasons expounded upon by the Court when denying intervention:

- Insurer is not a party to the underlying action, nor can it be.[8]
- Coverage is not at issue in the underlying action, nor can it be.[9]
- Plaintiff in underlying action is not required to introduce evidence relevant to the application of policy exclusions in anticipation of a coverage action, nor should it be.[10]

Indeed, requiring that the transcript of the merits hearing be the primary source of evidence in a declaratory judgment action regarding covered versus uncovered damages under a contract of insurance, and only allowing additional evidence at the discretion of the court, has the distinct potential to lay at the feet of the Association the very burden this Court sought to prevent:

- "[B]y motioning to intervene, the Insurers essentially sought to force the Association and the jury to itemize damages against each Insured, which was not otherwise required." (Opinion, pp. 51-2);

- "There are facts in the record supporting the trial court's decision that the Insurers' intervention would […] unnecessarily complicate the construction defect action, including altering the Association's burden of proof and possibly delaying the trial[…]." (*Id* at p. 54);

- "[W]e note that, absent the Insurers' intervention, the Association has no need to parse its damages into categories corresponding to the coverage provided in a CGL policy." (*Id.* at p 54);

- "[W]ith the addition of special jury interrogatories and verdict forms, the Association—as the plaintiff, with the burden of proof—would have a heightened burden to itemize its damages into Insurer-defined categories which the Association may not have intended to present to the jury." (*Id.* at p. 55).

[8] (Opinion, p. 51, fn.1, *citing Crocker v. Weathers*, 240 S.C. 412, 424, 126 S.E.2d 335, 340-41 (1962)).
[9] (*Id.*).
[10] (Opinion, pp. 51-2).

Under the Court's current dicta, the Court is still essentially requiring the Plaintiff to present testimony in the underlying case in support of the ultimate coverage issues. If Plaintiff fails, it risks having an inadequate record to support its position in the coverage-focused declaratory judgment action.

A hypothetical illustrating what Respondent believes to be an unintended consequence of introducing discretion into the framework may prove useful. An injured Plaintiff homeowner at trial against a roofer alleging negligence must prove, by a preponderance of the evidence, (1) duty; (2) breach; (3) causation; and (4) damages. Assume the Plaintiff succeeds and is awarded a monetary verdict against the roofer, an insured of ABC Insurance Company. ABC Insurance Company, who defended the action with a reservation of rights, brings a subsequent declaratory judgment action seeking a determination of its indemnification obligations. ABC argues that there is no coverage for the claim because there was no property damage to non-defective components caused by the roofer's negligent work. Plaintiff was not required to prove property damage to non-defective components in order to plead and prove roofer's liability, nor did it do so. Therefore, based upon the underlying trial on the merits, which is the "primary" source for determining coverage in subsequent declaratory judgment actions, the trial court, in its discretion, declines additional evidence and the insurer is granted summary judgment. Roofer has no coverage for the verdict. In this example, the insured and the underlying Plaintiff are the ones prejudiced because of their inability to introduce additional evidence relevant to the issue of coverage. This is a highly simplistic example and the difficulties illustrated would be exponentially greater in a typical construction defect trial, as the number claims, insurers, and coverage issues would multiply with each additional defendant.

The closer one scrutinizes this example, the more prejudicial this ruling becomes. Assume further that the roofer's work was performed by a subcontractor. Under the typical ISO CGL[11] policy, the "your work" policy exclusion is negated for any of "your work" performed by subcontractors. Again, there was no need for Plaintiff to prove this detail in its underlying defect case, but it has monumental implications in the later coverage case. If the transcript is primary, and additional evidence is discretionary, the underlying Plaintiff may be denied its opportunity to prove that its verdict is insured.

Note further, taken to its logical but absurd extreme, the insurance policies are not admitted as evidence in the underlying trial, and this opinion can be read to make their admission in the subsequent trial "discretionary." Respondents doubt that is what this Court intended, and simply seeks to help the Court clarify.

CONCLUSION

Requiring the subsequent trial court to consider whatever evidence may be necessary for a proper indemnity coverage analysis, including evidence beyond that which was presented at the trial in the underlying action, makes sense. In the underlying action, and insured is defending itself against the tort claims of a third party who has the burden of proof. In the coverage-focused declaratory judgment action pursued by the insurer, by contrast, the trial court is to determine whether the insurer is obligated to indemnify the insured for the judgment obtained in the underlying action. This determination does not often fit easily within the evidence presented at trial in the underlying action for the reasons already espoused by this Court in its Opinion.

[11] "ISO" is the acronym for "Insurance Services Office"; "CGL" is the acronym for "Commercial General Liability" insurance policies. The ISO provides standard insurance forms for insurers to incorporate into their policies.

While the transcript of the underlying trial may be "primary" as to the matters fully and fairly litigated therein, it cannot, and should not, be primary for matters which were not. Respondent respectfully requests that the Court modify its holding as follows:

> The transcript of the merits hearing will be the primary source of evidence *concerning matters litigated therein*; it will *not* be primary as to issues not litigated in and not necessary to the resolution of the underlying trial, e.g., policy interpretation, proof of consequential damages, and questions of coverage, and additional evidence will typically be admitted on these latter issues.

Stated differently, a correct statement from the Court would be the following: "Both insured and insurer are bound by the total judgment amount as the damages at issue, and the declaratory judgment action shall determine which, if any, of those damages are covered under the insurance contract." This Court said as much, but inadvertently clouded the issue in its procedural discussion.

Making this clarification, which is in accord with South Carolina jurisprudence, will reduce future confusion in trial courts such as that which resulted from *Newman* and *Harleysville,* which the Court sought to put to rest in this Opinion.

Respectfully submitted,

/s/ Justin O'Toole Lucey
Justin O'Toole Lucey, Esquire
SC Bar No.: 15438
Anna S. McCann, Esquire
SC Bar No.: 102314
Justin O'Toole Lucey, P.A.
415 Mill Street
Mount Pleasant, South Carolina 29201
Telephone: 843.849.8400
E-Mail: jlucey@lucey-law.com
amccann@lucey-law.com

Attorneys for the Respondents Palmetto Pointe at Peas Island Condominium Property Owners Association, Inc. and Jack Love, Individually, and on behalf of all others similarly situated

Mount Pleasant, South Carolina
May 28, 2020