THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM BERKELEY COUNTY
Court of Common Pleas

Roger M. Young, Sr., Circuit Court Judge

Case No. 2014-CP-08-02757

RECEIVED
Jul 13 2020
SC Court of Appeals

Portrait Homes – South Carolina, LLC; Portrait Homes – Persimmon Hill, LLC; and The Persimmon Hill Homeowners Association, Inc., Respondents,

v.

Pennsylvania National Mutual Casualty Insurance Company, Appellant.

Appellate Case No. 2020-000735

INITIAL BRIEF OF APPELLANT

John I. Malone, Jr.
David L. Brown
GOLDBERG SEGALLA LLP
701 Green Valley Road, Suite 310
Greensboro, North Carolina 27408
(336) 419-4900
Attorneys for Appellant

TABLE OF CONTENTS

STATEMENT OF ISSUES ON APPEAL 1

As to Appellee Persimmon Hill Homeowners Association, Inc *1*

As to Appellees Portrait Homes *1*

Issues Common to All Appellees *1*

STATEMENT OF THE CASE 1

STANDARD OF REVIEW 4

STATEMENT OF FACTS 4

1. Penn National Insurance Policies 4
2. JJA's Work at The Persimmon Hill Project 8
3. The Persimmon Hill Litigation 12
4. Portrait Homes' Additional Insured Tender 13
5. Castillo's Response to the Persimmon Hill Litigation 15

ARGUMENT 19

As to Appellee Persimmon Hill Homeowners Association, Inc. *19*

1. The Trial Court Improperly Awarded Coverage to Jose Castillo and JJA Construction, Inc. After Castillo Advised Penn National That He Did Not Want a Defense and Refused to Cooperate with Penn National 19

2. The Trial Court Improperly Failed to Conclude that Castillo Violated the Policies' Notice and Cooperation Conditions as a Matter of Law 23

   a. Castillo Violated the Policies' Notice Condition as a Matter of Law 24

   b. Castillo Violated the Policies' Cooperation Condition as a Matter of Law 28

3. Penn National Suffered Substantial Prejudice As a Result of Castillo's Breaches of Conditions Because Those Violations Led to Entry of Default and Default Judgment 29

4. The HOA's Claim for Indemnification as a Judgment Creditor of the Insureds Fails Because the Insureds are Not Entitled to Coverage 32

5. The Trial Court's Findings Were Insufficient to Satisfy the Legal Standards for a Bad Faith Claim 33

a. Penn National's "Failure to Conduct an Investigation" Was Not Unreasonable Conduct as a Matter of Law 34

b. Mailing Reservation of Rights Letters to an Incorrect Address Cannot Sustain a Bad Faith Claim Because that Act did not "Result In" a Denial of Benefits 36

c. Asking Castillo Whether He Wanted a Defense Was a Reasonable Behavior as a Matter of Law 37

d. No Competent Evidence Supports the Trial Court's Finding that Penn National "Violated its Own Policies and Procedures" 38

e. Penn National's References to Denying the Claim in its Claim Notes Did Not "Result In" Denial of the Claim 40

f. The Trial Court's Finding that Penn National Requested an Extension of Castillo's and JJA Construction's Answer Deadline Without Intention to Respond Is Unsupported By the Evidence and Cannot Support the Bad Faith Claim 40

6. The Trial Court's Findings of Fact Do Not Support a Punitive Damages Award 42

As to Appellee Portrait Homes 43

1. The Trial Court Improperly Considered Parol Evidence To Award Coverage to Portrait Homes Where Portrait Homes Did Not Qualify as an "Additional Insured" Under the Plain Language of the Penn National Policies 44

2. The Trial Court Improperly Considered Parol Evidence to Interpret the Unambiguous 2005-06, 2006-07, and 2007-08 Penn National Policies 46

a. The Unambiguous Terms of Endorsement 71 1145 Show that Portrait Homes Was Not Entitled to Additional Insured Coverage 46

b. The Trial Court's Consideration of Parol Evidence Was Improper Because the Policies Are Unambiguous 49

c. The Underwriting File Documents Do Not Establish that Castillo Intended to Continue as a Named Insured After He Formed JJA Construction, Inc. 51

d. Portrait Homes Had No Contract with JJA Construction, Inc. Even if it Did Business Under the Name JJA Framing 53

e. The Trial Court Improperly Relied on Certificates of Insurance to Find that Portrait Homes Qualified as an Additional Insured 54

f. The Master Agreement Did Not Govern JJA's Work at Persimmon Hill 56

3. The Trial Court Incorrectly Concluded that Penn National Waived its Right to Contest Portrait Homes' Additional Insured Status 59

4. Portrait Homes Sustained No Damages for Breach of the Duty to Indemnify Because It Was Fully Indemnified By Its Own Insurer 62

5. The Trial Court Erroneously Found that Portrait Homes Proved its Bad Faith Claim 66

a. Penn National's Investigation Was Not Performed In Bad Faith 67

b. Penn National Did Not Fail to Respond to Claim Communications 68

c. Penn National's Incomplete Statement of the Grounds for Denial Does Not Support the Bad Faith Claim 69

6. No Competent Evidence Supports the Trial Court's Finding of Willful Conduct or Reckless Disregard in Support of the Punitive Damages Award 70

Issues Common to Portrait Homes and the HOA *72*

1. The Trial Court Failed To Apply the Supreme Court's Time-On-Risk Formula for Apportioning Damages to Penn National's Policy Periods 72

2. The Trial Court Improperly Awarded Portrait Homes and the HOA Attorneys' Fees 75

a. Castillo and JJA Construction Incurred No Attorneys' Fees 76

b. Penn National Owed the HOA No Duty to Defend 77

c. Portrait Homes Was Defended in the Underlying Case and Does Not Satisfy the Requirements of Hegler 78

CONCLUSION 78

<u>TABLE OF AUTHORITIES</u>

PAGE(S)

CASES

Air Master & Cooling, Inc. v. Selective Ins. Co. of America,
452 N.J. Super. 35, 171 A.3d 214 (App. Div. 2017) 74

Austin v. Specialty Transp. Servs.,
358 S.C. 298, 594 S.E.2d 867 (Ct. App. 2004)..42

Auto-Owners Ins. Co. v. Rhodes,
405 S.C. 584, 748 S.E.2d 781 (2013) 52

Builders Mut. Ins. Co. v. Lacey Const. Co., Inc.,
No. 3:11-cv-400-CMC, 2012 WL 1032539 (D.S.C. March 27, 2012)..................................74

Campbell, Inc. v. Northern Ins. Co. of New York,
337 F.Supp.2d 764 (D.S.C. 2004)..55

Carolina Amusement Co., Inc. v. Connecticut Nat. Life Ins. Co.,
313 S.C. 215, 437 S.E.2d 122 (Ct. App. 1993)...54

Century Indem. Co. v. Golden Hills Builders, Inc.,
348 S.C. 559, 561 S.E.2d 355 (2002) 74, 75

Chapman v. Metropolitan Life Ins. Co.,
172 S.C. 250, 173 S.E. 801 (1934) 58

Cincinnati Cos. v. West Am. Ins. Co.,
183 Ill.2d 317, 701 N.E.2d 499 (1998)..27, 38, 43

Cock-N-Bull Steak House, Inc. v. Generali Ins. Co.,
321 S.C. 1, 466 S.E.2d 727 (1996) 33

Crossmann Cmtys. of N.C. v. Harleysville Mut. Ins. Co.,
395 S.C. 40, 717 S.E.2d 589 (2011) 72, 73

Crossmann Communities of North Carolina, Inc. v. Harleysville Mut. Ins. Co.,
No. 4:09-cv-1379-RBH, 2013 WL 5437712 (D.S.C. Sept 27, 2013)..........................65, 66, 74

Dan Ryan Builders W. Va., LLC v. Main St. Am. Assur. Co.,
No. 2:18-cv-00589-DCN, 2020 U.S. Dist. LEXIS 59188 (D.S.C. Apr. 3, 2020)....................55

Doub v. Weathersby-Breeland Ins. Agency,
268 S.C. 319, 233 S.E.2d 111 (1977) 61, 70

Erie Ins. Exchange v. Gosnell,
246 Md. 724, 230 A.2d 467 (1967) 55

First Bank of Turley v. Fidelity & Deposit Ins. Co. of Maryland,
928 P.2d 298 (Okla. 1996)...27

Flynn v. Nationwide Mut. Ins. Co.,
281 S.C. 391, 315 S.E.2d 817 (1984) 35

Founders Ins. Co. v. Richard Ruth's Bar & Grill LLC,
761 Fed. App'x 178 (4th Cir. 2019) 25

G.E. Tignall & Co., Inc. v. Reliance Nat. Ins. Co.,
102 F.Supp.2d 300 (D.Md. 2000)...55

Goldston v. State Farm Mut. Ins. Co.,
358 S.C. 157, 594 S.E.2d 511 (Ct.App. 2004)...49

Harleysville Group Ins. v. Heritage Communities, Inc.,
420 S.C. 321, 803 S.E.2d 288 (2017) . HOA Order, pp. 32-33.............................30, 60, 61, 74

Hartford Acc. & Indem. Co. v. Gulf Ins. Co.,
776 F.2d 1380 (7th Cir. 1985) 66

Hartford Acc. & Indem. Co. v. South Carolina Ins. Co.,
252 S.C. 428, 166 S.E.2d 762 (1969) 65, 77

Hatchett v. Nationwide Mut. Ins. Co.,
244 S.C. 425, 137 S.E.2d 608 (1964) 30

Hegler v. Gulf Ins. Co.,
270 S.C. 548, 243 S.E.2d 443 (1978) 75, 76, 77, 78

Howard v. State Farm Mut. Auto. Ins. Co.,
316 S.C. 445, 450 S.E.2d 582 (1994) .... *passim*

Hoyler v. State,
428 S.C. 279, 833 S.E.2d 845 (Ct. App. 2019)...4

Jackson v. Speed,
326 S.C. 289, 486 S.E.2d 750 (1997) 75

Janasik v. Fairway Oaks Villas Horizontal Property Regime,
307 S.C. 339, 415 S.E.2d 384 (1992) 42, 69, 70

Joe Harden Builders v. Aetma Cas. & Sur. Co.,
326 S.C. 231, 486 S.E.2d 89 (1997) 75

Johnson v. Amethyst Corp.,
463 S.E.2d 397 (N.C. App. 1995)....................31

Kuznik v. Bees Ferry Assocs.,
342 S.C. 579, 538 S.E.2d 15 (Ct.App. 2000)....................42, 70

Laidlaw Environmental Servs. (TOC), Inc. v. Aetna Cas. & Sur. Co.,
338 S.C. 43, 524 S.E.2d 847 (Ct. App. 1999)....................62

Liberty Mut. Fire Ins. Co. v. J.T. Walker Indus., Inc.,
554 Fed. App'x 176 (4th Cir. 2014) 76, 77

Little v. Town of Conway,
171 S.C. 27, 171 S.E. 447 (1933) 58

M.B.L., Inc. v. Federal Ins. Co.,
No. CV 13-03951 BRO, 2014 WL 12584437 (C.D. Cal. May 30, 2014) 20, 27

Madren v. Bradford,
378 S.C. 187, 661 S.E.2d 390 (Ct. App. 2008)....................4

Magnum v. Maryland Cas. Co.,
330 S.C. 573, 500 S.E.2d 125 (Ct. App. 1985)....................53

McManus v. City of Greenwood,
171 S.C. 84, 171 S.E.2d 473 (1933) 39

Merit Ins. Co. v. Koza,
274 S.C. 362, 364 S.E.2d 146 (1980) 25, 26, 27, 30

MGC Mgmt. of Charleston, Inc. v. Kinghorn Ins. Agency,
336 S.C. 542 520 S.E.2d 820 (Ct.App. 1999)....................49

Mulvey Const. Inc. v. Bituminous Cas. Corp.,
571 Fed. Appx 150 (4th Cir. 2014)....................55

National Union Fire Ins. Co. of Pittsburgh, PA v. Crocker,
246 S.W.3d 603 (Tex. 2008)..20, 26

Matter of Nationwide Ins. Co. (De Rose),
241 A.D.2d 607, 659 N.Y.S.2d 342 (3d Dep't 1997)...26

Nichols v. State Farm Mut. Auto. Ins. Co.,
279 S.C. 336, 306 S.E.2d 616 (1983) 36, 40, 41, 69

North American Rescue Products, Inc. v. Richardson,
411 S.C. 371, 769 S.E.2d 237 (2015) 50

Otis Elevator, Inc. v. Hardin Construction Co.,
316 S.C. 292, 450 S.E.2d 41 (1994). 62, 63, 64

Pennsylvania National Mut. Cas. Ins. Co. v. Portrait Homes-South Carolina, LLC, Civ. No. 3:18-CV-00561-KDB-DCK, 2019 WL 4491535, 2019 U.S. Dist. LEXIS 160414 (W.D.N.C. Sept. 18, 2019)...64

Pompa v. American Family Mut. Ins. Co.,
520 F.3d 1139 (10th Cir. 2008) 54

Prior v. S.C. Med. Malpractice Liab. Ins. Joint Underwriting Ass'n,
305 S.C. 247, 407 S.E.2d 655 (Ct. App. 1991)...24

S.C. Dep't of Natural Resources v. Town of McClellanville.,
345 S.C. 617, 550 S.E.2d 299 (2001) 23

S.C. Dep't of Transp. v. M&T Enterprises of Mt. Pleasant, LLC,
379 S.C. 645, 667 S.E.2d 7 (Ct. App. 2008)..45

S.C. Farm Bureau Cas. Ins. Co. v. Ausborn,
249 S.C. 627, 155 S.E.2d 902 (1967) 32

Sloan Const. Co., Inc. v. Central Nat. Ins. Co. of Omaha,
269 S.C. 183, 236 S.E.2d 818 (1977) 65, 66, 78

Snohomish Cnty. v. Allied World National Assur. Co.,
276 F.Supp.3d 1046,1053 (W.D. Wash. 2017)..27

South Carolina Dept. of Transp. v. Thompson,
357 S.C. 101, 590 S.E.2d 511 (Ct. App. 2003)..39

South Carolina Farm Bureau Mut. Ins. Co. v. Dawsey,
371 S.C. 353, 638 S.E.2d 103 (2006) 24

State National Ins. Co. v. Eastwood Construction LLC,
No. 6:16-cv-02607-AMQ, 2018 WL 8787543 (D.S.C. Sept. 5, 2018)....................20, 21, 31

State v. Garrard,
390 S.C. 146, 700 S.E.2d 269 (Ct.App. 2010)....................42

Summer Wood Property Owners Association, Inc. v. Pennsylvania National Mut. Cas. Ins. Co., No. 2:17-cv-350-BHH, 2019 WL 4415805, 2019 U.S. Dist. LEXIS 157353 (D.S.C. Sept. 16, 2019)....................64, 65, 66

Taylor v. Taylor,
291 S.C. 261, 353 S.E.2d 156 (Ct.App. 1987)....................50, 55

Towne Realty, Inc. v. Zurich Ins. Co.,
201 Wis.2d 260, 548 N.W.2d 64 (1996)....................27, 38, 43

Tucker v. State Farm Mut. Auto. Ins. Co.,
232 S.C. 615, 103 S.E.2d 272 (1958) 20, 21, 24, 29

Twin City Fire Ins. Co. v. Ben-Arnold-Sunbelt Beverage Co. of S.C.,
433 F.3d 365 (4th Cir. 2005) 20, 21, 23, 31

Universal Underwriters Ins. Co. v. Metropolitan Property and Life Ins. Co.,
298 S.C. 404, 380 S.E.2d 858 (Ct.App. 1989)....................49

Valentine v. Membrila Ins. Servs., Inc.,
118 Cal.App.4th 462 (2004) 27

Vermont Mut. Ins. Co. v. Singleton,
316 S.C. 5, 446 S.E.2d 417 (1994) 29

Williams v. Government Employees Ins. Co.,
409 S.C. 586, 762 S.E.2d 705 (2014) 49

Williams v. Moore,
400 S.C. 90, 733 S.E.2d 224 (Ct. App. 2012)....................4

Worthington Federal Bank v. Everest Nat. Ins. Co.,
110 F.Supp.3d 1211 (N.D. Ala. 2015)....................53

Yaun v. Baldridge,
243 S.C. 414, 134 S.E.2d 248 (1964) 42, 70

Statute

S.C. Code § 38-59-40...3

Treatises

3 Appleman on Insurance Law, §16.05(1)(c)(i) 44

3 Appleman on Insurance Law, §36.02(1)(a) 47

Other Authorities

S.C. R. Civ. P., Rule 12(a) 41

S.C. R. Civ. P., Rule 59 .... *passim*

S.C. R. Ethics, Rule 1.8(f) 31

S.C. R. Evid., Rule 1002 39

STATEMENT OF ISSUES ON APPEAL

As to Appellee Persimmon Hill Homeowners Association, Inc

1. Did the Trial Court Improperly Award Coverage to Jose Castillo and JJA Construction, Inc. After Castillo Advised Penn National That He Did Not Want a Defense and Refused to Cooperate with Penn National?

2. Did the Trial Court Improperly Fail to Find that Castillo's Conduct was a Violation of the Policy Conditions Precedent to Coverage?

3. Did the Trial Court Improperly Fail to Find that Breaches of the Policy Conditions Precedent to Coverage Resulted in Substantial Prejudice to Penn National?

4. Did the Trial Court Improperly Find as a Matter of Law that the HOA Satisfied the Elements of an Insurance Bad Faith Claim?

5. Did the Trial Court Improperly Find as a Matter of Law that Penn National Engaged in Willful, Reckless, or Wanton Behavior and award Punitive Damages?

As to Appellees Portrait Homes

1. Did the Trial Court Improperly Consider Parol Evidence To Award Coverage to Portrait Homes Where Portrait Homes Did Not Qualify as an "Additional Insured" Under the Plain Language of the Penn National Policies?

2. Did the Trial Court Improperly Find that Penn National Waived its Right to Contest Coverage such that the Waiver Operated to Expand Coverage to Uncovered Risks?

3. Did the Trial Court Improperly Find that Portrait Homes Sustained Damages for Breach of the Duty to Indemnify Where its Other Carriers Paid the Loss?

4. Did the Trial Court Improperly Find as a Matter of Law that Portrait Homes Satisfied the Elements of an Insurance Bad Faith Claim?

5. Did the Trial Court Improperly Find as a Matter of Law that Penn National Engaged in Willful, Reckless, or Wanton Behavior and award Punitive Damages?

Issues Common to All Appellees

1. Did the Trial Court Improperly Fail to Apply the Time-on-Risk Doctrine?

2. Did the Trial Court Improperly Award Attorneys' Fees?

STATEMENT OF THE CASE

This insurance coverage matter was commenced in the Court of Common Pleas for the

Ninth Judicial Circuit, Berkeley County, on December 29, 2014 when Appellees Portrait Homes – South Carolina, LLC and Portrait Homes – Persimmon Hill, LLC (together, "Portrait Homes") filed suit against various insurance carrier defendants, including Appellant Pennsylvania National Mutual Casualty Insurance Company ("Penn National"), and the Persimmon Hill Homeowners Association, Inc. (the "HOA")[1]. *See generally*, Summons and Complaint. Portrait Homes asserted a single cause of action for Declaratory Relief, seeking a declaration that it qualified as an additional insured under the insurer-defendants' policies, that it was owed a defense in underlying litigation, and that the insurer-defendants owed it for defense costs incurred to that point in time. Complaint, pp. 12-13. Portrait Homes' action arose out of two underlying construction defect actions asserted against it related to a townhome project for which it served as the developer and general contractor: (1) *The Persimmon Hill Homeowners Association, Inc. v. Portrait Homes-South Carolina, LLC,* et seq.", Case No. 2012-CP-08-03065 (the "Persimmon Hill HOA Lawsuit"); and (2) "*Cheryl L. Waker, on behalf of herself and others similarly situated v. Portrait Homes-South Carolina, LLC,* et seq.", Case No. 2012-CP-08-03066 (the "Persimmon Hill Class Action Lawsuit" and, together with the Persimmon Hill HOA Lawsuit, the "Persimmon Hill Litigation"), filed in the Court of Common Pleas, Berkeley County, South Carolina. Ultimately, Portrait Homes resolved its dispute with the carriers besides Penn National and amended its complaint to assert a cause of action against Penn National alone for breach of the duty to defend and indemnify with respect to the Persimmon Hill Litigation. *See generally*, Amended Complaint.

---

[1] The HOA is nominally included as a defendant in Portrait Homes' pleadings, but its causes of action never sought any relief against the HOA. *See* Complaint, pp. 12-13; Amended Complaint, p. 5. The HOA admitted all allegations of each version of Portrait Homes' Complaint. *See* HOA Answer to Complaint and Crossclaims, p. 2; HOA Answer to Plaintiffs' Amended Complaint, Crossclaims and Third Party Complaint, p. 2.

The HOA asserted cross-claims against Penn National for bad faith and violation of S.C. Code § 38-59-40 (contractual bad faith) and third party claims against defendants Jose Castillo d/b/a JJA Framing and "JJA Construction, Inc. d/b/a JJA Framing." *See generally*, Answer and Cross-Claims. The HOA sought (1) to collect on a default judgment entered in its favor and against Castillo and "JJA Construction, Inc. d/b/a JJA Framing"; and (2) to collect damages for bad faith conduct related to Penn National's handling of the insurance claim, which claim had been assigned it by Jose Castillo d/b/a JJA Framing and "JJA Construction, Inc. d/b/a JJA Framing." *Id*.

Penn National denied the allegations asserted against it and defended the action on the grounds that it owed no duty to defend Portrait Homes, Jose Castillo d/b/a JJA Framing, or "JJA Construction, Inc. d/b/a JJA Framing" in the Persimmon Hill Litigation and that it had not acted in bad faith. *See generally*, Pennsylvania National's Answer to Amended Complaint; Pennsylvania National's Answer to Crossclaims & Third Party Complaint.

The case proceeded to a bench trial before the Honorable Roger M. Young, Sr., heard February 4-7, 2019 and May 7-9, 2019. The court entered judgments in favor of Portrait Homes and the HOA on October 22, 2019. Order as to Persimmon Hill Homeowners Association, Inc.'s Claims of Bad Faith, Breach of Contract and Declaratory Judgment Against Pennsylvania National Mutual Casualty Insurance Company (the "HOA Order"); Order Regarding Additional Insured Coverage (the "Portrait Homes Order"). Penn National timely moved to alter or amend the judgments pursuant to Rule 59 of the South Carolina Rules of Civil Procedure, on November 1, 2019. The court denied Penn National's motions to alter the judgments and granted in part its motion to amend the judgments, requesting that the HOA and Portrait Homes make clarifications to the orders they had drafted. The court entered its final judgments in favor of Portrait Homes and the HOA on March 23, 2020 in the following amounts:

As to Portrait Homes:

• Breach of Contract – Duty to Defend	$42,791.24
• Breach of Contract – Duty to Indemnify	$2,500,000.00
• Prejudgment Interest	$807,693.50
• Attorneys Fees & Costs	$250,003.26
• Bad Faith Refusal to Pay	$3,892,791.24
• Punitive Damages	$3,892,791.24
• = Total Judgment for Portrait Homes	$11,386,070.48

As to the HOA:

• Bad Faith Refusal to Pay	$5,370,147.29
• HOA's Judgment Creditor Claim	$5,213,170.40
• Punitive Damages	$5,370,147.29
• = Total Judgment for the HOA	$15,953,464.98

Post-Trial Motions and Punitive Damages Order (the "Rule 59 Order"), at p. 69. Penn National timely served and filed its Notice of Appeal of the judgments on April 22, 2020.

STANDARD OF REVIEW

Penn National appeals from the trial court's ruling following a bench trial. "On appeal of a case tried without a jury, the appellate court's jurisdiction is limited to correction of errors at law." *Williams v. Moore*, 400 S.C. 90, 102, 733 S.E.2d 224, 230 (Ct. App. 2012). An appellate court "reviews all questions of law *de novo*." *Hoyler v. State*, 428 S.C. 279, 290, 833 S.E.2d 845, 851 (Ct. App. 2019). "The appellate court will not disturb the trial court's findings of fact as long as they are reasonably supported by the evidence." *Madren v. Bradford*, 378 S.C. 187, 192, 661 S.E.2d 390, 393 (Ct. App. 2008).

STATEMENT OF FACTS

1. Penn National Insurance Policies

Penn National issued a series of insurance policies to Jose Castillo DBA JJA Framing Company and, later, to an entity named JJA Construction, Inc. from 2002 through 2010 (Penn National refers to Jose Castillo the individual as "Castillo," his sole proprietorship as "JJA

Framing", the corporate entity as "JJA Construction," and these business entities collectively as "JJA"). Each of the relevant policies contains a $500,000 maximum per-occurrence limit of coverage. [Plaintiffs' Exhibit Nos. 14, at p. 2; 17, at p. 2; 21, at p. 2; 27, at p. 2; 29, at p. 2]. Each of the Penn National Policies contains the following "Conditions In The Event Of Occurrence, Offense, Claim Or Suit":

SECTION IV – COMMERCIAL GENERAL LIABILITY CONDITIONS

2. Duties In The Event Of Occurrence, Offense, Claim Or Suit

a. You must see to it that we are notified as soon as practicable of an "occurrence" or an offense which may result in a claim. To the extent possible, notice should include:

(1) How, when and where the "occurrence" or offense took place;

(2) The names and addresses of any injured persons and witnesses; and

(3) The nature and location of any injury or damage arising out the "occurrence" or offense.

b. If a claim is made or "suit" is brought against any insured, you must:

(1) Immediately record the specifics of the claim or "suit" and the date received; and

(2) Notify us as soon as practicable.

You must see to it that we receive written notice of the claim or "suit" as soon as practicable.

c. You and any other involved insured must:

(1) Immediately send us copies of any demands, notices, summonses or legal papers received in connection with the claim or "suit";

(2) Authorize us to obtain records and other information;

(3) Cooperate with us in the investigation or settlement of the claim or defense against the "suit"; and

(4) Assist us, upon our request, in the enforcement of any right against any person or organization which may be liable to the insured because of injury or damage to which this insurance may also apply.

d. No insured will, except at the insured's own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent.

[Plaintiffs' Exhibit Nos. 14, at pp. 48-49; 17, at pp. 30-31; 21, at pp. 49-50; 27, at pp. 40-41; 29,

at pp. 42-43]. Each of the Penn National Policies also contains an endorsement modifying, but not replacing, the "Conditions" language quoted above, titled "Extended Coverage Endorsement General Liability". The endorsement contains language modifying the insured's duties:

VII. Duties in the Event of Occurrence, Claim or Suit Redefined

> **b.** The requirement in Condition 2.b of CONDITIONS (Section IV) that you must see to it that we receive notice of a claim or "suit" will not be considered breached unless the breach occurs after such claim or "suit" is know [sic] to:
> **(1)** You, if you are an individual;
> **(2)** A partner, if you are a partnership; or
> **(3)** An officer of the corporation or insurance manager, if you are a corporation.

[Plaintiffs' Exhibit Nos. 14, at p. 60; 17, at p. 40; 21, at p. 23; 27, at p. 16; 29, at p. 19].

In each policy the word "you" is defined as "the Named Insured shown in the Declarations, and any other person or organization qualifying as a Named Insured under this policy." [Plaintiffs' Exhibit Nos. 14, at p. 39; 17, at p. 21; 21, at p. 40; 27, at p. 31; 29, at p. 33]. Certain policies – those effective from December 5, 2003 through January 31, 2008 -- contained additional insured endorsements relevant to this insurance coverage dispute. The first two policies were issued under policy number GL9 0601617 to named insured Jose Castillo DBA JJA Framing Company effective from December 5, 2003 to December 5, 2004 (the "2003-04 Policy") [Plaintiffs' Exhibit No. 14] and December 5, 2004 to December 5, 2005 (the "2004-05 Policy") [Plaintiffs' Exhibit No. 17]. Neither of these two policies extends additional insured status automatically; both instead require an endorsement extending such coverage to entities besides the named insured. Both policies contain endorsement CG 20 37 1001, which amends these policies' "Who Is An Insured" provision to include as an insured "the person or organization shown in the [endorsement's] Schedule [of specifically-named entities], but only with respect to liability arising out of '[the named insured's]

work' at the location designated and described in the schedule of this endorsement performed for [the additional insured] and included in the 'products-completed operations hazard.'" [Plaintiffs' Exhibit Nos. 14, at pp. 18-20; 17, at p. 4]. The endorsements attached to these two policies identify three specific Portrait Homes entities as insureds: Portrait Homes entities: Pasquinelli Construction Company, Pasquinelli Management LLC, and Portrait Homes Construction Company. [Plaintiffs' Exhibit Nos. 14, at pp. 18-20; 17, at p. 4].

On March 2, 2005, during the effective period of the 2004-05 Policy, Castillo submitted a Policy Change Request to change the named insured to a newly incorporated entity identified as JJA Construction, Inc. [Plaintiffs' Exhibit No. 18, p. 1]. Castillo executed articles of incorporation to form JJA Construction on December 15, 2004, [Defendant's Exhibit No. 62; Trial Transcript, Vol. 2, at 380:4-16], and filed them with the North Carolina Department of the Secretary of State on December 17, 2004, [Defendant's Exhibit No. 62]. As requested in the change form it received, Penn National changed the named insured on the 2004-05 Policy from Castillo to JJA Construction effective March 2, 2005 through the end of the effective period of the 2004-05 Policy. [Plaintiffs' Exhibit No. 17, at p. 9; Plaintiffs' Exhibit No. 19].

Three further policies conferred additional insured status in a different manner. These policies, issued under policy number GL9 0601617 to JJA Construction, were effective from December 5, 2005 to December 5, 2006 (the "2005-06 Policy") [Plaintiffs' Exhibit No. 21], from December 5, 2006 to December 5, 2007 (the "2006-07 Policy") [Plaintiffs' Exhibit No. 27], and from December 5, 2007 to January 31, 2008[2] (the "2007-08 Policy") [Plaintiffs' Exhibit No. 29]. These policies all contain an "Automatic Additional Insureds – Owners, Contractors and

[2] Penn National cancelled the 2007-08 Policy on January 31, 2008 due to JJA Construction, Inc.'s failure to pay premiums owed, terminating coverage as of that date. [Plaintiffs' Exhibit No. 31].

Subcontractors (Completed Operations)" endorsement, form 71 11 45 0105, that extends additional insured status to a person or entity for completed operations risks automatically where required by a written contract between the named insured (JJA Construction) and that other person or entity. [Plaintiffs' Exhibit Nos. 21, at p. 29; 27, at p. 20; 29, at p. 23].[3] The scope of coverage offered by this endorsement extends only to liability for "bodily injury" and "property damage" caused in whole or in part by the named insured's work for the additional insured at the location or project designated in the contract. [*Id*]. The relevant language in the "Automatic Additional Insureds – Owners, Contractors and Subcontractors (Completed Operations)" endorsement reads:

> **A.** The following provision is added to **SECTION II – WHO IS AN INSURED**:
>
> > **6.** Any person(s) or organization(s) (referred to below as additional insured) with whom you are required in a written contract or agreement to name as an additional insured for the "products-completed operations hazard", but only with respect to "bodily injury" or "property damage" caused, in whole or in part, by "your work", at the location or project designated and described in the contract or agreement, performed for that additional insured and included in the "products-completed operations hazard".
> >
> > A person's or organization's status as an additional insured under this endorsement ends when the obligation to provide additional insured status for the "products-completed operations hazard" in the written contract or agreement ends.

[*Id.*]. Penn National issued JJA Construction two additional policies later in time, but these policies did not contain additional insured coverage for completed operations.

2. JJA's Work at The Persimmon Hill Project

Portrait Homes was responsible for construction and development of a townhome project

[3] While the additional insured endorsement contained in the 2007-08 Policy was an updated form, the insuring language it contained is functionally identical to the language contained in prior versions of the endorsement contained in the 2005-06 Policy and 2006-07 Policy. [*Compare* Plaintiffs' Exhibit Nos. 23 & 28 *with* Plaintiffs' Exhibit No. 30].

of three hundred eighty-eight townhome units spread across seventy-four buildings in Berkeley County, South Carolina known as Persimmon Hill (the "Persimmon Hill Project"). [Trial Transcript, Vol. 1, 455:19-23, 503:5-25]. Construction permits were issued beginning in 2002 while occupancy permits were issued on a rolling basis as buildings were completed from 2003 through the project's completion in 2006. [*Id*. at 456:5-24; Defendant's Exhibit No. 16 (Certificates of Occupancy for the Persimmon Hill Project issued by the City of Goose Creek)].

Portrait Homes hired Jose Castillo, a sole proprietor doing business as JJA Framing, to perform framing work on certain buildings at the Persimmon Hill Project. [Trial Transcript, Vol. 1, 458:1-8]. JJA Framing was one of several framers involved in the project and performed work on a number of the units built as part of the Persimmon Hill Project. [*Id*]. The trial court found, based upon an estimation made by Portrait Homes' lawyer in the Persimmon Hill Litigation, that JJA Framing performed roughly 85% of the framing on the project. HOA Order, at p. 3 (citing Trial Transcript, Vol. 1, at p. 97). However, neither Portrait Homes nor Castillo produced records to show on which buildings JJA Framing performed framing work and which buildings were framed by another entity. [Trial Transcript, Vol. 1, at 145:25-143:3].

JJA Framing's work at the Persimmon Hill Project was governed by a "Housing and Purchase Order Contract" executed by Portrait Homes. [Plaintiffs' Exhibit No. 38]. The Housing and Purchase Order Contract is dated March 6, 2002, signed on behalf of Portrait Homes Construction Co. on the same date, and signed by Castillo on March 8, 2002. [Plaintiffs' Exhibit No. 38 at pp. 1, 6; Trial Transcript, Vol. 1, at 464:16-22]. The Housing and Purchase Order Contract is a project-specific document detailing JJA Framing's duties with respect to specific projects, which were designated on the first page of the contract. [Plaintiffs' Exhibit No. 38 at p. 1]. The projects identified on the first page of the contract are "Summerwood" and "Persimmon

Hill." [*Id*]. JJA Framing's scope of work on these projects was defined in a separate document attached to the contract. [Plaintiffs' Exhibit Nos. 39 (March 6, 2002 Scope of Work Addendum) & 41 (August 15, 2003 Scope of Work Addendum)]. The Housing and Purchase Order Contract required JJA Framing, as a pre-condition to commencing work, to procure various insurance coverage, present proof of the placement of such coverage and of payment for the policies, and to present a certificate of insurance "naming [Portrait Homes-South Carolina, LLC], the owner of the project, and any additional parties, as additional insured." [*Id.* at pp. 3-4]. The Housing and Purchase Order Contract did not specifically require that JJA Framing procure any completed operations coverage or that any policy issued to JJA Framing to name any Portrait entity as an additional insured for completed operations coverage. [*Id*].

JJA Framing also executed a Master Agreement with Portrait Homes-South Carolina, LLC dated October 25, 2002, approximately seven months after the Housing and Purchase Order contract was executed. The Master Agreement took effect from the date of its signing, and it was signed by Castillo on November 5, 2002. [Plaintiffs' Exhibit No. 37, at pp. 1, 4]. The Master Agreement identifies Castillo as a sole proprietor in its introductory language. [*Id*]. The contract provides a general set of terms that "shall be incorporated into any *future* purchase order contract by and between [Portrait Homes-South Carolina, LLC and Jose Castillo d/b/a JJA Framing] as if this Agreement had been set forth in said purchase order contract, in its entirety." [Plaintiffs' Exhibit No. 37, at p. 1 (Paragraph 1)] (emphasis added). The Master Agreement has no effect on previously-executed purchase order contracts. [*Id*]. Rather, the Master Agreement governed other projects (besides Persimmon Hill) on which Castillo was doing work for Portrait Homes.

With regard to those other projects, the Master Agreement required that Castillo defend and indemnify "Portrait [Homes – South Carolina], affiliated companies of Portrait, their partners,

joint ventures, representatives, members" and other representatives. [Plaintiffs' Exhibit No. 37, at pp. 1-2]. That contract also required that Castillo, "prior to [his] commencing (in the broadest possible sense of the word) any work or services or supplies," carry general liability insurance with a minimum $1 million per occurrence limit that provided coverage for completed operations losses. [*Id*. at p. 2].

The trial court identified no evidence that Portrait Homes executed a new Housing and Purchase Order Contract with Castillo for the Persimmon Hill Project after the Master Agreement was executed. Portrait Homes did require Castillo to execute a new Housing and Purchase Order Contract for the separate Summerwood Project, however. [Plaintiffs' Exhibit No. 46]. Portrait Homes also never entered in to a new Master Agreement or Housing and Purchase Order contract with JJA Construction, Inc. following its incorporation. [Trial Transcript, Vol. 1, at 488:18-23]. The trial court found, without citation to any evidence from the record, that "before the Housing and Purchase Order Contract for Persimmon Hill was entered into, there would have been an earlier Master Agreement in place between Portrait Homes and JJA Framing containing the same requirement of additional insured coverage for completed operations." Rule 59 Order, at pp. 7-8. No such Master Agreement was ever received in evidence.

Castillo provided Portrait Homes with two certificates of insurance involving two different Penn National Policies. First, Castillo provided to Portrait Homes, and Portrait Homes accepted, a certificate of insurance for the 2004-05 Policy. [Plaintiffs' Exhibit No. 7]. The certificate denotes the following entities as the "Certificate Holder[s]": Pasquinelli Construction Co.; Pasquinelli Management, LLC; and Portrait Homes Construction Co. [*Id*]. Attached to the certificate is a copy of a CG 20 37 1001 endorsement indicating that those three entities are included as additional insureds, subject to the endorsement's other limitations and restrictions. [*Id*. at p. 2]. The certificate

states that it "is issued as a matter of information only and confers no rights upon the certificate holder" and that it "does not amend, extend or alter the coverage afforded by [the policies to which it applies]." [*Id*. at p. 1].

Second, Castillo provided to Portrait Homes, and Portrait Homes accepted, a second certificate of insurance, this time concerning the 2005-06 Policy. [Plaintiffs' Exhibit No. 5]. The certificate denotes the following entities as the "Certificate Holder[s]": Pasquinelli Management, LLC; and Portrait Homes-South Carolina, LLC. [*Id*. at p. 1]. The certificate also attaches a copy of the "Automatic Additional Insureds – Owners, Contractors and Subcontractors (Completed Operations)" endorsement, form 71 1145, identical to the copy contained in the 2005-06 Policy. [*Id*. at p. 2-3].

3. <u>The Persimmon Hill Litigation</u>

The Persimmon Hill Litigation began on October 23, 2012 when the HOA and a class of the individual homeowners, respectively, each filed suit against Portrait Homes-South Carolina, LLC, Portrait Homes-Persimmon Hill, LLC, and Pasquinelli Homebuilding, LLC[4] claiming that defective construction on the Persimmon Hill Project had caused water intrusion into the homes and subsequent rot and deterioration. [Plaintiffs' Exhibit Nos. 1 & 2]. Portrait Homes' insurance carrier, Admiral Insurance Company, agreed to defend it in the Persimmon Hill Litigation and retained the Hood Law Firm to lead the defense. [*Id*. at 186:13-20].

The Complaints in the Persimmon Hill Litigation were amended on March 20, 2013 to add

---

[4] The Portrait Homes plaintiffs are part of a greater corporate structure involving other companies. First, Portrait Homes – South Carolina, LLC is a state-specific entity within the greater Portrait Pasquinelli corporate hierarchy and a direct subsidiary of Pasquinelli Construction. [Trial Transcript, Vol. 1, at 73:15-74:14]. Second, Portrait Homes – Persimmon Hill, LLC is an entity created specifically to oversee the Persimmon Hill Project and a direct subsidiary of Portrait Homes – South Carolina LLC. [*Id*]

two Castillo entities: "JJA Construction, Inc. d/b/a JJA Framing" and JJA Framing. [Plaintiffs' Exhibit Nos. 3 & 4]. Castillo was served with process on behalf of both his sole proprietorship and JJA Construction on September 8, 2013. HOA Order, at pp. 26, 29; [Penn National Exhibit Nos. 80 & 81]. Castillo did not ask his insurance carrier for a defense, did not retain counsel on his own behalf, and did not respond to the suit. On July 13, 2016, the court entered a default judgment in favor the Persimmon Hill HOA in the amount of $4,156,976.98. HOA Order, at p. 13; [HOA Exhibit No. 12; Trial Transcript, Vol. 1, at 377:16-20].

Portrait Homes ultimately settled the claims against it with the HOA and the Homeowners for $3,850,000 in March 2016. [Trial Transcript, Vol. 1, at 109:24-110:17]. The Portrait Homes settlement amount was paid by its insurance carriers, including Admiral. [*Id*. at 183:23-184:8]. Despite Portrait Homes having been indemnified for the settlement by its insurance carriers, the trial court found that the amount of the settlement was the amount of damages Portrait Homes sustained as a result of Penn National's election not to participate in the defense of the Persimmon Hill Litigation. Rule 59 Order, pp. 13-16. Portrait Homes paid only a total of $42,791.24 -- the $25,000 self-insured retention of the Admiral policy and $17,791.24 paid to a North Carolina firm that operated as its national counsel. Portrait Homes Order, at p. 43.

4. Portrait Homes' Additional Insured Tender

Portrait Homes first requested a defense for the Persimmon Hill Litigation from Penn National by letter dated June 5, 2013 from its defense counsel retained by Admiral Insurance Company. Portrait Homes Order, pp. 9-10; [Plaintiff's Exhibit No. 6; Trial Transcript, Vol. 1, at 87:16-19]. The letter requested a defense under the 2005-06 Policy. [*Id*]. Penn National's adjuster, Greg Gross, called Portrait Homes' defense counsel in an attempt to gather additional information about the claim, but was unable to reach him. [HOA Exhibit No. 4, at p. 2; Trial Transcript, Vol.

1, at 381:3-382:1, 392:17-394:4, 19-22, 399:6-21]. However, there is no evidence that Penn National responded to Portrait Homes' initial tender letter in writing. Portrait Homes Order, at p. 11. Portrait Homes' counsel sent a second tender letter to Penn National dated May 23, 2014 requesting a defense under the 2004-05 Policy. Portrait Homes Order, at p. 10; [Plaintiffs' Exhibit No. 8].

Gross, the Penn National adjuster, prepared a report to in-house counsel on May 29, 2014 that recommended denial of Portrait Homes' claim. Portrait Homes Order, at pp. 23-24; [Penn National Exhibit No. 78, at pp. 31-35]. Gross sent the report to his supervisor, Gary Gibson, on May 30, 2014, who forwarded it to Penn National's in-house claims counsel, Adam Parsons, on June 3, 2014. Portrait Homes Order, at p. 23. Parsons reviewed Gross' recommendation to deny additional insured coverage for Portrait Homes and, by email on June 16, 2014, requested that Gross provide additional analysis concerning the claim for additional insured coverage. Portrait Homes Order, at p. 24; [Penn National Exhibit No. 78, at p. 28; Trial Transcript, Vol. 1, at 416:21-417:13; Vol. 2, at 45:25-46:18]. Gross ultimately provided the requested information to Parsons by emails dated August 11, 2014 and August 26, 2014. Portrait Homes Order, at p. 24; [Penn National Exhibit No. 78, at pp. 22, 18, 16].

Parsons responded on September 11, 2014, noting that after Castillo incorporated JJA Construction and made it the named insured effective March 2, 2005, Portrait Homes no longer had a contract with the named insured requiring the insured to name Portrait Homes as an additional insured. Portrait Homes Order, pp. 12-13; [Penn National Exhibit No. 78, at p. 1-2]. As a result, Parsons reasoned that no defense was available to Portrait Homes under any policy issued after the named insured on the Penn National Policies was changed on March 2, 2005. [*Id*]. Parsons further opined that the entities that were specifically named as additional insureds under the 2003-

04 and 2004-05 Policies' CG 2037 additional insured endorsement were not named as Defendants in the Persimmon Hill Litigation and that no defense was owed to the Portrait Homes entities that had been sued in that action. [Trial Transcript, Vol. 2, at 54:6-56:18]. Parsons recommended that Portrait Homes' claim for coverage be denied. [*Id*].

Penn National then denied Portrait Homes' tender by letter dated September 30, 2014. Portrait Homes Order, at p. 10; [Plaintiffs' Exhibit No. 9]. Penn National cited as grounds for its denial that the policies under which Portrait Homes sought additional insured coverage did not contain completed operations coverage. Portrait Homes Order, at p. 11; [Plaintiffs' Exhibit No. 9]. Penn National admitted that this stated ground for its denial of Portrait Homes' claim was an incomplete explanation of the policies' contents because, while the policies at issue each contain completed operations coverage in one of the two forms discussed above (form CG 20 37 or 71 1145), Penn National concluded that such coverage was not available to the tendering Portrait Homes parties under the circumstances of this case. [Trial Transcript, Vol. 1, at 424:1-425:6; Vol. 2, at 80:8-81:2; 163:9-165:2; 171:9-172:25].

5. <u>Castillo's Response to the Persimmon Hill Litigation</u>

Penn National never received any correspondence or communication of any type from Castillo or JJA Construction, Inc. about the loss or suit. HOA Order, p. 26; [Trial Transcript, Vol. 2, at 374:6-24]. Upon being made aware of the lawsuit via Portrait Homes' tender letter, Penn National retained an independent adjuster, Gayle McLeod with Capstone ISG, to determine whether its insureds had been served with process and to discuss the facts and circumstances of the loss with Castillo. HOA Order, at p. 6; [Trial Transcript, Vol. 1, at 400:8-23].

On September 21, 2013, Penn National sent its first Reservation of Rights letter to Castillo. HOA Order, at p. 5; [HOA Exhibit No. 14 at pp. 2-7 (Bates Stamped 957-962)]. The letter was

addressed to Castillo at the address indicated on the declarations page of the Penn National Policies, in Ladson, South Carolina. [*Id*]. After the issuance of the 2008-09 Policy, Castillo had informed Penn National of an address change to a location in Huntersville, North Carolina. [Plaintiffs' Exhibit No. 34 at p. 52]. However, the letter was sent only to the address on the declarations page of the Policy. The letter was also copied to Castillo's agent, the Taylor Agency in Charleston, South Carolina. [HOA Exhibit No. 14, at p. 7 (962); Trial Transcript, Vol.1, at 402:12-403:21]. The letter was never returned as being undelivered. Nevertheless, the trial court found, without citation to evidence in the record, that Castillo never received this correspondence. HOA Order, at p. 6. Penn National received no correspondence in response to its September 21, 2013 letter from either The Taylor Agency or Castillo. *See* [HOA Exhibit No. 4 at p. 9 (Bates Stamped 1084) (indicating that Penn National had received no response and was retaining an Independent Adjuster to ascertain Castillo's intentions with regard to the Persimmon Hill Litigation)].

Penn National subsequently received notice that its insureds, JJA Framing and JJA Construction, had been served with process in the Persimmon Hill Litigation in a February 19, 2014 report from McLeod. HOA Order, at p. 6; [Defendant's Exhibit No. 82]. Penn National, having received no tender or other communication from Castillo regarding the litigation, requested that McLeod attempt to contact Castillo at his residence in order to inquire about suit representation, inquire whether Castillo wanted Penn National to handle the suit on his behalf, and to obtain direct contact information for Castillo. HOA Order, at p. 7; [Defendant's Exhibit No. 83; Trial Transcript, Vol. 2, at 88:2-11].

McLeod was initially unsuccessful in meeting Castillo in person. [HOA Exhibit Nos. 6, 7; Trial Transcript, Vol. 1, at 406:15-21; Vol. 2, at 88:21-25]. On the occasion of her first attempt to

meet with Castillo, in April 2014, McLeod traveled to his residence, rang his doorbell several times, left contact information and instructions to contact her on the two vehicles parked in Castillo's driveway, and left contact information with a woman residing next door who identified herself to McLeod as Castillo's tenant. [Trial Transcript, Vol. 2, at 89:1-20]. Penn National did not receive any communication from Castillo following McLeod's first visit to Castillo's property. [*Id*. at 26:19-27:9]. Penn National then requested that McLeod attempt to contact Castillo about the suit a second time. [HOA Exhibit No. 4 at p. 10 (1085)].

By report dated May 15, 2014, Penn National learned that McLeod had successfully met with Castillo in person at his property. HOA Order, at pp. 8-9; [HOA Exhibit No. 10; Trial Transcript, Vol. 1, at 407:6-11]. The meeting described in the report is the first instance in which a Penn National representative successfully established contact with Castillo in any form about the suit, despite his having been served with process more than eight months before. [Trial Transcript, Vol. 2, at 26:19-27:9; Penn National Exhibit Nos. 80 & 81 (certificates of service); HOA Exhibit No. 4 at pp. 3-10 (1078-1085)]. First, McLeod confirmed that she was speaking with Castillo. [Trial Transcript, Vol. 2, at 91:18-19]. McLeod then explained that Castillo needed to contact Penn National immediately about the Persimmon Hill Litigation and strongly encouraged him to do so. [*Id*. at 93:14-18, 94:22-95:1]. Given Castillo's failure to notify Penn National of the lawsuit despite his having been served with summons and complaint eight months earlier, McLeod asked Castillo whether he wanted Penn National to defend him in the Persimmon Hill Litigation. HOA Order, at p. 9. Without citation to evidence in the record or legal precedent, the trial court found that McLeod's asking Castillo whether he wanted to be defended in the Persimmon Hill Litigation "misled" him "with respect to the claim, coverage and policy benefits to which [he and JJA Construction were] entitled." HOA Order, at p. 9; Rule 59 Order, at p. 26.

In fact, Castillo affirmatively stated that he did **not** want Penn National to defend him in the Persimmon Hill Litigation. HOA Order, at p. 9; [Trial Transcript, Vol. 2, at 94:22-95:1, 386:2-6]. Castillo accepted contact information for the Penn National adjuster handling the claim from McLeod, and told her that he would reach out to Penn National directly to discuss the claim further. [HOA Exhibit No. 10; Trial Transcript, Vol. 1, at 407:17-408:8; Vol. 2, at 95:2-7]. McLeod then asked Castillo whether he would provide Penn National his contact information, but Castillo simply shook his head to indicate "no" walked away from her. [Trial Transcript, Vol. 2, at 95:8:22-96:8]. After refusing to provide his contact information to McLeod or Penn National, Castillo walked inside his house and closed the door, ending the conversation. [*Id*. at 95:18-96:8, 386:7-9]. Castillo never called Penn National to discuss the claim or suit following this May 2014 conversation with McLeod. [Trial Transcript, Vol. 1, at 408:2-4, 23-24].

After learning of Castillo's declination of a defense and refusal to provide contact information, Gross prepared the May 29, 2014 report recommending that the claim be denied because Castillo had failed to cooperate with Penn National's investigation. [Trial Transcript, Vol. 1, at 412:24-413:3; Penn National Exhibit No. 78, at pp. 31-35]. Castillo never tendered the lawsuit to Penn National for a defense after being served with process and never otherwise indicated that he desired a defense in the matter. [Trial Transcript, Vol. 2, at 37:11-23].

Parsons reviewed the report on June 16, 2014 and agreed with its conclusion that coverage should be denied to JJA for failure to cooperate. [Penn National Exhibit No. 78, at p. 28; Trial Transcript, Vol. 2, at 34:25-36:7]. To give Castillo the benefit of the doubt, Parsons recommended writing Castillo a final letter outlining Penn National's efforts to secure his cooperation, noting the ramifications of his failure to cooperate and declination of the defense offered him and his companies, and offering a final opportunity to avail himself the defense offered by his policies.

[Penn National Exhibit No. 78, at p. 28; Trial Transcript, Vol. 2, at 34:25-36:7].

Penn National sent letters to Castillo and JJA Construction, Inc. on August 11, 2014. HOA Order, at p. 11; [HOA Exhibit No. 14, at pp. 9-14, 16-21 (Bates Stamped 942-948, 950-955); Trial Transcript, Vol.1, at 418:18-20]. The letters gave Castillo through the end of August 2014 to respond to Penn National's attempts to contact him and warning that his failure to do so would result in the denial of his claim. [*Id*., at pp. 14, 21]. As of August 11, 2014, Penn National had received no additional communication from Castillo. [Trial Transcript, Vol. 1, at 419:2-4].

By letters dated October 2, 2014, Penn National denied the "claim" because Castillo had declined its offer of a defense in his meeting with McLeod. HOA Order, at pp. 11-12; [HOA Exhibit No. 14, at pp. 23-28, 30-35]. These letters were addressed to Castillo's address in Huntersville, North Carolina and copied to the Taylor Agency. [*Id*.]. Penn National never received a response to these letters from Castillo. . HOA Order, at pp. 11-12; [Trial Transcript, Vol. 2, at 374:6-24].

ARGUMENT

As to Appellee Persimmon Hill Homeowners Association, Inc.

1. The Trial Court Improperly Awarded Coverage to Jose Castillo and JJA Construction, Inc. After Castillo Advised Penn National That He Did Not Want a Defense and Refused to Cooperate with Penn National

The trial court correctly found that in response to being asked whether Castillo wanted Penn National to defend him in the Persimmon Hill Litigation, Castillo said "no." HOA Order, at p. 9 ("Castillo responded that he did not want a defense."); [HOA Exhibit No. 10; Trial Transcript, Vol. 2, at 94:22-95:1, 36:2-6]. As a matter of South Carolina law, Castillo's statement combined with his otherwise complete failure to communicate with Penn National was sufficient to terminate any duty that Penn National may have otherwise had to defend him.

Under South Carolina law, a policyholder may decline the benefits of his policy if he chooses, including a defense. *See, e.g., Twin City Fire Ins. Co. v. Ben-Arnold-Sunbelt Beverage Co. of S.C.*, 433 F.3d 365, 374 (4th Cir. 2005) (applying South Carolina law) (finding that the insured may refuse the defense conducted by the carrier and fund its own defense); *State National Ins. Co. v. Eastwood Construction LLC*, C/A No. 6:16-cv-02607-AMQ, 2018 WL 8787543, at *16 (D.S.C. Sept. 5, 2018) (indicating that the insured may "relieve the insurer of all obligations under the terms of the policy"); *Tucker v. State Farm Mut. Auto. Ins. Co*., 232 S.C. 615, 624-25, 103 S.E.2d 272, 277 (1958) (finding that the insured's statement that he was "not going to have any more to do with this case" relieved insurer of duty to defend); *see also National Union Fire Ins. Co. of Pittsburgh, PA v. Crocker*, 246 S.W.3d 603, 608 (Tex. 2008) ("Potential insureds, for a variety of reasons, might well opt against seeking a defense from an insurer."); *M.B.L., Inc. v. Federal Ins. Co*., No. CV 13-03951 BRO (AGRx), 2014 WL 12584437, at *7 (C.D. Cal. May 30, 2014) (quoting *Hartford Acc. & Indem. Co. v. Gulf Ins. Co*., 776 F.2d 1380, 1383 (7th Cir. 1985)) ("An insurance company is not required to intermeddle officiously where its services have not been requested."). For example, in *Twin City*, the insured declined its insurer's offer of a defense and instead elected to hire its own counsel to defend in the lawsuit. 433 F.3d at 374. The court there found that the insured's election relieved the carrier of its duty to defend under South Carolina law. *Id*. Here, Castillo's refusal likewise operated as a knowing and voluntary relinquishment of his rights under the policy that was fully viable under the law.

The trial court attempted to differentiate the above authorities on the basis that in those cases, the insurance carriers retained counsel to defend the insured and the insured directed its relinquishment of the defense to the attorney rather than, as here, to Penn National's adjuster. Rule 59 Order, at pp. 23-24. However, that "differentiating" fact represents a distinction without a

difference with respect to the point of law that an insured may decline policy benefits. The cases such as *Twin City*, *Eastwood Construction*, and *Tucker* all stand for the proposition that the insured may decline benefits under his policy if he chooses, but say nothing to the effect that such a declination must be made to counsel retained by the carrier. Here, Castillo, in direct response to being asked whether he wanted Penn National to provide him a defense in the Persimmon Hill Litigation, unequivocally answered "no." Under these authorities, that statement was a proper declination of the benefit.

Further, the trial court found that Castillo's statement did not operate as refusal of the policy benefit, apparently for two reasons: (1) that Penn National affirmatively misled Castillo about the risk to which he was exposed, specifically the prospect of a multimillion dollar judgment and that any attorney defending JJA would be paid at Penn National's expense (HOA Order at p. 31; Rule 59 Order, at p. 24); and (2) that Penn National failed to provide adequate consideration for what the trial court found was an alteration to the insurance policy (HOA Order, at p. 32). Neither of these purported justifications has a factual basis nor comport with South Carolina law.

First, the court's conclusion that Penn National "misled" Castillo about the particulars of the suit is untenable. There is no evidence in the record from which to reasonably conclude that Penn National engaged in such conduct. There is no evidence that, for example, Penn National sought to encourage Castillo to refuse the defense by minimizing the risk he faced or misrepresenting the policy terms. As a citation for its conclusion that Penn National had not provided Castillo "with all the pertinent factual information as to coverages available to him and for which he had already paid," the trial court cited to an excerpt of McLeod's testimony about why she elected not to gather additional information from Castillo about the nature of his work on the project and his contractual relationship with Portrait Homes. Rule 59 Order, at p. 24 (quoting

Trial Transcript, Vol. 2, at 100:24-101:7). The court's conclusion that Penn National misled Castillo based upon its independent adjuster's limited goal (contacting the insured and requesting that he contact the Penn National in-house adjuster) is completely unsupported by that record citation.

Further, the trial court determined that the purpose of Penn National's call to Castillo's residence was "to see if JJA wanted Penn National to provide a defense in the [Persimmon Hill] litigation." HOA Order, at p. 31; *see also id*. ("When asked if JJA wanted a defense in the pending Persimmon Hill litigation, the trial testimony was that Castillo responded that he did not."). The trial court did not find that this question was unreasonable or misleading. While Castillo testified that if Penn National had used different language, he would have responded differently (Rule 59 Order, at pp. 24-25), the trial court did not find and the record contains no evidence of any policy provision or other relevant policy-related information that Penn National misrepresented. The record simply contains no evidence from which the court could reasonably conclude that Penn National "misled" Castillo about the contents of the policy.

Second, the court's conclusion that Castillo could not decline the policy benefit of the defense Penn National offered him absent provision of consideration is at odds with the plain policy language and basic South Carolina contract law. The trial court found that Castillo could not have waived a defense orally and that such action would instead have required a written endorsement issued by Penn National and made a part of the policy. HOA Order, at p. 32. The court supported this finding using the following language from the Policies' conditions: "This policy's terms can be amended or waived only by endorsement issued by us and made a part of this policy." *Id*. Plainly, however, this condition does not apply to Castillo's ability to decline a defense in a particular claim. This language states that the "terms" of the policy cannot be waived

absent an endorsement issued by Penn National. Castillo was not waiving the "terms" of the policy, however. He was not, for example, altering the policy limits or a policy exclusion. Rather, he was declining a right under the policy with respect to this one case, a right that he maintained for other claims. *See, e.g., Twin City*, 433 F.3d at 374 (noting that the insured may decline a defense offered by a carrier at his option). Requiring *Penn National* to attach a written endorsement to the policy simply to memorialize the *insured's* one-time declination of a policy is a nonsensical interpretation of this provision. *S.C. Dep't of Natural Resources v. Town of McClellanville*., 345 S.C. 617, 623, 550 S.E.2d 299, 302 (2001) ("A contract is ambiguous when the terms of the contract are *reasonably* susceptible of more than one interpretation.") (emphasis added). Thus, the plain language of the policy does not support the court's finding.

The trial court's failure to conclude that Castillo's response of "no" when asked whether he wanted a defense in the litigation terminated Penn National's duty to defend was erroneous. The insured has the ability to decline a defense that the carrier offers him under South Carolina law. Here, he did so in unambiguous terms. The record contains no evidence to support the trial court's conclusion that Penn National misled Castillo about the exposure he faced or the nature of the policy terms governing the defense. Penn National was not, as a matter of law, required to provide consideration in exchange for Castillo's relinquishment of the defense in this case. Thus, the trial court's finding that Penn National's duty to defend continued beyond the point where Castillo declined the defense is incorrect as a matter of law.

2. The Trial Court Improperly Failed to Conclude that Castillo Violated the Policies' Notice and Cooperation Conditions as a Matter of Law

The trial court erroneously failed to conclude that Castillo and JJA Construction violated the Penn National Policies' notice and cooperation conditions. Under South Carolina law,

violations of these conditions may relieve insurers of coverage obligations if the violation substantially prejudices the insurer's ability to defend the claim. *South Carolina Farm Bureau Mut. Ins. Co. v. Dawsey*, 371 S.C. 353, 356, 638 S.E.2d 103, 104 (2006) (recognizing that insurers have the right to impose conditions on the coverage afforded by liability policies). South Carolina courts have recognized both the notice and cooperation conditions as valid conditions precedent to coverage. *Tucker*, 232 S.C. at 616, 103 S.E.2d at 273 (finding that an insurer properly denied coverage to its policyholder where he violated the notice and cooperation conditions of the policy); *Prior v. S.C. Med. Malpractice Liab. Ins. Joint Underwriting Ass'n*, 305 S.C. 247, 249–50, 407 S.E.2d 655, 657 (Ct. App. 1991) (holding that the insured was not entitled to coverage where he failed to provide timely notice of the claim and also failed to forward suit papers until approximately four months after he had received them).

As discussed below, the trial court failed to find that Castillo violated each of these conditions based on its findings of fact. This court should reverse that conclusion and find that Castillo violated both conditions as a matter of law.

a. Castillo Violated the Policies' Notice Condition as a Matter of Law

Castillo never satisfied the Policies' notice provision. The trial court implied that Penn National's receipt of the suit papers from an alternative source (Portrait Homes' separate request for "Additional Insured" coverage) satisfied Castillo's and JJA Construction's policy duties of notice. *See, e.g.,* HOA Order, at pp. 3 (noting that Penn National's receipt of the Portrait Homes tender letter "put Penn National on notice of the HOA's claims against its insured"), 29 ("Penn National had notice of the claim against JJA even before JJA was served with the complaint."). The court also made the unreasonable and unsupported factual findings that (1) Penn National conceded that Castillo and JJA complied with the Policies' notice condition during Castillo's

meeting with McLeod (HOA Order, at pp. 9-10, 26), and (2) that Penn National applied the incorrect duties provision in concluding that Castillo violated the notice provision (HOA Order, at pp. 26-28).

The undisputed facts in this matter are that Penn National received notice of the lawsuit in June 2013 by way of Portrait Homes' additional insured tender. Castillo and JJA Construction were not served with process in the Persimmon Hill Litigation until September 8, 2013, when Castillo was served personally and on behalf of JJA Construction. [Penn National Exhibit Nos. 80 & 81; Trial Transcript, Vol. 1, at 713:4-8]. At that point, therefore, Castillo became aware of the pending legal proceedings against him and against the corporation over which he exercised control. Castillo did not contact Penn National about the litigation after being served nor after being provided direct contact information for Penn National's adjuster assigned to the claim during his in-person meeting with McLeod. [Trial Transcript, Vol. 2, at 26:19-27:9; HOA Exhibit No. 4 at pp. 3-10 (1078-1085) (claim file notes indicating no contact from Castillo following service); [Trial Transcript, Vol. 1, at 408:2-4, 23-24].

In South Carolina, an insurer's knowledge of a claim or suit against an insured is insufficient to satisfy a policy's notice provision. *Merit Ins. Co. v. Koza*, 274 S.C. 362, 364 S.E.2d 146 (1980); *Founders Ins. Co. v. Richard Ruth's Bar & Grill LLC*, 761 Fed. App'x 178, 182-83 (4th Cir. 2019). In *Merit*, for example, the Supreme Court found that the insured's failure to tender suit papers to the carrier violated the notice duty even where the insurer was aware of the suit and had conducted settlement negotiations with the plaintiff on the insured's behalf. *Merit*, 274 S.C. at 364-66, 364 S.E.2d at 147-48. There, two injured parties sued an insured for damages arising out of an automobile accident. *Id*. at 363, 147. The insurer's claims manager began negotiating with the plaintiffs on behalf of the insured in an attempt to resolve claims arising out of the accident,

but the insured never forwarded a copy of the suit papers against him to the insurer. *Id*. at 363-64, 147. Negotiations between the insurer and plaintiffs ceased, the insured never responded to the suit and, as a result, a default was entered against the insured. *Id*. at 364, 147. In that situation, the court found that the insured had not complied with the notice provisions of the policy, that the insurer was prejudiced by entry of the default judgment, and that the insurer had not waived its right to rely on the notice provision of the policy by virtue of its having conducted negotiations with the plaintiffs with knowledge that the insured had been served with process. *Id*. at 364-66, 147-48.

Merit is at direct odds with the trial court's conclusion that Penn National's mere knowledge of ongoing legal proceedings provided by a third party satisfies the insured's duty of notice. Even though the insurer was aware of an accident in which its insured was alleged to have caused damages to third parties, the *Merit* court found that the insured's failure to forward suit papers to his insurer relieved the carrier of its duty to indemnify the insured for a default judgment entered arising out of the same incident. *Id*. The court applied that rule even where the insurer had negotiated directly with the claimants in an effort to resolve the claims against its insured. *Id*. The *Merit* court also held that the insurer's knowledge of the proceedings, without more, was insufficient to find that the insurer waived its right to rely on the notice condition in the policy.[5]

[5] Most other jurisdictions follow a similar rule requiring that the insured tender the claim for coverage in order to trigger an insurer's duty to defend it. *See, e.g., Crocker*, 246 S.W.3d at 608 ("[N]otice and delivery-of-suit provisions in insurance policies serve two essential purposes: (1) they facilitate timely and effective defense of the claim against the insured, and more fundamentally, (2) they trigger the insurer's duty to defend by notifying the insurer that a defense is expected."); *Matter of Nationwide Ins. Co. (De Rose)*, 241 A.D.2d 607, 608, 659 N.Y.S.2d 342, 343 (3d Dep't 1997) (noting that the "fact that the insurance company has notification of the accident does not vitiate the breach of the policy requirement [that the insured notify the insurer of a claim or suit]"); *M.B.L.*, 2014 WL 12584437, at *7 (quoting *Hartford*, 776 F.2d at 1383) ("[An insurer's] [m]ere knowledge that an insured is sued does not constitute tender of a claim. What is

Id. at 365-66, 147-48. The trial court cited no authority to support its conclusion that Penn National's awareness of the Persimmon Hill Litigation satisfied Castillo's notice requirement.

Indeed, even in jurisdictions where, unlike South Carolina, the insurer's mere notice of the claim triggers its duty to defend the insured even in the absence of any indication from the insured that it is making a claim, Castillo's affirmative declination of the offered defense would terminate that duty. In those jurisdictions, the insurer is required to do what Penn National did here: contact the insured directly and ascertain its wishes with respect to the claim asserted against it. *See, e.g., Cincinnati Cos. v. West Am. Ins. Co*., 183 Ill.2d 317, 327, 701 N.E.2d 499, 504 (1998) ("Where the insurer has actual notice of a claim against its insured, it would not be required to interpret the insured's silence as a desire for assistance. Rather, the insurer can simply ask the insured if the insurer's involvement is desired, thus eliminating any uncertainty on the question. … The insurer does not become liable simply by inquiring of the insured whether it desires the insurer to defend."); *Towne Realty, Inc. v. Zurich Ins. Co*., 201 Wis.2d 260, 269, 548 N.W.2d 64, 67 (1996) ("Therefore, we hold that if it is unclear or ambiguous whether the insured wishes the insurer to

---

required is knowledge that the suit is potentially within the policy's coverage coupled with knowledge that the insurer's assistance is desired. An insurance company is not required to intermeddle officiously where its services have not been requested."); *Valentine v. Membrila Ins. Servs., Inc*., 118 Cal.App.4th 462, 473 (2004) ("It is well understood, for example, that an insurer's duty [to defend] does not arise until defense is tendered by the insured and the known facts point to a potential for liability under the policy."); *Snohomish Cnty. v. Allied World National Assur. Co*., 276 F.Supp.3d 1046,1053 (W.D. Wash. 2017) ("[A]n insurer's duty to defend does not arise unless the insured specifically asks the insurer to undertake the defense of the action … [A]n insurer cannot be expected to anticipate when or if an insured will make a claim for coverage; the insured must affirmatively inform the insurer that its participation is desired."); *First Bank of Turley v. Fidelity & Deposit Ins. Co. of Maryland*, 928 P.2d 298, 304 (Okla. 1996) ("An insurer ordinarily has no duty to defend an insured absent a request to provide a defense, which act serves to trigger the insurer's performance under the contract. It is the insured's sole duty to give its insurer timely and adequate notice of a third-party claim to aid the insurer in the discovery of facts bearing on coverage.").

defend the suit, it becomes the responsibility of the insurer to communicate with the insured before the insurer unilaterally forgoes the defense. … [T]his holding should not create an onerous duty for insurers: a simple letter requesting clarification of the insured's position should suffice."). When Penn National approached Castillo, he declined coverage in unambiguous terms. Once he did so, Penn National's duty to defend – even if triggered by its mere knowledge of the suit, which is not the law in South Carolina – terminated. Thus, as made clear by the authorities from South Carolina and other jurisdictions, the court's legal conclusion that the Policies' notice condition was satisfied is mistaken.

The trial court's failure to conclude that Castillo and JJA Construction violated the policy notice provisions is at odds with South Carolina law. The trial court's factual findings in support of that conclusion are plainly erroneous and have no reasonable support in the record. This court should therefore find that Castillo and JJA Construction violated the notice provision in the Penn National Policies as a matter of law.

b. Castillo Violated the Policies' Cooperation Condition as a Matter of Law

The trial court failed to conclude that Castillo and JJA Construction violated the Policies' cooperation provision as a matter of law. The cooperation condition requires that the insured "[c]ooperate with [Penn National] in the investigation or settlement of the claim or defense against" the lawsuit for which coverage was requested. [Plaintiffs' Exhibit Nos. 14, at pp. 48-49; 17, at pp. 30-31; 21, at pp. 49-50; 27, at pp. 40-41; 29, at pp. 42-43]. Here, the trial court's actual findings of fact can lead to only one legal conclusion: that he and JJA Construction failed to comply with the Policies' cooperation provision. After Castillo failed to provide notice of the claim to Penn National, Penn National sent its independent adjuster, McLeod, to meet with him. HOA Order, at p.26. During this meeting, Castillo declined to provide contact information that would

allow Penn National representatives to contact him directly, indicated that he did not want Penn National to retain counsel to defend him in the Persimmon Hill Litigation, and stated that he would reach out to Penn National himself to discuss the matter further. [HOA Exhibit No. 10; Trial Transcript, Vol. 1, at 407:17-408:8; Vol. 2, at 95:2-7]. Castillo never contacted Penn National after this meeting. [Trial Transcript, Vol. 1, at 408:2-4, 23-24]. These behaviors violated the Policies' cooperation condition as a matter of law. *See Tucker*, 232 S.C. at 624-25, 103 S.E.2d at 277 (*finding that the insured's refusal to participate in the defense of the suit against him violated the* duty to cooperate and relieved the insurer of the duty to defend). At trial, even the HOA's "claim handling" expert agreed that Castillo's conduct in response to inquiries from McLeod violated his duty to cooperate with Penn National. [*Id.*, at 713:4-16, 735:13-736:13]. Thus, the court should have found, as a matter of fact and law, that Castillo and JJA Construction violated their duty to cooperate with Penn National.

3. Penn National Suffered Substantial Prejudice As a Result of Castillo's Breaches of Conditions Because Those Violations Led to Entry of Default and Default Judgment

Penn National was substantially prejudiced as a matter of law by Castillo's violations of the policy conditions because those violations led directly to entry of default against him and JJA Construction. "Where the rights of an innocent third party are jeopardized by the failure of the insured to comply with the notice requirements of an insurance policy, the insurer must show substantial prejudice to the insurer's rights." *Vermont Mut. Ins. Co. v. Singleton*, 316 S.C. 5, 12, 446 S.E.2d 417, 421 (1994). South Carolina courts have consistently held that the insured's failure to comply with the conditions for coverage under a liability policy will relieve an insurer of its obligation to provide coverage to the insured if prejudice results from such failure. *Id.*

Entry of a default judgment against an insured substantially prejudices an insurer as a

matter of South Carolina law. *Merit*, 274 S.C. at 364-66, 364 S.E.2d at 147-48. The trial court found, without citation to any authority, that this rule applies only where the insurer had no notice of the suit before default is entered. HOA Order, p. 30. *Merit*, however, stands for exactly the opposite proposition. There, the insurer had notice of the claim and legal proceedings against the insured and was conducting settlement negotiations on the insured's behalf. *Merit*, 274 S.C. at 363-64, 364 S.E.2d at 147. In that situation, where the insured failed to forward copies of the pleadings to the carrier, the court found that entry of default against the insured constituted substantial prejudice as a matter of law, even though the insurer was aware of the suit. *Id*. at 364-66, 147-48; *see also Hatchett v. Nationwide Mut. Ins. Co.*, 244 S.C. 425, 432–35, 137 S.E.2d 608, 612–13 (1964) (holding that the insurer was prejudiced by the default judgment entered against its insured because "[i]t was in large measure deprived of the opportunity…to investigate promptly, to negotiate a settlement without the handicap of a default position").

Furthermore, Penn National could not have unilaterally appointed counsel on Castillo's behalf (and thereby avoid entry of default) without his approval.[6] The South Carolina Rules of Professional Conduct clearly provide that a prospective client must approve counsel before that attorney can act on the client's behalf, and courts have interpreted that rule as applicable in the insurer-appointed-counsel context. *Twin City*, 433 F.3d at 374 (citing Rule 1.8(f)(1), Rule 407

---

[6] The trial court found that Penn National waived its argument that it could not have ethically retained counsel to act on Castillo's behalf because it was not raised in in its reservation of rights letters, apparently based on the authority of the decision in *Harleysville Group Ins. v. Heritage Communities, Inc*., 420 S.C. 321, 803 S.E.2d 288 (2017) ("*Heritage Communities*"). HOA Order, pp. 32-33. However, Penn National's inability to retain counsel on Castillo's behalf is not a ground upon which it sought to deny coverage here. Rather, the inability to hire counsel is the manner in which Penn National was prejudiced by Castillo's failure to tender the claim or cooperate, grounds specifically mentioned in the reservation of rights letter sent to Castillo following his refusal to cooperate with McLeod and in its denial of Castillo's claim. [HOA Exhibit No. 10, at pp. 9-14, 16-21, 23-28, 30-35].

SCACR) ("Of course, an insured must consent to the counsel assigned by the insurance company."); *Eastwood Construction*, 2018 WL 8787543, at *11 (noting that Rule 1.8(f) of the South Carolina Rules of Professional Responsibility requires that an insured consent to its representation by counsel employed by an insurer to act on its behalf); *see also Johnson v. Amethyst Corp.*, 463 S.E.2d 397 (N.C. App. 1995) (holding that where an insurer-retained-counsel made an appearance without knowledge of the insured, such counsel had no authority to set aside the default on behalf of the insured because two factors essential in establishing an attorney-client relationship were not satisfied – (1) the agent's authorization by the principal, and (2) the principal's control over the agent).

Without any basis, the trial court tried to overcome this issues with a "finding" that Penn National could properly have appointed counsel to act on Castillo and JJA Construction's behalf without having received affirmative consent. First, it found, without citation to South Carolina authority for this proposition, that consent existed by virtue of the insuring agreement and duty to defend. Rule 59 Order, at p. 28. However, authorities such as *Twin City* and *Eastwood Construction* stand in direct contrast to that unsupported conclusion, and hold that the insured must consent to counsel appointed by the carrier. Second, the trial court relied on Ethics Advisory Opinion 2019 19-04, an advisory opinion from the State Bar released eight years after the events in question (and after this issue was raised by Penn National in this litigation), for the proposition that an attorney could enter an appearance on behalf of the insured without the insured's affirmative consent to the representation. The trial court's reliance on this opinion is unavailing for two reasons. First, it is an advisory opinion that conflicts with the governing authority of the *Twin City* and *Eastwood Construction* decisions cited above. Second, the decision requires that the insured be "missing" in order for the insurer to proceed without the insured's consent. Here,

however, Castillo's location was not in dispute – Penn National's independent adjuster met with Castillo at his home, where he declined Penn National's offer to defend him in the suit. Rather than being "missing," Castillo simply refused to participate in the defense of the Persimmon Hill Litigation and affirmatively declined representation. The trial court's reasoning is therefore at odds with governing precedent.

Thus, Castillo's failure to provide notice and refusal to participate in the representation precluded Penn National from appointing counsel to protect his and its interests here, leading directly to entry of default.

4. The HOA's Claim for Indemnification as a Judgment Creditor of the Insureds Fails Because the Insureds are Not Entitled to Coverage

The trial court found that the HOA, as a judgment creditor and assignee of Penn National's insureds, could collect on its judgment as a result of Castillo and JJA Construction being entitled to coverage. HOA Order, at pp. 41-43. Because the trial court's conclusions as to the insureds' declination of coverage and violation of conditions precedent to coverage and resulting substantial prejudice to Penn National's rights are erroneous, as described above, the trial court's award on the judgment creditor claim should be reversed.

As a judgment creditor (or as a purported assignee) of the Castillo Entities' rights under the Penn National Policies, the HOA stands in the shoes of Castillo and JJA Construction in seeking coverage under the Penn National Policies and is only entitled to satisfy its award or judgment to the extent that the insureds would be entitled to coverage. *S.C. Farm Bureau Cas. Ins. Co. v. Ausborn*, 249 S.C. 627, 648, 155 S.E.2d 902, 913 (1967) (holding that judgment creditors of the insured are not entitled to coverage under a policy because the judgment creditors had no greater rights under an insurance policy than the insured who had made material

misrepresentations in the application for the policy). As such, the HOA – whether as the judgment creditor of Castillo and JJA Construction or as assignee of their rights under the Penn National Policies – is not entitled to coverage because Penn National appropriately denied coverage. As detailed above, the Castillo Entities are not entitled to coverage under the Penn National Policies because they breached the Conditions for coverage under the policies by failing to tender the Persimmon Hill Litigation to Penn National or to cooperate with Penn National in its investigation and defense of such litigation.

5. The Trial Court's Findings Were Insufficient to Satisfy the Legal Standards for a Bad Faith Claim

The trial court found that Penn National engaged in bad faith conduct and that this conduct caused extracontractual damages to Castillo and JJA Construction.[7] To prove a claim for insurance bad faith in South Carolina, the insured must show four elements: (1) the existence of a mutually binding contract of insurance between the plaintiff and defendant; (2) the refusal by the insurer to pay benefits due under the contract; (3) resulting from the insurer's bad faith or unreasonable action in breach of the implied covenant of good faith and fair dealing; and (4) causing damage to the insured. *Howard v. State Farm Mut. Auto. Ins. Co.*, 316 S.C. 445, 451, 450 S.E.2d 582, 586 (1994). Where a bad faith claim is premised upon a denial of benefits under the policy, the insured must show that the insurer had no reasonable basis to support its decision to deny the claim. *Cock-N-Bull Steak House, Inc. v. Generali Ins. Co.*, 321 S.C. 1, 6, 466 S.E.2d 727, 730 (1996). As explained below, the trial court improperly found in the HOA's favor as to the third and fourth elements of this claim.

[7] The trial court found that Castillo and JJA Construction assigned their bad faith rights to the HOA.

The court identified multiple alleged instances of conduct supporting its finding on the HOA's bad faith claim against Penn National: (1) failure to properly conduct an investigation by interviewing other witnesses and hiring experts; (2) mailing reservation of rights letters to an incorrect address; (3) directly asking Castillo whether he wished to be provided a defense and noting in its claims log that Castillo needed to request a defense; (4) violating its own policies and procedures; (5) noting in its claims log that the claim should be denied just a week after Castillo and JJA Construction had been served; and (6) requesting an extension to respond to the complaint on Castillo and JJA Construction's behalf with no intention to file a responsive pleading. HOA Order, at pp. 36-41; Rule 59 Order, at p. 33. Whether an insurer's conduct amounts to bad faith is based upon the specific circumstances of the claim and upon the information in the insurer's possession at the time it engaged in the behavior. *See Myrick*, 395 F.3d at 494 (finding that the insurer's investigation was "adequate…*under the circumstances*.") (emphasis added); *see also Howard*, 316 S.C. at 448, 450 S.E.2d at 584 ("Whether an insurance company is liable for bad faith must be judged by the evidence before at the time it denied the claim…"). These findings are unsupported by reasonable evidence in the record, and insufficient to sustain a bad faith claim as a matter of South Carolina law in any event.

a. Penn National's "Failure to Conduct an Investigation" Was Not Unreasonable Conduct as a Matter of Law

First, the trial court found that Penn National's choice not to "contact any witnesses, hire any experts, [or] gather any material information through its own efforts" supported a conclusion that Penn National engaged in bad faith. HOA Order, at p. 37. Here, however, Penn National received no communication from its insured and so its investigation necessarily focused on, first, confirming whether its insureds had even been served with process and, after confirming that

service had been effected, contacting the insured to determine his intentions with respect to the suit. [Trial Transcript, Vol. 1, at 400:8-23, Vol. 2, at 88:2-11, 374:6-24; Defendant's Exhibit No. 83]. Once it successfully contacted the insured and learned that the insured was declining the defense, the investigatory steps concerning the merits of the HOA's claim against the insureds became moot because the insured was not making a claim related to the suit and Penn National's denial was based on that declination, not on the facts of the underlying construction defect claim. HOA Order, at pp. 11-12; [HOA Exhibit No. 14, at pp. 23-28, 30-35]. In *Flynn*, which the trial court cited for the proposition that the carrier owes a duty of good faith investigation, the court found that the carrier's reliance on its attorney's opinion to deny a claim was unreasonable where an investigation would have uncovered information that the at-issue fire was not incendiary in nature and, therefore, not excluded by the terms of the policy. *Flynn v. Nationwide Mut. Ins. Co.*, 281 S.C. 391, 395-96, 315 S.E.2d 817, 820 (1984). Here, by contrast, the investigation that the trial court found that Penn National should have made was divorced from its basis for denying the claim, and its reasonable performance of the duties the trial court identified would not have revealed any additional information that would have indicated a potential for coverage. *Id*. Thus, Penn National's failure to interview witnesses, retain experts, or otherwise investigate the merits of the underlying construction defect claim was not unreasonable given the insured's lack of cooperation and declination of coverage.

Moreover, even assuming that this conduct satisfied the "bad faith" element of the claim, the trial court failed to find facts sufficient to show that Castillo and JJA Construction sustained damage as a result. The court did not connect Penn National's failure to retain experts or contact witnesses to tangible damage Castillo sustained. *See id*. (finding that the carrier's investigation revealed facts that it knew or should have known might have established coverage such that its

investigation was in bad faith). Instead, the damages the court found resulted from the bad faith – apparently the default judgment that was entered – were the result of Castillo telling Penn National that he did not want to be defended and his failure to thereafter contact Penn National. [HOA Exhibit Nos. 10; 14, at pp. 23-28, 30-35]. In short, the trial court offered and the record contains no evidence to connect Penn National's election not to investigate the merits of the claim and entry of the default judgment.

b. *Mailing Reservation of Rights Letters to an Incorrect Address Cannot Sustain a Bad Faith Claim Because that Act did not "Result In" a Denial of Benefits*

Castillo has provided two separate mailing addresses to Penn National. Some of Penn National's letters went to Castillo's older address, whereas later correspondence went to his new (correct) address. In any event, Penn National's mistaken mailing of certain reservation of rights letters to Castillo's previous address is insufficient to support the bad faith element of this claim because Penn National's denial of benefits to Castillo and JJA Construction did not "result from" that act. A causal connection between the behavior violating the covenant of good faith and fair dealing and the insurer's denial of benefits is required to support a bad faith claim. *See Howard*, 316 S.C. at 451, 450 S.E.2d at 586 (describing the elements of a bad faith claim and noting that the insurer's refusal to pay policy benefits must "result from" its bad faith or unreasonable conduct); *see also Nichols v. State Farm Mut. Auto. Ins. Co.*, 279 S.C. 336, 340, 306 S.E.2d 616, 619 (1983) (holding that an insured can recover "consequential damages" if it can "demonstrate bad faith or unreasonable action by the insurer in processing a claim"). Penn National did not deny the claim because of Castillo's and JJA Construction's failure to respond to these letters. Rather, Penn National's explicit grounds for the denial of the "claim" was Castillo's declination of the defense during his face-to-face meeting with McLeod in May 2014. HOA Order, at p. 12;

[Plaintiffs' Exhibit Nos. 35, at p. 5; 36, at p. 5 (denial letters to Castillo and JJA Construction noting that the grounds for denial of the claim were their declinations of the offered defense)]. Between this meeting on May 10, 2014 and the denial letter sent on or around October 2, 2014, Castillo persisted in his refusal to contact Penn National, in violation of the Policies' notice and cooperation provisions, despite his statement otherwise to McLeod. Only after those additional months of silence from Castillo and JJA Construction did Penn National deny the claim, giving the insureds additional time during which to request that the claims decision he prompted be reversed. Thus, the trial court's order failed to connect the mailing of the letters to the improper address with the denial of policy benefits such that this behavior cannot sustain the claim.

c. Asking Castillo Whether He Wanted a Defense Was a Reasonable Behavior as a Matter of Law

Penn National's asking Castillo directly whether he wanted to be defended in the Persimmon Hill Litigation was reasonable conduct under the circumstances. Before meeting with him in person in May 2014, Penn National was aware that Castillo and JJA Construction had been served with process in September 2013 but had received no correspondence from Castillo. [Penn National Exhibit Nos. 80 & 81 (certificates of service); HOA Exhibit No. 4 at pp. 3-10 (1078-1085) (claim file notes indicating no contact from Castillo)]. Under these circumstances, Penn National's conduct of asking Castillo whether he wanted Penn National to provide him a defense was reasonable: Castillo's actions to that point all suggested that he had no intention of cooperating with Penn National (and were also material violations of the conditions precedent for coverage). [*E.g.*, Trial Transcript, Vol. 2, at 596:21-598:8]. Further, as a matter of law, Penn National's question was reasonable – an insurer is not required to interpret an insured's silence on a claim as a demand for a defense and should instead ask the insured if its assistance is requested. *Cincinnati*

Cos., 183 Ill.2d at 327, 701 N.E.2d at 504 ("Where the insurer has actual notice of a claim against its insured, it would not be required to interpret the insured's silence as a desire for assistance. Rather, the insurer can simply ask the insured if the insurer's involvement is desired, thus eliminating any uncertainty on the question. … The insurer does not become liable simply by inquiring of the insured whether it desires the insurer to defend."); *Towne Realty*, 201 Wis.2d at 269, 548 N.W.2d at 67 ("Therefore, we hold that if it is unclear or ambiguous whether the insured wishes the insurer to defend the suit, it becomes the responsibility of the insurer to communicate with the insured before the insurer unilaterally forgoes the defense."). Thus, the court's finding that this behavior was unreasonable is in error.

d. No Competent Evidence Supports the Trial Court's Finding that Penn National "Violated its Own Policies and Procedures"

The trial court's conclusion that Penn National "violated its own policies and procedures" is not supported by competent evidence because no evidence of Penn National's policies and procedures was authenticated or admitted at trial. Rule 59 Order, at p. 33. This finding is apparently based upon the trial court's conclusion that Penn National violated its "claims manual" by failing to take Castillo's recorded statement during McLeod's May 10, 2014 meeting with him. HOA Order, at p. 37; Rule 59 Order, at p. 32. This finding of fact is completely unsupported by evidence in the record, as no "claims manual" was ever introduced as evidence. *See* HOA Order, at pp. 9, 378 (citing to HOA Exhibit 21 to establish the requirements of the Penn National claims handling

[8] In somewhat contradictory fashion, the trial court potentially withdrew its references to the claims handling manual immediately after having quoted Penn National's testimony about its contents. *See* Rule 59 Order at pp. 32-33 (finding that Penn National "did not take and/or attempt to take a recorded statement of Mr. Castillo in contravention of its policy" while later noting that it "disagrees with Penn National's contention" that the manual had not been properly authenticated but that its conclusion that Penn National acted unreasonably was "conclusively supported by other extensive evidence considered by this court," without actual citation to any such evidence).

manual); [Trial Transcript, Vol. 1, at 6-11, Vol. 2, at 4 (exhibit list not including HOA Exhibit 21)]. Indeed, the only evidence concerning the contents of the claims handling manual elicited at trial was Penn National's claims counsel's statement that a recorded statement may be required "depend[ing] on what type of claim" was being investigated. [Trial Transcript, Vol. 2, at 309:21-24]. No follow up questions to establish necessary foundation for the court's finding that Penn National violated its own procedures were asked, such as whether this type of claim satisfied Penn National's guidelines requiring that such a statement be taken. *See id*. Furthermore, the only characterization in the record of what HOA Exhibit 21 purports to be comes from questions posed by counsel for the HOA, which is not admissible evidence. *McManus v. City of Greenwood*, 171 S.C. 84, 89, 171 S.E.2d 473, 475 (1933) (holding that statements of fact appearing only in argument of counsel will not be considered as evidence); *South Carolina Dept. of Transp. v. Thompson*, 357 S.C. 101, 106, 590 S.E.2d 511, 513 (Ct. App. 2003) ("Arguments made by counsel are not evidence."). The trial court's consideration of the contents of the "claims manual" thus violated the rules of evidence, which require admission of the original document to prove its contents unless excused by circumstances not present in this case. *See* S.C. R. Evid. 1002 (requiring the admission of the original writing to prove its contents), 1004 (describing situations where other evidence of a writing's contents may be introduced).

Finally, the trial court again did not connect Penn National's "failure" to take a recorded statement to any damages sustained by the insured. *Howard*, 316 S.C. at 451, 450 S.E.2d at 586; *Nichols*, 279 S.C. at 340, 306 S.E.2d at 619. Instead, the court simply identified that Penn National

---

Besides citing to Penn National's counsel's testimony summarized above, however, the court never pointed to any evidence in the record to establish either that the manual was admitted or that other evidence supporting its finding that Penn National violated its policies or procedures.

did not take a recorded statement without showing how that failure detrimentally affected Castillo. In fact, the independent adjuster, McLeod, told Castillo to call the Penn National in-house adjuster, Greg Gross, to provide a statement. Castillo failed to do so. As previously noted, Penn National's lack of investigation into the merits of the claim was not the cause of the denial of policy benefits to Castillo and JJA Construction such that damages identified do not connect with the conduct.

Thus, the trial court lacked any evidence reasonably supporting its finding that Penn National violated its own policies and procedures or that such violations damaged the insureds such that this bad faith conduct cannot support the claim.

e. Penn National's References to Denying the Claim in its Claim Notes Did Not "Result In" Denial of the Claim

As noted above, Penn National denied the claim as a direct result of Castillo's declination of the policy benefit of defense. HOA Order, at p. 12; [Plaintiffs' Exhibit Nos. 35, at p. 5; 36, at p. 5]. A bad faith claim in South Carolina requires a causal connection between the bad faith conduct and the denial of benefits under the policy. *Howard*, 316 S.C. at 451, 450 S.E.2d at 586. As with Penn National's mailing letters to the incorrect address, the reference in the claim file notes was not tied to the denial of benefits, which did not occur until months later, when Castillo declined the defense in person. Thus, the trial court's finding on that point is insufficient to support the claim of bad faith.

f. The Trial Court's Finding that Penn National Requested an Extension of Castillo's and JJA Construction's Answer Deadline Without Intention to Respond Is Unsupported by the Evidence and Cannot Support the Bad Faith Claim

Finally, the trial court found that Penn National requested an extension of Castillo's and JJA Construction's answer deadline without intention to file a responsive pleading constituted bad faith conduct. Rule 59 Order, at p. 33. The trial court cited absolutely no evidence for the

proposition that Penn National had no intention to file a responsive pleading. *Id.*

The evidence in the record does not support the trial court's finding of fact. The evidence showed that on May 8, 2014, Penn National's adjuster, Greg Gross, contacted the HOA's attorney and requested additional time for Castillo and JJA Construction to respond to the HOA's Complaint against them. HOA Order, at p. 8. That request occurred months after Castillo's and JJA Construction's respective deadlines to respond to the HOA's complaint expired, on or about October 8, 2013 (based on their having been served on September 8, 2013). S.C. R. Civ. P. 12(a). Gross' request came on the heels of an April 24, 2014 letter to Penn National from the HOA's attorney noting that no responsive pleadings had been filed on behalf of Castillo or JJA Construction and that default would be taken within 15 days if no responsive pleading was filed. HOA Order, at p. 7. In the interim, on May 10, McLeod met with Castillo, who reported that he did not want a defense, after which Penn National chose not to retain defense counsel or to file a responsive pleading on his behalf. [HOA Exhibit No. 10]. Thus, there is no evidence that reasonably supports the finding that Penn National had no intention to file a responsive pleading.

Moreover, as is the case with many of the other acts that the trial court identified as bad faith conduct, there is no connection between Penn National's request for an extension and the denial of benefits under the policy. *Howard*, 316 S.C. at 451, 450 S.E.2d at 586; *Nichols*, 279 S.C. at 340, 306 S.E.2d at 619. Penn National ultimately denied coverage because of Castillo's declination, which had no connection to Penn National's request for additional time for he and JJA Construction to respond to the HOA's complaint. If anything, Penn National's request – made months after the HOA could have taken their default – conferred a benefit upon Castillo and JJA Construction. Thus, as a matter of law, this conduct is insufficient to support the claim.

As a result, none of the conduct the trial court identified is sufficient to sustain the HOA's

bad faith claim. The entry of judgment in its favor on this claim should be reversed.

6. The Trial Court's Findings of Fact Do Not Support a Punitive Damages Award

The trial court's punitive damages award does not satisfy the standards for punitive damages in the insurance bad faith context under South Carolina law. Punitive damages are awardable on an insurance bad faith claim only where the insured proves, by clear and convincing evidence, that the insurer's conduct was "was willful or in reckless disregard of [the insured's] rights under the contract." *Crossley*, 307 S.C. at 360, 415 S.E.2d at 397; *Austin v. Specialty Transp. Servs*., 358 S.C. 298, 313, 594 S.E.2d 867, 875 (Ct. App. 2004). South Carolina courts have defined "willful" in a variety of different contexts, and each requires that the party engaging in the conduct be conscious of the wrongdoing in order to be considered willful. *State v. Garrard*, 390 S.C. 146, 149-50, 700 S.E.2d 269, 271 (Ct.App. 2010) (citations omitted); *see also Kuznik v. Bees Ferry Assocs*., 342 S.C. 579, 611, 538 S.E.2d 15, 32 (Ct.App. 2000) (finding that in the punitive damages context, willfulness means "a conscious failure to exercise due care"). South Carolina courts do not appear to have enunciated a standard for what constitutes "reckless disregard of the insured's rights under the contract," but have defined recklessness as "doing…a negligent act knowingly" and a "conscious failure to exercise due care." *Yaun v. Baldridge*, 243 S.C. 414, 419, 134 S.E.2d 248, 251 (1964). Under this definition, therefore, the insured must prove some conscious recognition by the insurer that the insured's rights under the policy are being disregarded. *Id*; *Crossley*, 307 S.C. at 360, 415 S.E.2d at 397.

The bad faith conduct identified by the trial court, even taken as true, does not rise to the level of willfulness or reckless disregard of Castillo's and JJA Construction's rights sufficient to merit an award of punitive damages. Penn National's election not to retain experts, interview witnesses, or conduct a recorded statement with Castillo about the merits of the case was a reaction

to Castillo's silence with regard to the claim and, ultimately, to his declination of a defense. No evidence in the record suggests that these acts were taken in conscious disregard for protecting Castillo's interest in the litigation; rather, they were made in light of Castillo's declination of the policy benefits. Similarly, no record evidence supports the finding that Penn National's asking Castillo whether he desired its assistance in the matter was done in knowing contravention of Castillo's policy rights. Instead, the record shows that Penn National affirmatively sought his response on that issue following his failure to contact Penn National for more than six months after receiving the suit papers in September 2013. [HOA Exhibit No. 4 at p. 10 (1085)]. Prospectively asking Castillo whether he wanted a defense was reasonable as a matter of law given that the question followed months of silence following his failure to contact his insurer for months after being notified of the lawsuit pending against him and his corporation. *Cincinnati Cos*., 183 Ill.2d at 327, 701 N.E.2d at 504; *Towne Realty*, 201 Wis.2d at 269, 548 N.W.2d at 67. Finally, no evidence in the record shows that Penn National deliberately mailed its reservation of rights letters to an incorrect address. Rather, the adjuster, Gross, admitted that he made a mistake in addressing the letter to only one of the two addresses on file for Castillo, but did not admit to any deliberate or conscious decision to improperly mail the letter to an old address. [*See, e.g*., Trial Transcript, Vol. 1, at 349:21-25]. Further, all letters were copied to Castillo's agent, which suggests that there was no willing or reckless attempt to have Castillo waive any benefits due under the policy. [HOA Exhibit No. 14 at pp. 2-7, 9-14, 16-21].

Thus, the trial court's findings in support of its punitive damages award are not reasonably supported by the record evidence or governing legal authorities. Penn National respectfully requests that this court overturn the punitive damages award.

As to Appellee Portrait Homes

1. The Trial Court Improperly Considered Parol Evidence To Award Coverage to Portrait Homes Where Portrait Homes Did Not Qualify as an "Additional Insured" Under the Plain Language of the Penn National Policies

Additional insureds are entities or persons entitled to certain protection under an insurance policy, but who are not listed as a named insured on the declaration pages of a policy, or necessarily included under the "Who Is An Insured" provisions of the policy. 3 Appleman on Insurance Law, §16.05(1)(c)(i). Rather, they are added to the coverage provided by the policy by endorsement. The extent of the insurer's obligations to these third-parties is limited by the terms of the endorsement. The endorsement may require that the additional insureds be specifically named in the endorsement in order for coverage under the policy to be afforded to that third-party, or the endorsement may allow coverage for an unspecified additional insured through reference to documents outside the policy, such as a contract between the third-party and the named insured. *Id.* at §(c)(ii).

The trial court incorrectly determined that Portrait Homes qualified as an additional insured on the 2003-04 and 2004-05 Penn National Policies through consideration of parol evidence. These policies both used additional insured form CG 20 37, which extends additional insured coverage to specifically named entities. Portrait Homes Order, at pp. 27. However, those forms are unambiguous such that consideration of additional evidence was improper as a matter of law.

The plain terms of endorsement form CG 2037 attached to the 2003-04 and 2004-05 Policies extend additional insured coverage to specifically named entities for liabilities arising out of the named insured's work without the need for an additional contract. [Plaintiffs' Exhibit Nos. 14. at pp. 18-20; 17 at p. 4]. The CG 20 37 endorsements attached to these two policies show three entities in the Portrait corporate structure: Pasquinelli Construction Company, Pasquinelli Management LLC, and Portrait Homes Construction Company. *Id*. Neither Portrait Homes

plaintiff is shown in the schedule or on any policy form that might confer additional insured rights for this claim. *Id*. Here, the CG 20 37 endorsements unambiguously extend additional insured coverage only to the three listed entities. The plain terms reflect the extent of Penn National's and Castillo's intentions with respect to the award of such coverage. The court failed to find, and no evidence supports, any reasonable interpretation of the endorsement other than that it extends protection only to those named entities.

The trial court found, based upon Portrait Homes' testimony and the Master Agreement, that Penn National and Castillo intended to insure additional unlisted entities via this form. Portrait Homes Order, at pp. 32-34. However, where the terms of a contract are unambiguous, reliance on such evidence is improper. *B.L.G. Enterprises*, 334 S.C. at 535, 514 S.E.2d at 330; *S.C. Dep't of Transp. v. M&T Enterprises of Mt. Pleasant, LLC*, 379 S.C. 645, 656, 667 S.E.2d 7, 13 (Ct. App. 2008) ("A court must enforce an unambiguous contract according to its terms regardless of its wisdom or folly, apparent unreasonableness, or the parties' failure to guard their rights carefully."). Further, the evidence at trial showed that Portrait Homes reviewed and approved this particular form before allowing Castillo to commence work on the project, belying any "intention" to insure unnamed parties. For example, Shawn Belcher, a Portrait Homes purchasing manager who worked directly with subcontractors and executed contracts for Portrait Homes, testified that a subcontractor such as Castillo would not have been approved for work on a particular project if additional insured endorsements were not properly completed to Portrait Homes' satisfaction. [Trial Transcript, Vol. 1, at 485:24-486:25]. Castillo presented Portrait Homes with a copy of a certificate of insurance with a copy of form CG 20 37 (for the 2004-05 Policy) attached, and it showed only the three specifically named entities included as additional insureds. [Plaintiffs' Exhibit No. 7]. Portrait Homes accepted that endorsement at the time, only to change its mind

much later, after this litigation began.

The trial court's conclusion that interpreting the CG 2037 endorsement as extending coverage only to the entities specifically named renders its coverage "meaningless" – was also erroneous. The court provided no analysis for this point and instead relied on a string citation of case law establishing the general proposition that insurance policies should not be interpreted in a manner that leads to absurd and unreasonable results. Portrait Homes Order, at p. 33. Here, however, that line of authorities is inapposite. Contrary to the court's finding, interpreting the endorsement as being limited to the entities named on it would not render coverage meaningless; rather, it would fulfill the clear intention of the parties, to extend coverage only to those entities appearing on the form.

Thus, the trial court erroneously found that Portrait Homes is entitled to coverage under the 2003-04 and 2004-05 Policies as an additional insured.

2. The Trial Court Improperly Considered Parol Evidence to Interpret the Unambiguous 2005-06, 2006-07, and 2007-08 Penn National Policies

The trial court again relied on the parties' "intention," rather than addressing the clear and unambiguous terms of the governing contracts, in finding that Portrait Homes qualified as an additional insured under endorsement 71 1145 attached to the 2005-06, 2006-07, and 2007-08 Policies. The court's interpretation again fails to enforce the unambiguous terms of the insurance contracts and improperly relies on extrinsic evidence to reach its result.

a. The Unambiguous Terms of Endorsement 71 1145 Show that Portrait Homes Was Not Entitled to Additional Insured Coverage

To confer additional insured status under form 71 1145, four requirements must be satisfied: (1) there must be a written contract or agreement; (2) with the named insured shown on the declarations ("you"); (3) that requires that the third party be named as an additional insured;

and (4) that the additional insured status required in the contract specifically include completed operations coverage. *See, e.g.* [Plaintiffs' Exhibit No. 21, at pp. 29, 40]; Portrait Homes Order, at p. 12. Reading these provisions together, to receive additional insured rights under these policies pursuant to form 71 1145, a third party to the insurance policy such as Portrait Homes must have a written contract or agreement with JJA Construction, Inc. (the named insured on all three of these policies) under which JJA Construction, Inc. is required to name that third party as an additional insured under completed operations coverage.[9]

The only contracts in evidence are a March 6, 2002 "Housing and Purchase Order Contract" and an October 25, 2002 "Master Agreement." [Plaintiffs' Exhibit Nos. 37 (Master Agreement) & 38 (Housing and Purchase Order Contract)]. The trial court agreed that neither contract satisfies the requirements of form 71 1145 on its face. However, the trial court determined that JJA Construction, Inc. was a party to the construction contracts by consideration of parol evidence. *See* HOA Order, at pp. 13-27 (considering underwriting file documents, the underlying complaint against JJA Construction, Inc. and a certificate of insurance in determining that JJA Construction, Inc. was bound by the contracts in evidence despite not being named as a party to them).

The provisions of the Housing and Purchase Order Contract do not confer additional insured status upon Portrait Homes because that Contract is (1) not a contract between JJA Construction, Inc., the named insured, and Portrait Homes, and (2) even if JJA Construction, Inc.

---

[9] Completed operations coverage offers the insured protection for bodily injury or property damage, other than to the completed work itself, that occurs after the insured's work is completed. 3 Appleman on Insurance Law, §36.02(1)(a). This coverage differs from "ongoing operations" coverage, which covers those liabilities that arise before the insured's work on a project is completed. *Id.*

were a party to the Contract, the Contract terms do not satisfy the endorsement's requirements. First, the Housing and Purchase Order Contract, which by its terms governed Castillo's work at the Persimmon Hill Project, was between "JJA Framing" and Portrait Homes.[10] [Plaintiffs' Exhibit No. 38, at pp. 1, 6]. The named insured shown on the declarations page of the policies using form 71 1145 to confer additional insured status is "JJA Construction, Inc.", which was not a party to this agreement and in fact was not created for nearly three years after this Contract was executed in 2002. Second, the Housing and Purchase Order Contract does not require the named insured to purchase completed operations coverage or to name Portrait Homes-South Carolina, LLC as an additional insured under such coverage. Rather, the contract merely requires Castillo to purchase and name Portrait Homes-South Carolina, LLC as an additional insured under various coverages, including general liability coverage. [*Id*. at pp. 3-4]. The contract does not even require Castillo to purchase completed operations coverage for itself, much less to name Portrait Homes as an additional insured under that coverage. *Id*. Thus, the Housing and Purchase Order Contract fails to satisfy form 71 1145 and does not confer additional insured status to Portrait Homes under these policies.

Similarly, the Master Agreement is not a contract with the named insured under the 2005-06 through 2007-08 Policies sufficient to confer additional insured status under form 71 1145. The Master Agreement was between Portrait Homes-South Carolina, LLC and Castillo individually. [Plaintiffs' Exhibit No. 37, at pp. 1, 4]. Again, JJA Construction, Inc. was not a party to the contract and was not created until more than two years after Castillo executed the Master Agreement.

[10] The preamble to the contract indicates that the Portrait Homes entity being bound is Portrait Homes – South Carolina, LLC, a plaintiff in this action, while the signature page indicates that a different entity is bound, "Portrait Homes Construction Co." Portrait Homes Construction Co. is not a party to this action and was not a defendant in the underlying Persimmon Hill Litigation.

b. The Trial Court's Consideration of Parol Evidence Was Improper Because the Policies Are Unambiguous

First, irrespective of the contents of any documents outside the contract itself, the court's consideration of evidence outside the contract is improper because the policy terms were unambiguous. *Goldston v. State Farm Mut. Ins. Co*., 358 S.C. 157, 170, 594 S.E.2d 511, 518 (Ct.App. 2004) (quoting *Schulmeyer v. State Farm Fire & Cas. Co*., 353 S.C. 491, 495, 579 S.E.2d 132, 134 (2003)) (where a contract's language is "clear and unambiguous, the language alone determines the contract's force and effect.")). "[I]f the intention of the parties is clear, courts have no authority to torture the meaning of policy language to extend or defeat coverage that was never intended by the parties." *MGC Mgmt. of Charleston, Inc. v. Kinghorn Ins. Agency*, 336 S.C. 542, 548 520 S.E.2d 820, 823 (Ct.App. 1999). To create a contract ambiguity, the challenging party's interpretation must be reasonable. *Universal Underwriters Ins. Co. v. Metropolitan Property and Life Ins. Co*., 298 S.C. 404, 407, 380 S.E.2d 858, 860 (Ct.App. 1989), superseded by statute on other grounds as noted by *Williams v. Government Employees Ins. Co*., 409 S.C. 586, 602, 762 S.E.2d 705, 714 (2014) (quoting *Gordon Farms, Inc. v. Carolina Cinema Corp*., 294 S.C. 158, 160, 363 S.E.2d 235, 236 (Ct.App. 1987)) ("A contract is ambiguous only when it may fairly and reasonably be understood in more ways than one.").

The only reasonable interpretation of the Policies, and form 71 1145, is that the named insured was JJA Construction, Inc. and not Castillo or his sole proprietorship, JJA Framing. Form 71 1145 requires that "you" be compelled by written contract to protect an additional entity for completed operations liabilities. [Plaintiffs' Exhibit Nos. 21, at p. 29; 27, at p. 20; 29, at p. 23]. "You," as defined in each of the relevant Policies, means "the named insured *shown in the Declarations*, and any other person or organization qualifying as a Named Insured under this

policy." [Plaintiffs' Exhibit Nos. 21, at p. 40; 27, at p. 31; 29, at p. 33] (emphasis added). The only named insured shown on these Policies' declaration pages – and, thus, the only entity, in whatever form (individual or corporate), that the parties intended as an insured under these Policies – was "JJA Construction, Inc." Castillo's change form did not request that Castillo/JJA Framing continue to be a named insured under the Policies; rather, he requested that the named insured **change** from himself and to the different corporate entity. [Plaintiffs' Exhibit No. 18]. Regardless of whether "JJA Construction, Inc." was an individual or a corporate entity, it is clear that Castillo himself was no longer the named insured. [*Id*].

Further, Penn National's description of the business form as "Individual" and continued use of the same underwriting information even after this change is insufficient to override the clear intention of the parties as expressed by the completion of the "Named Insured and Address" space on the declarations page with "JJA Construction, Inc." No reference is made to Castillo the individual or even to his fictitious business name either in the declarations page or at any other point in these Policies. Absent inserting facts from outside the four corners of the policy – that Castillo was an owner and incorporator of JJA Construction, Inc. – there is no way to construe the terms of the policy, by themselves, as conferring any of its protections to Castillo as the named insured. *See Taylor v. Taylor*, 291 S.C. 261, 264, 353 S.E.2d 156, 158 (Ct.App. 1987) ("The parol evidence rule excludes evidence giving a perfectly clear agreement a different meaning or effect from that indicated by the plain language."); *North American Rescue Products, Inc. v. Richardson*, 411 S.C. 371, 379, 769 S.E.2d 237, 241 (2015) ("[O]nly if the document itself creates an ambiguity should a court look to outside evidence to aid in interpretation."). The court therefore improperly considered outside evidence to interpret an unambiguous contract.

c. The Underwriting File Documents Do Not Establish that Castillo Intended

to Continue as a Named Insured After He Formed JJA Construction, Inc.

Even if the trial court's consideration of extracontractual evidence was proper, its findings of fact from that exploration are unsupported by the record evidence. The trial court's order makes extremely selective and misleading quotations from the change request Castillo submitted to give the appearance that he intended to continue as a named insured and that JJA Construction, Inc. was functionally the same entity as Castillo's sole proprietorship, JJA Framing. These conclusions are not supported by the facts in evidence.

Contrary to the trial court's findings, the record evidence can reasonably lead to only one conclusion: that Castillo was removing himself as an insured and instead insuring his corporation, JJA Construction, Inc. The cover memo from the Taylor Agency to Penn National accompanying the change request form clarifies that Castillo asked Penn National to change the name on the Policies from himself to "JJA Construction, Inc." [Plaintiffs' Exhibit No. 18, at p. 1]. Castillo is not listed on this page of the request. *Id*. Further, while the "Name Change Only" line of the change form is checked, a review of the information provided further down the page clarifies that (1) Castillo intended to insure only "JJA Construction, Inc." and (2) that "JJA Construction, Inc." was indeed a corporation. *Id*. at p. 2. The ownership status of "JJA Construction, Inc." is also depicted differently, as both Castillo and his son, Emilio Castillo, are shown with ownership interests in excess of 5% of voting stock. *Id*. "JJA Construction, Inc." is also shown has having 200 total shares of voting stock issued. *Id*. This information can be interpreted in only one way: that Castillo/JJA Framing and "JJA Construction, Inc." are different entities and that Castillo intended that the insured be changed to the latter. Thus, the court's reliance on the underwriting file documents is both inappropriate, given the clear terms of the contract, and unreasonable, given its complete failure to recognize the plain evidence.

Seeking to justify its finding that two separate legal entities were, in fact, the same, the trial court found "particular guidance" in *Auto-Owners Ins. Co. v. Rhodes*, 405 S.C. 584, 748 S.E.2d 781 (2013), authority which is plainly inapposite to the facts of this case. Portrait Homes Order, at pp. 19-20. *Rhodes* considered whether the sole owner and shareholder of two corporations that were both insured under an insurance policy, both of which did business under the same fictitious business name, qualified as an insured under the policy's extension of coverage for the named insured's executive officers. *Id*. at 598-600, 788-89. The insurer acknowledged the fictitious trade name of these corporations as a named insured on the policy at issue. *Id*. at 599, 789. The underlying plaintiff sued the individual owner "d/b/a" the trade name of the corporations. *Id*. at 600, 789. On those facts, the Supreme Court found that the underlying plaintiff sued the individual defendant in his "corporate capacity" such that he qualified as an insured under the policies' extension of coverage to officers without the need to analyze whether he was sued with respect to his duties as an officer or director, which the policy language otherwise required. *Id*.

Here, unlike in *Rhodes*, the court was not called upon to determine whether the sole owner of a corporation qualifies for coverage under the "Executive Officer as Insured" extension of coverage. Rather, the court's task was to determine whether Castillo qualified as the "named insured shown in the declarations" for the purposes of determining whether Portrait Homes qualified for additional insured coverage under form 71 1145. *Rhodes* does not speak at all to that inquiry. Further, the court's reliance on *Rhodes*' language refusing to create "a separate legal entity for insurance purposes" based on the "d/b/a" indication on the policy does not apply here. The evidence indisputably shows that JJA Construction, Inc. is a separate legal entity for *all* purposes, including insurance: it was an incorporated entity (versus an individual), had owners besides Castillo himself, and distinguished itself as a different entity on the policy change request.

[Defendant's Exhibit No. 62 (JJA Construction's Articles of Incorporation); Plaintiffs' Exhibit No. 18 (Policy Change Request)]. The trial court's conclusion that JJA Construction "was not a separate legal entity for any purpose, especially not for the purposes of insurance," is thus at odds with the facts in evidence and with South Carolina law. Rule 59 Order, at p. 4; *Magnum v. Maryland Cas. Co.*, 330 S.C. 573, 577, 500 S.E.2d 125, 127 (Ct. App. 1985) ("A corporation is not a natural person and maintains a distinct identity apart from its shareholders.").

Thus, the trial court's interpretation of the policy change form and underwriting documents as evincing some sort of intention to maintain Castillo as a named insured is simply unsupported by competent evidence or by South Carolina law.

d. Portrait Homes Had No Contract with JJA Construction, Inc. Even if it Did Business Under the Name JJA Framing

The trial court also improperly found that because JJA Construction, Inc. did business as JJA Framing, it was bound by the Housing and Purchase Order Agreement and Master Agreement entered into between Castillo and Portrait Homes. Portrait Homes Order, at pp. 22-25; Rule 59 Order, at p. 3. The trial court relied both on allegations in the underlying complaints and on unspecified "evidence at trial" to find that JJA Construction also did business as JJA Framing, just as Castillo had. Rule 59 Order, at p. 3.

Even when treating the allegation that "JJA Construction, Inc." did business as "JJA Framing" as true, which is not required given the nature of the claim,[11] Portrait Homes does not

[11] While South Carolina's courts have not weighed in on this issue, many jurisdictions follow the rule that allegations irrelevant to the merits of the suit against the insured need not be treated as true for the purposes of assessing the duty to defend. *See, e.g., Worthington Federal Bank v. Everest Nat. Ins. Co.*, 110 F.Supp.3d 1211, 1235 (N.D. Ala. 2015) ("Indeed, acceptance of Plaintiff's argument would nullify nearly all policy provisions under which an insurer might argue that it has no duty to defend based upon any matter collateral to the substance of the underlying complaint, such as a lack of timely notice. That is not the law."); *Pompa v. American Family Mut.*

qualify as an additional insured. Both of the contracts through which Portrait Homes seeks to establish additional insured status predate the incorporation of JJA Construction, Inc. by more than two years. [Plaintiffs' Exhibit Nos. 38 (Housing and Purchase Order Contract, dated March 6, 2002), 37 (Master Agreement, dated October 25, 2002); Defendant's Exhibit No. 62 (articles of incorporation for JJA Construction, Inc. filed December 15, 2004)]. Absent some consideration to JJA Construction, therefore, these documents could not bind JJA Construction, Inc. *Carolina Amusement Co., Inc. v. Connecticut Nat. Life Ins. Co.*, 313 S.C. 215, 220, 437 S.E.2d 122, 125 (Ct. App. 1993) (noting that "sufficient consideration" is a requirement to bind a party to a contract). Portrait Homes presented no evidence at trial that it provided any consideration to JJA Construction in order to bind it to either of these contracts.

Further, the Master Agreement – the only of the two contracts in evidence that satisfies endorsement 71 1145's requirement that completed operations coverage be requested – indicates that it bound Jose Castillo the individual and not the trade name JJA Framing. For example, the entity identified in the Master Agreement as the "Contractor" is "Jose Castillo, a Sole Proprietor." [Plaintiffs' Exhibit No. 37, at p. 1]. Also, on the signature page, the Contractor is again identified as "Jose Castillo," this time with the inclusion "DBA JJA Framing." [*Id.* at p. 4]. That styling indicates that the contract binds Castillo and not the trade name more generally. Thus, even if JJA Construction, Inc. did business under the trade name "JJA Framing," the documents fail to establish a written contract between the named insured on the policies at issue with Portrait Homes.

e. The Trial Court Improperly Relied on Certificates of Insurance to Find that Portrait Homes Qualified as an Additional Insured

---

Ins. Co., 520 F.3d 1139, 1146-49 (10th Cir. 2008) (recognizing an exception to Colorado's version of the four corners rule where the carrier's denial of a defense is premised upon an "indisputable fact that is not an element of either the cause of action or a defense in the underlying litigation").

The trial court's finding that the certificate of insurance issued for the 2005-06 Policy affords Portrait Homes additional insured status fails as a matter of fact and law is erroneous as a matter of fact and law. First, the certificate is extracontractual evidence that may not be considered in the absence of an ambiguity in the policies, which is not the case here. *Taylor*, 291 S.C. at 264, 353 S.E.2d at 158. Second, the terms of the certificate clearly indicate that it is "provided for informational purposes only" and "does not amend, extend or alter the coverage afforded" by the 2005-06 Policy. [Plaintiffs' Exhibit No. 5]; *Dan Ryan Builders W. Va., LLC v. Main St. Am. Assur. Co.*, No. 2:18-cv-00589-DCN, 2020 U.S. Dist. LEXIS 59188, at *20-21 (D.S.C. Apr. 3, 2020) (noting that disclaimers in a certificate of insurance render a purported additional insured's reliance on them for the purposes of establishing coverage is unreasonable). Last, as a matter of law, certificates of insurance do not confer any rights or otherwise affect coverage under a policy, and instead merely serve as evidence that a policy is in place. *See Campbell, Inc. v. Northern Ins. Co. of New York*, 337 F.Supp.2d 764 (D.S.C. 2004) (holding that a statement by insurance adjuster effectively expanding coverage under a policy could not operate as waiver or estoppel to deny coverage); *see also Mulvey Const. Inc. v. Bituminous Cas. Corp.*, 571 Fed. Appx 150 (4th Cir. 2014) (unpublished) (holding certificates of insurance could not be relied on to extend coverage where certificate expressly stated that it conferred no rights upon certificate holder and did not amend, extend or alter coverage); *G.E. Tignall & Co., Inc. v. Reliance Nat. Ins. Co.*, 102 F.Supp.2d 300 (D.Md. 2000) (certificate identifying general contractor as "additional insured" did not bind insurer); *Erie Ins. Exchange v. Gosnell*, 246 Md. 724, 230 A.2d 467 (1967) (where terms of certificate of coverage conflict with terms of the policy, the policy terms control). Even to the extent that reliance on the certificate was proper, the certificate was issued for the 2005-06 Policy only and does not speak to either of the other policies for which the trial court used the certificate

as an interpretation aid. Thus, the court's reliance on the certificate to extend coverage was improper legally and factually.

f. The Master Agreement Did Not Govern JJA's Work at Persimmon Hill

Even assuming *arguendo* that the trial court correctly found that Castillo, Jose Castillo d/b/a JJA Framing, and JJA Construction, Inc. are the same entity, no coverage is available to Portrait Homes under form 71 1145. The trial court found that the Master Agreement applied to the Persimmon Hill project such that Portrait Homes is entitled to additional insured coverage under the Penn National Policies through that contract, which requires JJA Construction to name it as an additional insured for completed operations under its insurance policies. Rule 59 Order, at p. 6. However, there is no evidence to support that finding and the record evidence actually shows that the opposite is true: that the Housing and Purchase Order Contract, and not the Master Agreement, defined Castillo's obligations to Portrait Homes with respect to the Persimmon Hill Project, including his insurance obligations. As noted above, the Housing and Purchase Order Contract does not require Castillo to name Portrait Homes-South Carolina, LLC as an additional insured for completed operations and, as such, is insufficient to confer coverage under the 71 1145 endorsement attached to the 2005-06, 2006-07, and 2007-08 Penn National Policies.

The undisputed evidence is that Castillo executed the Housing and Purchase Order Contract with Portrait Homes first and that his work at the Persimmon Hill Project commenced before the Master Agreement came into effect. The Housing and Purchase Order Contract is dated March 8, 2002, when Castillo executed it, while the Master Agreement became effective about six months later, in November 2002. Portrait Homes Order, pp. 5-6. The Master Agreement does not mention the Persimmon Hill project at all.

Furthermore, the Master Agreement only applies prospectively and does not impact pre-

existing Housing and Purchase Order Contracts, such as the one governing the work at Persimmon Hill. In fact, the Master Agreement is replete with terms indicating that it applied only prospectively and not retroactively, and makes clear that its superseding terms applied only to later-executed housing and purchase order contracts and had no effect on those already in effect. For example, the Master Agreement indicates in multiple places that it was executed in anticipation that the parties would execute further, project-specific purchase orders in the future. [*See, e.g.,* Plaintiff's Exhibit 37, at p. 1 ¶ 1 ("Based on the nature of the services and/or materials to be provided by Contractor, it is anticipated that specific purchase order contracts will be executed…"), ¶ 5 ("The intent is that if any services and/or materials are procured and agreed to by both parties during the term of this Agreement, the terms and conditions of this Agreement shall apply.")]. The Master Agreement also indicates that its terms apply and supersede only housing and purchase order contracts executed after it took effect. [*Id*. at ¶¶ 1 ("…however the terms of this Agreement shall prevail in the event of any conflict between the terms of this Agreement and any future purchase order contract and it being further agreed that the terms and conditions shall be incorporated into any future purchase order contract by and between the parties hereto as if this Agreement had been set forth in said purchase order contract, in its entirety."), 3 ("It is the intent of the parties that these terms and conditions apply to any provision of services and/or materials by Contractor regardless of whether these terms and conditions are referenced in any purchase order, subsequent contract memo, etc. during the term of this Agreement."). Finally, the Master Agreement indicates that it would take "full force and effect from the date of signing." [*Id*. at ¶ 4]. Thus, the term of the Master Agreement commenced when it was signed on November 5, 2002, eight months after the Persimmon Hill Housing and Purchase Order Contract was entered.

These terms allow for only one interpretation of the two contracts: that the Housing and

Purchase Order Contract continued to govern Castillo's responsibilities at the Persimmon Hill Project. The Master Agreement does not indicate that its terms apply retroactively to previously-executed purchase order agreements, such as the Housing and Purchase Order Contract at issue here. *Little v. Town of Conway*, 171 S.C. 27, 171 S.E. 447, 448 (1933) ("[T]he maxim 'Expressio unius est exclusio alterius' is thus defined: 'When certain persons or things are specified in a law, contract, or will, an intention to exclude all others from its operation may be inferred.'"); *Chapman v. Metropolitan Life Ins. Co.*, 172 S.C. 250, 173 S.E. 801, 804 (1934) (applying "Expressio unius est exclusio alterius" to interpret a contract). Portrait Homes acted consistently with this interpretation: it required Castillo to execute a new Housing and Purchase Order Contract for the Summerwood project, which had been governed by the exact same Housing and Purchase Order Contract applicable to the Persimmon Hill Project. [Plaintiffs' Exhibit Nos. 38 & 46]. Portrait Homes submitted no evidence that it did the same for the Persimmon Hill Project.

The trial court nonetheless found, without any evidence to support its finding, that "there would have been another Master Agreement in place between Portrait Homes and JJA Framing before the Housing and Purchase Order Contract was initially signed." Rule 59 Order, at p. 6. The trial court's finding was based upon testimony offered by Shawn Belcher, who served as the purchasing and estimating manager for Portrait Homes from January 2004 through June 2009. *Id*. As is evident from the court's citation to his testimony, however, the trial court's conclusion concerning Portrait Homes' practices was unwarranted, as Belcher did not begin working at Portrait Homes until more than 14 months after the Master Agreement was executed and nearly two years after the at issue Housing and Purchase Order Contract was signed. Belcher did not testify to having seen such an earlier Master Agreement or that he had personal knowledge of the company's practices and procedures before his employment began. The court's reliance on that

testimony to establish what would have occurred at the company such a significant time before was unwarranted and not supported by the evidence in the record.

The trial court's finding that the Housing and Purchase Order Contract was re-executed (and, therefore, incorporated into the Master Agreement) is similarly premised upon unreasonable construction of record evidence. Rule 59 Order, at p. 6 fn. 2. The trial court's finding was based upon the execution of two addenda revising Castillo's scope of work at the project. *Id*. The terms of the Housing and Purchase Order Contract expressly contemplated the execution of documents ancillary to it as it expressly incorporated outside documents as "written instruments of [the] Contract," including Castillo's scope of work at the project. [Plaintiffs' Exhibit No. 38, at p. 5]. This conduct – executing addenda to a previously-executed contract that specifically contemplated such addenda – can be reasonably interpreted only one way: that the parties were modifying the obligations under the existing Housing and Purchase Order Contract, not executing it anew. The trial court's conclusion otherwise was not supported by any record evidence or testimony.

Portrait Homes fails to prove that it is entitled to additional insured status under the Penn National Policies. On the first two policies, the defendants named in the Persimmon Hill Litigation (the Portrait Homes plaintiffs here) are not named as additional insureds. For the last three policies, Portrait Homes had no contract with the named insured that would satisfy the additional insured endorsements attached to those policies. Therefore, Portrait Homes is not an additional insured entitled to coverage under the Penn National Policies.

3. The Trial Court Incorrectly Concluded that Penn National Waived its Right to Contest Portrait Homes' Additional Insured Status

The trial court improperly found that Penn National waived its right to contest coverage and that such waiver operated to extend coverage to uncovered risks, in reliance on *Heritage*

Communities.[12] Portrait Homes Order, at p. 38 ("Whatever can be waived be a deficient denial letter has been waived by Penn National's denial letter. Penn National has waived the ability to assert any exclusions or limitations on coverage."). That case, however, applies explicitly to reservation of rights letters that carriers send to insureds being defended subject to their insurer's reservation of its rights to later deny coverage and initiate litigation to determine those coverage issues. *Heritage Communities*, 420 S.C. at 336-44, 803 S.E.2d at 296-301. The court reasoned that insurers should properly inform insureds that coverage was disputed, the grounds for that dispute, and that the insurer might initiate litigation to adjudicate those issues, such that insureds know of the potential conflict of interest in their defense. *Id*. The court tied the insurer's duty of disclosure of potential coverage defenses to its right to control the insured's defense, describing it as an advantage that the insured no longer enjoys in its investigation of the claim. *Id*. at 341-42, 299.

Here, the circumstances differ in two material ways. First, Penn National was denying coverage to Portrait Homes. Unlike the insured in *Heritage Communities*, therefore, Portrait Homes was not uninformed about whether Penn National disputed coverage for the claim at issue or the grounds upon which is based its denial of coverage. In other words, Penn National was disputing coverage in that letter, not reserving the right to do so at a later point in time. Penn National was also ceding any right it had to control Portrait Homes' defense. *Id*. The trial court

---

[12] Somewhat confusingly, the trial court indicated that it had not found that Penn National waived its coverage defenses in a manner that created otherwise nonexistent coverage. Rule 59 Order, at pp 12-13. As to Portrait Homes' additional insured claim, Penn National's sole coverage defense was that the additional insured requirements were not met. While Penn National did not assert that exclusions barred coverage, the trial court nonetheless extensively reviewed the waiver doctrine and found that Penn National had waived exclusions and limitations on coverage. Since it is unclear from the trial court's orders which provisions, if any, have been waived, Penn National addresses this erroneous finding out of an abundance of caution, even though it does not believe that, per the terms of the trial court's orders, its coverage defenses asserted in this action have been waived.

rejected this argument by looking to the claims practices statute. Rule 59 Order, at p. 11. However, that analysis in inapposite because it deals with what constitutes an unfair claims practice rather than what is placed at issue by *Heritage Communities*: whether a carrier may later raise a coverage defense not identified in reservation of rights correspondence with the insured. Contrary to the trial court's finding, extending waiver to the denial letter context does not allow an insurer to act with "impunity," but instead triggers potential tort liability (where the elements are satisfied) rather than operating as a waiver of coverage defenses. The differing remedy makes sense because, unlike in the reservation of rights scenario, the insured retains control of its own defense.

Second, Portrait Homes possessed information suggesting that Penn National's explanation might be incomplete at the time it received the denial letter. Indeed, at that time, Portrait Homes possessed two certificates of insurance that informed it that additional insured coverage for completed operations was provided by the policies under certain circumstances. Portrait Homes cannot now claim not to have known the grounds for the denial, that Penn National disputed coverage, or that it lost the opportunity to investigate the situation itself and prepare a defense. *Heritage Communities*, 420 S.C. at 339, 803 S.E.2d at 298; *see also Doub v. Weathersby-Breeland Ins. Agency*, 268 S.C. 319, 327, 233 S.E.2d 111, 114 (1977) (noting that an insured cannot complain of a misrepresentation of policy terms where that party possesses information contradicting the misrepresentation). Rather, Penn National's communication was clear that it was disclaiming coverage and would not be providing Portrait Homes a defense. Portrait Homes, despite possessing information that potentially contradicted Penn National's stated grounds for a defense – attached to the very documents that the trial court found to be the basis for its tender to Penn National in the first place – did not respond or challenge Penn National's determination before it initiated this litigation.

Finally, Penn National cannot be deemed to have waived policy provisions in a manner that extends coverage to risks that were not intended to be insured. *Laidlaw Environmental Servs. (TOC), Inc. v. Aetna Cas. & Sur. Co*., 338 S.C. 43, 52, 524 S.E.2d 847, 852 (Ct. App. 1999). The trial court found that the waiver doctrine applied because of the incomplete denial letter, and the only basis for denial here is that Portrait Homes failed to satisfy the additional insured provisions. Clearly, establishing that a stranger to the contract is entitled to its benefits to which it is not otherwise entitled is an extension of coverage, especially in the face of claims correspondence stating exactly the opposite, albeit with an incomplete explanation. *Id*. (quoting *Janasik v. Fairway Oaks Villas Horizontal Property Regime*, 307 S.C. 339, 344, 415 S.E.2d 384, 387 (1992) ("A waiver is a voluntary and intentional relinquishment of a known right.")). The trial court did not find that Penn National merely waived a defense to coverage, such as a condition or exclusion (because it raised none), but rather to the issue of coverage itself, an impermissible use of the doctrine. *Id*. at 53, 852 (quoting *Alverson*, 287 S.C. at 434, 339 S.E.2d at 142 ("…[w]aiver cannot create coverage and bring into existence something not covered in the policy."). Thus, Penn National did not waive its right to contest coverage by its incomplete explanation of the grounds for its denial.

4. Portrait Homes Sustained No Damages for Breach of the Duty to Indemnify Because It Was Fully Indemnified by Its Own Insurer

The trial court erroneously found that Portrait Homes sustained damages in the amount of $3.85 million, the amount of its insurer-funded settlement of the underlying litigation, as a result of Penn National's breach of duty to indemnify. The court appears to rely on the application of the collateral source rule to bar consideration of Portrait Homes' insurers based on *Otis Elevator, Inc. v. Hardin Construction Co*., 316 S.C. 292, 300, 450 S.E.2d 41, 45-46 (1994). Portrait Homes

Order, p. 47 fn. 16; Rule 59 Order, at p. 15. It is undisputed that Portrait Homes' settlement in the underlying action was wholly paid by its insurance carriers. *Id*; *see also* [Trial Transcript, Vol. 1, at 183:23-184:8].

Otis Elevator is inapplicable to the situation at bar. *Otis Elevator* was an indemnity dispute between a general contractor, Hardin Construction, and its elevator subcontractor, Otis, arising out of a personal injury suit against Otis. There, the third party plaintiff was injured on the elevator and sued Otis for redress, which Otis ultimately settled for $892,000, of which its insurer paid $250,000. *Id*. at 295, 43. Otis had previously executed an indemnification agreement by which it agreed to allow Hardin to use the elevator on a temporary basis during construction. *Id*. at 294, 43. As a part of that agreement, Hardin agreed to defend and indemnify Otis Elevator completely for any losses, damages, or claims arising out of the use of the elevator (with the exception of losses, damages, or claims arising out of Otis' acts or omissions). *Id*. Following its settlement, Otis sought to enforce its indemnity agreement against Hardin and recoup the payments it made to resolve the suit. *Id*. at 295, 43. The jury found in favor of Otis and further found that no Otis act or omission caused the claimant's injuries. *Id*. However, the trial court reduced Otis' judgment by $250,000 to account for the insurance payment made on its behalf. *Id*. The court of appeals reversed the trial court on that count, finding that Hardin should not benefit from Otis' insurance premiums. *Id*. at 300, 45. Thus, *Otis Elevator* stands for the proposition that a wrongdoer-indemnitor may not reduce its own liability to a blameless indemnitee for underlying harm caused by the indemnitor's tortious conduct based on the indemnitee's insurance payments.

Here, by contrast, Penn National is not a tortfeasor or wrongdoer accused or proved to have caused damage to the Persimmon Hill Project, unlike the defendant in *Otis Elevator*. Nor was Portrait Homes adjudicated to be blameless in causing the damage at issue, unlike Otis, which the

jury found had not acted improperly. Indeed, the testimony here suggests that Portrait Homes contributed to the damage by supplying improper building materials and failing to properly supervise subcontractors, both of which helped cause the damage at the Persimmon Hill Project. *See, e.g.* [Plaintiff's Exhibit 39, at p. 1 (paragraph 2C); Trial Transcript, Vol. 1, at 549:5-550:13]. Rather than seeking indemnity in the sense discussed in *Otis Elevator*, Portrait Homes effectively seeks coverage from Penn National as a co-insurer of a loss for which it has already been completely indemnified.

Two federal district courts that recently considered this exact argument rejected it and instead found *Otis Elevator* inapplicable to this situation. *See Pennsylvania National Mut. Cas. Ins. Co. v. Portrait Homes-South Carolina, LLC ("Oak Bluff")*, Civ. No. 3:18-CV-00561-KDB-DCK, 2019 WL 4491535, at *5-6, 2019 U.S. Dist. LEXIS 160414, at *16-19 (W.D.N.C. Sept. 18, 2019); *Summer Wood Property Owners Association, Inc. v. Pennsylvania National Mut. Cas. Ins. Co.*, Civ. No. 2:17-cv-350-BHH, 2019 WL 4415805, at *6, 2019 U.S. Dist. LEXIS 157353, at *17-18 (D.S.C. Sept. 16, 2019). In *Oak Bluff*, as was the case in the instant litigation, Portrait Homes' insurance carrier, Admiral, completely indemnified it for its settlement in the underlying action. *Oak Bluff*, 2019 WL 4491535, at *3-4. In that situation, the court found *Otis Elevator* inapplicable because neither Penn National nor Portrait Homes were in the same positions as the parties in *Otis Elevator*. *Id*. at *6. Rather, the court found that *Otis Elevator* had no application in the insurance coverage context because Penn National was not an alleged tortfeasor seeking to reduce liability caused by its own wrongdoing based upon its alleged joint tortfeasor's insurance proceeds. *Id*.

In *Summer Wood*, the court came to the same conclusion, finding that allowing Portrait Homes to collect insurance proceeds where it had not paid the indemnity itself would represent

"an unjust windfall and double recovery." *Summer Wood*, 2019 WL 4415805, at *6 (quoting *Crossmann Communities of North Carolina, Inc. v. Harleysville Mut. Ins. Co. ("Crossmann Communities")*, No. 4:09-cv-1379-RBH, 2013 WL 5437712, at *26 (D.S.C. Sept 27, 2013)). In *Summer Wood*, like here, Admiral defended Portrait Homes in the underlying litigation and funded its settlement of the claims against it. *Id*. at *3. Portrait Homes asked the court to find that the settlement, paid by its insurer, was sufficient to constitute damages supporting its breach of contract claim against Penn National. The *Summer Wood* court adopted the *Crossmann Communities* court's reasoning that the collateral source rule does not apply to breach of contract claims because the goal of contract law, putting the wronged party into the same position he would occupy had the contract been performed, differs from that of tort law, punishment for wrongdoing and deterrence from engaging in similar behavior. *Id*. at *6 (citations and quotations omitted). Thus, the court concluded – on facts identical to those at bar here – that the plaintiff could not establish damages on its breach of contract action as a matter of law. *Id*.

These recent cases align with longstanding South Carolina precedents holding that an insured who was completely indemnified and defended by another insurer sustains no recoverable damage collectible from another of its insurers that breached a duty to defend and indemnify. *See, e.g., Sloan Const. Co., Inc. v. Central Nat. Ins. Co. of Omaha*, 269 S.C. 183, 187, 236 S.E.2d 818, 820 (1977) (finding that the insured sustained no damage where one of its two insurers defended and the other refused to do so where the insured sought to collect its attorneys' fees for defending the underlying action); *Hartford Acc. & Indem. Co. v. South Carolina Ins. Co.*, 252 S.C. 428, 436, 166 S.E.2d 762, 765 (1969) (excess carrier standing in the shoes of the insured could not collect defense fees because insured did not sustain that damage where the defense was provided to it without cost); *Crossmann Communities*, 2013 WL 5437712, at *27 (D.S.C. Sept. 27, 2013) ("[T]he

policies underlying the collateral source rule are less compelling in breach of contract cases than in tort actions. Tort law's focus on punishment and deterrence favors the risk of a plaintiff's double recovery over the risk of under-deterring the defendant. Unlike in tort law, the purpose of damages in contract law is not deterrence and punishment[, but rather] to put the plaintiff in as good a position as he would have been in if the contract had been performed. … Applying the collateral source rule to contract law would contravene this principle by awarding the non-breaching party more damages than necessary to compensate it for the breach.")(internal citations and quotations omitted). In fact, the *Crossmann Communities* court extensively cited decisions from other jurisdictions refusing to apply the collateral source rule where another insurance policy indemnified the insured for defense and indemnity, calling that holding a "clear majority" rule and a "national consensus." *Id.* at *26-27.

The trial court differentiated *Sloan* and *Hartford* (and completely ignored *Summer Wood* and *Crossmann Communities*) because they arose in the duty to defend context rather than indemnity. Rule 59 Order, at pp. 14-15. However, beyond describing those duties generally, the trial court did not analyze how the duty to defend context changed the damage analysis on the breach of contract claim. Simply put, Portrait Homes has no loss – is it out only $47,000 for which it can seek recovery. If Portrait Homes' own insurer, Admiral Insurance Company, wanted to pursue an action against Penn National for contribution between the two insurers, Admiral could have done so. It did not. Thus, the trial court misapplied South Carolina law in finding that Portrait Homes sustained damages on its breach of contract claim.

5. The Trial Court Erroneously Found that Portrait Homes Proved its Bad Faith Claim

The trial court identified three behaviors to support its conclusion that Penn National acted

in bad faith: (1) failing to investigate and discover that JJA Framing and JJA Construction were the same business entity; (2) failing to respond to claim communications from Portrait Homes; and (3) noting the incorrect reason for denying the claim in its denial letter. Portrait Homes Order, at pp. 53-54; Rule 59 Order, at pp. 20-22. None of these behaviors is sufficient to uphold the claim such that entry of judgment on bad faith should be reversed.

a. Penn National's Investigation Was Not Performed In Bad Faith

First, the trial court concluded that Penn National acted in bad faith by concluding that JJA Framing and JJA Construction were not the same business entity. First, the trial court's premise – that a sole proprietorship and a corporation – were the "same business entity" is erroneous on its face and is unsupported by the factual record, as discussed at length above. Penn National's Policies after March 2005 unambiguously insured "JJA Construction, Inc." and not any other entity. The underwriting file documents to which the court alludes in its order do not change that conclusion – rather, they support Penn National's assertion that JJA Framing, a sole proprietorship, was indeed a different business entity than JJA Construction, Inc., the entity to which Castillo transferred his rights under the Penn National Policies by his March 2005 policy change request.

Second, the notion that Penn National's independent adjuster, Gayle McLeod, could have questioned Castillo about the particulars of the case during her brief interaction with him is unsupported by the evidence at trial. According to McLeod's report and testimony summarizing her meeting with Castillo, the brevity of the conversation rendered steering it into the merits of the case impossible. [Trial Transcript, Vol. 2, at 119:21-22, 120:6-8]. Further, Castillo's demeanor during the conversation – as evinced by his expressions of indifference toward the suit and contacting Penn National and unilateral termination of the meeting – further showed that attempting to ask about the case or the corporate formalities of "JJA Construction, Inc." was simply

unrealistic. [*Id*. at 93:23-96:8, 386:2-9].

Third, the trial court's finding that Portrait Homes sustained damages is unsupported. The court selectively picked pieces of evidence from Penn National's underwriting file that supported Portrait Homes' claim for additional insured coverage while ignoring the overwhelming weight of the evidence contained in that file, which supports Penn National's interpretation of the unambiguous policy language. The court's order implies, without explicitly stating, that Penn National's denial of coverage on this basis is completely attributable to its failure to consider these policy documents, but that conclusion is unsupported when the documents are taken as a whole.

Finally, the Court cited and Portrait Homes solicited no testimony to establish that Penn National's investigation or failure to question Castillo directly violated its standard of care and, therefore, constituted unreasonable conduct. Therefore, the court's finding that the investigation was in bad faith is unsupported by competent evidence in the record.

b. Penn National Did Not Fail to Respond to Claim Communications

Second, the trial court's conclusion that Penn National failed to respond to claim communications is not reasonably supported by record evidence. The trial court was presented with authenticated and undisputed evidence showing that Penn National's adjuster made at least three unanswered phone calls to Portrait Homes counsel upon its receipt of the tender letter to request additional information about the claim. [HOA Exhibit No. 4, at p. 2; Trial Transcript, Vol. 1, at 381:3-382:1, 392:17-394:4, 19-22, 399:6-21]. The trial court's factual finding that Penn National "took nearly seventeen (17) months from the time of Portrait's first tender" to respond to the tender is unsupported by the record and therefore cannot form the basis for this bad faith claim.

Moreover, Portrait Homes cannot and did not show (and the trial court did not find) that it sustained any damage as a result of this purported delay. *Howard*, 316 S.C. at 451, 450 S.E.2d at

586; *Nichols*, 279 S.C. at 340, 306 S.E.2d at 619. During the entirety of the delay, Portrait Homes was being defended by its insurers, the same carriers who ultimately funded its settlement in the case. [Trial Transcript, Vol. 1, at 183:23-184:8]. Thus, even if this conduct occurred and was unreasonable, no evidence supports damages, a required element of the claim.

c. Penn National's Incomplete Statement of the Grounds for Denial Does Not Support the Bad Faith Claim

The uncontested evidence at trial is that the statement in Penn National's denial letter was a simple mistake. There is no evidence to show that this statement was made in bad faith. To the contrary, all Penn National testimony and documentary evidence on the subject shows that Penn National's intention was to explain that the completed operations endorsements that were attached to the policies at issue did not operate to extend coverage based on the facts and circumstances in the case. [Trial Transcript, Vol. 1, at 424:1-425:6; Vol. 2, at 80:8-81:2; 163:9-165:2; 171:9-172:25]. Thus, the trial court's finding that the incomplete denial letter satisfies the bad faith conduct element of the claim is erroneous.

Furthermore, even if the denial letter was unreasonable, the trial court made no findings to show how Portrait Homes was damaged by the letter. *Crossley*, 307 S.C. at 359-60, 415 S.E.2d at 396-97. Portrait Homes possessed documents suggesting the statement was erroneous at the time it received the letter, including copies of the additional insured endorsements at issue, yet Portrait Homes failed to respond to the letter, even at Penn National's invitation to do so. [Plaintiffs' Exhibit Nos. 7 (Certificate of Insurance for 2004-05 Policy), 5 (Certificate of Insurance for 2005-06 Policy), 9 (Denial Letter dated September 30, 2014)]. While such a failure would not excuse unreasonable or bad faith conduct by an insurer, Portrait Homes' silence while possessing contradictory information certainly weighs against any notion that it was damaged by Penn

National's erroneous statement in the denial letter. *Doub*, 268 S.C. at 327, 233 S.E.2d at 114 (noting that an insured cannot complain of a misrepresentation of policy terms where that party possesses information contradicting the misrepresentation). Moreover, as explained above, Portrait Homes does not qualify as an additional insured based on the language of the Policies and its contracts with JJA, so Portrait Homes sustained no damage from the letter itself.

6. No Competent Evidence Supports the Trial Court's Finding of Willful Conduct or Reckless Disregard in Support of the Punitive Damages Award

There is no record evidence from which the trial court could properly conclude that Penn National made a conscious decision to deny Portrait Homes its rights, as is required to impose punitive damages. As noted above, to prove a claim for punitive damages, the insured must show some conscious recognition by the insurer that the insured's rights under the policy are being disregarded. *Yaun*, 243 S.C. at 419, 134 S.E.2d at 251; *Crossley*, 307 S.C. at 360, 415 S.E.2d at 397; *Kuznik*, 342 S.C. at 611, 538 S.E.2d at 32.

No competent evidence supports the court's finding that Penn National intentionally or recklessly failed to fully investigate the claim. The trial court seems to conclude that had Penn National properly investigated its underwriting file and questioned Castillo about the structure of his businesses, it could have come to no other conclusion than that Portrait Homes was an additional insured. Rule 59 Order, at p. 47-48. First, as extensively described above, the conclusion that JJA Construction, Inc. was bound by contracts entered into by one of its individual owners years before its incorporation (or that JJA Framing, a sole proprietorship, is the "same business entity" as a corporation) is legally unsupportable. Second, there is no evidence that these supposed investigation failures were made deliberately or in reckless disregard of Portrait Homes' rights. As regards the underwriting file documents, Greg Gross, the Penn National adjuster assigned to the

claim, testified that he did review these documents. [Trial Transcript, Vol. 1, at 229:12-23]. This testimony conflicts with the court's unsupported finding that Penn National undertook "no meaningful efforts…to review or consider any of [the underwriting file's] contents." Portrait Homes Order, at p. 53; Rule 59 Order, at p. 48. As discussed above, the underwriting file in fact does not "conclusively [show] that Portrait should have been treated as an additional insured under the policies." *Id*.

Further, McLeod's failure to ask Castillo about the particulars of the claim during her meeting with him does not support a finding of willfulness or reckless disregard of rights. Given the context of the conversation and the undisputed fact that Castillo ended the conversation by walking away from McLeod [Trial Transcript, Vol. 2, at 93:23-96:8, 119:21-22, 120:6-8], there is no evidence to support the conclusion that McLeod intentionally decided not to ask him questions in order to prejudice Portrait Homes' rights under the policy or that Penn National ordered her not to undertake such an investigation.

Penn National's denial letter also does not support a finding of willfulness or reckless disregard of Portrait Homes' rights. Gross, the letter's author, never testified that his misstatement in the letter was deliberate or written consciously with the knowledge that he was violating Portrait Homes' rights. Rather, Gross acknowledged that he knew that the statement in his letter was incorrect at the time of trial – far removed from the time at which willfulness or reckless disregard are measured. [Trial Transcript, Vol. 1, at 434:20-23 ("…And *sitting here today right now* you know that's not right? A: That's correct.") (emphasis added)]; *Howard*, 316 S.C. at 448, 450 S.E.2d at 584 ("Whether an insurance company is liable for bad faith must be judged by the evidence before it at the time it denied the claim…"). Penn National's internal documents indicate its intention to communicate an accurate message to the insured. In his emails to Gross, Parsons (Penn

National staff claims counsel) indicated that JJA Construction, Inc. had no contract with Portrait Homes sufficient to trigger additional insured coverage, showing that Penn National in fact analyzed the provisions under which Portrait Homes sought coverage and found them not satisfied by the facts of the claim. [Penn National Exhibit No. 78, at pp. 1-2].

Finally, the trial court's conclusions about Penn National's request for a coverage question report ("CQR") forming the basis for a punitive damages award are unsupported. Rule 59 Order, at pp. 44-45. In fact, the claims log notes suggest no such deliberate or conscious attempt to deny Portrait Homes policy benefits. Rather, the undisputed evidence at trial was that Penn National's basis for denying the claim was its full review of the contracts and additional insured endorsements, discussed at length at trial. [*Id*. at p. 10; Trial Transcript, Vol. 1, at 424:1-425:6; Vol. 2, at 80:8-81:2; 163:9-165:2; 171:9-172:25].

Thus, the evidence elicited at trial fails to support the court's conclusion that Penn National engaged in willful conduct or reckless disregard of Portrait Homes' rights. Accordingly, Penn National respectfully requests that the court overturn the award of punitive damages.

Issues Common to Portrait Homes and the HOA

1. The Trial Court Failed to Apply the Supreme Court's Time-On-Risk Formula for Apportioning Damages to Penn National's Policy Periods

The trial court applied a "modified" time on risk analysis that it found was merited based upon different policy language than that used in the Supreme Court's *Crossmann II* decision, the supposed lack of evidence to differentiate between covered and non-covered claims, and on its finding that Penn National's breach of the duty to defend operated as a waiver of the time-on-risk allocation. Rule 59 Order, at pp. 17-20, 34-37. The court attached an exhibit to its Rule 59 Order showing the allocation, but the court did not explain the method for its allocation. The trial court

lacked any basis to depart from the time-on-risk formulation from the Supreme Court in *Crossmann II* and the order should be reversed.

The Supreme Court unambiguously adopted a time-on-risk approach in "defining the scope of each CGL insurer's obligation to its insured in a progressive damage case." *Crossmann Cmtys. of N.C. v. Harleysville Mut. Ins. Co.*, 395 S.C. 40, 66-67, 717 S.E.2d 589, 603 (2011) ("*Crossmann II*"). The Supreme Court explained that, while it would be "ideal … to determine precisely how much of the injury-in-fact occurred during each policy period and precisely what quantum of the damage award" is attributable to a particular policy, that it is "often both scientifically and administratively impossible to make such determinations." *Id*. at 64, 601 (citations and quotations omitted). The court found that the time-on-risk approach furthered important policy goals, such as encouraging businesses to purchase sufficient insurance to cover risks of progressive damage, and avoiding situations where a single policy is responsible for the entire progressive damage reaching across the effective periods of multiple policies. *Id*. at 62-63, 600-01.

The trial court applied its "modified" time-on-risk analysis based upon the inclusion of a clause in the insuring agreement stating that "'property damage' which occurs during the policy period…includes any continuation, change or resumption of that 'property damage' after the end of the policy period." Portrait Homes Order, at p. 49; Rule 59 Order at pp. 18, 35. The trial court justified its departure from governing Supreme Court precedent by noting that there were no decisions "in South Carolina or anywhere else in the country rejecting [its] modified time on risk analysis." Rule 59 Order, at p. 18. However, the court does not explain how the additional policy language changes the time-on-risk analysis or the justifications for rejecting Supreme Court precedent. Rather, the trial court simply applied its modified analysis without explanation.

In fact, courts in South Carolina and around the country have continued to apply the pro

rata time on risk allocation method even with the change in policy language. *See Builders Mut. Ins. Co. v. Lacey Const. Co., Inc*., C.A. No. 3:11-cv-400-CMC, 2012 WL 1032539, at *12 (D.S.C. March 27, 2012) (noting that the insurer would be responsible for the portion of damages that occurred during its time on the risk where policies at issue were issued beginning in 2002); *Crossmann Communities*, 2013 WL 5437712, at *18 (finding that "[n]o exclusion in the Harleysville Policy bars coverage, and Harleysville must indemnify in accordance with the *pro rata* time-on-risk method"); *Heritage Communities*, 420 S.C. 321, 348-57, 803 S.E.2d 288, 303-09; *see also, e.g., Air Master & Cooling, Inc. v. Selective Ins. Co. of America*, 452 N.J. Super. 35, 171 A.3d 214 (App. Div. 2017) (applying time-on-risk approach to a construction defect claim on commercial general liability policies effective between 2009 and 2012).

To the extent the court believes that the policy language compels a different approach than time-on-risk, the plain language of the statute suggests adoption of the injury-in-fact approach previously used in South Carolina. *See, e.g., Century Indem. Co. v. Golden Hills Builders, Inc*., 348 S.C. 559, 564, 561 S.E.2d 355, 357-58 (2002). In *Century*, the court determined that all property damage occurs (and the policy then in effect is triggered) "when the damage can be shown in fact to have first occurred." *Id*. at 564, 357. As a result, the *Century* court found "the insurance policy [in effect at the time property damage commences] provides coverage for property damage that occurred during the policy period <u>and</u> for any continuing damage." *Id*. at 564, 358 (emphasis in original).

Here, the Penn National Policies specifically state that any property damage that first occurs during its effective period "includes" all "continuation" of that property damage. In effect, that phrase indicates an adoption of the injury-in-fact trigger used in *Century* because it has the effect of deeming all continuous property damage as occurring within a single policy period. *See,*

Joe Harden Builders v. Aetma Cas. & Sur. Co., 326 S.C. 231, 236, 486 S.E.2d 89, 91 (1997). Therefore, where, as here, continuous property damage is at issue, the added policy language would trigger only the policy on the risk at the time that physical injury occurred, not later-in-time policies.

Thus, to the extent that the added policy language negates application of the Supreme Court's modified trigger time-on-risk analysis, the trial court should have applied the test described in *Century* as the injury-in-fact trigger of coverage, with all continuous property damage attributed to the policy in effect at the time of the beginning of the physical injury. The impact of this is that Portrait Homes and/or Castillo could only recover one policy limit of $500,000. There is no basis in law, fact, or logic in which the trial court did here – awarding multiple policy limits over many years while **rejecting** a continuous trigger of coverage.

2. The Trial Court Improperly Awarded Portrait Homes and the HOA Attorneys' Fees

The trial court improperly awarded both the HOA and Portrait Homes their attorneys' fees in violation of the established standards under South Carolina law for doing so. A victorious party in a civil action may not collect its attorneys' fees unless authorized to do so by statute or contract. *Jackson v. Speed*, 326 S.C. 289, 307, 486 S.E.2d 750, 759 (1997). The South Carolina Supreme Court has held that in a limited situation, an insurer in breach of its defense obligations to the insured must pay the insured's reasonable attorneys' fees. *Hegler v. Gulf Ins. Co.*, 270 S.C. 548, 550-51, 243 S.E.2d 443, 444-45 (1978). In *Hegler*, at issue was "whether an insured is entitled to recover attorney's fees incurred by him in the successful defense of a declaratory judgment action brought by the insurer in an effort to relieve itself of coverage under an automobile insurance policy." *Id.* at 443, 548. In that situation, the court found the insurance contract authorized the

award of attorneys' fees as a result of the duty to defend language contained in the standard policy form and the insurer's breach of that obligation. *Id*. at 549-50, 444. The court also implied that an insured who was wrongfully denied a defense by its carrier could collect the defense fees it incurred in defending the lawsuit at issue. *See id* at 550, 444. ("If [the insurer] had refused to initially defend, it would undoubtedly have been liable for the payment of counsel fees incurred by appellant in the defense of the damage action."). South Carolina courts "have not awarded attorneys' fees as consequential damages in [insurance bad faith] tort actions." *Liberty Mut. Fire Ins. Co. v. J.T. Walker Indus., Inc*., 554 Fed. App'x 176, 191 (4th Cir. 2014) (applying South Carolina law).

a. Castillo and JJA Construction Incurred No Attorneys' Fees

Castillo and JJA Construction, Inc., the insureds under the policies through whom the HOA's rights flow, did not incur any attorneys' fees with respect to the underlying action. In *Hegler*, the court sought to avoid awarding the policyholder merely a Pyrrhic victory where its defense costs that should have been paid by its insurer were the same as the attorney's fees spent litigating a coverage action to establish the insurer's duty to defend. *Hegler*, 270 S.C. at 550, 243 S.E.2d at 444. In that scenario, the insured really "won" nothing because it spent the same money recovering its defense fees as it incurred defending the underlying suit. Here, however, unlike in the situation described by the *Hegler* court, Castillo and JJA incurred no attorneys' fees in defending the underlying action. Instead, they simply elected not to respond to the suit and the court entered default judgment against them. Further, the court's judgment fully indemnifies Castillo and JJA Construction, Inc. Awarding attorneys' fees to Castillo or the HOA, the party standing in his shoes, would reimburse them for an expense they never incurred, resulting in a windfall.

b. Penn National Owed the HOA No Duty to Defend

Penn National owed the HOA no duty to represent it in the underlying action and *Hegler* therefore does not apply to its claims against Penn National here. *Hegler* may allow insureds to collect attorneys' fees where the insurer wrongfully breaches the duty to defend and the insured incurs defense costs in defending itself against a covered claim. *Hegler*, 270 S.C. at 550-51, 243 S.E.2d at 444-45. Here, the HOA is not the insured and so it has no independent right to fees under *Hegler*. Further, since the HOA's right to fees is derivative of Castillo and JJA Construction, Inc., each of whom themselves incurred no attorneys' fees in the underlying action, the HOA has no right to collect attorneys' fees. *Hartford*, 252 S.C. at 436, 166 S.E.2d at 765 (holding that a transferee of an insurance policy has no greater rights than the transferor).

Further, the HOA's request for an additional 33% contingency fee goes far beyond the scope of *Hegler*. As noted above, *Hegler* allows the insured to collect its reasonable defense fees against an insured's declaratory relief action. *Hegler*, 270 S.C. at 550-51, 243 S.E.2d at 444-45. Here, by contrast, the HOA asks that the court award it fees for prosecuting another action in an amount that almost certainly exceeds the amount it expended in doing so. *Compare*, Affidavit of Stanley C. Rogers (noting that counsel for Portrait Homes spent 960.8 hours on this matter for a total bill of $234,987.50, exclusive of costs) *with* Affidavit of John T. Chakeris In Support of Claim For Attorneys' Fees and Case Costs (noting that the HOA's attorneys expended "significant" time on the case and their contingency fee arrangement, which would award them approximately $1.7 million in fees). *Hegler* does not stand for the proposition that such an award is allowable or appropriate under these circumstances, and South Carolina courts have not awarded attorneys' fees as damages in bad faith actions. *J.T. Walker*, 554 Fed. App'x at 191. Thus, the trial court improperly awarded the HOA attorneys' fees.

c. Portrait Homes Was Defended in the Underlying Case and Does Not Satisfy the Requirements of Hegler

Unlike the hypothetical insured in *Hegler*, Portrait Homes was provided a defense in the underlying action, albeit by a different insurance carrier. Thus, unlike the situation contemplated in *Hegler*, where the court saw itself as compensating the insured for a consequential loss arising from the insurer's breach of the contract, here Portrait Homes sustained no such damage.

Further, South Carolina does not allow one insurance carrier to seek contribution from another with respect to fees and costs expended in defense of an action that both insurers are obligated to defend. *Sloan*, 269 S.C. at 186, 236 S.E.2d at 820 ("The duty to defend is personal to both insurers. The obligation is several and the insurer is not entitled to divide the duty nor require contribution from another absent a specific contractual right."). Allowing Portrait Homes to collect its fees here would effectively circumvent this longstanding prohibition, as it would allow an insurer to prosecute an action in the name of its indemnified insured in order to collect defense fees expended in defending that insured in covered litigation. Portrait Homes' affidavit suggests that Admiral, and not Portrait Homes, retained counsel to prosecute the action on its behalf. *See* Rogers Affidavit, at Ex. 1 (displaying Admiral Insurance Company and Admiral's claim number on all bill summaries). Thus, the court should decline to award fees here as violating South Carolina's prohibition on insurer contribution actions.

CONCLUSION

After being served with the Persimmon Hill construction defect lawsuit, Jose Castillo failed to communicate with Penn National in any way and failed to request a defense in that lawsuit. Penn National could have, under South Carolina law, simply done nothing more due to the insured's breach of its policy obligations and the resulting prejudice to Penn

National. However, Penn National knew about the lawsuit and so Penn National actually did more, hiring an independent adjuster to go to Castillo's' home on multiple occasions to track Castillo down and to make sure he understood the import of his failure to communicate with his insurer. Castillo responded by affirmatively, and unequivocally, stating that he did not want a defense from Penn National in the Persimmon Hill construction defect lawsuit, a fact that Castillo reiterated in his trial testimony below. That should have been the end of the story. An insurer cannot defend a wholly uncooperative insured and one with which neither the insurer nor its assigned defense counsel can communicate. However, the trial court engaged in conjecture about what else Penn National "could have done," without a proper evidentiary basis and in disregard of established South Carolina law.

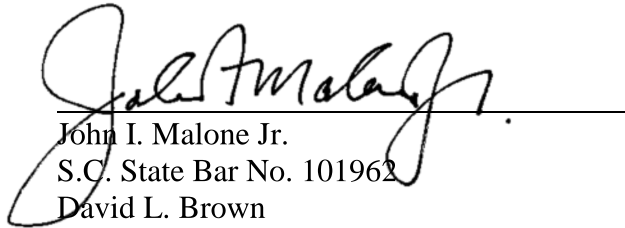
With regard to the claim by Portrait Homes for "Additional Insured" coverage under the policies issued by Penn National to Castillo, that coverage is governed by the endorsements themselves and, in later policy years, also by the contracts between Castillo and Portrait Homes. In the first two policies with "Additional Insured" endorsements, none of the Portrait entities actually sued in the Persimmon Hill construction defect lawsuit were covered. In the later three policy years, the "Additional Insured" coverage forms applied only if there was (a) a contract to provide such coverage in place between JJA Construction, Inc. (the named insured on those policies) and Portrait Homes and (b) if such contract required JJA Construction, Inc. to procure "completed operations" coverage (i.e. the kind of coverage that would apply to construction defect type lawsuits) for Portrait Homes. Neither condition was satisfied here. There was no contract in place between JJA Construction, Inc. and Portrait Homes and the purported contract did not require Castillo (or JJA Construction, Inc.) to get "completed operations" coverage for Castillo, much less for Portrait Homes. In an effort to avoid the plain language of the policies and the contracts, the

trial court relied on extensive, inadmissible "parol evidence" to "find" coverage where none existed under the plain policy terms. Not only was this effort in direct contravention of established South Carolina law, but so was the effect – to award coverage to a Portrait Homes entity that had already been fully defended and indemnified by its own insurer.

Based on the foregoing, this Court should vacate the judgment in favor of the Persimmon Hill HOA, as assignee of Castillo, and remand for entry of judgment in favor of Penn National due to Castillo's breach of his policy conditions, consistent with longstanding South Carolina law. This Court should also vacate the judgment in favor of Portrait Homes and remand for entry of judgment in favor of Penn National under the plain language of the "Additional Insured' endorsements and, separately, due to the fact that Portrait Homes sustained no damages given that it was fully defended and indemnified by its own insurer. Furthermore, even if this Court should affirm the finding of coverage in any respect, this Court should nonetheless vacate the judgment finding "bad faith" and awarding punitive damages in light of the fact that Penn National's coverage decisions as described above were reasonable and based on a good faith view of existing law.

Finally, even if this Court should affirm the finding of coverage in any respect, then the Court should vacate the existing award of damages and remand to the trial court for a proper determination of damages otherwise covered under the policies and a proper allocation of covered damages consistent with existing Supreme Court precedent.

July 13, 2020.



John I. Malone Jr.
S.C. State Bar No. 101962
David L. Brown
GOLDBERG SEGALLA LLP
701 Green Valley Road, Suite 310
Greensboro, North Carolina 27408
(336) 419-4900
Attorneys for Appellant Pennsylvania National Mutual Casualty Insurance Company

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Initial Brief Of Appellant was served on all counsel of record by electronic mail and by depositing a copy of the same in an official depository of the United States Mail in a postage-paid envelope addressed as follows:

Stanley C. Rodgers
LAW OFFICE OF STANLEY C. RODGERS
55 Broad Street, Suite 200
Charleston, South Carolina 29401
(843) 958-9881
Attorney for Respondents Portrait Homes – South Carolina, LLC and Portrait Homes – Persimmon Hill, LLC

John T. Chakeris
Alicia D. Petit
THE CHAKERIS LAW FIRM
231 Calhoun Street
Charleston, South Carolina 29401
(843) 853-5678

RECEIVED
Jul 13 2020
SC Court of Appeals

Phillip W. Segui, Jr.
SEGUI LAW FIRM, P.C.
864 Lowcountry Boulevard, Suite A
Mt. Pleasant, South Carolina 29464
(843) 884-1865
Attorneys for Respondent The Persimmon Hill Homeowners Association, Inc.

This the 13th day of July, 2020.

John I. Malone Jr.
S.C. State Bar No. 101962
David L. Brown
GOLDBERG SEGALLA LLP
701 Green Valley Road, Suite 310
Greensboro, North Carolina 27408
(336) 419-4900
Attorneys for Appellant Pennsylvania National Mutual Casualty Insurance Company
Facsimile: 336-419-4950
Attorney for Defendant-Appellant