EDGEFIELD COUNTY
CLERK OF COURT
SHIRLEY F. NEWBY
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STATE OF SOUTH CAROLINA) IN THE COURT OF COMMON PLEAS
)
COUNTY OF EDGEFIELD)

Civil Action No. 2011-CP19-00269

Dennis W. and Deborah C. Doerr, Robert and Linda K. Bishop, and William J. and Gayle G. Garry, Individually and as Class Representatives of a Class of Similarly Situated Persons,

Plaintiffs,

vs.

Mount Vintage Plantation Golf Club, LLC and Talmadge Knight,

Defendants.

ORDER GRANTING DEFENDANTS MOTION TO DISMISS PURSUANT TO SCRCP RULE (12)(b)(6)

THE ABOVE IS A TRUE COPY OF THE ORIGINAL WHICH IS ON FILE IN THE OFFICE OF THE CLERK OF COURT OF EDGEFIELD COUNTY, SC

Shirley F. Newby

8-9-12
DATED

SHIRLEY F. NEWBY, CLERK OF COURT
OF GENERAL SESSIONS AND
COMMON PLEAS, E.C.S.C.

This is a dispute over special assessment fees applied to transferable permanent golf club memberships. Plaintiffs filed a Summons and Complaint alleging a cause of action for violation of the South Carolina Uniform Securities Act, Section 35-1-101, et. seq. of the Code of Laws of South Carolina, 1976, as amended. Plaintiffs are represented by Edwin Russell Jeter of Jeter & Williams, P.A. Defendants are represented by Robert E. Stepp and Bess J. DuRant of Sowell Gray Stepp & Laffite, L.L.C. On November 11, 2011, Defendants filed a motion to dismiss for failure to state a claim pursuant to Rule 12(b)(6) of the South Carolina Rules of Civil Procedure, arguing that the golf club memberships in question are not securities for the purposes of the South Carolina Uniform Securities Act, that the plaintiffs have failed to allege fraud with any particularity and/or pursuant to Rule 9(b) SCRCP, and that the complaint against Defendant Knight should be dismissed because plaintiffs failed to sufficiently allege any primary violation of the South Carolina Uniform Securities Act and that therefore plaintiffs' claim based on controlling person liability must fail and that plaintiffs have failed to make sufficient allegations that Defendant Knight was a controlling person

subject to liability under S. C. Code 35-1-509(g)(1). Plaintiff filed a motion to certify a class of similarly situated individuals pursuant to Rule 23 of the SCRCP. For reasons following, Defendant's Motion to Dismiss pursuant to Rule 12(b)(6) of the SCRCP is **GRANTED**. Based on the Court's granting Defendant's 12(b)(6) motion, the Court declines to address class certification pursuant to SCRCP Rule 23.

FACTS

Mount Vintage Plantation is a residential development located in Edgefield County, South Carolina, consisting of a number of residential home sites and amenities, including the Mount Vintage Plantation Golf Course ("MV Golf Course"). Upon information and belief MV Golf Course was at all relevant times owned and operated by Mount Vintage Plantation Golf Club, LLC ("MVLLC"), a South Carolina limited liability company which is owned, controlled and/or managed by Defendant (Talmadge) Knight. As part of the promotion of Mount Vintage Plantation development project to the general public Defendant Knight, either individually and/or by and through MVLLC offered non-equity golf memberships in the Mount Vintage Plantation Golf Club ("MV Golf Club") to purchasers of real property within the development. MV Golf Club is not incorporated and owns no interest in MVLLC or MV Golf Course; it merely consists of property owners within the development who chose to purchase a membership to play golf. Memberships were sold for $7,500.00, more or less. The Plaintiffs herein purchased a membership in the MV Golf Club and paid an additional $2,000.00 to upgrade their membership to "Permanent Membership" in the MV Golf Club. Membership holders were granted the right to pay dues and subsequently use the MV Golf Course; "Permanent Membership" was represented to carry with it all of the benefits of membership with the added benefit that the "Permanent Membership" was

transferable to the future purchaser of the (permanent) member's property within the development upon terms which might result in a profit for the transferor.

Plaintiffs allege the "Permanent Memberships" in the MV Golf Club constitute securities as defined in the South Carolina Uniform Securities Act, Section 35-2-101(29), South Carolina Code of Laws, 1976 as amended (¶14,Complaint). Although required to be registered with the South Carolina Secretary of State, the "Permanent Memberships" offered by the Defendants in the MV Golf Club were not so registered and were not otherwise exempt from registration (¶15, Complaint).

The Plaintiffs purchased "Permanent Memberships" and received "Certificate[s] of Permanent Membership" as evidence of such. Plaintiffs allege they were not told that there would be any future requirement to pay additional fees to retain membership, only those fees and dues to the MV Golf Course. On or about July 19, 2010, MV Golf Club issued a special assessment in the amount of $4,600.00 against each development resident holding a Permanent Membership and $800 from each non-resident holding a Permanent Membership. Plaintiffs refused to pay and were then told that if they failed to pay the special assessment their "Permanent Memberships" in MV Golf Club would be forfeited. Plaintiffs were subsequently banned from the MV Golf Club thereby deprived of their "Permanent Membership" in the MV Golf Club. This suit followed.[1]

[1] Plaintiffs' Memorandum in Opposition to Motion to Dismiss alleges facts beyond the pleadings, inter alia, ...the Defendants sold permanent memberships in the golf club which were different from most golf club memberships in that it involved the opportunity to make a profit; in referring to Defendant Talmadge Knight as "one of two owners"; upon sale of the real property by the permanent member specially, one-third of the then current price of membership would have to be paid as a transfer fee to allow the home purchaser to become a member, which left the Plaintiffs and the purported class members with the opportunity to make a profit by setting a sales price of the transferrable membership for an amount between one-third of the then current price and the full current price. As an example, if a membership and permanent membership was purchased for $10,000.00 and appreciated in value to $30,000.00 at the time of the transfer upon purchase of the home, the seller's sunk costs would be $10,000.00, the transfer fee would be $10,000.00, and the permanent member could make a profit if he sold the membership for any amount over $20,000.00 up to $30,000.00. Further Plaintiffs allege the "offering materials" were misleading. These allegations from the Plaintiffs' Memo are beyond the scope of the pleadings and as such not within the standard the Court is directed to follow when ruling on a (12)(b)(6) motion.)

APPLICABLE LAW

I. Rule 12(b)(6) Standard of Review

When reviewing a motion to dismiss for failure to state a claim, the Court must base its ruling solely on allegations set forth in the complaint. HHHunt Corp. v. Town of Lexington, 389 S.C. 623, 631-32 669 S.E.2d 699, 703 (Ct. App. 2010); Doe v. Marion, 373 S.C. 390, 645 S.E.2d 245,247 (2007). The court must consider whether the facts and inferences drawn from the facts alleged in the complaint, viewed in the light most favorable to the plaintiff, state any valid claim for relief. Brazell v. Windsor, 384 S.C. 512, 515, 682 S.E.2d 824, 826 (2009). "Pleadings in a case should be construed liberally so that substantial justice is done between the parties. Further, a judgment on the pleadings is considered to be a drastic remedy". Russell v. City of Columbia, 305 S.C. 86, 89, 406 S.E. 2d 338, 339 (1991). On a 12(b)(6) motion the court is required to presume all well plead facts, not propositions of law, to be true Morrow Crane Co. v. T. R. Tucker Constr. Co. 296 S.C. 427, 429, 373.

II. Rule 9(b) SCRCP

(b) Fraud, Mistake, Condition of Mind. In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. The elements of fraud are 1) a representation, 2) its falsity, 3) its materiality, 4) either knowledge of its falsity or a reckless disregard of its truth or veracity, 5) intent that the representation be acted upon, 6) the hearer's ignorance if its falsity, 7) the hearer's reliance of its truth, 8) the hearer's right to rely thereon; and 9) the hearer's consequent and proximate injury.

As long as the complaint sets forth the basis for an action in fraud, it may not be necessary to list the nine elements explicitly. Eskew v Life Ins. Co. of Virginia, S.C. 515, 3 S. E. 2d 251 (1939), overruled on other grounds, Crystal Ice. Co. v. First Colonial Corp., 273 S.C. 306, 257 S. E. 2d 496 (1979). It is not necessary to plead fraud in haec verba. Eskew,at 255.[2]

III. **South Carolina Uniform Securities Act**

The term "security" is defined in the South Carolina Uniform Securities Act in Section 35-1-102(29) of the South Carolina Code of laws as follows:

> "Security" means any note; stock; treasury stock; security future; bond; debenture; evidence of indebtedness; certificate of interest or participation in a profit-sharing agreement; collateral trust certificate; preorganization certificate or subscription; transferable share; investment contract; voting trust certificate; certificate of deposit for a security; fractional undivided interest in oil, gas, or other mineral rights; put, call, straddle, option, or privilege on a security, certificate of deposit, or group or index of securities, including an interest therein or based on the value thereof; put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency; or, in general, an interest or instrument commonly known as a "security"; or a certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing. The term:
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> **(D)** includes an investment in a common enterprise with the expectation of profits to be derived primarily from the efforts of a person other than the investor and a "common enterprise" means an enterprise in which the fortunes of the investor are interwoven with those of either the person offering the investment, a third party, or other investors; and
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> **(E)** "Investment contract" may include, among other contracts, an interest in a limited partnership and a limited liability company and shall include an investment in a viatical settlement or similar agreement.

South Carolina Code of Laws.

The term "security" includes, among other things, a "transferable share" or "investment contract[.]" S.C. Code Ann. § 35-1-102(29). The term "includes an investment in a common enterprise with the expectation of profits to be derived primarily form the efforts of a person other

[2] "in these words", which refers to stating the exact language of an agreement in a complaint or other pleading rather than attaching a copy of the agreement as an exhibit incorporated into the pleading

than the investor", where a common enterprise is "an enterprise in which the fortunes of the investor are interwoven with those of either the person offering the investment, a third party, or other investors[.]" S.C. Code Ann. § 35-1-102(29)(D). An "investment contract" can include "an interest in a limited partnership and a limited liability company and shall include an investment in a viatical settlement or similar agreement." S.C. Code Ann. § 35-1-102(29)(E). The state definition of "security" is largely identical to that of federal securities law. S.C. Code Ann. § 35-1-102, n.28. "State courts interpreting the Uniform Securities Act definition of a security have often looked to interpretations of the federal definition of security." Id.

Historically, the term "investment contract" is undefined by the (Federal) Securities Act of 1933 or by relevant legislative reports. But the term was common in many state "blue sky" laws in existence prior to the adoption of the federal statute and, although the term was also undefined by the state laws, it had been broadly construed by state courts so as to afford the investing public a full measure of protection.[3] Form was disregarded for substance and emphasis was placed upon economic reality. An "investment contract" thus came to mean a contract or scheme for "the placing of capital or laying out of money in a way intended to secure income or profit from its employment." State v Gopher Tire and Rubber Co., 146 Minn. 52, 56, 177 N.W. 937, 938; SEC Commission v W. J. Howey, et.al. 66 Sup Ct. 1100, 1102 (1946).

In determining whether a particular investment constitutes a security, Courts look at the economic realities of the transaction, and not the label of the transaction. Garrett v. Snedigar, 293 S.C. 176, 181, 359 S.E.2d 283, 286 (Ct. App. 1987), overruled on other grounds, Olson v. Faculty House of Carolina, Inc., 354 S.C. 161, 580 S.E.23 440 (2003). "The question is whether an

[3] The name that is given to the law indicates the evil at which it is aimed, that is, to use the language of a cited case, "speculative schemes which have no more basis than so many feet of 'blue sky'; or, as stated by counsel in another case, 'to stop the sale of stock in fly-by-night concerns, visionary oil wells, distant gold mines and other like fraudulent exploitations.' " The Trading Stamp Cases, 240 U.S. 342, 391.

investor, as a result of the investment agreement itself or the factual circumstances that surround it, is left unable to exercise meaningful control over his investment." Robinson v. Glynn, 349 F.3d 166, 170 (4th Cir. 2003).

The test for determining whether an investment contract exists in South Carolina is set forth in Securities and Exchange Comm'n v. Howey, 328 U.S. 293 (1946). Under Howey, an investment contract exists where there is (1) an investment of money, (2) in a common enterprise, (3) with an expectation of profits garnered solely from the efforts of others. Majors v. S.C. Sec. Comm'n, 373 S.C. 153, 164, 644 S.E.2d 710, 716 (2007). To satisfy the first element, the investor must have "committed his assets to the enterprise in such a manner so as to subject himself to financial loss." Id. The second element is satisfied if "the promoter's gain is contingent on the investor's gain . . . ." Id. at 166, 644 S.E.2d at 717. The third element is fulfilled if the managerial efforts guiding the enterprise to success or failure are assumed by the promoter and not the investors. Id. at 167, 644 S.E.2d at 718.

ANALYSIS

The issue is not whether a "permanent membership" in the MV Golf Club is a security under Section 35-1-102 (29)(D), but rather, whether all the elements of a profit-seeking business venture are present here and if the permanent members provide the capital and share in the earnings and profits of a common enterprise.

As to the first element under Howey: Was the laying out of the money by the Plaintiffs who purchased "Permanent Memberships" intended to secure income or profits from the employment of that money? This Court determines it was not for a profit seeking motive. The $9,500.00 is not an investment of money. It is the purchase of the right to play golf at the MV Golf Course and be a member of the MV Golf Club. The money is transferred solely for

recreational or social purposes and not as an investment. Further, to satisfy this first element, the investor (permanent member) must have "committed his assets to the enterprise in such a manner so as to subject himself to financial loss." Majors v. S. C. Sec. Comm'n, 373 S.C. 153, 644 S. E. 2d 710 (2007). Money spent to purchase the right to play golf does not subject the spender to financial loss. It is a choice made by an individual as to whether or not he wants to pay the amount of money required for the right to engage in the recreational and social activity of golfing at the subdivision's golf course. It does not, as the synecdoche proclaims, give members "skin in the game" in a profit seeking business venture.

As to the second element of Howey: Was there a common enterprise? The second element is satisfied "if the promoter's gain is contingent on the investor's gain..." Id. at 166, 644 S. E. 2d at 717 . This is the "common enterprise" prong of SEC v. Howey, 328 U. S. 293 (1946). Further Majors v. SC Sec Comm'n and the notes to 35-1-102(29)(D) give guidance. The pertinent language in the comments states: "The Courts have divided over the interpretation of the "common enterprise" element of an investment contract." Id. at 166, 644 S.E. 2d at 717. Section 35-1-102 (29)(D) of the code "follows a significantly larger number of federal circuits and adopts a more restrictive form of vertical commonality that occurs only when there is profit sharing between two persons." Id. at 166, 644 S.E. 2d at 717. Majors, interprets the Code as adopting the strict vertical commonality test: "In interpreting all elements of the investment contract, the courts have emphasized substance over form. Clearly, it appears the Legislature intends a strict vertical commonality test to apply." Id. The strict commonality occurs only when there is profit sharing between two persons. Here the promoter's gain is not contingent on the investor's gain. As to this prong, the plaintiffs argue "[t]he Complaint alleges the common enterprise of the MV Golf Club within the Mount Vintage Plantation development." This does

not satisfy the second prong of Howey, there are no allegations that the promoter's gain, if any, is contingent on the investor's gain. In fact any gain to the investor would not flow through to the promoter. In the application of the "common enterprise" prong there is no gain to the promoter contingent on the investor's gain, if any.

As to the third element under Howey: Was there an expectation of profits derived solely from the efforts of the promoter or third parties? Any profits to the Plaintiffs would be solely the result of their own efforts and not derived from the efforts of the promoter or third party. The Plaintiffs argue that there is an expectation of profits due to the transferability of the "permanent membership" if the member sold his home in Mount Vintage Plantation. Plaintiffs further argue that future profit would depend upon the efforts of the issuers/developers in making the club attractive enough that the cost of membership goes up in value. This is based on speculation, conjecture and surmise. Plaintiffs would only make a profit if they sold their homes in Mount Vintage and transferred their permanent memberships to the purchasers of their homes for an amount in excess of the amount they paid for the permanent memberships. Even assuming a sale of the home and the transfer of the permanent membership for amount in excess of what was paid; this profit would not be derived solely from the efforts of the promoter or third parties.

The Plaintiffs have failed to meet the Howey test, and therefore, the Court concludes the "permanent memberships" in Mount Vintage Golf Club are not securities pursuant to Section 35-1-102(29)(D) and as such are not subject to registration with the Secretary of State. Defendants' Motion to Dismiss pursuant to Rule 12 (b)(6) of the SCRCP is GRANTED as to the cause of action alleging a violation of the South Carolina Uniform Securities Act.

Since the Court has concluded that the Permanent Memberships are not securities, the Court must determine whether the complaint, viewed in the light most favorable to the plaintiffs, states any valid claim for relief. A common sense review of the complaint would lead one to analyze a cause of action based on the elements of fraud. Plaintiffs allege Defendants either made untrue statements of material facts or omitted to state materials facts. Plaintiffs allege that Defendants failed to disclose that members may be subject to special assessments and that their rights to enjoy the benefits of permanent memberships were contingent upon payment of future assessments. The Court has carefully reviewed the complaint with particular focus on paragraphs 16, 17, 19, 20 and 21. These paragraphs read as follows:

> 16. In connection with the offering of the Permanent Memberships, the Defendants made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, including but not limited to the failure to disclose that members may be subject to special assessments which they would be forced to pay in order to enjoy the use and benefit of their Permanent Memberships.
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> 17. Plaintiffs acted upon the Defendants' offering and purchased a Permanent Membership in the MV Golf Club. There Plaintiffs were never told that the right to enjoy the benefits of the Permanent Membership was contingent upon the payment of future assessments, nor were the Plaintiffs ever advised of even the potential for future assessments.
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> 19. On or about July 19, 2010, MV Golf Club issued a special assessment in the amount of $4,600.00 against the outstanding Permanent Memberships for Mount Vintage Plantation residents who owned Permanent Memberships and $800 for non-resident owners of Permanent Memberships.
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> 20. While the Plaintiffs had operated under the belief that they had purchased enhanced ownership rights in the MV Golf Club and were never informed of even the potential for future assessments, they were told that if they failed to pay the special assessments their Permanent Memberships in the MV Golf Club would be forfeited.
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> 21. Plaintiffs and the absent class members refused to pay the special assessment and were subsequently banned from the MV Golf Club. They were thereby deprived of their "Permanent Membership" in the MV Golf Club.

Plaintiffs argue that Rule 9 (b) SCRCP does not apply "where no fraudulent intent is required, which includes the type of violation alleged here", that being a violation of the South Carolina Uniform Securities Act. Plaintiffs further argue that "Regardless of Rule 9's applicability, the Complaint is very specific with respect to what was the omission. The Complaint states that the offering documents failed to warn investors that they could be subject to future special assessments and that failure to pay those assessments could result in the loss of the Permanent Memberships." According to Plaintiffs "it is not possible to be more specific."

Construing the complaint herein liberally in favor of the plaintiff, the plaintiffs have failed to make any allegations as to the defendants' intent that the misrepresentation(s) (or material omission(s)) be acted upon. Ardis v Cox 314 S.C. 512, 431 S.E.2d 267 (S.C.App. 1993) Further, the court does not accept Plaintiffs' argument that "It is not possible to be more specific." Allegations of fraud must comply with the "particularity" standard of Rule 9(b).

As such the Defendants' Motion to Dismiss pursuant to Rule 12(b)(6) as to any claim of relief as to fraud is GRANTED.

Further, the court declines to rule on Plaintiffs' Motion for Class Certification pursuant to Rule 23, SCRCP as there is no stated cause of action.

And It Is So Ordered.

Lexington, SC
July 27, 2012

The Honorable R. Knox McMahon
Presiding Judge of the 11th Judicial Circuit