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Property

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PROPERTY

I. CAVEAT EMPTOR—SALE OF UNIMPROVED LAND

The South Carolina Supreme Court declined to continue its movement away from the doctrine of *caveat emptor* in the sale of residential real estate in *Jackson v. River Pines, Inc.*[1] The court held that an implied warranty of fitness for intended use does not spring from the sale of unimproved land upon which a new building is subsequently constructed and sold.[2] Consistent with the majority of American jurisdictions that have considered the issue,[3] this ruling signifies that developers will not be held strictly liable for defects in the sale of unimproved property.

The plaintiff purchased from the corporate defendant, River Pines, Inc., a lot that was subject to certain restrictive covenants limiting its use to residential home development.[4] The plaintiff and her husband, a contractor, constructed a house and a septic tank disposal system on the unimproved land and then sold the improved lot to third parties.[5] Upon discovering that the lot contained soil that would not support a septic system, the third parties sued and obtained a judgment against the plaintiffs.[6] Seeking indemnification for this judgment, plaintiffs sued River Pines, Inc. for breach of an implied warranty of fitness of the land for residential purposes.[7] The trial judge sustained the demurrer of the corporate defendant. On appeal the supreme court affirmed, holding that "no cause was stated since no such im-

1. 276 S.C. 29, 274 S.E.2d 912 (1981).

2. *Id.* at 31, 274 S.E.2d at 913.

3. *See, e.g.*, Scott v. Gill, 352 So. 2d 1143 (Ala. Civ. App. 1977); Stepanov v. Gavrilovich, 594 P.2d 30 (Alaska 1979); Witty v. Schramm, 62 Ill. App. 3d 185, 379 N.E.2d 333 (1978); Griffith v. Byers Constr. Co., 212 Kan. 65, 510 P.2d 198 (1973); Bennett v. Columbus Land Co., 70 Mich. App. 403, 246 N.W.2d 8 (1976); Beri, Inc. v. Salishan Properties, Inc., 282 Or. 569, 580 P.2d 173 (1978); Cook v. Salishan Properties, Inc., 279 Or. 333, 569 P.2d 1033 (1977).

4. 276 S.C. at 30, 274 S.E.2d at 914.

5. Record at 1; Brief for Respondents at 1.

6. 276 S.C. at 30, 274 S.E.2d at 912. This judgment was based on the breach of the implied warranty of fitness for a new house. Record at 17.

7. 276 S.C. at 30, 274 S.E.2d at 912.

plied warranty attaches in South Carolina."[8]

Noting that in the absence of fraud or misrepresentation the doctrine of *caveat emptor* generally governs the obligations of the parties in the sale of real estate, the court indicated that in South Carolina the purchaser of unimproved land must specifically covenant to protect whatever special rights or interests he expects to acquire in the land.[9] The court recognized that an implied warranty of fitness for intended use springs from the sale of a new building[10] but reasoned that different considerations attach to the sale of unimproved land. Quoting extensively from *Lane v. Trenholm Building Co.*,[11] the court concluded that the doctrine of *caveat emptor* continues to govern the sale of real estate in South Carolina.[12]

Since 1970, the South Carolina Supreme Court has narrowed considerably the scope of the doctrine in the sale of new homes by a vendor-builder.[13] The court has, however, emphasized the distinction between the sale of land and the sale of a residence and has limited its protection to the innocent purchaser of a house.[14] In *Lane*, the court buttressed this distinction with the following observations:

> The doctrine of merger of warranties in a deed is applicable to real estate sales but [is] not relevant to the sale of a product such as a building. When land is conveyed, there is often no

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8. *Id.*

9. *Id.* at 31, 274 S.E.2d at 913.

10. *Id.* (citing Lane v. Trenholm Bldg. Co., 267 S.C. 497, 229 S.E.2d 728 (1976); Rutledge v. Dodenhoff, 254 S.C. 407, 175 S.E.2d 792 (1970)).

11. 267 S.C. 497, 229 S.E.2d 728 (1976).

12. 276 S.C. at 31, 274 S.E.2d at 913.

13. Terlinde v. Neely, 275 S.C. 395, 271 S.E.2d 768 (1980); Lane v. Trenholm Building, 267 S.C. 497, 229 S.E.2d 728 (1976), Rutledge v. Dodenhoff, 254 S.C. 407, 175 S.E.2d 792 (1970).

14. In *Rutledge*, which held that an implied warranty applies when a new house is sold by the vendor-builder, the court recognized the inefficacy of *caveat emptor* because of the distinction "between the usual, normal sale of lands, and old buildings and a transaction where the vendor is also the builder of a new structure." 254 S.C. at 413, 175 S.E.2d at 794. Six years later in *Lane*, the court relied on this distinction to hold that when a new building is sold, an implied warranty of fitness for its intended use springs from the sale itself. 267 S.C. at 500, 229 S.E.2d at 729. Recently, in *Terlinde*, the court reasoned that *Lane*, coupled with the abandonment of the privity concept, mandated a holding that "an implied warranty for latent defects [of a home] extends to subsequent home purchasers for a reasonable amount of time." 275 S.C. at 399, 271 S.E.2d at 770. For a discussion of *Lane* and *Terlinde*, *see Property, Annual Survey of South Carolina Law*, 33 S.C.L. REV. 131 (1981).

clearly defined objective in the transfer making it impossible to imply a warranty of fitness for any purpose. Even when a particular purpose is contemplated, such as evidenced by restrictive covenants, the suitability of the land may depend on architectural proposals or other matters entirely independent of the conveyance. Finally, the purchaser can fully inspect undeveloped land so that the consequences of denying an implied warranty are not unfair or unjust.[15]

In light of *Lane*, the decision in *Jackson* is not surprising, but the fairness of the ruling may initially seem questionable. It seems harsh that plaintiffs purchased a lot restricted to residential purposes only to incur subsequent liability to third-party purchasers because of the land's inherent unsuitability for that purpose. On the other hand, plaintiffs were residential home builders who had ample opportunity to inspect the unimproved lot,[16] and it was their construction of the sewage system that precipitated the subsequent litigation. Clearly, plaintiffs in this case are not the innocent purchasers whom the South Carolina Supreme Court has sought to protect.

The court's decision in *Jackson* not to restrict the doctrine of *caveat emptor* in sales of unimproved land avoids the "injection of an element of uncertainty in real estate transactions. . . ."[17] Based on sound reasoning and ample authority, this limitation on the expanding number of exceptions to the doctrine seems appropriate.

II. FRAUDULENT CONVEYANCES

Based on a recodification of the English Statute of Elizabeth,[18] section 27-23-10 of the South Carolina Code provides

15. 267 S.C. at 501-02, 229 S.E.2d at 730. Concerning its third observation, the court cited as contrary authority Hinson v. Jefferson, 287 N.C. 422, 215 S.E.2d 102 (1975), which held that an implied warranty was breached when a lot subject to restrictive covenants limiting its use to construction of a single-family dwelling, could not be used for that purpose. 267 S.C. at 502 n. 2, 229 S.E.2d at 730 n. 2. In *Hinson*, the North Carolina Supreme Court rescinded a contract for breach of an implied warranty when a widow-purchaser discovered that her unimproved lot would not support a sewage system for a proposed dwelling. 287 N.C. at 436, 215 S.E.2d at 111. This decision's restriction of the doctrine of *caveat emptor* in a sale of land is unique to North Carolina.

16. Brief for Respondents at 10.

17. 276 S.C. at 32, 274 S.E.2d at 913.

18. An Act Againft Fraudulent Deeds, Alienations, &c., 1570, 13 Eliz., ch. 5.

that a debtor's conveyance intended to defraud his creditors shall be void.[19] In *Tuller v. Nantahala Park Co.*,[20] the South Carolina Supreme Court held that a creditor must reduce the debt owed to judgment and have an execution issued and returned *nulla bona*[21] before asserting the statute as a defense to void a fraudulent conveyance.[22] The reaffirmance of this common-law condition precedent indicates the court's intent to continue to require a plaintiff to exhaust available legal remedies before availing himself of an equitable remedy.[23]

Defendants Nantahala Park Company and Hilton Head Plantation Company, subsidiaries of Sea Pines Company, were land developers.[24] In October 1973, Nantahala obtained a $3.4 million loan[25] from plaintiff, Cousins Mortgage Equity and Investments.[26] Cousins received a mortgage on approximately 7,000 acres of Nantahala's real estate in North Carolina[27] and the parties agreed that some of Hilton Head's property would be pledged as further security for the loan.[28] Several weeks later,

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19. S.C. CODE ANN. § 27-23-10 (1976) provides:

> Every feoffment, gift, grant, alienation, bargain and conveyance of lands, tenements or hereditaments, goods and chattels, or of any of them, or of any lease, rent, commons or other profit or charge out of the same, by writing or otherwise, and every bond, suit, judgment and execution which may be had or made to or for any intent or purpose to delay, hinder or defraud creditors and others of their just and lawful actions, suits, debts, accounts, damages, penalties and forfeitures shall be deemed and taken (only as against that person or persons, his or their heirs, successors, executors, administrators and assigns, and every of them, whose actions, suits, debts, accounts, damages, penalties and forfeitures by such guileful, covinous or fraudulent devices and practices, as is aforesaid, are, shall or might be in any ways disturbed, hindered, delayed, or defrauded) to be clearly and utterly void, frustrate and of no effect, any pretense, color, feigned consideration, expressing of use, or any other matter or thing to the contrary notwithstanding.

20. ___ S.C. ___, 281 S.E.2d 474 (1981).

21. The latin phrase *nulla bona* means the defendant has no goods to levy upon in satisfaction of a judgment. W.J. Klein Co. v. Kneece, 239 S.C. 478, 123 S.E.2d 870 (1962).

22. ___ S.C. at ___, 281 S.E.2d at 476-77.

23. *See* G. GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES § 72 (rev. ed. 1940).

24. ___ S.C. at ___, 281 S.E.2d at 475.

25. Because the development loan agreement executed concurrently with the note provided for periodic funding, Nantahala only received a portion of the loan in October 1973. *Id.* at ___, 281 S.E.2d at 475; Record at 45.

26. Plaintiff Tuller was the nominee of the trustees of Cousins in this action.

27. ___ S.C. at ___, 281 S.E.2d at 475.

28. The Cousins-Nantahala agreement specified a first mortgage on 42.42 acres known as Bobbs Island and owned by Hilton Head; however, a 58-acre tract also owned by Hilton Head was later substituted for the 42.42 acres. Record at 18, 45.

Citibank and First National Bank of Chicago (collectively referred to as "Banks") entered into a revolving credit loan agreement with Hilton Head that was secured by a mortgage to 3,300 acres of Hilton Head's property. In April 1974, Hilton Head, pursuant to the Cousins-Nantahala agreement, gave Cousins a mortgage to a separate 58-acre tract on Hilton Head Island. Relying on this additional security, Cousins made further advances to Nantahala from the $3.4 million loan.

In late 1974, Sea Pines and its subsidiaries encountered financial difficulty. To avoid foreclosing on their loan, the Banks purchased all of the outstanding stock of Hilton Head.[29] In February of 1976, Cousins began foreclosure proceedings against Nantahala to satisfy its outstanding debt. Cousins acquired the mortgaged property at the foreclosure sale,[30] and sought to satisfy the remaining debt by foreclosing its mortgage on the 58-acre tract pledged by Hilton Head. As a defense,[31] defendants asserted that Hilton Head's mortgage to Cousins had been a fraudulent conveyance under the Statute of Elizabeth. The special referee concluded that the mortgage was a fraudulent conveyance. On appeal, the circuit court reversed and ordered foreclosure.[32] Defendants appealed the circuit court decision.

Adopting the decision of the circuit court judge, the South Carolina Supreme Court relied on the rule that "the obtaining of a judgment and a *nulla bona* return is a condition precedent to bringing a suit to void a voluntary transfer as a fraudulent conveyance."[33] Citing *Penning v. Reid*,[34] the court explained that a debtor's final solvency is determinative of whether his assets will satisfy his debts. According to *Penning*, if this final solvency shows that the debtor's property is insufficient to pay those debts existing when the debtor made the voluntary conveyance,

29. ___ S.C. at ___, 281 S.E.2d at 475.

30. *Id.* at ___, 281 S.E.2d at 475-76.

31. The court summarily rejected the additional defenses offered by Hilton Head Co. and the Banks. ___ S.C. at ___, 281 S.E.2d at 478-79.

32. *Id.* at ___, 281 S.E.2d at 476.

33. *Id.*

34. 167 S.C. 263, 166 S.E. 139 (1932). The special referee relied on *Penning* to conclude that the fraudulent conveyance was void. Record at 36. However, the South Carolina Supreme Court, in agreement with the circuit court judge, determined "that the special referee did not properly apply the law to the facts in this case." ___ S.C. at ___, 281 S.E.2d at 477.

the creditor is entitled to have the conveyance declared void.[35] Because the Banks did not foreclose, they were precluded from relying on the Statute of Elizabeth as a defense.[36]

The court reviewed the facts in *Tuller* and concluded that, unlike the usual voluntary conveyance case, substantial injury would result from setting aside the mortgage since the plaintiff had parted with valuable consideration. Cousins had relied on the additional security of the 58-acre tract before advancing further sums to Nantahala. In addition, the Banks should not be allowed to select their collateral and later invoke the law of fraudulent conveyances to reach other property.[37] The court was particularly unwilling to allow this result since the Banks chose not to foreclose, thus failing to "assiduously [observe] all of the prerequisites to such relief."[38]

By reaffirming the requirement of a judgment and a *nulla bona* return as a condition precedent to voiding a fraudulent conveyance, the South Carolina Supreme Court has preserved the common-law rule that developed in conjunction with the Statute of Elizabeth.[39] This rule, by requiring a judicial determination of the existence and amount of debt, forces a creditor to exhaust his legal remedies before seeking equitable relief. Thus, the equitable remedy is available only to a creditor with a bona fide claim. The rule ignores the hardships imposed on a creditor by delays in obtaining a judgment and the attendant multiplicity of lawsuits required to seek a remedy.

The Uniform Fraudulent Conveyance Act[40] and the Federal Rules of Civil Procedure[41] have removed the disadvantages of the common-law rule in some jurisdictions. Section 10 of the Act provides that a creditor's action to set aside a fraudulent con-

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35. 167 S.C. at 289, 166 S.E. at 148 (quoting from Richardson v. Rhodus, 48 S.C.L. (14 Rich.) 95 (1866)).

36. ___ S.C. at ___, 281 S.E.2d at 477.

37. *Id.*

38. *Id.* at ___, 281 S.E.2d at 478. The court found that since only a creditor can attack a debtor's conveyance as being fraudulent, Hilton Head had no standing to offer the Statute of Elizabeth defense. *See* Mitchell v. Cleveland, 76 S.C. 432, 57 S.E. 33 (1907). The court reasoned that the Banks, by acquiring all of the Hilton Head Co. stock, would "stand in the same equitable shoes . . ." and also have no standing to raise this defense. ___ S.C. at ___, 281 S.E.2d at 478.

39. *See* GLENN, *supra* note 23, at § 65.

40. Annot., 7A U.L.A. 161 (1978).

41. FED. R. CIV. P. 18(b).

veyance may proceed although the creditor's "claim has not matured."[42] In the twenty-five jurisdictions that have adopted the Act,[43] courts have generally interpreted the language of section 10 as an abrogation of the requirement of a prior judgment.[44] Section 9 of the Act, which concerns the rights of creditors whose claims have matured, has also been interpreted as abolishing the requirement of a prior judgment.[45] Furthermore, Rule 18(b) of the Federal Rules of Civil Procedure explicitly allows a creditor in the federal courts to set aside a fraudulent conveyance "without first having obtained a judgment establishing the claim for money."[46]

Although the facts in *Tuller* justify the court's decision to allow Cousins to foreclose, the court's holding may prevent future creditors from seeking the efficiency of a single lawsuit to obtain an equitable remedy. This result is particularly unjust because creditors will be forced to continue seeking foreclosure to avoid relinquishing their right to an equitable remedy. Adoption of the Uniform Fraudulent Conveyance Act or other legislative measures to abrogate the archaic rule applied in *Tuller* would provide the creditor with a simple choice: seeking the legal remedy followed by the necessary actions or resolving the entire matter in one action at equity.

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42. Annot., 7A U.L.A. at 358.

43. Annot., 7A U.L.A. 21 (Supp. 1981).

44. *See, e.g.*, Weisenburg v. Cragholm, 5 Cal. 3d 892, 489 P.2d 1126, 97 Cal. Rptr. 862 (1971); Park Oil, Inc. v. Getty Refining and Marketing Co., 407 A.2d 533 (Del. 1979); Churchill v. Palmer, 57 Mich. App. 210, 226 N.W.2d 60 (1974); Marion v. Miller, 239 Minn. 214, 58 N.W.2d 185 (1953); Merchants Nat'l Bank v. Sullivan, 96 N.H. 430, 78 A.2d 508 (1951); Lomonaco v. Goodwin, 108 N.J. Super. 83, 260 A.2d 10 (1969); State of Rio de Janeiro v. Rollins & Sons, Inc., 299 N.Y. 363, 87 N.E.2d 299 (1949); St. Paul Fire & Marine Ins. Co. v. State, Dept. of Natural Resources, Division of Forestry & Reclamation, 25 Ohio Misc. 26, 265 N.E.2d 814 (1970); Thomas v. Stewart, 178 Okla. 308, 62 P.2d 966 (1936); Malis v. Zinman, 436 Pa. 592, 261 A.2d 875 (1970); Fidelity Savings & Loan Ass'n v. Reese, 41 S.D. 546, 171 N.W. 812 (1919); Running v. Widdes, 52 Wis. 2d 254, 190 N.W.2d 169 (1971); Platte County State Bank v. Frantz, 33 Wyo. 326, 239 P. 531 (1925).

45. American Surety Co. v. Conner, 251 N.Y. 1, 7, 166 N.E. 783, 785 (1929).

46. FED. R. CIV. P. 18(b).

III. TESTAMENTARY TRUSTEES

In *Dunn v. North Carolina National Bank*,[47] the South Carolina Supreme Court significantly changed the law relating to the administration of testamentary trusts. The court ruled that South Carolina statutory provisions[48] that prohibited the naming of foreign corporations from contiguous states as testamentary trustees but allowed the selection of foreign corporations from any other state were in violation of the equal protection clause of article I, section 3 of the South Carolina Constitution.[49]

In *Dunn*, the testatrix was a resident of North Carolina at the time she executed a will naming North Carolina National Bank (NCNB) as trustee of her pour-over trust.[50] After retiring,

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47. 276 S.C. 202, 277 S.E.2d 143 (1981).

48. S.C. CODE ANN. § 21-29-40 (1976), provides in relevant part:

(a) No corporation created by another state of the United States . . . not having a place of business in the State of South Carolina shall be eligible or entitled to qualify, serve, or hold title to property in this State as testamentary trustee of an estate of any person domiciled in this State at the time of his death, . . . except however, such foreign corporations may act as testamentary trustee in this State if:

(1) It has a bona fide capital of at least two hundred fifty thousand dollars actually paid in;

(2) It is authorized to act as testamentary trustee in the state in which it is incorporated or if such foreign corporation be a national banking association in the state in which it has its principal place of business; and

(3) Any bank or other corporation organized under the laws of this State or a national banking association having its principal place of business in this State is permitted by law to act as testamentary trustee in the state in which such foreign corporation seeking to act in this State is organized or in which it has its principal place of business if it is a national banking association without further showing or qualification other than that it is authorized to act in such fiduciary capacity in this State and upon compliance with the laws of such other state, if any, concerning service of process on nonresident fiduciaries.

. . . .

(4) *Such foreign corporation is not domiciled or licensed to do business in a state contiguous to the State of South Carolina.*

(emphasis added).

S.C. CODE ANN. § 21-33-20 (1976), provides that "[n]otwithstanding anything to the contrary, no devise or bequest may be made by a will to the trustee of a trust where the trustee or all of the trustees could not qualify as a testamentary trustee under the laws of this State."

49. 276 S.C. at 207, 277 S.E.2d at 146.

50. Record at 1, 2. A pour-over trust is a provision in a will by which the testator

she and her husband moved to Myrtle Beach, South Carolina, where the testatrix subsequently died. During the administration of the estate, it was discovered that South Carolina law prohibited NCNB from serving as testamentary trustee. The executor then sought a declaratory judgment that the statutes preventing NCNB from serving as testamentary trustee were unconstitutional.[51]

The trial court ruled that the rights allegedly violated were those of NCNB and that the executor therefore had no standing to challenge the statutes.[52] The court further found that the statutes did not violate the equal protection clause of the South Carolina Constitution.[53] The South Carolina Supreme Court reversed on appeal and held that because the provisions precluded a free choice of trustee, the testatrix's interests were sufficiently affected to permit the challenge.[54] The court also held that the statutes' arbitrary discrimination between similarly situated testators violated the equal protection clause.[55]

Most states have statutory provisions that control the ability of foreign corporations to serve as testamentary trustees.[56] The majority, including South Carolina, condition testamentary representation on the granting of a reciprocal right by the foreign corporation's state of domicile[57] and on the fulfillment of certain statutory requirements.[58] South Carolina appears to have been unique, however, in precluding corporations from contiguous states from serving in this capacity.[59] Because the laws of

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leaves the residue of his estate to a trustee of a trust established during the testator's lifetime. BLACK'S LAW DICTIONARY 1355 (rev. 5th ed. 1979).

51. Record at 2.

52. *Id.* at 47, 48.

53. *Id.* at 55-59.

54. 276 S.C. at 205, 277 S.E.2d at 145.

55. *Id.* at 206, 277 S.E.2d at 146.

56. G. BOGERT, TRUSTS & TRUSTEES § 132 (2d ed. 1965 & Supp. 1980). *E.g.*, ARIZ. REV. STAT. ANN. § 10-107 (1977); COLO. REV. STAT. § 7-9-104 (1980).

57. A reciprocity clause allows a foreign corporation to serve as a testamentary trustee only if that corporation's state of domicile affords a similar right to the corporations of its state. *E.g.*, GA. CODE ANN. § 108-801 (1981); N.C. GEN. STAT. § 55-132 (1975); OKLA. STAT. ANN. tit. 18 § 476 (West 1953); TENN. CODE ANN. § 35-610 (1977).

58. These requirements generally are similar to those contained in S.C. CODE ANN. § 21-29-40. *See supra* note 48.

59. Particular statutory requirements vary widely. North Carolina permits *only* contiguous states with reciprocal provisions to serve. N.C. GEN. STAT. § 55-132 (1975). Nebraska limits the foreign corporate trustee's right to hold real property within the state.

North Carolina and Georgia contain reciprocal provisions,[60] South Carolina's former prohibition effectively denied corporations from these states a significant economic benefit that was available to corporations from any other state.

Dunn's removal of this prohibition has two significant effects on the administration of testamentary trusts in this state. South Carolina testators may now select otherwise qualified corporations from any state as testamentary trustees. Moreover, because both Georgia and North Carolina have reciprocal statutory provisions, South Carolina corporations may now serve as testamentary trustees in those states.

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NEB. REG. STAT. § 76-402 (1976). A few states prohibit altogether testamentary representation by foreign corporations. *E.g.*, KY. REV. STAT. ANN. §§ 287.030, 395.001 (Bobbs-Merrill Supp. 1980).

60. GA. CODE ANN. § 108-801 (1981); N.C. GEN. STAT. § 55-132 (1975).