USING MAXIMS AS A BEACON: HOW EQUITY HELPED THE GOOD GUY SURVIVE THE STORM.

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I. INTRODUCTION

It swept through South Carolina leaving a path of destruction. It uprooted families and forced businesses to close their doors. It was not a hurricane. It was not a tornado. It was not a natural disaster of any kind. What struck South Carolina’s coast in 2008 was a foreclosure epidemic, similar to what plagued the rest of the country. During the economic downturn that began in 2008, South Carolina was hemorrhaging jobs and the number of foreclosures was growing.¹ There were 25,163 foreclosures in 2009, amounting to a rate of one filing for every 80 households.²

Rewind the clock to 2006. Ray Covington, an experienced real estate broker known worldwide for his good eye for real estate,³ decided to purchase a lot in the Grand Dunes Development of Myrtle Beach. Grand Dunes is self-described as:

A TRULY ONE-OF-A-KIND COMMUNITY IN MYRTLE BEACH

As you’d expect, a place as beautiful and popular as Myrtle Beach offers a number of great choices for primary or second-home living. But Grande Dunes stands out from all the others as the most complete, inviting, and all-around best location in the area.

Throughout its 2200 master-planned acres encompassing breeze-swept oceanfront dunes and quiet longleaf pine forests, this remarkable community offers gracious coastal living at its best. Real estate opportunities include an outstanding selection of scenic single family homesites and villas with Intracoastal Waterway views.

² Id.
³ While enroute to a safari in the Republic of Nambia, Gene Trotter, a South Carolinian, strikes up conversation with a local South African who knew Ray Covington. Covington evidently owned a home in Cape Town, South Africa. Telephone Interview with Daryl G. Hawkins & Charles E. Usry, counsel for Ray Covington, Law Office of Daryl G. Hawkins, LLC (March 21, 2012) [hereinafter Telephone Interview with Hawkins & Usry]. Mr. Hawkins and Mr. Usry extend their appreciation to Professor Spitz for his publications and research in this field, which aided them in crafting their equitable arguments in this case.
World-class amenities offer extraordinary social, dining and recreational options throughout the year.  

Ray Covington did not just have his eye on any lot at Grand Dunes. He had selected Lot 38, a beautiful parcel of land located on the inland waterway, complete with a coveted dock permit. His plan was to build an extraordinary home for resale. This was, after all, Covington’s business; and business had been good.

II. CALM WATERS

In an effort to maintain the prestige and the caliber of homes within Grand Dunes, the development required potential purchasers to choose from a limited number of designated builders. The builder was required to buy the lot and complete construction first, and then the homeowner would take title to the lot upon completion. From these designees, Ray Covington selected Tom Wingard, a skilled builder with an artistic flair. Wingard was in the process of completing several other houses in Grand Dunes during this time.

On September 12, 2006, Covington and Wingard entered into a purchase agreement for Lot 38. On October 20, 2006, Covington wrote Wingard a check for $276,700 as down payment for the Lot according to the terms of the parties’ agreement. The remaining 90% would be payable once the home was complete. Covington also wrote a $10,000 check to Grand Dunes Properties on September 3, 2006.

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5 Id.
6 Id.
7 Id.
8 Id.
9 Id.
10 Id.
11 Id.
12 Id.
To get the funding to start construction, Wingard went to Regions Bank and mortgaged Lot 38 and two other lots as collateral for a $7 million revolving construction loan.\textsuperscript{13} "A construction loan . . . is a complex arrangement involving a multitude of documents and including within the purview of its concern numerous persons and legal relationships."\textsuperscript{14} As a precondition to the loan, Regions required that Wingard have a sales agreement for Lot 38.\textsuperscript{15} Regions approved the loan and funded the project because Wingard had already entered into a contract for sale with Covington, a qualified purchaser. Regions recorded its mortgage on November 13, 2006, one day before Wingard deposited Covington’s check.\textsuperscript{16} It was later discovered that Covington’s bank account lacked the funds to cover the check until that date.\textsuperscript{17} Construction on Lot 38 was roughly 75\% complete when the clouds started forming in the distance.

\textbf{III. A STORM ON THE HORIZON}

As mentioned before, Wingard had other projects in Grand Dunes underway. Like Covington, these purchasers had contracts with Wingard that only required a 10\% down payment with the remainder of the purchase price due upon completion. Wingard finished two other projects in Grand Dunes, only to find out that the contracted purchasers were insolvent. Wingard sought to remedy this predicament by asking Regions for an extension to finish and sell Lot 38. Instead, Regions sought to foreclose on its lien on all three lots.\textsuperscript{18}

\textsuperscript{13} \textit{Id.}
\textsuperscript{14} Robert M. Berger, \textit{Construction Financing Banking and Loans, in} 4-14 \textit{CONSTRUCTION LAW} P 14.03 (Matthew Bender & Co., 2012).
\textsuperscript{15} Regions, 394 S.C. at 247.
\textsuperscript{16} \textit{Id.}
\textsuperscript{17} \textit{Id.} at 352.
\textsuperscript{18} Telephone Interview with Hawkins & Usry, \textit{supra} note 3.
On December 28, 2007, Regions Bank filed a complaint seeking foreclosure against Wingard Properties.\textsuperscript{19} Regions did not name Ray Covington in the complaint, although it is clear that Covington had an interest in Lot 38. Covington found out about the foreclosure and on July 18, 2008, he filed a motion to intervene.\textsuperscript{20} The parties entered a consent order on August 20, 2008, allowing Covington to intervene in the pending action.\textsuperscript{21} Covington filed a response to the foreclosure complaint on September 9, 2008, arguing that he had a first-priority equitable lien superior to that of Regions.\textsuperscript{22}

IV. BALANCING THE EQUITIES – FINDING THE CALM AFTER THE STORM

“A mortgage foreclosure is an action in equity.”\textsuperscript{23} In determining whether Ray Covington should have first priority equitable lien over Regions Bank’s recorded mortgage, the court analyzed the applicable equitable maxims and legal principles.\textsuperscript{24} “For an equitable lien to arise, there must be a debt, specific property to which the debt attaches, and an express or implied intent that the property serve as security for payment of the debt.”\textsuperscript{25} First the court explained the history and background of the ancient reliance on maxims:

Equitable maxims are not binding legal precedent but represent notions and concepts of equity in various situations . . . Maxims developed, at least in part, to reflect the attempt by the courts of equity to create guiding principles, in the same way that the legal courts developed binding precedent . . . Even today, it is not unusual to find judges citing and applying these ancient maxims . . . in deciding whether or not to grant equitable relief . . . Thus, we view maxims only as offers of guidance in equitable cases.\textsuperscript{26}

\textsuperscript{19} Trial Court Order at 2, Regions Bank v. Wingard Prop., No. 26-8196, (July 13, 2009).
\textsuperscript{20} Id.
\textsuperscript{21} Id.
\textsuperscript{22} Id.
\textsuperscript{24} Id. at 249-50.
\textsuperscript{25} Id. at 250 (quoting First. Fed. Sav. & Loan Ass’n of S.C. v. Finn, 300 S.C. 228, 231 (1989)).
\textsuperscript{26} Id. at 249 (internal citations and quotation marks omitted).
The court addressed the following maxims in light of the facts of this case: equity regards as done that which ought to have been done; equity applies substance over form; equity abhors a forfeiture; equity follows the law; and one who seeks equity must do equity.\textsuperscript{27}

\textbf{A. Equity regards as done that which ought to have been done.}

This equitable maxim only applies in cases where the party seeking equitable relief establishes a "clear obligation, based upon a valuable consideration, that another do some act which he failed to perform, and looks to the substance of the controversy to determine the appropriate equitable remedy by dispensing with the formalities that would defeat the equity."\textsuperscript{28} In short, under Spitz's Ultimate Equitable Maxim (SUEM), "in equity, good guys should win and bad guys should lose."\textsuperscript{29}

Counsel for Regions Bank Stan McGuffin argued Regions Bank was the "good guy" in this case, because according to him, Covington was "gaming the system" by issuing a check that he knew he could not cover.\textsuperscript{30} In the San-A-Bel case, the court gave priority to an equitable lien made by purchasers over a lending bank when the purchasers paid a developer a down payment prior to the bank loaning the developer funds.\textsuperscript{31} But prior to hearing the Regions case, South Carolina courts had not ruled on the issue of equitable liens when one party issued a "bum check."\textsuperscript{32} "If there is one thing I know," said McGuffin, "it's that people in the construction

\textsuperscript{27} Id. at 250.
\textsuperscript{28} Id. at 253 (quoting Wilkie v. Phila. Life Ins. Co., 187 S.C. 382, 393-94 (1938); Randolph R. Lowell, Robert L. Reibold and Shealy Boland Reibold, South Carolina Equity: A Practitioner's Guide 28 (South Carolina Bar 2010).
\textsuperscript{29} Roger Young and Stephen Spitz, SUEM—Spit'z Ultimate Equitable Maxim: In Equity, Good Guys Should Win and Bad Guys Should Lose, 55 S.C.L. Rev. 175 (2003).
\textsuperscript{30} Telephone Interview with Stanley H. McGuffin, counsel for Regions Bank, Haynsworth Sinkler Boyd, P.A. (March 26, 2012) [hereinafter Telephone Interview with McGuffin]. Counsel for Covington remarked that each time Covington was asked if the check was bad he would reply, "That check was essentially good the minute I wrote it." Telephone Interview with Hawkins & Usry, \textit{supra} note 3.
\textsuperscript{32} Telephone Interview with McGuffin, \textit{supra} note 30.
business do not hold checks.\textsuperscript{33} Covington took the position that his word was his bond; but he was not in the position to make the check good even though he had the assets to do so.\textsuperscript{24}

The South Carolina Court of Appeals interpreted the facts differently, holding that in spite of Covington’s lack of available funds to cover his initial check, Regions Bank had sufficient notice of Covington’s interest in the land to place their lien behind that of Covington’s. “This case was decided on equitable principles, and in my opinion, decided correctly,” said Charles Usry, co-counsel for Ray Covington.\textsuperscript{35}

**B. Equity applies substance over form.**

When a party establishes an equitable right, the court will do away with “any mere formality, which, if required by the court, would otherwise defeat equity.”\textsuperscript{36} This equitable principle of focusing on intent rather than form is often applied to prevent the enforcement of forfeiture or relieve a party from imposition of a penalty that would be valid at law.\textsuperscript{37}

In the case at hand, Regions Bank made a loan to Wingard in reliance on the purchase contract and down payment by Covington.\textsuperscript{38} The trial court held that Regions Bank was not aware of any delay in depositing the funds from Covington before it recorded its mortgage, and also not prejudiced by the timing of the deposit.\textsuperscript{39} Therefore the court reasoned that Covington’s equitable interest was not defeated by Region Bank’s mortgage because Covington entered into a contract prior to Regions Bank filing its mortgage, and Regions was aware of this interest.\textsuperscript{40}

McGuffin acknowledges that Regions Bank bore some responsibility in failing to complete its due diligence regarding Covington. Yet McGuffin argues that in order for a court to

\textsuperscript{33} Id.
\textsuperscript{34} Id.
\textsuperscript{35} Telephone Interview with Hawkins & Usry, supra note 3.
\textsuperscript{36} LOWELL, RIEBOLD & RIEBOLD, supra note 28, at 31.
\textsuperscript{37} Id. at 30-31.
\textsuperscript{39} Id.
\textsuperscript{40} Id. at 255; S.C. CODE ANN. § 30-7-10 (LexisNexis 2011).
honor an equitable lien, the purchaser, in this case Covington, has to have incurred some risk of loss. Here, according to McGuffin, Covington had no funds at risk until Regions Bank committed more than a million dollars of its funds. McGuffin distinguishes the case at hand from *San-A-Bel*, where the purchasers were given priority on their equitable lien over that of the lender bank because the purchasers had committed their funds prior to the bank’s commitment to lend.\(^{41}\)

On the other hand, Daryl Hawkins and Charles Usry, co-counsel for Defendant Ray Covington, argued that their client had fulfilled all of the duties required of him to establish an equitable lien with priority over Regions Bank. Covington had a reputation as a successful developer with decades of experience, and according to Covington, his check was valid from the moment he wrote it. “We felt from the get-go that the bank knew who was Ray was, knew the money going into deal—knew he was paying. Ray did everything he was required to do under the contract,” said Hawkins.\(^{42}\)

C. **Equity abhors forfeiture.**

“A Court of equity abhors forfeitures and will not lend its aid to enforce them.”\(^{43}\) The court affirmed the trial court’s finding that there was a substantial likelihood that Covington’s $276,000 deposit on Lot 38 would be forfeited by the Regions foreclosure.\(^{44}\) The trial court looked at “case specific” factors in making this determination, including “the amount of equity the purchaser had accumulated, the length and number of defaults, the amount of forfeiture, the speed in which equity was sought, and the amount of money the purchaser would forfeit in

\(^{42}\) Telephone Interview with Hawkins & Usry, *supra* note 3.
\(^{43}\) *Regions*, 394 S.C. at 256.
\(^{44}\) *Id.*
relation to the purchase price of the property.”

Based on these factors, there was a substantial likelihood that the lot would bring in less at a judicial sale than the liens on the property, thus wiping out Covington’s interest.

D. Equity follows the law.

Regions Bank argued the court must abide by South Carolina’s recording statute and reward the party that filed first according to Section 30-7-10 of the South Carolina Code. Essentially, this statute creates a “First in Time is First in Right Rule,” the purpose of which is to protect a subsequent buyer without notice. Co-counsel for Ray Covington Charles Usry did not believe the First in Time, First in Right statute applied in this case: “We were only talking about two parties, both of whom had knowledge of each other the whole time. This was not a situation where you are talking about two creditors and one did not have notice of the other [thus needing the statute’s protection].”

But as established in Riggs v. Palmer, equity can trump statutory law on rare occasions. Here, the court opted to give Covington lien priority over Regions, because Regions had notice of Covington’s interest in the property prior to committing funds. “Courts have the inherent power to do all things reasonably necessary to ensure that just results are reached to the fullest
extent possible."\textsuperscript{51} For this court, it all boiled down to notice. "For one to have notice of an outstanding equitable interest, [one need not] know the identity of the third party or the extent of his interest. It is sufficient that one knows or ought to know that some third party exists."\textsuperscript{52} Here, Covington’s equitable interest was not defeated by Regions Bank’s mortgage because Covington entered into his purchase contract before Regions Bank filed its mortgage, and Regions was aware of the interest.\textsuperscript{53}

D. \textbf{One who seeks equity must do equity.}

Both Regions Bank and Covington made errors. Regions Bank was not thorough in its due diligence in ensuring Covington’s funds were collected prior to committing their own funds to the project. On the other hand, Covington wrote a check that he did not currently have funds to cover. One must do equity in order to receive equity. Courts have applied this maxim to actions for specific performance, cancellation of instruments, relief from judgments and judicial sales, injunctions, actions for divorce, and relief from mortgages and liens.\textsuperscript{54} A court of equity carefully scrutinizes the conduct of the plaintiff to be sure he has done all that he should have done to secure the action requested.\textsuperscript{55} In the case at hand, Covington argued that Regions’ failure to name him as a defendant in the foreclosure action proves that the bank was attempting to circumvent Covington’s interest.\textsuperscript{56} "We thought the bank had unclean hands; that they had not done equity and therefore they should not be able to receive equity."\textsuperscript{57} The court dismissed this argument, because Covington was able to intervene and suffered no prejudice.\textsuperscript{58}

\textsuperscript{51} Ex Parte Dibble, 279 S.C. 592, 595 (Ct. App. 1983).
\textsuperscript{53} \textit{Id.} at 255.
\textsuperscript{54} \textsc{Lowell, Riebold & Riebold}, \textit{supra} note 28 at 30.
\textsuperscript{55} \textit{Regions}, 394 S.C. at 259.
\textsuperscript{56} \textit{Id.}
\textsuperscript{57} Telephone Interview with Hawkins & Usry, \textit{supra} note 3.
\textsuperscript{58} \textit{Regions}, 394 S.C. at 259.
V. CONCLUSION

The South Carolina Court of Appeals applied ancient equitable maxims for guidance to determine where lien priority should lie. Under SUEM, the court’s result could have been predicted by determining who is the good guy and who is the bad guy. 59 However, as Professor Spitz and Judge Young noted, “(1) it is often difficult to know who is a bad guy and who is not; and (2) it is sometimes equally difficult to know if there really is a good guy in many cases.” 60

In this case, Regions Bank had actual notice of Covington’s interest in Lot 38. The Bank drafted its note and mortgage with Wingard, therefore it had the opportunity to prevent this situation from ever arising by simply adding in a clause subordinating all other liens to this mortgage. Further, Regions could have worked with Wingard by granting him an extension rather than immediately foreclosing. 61 The court used equitable principles and judicial discretion to dispense with the formality of recordation and acknowledge the fact that Covington’s interest, albeit unrecorded and formalized after the Bank’s lien was recorded, should prevail. Ray Covington was the “good guy” in this case, and equitable maxims pointed the court in the right direction by providing a way for his equitable lien to take priority over the Bank’s recorded mortgage.

59 Young & Spitz, supra note 29 at 175-76.
60 Id. at 188-89.
61 By Administrative Order issued May 3, 2011, Chief Justice Toal of the South Carolina Supreme Court halted mortgage foreclosure proceedings throughout the state by requiring that prior to foreclosing owner-occupied dwellings, the mortgagee’s attorney must certify that foreclosure intervention or loss mitigation has been explored. Admin. Order No. 2011-05-02-01. The Order was issued in response to the increasing number of mortgage foreclosure actions filed in the State and the “resulting burden on the resources of the Court . . . .” Id. Although the Regions case involved an investment property as opposed to an owner-occupied dwelling, the authors cannot help but wonder if this case would have ever been heard if Regions Bank offered Wingard an extension or modification of his construction loan obligations.