U.S. BANKRUPTCY COURT
District of South Carolina

Case Number: **20-02092-hb**
Adversary Proceeding Number: **20-80049-hb**

ORDER

The relief set forth on the following pages, for a total of 9 pages including this page, is hereby ORDERED.

FILED BY THE COURT
01/20/2021

Entered: 01/20/2021

Chief US Bankruptcy Judge
District of South Carolina

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH CAROLINA

In re, Foxwood Hills Property Owners Association, Inc., Debtor(s).	C/A No. 20-02092-HB Adv. Pro. No. 20-80049-HB Chapter 11
Foxwood Hills Property Owners Association, Inc., Plaintiff(s), v. 783-C, LLC *et al.* Defendant(s).	**ORDER DENYING DEFENDANT RICHARD F. DIXON'S MOTION TO DISMISS**

THIS MATTER came before the Court for a hearing on January 12, 2021, to consider the Motion to Dismiss Plaintiff's Amended Complaint filed by Defendant Richard F. Dixon.[1] The Motion asserts the Amended Complaint should be dismissed for lack of subject matter jurisdiction, failure to state a claim, and failure to join a necessary party pursuant to Fed. R. Civ. P. 12(b)(1), (6), and (7).[2] Plaintiff Foxwood Hills Property Owners Association, Inc. (the "Association") filed an Objection.[3]

FACTUAL ALLEGATIONS AND PROCEDURAL HISTORY

The Association is the property owners' association for a residential development known as Foxwood Hills (the "Community") located on Lake Hartwell in Oconee County, South Carolina. The Association filed a petition for voluntary Chapter 11 relief on May 8, 2020. This adversary

[1] ECF No. 84, filed Oct. 29, 2020.
[2] Made applicable to this adversary proceeding by Fed. R. Bankr. P. 7012. The parties raised other arguments at the hearing, including that the Court should abstain from this matter under 28 U.S.C. § 1334(c), which were not addressed in their pleadings and, therefore, will not be considered by the Court.
[3] ECF No. 128, filed Nov. 23, 2020.

proceeding was filed in July 2020 and includes over 3,300 defendants – many have answered or appeared, while others have not. The defendants are property owners of record of the approximate 4,100 lots within the Community.

This adversary proceeding seeks to resolve controversies regarding membership in the Association, voting rights, and the amount and calculation of the fees, dues, and assessments payable to the Association by the parties named. Pursuant to the Declaratory Judgment Act, 28 U.S.C. § 2201, *et seq.*, the Association seeks a declaratory judgment based on equitable grounds for relief that defendants are members of the Association with equal voting rights and are required to pay budget-based dues, fees, and assessments.[4] The Amended Complaint also asserts the various covenants and restrictions on certain deeds and recorded real property filings did not address membership in the Association and failed to contemplate an adequate source of funding for the privately maintained roads and amenities of the Community. The Association alleges the requested equitable relief is needed because enforcing these various restrictions, some of which have not been followed or enforced for decades, would cause a great wrong and leave the Association insolvent and inoperable. Therefore, the Association requests the covenants and restrictions be rescinded/cancelled or reformed to provide that all property owners within the Community are members of the Association, subject to its bylaws, and must pay budget-based dues, fees, and assessments.

Certain defendants were served by first class mail, but the mailings were returned "undeliverable" (the "Returned Mail Defendants"). Additionally, the Amended Complaint includes designated classes of defendants identified as the John Doe Defendants, Richard Roe

[4] The Association asserts the following equitable grounds for obtaining the requested declaratory relief: *quantum meruit*/implied contract, course of dealings/course of performance, laches, promissory estoppel, equitable estoppel, waiver, statute of limitations, equitable contribution, perpetual contracts are unreasonable and disfavored, and/or changed circumstances.

Defendants, and Steven Stoe Defendants and defined in detail therein. Pursuant to Fed. R. Bankr. P. 7004(c), on October 26, 2020, the Court granted the Association's request to serve by publication a summons for the Amended Complaint on the Returned Mail Defendants, as well as Doe, Roe, and Stoe Defendants.[5]

DISCUSSION

I. SUBJECT MATTER JURISDICTION

Primarily relying on *Stern v. Marshall*, 564 U.S. 462, 480, 131 S. Ct. 2594, 2607, 180 L. Ed. 2d 475 (2011), Dixon asserts this Court lacks subject matter jurisdiction to adjudicate the declaratory judgment claims asserted against him because they are state law claims not resolved in the claims allowance process. Dixon also argues this matter is not a core proceeding and the Court lacks subject matter jurisdiction over adversary proceedings that seek declaratory relief presenting only questions of state law. The Association contends Dixon's argument focuses on the issue of core versus non-core proceedings, which does not affect the Court's subject matter jurisdiction.

"Federal bankruptcy courts, like the federal district courts, are courts of limited jurisdiction." *Educ. Credit Mgmt. Corp. v. Kirkland (In re Kirkland)*, 600 F.3d 310, 215 (4th Cir. 2010). "Although they are related concepts . . . the scope of the bankruptcy courts' subject matter jurisdiction, their statutory authority to hear and/or determine any particular matter, and their constitutional authority to do so, each are delineated by different statutory, constitutional, and/or judicial authorities." *In re Dambowsky*, 526 B.R. 590, 595 (Bankr. M.D.N.C. 2015). Under 28 U.S.C. § 1334(a), the district courts "have original and exclusive jurisdiction of all cases under

[5] ECF No. 72.

title 11." They also have "original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases until title 11." 28 U.S.C. § 1334(b).

> A proceeding or claim "arising in" Title 11 is one that is not based on any right expressly created by Title 11, but nevertheless, would have no existence outside of the bankruptcy. Therefore, a controversy arises in Title 11 when it would have no practical existence *but for* the bankruptcy.

Valley Historic Ltd. P'ship v. Bank of New York, 486 F.3d 831, 835 (4th Cir. 2007) (emphasis in original) (internal quotation marks and citations omitted). A civil proceeding is "related to" a title 11 case if its outcome might have any conceivable effect on the bankruptcy estate. *Id.* at 836 (recognizing the Fourth Circuit's adoption of the test articulated by the Third Circuit in *Pacor, Inc. v. Higgins*, 743 F.2d 984, 994 (3d Cir. 1984)). "Therefore, 'an action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options or freedom of action (either positively or negatively) and it in any way impacts upon the handling and administration of the bankruptcy estate.'" *Id.* (quoting *Owens-Ill., Inc. v. Rapid Am. Corp. (In re Celotex Corp.)*, 124 F.3d 619, 625 (4th Cir. 1997). If the proceeding in question does not "arise in" or is not "related to" the bankruptcy, then the bankruptcy court has no jurisdiction to hear the matter. *See* 28 U.S.C. § 1334(b).

While 28 U.S.C. § 1334 determines subject matter jurisdiction, 28 U.S.C. § 157(b) and (c) determine "the bankruptcy court's authority to act once that jurisdiction is established." *Kirkland*, 600 F.3d at 315; *see also Stern*, 564 U.S. at 480 ("Section 157 allocates the authority to enter final judgment between the bankruptcy court and the district court. That allocation does not implicate questions of subject matter jurisdiction." (citing 28 U.S.C. § 157(b)(1), (c)(1), (2))). Under § 157, district courts can refer cases or proceedings under § 1334 to the bankruptcy courts. 28 U.S.C. § 157(a). Additionally, district courts may withdraw, in whole or in part, any case or proceeding

that it referred. 28 U.S.C. § 157(d). The District of South Carolina has referred to this Court any and all cases within the scope of § 1334. *See* Local Civ. Rule 83.IX.01 (D.S.C.).

Upon referral from the district court, "[b]ankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11 . . . and may enter appropriate orders and judgments." 28 U.S.C. § 157(b)(1). For non-core proceedings that otherwise relate to the bankruptcy case under title 11, "the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge . . ." 28 U.S.C. § 157(c)(1).

"Outside of a bankruptcy court's statutory authority to enter final orders in certain proceedings, however, the court must still possess the constitutional authority to do so." *MDC Innovations, LLC v. Hall*, 726 F. App'x 168, 171-72 (4th Cir. 2018) (citing *Stern*, 564 U.S. at 482-83)). In *Stern,* the Supreme Court held that despite having authority under § 157(b)(2)(C) to enter a final judgment, the bankruptcy court lacked authority under Article III of the Constitution where the debtor asserted a state law counterclaim against an entity that files a proof of claim in the case, unless that counterclaim "stems from the bankruptcy itself or would necessarily be resolved in the claims allowance process." 564 U.S. at 499. Under these circumstances, the bankruptcy court may not enter a final order absent the consent of the parties. *See Wellness Int'l Network, Ltd. v. Sharif,* 575 U.S. 665, 135 S. Ct. 1932, 191 L. Ed. 2d 911 (2015). Further, "when, under *Stern*'s reasoning, the Constitution does not permit a bankruptcy court to enter final judgment on a bankruptcy-related claim, [§ 157(c)] nevertheless permits a bankruptcy court to issue proposed findings of fact and conclusions of law to be reviewed *de novo* by the district court." *Exec. Benefits Ins. Agency v. Arkison*, 573 U.S. 25, 28, 134 S. Ct. 2165, 2168, 189 L. Ed. 2d 83 (2014).[6]

[6] The District of South Carolina issued the following order:

The Association's claims appear, at a minimum, *related to* its bankruptcy case because the outcome of this adversary proceeding affects its bankruptcy estate and ability to reorganize and continue operating. The relief sought will alter the Association's rights in a way that impacts the handling and administration of the bankruptcy estate because, as the Association has represented, its ability to declare all property owners within the Community members of the Association and require them to pay budget-based dues, fees, and assessments is how the Association intends to continue its operations. Accordingly, the Court has subject matter jurisdiction under 28 U.S.C. § 1334(b) and Dixon's Motion to Dismiss under Fed. R. Civ. P. 12(b)(1) must be denied.

II. FAILURE TO STATE A CLAIM

A motion to dismiss pursuant to Fed. R. Civ. P. 12(b)(6) tests the sufficiency of the complaint without resolving contests of fact or the merits of a claim. *Republican Party of N.C. v. Martin*, 980 F.2d 943, 952 (4th Cir. 1992), *cert. denied*, 510 U.S. 828 (1993). Thus, the Court's inquiry is limited to determining whether the allegations constitute "a short and plain statement of the claim showing the pleader is entitled to relief" pursuant to Rule 8(a)(2). To survive a motion to dismiss, factual allegations in the complaint must be sufficient to "raise a right to relief above a speculative level." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007). Consequently, a complaint will survive if it contains "enough facts to state a claim to relief that is plausible on its face." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Twombly*, 550 U.S. at 570). The Court

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> If a bankruptcy judge or district judge determines that entry of a final order or judgment by a bankruptcy judge would not be consistent with Article III . . . the bankruptcy judge shall, unless otherwise ordered by the district court, hear the proceeding and submit proposed findings of fact and conclusions of law to the district court. The district court may treat any order of the bankruptcy court as proposed findings of fact and conclusions of law in the event the district court concludes that the bankruptcy judge could not have entered a final order or judgment consistent with Article III . . .

Standing Order Concerning Title 11 Proceedings Referred Under Local Civil Rule 83.IX.01, Referral to Bankruptcy Judges, 3:13-mc-00471-TLW (D.S.C. Dec. 5, 2013).

must draw all reasonable factual inferences in favor of the plaintiff. *Priority Auto Grp., Inc. v. Ford Motor Co.*, 757 F.3d 137, 139 (4th Cir. 2014).

Dixon asserts the Amended Complaint fails to state a claim for relief because South Carolina law precludes the relief sought by the Association.[7] Dixon cites *Heritage Fed. Sav. & Loan Ass'n v. Eagle Lake & Golf Condos.*, 458 S.E.2d 561 (S.C. Ct. App. 1995), *Shipyard Prop. Owners' Assoc. v. Mangiaracina*, 414 S.E.2d 795 (S.C. Ct. App. 1992), and *Queen's Grant v. Greenwood Devel.*, 628 S.E.2d 902 (S.C. Ct. App. 2006), in support of his arguments that amendments to covenants are prohibited unless the developer expressly reserves a right to amend, and without the property owners' consent the Association is unable to amend the governing documents. Under South Carolina law, a party may bring a declaratory judgment action to invalidate a restrictive covenant based on equitable principles. *See SPUR at Williams Brice Owners Ass'n, Inc. v. Lalla*, 781 S.E.2d 115, 124-25 (S.C. Ct. App. 2015) (discussing the equitable principle change of conditions). Based on the allegations of the Amended Complaint, the cases relied on by Dixon may be distinguishable from the facts and issues presented here. Therefore, dismissal at this early stage of the litigation is not appropriate and Dixon's Motion pursuant to Fed. R. Civ. P. 12(b)(6) must be denied.

III. FAILURE TO JOIN NECESSARY PARTY

Dixon argues the Amended Complaint should be dismissed because the Association failed to join indispensable parties, as evidenced by serving certain defendants by publication. Under Rule 12(b)(7), a party may move to dismiss for "failure to join a party under Rule 19." Under Rule 19(a), a person or party must be joined in an action when:

[7] Dixon also argued grounds to dismiss under Fed. R. Civ. P. 12(b)(6) because the Court lacks subject matter jurisdiction. Having found this Court has jurisdiction over this matter under 28 U.S.C. § 1334, the Court need not address this argument.

> (A) in that person's absence, the court cannot accord complete relief among existing parties; or
> (B) that person claims an interest relating to the subject of the action and is so situated that the disposition of the action in the person's absence may:
>
> (i) as a practical matter impair or impede the person's ability to protect the interest; or
>
> (ii) leave an existing party subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations because of the interest.

Fed. R. Civ. P. 19(a). The burden is on the party raising the defense to "show that the person who was not joined is needed for a just adjudication." *Am. Gen. Life & Acc. Ins. Co. v. Wood*, 429 F.3d 83, 92 (4th Cir. 2005) (internal citations omitted).

Fed. R. Bankr. P. 7004(c) provides

> If a party to an adversary proceeding to determine or protect rights in property in the custody of the court cannot be served as provided in Rule 4(e)-(j) F.R.Civ.P. or subdivision (b) of this rule, the court may order the summons and complaint to be served by mailing copies thereof by first class mail, postage prepaid, to the party's last known address, and by at least one publication in such manner and form as the court may direct.

Fed. R. Bankr. P. 7004(c) provides relief to rectify an issue with service upon named parties. Dixon has not demonstrated how the Association failed to join a necessary party or how its service by publication on the Returned Mail Defendants as well as the Doe, Roe, and Stoe Defendants renders dismissal appropriate under Fed. R. Civ. P. 12(b)(7).

IT IS, THEREFORE, ORDERED that Dixon's Motion to Dismiss is denied. Pursuant to Fed. R. Bankr. P. 7012(a), Dixon shall file an Answer to the Amended Complaint within fourteen (14) days from entry of this order.

IT IS SO ORDERED.