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BUSINESS LAW

I. CORPORATIONS

A. *Tender Offer Disclosure Act*

On June 12, 1978, the South Carolina General Assembly enacted the Tender Offer Disclosure Act[1] in an effort to supplement the federal regulation of cash tender offers. Similar legislation has been passed by thirty-two other states,[2] but the Fifth Circuit Court of Appeals recently declared such a statute unconstitutional.[3] That decision creates much uncertainty regarding the validity of the South Carolina statute.

The tender offer statute passed by the South Carolina General Assembly is applicable to cash tender offers[4] for the acquisi-

1. S.C. CODE ANN. § 35-2-10 to -110 (Cum. Supp. 1978).

2. For citations to these statutes see Great Western United Corp. v. Kidwell, 577 F.2d 1256, 1261 n.2 (5th Cir. 1978), *rev'd on other grounds*, 99 S. Ct. 2710 (1979).

3. Great Western United Corp. v. Kidwell, 577 F.2d 1256 (5th Cir. 1978), *rev'd on other grounds*, 99 S. Ct. 2710 (1979). On appeal to the United States Supreme Court, the Court did not reach the merits of the case, but rather reversed because venue did not lie in the Northern District of Texas, where the case originated. 99 S. Ct. at 2716-18. The analysis of the merits by the Fifth Circuit, though now a legal nullity, is presumed correct.

4. S.C. CODE ANN. § 35-2-20(2)-(3) (Cum. Supp. 1978) defines "tender offer" and excludes certain kinds of offers from the coverage of the Act.

> "Tender offer" means the offer to acquire or the acquisition of any equity security of a target company, pursuant to a tender offer or request or invitation for tenders, if after acquisition the offeror would be directly or indirectly a record or beneficial owner of more than ten percent of any class of the outstanding equity securities of the target company.

Id. 35-2-20(2).

> "Tender offer" does not include:
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> (a) An offer to purchase equity securities to be effected by a broker, registered under the laws of this State, on a stock exchange or in the over-the-counter market if the broker performs only the customary broker's function, and receives no more than the customary broker's commissions, and neither the principal nor the broker solicits or arranges for the solicitation of orders to sell such equity securities.
>
> (b) An offer made by a corporation to purchase its own equity securities, or equity securities of another corporation if more than fifty percent of the shares entitled to vote in the election of directors of the other corporations are held

tion of equity securities[5] of a target company incorporated or having its principal place of business in South Carolina, or having located within the state five hundred or more employees or assets in excess of $10,000,000.[6] Any offeror[7] making a tender offer that

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directly or indirectly by the offering corporation.

(c) An offer the acceptance of which will require a vote by stockholders of the target company, under the certificate of incorporation or the applicable corporation statute, on a merger, consolidation share exchange, reclassification of securities or sale of corporate assets in consideration, in whole or in part, of the issuance of securities of another corporation.

(d) An offer in which the acquisition by the offeror, in the instant transaction and in all acquisitions of equity securities of the same class during the preceding twelve months, does not exceed two percent of that class of equity securities of the target company.

(e) An offer for the sole account of the offer to not more than twenty-five beneficial owners of the equity securities in question within any consecutive twelve month period, in good faith and not for the purpose of avoiding this chapter.

(f) An offer solely in exchange for other securities, except to the extent of cash for fractions of a unit of securities, for the sole account of the offeror, in good faith and not for the purpose of avoiding this chapter, where the offeror has registered the offer pursuant to the terms of the Securities Act of 1933, as amended, and where the offer has also been registered under the provisions of the law of this State or is exempted from registration by the terms of the law.

Id. § 35-2-20(3).

5. *Id.* § 35-2-20(6) defines "equity security."

"Equity security" means (1) any stock, bond or other obligation of a corporation, the holder of which has the right to vote for the election of members of the board of directors of the corporation;

(2) any security convertible into a security carrying such rights; or

(3) any right, option or warrant to purchase any of the foregoing.

Id.

6. *Id.* § 35-2-20(5). The Act also specifically excludes certain types of businesses from the definition of "target company."

This chapter shall not apply to:

(1) An offer in which the target company is: (i) a domestic insurance company, as defined in Item (5) of § 38-1-20, Code of Laws of South Carolina, 1976, (ii) a bank, as defined in § 34-23-20(a), or a bank holding company as defined in § 34-23-20(b); (iii) a public utility company or a holding company, as defined in Section 2 of the Federal Public Utility Holding Company Act of 1935, presently constituted as Section 79 of Title 15 of the United States Code, an acquisition of or by, or merger with which, is subject to approval by the appropriate federal agency as provided in such act, or (iv) a bank or bank holding company subject to the Federal Bank Holding Company Act of 1956, presently constituted as Sections 1841, *et seq.* of Title 12 of the United States Code, an acquisition of or by, or merger with which, is subject to approval by the appropriate federal agency as provided in such act.

(2) A company which is not subject to the registration requirements of the Securities Exchange Act of 1934, presently constituted as Section 78 of Title 15 of the United States Code; *provided,* however, that a company excluded under the provisions of this item (2) of § 35-2-30 may, upon application to the Securi-

falls within the scope of this Act first must comply with the requirements of the South Carolina law, in addition to complying with the federal requirements promulgated under the Williams Act.[8]

Prior to 1968 cash tender offers were largely unregulated and shareholders were given little information to assist them in determining whether to accept a tender offer.[9] Congress passed the Williams Act in 1968 for the purpose of making "all relevant facts known so that shareholders [would] have a fair opportunity to make their decision."[10] The provisions of the Williams Act include disclosure requirements and substantive restrictions on tender offers. Specific information must be provided by any party making a tender offer that would result in ownership of more than 5% of a class of equity securities registered under section 12 of the Securities Exchange Act of 1934.[11]

The South Carolina statute differs from the Williams Act in several significant respects. Federal law requires that the offeror file a statement with the Securities and Exchange Commission at any time prior to the first publication of the offer.[12] The South Carolina statute contains a more restrictive provision, which requires that the offeror file with the state Securities Commissioner (the Secretary of State) and also with the management of the target company. This filing must be made twenty to forty days before the offer becomes effective.[13] The Commissioner has the option of waiving the twenty-day requirement and allowing the offer to be made prior to the completion of the waiting period.[14]

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ties Commissioner, be covered by the provisions of this chapter.

Id. § 35-2-30.

7. *Id.* § 35-2-20(7) defines "offeror."

> "Offeror" means a person who makes a tender offer, and includes persons, acting jointly or in concert, or who intend to exercise jointly or in concert any voting rights attached to the securities for which the tender offer is made. An "offeror" does not include any bank, broker-dealer, attorney, accountant or consultant furnishing information or advice to an offeror and not otherwise participating in the tender offer.

Id.

8. 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1976 & U.S.C.A. Supp. Pamph. 1978).

9. Sowards & Mopley, *Corporate Take-Over Bids: Gap in Federal Securities Regulation,* 41 ST. JOHN'S L. REV. 499 (1967).

10. H.R. REP. No. 1711, 90th Cong., 2d Sess. 3, *reprinted in* [1968] U.S. CODE CONG. & AD. NEWS 2811, 2813.

11. 15 U.S.C. §§ 78m(d), 78n(d) (1976 & U.S.C.A. Supp. Pamph. 1978).

12. *Id.*

13. S.C. CODE ANN. § 35-2-50(1) (Cum. Supp. 1978).

14. *Id.* § 35-2-60(1)-(2).

Conversely, if additional documents or material information are furnished after the initial filing and fewer than twenty days before the effective date of the offer, the Commissioner can postpone the offer until twenty days after the date of the filing of these additional documents.[15]

Although the Williams Act contains no provision for a pre-offer hearing concerning the tender offer, the South Carolina statute provides for a hearing to be held pursuant to the Commissioner's order[16] or a request and payment of a $200 fee by the management of the target company.[17] The hearing must be called within fifteen days after the filing of the registration statement (or the amendments) and must commence within ten days after being called. Within fifteen days after the conclusion of the hearing, the Commissioner must issue an order either permitting or prohibiting the tender offer.[18]

The disclosure requirements of the Williams Act are considerably less stringent than those of the South Carolina statute. The federal Act requires the filing to include the identity and background of the offeror, the source and amount of the funds, the number of shares in the target company already held by the offeror, major changes planned for the company after acquisition, any arrangements regarding the disposition of the stock, any other information that the Securities and Exchange Commission may require, and any subsequent changes thereto.[19] The South Carolina statute expands the required information to include the consideration to be offered, the dates on which the offer will begin and end, and any conditions placed upon acceptance of the tendered shares.[20] More importantly, the offeror must file copies of all literature to be furnished to the shareholder "by means of which the offeror proposes to disclose to offerees all information material to a decision to accept or reject the offer . . . ."[21] This provision places the offeror in an uncertain position in that he must decide whether to disclose potentially excessive information or to risk having the information disclose found incomplete. If the disclosure subsequently is ruled inadequate, substantial delay

15. *Id.* § 35-2-50(2).
16. *Id.* § 35-2-60(3).
17. *Id.* § 35-2-110.
18. *Id.* § 35-2-60(4).
19. 15 U.S.C. §§ 78m(d)(1)-(2), 78n(d)(1) (1976 & U.S.C.A. Supp. Pamph. 1978).
20. S.C. CODE ANN. § 35-2-50(1)(c), (d), (f) (Cum. Supp. 1978).
21. *Id.* § 35-2-50(1)(h).

could result or the Commissioner could totally prohibit the offer.

Requirements of the South Carolina statute concerning the duration of the offer and the withdrawal rights of shareholders also differ from federal law. Although the Williams Act contains no express requirements concerning the duration of the offer, the provision requiring the offeror to accept, on a *pro rata* basis, all shares tendered during the first ten days of the offer has been interpreted as requiring a minimum tender period of ten days.[22] The state Act, on the other hand, expressly requires a tender offer to remain open for twenty days, commencing on the day after the date of the first invitation to tender the securities.[23] The Williams Act permits a shareholder to withdraw his shares prior to the end of the seventh day of the tender period or any time after the sixtieth day, provided these shares have not been purchased.[24] The South Carolina statute allows withdrawal during the first twenty days and also following the thirty-fifth day after commencement of the offer.[25]

As discussed above, the South Carolina statute contains several provisions that substantially conflict with the federal requirements. A significant possibility exists, therefore, that these provisions will be declared invalid. A similar Idaho statute was struck down in *Great Western United Corp. v. Kidwell,*[26] the first case in which a federal court examined the conflict between federal and state tender offer regulations.

The Idaho statute, like the South Carolina Act, contained provisions requiring the offeror to submit a copy of the filing statement to the management of the target company in addition to filing with state officials and also contained provisions granting a pre-offer hearing.[27] Substantial authority was given to the Idaho Director of Finance, including the power to summarily delay the effectiveness of the tender offer if the registration statement were determined to be insufficient.[28]

The Fifth Circuit Court of Appeals invalidated the Idaho statute on grounds that federal law had pre-empted the area and

22. E. ARANOW, H. EINHORN & S. BERNSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 214 (1977).
23. S.C. CODE ANN. § 35-2-70(2) (Cum. Supp. 1978).
24. 15 U.S.C. § 78n(d)(5) (1976 & U.S.C.A. Supp. Pamph. 1978).
25. S.C. CODE ANN. § 35-2-70(3) (Cum. Supp. 1978).
26. 577 F.2d 1256 (5th Cir. 1978), *rev'd on other grounds*, 99 S. Ct. 2710 (1979).
27. *Id.* at 1263.
28. *Id.*

that the statute unconstitutionally interfered with interstate commerce. The court did not address whether Congress had implicitly pre-empted *all* state tender offer statutes by passage of the Williams Act, but rather limited its ruling to situations in which the state statute conflicted with the federal legislation.[29]

The court placed great emphasis upon the conflict between the basic purpose of the Williams Act and the situation that would result from enforcement of the state statute. The Williams Act was designed "to maintain a neutral policy toward cash tender offers, by avoiding lengthy delay that might discourage their chances for success."[30] The Idaho statute, like the South Carolina Act, favored target companies through provisions not found in the federal Act, including advance notice of the tender offer and the means to delay the offer by utilizing the pre-offer hearing provisions.[31] The court held that the Idaho statute was pre-empted because the state's promanagement additions to the federal disclosure requirements produced a substantial obstacle to the accomplishment of the federal goal of enabling investors to make an objective and informed decision regarding a tender offer.[32]

Additionally, the court invalidated the statute on the ground that it substantially interfered with interstate commerce, finding that the statute significantly affected interstate transactions because it would apply even in situations in which no stockholder resided in Idaho and no securities transaction occurred within that state.[33] The state's interest in protecting investors and in regulating local companies was not sufficient to justify the great impact such legislation has upon interstate commerce. The burdens were held to be "disproportionate to the legitimate benefits" provided by the Idaho law.[34]

The decision in *Great Western United Corp. v. Kidwell* places the future of the South Carolina Tender Offer Disclosure Act upon unfirm ground. The South Carolina Act is similar to the Idaho Act, and therefore may be successfully challenged in federal court.

29. *Id.* at 1275.

30. *Id.* at 1278 (quoting H.R. REP. No. 1373, 94th Cong., 2d Sess. 12, *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 2572, 2644).

31. 577 F.2d at 1278.

32. *Id.* at 1280.

33. *Id.* at 1283.

34. *Id.* at 1286.

B. Fraudulent Sale of Securities

In *Bradley v. Hullander*[35] the South Carolina Supreme Court recognized a right of action under South Carolina Code section 35-1-1490[36] for rescission of a contract. The defrauded buyers were allowed to rescind the contract and additionally were granted costs and attorneys' fees, as provided by the statute. By bringing the action under section 35-1-1490 rather than common law fraud the buyers had a substantially less stringent burden of proof, which enabled them to prevail.

The conflict between the parties arose out of the sale to plaintiffs of the defendants' automobile dealership.[37] Following negotiations between the parties, a stock purchase agreement was signed that provided for a total purchase price of $200,000 plus any increase in net worth occurring between the date of the execution of the agreement and the time at which the plaintiffs assumed control of the business. The record evidences some disagreement regarding the extent to which plaintiffs examined the financial documents prior to closing the transaction.[38]

Shortly after the plaintiffs took over the daily business operations of the dealership, they employed the services of a certified public accountant to determine the financial status of the corpo-

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35. 272 S.C. 6, 249 S.E.2d 486 (1978).

36. S.C. Code Ann. § 35-1-1490 (1976) provides that:

Any person who:

(1) Offers or sells a security in violation of subsection (2) of § 35-1-170 or § 35-1-410 or § 35-1-810, or of any rule or order under § 35-1-50 which requires the affirmative approval of sales literature before it is used or of any condition imposed under § 35-1-950 or § 35-1-990; or

(2) Offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, the buyer not knowing of the untruth or omission, and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission;

Is liable to the person buying the security from him, who may sue either at law or in equity to recover the consideration paid for the security, together with interest at six per cent per year from the date of payment, costs, and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he no longer owns the security. Damages are the amount that would be recoverable upon a tender less the value of the security when the buyer disposed of it and interest at six per cent per year from the date of dispositon.

Id.

37. Brief of Appellants-Respondents at 3.

38. *See id.*

ration as of the date on which they had assumed control. This audit revealed substantial discrepancies between the actual financial condition of the business and the representations made in the sales agreement. The buyers immediately instituted legal action, alleging misrepresentation of the net worth of the company.[39] An agreement was reached that provided for partial rescission of the purchase and sale transaction and returned control of the corporation to the defendants. The case continued in the courts, however, to determine the extent of plaintiffs' recovery.[40]

Defendants asserted a two-fold argument regarding the merits of the case. First, the defendants claimed that the action was actually one for breach of warranty; therefore, no action could lie under the Uniform Securities Act[41] unless it were shown that the warranties were inserted voluntarily in the contract by the sellers, rather than at the insistence of the buyers, and that the sellers were aware of the falsity of such warranties.[42] The defendants argued that, in fact, the warranties had been inserted at the insistence of the buyers and therefore no action for breach of warranty should be allowed.[43]

Defendants' second argument rested on the ground that, in an action brought under section 35-1-1490, the buyer must prove that false representations were made by the seller and additionally, that the buyer had no knowledge of the truth.[44] In support of this contention, the defendants cited several federal decisions dealing with the Securities Act of 1933[45] upon which the South Carolina statute is based.[46] Furthermore, the defendants claimed

39. 272 S.C. at 13-14, 249 S.E.2d at 488-89.

40. *Bradley* also involved several complex procedural and evidentiary aspects that will not be discussed here. Defendants additionally questioned whether the financial statements actually contained any misrepresentation of the net worth of the company. The issue will not be discussed in this survey because both the trial judge and the supreme court felt that the evidence conclusively favored the buyers. For discussions of the contents of these financial statements, *compare* Brief of Appellants-Respondents at 21 *with* Brief of Respondents-Appellants at 18. Finally, the supreme court considered whether parole evidence was admissible to show any representations or warranties extrinsic to the writing. The court held that such evidence was not admissible. See note 44 *infra*.

41. S.C. CODE ANN. §§ 35-1-10 to -1590 (1976 & Cum. Supp. 1978).

42. Brief of Appellants-Respondents at 12-13.

43. *Id.*

44. *Id.* at 15. The trial judge refused to allow testimony of defendants on the question of whether the buyers knew of the unsoundness of the warranties on the grounds that this would violate the parole evidence rule and that a seller is estopped from asserting the untruth of his own statements as a defense. 272 S.C. at 28-33, 249 S.E.2d at 498-99.

45. 15 U.S.C. §§ 77a-77aa (1976 & U.S.C.A. Supp. Pamph. 1978).

46. Brief of Appellants-Respondents at 16.

that in order to allow recovery under section 35-1-1490 some evidence of actual fraud or scienter (intent to defraud) must be present in the seller's actions. The trial court had ruled that no such intent on the part of the sellers existed; therefore, defendants argued, no recovery should have been granted.[47]

In reply to the defendants' first argument, the plaintiffs contended that there is no South Carolina authority holding that a fraud action cannot be maintained based on false warranties extracted by the buyers; however, even if such authority did exist, it would not be applicable to actions brought under the Uniform Securities Act.[48] According to the plaintiffs, the Uniform Securities Act makes no distinction between breach of warranty and fraud.[49] The plaintiffs further argued that no finding of actual fraud or scienter on the part of the seller was necessary.[50] South Carolina Code section 35-1-1490, in effect, makes the seller liable regardless of his intent, unless the seller can demonstrate that his actions were free from negligence. A finding of lack of scienter is not equivalent to a finding of due diligence.[51]

The decision of the trial court in favor of the buyers was adopted in large part by the supreme court. The original order of Judge Coleman granting rescission and awarding costs and attorneys' fees was incorporated into the supreme court's ruling. Judge Coleman looked to section 12(2) of the Securities Act of 1933[52] for guidance in interpreting the South Carolina statute. Accordingly, he ruled that the plaintiffs were required to demonstrate only that the defendants misstated or omitted certain material facts and that the plaintiffs were not aware of the truth. The trial court further ruled that a seller may violate the Uniform Securities Act by mere negligence; no intent to defraud is necessary to maintain the action.[53]

The trial judge concluded that the written statements made by the sellers in the sales agreement "clearly [met] the test of materiality"[54] required by section 35-1-1490.[55] The Uniform Se-

47. *Id.* at 19.
48. Brief of Respondents-Appellants at 7.
49. *Id.*
50. *Id.* at 15.
51. *Id.* at 16.
52. 15 U.S.C. 77*l*(2) (1976).
53. 272 S.C. at 32-33, 249 S.E.2d at 499.
54. *Id.* at 23, 249 S.E.2d at 495.
55. See note 36 *supra.*

curities Act does not require buyers to show reliance, causation, or that the sale would not have occurred absent the misstatement of material fact.[56] Judge Coleman further concluded that the statements contained in the balance sheet were untrue and that the buyers were unaware of the falsity of the statements.[57]

The South Carolina Supreme Court unanimously agreed with Judge Coleman's reasoning and affirmed his order with one exception. The lower court had refused to order the sellers to reimburse the buyers for the brokerage commission that the buyers had paid. The supreme court reversed the ruling, holding that the commission was attributable to the sellers' fraudulent conduct and therefore was a proper element of the buyers' statutory recovery.[58]

The decision of the supreme court in *Bradley v. Hullander* opens the door for further litigation under section 35-1-1490. Defrauded buyers may utilize this statutory cause of action rather than rely on common-law fraud. As demonstrated by the court's ruling in *Bradley,* actions brought under this section are considerably less difficult to prove than common-law actions. As interpreted by the court, the statute requires only that material misrepresentations or omissions be made and that the plaintiff have no knowledge of the truth. Reliance and causation need not be proved,[59] nor is it necessary for the plaintiff to show that he could not have discovered the falsity through due diligence.[60] Perhaps most importantly, under the statute the seller must assume the burden of proving lack of negligence, but under common law the burden is on the buyer to show actual intent to defraud on the part of the seller.[61]

The statute relied upon in *Bradley* also provides for extensive damages.[62] In addition to rescission, the defrauded buyer can recover costs and attorneys' fees. This statutory damage provision is yet another advantage to bringing an action under section 35-1-1490 rather than relying upon common-law fraud.

56. 272 S.C. at 22, 249 S.E.2d at 495 (citing Hill York Corp. v. American Int'l Franchises, Inc., 448 F.2d 680, 696 (5th Cir. 1971) and Demarco v. Edens, 390 F.2d 836, 841 (2d Cir. 1968)).

57. 272 S.C. at 22, 249 S.E.2d at 495.

58. *Id.* at 39-40, 249 S.E.2d at 502.

59. *Id.* at 22, 249 S.E.2d at 494.

60. *Id.* (citing Gilbert v. Nixon, 429 F.2d 348, 356 (10th Cir. 1970)).

61. *Id.* (citing Wilko v. Swan, 346 U.S. 427, 431 (1953)).

62. See note 36 *supra.*

II. INSURANCE LAW — AUTOMOBILE INSURERS' RIGHT TO CANCEL CONTRACTS WITH INDEPENDENT AGENCIES

In *G-H Insurance Agency, Inc. v. Travelers Insurance Companies*[63] the South Carolina Supreme Court ruled that the state statute prohibiting insurers from cancelling an agency agreement primarily to avoid writing insurance for high risk customers was not intended merely for the protection of the public, but was also intended to protect the private rights of insurance agents.[64] This decision reversed the lower court's ruling[65] that South Carolina Code section 38-37-940(2)[66] did not create a private cause of action. The supreme court limited its decision to a determination that the cancellation of the agency contract was wrongful and a private right of redress existed. The issues of the constitutionality of the statute and the potential impairment of the right to contract were not resolved until later in the year when the court decided *Rowell v. Harleysville Mutual Insurance Co.*[67]

The conflict between the parties in *G-H Insurance Agency* arose out of Travelers' attempt to terminate the agency relationship that had existed between the parties since 1972. G-H had operated as an independent agency for several years, soliciting and writing automobile insurance for Travelers under an agency contract.[68] Prior to the 1974 enactment of Act 1177,[69] which revised South Carolina insurance law, Travelers had encouraged G-H to solicit and write insurance for persons classified as nonstandard or high risks.[70] Prior to 1974 these high risk individuals could be charged higher premiums than those charged standard risk individuals. As a result of Travelers' encouragement, approxi-

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63. 270 S.C. 147, 241 S.E.2d 534 (1978).

64. *Id.* at 152, 241 S.E.2d at 536.

65. *Reprinted in* 270 S.C. 147, 155-76, 241 S.E.2d 534, 537-48 (Littlejohn and Ness, JJ., dissenting).

66. S.C. CODE ANN. § 38-37-940(2). This subsection provides:

> No insurer of automobile insurance shall cancel its representation by an agent primarily because of the volume of automobile insurance placed with it by the agent on account of the statutory mandate of coverage nor because of the amount of the agent's automobile insurance business which the insurer has deemed it necessary to reinsure in the Facility.

Id.

67. ___ S.C. ___, 250 S.E.2d 111 (1978). See text accompanying notes 95-122 *infra*.

68. Brief of Appellant at 1.

69. Codified at S.C. CODE ANN. §§ 38-37-10 to -1520 (1976 & Cum. Supp. 1978).

70. 270 S.C. at 149, 241 S.E.2d at 534.

mately half of the policies that G-H wrote for Travelers were nonstandard risk policies.[71] Travelers consequently benefited from the higher premiums. Following revision of the state's insurance laws, classification of policy holders according to risk was no longer permitted except under plans promulgated by the Insurance Commissioner.[72] This change forced all automobile insurers, including Travelers, at least temporarily to charge standard rates to all customers.

Shortly after this revision in the state law, Travelers notified G-H that it wished to terminate the agency contract between the parties, giving rise to the present case. G-H, believing that Travelers desired to cancel the contract to avoid insuring the high risk customers that comprised a large portion of G-H's business, initially applied to the Insurance Commissioner to prohibit the termination. The Commissioner refused to take the requested action, claiming he was without authority to intervene. G-H then brought suit to enjoin the termination and also to recover damages resulting from the cancellation of the agency contract.[73]

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71. *Id.*

72. S.C. CODE ANN. § 38-37-320 (1976). The section provides:

> No distinctions shall be permitted nor made between policyholders or applicants for such automobile insurance as respects coverages, policy terms, rates, premium payment arrangements, claim services, or other services provided by the insurer directly or through its agents or employees except as such distinctions are relevant to and reflected in insurers' rating classifications under risk and territorial classification plans promulgated by the Commissioner and approved by the Commission. No such risk classification plan shall be so promulgated or approved unless the criteria used for classifying risks are objective, clear and unequivocal and based upon factually or statistically supported data, nor unless the classifications in the rating plan are calculated to render possible the compilation of credible statistical data both for purposes of determining premiums and losses and for comparing the relative relationships between the loss or expense experience or both of the respective classes. As regards its approval or disapproval of risk and territorial classification plans, the Commission shall be guided as respects the exercise of its discretion by the legislative intent of Articles 1 to 15 of this chapter which is to make it possible for the Commissioner to determine the total profit or loss and expense operating results of the entire line of automobile insurance and each component thereof and of each automobile insurer transacting insurance within the line and each component and to make price comparisons between the rates and premium charges of the various insurers; it being the further policy of Articles 1 to 15 of this chapter to render possible the evaluation by the Commissioner of the performance of the total insurance market and to enable him thereby to assist automobile insurance consumers in making appropriate consumer decisions.

Id.

73. 270 S.C. at 150, 241 S.E.2d at 535.

The lower court sustained Travelers' demurrer to the complaint, stating that section 38-37-940(2) did not grant a private cause of action.[74] Judge Bristow based his decision primarily on the fact that Act 1177 contained no provision establishing civil liability. According to the order granting the demurrer, because the statute expressly provided for administrative sanctions,[75] this remedy precluded any private recovery.[76] The issue was subsequently appealed to the South Carolina Supreme Court.

G-H argued that a private cause of action was created by section 38-37-940 on the ground that the revised state insurance laws had been enacted for the purpose of providing "a *system* of automobile insurance that makes insurance available to all qualified applicants on a nondiscriminatory basis."[77] In order to assure the success of this system, independent agents such as G-H must be given an important role in implementing the modification of the state's insurance laws brought about by Act 1177.[78] G-H argued that this Act modified Travelers' unilateral right to terminate the agency agreement that existed between the parties and that the state had the authority to modify this contractual right since regulation of the insurance industry is a responsibility and legitimate function of state government.[79] According to G-H, although Travelers had lost its right to terminate an insurance agent who primarily wrote policies for high risk customers, this statute was not completely one-sided. An insurance company such as Travelers is permitted to cede up to thirty-five percent of its total business to the Reinsurance Facility,[80] thereby spreading the risk among all companies doing business in South Carolina. This provision allows an insurance company to lessen the impact of any high risk policies written by its agents. Additionally, an insurance company may apply for higher premium rates in order to offset any losses caused by the volume of high risk business.[81]

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74. Record at 64, 66.

75. S.C. CODE ANN. § 38-37-940 states, in part: "Any act in violation of this section shall constitute an act of unlawful discrimination and unfair competition which, if willful, shall result in the suspension or revocation of the insurer's certificate of authority for not less than six months . . . ." *Id.*

76. Record at 64.

77. Brief of Appellant at 7 (emphasis added).

78. *Id.*

79. *Id.* at 15.

80. S.C. CODE ANN. §§ 38-37-710, -950 (1976).

81. *Id.* § 38-37-780.

G-H's cause of action was based upon the theory of "unfair competition."[82] The appellant claimed that Travelers' actions were discriminatory and could be characterized as unfairly competitive within the language and purposes of section 38-37-940.[83] G-H argued that conduct designed to avoid the statutory mandate of nondiscriminatory insurance coverage could be characterized as "unfair competition."[84] Travelers' cancellation of the agency contract merely because its agent had a high volume of nonstandard risk policies was indicative of the inherent imbalance of power between the insurance company and its independent agent and demonstrated the great potential for unfair trade practices.[85]

Travelers contended that no private cause of action was created by Act 1177 because section 38-37-940 was "plainly a regulatory statute designed to prohibit wrongs to the public."[86] Travelers asserted that the state legislature intended Act 1177 to be enforced by the Insurance Commission rather than by independent agents such as the appellant. The respondent relied upon the South Carolina Supreme Court's decision in *Taggart v. Home Finance Group, Inc.*[87] in which the court ruled that statutes regulating insurance companies and their agents do not establish any private right of action.[88]

Travelers also contended that, even if the statute in question could be construed to grant a private cause of action, G-H should not be included in the class of persons that the statute was designed to protect.[89] This argument was based on the assumption that the primary purpose of the statute was to protect members of the public; the statute was not intended to provide insurance agents with protection from the cancellation of their agency contracts.[90]

In reaching its decision in favor of G-H, the South Carolina Supreme Court viewed the action as one for the wrongful cancellation of an agency contract, rather than one raising the question

82. Brief of Appellant at 20.
83. *Id.* See note 75 *supra.*
84. Brief of Appellant at 23.
85. *Id.* at 26.
86. Brief of Respondent at 8.
87. 239 S.C. 345, 123 S.E.2d 250 (1961).
88. *Id.* at 346, 123 S.E.2d at 252.
89. Brief of Respondent at 16.
90. *Id.* at 18-19.

of whether the statute created a private cause of action.[91] According to the court, the statute was relevant only in determining whether the action taken by Travelers in cancelling the contract was unlawful. Chief Justice Lewis, writing for the majority, held that if section 38-37-940 were enacted for the agents' benefit, then clearly Travelers' action must be considered wrongful.[92] The court concluded that the purpose of Act 1177 extended beyond mere protection of the public. The language of the statute was interpreted to provide protection for the private rights of insurance agents as well as for the public at large. Therefore, any agent who was terminated for unlawful reasons could recover damages sustained as a result of such termination.[93]

Two members of the court dissented from the majority opinion in *G-H Insurance Agency.* The dissent incorporated Judge Bristow's original order sustaining Travelers' demurrer and was based upon an interpretation of legislative intent. According to the dissenting justices, the statute should not be interpreted to broaden its protection beyond members of the public.[94]

The court's decision in *G-H Insurance Agency* was limited to the issue of statutory interpretation. Several months later in *Rowell v. Harleysville Mutual Insurance Co.*,[95] the court was presented with the question of whether the statute interpreted in *G-H Insurance Agency*, section 38-37-940, was unconstitutional in that it operated as an impairment of the insurer's contractual right to cancel an agency relationship. The court, having previously held in *G-H Insurance Agency* that this provision permitted a private right of action by an independent agent against an insurance company that had unlawfully terminated an agency contract,[96] used the opportunity presented in *Rowell* to expand its previous ruling and hold that Act 1177 was not an unconstitutional impairment of the contractual rights of the insurance company.[97]

The facts in *Rowell* are quite similar to those in *G-H Insurance Agency.* In 1973 Harleysville Mutual Insurance Company entered into a contract with Rowell, an independent agency, au-

91. 270 S.C. at 152, 241 S.E.2d at 536.
92. *Id.*
93. *Id.*
94. *Id.* at 154, 241 S.E.2d at 537 (Littlejohn and Ness, JJ., dissenting).
95. ___ S.C. ___, 250 S.E.2d 111 (1978).
96. 270 S.C. at 152, 241 S.E.2d at 536.
97. ___ S.C. at ___, 250 S.E.2d at 114.

thorizing Rowell to solicit and write automobile insurance for Harleysville. Many of the policies written by Rowell were for nonstandard risk motorists for which Harleysville received higher than ordinary premiums.[98] Following the 1974 passage of Act 1177,[99] however, it was no longer permissible to charge higher premiums to nonstandard risks, making the business Harleysville received from Rowell much less profitable than it previously had been. Harleysville made several attempts to induce Rowell to reduce the amount of automobile insurance written for Harleysville. When these efforts were unsuccessful, Harleysville terminated the agency relationship pursuant to the terms of the contract between the parties, which permitted unilateral termination upon sixty days notice.[100]

Rowell subsequently brought an action for injunctive relief, alleging that Harleysville had violated section 38-37-940(2).[101] The lower court, in a hearing on the merits of the case, ruled in favor of Harleysville.[102] Judge Singletary, although recognizing that many other courts have ruled to the contrary,[103] concluded that the statutory prohibition against termination of an existing agency relationship operated as an unconstitutional modification of the obligations under the contract.[104] According to the lower court's order, the contract between the parties was in existence prior to the passage of Act 1177 and conformed to the law in effect at the time of its execution. A retroactive application of the statute would "render nugatory the consent which formed the basis of the contract."[105] This decision was subsequently appealed to the South Carolina Supreme Court.

Rowell advanced arguments similar to those that had been successful earlier in *G-H Insurance Agency*. Emphasis was placed upon the designation of the insurance statutes as a "system" designed to make automobile insurance available to all South Carolina drivers and to distribute the high risk business among all insurers doing business within the state.[106] Rowell further con-

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98. Brief of Appellant at 1-2.
99. See note 69 *supra*.
100. Brief of Appellant at 3.
101. See note 66 *supra*.
102. Record at 24.
103. *Id.* at 17.
104. *Id.* at 24.
105. *Id.* at 18.
106. Brief of Appellant at 9.

tended that the right to contract is not an absolute right, but may be reasonably regulated if such regulation is in the best interest of the community. Such legislation, because of the general power of the state, carries with it a presumption of constitutionality.[107] Rowell urged that these two principles combined to place the burden on Harleysville to prove that the enactment of the challenged statute was so arbitrary and unnecessary that the presumption of constitutionality should not stand.[108]

Rowell also argued that the authority of an insurance company such as Harleysville to operate within South Carolina originates with the license granted to the company by the state.[109] This license implies that the company is subject to all applicable state legislation. The appellant argued that the constitutional prohibition against impairment of contract does not extend to licenses, and thus any change in state regulations would continue to affect the licensee.[110] Rowell took issue with the lower court's characterization of Act 1177 as retroactive, arguing that the legislation was "remedial" because it was designed to remedy prior existing conditions;[111] therefore, it should not fall within the definition of a retroactive law. The appellant further argued that Harleysville had no reasonable expectation that the insurance law of South Carolina would not change because the statute clearly states that all insurance companies doing business within the state would be expected to "perform all duties now or hereafter prescribed by law."[112]

Harleysville countered these arguments by relying heavily on the consensual nature of the contract. According to the respondent, parties to a contract are entitled to rely upon the law that exists at the time the contract is executed. To allow such agreements to be subsequently altered by the state legislature would be contrary to the protection afforded contracts by the Constitution.[113] Additionally, Harleysville argued that the provision of the Act that prohibits the termination of an agency relationship[114]

107. *Id.* at 17-18 (citing Beaufort County v. Jasper County, 220 S.C. 469, 479, 63 S.E.2d 421, 426 (1951); Gaud v. Walker, 214 S.C. 451, 462, 53 S.E.2d 316, 320 (1949); Mosely v. Welch, 209 S.C. 19, 26-27, 39 S.E.2d 133, 137 (1946)).

108. Brief of Appellant at 21.

109. *Id.* at 33.

110. *Id.* at 40.

111. *Id.* at 49.

112. S.C. CODE ANN. § 38-5-70 (1976).

113. Brief of Respondent at 17.

114. See note 66 *supra*.

was not designed to serve a public purpose; therefore, Act 1177 should not be used to prevent the action taken by Harleysville.[115] The respondents pointed to the *G-H Insurance Agency* decision in which the supreme court held that the statute was designed not only to benefit the public, but also to provide relief for insurance agents. According to Harleysville, this statutory purpose was not sufficient to "require or warrant indefinite restriction of an existing contractual right."[116]

The South Carolina Supreme Court reversed the lower court and ruled that application of the statute to prevent the cancellation of insurance agency contracts could not be viewed as unconstitutionally impairing existing contractual rights or obligations.[117] In this decision, as in the earlier ruling in *G-H Insurance Agency,* the court relied heavily on the theory that Act 1177 was designed to provide a "system" of insurance coverage. The court accepted the contention that the respondents possessed no vested rights under the contract and therefore could claim no constitutional protection.[118] According to the court, Harleysville applied for and accepted the state license with full knowledge that the license was subject to the reservations set forth in section 38-5-70.[119] The provision restricting the company's right to terminate was well within the regulatory power of the state and was remedial in nature. The court indicated, however, that the statute was effective only in preventing *retaliation* by the insurance company against the agent and did not affect Harleysville's right to cancel the contract for any other reason.[120]

Justices Littlejohn and Ness dissented from the majority opinion, just as they had in *G-H Insurance Agency.* They found nothing in Act 1177 to indicate that the legislature intended to adversely affect existing contracts.[121] According to the dissent, the nullification of existing contractual rights allowed by the majority opinion constituted a violation of the constitutional prohibi-

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115. Brief of Respondent at 21.

116. *Id.* at 24.

117. ___ S.C. at ___, 250 S.E.2d at 114.

118. *Id.* at ___, 250 S.E.2d at 113.

119. S.C. CODE ANN. § 38-5-70 (1976) states: "Every insurance company shall, as a condition for the privilege of entering into and doing business in this State, pay all taxes and *perform all duties now or hereafter prescribed by law." Id.* (emphasis added). See text accompanying note 112 *supra.*

120. ___ S.C. at ___, 250 S.E.2d at 114.

121. *Id.* at ___, 250 S.E.2d at 115 (Littlejohn and Ness, JJ., dissenting).

tion against impairing the right to contract.[122]

The decisions of the supreme court in *G-H Insurance Agency, Inc. v. Travelers Insurance Companies* and *Rowell v. Harleysville Mutual Insurance Co.* seemingly foreclose future litigation on the issue of the rights given to insurance agents by section 38-37-940. Insurance companies can no longer terminate an agency relationship simply because it is unprofitable. Unless new legislation is passed altering section 38-37-940, an insurance company that desires to do business in South Carolina will be subject to an action for damages if it unlawfully cancels an agency agreement.

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122. *Id.* at ____, 250 S.E.2d at 116 (Littlejohn and Ness, JJ.. dissenting).