

Spring 2004

## Facing the Fear of Fraud: The Rise of Senate Bill 555 after the Fall of Carolina Investors

Jennifer L. Hess

Follow this and additional works at: <https://scholarcommons.sc.edu/sclr>



Part of the [Law Commons](#)

---

### Recommended Citation

Hess, Jennifer L. (2004) "Facing the Fear of Fraud: The Rise of Senate Bill 555 after the Fall of Carolina Investors," *South Carolina Law Review*. Vol. 55 : Iss. 3 , Article 17.

Available at: <https://scholarcommons.sc.edu/sclr/vol55/iss3/17>

This Article is brought to you by the Law Reviews and Journals at Scholar Commons. It has been accepted for inclusion in South Carolina Law Review by an authorized editor of Scholar Commons. For more information, please contact [dillarda@mailbox.sc.edu](mailto:dillarda@mailbox.sc.edu).

Hess: Facing the Fear of Fraud: The Rise of Senate Bill 555 after the F

# **FACING THE FEAR OF FRAUD: THE RISE OF SENATE BILL 555 AFTER THE FALL OF CAROLINA INVESTORS**

## **I. INTRODUCTION**

The economic well-being of thousands of South Carolinians was jeopardized by the recent discovery of the severe instability of two South Carolina companies. Last spring, Carolina Investors and HomeGold Financial filed for bankruptcy, leaving investors to question whether they will ever recover \$275 million in investments. Thousands invested their savings in Carolina Investors' investments. This money was then used by HomeGold to finance its lending operation. HomeGold's inability to turn a profit led to its eventual demise, leaving Carolina Investors without the money it owed its investors.

One outgrowth of this tragedy was Senate Bill 555, which Governor Mark Sanford signed into law on June 4, 2003. This piece of legislation seeks to protect investors by giving the state grand jury jurisdiction over crimes involving securities fraud. It also extends the statute of limitations period for these crimes to three years after the violations are discovered or after discovery should have been made by the exercise of reasonable diligence.

This Note focuses on the statute of limitations provision of this new law. Part II sets forth the background that led to the enactment of this legislation, as well as some of the legislative history. Part III analyzes the implications of this new law and explains the approaches of several other states. Part IV concludes that this legislation should boost investors' opportunities for recoveries in fraud cases and restore some of the confidence lost in the wake of recent events. However, the legislation may increase the liability of businesses in the state.

## **II. IMPETUS FOR THE ENACTMENT OF SENATE BILL 555**

### *A. Carolina Investors/HomeGold Financial Debacle*

The recent collapse of two South Carolina companies, Carolina Investors and HomeGold Financial, eroded the financial security of thousands of South Carolinians.<sup>1</sup> On March 24, 2003, Carolina Investors closed its offices, leaving 8,000 investors with little hope of recovering investments totaling about \$275 million.<sup>2</sup> For many, investments in Carolina Investors comprised life savings or

---

1. David Dykes, *Investors Case May Bring Stiff Punishments*, GREENVILLE NEWS, Sept. 4, 2003, at 11A.

2. *Id.*

retirement funds.<sup>3</sup> As the investigation continues to evolve, uncertainty and doubt surround the legitimacy of Carolina Investors/HomeGold's operations.<sup>4</sup>

Dwight Holder formed Carolina Investors in 1963 to help people purchasing his cemetery plots attain financing.<sup>5</sup> In 1991, Holder sold Carolina Investors to Emergent Group.<sup>6</sup> Emergent Group subsequently formed a subsidiary, HomeGold Financial.<sup>7</sup> This subsidiary specialized in non-prime mortgages, targeting home owners who needed loans for other purposes, such as for college tuition, but who had bad credit.<sup>8</sup> It profited by charging high interest rates to this high-risk market.<sup>9</sup> Carolina Investors, as one of HomeGold's subsidiaries, became a means to raise funds for HomeGold's mortgage lending.<sup>10</sup> Carolina Investors sold notes and bonds to investors that offered five to eight percent annual returns—substantially more than banks offer on savings and CD accounts.<sup>11</sup> However, unlike CDs from banks, the investments offered by Carolina Investors were not insured by the FDIC.<sup>12</sup> HomeGold used the money earned from the sales of these notes and bonds to finance its lending operations.<sup>13</sup> In 1998, HomeGold stopped making a profit and began losing money.<sup>14</sup> In an attempt to boost business, some HomeGold employees began making questionable loans which further contributed to the losses.<sup>15</sup> Losses continued over the next three years, and HomeGold continued to use Carolina Investors' proceeds to finance its operation.<sup>16</sup> In an alleged effort to get itself out of debt, HomeGold merged with a retail mortgage company, HomeSense, which was a South Carolina based, privately owned company that had a business similar to HomeGold. The significant distinction between the two companies was that

3. Joe Guy Collier, *Carolina Investors Held Community's Life Savings*, THE STATE (Columbia, S.C.), Apr. 6, 2003, at F1.

4. See, e.g., R. Kevin Dietrich & Chris Roberts, *\$280 Million in Debt and Key Assets Gone, Company Looks to Survive Bankruptcy*, THE STATE (Columbia, S.C.), Apr. 6, 2003, at F1.

5. WYFF The Carolina Channel.com, *From Gravesites to Death's Door: Carolina Investors' Rise and Fall* (July 28, 2003), available at <http://www.thecarolinachannel.com/money/2156722/detail.html>.

6. *Id.*

7. Dietrich & Roberts, *supra* note 4, at F3.

8. *Id.*

9. *Id.*

10. Joe Guy Collier, *Securities Investigations Tax S.C. Regulation System*, THE STATE (Columbia, S.C.), Apr. 9, 2003, at B6.

11. R. Kevin Dietrich, *HomeGold Unit to Seek Bankruptcy*, THE STATE (Columbia, S.C.), Apr. 5, 2003, at B8.

12. *Id.*

13. *Id.* at B6.

14. Steven A. Long, *How HomeGold Turned to Dust*, THE STATE (Columbia, S.C.), Apr. 6, 2003, at F1.

15. Dietrich & Roberts, *supra* note 4, at F3 (quoting former employees who stated they charged higher fees to customers and targeted less educated and desperate customers).

16. *Id.*

HomeSense was still profitable.<sup>17</sup> Losses continued while HomeGold borrowed more and more assets from Carolina Investors.<sup>18</sup>

In the face of nearly \$300 million in debt, public concern began to grow.<sup>19</sup> In 2001, the state Attorney General's Office began inquiring into the situation.<sup>20</sup> Several meetings were requested with HomeGold officials to discuss the massive debt owed to Carolina Investors.<sup>21</sup> In April 2002, Elliott Davis, HomeGold's accounting firm, questioned the company's financial stability.<sup>22</sup> Later that year, Elliott Davis resigned as HomeGold's auditor.<sup>23</sup>

On March 24, 2003, Carolina Investors closed its offices while reassuring investors that their investments were safe.<sup>24</sup> Days later, Henry McMaster, South Carolina Attorney General, announced a formal investigation of Carolina Investors.<sup>25</sup> On March 31, 2003, HomeGold announced it had filed for Chapter 11 bankruptcy.<sup>26</sup> Carolina Investors filed for Chapter 11 fewer than two weeks later.<sup>27</sup> The investors remain unpaid.

### B. *The Aftermath: Legislative History of Senate Bill 555*

Legislators proposed sweeping changes to South Carolina's securities laws soon after Carolina Investors filed for Chapter 11. State Senator Larry Martin of Pickens County introduced Senate Bill 555<sup>28</sup> as a direct response to the crisis. The Bill extends the statute of limitations for securities fraud from "three years after the contract for sale"<sup>29</sup> to three years from the time the fraud is discovered or should have been discovered by reasonable diligence.<sup>30</sup> It also empowers a state grand jury to investigate and enforce state securities laws.<sup>31</sup> Recognizing that charges have not been filed and may never be filed in the Carolina Investors case, Senator Martin hoped to take the necessary measures to ensure that the state would be able to

---

17. *Id.*

18. *Id.*

19. *From Gravesites to Death's Door: Carolina Investors' Rise and Fall*, *supra* note 5.

20. *Id.*

21. *Id.*

22. Dietrich & Roberts, *supra* note 4, at F3.

23. *Id.*

24. *Id.*

25. R. Kevin Dietrich, *HomeGold Files for Bankruptcy*, THE STATE (Columbia, S.C.), Apr. 1, 2003, at B6.

26. *Id.*

27. Dietrich, *supra* note 11, at B6.

28. S. 555, 115th Gen. Assem. (S.C. 2003).

29. S.C. CODE ANN. § 35-1-1530 (Law. Co-op. 1976 & Supp. 1987) (amended 2003).

30. S. 555, 115th Gen. Assem. (S.C. 2003).

31. *Id.*

handle future situations as well as deter others from committing securities fraud.<sup>32</sup>

Meanwhile, the investigations of Carolina Investors overwhelmed the South Carolina Attorney General's Office.<sup>33</sup> The Attorney General supported the bill and urged lawmakers to take action.<sup>34</sup> Specifically, the Attorney General wanted to expand the grand jury's powers to include securities fraud.<sup>35</sup> Prior to passage of Senate Bill 555, the State of South Carolina had limited powers to investigate securities fraud.<sup>36</sup> The state grand jury is "the only sophisticated investigatory tool in the state arsenal;" this reform was desperately needed to investigate the "sophisticated" area of securities laws.<sup>37</sup>

Senator Martin, supported by state Senators Ralph Anderson, Glenn McConnell, Robert Waldrep, Thomas Alexander, Phil Leventis, Arthur Ravenel and David Thomas, introduced Senate Bill 555 on April 3, 2003.<sup>38</sup> In its original form, Senate Bill 555 granted grand jury jurisdiction over securities fraud investigations, increased the statute of limitations, and extended liability to those "who knowingly and substantially assist[]" a person involved in securities fraud.<sup>39</sup> It was referred to the Senate Judiciary Committee the same day, and a favorable report was returned six days later.<sup>40</sup> The bill was sent to the House where it was amended and returned to the Senate. The House amendments deleted the "knowingly and substantially assists" provision and changed the statute of limitations provision to "the earlier of one year after discovery . . . or five years after the violation."<sup>41</sup> The Senate insisted that the original three years after discovery provision be kept; however, they compromised on the aider and abettor provision which was not reintroduced on the amended House version of the Bill.<sup>42</sup> This compromise was accepted by the House, and on June 4, 2003, Governor Mark Sanford signed the bill into law.<sup>43</sup>

Throughout the legislative process, Governor Sanford supported this important legislation.<sup>44</sup> He endorsed the legislation as a means to restore investor trust "and

---

32. Collier, *supra* note 10.

33. *Hearing on S.555 Before the Senate Judiciary Comm.*, 115th Sess. (S.C. 2003) (statement of Henry McMaster, Attorney General).

34. *Id.*

35. *Id.*

36. *Id.*

37. *Id.*

38. S. 555, 115th Gen. Assem. (S.C. 2003).

39. *Id.* Existing law required a cause of action to be filed within three years of the date the security was purchased. *See infra* Part III.A.i.

40. *Id.*

41. *Id.*

42. *Id.*

43. *Id.*

44. Press Release, State of South Carolina, Office of the Governor, Gov. Sanford Signs Securities Fraud Bill into Law: Bill Empowers Statewide Grand Jury, Extends Statute of Limitations (June 4, 2003) (on file with author).

stimulat[e] more investment in our economy.”<sup>45</sup> Recognizing that the Carolina Investors situation will not disappear merely as a result of Senate Bill 555’s passage, the Governor focused on prevention, deterrence, and investor confidence.<sup>46</sup>

Support for Senate Bill 555 was not unanimous. Some voiced concern that “passage of the bill as originally drafted would discourage competent lawyers from being involved in securities transactions.”<sup>47</sup> Others questioned the proposed statute of limitations, and advocated for a statute of limitations of “the earlier of two years after discovery of the untrue statement or omission, or five years after such violation.”<sup>48</sup> This proposal essentially adopted the federal statute of limitations as detailed in the Sarbanes-Oxley Act of 2002.<sup>49</sup>

### III. SENATE BILL 555 AND ITS RAMIFICATIONS ON INVESTORS’ CONFIDENCE AND THE INCREASED COSTS FOR BUSINESSES

Senate Bill 555 was passed swiftly to restore investor trust in the wake of the Carolina Investors/Home Gold fiasco. “However, these mob solutions born of outrage often have unintended consequences.”<sup>50</sup> Investor confidence is certainly an integral requirement if markets are to operate efficiently.<sup>51</sup> Investors need assurance that if they decide to invest their savings, they will be treated honestly and fairly.<sup>52</sup> However, if a regulation is overbroad, the possibility of frivolous claims and increased litigation costs may discourage a business’s decision to locate in the state. Accordingly, policy considerations on both sides need to be balanced to determine how best to serve the public interest.

#### *A. Effective Securities Laws Need Balance in Order to Maximize Efficiency*

A goal of securities laws is to balance the interests of investors with the interests of businesses in order to optimize market potential for growth.<sup>53</sup> Investors

---

45. *Id.*

46. *Id.*

47. Minutes from Corporate, Banking and Securities Section Council Meeting, South Carolina Bar Ass’n (Apr. 10, 2003) (on file with author).

48. *Id.*

49. Sarbanes-Oxley Act § 804, 28 U.S.C. § 1658 (2002).

50. Marianne M. Jennings, *A Primer on Enron: Lessons from A Perfect Storm of Financial Reporting, Corporate Governance and Ethical Culture Failures*, 39 CAL. W. L. REV. 163, 242–43 (2003).

51. Marc I. Steinberg, *Curtailing Investor Protection Under the Securities Laws: Good for the Economy?*, 55 SMU L. REV. 347, 353–54 (2002).

52. *Id.* at 354.

53. *Id.* at 353–54 (discussing balance between investor protection and capital formation).

need assurances that they will be protected from fraud.<sup>54</sup> Meanwhile, businesses need to be protected from limitless liability and baseless claims. The legislature must take both interests into account when fashioning a law, because if either of these competing interests is overemphasized, the cost of capital will rise.<sup>55</sup>

Securities laws seek to prevent fraud.<sup>56</sup> “Fraud decreases the public’s confidence in the securities markets and inhibits the efficient raising of capital.”<sup>57</sup> Investors who perceive too much risk in specific investments will not invest, thus stagnating the market.<sup>58</sup> Government can “remove [some] fear, or risks, that . . . inhibit the capital formation process” by enacting laws that strengthen investors’ rights.<sup>59</sup>

Achieving a balance between deterring crime, vindicating plaintiffs’ rights, and precluding stale claims from litigation necessitates a look at efficiency. Efficiency refers to the balancing of the benefits of a law with the costs associated with the law.<sup>60</sup> As applied to Senate Bill 555, the benefit of the extended statute of limitations is heightened investor confidence that a wrong will be remedied. The primary cost is the increased length of potential exposure for companies doing business or seeking to do business in South Carolina.

#### *i. Policies Served by Statutes of Limitations*

In order to determine the efficiency of Senate Bill 555, it is helpful to review the policies served by statutes of limitations. “[A] ‘statute of limitations’ establishes a fixed time period within which lawsuits must be commenced after a cause of action has accrued.”<sup>61</sup> Statutes of limitations are a legislative creation “intended to promote timely and efficient litigation of claims.”<sup>62</sup> They represent an attempt to balance the interest of affording “plaintiffs a reasonable time to present their claims”<sup>63</sup> with the interest of protecting defendants and the court system from

54. Christopher R. Leslie, *Den of Inequity: The Case for Equitable Doctrines in Rule 10b-5 Cases*, 81 CAL. L. REV. 1587, 1613 (1993) (arguing that equitable doctrines should be applied to securities fraud violations).

55. Steinberg, *supra* note 51, at 354.

56. Leslie, *supra* note 54, at 1613.

57. *Id.* at 1614.

58. See Steven A. Ramirez, *Fear and Social Capitalism: The Law of Macroeconomics of Investor Confidence*, 42 WASHBURN L.J. 31, 41 (2002) (explaining that law can protect investor confidence and optimize market growth).

59. *Id.* at 45.

60. Robert H. Frank, *Why Is Cost-Benefit Analysis So Controversial?*, 29 J. LEGAL STUD. 913, 913 (2000) (examining the cost-benefit analysis).

61. 51 AM. JUR. 2D *Limitation of Actions* § 9 (2000).

62. *Id.* § 13.

63. *Id.*

untimely and stale claims.<sup>64</sup> The statute provides the defendant with a fair opportunity to defend the claim by ensuring that the evidence is still in existence, memories have not faded and witnesses are still present.<sup>65</sup> Furthermore, defendants are allowed some sense of finality and are protected “from the protracted fear of litigation.”<sup>66</sup> Statutes of limitations also serve the public interest by preserving judicial economy and preventing the court system from litigating stale claims where evidence is not readily available.<sup>67</sup>

Similarly, a statute of repose terminates liability after a fixed amount of time.<sup>68</sup> The potential claim extinguishes, and the defendant can move on without the threat of stale claims, even if the claim is undiscovered by the plaintiff.<sup>69</sup> The same justifications and policies advanced for statutes of limitations hold for statutes of repose: fairness to the defendant, stale evidence, and business certainty.<sup>70</sup> The difference between statutes of limitations and repose for securities laws is that a statute of repose is not subject to equitable principles such as tolling or estoppel.<sup>71</sup>

Senate Bill 555 implements an open-ended statute of limitations that does not start running until discovery, and then provides the plaintiff with three years from this date to bring suit.<sup>72</sup> Formerly, a three-year statute of repose existed.<sup>73</sup> Eliminating the statute of repose in favor of a statute of limitations that tolls until discovery serves one of the goals of statutes of limitations, which is to provide a reasonable amount of time for the plaintiff to bring a claim.<sup>74</sup> A statute of repose in a fraud case can extinguish a claim before the victim has a chance to know about the fraud.<sup>75</sup> One purpose of Senate Bill 555 is to ensure that continued fraudulent concealment is not rewarded; the added discovery provision perpetuates an investor’s right to sue. However, Senate Bill 555 serves investors at the expense of providing certainty to businesses. The perpetuation of claims inhibits business planning. In Senate Bill 555, the legislature placed a higher value on the vindication of plaintiffs’ rights than on a business’s interest in extinguishing claims.<sup>76</sup> This is not surprising considering its enactment in response to the

---

64. *Id.* §§ 15, 17.

65. *Id.*

66. *Id.* § 16.

67. 51 AM. JUR. 2D *Limitation of Actions* § 17 (2000).

68. *Id.* § 18.

69. *Id.*

70. *Id.*

71. Leslie, *supra* note 54, at 1591–92 (explaining the basic concepts of statutes of limitations and repose).

72. S. 555, 115th Sess. (S.C. 2003).

73. S.C. CODE ANN. § 35-1-1530 (Law. Co-op. 1976 & Supp. 1987) (amended 2003).

74. 51 AM. JUR. 2D *Limitation of Actions* § 13 (2000).

75. *See id.* § 18.

76. S. 555, 115th Sess. (S.C. 2003).



### Carolina Investors/HomeGold collapse.

Senate Bill 555 established a clear rule that the statute of limitations would not begin to run on securities fraud violations until discovery.<sup>77</sup> South Carolina's absolute prior law allowed a cause of action to be brought only if filed within three years of the date the security was purchased.<sup>78</sup> Essentially, a fraud could be concealed for three years, and the investor would be out of luck. The new law adds a discovery element to bring securities law into line with most other causes of action in contract and tort law.<sup>79</sup>

#### ii. *The Benefit of Investor Confidence*

Investor confidence is essential to a growing economy.<sup>80</sup> Growth is dependent on entrepreneurs' ability to raise capital.<sup>81</sup> Capital is raised from investors with a willingness to invest in an idea on the hopes of a higher return in the future.<sup>82</sup> In order for investors to take on the risk of a cash outlay today for an increased return tomorrow, they demand confidence that their investments are adequately protected from dishonesty and unfairness.<sup>83</sup> If investors perceive the risk is too high to invest—because the markets are “unregulated or under-regulated”<sup>84</sup>—they may avoid securities markets and invest cash in other areas, thus “inhibit[ing] the capital formation process.”<sup>85</sup> Regulation can solve this problem by allaying some of the risks presented to investors in the market.<sup>86</sup>

#### iii. *The Cost to Businesses of Increased Length of Potential Exposure*

By extending the statute of limitations and hence heightening the risk of civil liability, the costs of doing business in South Carolina have arguably increased.<sup>87</sup> The “three years from the date of discovery”<sup>88</sup> amendment effectively tolls the statute of limitations so long as fraudulent concealment continues. This move may

77. Telephone Interview with Mitchell Willoughby, Attorney, (Sept. 14, 2003).

78. S.C. CODE ANN. § 35-1-1530 (amended 2003).

79. Telephone Interview with Mitchell Willoughby, *supra* note 77. *See also* S.C. CODE ANN. § 15-3-530 (West 2003).

80. Ramirez, *supra* note 58, at 41.

81. *Id.*

82. *Id.*

83. *Id.* at 44–45.

84. *Id.* at 67.

85. *Id.* at 45, 67.

86. Ramirez, *supra* note 58, at 45.

87. *See* Ralph K. Winter, *Paying Lawyers, Empowering Prosecutors, and Protecting Managers: Raising the Cost of Capital in America*, 42 DUKE L.J. 945, 948 (1993) (discussing how rules that do not consider efficiency raise the cost of capital and retard economic growth).

88. S. 555, 115th Sess. (S.C. 2003).

impede business planning and make future liability less predictable. There is some risk that businesses may have to act as insurers for investors.<sup>89</sup> For example, if an investment decision is not profitable for the investor, the “investors, believing that they have been deceived, will seek to hold allegedly-culpable parties responsible.”<sup>90</sup> Addressing this claim, legitimate or not, will add to the operating costs for that business in this state.<sup>91</sup> By limiting investors’ rights, legislators encourage capital formation because businesses perceive less risk in their investments.<sup>92</sup>

Also relevant to the assessment of the cost to business in South Carolina is the question of how much fraud actually exists in the state. Admittedly, the recent Carolina Investors/HomeGold scandal was enormous. It affected many South Carolinians, but one may question the likelihood of another event of this magnitude in South Carolina. South Carolina is a relatively small state looking to attract business and investors. Until this past spring, fraud was only a minor concern. When evaluated only against the Carolina Investors/HomeGold investigation, this legislation does not look excessive. However, when considering the competing goal of a business-friendly environment, Senate Bill 555 may exceed the investor protection needs of this state. Disproportionate regulations may “deter beneficial activity.”<sup>93</sup> If businesses are deterred from locating here, there will be no need to worry about protection of investors because they will have nothing in which to invest.

On the other hand, a defendant *should* be liable for his fraud, and no amount of time should extinguish his liability as long as the fraud remains concealed. This would not be fair to investors who have entrusted their money. These investors should be entitled to recourse to vindicate their rights. It is also unfair to honest businesses who have to compete with dishonest enterprises. Furthermore, “[t]rust is fragile, far easier to destroy than to create.”<sup>94</sup> Fraud of the magnitude of Carolina Investors/HomeGold has a significant negative effect on investors’ willingness to put cash at risk, and stronger regulation is needed to reinforce and restore trust.<sup>95</sup>

These are the primary concerns when considering the efficiency of the statute of limitations amendment in Senate Bill 555. Efficiency dictates that “we should take those actions, . . . whose benefits exceed their costs.”<sup>96</sup> The recent enactment of Senate Bill 555 reflects a legislative calculation that the benefits of investor

89. Steinberg, *supra* note 51, at 353.

90. *Id.*

91. See Ramirez, *supra* note 58, at 46.

92. See Steinberg, *supra* note 51, at 352.

93. Winter, *supra* note 87, at 963.

94. Rachel F. Moran, *Fear Unbound: A Reply to Professor Sunstein*, 42 WASHBURN L.J. 1, 8 (2002) (arguing that emotions should be considered in the regulatory process).

95. See *id.*

96. Frank, *supra* note 60 at 913.

confidence outweigh the costs to businesses. Certainly, wrongdoers should be liable for their wrongdoing. Vindication of investors' rights should not be trivialized at the expense of a more friendly business environment. Honest, hardworking business enterprises should not be forced to compete with crooks for money to meet investment needs. On the other hand, unnecessary and prolonged liability may deter both beneficial and harmful conduct.

### C. *Senate Bill 555 is Not Consistent with Federal Law*

The Securities and Exchange Commission (SEC) is primarily responsible for enforcing federal securities laws.<sup>97</sup> However, "each individual state has its own securities laws"—known as "blue sky laws"—which vary from state to state.<sup>98</sup> These varied blue sky laws regulate the offer and sale of securities, the reporting requirements of broker-dealers, and the investment advisors offering their services in the state.<sup>99</sup>

The statute of limitations of the fraud related provisions of the federal securities law has only recently been extended.<sup>100</sup> In July 2002, Congress passed the Sarbanes-Oxley Act, which increased criminal penalties for corporate wrongdoing and created a new Public Company Accounting Oversight Board.<sup>101</sup> Congress increased the limitations period from one year after discovery and three years from the date of violation to two years after discovery and five years after the date of violation.<sup>102</sup>

### D. *Other States' Approaches*

A comparison of nearby states may be helpful in assessing Senate Bill 555's impact on state efforts to recruit businesses to South Carolina. North Carolina's statute of limitations provides that no suit can be brought "more than two years after the sale or contract of sale" of the security.<sup>103</sup> Georgia's statute is the same.<sup>104</sup> Tennessee's statute of limitations for securities fraud deviates slightly from North Carolina's and Georgia's. It allows a suit to be brought "before the expiration of

---

97. Richard I. Alvarez, Esq. & Mark J. Astarita, Esq., *Introduction to the Blue Sky Laws*, at <http://www.seclaw.com/bluesky.htm>.

98. *Id.* The origin of the phrase "blue sky laws" is traced to United States Supreme Court Justice Joseph McKenna. *Hall v. Geiger-Jones Co.*, 242 U.S. 539, 550–51 (1917) (dealing with the constitutionality of state securities regulations).

99. Alvarez & Astarita, *supra* note 97.

100. Sarbanes-Oxley Act, 28 U.S.C. § 804, § 1658 (2002).

101. *Id.* at § 905, § 101.

102. *Id.* at § 1658.

103. N.C. GEN. STAT. § 78A-56(f) (2001).

104. GA. CODE ANN. § 10-5-14(d) (2000).

two (2) years after the act or transaction constituting the violation or the expiration of one (1) year after the discovery of the facts . . . , or after such discovery should have been made by the exercise of reasonable diligence, whichever first expires.”<sup>105</sup> This statute purports to give a discovery element to the fraud violation; however, it is limited with a statute of repose of two years.<sup>106</sup> Also, Tennessee allows for flexibility by adding the phrase “or transaction constituting the violation,”<sup>107</sup> which indicates that fraud occurring after the date of sale regarding a security will actually start the running of the statute of limitations (as opposed to a strict date of sale provision). Florida’s statute of limitations for security violations is more investor friendly than the above mentioned states<sup>108</sup> and is consistent with the Sarbanes-Oxley Act.<sup>109</sup> It allows a plaintiff to bring an action within two years from the date of discovery and has a five-year statute of repose.<sup>110</sup> Like Tennessee, the statute does not necessarily start running with the date of sale, but rather with the “facts giving rise to the cause of action.”<sup>111</sup>

This comparison illustrates the heightened investor protections that businesses observe when looking to locate in South Carolina. However, a few states have extended their statute of limitations on securities fraud violations to ensure greater protection of investors. Kentucky, like South Carolina, had a three-year statute of repose that extinguished a claim “three (3) years after the contract of sale.”<sup>112</sup> In 2001, the legislature amended it to add a discovery element allowing a victim to bring a claim until “three years after the date the occurrence of the act, omission, or transaction constituting a violation of this chapter was discovered, or in the exercise of reasonable care should have been discovered.”<sup>113</sup> Alabama’s provision also has a discovery element.<sup>114</sup> It allows a cause of action for a security fraud violation to be brought “within the earlier of two years after the discovery of the violation or two years after discovery should have been made by the exercise of reasonable care.”<sup>115</sup> Likewise, Mississippi allows an action to be maintained for “two (2) years after the discovery . . . or after such discovery should have been made by the exercise of reasonable diligence.”<sup>116</sup>

---

105. TENN. CODE ANN. § 48-2-122(h) (2002).

106. *Id.*

107. *Id.*

108. FLA. STAT. ANN. § 95.11(4)(e) (West 2002).

109. Sarbanes-Oxley Act, 28 U.S.C. § 804, § 1658 (2002).

110. FLA. STAT. ANN. § 95.11(4)(e) (West 2002).

111. *Id.*

112. KY. REV. STAT. ANN. § 292.480 (Michie 1998) (amended 2001).

113. *Id.*

114. ALA. CODE § 8-6-19(f) (2002).

115. *Id.*

116. MISS. CODE ANN. § 75-71-725 (2000).

Thus, South Carolina's new statute of limitation may seem investor friendly when compared with other states. If so, a company may be inclined to go to one of those other states to ensure that it is not subject to increased liability. This would adversely affect South Carolina's business recruitment efforts. However, considering the recent national scandals such as Enron and WorldCom, the trend may be heading in the direction of increased investor protection. This indicates that South Carolina may be leading the way to ensure that citizens and other honest businesses are no longer oppressed by fraudulent activity.

#### IV. CONCLUSION

The adoption of Senate Bill 555 indicated a legislative willingness to make investor protection and confidence a priority. Propelled by the collapse of Carolina Investors, the Bill was signed into law to bolster investor confidence and to deter future fraud. Wrongdoers are to be held accountable for their fraudulent activities, and investors are entitled to a clear rule of relief. In theory, this is consistent with the goals of securities law. However, Senate Bill 555, which provides more protection for investors than the federal law under the Sarbanes-Oxley Act, may overreach this objective and deter businesses from locating here, stunting South Carolina's economic growth. Companies may fear increased liability and locate elsewhere to be shielded from seemingly endless liability. Reconsideration of priorities might be necessary to achieve some balance.

*Jennifer L. Hess*