

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Policy and Steering Committee on Ways and Means

BILL: CS/SB 1126

INTRODUCER: Judiciary Committee, Senator Richter, and others

SUBJECT: Investor Protection

DATE: April 23, 2009

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Johnson</u>	<u>Burgess</u>	<u>BI</u>	Fav/1 amendment
2.	<u>Cellon</u>	<u>Cannon</u>	<u>CJ</u>	Favorable
3.	<u>McKay</u>	<u>Wilson</u>	<u>GO</u>	Favorable
4.	<u>Treadwell</u>	<u>Maclure</u>	<u>JU</u>	Fav/CS
5.	<u>Hendon</u>	<u>Kelly</u>	<u>WPSC</u>	Favorable
6.	_____	_____	_____	_____

Please see Section VIII. for Additional Information:

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|------------------------------|-------------------------------------|---|
| A. COMMITTEE SUBSTITUTE..... | <input checked="" type="checkbox"/> | Statement of Substantial Changes |
| B. AMENDMENTS..... | <input type="checkbox"/> | Technical amendments were recommended |
| | <input type="checkbox"/> | Amendments were recommended |
| | <input type="checkbox"/> | Significant amendments were recommended |

I. Summary:

In the last two years, multibillion dollar investment scandals have plagued Florida and other areas of the United States. Recent Florida-related cases include the following:

- Arthur Nadel provided false information to investors about the returns of six hedge funds and overstated the value of the funds by approximately \$300 million.¹
- Stanford Group Company, which had 19 locations in the United States, including four offices in Florida, fraudulently marketed and sold an estimated \$8 billion of “self-styled” certificates of deposits to investors.²
- Bernard Madoff engineered a Ponzi scheme that defrauded investors of an estimated \$50 billion. Approximately one in five of the investors were Florida residents.³

¹ U.S. Securities and Exchange Commission, *Litigation Release No. 20858* (Jan. 21, 2009), available at <http://www.sec.gov/litigation/litreleases/2009/lr20858.htm> (last visited Apr. 7, 2009).

² U.S. Securities and Exchange Commission, *Litigation Release No. 20901* (Feb. 17, 2009), available at <http://www.sec.gov/litigation/litreleases/2009/lr20901.htm> (last visited Apr. 7, 2009).

³ Michael Sallah, Patrick Danner, and others, *One in five Bernard Madoff investors from Florida*, MIAMI HERALD (Feb. 6, 2009), available at <http://www.miamiherald.com/486/story/890531.html> (last visited Apr. 7, 2009).

The complexity of fraudulent investments and the huge volume of investors may lead to delays in the investigation and prosecution of persons operating fraudulent schemes, thereby increasing the losses to investors. The bill provides greater enforcement tools and regulatory oversight for securities transactions in Florida, which will increase the state's effectiveness in combating securities fraud. The bill provides the following changes:

- Authorizes the Office of Statewide Prosecution to initiate and pursue investigations for securities transactions and money laundering and to prosecute criminal violations;
- Authorizes the Attorney General to investigate and bring actions against violations of the fraud provisions of ch. 517, F.S., the Securities and Investors Protection Act. The Attorney General may seek injunctive relief, restitution, and civil penalties. Currently, the Office of Financial Regulation (OFR) has the jurisdiction under ch. 517, F.S.;
- Requires the OFR to adopt disciplinary guidelines for persons who violate ch. 517, F.S.;
- Increases the cap on administrative fines from \$5,000 to \$10,000 per violation; and
- Authorizes the emergency suspension of persons subject to ch. 517, F.S., for failure to promptly provide books and records to the OFR.

The bill is expected to have a positive fiscal impact on the Office of Financial Regulation through increased fines. In addition, the bill could increase deposits into the Attorney General's Legal Affairs Revolving Trust Fund and the Anti-Fraud Trust Fund from court imposed costs and attorney fees.

This bill substantially amends the following sections of the Florida Statutes: 16.56, 517.021, 517.072, 517.12, 517.121, 517.1215, 517.1217, 517.141, 517.161, 517.191, 517.221, 517.275, and 905.34.

The bill also creates sections 517.1611 and 896.108, Florida Statutes.

II. Present Situation:

Office of Financial Regulation

The Office of Financial Regulation (OFR), which is under the Financial Services Commission, regulates state-chartered financial institutions, mortgage brokers, finance companies, securities transactions, and money services businesses.⁴ Chapter 517, F.S., the Florida Securities and Investor Protection Act, governs the regulation of securities transactions. The OFR's jurisdiction includes the registration, regulation, examination, and investigation of broker dealers, associated persons, branch offices, and investment advisors and the registration of securities.

As of June 30, 2008, the OFR reported 267,210 active agents, 7,545 dealers, and 10,734 branch offices in Florida. For fiscal years 2006-07 and 2007-08, the OFR imposed administrative fines totaling approximately \$1.5 million on ch. 517, F.S., registrants.

⁴ Section 20.121(3), F.S. The Financial Services Commission consists of the Governor, the Chief Financial Officer, the Attorney General, and the Commissioner of Agriculture.

The OFR is authorized to impose and collect an administrative fine not to exceed \$5,000 against any person who is found to have violated any provision of ch. 517, F.S., any rule or order of the OFR, or any agreement entered into between the person and the OFR.⁵ The OFR has the authority to seek injunctive relief and other remedies, including restitution.⁶ Violations of certain provisions of this chapter can be prosecuted as a third-degree felony, and for certain actions, if statutorily prescribed monetary and violation repetition thresholds are reached, such violations can be prosecuted as first-degree felonies. For fiscal year 2007-08, the OFR referred 34 cases to state and federal prosecutors.

The Securities Guaranty Fund, established under ch. 517, F.S., provides compensation to persons adjudged by a court of competent jurisdiction to have suffered monetary damages as a result of a violation of ss. 517.07, F.S., (registration of securities) or 517.301, F.S., (fraudulent transactions) by a ch. 517, F.S., licensee. Compensation from the fund is limited to the amount of the unsatisfied portion of a judgment or \$10,000, whichever is less. Compensation excludes costs and attorney's fees.

Regulation of Viatical Investments

In general, a viatical settlement transaction is an agreement under which the owner of a life insurance policy ("viator") sells the policy to another person ("viatical settlement provider") in exchange for an upfront payment, which is generally less than the expected death benefit under the policy. Rather than retaining the policy, the provider usually sells all or a part of the policy to one or more investors ("viatical settlement purchasers"). In return for providing funds, these investors receive the death benefit, or a proportionate share thereof, upon the passing of the insured. In 2005, legislation was enacted that requires the investment transaction to be regulated as a security under ch. 517, F.S. These investments must be registered with either the OFR or the federal Securities and Exchange Commission. In addition, persons offering such investments must register with the OFR and provide full and fair disclosures concerning viatical settlement investments to prospective investors.

Department of Legal Affairs

The Attorney General heads the Department of Legal Affairs. The Attorney General is responsible for the enforcement of state consumer protection and antitrust laws as well as civil prosecution of criminal racketeering. The only cases for which the Department of Legal Affairs can initiate an investigation on its own for securities violations, without a request by the OFR, are cases of securities fraud that also violate the Racketeer Influenced and Corrupt Organization Act (RICO).⁷

Office of Statewide Prosecution

⁵ Section 517.221(3), F.S.

⁶ Section 517.191, F.S.

⁷ See s. 895.02, F.S.

The Office of Statewide Prosecution (OSP) is housed within the Department of Legal Affairs.⁸ The Statewide Prosecutor is appointed by the Attorney General from a list of nominees selected by the Florida Supreme Court Judicial Nominating Commission. The mission of the OSP is to investigate and prosecute multi-circuit organized crime, and to aid other state and local law enforcement officials in their investigations of organized crime. The OSP has jurisdiction if the crime has occurred in more than one judicial circuit or is part of a conspiracy in more than one judicial circuit. The OSP is authorized to investigate and prosecute the crimes of bribery, burglary, carjacking, home-invasion robbery, usury, extortion, gambling, kidnapping, larceny, murder, prostitution, perjury, robbery, narcotics, RICO violations, Anti-Fencing Act violations, Anti-Trust Act violations, certain computer-related crimes, fraud, and certain violations of the Florida Drug and Cosmetic Act.⁹ During the past two years, the OSP made 18 arrests/prosecutions related to securities fraud, ordered \$30 million in restitution, and opened eight investigations regarding securities fraud.

Statewide Grand Jury

Current law limits the subject matter jurisdiction of the statewide grand jury and does not include criminal violations of the Florida Money Laundering Act or the Florida Securities and Investor Protection Act.¹⁰

Florida Money Laundering Act

The Florida Money Laundering Act criminalizes the act of money laundering, prohibits structuring transactions to evade federal filings, and provides civil and criminal forfeiture for violations.¹¹ Chapter 560, F.S., which relates to the regulation of money services businesses by the OFR, provides that money services businesses are subject to the provisions of ch. 896 F.S., relating to offenses related to financial transactions, and the OFR is authorized to take actions against any money services businesses violating ch. 896, F.S.

Rewards for Informants for Offenses Related to Financial Transactions

Under existing law, a law enforcement agency conducting any investigation under ch. 896, F.S., may pay a reward to an individual who provides original information that leads to a recovery of a criminal fine, civil penalty, or forfeiture.¹² The law enforcement agency may determine the amount of the award.¹³ However, the reward may not exceed the amount of reward authorized for similar activity by any federal law or guideline in effect at the time the information was provided.¹⁴ An officer or employee of the United States, a state or local government, or a foreign

⁸ Article IV, s. 4 of the Florida Constitution, and s. 16.56, F.S., provide the jurisdiction and authority of the Office of Statewide Prosecution.

⁹ Section 16.56(1)(a), F.S.

¹⁰ Section 905.34, F.S.

¹¹ Section 896.101, F.S.

¹² Section 896.107(1), F.S.

¹³ Section 896.107(2), F.S.

¹⁴ *Id.*

government who in the performance of their official duties provides information leading to a recovery, are ineligible to receive a reward.¹⁵

III. Effect of Proposed Changes:

The bill provides greater enforcement tools and regulatory oversight for securities transactions in Florida, which will increase the state's effectiveness in combating securities fraud. Following is a section-by-section analysis of the bill:

Sections 1 and 15 provide additional investigative and prosecutorial powers for the Office of the Statewide Prosecutor and the statewide grand jury. Sections 1 and 15 expand the jurisdiction of the Office of Statewide Prosecutor and the statewide grand jury, respectively, to include the investigation and prosecution of any criminal violation of the Florida Money Laundering Act and any criminal violation of the Florida Securities and Investor Protection Act. Currently, the Office of Statewide Prosecution can pursue money laundering as a RICO predicate. Currently, state attorneys have the authority to pursue criminal violations of ch. 517, F.S., and s. 896.101, F.S.

With respect to the Office of Statewide Prosecutor and prosecutions for any attempts, solicitations, or conspiracies to commit any of the enumerated crimes, the bill specifies that informations charging such offenses must contain general allegations stating the judicial circuits and counties in which crimes are alleged to have occurred or the judicial circuits and counties in which the crimes affecting those circuits or counties are alleged to have been connected with an organized criminal conspiracy.

Sections 2 and 3 revise provisions related to viatical settlement investments. Enumerated transactions excluded from the current definition of the term "viatical settlement investment" under s. 517.021(23), F.S., are transferred to s. 517.072, F.S., as self-proving exemptions that will be subject to the fraud provisions under ss. 517.301, 517.311, and 517.312, F.S. These excluded transactions would remain exempt from the registration requirements of s. 517.07 and s. 517.12, F.S.

Section 4 revises provisions related to the registration of dealers, associated persons, investment advisers, and branch offices. The bill clarifies that a registration application must contain information about "members" and "principals," in addition to directors. The terms "partner" and "officer" are removed from the statute. The term "principal" is defined in current law and includes partners and executive officers.¹⁶

Current law requires each applicant to file a set of fingerprints and does not require officers or directors of the applicant to submit fingerprint cards. The bill clarifies that any direct owners, principals, or indirect owners as required to be reported on Forms BD or ADV are required to file a complete set of fingerprints taken by an authorized law enforcement agency or in a manner approved by Financial Services Commission (commission) rule. The bill provides that the commission may waive, by rule, the requirement that direct owners, principals, or indirect owners to submit fingerprints.

¹⁵ Section 896.107(3), F.S.

¹⁶ See 517.021(17), F.S.

The section also revises the registration renewal process for branch offices to allow for reinstatement during a late period and payment of a reinstatement fee. Currently, a branch office that applies for renewal after December 31 must file a new application with the office, while dealers, investment advisers, and associated persons may request reinstatement with the office by January 31 if they do not meet the December 31 renewal deadline.

Section 5 authorizes the Office of Financial Regulation (OFR) to summarily suspend a registrant pursuant to s. 120.60(6), F.S., if the registrant fails to promptly provide books and records after a written request by OFR. Such suspension is immediately rescinded if the registrant submits the records to OFR. For purposes of s. 120.60(6), F.S., failure to provide such records constitutes an immediate and serious danger to the public health, safety, and welfare.

Sections 6 and 7 replace references to the terms “National Association of Securities Dealers” (NASD) and the term “New York Stock Exchange” (NYSE) with the term “Financial Industry Regulatory Authority” (FINRA) since the NASD and NYSE were merged to form FINRA.

Section 8 revises provisions relating to the Securities Guaranty Fund by clarifying that any payment from the Securities Guaranty Fund does not include post-judgment interest awarded by a court.

Section 9 expands the authority of the OFR by allowing the OFR to revoke, deny, or suspend the registration of any member, principal, or director of the applicant or registrant, or any person controlling the applicant or registrant, if certain violations occur. Currently, the OFR may take such actions against the applicant or registrant. The section also allows the OFR to revoke, deny, or suspend the registration if such person has been:

- convicted of, or has entered a plea of guilty or nolo contendere to, a crime, *regardless of whether adjudication was withheld*; or
- been arrested for any conduct that would authorize revocation under s. 517.161(1), F.S.

Section 10 requires the commission to adopt, by rule, disciplinary guidelines applicable to each ground for disciplinary action that may be imposed by the OFR. Such disciplinary guidelines would be based on the severity and repetition of specific offenses. The bill requires reasonable and meaningful notice to the public of likely penalties that may be imposed for proscribed conduct. In addition, the guidelines must ensure that penalties are imposed in a consistent manner by OFR. The guidelines may be adjusted based on aggravating and mitigating factors established by rule.

The section also requires the commission to adopt rules establishing licensure and renewal disqualifying periods for applicants based on criminal convictions of the applicant. The disqualifying periods will be:

- 15 years for a felony; and
- 5 years for a misdemeanor.

The waiting period must be related to crimes involving registration as a dealer, investment adviser, issuer of securities, associated person, or branch office or the application for registration or involving moral turpitude or fraudulent or dishonest dealing. The bill specifies that the rule may also consider mitigating factors, an additional waiting period based upon dates of imprisonment or community supervision, an additional waiting period based upon commitment of multiple crimes, and other factors reasonably related to the consideration of an applicant's criminal history. The bill specifies that an applicant is not eligible for registration until the expiration of the disqualifying period set by rule.

Section 11 expands the authority of the Attorney General to investigate and bring actions against violations of the fraud provisions of ch. 517, F.S., upon written approval of OFR. The fraud provisions include ss. 517.275, 527.301, 517.311, and 517.312, F.S.¹⁷ The Attorney General may recover any costs and attorney's fees related to the investigation or enforcement. Currently, the OFR only has enforcement authority. Moneys recovered by the Attorney General for costs, attorney's fees, and civil penalties must be deposited in the Legal Affairs Revolving Trust Fund.

In addition to any other remedy, the OFR is authorized to apply to the court to impose a civil penalty against any person found to have violated ch. 517, F.S., in an amount not to exceed \$10,000 for an individual or \$25,000 for any other person, or the gross amount of any gain to such defendant for each violation other than s. 517.301, F.S., plus \$50,000 for an individual or \$250,000 for any other person, or the gross amount of any gain to such defendant for each violation of s. 517.301, F.S. All civil penalties collected under this provision will be deposited into the Anti-Fraud Trust Fund.¹⁸

The bill expressly provides that if the Attorney General initiates a civil action under this section, this action will not preclude OFR from initiating an administrative action against the registrant. However, the bill provides that a person may not be subject to both a civil penalty and an administrative fine resulting from the same facts.

The bill provides that notwithstanding s. 95.11(4)(e), F.S., an enforcement action under this section may be initiated within six years after the facts giving rise to the cause of action were discovered or should have been discovered with the exercise of due diligence, but not more than 8 years after the date of the violation.¹⁹

Section 12 increases the administrative fine imposed against any person found to have violated ch. 517, F.S., any rule, or order to \$10,000 from \$5,000.

¹⁷ See s. 517.275, F.S., relating to commodities violations regulated under the federal Commodity Exchange Act or regulations of the Commodity Futures Trading Commission, relating to fraudulent transactions; s. 517.301, F.S., relating to fraudulent transaction; s. 517.311, F.S., relating to false representations in issuing or selling securities; and s. 517.312, F.S., providing for rescission and recovery of damages for fraudulent transactions.

¹⁸ The Anti-Fraud Trust Fund is created within OFR. Section 517.302(3)(a), F.S. Any amounts assessed as costs of investigation and prosecution under this subsection shall be deposited in the trust fund. Funds deposited in such trust fund shall be used, when authorized by appropriation, for investigation and prosecution of administrative, civil, and criminal actions arising under the provisions of this chapter. Funds may also be used to improve the public's awareness and understanding of prudent investing.

¹⁹ According to the OFR, the retention period for books and records range from a period of 3-6 years. Currently, s. 95.11, F.S., establishes limitations for actions other than for recovery of real property. These limitations range from a period of 30 days to 20 years, including two years for an action founded upon a violation of any provision of ch. 517, F.S.

The bill also authorizes the OFR to bar, permanently or for a specified time, any person found to have violated any provision of ch. 517, F.S., any rule or order adopted by the commission or the OFR, or any agreement entered into with the office.

Section 13 updates the references provisions of the Commodity Exchange Act and regulations of the Commodity Futures Trading Commission to include any amendments to those provisions.

Section 14 allows the Florida Department of Law Enforcement (FDLE) to use criminal proceeds to pay increased awards. As a result, seizures for the state will increase. More specifically, the bill provides that FDLE, when conducting an investigation of a violation of ch. 896, F.S., may enter into agreements and pay a reward to any person who provides original information that leads to recovery of a criminal fine, civil penalty, or forfeiture based in whole or in part upon a violation of federal law or Florida law.

The executive director of FDLE is authorized to determine the amount of the award. The executive director may, with written approval of the Attorney General, exceed the limits of rewards in s. 896.107, F.S., if the criminal fine, civil penalty, or forfeiture amount received by the state warrants an upward departure from the limits. Rewards paid may only be paid from seized assets awarded by the court.

The bill specifies that funds seized by FDLE under ch. 896, F.S., will be deposited into FDLE's Forfeiture and Investigative Support Trust Fund. Funds secured through federal forfeiture actions will be deposited in the Federal Law Enforcement Trust Fund. Officers or employees of the federal government, a state or local government, or a foreign government are not eligible for a reward if the information was obtained through the performance of their official duties. Payment of a reward does not affect the admissibility of testimony in any court proceeding.

Section 16 provides that the act will take effect on July 1, 2009.

The bill also provides technical, conforming changes throughout ch. 517, F.S. References to the terms "National Association of Securities Dealers" (NASD) and the term "New York Stock Exchange" (NYSE) are replaced with the term "Financial Industry Regulatory Authority" (FINRA) since the NASD and NYSE were merged to form FINRA.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

The increased enforcement authority the bill provides for the Attorney General, Office of Statewide Prosecution, and the Office of Financial Regulation (OFR) will greatly enhance the state's efforts in investigating and prosecuting securities fraud and money laundering related crimes.

The fingerprint processing fee of \$43.25 per applicant will also be paid by direct owners, principals, and certain indirect owners.

C. Government Sector Impact:

The bill allows the OFR to impose an immediate suspension in cases where firms fail to provide previously requested records, which will aid the OFR in its oversight of registrants. This additional authority for the OFR will ultimately protect consumers since such noncompliance could be indicative of more serious regulatory problems of a firm.

The increased fines authorized under the bill could generate an indeterminate increase in revenues for the OFR.

The bill allows the Attorney General to recover any costs and attorney fees related to the investigation or enforcement of ch. 517, F.S. Money recovered by the Attorney General for costs, attorney's fees, and civil penalties for a violation would be deposited in the Legal Affairs Revolving Trust Fund, while civil penalties collected under s. 517.191(4), F.S., would be deposited into the Anti-Fraud Trust Fund.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:**
(Summarizing differences between the Committee Substitute and the prior version of the bill.)**CS by Judiciary on April 15, 2009:**

The committee substitute:

- Clarifies that a registration application must contain information about “members” and “principals,” in addition to directors, and removes “partner” and “officer” from the statute;
- Provides that any direct owners, principals, or indirect owners, as required to be reported on Forms BD or ADV, are required to file a complete set of fingerprints taken by an authorized law enforcement agency or in a manner approved by Financial Services Commission (commission) rule;
- Replaces the 30-day requirement to produce records with the requirement that, if the registrant fails to promptly provide books and records after a written request, the Office of Financial Regulation (OFR) may summarily suspend registration;
- Removes changes made in the bill to s. 517.131, F.S., relating to the Securities Guaranty Fund;
- Removes the terms “partner” and “officer” in the revocation, denial, or suspension of registration provisions of the bill and replaces these terms with the term “principal”;
- Removes the provision that would authorize OFR to deny, suspend, or revoke a registration if a registrant was the subject of any award of any national securities, commodities, or option dispute resolution forum;
- Removes the definition of “state” and “national”;
- Replaces the 7-year disqualifying period by providing that OFR may adopt a 15-year disqualifying period for felony convictions and a 5-year disqualification period for misdemeanor convictions if those felonies or misdemeanors involve moral turpitude or fraudulent or dishonest conduct related to securities registration;
- Provides that all civil penalties collected under 517.191(4), F.S., will be deposited into the Anti-Fraud Trust Fund;
- Requires the Attorney General to obtain written approval from OFR before initiating an investigation or civil action to enforce securities laws;
- Provides that, if the Attorney General initiates a civil action, the action will not preclude OFR from initiating an administrative action against the registrant; however, the bill provides that a person may not be subject to both a civil penalty and an administrative fine resulting from the same facts;
- Removes the provision in the bill specifying that time limitations do not apply to any enforcement actions brought by OFR under ch. 517, F.S., and replaces this provision with the requirement that enforcement actions be initiated within 6 years after the facts giving rise to the cause of action were discovered or should have been discovered with the exercise of due diligence, but not more than 8 years after the date of the violation; and
- Allows the Department of Law Enforcement, when conducting an investigation of a violation of ch. 896, F.S., to enter into agreements and pay a reward to any person who provides original information that leads to recovery of a criminal fine, civil penalty, or forfeiture, based in whole or in part, upon a violation of federal law or Florida law.

B. Amendments:

None.

This Senate Bill Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.
