

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 1643 Securities
SPONSOR(S): Representative Kravitz
TIED BILLS: **IDEN./SIM. BILLS:** SB 1630

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) <u>Banking & Securities (Sub)</u>	<u>4 Y, 0 N</u>	<u>Cutchins</u>	<u>Whitfield</u>
2) <u>Commerce</u>	<u></u>	<u></u>	<u></u>
3) <u>Judiciary</u>	<u></u>	<u></u>	<u></u>
4) <u>Finance & Tax</u>	<u></u>	<u></u>	<u></u>
5) <u>Public Safety Appropriations (Sub)</u>	<u></u>	<u></u>	<u></u>
6) <u>Appropriations</u>	<u></u>	<u></u>	<u></u>

SUMMARY ANALYSIS

Chapter 517, Florida Statutes, is the Florida Securities and Investor Protection Act (the Act). The Office of Financial Institutions and Securities Regulation (office) of the Financial Services Commission¹ is charged with administering and enforcing all of the provisions of the Act, including conducting examinations and reviewing and investigating industry related complaints. In addition to being able to deny, revoke, restrict or suspend the registration of dealers, investment advisers, associated persons and branch offices for violations of ch. 517, F.S., the office is authorized to bring administrative action against any person engaged in, or about to engage in any act or practice constituting a violation of the chapter. Any violation of the provisions of this chapter can be prosecuted as a third degree felony, and for certain actions, if a statutorily prescribed monetary and violation repetition threshold is reached, such violations can be prosecuted as first degree felonies. Typically, the office calls upon the Attorney General's Statewide Prosecutor or the state attorney to prosecute warranted criminal violations of ch. 517, F.S.

This bill amends s. 517.03, F.S., to provide specific authority for the Attorney General to enforce certain provisions of ch. 517, F.S., relating to registration of securities, prohibited commodities practices, fraudulent transactions, false representations, prohibited securities and investment practices, and boiler room operations. The bill also amends s. 517.191, F.S., to provide authority for the Attorney General to bring civil actions to recover civil penalties for not more than \$10,000 for each violation of the chapter, rule or order under the chapter, and to recover costs and attorney's fees.

The bill then increases the severity of the offense from a third to a second degree felony, for offenses relating to prohibited commodities practices, fraudulent transactions, and false representations. Additionally, by removing language from the chapter, the bill effectively reduces the severity of the offense for threshold violations relating to fraudulent transactions and false representations from a first degree felony to a second degree felony, and reduces the severity of the offense for threshold violations relating to boiler room operations, from a first degree felony to a third degree felony.

Finally, the bill provides that funds in the office's Anti-Fraud Trust Fund may be used to compensate victims of criminal violations of ch. 517, F.S., if such use is authorized by appropriation. The Financial Services Commission is required to adopt rules for the disbursement of funds to victims, including developing application forms and methods for determining damages and determining priority of payments if funds are insufficient to compensate victims.

¹ The current statutes name the Department of Banking and Finance, but this authority was shifted to the Office of Financial Institutions and Securities Regulation on January 7, 2003, by Ch. 2002-404, L.O.F.

This document does not reflect the intent or official position of the bill sponsor or House of Representatives.

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DATE: April 16, 2003

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. DOES THE BILL:

- | | | | |
|--------------------------------------|------------------------------|--|---|
| 1. Reduce government? | Yes <input type="checkbox"/> | No <input checked="" type="checkbox"/> | N/A <input type="checkbox"/> |
| 2. Lower taxes? | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 3. Expand individual freedom? | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 4. Increase personal responsibility? | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 5. Empower families? | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |

For any principle that received a "no" above, please explain:

This bill gives the Attorney General the same investigation and enforcement powers over securities registrants and applicants that the Financial Services Commission's Office of Financial Institutions and Securities Regulation wields under Chapter 517, Florida Statutes, in effect authorizing two agencies to regulate some of the same activities for one industry.

B. EFFECT OF PROPOSED CHANGES:

Chapter 517, Florida Statutes, is the Florida Securities and Investor Protection Act (the Act). The Office of Financial Institutions and Securities Regulation (office) of the Financial Services Commission is charged with administering and enforcing all of the provisions of the Act, including conducting examinations and reviewing and investigating industry related complaints. In addition to being able to deny, revoke, restrict or suspend the registration of dealers, investment advisers, associated persons and branch offices for violations of ch. 517, F.S., the office is authorized to bring administrative action against any person engaged in, or about to engage in any act or practice constituting a violation of the chapter.

For purposes of regulation, the term "securities" includes stocks, notes, bonds or debentures, and certificates of deposit. Other responsibilities of the office include conducting examinations and reviewing and investigating industry related complaints. The office may perform examinations within or outside of Florida to determine if a violation of the Act or administrative rules has occurred. The office may administer oaths, examine witnesses, and issue subpoenas, as needed. If the office finds that a registrant or applicant has violated any provision of the Act or any departmental rule, engaged in any fraudulent conduct, demonstrated unworthiness to transact business or is of bad business repute, the office can deny, revoke, restrict or suspend the registration of dealers, investment advisers, associated persons and branch offices.

The anti-fraud provisions of the Act make it unlawful for a person to engage in any fraudulent conduct when rendering investment advice or in connection with the offer, sale or purchase of any investment or security. Violation of any criminal provision of the Act is a third degree felony with a Level 1 offense severity ranking. A violation of s. 517.312(1), F.S., is increased to a first degree felony with a Level 7 offense severity ranking if the offender obtained money or property with an aggregate value of more than \$50,000 from five or more persons. Section 517.312(1), F.S., incorporates violation of either s. 517.301, F.S., or s. 517.311, F.S., relating to fraudulent transactions and false representations respectively, as an element of the offense, and also addresses boiler room operations for the fraudulent or deceptive sale of securities.

This bill amends s. 517.03, F.S., to provide specific authority for the Attorney General to enforce the provisions of ss. 517.07, 517.275, 517.301, 517.311, 517.312, F.S., relating to registration of securities, prohibited commodities practices, fraudulent transactions, false representations, and securities, investments, and boiler room prohibited practices, respectively. This investigation could be initiated with or without receipt of a complaint. The Attorney General's investigative powers would be the same as those given to the office under ss. 517.201 and 517.2015, F.S. The bill also amends s. 517.191,

F.S., to provide authority for the Attorney General to bring civil actions to recover civil penalties for not more than \$10,000 for each violation of the chapter, rule or order under the chapter, and to recover costs and attorney's fees.

Under s. 517.2015, F.S., a certain amount of confidentiality is provided for information relative to an investigation or examination by the office. In certain instances, the office may be dependent on information provided by employees or associates of a registrant. Subsection (3) of this section provides a privilege against civil liability to a person who furnishes information or evidence to the office, unless that person acts in bad faith or with malice in providing such information or evidence. This bill removes that privilege, consequently subjecting such persons to the civil liability remedies provided by the bill to the Attorney General. The bill also reiterates that information relative to a civil investigation or examination by the Attorney General is subject to the chapter's provisions for information confidentiality.

The bill also amends s. 517.302(1), F.S., to increase the severity of the offense for a violation of ss. 517.275, 517.301, and 517.311, F.S., relating to prohibited commodities practices, fraudulent transactions, false representations, from a third degree felony to a second degree felony. The bill eliminates the provision in s. 517.302(2), F.S., for a threshold violation (violation in which the offender obtained money or property with an aggregate value of more than \$50,000 from five or more persons) effectively reducing the severity of the offense for such a violation of s. 517.312(1), F.S., relating to fraudulent transactions, and false representations, from a first degree felony to a second degree felony, and reducing the severity for the offense of such a violation of s. 517.312(1), F.S., relating to boiler room operations from a first degree felony to a third degree felony.

The increase from a third degree felony offense to a second degree felony offense will not automatically result in a state prison sentence, but will make a prison sentence more likely depending on the offender's prior record and whether there are any additional offenses. The decrease from a first degree felony offense to a third degree felony offense reduces the minimum permissible sentencing from 21 months in prison, assuming no additional offenses and no prior criminal record, to a sentence of any non-state prison sanction, which could include probation, a fine, or county jail time.

The regulation of securities sales is funded by the State General Revenue Fund and the Anti Fraud Trust Fund. The industry pays for the cost of regulation through the payment of fees for initial or renewal registration. Any surplus from fees is transferred to the General Revenue Fund. This Program also facilitates Consumer Financial Fraud Prevention and Detection. Section 517.302(3), F.S., establishes the Anti-Fraud Trust Fund and gives a sentencing court authority to assess costs of investigation and prosecution against an offender who is convicted of, or pleads guilty or no contest to, violations of the securities laws set forth in ch. 517, F.S. Any amounts assessed as costs of investigation and prosecution in these criminal actions are to be deposited in the trust fund.

The trust fund was authorized by the Legislature in 1986. The office indicates that the trust fund currently has a balance of \$5.7 million, and that the primary source of income is the collection of administrative fines for violations of the securities laws. In FY 2000-2001, \$348,000 was deposited into the trust fund; in FY 2001-2002, \$288,000 was deposited. This fiscal year, \$2.8 million has been deposited due to the collection of an atypically large fine.

When authorized by appropriation, the funds in the trust fund must be used for investigation and prosecution of administrative, civil, and criminal actions arising under ch. 517, F.S. The office indicates that the major expense of the trust fund is payment of expert witness fees. The trust fund is also the source of funding for three positions involved in complex litigation of securities fraud cases.

Victims of criminal violations of ch. 517, F.S., can receive compensation for damages by means of restitution orders made by a sentencing court. Victims may also file civil cases against the offender. If the victim prevails in a civil suit against a licensed dealer, investment adviser, or associated person for a violation of ss. 517.07 or 517.301, F.S., the victim may receive payment from the department's

Securities Guaranty Fund. Payments from the Securities Guaranty Fund are limited to the lesser of \$10,000 or the unsatisfied portion of the victim's judgment for actual or compensatory damages, with a total limit of \$100,000 for claims against any one offender.

The bill also amends s. 517.302(3)(a), F.S., to permit use of funds in the Anti-Fraud Trust Fund to compensate victims of criminal violations of ch. 517, F.S. Currently, the funds may only be used to pay costs of investigation and prosecution of administrative, civil, and criminal actions arising under the provisions of the Florida Securities and Investor Protection Act. Both the current statute and this bill condition use of the funds upon authorization by appropriation.

As noted, the trust fund has a current balance of \$5.7 million. During FY 2001-2002, \$99 million were lost by victims of violations of the securities transactions laws, and restitution orders were entered for a total of \$3.9 million. The department takes the position that payment of victim's restitution from the trust fund would deplete the fund and impair the department's ability to prosecute complex cases. However, the bill retains current language providing that funds in the trust fund **must** (subject to appropriation) be used to pay costs of investigation and restitution, while adding language providing that the trust fund **may** (also subject to appropriation) be used to pay victim restitution. This implies a priority for use of the trust fund for the purpose of paying costs of investigation and restitution.

The bill also requires the department to adopt rules for the disbursement of funds to victims, including developing application forms, methods for determining damages, and methods for determining priority of payments if funds are insufficient to compensate victims.

C. SECTION DIRECTORY:

Section 1 amends s. 517.03, F.S., creating subsection (3) authorizing the Attorney General to enforce the provisions of ss. 517.07, 517.12, 517.275, 517.301, 517.311, and 517.312, F.S., and to commence any proceeding, issue any order, or conduct any investigations and seek any remedy for violations of the chapter. This section also reiterates that any information relative to a civil investigation or examination by the Attorney General is subject to the chapter's provisions for information confidentiality.

Section 2 amends s. 517.191, F.S., authorizing the Attorney General to seek civil remedies for violations of ch. 517, F.S.

Section 3 amends s. 517.2015, F.S., removing a privilege against civil liability for persons who furnish information or evidence related to investigations of ch. 517, F.S., violations.

Section 4 amends s. 517.302, F.S., revising criminal penalties for violations of certain provisions of ch. 517, F.S. This section also authorizes the use of funds in the Anti-Fraud Trust Fund to compensate victims of criminal violations of ch. 517, F.S., conditioned upon authorization by appropriation.

Section 5 makes this act effective July 1, 2003.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

If authorized by appropriation and by departmental rule, payment of victim restitution from the Anti-Fraud Trust Fund would result in a reduction of the amount of money available in the trust fund for paying the costs of investigation and prosecution of securities fraud cases.

2. Expenditures:

The Criminal Justice Impact Conference has indicated that the changes in offense level would not have a significant impact on the state prison system.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

This bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds, does not reduce a county's authority to raise revenue and does not reduce the percentage of a state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

The bill requires the [office] department to adopt rules for the disbursement of trust fund monies to victims, including developing application forms, methods for determining damages, and methods for determining priority of payments if funds are insufficient to compensate victims.

C. DRAFTING ISSUES OR OTHER COMMENTS:

Recent changes to the governmental organization of the Department of Banking and Finance affected by the passage of Constitutional Amendment 8 and Chapter 2002-404, Laws of Florida, reassign the regulatory duties of the department to the Financial Services Commission and its Office of Financial Institutions and Securities Regulation. The 2002 Florida Statutes do not yet reflect the renaming of all of the references to the former department. Major conforming legislation introduced in the 2003 Regular Session addresses those changes and includes a provision, that in the event other legislation passes that also includes the sections covered by the conforming legislation; the changes made by the conforming legislation will take precedence. However, new legislation referencing the regulatory entities needs to accurately reflect the provisions of Amendment 8 and Chapter 2002-404, LOF. New language proposed by this bill in paragraph (a) of renumbered subsection (2) of s. 517.302, F.S., does not conform to those changes and should be amended to do so.

IV. AMENDMENTS/COMMITTEE SUBSTITUTE CHANGES

On April 14, the Subcommittee on Banking and Securities of the Commerce Committee adopted a strike everything amendment to the bill which substantively amends the original bill, by moving the newly granted

authority for the Attorney General to investigate and enforce against criminal securities violations to the section of the statutes relating to injunction authority²; by specifically authorizing the AG to use injunctive powers against securities violators; by increasing the administrative fines for securities violations from \$5,000 to \$10,000 per violation; and by removing one of the original bill's revisions of the severity level for certain criminal offenses.

² Section 517.191, F.S.