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Securities Law

Sale of Securities in Florida

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Introduction

The sale of securities is governed by both federal and state law. While the legislators and regulators responsible for drafting, implementing and enforcing the securities laws constantly seek to make the federal and state systems compatible, there nonetheless remain two distinct sets of securities laws.

The federal scheme of securities regulation relies on "disclosure"; that is, a company or other entity (called the "issuer") seeking to sell its securities must disclose to prospective investors all material information about the securities being offered.¹ The purpose of disclosure is to enable the prospective investor to make an informed decision on the proposed investment. Also under federal law, unless the sale of securities is exempt from registration, an issuer seeking to sell securities must register the securities with the United States Securities and Exchange Commission ("SEC") pursuant to the Securities Act of 1933 (the "33 Act").²

Florida is a "notification" state. This means that an issuer which registers its securities with the SEC under the 33 Act may sell those securities in Florida if it files a "notification" of the federal registration with Florida, together with the applicable filing fee.³ Securities that are subject to a federal registration statement do not undergo an independent review by the staff of the Florida Division of Securities.

Florida Registration Requirements

Securities which are "exempt" from registration under federal law that are offered and sold in Florida must register with Florida unless the offering or the security is specifically exempt from registration under Florida law.⁴ The major exception to this rule is a private placement⁵ that complies with Rule 506 of Regulation D of the 33 Act.⁶ By virtue of federal law enacted in 1996⁷, all state securities laws, including those of Florida, touching upon Rule 506 private placements have been preempted by federal law, other

than state filing fees and state anti-fraud laws. All other offerings, including those made under federal registration exemptions, must still comply with Florida law. While not identical, Florida's private placement exemption⁸ is very similar to those found in Rules 505 and 506 of Regulation D of the 33 Act and, as a practical matter, a carefully structured private placement offering that is exempt under the federal private placement safe-harbor rules should also be eligible for exemption from registration under Florida law.

Because of the foregoing considerations, the registration provisions of Florida law primarily apply to small *public offerings*⁹ that are governed by the SEC's Regulation A or Rule 504 of Regulation D, adopted under the 33 Act¹⁰.

Florida Merit Review

Like the federal government, Florida requires "disclosure" of material information by issuers to prospective investors to allow investors to make an informed investment decision. Additionally, Florida law prescribes a "merit" review of all securities registration statements filed with the state. This means that Florida imposes very specific standards, regarding the structure of a transaction and the health of a company, that must be met by issuers seeking to register their securities in Florida. Florida law requires the Department of Banking and Finance to find that "the terms of the sale of such securities would be fair, just, and equitable, and that the enterprise or business of the issuer is not based upon unsound business principles"¹¹

This statutory provision is implemented by the concrete requirements contained in Chapter 3E-700 of the Florida Administrative Code. These rules set forth requirements regarding the ratio of equity investment held by the company's "promoters" to the aggregate dollar amount of the public offering, requirements for voting rights except in specified situations, limitations on the granting of options or warrants to underwriters and to officers and employees, requirements that the proceeds of the sale of securities be placed in escrow, limitations on the issuance of preferred stock or debt securities, requirements on the offering price of equity securities, prohibitions on the registration of securities of issuers in unsound financial condition, and requirements regarding loans and material transactions with affiliates of the issuer.

Effective October 1997, Florida's version of the Small Corporate Offering Registration, better known as "SCOR", became law.¹² While providing a modicum of liberalization to the Florida registration requirements, a SCOR offering must still fulfill Florida's "merit" requirements.

Conclusion

Because of the significant restrictions and burdens placed upon issuers seeking to register a small public offering in Florida, it is imperative that a prospective issuer carefully review the applicable Florida statutes and rules before commencing any work on a proposed offering to confirm that its securities will be eligible for registration in Florida. Alternative approaches should also be evaluated, including a private placement or even a public offering registered with the SEC, to determine the most cost-effective approach for the prospective issuer.

1. Section 17(a)(2) of the Securities Act of 1933 provides, in relevant part: "It shall be unlawful for any person in the offer or sale of any securities ... to obtain money or property 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 were made, not misleading"
2. 15 U.S. Code Sec. 77a-77aa, as amended.
3. § 517.082, Florida Statutes.
4. § 517.081, Florida Statutes.
5. Although an oversimplification, the term "public offering" means the sale or offer of sale of securities by an issuer by means of general advertising or general solicitation and the term "private placement" means the sale or offer of sale of securities not involving a public offering, i.e. not made through general advertising or general solicitation.
6. The rules and regulations under the 33 Act appear in the Code of Federal Regulations at Title 17, Part 230 (17 CFR 230).
7. National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, 110 Stat. 3416 (1996).
8. See § 517.061(11)(a), Florida Statutes
9. See footnote 3 above.
10. Regulation A governs exempt public offerings up to \$5 million and Rule 504 governs exempt public and private placement offerings up to \$1 million.
11. See Section 517.081(7), Florida Statutes.
12. § 517.081(3)(g)2, Florida Statutes. SCOR offerings are governed by Rule 3E-700.028 of the Florida Administrative Code.