STATE OF FLORIDA
OFFICE OF FINANCIAL REGULATION

Statute Review

Biennial Report December 2024

Promoting a safe marketplace for financial success

Russell C. Weigel, III

Commissioner

Mission Statement: To protect Florida's financial services consumers, promote a safe and sound financial marketplace, and contribute to the growth of Florida's economy through fair, innovative, and excellent regulation of the financial services industry.

Vision Statement: The Office of Financial Regulation envisions Florida's capital market prominence, the strengthening of its financial marketplace, and the continuous availability and dissemination of financial education tools for Floridians to aid in their financial choices while effectively protecting them from predatory practices and wrongdoing.

Commissioner Russell C. Weigel, III

To: The Financial Services Commission

The Office of Financial Regulation (OFR) presents the following statute review report as an initial assessment of all Florida statutes under OFR purview compared to statutory and judicial changes in other states and considers whether Florida's laws should be updated.

The report is styled as "biennial" because the OFR intends to refresh this report every two years. The OFR is not required to prepare a report of this nature.

The OFR welcomes your feedback and hopes this report facilitates discussions and ideas aimed at continuing to modernize Florida's laws and develop any appropriate regulatory frameworks.

Sincerely,

Russell C. Weigel, III
Commissioner

WWW.FLOFR.GOV
200 East Gaines Street, Tallahassee, Florida 32399-0370
(850) 410-9601 • FAX (850) 410-9663

Statute Review Report

Table of Contents

I. Introduction

In 2022, the Office of Financial Regulation ("OFR" or "Office") undertook its first biennial comparison of OFR statutes to comparable statutory and judicial developments in other states. This updated biennial report highlights any changes in state and federal codes and judicial opinions and evaluates whether Florida law should be updated to address the issues other states have addressed.

The Divisions of Consumer Finance, Securities, Financial Institutions, and the Bureau of Financial Investigations have compiled their research and present the following findings.

II. Division of Consumer Finance

A. Current Regulatory Frameworks for Money Services Businesses:

Chapter 560, Florida Statutes ("Chapter 560"), provides for the licensure and regulation of money services businesses and their authorized vendors in the state of Florida. Chapter 560 and its areas of regulation are unique to the state of Florida. There are two model acts to compare with Chapter 560 but neither reaches all of the types of money services businesses covered by Chapter 560.

1. Uniform Money Services Act:

The Uniform Money Services Act ("UMSA") is a law approved by the Uniform Law Commission in 2000 which lays the regulatory framework for the Model Law and creates licensing provisions for various types of MSBs.

2. Model Money Transmission Modernization Act:

The Model Money Transmission Modernization Act ("Model Law")[1] was approved by the Conference of State Bank Supervisors ("CSBS") in 2021 and is a set of nationwide standards designed to replace state-specific money transmitter laws.

The below table highlights the differences between the UMSA and chapter 560, Florida Statutes, and discusses the pros and/or cons of those differences.

Uniform Money Services Act:

DIFFERENCES	PROS	CONS
Requires uniformity in the licensing process, including license applications, fee processing, background checks,	Attempts to unify state regulatory regimes by requiring uniformity in the application and	Only 12 states and territories have adopted the UMSA[2]; however, each state has its own interpretation of the

[1] The Model Money Transmission Modernization Act, also known as the Money Transmitter Model Law.
[2] Adopted by 12 states and territories, including Alaska, Arkansas, Hawaii, Iowa, New Mexico, North Carolina, Puerto Rico, South Carolina, Texas, U.S. Virgin Islands, Vermont, and Washington.

DIFFERENCES	PROS	CONS
applications for acquisitions of control, surety bonds (for money transmitters), reporting, collection and maintenance of records, and examinations.	license process across the states.	law, which defeats the purpose of having a uniform regulatory scheme.
Allows for license reciprocity between states.	A licensee may apply for a license in one state and once approved, may become licensed in another state without going through the entire license process.	Each state adopted its own version of the USMA. However, some states chose not to offer license reciprocity, others chose not to license persons engaged in check cashing, while others chose not to adopt all UMSA defined terms. If the Office adopted the UMSA, including its license reciprocity provisions, the Office would be required to conduct its own review of each application to ensure the applicant is in conformance with the USMA's provisions. With each state adopting its own provisions, the license reciprocity may not work as intended.
No virtual currency provisions.		Chapter 560 contains provisions regulating virtual currency transmissions. If the Office adopted in the UMSA in its entirety, the Office would lose such provisions.
Does not regulate deferred presentment providers.		Chapter 560 contains provisions regulating deferred presentment providers. If the Office adopted in the UMSA in its entirety, the Office would lose such provisions.

The table below highlights the differences between the Model Law and chapter 560, Florida Statutes, and discusses the pros and/or cons of those differences.

Model Money Transmission Modernization Act:

DIFFERENCES	PROS	CONS
Creates a uniform regulatory regime for money transmission, including stored value, sale of payment instruments, and transmission of fiat and virtual currency.	Attempts to unify state regulatory regimes by requiring uniformity in the license and regulation process across the states.	The law's uniform regulatory regime does not cover check cashing, currency exchange or payday lending.
Encourages states to participate in a multistate licensing process ("MMLA") to coordinate application processing for money transmission licenses, applications for the acquisition of control of a licensee, control determinations, or notice and information requirements for a change of key individuals.		Only twenty-three states have committed to participating in the MMLA. Currently, Florida is not a participant in the MMLA. The MMLA only applies to chapter 560, Part II activities. It would be inefficient to adopt a multistate licensing process for some license types in chapter 560 and not others.
Encourages and authorizes states to use the Nationwide Multistate Licensing System and Registry ("NMLS") for all aspects of licensing and encourages states to adopt standardized definitions and exemptions.		Currently, the Office does not utilize NMLS for the process of licensing chapter 560 applicants. If the Office used NMLS, licensees would be required to pay NMLS's filing fees in addition to the agency's statutory required fees. In addition, only Part II licensees would be able to take advantage of the NMLS licensure process. It would be inefficient to not have all chapter 560 license types utilize NMLS. Also, the Model Law makes CSBS the designated filing entity, giving it a monopoly on filings.
The Model Law seeks to regulate virtual currency business activity while excluding non-business virtual currency activities. Virtual-currency business activity means exchanging,		Currently, chapter 560 only requires the licensure of persons transmitting virtual currency through an intermediary. If adopted, persons not currently subject to regulation - those exchanging or storing virtual

DIFFERENCES	PROS	CONS
transferring, or storing virtual currency or engaging in virtual currency administration (issuing virtual currency with the authority to redeem the currency for money, bank credit, or other virtual currency).		currency, would need to become licensed under chapter 560 and abide by its provisions.
The law does not regulate deferred presentment providers.		Chapter 560 contains provisions regulating deferred presentment providers. If the Office adopted in the UMSA in its entirety, the Office would lose such provisions.

B. Uniform Regulation of Virtual Currency Business Act

Under traditional money transmission activity, an intermediary receives currency, monetary value, etc. from A for the purpose of transmitting the currency, monetary value, etc. to B. There is rarely a question as to whether the intermediary can move the currency, monetary value, etc. from A to B, but rather did the intermediary move the money as promised? However, with virtual currency transmission, the question is not only whether the virtual currency will be transferred as promised, but whether the intermediary has the proper control over the virtual currency to do so. Particularly, whether the intermediary holds the unique cryptographic keys to transfer the virtual currency, and if so, whether the intermediary has "control" over the keys.

As the Office incorporates more virtual currency provisions in its regulations, the Office should consider whether the subject of control should be addressed in future legislation. If so, the Office may look to the Uniform Law Commission Uniform Regulation of Virtual Currency Businesses Act ("VCBA") for inspiration. The VCBA was designed to create a uniform state-by-state statutory structure for regulating virtual currency business activity and requires a license "to engage in virtual currency business activity" or to hold oneself out as being able to do so. The VBCA defines the term "control" to mean, in relevant part, the "power to execute unilaterally or prevent indefinitely a virtual-currency transaction." The commentary makes clear, the VCBA is "focused on intermediary providers of virtual-currency products and services – not on the virtual currency itself or on the 'owner' of virtual currency" that can effect transactions on its own behalf.[3] In addition, the VCBA contains numerous consumer/user protections designed to assure persons of the safety and security of their virtual currency transactions.[4] Such protections include requirements for licensees and registrants to provide disclosures to potential customers about their products and services, such as any fees charged or whether there is insurance coverage, and to establish specific policies and compliance programs to

[3] McLaughlin and Love, *K&L Gates Discusses the Virtual-Currency Business Act and Coming Cryptocurrency Regulation*, The CLS Blue Sky Blog, Nov. 17, 2017, https://clsbluesky.law.columbia.edu/2017/11/17/kl-gates-discusses-the-virtual-currency-businesses-act-and-coming-cryptocurrency-regulation/.

[4] Kaplinsky and Spagnuolo, *Uniform Act to Regulate Virtual Currency Businesses Ready for State Adoption*, Ballard Spahr, Jan. 9, 2018, https://www.ballardspahr.com/insights/alerts-and-articles/2018/01/uniform-act-to- regulate-virtual-currency-businesses-ready-for-state-adoption.

guard against fraud, cyberthreats, and terrorist activity.[5] The VCBA prohibits a licensee or registrant from transferring a client's currency or using it as collateral for a loan to the licensee or registrant without prior consent.[6]

It should be noted that the VCBA not only requires the licensure of persons who engage in transferring virtual currency, but also the exchange and storing of virtual currency.[7] As such, the VCBA should only be used as a reference guide and should not be adopted verbatim within chapter 560, Florida Statutes. Adoption should focus on control and consumer protection provisions under the VCBA. Louisiana and Rhode Island are the only states that have adopted the VCBA. If a majority of states adopted the VCBA, any argument claiming a need for federal regulatory preemption of this area would be minimized.

As the transmission of virtual currency is uniquely different from that of traditional money transmission in terms of whether a person holds the cryptographic keys to transfer virtual currency and whether an intermediary has control over the keys, the Office should consider adding a separate part under chapter 560, Florida Statutes, for virtual currency transmissions. While chapter 560, part I, Florida Statutes, would continue to apply to all money services business activity, including virtual currency transmission, the more specific provisions related to virtual currency transmission would fall under a separate part. This separation would allow the Office to properly accommodate newer virtual currency activities without disturbing provisions related to traditional money transmission.

C. Streamlining of Consumer Lending Statutes

For the 2025 Legislative Session, the Office is proposing the streamlining of chapters 516, 537, and 520, Florida Statutes. The amendments would apply to consumer finance companies, title loan lenders, motor vehicle retail installment sellers, retail installment sellers, and sales finance companies. The streamlining of Florida's consumer lending statutes will provide greater efficiency and effectiveness by harmonizing these statutes in areas such as powers and duties, licensing standards, criminal background checks, examination authority, and disciplinary provisions. Additionally, the streamlining will include reduced application fees as the Office looks to coordinate these statutory changes with the implementation of REAL 2.0, a more robust system utilizing the latest in technology, including artificial intelligence. Creating this streamlined statutory framework for licensees engaged in lending would decrease regulatory variations between licensees, allow for less complicated examinations as examiners would not need to learn differing regulations for each license type, and would simplify the licensure process as applicants would submit substantially similar forms and analysts would review less materials, thereby decreasing the time taken to review applications.

D. Cybersecurity

Cybercrime is nothing new, but increased levels of connectivity, remote working, reliance on technology, and automation means the risk of attack is rising rapidly.[8] Sensitive consumer data is an alluring target for cyber criminals. In response, many states have enacted laws requiring their licensees

---

5 *Id.*
6 *Id.*
7 This runs afoul of the current licensure requirements in chapter 560, Florida Statutes.
8 Snaith and Pancholi, *Why Cybercrime is Increasing – and How to Stay Secure*, RSM UK Group, https://www.rsmuk.com/ideas-and-insights/why-cybercrime-is-increasing-and-how-to-stay-secure (last visited Aug. 18, 2022).

to institute cybersecurity policies. New York requires all financial services industry licensees to implement and maintain a written cybersecurity policy.[9] Effective March 1, 2017, the Superintendent of Financial Services promulgated 23 NYCRR Part 500, a regulation establishing cybersecurity requirements for financial services companies (referred to below as "the Cybersecurity Regulation" or "Part 500").[10] The regulation requires licensees to (1) maintain a cybersecurity program designed to protect the confidentiality, integrity and availability of the licensee's information systems; (2) use defensive infrastructure and the implementation of policies and procedures to protect the licensee's information systems; (3) detect cybersecurity events; (4) respond to identified or detected cybersecurity events to mitigate any negative effects; (5) recover from cybersecurity events and restore normal operations and services; and(6) fulfill applicable regulatory reporting obligations.[11] As the financial services industry expands and its reliance on internet technology grows, the Office is proposing legislation for the 2025 Legislative Session to address cybersecurity issues that are sure to arise from such growth and expansion.

E. Fair Debt Collection Practices Act Rules

On November 30, 2021, two new rules under the Fair Debt Collection Practices Act ("FDCPA") took effect.[12] In part, the rules attempt to clarify how debt collectors can use new communication technologies, expand the information debt collectors must provide at the outset of their debt collection efforts, and eliminate the practice of passive debt collection through credit reporting.[13]

In comparison to chapter 559, part VI, Florida Statutes, the new rules are more restrictive in nature and contain more expansive consumer protection measures. In keeping with its mission to protect Florida's financial services consumers, it may be wise for the Office to amend chapter 559, part VI, Florida Statutes, to track the FDCPA rule's language and/or prescribe that a violation of the FDCPA may constitute a violation of chapter 559, part VI, Florida Statutes.

F. Chapter 559, Part XII, Florida Statutes – Financial Technology Sandbox Program

In January 2021, Florida established a financial technology sandbox program ("sandbox") under the provisions of chapter 559, part XII, Florida Statutes, allowing participants to hold licensure for a period of two years with an opportunity to extend its licensure period for an additional 12 months. The sandbox program was designed to specifically allow financial technology innovators to test new products and services in a supervised, flexible regulatory sandbox using exceptions to specified general law and waivers of the corresponding rule requirements under defined conditions.[14]

---

[9] State of New York regulations do not apply to broker dealers and investment advisors as they do not fall under the definition of covered entities. The Securities and Exchange Commission and the Financial Industry Regulatory Authority have cybersecurity rules applicable to investment advisers (not state-registered) and dealers.

[10] Snaith and Pancholi, *Why Cybercrime is Increasing – and How to Stay Secure*, RSM UK Group, https://www.rsmuk.com/ideas-and-insights/why-cybercrime-is-increasing-and-how-to-stay-secure (last visited Aug. 18, 2022).

[11] 23 CRR-NY 500.

[12] 12 CFR Part 1006.

[13] Caren D. Enloe, *The Debt Collection Rule: Communications, Disclosures, and the Other Changes You Need to Know*, ABA, Sep. 21, 2021, https://www.americanbar.org/groups/business_law/publications/committee_newsletters/consumer/2021/202109/debt-collection-1/.

[14] § 559.952(2), Fla. Stat.

Over 10 states have established various fintech sandbox regulations, with the state of Arizona enacting the first regulatory sandbox in 2018.[15] Since its inception, Arizona's regulatory sandbox program has licensed thirteen businesses, with three businesses currently holding an active license.[16] However, most U.S. sandbox programs have been unsuccessful in attracting participants.[17] In fact, FinTech and insurance-focused sandboxes in Kentucky, Nevada, and Utah have yet to accept any participants — even though these states established their sandbox programs in 2020 or earlier.[18] Florida has had nine businesses apply for a sandbox license; however, none have completed the application process. Those who have applied have either withdrawn their application and sought a money services business license under Chapter 560, Florida Statutes,[19] or simply abandoned the licensure process altogether.

Sandbox applicants who have withdrawn their applications with the OFR have cited a cumbersome and confusing application process. During the application process, applicants must, among other things, prove that they have a physical presence in Florida; prove that they can provide a product or service that is innovative[20] in nature; specify each general law enumerated in section 559.952(4)(a), Florida Statutes, that prevents the innovative financial product or service from being made available to consumers and explain the reasons for the prohibition; maintain a net worth of at least $25,000, and maintain a surety bond of at least $75,000.[21] Sandbox programs in other jurisdictions are not quite as restrictive as the Office's sandbox program. In fact, programs in other jurisdictions allow for the provision of products and services related to mortgage lending, motor vehicle retail installment contracts,[22] check cashing,[23] and even vehicle title loans.[24] Other sandbox programs do not require net worth or bonding amounts.[25] Such programs simply require licensees to demonstrate that consumers will be financially protected for the duration of the test. Some sandbox programs do not require a business to establish state domicile but simply require the licensee to subject itself to the state's jurisdiction.[26]

Businesses applying for a license that is designed to be temporary in nature, may indeed find it burdensome (1) to comply with regulations requiring a licensee/applicant to specify each general law enumerated in section 559.952(4)(a), Florida Statutes, that prevents the innovative financial

---

[15] *Things to Know About Arizona's FinTech Sandbox*, Greater Phoenix Economic Council, Apr. 8, 2021, https://www.gpec.org/blog/things-to-know-about-arizonas-fintech-sandbox/.
[16] *Welcome to Arizona's FinTech Sandbox,* State of Arizona, Attorney General, https://www.azag.gov/fintech/participants (last visited Aug. 19, 2022).
[17] https://www.realclearpolicy.com/articles/2022/02/03/state_lawmakers_need_a_better_strategy_to_make_regulatory_sandbox_programs_a_success_814996.htm.
[18] https://www.realclearpolicy.com/articles/2022/02/03/state_lawmakers_need_a_better_strategy_to_make_regulatory_sandbox_programs_a_success_814996.html.
[19] Two such applicants currently hold a money services business license.
[20] Pursuant to section 559.952(3)(h), Fla. Stat., the term "innovative" means new or emerging technology, or new uses of existing technology, which provide a product, service, business model, or delivery mechanism to the public and which are not known to have a comparable offering in this state outside the Financial Technology Sandbox.
[21] For a licensee offering the product to no more than 7,500 consumers. The required amount increases as the number of consumers increase.
[22] *See supra* note 33.
[23] *See* West Virginia's regulatory sandbox provisions found at West Virginia Code §31A-8G-1, et. seq.
[24] *See supra* note 33.
[25] *See* Utah's regulatory sandbox provisions found at Utah Code 63N-16-101, et. seq. and *See* Arizona Revised Statutes §§ 41-5601, et seq.
[26] *See* Arizona Revised Statutes §§ 41-5601, et seq.

product or service from being made available to consumers and explain the reasons for the prohibition; (2) to meet current net worth and bonding requirements; and (3) to limit the provision of products/services offered to chapter 516 and chapter 560, Florida Statutes, activities. Initial versions of the legislation implementing Florida's sandbox program sought to create a more expansive program. In particular, the legislation allowed for the provision of products and services offered under banking, securities, consumer credit, and money transmission laws. If it is the Office's intention to attract more sandbox participants, then it may be worth revisiting the current sandbox program with an eye towards easing existing regulatory requirements and expanding permissible activities.

G. Chapter 494, Florida Statutes

Title V of P.L. 110-289, the *Secure and Fair Enforcement for Mortgage Licensing Act of 2008* ("SAFE Act"), was passed on July 30, 2008. The new federal law gave states two years to pass legislation requiring the licensure of mortgage loan originators according to national standards and the participation of state agencies on the Nationwide Multistate Licensing System (NMLS) (originally known as the Nationwide Mortgage Licensing System and Registry). The SAFE Act is designed to enhance consumer protection and reduce fraud through the setting of minimum standards for the licensing and registration of state-licensed mortgage loan originators. Mortgage loan originators who work for an insured depository or its owned or controlled subsidiary that is regulated by a federal banking agency, or for an institution regulated by the Farm Credit Administration, are registered. All other mortgage loan originators are licensed by the states.[27]

The SAFE Act requires state-licensed mortgage loan originators to pass a written qualified test, to complete pre-licensure education courses, and to take annual continuing education courses. The SAFE Act also requires all mortgage loan originators to submit fingerprints to NMLS for submission to the FBI for a criminal background check; and state-licensed mortgage loan originators to provide authorization for NMLS to obtain an independent credit report.[28]

1. Remove High School Diploma Requirement:

A person applying for a loan originator license pursuant to chapter 494, Florida Statutes, must have a high school diploma or equivalent. In addition to having a high school diploma, a loan originator applicant must complete twenty hours of NMLS approved pre-licensure education, and pass a written test developed by the NMLS. The twenty hours of pre-licensure education must include two hours of state-specific education covering the provisions of chapter 494 and the rules promulgated thereunder. To meet the testing requirement, an applicant must obtain the following:

a. Passing results on both the National and Florida State components of the SAFE Test; or
b. Passing results on both the National and Stand-alone UST components of the SAFE Test; or
c. Passing results on the National Test Component with Uniform State Content.

National standards does not address high school education requirement. They do address testing and education because it is part of the federal SAFE Act. To the Office's knowledge, Florida

[27] https://mortgage.nationwidelicensingsystem.org/safe/SitePages/default.aspx (last visited August 7, 2024).
[28] *Id.*

is the only state that requires a high school diploma. The lack of a high school diploma should not foreclose licensure since it is necessary for applicants to complete NMLS approved pre-licensure education and pass a written test developed by the NMLS. The Office should propose legislation removing the high school diploma requirement for loan originator applicants.

2. Remove State-Specific Fingerprinting Requirements:

Loan originators and control person(s) of mortgage brokers and mortgage lenders are required to complete a Florida state-specific criminal background check and an FBI criminal history background check. The state-specific criminal background check has proved to be redundant, as the FBI criminal history background check contains the same results found in the state-specific criminal background check. In addition, the state-specific background check for loan originators requires the Office to retain fingerprints, which requires a significant amount of administrative resources to manage. The Office should propose legislation removing the state-specific fingerprint requirement and rely solely on the FBI background check conducted through the NMLS.

H. Chapter 687, Florida Statutes: Loan Broker Definition

Section 687.14(4), Florida Statutes, defines a "loan broker" and currently excludes various persons licensed by the Office and other regulating bodies. For instance, the definition expressly excludes "any mortgage broker or lender." However, the definition currently does not exclude mortgage loan originators. This provision was last amended in 2003, back when mortgage brokers and mortgage lenders were the only licenses issued pursuant to chapter 494 Florida Statutes.

In 2008, chapter 494, Florida Statutes, was amended extensively to comply with the federal Secure and Fair Enforcement for Mortgage Licensing ("SAFE") Act. The 2008 amendments to chapter 494 created a new type of licensee supervised by the Office, called a "loan originator." Thus, loan originators did not exist in 2003 when section 687.14, Florida Statutes, was last amended.

While it is true that an individual mortgage broker license is the historical equivalent of a loan originator license, a statutory modification to section 687.14, Florida Statutes, would make it clear that loan originators who engage in activity authorized by that license are not also "loan brokers" subject to further regulation pursuant to chapter 687, Florida Statutes.

For the sake of clarity and consistency in statutory references, therefore, the Office might consider simply amending the definition of "loan broker" found in section 687.14(4), Florida Statutes, to exclude "any mortgage broker, lender, or loan originator."

III. Division of Securities

A. Registration of Finders

In October 2020, the Securities and Exchange Commission ("SEC") voted to propose a new limited, conditional exemption from broker registration requirements for "finders" who are natural persons who assist issuers with raising capital in private markets from accredited investors. The proposal would create two classes of finders, Tier I Finders and Tier II Finders, that would be subject to conditions tailored to the scope of their respective activities. A Tier I Finder would be limited to providing contact information of potential investors in connection with only a single capital raising transaction by a single issuer in a 12-month period. A Tier II Finder could solicit investors on behalf of an issuer, but the solicitation-related activities would be limited to: (i) identifying, screening, and contacting potential investors; (ii) distributing issuer offering materials to investors; (iii) discussing issuer information included in any offering materials, provided that the Tier II Finder does not provide advice as to the valuation or advisability of the investment; and (iv) arranging or participating in meetings with the issuer and investor.[29]

The North American Securities Administrators Association ("NASAA") has voiced its opposition to the SEC's proposal stating that fraud and other harms are more likely to occur where either a security being offered, an intermediary involved in the sale of securities, or both are unregistered.[30]

As of September 2024, the SEC has not taken any further action on its proposal. Currently California, Texas, and Michigan explicitly identify and regulate finders. The Office should evaluate finder activity in Florida and consider whether explicit regulation of finders in Florida is warranted.

B. Information Security and Privacy

On May 19, 2019, NASAA adopted its "Investment Adviser Information Security and Privacy Rule." The rule requires state registered investment advisers to establish, implement, update, and enforce written physical security and cybersecurity policies and procedures reasonably designed to ensure the confidentiality, integrity, and availability of physical and electronic records and information. The policies and procedures must be tailored to the investment adviser's business model and reviewed at least annually. The rule further requires that an investment adviser deliver to its clients a privacy policy. The model rule has been adopted or proposed for adoption by at least seven NASAA jurisdictions.

On November 24, 2020, NASAA adopted its Model Rule for Investment Adviser Written Policies and Procedures Under the Uniform Securities Acts of 1956 and 2002.[31] The model rule requires investment advisers to establish, maintain, and enforce written policies and procedures that address: regulatory compliance, supervision, proxy voting, *physical security and cybersecurity*, business continuity and succession, code of ethics compliance, and the handling of material non-public information.

On July 26, 2023, the SEC adopted rules requiring its registrants to disclose material cybersecurity incidents they experience and to disclose on an annual basis material information regarding their cybersecurity risk management, strategy, and governance. The SEC also adopted rules requiring foreign private issuers to make comparable disclosures. The new rules will require

[29] Press Release, SEC, *SEC Proposes Conditional Exemption for Finders Assisting Small Businesses with Capital Raising* (Oct. 7, 2020), https://www.sec.gov/news/press-release/2020-248.
[30] Comment Letter, NASAA, *NASAA Outlines Opposition to SEC's Proposed Federal Broker-Dealer Exemption for Private Placement Finders* (Nov. 13, 2020), https://www.nasaa.org/56150/nasaa-outlines-opposition-to-secs- proposed-federal-broker-dealer-exemption-for-private-placement-finders/.
[31] NASAA Model Rule for Investment Adviser Written Policies and Procedures Under the Uniform Securities Acts of 1956 and 2002 (adopted 11/24/2020), https://www.nasaa.org/wp-content/uploads/2020/07/NASAA-IA-PandP- Model-Rule-and-Sample-Compliance-Grid.pdf.

registrants to disclose on Form 8-K any cybersecurity incident they determine to be material four business days after such determination is made.[32]

On May 16, 2024, the SEC adopted rule amendments that will require brokers and dealers, investment companies, investment advisers registered with the SEC, funding portals, and transfer agents registered with the SEC or another appropriate regulatory agency as defined in the Securities Exchange Act of 1934 ("transfer agents") to adopt written policies and procedures for incident response programs to address unauthorized access to or use of customer information, including procedures for providing timely notification to individuals affected by an incident involving sensitive customer information with details about the incident and information designed to help affected individuals respond appropriately. In addition, the amendments extend the application of requirements to safeguard customer records and information to transfer agents; broaden the scope of information covered by the requirements for safeguarding customer records and information and for properly disposing of consumer report information; impose requirements to maintain written records documenting compliance with the amended rules; and conform annual privacy notice delivery provisions to the terms of an exception provided by a statutory amendment to the Gramm-Leach-Bliley Act.[33]

In Florida, dealers, and federal covered advisers are required to comply with section 248.30 of Regulation S-P (17 C.F.R. §248.30).[34] Regulation S-P requires dealers and federal covered advisers to "adopt written policies and procedures that address administrative, technical, and physical safeguards for the protection of customer records and information."[35]

Florida investment advisers are not required to comply with section 248.30 of Regulation S-P. However, section 501.171, Florida Statutes, requires a sole proprietorship, partnership, corporation, trust, estate, cooperative, association, or other commercial entity that acquires, maintains, stores, or uses personal information to take reasonable measures to protect and secure data in electronic form containing personal information. Such entities must provide notice to the Department of Legal Affairs (OAG) of any breach of security affecting 500 or more individuals in the state. This section also requires entities to take all reasonable measures to dispose of such records. Such disposal shall involve shredding, erasing, or otherwise modifying the personal information in the records to make it unreadable or undecipherable through any means. A violation of this section is treated as an unfair or deceptive trade practice in any action brought under section 501.207, Florida Statutes, against an entity. Additionally, violators may be subject to a civil penalty.

Section 517.0611(12)(f), Florida Statutes, requires intermediaries or the issuer of securities under Florida's Limited Offering Exemption to "[t]ake reasonable steps to protect personal information collected from investors, as required by s. 501.171."

The Office should evaluate its investment advisers' current cybersecurity practices and decide

[32] SEC, Cybersecurity Risk Management, Strategy, Governance, and Incident Disclosure, 88 FR 51896 (Aug. 4, 2023), https://www.govinfo.gov/content/pkg/FR-2023-08-04/pdf/2023-16194.pdf.
[33] SEC, Regulation S–P: Privacy of Consumer Financial Information and Safeguarding Customer Information, 88 FR 47688, Final Rule (June 3, 2024), https://www.govinfo.gov/content/pkg/FR-2024-06-03/pdf/2024-11116.pdf.
[34] § 517.1217, Fla. Stat. and Rule 69W-600.013, Fla. Admin. Code.
[35] *See* Release 34-42974, Privacy of Consumer Financial Information (Regulation S-P), Section III, Subpart E - Safeguard Procedures, (June 22, 2000).

whether it is necessary to adopt regulations like the NASAA model rule. In addition to the protections of section 501.171, Florida Statutes, discussed above, investment advisers are fiduciaries and are required to maintain policies and procedures to ensure compliance with chapter 517, Florida Statutes. Further, many investment advisers do not have custody of investor funds; accordingly, the risk of directly losing investor funds in a cyberattack is low. The risk of losing customer identifying information in a cyberattack that could be exploited elsewhere remains. These facts should then be balanced against the cost associated with implementing policies and procedures as contemplated by the NASAA model rule.

C. NASAA Model Act to Create Restitution Assistance Funds for Victims of Securities Violations

On May 17, 2021, NASAA adopted model legislation which creates a restitution assistance fund for victims of securities violations. The model act provides financial assistance to victims of securities law violations who are awarded restitution in a final order but do not receive full payment. The model act defines "final order" as a "final order issued by the [jurisdiction] under this chapter or a final order issued by the court in a legal action initiated by the [jurisdiction] under this chapter." The model act establishes a state securities restitution assistance fund, outlines eligibility requirements for victims seeking restitution assistance, sets payment caps on the amount of restitution assistance awards, prohibits and forfeits awards in certain circumstances, and provides for recovery mechanisms. The model act also calls for restitution assistance awards to be doubled for victims of securities violations who meet certain criteria to be considered vulnerable persons, whether by age or other factors.[36] Restitution assistance awards are capped at the lesser of $25,000 or 25% of the amount of unpaid restitution awarded in the final order. These limits are doubled when the victim is a vulnerable person.

According to NASAA, "the model act draws upon similar legislation in Indiana, Montana, Vermont, Kansas and Maine." In a press release, NASAA President Lisa A. Hopkins said, "Indiana and Montana enacted this type of legislation nearly a decade ago and have reported that their restitution assistance programs are successful. For example, since the inception, Indiana has issued approximately $1 million in restitution assistance awards to 102 claimants, and Montana has awarded approximately $1.8 million to 134 claimants. The average age of a restitution recipient was 64 years old in Indiana, and 82% of restitution recipients were over 60 years old in Montana."[37] In 2023, North Dakota established a fund based on the model act.[38]

Effective October 1, 2024, the Florida Securities Guaranty Fund, was revised by chapter 2024-168, Laws of Florida. Section 517.131, Florida Statutes, establishes Florida's Securities Guaranty Fund. This fund provides monetary relief to victims of securities violations under chapter 517, Florida Statutes, who are entitled to monetary damages or restitution and who cannot recover the full amount of such monetary damages or restitution from the wrongdoer. A person is eligible for payment from the Securities Guaranty Fund if the person: 1) holds an unsatisfied final judgment

[36] NASAA Model Legislation to Create Restitution Assistance Funds for Victims of Securities Violations (May 17, 2021), https://www.nasaa.org/wp-content/uploads/2021/05/NASAA-Restitution-Assistance-Fund-Model-Act-Approved-May-17-2021.pdf.

[37] Press Release, NASAA, *NASAA Members Approve Model Act to Create Restitution Assistance Funds for Victims of Securities Violations* (May 18, 2021), https://www.nasaa.org/57582/nasaa-members-approve-model-act-to-create-restitution-assistance-funds-for-victims-of-securities-violations/.

[38] *See* SB 2325, https://legiscan.com/ND/text/SB2325/2023.

entered on or after October 1, 2024, in which a wrongdoer was found to have violated section 517.07 or section 517.301, Florida Statutes, has applied any amount recovered from the judgment debtor or any source to the damages awarded by the court or arbitrator, and is a natural person who was a resident of this state, or is a business entity that was domiciled in this state, at the time of the violation giving rise to the claim; or 2) is a receiver appointed pursuant to section 517.191(2), Florida Statutes, by a court of competent jurisdiction for a wrongdoer ordered to pay restitution under section 517.191(3), Florida Statutes, as a result of a violation of section 517.07, Florida Statutes, or section 517.301, Florida Statutes, which has requested payment from the Securities Guaranty Fund on behalf of a person eligible for payment. Section 517.131, Florida Statutes, specifies that the term "final judgment" includes arbitration awards confirmed by a court of competent jurisdiction. Payments from the fund are capped at $15,000/person or $25,000/person if the eligible person is a specified adult and $250,000 in the aggregate.

The Model Act differs from the Securities Guaranty Fund in that the Model Act is limited to providing restitution assistance for unpaid restitution awarded in a final order by an agency or by a court of competent jurisdiction in an action initiated by an agency; while the Securities Guaranty Fund provides monetary relief to victims entitled to monetary damages or restitution which are awarded by a court of competent jurisdiction (the action does not need to be initiated by the Office), which is potentially broader relief. However, the Model Act provides for higher awards.

The Office should continue to monitor developments in this area.

D. <u>NASAA Model Whistleblower Award and Protection Act</u>

On August 31, 2020, NASAA adopted its Model Whistleblower and Protection Act. The Act authorizes securities administrators to make a monetary award to whistleblowers who voluntarily provide original information about violations of state securities laws. The aggregate amount of awards that may be awarded in connection with an administrative or judicial action may not be less than ten percent (10%) nor more than thirty percent (30%) of the monetary sanctions imposed and collected in the related administrative or judicial action. The exact amount of the award is at the discretion of the agency and based on certain factors. The model act also would protect whistleblower confidentiality, prohibit retaliation by an employer against a whistleblower, and create a cause of action and provide relief for whistleblowers retaliated against by their employer.

In a press release, NASAA stated that "[t]he model act draws upon the whistleblower award provisions contained in section 922 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as well as from current state law in Indiana and Utah."[39] Since its adoption in 2020, the Model Act has been adopted in whole in or part in Montana, Vermont, and Washington.[40]

Sections 112.3187-112.31895, Florida Statutes, make up Florida's Whistle-blower's Act (the "Act"). The Act prohibits an agency or an independent contractor (a person, other than an agency, engaged in any business and who enters into a contract, including a provider agreement, with an

[39] Press Release, NASAA, *NASAA Members Adopt Model Act to Award and Protect Whistleblowers* (Aug. 31, 2020), https://www.nasaa.org/55628/nasaa-members-adopt-model-act-to-award-and-protect-whistleblowers/#:~:text=Among%20other%20provisions%2C%20the%20NASAA%20Model%20Whistleblower%20Award,up%20to%2030%20percent%20of%20the%20amount%20recovered.

[40] *See* MONT. CODE ANN. § 30-10-1111 (2023); VT. STAT. ANN. tit. 9, § 5617 (2023); WASH. REV. CODE Ch. 21.40 (2023).

agency) from taking certain adverse actions against an employee for disclosing information under the Act. The information disclosed under this section must include: (a) any violation or suspected violation of any federal, state, or local law, rule, or regulation committed by an employee or agent of an agency or independent contractor which creates and presents a substantial and specific danger to the public's health, safety, or welfare; or (b) any act or suspected act of gross mismanagement, malfeasance, misfeasance, gross waste of public funds, suspected or actual Medicaid fraud or abuse, or gross neglect of duty committed by an employee or agent of an agency or independent contractor. The Act also creates a cause of action and provides relief for whistleblowers retaliated against such persons.

The Act differs from the Model Act in that it is limited to information provided concerning a possible violation of state or federal securities laws by an employee or agent of an agency or an independent contractor; it does not allow the Office to provide whistleblower awards, and it does not apply to an employer that is not an agency or independent contractor.

The Office is vetting whether a whistleblower provision similar to the Model Act would be helpful to assist its examinations and investigations by creating a safe environment for individuals to come forward to report suspected wrongful practices not only in the securities area, but also the other program areas of the Office.

E. <u>The Uniform Securities Act</u>

The Uniform Law Commission has developed model acts for states to use as the basis of their own statutes to bring about uniformity throughout the United States. The Uniform Securities Act of 2002 (the "2002 Act") is the current model and supersedes the two prior models, known as the Uniform Securities Act of 1956 (the "1956 Act") and the Revised Uniform Securities Act of 1985, as amended in 1988 (the "1985 Act").

The majority of states have adopted some version of the model act. However, a few, including Florida, have not. Chapter 517, Florida Statutes, is loosely based on the 1956 Act and contains many of the same provisions.

Some of the differences between the 2002 Act and chapter 517, Florida Statutes, include:

- <u>Registration by Coordination</u>: The 2002 Act provides for registration by coordination. Coordinated review programs for state registration of securities or franchise offerings allow an issuer to file one application for review and approval by multiple states. The states, under the auspices of NASAA, have created coordinated review protocols for equity, small company, franchise offerings, direct participation program securities, and certain Regulation A securities.

- Exempt Transactions: Section 517.061, Florida Statutes, contains a number of exemptions from the securities registration requirements of section 517.07, Florida Statutes. Chapter 2024-168, Laws of Florida, effective October 1, 2024, significantly reorganized this section and revised many of the exemptions to more closely resemble the exemptions found in Section 202 of the 2002 Act. However, Chapter 2024-168, Laws of Florida, also added several new exemptions from securities registration not found in the 2002 Act including: NASAA's Model Accredited Investor Exemption, the Florida Limited Offering Exemption, and the Florida Invest Local Exemption.[41]

Further, it is important to note that some of the topics covered by the 2002 Act are addressed in other chapters of the Florida Statutes. For example, public records and confidentiality of records is addressed in the 2002 Act. This topic is addressed in chapter 517, Florida Statutes, but also chapter 119, Florida Statutes. Additionally, the 2002 Act grants the securities administrators significant rule-making authority and leaves many items up to the securities administrator's discretion which may not be permissible or feasible under chapter 120, Florida Statutes, and other Florida law.

F. Regulation of Digital Assets and Market Participants

There are strong parallels to various aspects of the regulated securities industry and the cryptocurrency industry such as how cryptocurrencies are issued, how cryptocurrencies are traded and sold on the secondary market, and the intermediaries facilitating the buying and selling of cryptocurrencies.[42]

For example, a technology business creating and issuing a digital asset offered for investment purposes or having the characteristics of a traditional security, such as common stock, a bond, or an investment contract, is likely acting as an "issuer" and creating a "security" within the meaning of Florida's securities laws. Such activities are often referred to as initial coin offerings (ICOs) and are akin to initial public offerings (IPOs) of securities. Once such securities are issued and subsequently traded by their owners for economic gain, the transactions may look like ordinary securities market transactions but may nonetheless be found to not constitute the offer and sale of securities.

It is important to look closely at the transaction. In *SEC v. Ripple Labs, Inc., et al.,* 682 F.Supp.3d 308 (S.D.N.Y. 2023), the U.S District Court for the Southern District of New York considered whether Ripple offered to sell or sold XRP, the primary digital token at issue in the matter, as a security. Ripple engaged in three categories of XRP offers and sales: institutional sales (direct sales to certain counterparties pursuant to written contracts), programmatic sales (XRP sales on digital asset exchanges or through the use of trading algorithms), and other distributions under written contracts (payment for services). The court applied the *Howey* test and considered the economic reality and totality of circumstances surrounding the offers and sales and held that Ripple's Institutional Sales of XRP constituted the unregistered offer and sale of investment contracts while the other offers and sales did not. In determining that the programmatic sales did not constitute the unregistered offer and sale of

[41] *See* §§ 517.061, 517.0611, and 517.0612, Fla. Stat.
[42] In December 2022, the Office completed its white paper titled "Assessment of Commerce and Regulatory Issues Presented by Blockchain Technology and Virtual Currency," which comprehensively treats this topic.

investment contracts, the court emphasized the fact that the sales failed the third prong of *Howey* because they were made through blind bid/ask transactions and programmatic buyers could not have known if their money went to Ripple, or any other seller.

Digital assets meeting the definition of a "security" under Florida law ("digital asset securities") are regulated pursuant to the Florida Securities and Investor Protection Act, and the rules promulgated thereunder. Such digital assets are subject to the registration requirements under section 517.07, Florida Statutes, and must be registered with the Office or exempt from registration. The offer and sale of digital assets found to be securities are also subject to the anti-fraud provisions of section 517.301, Florida Statutes.

Intermediaries who open accounts for digital asset securities traders or investors, facilitate transactions in digital asset securities, create a market for digital asset securities, or give advice to those seeking to purchase digital asset securities are akin to traditional securities intermediaries such as securities broker- dealers, and investment advisers. Participants in the digital asset securities ecosystem who offer, sell, or recommend digital asset securities to Florida residents must register as a dealer or investment adviser under section 517.12, Florida Statutes, unless exempt or excluded from the requirements.

The Office, like other securities regulators, will need to continue to monitor the digital asset ecosystem as it evolves and matures and identify and analyze new digital assets and transactions involving digital assets or distributed ledger technologies (DLTs) on a case-by-case basis to determine whether they are securities under Florida's securities laws and how to best regulate new other products such as stable coins. Policy makers should consider whether additional disclosures should be required for digital asset securities to address: the high degree of fraud associated with such securities offerings; cybersecurity risks, including theft of digital assets by hackers; and the lack of liquidity, volatility and pricing speculation in the digital asset securities market. Further, policymakers should evaluate whether Florida's securities laws adequately regulate all the appropriate participants in the digital asset securities markets and, if not, whether Florida should modify its securities laws or create a separate regulatory scheme in this area. For instance, the Office is considering whether it is appropriate to regulate cryptocurrency exchanges as "dealers."

G. Regulation of Investment Adviser Solicitors

A solicitor is anyone who, directly or indirectly, solicits any client for, or refers any client to, an investment adviser. Solicitors are generally viewed as persons associated with an investment adviser and thus must register as such unless exempt from registration.

At the federal level, payment of a cash fee, directly or indirectly, to a solicitor is prohibited unless it meets the requirements of SEC Rule 206(4)-1.[43] The rule requires that an investment adviser be registered with the SEC and not disqualified. Fees must be paid pursuant to a written agreement and certain disclosures must be provided to prospective clients.

[43] 17 U.S.C. §275.206(4)-1 (effective May 4, 2021) formerly 17 U.S.C. §275.206(4)-3. The amended rule replaces and updates the SEC's former advertising rules and cash solicitation rules.

States, on the other hand, have various regulations depending on the activity of the solicitor and the solicitor's relationship with the investment adviser. Most states view solicitation activity as activity requiring registration. The Uniform Securities Act, which is adopted by many states, defines "investment adviser representative" as "an individual employed by or associated with an investment adviser or federal covered investment adviser and who . . . receives compensation to solicit, offer, or negotiate for the sale of or for selling investment advice." Other states do not require solicitors to register under their securities acts, require registration but with fewer requirements, provide exclusions for certain solicitors, or have de minimis exemptions for solicitation activity.[44]

Florida should consider whether to amend existing law to more clearly define whether solicitors are required to register and under what circumstances.

H. <u>Business Continuity</u>

On April 13, 2015, NASAA adopted its Model Rule on Business Continuity and Succession Planning. The rule requires investment advisers to establish, implement, and maintain written procedures relating to a business continuity and succession plan. The rule contemplates the plan being tailored to the investment adviser's business model and specifies elements that must be included.

In Florida, dealers are required to create and maintain a written business continuity plan. Investment advisers, however, are not explicitly required to have such a plan. Investment advisers are fiduciaries and are required to have written policies and procedures to ensure compliance with the securities laws.

The Office should determine whether a specific requirement is necessary or whether an investment adviser's obligation to look out for the interests of their clients, which would include a client's ability to continue to obtain advisory services, and guidance from the Office recommending that a business continuity plan be included in an investment adviser's written policies and procedures will suffice. Legislation is necessary to require a business continuity plan as discussed above.

---

[44] *See* Missouri Secretary of State, Registration of Brokers & Advisers FAQs, FAQ#7, https://www.sos.mo.gov/securities/licensing_faq#faq8 (Missouri does not require solicitors to register as investment adviser representatives); 10 CCR §260.236(c)(2), California Code of Regulations (California requires solicitors to register as an investment adviser representative but does not require the solicitor to take qualifying examinations); Rule 590-4-4-.12(2), Georgia Administrative Code (excludes CPAs and attorneys licensed in Georgia that solicit their own pre-existing accounting or legal clients on behalf of an RIA from the definition of investment adviser representative, and also has what amounts to a "de minimis" threshold that permits any other Georgia resident to solicit on behalf of an investment adviser so long as the annual clients solicited is capped at ten); Texas State Securities Board, FAQs for Investment Advisers and their Representatives, FAQ 1.B.3 and 1.B.4, https://www.kitces.com/blog/solicitor-rule-206-4-3-sec-state-ria-pay-cash-for-client-referral-attorney-accountant/ (distinguishing between solicitors for SEC registered investment advisers and state registered investment advisers).

I. Choice-of-Law Provisions

FINRA Rule 2268[45] establishes minimum disclosure requirements and requires that any predispute arbitration clause must be highlighted in the customer agreement and immediately preceded by specified disclosures that describe the consequences of agreeing to arbitration.

It also prohibits any pre-dispute arbitration agreement from including any condition that: (1) limits or contradicts the rules of any self-regulatory organization; (2) limits the ability of a party to file any claim in arbitration; (3) limits the ability of a party to file any claim in court permitted to be filed in court under the rules of the forums in which a claim may be filed under the agreement; or (4) limits the ability of arbitrators to make any award. FINRA interprets this provision to require that, "if a choice-of-law provision is used, there must be an adequate nexus between the law chosen and the transaction or parties at issue."[46]

Choice-of-law provisions can be harmful to customers when the customer does not understand the provision and a particular state's laws are selected by a firm to limit the scope of their liability or damages. FINRA Rule 2268 is incorporated into the Office's rules by reference, and a violation of the rule is considered a prohibited business practice Yet, this requirement does not apply to investment advisers, nor are investment advisers prohibited from imposing choice of venue provisions that favor the advisory firm and may require a venue in a different state than that of the claimant.

Notwithstanding, Rule 69W-600.0131(1)(s), Florida Administrative Code, applies to investment advisers and states that "[i]ncluding, in an advisory contract, any condition, stipulation, or provisions binding any person to waive compliance with any provision of Chapter 517, F.S., or with any provision of, or with any rule, regulation, or order issued under, the Investment Advisers Act of 1940" is a prohibited business practice.

The Office has received questions from industry on whether a particular choice-of-law provision in their customer contracts would violate Florida's securities laws. The Office should consider whether it is necessary to explicitly prohibit the use of certain choice-of-law provisions by statute or if it is sufficient to leave it to the courts to decide whether a choice-of-law provision or choice of venue provision is valid.

J. Model Rule Exempting Certain Merger & Acquisition Brokers ("M&A Brokers") From Registration

On September 29, 2015, NASAA adopted its "Model Rule Exempting Certain Merger & Acquisition Brokers ("M&A Brokers") from Registration." The rule was amended on May 6, 2024. The Rule was amended to: 1) expand the list of excluded activities for which an M&A Broker is not

[45] FINRA member firms are required to arbitrate all customer and employment claims. *See, e.g.,* FINRA Industry Code Rule 2263. FINRA arbitration hearings are generally conducted near where the customer resided at the time of the complaint or in employment disputes near where the employee resided at the time of the complaint. FINRA Customer Code Rule 12213; FINRA Industry Code Rule 13213. Investment adviser firms do not have a self-regulatory association like FINRA that imposes arbitration requirements on advisory firms. Thus, all disputes between investment advisory firms and their customers or employees are based on the terms of their respective contractual agreements.
[46] *NASD Notices to Members* 05-09, https://www.finra.org/rules-guidance/notices/05-09.

exempt; (2) reword the disqualifications section; (3) add a definition for "Business Combination Related Shell Company"; (4) amend the definition of "Control" to: a. remove the clause "is a director, general partner, member, or manager of a limited liability company or officer exercising executive responsibility (or has a similar status or functions)," and b. increase the percentage of voting stock and capital contributions from 20% to 25%; (5) include a provision with discretion for regulators to modify the dollar amounts for the eligibility of a privately held company; (6) include more specificity as to what types of transactions a Mergers and Acquisitions Broker can effect; and (7) amend the definition of a "shell company" to no longer include public companies.[47]

The Office plans to incorporate the changes to the rule in its forthcoming proposal to amend chapter 517, Florida Statutes.

K. Uniform Securities Act Manual Exemption

The Uniform Securities Act of 2002 contains a manual exemption which is more restrictive than that contained in previous Uniform Acts. The manual exemption contained in Section 202(2) of the USA (2002) generally exempts "a nonissuer transaction by or through a broker-dealer registered, or exempt from registration . . . and a resale transaction by a sponsor of a unit investment trust registered under the Investment Company Act of 1940, in a security of a class that has been outstanding in the hands of the public for at least 90 days" provided the following five conditions are satisfied:

1. The issuer is not in the organizational stage and is not a blank check, blind pool or shell company with no specific business plan;
2. The security is sold at a price reasonably related to its current market price;
3. The security is not part of an underwritten offering;
4. The security is listed in a nationally recognized securities manual that is publicly available and that contains:
    - o A description of the business and operations of the issuer;
    - o The names of the issuer's executive officers and the names of the issuer's directors, if any;
    - o An audited balance sheet of the issuer dated within 18 months of the transaction; and
    - o An audited income statement for the past two fiscal years; and
5. One of the following requirements is met:
    - o The issuer has a class of equity securities listed on a national exchange or designated for trading on the NASDAQ;
    - o The issuer is a unit investment trust registered under the Investment Company Act of 1940;
    - o The issuer has been engaged in continuous business for at least 3 years; or
    - o The issuer has total assets of at least $2,000,000 based on an audited balance sheet dated within 18 months prior to the transaction.

Most states, including Florida, recognize Mergent's Investor Service (formerly known as Moody's) as a nationally recognized securities manual under the exemption. A large number of states also recognize the website operated by the OTC Markets, Inc. with respect to securities of issuers

[47] NASAA, *Model Rule Exempting Certain Merger & Acquisition Brokers ("M&A Brokers") from Registration* (Adopted September 29, 2015; Amended May 6, 2024), https://www.nasaa.org/wp-content/uploads/2024/05/Model-Rule-Exempting-Certain-Merger-and-Acquisition-Brokers-From-Registration-_5-6-2024.pdf.

that trade through the OTCQX and OTCQB markets. Florida does not.

On April 26, 2023, NASAA solicited comments concerning "whether the existing requirements of the manual exemption provide an appropriate level of protection to investors who purchase securities from sellers relying on the manual exemption."[48] The Notice of Request for Comment stated that "the advent of electronic trading platforms has greatly expanded the ability of investors to engage in secondary trading of securities that are not otherwise listed on an exchange in reliance on the manual exemption. As noted in a 2016 report by staff at the U.S. Securities and Exchange Commission, securities of issuers that trade on these platforms present significant risks. Some of these risks (such as lack of liquidity) apply to securities traded in reliance on the manual exemption outside an electronic trading platform. Given these risks, the members of the Project Group question whether the existing requirements of the manual exemption as promulgated in the USA (2002) sufficiently mitigate the risks to investors who purchase securities under the manual exemption." As of September 2024, no model rule has been proposed.

L. Know Your Customer and Anti-Money Laundering Requirements for Federal Covered Advisors

On February 15, 2024, the United States Treasury's Financial Crimes Network ("FinCEN") issued a proposed rule which would designate certain investment advisers as "financial institutions" under the Bank Secrecy Act ("BSA") and subject them to anti-money laundering/countering the financing of terrorism ("AML/CFT") program requirements and Suspicious Activity Report ("SAR") filing obligations, as well as other BSA requirements ("AML/CFT Program and SAR Proposed Rule").[49] The AML/CFT Program and SAR Proposed Rule only applies to investment advisers registered or required to be registered with the Securities and Exchange Commission ("SEC") ("RIAs") and those exempt from registration under sections 203(l) or 203(m) of the Investment Advisers Act of 1940 (ERAs). On August 28, 2024, FinCEN issued its final rule which will become effective on January 1, 2026.[50]

Notably, the final rule adopts a narrower definition of "investment adviser" than initially proposed, and excludes from the definition: (A) RIAs that register with the SEC solely because they are (i) mid-sized advisers, (ii) multi-state advisers, or (iii) pension consultants; as well as (B) RIAs that are not required to report any AUM to the SEC on Form ADV.

On May 13, 2024, the SEC and FinCEN jointly proposed a rule that would require RIAs and ERAs to establish, document, and maintain written customer identification programs ("CIPs"). Under the proposed rule, RIAs and ERAs would be required to implement reasonable procedures to identify and verify the identity of their customers, among other requirements, in order to form a reasonable belief that RIAs and ERAs know the true identity of their customers.[51] This rule is not yet final.

---

[48] Notice of Request for Comment Regarding the uniform Securities Act Manual Exemption, pg. 4 (April 26, 2023), available at https://www.nasaa.org/wp-content/uploads/2023/04/NASAA-Request-for-Comment-on-Potential-Revisions-to-the-Manual-Exemption-4-26-2023.pdf.

[49] *See* FinCEN, Anti-Money Laundering/Countering the Financing of Terrorism Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers and Exempt Reporting Advisers, Notice of Proposed Rulemaking, 89 FR 12108 (Feb. 15, 2024).

[50] *See* FinCEN, Anti-Money Laundering/Countering the Financing of Terrorism Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers and Exempt Reporting Advisers, Final Rule, 89 FR 72156 (September 4, 2024).

[51] *See* FinCEN & SEC, Customer Identification Programs for Registered Investment Advisers and Exempt, Notice of Proposed Rulemaking, 89 FR 44571 (May 21, 2024).

The Office should continue to monitor developments in this area and determine whether state registered investment advisers should also be required to have some form of anti-money laundering program or customer identification program.

IV. Division of Financial Institutions

A. Updates to December 2022 Report

Investment Caps for Credit Unions. The deletion of s. 657.042(5), Florida Statutes, to achieve competitive equality with federal credit unions has been included in the 2025 Legislative Proposals.

B. Special Purpose Charters

Over the past several years, so-called "special purpose charters," i.e., bank charters authorizing only limited financial services, have become an increasingly popular topic of conversation within the regulatory community. Between the unbundling of financial services and the rise of fintech companies whose businesses do not fall cleanly within the traditional model, several states and the federal government have been contemplating developing special purpose charters to effectively enable and regulate these businesses. These special purpose charters do not accept deposits and are therefore not insured by the FDIC or otherwise. The Office should contemplate (1) whether special purpose charters have a place in Florida, (2) what activities would be considered permissible under the special purpose charters, and (3) whether such charters are due reciprocity under the financial institutions codes.

1. Federal Charters

In 2016, the Office of the Comptroller of the Currency (OCC) published a white paper that interpreted the National Bank Act's powers provision, 12 U.S.C. § 24 (Seventh), broadly to authorize the OCC to issue a special purpose charter for fintech companies.[52] In 2018, the OCC followed the white paper with a policy statement indicating that the agency would consider applications from fintech companies who were engaging in the business of banking, but not taking deposits, provided that they meet the existing requirements and standards for obtaining a charter.[53] There was significant backlash to the idea. The Conference of State Bank Supervisors initiated several lawsuits beginning in 2017,[54] alleging in various ways that the OCC lacked the authority to issue a special purpose charter and corresponding regulations, failed to follow rulemaking

---

[52] OCC, Exploring Special Purpose National Bank Charters for Fintech Companies (December 2016), available at: https://www.occ.gov/publications-and-resources/publications/banker-education/files/pub-special-purpose-nat-bank-charters-fintech.pdf.

[53] OCC, Policy Statement on Financial Technology Companies' Eligibility to Apply for National Bank Charters (July 31, 2018), available at: https://www.occ.gov/news-issuances/news-releases/2018/pub-other-occ-policy-statement-fintech.pdf. *See also*: 12 C.F.R. § 5.20(e), promulgated back in 2003, which OCC argued gave it the power to charter a special purpose bank that conducts at least one of three core banking functions: receiving deposits, paying checks, or lending money.

[54] *Conference of State Bank Supervisors v. Office of the Comptroller of the Currency*, 313 F. Supp. 3d 285 (D.D.C. 2018), *Conference. of State Bank Supervisors v. Office. of the Comptroller of the Currency*, No. 18-cv-2449 (DLF), 2019 WL 4194541 (D.D.C. Sept. 3, 2019).

procedures, and acted arbitrarily and capriciously. The cases were dismissed for lack of standing, failure to allege injury, and being unripe. In 2021, the Superintendent of the New York State Department of Financial Services (NYDFS) brought an APA action against the OCC challenging the OCC decision to begin accepting applications for, and potentially granting special purpose charters to, fintech companies. The Southern District of New York found in NYDFS's favor, and the OCC appealed. The Second Circuit reversed and remanded the case on bases similar to those in the CSBS cases: the alleged threat of federal preemption and regulatory harm was not concrete and imminent and thus insufficient to establish the injury in fact required for standing, and that the claims were unripe.[55] While the state of the law favors OCC's ability to grant special purpose charters, it has yet to issue any.

2. State Charters

In an effort to attract financial technology companies, **s**everal states have enacted legislation creating special purpose charters in recent years.

Wyoming created a "special purpose depository institution" (SPDI) which is intended to act like a fully reserved bank that receives deposits and conducts other activities incidental to the business of banking, but with a focus on digital assets.[56] SPDI banks were designed to provide a connection from crypto-asset companies to the U.S. payments system. A Wyoming SPDI, Custodia Bank, drew national attention in its bid to obtain a master account from the Federal reserve (see below). Wyoming supported the bank, and its SPDIs in general, when its Attorney General filed an amicus brief in federal district court, supporting the application.

Connecticut revived a dormant banking charter provision to attract fintech companies to the state. A law from the 1990s which allowed the issuance of uninsured bank charters, was rebranded as an "innovation bank charter" (IBC). Originally intended for institutions that wanted to offer some financial services but would not be taking federally insured deposits from the public, the charter is now being marketed as ideal for entities performing financial-related activities such as wholesale banking and merchant banking.[57]

Georgia recently received an application from one of the nation's largest non-bank merchants in an effort to be granted a charter as a "merchant acquirer limited purpose bank" (MALPB). This charter would allow the company to authorize, settle, and clear payments transactions for merchants as well as to enter card networks directly rather than through a bank sponsor. In doing so, a MALPB could own the transactions from end to end and eliminate various third-party risks.

Nebraska enacted the Financial Innovation Act in 2021. The law creates a bank charter dubbed "digital asset depository institution" for companies that hold cryptocurrencies. The new act defines "digital asset depository institutions" as banks or financial institutions that hold certain digital assets and will allow existing state-chartered banks to establish areas focused on cryptocurrency services. New businesses will also be able to gain a state banking charter as digital asset depositories.

---

[55] *Lacewell v. Office of the Comptroller of the Currency*, 999 F.3d 130 (2d Cir. 2021).

[56] Wyo. Stat. § 13-12-101, et seq. See also Wyoming Division of Banking, *Special Purpose Depository Institutions,* www.wyo.gov. https://wyomingbankingdivision.wyo.gov/banks-and-trust-companies/special-purpose-depository-institutions (last visited August 19, 2024). *See* https://wyomingbankingdivision.wyo.gov/banks-and-trust-companies/special-purpose-depository-institutions.

[57] https://portal.ct.gov/dob/financial-institutions-division/fid-applications/innovation-charter-application.

3. Master Accounts

Coveted master accounts provide access to Federal Reserve payment and settlement systems and allow banks to transfer money directly to other entities with master accounts, cutting out the need to use a third party for transactions. A state special purpose charter without a Federal Reserve master account may not be an attractive option for most special purpose banks and fintech companies. Therefore, the Fed's willingness to grant master accounts is important to the analysis.

In 2023, Wyoming's Custodia Bank was denied a master account by the Federal Reserve. The company sued in Federal District Court, but in March 2024 was ultimately unsuccessful in its bid to obtain the host of necessary services associated with a master account.[58]

In May 2024, notwithstanding the Federal Reserve's Custodia Bank denial and resulting court battle, a similarly situated Connecticut-based International Bank of Commerce (Numisma) was, in fact, granted a master account. The disparate treatment between the two level 3 banks drew commentary. and it is speculated that the Federal Reserve is under pressure to grant more master accounts to state special purpose banks.[59]

4. Possibilities for Florida

While we may be witnessing the beginning of a trend toward special purpose charters, as uninsured institutions they are not without risk of failure. Additionally, DFI shares the concerns of the Division of Securities with regard to regulation of digital assets and is mindful financial institutions may seek special purpose charters primarily to avoid regulation under securities laws. The Department would want to minimize risk of loss to consumers as well as the risk of receivership responsibilities in the event of a failure. Solutions to consider may be possible future federal insurance agreements and state licensing rather than charters to be able to maintain closer oversight.

C. Director Experience, Banks and Trust Companies

Section 658.21(4)(b), Florida Statutes, prescribes an experience requirement for certain proposed directors of a de novo bank or trust company. At least two of the proposed directors, who are not also proposed officers, must have had at least one year of experience as an executive director, regulator, or director of a financial institution within the 5 years before the date of the application (the "5 Year Requirement"). The 5 Year Requirement is not without exception; if at least one of the proposed directors has "very substantial" experience in those roles more than 5 years prior to the date of the application, the Office may still approve the application if the applicant has only one director with direct financial institution experience within the last 5 years. While the need for directors to have recent experience is valid, the 5 Year Requirement sets an arbitrary value on what is considered recent. Eliminating the 5 Year Requirement would give more freedom to de novo banks and trust companies by expanding the pool of qualified directors and allowing them to pick directors who best serve the needs of the institution.

---

[58] *Custodia Bank, Inc. v. Federal Reserve Board of Governors and Federal Reserve Bank of Kansas City,* 2024 WL 1788900 (D.Wyo. March 29, 2024).

[59] Gabrielle Saulsbery, *Small Bank Receives Rare Conditional Fed Master Account Approval,* BankingDive, May 24, 2024, https://www.bankingdive.com/news/small-bank-receives-rare-conditional-fed-master-account-numisma/717125/#:~:text=Numisma%20Bank%20has%20been%20granted,Fox%20Business%20and%20American%20Banker.

D. Lending Limits - State Backed Investments

Pursuant to s. 655.061, Florida Statutes, on September 22, 2023, the Office issued an order of general application (OGA), which authorized Florida state-chartered banks to make certain loans to the extent guaranteed or secured by a general obligation of a state or political subdivision, without regard to the legal lending limits prescribed by s. 655.48, Florida Statutes.[60] This OGA was ordered to ensure competitive equality between Florida's state charters and national banks, which are eligible to make such loans without regard to legal lending limits pursuant to 12 C.F.R. § 32.3(c)(5)(ii). While the OGA carries the weight of law, the Division of Financial Institutions suggests codifying this type of investment in s. 655.48, Florida Statutes, for clarity and convenience for the industry.

E. Compensation for Credit Union Directors

Pursuant to s. 657.028, Florida Statutes, a director of a credit union may not be compensated for his or her service as such.[61] Florida statutes are silent as to whether reimbursement for expenses and the payment of stipends or per diem fees are permissibly classified as non-compensation. The Division has been approached by at least one credit union, that may already be paying stipends to its board members, seeking guidance.

Approximately eighteen states allow direct compensation to be paid to credit union directors for services rendered: Arizona, Colorado, Georgia, Indiana, Kentucky, Maryland, Minnesota, Nevada, New Jersey, North Dakota, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Washington, Wisconsin, and Wyoming.[62] An additional twenty five states permit the reimbursement of necessary expenses: Alabama, California, Hawaii, Illinois, Kansas, Louisiana, Michigan, Montana, Nebraska, Nevada, New Mexico, North Carolina, Ohio, South Carolina, Texas, Vermont, Virginia, West Virginia, Arkansas, Idaho, Iowa, Massachusetts, New Hampshire, Utah, and Washington. Texas permits a per meeting fee to be paid to directors.

While federal law also prohibits compensation for directors, the National Credit Union Association (NCUA) has followed the trend of the majority of states by loosening payment restrictions, and permitting small gifts, reimbursement for training expenses; reimbursement for travel, meals, and accommodations; and reimbursement for computers, cell phones and internet to the extent used for official duties.[63]

In summary, Florida sits amongst the minority states, those primarily situated in the northeast United States, which does not expressly allow compensation, expense reimbursement, stipends, or fees to be paid to directors.[64] While some in the industry feel that paying credit union boards is anathema to the cooperative spirit of these institutions, others are concerned that Florida chartered

---

[60] *In Re: Loans Guaranteed or Secured by a General Obligation of a State or Political Subdivision*, 117950, 2023-211(OGA), September 22, 2023.

[61] Pursuant to s. 657.41(3), Florida Statutes, credit unions may pay the premiums for reasonable health, accident, and related types of insurance for members of the board of directors, credit committee, supervisory committee, or other volunteer committee established by the board, with the prior approval of members of a credit union and the Office.

[62] Kaufman & Canoles, *Credit Union Legal Update - Credit Union Board Compensation & In-Kind Gifts*, www.kaufcan.com, https://www.kaufcan.com/news/articles/credit-union-legal-update-credit-union-board-compensation-in-kind-gifts/ (last visited August 19, 2024).

[63] *See* NCUA's Letters to Credit Unions. (11-0152, 11-0805, 10-0919, 99-0621, 97-0305, 91-0215).

[64] Connecticut, Delaware, Maine, and New York do not permit for compensation, reimbursement or insurance.

credit unions face difficulties finding and retaining knowledgeable and capable individuals to serve as directors. Therefore, the Division is interested in exploring whether Florida law should be amended to help its credit unions attract directors by permitting compensation, or at least clarifying that reimbursement for necessary expenses and nominal stipends or fees are not to be considered as compensation.

V. Bureau of Financial Investigations

A. Aiding and Abetting Liability

Currently, there appears to be no tool found in chapter 517, Florida Statutes, which would specifically allow the Office to pursue an administrative enforcement action against individuals who aid or abet other securities violators. The only explicit mention of "aiding" is found in the private civil remedies provision, section 517.211(2), Florida Statutes. This provides for joint and several liability in rescission actions involving securities fraud or misstatement violations to be distributed between the violator and certain persons (e.g., officers, partners, agents of a violating securities purchaser or seller) who "aided" in the violation.

Meanwhile, section 517.191(1), Florida Statutes, allows the Office to pursue injunctive relief (and, potentially, civil penalties and restitution) in a circuit court against securities violators "and any other person concerned in or in any way participating in or about to participate in such practices or engaging therein or doing any act or acts in furtherance thereof or in violation of this chapter." Moreover, with the recent enactment of SB 532, section 517.191(6) now provides: "For purposes of any action brought by the [O]ffice under this section, a person who knowingly or recklessly provides substantial assistance to another person in violation of this chapter or any rule adopted thereunder is deemed to violate this chapter or the rule to the same extent as the person to whom such assistance is provided." However, this provision makes clear that this new "substantial assistance" liability only applies to a *civil* action brought by the Office under section 517.191, Florida Statutes, but would not apply to an *administrative* action pursuant to section 120.57(1) or (2), Florida Statutes.[65]

Accordingly, although the new addition above is useful in civil actions, there is still no enforcement tool available in chapter 517 which would enable the Office to bring an administrative action seeking to discipline an aider or abettor of a securities violation through, e.g., imposition of a cease-and-desist, administrative fine, or registration denial, suspension or revocation.

Examples of other chapters of Florida law regulated by the Office which currently include aiding and abetting provisions for administrative enforcement purposes include chapters 560, 494, and 559, Florida Statutes. Section 560.114(1)(s), Florida Statutes, extends aiding and abetting liability for *any violation* of the chapter. However, sections 494.00255(1)(i) and 559.730(1)(c), Florida Statutes, extend such liability only to aiding, abetting, or conspiring in violations involving "fraud,

---

[65] The new provision appears to borrow language from 15 U.S. Code § 78t(e), included in section 20(e) of the Securities Exchange Act of 1934 (as amended by the 1995 Private Securities Litigation Reform Act), which provides a mechanism, in S.E.C. civil enforcement actions seeking injunctive relief and disgorgement, for creating liability of controlling persons and persons who aid and abet certain federal securities violations (i.e., "any person that knowingly or recklessly provides substantial assistance to another person in violation of a provision of this chapter, or of any rule or regulation issued under this chapter").

misrepresentation, concealment, or dishonest dealing by trick, scheme, or device; culpable negligence; breach of trust in any business transaction in any state, nation, or territory." In the context of securities violations under chapter 517, the Office may not want to limit liability purely to cases of fraud, misrepresentation, concealment, or deceit (i.e., violations of section 517.301, Florida Statutes). For instance, in clear cases of unregistered activity where suspected fraud is not chargeable due to evidentiary weaknesses, it might be useful to be able to proceed nonetheless against all involved parties. Thus, chapter 560's open-ended provision appears to be preferable in providing the Office with the most flexibility.

Also consider section 604(a) of the Uniform Securities Act of 2002, which provides for administrative enforcement actions by state regulators seeking a cease-and-desist order (or an order limiting or denying an exemption) against a securities violator or a "person [who] has, is, or is about to *materially aid* an act, practice, or course of business constituting a violation of this [Act] or a rule adopted or order issued under this [Act]." The use of "materially" here would seem to raise a regulator's burden of proof and could create more of a barrier to such enforcement actions.

In the criminal context, section 777.011, Florida Statutes, states that a person who "aids, abets, counsels, hires, or otherwise procures [a criminal offense] … [where] such offense is committed or is attempted to be committed [is a] principal in the first degree [who, just like the principal offender,] may be charged, convicted, and punished as such, *whether he or she is or is not actually or constructively present at the commission of such offense*." The utility of this language may seem limited to the criminal context, where guilt must be proven beyond a reasonable doubt, thus making presence during commission of an offense an otherwise critical element unless removed by statute, as here. However, considering the nature of many securities fraud cases brought under chapter 517 (e.g., where a sales agent may be actively offering or selling the securities to an investor by way of fraud or misrepresentation, at the direction of his employers who are typically located at a safe distance, far away from the violation), it could make sense to expressly remove the "presence" obstacle from the Office's burden of proof in an aiding or abetting provision under this chapter.

Therefore, the Office may consider seeking to close this apparent gap in chapter 517 for the purposes of administrative enforcement actions. This may be achieved by adding a provision creating aiding and abetting liability that contains open-ended language similar to that found in section 560.114(1)(s), Florida Statutes, which provides for a range of disciplinary actions and penalties for violations involving "[a]iding, assisting, procuring, advising, or abetting any person in violating a provision of this chapter or any order or rule of the office or commission."

Alternatively, proposed language might include the "knowingly or recklessly" verbiage found in the new section 517.191(6), Florida Statutes, (similar to 15 U.S. Code § 78t(e)), since the express inclusion of recklessness would likely make it slightly easier for the Office to prove the generally required scienter element in administrative actions against aiders or abettors of securities violations. Finally, it is worth thinking about whether, given the unique modus operandi found in securities fraud cases discussed above (i.e., sales agents and their distant, yet culpable, employers), it may be prudent to *expressly exclude* a "presence" requirement from the provision, similar to section 777.011, Florida Statutes ("whether he or she is or is not actually or constructively present at the commission of such offense").

By seeking to amend chapter 517, Florida Statutes, with an aiding or abetting provision using some or all of the language above, the Office may be able to close this apparent gap in Florida securities law and gain a useful administrative enforcement tool which holds liable additional individuals or entities who are indirectly responsible for securities violations against Florida investors.

B. Control Person Liability

The Office should consider amending chapter 517, Florida Statutes, to specifically define a "control person" and add a provision that provides greater liability in administrative enforcement actions for control persons who engage in securities violations. Currently, under chapter 517, there appears to be no direct liability for control persons, even though parts of the statute clearly refer to the actions of control persons.

For example, section 517.111(1), Florida Statutes, provides that the Office may revoke or suspend the registration of any security, or may deny any application to register securities, if its issuer, or the issuer's control person or officer has committed any of the violations in subsections (b) through (g). However, this subsection only applies to registration of securities (i.e., it does not make a control person liable, for instance). Further, there is no definition of "control person" in this section, or in the general definitions located in section 517.021, Florida Statutes. The closest we get is a definition of "control person" located in section 517.12(21)(a)2., Florida Statutes,[66] which makes clear that this definition only applies "[a]s used in this subsection."

Progress has been made in this area with the recent enactment of SB 532, as newly added section 517.191(5), Florida Statutes, now provides for control person liability in the Office's *civil* actions, stating: "For purposes of any action brought by the [O]ffice under this section, a control person who controls any person found to have violated this chapter or any rule adopted thereunder is jointly and severally liable with, and to the same extent as, the controlled person in any action brought by the [O]ffice under this section unless the control person can establish by a preponderance of the evidence that he or she acted in good faith and did not directly or indirectly induce the act that constitutes the violation or cause of action." However, this provision makes clear that this new "control person" liability only applies to a *civil* action brought by the Office under section 517.191, Florida Statutes, but would not apply to the Office's *administrative* action brought under either section 120.57(1) or (2), Florida Statutes.

The Uniform Law Commission's "2002 Act" has a specific provision for control person liability which the Office might consider adopting. The applicable provision is as follows:

---

[66] Section 517.12(21)(a)2., Florida Statutes, defines a "control person" as an individual or entity that possesses the power, directly or indirectly, to direct the management or policies of a company through ownership of securities, by contract, or otherwise. A person is presumed to be a control person of a company if, with respect to a particular company, the person:
a. Is a director, a general partner, a member, or a manager of a limited liability company, or is an officer who exercises executive responsibility or has a similar status or function;
b. Has the power to vote 20 percent or more of a class of voting securities or has the power to sell or direct the sale of 20 percent or more of a class of voting securities; or
c. In the case of a partnership or limited liability company, may receive upon dissolution, or has contributed, 20 percent or more of the capital.

(h) [Control person liability.] A person that controls, directly or indirectly, a person not in compliance with this section may be disciplined by order of the administrator under subsections (a) through (c) to the same extent as the noncomplying person, unless the controlling person did not know, and in the exercise of reasonable care could not have known, of the existence of conduct that is a ground for discipline under this section.

Even if the 2002 Act is not adopted, the Office might alternatively consider moving the "control person" definition currently located in section 517.12(21)(a)2., Florida Statutes, to section 517.021(6), Florida Statutes, which is the general definitional section of the chapter.

The new section 517.021(6), Florida Statutes, would therefore read as follows:

"Control person" means an individual or entity that possesses the power, directly or indirectly, to direct the management or policies of a company through ownership of securities, by contract, or otherwise. A person is presumed to be a control person of a company if, with respect to a particular company, the person:

a. Is a director, a general partner, a member, or a manager of a limited liability company, or is an officer who exercises executive responsibility or has a similar status or function;

b. Has the power to vote 20 percent or more of a class of voting securities or has the power to sell or direct the sale of 20 percent or more of a class of voting securities; or

c. In the case of a partnership or limited liability company, may receive upon dissolution, or has contributed, 20 percent or more of the capital.

This proposed amendment would bring greater clarity to the definition of control person, as it would apply consistently throughout chapter 517. Currently, the only definition of "control person" found in the chapter applies only to section 517.12, Florida Statutes, even though the term appears in several other sections of chapter 517, Florida Statutes.[67] The Office could also consider whether control person liability, for the purposes of an administrative enforcement action, should be added elsewhere in chapter 517 (i.e., in its various prohibitional sections, e.g., section 517.12, Florida Statutes, for unregistered activity, or section 517.301, Florida Statutes, for fraud or material misrepresentation).[68]

Thus, the Office should consider amending chapter 517, Florida Statutes, to add provisions defining a control person and establishing the liability of control persons who commit violations of chapter 517, Florida Statutes, for the purposes of an administrative enforcement action.

C. Virtual Currency Kiosks: Striking a Balance Between Consumer Protection and Limited Regulation

A virtual currency kiosk (e.g., "Bitcoin ATM") is a machine that allows consumers to

[67] §§ 517.0611, 517.111, Fla. Stat
[68] Of course, liability for fraud or misrepresentation under section 517.301, Florida Statutes, may be assigned to any "person," including a control person of a dealer, adviser, or issuer. However, it may be advisable to have a separate provision that clarifies a control person's liability where, say, an adviser engages in fraud.

exchange fiat currency for virtual currency, or vice versa.[69] In Florida, these kiosks have quickly become ubiquitous. While there are 26 known providers of virtual currency kiosks around the state, only nine are licensed as money transmitters; eight providers have either terminated their license or withdrawn applications, and nine others are unlicensed.[70] Importantly, providers of virtual currency kiosks who conduct *only* "peer-to-peer" (two-party) transactions with a consumer are not required to be licensed as money transmitters under chapter 560, Florida Statutes. As such, the Office lacks authority to regulate these kiosk providers unless they are transmitting funds as intermediaries (i.e., *three-party* transactions). However, many kiosks are set up with woefully inadequate consumer protections. As a result, virtual currency kiosks are a useful tool of fraudsters and scammers whereby unsuspecting consumers get lured into sending funds to unknown wallets.[71]

One approach to prevention of kiosk-related crypto fraud has been consumer notifications. For instance, the United States Secret Service's Cyber Task Force has successfully posted warning signs in and around hundreds of kiosks at stores in Central Florida, notifying consumers of potential red flags for fraud and other scams.[72] But perhaps it should be the kiosk operators themselves who are legally required to post consumer disclosures, even when they are not engaging in money transmission activity that requires a license. One legislative approach might consider attempting to strike a balance between valid consumer concerns and encouragement of new financial technology and industry. Through a common-sense legislative solution, therefore, the Office could play an important role in supervising such operators' compliance with limited consumer disclosure requirements.

The transmission of virtual currency was not explicitly regulated under chapter 560, Florida Statutes, until the enactment of CS/HB 273 in 2022. That bill not only created a statutory definition for "virtual currency" but also clarified (through a modified definition of "money transmitter") that a license is not required for peer-to-peer transactions unless an "intermediary" is involved (i.e., a three-party transaction).[73] Even before that amendment, providers of virtual currency kiosks had already been operating in Florida as licensed money services businesses (MSBs) authorized to conduct money transmission.[74]

The Federal Bureau of Investigation (FBI) and the Federal Trade Commission (FTC) have received complaints from Florida of alleged victim losses totaling between $16 and $21 million from

---

[69] National Association of Attorneys General, Y*our Bitcoin on Every Block: An Introduction to Cryptocurrency Kiosks*, May 4, 2022, available at: https://www.naag.org/attorney-general-journal/your-bitcoin-on-every-block-an-introduction-to-cryptocurrency-kiosks/ (last visited Aug. 7, 2024)

[70] Florida Office of Financial Regulation. (2024). *Regulatory Enforcement and Licensing System (REAL).*

[71] See, e.g.: https://www.cbsnews.com/news/crypto-atm-scams-unregulated-machines/;
https://dfi.wa.gov/consumer/alerts/bitcoin-atms;
https://www.fincen.gov/sites/default/files/shared/FinCEN_Alert_Pig_Butchering_FINAL_508c.pdf;
https://portal.ct.gov/-/media/dob/consumer/joint-consumer-alert---virtual-currency-kiosk.pdf;
https://www.aarp.org/money/scams-fraud/info-2019/cryptocurrency.html?cmp=KNC-DSO-FRAUD-Fraud-CryptocurrencyScams-NonBrand-Phrase-47477-Bing-CryptocurrencyFraud-Phrase-NonBrand&gclid=f3f7f0c07051195d59b69674152721b4&gclsrc=3p.ds&msclkid=f3f7f0c07051195d59b69674152721b4&utm_source=bing&utm_medium=cpc&utm_campaign=Fraud-CryptocurrencyScams-NonBrand-Phrase&utm_term=virtual%20currency%20scams&utm_content=Cryptocurrency%20Fraud

[72] https://www.clickorlando.com/getting-results/2023/11/30/us-secret-service-launches-central-florida-bitcoin-atm-warning-campaign/.

[73] https://www.flsenate.gov/Session/Bill/2022/273/Analyses/h0273c.COM.PDF

[74] Florida Office of Financial Regulation. (2024). *Regulatory Enforcement and Licensing System.* [Database]. Retrieved from https://flofr.gov/sitePages/verifyalicense.htm.

January 2020 to March 2024.[75] Since April 2023, the Office has opened approximately 40 investigations relating to virtual currency kiosk losses.[76]

1. Some Virtual Currency Kiosk Operators Require a Money Transmitter License

It's important to understand when a Florida money transmission license is required to operate virtual currency kiosks and when it is not. The exception to licensure only applies if the kiosk operator does not act as an intermediary. For instance, an operator must always have the requisite "inventory" of virtual currency prior to receiving the funds of a consumer who places an order through a kiosk. By contrast, an operator who immediately accepts the consumer's funds while lacking the inventory to complete the order, subsequently purchasing additional inventory from a third-party exchange so the consumer's order can later be completed (say, a day after the consumer uses the kiosk) acts as an "intermediary" in money transmission and therefore must be licensed with the Office.[77]

Additionally, a money transmitter license is also required for virtual currency kiosk operators who take custody of consumer funds by, e.g., providing virtual wallets for customers to store and transmit their funds to other wallet addresses. Where a kiosk operator holds the private keys to a customer's wallet and may "unilaterally execute or indefinitely prevent" a customer's transaction (e.g., sending bitcoin from the kiosk operator-hosted wallet to some other wallet), the operator acts as an "intermediary" and must therefore be licensed with the Office.

2. CS/SB 662 and HB 911: A Regulatory Framework for Virtual Currency Kiosk Businesses

In the 2024 Legislative Session, Sen. Colleen Burton and Rep. Kevin Steele filed bills to create a regulatory framework for virtual currency kiosk businesses. The legislative intent of the bills was to reduce unlawful and fraudulent activities. The bill would have provided protections for user of the kiosks by requiring such businesses to register with the Office, requiring certain disclosures, restricting the name under which such business may transact, and providing penalties for specified violations.[78]

The bill would have required kiosk operators to disclose to consumers the risks and potential pitfalls of using the kiosks to send funds. It would have also required a confirmation page requiring users to confirm they were using the kiosk explicitly to send virtual currency to their own wallet and not someone else's wallet. This disclosure requirement would not apply to virtual currency kiosk operators that are licensed MSBs and already under the Office's supervision. Additionally, the bill would have also required the use of blockchain analytics software to monitor transactions and block

---

[75] Email from Jason Holloway, Director of Fintech Policy, OFR, to Jacqueline Moody, Florida Senate Committee on Banking and Insurance, Senior Attorney, Fwd: Kiosk Data, (Jan. 17, 2024) (on file with Senate Committee on Banking and Insurance) (noting that, from January 2020 to the present, the FBI and the FTC reports for losses from Bitcoin and Crypto ATMs total approximately $16 and $5.8 million, respectively; if an alleged victim reported losses to both the FBI and the FTC then the data could be duplicative so the range of loss reported from both agencies is between $16 and $21 million).

[76] *Id.*

[77] https://flofr.gov/sitePages/MoneyTransmitters.htm.

[78] https://www.flsenate.gov/Session/Bill/2024/662/Analyses/2024s00662.aeg.PDF.

transactions to addresses known to be linked to illicit activity.[79]

CS/SB 662 and HB 911 did not pass the Florida Legislature in the 2024 Legislative Session. Had the legislation passed, it likely would have had a de minimis fiscal impact on the Office and could have been implemented without an additional budget allotment.[80]

Industry participants, including Coinflip, Athena Bitcoin, Bitcoin Depot and Genesis Coin, have all expressed interest in continuing to work on a bill for the upcoming 2025 legislative session.

D. Sworn Statements and Subpoena Language Under 517.201, Florida Statutes

The Office should consider amending section 517.201, Florida Statutes, which authorizes the Office to make investigations and examinations, to require or permit a person to make a sworn statement, and to issue and serve subpoenas. There are two problems with section 517.201: (1) there are no enforcement mechanisms nor penalties for failure to make a sworn statement; and (2) the subpoena language does not give the Office enough flexibility to assist other states in investigations.

First, the provision regarding sworn statements[81] seems to be substantially similar to the provisions in other statutes.[82] However, none of these comparable statutes have specific enforcement mechanisms. Sworn statements are useful when litigating cases, such as to refresh a witness's recollection,[83] and when the refusal to make a sworn statement could result in negative inferences.

At a minimum, the Office should consider adding language that failure to make a sworn statement as required within 30 days creates a rebuttable presumption that the person has failed to comply with the Office's investigation. Additionally, the Office should consider amending the statute to enable the Office to compel an individual to respond the Officer's sworn demand for a sworn written statement, to the same degree the statute enables the Office to seek to compel compliance with a subpoena.

Second, the Office should consider adding language that gives the Office the power to assist other States in securities investigations. For example, Arizona law grants the Arizona Corporation Commission the authority to (1) issue and enforce subpoenas in Arizona at the request of an agency or administrator of another state; and, (2) order financial institutions to not disclose the content or existence of a subpoena to individuals not affiliated with the financial institution.[84]

As another example, New Mexico authorizes its Director of the Securities Division of the Regulation and Licensing Department to aid a securities regulator of another state to determine if a person has, is, or is about to violate a law or rule of the other state.[85]

Accordingly, the Office should consider adding language to section 517.201, Florida Statutes, that gives the Office the flexibility to assist other states in investigations. Specifically, such language

[79] *Id.*
[80] *Id.*
[81] § 517.201(1)(b), Fla. Stat.
[82] *See* §§ 17.05, 559.726, & 718.501, Fla. Stat.
[83] § 90.803, Fla. Stat.
[84] § 44-1823(B) & (C), A.R.S. (2021).
[85] § 58-13C-602, N.M. Stat. (2017).

should combine the Arizona and New Mexico provisions, in a way that gives the Office the option to (1) enforce an out-of-state subpoena; (2) issue its own subpoena to assist an out-of-state regulator's investigation; and (3) issue a non-disclosure order to banks in connection with such subpoenas. Such language could read as follows:

> The Office may, at the request of a securities agency or administration of another state:
>
> (1) Issue and enforce a subpoena from another state in Florida if the activities constituting an alleged violation for which the information is sought would be a violation of this chapter if the activities had occurred in Florida; and,
>
> (2) Provide other assistance if the requesting regulator demonstrates that it is conducting an investigation to determine whether a person has violated, is violating, or is about to violate a law or rule of the other state relating to securities matters administered or enforced by the requesting securities agency or administration. The office may provide such assistance by using the authority to investigate and the powers conferred by this section as it determines is necessary or appropriate. The assistance may be provided without regard to whether the conduct described in the request would also constitute a violation of the Florida Securities and Investor Protection Act or other law of Florida if occurring in Florida. In deciding whether to provide the assistance, the office may consider whether the requesting regulator is permitted and has agreed to provide assistance reciprocally within its state or foreign jurisdiction to the office on securities matters when requested; whether compliance with the request would violate or prejudice the public policy of Florida; and the availability of resources and employees of the director to carry out the request for assistance.
>
> (3) Issue a non-disclosure order to a bank in connection with a subpoena issued by the Office seeking the bank customer's records in an investigation by the Office or in connection with related subpoena efforts.

E. <u>Enhancing Penalties When Older Victims and Other Specified Groups Are Targeted</u>

The Office recognizes that the victimization of the elderly, veterans, and other uniquely situated investor groups through fraudulent and deceptive practices in the securities industry is a serious and ongoing issue in Florida. However, in a securities fraud involving large groups of victims with increased vulnerability, such as a Ponzi scheme, there is no provision currently found in chapter 517, Florida Statutes, which adequately enhances criminal penalties to deter this commonly found recurring aggravating circumstance found in such egregious cases.

The only provision addressing the elderly currently found in chapter 517 is section 517.191(4), Florida Statutes, which addresses enhanced civil penalties for securities violations involving "specified adults" (i.e., persons who are at least 65 years old or other "vulnerable adults" as defined by section 415.102(28), Florida Statutes). While this provision may be useful in certain kinds of civil actions brought under that section, it does not apply in criminal cases.

Section 517.302, Florida Statutes, is the only provision in the chapter which addresses criminal violations of securities fraud involving larger groups of victims, such as a boiler room operation or a Ponzi scheme. Such a case, involving at least five victims and $50,000 in investment funds, is a first-degree felony that carries limited enhancements in penalties that may not be substantial enough to provide an adequate punishment or deterrence effect.

However, the White-Collar Crime Victim Protection Act ("WCCVPA") contained in section 775.0844, Florida Statutes, seeks to protect the elderly, veterans, and groups of 20 victims or more, against nonviolent frauds and swindles by enhancing criminal penalties for certain felony offenses, including those classified as "white collar crime" involving violations specified in eleven (11) in eleven enumerated chapters of Florida statutes, such as chapter 560, Florida Statutes (which governs money services businesses, including money transmitters and check cashers). Such a white collar crime, when "aggravated" circumstances are present (as defined in subsection (4)), is a first- degree felony carrying significantly enhanced penalties, including "a fine of $500,000 or double the value of the pecuniary gain or loss, whichever is greater," as well as restitution. It is unclear why chapter 517, Florida Statutes, which governs the securities industry in Florida, is not currently listed among these 11 enumerated chapters in section 775.0844(3), Florida Statutes. Consequently, section 775.0844(5), pertaining to "aggravated white-collar crime" that victimizes 10 or more elderly persons or veterans, or 20 or more persons generally, does not reach criminal cases involving large scale securities fraud with voluminous victims, such as a major Ponzi scheme. As such, a prosecutor would not be able to charge a securities fraud defendant under the WCCVPA with aggravated white-collar crime involving a large group of vulnerable victims, including the elderly and veterans. This unfortunate oversight prevents a Florida prosecutor, likewise, from seeking to recover the significantly enhanced penalties available in this section.

To help remedy this apparent oversight and provide an additional tool in protecting larger groups of investors who may be elderly, vulnerable, veterans, etc., the Office should consider seeking to amend both (1) section 775.0844(3)(a), Florida Statutes (i.e., the WCCVPA) and (2) section 517.302, Florida Statutes.

An amendment to the WCCVPA, section 775.0844(3)(a), Florida Statutes, would merely require the insertion of the following verbiage above the current subsection (3)(a)1.: "Chapter 517, relating to fraudulent or deceptive practices in the securities industry." This simple addition would then include chapter 517 as an enumerated chapter covered by the WCCVPA, and a prosecutor could utilize that section to bring aggravated white collar criminal charges against a securities fraud violator with a large group of victims, including the elderly, veterans, and others. Such a defendant would then face the significantly enhanced criminal penalties permitted by the WCCVPA.

Additionally, section 517.302, Florida Statutes, which governs criminal penalties for securities violations under chapter 517, would also be amended by including a new subsection after subsection (2) (i.e., enhanced penalties for securities fraud violations involving 5 or more people). This new subsection could look similar to subsection (2), reading: "Any person who violates the provisions of s. 517.301 by obtaining or attempting to obtain money or property of an aggregate value exceeding $50,000 from ten or more elderly persons, as defined in s. 825.101, or veterans, as defined in s. 1.01, or twenty or more persons, as defined in s. 1.01, is guilty of a felony of the first degree, punishable as provided in s. 775.082, s. 775.083, or s. 775.0844." This proposed language, borrowed from the WCCVPA found in section 775.0844(5)(a) through (c), Florida Statutes, would provide a clear link between chapter 517 and the WCCVPA.

These two proposed interconnected amendments to Florida law would make it perfectly clear that chapter 517 violators who use fraudulent or deceptive practices to target groups of the elderly, veterans, and groups of 20 or more victims will be subject to significantly enhanced criminal penalties under the WCCVPA.

F. <u>Simplify and Broaden Chapter 655, Florida Statutes, Subpoena Authorization Language</u>

Chapter 655, Florida Statutes, provides general rules for financial institutions. The provision at issue is section 655.032(2)(a), Florida Statutes, which authorizes the Office to administer oaths and affirmations, take testimony and depositions, and issue and serve subpoenas. The problem with this provision is that it is unnecessarily complex, narrow, and does not align with similar provisions in other chapters. Accordingly, the Office should consider amending section 655.032(2)(a), Florida Statutes, to (1) simplify and broaden chapter 655's subpoena, oaths and affirmation, and testimony and depositions authority; and (2) conform its language with that of other similar statutes.

Section 655.032(2)(a), Florida Statutes, reads as follows:

(2)(a) In the course of or in connection with an investigation by the office pursuant to the provisions of subsection (1) or an investigation or examination in connection with any application to the office for the organization or establishment of a state financial institution or a branch thereof, and in connection with an examination of a state financial institution, subsidiary, or service corporation by the office, the office, or any of its officers holding no lesser title and position than examiner in charge or attorney at law, shall have the power:

1. To administer oaths and affirmations;

2. To take or cause to be taken testimony and depositions; and

3. *To issue, revoke, quash, or modify subpoenas and subpoenas duces tecum under the seal of the office* or to cause any such subpoena or subpoena duces tecum to be issued by any county court judge or clerk of the circuit court or county court to require persons to be or appear before the office at a time and place to be therein named and to bring such books, records, and documents for inspection as may be therein designated. Such subpoenas may be served by a representative of the office or may be served as otherwise provided for by law for the service of subpoenas.

Currently, 655 is bulky and causes problems for BFI, while other statutes do not. For example, chapters 517[86] and 687[87] have the following subpoena authorization language, "[s]ubpoenas for witnesses whose evidence is deemed material to *any investigation or examination may be issued by the office under the seal of the office*[.]" Additionally, chapters 494[88] and 520[89] begin their authorization language with "The office may [] [i]ssue and serve subpoenas."

The language from these statutes is simple and broadly authorizes "the office" to issue subpoenas. This broad authorization appears to permit the Commissioner to delegate the power to issue subpoenas to any employee of the Office rather than "officers holding no lesser title and position than examiner in charge or attorney at law[.]"[90] Additionally, the broad authorization applies

[86] § 517.201(3), Fla. Stat.
[87] § 687.144(3), Fla. Stat.
[88] § 494.00135(1)(a), Fla. Stat.
[89] § 520.994(1), Fla. Stat.
[90] § 655.032(2)(a), Fla. Stat.

to "any investigation or examination," rather than the current longwinded authorization.[91]

Accordingly, a proposed amended version of section 655.032(2)(a), Florida Statutes, could read as:

(2)(a) In connection with any investigation or examination pertaining to this chapter, the Office or its representatives may:

1. Issue, serve, revoke, quash, and modify subpoenas and subpoenas duces tecum to compel the attendance of witnesses and the production of all books, accounts, records, and other documents and materials relevant to an examination or investigation conducted by the Office;

2. Administer oaths and affirmations; and

3. Take or cause to be taken testimony and depositions.

This proposed amendment is simpler than the current 655 section,[92] and it broadly authorizes its powers to the office. This gives the Commissioner broad authority to delegate the power of issuing subpoenas, administering oaths and affirmations, and taking testimony and depositions, to a wider variety of Office staff. Additionally, the proposed amendment is in conformance with other statutes which creates harmony within Florida law.

In sum, the Office should consider adopting an amendment to section 655.032(2)(a), Florida Statutes. Such an amendment, like the proposed amendment above, should (1) simplify and broaden chapter 655's subpoena authority; and (2) conform its language with other similar statutes.

G. **Chapter 687, Florida Statutes, Trust Fund**

Section 687.143, Florida Statutes, states that all fines collected pursuant to this chapter shall be deposited into the Bureau of Financial Investigations Administrative Trust Fund. However, given the small volume of fines collected,[93] all of these funds have been maintained in the general administrative regulatory trust fund, and have been classified under Revenue Source Code 697, to delineate that the funds were collected pursuant to chapter 687, Florida Statutes.

For background, this section of the statutes was last amended in 2003 to reflect the name change of the Bureau of Financial Investigations (prior thereto known as the "Division of Financial Investigations"). The substantive change occurred in 1997, when the language was changed from the "Finance Regulatory Trust Fund" to the "Financial Investigations Administrative Trust Fund." Prior to 1997, all funds collected were to be deposited under the Division of Finance Regulatory Trust Fund, which is still in place to this day.

---

[91] § 655.032(2)(a), Fla. Stat. ("In the course of or in connection with an investigation by the office pursuant to the provisions of subsection (1) or an investigation or examination in connection with any application to the office for the organization or establishment of a state financial institution or a branch thereof, and in connection with an examination of a state financial institution, subsidiary, or service corporation by the office").

[92] § 655.032(2)(a), Fla. Stat.

[93] Since 2014, only 5 fines have been collected totaling $40,000, and no fines have been collected since 2017.

The Office may want to consider amending this language to reflect the actual ongoing practice.

VI. Legal Case Highlights

A. *SEC v. Jarkesy*, 603 U.S. ___ (2024)

In June 2024, the U.S. Supreme Court held in *SEC v. Jarkesy,* 603 U. S. ____ (2024) that defendants facing administrative civil penalties in a securities fraud case are guaranteed the right to a jury trial under the Seventh Amendment. Experts contend that *Jarkesy* will create a race to the courthouse and a flood of litigation that threatens to change the way enforcement cases are brought against defendants by federal agencies, which may be problematic. Although some agencies like the Securities and Exchange Commission ("SEC") have statutory discretion in choosing whether to seek civil penalties in district court or via in-house administrative proceedings, others (like OSHA) may only bring such enforcement cases through in-house administrative proceedings. In her *Jarkesy* dissent, Justice Sotomayor remarked that "the Constitutionality of hundreds of statutes may now be in peril, and dozens of agencies could be stripped of their power to enforce laws enacted by Congress." Some experts have also suggested that state agencies' in-house administrative proceedings could face constitutional challenges as well.

1. What happened in *Jarkesy*?

Following an investigation dating back in 2011, the SEC filed an administrative complaint against Jarkesy, an investment adviser, and his hedge fund, known as Patriot28. The complaint alleged violations of antifraud provisions of the federal securities laws and sought civil penalties. Using discretionary authority delegated by Congress under the Dodd-Frank Act, the SEC opted to adjudicate Jarkesy's matter before an Administrative Law Judge ("ALJ") rather than litigate a civil action in a federal district court. Following the ALJ's initial order, the SEC's final order imposed a $300,000 civil penalty, disgorgement, a bar, and other penalties against Jarkesy and his fund. Jarkesy successfully appealed to the Fifth Circuit, which vacated the SEC order after holding, among other things, that the SEC's unilateral decision to proceed with an agency hearing rather than a civil action unconstitutionally denied Jarkesy the right to a jury trial guaranteed by the Seventh Amendment.

The SEC appealed the case to the United States Supreme Court, which affirmed the Fifth Circuit in holding that a securities fraud action that seeks civil penalties triggers the defendant's constitutional right to a jury trial. That right applies to "[s]uits at common law," including statutory claims that are "legal in nature" (i.e., as opposed to an action *in equity*, which does not require a jury trial). The Court reasoned that a securities fraud claim is "legal in nature" because of its similarity to a common law fraud claim, which is traditionally heard by juries in a courtroom. The Court found the SEC may not shoehorn such a fraud claim against a defendant into an administrative hearing before an ALJ. Because the SEC's claim against Jarkesy 1) targeted misconduct that closely resembled *common law fraud*, a claim "legal in nature" and traditionally heard by juries and 2) was intended to punish and deter that misconduct, the Court held that the Seventh Amendment entitled Jarkesy to a jury trial.

The Court's current six-justice majority's disapproval towards administrative agencies was illustrated by *Jarkesy* and another opinion issued one day later, *Loper Bright Enterprises v. Raimondo*. In *Loper*, the Court overruled the forty-year-old *Chevron* doctrine, holding that because the Administrative Procedures Act requires courts to exercise independent judgment in deciding whether an agency has acted within its statutory authority, judges may not defer to an agency's interpretation of the law just because a statute is ambiguous. Between *Jarkesy* and *Loper*, and another case issued just before them, *Lucia v. SEC*, 585 U.S. 237 (2018),[94] The Supreme Court has armed litigants with viable tools for defending against agency enforcement actions by challenging the constitutional validity of the actions themselves, and by offering competing interpretations of ambiguous rules and regulations.

State litigants and defense counsel inspired by the judicial shift at the federal level are likely to "test the waters" in state courts with *Jarkesy* challenges to state agencies seeking civil penalties in administrative hearings. Since the OFR and other state agencies often have some discretion whether to file enforcement cases in a Florida circuit court or in an administrative proceeding presided over by an ALJ or a hearing officer, state agencies could very well face similar litigation challenges in the future.

2. *Jarkesy*'s Impact on State Agencies?

Jarkesy does not directly apply to state administrative agencies. The right to a civil jury trial under the Seventh Amendment has not been incorporated into the states. See *City of Monterey v. Del Monte Dunes at Monterey, Ltd.*, 526 U.S. 687 (1999); *Minneapolis & St. Louis Railroad Co. v. Bombolis* (1916). However, in certain types of cases nearly all states provide the right to a civil jury trial guaranteed in their state constitutions. For example, Art. I, s. 22 of the Florida constitution provides that "[t]he right of trial by jury shall be secure to all and remain inviolate." See also Fla. R. Civ. P. 1.430 ("The right of trial by jury as declared by the Constitution or by statute shall be preserved to the parties inviolate.").

Florida state courts have yet to rule on whether this constitutional right to a jury trial applies to administrative procedures in Florida. Many enforcement actions initiated by state agencies in Florida seek civil penalties either at the Division of Administrative Hearings in cases involving disputed issues of material fact pursuant to section 120.57(1), Florida Statutes, or through "informal" proceedings before an agency hearing officer in cases not involving disputed issues of material fact pursuant to section 120.57(2), Florida Statutes. Because the reasoning and logic underlying the *Jarkesy* decision could arguably be similarly applied to state agencies, this system – and the Florida Administrative Procedures Act (chapter 120, Florida Statutes) that sets forth its infrastructure – would require legislative transformation if Florida courts, inspired by the United States Supreme Court's decision in *Jarkesy*, are persuaded that Florida's constitutional right to a jury trial has been violated by such administrative proceedings.

---

[94] *Lucia* held that the SEC's ALJs are considered inferior officers of the United States and so are subject to the Appointments Clause and must be appointed through the President or other delegated officer of the United States, rather than hired by the SEC.

Jarkesy has already had the effect of emboldening securities respondents in enforcement actions taken by some states and the Financial Industry Regulatory Authority ("FINRA") to petition courts to affirm their constitutional right to a jury trial in these cases. A recent enforcement case brought in an administrative proceeding by Arizona's securities regulator illustrates how respondents are jumping on the *Jarkesy* train. See *Peterson v. Arizona Corp. Comm'n*, 1 CA-CV 23-0253, 2024 WL 1167387, at *1 (App. Mar. 19, 2024). The respondent in *Peterson* filed a civil action on several grounds which included the argument that an ALJ cannot constitutionally adjudicate the matter because, under the Fifth Circuit's *Jarkesy* decision, he had a right to a jury trial. However, the respondent's argument was rejected by the state appellate court, which found that *Jarkesy* will not be binding for the interpretation of Arizona administrative procedures because the case only construes federal law in view of the Seventh Amendment right to a jury trial.[95]

In July 2024, FINRA was sued in a Pennsylvania federal district court by D. Allen Blankenship, a registered securities dealer seeking to enjoin a pending disciplinary hearing based in part on the recent *Jarkesy* holding, which he argued entitled him to a jury trial. See *Blankenship v. FINRA*, case number 2:24-cv-03003 (E.D., Pa.). Although FINRA's suitability claims against Blankenship concerning his mutual fund trading did not explicitly allege "securities fraud," Blankenship argued that it was "ultimately a case for common law fraud disguised under regulatory language" and that FINRA's case was "punitive" because it was seeking disgorgement and restitution with interest. Blankenship asserted that FINRA's case belongs in a jury trial, because both the claims and the remedies sought are "legal in nature" per *Jarkesy*. The district court dismissed Blankenship's Seventh Amendment claims for lack of subject matter jurisdiction without reaching the merits of his motion for an injunction.

###

[95]See *Review of SEC v. Jarkesy, and its impact on the Securities Industry*. www.robertdmitchell.com/ news/review-of-sec-v-jarkesy-and-its-impact-on-the-securities- industry.