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Florida's Response to the Need for Uniformity in Federal and State Securities Registration Exemption Requirements

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FLORIDA'S RESPONSE TO THE NEED FOR UNIFORMITY IN FEDERAL AND STATE SECURITIES REGISTRATION EXEMPTION REQUIREMENTS

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I. INTRODUCTION

The federal Securities Act of 1933[1] mandates that all securities sold or offered for sale in interstate commerce or through the mails must be registered with the Securities Exchange Commission (the Commission).[2] However, expenses associated with registration are often so excessive that many small issuers are deterred from even contemplating registration of their securities.[3] Instead, these smaller firms seek to qualify for an exemption from the federal registration requirement.[4]

Section 4(2) of the Securities Act grants an exemption if the transaction in question does not involve any "public offering."[5] As a general rule, this means that there is a limited number of offerees and purchasers.[6] This category of securities offerings is known as a "private placement" or "private offering." Section 3(b) of the Securities Act does not create an exemption, but confers upon the Commission the authority to promulgate rules exempting issues of securities if it finds that, "by reason of the small amount involved or the limited character of the public offering," registration is "not necessary in the public interest and for the protection of investors."[7] The offerings made under the exemptions created pursuant to section 3(b) are referred to as "limited offerings."

The Commission has recently adopted a series of rules collectively referred to as Regulation D.[8] The purpose of these rules is to clarify the private placement exemption granted under section 4(2) of the Securities Act and to create limited offering exemptions as authorized by section 3(b). Regulation D represents an effort by

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1. 15 U.S.C. §§ 77a-77aa (1982) (hereinafter "Securities Act").
2. Securities Act § 5, 15 U.S.C. § 77e (1982).
3. *See generally* Mofsky, *Reform of the Florida Securities Law*, 2 FLA. ST. U.L. REV. 1 (1974).
4. There are two basic methods of avoiding the registration requirements of § 5 of the Securities Act. The securities themselves may qualify for an exemption under § 3, 15 U.S.C. § 77c (1982), or the transactions may qualify for an exemption under § 4, 15 U.S.C. § 77d (1982). Some exemptions are created statutorily by the Securities Act, while others are created by administrative bodies acting pursuant to statutorily granted authority.
5. Securities Act § 4(2), 15 U.S.C. § 77d(2) (1982).
6. *But see* SEC v. Ralston Purina Co., 346 U.S. 119 (1953).
7. Securities Act § 3(b), 15 U.S.C. § 77c(g) (1982).
8. 17 C.F.R. §§ 230.501-.506 (1982).

the Commission to incorporate earlier private placement and limited offering exemptions for small businesses into a more coherent scheme.[9] The rules attempt to reduce the expense and burden of registration for small issuers while at the same time providing adequate protection for the investing public.

Once the issuer has determined that one of the federal transactional exemptions is available, there remain the state registration requirements of each state in which the securities will be sold. These so called "blue sky" requirements,[10] like their federal counterpart, are often onerous, expensive, and time-consuming.[11] Accordingly, issuers usually seek an exemption from the state registration requirements as well as from the federal requirements.

In many cases the state registration requirements differ from, or are incompatible with, Regulation D. Additionally, the state registration requirements often differ from, or are incompatible with, one another. This lack of uniformity between state and federal exemption requirements and among state requirements causes needless expense and imposes unwarranted burdens on issuers seeking to sell their securities. In turn this hampers capital formation, and its effect is greatest upon small businesses for whom the costs of registration or of compliance with multiple exemption requirements are proportionally greater and may be prohibitive.

Congress recognized the problems inherent in multiple registration requirements when it enacted the Small Business Investment Incentive Act of 1980, adding section 19(c) of the Securities Act which authorizes the Commission "to cooperate with any association composed of duly constituted representatives of State governments whose primary assignment is the regulation of securities business within those States" for purposes of "the development of a uniform exemption from registration for small issuers which can be agreed upon among several States or between the States and

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9. An Analysis of Regulation D, FED. SEC. L. REP. (CCH) ¶ 83,631, at 86,888 (May 1984) (citing Securities Act Release No. 33-6339 (Aug. 7, 1981)).

10. The term "blue sky" is attributed to a variety of origins. *See, e.g.*, Hall v. Geiger Jones Co., 242 U.S. 539, 550 (1931) ("speculative schemes which have no more basis than so many feet of 'blue sky' "); Mofsky, *supra* note 3, at 1 n.1 (citing L. Loss & E. COWETT, BLUE SKY LAW 7 n.22 (1958)) ("The term 'blue sky' was first used to describe the business practices of promoters and securities salesmen in Kansas at the turn of the century. The activities of these individuals, it was claimed, bordered on the 'sale of building lots in the blue sky in fee simple.' ").

11. *See generally* Royalty & Jones, *The Private Placement Exemption and the Blue Sky Laws—Shoals in the Safe Harbor*, 33 WASH. & LEE L. REV. 877 (1976); Note, *A Primer on Private Offerings*, 24 U. FLA. L. REV. 458 (1972). The Securities Act expressly provides in § 19(c)(3)(C) that the state laws are not preempted. 15 U.S.C. § 77s(c)(3)(C) (1982).

the Federal Government."[12] Pursuant to the authorization of section 19(c), the Commission cooperated with the North American Securities Administrators Association (NASAA), an organization composed of securities administrators from all states, the Canadian provinces, Mexico, the Commonwealth of Puerto Rico, and Guam, in the development of Regulation D.[13] Not only was Regulation D designed to provide a more coherent scheme of exemptions, but it was also created to serve as a basis for a uniform federal-state exemption.[14] At this time approximately twenty-eight states have adopted an exemption which coordinates to some extent with Regulation D.[15]

While Regulation D served to promote uniformity between state and federal exemption requirements, it only indirectly addressed the problem of uniformity among the states. However, in September 1983, just eighteen months after the Commission's adoption of Regulation D, NASAA endorsed a revised version of the Uniform Limited Offering Exemption (ULOE), an exemption scheme intended to coordinate with Regulation D and to serve as a basis for uniformity among the states.[16] In April 1984, the Commission and NASAA met and agreed to undertake several substantive and procedural initiatives whose goals are (1) the development of mechanisms to foster cooperation among federal and state securities regulators, and (2) the enhancement of uniform federal and state regulations. As part of that effort NASAA intends to urge states which have not yet done so to adopt a uniform limited offering exemption to coordinate with Regulation D, and to request states which have adopted such exemptions to conform them to the ULOE.[17] Even more recently, in May 1984, the Section of Corporation, Banking and Business Law of the American Bar Association issued a report to the House of Delegates in which it recommended the adoption in all states of a slightly modified version of the ULOE as endorsed by NASAA.[18]

The purpose of this comment is to examine the extent to which

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12. Securities Act § 19(c)(3)(C), 15 U.S.C. § 77s(c)(3)(C) (1982).

13. American Bar Association Section of Corporation, Banking and Business Law, Report to the House of Delegates 1-2 (May 1984) [hereinafter cited as Report].

14. An Analysis of Regulation D, *supra* note 9, at 86,887.

15. *Id.*

16. Securities and Exchange Commission and North American Securities Administrators Association Conference on Federal-State Securities Regulation, FED. SEC. L. REP. (CCH) ¶ 83,610, at 86,753 (Apr. 1984).

17. *Id.* at 86,754.

18. Report, *supra* note 13, at 1.

Florida has responded to the need for uniformity with the federal exemption requirements and to discuss the steps Florida should take in the future to more closely align its exemption scheme with that of Regulation D and of the ULOE. The following discussion is based on the premise that while uniformity is a desirable goal, it is one which should not be sought without due consideration for the needs and interests of investors as well as those of issuers.

II. The Federal Exemptions

Discussion of Florida's most appropriate response to the need for uniformity with federal registration exemption requirements necessarily begins with an analysis of the federal scheme. In the first place, a working knowledge of the federal exemptions is needed to provide a basis for comparison with the Florida requirements. Furthermore, there is an interplay between the federal and Florida registration requirements, as each must be satisfied, and the practical operation of the state exemption may only be determined with reference to the federal scheme. Moreover, an understanding of the federal exemption scheme's treatment of the competing needs of investors for protection and of issuers for efficient capital formation is helpful for purposes of determining, from a policy point of view, the extent to which Florida should align its exemption requirements with those of Regulation D and of the ULOE.

The primary purpose of the registration requirement of section 5 of the Securities Act is to ensure that complete disclosure of the business operations of the issuer is made to all offerees so that an informed investment decision can be made. This reflects an underlying assumption of the federal securities laws which holds that disclosure provides investor protection.[19] An issuer's failure to comply with the substantive and procedural conditions of the Securities Act may result in a purchaser's actions for damages or return of any consideration paid,[20] in an injunctive action by the Commission,[21] or, in specified circumstances, in criminal prosecution.[22]

When Congress drafted the Securities Act, however, it determined that certain transactions, because of their small offering

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19. *See* L. Loss, Fundamentals of Securities Regulation 7 (1983).
20. Securities Act § 12(1), 15 U.S.C. § 77*l* (1982).
21. *Id.* § 20, 15 U.S.C. § 77t(b).
22. *Id.* § 24, 15 U.S.C. § 77x.

amount or small number of purchasers, should not be subject to federal registration. Therefore, Congress established the private placement exemption of section 4(2) and at the same time granted the Commission authority under section 3(b) to exempt limited offerings. The underlying rationale expressed for these exemptions was that small businesses could not afford the burdensome transactional costs generally associated with complete registration.[23]

Section 4(2) initially proved to be so vague that its use was restricted as a practical matter. Uncertainty existed in the minds of issuers as to what constituted a "public offering," and the potential consequences of wrong judgment dissuaded many issuers from risking reliance upon the exemption. In 1935, however, the general counsel for the Commission issued a memorandum which emphasized the relevance of factors other than the number of offerees in determining whether an offering was public, but also suggested that under ordinary circumstances a twenty-five purchaser issue was probably not large enough to constitute a public offering.[24] This rule of thumb was widely relied upon until the 1953 case of *SEC v. Ralston Purina Co.*, in which the United States Supreme Court said that because the purpose of the Securities Act was "to protect investors by promoting full disclosure of information thought necessary to informed investment decisions,"[25] it naturally followed that "the exemption question turns on the knowledge of the offerees"[26] and on their need for the protections afforded by registration. *Ralston Purina* held that section 4(2) required that each *offeree*, and not just each purchaser, must have "access to the same kind of information that the act would make available in the form of a registration statement."[27]

The *Ralston Purina* decision effectively limited private placements to issues in which each offeree and purchaser had access to information comparable to that disclosed by registration, an op-

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23. *See* Note, *Regulation D: Coherent Exemptions for Small Businesses Under the Securities Act of 1933*, 24 WM. & MARY L. REV. 121, 123 n.20 (1982). *See also* SEC v. Ralston Purina Co., 346 U.S. 119, 122 (1953) (quoting H.R. REP. No. 85, 73d Cong., 1st Sess. 5 (1933)) (intent of the exemptions is to exempt offers and sales "where there is no practical need for the [Securities Act's] application or where the public benefits are too remote").

24. Coles, *Has Securities Law Regulation in the Private Capital Markets Become a Deterrent to Capital Growth: A Critical Review*, 58 MARQ. L. REV. 395, 435 (1975) (citing Securities Act Release No. 285, 11 Fed. Reg. 10,952 (1935)). In 1935, current § 4(2) was numbered § 4(1).

25. SEC v. Ralston Purina Co., 346 U.S. at 124.

26. *Id.* at 126-27.

27. *Id.* at 125. *See generally* Coles, *supra* note 24.

portunity to verify that information, and the knowledge and experience required to evaluate the merits and risks of the investment. Moreover, other judicial decisions involving interpretation of section 4(2) were viewed by many practitioners as tightening the eligibility requirements for private placement offerings even beyond the requirements of *Ralston Purina*.[28] As a result of these developments, issuers and commentators urged the Commission to promulgate "safe harbors,"[29] compliance with which would ensure compliance with section 4(2). Rule 146[30] was the first safe harbor provision and was the predecessor of Regulation D's safe harbor provision contained in Rule 506.

Section 3(b) also experienced growing pains as the Commission attempted to promulgate rules pursuant to its authority granted in that section. Originally the Securities Act limited application of section 3(b) to issues not exceeding $100,000. Since then, the cap has been repeatedly raised and is currently set at $5,000,000.[31]

At the time it approved section 3(b), the House committee commented that the Commission's power under that section to exempt

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28. *See* SEC v. Continental Tobacco Co., 463 F.2d 137 (5th Cir. 1972); Hill-York Corp. v. American Int'l Franchises, Inc., 448 F.2d 680 (5th Cir. 1971).

29. In securities law, a safe harbor is a rule which clarifies and defines a statute. It is nonexclusive in nature and permits the user the option of relying on the statutory exemption should compliance with the safe harbor be defective. L. Loss, *supra* note 19, at 375.

30. 17 C.F.R. § 230.146 (1982) (repealed 1982). See Schwartz, *Rule 146: The Private Offering Exemption—Historical Perspective and Analysis*, 35 Ohio St. L.J. 738 (1974), for a complete discussion of Rule 146. *See also* Carney, *The Perils of Rule 146*, 8 U. Tol. L. Rev. 343 (1977); Casey, *SEC Rules 144 and 146 Revisited*, 43 Brooklyn L. Rev. 571, 589 (1977).

Basically, Rule 146 contained a codified version of all the elements of a private placement thought necessary to balance the competing interests of investor protection and issuer access to financial markets. It required, in part:

> (1) maximum of 35 purchasers, excluding certain relatives and persons who individually acquire an aggregate amount of $150,000 or more of the issue of securities;
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> (2) disclosure of relevant, material information to each *offeree* or his representative;
>
> (3) criteria for determination of *offeree* and purchaser sophistication or wealth;
>
> (4) prohibition on general solicitation and advertising;
>
> (5) resale restrictions including determination of "investment intent," placing a restrictive legend on the security, and issuing a stop-order instruction; and
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> (6) mandatory notification to the Commission.

Rule 146 was considered a failure by practitioners who were "disappointed by the complexity, precision, and obscurity of . . . the Rule, and particularly by its 'all or none' approach, which require[d] satisfaction of all conditions of the Rule or loss of its exemption." Carney, *supra*, at 346 (footnote omitted).

31. The ceiling was raised to $5,000,000 as part of the Small Business Simplification Act of 1980, Pub. L. No. 96-477, § 301, 94 Stat. 2291 (codified at 15 U.S.C. § 77c(b) (1982)).

securities from the registration requirements of the Securities Act was "expected to be used only in a sparing manner."[32] The Commission heeded that directive and, prior to Regulation D, made only a few attempts to promulgate limited offering exemptions.[33]

These early (pre-Regulation D) section 3(b) exemptions sought to strike a balance between the competing needs of investors for protection and of small issuers for capital. The needs of issuers were aided by provisions reducing disclosure requirements and eliminating subjective criteria. For example, Rule 240[34] contained no requirements for disclosure of information. This rule, which applied to offerings up to $100,000, relied entirely upon the antifraud provisions of the federal laws to provide investor protection.[35] Rule 242,[36] which was available for offerings up to $2,000,000, abandoned subjective purchaser sophistication requirements and replaced them with a provision restricting sales to any thirty-five persons without qualification plus any number of "accredited investors."[37] Although Rules 240 and 242 were a significant induce-

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32. 1 L. Loss, SECURITIES REGULATION 606 (1961) (quoting the House Comm. on Int. & For. Commerce, H.R. REP. No. 85, 73d Cong., 1st Sess. 6-7 (1933)).

33. The Commission's most notable limited offering exemption prior to Rules 504 and 506 of Regulation D was Regulation A, 17 C.F.R. §§ 230.251-.263 (1982), discussed in Green & Brecher, *When Making a Small Public Offering Under Regulation A*, 26 PRAC. LAW., Mar. 1, 1980, at 25, 41. Regulation A is frequently referred to as "short-form registration," although it is actually not registration at all, but is a conditional exemption. While § 12(2) and § 10b-5 are applicable, § 11 liability for false registration statements does not apply to literature employed in Regulation A offerings. L. Loss, *supra* note 19, at 340.

34. 17 C.F.R. § 230.240 (1975) (repealed 1982).

35. *Id.* Rule 240 contained, generally, six conditions:

(1) Prohibition on general advertising and solicitation;
(2) Disposition and resale restriction;
(3) Filing of notice;
(4) Prohibition on paying sales commissions or similar remuneration;
(5) $100,000 offering limit for 12 months preceding each sale;
(6) Limit of 100 beneficial owners, excluding spouses, relatives, and certain entities beneficially owned by purchasers.

See Carney, *Exemption from Securities Registration for Small Issuers: Shifting from Full Disclosure—Part III: The Small Offering Exemption and Rule 240*, 11 LAND & WATER L. REV. 483 (1976).

36. 17 C.F.R. § 230.242 (1982) (repealed 1982).

37. Rule 242 introduced the important concept of the accredited person. This concept was an attempt to "link" the numerical limitation of 35 purchasers with a sophistication requirement by excluding from the computation of the 35 purchasers a category of presumptively sophisticated institutional investors including banks, insurance companies, employee benefit plans, investment companies, directors and officers of the issuer, and any purchaser of $100,000 or more of the issuer's securities. *See* Parnall, Kohl & Huff, *Private and Limited Offerings After a Decade of Experimentation: The Evolution of Regulation D*, 12 N.M.L. REV. 633, 663 (1982). Rule 242 also included the concept of the qualified issuer. Investment companies and oil and gas operations were deemed unqualified issuers because of their

ment to capital formation by small issuers, their technical and practical flaws evoked substantial criticism. Rule 240 was criticized because of its small offering amount and was deemed "not especially helpful to small business,"[38] and Rule 242 contained burdensome disclosure requirements which limited its use by small companies whose capital needs exceeded the $100,000 amount permitted under Rule 240.[39]

Not long after Rule 242 was adopted, the Commission developed Regulation D which replaced Rules 240, 242, and 146.[40] Regulation D is composed of six rules, three of which establish or clarify exemptions from the registration requirements of the Securities Act. Rules 504 and 505, promulgated pursuant to section 3(b) of the Securities Act, create limited offering exemptions, while Rule 506 is merely a safe harbor under the private placement exemption of section 4(2). Rules 501, 502, and 503 contain general conditions applicable to offerings under the operative rules, Rules 504, 505, and 506.

Regulation D begins with a set of six introductory and explanatory notes. The first of these reiterates the fact that an issuer is subject to the antifraud and civil liability provisions of the securities laws notwithstanding an exemption from registration.[41] It also reminds issuers of their obligation to provide additional material information when needed to ensure that any required disclosure made is not misleading. The second note recognizes the need for issuers to comply with applicable state laws. It emphasizes the Commission's intention that Regulation D function in a uniform

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greater potential for abusing the rule. Securities Act Release No. 6180 (Jan. 17, 1980), [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,426, at 82,815. *See* Parnall, Kohl & Huff, *supra*, at 662. In addition to these provisions, Rule 242 contained a proscription against general advertising and resales, various notification provisions, a limitation of 35 purchasers, a $2,000,000 offering ceiling, and liberal disclosure provisions. *See generally* Thomforde, *Relief for Small Business: Two New Exemptions from SEC Registration*, 48 TENN. L. REV. 323 (1981).

38. *See* Securities Act Release No. 6180, *supra* note 37, at 82,813. *See also* Securities Act Release No. 5914 (Mar. 6, 1978), [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,530, at 80,149 (announcing a series of Commission-sponsored hearings which were subsequently held and at which these difficulties were noted).

39. *See* Parnall, Kohl & Huff, *supra* note 37, at 664-66.

40. *See* An Analysis of Regulation D, *supra* note 9, at 86,886. Regulation D is codified at 17 C.F.R. §§ 230.501-.506 (1982). The provisions of Regulation D are hereinafter cited by rule number and paragraph designation. Regulation D was adopted in Securities Act Release No. 6389 (Mar. 8, 1982), [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 83,106, at 84,907.

41. The protections of these provisions are available for investors in addition to whatever protections are built into the requirements of the exemptions themselves.

system of federal and state limited offering exemptions. The third preliminary note assures issuers that unsuccessful attempted compliance with any rule under Regulation D does not act as an exclusive election which prevents reliance upon other rules and statutes. It provides that if the issuer fails to qualify under Rule 506, Regulation D does not preclude reliance upon section 4(2) of the Securities Act. The fourth note highlights the fact that Regulation D is merely a *transactional* exemption and the securities themselves are not exempt. Therefore, the exemption is available only to an issuer and will not exempt sales made by affiliates[42] or resales made by purchasers.[43] The fifth note confirms that Regulation D is available to business combinations, while the sixth note warns that technical compliance with the applicable conditions and rules may be insufficient in some circumstances.[44]

Rule 501, the first rule of Regulation D, discusses the method of counting the number of purchasers. It excludes from the calculation certain persons and entities which are deemed protected by virtue of their relationship to, or dominance by, an issuer, and the resulting information about the issuer which they are presumed to possess.[45] Rule 501 also defines several terms not defined elsewhere in the securities laws, including affiliate,[46] aggregate offering price,[47] business combination,[48] executive officer,[49] issuer,[50] pur-

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42. *See infra* note 46 for the definition of affiliate.

43. *See infra* note 70 and accompanying text.

44. Note 6 does not provide any examples of situations in which technical compliance would be insufficient, but speaks of transactions which are "part of a plan or scheme to evade the registration provisions of the Act."

45. Rule 501(e).

46. "An 'affiliate' of, or person 'affiliated' with, a specified person shall mean a person that directly, or indirectly through one or more intermediaries, controls or is controlled by, or is under common control with, the person specified." Rule 501(b). *Cf.* Rule 242(a)(2), 17 C.F.R. § 230.242(a)(2) (1982) (repealed 1982).

47. " 'Aggregate offering price' shall mean the sum of all cash, services, property, notes, cancellations of debt, or other consideration received by an issuer for issuance of its securities." Rule 501(c).

48. 'Business combination' shall mean any transaction of the type specified in paragraph (a) of rule 145 . . . and any transaction involving the acquisition by one issuer, in exchange for all or a part of its own or its parent's stock, of stock of another issuer if, immediately after the acquisition, the acquiring issuer has control of the other issuer (whether or not it had control before the acquisition).

Rule 501(d). *Cf.* Rule 146(f)(1), 17 C.F.R. § 230.146(f)(1) (1982) (repealed 1982).

49. " 'Executive Officer' shall mean the president, any vice president . . ., any other officer who performs a policy making function, or any other person who performs similar policy making functions for the issuer." Rule 501(f). *Cf.* Rule 242(a)(3), 17 C.F.R. § 230.242(a)(3) (1982) (repealed 1982).

50. "The definition of the term 'issuer' in section 4(2) of the Act shall apply. . . ." Rule

chaser representative,[51] and accredited investor.[52] This last term refers to an investor who is considered sufficiently wealthy or financially sophisticated so as to be able to bargain for any necessary information concerning the proposed offering. Regulation D borrowed the accredited investor concept from Rule 242, expanding it to include its present eight categories of investors deemed able to "fend for themselves."[53]

Rule 502 delineates the general conditions relating to integration of offerings, the manner of offerings, disclosure requirements, and resale provisions. Noticeably absent from the general conditions is any provision prohibiting the payment of commissions to brokers, dealers, or other putative salespersons.[54]

Regulation D's provisions with respect to integration[55] are im-

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501(g). Section 4(2) defines "issuer" as "every person who issues or proposes to issue any security" and then enumerates various exceptions to that general definition. Securities Act § 4(2), 15 U.S.C. § 77b(4) (1982). *Cf.* Rule 146(a)(2), 17 C.F.R. § 230.146(a)(2) (1982) (repealed 1982).

51. A purchaser representative is, broadly speaking, one who is unrelated to the issuer, who is financially sophisticated, and who is acknowledged by the purchaser as his purchaser representative. Rule 501(h). See Kessler, *Private Placement Rules 146 and 240—Safe Harbor?*, FORDHAM L. REV. 37, 63-65 (1975), for an explanation of the definition of "offeree representative."

52. The current "accredited investor" category includes any person or entity the issuer reasonably believes falls within one of the following categories:

(1) Qualified institutional investors, including certain banks, investment companies, and employee benefit plans;

(2) Private business development companies;

(3) Tax exempt organizations with assets in excess of $5,000,000;

(4) Directors, executive officers, and general partners of the issuer;

(5) Persons who purchase at least $150,000 of the securities, so long as not in excess of 20% of the purchaser's net worth;

(6) Natural persons with individual or joint net worth exceeding $1,000,000;

(7) Natural persons with income in excess of $200,000 for each of the past two years; or

(8) Any entity in which all of the equity owners are accredited investors under Rule 501(a)(1), (2), (3), (4), (6), or (7).

Rule 501(a). There are significant qualifications to each category. *See* Securities Act Release No. 6389, *supra* note 40.

53. *See* Note, *supra* note 23, at 133.

54. In the past such sales commissions were restricted. This prohibition greatly reduced employee incentive to assist the issuer in selling securities. The proscription ensured "that the securities [were] not offered or sold by the use of 'high pressure tactics or otherwise through organized securities distribution media,'" but at the same time it hampered the issuer's ability to locate potential investors. *See* Parnall, Kohl & Huff, *supra* note 37, at 655 (citing Securities Act Release No. 5560 (Jan. 24, 1975), [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,066, at 84,948).

55. "Integration" is a term unique to the securities field. It refers to the time frame in which an offering will be presumed to have occurred. Occasionally, what may be planned as two separate and distinct offerings may be deemed integrated and therefore one large offer-

portant for purposes of determining the offering period within which the number of purchasers or the offering price will be calculated. Under the traditional test there were five factors which were considered in determining whether offers and sales should be integrated.[56] Rule 502 provides an objective "safe harbor" whereby sales and offers for sale occurring six months prior to or subsequent to the date of a Regulation D transaction will not be integrated. In situations where the safe harbor is not available, however, the traditional test applies.[57]

With regard to required disclosure, Regulation D has adopted a dichotomous arrangement. On the one hand, for any offering made pursuant to Rule 504 and for those offerings pursuant to Rule 505 or 506 which are restricted solely to accredited investors, Rule 502 does not require that any specific information be furnished to purchasers.[58] On the other hand, for offerings under Rule 505 or 506 which involve a sale to any purchaser who is not an accredited investor, there are specific disclosure requirements which vary according to the size of the offering and the nature of the issuer.[59]

The nature of the issuer depends upon whether the issuer is a reporting company under section 13 or 15(d) of the Exchange Act. If it is, the size of the offering is irrelevant, but if the issuer is a nonreporting company, the disclosure requirements turn on whether the issue exceeds $5,000,000.[60]

Since adequate information is already publicly available regard-

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ing. The consequences of such an occurrence may be disastrous as in the case of two distinct private placements qualifying separately for the § 4(2) exemption which, if integrated, would together constitute a nonexempt public offering. *See* Deaktor, *Integration of Securities Offerings*, 31 U. FLA. L. REV. 465, 472-74 (1979) ("Integration under the [Securities Act] is designed to prevent an issuer from avoiding registration of a nonexempt transaction by accomplishing the transaction through two or more ostensibly distinct offerings each of which, if treated as a separate transaction, would conform to the statute.").

56. Securities Act Release No. 33-4552 (Nov. 6, 1962), 27 Fed. Reg. 11,316 (1962). *Cf.* Securities Act Release No. 33-4434 (Dec. 6, 1961), 26 Fed. Reg. 11,896 (1961). The traditional integration test involves subjective weighing of the following five factors:

(a) Whether the offerings are part of a single plan of financing;

(b) Whether the offerings involve issuance of the same class of security;

(c) Whether the offerings are made at or about the same time;

(d) Whether the same type of consideration is to be received;

(e) Whether the offerings are made for the same general purpose.

57. Rule 502(a).

58. Rule 502(b)(i).

59. Rule 502(b)(ii).

60. This distinction exists because Form S-18 is unavailable for reporting companies or issues greater than $5,000,000. *See* Securities Act Release No. 6389, *supra* note 40, at 84,916 n.21.

ing reporting companies, those issuers may simply furnish offerees either (1) their most recent shareholders' annual report and proxy statement (and Form 10-K[61] if requested), or (2) information contained in their annual report on Form 10-K or in a registration statement on Form S-1[62] or Form 10.[63] In either case the issuer must furnish a brief description of the securities, the use of proceeds from the offering, and any material changes in its affairs which are not reflected in the foregoing documents.[64] Nonreporting companies, on the other hand, must furnish offerees the same information which would have been included in a prospectus if the offer had been registered.[65] In all cases the issuer must furnish investors an opportunity to ask questions and obtain additional information.[66] This last requirement is usually met by holding a "seminar" at which management makes a presentation and then answers questions.

Rule 502 provides, with respect to the manner of offerings, that the issuer generally may not utilize any form of general solicitation or general advertising.[67] Newspaper and magazine advertisements are forbidden, as are television and radio communications. Likewise, general solicitations and open invitations to seminars or meetings are proscribed. In many instances issuers may be forced to develop lists of potential customers and then personally solicit them. The rule does not, however, absolutely prohibit the use of mail as a means of inviting persons to seminars.[68] Additionally, in states which require registration of the securities and delivery of a disclosure document, the federal restriction on the manner of offering is preempted in an offering under Rule 504 in favor of any requirements the state imposes.[69]

Rule 502 expressly provides that securities acquired in a Regulation D offering cannot be resold by the purchaser absent registration or an applicable exemption.[70] Without this provision, sales

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61. 17 C.F.R. § 249.310 (1982).
62. *Id.* § 239.11.
63. *Id.* § 249.210.
64. Rule 502(b)(2)(ii).
65. Rule 502(b)(2)(i). There is, however, an available escape valve. If an audited financial statement cannot be prepared "without unreasonable effort or expense," then all that is required is a very recent balance sheet. Rule 502(b)(2)(i)(A)-(B). There is a slightly different escape valve provided for limited partnerships. *Id.*
66. Rule 502(b)(2)(v).
67. Rule 502(c). *Cf.* Rule 146(c), 17 C.F.R. § 230.146(c) (1982) (repealed 1982).
68. Securities Act Release No. 6389, *supra* note 40, at 84,917 n.23.
69. Rule 502(c).
70. Rule 502(d).

under the private placement exemption might merely be the first step in a conduit by way of which unregistered securities flow from the issuer to the public. Rule 502 also provides that the issuer shall exercise "reasonable care" to ensure that purchasers are not statutory "underwriters" as defined in section 2(11) of the Securities Act.[71] If a purchaser becomes an underwriter by virtue of the resale of the securities, the issuer may lose its exemption.[72] The required care can be presumptively shown by the issuer if it demonstrates (1) reasonable inquiry to determine whether the purchaser is acquiring the securities for his own investment or on behalf of another; (2) presale written disclosure informing each purchaser that the securities have not been registered and therefore cannot be resold unless they are registered or unless an exemption from registration is available; and (3) placement of a legend on the certificate indicating that the securities have not been registered and that there are restrictions on their transferability.[73] If, however, the securities are issued pursuant to Rule 504 in states which require registration of the securities and delivery of a disclosure document, there are no resale restrictions.[74]

Unlike its predecessor rules, Regulation D employs uniform forms for use with any of the three operative rules. Notice of sale is accomplished under Rule 503 by filing Form D[75] with the Commission at various specified times during the course of an offering.[76] The purpose of the notice requirement is to provide a means of assessing the effectiveness and usefulness of Regulation D as a capital raising device for small businesses.[77]

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71. *Id.*

72. This is so because the resale of unregistered securities generally is permitted under § 4(1) of the Securities Act, which provides that the registration requirements of § 5 shall not apply to "transactions by any person other than an issuer, underwriter, or dealer." 15 U.S.C. § 77d(1) (1982). If, however, a purchaser is an underwriter as defined in § 2(11), the exemption of § 4(1) is not available. Because determination of a person's status as an underwriter under § 4(1) in turn involves several subjective determinations such as whether a purchase was "with a view to" the "distribution" of any security, the safe harbor provision of Rule 144, 17 C.F.R. § 230.144 (1982) is often relied upon as a means of ensuring compliance with § 4(1).

73. Rule 502(d). *Cf.* Rule 242(g), 17 C.F.R. § 230.242(g) (1982) (repealed 1982).

74. Rule 502(d).

75. 17 C.F.R. § 230.500 (1982).

76. In addition, upon request, the issuer must provide the Commission with copies of information furnished by nonaccredited investors. Rule 503(d).

77. Rule 503(a)(2). *See* Securities Act Release No. 6339 (Aug. 7, 1981), [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 83,014, at 84,465. The Commission has recently issued a release reporting results of a study of the general operation of Regulation D in its first year (Apr. 15, 1982—Apr. 14, 1983). *See* An Analysis of Regulation D, *supra* note 9, at

Rule 504 is a de minimis exemption which applies to offerings of less than $500,000.[78] It is intended to be used to "facilitate the capital formation needs of the small start-up company seeking venture capital, and not seasoned issuers for which information is readily available by means of Exchange Act documents."[79] Therefore, it is restricted to issuers that are not already reporting companies or investment companies (mutual funds).[80] In determining the offering price of $500,000, the rule requires aggregation of all sales during the preceding twelve months made pursuant to Rule 504, Rule 505, or Regulation A, and of all sales made in violation of section 5 of the Securities Act.[81] Rule 504 contains no investor qualification standards and permits sale to an unlimited number of investors. Sales commissions are permitted under the rule, but general solicitation and general advertising[82] and resale[83] are prohibited unless the securities are offered and sold exclusively in states requiring delivery of a disclosure document.

Rule 505's exemption is available to all issuers with the exception of investment companies.[84] It is available for offerings whose aggregate offering price does not exceed $5,000,000 or, if securities have been sold within the last twelve months, $5,000,000 less the aggregate offering price for all securities sold under a Regulation D exemption within the twelve months before and during the offering in question.[85] Rule 505 permits an offering to as many as thirty-five investors without qualifications plus any number of accredited investors.[86] Sales commissions are permitted under the rule, but

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86,886. The findings indicate that issuers claiming an exemption under Regulation D offered an estimated $15.5 billion of securities, approximately 17% of the total amount effectively registered for cash sale to the public. Almost 50% of all Regulation D offerings claimed a Rule 506 exemption; 25% claimed Rule 504; 13% claimed Rule 505; and another 13% claimed more than one exemption. The average size for an offering was $2,100,000, indicating Regulation D is being used primarily by small issuers. The typical corporate issuer tends to have five or fewer employees, an operating history of two years or less, four shareholders, 500,000 or fewer shares outstanding, revenues and assets of $500,000 or less, and shareholders' equity of $50,000 or less. Accredited investors provided 71% of all monies raised, and over one-third of all monies raised resulted from offerings sold only to accredited investors. *Id.*

78. Rule 504(b)(2).
79. Securities Act Release No. 6339, *supra* note 77, at 84,467.
80. Rule 504(a).
81. Rule 504(b)(2).
82. Rule 504(b)(1).
83. *Id.*
84. Rule 505(a).
85. Rule 505(b)(2)(i).
86. Rule 505(b)(2)(ii).

general solicitation is prohibited and resale is restricted.[87]

Rule 506, the private placement exemption safe harbor, is available to any issuer which meets the requirements of Rules 501, 502, and 503.[88] It permits the issuer to raise an unlimited amount of capital and permits sale to as many as thirty-five qualified (sophisticated) investors plus any number of accredited investors.[89] While accredited investors are presumed to be sophisticated, with respect to all other purchasers Rule 506 requires that the issuer reasonably believes, prior to sale, that the investor has, either alone or with his purchaser representative,[90] "such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment."[91]

This last qualification is important because ignoring the business acumen of offerees raises the spectre of forfeiting the independent statutory exemption of section 4(2). Although imperfect compliance with the safe harbor of Rule 506 does not preclude an issuer from relying on section 4(2), offeree sophistication is a virtual condition precedent to utilization of section 4(2), and if the issuer fails to qualify for a Rule 506 exemption because of failure to comply with the purchaser sophistication requirement of Rule 506, it most likely simultaneously fails to otherwise qualify for a section 4(2) exemption.[92]

III. THE FLORIDA EXEMPTION

Just as the federal securities law has developed over the years, so too has the Florida law, often in response to the federal evolution.[93] Regulation D became effective in 1982, and in 1983 the

87. Rule 505(b)(1).

88. Rule 506(a).

89. Rule 506(b)(2)(i).

90. *See supra* note 51.

91. Rule 506(b)(2)(ii).

92. *But see* Waters, *Sophistication and the Private Offering of Securities in Alabama—A Lack of Federal and State Law Coordination*, 44 ALA. LAW. 240 (1983).

93. The original Florida blue sky law was enacted in 1913. It was patterned after the Kansas act which had first alerted the country to the necessity of securities regulation. *See* J. MOFSKY, BLUE SKY RESTRICTIONS ON NEW BUSINESS PROMOTIONS 20 (1971); Ch. 6422, 1913 Fla. Laws 56. The later 1931 Florida Sale of Securities Law was a modified version of the original Uniform Sale of Securities Law. It was adopted with the intention of making Florida securities laws consistent with the Uniform Act and regulations of other states. The Uniform Act proved to be a failure and eventually was removed from the list of approved acts in 1944. *See* Robinton & Sowards, *Florida's Blue Sky Law: The Lawyer's Approach*, 6 MIAMI L.Q. 525, 527 n.7 (1952); Ch. 14899, § 22, 1931 Fla. Laws 797. Interestingly, the Florida legislature very recently changed the name of ch. 517, Florida Statutes from "Florida

Florida legislature responded by making modifications to the Florida scheme of exemptions.[94] Although these modifications served to increase uniformity between the federal and state law, the Florida exemption scheme is not yet wholly compatible, on its face or in operation, with the currently existing federal scheme.

The primary Florida exemption is found in section 517.061(12), Florida Statutes.[95] This exemption is available to any issuer and contains no aggregate offering price limitation. The exemption permits an offering to as many as thirty-five investors in the state in any twelve-month period.[96] It contains no investor sophistication requirements[97] but excludes from the computation of the number of purchasers all accredited investors, certain relatives of purchasers; certain affiliated trusts, estates, and corporations, and certain purchasers making an investment of $100,000 or more.[98]

Section 517.061(12) prohibits general solicitation and general advertising[99] and proscribes the payment of sales commissions to unregistered dealers.[100] The exemption provides for a three-day voidability period when sales are made to five or more purchasers.[101] It also requires that each purchaser or his representative be provided with, or given reasonable access to, "full and fair disclosure of all material information" prior to the sale.[102] With respect to integration of offerings, the Florida exemption provides for a six-month safe harbor period.[103] It further provides for consideration

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Securities Act" to "Florida Investor Protection Act." 1984 Fla. Sess. Law Serv. 84-159 (West). Additionally, the legislature increased the scope of the act by broadly defining "investment" to mean, with several exceptions, "any commitment of money or property, not otherwise a security as defined in this chapter, in expectation of receiving an economic benefit, offered or sold in violation of s. 517.301 or s. 517.311." *Id.*

94. Ch. 83-184, 1983 Fla. Laws 716 (current version at FLA. STAT. §§ 517.021, .061(12)(a)-(b), .12(10), (14) (1983). *See* Van Nortwick & Thompson, *Regulation and the Amended Florida Private Placement Exemption,* 57 FLA. B.J. 578 (1983).

95. There are other transactional exemptions in § 517.061, including § 517.061(19) which exempts offers and sales of securities federally registered with the Commission. *See* FLA. STAT. § 517.061 (1983).

96. FLA. STAT. § 517.061(12)(a)(1) (1983).

97. *But see* FLA. ADMIN. CODE R. 3E-500.07(3) (Supp. 1983). *See also infra* note 107 and accompanying text.

98. FLA. STAT. § 517.061(12)(b) (1983). *See also* FLA. ADMIN. CODE R. 3E-500.04 (Supp. 1983).

99. FLA. STAT. § 517.061(12)(a)(2) (1983). *But see* FLA. ADMIN. CODE R. 3E-500.07(3) (Supp. 1983).

100. FLA. STAT. § 517.061(12)(a)(4) (1983). *See also* FLA. ADMIN. CODE R. 3E-500.06 (Supp. 1983).

101. FLA. STAT. § 517.061(12)(a)(5) (1983).

102. *Id.* § 517.061(12)(a)(3). *See also* FLA. ADMIN. CODE R. 3E-500.05 (Supp. 1983).

103. FLA. STAT. § 517.061(12)(c)(1) (1983). *See also* FLA. ADMIN. CODE R. 3E-500.01

of "the particular facts and circumstances in each case" in determining whether offers and sales not falling within the safe harbor provision will be integrated.[104]

In addition to the exemption created under section 517.061(12), there is a statutory provision authorizing the Department of Banking and Finance (the Department) to adopt rules creating exemptions from Florida registration upon a finding by the Department that registration "is not necessary in the public interest and for the protection of investors because of the small dollar amount of securities involved or the limited character of the offering."[105] To date, however, no exemptions have been created by the Department pursuant to this authority.

Section 517.061(12) is perhaps most analogous to Rule 506 of Regulation D. It is not, however, a pure private placement exemption, but contains a curious assortment of federal private placement and limited offering exemption features. It also contains several features which have no federal counterpart.

Perhaps the most striking feature of the Florida exemption is its provision for an unlimited offering amount coupled with the absence of any investor sophistication requirements. At first glance this state scheme appears to provide less investor protection than the federal scheme. It must be remembered, however, that an issuer seeking exemption from state registration is likely to be seeking exemption from federal registration as well. If so, the issuer will probably need to comply with the requirements of one of Regulation D's exemptions. None of those exemptions permits an unlimited offering to a potentially unsophisticated group of investors. Rules 504 and 505 have limited offering amounts of $500,000 and $5,000,000, respectively, while Rule 506 requires purchaser sophistication or accredited investor status. Thus, for practical purposes, an issuer seeking exemption from Florida registration will most likely be subject, under federal requirements, to either an offering price limitation or the requirement of purchaser sophistication or accredited investor status. On the other hand, in limited instances an issuer may be simultaneously seeking exemption from federal registration under the intrastate exemption of section 3(a)(11) of the Securities Act[106] and from state registration under the Florida exemption of section 517.061(12). In those situations the issuer is

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(Supp. 1983).

104. FLA. STAT. § 517.061(12)(c)(2) (1983).

105. *Id.* § 517.061(21).

106. Securities Act § 3(a)(11), 15 U.S.C. § 77c(a)(11) (1982).

not subject under the federal exemption to either an offering amount limitation or the requirement of purchaser sophistication or accredited investor status.

However, it should be noted that while there are no investor sophistication requirements in section 517.061(12), the Division of Securities of the Florida Department of Banking and Finance has, by way of rule, indirectly imposed investor sophistication requirements. Rule 3E-500.07 defines general solicitation and general advertising to include seminars, meetings, letters, circulars, notices, and other written communications unless the issuer has reasonable grounds to believe after inquiry and does believe that those invited to or attending any seminar or meeting or receiving any letter, circular, notice, or other written communication are both "able to bear the economic risk to the prospective investment" and "have such knowledge and experience in financial and business matters as to be capable of evaluating the merits and risks of the prospective investment" or, if invited to or attending any seminar or meeting, are accompanied by an investment adviser.[107] Thus, there are investor sophistication requirements under the Florida exemption in any offerings where the issuer employs seminars, meetings, letters, circulars, notices, and other written communications to advertise the securities and solicit purchases of those securities.

Another noteworthy feature of the Florida exemption is its treatment of the resale of securities. The exemption of section 517.061(12) applies only to issuers and thus is not available to reselling purchasers.[108] Rather, section 517.061(3), the Florida counterpart to federal section 4(1), is the section applicable to purchasers seeking to resell securities acquired in a transaction exempt from registration under the primary Florida exemption. Section 517.061(3) exempts isolated sales and offers for sale made by or on behalf of a seller who is not the issuer or underwriter and who, as the bona fide owner, makes the disposition on his own behalf. Such isolated offers and sales include specifically those made in a transaction exempt under section 4(1) of the Securities Act[109] or in a transaction satisfying all the requirements of section 517.061(12) except the three-day voidability provision.[110] Section

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107. FLA. ADMIN. CODE R. 3E-500.07(3) (Supp. 1983).

108. FLA. STAT. § 517.061(12)(a) (1983) ("[t]he offer or sale, *by or on behalf of an issuer*, which offer or sale is part of an offering made in accordance with all of the following conditions . . .") (emphasis added).

109. FLA. STAT. § 517.061(3)(b) (1983).

110. *Id.* § 517.061(3)(a).

517.061(3) also provides that no person shall be deemed an underwriter or issuer with respect to any securities he has beneficially owned for at least a year. This presumably includes unregistered securities acquired in a section 517.061(12) transaction.

In most instances, the Florida resale provision will have no practical effect. When the original purchaser is seeking to resell securities acquired in a Regulation D transaction, a section 4(1) exemption is theoretically available,[111] but as a practical matter the seller will be required to comply with the safe harbor provisions of Rule 144.[112] Otherwise the reselling investor risks being deemed a nonexempt statutory underwriter. This not only results in the seller violating section 5, but may cost the issuer the loss of its exemption, exposing it to potential section 12(1) civil liability. On the other hand, by satisfying the requirements of Rule 144 (and thus section 4(1)), a selling shareholder also satisfies the section 517.061(3) exemption. The Florida exemption also contains what is basically a safe harbor in its provision that any person, including, without limitation, a promoter or affiliate of an issuer, who has beneficially owned securities for at least one year "shall not be deemed an underwriter, an issuer, or a person acting for the direct or indirect benefit of the issuer or an underwriter" with respect to those securities.[113] While this provision makes it easier to avoid underwriter status than does the federal law,[114] a selling shareholder must still comply with Rule 144's two-year holding period in order to qualify for the federal section 4(1) exemption. Thus, the Florida resale provisions of section 517.061(3) have no operative effect except to the extent they allow state, as well as federal, enforcement of resale restrictions. Moreover, they may in fact be misleading and confusing to issuers and investors since they invite resale after one year and thus loss of Rule 144's safe harbor.

In contrast to federal Rule 502, which requires particularized disclosure,[115] the Florida exemption essentially codifies the antifraud rules in its requirement that the issuer provide purchasers with, or afford them reasonable access to, "full and fair disclosure of all *material* information."[116] Additionally, while Regulation D does not require any specific disclosure when the securities are sold

111. *See supra* note 72 and accompanying text.
112. 17 C.F.R. § 230.144 (1982).
113. FLA. STAT. § 517.061(3) (1983).
114. *See supra* note 72 and accompanying text.
115. *See supra* note 59 and accompanying text.
116. FLA. STAT. § 517.061(12)(a)(3) (1983) (emphasis added).

only to accredited investors,[117] the Florida exemption contains no comparable exception to its disclosure requirements in the case of offerings made only to accredited investors.[118] To the extent that the Florida exemption requires disclosure of information which an issuer must already disclose under federal law to prevent liability under Rule 10b-5, the Florida requirement seems unnecessary, and the absence of an exception for offerings made only to accredited investors seems insignificant. On the other hand, the presence of a disclosure requirement in the Florida exemption permits state, as well as federal, regulation of issuers' disclosure practices.[119] In some instances it may also result in liability under state law where there would be no comparable liability under federal law.

For example, in the case of an offering made only to accredited investors, the only potential liability under federal law for improper disclosure would be liability under Rule 10b-5, which requires proof of scienter.[120] Because there is no disclosure requirement in Regulation D itself for offerings made only to accredited investors, improper disclosure would not result in absolute liability under section 12(1). However, because the Florida exemption requires disclosure regardless of who the purchasers are, and because the disclosure requirement is contained in section 517.061(12) itself, under Florida law there would be potential liability under both section 517.211(1) (the Florida counterpart to section 12(1)) *and* section 517.301(1) (the Florida anitfraud provision) for an offering made only to accredited investors for which there was improper disclosure. Under either of these provisions, liability may lie even without proof of scienter,[121] and there might thus be liability under state law without scienter in situations where there would be no liability under federal law unless scienter were proved.

Another respect in which the Florida exemption differs from Regulation D is in the area of sales commissions. Regulation D does not prohibit the payment of sales commissions,[122] a subject which is intentionally left to state regulation. The Florida exemption prohibits the payment of a commission or compensation for the sale of the issuer's securities to any dealer who is not regis-

117. *See supra* note 58 and accompanying text.

118. *See supra* note 102 and accompanying text.

119. There are numerous remedies available under ch. 517 of the Florida Statutes. *See, e.g.*, FLA. STAT. §§ 517.191, .211, .221, .241 (1983).

120. *See generally*, L. LOSS, *supra* note 19, at 870-900 (1983).

121. *See* FLA. STAT. §§ 517.211(1), .301(1) (1983).

122. *See supra* note 54 and accompanying text.

tered.[123] It permits payment to registered dealers and, by virtue of the definition of dealer, permits payment to certain other individuals, including any "bona fide employee of the issuer who has not participated in the distribution or sale of any securities within the preceding twelve months and who primarily performs or is intended to perform at the end of the distribution, substantial duties . . . other than in connection with transactions in securities."[124] The practical effect of the Florida exemption is to place an additional burden upon issuers, not present under federal law, to ensure that any dealers participating in the issue are registered. It is questionable whether dealer licensing is so useful that this provision actually affords additional investor protection. If it is not, and the Florida provision does not afford enhanced investor protection, the added burden on issuers is not justifiable.

With respect to the manner of offering, section 517.061(12) contains a blanket prohibition on general solicitation and general advertising.[125] So, too, do Rules 505 and 506 of Regulation D, and so also does Rule 504 except for offers and sales made exclusively in, and in compliance with the requirements of, states which provide for registration of securities and which require the delivery of a disclosure document before sale.[126] While the Florida exemption might, by virtue of its unqualified prohibition on general solicitation and general advertising, be viewed as more restrictive than Rule 504, it should be noted that an offering as limited in amount as one under Rule 504 would most often not require general solicitation and general advertising. In those cases, the Florida exemption's more restrictive provision would have no operative effect. However, there may be situations where section 517.061(12) prohibits solicitation or advertising that would otherwise be allowed, and in any event the prohibition, by virtue of its position in the Florida exemption, is thereby subject to both state and federal enforcement.

In its provisions relating to the integration of offerings, the state exemption is compatible with Regulation D.[127] Similarly, the two schemes contain identical definitions of accredited investor.[128]

123. FLA. STAT. § 517.061(12)(a)(4) (1983).

124. *Id.* § 517.021(7).

125. *Id.* § 517.061(12)(a)(2). *But see* FLA. ADMIN. CODE R. 3E-500.07 (Supp. 1983).

126. *See supra* note 82 and accompanying text.

127. *See* FLA. STAT. § 517.061(12)(c) (1983). *See also supra* note 55 and accompanying text.

128. *See* FLA. STAT. § 517.021(1) (1983). *See also supra* note 52 and accompanying text.

With respect to the calculation of the number of purchasers, the Florida scheme diverges from the federal scheme in one respect. While both Regulation D and section 517.061(12) exclude from the calculation of number of purchasers all accredited investors, certain relatives of the purchasers, and certain related trusts, estates, and corporations,[129] section 517.061(12) also excludes "[a]ny purchaser who makes a bona fide investment of $100,000 or more, provided such purchaser or his representative receives, or has access to, the information required to be disclosed by [section 517.061(12)(a)(3)]."[130] This facial difference in the Florida exemption has little operative effect, however. Since such purchasers must be counted towards the thirty-five-purchaser limit in Rules 505 and 506, the Florida provision, although more lenient than Rules 505 and 506, cannot be used in Rule 505 or 506 offerings. Interestingly, the Florida provision can be utilized in conjunction with Rule 504, but there the Florida provision is more restrictive than Rule 504 which permits an unlimited number of investors. In Rule 504 offerings, however, the Florida exemption's thirty-five-purchaser limit probably seldom is of concern to issuers. Because Rule 504 offerings have an aggregate price offering limitation of only $500,000, such offerings do not generally involve a large number of purchasers.

Perhaps the most distinctive feature of the Florida exemption, when compared with Regulation D, is the three-day voidability provision of section 517.061(12)(a)(5).[131] This feature has no federal counterpart and affords a measure of protection unavailable under the federal exemptions. In the event an investor is subjected to high pressure sales tactics, he has three days in which to reflect upon his investment and, if need be, rescind it. Not only does the Florida voidability feature afford additional investor protection, but it does so with comparatively little cost to the issuer. Essentially, the provision means little more to the issuer than that it must wait three days before treating a sale as final.

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129. *See* FLA. STAT. § 517.061(12)(b) (1983). *See also* Rule 501(e).

130. FLA. STAT. § 517.061(12)(b)(4) (1983).

131. This feature of the Florida exemption provides:

> When sales are made to five or more persons in this state, any sale in this state made pursuant to this subsection shall be voidable by the purchaser in such sale either within three days after the first tender of consideration is made by such purchaser to the issuer, an agent of the issuer, or an escrow agent or within three days after the availability of that privilege is communicated to such purchaser, whichever occurs later.

FLA. STAT. § 517.061(12)(a)(5) (1983).

IV. THE UNIFORM LIMITED OFFERING EXEMPTION

The ULOE as endorsed by NASAA begins with three preliminary notes. The first of these provides that the antifraud provisions of the state's securities laws are applicable notwithstanding an issuer's compliance with the ULOE.[132] The second note provides that an exemption may not be available, despite technical compliance with the exemption, if the transaction "is part of a plan or scheme to evade registration or the conditions or limitations explicitly stated in [the] rule."[133] The third note states that the exemption in no way relieves registered broker/dealers and agents from applicable requirements of law including the due diligence, suitability, and know-your-customer standards.[134]

The ULOE provides exemption from state registration for transactions which comply with Rule 505 and with a number of further conditions and limitations. It also provides an optional exemption for transactions which are exempt from federal registration under Rule 506 and which also comply with certain additional conditions and limitations.[135] The ULOE prohibits payment of commissions, fees, or other remuneration to any person for soliciting prospective purchasers unless the person is appropriately registered in the state.[136] An alternate provision, however, would require *all* persons who offer or sell securities to accredited or nonaccredited investors to be registered.[137] The ULOE is unavailable if the issuer, its predecessors, or its affiliates have been or are currently subject to certain specified securities enforcement measures.[138] The basic ULOE requires presale filing of notice on Form D with the state administrator in addition to notice to the Commission as required by Rule 503,[139] although an alternate provision would permit postsale notice only.[140] The exemption also requires that, in the case of sales

132. ULOE, preliminary note 1, 1 BLUE SKY L. REP. (CCH) ¶ 5294, at 1273 (1983).

133. ULOE, preliminary note 2, *id.*

134. ULOE, preliminary note 3, *id.*

135. The text of the ULOE provides, in Rule 1, that an exemption is available for "[a]ny offer or sale of securities offered or sold in compliance with [the] Securities Act of 1933, Regulation D, Rules 230.501-230.503 and 230.505 (*and/or 230.506*) . . ." (emphasis added). Footnote 1 of the ULOE states that "it would not be inconsistent with the regulatory objectives of this exemption for a state to elect to accept Rule 506 offerings within the ambit of this exemption." ULOE, note 1, *id.* at 1273-4.

136. ULOE, Rule 1A, *supra* note 132, at 1273.

137. ULOE, note 2, *id.* at 1273-5.

138. ULOE, Rule 1B, *id.* at 1273-3.

139. ULOE, Rule 1C, *id.* at 1273-3.

140. ULOE, note 4, *id.* at 1273-5.

to nonaccredited investors, the issuer "[must] have reasonable grounds to believe and after making reasonable inquiry [must] believe that" either (1) the investment is "suitable for the purchaser" based upon disclosed facts relating to the purchaser's security holdings and financial situation and needs, or (2) the purchaser, alone or with a representative, has sufficient knowledge and experience in financial and business matters so as to be capable of evaluating the prospective investment's merits and risks.[141] With respect to the former possibility, the ULOE provides a safe harbor if the investment does not exceed ten percent of the purchaser's net worth.[142] Finally, the ULOE provides that transactions exempt under its provisions may not be combined with other exempt offers and sales,[143] that unsuccessful reliance on the ULOE does not preclude reliance on other applicable exemptions,[144] and that the administrator may increase the number of purchasers or waive other provisions of the exemption.[145]

Recently the Section of Corporation, Banking and Business Law of the American Bar Association (ABA) suggested, with three qualifications, adoption of the ULOE as endorsed by NASAA. The first qualification is that Rule 506, suggested only as a footnote alternative in the NASAA version of the ULOE, should be a part of the ULOE as adopted by the states. Second, the ABA noted that footnote 2 would require uncompensated persons involved in sales to register. This requirement was viewed as a "major departure from present state securities laws, in that the exemption could be jeopardized by casual telephone calls made by persons not compensated by (and perhaps even unknown to) the issuer."[146] Therefore, the ABA qualified its endorsement of the ULOE with the comment that this alternate provision should not be part of the uniform exemption. The ABA's final qualification with respect to endorsement of the NASAA version of the ULOE relates to the presale notice requirement. The ABA's position was that Regulation D's postsale notice, recognized by NASAA as an acceptable alternative, was preferable and should be made part of the uniform exemption.[147]

141. ULOE, Rule 1D, *id.* at 1273-4.
142. *Id.*
143. ULOE, Rule 2, *id.* at 1273-4.
144. *Id.*
145. ULOE, Rule 3, *id.*
146. Report, *supra* note 13, at 3.
147. *Id.* at 1.

The ABA's recommendations for modification of the NASAA version of the ULOE seem well-advised. NASAA did not affirmatively recommend inclusion of Rule 506 offerings within the ambit of the ULOE because of concern over the difficulty in large private offerings of determining that all investors are sophisticated and the magnification of the difficulty of controlling the manner and scope of the offering. NASAA also mentioned concern over the potential use of Rule 506 for tax shelter offerings which "have a greater potential for regulatory concerns."[148] The utility of the ULOE would be considerably enhanced by inclusion of Rule 506, however, since many small businesses need more than the $5,000,000 permitted by Rule 505. The flexibility and utility of a ULOE which includes Rule 506 offerings seem to outweigh the potential problems inherent in such a scheme. Additionally, the ABA's concern about requiring registration of uncompensated persons engaging in offering and selling seems well-founded. Because such a requirement might create situations where the exemption could inadvertently be jeopardized, and because that requirement would be a major departure from current law, that alternative in NASAA's ULOE should be rejected. Finally, there does not appear to be any particular benefit to investors in the basic ULOE's requirement of presale notice, and this added burden on issuers should be avoided, as recommended by the ABA.

In its report, the ABA noted that "substantial variations exist among the versions of ULOE adopted in the several states which have acted by rule or statute." The ABA stated it will seek to

> persuade those states with nonconforming ULOE's to adopt the current version or some less stringent conforming standard. . . .
>
> The overall objective is to achieve a national exemptive structure whereby an issuer, which observes the most restrictive ULOE version in effect, can be assured of compliance with all applicable securities regulations, both state and federal, by properly completing the joint NASAA/SEC Form D and filing it, along with the appropriate fee, if any, with the SEC and the applicable states and have no further concern about technical filing, disqualification or disclosure requirements.[149]

148. ULOE, note 1, *supra* note 132, at 1273-4.

149. Report, *supra* note 13, at 4.

V. Florida's Response to the Call for Uniformity

A. *Uniformity Between the Federal and State Exemption Schemes*

Examination of section 517.061(12) in relation to Regulation D reveals a state exemption scheme which is fairly compatible with the federal exemption scheme. This compatibility exists with respect to the practical operation of the Florida exemption requirements in conjunction with the federal requirements and exists in spite of the fact that section 517.061(12) appears, on its face, to differ from Regulation D in several significant respects. To the extent that section 517.061(12) is more lenient than Regulation D, the more restrictive provisions of the federal scheme define the requirements with which an issuer must comply in order to qualify for an exemption from both federal and state registration. Only to the extent that section 517.061(12) is more restrictive than Regulation D is the Florida exemption incompatible in operation with the federal scheme. The most notable respects in which the Florida exemption is more restrictive than Regulation D include the prohibition of the payment of a commission or compensation to unregistered dealers, the blanket prohibition on general solicitation and general advertising which is more restrictive only with respect to Rule 504 offerings, and section 517.061(12)'s requirement of a three-day voidability provision. Additionally, the investor sophistication requirements injected into the exemption by rule 3E-500.07 of the Florida Administrative Code are incompatible with Regulation D.

Elimination of these requirements from the Florida exemption standards would complete operational uniformity between the federal and state schemes. Such action would be well-advised, however, only if the advantage to issuers is not outweighed by unwarranted dilution of investor protection. The Florida prohibition on the payment of commissions or compensation to unregistered dealers could, it seems, be eliminated without significant consequences to investors. Because the payment of commissions to registered dealers and nondealers is permitted, it is questionable whether much protection is afforded investors by the current prohibition. Additionally, it seems inappropriate to involve issuers in policing dealer licensing rules by means of a scheme which places a great premium on dealer status. Similarly, it seems that little investor protection would be sacrificed by allowing general solicitation and general advertising in the case of Rule 504 offerings. Because these offerings are limited to $500,000, it seems that issuers would seldom need or want to utilize such measures even if permitted. However, as to the three-day voidability provision of section 517.061(12), the case for keeping the Florida requirement is stronger. This requirement seems to offer significant investor protection from high-pressure salesmen. In this instance, lack of compatibility with Regulation D may be justified when the interests of investors are considered.

Although section 517.061(12) and Regulation D are largely compatible in operation, such compatibility is evident only after thoughtful study and comparision of the two schemes. Furthermore, the compatibility is in one sense a one-sided proposition. That is, while an issuer who complies with Regulation D comes close to full compliance with section 517.061(12), the reverse is not true. To the extent that the Florida exemption is more lenient than Regulation D, compliance with 517.061(12) does not ensure compliance with Regulation D. Moreover, the facial differences between the schemes are misleading and confusing, and the burden on issuers to compare and analyze the respective requirements of the two schemes to determine their operative effect seems unnecessary and unwarranted.

Florida could easily act to remedy not only the remaining operational differences but also the existing facial differences between the state and federal schemes. The legislature could replace the single Florida exemption of section 517.061(12) with three exemptions corresponding to Rules 504, 505, and 506. Alternatively, the legislature could make the exemption of section 517.061(12) a true private placement exemption, analogous to Rule 506, and the Department of Banking and Finance could, pursuant to its authority in section 517.061(21), create limited offering exemptions corresponding to Rules 504 and 505. Additionally, in either event the Department could, and should, modify rule 3E-500.07 of the Florida Administrative Code to conform with Regulation D. Not only does that rule contain a trap for issuers by imposing purchaser sophistication requirements not readily evident from the face of the statute, but it is more restrictive even than former Rule 146 and certainly more so than current Regulation D.[150] Moreover, it constitutes a step *away* from uniformity with Regulation D while Flor-

150. In effect, Rule 3E-500.07 requires the purchaser to be not only sophisticated (either in his individual capacity or with a representative/adviser), but also wealthy. *Cf.* Rule 146, 17 C.F.R. 230.146 (1982) and Rule 506(ii).

ida's recent trend, as evidenced by the 1983 revisions to chapter 517, has been *towards* uniformity, or at least conformity, with Regulation D. Because Florida could increase operational uniformity with Regulation D with comparatively little effect on investor protection, the state should consider modifying its current exemption scheme to achieve such uniformity. Furthermore, because Florida could, where there is already operational uniformity, achieve facial uniformity with Regulation D at no cost to investors, the state should act to effect such uniformity by statute or by statute and rule.

B. Uniformity Among the State Exemption Schemes

The ULOE as endorsed by NASAA provides an exemption which is compatible with Rules 505 and 506. It incorporates the requirements of Rules 501, 502, and 503 as well as those of Rule 505 and, under the ABA's recommendation, those of Rule 506. It also contains additional requirements not found in Regulation D.

It should first be noted that to the extent the ULOE contains requirements beyond those of Regulation D, the ULOE is, in one sense, inconsistent with the federal exemption scheme. That is, an issuer could not, by complying with Regulation D, ensure compliance with the ULOE. However, the ULOE contemplates a situation where an issuer complies with *its* requirements and thereby ensures compliance with Regulation D and the exemptions of other states. Furthermore, the call for adoption of the ULOE is actually a call to the states to adopt the current version of the ULOE or some less stringent conforming standard. If all states responded, an issuer could, by complying with the requirements of NASAA's version of the ULOE, be assured of complying with the requirements of those states.

The Florida exemption of section 517.061(12) is not far from conforming to the ULOE. In fact, modification of Rule 3E-500.07 and elimination of the three-day voidability period and the prohibition against the payment of commissions to unregistered dealers would create a conforming Florida exemption. As previously noted, the only one of the statutory modifications which might significantly affect investor protection is the elimination of the three-day voidability period. The additional step of eliminating the prohibition on general solicitation and general advertising in Rule 504-type offerings would result in an exemption which is compatible with Regulation D *and* which conforms with the ULOE.

VI. Conclusion

The current Florida exemption scheme is, in operation, largely compatible with Regulation D. This compatibilty is not, however, readily apparent from the face of section 517.061(12). The Florida exemption also comes close to conforming with the ULOE. The same modifications to the Florida exemption which would produce an exemption scheme facially and operationally compatible with Regulation D would simultaneously cause the Florida exemption to conform to the ULOE. Most of the changes needed to effect uniformity would not cause significant dilution of investor protection, and those which might must be considered with respect to the needs of issuers as well as those of investors. In light of the fact that such changes would significantly aid issuers seeking federal and state exemption from registration and, to a lesser extent, aid issuers seeking exemption from registration in multiple states, the Florida legislature and the Department of Banking and Finance should seriously consider taking these further steps towards uniformity in federal-state and multistate securities registration exemption requirements.