Developments in Florida Corporate Law and Securities Regulation

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The author traces and analyzes some of the more important judicial and legislative developments in the areas of corporate law and securities regulation occurring during the survey period. Among the topics discussed are the enactment of the Florida General Corporation Act, interpretive decisions on venue, corporate amenability to long-arm jurisdiction, the rights and responsibilities of corporate management, the rights of shareholders, shareholder derivative actions, voluntary dissolution, the enactment of the Investor Protection Act and related interpretations of the Division of Securities, the interface between federal and state securities law, and the anti-fraud and remedial provisions of the Florida Sale of Securities Law.

* The survey period includes legislation during the 1976 and 1977 sessions of the Florida Legislature and judicial decisions recorded from 311 So. 2d through 349 So. 2d, 512 F.2d through 561 F.2d and 391 F. Supp. through 436 F. Supp., inclusive.

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I. CORPORATE LAW

A. *New Legislation*

The Florida General Corporation Act which took effect on January 1, 1976,[1] was subject to limited revision and clarification in the 1976 and 1977 legislative sessions. The 1976 amendments[2] revised and clarified certain sections of the Act by: (1) eliminating the distinction between a resident agent for service of process and a registered agent;[3] (2) authorizing a corporation to serve as a general partner or as a limited partner of a limited partnership;[4] (3) providing that the defense of ultra vires does not render a corporate encumbrance of real or personal property invalid;[5] (4) allowing the reservation of a corporate name to be renewed;[6] (5) permitting the use of a promissory note in payment for shares of capital stock;[7] (6)

1. FLA. STAT. §§ 607.001-.414 (1975). *See also* FLORIDA CONTINUING LEGAL EDUCATION, BASIC CORPORATE PRACTICE (1977).

2. 1976 Fla. Laws, ch. 76-209 (current version at FLA. STAT. §§ 607.011-.371 (1977)).

3. *Id.* §§ 1, 5 & 20 (current version at FLA. STAT. §§ 48.091, 607.034 & .361(4) (1977)).

4. *Id.* § 2 (current version at FLA. STAT. § 607.011(2)(n) (1977)).

5. *Id.* § 3 (current version at FLA. STAT. § 607.021 (1977)).

6. *Id.* § 4 (current version at FLA. STAT. § 607.027(1) (1977)).

7. *Id.* § 6 (current version at FLA. STAT. § 607.054(6) (1977)). As revised, this section provides that "[f]uture services shall not constitute payment or part payment of issuance of shares of a corporation." *Id.* Previously, this section provided that "[n]either promissory notes nor future services shall constitute payment or part payment for the issuance of shares of a corporation." FLA. STAT. § 607.054(6) (1975). Presumably, therefore, promissory notes may be utilized to acquire non-assessable shares of capital stock in a Florida corporation. It should be noted, however, that shares of stock with par value must be issued for consideration "having a value not less than the par value of the shares issued." FLA. STAT. § 607.054(1) (1977). In comparison, shares of capital stock without par value "may be issued for such consideration as is determined from time to time by the Board of Directors." *Id.* § 607.054(2). It may be, therefore, that non-assessable par value shares may not be issued for promissory notes except to the extent that the total consideration exceeds the par value. *But see* Lundquist v. Gulfshore Television Corp., 328 So. 2d 202 (Fla. 2d Dist. 1976). In such a case only the par value amount would have to be paid in cash or other property and the excess amount could be paid by promissory note. With repect to no par value stock, the board of directors should be able to determine that a promissory note is sufficient consideration to issue such stock as fully paid and non-assessable. *See, e.g.*, 11 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS, §§ 5182-98 (rev. perm. ed. 1971); Speakman v. Bernstein, 59 F.2d 52 (5th Cir. 1952); Cahall v. Lofland, 12 Del. Ch. 299, 114 A. 224 (1921).

In determining whether a promissory note may be received for the issuance of non-assessable par value capital stock, it is important to remember that the authority of the board of directors is not to determine what consideration may be received but, rather, the value of the consideration. For this reason, it is suggested that if it is desirable to utilize a promissory note in connection with the issuance of capital stock of a Florida corporation, then either no par value stock should be utilized or capital stock having a minimal value (e.g., one cent per share) should be utilized and the purchase price of the stock established in excess of par value. In the latter case, the acquiring stockholder can purchase his shares by cash payment equal in par value plus a promissory note for the balance. This would result in a minimum amount of a paid-in capital (the cash payment) and a maximum amount of paid-in surplus (the note payments).

broadening the right of access to the corporate books and records to those persons who have held one-quarter of one percent of the shares of capital stock of a company for at least six months;[8] (7) requiring the filing of one set of articles of incorporation and articles of dissolution rather than in duplicate;[9] (8) permitting, rather than requiring, a copy of the articles of merger or consolidation to be recorded in the public records for purposes of clarifying the chain of title to corporate real property;[10] (9) requiring a foreign surviving or new corporation in a merger or consolidation to obtain an authorization to do business as a foreign corporation only if it intends to transact business in the state and, in all cases, requiring it to file an undertaking with the Department of State that it will promptly pay to dissenting shareholders of a Florida corporation which is the subject of the merger or consolidation the amounts to which they are entitled under the Act;[11] (10) providing that voluntary dissolution proceedings may be revoked only prior to the filing of the articles of dissolution by the Department of State;[12] (11) clarifying the provisions establishing proceedings to liquidate the assets and business of a Florida corporation by specifically stating that such proceedings do not affect the enforceability of recorded and perfected security interests, mortgages and liens on corporate real and personal property and the rights of persons in possession of such property;[13] (12) establishing that the acts of a majority of the board of trustees of a corporation in dissolution constitute the acts of the board and providing for a means of conclusively establishing authority to act by the board;[14] (13) clarifying the procedure for a foreign corporation to do business in the state under a name other than its corporate name;[15] (14) expressly setting forth that the failure of a foreign cor-

8. 1976 Fla. Laws, ch. 76-209, § 7 (current version at FLA. STAT. § 607.157(4) (1977)). Previously, any stockholder who had been such for a period of at least six months had the right to inspect the books and records of account, the minutes of meetings and records of stockholders. Presumably, no change in prior Florida case decisional law will occur regarding the additional rights of stockholders to audit the books and records of Florida corporations for proper purposes. *See, e.g.*, Sage v. Perrone, 313 So. 2d 461 (Fla. 3d Dist. 1975).

9. 1976 Fla. Laws, ch. 76-209, §§ 8, 11 & 13 (current version at FLA. STAT. §§ 607.161, .251(2)(a) & .267(1) (1977)).

10. *Id.* § 9 (current version at FLA. STAT. § 607.224(3) (1977)).

11. *Id.* § 10 (current version at FLA. STAT. § 607.234(1) (1977)). Previously, the surviving or new foreign corporation had to file additional undertakings with the Department of State that it could be served with process in Florida in any proceeding for the enforcement of any obligation of the domestic corporation which was a party to the merger or consolidation and an irrevocable appointment of the Secretary of State as its agent to accept such service of process.

12. *Id.* § 12 (current version at FLA. STAT. § 607.261(1) (1977)).

13. *Id.* § 14 (current version at FLA. STAT. § 607.284 (1977)).

14. *Id.* § 15 (current version at FLA. STAT. § 607.304(4) (1977)).

15. *Id.* § 16 (current version at FLA. STAT. § 607.314 (1977)).

poration to obtain authority to transact business in the state does not impair the validity of any deeds, mortgages, security interests and liens as well as any contracts or other acts of the corporation;[16] (15) requiring that the name and mailing address of each director be included in the annual report;[17] (16) empowering the Department of State to promulgate rules to carry out its duties and functions under the Act;[18] and (17) making editorial and clarifying revisions to certain sections without substantive change.[19]

The 1977 session passed a reviser's bill to conform certain sections of the act to bracketed words and phrases editorially inserted or substituted in the interest of clarity in the 1975 Florida Statutes and its 1976 Supplement.[20] In addition, effective January 1, 1978, the fee for filing the corporate annual report has been increased from five dollars to ten dollars.[21]

B. *Recent Decisions*

1. VENUE

In general, actions against Florida corporations may be brought only in the county in which the corporation has or usually keeps an office for the transaction of its customary business, where the cause of action accrued or where the property which is the subject matter of the litigation is located. On the other hand, actions against foreign corporations doing business in the state are properly brought in the county where the corporation has an agent or other representative, where the cause of action accrued or where the property which is the subject matter of the litigation is located.[22]

When an action is filed against two or more defendants residing in different counties, the action may be brought in any county in which any defendant resides.[23] Of course, a Florida corporation may have more than one office for the transaction of its customary business and a foreign corporation may have agents and representatives in more than one county in Florida. Therefore, corporations may have more than one "residence."[24] In *Walt Disney World Co. v.*

16. *Id.* § 18 (current version at FLA. STAT. § 607.354(2) (1977)).
17. *Id.* § 19 (current version at FLA. STAT. § 607.357(1)(f) (1977)).
18. *Id.* § 21 (current version at FLA. STAT. § 607.371 (1977)).
19. *Id.* §§ 13, 17 (current version at FLA. STAT. §§ 607.267, .337 (1977)).
20. 1977 Fla. Laws, ch. 77-174.
21. FLA. STAT. § 607.361(2) (1977).
22. *Id.* § 47.051. The election of venue is with the plaintiff and the burden of pleading and proving that venue is improper is upon the defendant. *See, e.g.,* Florida Forms, Inc. v. Barkett Computer Serv., Inc., 311 So. 2d 730 (Fla. 4th Dist. 1975).
23. FLA. STAT. § 47.021 (1977).
24. *See, e.g.,* Enfinger v. Baxley, 96 So. 2d 538 (Fla. 1957).

Leff,[25] the plaintiff filed a personal injury action against the corporate defendant, Disney, and its corporate insurer in Broward County, Florida. Disney, a foreign corporation, had only one "residence" which was located in Orange County, Florida, while the corporate insurer, also a foreign corporation, had "residences" in both Orange and Broward Counties. Nevertheless, the District Court of Appeal, Fourth District, held that the plaintiff's right to institute the litigation in Broward County against multiple defendants pursuant to the venue statute was not applicable inasmuch as this section applied only when the co-defendants resided in different counties.[26] When all of the defendants in an action had residences in one county, the section did not apply even though one or more corporate co-defendants resided in other counties. In so holding, the court relied on the rationale and decisions of the Supreme Court of Florida and the District Courts of Appeal for the Second and Third Districts in a number of similar cases.[27] In addition, the court rejected an argument of the plaintiff that Disney was actively doing business in Broward County by virtue of its advertisements and solicitations of business throughout Florida and, therefore, that venue was proper in Broward County. In so ruling, the court rejected, as dicta, the comment of the supreme court in *Mann v. Goodyear Tire & Rubber Co.,*[28] that where a foreign corporation is doing business may be relevant even though that fact is not within the statutory standard.

2. LONG-ARM JURISDICTION

The principal long-arm statutes available to a plaintiff against a foreign corporation are found in sections 48.181(1) and 48.193(1)(a) of the Florida Statutes (1977). Essentially, they provide that a foreign corporation which operates, conducts, engages in or carries on a business or business venture in Florida or has an office or agency in the state subjects itself to the jurisdiction of Florida courts for any cause of action arising out of the transaction or operation of such activity.[29] In addition, section 48.181(3) of the Florida Statutes (1977) provides that any corporation which sells, consigns

25. 323 So. 2d 602 (Fla. 4th Dist. 1975).

26. *Id.*

27. *Id.* at 604 and the cases cited therein; Cadillac Fairview Corp. v. SWD Inv., Inc., 343 So. 2d 933 (Fla. 3d Dist. 1977); Warren Bros. Co. v. Joslin, 338 So. 2d 855 (Fla. 3d Dist. 1976).

28. 300 So. 2d 666, 668 (Fla. 1974). "We conclude that, when suing a foreign corporation, one has the right to bring one's action anywhere business is transacted in Florida . . . ." *Id.*

29. *Compare* FLA. STAT. § 48.181(1) (1977) *with* FLA. STAT. § 48.193 (1)(a) (1977).

or leases tangible or intangible personal property through brokers, jobbers, wholesalers or distributors to any person in the state is conclusively presumed to be operating, conducting, engaging in or carrying on a business venture in the state, even though such conduct may not constitute carrying on of business for purposes of section 48.181(1).[30]

During the survey period a number of courts reaffirmed that, for purposes of section 48.181(1), the plaintiff has the burden of proving facts which clearly justify, as a matter of law, that substituted service of process pursuant to the statute was proper.[31] Similarly, the courts held that the burden of proof for the jurisdictional purposes of section 48.193(1) was also on the plaintiff.[32]

During the survey period, a federal district court ruled that the similarity between language contained in sections 48.181(1) and 48.193(1)(a) was such that judicial interpretation regarding what constituted doing business for purposes of either statute should be the same. In *Escambia Treating Co. v. Otto Candies, Inc.*,[33] the court found that the language of section 48.193(1)(a) was identical to the language of section 48.181(1), and, therefore, the Florida state courts would give the language contained in the former the same construction as the language in the latter had been given by the earlier decisions.[34] The court further noted that the comment in *Youngblood v. Citrus Associates of the New York Cotton Exchange, Inc.*,[35] to the effect that the statute requires more activity or contact than was currently required by the decisions of the Supreme Court of the United States, has been supported by a recent federal decision,[36] notwithstanding earlier decisions which suggested that section 48.181(1) should be interpreted as coextensive with the limits of constitutional due process.[37]

30. *See* Dinsmore v. Martin Blumenthal Assoc., 314 So. 2d 561, 564 (Fla. 1975) (construing FLA. STAT. §§ 48.181(1) & (3) (1975)).

31. *See, e.g.*, Palmer Johnson Yachts v. Ray Richard, Inc., 347 So. 2d 779 (Fla. 3d Dist. 1977); Chase Manhattan Bank, N.A. v. Banco Del Atlantico, 343 So. 2d 936 (Fla. 3d Dist. 1977).

32. *See, e.g.*, Palmer Johnson Yachts v. Ray Richard, Inc., 347 So. 2d 779 (Fla. 3d Dist. 1977); Simboli v. Miller, 326 So. 2d 251 (Fla. 3d Dist. 1976); Georgia Sav. & Loan Serv. Corp. v. Delwood Estates, Inc., 315 So. 2d 237 (Fla. 1st Dist. 1975), *cert. denied*, 341 So. 2d 236 (Fla. 1976). For an excellent summary of the procedural aspects of challenging long-arm service of process, see Elmex Corp. v. Atlantic Fed. Sav. & Loan Assoc., 325 So. 2d 58, 61-62 (Fla. 4th Dist. 1976).

33. 405 F. Supp. 1235 (N.D. Fla. 1975).

34. *Id.* at 1236.

35. 276 So. 2d 505, 507-08 (Fla. 4th Dist. 1973). *See also* American Baseball Cap, Inc. v. Duzinski, 308 So. 2d 639 (Fla. 1st Dist. 1975).

36. 405 F. Supp. at 1236. *See also* Note, *In Personam Jurisdiction—Due Process and Florida's Short "Long-Arm,"* 23 U. FLA. L. REV. 336 (1971).

37. *See* Babson Bros. Co. v. Allison, 298 So. 2d 450 (Fla. 1st Dist. 1974); Fischer v.

Disputes regarding the reach of Florida's long-arm statute principally centered around two aspects of the statute: first, on a case by case basis, what acts constitute "doing business" in Florida for purposes of sections 48.181(1) and 48.193; and second, what degree of control over the property of a distributor is necessary for a finding that a foreign corporation is doing business in Florida under the same sections.

In *Dinsmore v. Martin Blumenthal Associates*,[38] the Supreme Court of Florida discussed both aspects of "doing business" in Florida. The plaintiff, a broker, sued the individual nonresident defendants to recover a brokerage commission resulting from the exchange of stock of a foreign corporation with a Florida corporation. In effecting the exchange, the negotiations and closing of the transaction occurred outside of Florida and on only one occasion did any of the individual nonresident defendants come to Florida for a meeting with an officer of the Florida corporation. In finding section 48.181(1) inapplicable, the court noted that the plaintiff failed to show that the defendants were conducting a general course of business activity in Florida and held that a nonresident's mere giving of a listing to sell stock in a foreign corporation to a brokerage firm which does business in Florida does not indicate a general course of business activity.[39]

The court further analyzed the case to determine whether or not section 48.181(3) could be applied on the basis that the nonresidents sold personal property by means of a broker located in Florida. First, the court ruled that an exchange of securities falls within the ambit of a sale of personal property for purposes of the Act.[40] Next, the court held that the prior decisions of lower courts regarding the need for control of the property or of the broker in disposing of the property in Florida should be adopted and applied in this case.[41] Applying this standard, the court found that the listing of the securities for sale with the broker by the nonresident defendants indicated the requisite control over the activities of the broker inasmuch as the ownership of the securities remained with the nonresident defendants and, therefore, they could exercise such discretion as

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Premiere Realty Co., 298 So. 2d 447 (Fla. 1st Dist. 1974).

38. 314 So. 2d 561 (Fla. 1975).

39. *Id.* at 564.

40. *Id.*

41. *Id.* at 564-66 (citing with approval Talcott v. Midnight Publishing Corp., 427 F.2d 1277 (5th Cir. 1970); Jenkins v. Fawcett Publications, Inc., 204 F. Supp. 361 (N.D. Fla. 1962); Cook-Waite Lab., Inc. v. Napier, 166 So. 2d 675 (Fla. 2d Dist. 1964); Fawcett Publications, Inc. v. Brown, 146 So. 2d 899 (Fla. 2d Dist. 1962); Fawcett Publications, Inc. v. Rand, 144 So. 2d 512 (Fla. 3d Dist. 1962)).

they wished in the disposition of the securities in Florida.[42] Finally, however, the court found that the securities were not sold "in the state" as the closing of the transaction occurred elsewhere. The court held that if the signing of the agreement for sale and the closing took place outside the state of Florida, section 48.181(3) could not be invoked to submit the nonresident defendants to the jurisdiction of the Florida courts.[43]

The decision of the supreme court in *Dinsmore* is neither surprising nor striking. Other than the holding that an exchange of securities constitutes a sale of property, the case did not "plow any new ground" in this area of the law. Rather, the court followed a preexisting line of lower court decisions and confirmed the comment of the Fourth District in *Youngblood* that more activity and contact are required in Florida to sustain "long-arm" service of process than are currently required by the decisions of the Supreme Court of the United States.[44]

A number of other courts followed the letter and spirit of *Dinsmore*. For example, in *Spencer Boat Co. v. Liutermoza*,[45] the Fifth Circuit held that section 48.181(1) was not broad enough to "long-arm" nonresident defendants who had purchased a pleasure boat while visiting Florida and who had refused to pay a bill for repair work done in Florida which was mailed to their residence out of state. The court noted that the Florida courts have consistently held that the nonresident defendant must be seeking pecuniary benefit in Florida in order to bring his conduct within the ambit of section 48.181(1) and that, absent the availability of section 48.193(1)(g) (regarding breaches of contract in this state by failure of performance of acts required to be performed in the state), such transactions did not constitute doing business within the meaning of section 48.181(1).[46] Similarly, in *Elmex Corp. v. Atlantic Federal Savings & Loan Association*,[47] the District Court of Appeal, Fourth District, held that the single isolated act of a nonresident defendant shipping merchandise from Texas to the plaintiff in Florida did not constitute "doing business" in Florida so as to invoke the application of section 48.181(1). The decision of the same court in

42. 314 So. 2d at 566.

43. *Id.* at 567.

44. Youngblood v. Citrus Assocs. of the N.Y. Cotton Exch., 276 So. 2d 505, 508 (Fla. 4th Dist. 1973).

45. 498 F.2d 332 (5th Cir. 1974).

46. *Id.* at 333 (construing FLA. STAT. § 48.193(1) (1973)).

47. 325 So. 2d 58, 63 (Fla. 4th Dist. 1976); *accord*, Radlin v. Aero Sys., Inc., 340 So. 2d 1260, 1261 (Fla. 3d Dist. 1976).

Buckingham v. Atlas Aircraft Corp,[48] represents an application of the same basic principle as applied in *Elmex* to the opposite factual situation. In *Buckingham,* the court found that the nonresident corporate defendant was in the regular commercial business of selling aircraft manufactured in Florida. The defendant received title to many of the aircraft in Florida, took delivery in Florida, procured pilots to fly the aircraft to Colorado and, on occasion, brought customers to Florida to pick up the aircraft they had purchased. The court noted that while no single one of these activities or events alone would be sufficient to subject the nonresident corporate defendant to the jurisdiction of the Florida courts, their combination "irresistibly establishes a pattern of 'doing business' "[49] in Florida for purposes of a suit arising out of injuries sustained in an air crash in Alabama while plaintiff was aboard one of the aircraft owned by the nonresident corporate defendants.

In two companion cases, both styled *Beckham v. Holborn,*[50] the District Court of Appeal, First District, ruled that a nonresident individual and corporate defendant were not subject to service of process under section 48.181 even though the individual defendant was found to be a participant in the unlawful sale of unregistered securities and subject to the remedial provisions of section 517.21(1).[51] In these cases, the court affirmed the trial court's finding that there was insufficient evidence to show that the corporate defendant conducted business or a business venture in Florida with respect to the sale of its stock to the plaintiff. Thus it held that a cause of action would not lie against the individual defendant as a participant who aided the corporate defendant to make the sale.[52] Review of the summary facts set forth in the opinion suggests that the only activity of the corporate defendant in Florida was the sale of its securities as an issuer. Furthermore, it appears that the court was impressed by the corporate defendant's acceptance of plaintiff's check in payment of the stock while in Florida on other business and delivery of the stock certificate to the plaintiff in Florida, also while on other business. The court seemed to conclude therefore, that

48. 343 So. 2d 654 (Fla. 4th Dist. 1977).

49. *Id.* at 656; *accord,* Washington Star Syndicate, Inc. v. Wright, 313 So. 2d 444 (Fla. 3d Dist. 1975). The contract, which was the subject of the action, was entered into in Florida, the products produced in Florida and the nonresident corporate defendant considered itself a joint venturer in Florida for the purpose of producing the products. *See also* International City Bank & Trust Co. v. Forest Shores, Inc., 340 So. 2d 530 (Fla. 1st Dist. 1976).

50. 330 So. 2d 101 (Fla. 1st Dist. 1976); 332 So. 2d 682 (Fla. 1st Dist. 1976), *cert. denied,* 345 So. 2d 423 (Fla. 1977).

51. 332 So. 2d at 682-83 (construing FLA. STAT. §§ 48.181 & 517.21(1) (1975)).

52. 330 So. 2d at 102.

there was sufficient evidence to support the trial court's decision that the plaintiff had not sustained his burden of showing that the corporate defendant conducted a business or business venture in Florida.[53]

In the discussion in both opinions, the factual circumstances surrounding the conduct of the corporate defendant, as an issuer of securities, are insufficient to determine the extent of the offering in Florida. Nevertheless, assuming that the plaintiff was the only offeree and/or purchaser of the securities located in Florida and that all negotiations took place in Florida, then the sale of the stock was certainly completed upon the payment and delivery of the shares which admittedly took place in Florida. Therefore, even if the court found that this isolated sale to a Florida resident by the corporate defendant through the services of its president (the individual defendant) did not constitute "doing business" in Florida, it would seem to constitute the sale of personal property by means of an agent "in this state" within the meaning of section 48.181(3) thereby subjecting both the agent and his principal to the jurisdiction of the Florida courts.[54] Finally, the opinions of the court in both cases leave unanswered the interesting question of whether an issuer may violate the registration provision[55] and/or anti-fraud provision[56] of Florida securities law without subjecting itself to service of process for doing business in this state under sections 48.181(1) or 48.193(1)(a). While it is conceivable that a court could so rule (and the District Court of Appeal, First District, seems to have so ruled in this case), as a practical matter it is inconceivable that a foreign issuer, who, through corporate agents or broker-dealers, violates the registration and/or anti-fraud provisions of the Florida securities law, should not subject itself and its agents to service of process in Florida pursuant to the provisions of sections 48.181(1) or 48.193(1)(a).[57]

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53. *Id.*

54. *See, e.g.*, Radlin v. Aero Sys., Inc., 340 So. 2d 1260 (Fla. 3d Dist. 1976). Since the defendant's contracts in Florida were for his pecuniary benefit, the court refused to dismiss for lack of jurisdiction.

55. FLA. STAT. § 517.07 (1977), *repealed by* 1976 Fla. Laws, ch. 76-168, § 3, *effective* July 1, 1980.

56. *Id.* § 517.301, *repealed by* 1976 Fla. Laws, ch. 76-168, § 3, *effective* July 1, 1980.

57. The Florida Sale of Securities Law, *Id.* §§ 517.01-.33, provides that no securities may be offered or sold "within this state" unless the securities have been registered or an exemption from registration is available. *Id.* § 517.07. Furthermore, the anti-fraud provisions of the act provide that it is a violation of the provisions of the act for any person, in connection with the purchase or sale of any security "in this state," to engage in certain manipulative and deceptive practices. *Id.* § 517.301(1). The question is, therefore, whether an issuer's conduct can invoke the substantive provisions of the Florida Sale of Securities Law (sell securities "within" or "in" Florida) without, as a matter of law, operating, conducting, engaging in or

With respect to the requirement that the nonresident defendant exercise control over the product or distributor located in Florida, engrafted on to the statute by case law, the supreme court in *AB CTC v. Morejon*[58] restated its holding in *Dinsmore* and held that a nonresident defendant must be shown to exercise control over the brokers, jobbers, wholesalers or distributors or control over the personal property in the hands of these persons before that defendant will be held to be doing business in Florida for purposes of sections 48.181(1) or 48.181(3).[59] In this case the corporate defendant, AB CTC, a Swedish corporation, was the subject of an action by the plaintiff for personal injuries alleged to have been caused by the negligent manufacture of a washing machine sold by the defendant to an independent distributor, who in turn sold it to the plaintiff. In finding that there was insufficient proof to show the requisite control, the court noted that while "a parent company has 'control' over a subsidiary, a manufacturer does not necessarily have 'control' over a sole distributor."[60] Therefore, absent further proof regarding control over the product or the distributor, the burden had not been carried and the cause was dismissed as against the corporate defendant.[61]

The language of the court noting that "a parent company ha[d] 'control' over a subsidiary" seems to indicate that, as a matter of law, where the subsidiary acted as the distributor, broker, jobber or wholesaler, the parent would be held to have sufficient control for purposes of subjecting it to long-arm jurisdiction. This inference was quickly rejected by the District Court of Appeal, First District, in *Volkswagenwerk A.G. v. McCurdy*,[62] where the court held that the fact that the American subsidiary of Volkswagenwerk was wholly owned by the parent was insufficient, in and of itself, to overcome the prima facie showing made by the foreign corporate defendant that it was not otherwise doing business in Florida. The

carrying on a business or business venture in Florida. In Radlin v. Aero Sys., Inc., 340 So. 2d 1260 (Fla. 3d Dist. 1976), the district court seemed to indicate that it could not. In Dinsmore v. Martin Blumenthal Assocs., 314 So. 2d 561 (Fla. 1975), the Supreme Court of Florida also seemed to indicate that an isolated offer and sale to one Florida resident would not constitute doing business in Florida by the issuer for purposes of §§ 48.181(1) or 48.193(1)(a). The supreme court, however, left the inference that such activity would subject the issuer and its "brokers" to service of process on the basis of § 48.181(3). *See* FLA. STAT. §§ 517.02(4), (5) & (7) (1977) (defining a dealer, issuer, and broker). In essence, the argument could be made that, for service of process under § 48.181(3), a broker should include persons who would be deemed dealers, brokers and issuers under Florida securities law.

58. 324 So. 2d 625 (Fla. 1975).

59. *Id.* at 627.

60. *Id.*

61. *Id.*

62. 340 So. 2d 544 (Fla. 1st Dist. 1976).

court stated that only when the plaintiff could show that the parent corporation exercised such a degree of control over its subsidiary that the activities of the subsidiary were in fact the activities of the parent within Florida was substituted service of process by use of section 48.181 applicable.[63] This decision accords with the prior ruling by the United States District Court for the Southern District of Florida in *Hitt v. Nissan Motor Co.*[64] The court there found that the Japanese parent exercised sufficient control over its American subsidiary in the sale of Datsun automobiles so that the parent was indeed doing business in Florida for purposes of section 48.181 in connection with the alleged violations of various federal antitrust laws.[65] In so ruling, the court considered the degree of control exercised in fact by the parent over the subsidiary to be significant; the exchange of officers and employees between the parent and subsidiary and the common directors of the companies. In addition, the contractual arrangement between the parent and subsidiary with respect to the distribution of the parent's motor vehicles was deemed significant in finding that the parent was doing business in Florida.[66]

3. PROFESSIONAL RESPONSIBILITY

The District Court of Appeal, Third District, reaffirmed in two cases the principle first announced in *Investment Corp. of Florida v. Buchman*[67] that, absent (i) conduct which would furnish evidence leading to an inference of fraud or (ii) a contractual relationship or its equivalent with the party plaintiff, accountants cannot be held liable in preparing financial statements even though they are aware that the financial statements will be used and relied upon by third parties. Ordinary negligence, absent such a contractual relationship or its equivalent, is not sufficient to impose liability.[68] First, in

63. *Id.* at 546.

64. 399 F. Supp. 838 (S.D. Fla. 1975).

65. *Id.* at 845-46, 850-52.

66. *Id.* at 845-46. *See also* International City Bank & Trust Co. v. Forest Shores, Inc., 340 So. 2d 530, 532-33 (Fla. 1st Dist. 1977).

67. 208 So. 2d 291 (Fla. 2d Dist. 1968).

68. *Id.* at 293-96. In the *Buchman* case the District Court of Appeal, Second District, relied on the holdings of the New York Court of Appeals in State Street Trust Co. v. Ernst, 278 N.Y. 104, 15 N.E.2d 416 (1938), and in Ultramares Corp. v. Touche Ross & Co., 255 N.Y. 170, 174 N.E. 441 (1931).

It should be noted that *Buchman* did not involve a claim under the Florida securities law. Therefore, assuming that the negligent preparation of financial statements in connection with the sale of securities might constitute a violation of FLA. STAT. § 517.301(1) (1977) (*see* note 56 *supra*), the question remains unanswered whether such conduct by the professional would constitute participation or aiding in making the sale of securities sufficient to establish

Dubbin v. Touche Ross & Co.,[69] the court held that the stockholders of a corporation are not third party beneficiaries to the contract for services between that corporation and its accountants. Specifically, the court held that the stockholders' efforts to have their securities registered with the Securities and Exchange Commission, as an adjunct to the corporation's application to register securities, did not make them third party beneficiaries to the contract of professional service between the accountants and the corporation.[70] The decision in *Dubbin* was cited with approval in the subsequent case of *Mulligan v. Wallace.*[71] In *Mulligan,* the court held that officers, directors and stockholders of the corporate client as well as former corporate officers and directors are not third party beneficiaries of the contract between the corporation and the professionals; absent some specific evidence supporting a contract or agreement between the plaintiffs and the accountants, no liability attached to the accountants for errors and mistakes in the annual report prepared by the accountants as experts and filed with the Securities and Exchange Commission.[72] None of these cases expands on the rationale and reasoning of prior case law in Florida and elsewhere. Rather, the cases can be considered as the most recent progeny of a line of cases originating with *Ultramares Corp. v. Touche Ross & Co.*[73]

4. PROMOTER'S LIABILITY

As a general rule, the promoter of a corporation is personally liable on contracts entered into on behalf of the proposed corpora-

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liability against the professional under the remedial provisions of § 517.21(1) (*see* note 55 *supra*). This section provides:

> Every sale made in violation of any of the provisions of this chapter shall be voidable at the election of the purchaser; and the person making the sale and every . . . agent of or for the seller, if the . . . agent has *personally participated or aided in any way in making the sale,* shall be jointly and severally liable to the purchaser . . . .

Id. (emphasis added).

69. 324 So. 2d 128 (Fla. 3d Dist. 1975).

70. *Id.* at 129.

71. 349 So. 2d 745 (Fla. 3d Dist. 1977).

72. *Id.* at 746-47; *accord*, Nortek, Inc. v. Alexander Grant & Co., 532 F.2d 1013 (5th Cir. 1976). In *Nortek,* the Fifth Circuit specifically relied on the holding of Judge Cardozo in Ultramares Corp. v. Touche Ross & Co., 255 N.Y. 170, 171 N.E. 441 (1931) and State Street Trust Co. v. Ernst, 278 N.Y. 104, 15 N.E. 2d 416 (1938) as adopted in Investment Corp. v. Buchman, 208 So. 2d 291 (Fla. 2d Dist. 1968).

73. 255 N.Y. 170, 174 N.E. 441 (1931). The New York Court of Appeals held that in a negligence action brought against accountants to recover losses suffered in reliance upon their certified audit, accountants will be liable for fraudulent representations. The duty to make the certificate without fraud extends to investors to whom the accountant's employer exhibits the certificate. Liability for mere negligence, however, is governed by contract and is to be enforced between the parties by whom the contract has been made.

tion, absent a specific understanding that the other party will look only to the corporation upon formation. The promoter's liability is said to be original and primary because the promoter, at the time of the contract, has no principal.[74] This general rule was restated and readopted in the case of *Vodopitch v. Collier County Developers, Inc.*: "In our opinion, before the promoter may escape liability, it must be shown that the parties agree to bind the corporation alone."[75] The court specifically relied on the prior decision of the Supreme Court of Florida in *Hunt v. Adams*,[76] in which it was held that a promoter was not personally liable on a written contract made for the benefit of an unincorporated charitable society when the contract on its face clearly indicated that the promoter or representative was not to be personally bound.[77]

5. DIRECTORS' AND MANAGEMENT'S RIGHTS AND RESPONSIBILITIES

The Florida General Corporation Act provides that the business and affairs of the corporation are managed under the direction of the board of directors, acting as a board, and that all corporate power is exercised by or under the authority of the board.[78] The authorities, duties and responsibilities of the officers are derived from the board of directors by means of the bylaw provisions or resolutions adopted by the board establishing the officers.[79] Most of the judicial decisions in this area interpreting the rights and responsibilities of officers and directors were rendered prior to the adoption of the General Corporation Act which became effective in 1976. Nevertheless, the prior decisions are generally in accord with the majority positions of courts of other jurisdictions under similar general corporation acts.

Directors and officers are deemed to be fiduciaries of the corporation. Thus, directors' and officers' relationships to the corporation and its shareholders is one of trust. The standard of conduct to which directors must conform is set forth in section 607.111(4) of the Florida Statutes (1977) which provides that "[a] director shall perform his duties as a director . . . in good faith, in a manner he reasonably believes to be in the best interests of the corporation, and with such care as an ordinarily prudent person in a like position

74. 1 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 215 (1974).

75. 319 So. 2d 43, 44 (Fla. 2d Dist. 1975).

76. 111 Fla. 1164, 149 So. 24 (1933).

77. Vodopitch v. Collier County Developers, Inc., 319 So. 2d 43, 45 (Fla. 2d Dist. 1975).

78. *See* FLA. STAT. § 607.111(1) (1977). For an excellent general discussion of this area of the law, see R. STRUDLER & I. HEIMBINDER, *Officers' and Directors' Responsibilities* in FLORIDA BASIC CORPORATE PRACTICE (1977).

79. FLA. STAT. § 607.151 (1977).

would use in similar circumstances."[80] As a general rule, the courts have traditionally viewed the action of the board of directors as presumptively proper, have permitted wide discretion to the directors and officers in the exercise of their best business judgment and will not substitute the judgment of the court for that of the board or management, provided that judgment of the board has been exercised in good faith for the corporate interest.[81]

Three cases were decided by the Florida appellate courts during the survey period with respect to this area of the law. First, in *Recarey v. Rader,*[82] the District Court of Appeal, Third District, without reviewing the facts, refused to appoint a receiver for the management of a hospital corporation on the petition of minority stockholders. The court stated that the appointment of a receiver is "drastic relief" which should not be utilized unless "the exigencies of the case demand it and no other protection to the applicants can be devised by the court. In other words, the appointment of [a] receiver for a going corporation is a last-resort remedy, and should not be employed when another adequate remedy is available."[83]

In contrast to the result in *Recarey,* which involved an attempt to unseat management by appointing a receiver, the District Court of Appeal, Fourth District, in *Procacci v. Solomon,*[84] permitted a corporation's president and director to purchase formerly owned corporate property from a bank which had obtained the property by foreclosing and purchasing it at the judicial sale. The court held that absent evidence of conspiracy or some malicious plan between the director and the bank, the director did not breach any fiduciary or quasi-fiduciary relationship to the corporation and its stockholders or otherwise acquire a personal advantage to the detriment of the corporation or its stockholders.[85] Without citing the case, the court obviously distinguished the factual situation in *Procacci* from *News-Journal Corp. v. Gore,*[86] in which the Supreme Court of Florida found a breach of an officer's fiduciary duty in purchasing at the foreclosure sale property of the corporation which was the subject matter of the foreclosure.[87]

80. *Id.* § 607.111(4); *see* Schein v. Caesar's World, Inc., 491 F.2d 17, 20 (5th Cir. 1974). For an excellent summary of the general state of the law regarding a director's rights and responsibilities see Subcommittee on Functions & Responsibilities of Directors, Comm. on Corporate Laws, ABA, *Corporate Director's Guidebook,* 32 Bus. Law. 5, 11-39 (1976).

81. *See* Schein v. Caesar's World, Inc., 491 F.2d 17, 20 (5th Cir. 1974).

82. 320 So. 2d 28 (Fla. 3d Dist. 1975).

83. *Id.* at 30.

84. 317 So. 2d 467 (Fla. 4th Dist. 1975).

85. *Id.* at 468; *accord,* City of Miami Beach v. Smith, 551 F.2d 1370, 1376 (5th Cir. 1977).

86. 147 Fla. 217, 2 So. 2d 741 (1941).

87. *Procacci* may be distinguished from *News-Journal* on the basis of the importance of

In *State ex rel. Blatt v. Panelfab International Corp.*,[88] the District Court of Appeal, Third District held that mandamus was not the appropriate relief for a director[89] who, having successfully defended charges against him and having received a judgment of acquittal, suffered a refusal by the corporation to indemnify him for his attorneys' fees and costs. In the absence of any allegation in the petition that the plaintiff was without adequate legal remedies at law or in equity, and because it was uncertain whether the charges resulted from conduct within the scope of plaintiff's duties as an officer,[90] plaintiff would have to resort to other legal or equitable relief.[91]

6. DISREGARDING THE CORPORATE ENTITY

As a general rule, a corporation will be looked upon as a legal entity until sufficient reason appears to the contrary. When the legal entity is used to defeat the public convenience, to justify a wrong, to protect a fraud or to defend a crime, however, the law will regard the corporation as an association of persons and "pierce the corporate veil" for the benefit of the public or third persons.[92] Furthermore, if the corporation is the mere alter ego or business conduit of an individual, the courts will also disregard it for the benefit of the public and third persons. The alter ego theory was adopted by the courts to respond to the corporate entity that has been used as a subterfuge and used to work an injustice. In order to establish the doctrine, it must be shown that the stockholders disregarded the corporate entity, making it a mere instrumentality for the transaction of their own affairs; that there is such a unity of interest and ownership that the separate personalities of the corporation or corporations and the owners no longer exist; and, that to adhere to the doctrine of corporate entity would promote injustice or protect a fraud.[93] With respect to a corporate agency or affiliate, the courts

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the purchased property to the corporation. In *News-Journal,* the property purchased by the officer was of the utmost importance to the welfare of the corporation. The supreme court found that if the officer had made efforts to purchase the property on behalf of the corporation, the corporation would have greatly benefited. In contrast, the property purchased in *Procacci* was as inherently necessary to the corporation. *See also* Etheredge v. Barrow, 102 So. 2d 660, 662 (Fla. 2d Dist. 1958).

88. 314 So. 2d 196 (Fla. 3d Dist. 1975).

89. Petitioner relied on FLA. STAT. § 608.13 (1975), providing a right of indemnification for a corporate director who was a defendant in a lawsuit arising from actions committed in his capacity as director.

90. 314 So. 2d at 196.

91. *Id.*

92. W. FLETCHER, *supra* note 74, at § 41 *et seq. See also* Edwards, *Corporate Law and Securities Regulation,* 30 U. MIAMI L. REV. 401, 405-08 (1976).

93. W. FLETCHER, *supra* note 74, at § 41. *See also* House of Koscot Dev. Corp. v. Ameri-

have applied the alter ego theory or mere instrumentality concept by requiring proof that the controlled corporation has no separate mind, will or existence of its own, but that it is rather a business conduit for its principal. Ownership of all or a majority of the stock of the corporation coupled with common management and direction does not, however, operate as a merger of the two entities. Instead, there must be some showing that the control by one corporation of another is so complete that the general rules of agency are applicable, and the controlled corporation may be deemed an agent of its principal.[94]

Two cases recently decided by Florida appellate courts have applied these general principles without variation. In both cases, the courts found that the individual stockholders had not used the corporation for a fraudulent purpose or as their alter ego and that the parent-subsidiary relationship was sufficiently independent so that the subsidiary was not a mere instrumentality of the parent. In the first case, *Computer Center, Inc. v. Vedapco, Inc.*,[95] the court found the evidence insufficient to establish that the corporate entity should be disregarded in order to prevent fraud, illegality or injustice, or that the corporation was a mere device or sham used to mislead creditors. In *Vedapco*, the corporation was owned by a husband and wife; the assets were sold two months after the plaintiff, a creditor, filed its action, and the proceeds from the sale of the assets were used to pay creditors of the corporation with the exception of the plaintiff and a stockholder who had loaned the corporation over three million dollars without receiving repayment. The court noted that the fact that the husband and wife personally guaranteed the indebtedness on the building purchased by the corporation does not, by itself, constitute a "badge of fraud."[96] Therefore, the court ruled that the plaintiff-creditor failed to carry the burden of proof necessary to warrant disregarding the corporate entity and refused to fix personal liability on the stockholders.[97]

In the second case, *Unijax, Inc. v. Factory Insurance Association*,[98] the parent corporation brought an action against the insurer of its subsidiaries to recover benefits on a business interruption insurance policy of the subsidiaries for fire loss to a paper mill

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can Line Cosmetics, Inc., 468 F.2d 64 (5th Cir. 1972); Aztec Motel, Inc. v. State *ex rel.* Faircloth, 251 So. 2d 849 (Fla. 1971).

94. *See, e.g.*, House of Koscot Dev. Corp. v. American Line Cosmetics, Inc., 468 F.2d 64, 66-67 (5th Cir. 1972).

95. 320 So. 2d 404 (Fla. 4th Dist. 1975).

96. *Id.* at 406-07.

97. *Id.* at 407.

98. 328 So. 2d 448 (Fla. 1st Dist. 1976).

owned by the subsidiaries. After discussing the general rules regarding piercing the corporate veil, the court found that there were three separate and distinct corporate entities, each of which must maintain an action to recover for its loss.[99] Inasmuch as the parent and subsidiaries were incorporated in various states, including Florida, the court, *sub judice,* used general common law principles, evident in decisions from many states, as a guide. In essence, the case provides a distillate exposition of general case law regarding parent-subsidiary relationships and, therefore, provides an excellent summary of this aspect of corporate law.[100]

Medley Harwoods, Inc. v. Novy[101] provided counsel with an opportunity to invoke a novel theory of law: the stockholders of a foreign corporation, not qualified to do business in Florida but which is doing business, are individually liable for debts incurred by the corporation in Florida. Counsel advanced the theory citing in support two supreme court cases decided in 1895 and 1896.[102] The court held, however, that the reasoning of these cases had been receded from in 1931[103] and, on the basis of the well-reasoned decision of the District Court of Appeal, Second District, in *Mysels v. Barry,*[104] held that an officer or shareholder of a foreign corporation cannot be held personally responsible for the debts of the corporation incurred in Florida solely because the corporation has failed to qualify to do business in Florida.[105] The court in *Mysels* perceived the majority rule of law to be that, in the absence of definite statutory authority, the officers, stockholders, incorporators and other persons contracting for, or on behalf of, a noncomplying foreign corporation cannot be held liable for its debts as partners. The court based its decision on statutory law then existing in chapter 613 of the Florida Statutes (1973). The court noted that chapter 613 had been repealed effective January 1, 1976 and replaced by the Florida General Corporation Act which, "on the subject of the failure of a foreign corporation to qualify, does not appear to have been substantially changed."[106]

99. *Id.* at 453-54.

100. *Id.*

101. 346 So. 2d 1224 (Fla. 3d Dist. 1977).

102. Duke v. Taylor, 37 Fla. 64, 19 So. 172 (1896); Taylor v. A. G. Branham & Co., 35 Fla. 297, 17 So. 552 (1895).

103. Herbert H. Pape, Inc. v. Finch, 102 Fla. 425, 136 So. 496 (1931).

104. 332 So. 2d 38 (Fla. 2d Dist. 1976).

105. 346 So. 2d at 1226.

106. 332 So. 2d at 39-40, n.1. *But see* FLA. STAT § 607.397 (1977) and *compare with* FLA. STAT. §§ 607.304(1), .307 (1977).

7. RIGHTS OF SHAREHOLDERS

Under the Florida General Corporation Act, a shareholder[107] has a number of specific rights. Subject to the provisions of the articles of incorporation and, in certain circumstances, the bylaws, a shareholder has the right to exercise his vote for all matters on which shareholders are entitled to vote,[108] to receive dividends if declared by the board of directors,[109] to inspect the books and records of the corporation at reasonable times for proper purposes,[110] to receive a certificate evidencing the shares of the corporation of which he is the owner,[111] to exercise a vote with respect to mergers and consolidations,[112] and, upon the sale of the assets of the corporation, or upon a merger or consolidation, to exercise rights of dissent and appraisal.[113] Furthermore, the case law provides a shareholder with certain additional and supplementary rights.[114]

In *Applied Digital Data Systems, Inc. v. Milgo Electronic Corp.*,[115] the Southern District of New York, applying Florida law, found that the right of inspection and access to the shareholder list of a Florida corporation is governed by the Florida General Corporation Act and is expressly limited to stockholders.[116] Thus the plaintiff corporation, which was making a tender offer to acquire common stock of the defendant, a Florida corporation, was held not to be legally entitled to the shareholder list because it was not a stockholder. Nevertheless, the district court granted a mandatory injunction ordering the defendant to turn over this list so that the plaintiff could directly solicit the stockholders. The court rested its decision on the view that the federal securities laws expressed a congressional concern that both the offeror and management have an equal opportunity to present their cases to the public stockholders who are

107. FLA. STAT. § 607.004(6) (1977) which defines a "shareholder" or "stockholder" as the holder of record of shares in a corporation.

108. *See Id.* §§ 607.091, .094, .097, .101, .114 & .117.

109. *See Id.* § 607.137.

110. *See Id.* § 607.157.

111. *See Id.* § 607.067.

112. *See Id.* § 607.221.

113. *See Id.* §§ 607.241, .244 & .247.

114. *See, e.g.*, Florida Tel. Corp. v. Peninsular Tel. Co., 111 So. 2d 677 (Fla. 1st Dist. 1959) (the statutory right of inspection of books and records of private corporations given to stockholders does not abridge the right of the stockholder as it existed at common law to exercise this prerogative, but rather enlarges and extends the right by removing some of the common law limitations). This case was decided under preexisting FLA. STAT. ch. 608 and presumably is still applicable under FLA. STAT. ch. 607 (1977). *See also* Fussell v. McLendon, 109 So. 2d 783 (Fla. 3d Dist. 1959); Liebman v. Pinks, 136 So. 2d 645 (Fla. 3d Dist. 1962).

115. 425 F. Supp. 1163 (S.D.N.Y. 1977).

116. *Id.* at 1164.

confronted by a cash tender offer.[117]

In dealing with areas of shareholders' rights to disclosure of material information in connection with the purchase and sale of securities, counsel normally looks first to the anti-fraud provisions of federal and state securities laws. Two cases during the survey period, however, passed on this issue and reached opposite conclusions without invoking the provisions of either federal or Florida securities law. In *Morton v. Young*,[118] the plaintiff appealed an adverse judgment in an action for rescission of a contract on the basis of fraud, alleging that the defendant offered to sell him unregistered stock in a Florida corporation on the representation that the stock would be registered no later than approximately a year and one-half. Plaintiff purchased the shares and over a year later the defendant informed him that the shares would not be registered. The trial court found that the transaction was at arm's length; that the plaintiff did not have the right to rely on the oral promise of the defendant to have the stock registered; that the plaintiff was an experienced businessman, although not an "astute stock manipulator" who had not consulted the accountants, lawyers and stockbrokers whom he had available; and, that the plaintiff knew that the defendant was not the majority holder of the stock in the corporation. The court, therefore, found that the facts did not show either the existence of a confidential relationship or justifiable reliance on the representation of the defendant, and the plaintiff could not invoke the equitable remedy of rescission based on fraud.[119]

Morton v. Young presents an excellent summary of Florida decisional law regarding the elements of a cause of action which must be proved in order to establish the right to rescind a contract when there is a material misrepresentation of fact or breach of a confidential relationship between the parties. Furthermore, because the case is well written and well reasoned, it provides an excellent rationale on the import and necessity of the anti-fraud provisions of federal and Florida securities law.[120]

117. *Id.* at 1165. The court attached, as an appendix to its opinion, a letter subsequently received from the general counsel for the Securities and Exchange Commission regarding an inquiry whether it was the position of the Securities and Exchange Commission that a federal court may order a company to provide a tender offeror for that company's shares with a list of the company's shareholders. Essentially, the general counsel indicated that the Commission was then contemplating amendments to the regulations under the Williams Act by means of providing a new Rule 14e-1 under section 14 of the Securities Exchange Act of 1934 which would impose such a requirement on the company. Nevertheless, it was the Commission's position that the inherent equity powers of the court would allow the court to make such an order irrespective of the adoption of Rule 14e-1, as proposed.

118. 311 So. 2d 755 (Fla. 3d Dist. 1975).

119. *Id.* at 756-57.

120. *See, e.g.*, Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Byrne, 320 So. 2d 436 (Fla.

In *Watson v. Khachab*,[121] the court affirmed the entry of a judgment in favor of the plaintiff on the following findings of fact made by the trial court. Plaintiffs were the majority stockholders, officers and directors of the corporation. On the other hand, defendants were minority stockholders, of which one of them was also an officer and director. After agreeing to sell the business through a stock sale, the parties advertised the corporation for sale at a given price. The defendants, having access to all incoming calls responding to the advertisement, represented to the plaintiffs that a named individual had offered to buy the business for a lesser figure. The attorney handling the sale refused to disclose the names of the principals whom the named individual represented. In response to defendants' threats to quit the business unless the sale was confirmed to the named person on behalf of his undisclosed principals, plaintiffs agreed to sell the business to the named purchaser. Subsequent to the sale, plaintiffs discovered that the defendants were the real parties in interest and that the named person was merely a straw party used for the purpose of concealing the true interest of the defendants in the purchase. Notwithstanding the fact that the plaintiffs were officers and directors of the corporation and had knowledge of the value of the corporation's property, the trial court characterized these facts as a willful and wanton misrepresentation, made in complete disregard of the rights of the plaintiffs, which constituted a breach of defendants' trust to the plaintiffs. The court, therefore, found for the plaintiffs in the amount of their damages.[122]

The appellate court affirmed the decision, citing prior cases dealing with the presumed correctness of the findings of fact and rulings of law by a trial court. Thus, implicitly the appellate court found that, on these facts, the plaintiffs had established a case under the Florida common law of breach of a fiduciary duty and/or fraud in the inducement. To the extent that a general principle regarding shareholder rights may be extrapolated, this case may suggest the possibility that in certain circumstances there could exist a fiduciary duty of fair and honest dealing between shareholders in connection with the sale of their shares of capital stock.[123]

8. SHAREHOLDER DERIVATIVE ACTIONS

A significant decision was rendered by the Supreme Court of

3d Dist. 1977), and text accompanying notes 247 & 248 *infra*. *But see* Freud v. Gross, 345 So. 2d 1097 (Fla. 3d Dist. 1977).

121. 334 So. 2d 78 (Fla. 3d Dist. 1976).

122. *Id.* at 79-80.

123. *See generally* Morton v. Young, 311 So. 2d 755, 756 (Fla. 3d Dist. 1975).

Florida in *Schein v. Chasen*,[124] on certification of the following question from the United States Court of Appeals for the Second Circuit:

> Are investors, who sell stock on the basis of inside information about the issuer corporation which they received from a stockholder who in turn received the information from the president of the issuer corporation liable to the corporation in a shareholder derivative suit under Florida law for the profits realized by the investors on the sale of that stock?[125]

The court answered the question in the negative, holding and reaffirming that under Florida case law three conditions precedent to such an action must exist: (1) the ownership of the shares in the corporation at the time the wrong was committed;[126] (2) the directors' unjustified refusal, on plaintiff's demand, to bring suit in the corporation's behalf;[127] and (3) damage to the corporation.[128]

Three specific aspects of the case, however, bear comment. First, as dicta, the court indicated that it would "not choose to adopt the innovative ruling"[129] of the New York Court of Appeals in *Diamond v. Oreamuno*[130] which, applying New York corporate law, held that officers and directors of a corporation may be held accountable to their corporation for gains realized by them from transactions in the company's stock as a result of their use of material inside information. In essence, the court in *Diamond* found that there was a fiduciary duty owed by corporate officials to the corporation to maintain corporate information in confidence as a corporate asset.[131] As noted by the court, the application of the rule in *Diamond* to the facts in this case would have required an extension of that holding to persons other than officers and directors and specifically would have required the court to find that a similar

124. 313 So. 2d 739 (Fla. 1975) (cited in Schein v. Chasen, 519 F. 2d 453 (2d Cir. 1975)). For a detailed commentary on this case and a discussion of the interplay between state corporate law and the insider trading provisions of the Securities Exchange Act of 1934 see Comment, *Corporations: Florida Common Law Liability of Tippees in a Shareholders' Derivative Suit*, 28 U. FLA. L. REV. 223 (1975).

125. 519 F.2d 453, 454-55 (2d Cir. 1975). The Second Circuit also certified the question whether the stockbroker who relayed the material information from the president to the investors would be jointly and severally liable with them for the profits they would realize in a shareholders' derivative suit. *See* 313 So. 2d at 739-40. By virtue of the court's expansive holding, this question was also answered in the negative without the necessity of a direct statement.

126. *See* News-Journal Corp. v. Gore, 147 Fla. 217, 2 So. 2d 741 (1941).

127. *See* Talcott v. McDowell, 148 So. 2d 36 (Fla. 3d Dist. 1962).

128. *See* Orlando Orange Groves Co. v. Hale, 119 Fla. 159, 161 So. 284 (1935).

129. 313 So. 2d at 746.

130. 24 N.Y.2d 494, 248 N.E.2d 910, 301 N.Y.S.2d 78 (1969).

131. 313 So. 2d at 744 (citing with approval Schein v. Chasen, 478 F.2d 817, 825 (2d Cir. 1973) (Kaufman, J., dissenting)).

fiduciary duty exists and is owned by stockholders to their corporation.[132] The dicta is an unfortunate gratuity since the court apparently had previously adopted principles of liability similar to those enunciated in *Diamond*. Underlying the rejection of *Diamond* in the instant case is the court's strong adherence to the principle "that actual damage to the corporation must be alleged in the complaint to substantiate a stockholder's derivative action."[133] Perhaps in an appropriate case, a cause of action could be sustained if special corporate damages are alleged in the derivative action against an officer or director who has utilized confidential information for his own profit and/or the corporation's damage. This position finds special support in the opinion of Justice England who concurred specially with the majority.[134] In addition, the extensive quotation of the court from the reasoning of Judge Kaufman indicates that the court might rule that a derivative cause of action exists on behalf of the corporation in a case where an officer or director of the corporation uses confidential corporate information for his own enrichment at the insistence of or in conspiracy with a third party. Judge Kaufman specifically recognized the existence of such a cause of action based on section 312 of the American Law Institute's *Restatement (Second) of Agency*.[135] Nevertheless, the court will probably require the proof of special damage to the corporation.

Finally, the general tenor of the decision, and especially the extensive quotation of Judge Kaufman's remarks, seem to indicate that the court in the future will not extend substantive or procedural Florida decisional or statutory law in order to parallel the provisions of federal securities law.[136] What is left unresolved is the liberality with which the court will apply the remedial provisions of Florida securities law for the benefit of investors. Given the court's comment in *Schein*, declining to engage in "unprecedented expansive reading" of case law in order to achieve a recognized salutary benefit such as prohibiting trading on inside information, it would seem that the court will not be very "expansive" in this area either.[137]

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132. *Id.* at 746.

133. *Id.*

134. Rather than expressly reject the principle of *Diamond*, as did the majority, Justice England argued: "I would answer both certified questions in the negative on the narrow grounds (i) that Florida law requires an allegation of corporate damage as a predicate to maintenance of a shareholder's derivative suit, and (ii) that an action for civil damages must allege more than merely speculative damages." *Id.* at 747-48. *See also* Renpack, Inc. v. Oppenheimer, 104 So. 2d 642 (Fla. 2d Dist. 1958).

135. 313 So. 2d at 745.

136. *Id.* at 746 n.2.

137. *Id.* at 743. The opinion cited with approval the following remarks of Judge Kaufman:

Perhaps this case will become a classic example of the old adage that hard facts indeed make bad law, Judge Kaufman's reasoning to the contrary notwithstanding.[138]

9. SHARES AND CERTIFICATES

Subject to the regulatory provisions of federal and Florida securities laws, the basic law regulating the issuance of shares of capital stock in a Florida corporation, the after-market trading and sale of the shares and delivery of the certificates evidencing the shares is governed by the interplay between the Florida General Corporation Act[139] and Article 8 of the Uniform Commercial Code as adopted in Florida.[140] The certificate itself is the instrument or document which constitutes evidence of the shareholders' proprietary interest in the corporation.[141] While it may not be necessary to issue a certificate in order to establish that the proprietary interest of the shareholder exists, the sale does not take place until the certificate is actually delivered.[142] Moreover, before the shareholder is recorded in the books of the corporation, he has no right to exercise franchises granted to shareholders by virtue of stock ownership.[143] Furthermore, the kind of consideration and the value of it which may be accepted by the issuer for an orginal issue of shares is statutorily provided.[144]

In *Lundquist v. Gulfshore Television Corp.*,[145] the court held that a corporation was precluded by estoppel and/or acquiescence from asserting that stock was illegally issued *inter se* the parties. The court found that the corporation had submitted documents to a federal agency attesting that the stockholder was the majority stockholder, and as a result, the federal agency had issued an oper-

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> In my view, it is no longer debatable that trading on inside information merits universal condemnation. The undesirable nature of "inside trading" is reflected in the prophylactic provisions of Section 16(b) of the Securities Exchange Act of 1934 and the more general antifraud principles of Section 10(b) of that Act. . . . But the adage that hard facts make bad law is about to come true here, despite . . . Justice Cardozo's warning that judges are not free agents roaming at will to create law to fit the facts.

Id.

138. *Id.*

139. FLA. STAT. §§ 607.001-.414 (1977).

140. *Id.* §§ 678.101-.406. *See also* Mann, *Investment Securities,* 32 BUS. LAW. 1121 (1977).

141. *See* FLA. STAT. § 607.067 (1977). *See also* Baywood Furniture Mart, Inc. v. Kennedy, 295 So. 2d 350 (Fla. 2d Dist. 1974).

142. *See* FLA. STAT. §§ 678.301(1) & .313(1)(a) (1977).

143. *See id.* §§ 607.004(6), .067(1) & .091(1).

144. *Id.* § 607.054; *see* note 7 *supra.*

145. 328 So. 2d 202 (Fla. 2d Dist. 1976).

ating license in reliance on the corporate representations regarding ownership. Although there was an issue as to whether the stock had been lawfully issued for a promissory note because of a certain provision in the articles of incorporation and lack of official action by the board of directors, the court did not find this persuasive, especially in view of the acceptance by the corporation of payments on the note.[146]

In the event of a breach of a contract to sell common stock, specific performance is not a proper remedy unless the market value of the stock is not easily ascertainable or the stock is not freely tradable in the market so that it may be readily replaced.[147] In *Camp v. Parks,*[148] however, the court found that where the contract for sale of a closed corporation's stock was dependent on the active participation of the corporation which was impossible to secure because of personal antagonisms between the officers, and where the corporation was not a party to the agreement, specific performance of the contract was an inappropriate remedy. Thus, the plaintiff had to seek money damages even though he might not be able to readily establish a fair market value for the stock.[149]

In *Florida Boca Raton Housing Association v. Malone,*[150] the District Court of Appeal, Fourth District, held that there was no legal basis for a court to order an issuer to reissue a new stock certificate when the old certificate was outside the jurisdiction of the court. The court had been requested to grant such relief in order to satisfy a judgment creditor's unsuccessful attempted levy on the stock certificate owned by the stockholder judgment debtor.[151]

In an analogous situation, the Sixth Circuit, in *Wilkie v. Brooks,*[152] applied Florida law and passed on the rights of a secured creditor with respect to a certificate of stock issued by a Florida corporation. First, the court ruled that Article 9 of the Uniform Commercial Code as adopted in Florida,[153] was merely a codification of prior case law, and that in order to perfect a security interest in a stock certificate, endorsement of the certificate and delivery of possession to the secured party was all that was required.[154] In addition, the court noted that if one of the certificates delivered to the

146. *Id.* at 203-04.
147. Jackson Land Co. v. Harbeson, 153 So. 2d 826, 827 (Fla. 1963).
148. 314 So. 2d 611 (Fla. 4th Dist. 1975).
149. *Id.* at 613-14.
150. 325 So. 2d 22 (Fla. 4th Dist. 1976).
151. *Id.* at 23.
152. 515 F.2d 741 (6th Cir.), *cert. denied,* 423 U.S. 996 (1975).
153. FLA. STAT. §§ 679.101-.507 (1975).
154. 515 F.2d at 745.

secured party bore the forged signature of the secretary, then under Florida law the certificate would be invalid and not subject to a perfected security interest.[155] This would not affect, however, the security interest that the secured party had in the validly executed and endorsed certificates.[156] The interplay of the rulings of the district court in *Malone* and the circuit court in *Wilkie* reinforces the strong presumption with respect to ownership of stock certificates.

Finally, in *Ford v. Cannon*,[157] a case of first impression, a federal district court was faced with a claim for relief founded under the provisions of the Securities Exchange Act of 1934 and Article 8 of the Uniform Commercial Code. Plaintiff had lent money to a third party who had pledged to the lender unregistered stock which had not been "lettered" in accordance with the rules of the Securities and Exchange Commission. Lettering the stock restricts the ability of the debtor to pledge the securities and the ability of the lender to resell them in the event of a default. The lender sued his debtor's transferor for violation of the warranty contained in section 8-306(2)(c)[158] of the Uniform Commercial Code, which provides that a "person by transferring a security to a purchaser for value warrants only that . . . he knows no fact which might impair the validity of the security." Even though there was some evidence that the lender independently knew that the stock was not freely tradable, the court found that the lender was not the purchaser contemplated by the statute as the one who would receive the benefit of the warranty as against the defendant. Specifically, the court found that in other areas under the Uniform Commercial Code, where a warranty had been extended beyond the immediate person having contractual or other direct commercial privity with the one sought to be held liable, the extent of the warranty's reach had been stated.[159]

155. *Id.* at 747; *see* FLA. STAT. § 608.41 (1977).

156. 515 F.2d at 747. *Compare* FLA. STAT. § 608.41(1)(a) (1977) *with* FLA. STAT. § 607.067(1) (1977).

157. 413 F. Supp. 1393 (M.D. Fla. 1976) (discussed in Mann, *supra* note 140, at 1130).

158. FLA. STAT. § 678.306(2)(c) (1975).

159. 413 F. Supp. at 1398. It is interesting to note that the court in this case found that the original transferor had not fully informed the transferee-debtor of the restricted nature of the stock. The Securities and Exchange Commission contends that such an act constitutes a prima facie violation of Rule 10b-5 which was promulgated under section 10(b) of the Securities Exchange Act of 1934. Sec. Act Rel. No. 5226 (Jan. 10, 1972), FED. SEC. L. REP. (CCH) ¶ 2785. The court seemed to overlook this release in its discussion of the merits of the 10b-5 claim. 413 F. Supp. at 1397. Assuming the use of an instrumentality of interstate commerce, the transferee-debtor would have a cause of action under 10b-5 against the defendant-transferor for rescission on the basis of the Commission's release; and the plaintiff-lender, on the basis of the substantive provisions of Article 8 of the UCC, would have succeeded to that claim if he had no notice of the restriction.

10. VOLUNTARY DISSOLUTION

Under the Florida General Corporation Act, a voluntary dissolution of an ongoing corporation may be accomplished by consent of the shareholders[160] or by resolution of the directors as affirmed by the shareholders' vote.[161] Following the vote, the corporation delivers the articles of dissolution to the Department of State. When the Department of State is satisfied that the articles conform with law, the Department files the articles and the corporation ceases.[162] The articles may not be filed until all liabilities and obligations of the corporation have been paid or discharged or adequate provision has been made therefor and all of the remaining property and assets of the corporation have been distributed to its shareholders according to their respective rights and interests.[163] The directors of the corporation at the time of its dissolution constitute a board of trustees for any property owned or acquired by the dissolved corporation. The trustees have the power to convey any property or interest remaining in or acquired by the corporation after dissolution. The trustees are required to utilize any such property for the payment of any corporate debts, liabilities or obligations known to them, and if there are none, they are required to distribute the property or the proceeds from the sale of the property to the persons who were shareholders of the corporation at the time of dissolution.[164]

In *United States Fire Insurance v. Morejon,*[165] a case arising under chapter 608 of the Florida Statutes (repealed), the court affirmed the entry of a judgment against an individual who was an officer, director and sole stockholder of a dissolved Florida corporation in favor of a judgment creditor who had obtained the judgment prior to the dissolution of the corporate judgment debtor and who had not been paid. Citing section 608.30 of the Florida Statutes (1975), the court stated that it could find no error in the trial court's entry of a judgment against the individual because he had liquidated the corporation and had received all of the assets as the sole stockholder. Furthermore, the court noted that, as a surviving

160. FLA. STAT. §§ 607.254, .257, .261, .264 & .267 (1977). *See also* James Talcott, Inc. v. Crown Indus., Inc., 323 So. 2d 311, 314 (Fla. 2d Dist. 1975).

161. FLA. STAT. § 607.257 (1977).

162. *Id.* § 607.267(2)-(3). In *Talcott,* the court held that once the decision had been made to "liquidate the corporation and wind up its business," then the corporation was insolvent within the meaning of § 608.55 (1975). There is no comparable section in the Florida General Corporation Act to the repealed § 608.55 (1975) prohibiting transfers in contemplation of insolvency.

163. FLA. STAT. § 607.267(1) (1977).

164. *Id.* §§ 607.301(1)-(2).

165. 338 So. 2d 223 (Fla. 3d Dist. 1976).

director, the individual was required as a trustee to maintain and manage an amount of assets sufficient to satisfy creditors' claims.[166]

The decision of the court does not specify whether the individual was held liable because he was the sole stockholder and received the assets, or because he was a surviving director who was charged with managing the fund for the interests of the creditors. Under the repealed statute,[167] a trustee is charged with "a personal obligation to distribute assets first to creditors and second to stockholders." However, the corresponding section of the Florida General Corporation Act, Florida Statutes section 607.301 (1977), does not have comparable language to that found in the repealed statute. Therefore, under the new act there exists an open question as to whether the director-trustee in dissolution is personally liable for a failure to satisfy a corporate debt, liability or obligation which is known to him. Similarly, chapter 607, in light of the *Morejon* opinion, leaves open the question of the liability of a sole stockholder who has received all the assets of a dissolved corporation in lieu of satisfaction of the corporation's outstanding debts, liabilities and obligations.

II. SECURITIES REGULATION

A. *New Legislation*

The Florida Sale of Securities Law is contained in chapter 517 of the Florida Statutes (1977). Under the "Sunset Law" passed in the 1976 session of the legislature, the chapter is subject to repeal effective July 1, 1980.[168]

During the 1977 session of the legislature, two revisers' bills were passed, the purposes of which were to correct grammatical and typographical errors in sections 517.11 and 517.12(4) of the Florida Statutes (1975). The revisions in section 517.11 restructured the section for clarity and to facilitate correct interpretation. The revisions of section 517.12(4) were drafted to conform the section to amendments made to other sections of the act when the bond required of a dealer was increased from \$5,000 to \$50,000 during the 1975 session of the legislature.[169] In addition, section 20.12(2) of the

166. *Id.* at 224.

167. FLA. STAT. § 608.30(5) (1975) (repealed).

168. 1976 Fla. Laws, ch. 76-168, § 3.

169. 1977 Fla. Laws, ch. 77-104, § 194. *See also* the revisers' notes to the 1977 supplement to the Florida Statutes.

Prior to the amendment, the Division of Securities required investment advisors to post only a \$5,000 bond. The basis for this decision was an attorney general's opinion which attempted to make some sense of the conflicting provisions of FLA. STAT. §§ 517.12(4), .13-

Florida Statutes (1975) regarding denials of applications to register securities was amended, transferred and renumbered as section 517.0901.[170]

In the 1977 session, the Florida legislature enacted tender offer legislation entitled the Investor Protection Act which took effect October 1, 1977.[171] The Act applies to tender offers, defined as "an offer, other than an exempt offer, to acquire any equity security of an offeree company or a request or invitation for tenders,"[172] if after the acquisition the offeror is the beneficial holder of ten percent or more of the offeree's outstanding equity securities which were the subject of the offer.[173] Those transactions which are deemed to be exempt offers include: (1) an offer to acquire equity securities which would not exceed two percent of the class of the securities subject to acquisition in any twelve-month period; (2) an offer made by a corporation to acquire its own equity securities; (3) an offer to acquire equity securities of a class not registered under section 12 of the Securities Exchange Act of 1934; (4) an offer to acquire equity securities in an unsolicited broker's transaction; and (5) an offer which the Division of Securities exempts from the provisions of the Act as one not entered into for the purpose of and not having the

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.15 (1973). [1974] FLA. ATT'Y GEN. REP. 619. In essence, the Attorney General opined that an investment advisor, although a statutory dealer, was not a dealer in securities and therefore needed to file only a $5,000 bond pursuant to § 517.12(4), while dealers in securities were required to file a $50,000 bond pursuant to § 517.15.

Since the amendment, the Division of Securities has been requiring investment advisors in addition to other dealers, including issuers, to file a $50,000 bond on the basis that an investment advisor is specifically defined as a statutory dealer. An issuer is considered to offer and sell securities as a principal and, therefore, is also a statutory dealer. *See* FLA. STAT. § 517.02(4) (1977). Although there is no case law supporting the author's position, an argument may be made that an issuer, at least, is not a dealer for purposes of §§ 517.12-.15 on either of two theories: first, an issuer is not explicitly included in the definition of a dealer as is an investment advisor; second, the references in §§ 517.12(1)-(10) to a dealer are in a context which does not indicate that the term "dealer" includes an issuer. ("When used in this chapter, the following terms shall, *unless the text otherwise indicates*, have the following respective meanings . . . .") (emphasis added). *See id.* § 517.02. Unfortunately, when an issuer is "in registration" time does not permit counsel the luxury of litigating the issue with the Division of Securities.

170. 1977 Fla. Laws, ch. 77-106.

171. *Id.* ch. 77-441, *as amended by id.* ch. 77-450. As of the date of this article, approximately 33 states have enacted takeover or tender offer legislation as a supplement to their general corporation act or their securities regulation law. At the time of the proposal of the Florida Investor Protection Act, 26 states had enacted such legislation. As codified, the act appears in FLA. STAT. §§ 517.35-.363 (1977).

172. FLA. STAT. § 517.351(13) (1977). Presumably the scope of the legislation extends to all tender offers made to a person "in this state." *See id.* § 517.353(1). In addition, the act seems to extend to an offer for securities of a corporation incorporated in Florida even if such a corporation had no stockholders located or resident in Florida. *See id.* § 517.355(1).

173. *Id.* § 517.351(5).

effect of changing or influencing the control of the offeree company.[174]

If not exempt, an offeror is required to file with the Division of Securities and with the offeree's registered agent in Florida copies of the information required by the Williams Act[175] "at the time of making" the tender offer.[176] The Act requires that: (1) the substantive provisions of the offer must be the same to all holders of the offeree company's equity securities whether the holders are located or resident in Florida or another state, and the offer must remain open for at least thirty days; (2) a tendering stockholder is permitted to withdraw his deposit of securities at any time within the first fifteen days of the offer and at any time after sixty days from the tender offer; and (3) where the offer is made for less than all of the securities, and more securities are deposited than the offeror is bound or willing to take up, then the offeror is required to take up the securities, pro rata, according to the number deposited by each offeree. In addition, if the offeror varies the terms of the offer by increasing the price, the offeror is required to pay the increased price to all accepting offerees irrespective of when the securities were tendered.[177] Recommendations by management to accept or reject the offer must be filed with the Division of Securities (but apparently not with the registered agent of the target company) "not later than the time" that the recommendations were first published or sent to the stockholders.[178]

The Act provides for civil liability as against the tender offeror, participants and aiders and abettors who violate the provisions of the Act (subject to due diligence defenses) for rescission or damages in the event the offeror no longer owns the securities. An action must be commenced within two years "after the transaction upon which it is based." However, if the offeror has made a written offer to rescind the transaction and the offeree has failed to accept the offer within thirty days of its receipt, the offeree may not maintain the suit.[179] In addition to the private enforcement remedies contained in the Act, the Division of Securities is given the authority to seek an

174. *Id.*

175. The Williams Act is an amendment to §§ 13 & 14 of the Securities Exchange Act of 1934. 15 U.S.C. §§ 78m-78n (1970). The information now required to be furnished to the stockholders of the target company and filed with the Securities and Exchange Commission is called for in Regulation 14D and Schedule 14D.

176. FLA. STAT. § 517.355(1) (1977).

177. *Id.* § 517.353.

178. *Id.* § 517.357. Nevertheless, the author would recommend the filing of the information with the registered agent so as to facilitate distribution to stockholders or to facilitate public access to the information through that office.

179. *Id.* § 157.359.

injunction to prohibit a violation of and to enforce compliance with the Act.[180] Furthermore, the Division is granted rule making power with respect to the administration and enforcement of the provisions of the Act.[181]

Florida's Investor Protection Act, modeled on Colorado's Act,[182] is based largely upon the report of the Subcommitee on Proxy Solicitations and Tender Offers of the Federal Regulation of Securities Committee of the American Bar Association.[183]

B. *Administrative Interpretations*

It has not been and is not now the policy of the Division of Securities to issue what the securities bar has known as "no action letters," that is, written interpretations of either the substantive provisions of the Florida Sale of Securities Law or the regulations issued thereunder. Nevertheless, the Division has historically made its opinions known with respect to certain provisions of the statute and the regulations in conversations between counsel and the staff of the Division.

Traditionally, it had been the position of the staff of the Division that the number of offerees and purchasers set forth in the exemption from registration afforded by section 517.06(11) of the Florida Statutes (1977) should be interpreted to mean twenty persons *in total* irrespective of the state or jurisdiction of their residency. In May, 1977, the staff reversed its position and informed counsel that the twenty-person limitation set forth in this section meant twenty persons resident or otherwise located in Florida. The Division would, therefore, no longer take action against an issuer or dealer participating in an unregistered offering in which more than twenty persons were solicited or sold securities, provided that no more than twenty persons resident or otherwise located in Florida were solicited or sold securities. Section 517.06(11) had not been amended to warrant this change of opinion. The change is internally motivated and is apparently based on a perception that the prior interpretation gave unjustified and illegal extraterritorial effect to

180. *Id.* § 517.361.

181. *Id.* § 517.363.

182. COLO. REV. STAT. §§ 11-15.5 *et seq.* (1975).

183. *See* Subcommittee on Proxy Solicitations & Tender Offers, Fed. Regulation of Sec. Comm., ABA, *State Take Over Statutes and the Williams Act,* 32 BUS. LAW. 187 (1976). For an excellent discussion of state tender offer and takeover legislation, see Langvoort, *State Tender-Offer Legislation: Interests, Effects, and Political Compentency,* 62 CORNELL L. REV. 213 (1977); Wilner & Landy, *The Tender Trap: State Takeover Statutes and Their Constitutionality,* 45 FORDHAM L. REV. 1 (1976).

transactions not occurring within the State of Florida.[184] While either interpretation may be correct, the issue has not been addressed in any reported decision to date. In the absence of either regulations regarding the Division's present opinion, an appropriate amendment to the statute or a definitive case interpreting the statute, counsel can take little comfort in the Division's oral interpretation.

While no rules or regulations have been promulgated under the Investor Protection Act, it is anticipated that by the summer of 1978 rules and regulations will be available for public comment and adoption by the Division. It is the present oral opinion of the staff of the Division, however, that the Investor Protection Act applies to all statutory nonexempt "tender offers," including a negotiated sale of control securities by a person or group of persons to another person or group of persons.[185] Furthermore, the staff contends that while such a sale of securities may not be considered a customary "tender offer," it is a statutory "tender offer" for purposes of the Act.[186] The draftsman of the Act has indicated,[187] however, that it

184. *But see* [1955-1956] FLA. ATT'Y GEN. BIENNIAL REP. 659, 660. In this opinion, the Attorney General noted that the Florida Securities Act could not be given extraterritorial effect so as to apply to a sale of securities consummated in another state. The statute, however, is also directed against negotiations and solicitations within the state and if these occur a violation of the Act will occur even though the sale has not been consummated in the state. *But cf.* Dokken v. Minnesota-Ohio Oil Corp., 201 So. 2d 926 (Fla. 2d Dist. 1967).

The original Florida Sale of Securities Law was adopted in 1931 but did not contain an exemption comparable to § 517.06(11). In 1935, however, the Act was amended to provide an exemption from registration for the following transactions: "The sale of its shares by a corporation organized under the laws of this state when the *total number* of shareholders does not and will not after such sale exceed twenty . . . ." 1935 Fla. Laws, ch. 17253 (emphasis added).

Subsequent to 1935, a number of revisions were made so that the Act now provides an exemption from the registration provisions of § 517.07 for the following transaction: "The sale of its securities by a corporation, partnership or trust during any period of twelve consecutive months to not more than 20 persons . . . ." FLA. STAT. § 517.06(11) (1977).

The legislative purpose underlying § 517.06(11) was apparently to provide an exemption for certain smaller business entities: closely-held corporations, partnerships and trusts. If indeed this is the proper interpretation, then it follows that 20 persons means 20 in total, rather than 20 resident within the state. Under the latter interpretation, for example, any corporation could make a public offering of its equity securities as long as only 20 persons in Florida were solicited and sold such securities and the offering met the other provisions of the exemption.

On the other hand, the Uniform Securities Act, § 402(b)(9), provides an exemption from registration for sale to a certain number of persons with the phrase "in this state" expressly stated. All of the states which have enacted the Uniform Securities Act have adopted this exemption (with variations in numbers) and have included the phrase "in this state" in the language of the section. Therefore, it can be maintained that if the legislature had intended that the computation be limited to persons resident or otherwise located "in this state" it would have expressly so stated as did the draftsmen of the comparable provision of the Uniform Securities Act.

185. See the definition of a tender offer set forth in FLA. STAT. § 517.315(13) (1977).

186. *See id.* § 517.351(5)(e). This section provides that the Division by order may exempt

was not contemplated that the Act would include privately negotiated sales of equity securities, inasmuch as the term "tender offer" has been defined in federal cases under the Williams Act as not including privately negotiated purchases from a limited number of securities holders.[188] Furthermore, tender offer or takeover legislation at the state level has not been in response to a perceived need to regulate any truly negotiated private transactions but, rather, those transactions which are the antithesis of a privately negotiated transaction: the *blitzkrieg* takeover by a corporate raider.[189]

Including a negotiated transaction, which is otherwise not exempt from the provisions of the Investor Protection Act, as a statutory tender offer would have widespread and devastating impact on such transactions. Such an interpretation would prohibit the privately negotiated sale of control securities by a person or group of persons to an acquiring company by virtue of the provisions of section 517.353 of the Florida Statutes (1977). These provisions of the Act provide that no offeror (the acquiring company) may make a tender offer (negotiate an acquisition of control securities) which is not made to all holders of the securities to be acquired on substantially the same terms. Furthermore, to the extent that the offeror (acquiring company) receives tenders in excess of the number which it is bound or willing to take, it must accept on a pro rata basis those securities tendered.

C. *Prospective Legislation*

Presently, the Division of Securities is proposing revisions and amendments to the Florida Sale of Securities Law. It is anticipated that discussions between the staff of the Division, industry representatives and representatives of the Florida Bar will continue with a view toward presenting either proposed amendments or a complete revision of this law in the 1978 session of the legislature. Since Professor James S. Mofsky of the University of Miami School of Law

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from the provisions of the Act any transaction which does not have as its effect the purpose of changing or influencing the control of the target company. The exemption does not contemplate a "tender offer" in the classic sense of the term but rather contemplates that a "tender offer" is any transaction which results in a change of control of the acquired company.

187. *See* Letter from James W. Beasley to Representative Paul B. Steinberg (April 1, 1977) (on file U. MIAMI L. REV.).

188. *See, e.g.*, GAF v. Milstein, 453 F.2d 709, 720 (2d Cir. 1971); D-Z Investment Co. v. Holloway, [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,771 (S.D.N.Y. 1974); Nachman Corp. v. Halfred, Inc., [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,455 (N.D. Ill. 1973); Water & Wall Assocs., Inc. v. American Consumer Indus., Inc., [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 93,943 (D.N.J. 1973); *cf.* Cattlemen's Inv. Co. v. Fears, 343 F. Supp. 1248 (W.D. Okla. 1972).

189. *See* Letter, *supra* note 187.

first brought to light the dire need for statutory revision, a number of proposed revisions and amendments to the Act have been submitted not only by Professor Mofsky, but by the Division of Securities. To date, however, the Division, the industry and the Florida Bar have not been able to arrive at a suitable compromise; nor have they worked together in a joint drafting committee such as that utilized in Georgia in 1973, which resulted in the adoption of a complete, logically organized and modern security law for that state. It is hoped that the 1978 session of the legislature will see the adoption of significant changes to the present act as a culmination of Professor Mofsky's initiative.

Of more limited impact to Florida securities regulation is the completion of the American Law Institute's proposed Federal Securities Code under the leadership of Professor Louis Loss of Harvard University.[190] At the sixtieth annual conference of the North American Securities Administrators Association (NASAA) in October, 1977, the NASAA went on record as supporting the enactment of the code as proposed by Congress. If and when Congress adopts the proposed code, a complete revision of state securities regulation laws probably will be required.

D. *Recent Decisions*

1. FEDERAL PREEMPTION OF STATE JURISDICTION

Section 27 of the Securities Exchange Act of 1934, as amended, provides that the federal district courts have exclusive jurisdiction of violations of the Act or the rules and regulations promulgated thereunder and of all suits in equity and actions in law brought to enforce any liability or duty created by the Act, its rules or regulations.[191] In addition, section 28(a) provides that nothing in the Act is intended to affect the jurisdiction of state securities regulatory authorities insofar as such jurisdiction over any security or any person "does not conflict with provisions of this chapter or the rules and regulations thereunder."[192]

The foregoing provisions have provided the basis for two decisions during the survey period which may have a significant impact on the Florida Sale of Securities Law and the Investor Protection

190. For a recent symposium discussion of the provisions of the Code, see *American Law Institute's Proposed Federal Securities Code,* 30 VAND. L. REV. 311 (1977).

191. 15 U.S.C. § 78aa (1976).

192. *Id.* § 78bb(a). In comparison, § 18 of the Securities Act of 1933, 15 U.S.C. § 77r (1976), provides that nothing in the Securities Act of 1933 will affect the jurisdiction of any state securities regulatory agency over any security or person.

Act. In *Community National Bank & Trust Co. v. Vigman*,[193] the plaintiff filed an action alleging violations of margin limitations and credit restrictions imposed by the Securities Exchange Act of 1934 (Regulations T and U).[194] The complaint was dismissed by the state trial court with leave to amend. Thereupon, plaintiff amended his complaint seeking to avoid a finding that his cause of action arose under or was to enforce a liability or duty created by the Securities Exchange Act of 1934 and the attendant regulations. The trial court granted the motion to dismiss the amended complaint with leave to file a second amended complaint. The second amended complaint was filed and the motions to dismiss, which were refiled on the same grounds, were denied. The defendants appealed from the denial of the motions to dismiss.[195]

The second amended complaint alleged that: (1) the loans were arranged through the broker with the bank for the purpose of purchasing securities which were used as collateral for the loans; (2) such activities are not customary and ordinary; (3) because of a decline in value of the collateralized securities the plaintiff suffered loss; (4) such activities constituted a fraud on the plaintiff by the defendants; and (5) the broker stood in a fiduciary relationship to the plaintiff and, for the alleged purpose of promoting increased trading to create commissions ("churning"), was negligent in recommending the purchase of the securities. Plaintiff demanded rescission pursuant to the provisions of section 517.21(1) of the Florida Statutes (1975) but made no offer to tender the securities.[196]

The court opined that the determinative question regarding the existence or nonexistence of jurisdiction was whether the substance of the second amended complaint alleged a violation of the provisions of the Securities Exchange Act of 1934 and its regulations relating to excessive credit and margin in stock purchases, irrespective of how the plaintiff pled the case.[197] If in fact the plaintiff was alleging a breach of duties imposed on the defendants by virtue of this Act and the regulations thereunder, then the state court was without subject matter jurisdiction by virtue of the provisions of section 27 of the Securities Exchange Act of 1934[198] and section 517.25 of the Florida Statutes (1975).[199]

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193. 330 So. 2d 211 (Fla. 3d Dist. 1976).
194. 12 C.F.R. §§ 220-21 (1977).
195. 330 So. 2d at 213-14.
196. *Id.*
197. *Id.*
198. 15 U.S.C. §§ 78a-78kk (1976).
199. 330 So. 2d at 214-15.

Independently of the Securities Exchange Act of 1934, the court analyzed the allegations and found that no violation of law had occurred regarding the loans by the bank in furtherance of its normal business, the allegations against the broker concerning churning and failure to warrant the future market action of the securities, and the extension of excessive credit for stock purchases by the broker to his customer.[200] Accordingly, the court found that, apart from the Securities Exchange Act of 1934, the plaintiff had failed to state a cause of action. The court concluded that as to plaintiff's assertions that the transactions involving excessive credit or undercollateralized loans made by the bank for the purchase of securities constituted a cause of action against the bank under the Florida Sale of Securities Law, "there would be no jurisdiction therefor in the state court, because it would be in conflict with the federal law whereby action therefor is maintainable only in the federal courts."[201]

The court's reasoning and opinion in *Vigman* is quite persuasive to the extent that it finds that a state court cannot create subject matter jurisdiction where none exists and where federal statutes have exclusively reserved such jurisdiction to federal courts. Furthermore, the court's holding that Congress has preempted the field of credit regulation and margin requirements regarding the purchase of certain securities is economically supportable and legally justifiable.

The court noted that the allegation that the broker "churned" the account of the plaintiff "had reference to a matter which would be a violation of the Securities Exchange Act of 1934, the jurisdiction for action upon which would be in the United States district courts."[202] An allegation of churning would constitute a violation of the Securities Exchange Act on the basis of a violation of rule 10b-5,[203] the language of which is almost identical with the provisions of section 517.301 of the Florida Statutes (1975).[204] Therefore, the court, *sub judice*, either held that "churning:" (1) does not constitute a violation of section 517.301(1)(c) of the Florida Statutes

200. *Id.* at 215-16.

201. *Id.* at 216.

202. *Id.*

203. 17 C.F.R. § 240.10b-5 (1977).

204. *See, e.g.*, Stromillo v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 54 F.R.D. 396 (E.D.N.Y. 1971). *Compare* 17 C.F.R. § 240.10b-5 (1977) *with* FLA. STAT. § 517.301(1)(c) (1977). Both the rule and the statute provide that in connection with the purchase and sale of a security it is unlawful to engage in "any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon any person." *Accord*, 17 C.F.R. § 240.15c1-2 (1977). *See also id.* § 240.10b-3(a) & .10b-16(a).

(1975); (2) does constitute a violation of this section but has been preempted by the Securities Exchange Act of 1934; or (3) does constitute a violation of this section but the plaintiff, having failed to tender the securities or otherwise offer to return the parties to the status quo, failed to make a material allegation required by section 517.21(1)1 of the Florida Statutes (1975). If the second theory, federal preemption, is determined to be the basis of the opinion, the applicability of section 517.301 of the Florida Statutes (1977) to interstate transactions, especially in light of the recent holding of a federal district court in *Great Western United Corp. v. Kidwell,*[205] is subject to doubt.

In *Great Western United Corp. v. Kidwell,* a United States district court found that the Idaho takeover statute[206] effectively destroyed the congressional plan set forth in the Williams Act for making cash tender offers and, therefore, was preempted by that Act. The court ruled that the Williams Act regulates the making of tender offers for the benefit of stockholders while the Idaho statute regulates the making of tender offers primarily for the benefit of management of the target company. The court found that the Idaho statute violated the commerce clause of the Constitution because it did not regulate a legitimate local interest, it had a substantial effect on interstate commerce, and the burden imposed on interstate commerce was excessive in relation to any local benefits derived from the statute.

Undoubtedly, this case will be the subject of much commentary.[207] Nevertheless, the validity of the Investor Protection Act, as adopted in the 1977 session of the Florida Legislature, is subject to question by virtue of the ruling of the district court in *Great Western.* While the court did not find that the Williams Act was intended to occupy the field of tender offer or takeover legislation and that the dominance of the federal interest in securities regulation does not preempt state regulation, it did find that the Idaho

205. 439 F. Supp. 420 (N.D. Tex. 1977). The case was on appeal to the United States Court of Appeals for the Fifth Circuit when settled.

206. IDAHO CODE §§ 30-1501 to 1513 (Supp. 1977). The statute required that a tender offeror register his offering with an appropriate state officer and withhold making an offer until the registration was declared effective. Prior to the effective date, management could demand a hearing in order to determine whether the registration should be declared effective. Moreover, extraterritorial effect was given to the statute by forbidding a tender offer to be made to stockholders of a target company in any state until approved in Idaho for purposes of stockholders located therein. Finally, the statute exempted from regulation a "friendly tender offer," that is, an offer which the management of the target company recommended to its shareholders.

207. The case has already been the subject of two significant articles. *See* Langevoort, *supra* note 183, at 241-56; Wilner & Landy, *supra* note 183, at 15-31.

statute conflicted with the Williams Act and was therefore preempted by the Williams Act in a number of particulars. There is a justification for distinguishing the Idaho Act from its Florida counterpart, however, on the basis that its cumulative effect was to weigh the scales heavily in favor of management of the target company without considering the protection of the stockholders. Accordingly, the usefulness of the Williams Act was affected and, therefore, the Idaho act was preempted.[208] The Investor Protection Act, as adopted in Florida, does not contain any of the provisions which the district court in *Great Western* found so offensive.[209] The Act does not mirror the Williams Act but is based on the same policy considerations as is the Williams Act; that is, a stockholder who is the subject of a tender offer should be given fair and full disclosure of material information regarding the cash offer and a meaningful opportunity to consider the offer so that he may intelligently determine whether to accept or reject it. The principal differences between the provisions of the Williams Act and the provisions of the Investor Protection Act are as follows. The Williams Act comes into play when a transfer of more than five percent of the outstanding equity securities of the offeree company are traded,[210] whereas the Investor Protection Act is applicable when a ten percent transfer takes place.[211] Moreover, the Williams Act requires that the offer remain open for a minimum of seven days,[212] and the Investor Protection Act requires that the offer remain open for a minimum of thirty days.[213] In addition, the Williams Act permits the tendering stockholder to withdraw his tender any time after the first seven days of an offer,[214] while the Investor Protection Act provides that the stockholder may withdraw the tender at any time within the first fifteen days of the offer.[215] Finally, the Williams Act provides for proration for shares tendered when an offer is made for less than

208. *See* note 207 *supra*.

209. The same cannot be said for the takeover legislation contained in FLA. STAT. §§ 628.461 & 659.14 (1977) with respect to Florida based insurance companies and banks.

210. Securities Exchange Act of 1934, § 14(d)(5) (codified at 15 U.S.C. § 78n(d)(5) (1976)).

211. FLA. STAT. § 517.351(13) (1977). To the extent that a statutory tender offer under the Investor Protection Act is deemed to include privately negotiated transactions in which control securities are sold, the scope of the Act may be subject to a federal preemption challenge inasmuch as the Williams Act has not been so extended.

212. Securities Exchange Act of 1934, § 14(d)(5) (codified at 15 U.S.C. § 78n(d)(5) (1976)).

213. FLA. STAT. § 517.353(2) (1977).

214. Securities Exchange Act of 1934, § 14(d)(5) (codified at 15 U.S.C. § 78n(d)(5) (1976)).

215. FLA. STAT. § 517.353(3) (1977).

all of the outstanding shares and a greater number of shares are tendered if the tenders occur within the first ten days of the offer; thereafter, an offeror may purchase shares on a first-come-first-serve basis.[216] On the other hand, the Investor Protection Act provides for proration for all tendering shareholders irrespective of when the tenders were received.[217]

While the Florida act is certainly less burdensome on interstate commerce than the Idaho act, it is not clear whether it will survive the test established by the court in *Great Western.* It certainly has a better chance than the Idaho act and a better chance than other state takeover legislation which is similar to that act. A definitive ruling in the area which will be a sufficient guide to counsel probably will not be forthcoming until an appellate court reviews the substantive decision of the district court.[218]

2. DEFINITION OF A SECURITY

Section 517.02(1) of the Florida Statutes (1977) defines a security for purposes of securities regulatory law in Florida. The statutory definition is virtually the same as that contained in section 2(1) of the Securities Act of 1933,[219] and similar to that contained in section 3(a)(10) of the Securities Exchange Act of 1934.[220] In all three acts, a security is broadly defined with the explicit objective of including all types of instruments that, in the ordinary course of financial and commercial dealings, fall within the concept of a security including bonds, debentures and common and preferred stock. Furthermore, a security includes all types of mediums of investment of a more general character which conceptually include a "certificate of interest or participation in any profit sharing agreement . . . , [an] investment contract . . . , or in general, any instrument commonly known as a 'security.' "[221]

The most recent decision of the Supreme Court of the United States in this area is *United Housing Foundation, Inc. v. Forman.*[222] There, the Court noted that the focus of the Securities Act of 1933

216. Securities Exchange Act of 1934, § 14(d)(6) (codified at 15 U.S.C. § 78n(d)(6) (1976)).

217. FLA. STAT. § 517.353(4) (1977).

218. The brief of the appellants suggested to the appellate court that the district court's invalidation of the Idaho statute implicitly invalidates all state takeover legislation which is similar to the Idaho act. The appellants included the Investor Protection Acts of Colorado and Florida in their list of similar takeover legislation.

219. 15 U.S.C. § 77b(1) (1976).

220. *Id.* § 78c(10).

221. *Id.*

222. 421 U.S. 837 (1975).

and the Securities Exchange Act of 1934 is on the regulation of the capital markets of the free enterprise system; the regulation of the movement of capital from those who have it to those who need it, with the expectation and purpose of making a profit on the utilization of the capital.[223] Therefore, the Court found that the phrase "investment contract," as utilized in both federal acts and as defined by prior case decisional law,[224] is the same an any "instrument commonly known as a 'security.' "[225] In either case, the Court added, "[t]he touchstone is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others."[226] By profits, the Court had reference either to "capital appreciation resulting from the development of the initial investment . . . or [to] a participation in earnings resulting from the use of the investors' funds."[227] In such cases, the Court noted, the investor is "attracted solely by the prospects of a return on his investment."[228]

Applying this approach to the relevant facts, the Court in *Forman* found that purchaser of "common stock" in the government subsidized cooperative housing project were "attracted solely by the prospect of acquiring a place to live, and not by financial returns on their investments."[229] The Court observed that no profit traditionally associated with securities was offered as an inducement to the purchasers. The Court specifically noted that there was no chance of "capital appreciation" upon resale of the stock, and that income derived from the leasing of the cooperative's commercial facilities would be used to reduce tenant rental costs and was far too speculative and insubstantial to be a factor in the determination. Furthermore, the Court stated that tax benefits accruing to an apartment owner by virtue of the deductibility of interest payments on his mortgage did not constitute a profit inasmuch as they are "nothing more than that which is available to any homeowner who pays interest on his mortgage."[230] The common stock was thus held not to be a security for purposes of federal securities law.

The similarity of statutory definition in the Florida Sale of

223. *Id.* at 849.

224. Tcherepnia v. Knight, 389 U.S. 332, 339 (1967); SEC v. W.J. Howey Co., 328 U.S. 293, 298-99 (1946); SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344, 352 (1943); SEC v. Koscot Interplanetary Inc., 497 F.2d 473 (5th Cir. 1974); SEC v. Glenn W. Turner Enterprises, Inc., 474 F.2d 476 (9th Cir.), *cert. denied*, 414 U.S. 821 (1973).

225. 421 U.S. at 852.

226. *Id.*

227. *Id.*

228. *Id.*

229. *Id.* at 853.

230. *Id.* at 855.

Securities Law and the Securities Act of 1933 supports prior decisions of Florida courts holding that the definitions of a security under federal and Florida law closely parallel one another.[231] The most recent Florida case reasserting this principle is *Levine v. I.R.E. Properties, Inc.*[232] In *Levine,* the court reversed the entry of summary judgment against two individual plaintiffs on the issue of whether realty agreements, by which the plaintiffs purchased an apartment complex from the corporate defendant, constituted a security. In addition to the sale of the complex, the agreement also provided that the defendant would manage the property for the benefit of the plaintiffs as the plaintiffs' agent. The agreement, however, was cancellable by either party upon thirty days' written notice. There was no evidence that the defendant solicited sales, sold improved real property with a management contract on a regular basis as a business, or promoted the sale of the complex on the basis of an expectation of "tax sheltered" profit or otherwise.

Presumably, the trial court had found that no common enterprise existed and the purchasers were not expecting profits from the efforts of the defendants because of the thirty day cancellation provision in the management contract.[233] Citing for support decisions of the Supreme Court of the United States under the Securities Act of 1933 and the United States district court in *Sunshine Kitchens v. Atlanthus Corp.*,[234] the court ruled that the fact that the management contract was cancellable on thirty days' notice was not conclusive with respect to whether the agreements constituted an investment contract and, therefore, a security. The court found that, on the basis of prior decisional law, there were genuine issues of material fact with respect to whether the agreements were a security, and that it would be necessary for the trial court to consider evidence and proof beyond the agreements themselves. Therefore, the court reversed the entry of summary judgment and remanded for further proceedings.[235]

In *Sunshine Kitchens,* the district court found that the purchase of computers by the plaintiff, under an agreement whereby the defendant would manage the leasing arrangement of the computers for the plaintiff, did not constitute the sale of a security

231. *See* O'Neill v. State, 336 So. 2d 699, 701 (Fla. 4th Dist. 1976); Frye v. Taylor, 263 So. 2d 835, 839-40 (Fla. 4th Dist. 1972); Florida Discount Centers, Inc. v. Antinori, 226 So. 2d 693, 695 (Fla. 2d Dist. 1969), *aff'd,* 232 So. 2d 17 (Fla. 1970). *Compare* SEC v. W.J. Howey Co., 328 U.S. 293 (1946) *with* McElfresh v. State, 151 Fla. 140, 9 So. 2d 277 (1942).

232. 344 So. 2d 938 (Fla. 3d Dist. 1977).

233. *See* 344 So. 2d at 939-40 (dicta).

234. 403 F. Supp. 719 (S.D. Fla. 1975).

235. 344 So. 2d at 940.

within the meaning of the federal and Florida securities laws on the basis of prior Supreme Court rulings, including *Forman*. The transaction was structured and sold by the defendant as a tax shelter so that the plaintiff would be able to utilize the investment tax credit and accelerated depreciation provisions of the Internal Revenue Code of 1954 to "shelter" any "income" received from leasing of the computers or to "shelter" income received from other sources, thereby providing an investment return in cash proceeds without concomitant taxable income. In addition, plaintiff alleged that it expected a cash return on its investment when the computers were sold some years later.[236]

Interpreting the decisions of the United States Court of Appeals for the Fifth Circuit in *SEC v. Koscot Interplanetary, Inc.*[237] and *SEC v. Continental Commodities Corp.*,[238] the court was of the opinion that the "common enterprise" criterion of an investment contract were not met solely by a common enterprise in which the plaintiff and the defendant are the only two parties to the transaction. Since there was no evidence that additional persons were solicited or sold similar computer sale-leaseback management packages, the court seemingly found that the common enterprise test of an investment contract was not met.[239]

The court in *Sunshine Kitchens* further held that anticipation of favorable income tax benefits because of the tax shelter character of the investment did not constitute "profits" of an investment contract according to the *Forman* tests. The court reasoned that the "economic realities of the situation" were an interest in showing a loss on the plaintiff's records, rather than profits stemming from the defendant's efforts.[240] Therefore, the court found that the transaction did not involve the sale of a security for purposes of federal securities law and granted the motion of the defendant for summary judgment on all counts based upon alleged violations of federal and state securities law.[241]

The decision of the district court in this case is arguably incorrect. It reflects a misunderstanding of the investment motivation of the purchaser of a tax shelter and the effect a tax shelter has in generating actual cash profits to an investor. This sheltering of cash receipts from the tax shelter business or from other business sources would otherwise be treated as taxable income. In addition, the deci-

236. 403 F. Supp. at 720.
237. 497 F.2d 473 (5th Cir. 1974).
238. 497 F.2d 516 (5th Cir. 1974).
239. 403 F. Supp. at 721-22.
240. *Id.* at 722.
241. *Id.* at 723.

sion reflects a lack of understanding of the vital role of the promoter in structuring the tax shelter and maintaining it as a shelter during the course of the business. The court strictly construed the rulings of the United States Court of Appeals for the Fifth Circuit in *Continental Commodities* and *Koscot Interplanetary* to require that the promoter solicit and sell to many investors the same arrangement or scheme in order to constitute, by definition, an investment contract.

It has been suggested that this interpretation of the appellate court opinions in these cases is overly restrictive[242] and seems to be in possible conflict with the opinion of the District Court of Appeals for the Third District in *Levine*. Furthermore, the Supreme Court of the United States' opinion in *Forman*, to the effect that the primary purpose and focus of the federal securities laws is the regulation of the movement of capital in the free enterprise system based on the prospect of making profit, is as applicable to the mechanics of a tax shelter as to any other securities transaction. In essence, the district court in *Sunshine Kitchens* may have lost sight of the basic economic policies inherent in the securities acts as expressed by the Supreme Court[243] and, in so doing, misapplied the law to the facts.

Notwithstanding the shortcomings of the court's decision, the case is significant. It is the first case in which the Fifth Circuit, under the Florida Sale of Securities Law, passed on whether a "common enterprise" may exist where the agreement or scheme involves only one investor and one promoter. Further, it is authority for the proposition that a "pure tax shelter" does not constitute a medium of investment which can be characterized as an investment contract and, therefore, as a security. Consequently, promoters of

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242. *See, e.g.*, Jones v. International Inv., Inc., 429 F. Supp. 119, 123-24 (N.D. Ga. 1977); Huberman v. Denny's Restaurant, Inc. 337 F. Supp. 1249, 1251 (N.D. Cal. 1972).

243. *See* 421 U.S. at 852. Another way to analyze this case, by analogy to *Forman*, would be to determine whether the defendant intended to use the computer "in house" and lease it out on a time-sharing basis in order to subsidize its cost of utilization, or whether the plaintiff purchased the computer as a tax shelter to make money by leasing it to others; and, not knowing how to lease computers, engaged the defendant as a part of the transaction. In the former case an argument could be made that under *Forman* no sale of a security occurred since the lease of the equipment to others was simply to lower its costs to the purchaser. *See id.* at 853. On the other hand, under the latter analysis there would be a sale of a security under *Forman*, as the expectant profit is based on the efforts of others. These contrasting possibilities are suggested by the Court's language in *Forman*, where it stated:

> There is no doubt that purchasers in this housing cooperative sought to obtain a decent home at an attractive price. But that type of economic interest characterizes every form of commercial dealing. What distinguishes a security transaction—and what is absent here—is an investment where one parts with his money in hope of receiving profits from the efforts of others, and not where he purchases a commodity for personal consumption or living quarters for personal use.

Id. at 858.

tax shelters who contend they are not selling securities will probably rely on the decision.

3. VIOLATION OF THE ANTI-FRAUD PROVISIONS

The basic anti-fraud provisions of the Florida Sale of Securities Law are contained in section 517.301 of the Florida Statutes, adopted in 1965.[244] The statute is based on the substantive provisions of section 17 of the Securities Act of 1933[245] and Rule 10b-5 promulgated under section 10(b) of the Securities Exchange Act of 1934.[246]

In *Merrill Lynch, Pierce, Fenner & Smith, Inc., v. Byrne,*[247] the court opined that both the better reasoned decisions and the clear weight of authority held that scienter was not a necessary element to recovery under the comparable sections of federal law and thus should not be required under section 517.302(1) of the Florida Statutes (1975).[248]

Subsequent to the decision of the court in *Byrne,* however, the Supreme Court of the United States, in *Ernst & Ernst v. Hochfelder,*[249] found that the nature of the conduct proscribed by section 10(b) of the Securities Exchange Act of 1934 was such that the Court found it difficult to believe that "any lawyer, legislative draftsman, or legislator would use these words if the intent was to create liability for merely negligent acts or omissions."[250] The Court noted that the administrative history of the rule likewise supported an interpretation that the rule was "intended to apply only to activities that involved scienter."[251]

Since *Hochfelder,* no cases have been decided under section

244. 1965 Fla. Laws, ch. 65-428.

245. 15 U.S.C. § 77q (1970).

246. *Compare* FLA. STAT. § 517.301(1) (1977) *with* 15 U.S.C. § 77q (1976); 17 C.F.R. § 240.10b-5 (1977).

247. 320 So. 2d 436 (Fla. 3d Dist. 1975).

248. *Id.* at 440.

249. 425 U.S. 185 (1976).

250. *Id.* at 203.

251. *Id.* at 212. The question expressly left open by the Court in *Hochfelder* was the precise definition of "scienter." The Court defined "scienter" as the "mental state embracing intent to deceive, manipulate, or defraud." *Id.* at 193 n.12. Furthermore, the Court stated that § 10b of the Securities Exchange Act "was intended to proscribe knowing or intentional misconduct." *Id.* at 197. The Court, however, specifically left open the question of whether reckless behavior was sufficient for civil liability under this section and rule.

In the majority of district and circuit court cases passing on this question since the decision in *Hochfelder,* the courts have tended to find that scienter, for purposes of imposition of civil liability under § 10b and Rule 10b-5, encompassed knowing or intentional misconduct as well as conduct which could be characterized as a reckless disregard for the truth. *See, e.g.,* McLean v. Alexander, 420 F. Supp. 1057, 1080 (D. Del. 1976). *See also* Castruccio, *Developments in Federal Securities Regulation - 1976,* 32 BUS. LAW. 1537, 1555-63 (1977).

517.301(1) passing on whether this section also requires an allegation and proof of "scienter" contrary to the dicta in *Byrne*. In light of the *Hochfelder* decision, the District Court of Appeal, Third District, was arguably incorrect in its interpretation. The section can only be traced back to 1965 but is apparently based on federal law, subject to the interpretation by the Supreme Court in *Hochfelder*. This suggests that knowing or reckless conduct is required in order to sustain a cause of action under section 517.301(1) of the Florida Statutes (1977).[252]

4. REMEDIAL PROVISIONS

Section 517.21(1) of the Florida Statutes (1977) provides that the purchaser of securities has the right to rescind the transaction upon the tender of the security sold against the person making the sale and "every director, officer or agent of or for the seller, if the director, officer, or agent has personally participated or aided in any way making the sale." The liability of such a participant or aider is for the full amount paid by the purchaser with interest, court costs and reasonable attorney's fees.[253] The seller may cut off liability against itself and participants and aiders by making a "rescission offer" to the purchaser which must be accepted within thirty days from the date of tender.[254]

Two recent decisions passed on issues arising under the remedial provisions of the Florida Sale of Securities Law. In *Merrill*

252. *Cf.* Haygood v. Adams Drugs, Inc., 346 So. 2d 612 (Fla. 2d Dist. 1977) (dismissal of a complaint seeking rescission of securities sale reversed even though complaint contained no specific allegations of securities law violations).

To the extent that decisions after *Hochfelder* do determine that a civil action for violation of FLA. STAT. § 517.301(1) (1977) must allege scienter (*i.e.*, either intentional, knowing or reckless conduct), so also a criminal action should require, at least, a general *mens rea*. There is no case passing directly on a criminal violation of § 517.301; however, the supreme court in State v. Houghtaling, 181 So. 2d 636 (Fla. 1965) held that the 1935 amendment to the Florida Sale of Securities Law eliminated any requirement to prove scienter for purposes of establishing a criminal conviction for participation in the unlawful sale of unregistered securities and/or the failure to register as a dealer or salesman under the act. As noted, the case did not pass on a criminal prosecution for violations of the anti-fraud provisions of the act presently contained in FLA. STAT. § 517.301(1) (1977). Nevertheless, a number of states attorneys have attempted to prosecute criminal violations of § 517.301(1) without specific allegations of scienter either as a general *mens rea* or a specific *mens rea*.

253. In addition to the civil remedies available under FLA. STAT. § 517.21 (1977), § 517.23 provides that the same civil remedies available under the Securities Act of 1933 and the Securities Exchange Act of 1934 are available to purchasers of securities for violations of the Florida Sale of Securities Law. The only statutory remedy for sellers of securities is available under § 517.359 for violations of the Investor Protection Act.

254. It is not clear whether the "rescission offer" provision of FLA. STAT. § 517.21(1) (1977) would cut off damages sought by the civil litigant under the provision of § 517.23. This issue has not been addressed in any reported case.

Lynch, Pierce, Fenner & Smith, Inc. v. Byrne,[255] the court read the remedial provisions of the act strictly with regard to the facts before it. The plaintiff had placed an order with the defendant broker to purchase securities at the market price with a stop loss order to sell the stock whenever its market price decreased to a designated price. The defendant placed the order but for a number of reasons, none of which could be characterized as intentional, was unable to place the stop loss order. The defendant did not inform the plaintiff that it had not placed the stop loss order, but from time to time did report the market value of the securities at less than the stop loss price as well as prices in excess of the stop loss price. The plaintiff knew, therefore, and had an opportunity to sell the securities in excess of the stop loss price but at less than the purchase price.

The trial court found that the defendant's failure to advise the plaintiff that a stop loss order could not be and had not been entered constituted an omission to state a material fact in violation of section 517.301(1)(b) of the Florida Statutes (1975). The court rejected the defenses of estoppel, waiver and ratification, although noting that such defenses were available in an alleged violation of section 517.301(1). Furthermore, the court stated that the defendant had not made a rescission offer which would constitute a defense to the remedial provisions of section 517.21(1) of the Florida Statutes (1975). Therefore, the court entered judgment in favor of the plaintiff for rescission.[256]

In affirming the decision, the appellate court rejected the defendant's argument that the later rise in the market value of the securities above the stop loss price, accompanied by the action of the defendant in advising the plaintiff and urging him to sell at the price above the stop loss price but at less than the original acquisition price, constituted a waiver of remedies or ratification of the improper acts of the defendant by the plaintiff. Nor did such action bar the plaintiff from asserting his statutory rights: "We think this argument is untenable here because the statute clearly and unmistakably places the burden on the broker to 'offer in writing' to take back the securities and refund the purchase price in full together with interest. . . ."[257] The court concluded:

> And so, if we literally apply the statute - which we must - the simple answer is that the broker should have *immediately* told the buyer he could have his money back and offered it "in writing" to him. This was not done. The buyer is guilty of noth-

255. 320 So. 2d 436 (Fla. 3d Dist. 1975).
256. *Id.* at 438-40.
257. *Id.* at 441.

> ing. He is protected by the statute. He has the right to invoke its sanctions. He has done so within the time the statute prescribed and in the manner prescribed and the trial court was correct in requiring the broker to do what the statute says it should do and to add to the judgment the additional charges authorized.[258]

This decision may be viewed as holding that a plaintiff is estopped from asserting or has waived his right to rescind by ratification only when the seller of the securities makes a rescission offer in writing which has not been accepted by the buyer within thirty days of its tender. Alternatively, the decision could be more narrowly read as stating that insufficient facts were shown to invoke these defenses. There is authority which tends to support the former interpretation[259] although prior decisions of courts of appeal would tend to support the latter interpretation.[260] Most likely, if the price of the securities had risen above the acquisition price and the plaintiff had been informed of this fact, a much better case for estoppel or waiver might have been made out. Under such circumstances, Merrill Lynch would probably have advised the defendant of its inability to place the stop loss order and would have made the rescission offer in the hope that it would not have been accepted, or if it had, gambling that they could "sell short."

In *Haygood v. Adams Drug, Inc.*,[261] the court passed on the activity of the defendants alleged to be participants and aiders in the sale of securities made in violation of sections 517.301(1)(b) and 517.301(1)(c) of the Florida Statutes (1975). The court reviewed the interpretation of the phrase "personally participated or aided in any way in making the sale" by noting the interpretation of the Supreme Court of Florida decision in *Nichols v. Yandre*[262] that the phrase " 'implies some activity in inducing the purchaser to *invest*.' "[263] One defendant had personally solicited the plaintiff to make the stock purchase. This act seemed to constitute participation in the sale of common stock. Three other individual defendants, however, did not participate directly; rather, they were alleged to have known that the sale would be made by means of financial statements con-

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258. *Id.*

259. *See* Dokken v. Minnesota-Ohio Oil Corp., 232 So. 2d 200, 205 n.2 (Fla. 2d Dist. 1970) (McNulty, J., dissenting).

260. *See* Henderson v. Hayden, Inc., 461 F.2d 1069, 1073 (5th Cir. 1972); Dokken v. Minnesota-Ohio Oil Corp., 232 So. 2d 200, 203 (Fla. 2d Dist. 1970).

261. 346 So. 2d 612 (Fla. 2d Dist. 1977).

262. 151 Fla. 87, 9 So. 2d 157 (1942).

263. 346 So. 2d at 614 (quoting *Nichols*, 9 So. 2d at 160) (emphasis added). *See also* Ruden v. Medalie, 294 So. 2d 403, 406 (Fla. 3d Dist. 1974) (discussed in Edwards, *supra* note 92).

taining material omissions or misstatements regarding a prior stock split and shortages in stock and trade which had resulted in substantial net operating loss not shown in the financial statements. It was further alleged that these defendants either prepared or assisted in the preparation of the statements and, knowingly concealed the inventory shortage, the net operating loss and the stock split.[264]

The court concluded that the plaintiff's complaint, for purposes of a motion to dismiss, was sufficient to allege a cause of action against all individual defendants in their capacities as officers and/or directors who participated or aided in a violation of the act. The court found that the plaintiff had pled knowledge of the matters which were omitted in the financial statements, awareness that the financial statements would be issued and relied upon by prospective investors in connection with the purchase of the offered securities, and concealment of the existence of the material facts from disclosure in the financial statements. The court held that such activity violated the Act and that it constituted participation or aiding in the unlawful sale of securities within the meaning of section 517.21 (1) of the Florida Statutes (1975), thereby subjecting all defendants to liability under that section.[265]

264. 346 So. 2d at 613-14.
265. *Id.* at 614.