IN THE SUPREME COURT OF FLORIDA

CASE NO. 72,361

E.F. HUTTON & COMPANY INC.,

Defendant-Appellant,

v.

CHRIST ROUSSEFF,

Plaintiff-Appellee,

CERTIFICATION FROM UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

APPELLANT'S REPLY BRIEF

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STATEMENT OF THE CASE

Rousseff's statement of the facts is incomplete, inaccurate and contains many facts irrelevant to the issue at hand. The Eleventh Circuit has framed the issue by an appropriate statement of the facts. Those facts provide the background for the certified question.

ARGUMENT AND CITATION OF AUTHORITY

I. The source of the proximate cause requirement is Section 517.301.

The most telling point of Rousseff's brief is his failure to address § 517.301, Fla. Stat., the fraud liability provision. Rousseff goes to great length to characterize § 517.211 as the "civil liability" provision when it is by its own title the "remedies" provision. Whether proximate cause is an element of a Florida Act fraud claim is dictated by the liability provision, not the remedies provision. To interpret the Act otherwise wrongfully puts the cart before the horse.

Proximate cause is an element of § 517.301. Rousseff misses this important point. Section 517.211 specifies the remedies available to a claimant upon proof of certain liability provisions. An underlying Chapter 517 violation must be proved before the remedies provision may be invoked. See generally Haygood v. Adams Drugs, Inc., 346 So.2d 612

(Fla.2d DCA 1977)(to invoke remedy under § 517.21(1), there must be showing of a "violation under the securities statute"); Citizens Fed. Sav. & Loan Ass'n v. Loeb Rhoades, 473 So.2d 679 (Fla. 4th DCA 1984)(Act does not provide for award of attorney fees under § 517.211(b) to successful counterclaimant in Chapter 517 lawsuit because breach of contract claim was not a 517 violation). By its terms, § 517.211(2) (which is the provision under which Rousseff claimed his remedy) requires the claimant to prove a "violation of 517.301." Hutton is not asking the Court to rewrite § 517.211, as suggested by Rousseff. Rather, Hutton is asking the Court to interpret § 517.301 consistently with its federal counterpart.

II. Statutory construction principles support the conclusion that proximate cause is an element of a § 517.301 violation.

Rousseff maintains that the Florida Act does not require proof of proximate cause because the words "proximate cause" or "loss causation" are not written in §§ 517.301 or 517.211. Again, the proper focus is § 517.301. The fact that the words "proximate cause" are not a part of § 517.301 is not surprising since the statute tracks federal Rule 10b-5 almost verbatim and the words "proximate cause" are not used in 10b-5. This fact does not lead to the ultimate conclusion, as argued by Rousseff, that the Florida legislature did not intend to require proof of proximate cause. To the

contrary, the Act's silence reinforces Hutton's point that the legislature undoubtedly intended Florida's antifraud statute to be interpreted consistently with federal law.

Rousseff agrees that the overriding concern of this Court should be the "effectuation of the manifest intention of the Legislature." See Sebesta v. Niklas, 272 So.2d 141, 145 (Fla. 1972). The Florida courts cautiously avoid judicial speculation when the intent of the Legislature is unclear. Id. Here, however, the legislature has spoken in clear and unequivocal terms -- it adopted a federal law virtually word for word. Section 517.301 has remained largely unchanged for 23 years.[1] There is no clearer legislative message.

Furthermore, adoption of Rousseff's "plain meaning" argument leads to anamolous results in this instance. First, his purportedly "restrictive" statutory construction approach results in a very broad reading of the statute. This approach contradicts the long-standing rule that statutes in derogation of the common law should be construed narrowly. Southern Attractions, Inc. v. Gran, 93 So.2d 120 (Fla. 1956); Sullivan v. Leatherman, 48 So.2d 836 (Fla. 1950). Second, it

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[1] See pages 14 - 15, infra, discussing amendments to Fla. Stat. § 517.301.

leads erroneously to the conclusion that this Court cannot define the elements of a legislated cause of action, such as whether or not scienter is necessary to establish a violation of § 517.301.[2]

Rousseff points to the other subsections of § 517.211 as "indicia of legislative intent" that loss causation has been rejected by the legislature. (Rousseff Brief pp. 12-16). The analysis is flawed and misleading. First, the fact that §§ 517.211(1) and 517.211(2) both provide for the remedy of rescission upon proof of violations of §§ 517.07 (securities registration), 517.12 (registration of securities sellers) and 517.301 (antifraud provision) does not lead to the sweeping conclusion that the legislature meant to require the same elements of proof for each of the underlying violations. To hold that § 517.301 requires proof of proximate cause does not rewrite § 517.211(2) or make § 517.211 internally

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[2] This Court has never determined whether scienter, or mere negligence, is necessary to establish a violation of § 517.301. In 1975, the Third District Court of Appeals in Merrill Lynch, Pierce, Fenner & Smith v. Byrne, 320 So.2d 436 (Fla. 3d DCA 1975) held that negligence was sufficient, choosing to follow existing federal authorities holding that negligence was sufficient to establish liability under 10b-5. In 1976, the United States Supreme Court resolved a conflict among federal courts when it ruled that proof of intent to deceive or "scienter" is a required element in Rule 10b-5 cases. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 96 S.Ct. 1375, 47 L.Ed.2d 668 (1976). In 1977, this Court discharged the writ of certiorari initially granted in the Byrne case. Merrill Lynch, Pierce, Fenner & Smith v. Byrne, 341 So.2d 498 (Fla. 1977). Thus, this Court has not addressed the issue since federal law has been clarified.

inconsistent. The legislature fully understood that the elements of the statutory violations could differ even though the remedies for violation are similar.

Second, the history of § 517.211, which Rousseff fails to discuss, suggests that the legislature acknowledged differences between claims premised upon §§ 517.07 and 517.12, on the one hand, and § 517.301, on the other.[3] Rousseff argues that the statutory "cut off" mechanism in 517.211 (allowing the defendant to "cut off" a claimant's right to sue by tendering back the full amount of the consideration paid) shows that the legislature did not intend to superimpose a causation requirement because it requires the return of the "full amount paid" rather than a lesser sum. (Rousseff Brief pp. 14-15). No such inference necessarily follows. However, even if it did, a cursory review of § 517.211 shows that the statutory offer provision only applies to cases brought under §§ 517.07 and 517.12, not 517.301. Compare § 517.211(1) with 517.211(2). Rousseff's statement that the "statutory offer" provision "applies as well to suits under subsection (2) of Section 211" is flatly wrong.[4] Rousseff Brief p. 15, n.4. Furthermore, the

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[3] Predecessor statutes to § 517.211 are reproduced in the Reply Brief Appendix.

[4] Rousseff cites Merrill Lynch, Pierce, Fenner & Smith v. Byrne, 320 So.2d 436 (Fla. 3d DCA 1975), writ discharged, 341 So.2d 498 (Fla. 1977), for (continued on the following page)

1979 revisions to § 517.211 are noteworthy. Prior to 1979, the so-called "statutory offer" provisions applied to "every sale made in violation of any of the provisions of this part." In 1979, the legislature rewrote § 517.211, making the "statutory offer" provisions applicable only to violations of §§ 517.07 and 517.12. See Ch. 79-381, Laws of Fla. This fact, ignored by Rousseff, shows unequivocally that the legislature viewed the underlying violations as inherently different. Thus, even if the legislature viewed the failure to register securities or the sale of securities by unlicensed sellers as "per se" violations of the Act, § 517.301 stands on a different footing. Requiring proof of proximate cause under § 517.301 in no way undermines Florida's other regulatory provisions.

III. This Court should look to Section 10b of the 1934 Act as the analogous statute to § 517.301.

Rousseff's tortured attempt to bootstrap § 517.301 under the umbrella of the Securities Act of 1933 (the "1933 Act") defies common sense and ignores the authorities he cites. Essentially, Rousseff attempts to link the Florida Act with

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(Continuation of [4])

this point but fails to tell the Court that Byrne was decided under the predecessor statute to § 517.211, § 517.21, that was repealed in 1978. The 1978 statute, § 517.211, was substantially rewritten in 1979, after Byrne.

the Uniform Securities Act of 1956 and then tie the Uniform Securities Act to Section 12(2) of the 1933 Act. (Rousseff Brief p. 25.) While there indeed may be a link between the Uniform Securities Act and the 1933 Act, the point is meaningless because Florida has not adopted the Uniform Act. National Conference of Commissioners on Uniform State Laws, 1987-88 Reference Book and list of states adopting Uniform Securities Act; J. Mofsky, Reform of the Florida Securities Law, 2 Fla. State University Law Review 1, 8 (1974); L. Loss, Fundamentals of Securities Regulation 878 n. 2 (2nd ed. 1988).[5] Florida has never adopted the Uniform Securities Act, and Rousseff's suggestion that the Florida statute is premised on the Uniform Act flies in the face of legislative history.

Rousseff next argues that the drafters of the Florida Act modeled the "civil liability" provisions of the Act on the Uniform Securities Act, citing Professor Mofsky. This is an egregious misstatement on Rousseff's part. Rousseff leads the Court to believe that the Florida Act was substantially revised in 1975. In fact, the legislature did not pass the proposed amendments to the Act in 1975. See History of Legislation, 1975 Regular Session, Florida Legislature (prepared by Legislative Information Division). There were

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[5] In fact, Professor Loss acknowledges that § 517.301 is "modeled on the SEC's Rule 10b-5." VI L. Loss, Securities Regulation 3789 (1969) (supplementing Vol. III, p. 1636 n. 30).

no changes at all to §§ 517.301 or 517.21 in 1975. Id. In fact, the civil liability provision commented on by Professor Mofsky has never been adopted by the legislature. See Proposed bill entitled "An act relating to securities" dated April 24, 1975, § 517.55. Rather, the legislature has retained in substantially the same language the antifraud provision drawn from Rule 10b-5. Thus there is no persuasive authority pointing to § 12(2) of the 1933 Act as the prototype for the Florida Act.

This Court need look no further than the words of § 517.301 and Rule 10b-5 to determine that Rule 10b-5 is the analogous statute. Rousseff's strained comparison between § 12 of the 1933 Act and the Florida Act is superficial at best. It is true that both the Florida Act and § 12 of the 1933 Act provide express, rather than implied, remedies for civil liabilities. Both the Florida Act and the 1933 Act govern similar conduct. But this fact does not mean that the 1933 Act is the analogous statute to § 517.301 to the exclusion of Rule 10b-5. The Florida Act governs conduct regulated by both the 1933 Act and the 1934 Act. Yet a substantive comparison between § 517.301 and 10b-5 actions shows that these similar provisions govern fraud actions and give much broader relief than that afforded under the 1933 Act.

- Only purchasers may sue under § 12 of the 1933 Act while both purchasers and sellers have a cause of action under the 1934 Act and the Florida Act. Compare § 12 of the 1933 Act (15 U.S.C. § 77l) with 17 C.F.R. 240.10b-5 and §§ 517.301(1)(a) and 517.211(2), Fla. Stat.

- Section 12 imposes liability only on one who "offers or sells a security." 15 U.S.C. § 77l. Rule 10b-5 and the Florida Act extend liability to persons other than those in strict privity with the claimant. 17 C.F.R. 240.10b-5; §§ 517.301(1)(a) and 517.211(2), Fla. Stat.

- The statute of limitations for actions brought under § 12 of the 1933 Act is short -- one year from the time the claimant knew or should have known of the untrue statement or omission but no more than three years from the date of sale. 15 U.S.C. § 77m. The limitations period for 10b-5 and Florida blue sky fraud actions is two years from the time the claimant knew or should have known of the misrepresentation or omission but no more than five years from the date of sale. § 95.11(4)(e), Fla. Stat.; Hudak v. Economic Research Analysts, Inc., 499 F.2d 996 (5th Cir. 1974), cert. denied 419 U.S. 1122, 95 S.Ct. 805, 42 L.Ed.2d 821 (1975).

- A 10b-5 and § 517.301 claimant must prove reliance on the fraudulent representations. See Alna Capital Assoc. v. Wagner, 758 F.2d 562, 565 (11th Cir. 1985); § 517.301(1)(a), Fla. Stat. A 1933 Act claimant does not need to prove reliance. Junker v. Crory, 650 F.2d 1349, 1359 (5th Cir. 1981).

- Claims under the 1934 Act and the Florida Act are arbitrable. Shearson/American Express, Inc. v. McMahon, ____ U.S. ____, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987); Oppenheimer & Co., Inc. v. Young, 475 So.2d 221 (Fla. 1985) (on remand); Melamed v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 476 So.2d 140 (Fla. 1985). The United States Supreme Court has not yet explicitly held 1933 Act claims arbitrable.[6] Wilko v. Swann, 346 U.S. 427, 74 S.Ct. 182, 98 L.Ed. 168 (1953).

In sum, the mere fact that the Florida Act and the 1933 Act specify a rescission remedy does not transform § 517.301 into an offspring of the 1933 Act. There are important differences in the liabilities giving rise to the rescission

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[6] Although Wilko v. Swann has not yet been specifically overruled by the Supreme Court, several courts have held that 1933 Act claims are arbitrable. See, e.g., Rodriguez de Quijas v. Shearson/Lehman Bros., Inc., 845 F.2d 1296 (5th Cir. 1988).

remedies. It is readily apparent that the antifraud provisions of the 1934 Act and the Florida Act strike common ground. It is no accident. In general, Rule 10b-5 covers a much broader range of conduct than § 12 of the 1933 Act. See Huddleston v. Herman & MacLean, 640 F.2d 534 (5th Cir. 1981), aff'd in part and reversed in part on other grounds, 459 U.S. 375, 103 S.Ct. 683, 74 L.Ed.2d 548 (1983); Berger v. Bishop Investments, 695 F.2d 302, 308 (8th Cir. 1982); Ross v. A.H. Robins Co., Inc., 607 F.2d 545 (2d Cir. 1979), cert. denied, 446 U.S. 946, 100 S.Ct. 2175, 64 L.Ed.2d 802 (1980); Chiarella v. United States, 445 U.S. 222, 100 S.Ct. 1108, 63 L.Ed.2d 348 (1980). The legislature's enactment of § 517.301 in 1965 obviously was to incorporate this expanded civil liability into the Florida Act.[7] Rousseff's position is a radical departure from the broad yet defined parameters of 10b-5. With this background in mind, the Court should construe § 517.301 and Rule 10b-5 consistently to require proof of proximate cause.

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[7] Rousseff is incorrect when he states that "long before 1965" the Florida Act provided private civil remedies for fraud in the sale of securities (Rousseff Brief p. 41). The predecessor statute to § 517.301, § 517.31, prohibited the making of false or fraudulent statements "in any matter within the jurisdiction of the Florida Securities Commission" and provided criminal penalties for its violation. Former § 517.31 was not a civil liability provision. The civil remedies applied to registration and licensing violations. See Ch. 14899, Fla. Laws (1931); former Fla. Stat. § 517.21; former Fla. Stat. § 517.19. The Florida cases cited by Rousseff are irrelevant since they pre-date the enactment of former § 517.31 and § 517.301 and were not brought under a Florida Act antifraud provision.

IV. Under Rule 10b-5, the loss causation requirement is an element of liability, not a damage limitation.

The federal courts have repeatedly recognized that loss causation under 10b-5 springs from the rule itself, not § 28 of the 1934 Act. See, e.g., Huddleston, supra; Gochnauer v. A. G. Edwards & Sons, Inc., 810 F.2d 1042, 1046 (11th Cir. 1987); Bastian v. Petren Resources Corp., 681 F. Supp. 530, reconsideration denied, 682 F. Supp. 956 (N.D. Ill. 1988). Section 28 defines the measure of damages when damages is the remedy of a Rule 10b-5 violation. Rousseff claims that because the Florida Act does not contain the equivalent of § 28 of the 1934 Act, there is no loss causation requirement. Again Rousseff invites this Court to confuse the underlying violation with the remedy. Huddleston, supra, makes it clear that proof of proximate cause is an element of the 10b-5 fraud claim that must be shown irrespective of whether the claimant's 10b-5 remedy is damages or rescission. See also Rousseff v. Hutton, 843 F.2d 1326 (11th Cir. 1988).[8] The Eleventh Circuit in Rousseff did not rely upon § 28 as the basis for requiring loss causation. Indeed, the Eleventh Circuit could not have concluded that a 10b-5 rescission case requires proof of proximate cause if, as Rousseff suggests, § 28 is the sole source of the requirement.

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[8] The Eleventh Circuit assumed, but did not decide, that the rescission remedy was available in federal securities actions. Rousseff, supra at 1328-29. The court noted that "the potential availability of this remedy does not alter the essential elements of the cause of action." Id.

Rousseff implies that Florida's statutory rescission remedies are fundamentally incompatible with proximate cause. This is not the case. The Eleventh Circuit found no inconsistency in requiring that Rousseff prove proximate cause despite his purported entitlement to rescission under 10b-5. "The causation requirement is satisfied in a Rule 10b-5 case only if the misrepresentation touches upon the reasons for the investment's decline in value." Huddleston, supra at 549. Having proved the link, a claimant is then entitled to whatever relief is afforded by § 517.211.

V. States that have adopted the Uniform Securities Act require proof of proximate cause.

Rousseff unequivocally claims that the states that have enacted the Uniform Securities Act do not require proof of loss causation. This statement is blatantly wrong.[9] In addition to Michigan, Minnesota and Washington have adopted the Uniform Securities Act and, unlike Indiana, their courts have held that proximate cause is an element of a fraud claim

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[9] As discussed in Hutton's main brief, the court in Campbell v. Shearson/American Express, Inc., Nos. 85-1703, 85-1714 (6th Cir. Sept. 9, 1987), concluded that Michigan's securities law (patterned after the Uniform Securities Act) required a showing of proximate cause. Rousseff dismisses this case as "wrongly decided." (Rousseff Brief p. 35.) Rousseff also cites Texas and New Hampshire cases, implying that these states have adopted the Uniform Securities Act and have interpreted their statutes to require proximate cause. In fact, Texas has not adopted the Uniform Securities Act, and the case cited by Rousseff involved a registration claim. See National Conference of Commissioners on Uniform State Laws, 1987-88 Reference Book and list of states adopting Uniform Securities Act. New Hampshire is a Uniform Act state, but the case cited by Rousseff was decided in 1917, long before the Uniform Securities Act was promulgated in 1956.

under state securities law. See Specialized Tours, Inc. v. Hogen, 392 N.W.2d 520 (Minn. 1986); Interlake Porsche & Audi v. Bucholz, 45 Wash. App. 502, 728 P.2d 597 (1986).

VI. Public policy factors favor requiring proof of proximate cause in fraud actions.

Rousseff and the amicus urge this Court, under the mantle of "investor protection," to make an unprecedented departure from legislative history and case law. The parties agree that the Florida Act serves the dual purposes of investor protection and full and fair disclosure. These goals are also the aim of Rule 10b-5 and the 1934 Act. See, e.g., Securities & Exchange Comm'n v. Southwest Coal & Energy Co., 624 F.2d 1312 (5th Cir. 1980); Cole v. Schenley Industries, Inc., 563 F.2d 35 (2d Cir. 1977). These purposes, however, did not compel the federal courts and should not, in itself, compel this Court to adopt an aberration unsupported by legislative history and case law.

The amicus claims that the legislature's most recent amendments to the Florida Act indicate tacit legislative approval of an expansive interpretation of § 517.301 where proximate cause is abandoned. Recent amendments, however, have not materially altered the substance of § 517.301(1) and are not inconsistent with a proximate cause requirement. In 1984, the legislature broadened § 517.301's parameters by making it applicable to "investments" in addition to

securities. In 1986, the legislature carefully revised the definition of "investment", declining to adopt the broad definition proposed by the 1985-86 Securities Regulation Task Force. Compare Appendix II of Amicus Brief, pp. 27, and 127 with Chapter 86-85, §§ 3 and 12, Laws of Florida (1986). Importantly, the legislature determines how and where the Florida Act diverges from its prototype. The enactment of stiffer criminal penalties for § 517.301 violations under certain circumstances presents no valid reason for fundamentally altering the liability elements. Contrary to the amicus, Hutton is not "creating" a technical defense. In this case, it simply seeks to have the fact finder determine whether the omission proximately caused the investor's loss.

It is true that Florida may impose stricter regulations than that provided by federal law. In fact, the Florida Act presently provides enhanced protection to the investor. For example, as noted by the amicus, § 517.301 applies to fraud in the sale of investments, not just securities as covered by the 1933 and 1934 Acts. Also, unlike federal law, the Florida Act permits the prevailing party to recover attorney fees. See Fla.Stat. § 517.211(6).[10] However, these

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[10] Additionally, a Florida court has held in a § 517.301 action that a claimant only has to prove that a defendant acted negligently rather than with scienter as required under federal law. See discussion, supra at 4 n. 2.

variances from federal law expanding investor protection are explicit in the statute and are not the result of judicial construction. In short, significant departures from federal law historically have been made by the legislature. Any further departures should be the subject of legislative action.

Like the Eleventh Circuit, this Court should not confuse protection with insurance. Neither Rule 10b-5 nor the Florida Act has any deterrent effect when the real cause of an investor's loss is a dramatic and unforeseen plummet in the market that is completely out of a defendant's control. This Court should decline to construe the antifraud provision of the Florida Act in such a way that is at odds with its federal counterpart and that transforms it into a strict liability statute.

CONCLUSION

The Florida antifraud provision is modeled after federal Rule 10b-5. Legislative history shows that the legislature intended it to be interpreted consistently with its prototype. A claimant under the 1934 Act must show proximate cause as an element of his claim whether the remedy is rescission or damages. There is no compelling reason for the Florida Act to deviate from these standard elements of

proof. Simply because the Florida Act expressly provides for a rescission remedy does not alter the conclusion that a claimant should show proximate cause in order to be entitled to the remedy. Statutory goals of investor protection and full disclosure are not frustrated by requiring proof of loss causation. The certified question should be answered "Yes."

Respectfully submitted,

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