



California Corporate & Securities Law

In A Securities Fraud Action, The Date Of Filing May Determine Whether You Win Or Lose (And I'm Not Referring To The Statute Of Limitations)

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Yesterday, I discussed one-half of the battle in [Zalkind v. Ceradyne, Inc.](#) Today, I address the securities law issues raised by Ceradyne's cross-complaint.

To recap, the Zalkinds (Stanley, Elizabeth and a limited partnership that they owned) sold assets to Ceradyne for stock and cash. The Zalkinds' suit against Ceradyne for failure to timely register the stock was the subject of yesterday's post. Today's post is dedicated to Ceradyne's cross-complaint for securities fraud under Corporations Code § 25401.

This case is noteworthy because it is a claim by an issuer (Ceradyne) against a purchaser (the Zalkinds) for securities fraud. The fact that a seller is able sue under § 25401 should come as no surprise because the statute makes it unlawful for any person to sell *or buy* a security in California by means of any written or oral communication that includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

Ceradyne's cross-complaint alleged the Zalkinds made misrepresentations and omitted material facts to inflate the value of the assets sold in exchange for stock. This post, however, isn't about Ceradyne's allegations. Rather, it concerns whether Ceradyne suffered damages.

Corporations Code § 25501 establishes alternative remedies for violations of § 25401. A seller may sue for rescission or damages. In this case, Ceradyne, the seller, sued for damages. Under § 25501, damages are determined by subtracting the price at which the security was sold (plus interest) from the value of the security *at the time of the filing of the complaint* (plus the amount of any income received by the defendant on the security).

If the "complaint" referred to in § 25501 is the complaint filed by the Zalkinds, then Ceradyne suffered (according to the court's calculation) damages of nearly \$1.6 million. However, if the "complaint" is understood to refer to Ceradyne's cross-complaint, then Ceradyne suffered no damages (again according to

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the court's calculation). Without getting into the details, the reason for this result was a steep decline in the value of Ceradyne's stock during the 11 months between the Zalkinds' filing of their complaint and Ceradyne's filing of its cross-complaint. The court concluded that the "complaint" in § 25501 refers to the pleading filed by the seller of securities asserting a violation of § 25401.

The court supported its conclusion about the meaning of "complaint" in § 25501 with extensive quotations from Marsh & Volk, *Practice Under the California Securities Laws*, a treatise for which I've served as a practice consultant for the last several years. (No, I don't receive a commission on sales, but I do receive a flat fee for consulting annual updates.)

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