



# California Corporate & Securities Law

## Section 25501.5 – What Do It Mean?

Posted In [California Securities Laws, Securities Litigation](#)

12/3/2010

In 2004, the California Legislature added Section 25501.5 to the Corporate Securities Law of 1968. Ever since then, I've been asked "[What do it mean?](#)"

Corporations Code Section 25501.5 generally authorizes an action for rescission (or damages, if the security is no longer owned) by any person "who purchases a security from or sells a security to a broker-dealer that is required to be licensed and has not". A right of rescission makes sense when the unlicensed broker-dealer is acting as a principal (*i.e.*, as a dealer). The statute makes less sense when the broker-dealer is acting as an agent (*i.e.*, as a broker). When a broker-dealer is acting as an agent, the purchaser acquires the security *from* the security's owner– not *from* the broker. It is certainly debatable whether a security owner should face a claim for rescission or damages when it is the broker-dealer that is violating the licensing requirement.

The questions of the scope of Section 25501.5 often arises in discussions of finders. The question of whether and under what circumstances an unlicensed person may be compensated for finding investors continues to bedevil issuers and their legal counsel. See Task Force on Private Placement Broker-Dealers, ABA Section of Business Law, "Report and Recommendations of the Task Force on Private Placement Broker-Dealers," 60 Business Lawyer 959 (May 2005). If a finder is required to be licensed as a broker-dealer but is not in fact licensed, what does it mean for the issuer under Section 25501.5? In this case, the finder is acting as agent rather than principal. The issuer, moreover, is likely to point out that the statute applies to "a person who purchases a security *from* . . . a broker-dealer . . ." and the securities are not being purchased *from* the finder. The debate then would seem to turn on what the meaning of "from" is.

The legislation was sponsored by the [Conference of Delegates of California Bar Associations](#) ("CCBA") and the legislative history does suggest that the legislation was aimed at unlicensed broker-dealers and not sellers. For example, the Senate Floor [analysis](#) states:

*Consequently, although we require brokers to be licensed, there is no provision in California that allows the injured party to bring an action for recession [sic] or seek damages **against a broker** for failing to comply with their license.*

The Assembly Floor [analysis](#) similarly states that according to the CCBA:

Please contact [Keith Paul Bishop](#) at Allen Matkins for more information [kbishop@allenmatkins.com](mailto:kbishop@allenmatkins.com)

<http://www.calcorporatelaw.com/>

*this bill is designed to address the problem of 'bucket shops' or 'boiler rooms' that engage in securities fraud. According to the sponsor, it specifically targets 'disreputable brokers who victimize consumers by operating illegally; unlicensed persons who sell products such as viaticals, mortgage pools, and pyramid or 'Ponzi' schemes; and persons licensed in a related field, like insurance, who sell securities to their existing clients without obtaining the proper securities licenses'.*

It remains to be seen how the courts will deal with Section 25501.5. By the way, that is not me in the video linked above – although I do own a brace of banjos. If you are wondering about what a bucket shop might be, see this [post](#) from last August.

Please contact **Keith Paul Bishop** at Allen Matkins for more information [kbishop@allenmatkins.com](mailto:kbishop@allenmatkins.com)

<http://www.calcorporatelaw.com/>