



# California Corporate & Securities Law

## The CSL And Membership Interests In LLCs

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Two decades ago, [Bob Rizzi](#) and I wrote an article for the California Business Law Reporter asking whether limited liability company legislation would ever be enacted in California. Only three years later, California enacted the Beverly-Killea Limited Liability Company Act, Corporations Code Section 17000 *et seq.* Stats. 1994, c. 1200 (SB 469).

As a member of the Senate Commission on Corporate Governance, Shareholder Rights and Securities Transactions, I participated in the drafting of the LLC act. Later, I entered state government during the period of time that SB 469 was wending its way through the legislature, serving initially as Deputy Secretary and General Counsel for the California [Business, Transportation & Housing Agency](#). The [Department of Corporations](#) is part of the BT&H Agency and I had responsibility for policy for the Department. Later, I served as Commissioner of Corporations.

At the time, the Department was concerned that it might be difficult and expensive to prove in each case that a membership interest in an LLC constituted a security for purposes of the Corporate Securities Law of 1968. In fact, at least one early commentator had concluded that LLC interests were probably not securities under the federal securities laws. Sargent, *Are Limited Liability Company Interests Securities?* 19 Pepperdine Law Review 1069, 1082 (1992). Thus, the Department pressed for an amendment to Corporations Code Section 25019 to include LLC membership interests in the laundry list of items that are securities. You can read more about the history of California's LLC legislation in my article, *Limited Liability Companies: Now That They Are Here, Some Words of Caution*, 16 CEB California Business Law Reporter 296 (1995).

Section 25019 does include one significant exception – an LLC interest is not considered a security if the person claiming the exception “can prove that all of the members are actively engaged in the management” of the LLC. Evidence of voting or informational rights or evidence of the right to participate in the LLC's affairs does not establish, without more, that all members are actively engaged in the management of the LLC.

The most obvious consequence of defining membership interests as securities is that the offer and sale of those interests by the LLC are subject to qualification pursuant to Corporations Code Section 25110. A much less obvious consequence is that changes in the member rights may be subject to qualification pursuant to Corporations Code Section 25120 (governing changes in the rights, preferences, privileges, or restrictions of or on outstanding securities). See my article, *No Way, Amending an Agreement can Violate State Securities Laws*, Los Angeles Daily Journal (June 14, 2010).

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