

*How to Use the California State Securities Act

Establish whether the Act applies to your particular transaction by reviewing Cal. Corp. Code Sec. 25008. Note that a sale can be deemed to occur in California even when the purchaser is in another state, and even when she or he communicates acceptance in the other state; see *Diamond Multimedia Sys., Inc. v. Superior Court*, 19 Cal 4th 1036, 1050 (Cal S. Ct. 1999).

First Swing under the Act

Surprisingly often you will find that an otherwise competent transactional lawyer has failed to properly qualify an offering for an exemption. The Act allows rescission of the entire transaction and all money back even if your client's plaintiff's case is problematic otherwise.

Ask for a certificate of non-registration from the California Department of Corporations. Under Cal. Corp. Code sections 25110 and 25102, the other side must then prove that a valid exemption applied as an affirmative defense.

Second Swing under the Act

Cal. Corp. Code section 25401 prohibits the offer, sale or purchase of a security through communications that include an untrue statement or omit a material fact. Remedies under Cal. Corp. Code section 25501 include rescission or a suit for damages.

Importantly, note what is **not** required:

- proof of reliance
- proof of causation
- proof of defendant's negligence

Rather, the affirmative defenses allowed under section 25501 are:

- proof that the defendant exercised reasonable care and did not know of the untruth or omission
- proof that even if the defendant had exercised reasonable care, he would not have known of the untruth or omission
- proof that the plaintiff knew the facts concerning the untruth or omission

See *Bowden v. Robinson*, 67 Cal. App. 3d 705, 715 (Cal. Ct. App. 1977)

Damages Include Interest

In *Boam v. Trident Financail Corporation*, (1992) 6 Cal.App.4th 738, the Court held that recovery under the Act **must** be calculated as follows: “Consideration” + “10% Annual Interest” less “Income received” = “Recovery”

Damages Can Include More than Interest

Legal fees will be included if financial elder abuse is shown or as a component of exemplary or punitive damages.

Claims Involving Registered Investment Advisers

When your client has entered into a contract for advisory services with a registered investment adviser, you should take a look at the Investment Advisers Act of 1940 because the U.S. Supreme Court has ruled that a limited private right of action exists under Section 215 for rescission if any portion of that Act has been violated. *Transamerica Mortgage Advisors, Inc. v. Lewis*, (1979) 444 U. S. 11, 19: “. . . customary legal incidents of voidness . . . follow, including the availability of a suit for rescission or for an injunction against continued operation of the contract, and for restitution.”

- If compensation to the adviser was based on appreciation of the assets, the client must have been a “qualified client” under Rule 205-3 [net worth in excess of \$1,500,000].
- Offering documents often confuse qualified investor with accredited investor qualifications—another legal give-me for the investor/plaintiff looking for securities violations.