Why Your Stock Certificate Is Not A Security

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Securities lawyers typically concern themselves with the federal securities laws (principally, the Securities Act of 1933, the Securities Exchange Act of 1934, and the two '40 Acts) and state "blue sky" laws (e.g., the California, the Corporate Securities Law of 1968). I find that practitioners tend to be far less familiar with Article 8 of the Uniform Commercial Code even though it is entirely devoted to investment securities.

California does not have an "Article 8" of the UCC. Rather, it is codified as "Division 8". In 1996, the California legislature repealed existing Division 8 and replaced it with a new Division 8 based on the 1994 revised UCC version. Cal. Stats. 1996, ch. 497 (SB 1591). The primary purpose of 1994 revisions was to address the indirect holding system of securities.

Division 8 defines "security" to include, among other instruments, "a share or similar equity interest issued by a corporation". Cal. Comm. Code § 8103(a). One might therefore assume that a stock certificate is a security. Conceptually, however, Division 8 distinguishes between the underlying intangible asset (i.e., the shares) and representations of that asset (e.g., a piece of paper that represents the asset). Thus, Division 8 refers to a "certificated security" and an "uncertificated security". Cal. Comm. Code §§ 8102(a)(4) & (18). A "securities certificate" means a certificate representing a security, it is not the security itself. Cal. Comm. Code § 8102(a)(16). This distinction is necessary so that Division 8 can have different rules for certificated and uncertificated securities.
For example, Section 8204 provides that a restriction on transfer imposed by an issuer, even if otherwise lawful, is ineffective against a person without knowledge of the restriction unless either (i) the security is certificated and the restriction is noted conspicuously on the security certificate; or (ii) the security is uncertificated and the registered owner has been notified of the restriction.

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