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Unanimous Supreme Court Sharply Limits Liability under Section 11 for Companies Issuing Securities Through Direct Listings

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In a unanimous decision, the U.S. Supreme Court held in *Slack Technologies v. Pirani*, No. 22-200, 2023 WL 3742580, 598 U.S. __ (June 1, 2023) that a claim under Section 11 of the Securities Act of 1933 is not viable unless a plaintiff is able to prove that the shares purchased were among the shares formally registered through the company's registration statement. In so holding, the Court vacated the Ninth Circuit's decision in *Pirani v. Slack Technologies*, 13 F.4th 940 (9th Cir. 2021) and followed historical precedent by sharply limiting liability under Section 11 claims related to direct listings.

Section 11 of the Securities Act of 1933

As discussed in detail in our prior insight on this case, Section 11 establishes a private cause of action for persons who acquired "such security" connected to a company's registration statement. To prevail on a Section 11 claim, a plaintiff must establish that: (1) the defendant is a signer of the registration statement, a director of the issuer, or an underwriter for the offering; (2) the plaintiff purchased the registered securities; and (3) any part of the registration statement for the offering contained an untrue statement of a material fact or omitted a material fact necessary to make the statements not misleading. This section imposes strict liability on defendants who make such untrue statements.

But Section 11?s requirement that only persons who acquired "such security" may bring a claim limits standing to those investors who purchased securities that were issued *under that registration statement*. For example, an investor who cannot determine whether the stock purchased was registered through the registration statement at issue or through an earlier (or later) registration of identical stock would not be able to maintain a Section 11 claim, because that investor would be unable to trace his stock to the allegedly misleading registration statement.

Supreme Court Vacates the Ninth Circuit's Holding

This case arises out of Slack Technologies' (Slack) "direct listing," a new alternative offering to the classic initial public offering introduced by the New York Stock Exchange in 2018 and later approved by the SEC, where companies can enter the public market without using underwriters or issuing any new shares, but, rather by permitting all existing shareholders to sell their unregistered shares publicly simultaneously with the company's own newly registered shares. Slack issued 118 million registered shares and 165 million existing unregistered shares in its direct listing, and the plaintiff purchased 250,000 Slack shares on the day Slack went public and over

the course of the next few months. When the price dropped, plaintiff filed a class action lawsuit against Slack, alleging the company violated Sections 11 and 12(a)(2) of the 1933 Securities Act by filing a materially misleading registration statement.

Slack moved to dismiss the complaint, arguing that since the plaintiff could not trace his shares to registered shares issued in the direct listing, he could not maintain his claims against the company under these statutes. The district court denied Slack's motion to dismiss, and in a case of first impression, the Ninth Circuit affirmed that ruling, holding that companies can face liability under Section 11 even where plaintiffs cannot prove their shares were issued from a registration statement. This holding had the potential to upend decades of precedent, as the Ninth Circuit became the first and only appellate court to hold that an investor plaintiff need not prove his shares were registered under a registration statement. Rather, the Ninth Circuit held that a plaintiff could maintain his or her claims if he or she could show that the shares were purchased in connection with a registration statement, even if the shares themselves were unregistered.

The Supreme Court granted *certiorari* to resolve this circuit split, and it held that Section 11 requires a plaintiff to plead and prove that he or she purchased securities registered under a materially misleading registration statement. Writing for a unanimous Court, Justice Gorsuch focused on the words "such security" and explained that "the statute repeatedly uses the word 'such' to narrow the law's focus."[1] This language suggests, according to the Court, that the securities referenced in Section 11 must be "registered under the particular registration statement alleged to contain a falsehood or misleading omission."[2] The Court, in further support, cited to other relevant portions of the Securities Act of 1933, such as Sections 5 and 6 and other subsections of Section 11, to show that the use of the word "such" requires that the security at issue be registered in order for Section 11 liability to attach.[3]

The Supreme Court Distinguishes Section 12 from Section 11

In a footnote at the end of its opinion, the Court was careful to explain that Sections 11 and 12 should be considered independent of each other, and "caution[ed] that the two provisions contain distinct language that warrants careful consideration."[4] The Court did not go any further than this, though, as it noted it had "no need to reach the merits" of whether Section 12 liability can attach for unregistered shares.[5] This caveat is, in part, based on the different statutory language found in each section: while Section 11 focuses on false or materially misleading registration statements, Section 12 creates liability for any person who "offers or sells a security . . . by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact."[6] Section 12, notably, does not specifically reference registration statements.[7]

The Future of Section 11 and Section 12 Cases Based on Direct Listings

This opinion provides much-needed clarity for businesses seeking to go public and pursue a direct listing instead of the classic IPO, at least with respect to Section 11 liability. The Supreme Court was clear in reaffirming decades of precedent and in holding that a plaintiff must plead and prove his or her security was registered under a registration statement (*i.e.*, traceable) in order for Section 11 liability to attach. Companies that go public through a direct listing may be able to forgo the risks associated with a potential Section 11 lawsuit. However, the Supreme Court's caveat with respect to Section 12(a)(2) may lead to lower courts allowing such cases based on direct listings to move forward. This could lead to a further circuit split as courts decide how to treat direct listings, which

are still relatively new to the public offering sphere.

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[1] *Slack Techs.*, 2023 WL 3742580, at *5.

[2] *Id.*

[3] *Id.*

[4] *Id.* at 6 n.3.

[5] *Id.*

[6] 15 U.S.C. § 77*l*(a)(2).

[7] *Id.*

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