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## *The Supreme Court Clarifies Who May Sue Under Section 11 of the Securities Act*

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On June 1, 2023, the Supreme Court issued a unanimous decision in *Slack Technologies, LLC v. Pirani*,<sup>1</sup> holding that a plaintiff asserting a claim under Section 11 of the Securities Act of 1933 (the "Securities Act")<sup>2</sup> must plead and prove that the securities they purchased are traceable to an allegedly misleading registration statement, even if the issuer has used a "direct listing" to offer its securities to the public. The opinion confirms that the decades-old tracing requirement will continue to be required for Section 11 claims, though the decision left open whether the same requirement would apply for claims under Section 12 of the Securities Act.

### **Background**

Under the Securities Act, companies are generally required to file a registration statement with the SEC before selling securities in a traditional initial public offering ("IPO").<sup>3</sup> To ensure that information contained in a registration statement is complete and accurate, the Securities Act created two private rights of action: under Section 11, where a plaintiff can bring an action for misstatements or omissions in a registration statement,<sup>4</sup> and under Section 12, where a plaintiff can bring claims for misstatements or omissions in other written or oral communications.<sup>5</sup> The Securities Act also exempts certain shares and transactions from the registration statement requirement.<sup>6</sup>

In recent years, some companies have pushed for ways to have their shares sold to the public without going through an IPO, which can be expensive and burdensome. In response, the New York Stock Exchange proposed, and the SEC approved, rules that would permit so-called "direct listings," whereby existing shareholders would be permitted to sell their shares directly to the public on an exchange without a registration statement. However, because other securities laws require certain shares to be registered, a direct listing creates the potential for both registered and unregistered shares to be sold to the public at the same time.

In 2019, Defendant Slack Technologies, LLC ("Slack") went public through a direct listing. As a result of the direct listing, both registered and unregistered Slack shares were simultaneously offered and sold to the public. A shareholder filed a class action complaint against Slack, alleging that Slack's registration statement and prospectus were misleading under both Section 11 and Section 12 of the Securities Act. The shareholder could not determine whether the shares he purchased were registered under the registration statement.

Slack moved to dismiss the shareholder's claims, arguing that Sections 11 and 12 only authorize a plaintiff to sue for misstatements or omissions in a registration statement if their shares were issued

pursuant to that registration statement. The trial court denied Slack's motion to dismiss, but certified its decision for an interlocutory appeal, and a divided panel of the Ninth Circuit affirmed the trial court's decision.

### **The Supreme Court's Decision**

The question before the Supreme Court was whether a plaintiff asserting a Section 11 claim is required to plead and prove that their securities were traceable to an allegedly misleading registration statement. In answering yes, the Court focused on the following Section 11 language:

In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue [certain enumerated parties].<sup>7</sup>

The Court analyzed whether the term "such security" refers to a security issued pursuant to the allegedly misleading registration statement or if it also encompassed a security that was not issued pursuant to that statement. The Court determined from various contextual clues that the statute was only referring to securities issued pursuant to the allegedly misleading registration statement. These clues included the fact that the statute refers to "*the* registration statement" such that the definite article references a "particular registration statement alleged to be misleading, and in this way seems to suggest the plaintiff must 'acquir[e] such security' under that document's terms."<sup>8</sup>

The Court also observed its decision was consistent with longstanding authority across the courts of appeal, which, until this case, had uniformly held that to bring a claim under Section 11, the securities held by the plaintiff must be traceable to the particular registration statement alleged to be false or misleading.<sup>9</sup>

The Supreme Court expressly reserved judgment on whether the same tracing requirement would apply to the shareholder's Section 12 claim. In affirming the denial of Slack's motion to dismiss the Section 12 claim, the Ninth Circuit noted that its analysis on the Section 12 claim "follow[ed] from" its analysis of the Section 11 claim.<sup>10</sup> After rejecting the Ninth Circuit's Section 11 analysis, the Supreme Court vacated the judgment on the Section 12 claim for reconsideration. While the Supreme Court said it "express[ed] no views about the proper interpretation of §12 or its application to this case," it did "caution that the two provisions contain distinct language that warrants careful consideration" and that it did not "endorse the Ninth Circuit's apparent belief that §11 and §12 necessarily travel together."<sup>11</sup>

### **Key Takeaways**

The decision preserves what has been a bedrock principle of Section 11 jurisprudence for many years—that shareholders who allege a Section 11 violation must be able to trace the purchase of their shares to the allegedly misleading registration statement. A contrary ruling would have significantly expanded the potential scope of liability for issuers, particularly for those who use offerings exempt from the registration requirement. Whether the tracing requirement will apply to Section 12 claims remains to be seen in light of the Court's holding and remand to the Ninth Circuit on that issue. And, whatever the outcome of the Section 12 claim is in the court below, it is quite possible the Supreme Court will be asked to take up the same question on the traceability requirement for Section 12 claims.



*If you have any questions concerning these developing issues, please do not hesitate to contact either of the following Paul Hastings New York lawyers:*

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<sup>1</sup> No. 22-200, slip op, (U.S. June 1, 2023).

<sup>2</sup> 15 U.S.C. § 77k.

<sup>3</sup> *Id.* § 77e.

<sup>4</sup> *Id.* § 77k.

<sup>5</sup> *Id.* § 77l.

<sup>6</sup> *Id.* § 77c-d.

<sup>7</sup> *Id.* § 77k(a).

<sup>8</sup> *Slack*, slip op. at 6.

<sup>9</sup> *See, e.g., Barnes v. Osofsky*, 373 F.2d 269, 272 (2d Cir. 1967).

<sup>10</sup> *Slack*, slip op. at 10 n.3 (quoting 13 F.4th 940, 949 (9th Cir. 2021)).

<sup>11</sup> *Id.*

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