Supreme Court Clarifies Pleading Requirement for Claims Arising Under the Securities Act of 1933

By: Eric J. Belfi and Guillaume Buell, Labaton Keller Sucharow LLP

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The U.S. Supreme Court recently clarified the scope of certain claims for securities class actions brought pursuant to Section 11 of the Securities Act of 1933. The Court held that an investor who alleges claims regarding a purportedly defective registration statement (often issued in connection with an IPO or secondary public offering), must specifically allege that he purchased some shares traceable to that registration statement.

Facts of the Case

The case involved claims against Slack Technologies, a company that offers a platform for instant messaging. In 2019, Slack conducted a "direct listing" on the New York Stock Exchange. Because Slack "employed a direct listing rather than an IPO, there was no underwriter and no lockup agreement" and thus, "holders of preexisting unregistered shares were free to sell them to the public right away." Using a direct listing rather than an IPO purportedly allowed Slack to avoid paying "significant transaction costs." The direct listing "offered for purchase 118 million registered shares and 165 million unregistered shares" to which the Plaintiff in the case bought 30,000 Slack shares on the day the direct listing went public, and 220,000 additional shares over the next few months. After the Plaintiff purchased the shares, Slack's stock price dropped, leading to a class-action lawsuit. *Slack Technologies* v. *Pirani*, 598 U.S. 759, 764 (2023).

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The lawsuit alleged that Slack violated Section 11 by filing a materially misleading registration statement: which touted the business and "implied that the Slack App was a market leader with unique advantages over its competitors and that [Slack] possessed the ability to scale up its services to reach more lucrative enterprise customers," However, Slack's "growth was [allegedly] slowing down in several aspects, including its key metric, [daily active users]." *Pirani* v. *Slack Technologies*, 445 F. Supp. 3d 367, 374 (N.D. Cal. 2020).

The 1933 Act requires a company to "register the securities it intends to offer to the public with the Securities and Exchange Commission" and "[a]s part of that process, a company must prepare a registration statement that includes detailed information about the firm's business and financial health so prospective buyers may fairly assess whether to invest." And the "law imposes strict liability on issuing companies when their registration statements contain material misstatements or misleading omissions." *Slack*, 598 U.S. at 762.

The case resolved a dispute among lower federal courts about the reach of Section 11 claims. To interpret the scope of Section 11 standing, the Supreme Court analyzed whether the term "such security" in the statute refers only to a security issued pursuant to the allegedly misleading registration statement, or also includes a security not issued pursuant to that registration statement. *Id.* at 766-767.

The Supreme Court concluded that the statute "imposes liability for false statements or misleading omissions in 'the registration statement'" and "[t]he statute uses the definite article to reference the 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." As a result, Section 11 "requires a plaintiff to plead and prove that he purchased shares traceable to the allegedly defective registration statement." *Id.* at 766-767, 770.

Key Takeaways

Going forward, shareholders bringing Section 11 claims will have to plead and prove they purchased shares traceable to the defective registration statement they claim caused them to suffer harm. A future battle before the Supreme Court may also be in the offing with respect to claims under Section 12 of the 1933 Act, which the Court declined to address. ◆

Eric J. Belfi and Guillaume Buell *are Partners in the New York office of Labaton Keller Sucharow LLP.*

An accomplished litigator, Eric Belfi represents many of the world's leading pension funds and other institutional investors concerning the merits of U.S. and non-U.S. securities, shareholder, and other investment-related litigation. Eric advises clients throughout the lifecycle of an action, participating in the complaint drafting process, as well as litigation, mediation, and settlement strategy meetings. Eric is a member of the Firm's Executive Committee and head of the Client Development Group.

With over a decade of experience in securities law, Guillaume Buell represents investors based in the United States, the United Kingdom, and Europe in connection with domestic and international securities litigation, corporate governance matters, and shareholder rights disputes. His clients include a wide range of pension funds, asset managers, insurance companies, and other sophisticated investors.