

Ninth Circuit: Plaintiff Who Purchased Shares in a Direct Listing Has Standing Under Section 11 and Section 12(a)(2) Regardless of Whether Shares Were Registered or Unregistered

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On September 20, 2021, the Ninth Circuit affirmed a ruling that a stockholder who purchased shares of a company that went public through a direct listing had standing under Section 11 and Section 12(a)(2) of the Securities Act even though he could not determine if he had purchased registered or unregistered shares in the direct listing. *Pirani v. Slack Techs.*, 2021 WL 4258835 (9th Cir. 2021) (Restani, J.). The court held that plaintiff had standing because his shares “could not be purchased without the issuance of [the company’s] registration statement, thus demarking these shares, whether registered or unregistered, as ‘such security’ under Sections 11 and 12 of the Securities Act.”

Background and Plaintiff’s Allegations

In 2019, plaintiff purchased shares on the day the company went public through a direct listing. Following a stock price drop related to service disruptions, plaintiff brought a class action against the company, its officers and directors, and venture capital fund investors, based on the company’s registration statement and prospectus issued in the direct listing. Plaintiff brought claims for violations of Section 11 and Section 12(a)(2) of the Securities Act alleging the company’s registration statement was inaccurate and misleading. The company challenged whether plaintiff had statutory standing to sue under Section 11 and Section 12(a)(2) because he could not prove that his shares were registered under the allegedly misleading registration statement.

Standing Exists Under Section 11 Because a Direct Listing Registration Statement Simultaneously Allows Sales of Both Registered and Unregistered Shares

Noting that this is a case of first impression, the court framed the issue as “what does ‘such security’ mean under Section 11 in the context of a direct listing, where only one registration statement exists, and where registered and unregistered securities are offered to the public at the same time, based on the existence of that one registration statement[.]”^[1] The court explained that under the NYSE’s direct listing rule^[2] a company must file a registration statement in order to engage in a direct listing. The court continued that the SEC “interprets this reference to a registration statement in the rule as an effective registration statement filed pursuant to the Securities Act of 1933.” The court then noted

that a direct listing—as opposed to an IPO—has no bank-imposed lock-up period during which unregistered shares are kept out of the market, both registered and unregistered shares are immediately sold to the public at the time of the effectiveness of the registration statement, and the same registration statement makes it possible to sell both types of shares.

The court determined that the company’s “unregistered shares sold in a direct listing are ‘such securities’ within the meaning of Section 11 because their public sale cannot occur without the only operative registration in existence.” As there was only one registration statement here, the court stated that all of the stock sold in this direct listing, whether labeled as registered or unregistered, was traceable to that one registration. The court determined that plaintiff pled facts sufficient to establish standing under Section 11 and affirmed the denial of dismissal. Separately, the court stated that “Section 12 liability (resulting from a false prospectus) is consistent with Section 11 liability (resulting from a false registration statement).” Accordingly, statutory standing exists under Section 12(a)(2) to the extent it parallels Section 11.

Circuit Judge Miller Dissents

Circuit Judge Miller dissented stating that he would have reversed and remanded with instructions to dismiss in full. Judge Miller explained that plaintiff lacked standing under Section 11 because he could not show that the shares he purchased “were issued under the allegedly false or misleading registration statement[.]” If “such security” meant that a plaintiff must have purchased shares “issued under the allegedly false or misleading registration statement” in successive-registration cases, then that is what it should also mean in direct-listing cases. He cited similar reasons for concluding that plaintiff also lacked standing under Section 12.

[1] Section 11 of the Securities Act states, “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 mis-leading, any person acquiring *such security* . . . may, either at law or in equity, in any court of competent jurisdiction, sue—(1) every person who signed the registration statement” (emphasis added).

[2] NYSE Listed Company Manual, Section 102.01B, Footnote E.

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