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The Supreme Court Maintains Limitations on 1933 Act Claims for Direct Listings

***by* Susan E. Hurd** and **Madeleine G. Juszynski**

On June 1, 2023, the Supreme Court issued its unanimous opinion in the *Slack Technologies LLC, et al. v. Pirani* appeal.[1] The appeal addressed the question of what the scope of liability should be for claims brought under Sections 11 and 12 of the Securities Act of 1933 ("the 1933 Act") when a company has gone public through what is known as a "direct listing." A direct listing allows a company to make shares available for public trading without going through a traditional underwritten initial public offering.

A company must still file a registration statement to be able to pursue a direct listing. The registration statement will allow existing shares held by employees or early investors to be sold publicly, but unregistered shares (those that would otherwise be exempt from the registration requirement) may be sold simultaneously alongside the registered shares. In this type of direct listing, which Slack underwent in June 2019, an investor who purchases shares may not know whether the particular shares they purchased were registered or unregistered.

Sections 11 and 12 of the 1933 Act allow an investor to sue for allegedly false and misleading statements in a registration statement or prospectus. Under the existing body of case law, much of which was developed prior to the advent of direct listings, a private plaintiff cannot sue under these provisions unless he or she can prove that the shares they purchased were registered under the particular registration statement being challenged as false or misleading. This limitation on who can bring claims is known as the "tracing" requirement. Pirani had successfully argued before the Ninth Circuit that this traditional concept of tracing should not be applied when shares began to trade publicly through a direct listing. The Supreme Court disagreed.

The Court's decision focused on Section 11, presumably because of the well-developed and largely uniform case law that had long recognized tracing as a requirement for Section 11 claims. The Supreme Court engaged in a textual analysis of Section 11 and other provisions of the 1933 Act before determining that this

[1] *Slack Technologies, LLC, fka Slack Technologies, Inc., et al. v. Pirani*, No. 22-200 (June 1, 2023). Justice Gorsuch delivered the opinion of the Court.

analysis supported the existing rule of law – namely, that tracing was required for Section 11 claims.[2] Indeed, until the Ninth Circuit's judgment in this case, every court of appeals to have considered the question for over 50 years had reached that same conclusion.

The Supreme Court vacated the Ninth Circuit's judgment that tracing for Section 11 claims was not required in direct listings and instructed the court below to apply that rule to Pirani's claims on remand.[3] On appeal, Slack voiced the opinion that Pirani had already conceded tracing would be impossible for him. If that is the conclusion the lower court reaches on remand, then Pirani's Section 11 claims should be dismissed.

Pirani had also argued on appeal that he should be allowed to pursue claims under Section 12 of the 1933 Act because, in his opinion, tracing was not required for such claims. The Supreme Court declined to address that issue. This was not particularly surprising. At oral argument, certain Justices made comments suggesting that they were reluctant to issue a substantive opinion on Section 12 because (1) the case law is less developed for Section 12 claims compared with Section 11 claims; (2) the lower court failed to engage in a separate analysis of Section 12 and instead ruled that liability under Section 12 necessarily followed whenever liability existed under Section 11; and (3) the text of Section 12 is different from that of Section 11, which meant that a separate analysis of Section 12 should have occurred.

The Supreme Court nevertheless vacated the Ninth Circuit's judgment that tracing was not required for Section 12. The Supreme Court explained that the Ninth Circuit's decision that Pirani's Section 12 claims could "proceed 'follow[ed] from' its analysis of his [Section] 11 claim."[4] Accordingly, because the Court held the Ninth Circuit's analysis of Section 11 was "flawed, … the best course [was] to vacate its judgment with respect to Mr. Pirani's [Section] 12 claim as well for reconsideration in light of [the] holding … about the meaning of [Section] 11."[5]

While some commentators previously expressed concern that this appeal could expand the scope of liability for companies engaging in direct listings (as well as for companies that chose to go public through more traditional means), that always seemed like an unlikely scenario in light of the well-established precedent on Section 11. The fact that direct listings were a relatively new phenomenon did not, standing alone, justify a substantial departure from the prevailing view that Section 11 liability should be more narrow than other provisions of the federal securities laws. Of most interest on remand will be how the lower court addresses the criticism that it did not engage in an independent analysis of Section 12 and the Supreme Court's directive that it should give "careful consideration" to the "distinct language" of that provision.[6]

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2 Slip op. at 6-8.

3 *Id.* at 9-10.

4 *Id.* at 10 n.3.

5 *Id.*

6 *Id.*

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Securities Litigation Group

Gidon M. Caine
650.838.2060
gidon.caine@alston.com

Elizabeth Gingold Clark
404.881.7132
elizabeth.clark@alston.com

Charles W. Cox
213.576.1048
charles.cox@alston.com

Mary C. Gill
404.881.7276
mary.gill@alston.com

Susan E. Hurd
404.881.7572
susan.hurd@alston.com

Brett D. Jaffe
212.210.9547
brett.jaffe@alston.com

John A. Jordak, Jr.
404.881.7868
john.jordak@alston.com

John L. Latham
404.881.7915
john.latham@alston.com

Robert R. Long
404.881.4760
robert.long@alston.com

Cara M. Peterman
404.881.7176
cara.peterman@alston.com

Theodore J. Sawicki
404.881.7639
tod.sawicki@alston.com

Andrew Sumner
404.881.7414
andy.sumner@alston.com

ALSTON & BIRD

WWW.ALSTON.COM

ATLANTA: One Atlantic Center ■ 1201 West Peachtree Street ■ Atlanta, Georgia, USA, 30309-3424 ■ +1 404 881 7000 ■ Fax: 404.881.7777
BEIJING: Hanwei Plaza West Wing ■ Suite 21B2 ■ No. 7 Guanghua Road ■ Chaoyang District ■ Beijing, 100004 CN ■ +86.10.85927500
BRUSSELS: Rue Guimard 9 et Rue du Commerce 87 ■ 3rd Floor ■ 1000 Brussels ■ Brussels, 1000, BE ■ +32 2 550 3700 ■ Fax: +32.2.550.3719
CHARLOTTE: 1120 South Tryon Street ■ Suite 300 ■ Charlotte, North Carolina, USA 28203-6818 ■ +1 704 444 1000 ■ Fax: +1 704 444 1111
DALLAS: Chase Tower ■ 2200 Ross Avenue ■ Suite 2300 ■ Dallas, Texas, USA, 75201 ■ +1 214 922 3400 ■ Fax: 214.922.3899
FORT WORTH: Bank of America Tower ■ 301 Commerce ■ Suite 3635 ■ Fort Worth, Texas, USA, 76102 ■ +1 214 922 3400 ■ Fax: 214.922.3899
LONDON: LDN:W ■ 6th Floor ■ 3 Noble Street ■ London ■ EC2V 7DE ■ +44 20 8161 4000
LOS ANGELES: 333 South Hope Street ■ 16th Floor ■ Los Angeles, California, USA, 90071-3004 ■ +1 213 576 1000 ■ Fax: 213.576.1100
NEW YORK: 90 Park Avenue ■ 15th Floor ■ New York, New York, USA, 10016-1387 ■ +1 212 210 9400 ■ Fax: 212.210.9444
RALEIGH: 555 Fayetteville Street ■ Suite 600 ■ Raleigh, North Carolina, USA, 27601-3034 ■ +1 919 862 2200 ■ Fax: 919.862.2260
SAN FRANCISCO: 560 Mission Street ■ Suite 2100 ■ San Francisco, California, USA, 94105-0912 ■ +1 415 243 1000 ■ Fax: 415.243.1001
SILICON VALLEY: 755 Page Mill Road ■ Building C - Suite 200 ■ Palo Alto, California, USA 94304-1012 ■ +1 650 838 2000 ■ Fax: 650.838.2001
WASHINGTON, DC: The Atlantic Building ■ 950 F Street, NW ■ Washington, DC, USA, 20004-1404 ■ +1 202 239 3300 ■ Fax: 202.239.3333