Section 11 Elements and Defenses under the Securities Act

Go to: Elements of a Section 11 Claim | Defenses to Section 11 Claims | Practical Considerations
Maintained

by *Kenneth P. Held*, Fletcher Held, PLLC

This practice note summarizes the elements of a claim for securities fraud under Section 11 (*15 U.S.C. § 77k*) of the Securities Act of 1933, as amended (Securities Act), and the available defenses. After discussing various considerations for Section 11 plaintiffs and defendants and the elements of a Section 11 claim, this note focuses on Section 11 defenses, including (1) the one-year statute of limitations and three-year statute of repose, (2) the due diligence defense, (3) negative causation, and (4) the plaintiff's actual knowledge of misstatements or omissions.

For further information on securities fraud claims and related issues, see *Liability under the Federal Securities Laws for Securities Offerings*, *Liability for Securities Offerings Checklist*, and *U.S. Securities Laws*.

For additional information on liability provisions and potential defenses under the federal securities laws, see *Securities Act and Exchange Act Liability Provisions*, *Section 12(a)(2) Elements and Defenses under the Securities Act*, *Control Person Liability*, *Reliance in Securities Fraud Actions*, *Materiality in Securities Fraud Actions*, *Scienter Defenses in Securities Fraud Actions*, *Special Litigation Committees*, *Securities Litigation under the Private Securities Litigation Reform Act (PSLRA)*, *U.S. Supreme Court Securities Litigation Decisions*, *Defense Strategies under the Securities Act*, *Jurisdictional Defenses under the Exchange Act*, and *Jurisdictional Defenses under the Securities Act*.

Elements of a Section 11 Claim

Overview

Section 11 imposes strict liability on issuers and signatories and negligence liability on underwriters if, at the time a registration statement became effective, the statement either contained an untrue statement of a material fact or omitted to state a material fact required to make the registration statement not misleading. *15 U.S.C. § 77k(a)*; see also *City of Pontiac Policemen's & Firemen's Ret. Sys. v. UBS AG, 752 F.3d 174, 182 (2d Cir. 2014)*.

In a Section 11 suit, a plaintiff must show that it purchased securities in the offering or that its securities are traceable to the offering. The plaintiff generally does not need to show that:

- It relied on the relevant registration statement
- The misstatement or omissions caused its losses –or–
- The defendant had a culpable state of mind (also known as scienter)

See *N.J. Carpenters Health Fund v. Royal Bank of Scot. Group., PLC, 709 F.3d 109, 120 (2d Cir. 2013)*.

In addition, Section 11(e) of the Securities Act limits the damages available to a Section 11 plaintiff to the difference between:

- The amount paid for the security (not exceeding the price at which the security was offered to the public) –and–
- Either:
  - The value of the security as of the time the suit was brought
  - The price at which the security was disposed of in the market before suit –or–

○ The price at which the security was disposed of after the suit but before judgment if it is less than the difference between the purchase price and the value of the security at the time of suit

15 U.S.C. § 77k(e). This list of damages theories is exclusive.

Section 11 Plaintiffs

A plaintiff bringing suit under Section 11 must plead and show that it has standing under Article III of the U.S. Constitution as well as statutory standing under the Securities Act. Defendants can challenge plaintiff's standing in a motion to dismiss under *Federal Rule of Civil Procedure (FRCP) 12(b)(1)*—because a plaintiff's lack of standing divests the court of subject matter jurisdiction over the plaintiff's claim—or on the merits of the case in a motion to dismiss under *FRCP 12(b)(6)*.

A plaintiff may pursue claims on behalf of a putative class of investors for securities that they did not purchase if they allege both Article III standing and class standing. *NECA-IBEW Health & Welfare Fund v. Goldman Sachs & Co., 693 F.3d 145, 162 (2d Cir. 2012)*. In the context of class actions, Article III standing requires that "for every named defendant there must be at least one named plaintiff who can assert a claim directly against that defendant." *NECA, 693 F.3d at 159*. If that requirement is satisfied, the inquiry shifts to a class standing analysis. *NECA, 693 F.3d at 159*. Class standing requires that the conduct allegedly causing plaintiffs' Article III loss "implicates the same set of concerns as the conduct alleged to have caused injury to other members of the putative class by the same defendants." *NECA, 693 F.3d at 162* (holding that plaintiffs had standing to assert claims for mortgage-backed securities they did not purchase where the claims were based on same registration statement for securities they did purchase, but plaintiffs did not have standing to assert claims against originators from whom they did not purchase securities). Where the alleged injury is based on misrepresentations, "the misconduct alleged will almost always be the same," but "[w]hether that conduct implicates the same set of concerns . . . will depend on the nature and content of the specific misrepresentation alleged." *NECA, 693 F.3d at 162*. See also *Youngers v. Virtus Inv. Partners, Inc., 195 F. Supp. 3d 499 (S.D.N.Y July 1, 2016)* (finding Article III standing to assert claims regarding securities plaintiff did not purchase (and involving different investment strategies) where claims were based on same prospectus that included allegedly false statements of performance history.).

Purchasers may sue under Section 11 if they either:

- Purchased the securities at the time of the initial public offering (IPO) –or–
- Made aftermarket purchases and can trace their shares to the allegedly misleading registration statement

15 U.S.C. § 77k(a); *Bradley v. ARIAD Pharms. (In re Ariad Pharms. Inc. Sec. Litig.), 842 F.3d 744, 755–56 (1st Cir. 2016)*; *DeMaria v. Andersen, 318 F.3d 170, 178 (2d Cir. 2003)*. The tracing requirement sometimes raises fact issues that cannot be resolved on a motion to dismiss, but is often a proper subject for a motion for summary judgment.

Aftermarket purchasers must trace their securities to the challenged offering. This is often a hurdle for plaintiffs and becomes increasingly difficult when an issuer makes more than one offering of the securities or the securities have entered the market by other means (such as founders' shares, employee benefit plans, or secondary offerings). Courts have rejected plaintiffs' attempts to establish that their shares are traceable to the offering:

- By tracing their securities using statistical analysis (see *Krim v. PCOrder.com, 402 F.3d 489, 494–502 (5th Cir. 2005)*; *In re Puda Coal Secs., Inc., 2013 U.S. Dist. LEXIS 142081, at *6–9 (S.D.N.Y. Oct. 1, 2013))*
- When other securities not issued in the relevant offering enter the market, including in a secondary offering of securities (see *Petzschke v. Century Aluminum Co. (In re Century Aluminum Co. Sec. Litig.), 729 F.3d 1104, 1110 (9th Cir. 2013))*
- If the purchaser acquired its stock after the filing of the initial registration statement but before the filing of a misleading amendment (see *Guenther v. Cooper Life Sciences, 759 F. Supp. 1437, 1440 (N.D. Cal. 1990))*

The First Circuit recently held that a plaintiff had standing to sue under Section 11 and Section 12(a)(2) even though he could not determine if he had purchased registered or unregistered shares in a direct listing authorized by a 2018 NYSE rule. *Pirani v. Slack Techs., Inc., 13 F.4th 940, 943 (9th Cir. 2021)*. The Court concluded that plaintiff had standing because his shares could not be purchased without the issuance of the registration statement. The shares sold in the direct listing, both registered and unregistered, were sold “by means of a prospectus” because the prospectus was part of offering materials (i.e., registration statement and prospectus) that permitted shares to be sold to public.

Section 11 Defendants

The following persons can be held liable under Section 11 for material misstatements or omissions in an issuer's registration statements:

- The issuer
- Persons who sign the registration statement
- Directors of or partners in the issuer
- Any individual named in the registration statement as being or about to become a director of or partner in the issuer
- Professionals named with their consent as having prepared or certified any part of the registration statement, including accountants, engineers, and appraisers
- The underwriters of the security

See *15 U.S.C. § 77k(a)*; *Herman & MacLean v. Huddleston, 459 U.S. 375, 381–82, 386 n.22 (1983)*.

Because Section 11 imposes a stringent standard of liability, courts construe these exclusive categories narrowly. Even if an individual played a part in preparing the registration statement, they cannot be liable under Section 11 if they do not fall into one of the enumerated categories. For example, officers of a corporation are not proper Section 11 defendants if they do not otherwise fall into one of the Section 11 categories listed above. See *Huddleston, 459 U.S. at 386 n.22*.

Section 11 Claim Key Requirements

Section 11 imposes strict liability on issuers and signatories and negligence liability on underwriters if the registration statement for the securities contains an untrue statement of a material fact or omits to state a material fact required to make it not misleading. *15 U.S.C. § 77k(a)*; see also *City of Pontiac Policemen's & Firemen's Ret. Sys. v. UBS AG, 752 F.3d 173, 182 (2d Cir. 2014)*.

A material fact is one that a reasonable investor would have viewed as "having significantly altered the 'total mix' of information made available." *TSC Indus. v. Northway, Inc., 426 U.S. 438, 449 (1976)*.

Courts have found that the analysis for materiality under Section 11 is similar to the analysis under Section 10(b) (*15 U.S.C. § 78j*) and may apply case law from the Section 10(b) context to Securities Act claims. See, e.g., *McMahan & Co. v. Wherehouse Entertainment, 900 F.2d 576, 579 (2d Cir. 1990)*.

Omitted information may serve as the basis for a Section 11 claim if the plaintiff establishes that all of the following are true:

- The prospectus contained an omission.
- The omission was material.
- The defendant was under a duty to disclose the omitted information because the omission either violates a company's affirmative legal disclosure obligations or is necessary to prevent a material existing disclosure from being misleading.

• The omitted information existed at the time the prospectus became effective.

See *Oxford Asset Mgmt. v. Jaharis, 297 F.3d 1182, 1189 (11th Cir. 2002)*; *Litwin v. Blackstone Group, L.P., 634 F.3d 706, 715–16 (2d Cir. 2011)*. The failure to disclose information required under Items 105 (“the material factors that make an investment in the registrant or offering speculative or risky”) and 303 (“any known trends or uncertainties that have had or that are reasonably likely to have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations.”) of SEC Regulation S–K can serve as the basis of claims under Section 11. *Garnett v. RLX Tech. Inc., No. 21 CIV. 5125 (PAE), 2022 U.S. Dist. LEXIS 179365, at *15 (S.D.N.Y. Sept. 30, 2022)*. If the omitted information is publicly known, however, it need not be disclosed. Wandel v. Gao, No. 1:20-CV-03259 *(PAC), 2022 U.S. Dist. LEXIS 45099, at *8 (S.D.N.Y. Mar. 14, 2022)* (for the issuer “to be liable under the Securities Act, it would have had to possess some special, non-public insight into how these public developments [regarding COVID] could affect its business.”).

Materiality is a mixed question of law and fact requiring a contextual analysis. The U.S. Supreme Court has cautioned against the use of statistical thresholds to establish that a fact was not material. *Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 40–41 (2011)*. However, courts may dismiss claims where the alleged misrepresentation or omission is so obviously unimportant that reasonable minds cannot differ on its immateriality. See *Klein v. General Nutrition Cos., 186 F.3d 338, 342–43 (3d Cir. 1999)*; *Parnes v. Gateway 2000, 122 F.3d 539, 546–47 (8th Cir. 1997)*.

For more information on materiality, see *Materiality: Relevant Laws, Guidance, and Determination Guidelines* and *Materiality in Securities Fraud Actions*.

Statements of Opinion

In *Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension Fund, 135 S. Ct. 1318 (2015)*, the Supreme Court addressed the scope of liability for false opinion statements under Section 11 of the Securities Act. The Court held that "a sincere statement of pure opinion is not an 'untrue statement of material fact,' regardless whether an investor can ultimately prove the belief wrong." *Omnicare, Inc., 135 S. Ct. at 1327*. Under that standard, opinion statements give rise to liability under only three circumstances:

• When the speaker does not "actually hold[] the stated belief"

• When the statement contains false "embedded statements of fact"

• When the omitted facts "conflict with what a reasonable investor would take from the statement itself"

Omnicare, Inc., 135 S. Ct. at 1326–27, 1329.

A threshold question is whether the statement at issue is one of fact or opinion. For example, the First Circuit found certain statements to be actionable statements of fact. The court found the statement “[T]he company’s software ‘improves our performance for backing up virtual environments and makes us really competitive” could be construed as a statement of fact “at least to the extent that it plainly implied some better ‘performance for backing up virtual environments.’” The Court also found the statement “we have put something out that we think is just completely competitive and just a super strong product” conveyed three facts (1) that defendant “actually believed [the product] to be ‘completely competitive’ and ‘super strong,’” (2) that “his opinion ‘fairly align[ed] with the information’ that [defendant] possessed at the time,” and (3) that “his opinion was based on the type of reasonable inquiry that an investor in context would expect to have been made.” *Constr. Indus. & Laborers Joint Pension Tr. v. Carbonite, Inc., 22 F.4th 1, 7 (1st Cir. 2021)*. On the other hand, the Eleventh Circuit found that statements made by a pharmaceutical company’s (Axogen) statements about the number of people that suffer nerve damages each year and require nerve repair procedure, thus requiring Axogen’s products, to be statements of opinion. Thus, plaintiff’s “failure to plausibly allege—or even attempt to argue on appeal—Axogen's actual knowledge dooms its 33 Securities Act claims.” *Einhorn v. Axogen, Inc., 42 F.4th 1218, 1225 (11th Cir. 2022)*.

The *Omnicare* decision provides a powerful defense to misrepresentation claims based upon statements of opinion. For example:

- The Third Circuit affirmed the district court's partial dismissal of a shareholder suit arising out of a merger between two banks in *Jaroslawicz v. M&T Bank Corp., 962 F.3d 701 (3d Cir. 2020)*. The court rejected the shareholders' argument that the bank's projection of when the merger would close provided grounds for liability because the opinion turned out to be wrong, reaffirming that "a plaintiff cannot state a claim by alleging only that an opinion was wrong." *Jaroslawicz, 962 F.3d at 717* (quoting *Omnicare, 575 U.S. at 194*).
- In *Chapman v. Mueller Water Prods.*, plaintiffs alleged false and misleading statements concerning the company's financial health, including reports on the defendant company's financial results, its risk disclosures, and a $9.8 million warranty charge; statements made during an investor call discussing quarterly results; and in Sarbanes-Oxley certifications. *Chapman, 2020 U.S. Dist. LEXIS 102389 at *28–29*. The court dismissed the claims because plaintiffs offered no evidence suggesting that defendants lacked an "honest belief" in these statements, that defendants knew the information was false, or that the omitted information made the opinions misleading to a reasonable investor. *Chapman, 2020 U.S. Dist. LEXIS 102389, at *30–31, 71*.
- In *In re Adient PLC Secs. Litig., 2020 U.S. Dist. LEXIS 58730 (S.D.N.Y. Apr. 2, 2020)*, plaintiffs alleged that defendant had made false and misleading statements that it was positioned to expand its profit margins. The court dismissed plaintiffs' claims because plaintiffs failed to adequately show that "any Defendant falsely or unreasonably held the opinions they public discussed," and the statements at issue were mere statements of goals and belief that do not run afoul of *Omnicare. In re Adient PLC Secs. Litig., 2020 U.S. Dist. LEXIS 58730, at *55–56*.
- In *In re Ocular Therapeutix, Inc. Secs. Litig.*, the court found that a chief executive officer's (CEO's) statement that the company "think[s]" it had remedied deficiencies leading to the FDA's denial of its New Drug Application was inactionable, even where the FDA later rejected the resubmitted application. *In re Ocular Therapeutix, Inc. Secs. Litig., 2019 U.S. Dist. LEXIS 77120, at *26–27 (D. Mass. Apr. 30, 2019)*. Not only did the CEO's language "signal[] to investors that his statement was an opinion and not a guarantee," but he also cautioned that it was up to the FDA to determine whether or not those deficiencies were corrected. *2019 U.S. Dist. LEXIS 77120, at *26–27*.

The key question is often whether a complaint sufficiently pled the omission of contrary facts that rendered positive opinions regarding the company's business misleading, and failure to plead such facts has led to dismissal of a number of claims based on statements of opinion. See, e.g., *Carvelli v. Ocwen Fin. Corp., 934 F.3d 1307, 1323 (11th Cir. 2019)* (plaintiff's allegations failed to show the defendant's "statements of opinion are mutually exclusive of—or even inconsistent with—[the company]'s alleged knowledge," and therefore fell short of *Omnicare*'s pleading standard.) *Police & Fire Ret. Sys. v. Plains All Am. Pipeline, L.P., 777 Fed. Appx 726, 731 (5th Cir. 2019)* (Plains II) (Despite the fact a regulatory agency had identified issues concerning a small part of the company's varied operations, the company's "belief statements" regarding its compliance "were broadly applicable and therefore were not rendered false or misleading" by issues that affected "a small percentage" of the company's pipelines.).

Forward-Looking Statements

Forward-looking statements refer to information, such as estimates, projections, plans, and objections. *15 U.S.C. §§ 77z-2(i) and 78u-5(i)*. Depending on the facts, the defendant may challenge a Section 11 claim based on forward-looking statements under either the statutory safe harbor under the Private Securities Litigation Reform Act (PSLRA) or the "bespeaks caution" doctrine.

This PSLRA safe harbor applies if one of the following two prongs are met:

- **First prong.** The statements are identified as forward-looking and are accompanied by meaningful cautionary language or are immaterial.

- **Second prong.** Plaintiff fails to prove that the statements were made with actual knowledge that they were false.

See *15 U.S.C. § 77z-2*. In ruling on a motion to dismiss, the court can consider both the forward-looking statement and the accompanying cautionary language, even if the cautionary language is not quoted in the complaint. However, this safe harbor does not protect defendants from claims based on forward-looking statements made in connection with an IPO. *15 U.S.C. §§ 77z-2, 78u-5*.

The judicially-developed "bespeaks caution" doctrine, which pre-dated the enactment of the PSLRA, also provides that forward-looking statements accompanied by meaningful cautionary language are not actionable. Bespeaks caution, however, may be used in situations where the PSLRA does not apply, such as an IPO. Like the PSLRA, the doctrine requires that the cautionary language and disclosures must be precise and fact-specific and address the substance of each forward-looking statement. Generalized, boilerplate warnings are not sufficient. See *Grossman v. Novell, Inc., 120 F.3d 1112, 1120 (10th Cir. 1997)*; *Miller v. Pezzani (In re Worlds of Wonder Sec. Litig.), 35 F.3d 1407, 1414 (9th Cir. 1994)*.

Defenses to Section 11 Claims

Statute of Limitations and Statute of Repose

Statute of Limitations – Discovery vs. Inquiry Standard

Under Section 13 (*15 U.S.C. § 77m*) of the Securities Act, a plaintiff must bring a suit asserting Section 11 claims within one year after the plaintiff discovered the violation or, with reasonable diligence, could have discovered the violation. Appellate courts generally agree that the "discovery notice" standard (as opposed to the stricter "inquiry notice" standard) applies to determine when the plaintiff was on notice of the plaintiff's claim. Under the discovery standard, the limitation period does not begin to run until the plaintiff discovers or should have discovered the facts constituting the offense. Under the inquiry notice standard, the statute begins to run when the facts would lead a reasonably diligent plaintiff to investigate further, regardless of when the plaintiff actually discovered or could have discovered those and other facts constituting the offense.

The U.S. Supreme Court has held that the discovery standard applies to fraud claims under the Securities Exchange Act of 1934, as amended (Exchange Act). See *Merck & Co. v. Reynolds, 559 U.S. 633, 653 (2010)*. Under the *Merck* standard, the court may consider the plaintiff's inquiry notice to show a time when the facts would have prompted a reasonably diligent plaintiff to begin investigating. However, the limitations period does not begin to run until the plaintiff discovers, or a reasonably diligent plaintiff would have discovered, the facts constituting the offense, regardless of whether the actual plaintiff undertook a reasonably diligent investigation.

The appellate courts that have considered the issue agree that the discovery standard announced in *Merck* applies not only to the Exchange Act claims but also to the Securities Act claims. See *Fed. Hous. Fin. Agency v. Nomura Holding Am., Inc., 873 F.3d 85, 119 (2d Cir. 2017)*; *Pension Trust for Operating Eng'rs v. Mortgage Asset Securitization Transactions, Inc., 730 F.3d 263, 273 (3d Cir. 2013)*. Although lower courts remain divided, the weight of the authority leans toward the courts that have applied the discovery standard to Securities Act cases. See *Yi Xiang v. Inovalon Holdings, Inc., 268 F. Supp. 3d 515, 520–21 n.1 (S.D.N.Y. 2017)* (collecting cases).

Statute of Repose

Plaintiffs must assert Section 11 claims within three years after the offering of the security to the public. *15 U.S.C. § 77m*. This statute of repose begins when the security is "bona fide offered to the public," which most courts consider to be the effective date of the registration statement. See, e.g., *Yates v. Mun. Mortg. & Equity, LLC, 744 F.3d 874, 898 (4th Cir. 2014)*; *Footbridge Ltd. Trust v. Countrywide Fin. Corp., 770 F. Supp. 2d 618, 623 (S.D.N.Y. 2011)*.

Due Diligence Defense

Defendants other than the issuer can avoid liability under Section 11 by demonstrating that they conducted a reasonable investigation with regard to the information contained or incorporated in the registration statement. *15 U.S.C. § 77k(b)(3)*.

Underwriters and other nonexpert defendants, such as directors or officers, can defeat liability under the Section 11 due diligence defense by showing they met the applicable standard of care, which depends on whether the challenged portion of the registration statement was "made on the authority of an expert." *15 U.S.C. § 77k(b)(3)*. The standard applies as follows:

- **Expertized portions.** A non-issuer defendant can avoid liability for the expertized portions of a registration statement if they had no reasonable ground to believe and did not believe that a material misstatement or omission existed. This is sometimes referred to as the reliance defense because the underwriters and other non-issuer defendants are permitted to rely in good faith on the work of the relevant expert for those portions of the registration statement. Examples of expertized portions of a registration statement include the audit opinion from an independent registered accounting firm concerning the registrant's financial statements or a report from an independent petroleum engineer concerning a registrant's oil and gas reserves.
- **Non-expertized portions.** A non-issuer defendant can avoid liability for non-expertized portions of a registration statement if the defendant shows that it had, after reasonable investigation, reasonable ground to believe and did believe that there was no material misstatement or omission. *15 U.S.C. § 77k(b)(3)(A)*. Courts generally hold non-issuer defendants to a negligence standard of care under this provision.

For non-expertized portions of the registration statement, a defendant must conduct a reasonable investigation to provide reasonable grounds for the belief that the registration statement did not contain any material misrepresentations or omit any material facts. What constitutes a reasonable investigation depends on a person's level of authority and involvement with the issuer. Executive officers who sign the registration statement and management directors are held to such a high due diligence standard that their liability approaches the near absolute liability of the issuer. Outside directors are held to a lesser standard but must nevertheless investigate to gain knowledge of all the relevant facts, and may not merely rely on management's representations, especially if there are any "red flags."

Negative Causation

In contrast with claims under *Rule 10b-5*, in which plaintiff bears the burden to plead and prove that an alleged misstatement or omission caused its losses, Section 11 of the Securities Act does not require a plaintiff to prove causation, but rather provides a statutory affirmative defense that can limit or eliminate damages to the extent that the defendants establish that other factors caused the plaintiff's losses. *15 U.S.C. § 77k(e)*.

The defendant bears the burden of demonstrating that something other than the alleged omissions or misstatements caused the plaintiff's loss. Where a defendant meets this heavy burden, a plaintiff must then come forward with evidence that the price decline actually resulted from the alleged misstatement or omission. *In re Barclays Bank PLC Sec. Litig., 2017 U.S. Dist. LEXIS 148695, at *40–41 (S.D.N.Y. Sep. 13, 2017)*.

To overcome a negative causation defense at the pleading stage, the plaintiff simply has to allege that the misrepresentation relates to the reasons for an investment's decline in value. *Hildes v. Arthur Andersen LLP, 734 F.3d 854, 861 (9th Cir. 2013)*; *In re Facebook, Inc., 986 F. Supp. 2d 487, 523 (S.D.N.Y. 2013)*. Some courts, however, have found that the allegations on the face of a complaint may provide a complete causation defense where the court cannot attribute most of a security's decline to an alleged corrective disclosure, such as when:

- The drop in stock price occurs before the disclosure of negative information to the public. See, e.g., *In re Giant Interactive Group, Inc. Sec. Litig., 643 F. Supp. 2d 562, 572 (S.D.N.Y. 2009)*.
- The plaintiff sells the stock at a price higher than its purchase price. See, e.g., *In re Velti PLC Sec. Litig., 2015 U.S. Dist. LEXIS 135004, at *89 (N.D. Cal. Oct. 1, 2015)*.

The negative causation defense in Section 11 mirrors the loss causation requirement in Section 10(b), and courts apply the case law addressing loss causation under Section 10(b) and *Rule 10b-5* to Section 11 claims. See, e.g., *Amorosa v. AOL Time Warner, Inc., 409 Fed. Appx. 412, 415–16 (2d Cir. Feb. 2, 2011)*; *Ning Yu v. State Street Corp. (In re State Street Bank & Trust Co. Fixed Income Funds Invs. Litig.), 774 F. Supp. 2d 584, 590 & n.4 (S.D.N.Y. 2011)*.

Plaintiff's Actual Knowledge of Specific Misstatement or Omissions

A defendant can defeat liability under Section 11 if it proves that the plaintiff knew about the falsity of the alleged misrepresentation at the time it purchased the security. *15 U.S.C. § 77k(a)*. See also *Miles v. Merrill Lynch & Co. (In re Initial Pub. Offering Sec. Litig.), 483 F.3d 70, 73 n.1 (2d Cir. 2007)*; *DeMaria v. Andersen, 318 F.3d 170, 175 (2d Cir. 2003)*.

The defendant bears the burden of showing that, at the time when the plaintiff purchased the security at issue, the plaintiff had actual knowledge of the untruth or omission. A defendant may rely on a plaintiff's individual communications or widely known information exposing an untruth or omission to assert this defense. Constructive knowledge or suspicion of falsity, however, does not bar a purchaser's recovery under Section 11. See, e.g., *Royal Bank, 709 F.3d at 127 n.12*; *Fed. Hous. Fin. Agency v. HSBC N. Am. Holdings, Inc., 33 F. Supp. 3d 455, 480 (S.D.N.Y. 2014)*.

Practical Considerations

Although Section 11 imposes strict liability on issuers and signatories and negligence liability on underwriters if the registration statement for the securities contains an untrue statement of a material fact or omits to state a material fact required to make it not misleading, there are a number of defenses to Section 11 claims that you as defense counsel should analyze when the complaint is filed, many of which can be raised in a motion to dismiss the complaint. These potential defenses include:

- Lack of standing, either because plaintiff did not (1) purchase the securities at issue or (2) purchase the securities in the offering or cannot trace their purchase to the offering because they purchased their securities in the secondary market when there has been a prior offering of the security
- Plaintiff failed to allege a material misstatement or omission because the claims are based on:
  - Statements of opinion that are not actionable under *Omnicare*
  - Forward-looking statements (identified as such) that are accompanied by meaningful cautionary language and protected by the PSLRA safe harbor
- Due diligence defense for underwriters
- The one-year statute of limitations or three-year statute of repose
- The negative causation defense, especially where the facts alleged in the complaint demonstrate that something other than the alleged omissions or misstatements caused the plaintiff's loss

Current as of: ***10/28/2022***

End of Document