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Circuits split over whether social media posts may give rise to section 12 seller liability

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Section 12 of the Securities Act of 1933 imposes liability on a person who "offers or sells" unregistered securities or registered securities "by means of a prospectus or oral communication" containing material misstatements or omissions to "the person purchasing such security from him." 15 U.S.C. § 12(a). A person can qualify as a seller under the statute if he or she passes the security's title to the plaintiff or solicits the plaintiff's purchase of the securities. *Pinter v. Dahl*, 486 U.S. 622, 643 (1988).

Most courts have held that to qualify the defendant as a seller, the defendant's solicitation must directly target the plaintiff. Otherwise, the plaintiff did not purchase the security "from" the defendant, as the statute requires. However, some courts appear to be calling that long-standing requirement into question, as recent decisions from the 9th and 11th U.S. Circuit Courts of Appeals suggest that mass communications made on social media can make a person a statutory seller.

Wildes v. BitConnect Int'l PLC and *Pino v. Cardone Capital*, two cases decided in the past year from the 11th and 9th Circuits, respectively, held that public social media posts can qualify as solicitations under Section 12. *See Wildes v. BitConnect Int'l PLC*, 25 F.4th 1341 (11th Cir. 2022), *cert. denied sub nom. Arcaro v. Parks*, 143 S. Ct. 427 (2022); *Pino v. Cardone Cap*., LLC, 55 F.4th 1253 (9th Cir. 2022).

The 11th Circuit's February 2022 decision arose from an alleged cryptocurrency platform's promotional videos. Defendant BitConnect minted a token, the BitConnect coin, and promoters subsequently made thousands of online videos encouraging consumers to purchase the coin. They also provided free online cryptocurrency courses, which helped viewers create BitConnect accounts. These videos generated millions of views. Once the coin's price fell, however, two plaintiffs sued under Section 12, alleging that the company and its promoters sold unregistered securities, in an attempt to recoup their alleged losses.

The district court dismissed the claim on the grounds that the plaintiffs based their case on having watched the videos, which were made for and viewed by millions of people. It reasoned that a person was a statutory seller under Section 12 only if he or she made a direct or personal solicitation. The plaintiffs repleaded, amending their complaint to add additional plaintiffs who allegedly purchased BitConnect through the promoters' referral links. The district court also dismissed the amended complaint, finding that the new plaintiffs likewise never received any "personal solicitation" or targeted communications from the promoters.

On appeal, the 11th Circuit reversed. The panel rejected the argument that Section 12 requires a targeted solicitation to a specific, prospective buyer. It noted that the Securities Act prohibits a person from using "any means or instruments of . . . . communication in interstate commerce" to sell an unregistered security.

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Further — and notably citing only cases that did not arise under the Securities Act — the court reasoned that "people understood solicitation" to include circulars and radio at the time the Securities Act was enacted. Accordingly, it reasoned that it does not matter whether a person pitches a security in a letter or video, as the liability would potentially attach either way. The court ultimately concluded that the plaintiffs sufficiently alleged that the videos constitute solicitations, making the defendants statutory sellers under Section 12.

Similarly, the 9th Circuit's December 2022 decision derived from promotions a real estate investment fund made across its social media accounts. Two private equity funds, Cardone Equity Fund V (Fund V) and Cardone Equity Fund VI (Fund VI), were classified as emerging growth companies under the 2015 U.S. JOBS Act and were subject to Regulation A, a rule exempting certain offerings from SEC registration requirements.

Fund V raised $50 million in September 2019, prompting its parent's CEO to promote both funds' investment opportunities on the company's Instagram account and YouTube page. Fund VI

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subsequently raised $50 million by June 2020. Investors filed a putative class action soon after, alleging that the fund and its members made material misstatements or omissions under Sections 12 and 15 of the Securities Act of 1933 regarding the returns investors could expect to receive from the fund, and that statements in social media posts and offering circulars lacked cautionary language identifying the risks associated with the investments.

The district court dismissed the claims, holding that neither the CEO nor the parent qualified as a statutory seller under Section 12, thus precluding all claims. In its ruling, the district court, like the district court in the 11th Circuit, emphasized the lack of relationship between the plaintiff and defendants, noting the posts consisted entirely of general statements made on public social media accounts that highlighted the benefits of investing in Funds V and VI.

In light of the emerging split, litigants will likely continue to dispute whether mass communications made over social media can make a person a statutory seller. This divergence, in turn, adds a new layer of considerations for businesses seeking to raise capital.

The 9th Circuit reversed. Adopting the 11th Circuit's reasoning from 10 months prior, the Court held the social media posts qualified as solicitations under Section 12. The Court found that "the advertisements at issue in this case — Instagram posts and YouTube videos — are the types of potentially injurious solicitations that are intended to command attention and persuade purchasers to invest in funds," even if they are generalized and do not target specific purchasers. Accordingly, the Court held the investors plausibly alleged that the defendants were sellers under § 12(a)(2).

In rejecting the rule that a solicitation must target the plaintiff, the 9th and 11th Circuit decisions appear to create a circuit split. While no other circuit has yet addressed whether use of social media can make a defendant a statutory seller, the 2nd U.S. Circuit Court of Appeals, for instance, has held that a plaintiff must demonstrate the defendant "actually solicited" the plaintiff's specific investment in order for the defendant to qualify as a seller under Section 12. *See Capri v. Murphy*, 856 F.2d 473, 478–79 (2d Cir. 1988).

In *Capri*, investors in a coal mining venture sued the venture's general partnership, alleging that the entity, its general partners, and the venture's promoter were liable as a seller under Section 12. *Id*. at 476-77. The court found that the general partners and the promoter were liable as Section 12 sellers, but the partnership was not. *Id*. at 479. It reasoned that even though the record contained "extensive correspondence" on the partnership's behalf discussing the promotional efforts, this was insufficient to demonstrate Section 12 liability, as it lacked evidence of actual solicitation. *Id*. In contrast, the general partners had "circulated the prospectus to plaintiffs" and "contemplated and authorized" the promoter's interactions with plaintiffs, satisfying the actual solicitation requirement of Section 12. *Id*. at 478. Likewise, the promoter was in "direct communication with plaintiffs" throughout, further cementing his liability as a Section 12 seller. *Id*.

Similarly, the 3rd U.S. Circuit Court of Appeals requires that a defendant engage in a "direct and active" solicitation of a plaintiff to qualify as a Section 12 seller. *See Craftmatic Sec. Litig. v. Kraftsow*, 890 F.2d 628, 636 (1989). In *Craftmatic*, investors alleged a furniture company that issued securities, among others, qualified as a seller under Section 12 because it prepared the purportedly misleading prospectus. *Id*., at 631-32.

The 3rd Circuit rejected this argument, concluding "[t]he purchase must demonstrate direct and active participation in the solicitation of the immediate sale to hold the issuer liable as a § 12(2) seller." *Id*. at 636. Because Section 12 requires that the plaintiff purchase the security "from" the defendant, the inquiry focuses "on the relationship between the purchaser and the" defendant. *Id*.

The 5th and 10th U.S. Circuit Courts of Appeals have also endorsed this perspective. For example, in *Lone Star Ladies Inv. Club v. Schlotzsky's Inc*., the 5th Circuit held that an issuer who promoted shares in a sandwich franchise by preparing a prospectus and conducting a road show could not be held liable as a Section 12 seller based solely on these activities. *See Lone Star Ladies Investment Club v. Schlotzsky's Inc*., 238 F.3d 363, 370 (5th Cir. 2001). Rather, investors had to show that the issuer went beyond its "usual" role and "became a vendor's agent." *Id*.

Similarly, the 10th Circuit held in *Maher v. Durango Metals, Inc.* that a company and its owner were not liable as statutory sellers under Section 12 because the plaintiff "alleged no facts indicating that either [defendant] solicited his purchase of the Durango stock." *Maher v. Durango Metals, Inc.*, 144 F.3d 1302, 1307 (10th Cir. 1998).

The reasoning from the 2nd, 3rd, 5th and 10th Circuits is in accord with the requirement in Section 12 that the defendant be liable only to the person who "purchas[ed] such security from him." *Craftmatic*, 890 F.2d at 636. However, the courts in *Wildes* and *Pino* declined to address both the statutory language and this reasoning.

In light of the emerging split, litigants will likely continue to dispute whether mass communications made over social media can make a person a statutory seller. This divergence, in turn, adds a new layer of considerations for businesses seeking to raise capital. Because social media communications have given rise to potential statutory seller status in two of the 12 circuit courts across the United States, plaintiffs may seek jurisdictions that follow the approach endorsed by the 9th and the 11th Circuits.

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