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Tenth Circuit Holds that "Forced Sellers" Resulting From a Squeeze Out Merger Lack Standing to Assert Claims Under Sections 11 and 12(a)(2) the Securities Act of 1933

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In *Katz v. Gerardi*, No. 10-1407, 2011 WL 3726279 (10th Cir. Aug. 25, 2011), the United States Court of Appeals for the Tenth Circuit affirmed the dismissal of claims alleging violations of Section 11 and Section 12(a)(2) of the Securities Act of 1933 (the "1933 Act"), 15 U.S.C. §§ 77k, 77*l*(a)(2), against a real estate investment trust ("REIT"). The claims were brought by a former minority unitholder of a REIT who, as part of a "squeeze-out merger" of the REIT with another entity, exchanged his units for cash. The Court held that the merger did not force the plaintiff to purchase newsecurities, but only to sell his old securities. Because Sections 11 and 12(a)(2) of the 1933 Act provide a private right of action only for purchasers, *not* sellers, of securities, the Tenth Circuit held that plaintiff lacked standing to assert a claim. The decision confirms that shareholders involved in forced sales resulting from a merger may not bring claims under the Section 11 and 12(a)(2) of the 1933 Act.

This action centers around Jack P. Katz ("Katz"), a minority unitholder in a REIT controlled by the majority unitholder, Archstone Smith Trust, a public company. Katz held his interest in the Archstone REIT in the form of "A-1 Units." The A-1 Units had certain advantages — liquidity rights, dividend rights and tax indemnification — that allegedly made them particularly valuable to Katz. Archstone entered into a merger agreement in which two investors

acquired all of Archstone's outstanding public shares. As part of the merger, Katz was squeezed out of the REIT and had the option of receiving either cash or stock in the newly formed entity in exchange for his shares. Katz opted for cash. Claiming the offering documents associated with the merger contained false and misleading statements or omissions, Katz sued alleging violations of Sections 11 and 12(a)(2) of the 1933 Act. Section 11 of the Securities Act imposes liability on issuers and other signatories of a registration statement that "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 misleading." Similarly, Section 12(a)(2) imposes liability under similar circumstances with respect to prospectuses. The United States District Court for the District of Colorado dismissed Katz's 1933 Act claims, holding that he was not a purchaser of securities when he opted to sell his shares and therefore lacked standing under the statute. Katz appealed.

Katz argued that he was a purchaser under the securities laws for a single reason: the merger caused a "fundamental change" of his A-1 units that so altered the nature of his investment as to transform them into "new" A-1 Units. In his view, the A-1 Units lost their valuable liquidity, dividend and tax indemnification features "the minute the Archstone board accepted the Merger, creating *de facto* new A-1 units." Katz argued that the merger effectively forced him to purchase the "new" A-1 Units, which lacked the advantageous characteristics of the "old" units, for purposes of his Sections 11 and 12(a)(2) claims.

The Tenth Circuit rejected this argument. The Court held that the merger did not force Katz to purchase new securities, but only to sell his A-1 Units for cash or new units. Furthermore, the Tenth Circuit held that the "fundamental change" or "forced seller" doctrine — which enables a shareholder, whose investment has been fundamentally changed, to meet the causation and reliance requirements of the securities laws even though the shareholder has not made an actual purchase or sale of securities — did not apply because (1) the doctrine only

applies to claims under the Securities Exchange Act of 1934, whereas Katz's claims arose under the 1933 Act, and (2) even assuming the doctrine did apply to Katz's claims, the doctrine did not make him a "purchaser" of securities because "in a forced sale, he [was] still a *seller*, not a purchaser." Thus, since Katz's claims only gave standing to purchasers of securities, which Katz was not, the Tenth Circuit held that his claims were properly dismissed.

This decision confirms that claims under Sections 11 and 12(a)(2) of the 1933 Act are limited to "purchasers" of securities, and are not available to "forced sellers" resulting from squeeze-out mergers.

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