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Supreme Court to Review Second Circuit's Decision That *American Pipe* Tolling Does Not Apply to the Securities Act's Three-Year Statute of Repose

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The Supreme Court of the United States has granted certiorari in *Public Employees' Retirement System of Mississippi v. IndyMac MBS, Inc.*, taking up an issue that affects the management of class action securities litigation. Specifically, the United States Court of Appeals for the Second Circuit held that the tolling rule of *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974) – tolling statutes of limitations for putative class members upon the commencement of a class action – does not apply to the three-year statute of repose that governs claims under Sections 11, 12(a), and 15 of the Securities Act of 1933 (the “Securities Act”).¹ See *Police & Fire Ret. Sys. of Detroit v. IndyMac MBS, Inc.*, 721 F.3d 95 (2d Cir. 2013). The Supreme Court's review of the Second Circuit's holding in *IndyMac* is likely to resolve an issue on which some courts have disagreed.

¹ Section 13 of the Securities Act establishes a one-year statute of limitations, triggered for Section 11 and Section 12(a)(2) claims by “the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence,” and for Section 12(a)(1) claims by “the violation upon which it is based.” Continuing, Section 13 establishes a three-year statute of repose, as follows: “In no event shall any such action be brought to enforce a liability created under [Section 11 or Section 12(a)(1)] ... more than three years after the security was bona fide offered to the public, or under [Section 12(a)(2)] ... more than three years after the sale.” 15 U.S.C. § 77m.

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Competing Views on Applicability of *American Pipe* Tolling

American Pipe and its progeny establish that “the commencement of a class action suspends the applicable *statute of limitations* as to all asserted members of the class who would have been parties had the suit been permitted to continue as a class action,” regardless of whether putative class members seek to intervene in the class or file their own independent actions. *IndyMac*, 721 F.3d at 100, 105 (emphasis added) (quoting *American Pipe*, 414 U.S. at 554). The Court in *American Pipe* reasoned that tolling was appropriate because class action lawsuits satisfy the concerns behind limitations periods as to all putative class members. 414 U.S. at 550-51. The primary focus of *IndyMac* is whether class action tolling extends to the statute of repose found in Section 13 of the Securities Act, which, according to the Second Circuit, defines the contours of the plaintiff’s underlying right to bring a lawsuit and the defendant’s right to be free from liability after a fixed period of time. 721 F.3d at 106-07.

The Second Circuit, in *IndyMac*, and the Tenth Circuit, in *Joseph v. Wiles*, 223 F.3d 1155 (10th Cir. 2000), agree that if *American Pipe* tolling is considered an “equitable” rule derived from fairness concerns, then the rule cannot apply to Section 13’s statute of repose in light of the Supreme Court’s decision in *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350, 363 (1991), which held that equitable tolling did not apply to certain repose periods in the federal securities laws (including the repose period in Section 13).² The Tenth Circuit held, however, that the *American Pipe* tolling rule applied to Section 13’s statute of repose because *American Pipe* tolling is a “legal” rule based on Rule 23 of the Federal Rules of Civil Procedure, governing class action lawsuits. The Second Circuit, in contrast, held that even if *American Pipe* tolling were considered to be a “legal” rule, extending it to Section 13’s statute of repose nevertheless would be impermissible as contrary to the Rules Enabling Act (which forbids interpreting any Federal Rule as abridging, enlarging, or modifying any substantive right)—an issue that the Tenth Circuit did not address.

As for Rule 23’s concerns for the efficient administration of class action lawsuits, the Tenth Circuit reasoned that “[i]f all class members were required to file claims in order to insure the limitations period would be tolled, the point of Rule 23 would be defeated.” *Joseph*, 223 F.3d at 1167-68. The court further observed that “in a sense,” application of *American Pipe* tolling to this type of situation “does not involve ‘tolling’ at all” because the plaintiff “has effectively been a party” since the class action was filed, thereby satisfying the purposes behind Section 13’s repose period. *Id.* The Second Circuit, on the other hand, determined that given “the sophisticated, well-counseled litigants involved in securities fraud class actions,” failing to apply *American Pipe* tolling to Section 13 would not necessarily “disrupt the functioning of class action litigation.” *IndyMac*, 721 F.3d at 109-10. The Second Circuit further explained that even if refusing to toll Section 13’s repose period would lead to additional lawsuits and

² Several district courts have also addressed these issues, coming to different conclusions.

motions for intervention, it is for Congress, rather than the courts, to modify the “absolute” right created by Section 13’s statute of repose. *Id.* at 110.

IndyMac Background

The particular case that the Supreme Court will consider began when investors in residential mortgage-backed securities (“RMBS”) issued by *IndyMac* filed two putative class actions alleging that the offering documents for 106 different *IndyMac* RMBS offerings contained material misstatements in violation of Sections 11, 12(a)(2), and 15 of the Securities Act. Following consolidation, the United States District Court for the Southern District of New York dismissed for lack of standing all claims based on RMBS that the named plaintiff did not itself purchase.

Following this ruling, six unnamed members of the putative class sought to intervene to assert claims with respect to RMBS that those entities had purchased, but which the named plaintiff had not. The intervenors’ claims were facially barred by Section 13’s three-year statute of repose. However, the intervenors argued their claims were timely because: (i) the *American Pipe* tolling rule suspended the running of the Securities Act’s statute of repose, and (ii) even if *American Pipe* tolling did not apply, their claims “related back” to the named plaintiffs’ surviving claims pursuant to Rule 15(c) of the Federal Rules of Civil Procedure. The district court rejected both arguments and denied the motions to intervene.

The Second Circuit’s Decision

The Second Circuit affirmed. It held, as described above, that *American Pipe* tolling applies only to statutes of limitations and not to statutes of repose. The Second Circuit reasoned that whereas statutes of limitations are procedural in nature and operate to limit a plaintiff’s remedy, statutes of repose affect a plaintiff’s underlying substantive right and are therefore “absolute,” regardless of equitable considerations related to the plaintiff’s ability to have brought its claim earlier. *IndyMac*, 721 F.3d at 106-07.

Significance of the Supreme Court’s Decision to Review *IndyMac*

The Second Circuit’s decision in *IndyMac* is significant for issuers, underwriters, officers, and directors (who are often named as defendants in Securities Act cases). The Second Circuit provided these parties with the benefit of a readily identifiable date, at least within the Second Circuit, by which Securities Act claims will be considered untimely unless asserted by an individual, named plaintiff. For claims brought under Sections 11 and 12(a)(1), this date will be three years from the offering date, and for Section 12(a)(2) claims, this date will be three years from the sale of the security.

In addition, although *IndyMac* addressed only the three-year statute of repose under the Securities Act, defendants in securities fraud cases can be expected to argue, based on the Second Circuit’s reasoning, that the *American Pipe* tolling rule does not apply to the five-year statute of repose governing claims under Section 10(b) of the Exchange Act. Further, the decision may provide support for arguments that other statutes of repose should not be subject to *American Pipe* tolling, such as those under certain state Blue Sky laws.

Other practical issues implicated by the *IndyMac* decision relate to whether absent putative class members will take individual steps to preserve their claims, and whether motions and decisions on class certification will be accelerated in order to be resolved, within the repose period. The Second Circuit was not convinced by the proposed intervenors' argument about the potential for disruption that might ensue from the refusal to extend *American Pipe* tolling to statutes of repose (and there has been little, if any, evidence validating the proposed intervenors' concerns thus far), but the parties continued to discuss this subject in their certiorari briefing.

For all these reasons, the Supreme Court's *IndyMac* decision should be closely watched.

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This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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