A Significant Victory For Securities Class Action Defendants

By **Susan Saltzstein and Robert Fumerton**

Law360, New York (June 28, 2017, 5:07 PM EDT) -- In one of the first cases argued before new Justice Neil Gorsuch, the U.S. Supreme Court in California Public Employees' Retirement System v. ANZ Securities Inc., No. 16-373, slip op. at 16-17 (June 26, 2017), decided on Monday that the filing of a putative class action does not toll Section 13's statute of repose for an individual plaintiff's Section 11 claims.

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Background

The road to CalPERS began with the Supreme Court's 1974 decision in American Pipe & Construction Co. v. Utah, which established a class action tolling rule pursuant to which certain limitations periods are tolled for unnamed members of a putative class until class certification is decided. Since that decision, the federal circuit courts have been divided on whether the American Pipe tolling rule properly can be applied to toll statutes of repose or should instead be confined to statutes of limitations. Even those courts reaching the same conclusion on the issue have employed disparate reasoning, and recent decisions have only deepened the divide.

Recognizing this circuit split, the Supreme Court first granted certiorari on the question following the Second Circuit's 2013 decision in Police & Fire Retirement System of the City of Detroit v. IndyMac MBS Inc. The writ of certiorari in that case was dismissed as improvidently granted, however, when the court learned of a pending settlement agreement before the district court. Thus, just a few years later, CalPERS provided the court with another opportunity to speak definitively on the reach of the American Pipe tolling rule.

The dispute in CalPERS dates back to the collapse of Lehman Brothers Holdings Inc. Before its bankruptcy, Lehman raised over $31 billion through debt offerings, and CalPERS allegedly bought millions of dollars of those securities between July 2007 and January 2008. In June 2008, another retirement fund that also purportedly purchased those securities filed a putative class action in the Southern District of New York. The complaint alleged that the debt offerings' underwriters were liable for false and misleading statements made in the registration statements. The parties to the putative class action agreed to a settlement that same year, however, and CalPERS opted out to pursue an individual action when the district court certified a settlement class.

CalPERS commenced its individual action in February 2011, more than three years after the debt offerings. Section 13 of the Securities Act provides that all claims under the act must be brought within one year of the "discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence." Importantly, Section 13 also imposes a three-year time bar: "In no event shall any action be brought to enforce a liability created under [Section 11] ... more than three years after the security" was offered to the public. 15 U.S.C. § 77m. Because the Lehman debt offerings were first offered to the public more than three years before CalPERS commenced its action, the district court concluded that the action was untimely under Section 13's three-year repose period.

CalPERS appealed to the Second Circuit, and, on July 8, 2016, the panel unanimously affirmed the district court's order. The Second Circuit applied its reasoning from IndyMac to conclude that the prior filing of a securities class action does not toll Section 13's three-year limitations period, which it deemed a statute of repose. In affirming the district court, the Second Circuit highlighted the circuit split concerning the reach of the American Pipe tolling rule. Specifically, the court opined that the question "may be ripe for resolution by the Supreme Court" but "unless and until the Supreme Court informs us that our decision was erroneous, IndyMac continues to be the law of the Circuit and its reasoning controls the outcome of the case." The Supreme Court, as in IndyMac, accepted the Second Circuit's invitation.

The Parties' Arguments

In its briefing and at argument, CalPERS urged the court to adopt one of several rationales to conclude that its complaint was timely filed. The first and, according to CalPERS, easiest rationale (i.e., one not dependent upon tolling) was that the class complaint "brought" all of the individual class members' claims against the respondents. CalPERS' individual action was thus timely commenced upon the filing of the putative class action complaint. According to this argument, CalPERS' opt-out complaint ought not be viewed as a new "action" but rather the assertion of control over the individual plaintiff's claim first alleged by the class representative.

The respondents chided CalPERS for asserting procedurally improper arguments given that the court expressly declined to grant certiorari on the question of whether a member of a timely filed putative class action may file an individual suit on the same causes of action before class certification is decided, even where the relevant time limitations have expired. E.g., Resp. br. at 39. Moreover, the respondents contended that CalPERS' rationale would not apply under the facts of the case because CalPERS opted out before class certification, negating its claim that the filing of the class action complaint initiated its individual "action." Id. at 45.

CalPERS then offered two alternative arguments: (1) if the court determined that tolling principles were implicated, American Pipe tolling — even if a form of equitable tolling — applied because the timely filed class action complaint initiated its action, Pet. br. at 41-42; and (2) in any event, Section 13's three-year period is a statute of limitations rather than a statute of repose. Id. at 43-45.

The respondents, in contrast, argued that (1) the American Pipe tolling rule is equitable in nature, and statutes of repose are not subject to equitable tolling, Resp. br. at 27-30, and (2) Section 13's text, structure and history show that its three-year period is a "classic statute of repose" meant to establish the outer limit of a defendant's liability under Section 13. Id. at 21. Specifically, the respondents emphasized Section 13's legislative history, use of categorical language, and "two-tiered" structure to assert that Congress intended Section 13's three-year bar to reflect a finite limit on Section 11 claims, balancing the interests of both plaintiffs and defendants. Id. at 18-26.

At oral argument in April, Justice Gorsuch was vocal in staking out a "plain language" interpretation of the statute. When CalPERS pressed its first argument — that the opt-out complaint was not a new "action" for purposes of the statute of repose — Justice Gorsuch parsed the distinction between the terms "action" and "claim." Section 13 uses "action" and accordingly, Justice Gorsuch suggested, even if CalPERS brings "the same claims ... it's a different action."

CalPERS attempted to resist Justice Gorsuch's text-driven position with policy arguments, but Justice Gorsuch reiterated his focus on the statute's text: "I mean, I don't like the policy consequences, but as a matter of plain language," he seemed unconvinced. And later, when CalPERS argued that the statute's "in no event" language contained an ambiguity, Justice Gorsuch pointedly asked: "Where is the ambiguity in 'in no event'?"

Justice Gorsuch's focus on "plain language" marks an early trend in his Supreme Court jurisprudence. Indeed, Justice Gorsuch's first question as a Supreme Court justice, which came earlier on the same day in a case captioned Perry v. Merit Systems Protection Board, asked, "Where in the statute is that provided?" And when the lawyer replied by reciting the court's precedent, Justice Gorsuch asked him to "put[ ] aside" the decision and "look[ ] at the plain language of the statute."

Meanwhile, Justice Sonia Sotomayor focused primarily on the practical ramifications of ANZ's argument. She, Justice Elena Kagan and Justice Ruth Bader Ginsburg all expressed concern about the potential for Section 13's repose period to clog the courts with duplicative litigation, unnecessary paperwork and less sophisticated plaintiffs pursuing individual actions. "This is a rule that's kind of guaranteed to create make-work for district courts," Justice Kagan said, "and for small investors to lose their claims."

The Supreme Court's Decision

In an opinion authored by Justice Anthony Kennedy, a 5-4 majority of the court concluded that Section 13's three-year time limit is a statute of repose not subject to American Pipe tolling. Justice Kennedy was joined by Justices John Roberts, Clarence Thomas, Samuel Alito and Gorsuch in affirming the Second Circuit's underlying decision. Justice Ginsburg wrote the dissenting opinion, joined by Justices Stephen Breyer, Sotomayor and Kagan. The opinion, which marks a victory for defendants by holding that the statute of repose is not subject to equitable tolling, described Section 13 as a "complete defense to any suit after a certain period." (Op. at 9.)

With respect to the petitioner's argument that tolling was not implicated because the timely filing of the class action complaint timely brought its individual "action," the court said it "defied ordinary understanding that [CalPERS'] filing — in a separate forum, on a separate date, by a separate named party — was the same action[.]" (Op. at 15.) The court instead applied a "straightforward analysis" and held that "[t]he 3-year time bar in Section 13 of the Securities Act is a statute of repose." (Op. at 16.) The majority concluded that the "statute displaces the traditional power of courts to modify statutory time limits in the name of equity." (Id.)

Writing in dissent, Justice Ginsburg expressed concern that the court's opinion "disserves the investing public that Section 11 was designed to protect." (Op. at 4) (Ginsburg, J., dissenting). "[T]he risk is high," Justice Ginsburg cautioned, "that class members failing to file a protective claim will be saddled with inadequate representation or an inadequate judgment." (Id.) Justice Ginsburg concluded her dissent with a warning: "Today's decision impels courts and class counsel to take a more active role in protecting class members' opt-out rights." (Id. at 5.)

Although he did not write an opinion in this case, Justice Gorsuch also made his presence felt. In substance, the majority opinion corresponded closely with Justice Gorsuch's

questioning at oral argument back in April: his insistence on reading the "plain language" of Section 13's "in no event" language, for example, can be seen in Justice Kennedy's statement that the statute "admits of no exception and on its face creates a fixed bar against future liability." (Op. at 5.) Justice Gorsuch's skepticism about CalPERS' "same action" argument was similarly echoed in the majority opinion.

Going Forward: More Certainty for Defendants and Potential Limitations on Class Certification

The decision represents a significant victory for securities class action defendants. Most directly, they now no longer face the threat of liability from opt-outs more than three years following an offering of securities. Once a class action has been filed, the decision effectively eliminates the ability of individual class members to opt out after the three-year cutoff unless they have first filed a protective claim on their own behalf within the three-year period. As Justice Kennedy noted, this kind of "certainty and reliability ... are a necessity in a marketplace where stability and reliance are essential components of valuation and expectation for financial actors." (Op. at 16.) Defendants will now be able to calculate their exposure to opt-out actions and other liability stemming from a securities class action with much greater confidence and precision.

This decision also has the potential to spur courts to go even further in limiting securities class actions. While on its face, the Supreme Court's holding does not prevent a class from being certified outside of the three-year repose period, there is an argument that this precedent could be applied to preclude putative class members from joining a class after that period of time. In other words, if putative class members — as opposed to the named plaintiffs themselves — are not deemed to have been part of an action until a class is certified, it is not clear why the three-year repose period would not bar claims by these individuals as well. While some may argue that this would be a harsh result, it bears emphasis that the advent of class actions and Rule 23 came well after Congress enacted the three-year repose period in the Securities Act.

Moreover, given that class members can no longer opt out of a class that is certified after the three-year cutoff — and, as the dissent here stressed, the Supreme Court in Wal-Mart held that opt-out rights are an essential element of due process in class actions — courts could refuse to certify any class after the three-year cutoff on that basis as well.

The effect of this type of ruling could potentially be even more devastating for securities plaintiffs, particularly where putative class actions are not commenced until a couple of years into the three-year repose period. In those situations, plaintiffs would have significant difficulties in getting through the pleading stage and moving for class certification before the three-year cut-off expired.

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