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U.S. SUPREME COURT HOLDS THAT SECURITIES ACT'S THREE-YEAR LIMITATION PERIOD IS NOT SUSPENDED BY A PENDING CLASS ACTION

July 2017

A June 26, 2017 decision by the U.S. Supreme Court restricting the period in which class members may pursue claims for securities violations pursuant to the Securities Act of 1933, *California Public Employees' Retirement System v. ANZ Securities, Inc.*, 582 U.S. __ (2017), has significant implications for investors considering opting out of securities class action litigation.

Section 13 of the Securities Act includes dual limitation periods for claims brought under Sections 11 and 12(a)(2). The shorter of the limitation periods requires investors to bring claims within one year of the discovery of a violation, or after such discovery should have been made using reasonable diligence. Meanwhile, the longer limitation period requires claims to be brought within three years of the subject securities offering. Under prior U.S. Supreme Court precedent, *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974), the shorter one-year limitation period is "tolled" during the pendency of class actions until such a time as the plaintiff is no longer covered by the class definition. Tolling is a legal doctrine, which allows for the pausing or delaying of the running of a limitations period. The Supreme Court referred to the type of tolling permitted by *American Pipe* as "equitable tolling." But recently, courts remained split on whether the longer three-year limitation period was subject to the same equitable tolling principles.

In a narrowly divided 5-4 opinion, the U.S. Supreme Court held on June 26, 2017, that the three-year time limit included in Section 13 of the Securities Act is properly characterized as a "statute of repose" (a legally prescribed time limit in which a suit must be filed) and therefore cannot benefit from equitable tolling under *American Pipe*. Under the majority's view, Congress made clear that Section 13 offers defendants "full and final security" from newly filed suits after three years, regardless of any equitable powers that courts ordinarily enjoy.

This decision means that relevant statutes of repose may expire during the pendency of a class case prior to class certification or settlement—the stages that impose deadlines for opting out of a class action. Investors can no longer rely on *American Pipe* tolling principles in deciding whether to opt out, and instead must carefully consider early on whether to take proactive steps to avoid the relinquishment of certain claims. Notably, while the Court's tolling analysis applied to a claim brought under Section 11 of the Securities Act, the logic is likely to be used by defendants to argue that it encompasses other claims, including claims brought under Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act").[1]

Case Background

Lehman Brothers Holdings Inc. ("Lehman Brothers"), one of the largest investment banks in the mid-2000s, raised capital through various public securities offerings issued in 2007 and 2008. Lehman Brothers subsequently filed for

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[1] *See, e.g.*, *In re Bear Stearns Companies, Inc. Securities, Derivative, & ERISA Litigation* 995 F. Supp. 2d 291, 300 (S.D.N.Y. 2014) (applying similar logic to Exchange Act claims).

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bankruptcy during the financial crisis in September 2008. A class action was filed shortly thereafter in the U.S. District Court for the Southern District of New York against the underwriters and various other defendants, alleging that documents filed in connection with the offerings contained material misstatements or omissions giving rise to Section 11 liability under the Securities Act. While California Public Employees' Retirement System ("CalPERS") was not one of the named plaintiffs in the class action, it was a passive member of the proposed class by virtue of its purchase of the relevant securities.

While the class action was still pending, in February 2011—more than three years after the securities transactions at issue—CalPERS filed its own separate complaint alleging violations of Section 11 against the same defendants. The class action soon reached a proposed settlement, but CalPERS opted out of the class in an effort to pursue its own recovery. The defendants moved to dismiss the individual suit on the basis that the Section 11 claim was time-barred by the three-year time period set forth in Section 13. CalPERS argued in opposition that the time period was tolled under *American Pipe*. The district court granted defendants' motion, and the Second Circuit affirmed.[2] CalPERS petitioned the U.S. Supreme Court for review, which the Court granted on the question of whether the *American Pipe* doctrine tolls the Securities Act's three-year limitations period.

The U.S. Supreme Court's June 26, 2017 Decision

The Majority Opinion

On June 26th, the Court issued its decision in the matter of *CalPERS v. ANZ Securities, Inc*. In it, the Court made clear that the three-year time period in Section 13 is a statute of repose. The Court explained that statutes of repose "are enacted to give more explicit and certain protection to defendants," and given the language of Section 13,[3] Congress clearly intended to insulate defendants from ongoing liability.

The Court went on to explain that "[i]n light of the purpose of a statute of repose, the provision is in general not subject to tolling." Indeed, the only exception to this rule is when a statute of repose provides a "particular indication" that the legislature anticipated the extension of the statutory period under certain circumstances. "The purpose and effect of a statute of repose . . . is to override customary tolling rules arising from the equitable powers of courts."

In holding that the statute of repose in the Securities Act is not subject to equitable tolling, the Court rejected the application of *American Pipe*. In *American Pipe*, the Court had concluded that a statute of limitations was tolled as to all members of the putative class as soon as the class action had been commenced. But the Court clarified that *American Pipe* was rooted in "the judicial power to promote equity, rather than to interpret and enforce statutory provisions." And, because a statute of repose is designed to "grant complete peace to defendants," the time period "supersedes the

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2 *In re Lehman Brothers Securities and ERISA Litigation*, 655 Fed. Appx. 13, 15 (2d Cir. 2016).

3 "In no event shall any such action be brought . . . more than three years after the security was bona fide offered to the public."

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application of a tolling rule based in equity." In short, the Court concluded that the Securities Act's three-year statute of repose is not subject to principles of equitable tolling and affirmed the Second Circuit's dismissal of CalPERS' opt-out action as untimely, leaving CalPERS with no ability to recover from the opt-out or class action suits.

Justice Ginsburg's Dissent

In a dissenting opinion, Justice Ginsberg warned that the "harshest consequences [from this decision] will fall on those class members . . . who fail to file a protective claim within the repose period." She explained that "those members stand to forfeit their constitutionally shielded right to opt out of the class and thereby control the prosecution of their own claims for damages." Justice Ginsberg also emphasized that because class certification is typically decided several years after a class action is filed, there is a substantial risk that many class members "will be saddled with inadequate representation or an inadequate judgment" should they wait too long to opt out and file their own individual actions.

The dissent's warnings serve as an important reminder to investors that recovery strategies should be formulated at an early stage of the proceedings.

Discussion and Recommendations

While the *ANZ Securities* decision brings clarity to lower courts split on the tolling issue, it also has important implications for investors, as Justice Ginsburg details in her dissent. Initially, investors considering an opt-out strategy can no longer employ a wait-and-see approach as the class action is litigated before deciding whether to opt out and pursue individual claims. As such, we expect that more investors will consider their recovery options at an earlier stage of class action proceedings so as to avoid the risk of untimely opt-out claims. Also, while the Court's discussion centered on the Securities Act's three-year statute of repose, we anticipate that defendants will argue that the logic is broad enough to encompass other claims, including claims brought under Section 10(b) of the Exchange Act.

Given these consequences, we recommend that investors monitor class actions carefully and discuss their potential recovery opportunities early on with counsel to minimize any risk of the statute of repose foreclosing their ability to opt out of the class action should they seek to do so. Additionally, investors should consider the benefits of negotiating tolling agreements with defendants at an early stage of the litigation so as to adequately protect against expiring limitation periods.

Labaton Sucharow attorneys are available to address any questions you may have regarding these developments and any specific securities actions. We welcome you to contact our team.

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