



SOUTHERN DISTRICT CIVIL PRACTICE ROUNDUP

Expert Analysis

Clock Ticks On: No 'American Pipe' Tolling of Statutes of Repose

Two recent decisions by judges from the U.S. District Court for the Southern District of New York have put the federal securities laws on a collision course with the basic principles of economy and efficiency animating Federal Rule of Civil Procedure 23 governing class actions. In *Footbridge Ltd. Trust v. Countrywide Fin. Corp.*,¹ and *In re Lehman Bros. Sec. and ERISA Litig.*,² Southern District Judges P. Kevin Castel and Lewis A. Kaplan respectively, each dismissed as untimely efforts to cure defective class action claims after the outer statutory time limits for asserting such claims had run.

Both cases concluded that the tolling principle embodied in *American Pipe and Constr. Co. v. Utah*³—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”—could not be used to extend the applicable “statute of repose” which provides that “[i]n no event shall any...action be brought...more than three years after” the offering or sale of the security in question.⁴ These decisions, discussed in detail below, are likely to shake up the plaintiffs’ securities bar, and may well result in a greater number of plaintiffs demanding a seat at the table if they lose confidence that the time clock will be suspended during a class action that purports to cover their claims.

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Dual Time Limits

Both the Securities Act of 1933 (hereinafter the Securities Act or the '33 Act) and the Securities Exchange Act of 1934 (hereinafter the Exchange Act or the '34 Act) contain dual time limits consisting of a statute of limitations, setting forth how long after discovery of the violation a suit may be brought, and a statute of repose, pegged

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to the time of the alleged violation, that defines the outer limit after which an action may not be brought under any circumstances. For example, the statute of limitations for civil actions brought under the '33 Act for false representations in a registration statement or prospectus is one year after the discovery of the violation (or after discovery should have been made by the exercise of reasonable diligence), and the accompanying statute of repose is three years after the offering or sale of the security.⁵ Similarly, under the '34 Act, a fraud claim under Section 10(b) and Rule 10b-5 must be commenced within two years of

discovery of the facts constituting the violation, or five years of such violation.⁶

Although they both serve to limit the time in which an action may be commenced, statutes of limitation and repose are “fundamentally different” from one another. Statutes of limitation “bear on the availability of remedies,” whereas statutes of repose address the “availability of the underlying right: That right is no longer available on the expiration of the specified period of time.”⁷ “A statute of repose extinguishes the claim after a fixed period” and is absolute (subject only to legislatively created exceptions).⁸ One distinction that becomes central to the decisions in *Footbridge* and *Lehman Bros.* is that statutes of limitation are subject to equitable tolling, whereas statutes of repose are not.⁹

Seeking to Cure Defects

In both *Footbridge* and *Lehman Bros.*, plaintiffs sought to cure defects in earlier actions or pleadings asserting claims brought under the '33 Act after the statute of repose had expired. Both cases involved claims by purchasers of mortgage-backed securities challenging the accuracy of statements made in offering documents and prospectuses for those securities.

In *Footbridge*, plaintiffs alleged that defendants included untrue statements and omissions of material fact in registration statements and prospectus supplements for mortgage-backed securities purchased by plaintiffs between June and October 2006. The offerings at issue had been the subject of a timely filed consolidated class action in California state court, which was dismissed in January 2010 after the state court concluded that it lacked subject matter jurisdiction under the Securities Litigation Uniform Standards Act of 1998.

Less than two weeks after the state court dismissal, the *Footbridge* plaintiffs filed their

federal complaint in the Southern District of New York, alleging violations of Sections 11, 12(a)(2), and 15 of the '33 Act related to statements made in the 2006 offering documents. The defendants sought summary judgment on the basis that the federal action was untimely because it was commenced after the expiration of the three-year statute of repose.

Judge Kaplan's decision *In re Lehman Bros.* concerned the efforts of two parties to intervene in order to cure a standing defect in that class action, also involving mortgage-backed securities. Specifically, although the complaint asserted claims in connection with 94 offerings, Judge Kaplan had earlier dismissed most of those claims for lack of standing, finding that the named plaintiffs had purchased in only nine of the 94 offerings at issue. Two institutional plaintiffs sought to intervene to cure the standing defect as to eight offerings in which they had participated. Because the latest of those offerings occurred more than three years before the new putative plaintiffs sought to intervene, defendants opposed the motions arguing that the statutes of limitation and repose had both expired as to the intervenors.

On their face, then, absent tolling, the new action in *Footbridge* and the motions to intervene in *Lehman Bros.* were barred by the '33 Act's three-year statute of repose. Plaintiffs in both cases argued that the statutes of repose had been tolled during the pendency of the earlier litigation under the *American Pipe* doctrine—a position consistent with the weight of authority in this and other jurisdictions up to that point.

'American Pipe' Tolling

In *American Pipe*, the Supreme Court articulated the general principle 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."¹⁰ The Court noted that a contrary holding would "induce[]" potential class members to file repetitious motion papers to protect their interests, thereby thwarting Rule 23's purpose of reducing multiplicity of activity in such cases.

Further, the Court concluded that the tolling rule was not inconsistent with the purpose of a statute of limitation because defendants would be on notice of the underlying claims within the limitations period, satisfying the "policies of ensuring essential fairness to defendants and of barring a plaintiff who 'has slept on his rights.'"¹¹

Statutes of Repose

Judge Castel in *Footbridge* and Judge Kaplan in *Lehman Bros.* rejected the argument advanced by the plaintiffs in both cases that the three-year statute of repose which would otherwise bar their claims should be tolled pursuant to *American Pipe*.

Judge Castel, who filed his decision a month before Judge Kaplan's decision in *Lehman Bros.*, found that the unambiguous language in Section 13 of the '33 Act providing that "in no event" shall an action be brought more than three years after the offering or sale of the security at issue, precluded the application of *American Pipe*. He found support for this conclusion in another Supreme Court case, *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*,¹² which held, in the context of non-class claims for securities fraud asserted under the '34 Act, that the statute of repose is not subject to equitable tolling.

Both judges noted that the '33 Act does not itself provide for tolling, and they rejected the notion that in the class action context, Rule 23 should somehow be read to supply a statutory rather than an equitable basis for 'American Pipe's' tolling doctrine.

Judge Castel also relied on the U.S. Court of Appeals for the Tenth Circuit decision in *Anixter v. Home-Stake Prod. Co.*, which concluded, after a lengthy review of the legislative history of Section 13's statute of repose, that "Congress included statutes of repose because of fear that lingering liabilities would disrupt normal business and facilitate false claims. It was understood that the three-year rule was to be absolute."¹³ Judge Castel adopted the Tenth Circuit's finding that the application of equitable tolling principles to extend the three-year period of repose would contravene congressional intent.¹⁴

Based on these considerations, the critical question becomes, as Judge Kaplan observed in *Lehman Bros.*, "whether tolling under *American Pipe* reflects a judicially created amelioration of a statute of limitations or a legislatively sanctioned means of extending a statute of repose."¹⁵ If the former, *American Pipe* would be a form of equitable tolling and could not, consistent with *Lampf*, be used to toll the statute of repose, whereas if

the latter, *American Pipe* would fall outside of *Lampf's* prohibition and could provide a basis for permitting assertion of claims beyond the three-year cut-off imposed by the statute of repose. Both Judge Castel and Judge Kaplan found that *American Pipe* constituted equitable tolling and thus could not extend the statute of repose.

Judges Castel and Kaplan each acknowledged that their conclusion ran counter to decisions from other circuits as well as from the Southern District of New York, which had applied *American Pipe* to toll statutes of repose.¹⁶ For example, in *In re Flag Telecom Holdings, Ltd. Secs. Litig.*, the late Southern District Judge William C. Conner specifically applied *American Pipe* to the statute of repose set forth in Section 13 of the '33 Act, finding that a plaintiff not named until the third consolidated amended complaint, filed more than a year after the expiration of the statute of repose, "should not be punished simply because he failed to anticipate that...[the Securities Act] claims would be dismissed because none of the named plaintiffs in the action had standing to sue on those claims."¹⁷

In applying the *American Pipe* rule, Judge Conner relied on *Official Comm. of Asbestos Claimants of G-I Holding Inc. v. Heyman*, which held that *American Pipe* tolling is "legal rather than equitable in nature," and that accordingly, neither *Lampf* nor *Anixter* bar its application to a statute of repose.¹⁸ Judge Conner reasoned that the failure to apply *American Pipe* would undermine the policies of Rule 23 and class action litigation, as well as those set forth in the Private Securities Litigation Reform Act, which encourage investors to refrain from filing separate complaints or intervening in actions where "their interests are adequately protected in a proposed class action that has already been filed."¹⁹

Rejecting this approach, Judge Castel in *Footbridge* held that *American Pipe* is equitable, rather than statutory, inasmuch as it is a "judicially-created rule premised on 'traditional equitable considerations' of fairness, judicial economy and needless multiplicity of lawsuits." He contrasted this tolling doctrine with those instances where the governing statute specifically contemplates a tolling of the limitations period.²⁰ Reaching the same conclusion, Judge Kaplan stressed that *American Pipe* was a case about a statute of limitation (not a statute of repose) and noted that both the Supreme Court and the U.S. Court of Appeals for the Second Circuit have referred to *American Pipe* as an example of equitable tolling.²¹

Both judges noted that the '33 Act does not itself provide for tolling, and they rejected the notion that in the class action context, Rule 23 should somehow be read to supply a statutory rather than an equitable basis for *American Pipe*'s tolling doctrine. Acknowledging that the Supreme Court had Rule 23's goals in mind when deciding *American Pipe*, Judge Kaplan nevertheless found that the rule itself "makes no mention whatsoever of the tolling principle" and that even if it did imply such a rule, "the Federal Rules of Civil Procedure may 'not abridge, enlarge or modify any substantive right,'" such as that right granted securities defendants under section 13 of the Securities Act.²²

Judge Castel in *Footbridge* and Judge Kaplan in *Lehman Bros.* both expressly conceded that their decisions are in conflict with the underlying purpose of Rule 23, but concluded that it is for Congress, rather than the judiciary to resolve this tension. Judge Castel observed: "[t]rue, many of the policy considerations present in *American Pipe* would support tolling of a statute of repose. But the issue presented is not one of policy but of enforcement of the statute as written. Lawmakers are free to adjust the repose period as they have in the past."²³ Judge Kaplan similarly commented that: "[w]hen it comes to statutes of repose, however, the relevant policies are those of Congress rather than any that courts might think preferable."²⁴

Conclusion

The decisions in both cases have been appealed to the Second Circuit.²⁵ Given the degree of conflicting authority interpreting important Supreme Court precedent, the high stakes in the resolution of this question, and the important statutory and equitable considerations in play, it seems likely that this question may make its way to the Supreme Court. In the meantime, at least in the Southern District of New York, cautious plaintiffs' counsel are likely to file placeholder lawsuits or motions to intervene in order to preserve their positions where class claims may not survive beyond the expiration of the statute of repose.

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1. __F.Supp.2d__, 2011 WL 907121 (SDNY March 16, 2011).

2. 2011 WL 1453790 (SDNY April 13, 2011).

3. 414 U.S. 538 (1974), reh'g denied, 94 S. Ct. 1477 (1974).

4. 15 U.S.C. §77m.

5. Id.

6. 28 U.S.C. §1658(b). Because the implied private right of action in the '34 Act for fraud or deception in connection with the purchase or sale of a security, 15 U.S.C. §78j(b), 17 C.F.R. §240.10b-5, was judicially created, it had no statute of limitation.

Historically, most courts borrowed the statute of limitations from the closest analogous state law cause of action. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 210 n.29 (1976). In *Lampf, Pleva, Lipkind, Prupis & Pettigrow v. Gilbertson*, the Supreme Court imposed a uniform one-year statute of limitation and three-year statute of repose drawn from other provisions of the '34 Act. 501 U.S. 350, 361-362 (1991). In the Sarbanes-Oxley Act of 2002, Congress codified and extended those limits to a two-year statute of limitation and five-year statute of repose. 28 U.S.C. §1658(b). The statutes were extended out of concern that the one-and-three year structure "unfairly limit[ed] recovery for defrauded investors in some cases." S. Rep. No. 107-146, at 8 (2002).

7. 2011 WL 1453790, at *3 (quoting *P. Stolz Family P'ship L.P. v. Daum*, 355 F.3d 92, 102 (2d Cir. 2004) (internal citation omitted)).

8. 2011 WL 907121, at *3 (citing Calvin W. Corman, Limitation of Actions, §1.1, at 4-5 (1991)).

9. *Lampf*, 501 U.S. at 363.

10. 414 U.S. at 554. *American Pipe* found that the statute was tolled as to intervenors. Its tolling principle was later expanded to apply to putative class members in *Crown, Cork & Seal Co. v. Parker*, 462 U.S. 345, 350 (1983).

11. Id. at 554-55 (quoting *Burnett v. New York Cent. R.R. Co.*, 380 U.S. 424, 428 (1965)).

12. 501 U.S. 350.

13. 939 F.2d 1420, 1435 (10th Cir. 1991), vacated on other grounds sub nom. *Dennler v. Trippet*, 503 U.S. 978 (1992) (quoting *Norris v. Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), cert. denied, 484 U.S. 943 (1987)).

14. 2011 WL 907121, at *5 n.2.

15. 2011 WL 1453790, at *3.

16. See, e.g., *Joseph v. Wiles*, 223 F.3d 1155 (10th Cir. 2000); *Maine State Ret. Sys. v. Countrywide Fin. Corp.*, 722 F.Supp.2d 1157 (C.D. Cal. 2010); *Arivella v. Lucent Technologies Inc.*, 623 F. Supp. 2d 164 (D. Mass. 2009); *In re Flag Telecom Holdings, Ltd. Sec. Litig.*, 352 F.Supp.2d 429 (SDNY 2005); *Official Comm. of Asbestos Claimants of GI Holding Inc. v. Heyman*, 277 B.R. 20 (SDNY 2002).

17. 352 F.Supp.2d at 456.

18. 277 B.R. at 31-32. Although not discussed by either court in *Footbridge* or *In re Lehman*, several courts have questioned whether *American Pipe* tolling applies if the action is dismissed prior to resolution of the class certification question. See *New Jersey Carpenters Health Fund v. Residential Capital, LLC*, 2010 WL 5222127, at *5 (SDNY Dec. 22, 2010) (noting that some district courts within the Second Circuit support the proposition that a limitations period is not tolled where the original plaintiff lacked standing); *Maine State Ret. Sys. v. Countrywide Fin. Corp.*, 722 F.Supp.2d 1157, 1167 (C.D. Cal. 2010) ("This Court shares the concern of other district courts that extending *American Pipe* tolling to class action claims the original named plaintiffs had no standing to bring will encourage filings made merely to extend the period in which to find a class representative."). But see *In re Wachovia Equity Sec. Litig.*, 753 F.Supp.2d 326, 372 (SDNY 2011) (applying *American Pipe* to class action claims dismissed for

lack of standing, stating that "additional Plaintiffs should not be punished for their failure to anticipate or timely remedy the standing deficiencies of the original...Complaint").

19. 352 F.Supp.2d at 456.

20. 2011 WL 907121, at *6 (internal citation omitted) (providing as an example the statutory provision governing post-conviction review, set forth in 28 U.S.C. §2244(d)(2), which specifically states that the time for post-conviction or other collateral review "shall not be counted toward any period of limitation").

21. 2011 WL 1453790, at *3 (citing *Young v. United States*, 535 U.S. 43, 49 (2002); *Veltri v. Building Service 32B-J Pension Fund*, 393 F.3d 318, 322-23 (2d Cir. 2004)).

22. Id. (citing 28 U.S.C. §2072(b)).

23. 2011 WL 907121, at *7. See id. at *7, n.3 (referring to instances in which Congress has shortened or lengthened the statutes of repose set forth in the securities laws).

24. 2011 WL 1453790, at *3.

25. The opening brief in *Footbridge* is scheduled to be filed on June 29, 2011. *Footbridge Ltd. Trust v. Countrywide Fin. Corp.*, No. 11-1158, Order (April 6, 2011). No briefing schedule has been set in *In re Lehman Bros. In re Lehman Bros. Mortgage-Backed Sec. Litig.*, No. 11-1982.