ALERT MEMORANDUM

Sixth Circuit Follows Second Circuit in Holding That Statutes of Repose Are Not Subject to Class Action Tolling

May 20, 2016

The Supreme Court acknowledged the significant differences between statutes of limitations and statutes of repose in *CTS Corporation v. Waldburger*, 134 S. Ct. 2175 (2014). The Sixth Circuit's opinion in *Stein v. Regions Morgan Keegan Select High Income Fund, Inc.*, Case Nos. 15-5903, 15-5905 (6th Cir. May 19, 2016), is the first by a circuit court to apply *CTS* to the statutory time limits applicable to private civil actions under the federal securities laws. *Stein* held that class action tolling does not toll the statutes of repose applicable to claims under Sections 11 and 12(a)(2) of the Securities Act of 1933 and Section 10(b) of the Securities Exchange Act of 1934. In so ruling, *Stein* embraced the Second Circuit's conclusion in 2013 that repose periods are not subject to class action tolling, and rejected the opposite view reached in 2000, before *CTS*, by the Tenth Circuit. Whether statutes of repose can be tolled is a recurring issue with material consequences. Cases pending before two other circuits may result in a deeper split making Supreme Court review more likely, or a growing consensus reducing the likelihood of such review.

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Background

Andrew M. Stein, Stein Holdings Inc., Stein Investments, LLC, Warren Canale, and Canale Funeral Directors, Inc. (together, "Plaintiffs") invested in five investments funds, which suffered losses in 2007 and 2008 allegedly because they were overvalued and heavily concentrated in certain risky securities.[1]

[1] *See* Slip op. at 2.

Plaintiffs filed the lawsuits subject to the appeal more than five years later, on October 25, 2013, alleging that the defendants violated Sections 11, 12(a)(2), and 15 of the Securities Act, Sections 10(b) and 20(a) of the Exchange Act, and Rule 10b-5, in addition to common law vicarious liability, by concealing the funds' risks, overvaluation, and lack of diversification.[2] (Notably, Plaintiffs had filed several arbitrations and state court actions during 2008 and 2009 raising similar claims, which demonstrated that Plaintiffs were aware of their claims more than two years before they filed suit in federal court.[3])

Two related class actions were also filed in December 2007 against certain of the defendants named in Plaintiffs' lawsuits. In one of those class actions, a class certification motion was granted prior to the date Plaintiffs' lawsuits were filed; in the other class action, the class certification motion remained pending on that date.[4]

In September 2014, the district court presiding over Plaintiffs' actions granted in part and denied in part the defendants' motions to dismiss. With respect to timeliness issues, the District Court initially ruled that the limitations periods applicable to Plaintiffs' claims were tolled by the related class actions, after concluding that a prior Sixth Circuit decision, which held that class action tolling did not apply to absent class members who filed separate lawsuits prior to a decision on class certification, was no longer binding precedent.[5] The District Court, however, subsequently reconsidered that decision and dismissed Plaintiffs' claims in full on the grounds that class action tolling was not applicable in that situation.[6]

On appeal, the defendants once again argued that Plaintiffs' claims were untimely under both the applicable statutes of limitations and statutes of repose.[7]

The Sixth Circuit's Opinion

In its opinion, the Sixth Circuit first found that the District Court correctly ruled on reconsideration that its precedent "declin[ing] to extend *American Pipe* tolling to plaintiffs who file individual actions *before* the district court rules on class certification" remained controlling law.[8] The Sixth Circuit, however, concluded that ruling did not render all of Plaintiffs' claims untimely under the applicable one- and two-year statutes of limitations because some of those claims were at issue in the class action that was certified prior to Plaintiffs' lawsuit.[9] The Court therefore went on to consider the additional issue of whether the three- and five-year statutes of repose applicable to Plaintiffs' federal securities law claims were subject to class action tolling.

In addressing that issue, the Court recognized that its "fellow Circuits are split" on whether "to extend *American Pipe* tolling to statutes of repose."[10] In particular, the Sixth Circuit recognized that "[t]he Tenth Circuit held that *American Pipe* tolled statutes of repose pending class certification in *Joseph v. Wiles*, 223 F.3d 115 (10th Cir. 2000), while the Second Circuit came to the opposite conclusion in *Police & Fire Ret. Sys. of City of Detroit v. IndyMac MBS, Inc.*, 721 F.3d

[2] *Id.* at 3, 5.

[3] *Id.* at 3-5.

[4] *Id.* at 5.

[5] *Id.* at 5-6, 10-11 (citing *Wyser-Pratte Mgmt. Co. v. Texlon Corp.*, 413 F.3d 553 (6th Cir. 2005)).

[6] *Id.* at 5-6.

[7] *Id.* at 7.

[8] *Id.* at 11.

[9] *Id.* at 14.

[10] *Id.* at 16.

94 (2d Cir. 2013)."[11] After surveying the reasoning of both decisions—including the Tenth Circuit's conclusion that statutes of repose are subject to class action tolling because an absent class member is effectively a party to the class action,[12] and the Second Circuit's contrary holding that class action tolling could not apply to statutes of repose because such statutes are not subject to equitable tolling and applying Rule 23 to extend a statute of repose would violate the Rules Enabling Act's prohibition on abridging, enlarging or modifying substantive rights—the Sixth Circuit stated, "[o]f these two cases, *IndyMac* has the more cogent and persuasive rule."[13]

In deciding to adopt the Second Circuit's *IndyMac* holding, the Sixth Circuit further observed that *IndyMac* was "also more consistent with the Supreme Court's subsequent decision in *CTS*," which "discussed at length the incompatibility of equitable tolling and statutes of repose."[14] The Sixth Circuit likewise concluded that "[t]he Supreme Court's discussion of the purposes of statutes of repose in *CTS* . . . is no less pertinent even assuming *American Pipe* tolling is a form of class-action tolling deriving its authority from Rule 23" because the conclusion that "statutes of repose vest a substantive right in defendants to be free of liability is underscored by the Supreme Court's analogies in *CTS* between statutes of repose and the ability to discharge debts in bankruptcy or to be free of double jeopardy in criminal proceedings."[15] Based on this observation, the Sixth Circuit concluded that, "[b]ecause statutes of repose give priority to defendants' rights to be free of liability after a certain absolute period of time (rather than plaintiffs' ability to bring claims), we cannot endorse the Tenth Circuit's view—expressed prior to *CTS*—that 'defendants' potential liability should not be extinguished simply because the district court left the class certification issue unresolved.'"[16] The Sixth Circuit therefore "join[ed] the Second Circuit in holding that, regardless of whether *American Pipe* tolling is derived from courts' equity powers or from Rule 23, it does not apply to statutes of repose," and affirmed the District Court's dismissal of Plaintiffs' claims in full on the ground that they were barred by the applicable statutes of repose.[17]

Significance of *Stein*

After the Sixth Circuit's decision, the majority of circuit courts to consider the issue have now held that class action tolling does not apply to statutes of repose. The Sixth Circuit's ruling is also significant in that it recognizes the Tenth Circuit's contrary holding is irreconcilable with the Supreme Court's recent decision in *CTS*, which reflected a now widely-held recognition of the significant differences between statutes of limitations and statutes of repose that was less well-articulated at the time of the Tenth Circuit's prior ruling. The Sixth Circuit's decision therefore provides a compelling basis for the Third and Ninth Circuits, where appeals raising the same issue remain pending, to likewise hold that statutes of repose are not subject to class

[11] *Id.*

[12] While not mentioned by the Sixth Circuit in *Stein*, in *Smith v. Bayer Corporation*, 131 S. Ct. 2368, 2379 (2011), the Supreme Court effectively rejected *Wiles*'underpinning, by referring to the "argument that a nonnamed class member is a party to the class-action litigation *before the class is certified*" as "novel and surely erroneous."

[13] *Id.* at 16-17.

[14] *Id.* at 17.

[15] *Id.* at 17-18 (citing *CTS*, 134 S. Ct. at 2183).

[16] *Id.* at 18 (quoting *Joseph*, 223 F.3d at 1168).

[17] *Id.* at 17-19.

action tolling, and thereby further diminish the prior circuit split that led the Supreme Court to agree to consider the issue in *IndyMac*, before dismissing the writ of certiorari as improvidently granted.[18]

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[18] *See Pub. Emps.' Ret. Sys. of Miss. v. IndyMac MBS, Inc.*, 135 S. Ct. 42 (2014).