

## 3rd Circ. Eases Limitations Test For Securities Claims

*Law360, New York (October 25, 2013, 11:33 AM ET)* -- In *Pension Trust Fund for Operating Engineers v. Mortgage Asset Securitization Transactions Inc.*, No. 12-3454, (3d Cir. Sept. 17, 2013), the U.S. Court of Appeals for the Third Circuit joined the Seventh, Ninth and Eleventh Circuits, holding that Section 13 of the Securities Act of 1933 ("1933 Act"), 15 U.S.C. § 77m, does not require plaintiffs asserting a claim under the 1933 Act to plead with particularity compliance with the statute of limitations.

In doing so, the Third Circuit split from the First, Eighth and Tenth Circuits, potentially triggering review by the U.S. Supreme Court.

Plaintiffs, purchasers of mortgage-backed securities, sued UBS AG and several of its subsidiaries (collectively, "UBS") for alleged misrepresentations in the securities' offering documents and registration statements. As of Sept. 18, 2007, when plaintiffs purchased the securities, both Moody's Investors Service Inc. and Standard & Poor's had rated the securities AAA.

However, being comprised entirely of loans originated by Countrywide Home Loans Inc. and Indymac Bank FSB, the securities rapidly lost value, and were subsequently downgraded — to B2 by Moody's on Feb. 20, 2009, and to B by S&P on Aug. 13, 2009. Between late 2007 through 2009, as the financial crisis began to unfold, many news articles also highlighted the alarming default rate for Countrywide and Indymac loans.

Plaintiffs filed their original complaint on Feb. 22, 2010, asserting claims under Sections 11, 12(a)(2) and 15 of the 1933 Act, 15 U.S.C. §§ 77k, 77l(a)(2) and 77o. Plaintiffs subsequently filed an amended complaint, which the U.S. District Court for the District of New Jersey dismissed without prejudice, ordering plaintiffs to plead with particularity in a further amended complaint that their claims were timely under the applicable statute of limitations set out in Section 13 of the 1933 Act.

Defendants moved to dismiss the second amended complaint on the basis that the 1933 Act claims were untimely. The district court agreed, applying an inquiry notice standard to determine that the plaintiffs' claims were untimely, and dismissed the SAC with prejudice. Plaintiffs appealed.

The Third Circuit first took issue with the district court's ruling that plaintiffs must plead compliance with Section 13. Section 13 requires 1933 Act claims to be brought "within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence." 15 U.S.C. § 77m.

The Third Circuit rejected the reasoning adopted by the First, Eighth and Tenth Circuits that plaintiffs asserting 1933 Act claims must affirmatively plead in the complaint compliance with Section 13 because “when the very statute which creates the cause of action also contains a limitation period, the statute of limitations not only bars the remedy but also destroys the liability.” *Cook v. Avien Inc.*, 573 F.2d 685 (1st Cir. 1978).

Instead, the Third Circuit joined with the Seventh, Ninth and Eleventh Circuits, holding that “requiring a plaintiff to plead compliance with a statute of limitations would effectively ensure that a timeliness issue would always appear on the face of a complaint, thereby shifting the burden to the plaintiff to negate the applicability of the affirmative defense.”

The Third Circuit next considered the district court’s application of the inquiry notice standard to determine when the plaintiffs’ limitations period began to accrue. Under the inquiry notice standard, statutes of limitations start to run when a plaintiff “would have discovered general facts about the fraudulent scheme by the defendant rather than specific facts about the fraud perpetrated on her.”

The court held that the district court failed to apply the discovery standard announced by the U.S. Supreme Court in *Merck & Co. v. Reynolds*, 130 S. Ct. 1784 (2010). In *Merck*, the Supreme Court held that a claim under Section 10(b) of the Securities Exchange Act of 1934 (“1934 Act”), 15 U.S.C. § 78j(b), accrued “(1) when the plaintiff did in fact discover, or (2) when a reasonably diligent plaintiff would have discovered, ‘the facts constituting the violation’ — whichever comes first.” *Id.* at 1789-90, 1793.

The Third Circuit held that *Merck*, though it dealt with claims under the 1934 Act, was still applicable to the instant 1933 Act claims, because “both statutes incorporate the word ‘discovery,’ which the *Merck* court identified as a term of art representing the discovery rule.”

The Third Circuit went on to adopt the Second Circuit’s reasoning in *City of Pontiac General Employees’ Retirement System v. MBIA Inc.*, 637 F.3d 169, 174-75 (2d Cir. 2011) (blog article [here](#)), holding that “a fact is not deemed ‘discovered’ until a reasonably diligent plaintiff would have sufficient information about that fact to adequately plead it in a complaint ... with sufficient detail and particularity to survive a 12(b)(6) motion to dismiss.” *Id.*

Despite holding for plaintiffs on both the pleading requirements and applicable standard for measuring timeliness, the Third Circuit ultimately upheld the district court’s dismissal of the SAC. Plaintiffs argued that a reasonably diligent plaintiff would not have discovered the misrepresentations regarding the securities until the rating downgrade by Moody’s on Feb. 20, 2009.

The court disagreed, noting that on Sept. 9, 2008, a class of plaintiffs that included the lead plaintiffs in the instant action had “filed an amended class action complaint in the California Superior Court against both Countrywide and UBS Securities, asserting claims under Sections 11, 12(a)(2), and 15 of the [1933] Act that were substantially similar to those in this case.”

Given that plaintiffs had been aware of serious issues involving mortgage-backed securities sold by UBS and comprised of loans originated by Countrywide and Indymac in September 2008, and that a subsequent investigation that would lead to the discovery that plaintiffs may have viable claims would take no more than two months, plaintiffs were precluded from bringing the instant action any later than November 2009.

Pension Trust has not only placed the burden of testing whether 1933 Act claims are time-barred squarely on defendants, but also has eased the standard for measuring the limitations period in plaintiffs’ favor. Furthermore, there is a clear spilt among the circuits regarding the issue of pleading timeliness of 1933 Act claims, potentially triggering review by the Supreme Court in the future.

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