Second Circuit Elucidates Statute of Repose for Section 14(a) Claims

On March 17, 2016, the United States Court of Appeals for the Second Circuit held that claims pursuant to Section 14(a) of the Securities Exchange Act of 1934[1] for false representations and material omissions in a proxy statement are subject to a three-year statute of repose, unaffected by enactment of the Sarbanes-Oxley Act of 2002 ("SOX"), which extended the statute of repose to five-years for certain private rights of actions involving claims of fraud, deceit, manipulation and contrivance, such as those brought under Sections 9(f) and 18(a) of the Exchange Act.[2] The Court also clarified that operation of Section 14(a)'s statute of repose begins to run on the date of the defendant's last culpable act or omission and reiterated the established legal edict that statutes of repose are unamenable to equitable tolling principles.[3]

I. Factual Background and Procedural Posture[4]

The DeKalb County Pension Fund ("DeKalb") litigation arose from a proxy statement distributed by Transocean Inc. ("Transocean") to shareholders of GlobalSantaFe ("GSF") in October 2007 regarding a proposed merger between GSF and Transocean. In September 2010 – less than three years later – a union fund plaintiff filed a putative class action against Transocean alleging that its proxy statement contained false representations and material omissions concerning Transocean's compliance with environmental laws, which plaintiff claimed came to light after a Transocean drilling rig exploded in April 2010. The claim was asserted under Section 14(a).

DeKalb made its first appearance in the class action in December 2010 – more than three-years after issuance of the proxy statement – when it sought appointment as lead plaintiff along with the union fund, which the District Court granted. However, in April 2012 DeKalb filed an amended class action complaint when the union fund was dismissed from the case for lack of standing, leaving it as the only remaining named plaintiff.

Defendant Transocean then moved to dismiss DeKalb's suit as time-barred by Section 14(a)'s statute of repose. In granting the motion, the District Court (Schofield, J.) relied on binding Second Circuit precedent from 1990 and concluded that the statute of repose for Section 14(a) claims was three years – the same statute of repose that had applied to Sections 9(f) and 18(a) prior to the enactment of SOX– and that a Section 14(a) claim did not qualify for SOX's enlarged five-year statute of repose. The District Court further noted that the requisite statute of repose began to run from the date of the alleged violation, the October 2007 dissemination of the proxy statement, and was not subject to equitable tolling principles. Accordingly, plaintiff's late entry into the litigation resulted in its claims being time-barred.

II. The Circuit Court Decision

On March 17, 2016, the Second Circuit affirmed the District Court decision. In so doing, the Court of Appeals reconciled its pre-SOX holding in *Ceres Partners v. GEL Associates*[5] with the post-SOX landscape.

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[1] *See* 15 U.S.C. § 78n(a).

[2] *See* 15 U.S.C. §§ 78i(f), 78r(a).

[3] *DeKalb Cty. Pension Fund v. Transocean Ltd.*, No. 14-0894-cv, 2016 WL 1055363 (2d Cir. Mar. 17, 2016), available at http://www.ca2.uscourts.gov/decisions/isysquery/60faedc6-2a95-443c-92d9-00ec7645fbc4/6/doc/14-894_opn.pdf (the "Opinion").

[4] The factual background has been summarized from the facts set forth in the Opinion.

[5] 918 F.2d 349 (2d Cir. 1990).

Writing for a unanimous three-judge panel, Judge José A. Cabranes noted that because the private right of action in Section 14(a) is implied and not express, the text of Section 14(a) is silent as to a statute of repose.[6]

Confronted with inferring a statute of repose to Section 14(a) claims, twelve years prior to the enactment of SOX, the Second Circuit, in *Ceres Partners v. GEL Associates*, had borrowed the three-year statutes of repose expressly provided for in Sections 9(f) and 18(a) and "applied them to the implied private rights of action" concluding that Section 14's implied private rights of action were sufficiently "analogous" to the express private rights of action in those sections.[7] Specifically, *Ceres* rationalized this approach by recognizing that Sections 14, 9(f) and 18(a) shared a common purpose – "to ensure full disclosure, [and] to prohibit conduct recognized as manipulative and deceptive."[8]

The DeKalb panel then addressed SOX's subsequent establishment of a five-year statute of repose for "private right[s] of action that involve[] a claim of fraud, deceit, manipulation, or contrivance . . . concerning the securities laws"[9] and its impact on the *Ceres* decision. The Second Circuit concluded that claims under Sections 9(f) and 18(a) provided express "private right[s] of action that involve[] a claim of fraud, deceit, manipulation, or contrivance" and thus fall within the ambit of SOX's five-year statute of repose.[10] But, the Court held that SOX's five-year statute of repose had no bearing on claims brought under Section 14(a) because "Section 14(a) does not provide such a private right of action,"[11] the right therein being judicially implied. The Court also emphasized that Section 14(a) claims do not require proof of fraud, deceit, manipulation, or contrivance with negligence being the minimum standard of culpability. Accordingly, the Court concluded that its pre-SOX decision in *Ceres*, which applied a three-year statute of repose to Section 14(a) claims, retained its vitality.

Turning to the question of when Section 14(a)'s statute of repose begins to run, the panel rejected DeKalb's argument that "Section 18(a)'s 'accrual' standard rather than Section 9(f)'s 'violation' standard'"[12] applied. Pursuant to Section 18(a)'s "accrual" standard, DeKalb's claim would have been timely because it accrued in April, 2010, the date the Transocean drilling rig exploded. However, the Court rejected DeKalb's argument, adhering to Second Circuit[13] and Supreme Court precedent, which dictated that statutes of repose for implied rights of action pursuant to the Exchange Act "begin[] to run when 'the violation' occurs"[14] – here, in October 2007, when the proxy statement was issued.

Focusing on the important distinction between a statute of limitations and a statute of repose, the Second Circuit noted that statutes of repose "are surgical strikes by the legislature"[15] operating as "an absolute bar on a defendant's temporal liability"[16] thus militating against an accrual standard or the discovery rule.[17] Essentially,

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[6] Opinion at *1.

[7] Opinion at *4.

[8] *Id.*

[9] 28 U.S.C.A. § 1658

[10] Opinion at *2.

[11] *Id.*

[12] Opinion at *9.

[13] *See, e.g., Block v. First Blood Assocs.*, 988 F.2d 344, 346 (2d Cir. 1993); *Henley v. Slone*, 961 F.2d 23, 24 (2d Cir. 1992).

[14] *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350, 364 (1991).

[15] Opinion at *9.

[16] Opinion at *1.

[17] Common in fraud or malpractice litigation, the discovery rule dictates that a "cause of action accrues, and the limitation

an injury need not have materialized, let alone be "discovered, for the statute of repose to begin to run."[18] In the same vein, the Court emphasized that statutes of repose were not subject to equitable tolling principles.

III. Significance of the Decision

The DeKalb decision clarifies that Section 14(a) claims are subject to a three-year statute of repose, which begins to run as of the date of the last culpable act or omission. The opinion reinforces the rigidity inherent in statutes of repose which are not subject to equitable tolling principles and operate as an absolute temporal bar extinguishing a litigant's ability to bring a claim. As such, a statute of repose is part and parcel of a plaintiff's affirmative burden of proof, a condition precedent with which a plaintiff must plead compliance.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; John Schuster at 212.701.3323 or jschuster@cahill.com; or Fria Kermani at 212.701.3159 or fkermani@cahill.com.

period begins to run, when a claimant knows or in the exercise of ordinary diligence should have known of the injury." 54 C.J.S. *Limitations of Actions* § 136.

[18] Opinion at *9.