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U.S. District Court in New Jersey Rules that the Two-Year Limitations Period for Suits to Recover Short-Swing Profits under Section 16(b) of the Securities Exchange Act of 1934 Is a Statute of Repose that Is Not Subject to Tolling

Last week, a judge in the United States District Court for the District of New Jersey ruled on an issue that has remained unresolved since the United States Supreme Court split 4-4 on it four years ago: whether the two-year limitations period for bringing claims to recover short-swing profits under Section 16(b) of the Securities Exchange Act of 1934 (the “Exchange Act”) is an ordinary statute of limitations that is subject to extension under the doctrine of equitable tolling, or whether it is a statute of repose that is not subject to extension or tolling under any circumstances.

After a thorough review of the statutory language and statutory framework, Judge Kevin McNulty ruled in a case entitled *Klawonn v. YA Global Investments, L.P.*, that the two-year limitations period is a statute of repose that is not subject to tolling. Quoting the Supreme Court’s language in *CTS Corporation v. Waldburger*, 134 S. Ct. 2175 (2014), Judge McNulty noted that a statute of repose “reflects Congress’s judgment that defendants should be free from liability after a legislatively determined period of time, beyond which the liability will no longer exist and will not be tolled for any reason” — language that defendants may find helpful in other cases in which plaintiffs seek to find exceptions to extend a statute of repose.¹

Section 16(b) of the Exchange Act provides for the disgorgement of profits realized by a beneficial owner of more than 10% of any class of any equity security from any purchase and sale of that security within a less-than six month period. It provides that either the issuer or another shareholder of the issuer may bring suit to recover such short-swing profits, but that “no such suit shall be brought more than two years after the date such profit was realized.”

The issue of whether that two-year limitations period is an ordinary statute of limitations that is subject to equitable tolling or whether it is a statute of repose that is not subject to tolling was presented to the Supreme Court *Credit Suisse Securities (USA) LLC v. Simmonds*, 132 S. Ct. 1414 (2012). The Court split

¹ Recently, the United States Court of Appeals for the Third Circuit granted interlocutory review in a case entitled *North Sound Capital LLC v. Merck & Co Inc*, which presents the issue of whether the *American Pipe* tolling doctrine, which allows courts to toll certain statutes of limitation for members of a putative class who later seek to assert the same claims at issue in the class action, also applies to toll a statute of repose.

4-4 on the issue, with Chief Justice Roberts not participating. The Court ruled 8-0, however, that earlier rules adopted by the United States Court of Appeals for the Second and Eleventh Circuits regarding tolling of the limitations period in Section 16(b) cases were incorrect, and that, if tolling were allowed at all, it should be pursuant to ordinary rules of equitable tolling, not special rules adopted in the Section 16(b) context.

The plaintiff's claims in *Klawonn* raised the precise issue left open by the Supreme Court's split decision. The plaintiff was seeking recovery of short-swing profits allegedly realized prior to November 7, 2007, in a suit that was first filed more than two years later, on April 26, 2010. The defendant, YA Global, moved for summary judgment on the ground that the claims were time-barred, both because the two-year limitations period was a statute of repose and because, even if tolling were allowed, it would not apply in this case because the facts underlying plaintiff's claims were disclosed in the issuer's SEC filings more than two-years before the complaint was filed.

Judge McNulty ruled that the two-year limitations period is a statute of repose. He ruled that the "no such suit shall be brought" language "does not seem to invite equivocation," and that, if Congress had intended that the limitations period be subject to tolling, it "could easily have included language explicitly stating, or at least strongly suggesting, that the two year time period is subject to tolling." He also noted that there is a strong parallel between the language in Section 16(b) and the repose component of the dual time limitations governing the Sarbanes-Oxley Act, and that the statute-of-repose interpretation "comports well" with the fact that Section 16(b) imposes "no-fault liability."

Judge McNulty also ruled that, even if the limitations period were not a statute of repose, equitable tolling would not apply in any event, because the issuer's filings disclosed the facts underlying the plaintiff's claims more than two years before the complaint was filed.

Judge McNulty's opinion may be helpful to defendants in other cases involving other statutes in which there is an issue as to whether a limitations period is a statute of limitations or a statute of repose, and in which the language provides that no suit shall be brought after a specified time since the defendant acted. Judge McNulty found that type of unequivocal language is indicative of a statute of repose.

Judge McNulty's opinion also underscores that a statute of repose is not subject to equitable tolling, and that, even if a limitations period is not a statute of repose, a plaintiff cannot rely upon equitable tolling to extend the limitations period where SEC filings disclose the facts underlying the plaintiff's claim.

Paul, Weiss represented defendant YA Global in this matter.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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