The Statute of Limitations for Section 10(b) Claims and SEC Complaints


Limitations periods can affect substantive rights of litigants. For claims brought under Section 10(b) and Rule 10b-5, Congress provided a 2-year statute of limitations and a 5-year statute of repose. See 28 U.S.C. §1658(b). In *Merck & Co. v. Reynolds*, 130 S. Ct. 1784 (2010), the Court held that the period of limitations begins to run when the plaintiff has discovered, or in the exercise of reasonable diligence could have discovered, the facts that constitute the violation. The Court added that the essential “facts” include the defendant’s mental state, or “scienter.” In *Premium Plus Partners v. Goldman, Sachs & Co.*, Nos. 09-4010, 10-1118, & 10-1119 (7th Cir. Aug. 5, 2011), the Seventh Circuit put further judicial gloss on this rule and answered important questions on the impact of an SEC investigation on the statute of limitations.

In October 2001, Peter Davis attended a meeting of the Treasury Department and learned that the government was going to suspend the sale of its 30-year bonds. Defying an embargo, Davis passed the information to a client who worked at Goldman Sachs; the client then passed the information to traders at Goldman Sachs, and Goldman Sachs reaped a substantial profit from trading activity. The SEC was alerted to abnormal trading, and on September 4, 2003, filed a civil action against Goldman Sachs. Premium Plus Partners filed an action in March 2004 against Goldman Sachs, seeking to represent a class of investors who held short positions and were on the losing end of Goldman’s trades. Class allegations suspend the running of the statute of limitations. See *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974). The district court eventually denied the motion for class certification, which restarted the statute of limitations. Then another group of plaintiffs filed suit. The district court dismissed this suit as untimely.
On appeal, the plaintiffs whose suit was dismissed as untimely argued that the statute of limitations did not start to run until the SEC filed its complaint in September 2003. The plaintiff conceded that they knew of the injury in October 2001 and that they learned in November 2001 that Goldman Sachs traded on the basis of inside information. But, the plaintiffs insisted, scienter was in doubt until the SEC filed its complaint.

The Seventh Circuit held that the plaintiffs could have discovered the facts constituting a violation of Section 10(b) and Rule 10b-5 at the time of the abnormal trading, and thus, the statute of limitations started then. According to the court, the plaintiffs’ argument:

[A]mounts to a contention that a claim for [securities fraud] does not accrue until the defendant has confessed or a court has adjudicated its liability. That’s not the law—nor can the same result be achieved by saying that the period of limitations is tolled until the defendant confesses, or that denial of liability equitably estops the defendant to plead the statute of limitations.

The focus of the inquiry for the purpose of applying the statute of limitations, the court continued, is “on what the plaintiff knows or could have found out, not what the defendant admits or denies—or for that matter on what a federal agency such as the SEC believes.” The court said that the SEC’s filing of its civil action is of limited value:

There’s no magic in the filing date of the [SEC’s] complaint, which did not reveal to the public any facts previously unknown. It tells us what the [SEC] believed about the defendants’ mental state, but not when a reasonably diligent person would have reached that conclusion. It would be silly to conclude that, because the SEC did not file its complaint until September 2003, no reasonably diligent per-
son could have inferred *scienter* earlier. Obviously the [SEC’s] investigators drew that inference long before September 2003; it takes months (if not years) for a proposed complaint to wend its way through the agency’s labyrinthine processes.

Ultimately, the Seventh Circuit concluded that all the facts necessary to allow a reasonable plaintiff to discover the violation were available in October 2001, and thus, the plaintiff’s claim was untimely.

The Seventh Circuit’s decision is available here:  