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Report from Washington

Supreme Court Considers Whether Unnamed Class Members With Tolled and Timely Claims Can Bring a New Class Action After Expiration of the Otherwise Applicable Limitations Period

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Introduction

On March 26, 2018, the Supreme Court heard oral arguments in an important class action case, *China Agritech, Inc. v. Resh*, No. 17-432. In *China Agritech*, the petitioner asks the Court to consider if an absent class member whose individual claims are timely as a result of the tolling doctrine established in *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974), may file a new class action after the expiration of the otherwise applicable limitations period.

Under existing *American Pipe* Supreme Court Doctrine, a pending class action tolls the applicable statute of limitations, allowing absent would-be class members to intervene in a pending case or file new **individual** suits after the denial of class certification when the statute of limitations period would have otherwise expired. The moment class certification is denied or vacated, or the case is dismissed without a class being certified, the statute resumes running as to the previously asserted members of the class and they have whatever time remained to them when the prior class suit was filed within which to pursue an individual claim. In *China Agritech*, the Court must determine whether the *American Pipe* tolling doctrine extends to subsequent **class action** suits, permitting so-called “stacking” of successive class actions in order to continue indefinitely the toll otherwise ended by denial of class certification in a prior class action.

The Court's decision will finally resolve several circuit court splits on the issue.

Background

China Agritech shareholders brought two consecutive class actions against the company, alleging various violations of securities laws. The first action accused China Agritech of

materially misstating its net revenue and income in SEC filings. The district court denied class certification because plaintiffs failed to demonstrate the predominance requirement of Rule 23. The second case's complaint was almost identical to the first, but alleged only violations of the Exchange Act. The court again denied the plaintiffs' motion for class certification, this time for failing to meet typicality and adequate representation requirements.

Michael Resh, an absent putative class member in the first two class actions, filed a third class action against China Agritech and various individual defendants based on the same facts. The district court dismissed Resh's class action complaint as untimely, finding that the application of *American Pipe* tolling to class action claims would "allow tolling to extend indefinitely as class action plaintiffs repeatedly attempt to demonstrate suitability for class certification on the basis of different expert testimony and/or other evidence."

The Ninth Circuit reversed, reasoning that "permitting future class action named plaintiffs, who were unnamed class members in previously uncertified classes, to avail themselves of *American Pipe* tolling would advance the policy objectives that led the Supreme Court to permit tolling in the first place." The court reasoned that the later class actions would not unfairly surprise defendants because the preceding class action would have alerted defendants to the relevant substantive claims and potential class members. The court concluded that its decision would not lead to the abusive filing of class actions, believing potential plaintiffs and their attorneys would have little to gain from the financial risk of filing successive class actions when class certification is unlikely. The court noted that "ordinary principles of preclusion and comity will further reduce incentives to re-litigate frivolous or already dismissed class claims, and will provide a ready basis for successor federal district courts to deny class action certification."

In so holding, the Ninth Circuit joined with the Sixth and Seventh Circuits in finding that the *American Pipe* tolling doctrine applies to subsequent class actions. In contrast, the First, Second, Fifth, and Eleventh Circuits limit the *American Pipe* tolling doctrine to claims by **individual** plaintiffs. The Third and Eighth Circuits have taken an intermediary position, only allowing subsequent class actions when class certification was denied for reasons that were unrelated to the validity of the class, such as where the denial was based solely on lead plaintiffs' deficiencies as class representatives.

The Supreme Court granted China Agritech's petition for writ of certiorari on December 8, 2017, to resolve the circuit split and determine the scope of *American Pipe*'s tolling doctrine.

Oral Argument Highlights

The oral argument focused heavily on the traditional requirements of tolling as an equitable remedy, which include that plaintiffs must demonstrate “diligence,” meaning that they have taken action to defend their own legal rights, *and* some extraordinary circumstance. Here, the attorneys disagreed on the level of diligence plaintiffs are required to show to toll the statute of limitations under the *American Pipe* tolling doctrine. The attorneys also debated whether the “extraordinary circumstance” relevant to *American Pipe* tolling is the desire to avoid multiple **individual** claims while a class action is pending, or the prevention of duplicative cases in general, whether they be individual or class actions, while a class action is pending.

“Rule 23 would indicate that we don't want to have a million individual suits but instead want to encourage a class.”

—Justice Kagan

Counsel for China Agritech argued that the Court permitted equitable tolling for individual plaintiffs in *American Pipe* because: (1) after the denial of class certification, plaintiffs show the diligence required for tolling when they bring their own individual claims in court; and (2) the enforcement of the statute of limitations would undermine the point of Rule 23 by encouraging plaintiffs to bring duplicative independent claims during a pending class action litigation instead of relying on the class action to represent their interests. The company's attorney argued that neither of those reasons are applicable to the tolling of class action claims because: (1) the absent class action members have not shown the diligence required by equity as they are still absent and are not taking action to protect their individual rights even after class certification is denied; and (2) after the denial of class certification, there is no “extraordinary circumstance,” as the concern about plaintiffs filing redundant protective individual claims that detract from the value of a pending class action is no longer relevant.

“[W]hat about honoring Rule 23? It seems to me that [counsel for China Agritech is] creating an exception to the rule. If you just read it on its face, the statute of limitations hasn't run because of American Pipe . . . , so why shouldn't that rule be available . . . ?”

—Chief Justice Roberts

Justice Kagan acknowledged that she was a little “skeptical” of China Agritech's arguments. She noted that the Court's *American Pipe* decision was motivated because: (1) the Court thought plaintiffs were sufficiently diligent when they relied on a pending class action to represent their interests; and (2) the policies behind Rule 23 indicated that the Court should encourage class actions over individual actions in general. She noted that, in this case, “the exact same thing is true. Diligence is shown in the same way by reliance on the class, and, once again, even after the denial of a single motion for class certification, Rule 23 would indicate that we don't want to have a million individual suits but instead want to encourage a class.”

Counsel for Resh agreed with Justice Kagan, claiming that: (1) class members in this case *had* shown diligence by relying on the tolling doctrine in *American Pipe*; and (2) the purpose of Rule 23 would be best served by allowing class actions to toll the statute of limitations for other class action claims because it avoids the potential of having an overabundance of

“Rule 23 says nothing about tolling. Tolling is, as you have said, an equitable doctrine. Tolling is made up by courts. Courts decide if there is tolling, how long the tolling will be. [T]olling questions are not resolved by the federal rules.

Equitable tolling is court-made law, not rule-made law.”

—Justice Ginsburg

“[I]f we were to rule against [Resh], it seems to me the effect might be that we would encourage more protective filings. And that would solve the problem, wouldn't it? We wouldn't have to create these extraordinary rules in extending American Pipe in new ways; we'd just create a new incentive structure that would ensure that there are backup class actions available. . . . [W]hat's wrong with that?”

—Justice Gorsuch

individual claims filed by plaintiffs after the denial of class certification and the expiration of the statute of limitations. He argued that the “extraordinary circumstance” here is the desire to enforce the principles behind Rule 23 and to “incentivize people not to bring duplicative claims.”

China Agritech’s attorney argued that unnamed class action plaintiffs could never show diligence by relying on a class action that was filed outside of the statute of limitations. He claimed that *American Pipe* stands for the principle that plaintiffs should not bring individual actions while the class action is pending and does not indicate other class actions should not be brought during that same period. Counsel for Resh countered that, when evaluating plaintiffs’ diligence, it is proper to look at the due diligence of the person *before* the case was filed. He noted that the due diligence of the plaintiffs was demonstrated by their reliance on the *American Pipe* tolling doctrine.

Justice Sotomayor pressed the parties on their view of the Third and Eighth Circuit approach, which holds that the application of the tolling doctrine depends on the reason for the denial of class certification. Both parties distanced themselves from this rule. Counsel for Resh, while recognizing that such a holding would be beneficial for him, noted that “as a matter of equity, it does not seem fair where you're talking about a rule that is allowing potentially meritorious claims to go forward to be snuffed out simply because the person who got to the courthouse first happened not to be competent in bringing about the kind of case that would be representative of all of the various plaintiffs.”

The arguments also focused on the purpose of Rule 23 and which approach best fulfills the interests underlying the rule. Chief Justice Roberts questioned counsel for China Agritech on how his approach was consistent with Rule 23, noting that it seemed like China Agritech’s attorney was “creating an exception to the rule. If you just read [Rule 23] on its face, the statute of limitations hasn't run because of *American Pipe* . . . so why shouldn't that rule be available. . . .?” Counsel for China Agritech claimed that *American Pipe* did not originate from Rule 23, but rather was rooted in “traditional principles of equity, and those principles require diligence and extraordinary circumstances.”

Justice Ginsburg pressed Resh’s attorney on his Rule 23 argument, noting that “Rule 23 says nothing about tolling. Tolling is, as you have said, an equitable doctrine. Tolling is made up by courts. Courts decide if there is tolling, how long the tolling will be. [T]olling questions are not resolved by the federal rules. Equitable tolling is court-made law, not rule-made law.” Counsel for Resh responded that, while equitable tolling for class actions may not be

mentioned in Rule 23, all of the Rules of Civil Procedure automatically apply when a plaintiff has a timely claim.

The Justices showed concern for small value claims that would not be worthwhile to bring as individual actions. Justice Kagan observed that the reason for Rule 23 “is that we understand that with respect to some category of claims, we’re not going to have them individually or it will be so ridiculous if we have them individually that we would prefer the class action devices.” Counsel for China Agritech argued that those with small claims should file their own class actions within the period of the statute of limitations if they were concerned about the financial feasibility of filing an individual claim. Justice Gorsuch was receptive to this argument, commenting: “[I]f we were to rule against [Resh], it seems to me the effect might be that we would encourage more protective filings. And that would solve the problem, wouldn’t it? We wouldn’t have to create these extraordinary rules in extending *American Pipe* in new ways; we’d just create a new incentive structure that would ensure that there are backup class actions available. . . . [W]hat’s wrong with that?” Counsel for Resh countered that the idea behind a representative action was the importance of aggregating claims of small value. Therefore, the application of the *American Pipe* tolling doctrine to class actions best fulfills the goals promoted by Rule 23.

“[C]an you stack [class actions] forever, so that try, try again, and the statute of limitations never really has any force in these cases. What do we do about that, given the congressional judgment that there should be a statute of limitations?”

—Justice Gorsuch

Justice Gorsuch showed concern about the perpetual filing of class actions, asking if plaintiffs could “stack them forever, so that try, try again, and the statute of limitations never really has any force in these cases.” Resh’s counsel responded that the repose period is the outer limit in securities litigation and that comity will be a “powerful mechanism” to limit serial motions for class certification.

Implications

The Court’s decision could have important implications for how and when future class action suits are filed. A decision in the shareholder class’s favor could expose defendants to repetitive class actions, tempting plaintiffs to file one substantially identical class action after another in an attempt to toll the statute of limitations indefinitely until a court grants class certification. Alternately, a decision limiting the tolling of the statute of limitations to subsequent individual filings could encourage the plaintiffs’ bar to file duplicative class actions during the tolling period. Either way, the Court’s decision in *China Agritech* will clarify the *American Pipe* tolling doctrine, allowing plaintiffs to know when they must bring class actions in order for them to be timely.

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