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Learning to Stand Again: Revisiting RMBS Class Claims in Light of *NECA-IBEW*

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In this article, the authors review a recent U.S. Court of Appeals for the Second Circuit decision addressing class claims in the residential mortgage-backed securities market.

In the last few years, some courts developed a trend that limited investors from representing others in cases for fraud in the residential mortgage-backed securities ("RMBS") market. Specifically, certain courts precluded class plaintiffs from suing for those who purchased securities derived from the same shelf statement but who did not purchase the same security. Other courts limited classes to investors in the same trust (regardless of tranche level). But those limitations, at least for some, were lifted by the U.S. Court of Appeals for the Second Circuit in *NECA-IBEW Health & Welfare Fund v. Goldman Sachs & Co.*,[1] so it may be time to rethink class membership.

RMBS CLASS ACTIONS

After investors incurred huge losses and learned of misrepresentations for RMBS purchased from 2005 to 2008, some plaintiffs brought class actions

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under the Securities Act. Class plaintiffs often sought recompense for all that purchased securities derived from the given shelf statement. That document and its supplements attested to loan quality and compliance with underwriting standards — representations alleged false. The class-action mechanism ostensibly allowed investors that did not litigate themselves to have a chance at a remedy.

But several rulings in 2010 excluded investors from classes if they did not purchase the exact security as named representatives. These rulings were based on the "class standing" doctrine, which holds that a plaintiff may not represent a class if he or she has not been injured by the same conduct as other class members. According to these rulings, class standing failed because named plaintiffs did not allege injury from the same securities.

NECA-IBEW

The Second Circuit may have reopened the door when it reversed one of those decisions in *NECA-IBEW.* In that case Goldman Sachs made representations in a shelf statement about underlying loans from several originators, and created 17 tranches with different risk levels and securities available for purchase. The plaintiff pension fund based its claims on misstatements in the shelf statement, but Goldman argued that the claims should be limited to those who purchased certificates in the tranches from which the pension fund made purchases.

The Second Circuit rejected Goldman's argument, holding the class proper because (1) the pension fund suffered actual injury as a result of the alleged illegal conduct and (2) that conduct implicated the same set of concerns as that which harmed other class members. The concerns were that origination practices for the loans were falsely stated. This meant that the pension fund had standing to assert claims for other investors who received the same shelf statement, so long as the originators for those loans were the same.

The Second Circuit reaffirmed *NECA-IBEW* on March 1, 2013 when it reversed another dismissal of class claims on standing doctrine. In *New Jersey Carpenters Health Fund v. Royal Bank of Scotland Group PLC*, the court relied on the law of *NECA-IBEW*: "[W]here an issuer had issued multiple securities under the same shelf registration statement, a plaintiff who had invested in at

least some of those securities could, as the representative of a putative class, bring claims based on securities in which it had not invested so long as all of the relevant claims implicated 'the same set of concerns.'"[2]

And on March 18, 2013, the U.S. Supreme Court denied *certiorari* review for *NECA-IBEW*.

RMBS CLASS RULINGS REVISITED

So what are the ramifications for investors previously kicked out of classes? The answer may depend on several factors:

First is settlement. For many cases where the class was before restricted, the parties may have settled before *NECA-IBEW*. Previously excluded investors probably would not have been covered by those settlements, and thus would have to bring their own claims (if they are still valid).

A second issue is the jurisdiction of potential class claims. For investors with claims relating to shelf statements asserted by Second Circuit plaintiffs, those claims may now be valid or subject to reinstatement, if the case is ongoing. Some New York federal judges have gone back on their old holdings excluding non-certificate holding class members.[3] But for cases outside the Second Circuit, the question is more difficult. The U.S. Court of Appeals for the First Circuit, for example, said in 2011 that an RMBS class can only be made up of the same certificate holders.[4] District courts in other areas of the country have taken that view, and a California federal court affirmed its disagreement with *NECA-IBEW* in 2012.[5]

One other difficulty is the condition that underlying loans be originated by the same entities. According to the ruling, only representations regarding the same originator underwriting practices invoke the "same set of concerns" and thus justify class standing. Some New York federal courts have been careful of this distinction.[6]

As of now, below are the statuses of some RMBS class litigation[7] that had previously excluded as class plaintiffs those who did not hold the plaintiff's specific certificates:

CASE	POST-*NECA-IBEW* ACTION?
N.J. Carpenters Health Fund v. RALI Series 2006-QQ1 Trust, No. 08-cv-08781 (S.D.N.Y.)	April 30, 2013 Order for reconsideration granted and certain class claims revived
N.J. Carpenters' Vacation Fund v. The Royal Bank of Scotland Group, No. 08-cv-05093	April 30, 2013 Order for reconsideration granted and certain class claims revived
City of Ann Arbor Employees Retirement v. Citigroup Mortg. Loan Trust, No. 08-cv-01418 (E.D.N.Y.)	Claims settled before chance for reconsideration
NECA-IBEW Health & Welfare Fund v. Goldman Sachs & Co., No. 08-cv-10783	Reversed and Remanded by Second Circuit, some class claims reinstated
In re Wells Fargo Mortg. Backed Certificates Litig., 09-cv-01376 (N.D. Cal.)	Claims settled before chance for reconsideration
Pub. Employees' Retirement System of Miss. v. Merrill Lynch & Co., No. 08-cv-10841 (S.D.N.Y.)	Claims settled before chance for reconsideration
In re Indy-Mac Mortgage Backed Sec. Litig., 09-cv-04583 (E.D.N.Y.)	Nov. 16, 2012 Order for reconsideration denied pending Supreme Court action
In re Morgan Stanley Mortg. Pass-Through Certificates Litig., 09-Civ-02137 (S.D.N.Y.)	Jan. 11, 2013 order reversed prior holding and will allow plaintiff to assert claims for 14 offerings

IMPLICATIONS

The bottom line is that investors that relied on potential class membership and who felt thwarted by prior rulings should re-assess their options in light of the Second Circuit's rulings. Those investors may have renewed claims as class members, and would thus need to decide whether they should opt out and bring their own suit or can rely on class membership.

What is also uncertain is how these issues translate into the validity of remaining claims, specifically the statute of limitations. Sometimes a class action covering a claim will toll the limitations period for an overlapping

individual claim, often at least until that class claim is dismissed or the class is redefined to exclude the individual claim. Since the statute of limitations under the Securities Act (for Sections 11, 12, and 15) is one year from discovery or three years from either the security's offering or sales date, tolling may be essential for any new claim based on conduct from 2005 through 2008.

The Second Circuit's ruling has opened up potential claims for many investors, but the ruling's requirements for shared loan originators and jurisdictional limitations require prompt and diligent consideration of any chances for recovery.

NOTES

[1] 693 F.3d 145 (2d Cir. 2012).

[2] __ F.3d. __, No. 12-1707-cv (2d Cir. March 1, 2013).

[3] *In re Lehman Bros. Secs. & ERISA Litig.*, 09 MD 2017, 2013 U.S. Dist. LEXIS 13999, *20 n.3 (S.D.N.Y. Jan. 23, 2013); *N.J. Carpenters Health Fund v. RALI Series 2006-QO1 Trust*, No. 2:08-cv-08781 (S.D.N.Y. May 1, 2013).

[4] *Plumbers' Union Local No. 12 Pension Fund v. Nomura Asset Acceptance Corp.*, 632 F.3d 762, 770 (1st Cir. 2011).

[5] *FDIC v. Countrywide Financial Corp.*, No. 2:12-CV-4354, 2012 U.S. Dist. LEXIS 167696 (C.D. Cal. Nov. 21, 2012).

[6] *See N.J. Carpenters Health Fund v. DLJ Mortg. Capital*, No. 08 Civ. 5653, 2013 U.S. Dist. LEXIS 12630, *22 (S.D.N.Y. Jan. 23, 2013); *Plumbers' & Pipefitters Local # 562 Supp. Plan & Trust v. J.P. Morgan Acceptance Corp. I* ("Local 562"), No. 08 Civ. 1713 (ERK), 2012 U.S. Dist. LEXIS 132057 (E.D.N.Y. Sept. 14, 2012).

[7] Many other cases have certainly been affected by the *NECA-IBEW* ruling.