

An individual investor purchased stock through a company's stock offering. When the price of the stock plummeted, the investor sued the company in a state court in State A, claiming that the company's offering materials had fraudulently induced him to purchase the stock and seeking \$25,000 in damages.

A university that had purchased the company's stock through the same offering sued the company in federal court in State B, claiming that the offering materials violated federal securities laws and seeking \$1 million in damages.

The individual investor's suit proceeded to trial. The state court ruled that the company's offering materials contained false information and awarded the investor a \$25,000 judgment. The university immediately moved for partial summary judgment in its federal action against the company, arguing that the state court judgment bound the federal court on the issue of whether the company's offering materials contained false information.

Neither State A nor State B permits nonmutual issue preclusion.

Should the court grant the university's motion?

- A. No, because State A does not permit nonmutual issue preclusion.
- B. No, because the federal court sits in a state that does not permit nonmutual issue preclusion.
- C. Yes, because federal law permits nonmutual issue preclusion.
- D. Yes, because the issue of whether the materials contained false information was actually litigated and necessarily decided.

Explanation:

Issue preclusion (ie, collateral estoppel) precludes subsequent litigation of the *same* issue actually litigated, determined, and necessary to a valid final judgment issued on an earlier claim. There are two types of issue preclusion:

- **Mutual** – issue preclusion in second action **asserted by parties** to the first action against other parties to the first action
- **Nonmutual** – issue preclusion in second action **asserted by nonparties** to the first action against parties to the first action

The court will look to the court that entered the first judgment to determine which issue-preclusion rule applies to the second action. A judgment entered by a *federal* court means *federal* preclusion law applies,* while a judgment **entered by a state court** means that **state's preclusion law applies**.

Here, the state court in State A entered the first judgment, so State A's preclusion law applies to the second action in federal court. State A does not permit nonmutual issue preclusion. As a result, the university (a nonparty to the first action) cannot argue that the state court judgment bound the federal court on the same issue. The federal court should therefore deny the university's motion for partial summary judgment.

*A federal court sitting in diversity will generally apply the preclusion law of the state in which it sits unless the state law is incompatible with federal interests.

(Choice B) A judgment's preclusive effect is determined by the law of the forum that entered the judgment (here, State A)—not the forum where the second court sits (here, State B).

(Choice C) Although federal law permits nonmutual issue preclusion, the State A law prohibiting nonmutual issue preclusion applies.

(Choice D) The issue of whether the company's materials contained false information was actually litigated and necessarily decided in the first action. But since State A does not permit nonmutual issue preclusion, the university cannot assert it in the second action.

Educational objective:

Issue preclusion can be asserted by parties to the first action (mutual) OR by nonparties to the first action (nonmutual) against parties to the first action. If the first action was decided by a state court, then that state's issue-preclusion rule applies.

References

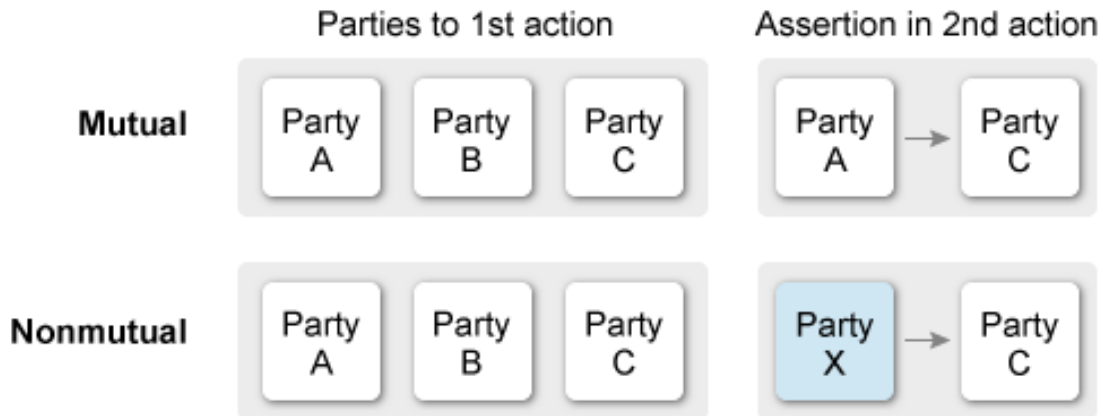
- Allen v. McCurry, 449 U.S. 90, 96 (1980) (stating that federal courts must give the same preclusive effect to state court judgments that courts in the judgment-rendering state would apply).

- 47 Am. Jur. 2d Judgments § 549 (2020) (explaining mutual and nonmutual estoppel).
- 28 U.S.C. § 1738 (full faith and credit statute).

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Mutual v. Nonmutual issue preclusion



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