THE NATIONAL LAW REVIEW

New York Court of Appeals Rules that Civil Securities Fraud Claims Brought Under Martin Act are Subject to Three-Year Statute of Limitations

SheppardMullin

Article By
Sarah E. Aberg
Kate Ross
Sheppard, Mullin, Richter & Hampton LLP
Corporate & Securities Law Blog

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Friday, July 13, 2018

In *People v. Credit Suisse Securities (USA) LLC*, No. 40, 2018 WL 2899299 (N.Y. June 12, 2018), the Court of Appeals for the State of New York ruled that the three-year statute of limitations of Section 214(2) of the New York Civil Practice Law & Rules ("CPLR") applies to civil enforcement actions brought under the Martin Act (General Business Law article 23-A) on the basis of a "fraudulent practice" as defined in General Business Law § 352(1). In doing so, the Court overruled both the New York Supreme Court and the Appellate Division and rejected the New York Attorney General's ("NYAG") attempt to apply a six-year statute of limitations under CPLR 213(8), which governs the limitations period for common law fraud. The Court's decision narrows the window of opportunity to assert civil securities fraud claims under the Martin Act's more forgiving standard. Prosecutors wishing to avail themselves of CPLR 213's generous six-year statute of limitations will now be required to demonstrate their civil securities fraud claims meet all of the elements of common law fraud.

In November 2012, NYAG brought a civil enforcement action against Credit Suisse Securities (USA) LLC and its affiliates ("Credit Suisse"), alleging that Credit Suisse engaged in fraudulent acts in connection with the creation and sale of residential mortgage-backed securities in 2006 and 2007. Specifically, NYAG's complaint alleged that Credit Suisse misrepresented the quality of loans underlying these securities, as well as the thoroughness of its due diligence. NYAG asserted causes of action under both the Martin Act and Executive Law § 63(12), which authorizes NYAG to bring an action to "enjoin the continuance . . . of any fraudulent or illegal acts, [and] direct[] restitution and damages" for "repeated fraudulent or illegal acts." Credit Suisse moved to dismiss the Martin Act claim, arguing that it was time-barred under CPLR 214(2)'s three-year statute of limitations. The New York Supreme Court denied the motion, and the Appellate Division affirmed.

At issue was which CPLR provision — 214(2) or 213(8) — governs the timeliness of a Martin Act claim. The Court held that under *Gaidon v. Guardian Life Ins. Co. of Am.*, 96 N.Y.2d 201, 208-209, 750 N.E.2d 1078 (2001), CPLR 214(2)'s three-year limitation applies only "where liability 'would not exist but for a statute,'" though "akin" to common law causes of action. *Credit Suisse*, 2018 WL 2899299, at *4.

The Martin Act "authorizes the Attorney General to investigate and enjoin fraudulent practices in the marketing of stocks, bonds and other securities within or from New York State." *Kerusa Co. LLC v. W10Z/515 Real Estate Ltd. Partnership*, 12 N.Y.3d 236, 242, 906 N.E.2d 1049 (2009). Since former Attorney General Eliot Spitzer dusted it off following his 1998 election, the Martin Act has served as a powerful prosecutorial tool to combat securities fraud because it eliminates the scienter and reliance requirements of common law fraud claims. These requirements entail establishing (1) a material misrepresentation of fact, (2) knowledge by the defendant of its falsity, (3) an intent to induce reliance (known as scienter), (4) justifiable reliance and (5) damages. *See Eurycleia Partners LP v. Seward & Kissel, LLP*, 12 N.Y.3d 553, 559, 910 N.E.2d 976 (2009); *Ross v. Louise Wise Servs.*, 8 N.Y.3d 478, 488, 868 N.E.2d 189 (2007).

The act prohibits "any representation or statement which is false, where the person who made such representation or statement: (i) knew the truth; or (ii) with reasonable effort could have known the truth; or (iii) made no reasonable effort to ascertain the truth; or (iv) did not have knowledge concerning the representation or statement made." General Business Law § 352-c(1)(b), (1)(c). This language creates a more lenient standard by eliminating the scienter (or "intentional fraud") and reliance requirements. In doing so, the Martin Act creates liability for a substantially broader range of conduct than could be captured under a common law fraud theory, as prosecutors need only allege "material misrepresentations intended to influence the bargain . . . ." *People v. Federated Radio Corp.*, 244 N.Y. 33, 38-39, 154 N.E. 655 (1926); *see also State of New York v. Sonifer Realty Corp.*, 212 A.D.2d 366, 367, 622 N.Y.S.2d 516 (App. Div. 1995).

In its decision, the Court of Appeals reasoned that because the Martin Act does not require a showing of scienter or reliance, this cause of action "encompasses 'wrongs' not cognizable under the common law" and thus is subject to *Gaidon*'s test. As a result, the Court dismissed NYAG's Martin Act claim, as it was filed more than three years after the time of Credit Suisse's alleged misconduct.

The Court left open the question of Credit Suisse's liability for common law fraud, and its applicable six-year statute of limitations, under Executive Law § 63(12). Executive Law § 63(12) gives NYAG "standing to redress liabilities recognized elsewhere in the law" (*i.e.*, beyond the scope of the Martin Act), thereby "expanding the scope of available remedies." The Court ruled that if the conduct underlying the Executive Law § 63(12) claim amounts to "a type of fraud recognized in the common law," the action would be governed by a six-year statute of limitations under CPLR 213(8). The Court remanded the case for further proceedings to consider whether NYAG had stated a cause of action for common law fraud. The Court's decision also did not address whether CPLR 214(2) applies to criminal claims, or other civil claims brought under the Martin Act.

Credit Suisse establishes an important defense for New York defendants facing securities fraud claims in civil enforcement proceedings. Unless the prosecution can establish the elements of scienter and reliance, these types of proceedings will be limited to a three-year statute of limitations period.