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June 14, 2018

## **The New York Court of Appeals Rules That Martin Act Claims Are Subject to a Three-Year Statute of Limitations**

On June 12, 2018, in *People v. Credit Suisse Securities (USA) LLC, et al.*, the New York Court of Appeals held that claims brought under the Martin Act—New York’s uniquely broad Blue Sky Law, a powerful tool that permits the Attorney General to bring claims concerning the purchase or sale of securities that do not require proof of scienter or reliance—are subject to a three-year statute of limitations. The Court rejected the New York Attorney General’s argument that Martin Act claims should be subject to a longer, six-year statute of limitations.

The Court also considered the statute of limitations applicable to New York Executive Law § 63(12), which parallels, to some extent, the language of the Martin Act and proscribes “repeated fraudulent or illegal acts or otherwise [ ] persistent fraud or illegality in the carrying on, conducting or transaction of business . . . .”<sup>1</sup> The Court held that, unlike for claims under the Martin Act, the statute of limitations applicable to actions under Executive Law § 63(12) depends on the nature of the specific claim alleged. The Court ruled that a six-year statute of limitations would apply to the Attorney General’s claims against Credit Suisse under Executive Law § 63(12) only if the trial court determines that the Attorney General pleaded a cause of action that, if proven, would amount to common law fraud. The Court remanded the case to the Supreme Court for determination of that issue.

In short, the holding in *Credit Suisse* will narrow the window in which the New York Attorney General (“NYAG”) can assert Martin Act claims, requiring the NYAG to act more quickly to bring cases under that unusual statute, or else it will be required to rely on scienter-based claims, which present higher hurdles for the enforcement authorities.

### **Background & Procedural History**

Around the time of the 2008 financial crisis, the NYAG began an investigation into whether Credit Suisse’s practices, in 2006 and 2007, in issuing certain residential mortgage-backed securities (“RMBS”) violated state law, including the Martin Act. The Martin Act “authorize[s] the Attorney General to investigate and enjoin fraudulent practices in the marketing of stock, bonds and other securities within or from New York State [ ].”<sup>2</sup>

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<sup>1</sup> Op. at 3, 11–12.

<sup>2</sup> Op. at 6.

In March 2012, Credit Suisse entered into a tolling agreement with the NYAG. In November 2012, the NYAG commenced an action against Credit Suisse in New York Supreme Court, alleging violations of the Martin Act and Executive Law § 63(12) based on Credit Suisse's conduct in 2006 and 2007.<sup>3</sup> Both causes of actions were based on the same basic facts, which, as alleged by the NYAG, were that Credit Suisse misled investors as to the quality of the loans underlying the RMBS and the nature of the due diligence that Credit Suisse was performing on the underlying loans.

Credit Suisse timely moved to dismiss on the grounds that the applicable statute of limitations for Martin Act and Executive Law § 63(12) claims is three years, and thus the limitations period for conduct in 2006 and 2007 had expired prior to Credit Suisse signing the March 2012 tolling agreement. The Supreme Court denied Credit Suisse's motion, and the First Department affirmed, over the dissent of two justices.

### Decision

On June 12, 2018, the Court of Appeals reversed the First Department's decision, holding that a three-year statute of limitations applies to Martin Act claims and that the statute of limitations applicable to claims brought under § 63(12) of the Executive Law is dependent on the nature of the specific action alleged. The Court of Appeals dismissed the Martin Act claims against Credit Suisse and remanded the action to the trial court to determine whether the NYAG's complaint adequately pleaded the elements of common law fraud, in which case the applicable statute of limitations for the Executive Law § 63(12) claims would be six years.

With respect to the Martin Act claims, the Court reasoned that the "Martin Act imposes numerous obligations—or 'liabilities'—that did not exist at common law, justifying the imposition of a three-year statute of limitations under CPLR 214(2)," which generally applies to "action[s] to recover upon liability, penalty or forfeiture created or imposed by statute . . ."<sup>4</sup> The Court noted that the definition of "'fraudulent practices,' as repeatedly amended by the Legislature and interpreted by the courts, encompasses 'wrongs' not cognizable under the common law and dispenses, among other things, with any requirement that the Attorney General prove scienter or justifiable reliance on the part of investors."<sup>5</sup> The Court therefore held that the decision to apply a three-year statute of limitations to Martin Act claims was guided by the Court's prior precedent in *Gaidon v. Guardian Life Insurance Company of America*, where the Court ruled that claims under General Business Law § 349 were subject to the three-year statute of limitations under CPLR § 214(2) because the statute "both lacks a scienter requirement and encompasses a wider range of deceptive business practices than were condemned at common law."<sup>6</sup>

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<sup>3</sup> *People v. Credit Suisse, et al.*, 145 A.D.3d 533, 533 (1st Dep't 2016).

<sup>4</sup> *Op.* at 10–11.

<sup>5</sup> *Op.* at 10.

<sup>6</sup> *Gaidon v. Guardian Life Ins. Co. of Am.*, 96 N.Y.2d 201, 208 (2001).

With respect to the Executive Law claims, the Court held that although Executive Law § 63(12) was amended with the intention to “equate the meaning of the words ‘fraud’ and ‘fraudulent’ as used therein with the provisions of the Martin Act,” the statute gives the NYAG “standing to redress liabilities recognized elsewhere in the law, expanding the scope of available remedies.”<sup>7</sup> Therefore, the Court held, courts are required to “‘look through’ Executive Law § 63(12) and apply the statute of limitations applicable to the underlying liability.”<sup>8</sup> The Court noted that the lower courts in *Credit Suisse* had held that the statute of limitations applicable to Executive Law § 63(12) was six years without considering whether the NYAG had alleged all the elements of common law fraud. The Court therefore remanded the action to the Supreme Court to determine whether the NYAG had adequately alleged the elements of common law fraud; if not, the Court advised, the NYAG’s case would be subject to dismissal as time-barred.

The majority decision was authored by Chief Judge DiFiore, and Judges Stein, Fahey and Feinman concurred. Judge Feinman wrote a separate concurring opinion, which was joined by Judge Fahey. In that decision, Judge Feinman adopted the opinion of the Court with respect to the Martin Act statute of limitations, but wrote separately to provide additional guidance as to how, in his view, lower courts should apply the Court’s guidance with respect to Executive Law § 63(12). Judge Feinman reasoned that the lower courts should apply a six-year statute of limitations to the NYAG’s claims if the NYAG pleads either “equitable” or “actual” fraud, as those terms are understood in the common law. This interpretation would permit the NYAG’s claims against *Credit Suisse* to go forward based on allegations of either intentional misrepresentation or justifiable reliance. If the complaint merely alleges “conduct that would tend to deceive or mislead,” Judge Feinman reasoned, such a claim would be beyond anything “actionable at common law” and therefore the narrower three-year statute of limitations set forth in CPLR § 214(2) would apply.<sup>9</sup>

Judge Rivera dissented. In a separate opinion, Judge Rivera disagreed with both the majority’s textual interpretation of CPLR § 214(2) and its analysis of the case law, particularly as it relates to the Martin Act. Judge Rivera asserted that the majority decision was inconsistent with the intent of the legislature to invest the NYAG with “broad powers” to “protect the integrity of the securities markets and the interests of investors.”<sup>10</sup> Judge Rivera implored the state legislature to intervene and make explicit that a six-year statute of limitations applies to Martin Act claims.

Judges Garcia and Wilson took no part in the decision.

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<sup>7</sup> Op. at 11–12.

<sup>8</sup> Op. at 12.

<sup>9</sup> Concurring Op. at 11 (Feinman, J.).

<sup>10</sup> Dissenting Op. at 20 (Rivera, J.).

**Analysis**

The Credit Suisse decision is significant for defendants facing potential Martin Act and Executive Law § 63(12) charges by the New York Attorney General. The NYAG will now have to pursue claims against parties under the Martin Act more quickly to be actionable. The NYAG may be more aggressive in pursuing tolling agreements as a result, but regardless, the pressure on the office to initiate and conclude investigations more quickly will increase.

If the NYAG seeks to avoid the narrower statute of limitations under the Martin Act and instead pursue claims based on similar facts under Executive Law § 63(12), it will have to prove the elements of common law fraud, including scienter, in order to receive the benefit of a six-year statute of limitations. In effect, the twin holdings in Credit Suisse mean that if the NYAG wishes to pursue non-scienter based claims under either statute, it must do so within three years. Given the overwhelming breadth of the Martin Act, this is a significant limitation on one of the most important tools in the NYAG's enforcement toolbox.

The Credit Suisse decision may also signal broader implications, following significant recent turnover on the Court of Appeals. Notably, six of the seven judges on the Court of Appeals have been appointed within the last three years, and barring unforeseen circumstances, no vacancies are expected until the end of 2021. The four-one split among the judges, with Judges Garcia and Wilson recused, suggests the Court potentially taking a more business-friendly approach to enforcement matters before it, a trend which remains to be seen as the substantially reconstituted Court this June completes its first of several terms sitting together.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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