To be Argued:
FOR MAURICE R. GREENBERG
BY DAVID BOIES
BOIES, SCHILLER & FLEXNER LLP
(Time Requested: 30 Minutes)

FOR HOWARD I. SMITH
BY VINCENT A. SAMA
KAYE SCHOLER LLP
(Time Requested: 30 Minutes)

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Court of Appeals
of the
State of New York

THE PEOPLE OF THE STATE OF NEW YORK
by Eric T. Schneiderman, Attorney General of the State of New York,

Plaintiff-Respondent,

– against –

MAURICE R. GREENBERG and HOWARD I. SMITH,

Defendants-Appellants.

JOINT BRIEF FOR DEFENDANTS-APPELLANTS

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Defendants-Appellants Maurice R. Greenberg and Howard I. Smith ("Appellants") respectfully submit this Memorandum of Law in support of their appeal from the April 16, 2015 Decision and Order of the Appellate Division, First Department affirming the May 28, 2014 Decision and Order of the Supreme Court, New York County (Ramos, J.) (the "motion court") denying Appellants' July 26, 2013 motion for summary judgment.

PRELIMINARY STATEMENT

The Complaint filed in this action on May 26, 2005 alleged that improper accounting for numerous transactions had improperly inflated the net income for American International Group, Inc. ("AIG") by $907 million and shareholder equity for AIG by $2.029 billion. The only claims that remain today relate to two transactions, neither of which had *any* effect on AIG's shareholder equity or net income.

For the first eight years of this litigation, Plaintiff-Respondent Attorney General of the State of New York ("NYAG" or "Respondent") only pursued claims for damages, which it characterized as a "pursuit of compensation for the injured AIG shareholders." (R. 176.) However, after Appellants participated in settlements with and obtained general releases from AIG and AIG's shareholders, those damages claims were voluntarily

dismissed pursuant to this Court's decision in *People v. Applied Card Systems, Inc.*, 11 N.Y.3d 105 (2008) ("*Applied Card*").

At this point, rather than accept that the case was over, NYAG added new claims for disgorgement and injunctive relief even though:

- Neither disgorgement nor injunctive relief of the type sought by NYAG is available under the two statutes on which NYAG's claims are based – the Martin Act, N.Y. Gen. Bus. Law §§ 352-359, and Executive Law § 63(12).
- NYAG's attempt to seek disgorgement is a transparent effort to obtain damages that either are barred under *Applied Card* or would constitute an impermissible penalty.
- The bonuses that NYAG seeks to disgorge from Appellants were paid by AIG, not by the State or public investors, and AIG and its shareholders have released any and all claims that they might have had against Appellants.
- Appellants entered into consent judgments with the SEC, agreed to the entry of injunctive relief against them, and paid disgorgement to the SEC regarding issues that included the two transactions remaining at issue.

- NYAG had not presented any evidence showing any causal link between the alleged wrongful conduct and the alleged ill-gotten gains.
- The entry of injunctive relief against Appellants would constitute an impermissible penalty where the alleged violation occurred fifteen years ago and NYAG has not alleged that any violations have occurred since then; Appellants (who are ninety and seventy years old, respectively) have not been employed in any capacity by a public company for over ten years; and during the ten years in which this action has been pending, no preliminary injunctive relief was ever sought and no evidence was presented of any risk of imminent or irreparable harm.
- Appellant Smith has already served a now-expired, voluntary three-year ban on service as an officer or director of a public company pursuant to the SEC consent judgment referred to above, which covered the only two transactions remaining at issue in this case.
- NYAG's claims for disgorgement and injunctive relief are barred by the Supremacy Clause of the United States Constitution, particularly where Appellants have entered into consent judgments with the SEC agreeing to injunctive relief and paying disgorgement.

- NYAG did not take any discovery on those two claims for relief, even though all relevant discovery was completed, and the trial of this action has not been bifurcated into liability and remedies phases.

Appellants submitted evidence on their motions for summary judgment that established a *prima facie* case regarding each of these evidentiary points, and NYAG failed to present any evidence rebutting Appellants' *prima facie* showing. The courts below failed to address most of these issues, and erroneously analyzed the issues that were addressed.

This case previously was before this Court on appeal from the denial of Appellants' motions for summary judgment regarding NYAG's damages claims. Between the briefing and argument of that appeal, NYAG dropped its damages claims and asserted claims for disgorgement and injunctive relief that had not been considered by the courts below. Appellants argued that, with the dismissal of NYAG's damages claims, this Court should dismiss the case in its entirety. However, this Court remanded with directions that the courts below decide "in the first instance" "the availability of any other equitable relief," *People v. Greenberg* (*Greenberg II*), 21 N.Y.3d 439, 447-48 (2013), and determine whether Appellants' summary judgment motion should be granted.

On remand, the motion court erroneously held that the availability of disgorgement and the injunctive relief now claimed by NYAG had already been decided by this Court, and that this Court had instructed that the case *proceed to trial* on the question of injunctive relief. But there is a difference between a lower court deciding a question "in the first instance" – which can include addressing the issue through a motion to dismiss or a motion for summary judgment – and an instruction to conduct a trial on the merits. The motion court misread this Court's carefully circumscribed remand order, and – unless reversed – the result will be an unnecessary trial in a case that should have been resolved on summary judgment. The Appellate Division took no issue with that holding.

This Court should reverse the decisions below, grant summary judgment in Appellants' favor and dismiss the action because NYAG cannot succeed on its claims for relief. In the alternative, this Court should reverse the decisions below and remand the action to the motion court with a direction to follow the procedure set forth in this Court's June 25, 2013 Order by reviewing the evidence submitted on summary judgment and issuing a new decision considering that evidence.

STANDARD OF REVIEW

The Court of Appeals is generally "limited to the review of questions of law." N.Y. Const. art. VI, § 3(a); *Hunt v. Bankers & Shippers Ins. Co. of N.Y.*, 50 N.Y.2d 938, 940 (1980). *See also* CPLR 5501(b); Arthur Karger, *The Powers of the New York Court of Appeals* § 13.1 at 447-48 (rev. 3d ed. 2005). Review is *de novo* and the Court "need not defer to Supreme Court's judgment" on questions of law, *Andrea v. Arnone, Hedin, Casker, Kennedy & Drake, Architects & Landscape Architects, P.C.*, 5 N.Y.3d 514, 521 (2005), including whether an order denying a motion for summary judgment should have been granted. *See, e.g.*, *Martino v. Stolzman*, 18 N.Y.3d 905, 908-09 (2012) (reversing denial of summary judgment and dismissing complaint).

ISSUES PRESENTED

1. Is disgorgement an available remedy under the Martin Act and New York Executive Law § 63(12), where those statutes do not provide for disgorgement as a remedy?

2. Is disgorgement an available remedy under the Martin Act and New York Executive Law § 63(12), where Respondent's request for "disgorgement" constitutes an attempt to seek damages barred by *People v.*

Applied Card, 11 N.Y.3d 105 (2008), or an attempt to seek an impermissible penalty?

3. If disgorgement is an available remedy, did the courts below nevertheless err in refusing to grant Appellants' motion for summary judgment where it is undisputed that the entity that paid the amounts sought to be disgorged (AIG) already settled any and all claims it had against the Appellants and:

a. Appellants did not receive compensation from the State or public investors;

b. Appellants paid disgorgement in connection with their respective SEC consent judgments dated August 7, 2009;

c. On November 25, 2009, Appellants received general releases from AIG, the entity that paid Appellants the bonuses sought to be disgorged; and

d. On April 11, 2013, a federal court approved a settlement of a federal securities class action lawsuit against Appellants concerning the same transactions that are at issue in this litigation?

4. If disgorgement is an available remedy and the releases and judgments do not bar the remedy as a matter of law, did the courts below nevertheless err when refusing to grant summary judgment to Appellants

where Respondent did not present *any* evidence at the summary judgment stage of this action showing any causal link between the alleged wrongful conduct and the alleged illicit gains such that there is no material issue in dispute for trial?

5. Is it proper on a motion for summary judgment to shift the burden of proof away from Respondent, who is the plaintiff in this action, onto Appellants, who are the defendants in this action, and who will not have the burden at trial?

6. Is injunctive relief that would bar Appellants from serving as officers or directors of a public company, or from participating in the securities industry, available:

a. Under the Martin Act or Executive Law § 63(12), where neither statute provides for those remedies?

b. In a Martin Act or Executive Law § 63(12) action where such relief constitutes an impermissible penalty?

c. In a Martin Act or Executive Law § 63(12) action where:

i. The alleged violations occurred fifteen years ago;

ii. There has been no alleged violation in the last fifteen years;

iii. Appellants have not been employed in any capacity in a public company for over ten years;

iv. Mr. Greenberg is over ninety years old and Mr. Smith is over seventy years old;

v. The action has been ongoing for more than ten years;

vi. No preliminary injunction was ever moved for;

vii. Mr. Smith has already served a now-expired, voluntary three-year ban on service as an officer or director of a public company pursuant to an SEC consent judgment that covered the only two transactions remaining at issue in this case; and

viii. No evidence was presented of any risk of imminent or irreparable harm?

7. Is Respondent's attempt to seek disgorgement and injunctive relief under the Martin Act and New York Executive Law § 63(12) barred by the Supremacy Clause of the United States Constitution?

STATEMENT OF JURISDICTION

This Court has jurisdiction on this appeal pursuant to CPLR 5602(b)(1). This action is pending in the Commercial Division of the Supreme Court, New York County, before Justice Charles E. Ramos. On May 28, 2014, that court entered its decision and order denying Appellants' motion for summary judgment. (R. 18-23.) Appellants timely appealed to the Appellate Division, First Department. (R. 13-15.) On April 16, 2015,

the Appellate Division affirmed the denial of Appellants' motion for summary judgment. (R. 587-89.) Appellants moved the Appellate Division for leave to appeal to this Court on April 21, 2015.[1] The Appellate Division granted Appellants' motion for leave to appeal on June 18, 2015. (R. 586.)

STATEMENT OF THE CASE

I. PARTIES.

Mr. Greenberg served as AIG's President and Chief Executive Officer from 1968 to 1989, as its Chairman and Chief Executive Officer from 1989 until his retirement in 2005, and as a member of its Board of Directors from 1967 to 2005. Under the leadership of Mr. Greenberg, AIG grew to become the largest insurance company in the world.

Mr. Smith, formerly a Partner at the accounting and auditing firm of Coopers & Lybrand LLP, served as AIG's Vice President and Comptroller from 1984 to 1996, as AIG's Chief Financial Officer, Executive Vice President, and Comptroller from 1996 to 2005, and as a Director of AIG from 1997 to 2005.

[1] *See* Notice of Defendants-Appellants' Motion for Leave to Appeal to the Court of Appeals, or in the Alternative, for Reargument, *People v. Greenberg*, Index No. 401720/05 (1st Dep't Apr. 21, 2015).

II. PROCEDURAL HISTORY OF THE ACTION.

A. The Original Complaint.

On May 26, 2005, shortly after Mr. Greenberg publicly criticized the then-New York Attorney General for bringing prosecutions that turned "foot faults into murder charges" (R. 493), NYAG and the Superintendent of Insurance of the State of New York filed their original complaint against AIG, Mr. Greenberg and Mr. Smith alleging violations of Executive Law § 63(12), the Martin Act, and common law fraud, in connection with nine transactions entered into, or accounting entries made, by AIG while Appellants Greenberg and Smith were CEO and CFO. *See* Complaint at 35-36, *People v. Greenberg*, Index No. 401720/05 (Sup. Ct. N.Y. County May 26, 2005) ("Original Complaint"). The "Wherefore" clause of the Original Complaint included a boilerplate demand for equitable relief in the forms of disgorgement and injunctive relief. *Id.* at 36-37.

B. The Evolution Of NYAG's Claims.

On September 5, 2006, NYAG filed an Amended Complaint against Appellants that (a) dropped the allegations in the Original Complaint with respect to five of the nine transactions or accounting entries, and (b) dropped all common law fraud claims against Appellants. (*See generally* R. 119-41.)

On July 15, 2009 and January 21, 2011, NYAG dropped its allegations relating to two of the remaining four transactions or accounting entries, leaving only two transactions at issue: (i) a finite risk reinsurance transaction entered into by a subsidiary of AIG in the last quarter of 2000 and the first quarter of 2001 (the "Gen Re Transaction"), and (ii) a reinsurance transaction entered into by a subsidiary of AIG in the third quarter of 2000 (the "CAPCO Transaction").

During the first eight years of this action, the only relief NYAG pursued was for money damages, which are expressly authorized under the Executive Law. (R. 176.) NYAG never sought *any* preliminary injunctive relief against Appellants or *any* discovery concerning injunctive relief or disgorgement. Although NYAG did not delete those remedies from the "Wherefore" clause of the Amended Complaint it filed in 2006, after dropping its common law fraud claim (R. 140-41), NYAG did not pursue any such claim until the Spring of 2013. Moreover, the boilerplate "Wherefore" clause of the Amended Complaint does not include the injunctive relief currently sought.[2] *Id.*

[2] The Amended Complaint contained a boilerplate request for an injunction "[e]njoining and restraining defendants" "from engaging in any conduct, conspiracy, contract, or agreement, and from adopting any practice, plan, program, scheme, artifice or device similar to, or having a purpose and effect similar to, the conduct complained above." (R. 140.) Notably, the Amended Complaint did not seek (a) an officer or director bar; or (b) a ban from participation in the securities industry – the permanent

On the contrary, at an April 26, 2007 hearing, NYAG (a) did not dispute Justice Ramos' statement: "It's not alleged that he [Mr. Greenberg] made any particular money himself from these transactions" (R. 289); and (b) in response to the motion court's statement that "we are not looking at disgorgement here," acknowledged that it was pursuing a "damages" case based on "a fraud on the market" theory. (R. 290.)

In September 2009, after over four years of extensive discovery and motion practice, the parties cross-moved for summary judgment concerning the two remaining transactions. On October 21, 2010, the motion court denied Appellants' summary judgment motions, granted NYAG's summary judgment motion regarding liability on the CAPCO Transaction, and denied NYAG's summary judgment motion regarding the Gen Re Transaction. *See People v. Greenberg*, Index No. 401720/05, 2010 WL 4732745, at *83 (Sup. Ct. N.Y. County Oct. 21, 2010).

Shortly thereafter, on January 20, 2011, NYAG filed a Note of Issue that included claims for damages and injunctive relief but that did not include a claim for disgorgement. (R. 167-70.) NYAG represented in the Note of Issue that all discovery "now known to be necessary" was complete. (R. 168.)

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injunctive relief NYAG announced it would pursue after abandoning its damages claim in April 2013. (R. 197-98.)

On May 8, 2012, the Appellate Division, First Department, reversed the motion court's grant of summary judgment in favor of NYAG regarding liability on the CAPCO Transaction and affirmed in all other respects. *People v. Greenberg* (*Greenberg I*), 95 A.D.3d 474, 484-85 (1st Dep't 2012). The Appellate Division then granted Appellants leave to appeal that ruling to this Court. (R. 5.)

C. Prior Proceedings Before This Court.

On that appeal to this Court, the parties briefed, *inter alia*, the issue of whether NYAG could seek damages on behalf of AIG's shareholders in light of Appellants' August 10, 2009 settlement of a federal class action brought by AIG's shareholders and this Court's decision in *Applied Card*.

On April 25, 2013, while the appeal was pending before this Court, and two weeks after the final approval of the settlement of that federal class action (R. 153),[3] NYAG withdrew its damages claim. (R. 197-98.) Rather than voluntarily terminate its action at that point, NYAG announced for the first time that it intended "to pursue vigorously" a permanent injunction

[3] The federal court's final approval of Appellants' settlement with AIG's shareholders was not obtained until April 11, 2013 (R. 153-66), in part because the settlement was contingent on final approval of AIG's settlement with the same class and in part because of NYAG's unsuccessful attempts to oppose that settlement. (R. 171-96.) *See In re Am. Int'l Grp., Inc. Sec. Litig.*, No. 1:04-cv-08141-DAB (S.D.N.Y.), ECF Nos. 650-53, 657-61, 665, 670 ("*In re AIG*").

barring Appellants from becoming officers or directors of a publicly traded company and from participating in the securities industry. (R. 197.)

Notably, NYAG's April 25, 2013 letter to this Court (the "April 25 Letter") did not mention disgorgement. (R. 197-98.) However, at oral argument before this Court one month later, NYAG informed the Court and Appellants for the first time that it was "looking into" pursuing disgorgement (R. 221-22), even though the Solicitor General conceded NYAG had not taken discovery on disgorgement, and therefore could not offer evidence of any potentially disgorgeable gains made by Appellants as a result of the Gen Re or CAPCO Transactions. (R. 223-24.)

This Court questioned NYAG's sudden change of course and uncertainty about the availability of remedies NYAG was considering seeking eight years into this action. (R. 219-27.) However, as NYAG stated in its April 25 Letter, the availability of "non-damages remedies" was "not properly before the Court," and because the injunctive relief "claim has never been squarely raised in or addressed by any court in this matter," it "should be addressed, in the first instance, by the trial court rather than by this Court." (R. 198.)

Agreeing with NYAG, this Court then directed the lower courts to determine, "in the first instance," whether NYAG's newly suggested

remedies (permanent injunctive relief banning Appellants from serving as officers or directors of a public company or participating in the securities industry and, possibly, disgorgment about which NYAG was non-committal) could be granted on the facts of this case:

> "On the merits, we cannot say as a matter of law that no equitable relief may be awarded. There is no doubt room for argument about whether the lifetime bans that the Attorney General proposes would be a justifiable exercise of a court's discretion; but *that question* [i.e., the question of the availability of permanent injunctive relief of the type sought here], as well as the availability of any other equitable relief that the Attorney General may seek, must be decided by the lower courts in the first instance."

Greenberg II, 21 N.Y.3d at 447-48 (emphasis added).

III. ALL INTERESTED PARTIES SETTLED THEIR CLAIMS AGAINST APPELLANTS.

During the discovery and original summary judgment process in this litigation, all parties with any legitimate interest in the transactions at issue here settled their claims and released Appellants.

A. The SEC Settled With Appellants.

On August 7, 2009, Appellants received releases related to the Gen Re and CAPCO Transactions when they separately settled with the SEC. (R. 86-97, 102-16.) Mr. Greenberg (as a control person) and Mr. Smith also consented to the entry of federal injunctions barring them from "any act, practice, or course of business which operates or would operate as a fraud or

deceit upon any person" in connection with the purchase or sale of securities. (R. 86-87, 102-03.) With one exception, those injunctions remain in force.[4] (R. 86-89, 102-08.) Appellants have complied fully with those consent judgments. (R. 36-37, 99.) There has been no allegation by the SEC that either Mr. Greenberg or Mr. Smith has violated the consent judgments or otherwise engaged in wrongful or unlawful conduct since they consented to the injunctions. (R. 37, 99.)

B. AIG's Shareholders Released Appellants From All Claims Arising Out Of Or Relating To The Gen Re And CAPCO Transactions.

On August 10, 2009, AIG's common shareholders agreed to release all their claims against Appellants. That settlement received federal court approval on April 11, 2013 and an Order and Final Judgment was later entered in a securities class action brought by those stockholders. (R. 153-66). NYAG had urged the federal court not to approve the settlement on the grounds that such approval would end NYAG's case against Appellants here. (R. 171-96.) The settlement was approved over NYAG's objections and a final order of approval was duly entered. (R. 153-66.)

[4] Mr. Smith voluntarily consented to a bar on serving as an officer or director of a public company for a three-year period commencing on August 7, 2009 and ending on August 7, 2012 – over three years ago. (R. 99-100, 107-08.) The SEC did not seek an officer or director bar against Mr. Greenberg. (R. 36.)

C. AIG And Appellants Entered Into Mutual General Releases Resolving All Litigation Between Them.

On November 25, 2009, AIG and Appellants entered into a settlement in which, among other things, AIG expressly released any and all claims it had against Appellants, including all of its claims in an action then pending in the Delaware Chancery Court, captioned *American International Group, Inc. Consolidated Derivative Litigation*, No. 769-VCS (Del. Ch.), filed Oct. 29, 2003 ("Delaware Derivative Action"). (R. 142-152.) The Delaware Derivative Action had been commenced by certain AIG stockholders as a derivative action, which alleged, among other things, that Appellants had damaged AIG in connection with the Gen Re and CAPCO Transactions.[5] AIG later assumed direct control over a part of the Delaware Derivative Action against Appellants, including claims relating to the Gen Re and CAPCO Transactions.

As part of the global settlement between AIG and Appellants, AIG released Appellants from any and all claims it had against Appellants. That release expressly encompassed any claims AIG had or could have had

[5] *See* the First Amended Combined Complaint filed in the Delaware Derivative Action on April 14, 2008 (D.E. 23350684) at ¶¶ 1-6, 18-24, 41-47 (allegations relating to the Gen Re and CAPCO Transactions). That complaint also alleged injury to AIG resulting from other transactions. This Court may take judicial notice of publicly filed court documents in other cases, such as the First Amended Combined Complaint. *See Khatibi v. Weill*, 8 A.D.3d 485, 485 (2d Dep't 2004).

against Appellants arising out of or related to the Gen Re or CAPCO Transactions. (R. 142-52.) This necessarily included any claims for disgorgement. AIG later dismissed those claims with prejudice.[6]

D. AIG's Shareholders Released All Derivative Claims Against Appellants, Including Those Relating To The Gen Re And CAPCO Transactions That Had Not Been Assumed By AIG.

AIG also provided a similar release to Appellants on January 25, 2011, as part of the court-approved settlement of that part of the Delaware Derivative Action that had not been assumed directly by AIG. *See* Order and Final Judgment, *Am. Int'l Grp., Inc. Consol. Derivative Litig.*, No. 769-VCS, 2011 WL 244179 (Del. Ch. Jan. 25. 2011).

IV. APPELLANTS' 2013 SUMMARY JUDGMENT MOTION.

On July 26, 2013, after all the settlements and releases were finalized, and after this Court's remittur, Appellants moved for summary judgment regarding NYAG's newly asserted claims for relief – the only claims for relief remaining in this case. (R. 24-25.)

In support of their summary judgment motion, Appellants made a *prima facie* showing that NYAG could not seek disgorgement because:

[6] *See* Delaware Derivative Action, Stipulation and Notice of Voluntary Dismissal With Prejudice, Doc. No. 2046, Trans. ID 37047854 (Feb. 5, 2010).

- On May 28, 2013, NYAG acknowledged to this Court that despite the close of discovery, it lacked the evidence necessary to establish a case for disgorgement.[7] (R. 222-23.)

- At the same time, NYAG admitted that it had never taken discovery on disgorgement,[8] even though discovery had been completed.[9]

- NYAG did not dispute the motion court's observation at a conference on April 26, 2007 that disgorgement was not among the remedies sought. (*See* R. 290 ("The Court: We are not looking at disgorgement here of any insider trading or anything like that").)

- NYAG did not include disgorgement as a remedy sought in its January 20, 2011 Note of Issue, and represented that all discovery "now known to be necessary" was complete, despite having taken no discovery regarding disgorgement. (R. 167-69.)

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[7] "We're saying we are looking – *I can't promise we will be able to establish it. We are entitled to attempt to determine – to find performance based compensation*, that's what disgorgement would be, performance based compensation that was effected by these frauds . . . not the damages they inflicted . . . ." (R. 222) (emphasis added); *see also id.* at 223 ("Judge Pigott: And how much is that? Ms. Underwood: We don't --- *I can't put a finger on it now*, but we are entitled to pursue that.") (emphasis added).

[8] "Judge Pigott: . . . Has there been discovery as to how much you would be seeking in terms of disgorgement? Ms. Underwood: No. I think that it's – I don't believe so...." (R. 223-24.)

[9] Pre-trial discovery is complete with the exception of the reopening of the deposition of one fact witness and the deposition of one previously undeposed fact witness. Neither of those witnesses is relevant to NYAG's claims for disgorgement or injunctive relief. Because the motion court has not bifurcated the trial into liabilities and remedies phases (*see* R. 566-67), NYAG cannot defer proving disgorgeable gains until a subsequent (non-existent) remedies phase of the trial.

- Appellants did not receive any compensation from public investors or from the State of New York during the many years they served as officers of AIG. (R. 38, 101.)

NYAG did not submit any evidence to rebut Appellants' *prima facie* case that NYAG could not seek disgorgement.

Appellants also demonstrated as a legal matter that: (a) disgorgement is not an available remedy under the Martin Act and Executive Law § 63(12); (b) NYAG's attempt to seek disgorgement against Appellants was prohibited by this Court's decision in *Applied Card*, or was an impermissible penalty; (c) disgorgement was prohibited by the general releases provided by AIG and its shareholders in settlements of other litigations and by the prior disgorgements of funds by Appellants as part of consent judgments they entered into with the SEC (R. 86-97, 102-16, 142-52, 153-66); (d) NYAG lacked standing to pursue disgorgement in this case; and (e) NYAG's attempt to seek disgorgement against Appellants was prohibited by the Supremacy Clause of the U.S. Constitution.

Regarding NYAG's claim for a permanent injunction, Appellants submitted affidavits in support of their motion for summary judgment demonstrating that:

- Appellants have not served as officers or directors of a public company since 2005 and have no intention of doing so in the future. (R. 36, 99.) Mr. Greenberg is the Chairman, CEO and a member of the Board of Directors of C.V. Starr & Co., Inc. ("C.V. Starr") and Starr International Company, Inc. ("Starr International"), which are privately-held corporations, and Mr. Smith is a Director and the Vice Chairman of Finance of each of these private corporations. (R. 35-36, 98-99.)

- Appellants do not personally engage in the sale or offering of securities or rendering advice to the public within or from the State of New York or elsewhere, nor have they ever done so. (R. 37, 100.)

- Neither Appellant has a license to act as an investment adviser or as a broker-dealer in the purchase, offering or sale of securities to the public within or from the State of New York or otherwise.[10] *Id.*

Appellants also submitted evidence that:

- Appellants are beyond the age at which they could reasonably be expected to engage in the activities that NYAG seeks to enjoin, since

[10] C.V. Starr owns Starr Investment Holdings, Inc. ("SIH"), a limited liability company which is registered with the SEC as an investment adviser under the Investment Company Act of 1940. (R. 37, 100.) Starr International is the indirect 100% owner of Starr Strategic Partners, LLC ("SSP"), which is broker-dealer registered with the SEC. Neither Mr. Greenberg nor Mr. Smith is personally involved in the solicitation of investments or investment advice rendered to third parties by SIH or SSP. *Id.*

Mr. Greenberg is ninety years old and Mr. Smith is seventy years old. (R. 36, 99.)

- There have been no allegations or evidence that either Appellant has engaged in any misconduct in the decade since this action was filed, and the activities discussed in NYAG's Amended Complaint occurred nearly fifteen years ago.[11] (R. 35-37, 99-100.)

- Mr. Greenberg (as a control person) and Mr. Smith entered into federal court-approved consent judgments enjoining them from participating in "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person" (R. 87, 103) and there is no allegation that Appellants have failed to comply with those injunctions. (R. 36, 99).

- Mr. Smith has already served a three-year bar of service as an officer or director of a public company under the August 7, 2009 consent judgment with the SEC. (R. 99, 107-108.)

This evidence constituted a *prima facie* showing that no likelihood of irreparable harm or recurrent illegality exists to justify a permanent

[11] The insurance companies owned and operated by Starr International are regulated by various state and international insurance departments. None of the many insurance departments and other regulators who regulate these insurance companies has accused either Appellant of any misconduct or unlawful activity concerning the activities they have engaged in since leaving AIG more than a decade ago. (R. 37, 100.)

injunction against Appellants. In response, NYAG did not submit any admissible evidence, and instead submitted only an affirmation by NYAG's trial counsel containing speculation about Appellants' possible future conduct. (R. 332-35.)

Appellants also argued that: (a) director and officer bars and prohibitions on participation in the securities industry are not remedies authorized by the Martin Act and Executive Law § 63(12); (b) NYAG had no sovereign interest in pursuing a permanent injunction and therefore lacks standing to try this case; and (c) NYAG's attempt to seek the type of permanent injunctive relief it now seeks against Appellants is prohibited by the Supremacy and Due Process Clauses of the U.S. Constitution. (R. 8-9, 21-22, 550-51, 568-69.)

A. The Motion Court's May 28, 2014 Order.

On May 28, 2014, the motion court denied Appellants' summary judgment motion. (R. 16-23.) The motion court misinterpreted the prior mandate of this Court, which directed the lower courts to consider "in the first instance" the legal availability of NYAG's newly advanced demands for equitable relief, and instead concluded that "[t]he guidance from the Court of Appeals could not be more clear that [NYAG] may *proceed to trial seeking equitable relief*." (R. 21 (emphasis added).) This holding

misconstrued the language from this Court's ruling that "on the present record" available to this Court at that time, NYAG was not barred "as a matter of law from obtaining any equitable relief." (R. 21.) This Court's June 25, 2013 ruling did not conclude that the relief *was available*, but rather – consistent with NYAG's suggestion to this Court on April 25, 2013 (*see supra* Statement of the Case II.C) – that the courts below would have to determine "in the first instance" whether those claims *could* be tried.

The motion court also erred in summarily rejecting Appellants' argument that disgorgement is not a remedy authorized by the Martin Act and Executive Law § 63(12). In holding that NYAG "may also seek disgorgement under the Martin Act as an equitable remedy" (R. 22), the motion court relied solely upon the Appellate Division's then-recent decision in *People v. Ernst & Young LLP*, 114 A.D.3d 569 (1st Dep't 2014) ("*Ernst & Young*") – a decision of state-wide importance that has not been reviewed by this Court – and did not address any of Appellants' arguments regarding disgorgement or NYAG's failure to rebut Appellants' *prima facie* showing on that issue.

The motion court also erroneously and summarily found that NYAG was entitled to proceed to trial with its claim for permanent injunctive relief. Although the motion court acknowledged that Appellants had argued that

NYAG lacked standing to pursue injunctive relief under the facts of this case (R. 20), the motion court did not rule on that argument (*see* R. 19-23). The motion court found that the injunctive relief sought by NYAG was proper under the Martin Act because that Act permits injunctions barring a defendant from "selling or offering for sale to the public . . . as principal, broker or agent, or otherwise, any securities issued or to be issued" (R. 21-22) (internal quotation marks omitted), even though Appellants demonstrated that they have never engaged in those activities and have no intention of doing so. The motion court further relied on this Court's opinion in *People v. McCann*, 3 N.Y.2d 797 (1957), to hold that the Martin Act permits NYAG to seek officer and director bars (R. 422), even though *McCann* did not address that question.

B. The Appellate Division's April 16, 2015 Order.

Appellants timely appealed to the Appellate Division, which on April 16, 2015, affirmed the decision of the motion court in its three-page Decision. (R. 587-89.)

The Appellate Division erred in summarily affirming the motion court's erroneous decision:

- The Appellate Division erred in concluding that disgorgement claims may be brought under the Martin Act and Executive Law

§ 63(12), relying solely on its own recent decision in *Ernst & Young*. (R. 587.)

- The Appellate Division erred in ruling that "The State's disgorgement claim was legally viable, despite the settlement of actions brought by American International Group, Inc. shareholders and the corporation, and the accompanying releases." *Id.*

- The Appellate Division erred in ruling that Appellants "failed to carry their *prima facie* burden of demonstrating the lack of incentive compensation paid to defendants as a result of the sham transactions . . . ." (R. 587-88.) The Appellate Division did not acknowledge or even discuss the evidence presented by Appellants that carried their burden, nor did it acknowledge NYAG's failure to present *any* evidence of a causal link between the bonuses paid to Appellants and the transactions at issue, particularly in light of NYAG's previous acknowledgement that it had no evidence of and was not pursuing disgorgement. (R. 587-89.)

- The Appellate Division erred in holding that NYAG is entitled to seek permanent injunctions barring Appellants from serving as public company officers and directors or participating in the securities industry, without analyzing whether such relief is available under the Martin Act

or Executive Law § 63(12), and if so, how that is constitutionally permissible relief. (R. 588-89.)

- The Appellate Division erred in holding that Appellants failed to "demonstrate conclusively" that an injunction was not warranted "under the circumstances, which at least raised issues of fact as to the imminence of harm" without discussing the evidence presented by Appellants and NYAG's failure to present any contradictory evidence. (R. 588.)

Appellants timely moved the Appellate Division for leave to appeal on April 21, 2015, which motion was granted on June 18, 2015. (R. 586.)

ARGUMENT

I. SUMMARY JUDGMENT STANDARD.

Summary judgment "shall be granted if . . . [the] defense shall be established sufficiently to warrant the court as a matter of law in directing judgment in favor of any party." CPLR 3212(b). If the movant makes a *prima facie* showing of entitlement to judgment as a matter of law, "the burden shifts to the party opposing the motion for summary judgment to produce evidentiary proof in admissible form sufficient to establish the existence of material issues of fact which require a trial of the action." *Alvarez v. Prospect Hosp.*, 68 N.Y.2d 320, 324 (1986) (citations omitted).

Failure to tender admissible, competent evidence in opposition to a defendant's *prima facie* showing requires dismissal of plaintiff's complaint. *See Colarossi v. Univ. of Rochester*, 2 N.Y.3d 773, 774 (2004) (holding that summary judgment dismissing complaint was properly granted where "[i]n opposition to defendant's *prima facie* showing of entitlement to summary judgment, plaintiff presented no evidence other than '[m]ere conclusions, expressions of hope or unsubstantiated allegations.'" (second alteration in original)).

II. DISGORGEMENT IS NOT AUTHORIZED BY THE MARTIN ACT OR EXECUTIVE LAW § 63(12).

The plain language and the statutory history of the Martin Act and Executive Law § 63(12) demonstrate that the New York Legislature never authorized NYAG to seek disgorgement under either statute.

When analyzing the statutory language and history in this case, it is important to recognize the differences between "disgorgement," "restitution," and "damages." Each of these three distinct remedies serves a different purpose. The Legislature's decision not to include disgorgement is therefore a deliberate choice about the nature of the remedial schemes of those statutes.

Restitution is intended to make injured parties whole. It is tied to the harm that victims have suffered. Thus, when NYAG seeks restitution under

the Martin Act, NYAG "seek[s] monetary restitution on behalf of investors who were the victims of fraudulent activity." *Assured Guar. (UK) Ltd. v. J.P. Morgan Inv. Mgmt. Inc.* (*Assured Guaranty II*), 18 N.Y.3d 341, 350 (2011). Like restitution, damages under Executive Law § 63(12) serve a compensatory purpose – they are intended to make whole those harmed by an alleged fraud. *See State v. Solil Mgmt. Corp.*, 128 Misc. 2d 767, 773 (Sup. Ct. N.Y. County 1985) (holding that under Executive Law § 63(12), NYAG "is limited to obtaining *restitution* or *compensatory* damages on behalf of the injured" victims (emphasis added)).

In contrast, disgorgement is "an equitable remedy distinct from restitution." *Applied Card*, 11 N.Y.3d at 125. Disgorgement is focused on the *gains received by alleged wrongdoers*. It is "aimed at 'forcing a defendant to give up the amount by which he was unjustly enriched.'" *J.P. Morgan Secs., Inc. v. Vigilant Ins. Co.*, 91 A.D.3d 226, 230 (1st Dep't 2011), *rev'd on other grounds*, 21 N.Y.2d 324 (2013). In other words, a "claim for restitution seeks to restore what was wrongfully taken while a disgorgement remedy requires the wrongdoer to turn over any gains it generated as a result of its wrongdoing." 28 N.Y. Practice, *Contract Law* § 4:21 (2015).

A. Nothing In The Language Of The Martin Act Or Executive Law § 63(12) Authorizes NYAG To Seek Disgorgement.

The Martin Act specifies that NYAG may seek four remedies: (a) an injunction against "continuing such fraudulent practices," N.Y. Gen. Bus. Law § 353(1); (b) a permanent injunction against "selling or offering for sale to the public within this state, as principal, broker or agent, or otherwise, any securities issued or to be issued," *id.*; (c) "restitution of any moneys or property obtained directly or indirectly by any such fraudulent practice," *id.* § 353(3); and (d) "a sum not in excess of two thousand dollars as an additional allowance," *id.* § 353(1). None of these statutory provisions authorizes disgorgement.

Similarly, Executive Law § 63(12) specifies that NYAG may seek the following remedies: (a) "an order enjoining the continuance of [fraudulent or illegal] business activity or of any fraudulent or illegal acts"; (b) an order directing "restitution and damages"; and (c) an order revoking the ability to do business in New York as a partnership or under an alias. N.Y. Exec. Law § 63(12). None of these statutory provisions authorizes disgorgement either.

New York law recognizes the "*expressio unius*" doctrine by providing that where "a law expressly describes a particular act, thing or person to which it shall apply, *an irrefutable inference must be drawn* that what is omitted or not included was intended to be omitted or excluded." N.Y. Stat.

§ 240 (emphasis added). *See also* Antonin Scalia & Bryan A. Garner, *Reading Law* § 10, at 107 (2012) ("[T]he principle that specification of the one implies exclusion of the other validly describes how people express themselves and understand verbal expression.").

"[I]t is an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it." *Meghrig v. KFC W., Inc.*, 516 U.S. 479, 488 (1996) (alteration in original) (internal quotation marks omitted). This Court has recognized that canon's binding effect in interpreting statutory language. *See Thoreson v. Penthouse Int'l, Ltd., Inc.*, 80 N.Y.2d 490, 499 (1992) ("The logical inference, of course, from the Legislature's action in expressly permitting punitive damages in housing cases is that such damages were not then recoverable for discrimination in other areas including employment.") (citing N.Y. Stat. Law § 240). *See also Nat'l R.R. Passenger Corp. v. Nat'l Ass'n of R.R. Passengers*, 414 U.S. 453, 458 (1974) (invoking *expressio unius* canon to conclude that "when legislation expressly provides a particular remedy or remedies, courts should not expand the coverage of the statute to subsume other remedies."). New York courts have applied this doctrine to both the Martin Act and Executive Law. *See People v. Michael Glenn Realty Corp.*, 106 Misc. 2d 46, 47 (Sup. Ct. N.Y. County 1980)

(Martin Act's specific reference to "public offerings" suggests private offerings are not regulated); *see also Matter of Mayfield v. Evans*, 93 A.D.3d 98, 106 (1st Dep't 2012) (the enumerated list of dispositions in the Executive Law warrants an irrefutable inference that omitted items were intentionally excluded). Even if disgorgement is an equitable remedy available in common law actions, it is not authorized by the plain language of the statutes at issue here, the Martin Act and Executive Law, which control the relief that NYAG may seek. *See Fumarelli v. Marsam Dev., Inc.*, 92 N.Y.2d 298, 305 (1998) (common-law remedies and substantive common-law requirements are displaced by statutory scheme); *see also, e.g.*, *Sheehy v. Big Flats Cmty. Day, Inc.*, 73 N.Y.2d 629, 636 (1989) (finding no private right of action where legislature has "made express provision for civil remedy"); *Steinberg v. Steinberg*, 46 A.D.2d 684, 684 (2d Dep't 1974) (holding that in "an area comprehensively covered by the legislature, the courts may not fashion remedies not provided by statute").

Thus, because disgorgement is not included in the remedies identified in the Martin Act and Executive Law, there is "an irrefutable inference" that the New York Legislature deliberately excluded disgorgement from the remedies that can be sought under those statutes. *See* N.Y. Stat. § 240. This result does not change when NYAG is the plaintiff. *See People v. Grasso*,

11 N.Y.3d 64, 70 (2008) ("That the plaintiff here is the Attorney General as opposed to a private party does not preclude application of these decisions;" NYAG must enforce statutes "while maintaining the integrity of calculated legislative policy judgments").

NYAG cannot seek and the courts cannot order disgorgement in the absence of legislative authorization to do so because "[t]he statute 'must be read and given effect as it is written by the Legislature.'" *Parochial Bus Sys., Inc. v. Bd. of Educ. of the City of N.Y.*, 60 N.Y.2d 539, 548-49 (1983) (citations omitted). As this Court observed in *Morales v. Cnty. of Nassau*: "Where the Legislature has spoken, indicating its policy preferences, it is not for courts to superimpose their own." 94 N.Y.2d 218, 224 (1999); *see also* N.Y. Stat. § 92 ("The primary consideration of the courts in the construction of statutes is to ascertain and give effect to the intention of the Legislature.").

B. The Statutory History Of The Martin Act And Executive Law § 63(12) Confirms That The Legislature Did Not Authorize Disgorgement.

The statutory history of these statutes further confirms that the New York Legislature did not intend to authorize disgorgement as a remedy.[12] If

[12] The New York Legislature understands how to include the remedy of disgorgement where desired. *See, e.g.*, N.Y. Arts & Cult. Aff. Law § 34.07(2); N.Y. Lab. Law § 220(3)(d)(iii).

all equitable remedies, including disgorgement, were available under the Martin Act and the Executive Law, then the statutory language would be rendered superfluous, and previous legislative amendments to those statutes would have been unnecessary and meaningless.

1. The Martin Act.

The only remedy that could be sought under the Martin Act when it was originally enacted in 1921 was an injunction against continuing acts. *Assured Guaranty II*, 18 N.Y.3d at 350; *see also Assured Guar. (UK) Ltd. v. J.P. Morgan Inv. Mgmt. Inc.* (*Assured Guaranty I*), 80 A.D.3d 293, 298-99 (1st Dep't 2010).

The New York Legislature has amended the Martin Act to add other specific remedies. *First*, in 1923, the Legislature authorized NYAG to seek to enjoin completed frauds in addition to frauds that were contemplated or ongoing. N.Y. Gen. Bus. Law §353. *Assured Guaranty I*, 80 A.D.3d at 299. *Second*, in 1976, the Legislature authorized NYAG to seek restitution "on behalf of investors who were the victims of fraudulent activities." *Assured Guaranty II*, 18 N.Y.3d at 341, 350.[13]

[13] The Martin Act also was amended in 1925 to permit NYAG to seek receiverships, *Assured Guaranty I*, 80 A.D.3d at 299, and in 1955 to authorize NYAG to bring criminal proceedings, *Assured Guaranty II*, 18 N.Y.3d at 350.

Those amendments did not authorize NYAG to seek disgorgement under the Martin Act.[14] The absence of disgorgement from the enumerated remedies available under the Martin Act reflects the Legislature's specific choice not to include disgorgement as a remedy available under that statute. *See Theurer v. Trs. of Columbia Univ. in the City of N.Y.*, 59 A.D.2d 196, 198 (3d Dep't 1977) (stating that courts may assume that the Legislature "knew how to draft a bill to effectuate their objectives").

Moreover, the Legislature's choice to include restitution but not disgorgement is consistent with the overall purpose of the Martin Act. The statute is not primarily a punitive statute. "Martin Act injunctions are granted, not as punishment to the individual but as protection to the public . . . ." *People v. Lexington Sixty-First Assocs.*, 38 N.Y.2d 588, 597 (1976) (internal quotation marks omitted). This Court has recognized that, although the statute has a remedial purpose and should be construed broadly, it achieves that purpose through specific authorizations to the Attorney General. *People v. Federated Radio Corp.*, 244 N.Y. 33, 37-38 (1926)

[14] Nor is disgorgement authorized by the language of § 353-a of the Martin Act, which provides that "the court may grant such other further relief as may be proper." N.Y. Gen. Bus. Law § 353-a . That language appears only in the section of the Martin Act pertaining to the appointment of a receiver to manage funds seized by NYAG, and does not appear in the portion of the Martin Act that grants NYAG power to pursue specific remedies. *See id.* § 353. It thus is limited to the scope of the court's powers with regard to the appropriate functioning of the receiver.

(enumerating powers granted to NYAG to implement remedial nature of Martin Act). But the broad remedial purpose of the Martin Act provides "no sanction to ignore the plain language of" the statute. *First Energy Leasing Corp. v. Attorney-Gen. of the State of N.Y.*, 68 N.Y.2d 59, 63-64 (1986). *See also People v. Litto*, 8 N.Y.3d 692, 705 (2007) ("[T]he implementation of an action should not be judicially sanctioned if it is incompatible with the enforcement mechanism chosen by the Legislature or with some other aspect of the over-all statutory scheme." (internal quotation marks omitted)).

2. Executive Law § 63(12).

As with the Martin Act, the New York Legislature initially authorized only a single remedy under Executive Law § 63(12) – injunctive relief. In 1970, the Legislature added restitution – but not disgorgement – as an additional remedy available under the statute. N.Y. Exec. Law § 63(12) (amended 1970). In 1977, the New York Legislature further amended Executive Law § 63(12) to permit the recovery of "damages," but again did not add disgorgement as a remedy. N.Y. Exec. Law § 63(12) (amended 1977). Courts must acknowledge that the Legislature did *not* add disgorgement as a remedy in either the 1970 or 1977 amendments to Executive Law § 63(12). That the statute was amended twice – once to allow for restitution and once to allow for damages in certain circumstances

– shows that the Legislature had two opportunities to add disgorgement as a remedy, but did not do so. The absence of the remedy of disgorgement from both amendments underscores that it is not an intended remedy under Executive Law § 63(12).

C. The Court Should Reject The Appellate Division's Analysis Of The Availability Of Disgorgement As A Remedy Under Executive Law § 63(12) In *Ernst & Young*.

Both the motion court and Appellate Division relied on *Ernst & Young* to hold that disgorgement is a permissible remedy under the Martin Act and Executive Law. (R. 22, 587.) This Court should reject those determinations and clarify that *Ernst & Young* was erroneously decided.

Prior to the Appellate Division's 2014 decision in *Ernst & Young*, New York courts had held that disgorgement was not a remedy under the Martin Act and Executive Law § 63(12). For example, in *People v. Direct Revenue LLC*, 19 Misc. 3d 1124(A), 2008 Slip Op. 50845(U) at *8 (Sup. Ct. N.Y. County Mar. 12, 2008), the court rejected NYAG's effort to seek disgorgement under Executive Law § 63(12) and General Business Law §§ 349-350, holding that "while the Executive Law and the GBL permit monetary relief in the form of restitution and damages to consumers, *the statutes do not authorize the general disgorgement of profits received from sources other than the public*." *Id.* (emphasis added). The *Direct Revenue*

court also determined that disgorgement of profits to the State where the State had no direct monetary interest would constitute "punitive damages not authorized by statute." *Id.*

The motion court in *Ernst & Young* properly determined that disgorgement was not available under the Martin Act and Executive Law. The court explained that disgorgement of funds not paid to the defendant by consumers was "a penalty. It becomes punitive." *Ernst & Young* Tr. at 31.[15]

The Appellate Division's reversal relied on four erroneous propositions. *First*, it incorrectly assumed that this Court's statement in *Applied Card*, that disgorgement "might" be an available remedy to NYAG in that case, 11 N.Y.3d at 125-26, meant that disgorgement is a universally available remedy under the Martin Act and Executive Law § 63(12). *See Ernst & Young*, 114 A.D.3d at 569-70 (citing *Applied Card*, 11 N.Y.3d at 125-26). *Second*, it erroneously concluded that disgorgement is an available remedy under Executive Law § 63(12) because "maintaining disgorgement as a remedy within the court's equitable powers is crucial, particularly where

[15] "*Ernst & Young* Tr." refers to the December 12, 2012 Hearing Tr. in *People v. Ernst & Young LLP*, Index No. 451586/2010 (Sup. Ct. N.Y. County), available at: https://iapps.courts.state.ny.us/webcivil/FCASMain, Doc. No. 34. NYAG conceded before the motion court in *Ernst & Young* that the cases it relied on to support its position that disgorgement is an available remedy under the Martin Act and Executive Law involved funds that were either paid by investors or by the state. *Ernst & Young* Tr. at 11. The funds that NYAG seeks here, by contrast, were paid as bonuses to Appellants by a private company (AIG) that has released any claim to recover those funds.

the Attorney General may be precluded from seeking restitution and damages if defendant settled the private class action against it." *Id.* at 570. *Third*, it improperly relied on federal case law interpreting federal statutes, that, in contrast to the Martin Act and Executive Law § 63(12), expressly empower the SEC to seek broad equitable relief. *Fourth*, it ignored principles of separation of powers by impermissibly empowering NYAG to seek remedies beyond those authorized by the Legislature.[16]

1. *Applied Card* Does Not Authorize Disgorgement Under The Martin Act Or Executive Law § 63(12).

Plainly, *Applied Card* does not hold that disgorgement is available under the Martin Act, which was not even at issue in that case. Nor does *Applied Card* hold that disgorgement is available under Executive Law § 63(12).

In *Applied Card*, this Court held only that *res judicata* barred NYAG from seeking *restitution* under a consumer protection statute for consumers who participated in the settlement of a nationwide class action venued in

[16] Even if disgorgement were an available remedy under the Executive Law, disgorgement may not be obtained in the case at bar. Unlike *Ernst & Young*, which was decided at the motion to dismiss stage, here, after years of discovery (and where all relevant discovery is now closed), NYAG has not offered any evidence linking the alleged "ill-gotten gains" (bonuses that AIG paid Appellants from 2000 to 2005) to the two transactions remaining at issue. *See infra* Argument Section VII.A. In addition, unlike the case at bar, there was nothing in the record in *Ernst & Young* indicating that the entity that made the payments sought to be disgorged had released the payees of all claims relating to those funds.

California that included New York consumers regarding the same transactions. *Id.* at 125. The Court nonetheless observed that, in the specific circumstances of that case, NYAG "*might* be able to obtain disgorgement – an equitable remedy distinct from restitution – of profits that respondents derived from all New York consumers." *Id.* (emphasis added). This non-committal observation on an issue not before the Court does not equate to a holding that disgorgement is a generally available remedy under Executive Law § 63(12). The *Applied Card* parties did not argue, and this Court did not decide, whether disgorgement was authorized by Executive Law § 63(12).[17]

In all events, this Court's *dicta* in *Applied Card* provides no support for the Appellate Division's decisions in *Ernst & Young* and this case. That *dicta* supports only the conclusion that, even if disgorgement were available under Executive Law § 63(12), it would be limited to NYAG seeking "disgorgement . . . *of profits that respondents derived from all New York consumers.*" *Id.* (emphasis added). Here, NYAG does not seek such profits, but rests its case entirely on seeking disgorgement of monies received by

[17] Since *Applied Card*, this Court has referred to the remedies available under Executive Law § 63(12) without mentioning disgorgement. *See, e.g.*, *People v. Coventry First LLC*, 13 N.Y.3d 108, 111 (2009) (noting that NYAG is "authorized by statute" to seek "an order enjoining the continuance of such business activity or of any fraudulent or illegal acts, [and] directing restitution and damages" (alteration in original) (internal quotation marks omitted)).

Appellants *from AIG*. *Applied Card* thus closes rather than opens a door for NYAG's disgorgement claim in this case.

2. Whether To Include Disgorgement As A Remedy Under The Statutes Is A Question For The New York Legislature To Determine.

Although the Appellate Division in *Ernst & Young* may have considered it "crucial" for NYAG to invoke disgorgement as a remedy, 114 A.D.3d at 570, as discussed *supra* Argument Section II.A & B, that question is for the New York Legislature – not the courts – to decide. *See Morales*, 94 N.Y.2d at 224-25; *Sheehy*, 73 N.Y.2d at 636. *See also Klostermann v. Cuomo*, 61 N.Y.2d 525, 541 (1984) ("The activity that the courts must be careful to avoid is the fashioning of orders or judgments that go beyond any mandatory directives of existing statutes and regulations and intrude upon the policy-making and discretionary decisions that are reserved to the legislative and executive branches"); *I.L.F.Y. Co. v. City Rent & Rehab. Admin.*, 11 N.Y.2d 480, 489-90 (1962) ("[T]he courts may not dictate to the legislative body the choice of remedy to be selected; questions as to wisdom, need or appropriateness are for the Legislature.").

Moreover, there is an adequate remedy at law – the legislatively determined set of remedies under the Martin Act and Executive Law § 63(12). *See Fumarelli*, 92 N.Y.2d at 305; 55 N.Y. Jur. 2d *Equity* § 18

(2015) ("equity will not entertain jurisdiction when there is an adequate remedy at law").

3. The *Ernst &Young* Court's Reliance, In Part, On Federal Authority Merely Highlights That Disgorgment Is Not An Available Remedy Here.

In addition to *Applied Card*, the Appellate Division in *Ernst & Young*, 114 A.D.3d. at 569-70, relied on *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 102 (2d Cir. 1978), which interpreted federal securities laws. The Appellate Division's reliance on *Commonwealth* was erroneous because it failed to take into account that, unlike the Martin Act and Executive Law, the federal securities laws contain explicit catch-all provisions empowering the SEC to seek broad forms of equitable relief, including "all other rights and remedies that may exist at law or in equity." 15 U.S.C. § 77p(a); 15 U.S.C. § 78bb(a)(2). Neither the Martin Act nor the Executive Law authorizes NYAG to seek broad equitable relief.[18]

[18] The Appellate Division relied on two other New York cases, neither of which relates to what relief NYAG may seek under the Martin Act or Executive Law. *Excelsior 57th Corp. v. Lerner*, 160 A.D.2d 407 (1st Dep't 1990), and *In re Matter of Blumenthal (Kingsford)*, 32 A.D.3d 767 (1st Dep't 2006), address purely private lawsuits: the former was a breach of fiduciary duty action brought by a cooperative corporation against an attorney and others and the latter involved an action by an estate against its former executor.

4. *Ernst & Young* Ignores Principles Of Separation Of Powers.

The reasoning in *Ernst & Young* that disgorgement furthers the "deterrence" purpose of the Martin Act, *see* 114 A.D.3d at 569-70, provides no basis for reading a remedy into the Martin Act where the Legislature has had ample opportunity to include the remedy and has not done so. Inferring additional remedies, such as disgorgement, creates the risk of adding impermissibly punitive judicial remedies beyond what the Legislature intended as the proper scope of deterrence under the Martin Act.

That interpretation violates the fundamental role of the courts in statutory interpretation, which is "to ascertain and give effect to the intention of the Legislature." N.Y. Stat. § 92. Just last year, this Court unanimously reaffirmed that fundamental principle of separation of powers when it ruled that state bodies may act only within the powers granted to them by statutory authority. *See Baldwin Union Free Sch. Dist. v. Cty. of Nassau*, 22 N.Y.3d 606, 611 (2014) ("Beyond its constitutional authority, neither a county nor the State can act, regardless of the perceived wisdom of its conduct or the nobility of its aims.").

If NYAG believes that the remedy of disgorgement is needed to effectuate the goals of the Martin Act and Executive Law § 63(12), it should petition the Legislature to add that remedy to those statutes. *Id.* at 628

("With respect to any policy concerns, 'appeal lies to the ballot and to the legislative processes of democratic government, not to the courts.'"). But there has been no such amendment and the legislative intent is manifest in the existing statutory language that NYAG is not empowered to seek disgorgement as a remedy for a violation of the Martin Act or Executive Law § 63(12).

III. NYAG'S CLAIM FOR DISGORGEMENT IS EITHER A PROHIBITED ATTEMPT TO SEEK REMEDIES BARRED BY *APPLIED CARD* OR AN ATTEMPT TO OBTAIN AN IMPERMISSIBLE PENALTY.

A. NYAG's Claim For Disgorgement Is Barred By This Court's Decision In *Applied Card*.

AIG voluntarily settled and released any existing and potential claims it had against Appellants (R. 146), including *any claims for restitution or disgorgement*, and paid Appellants $150 million. (R. 147.) NYAG has never raised any issues concerning the adequacy of AIG's settlement with Appellants, but now seeks disgorgement of Appellants' bonuses[19] even though the principles of *res judicata*, as they were explained in *Applied*

[19] NYAG did not identify what it sought to disgorge during the briefing on the summary judgment motion either in the motion court or on appeal, clarifying the issue only in its January 29, 2015 pretrial memorandum. Plaintiff's Pre-Trial Memorandum, *People v. Greenberg*, Index No. 401720/05 (Sup. Ct. N.Y. County Jan. 29, 2015) at 33, n.23 ("[T]he State has limited its disgorgement claim to the cash bonuses defendants were paid."); *id.* at 3 ("Greenberg and Smith received $24,500,000 million and $3,065,000 million, respectively, in bonuses for the years 2000 through 2004 (and in Smith's case, for early 2005), to which they are not entitled in light of the frauds they engineered.").

Card, bar any such claims.[20] *See Applied Card*, 11 N.Y.3d at 122 ("In New York, res judicata, or claim preclusion, bars successive litigation based upon the 'same transaction or series of connected transactions.'").

Permitting NYAG to attempt to disgorge from Appellants the bonuses paid by AIG would "destroy or impair rights" created in Appellants' previous settlements with AIG and its shareholders. *Cf. Applied Card*, 11 N.Y.3d at 124 ("Permitting the Attorney General to seek additional restitution on behalf of the *Allec* settlement class members would undoubtedly 'destroy or impair rights' conclusively established in the *Allec* case.").

B. NYAG's Claim For Disgorgement Is Either A Request For Punitive Damages Or A Request For An Impermissible Penalty.

During the May 28, 2013 oral argument before this Court on the prior appeal in this case, the Solicitor General explained that NYAG might pursue a disgorgement claim because "we're looking for *a deterrent effect* for these people and for people who engage in comparable activities." (R. 225.) Because deterrence is precisely the purpose of punitive or other exemplary damages, which NYAG cannot seek under the Martin Act, there is no basis

[20] Similarly, NYAG never expressed any concern for the adequacy of Appellants' August 7, 2009 settlement with the SEC in which Appellants disgorged $8.25 million to the SEC in connection with the entry of consent judgments. (R. 89, 108.)

for inferring disgorgement as a deterrent remedy either. *See Solil Mgmt. Corp.*, 128 Misc. 2d at 773 (rejecting NYAG claims for punitive and treble damages as not specified under the language of Executive Law § 63(12)); *State v. Hotel Waldorf Astoria Corp.*, 67 Misc. 2d 90, 92 (Sup. Ct. N.Y. County 1971) (treble damages not available under Executive Law § 63(12)). *See also State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 416 (2003) ("[P]unitive damages serve a broader function; they are aimed at deterrence and retribution."); *Guariglia v. Price Chopper Operating Co. Inc.*, 38 A.D.3d 1043, 1043 (3d Dep't 2007) ("The purpose of *punitive damages* goes beyond simply punishing the perpetrator for the morally culpable act committed, but is also intended to *deter* repetition of such acts." (emphasis added) (citation omitted)).

If NYAG's disgorgement claim does not amount to impermissible punitive damages, then it is an attempt to impermissibly impose a penalty on Appellants. The hallmark of penalties is that they are "intended to punish culpable individuals," not "to extract compensation or restore the status quo." *See Tull v. United States*, 481 U.S. 412, 422 (1987). *See also Gabelli v. SEC*, 133 S. Ct. 1216, 1223 (2013) ("In a civil penalty action, the Government is not only a different kind of plaintiff, it seeks a different kind

of relief," namely, "penalties, which go beyond compensation, are intended to punish, and label defendants wrongdoers").

However, the Martin Act allows only for remuneration in "a sum not in excess of two thousand dollars," N.Y. Gen. Bus. Law § 353(1), and the CPLR only allows the court to award "a sum not exceeding two thousand dollars against each defendant" in actions brought by NYAG under either the Martin Act or Executive Law § 63(12). CPLR 8303(6). Thus, NYAG's attempt to disgorge the bonuses Appellants received from AIG from 2000 to 2005 is not authorized by those statutes. *See, e.g.*, *Chew Wah Bing v. Sun Wei Ass'n*, 205 A.D.2d 355, 356 (1st Dep't 1994) (error to impose fines that exceeded statutory allowance).

IV. EVEN IF DISGORGEMENT WERE AN AVAILABLE REMEDY UNDER THE MARTIN ACT AND EXECUTIVE LAW, IT IS NOT AVAILABLE UNDER THE FACTS OF THIS CASE.

A. NYAG's Disgorgement Claim Is Barred By Appellants' Direct And Derivative Settlements With AIG And Its Shareholders.

NYAG's disgorgement claim also fails in this case because of AIG's settlement with Appellants. "[A] valid release constitutes a complete bar to an action on a claim which is the subject of the release." *Global Mins. & Metals Corp. v. Holme*, 35 A.D.3d 93, 98 (1st Dep't 2006); *see also Booth v. 3669 Delaware*, 92 N.Y.2d 934, 935 (1998) (citing *Mangini v. McClurg*, 24

N.Y.2d 556, 563 (1969)). Here, AIG agreed to release "any claims" against Appellants "that could have been brought, arising in whole or in part prior to" November 25, 2009, the date of the settlement. (R. 146.) Those claims included any claims regarding bonuses paid to Appellants by AIG from 2000 to 2005. This unambiguous release extinguishes AIG's right to disgorgement, and prevents NYAG from seeking to disgorge those same funds. *See Applied Card*, 11 N.Y.3d at 124 n.16 ("[T]he members of the *Allec* settlement class, on whose behalf the Attorney General sues, have already had their 'day in court.'").

Moreover, the settlement of AIG's claims against Appellants in the Delaware Derivative Action and the settlement of the claims of AIG's shareholders against Appellants in the federal class action further bar NYAG's effort to seek disgorgement here. *See supra* Statement of the Case III.B-D. *See also Betz v. Blatt*, 116 A.D.3d 813, 816-17 (2d Dep't) (affirming dismissal of disgorgement claim as duplicative where the claim was "based on the same facts" as other causes of action for money damages and therefore "did not allege distinct causes of action"), *appeal dismissed*, 23 N.Y.3d 1028 (2014).

Under established *res judicata* principles, "successive litigation based upon the same transaction or series of connected transactions" is barred "if

(i) there is a judgment on the merits rendered by a court of competent jurisdiction, and (ii) the party against whom the doctrine is invoked was a party to the previous action or in privity with a party who was." *Applied Card*, 11 N.Y.3d at 122. These elements are met here because the transactions at issue were also at issue in those actions and final judgment was entered in each action, thereby resolving all claims against Appellants. *See*, *e.g.*, Order and Final Judgment at 3-4, *Am. Int'l Grp., Inc. Consol. Derivative Litig.*, No. 769-VCS (Del. Ch. Jan. 25, 2011), 2011 WL 244179; *see also* R. 153-62 (judgment in *In re AIG*). The requirement of privity is met because NYAG here seeks to stand in AIG's shoes to obtain disgorgement of Appellants' bonuses, thus putting NYAG in privity with AIG for purposes of *res judicata*. *Applied Card*, 11 N.Y.3d at 122-24. *See also* 19A N.Y. Jur. 2d *Compromise, Accord, and Release* § 97 at 158 (2010) (although a release "cannot be held to bar the claim of a person who did not sign it, the nonsigner's claims will be delimited by the covenant insofar as they are derivative from the claims of one who did sign the agreement"); *Andrew Greenberg, Inc. v. Svane, Inc.*, 36 A.D.3d 1094, 1096-97 (3d Dep't 2007) (subsequent derivative claims were barred where corporation had settled the claims); *Charter Oak Fire Ins. Co. v. Borrelli*, 273 A.D.2d 797, 798-99 (4th Dep't 2000) (interpleader action should have been dismissed

where plaintiff had already settled with and obtained releases from defendants); *Miller v. Jetblue Airways Corp.*, 24 Misc. 3d 1237(A), N.Y. Slip Op. 51780(U) at *1-2 (Sup. Ct. N.Y. County 2009) (derivative claim barred where injured party had released the underlying claim).[21]

B. Disgorgement Is Not Appropriate Where Appellants Did Not Receive Compensation From The State Or Public Investors.

It is a longstanding principle that "[t]he State cannot, any more than an individual, have a civil action for the recovery of money . . . except upon proof of title or ownership." *People v. Ingersoll*, 58 N.Y. 1, 13-14 (1874). "It is not sufficient for the People to show that wrong has been done to someone; *the wrong must appear to be done to the People* in order to support an action by the People for its redress." *People v. Lowe*, 117 N.Y. 175, 192 (1889) (emphasis added). That is because there is no public interest where private parties "have ample remedies to redress their wrongs by proceedings in their own names." *Id.* at 195. NYAG must show that it sues to remedy an injury to one of its quasi-sovereign interests, *Ingersoll*, 58 N.Y. at 14, which it cannot do here.

[21] Even in federal securities enforcement cases, where the SEC is expressly authorized by statute to seek disgorgement, the ability to obtain disgorgement is not limitless. Clawbacks of executive bonuses under the Dodd-Frank and Sarbanes-Oxley laws are returned to the *issuer*. *See* 15 U.S.C. § 78j-4(b) (Dodd-Frank Act § 954); 15 U.S.C. § 7243(a) (Sarbanes-Oxley Act § 304). In this action, NYAG has not suggested that it will return the money to AIG or its shareholders.

Where "wrongs are wrongs to individual citizens and not to the State," they "are remediable at the suit of the parties injured *only*," even where a case is "presented to the court as one of equitable consideration." *People v. Albany & Susquehanna R.R. Co.*, 57 N.Y. 161, 168, 170 (1874) (emphasis added); *see New York v. Seneci*, 817 F.2d 1015, 1017 (2d Cir. 1987) (dismissing suit under Executive Law § 63(12) and RICO for lack of standing because the "state cannot merely litigate as a volunteer the personal claims of its competent citizens").

As explained by the Appellate Division, a "for-profit entity" (such as AIG here) possesses "unquestionably . . . powerful financial incentives to prosecute an action" without the assistance of NYAG, and in such cases NYAG must point to an applicable public interest to show its "authority to prosecute" the action. *People v. Grasso*, 54 A.D.3d 180, 194 (1st Dep't 2008). Otherwise, the action "vindicates no public purpose" and raises "serious constitutional questions" in light of the New York State Constitution's prohibition against spending public funds to aid private entities. *Id.* at 196-97.

Similarly, in *Seneci*, the Second Circuit rejected NYAG's attempt to shoehorn a civil RICO claim on behalf of private parties into a *parens patriae* action:

> "The state cannot merely litigate as a volunteer the personal claims of its competent citizens. Where the complaint only seeks to recover money damages for injuries suffered by individuals, the award of money damages will not compensate the state for any harm done to its quasi-sovereign interests. Thus, the state as *parens patriae* lacks standing to prosecute such a suit."

817 F.2d at 1017 (citations omitted).

Here, NYAG does not seek to recover funds purportedly lost by the State or public investors. Rather, NYAG seeks only to recover funds paid by AIG to Appellants as bonuses when they were officers of AIG. This new "disgorgement" remedy is nothing more than a thinly veiled attempt to circumvent the prohibitions on NYAG's withdrawn claim for money damages.[22] NYAG does not allege it seeks funds to which the State has legal entitlement. *See Greenberg I*, 95 A.D.3d at 492 (Catterson, J., dissenting in part and concurring in part) ("[P]rivate shareholders who have cause to complain have no need of NYAG to protect their rights. There is simply no wrong committed 'directly against the State or the people of the State' as required by *Ingersoll*, *Lowe* and *Grasso*."). Accordingly, NYAG

[22] In *Ernst & Young*, NYAG acknowledged that it brought its disgorgement claim only as a work-around to *Applied Card*. *See Ernst & Young* Tr. at 16 (the effect of *Applied Card* was that NYAG "cannot get money for the victims who have been satisfied and given relief"); *id.* at 24 ("Over in the federal court, you can't, under *Applied Card*, now get damages for the people except for a few people might opt out. All right. That's part of the life. That's what the *Applied Card* case was about. *But it is for that reason, among others, among others, that our ability to get disgorgement of some or all of the fees that they received in doing a non-audit, an improper audit, that we have that power and that right*." (emphasis added)).

cannot maintain its disgorgement claim because it fails to allege the requisite direct injury.

C. NYAG Failed To Submit Any Evidence Supporting A But-For Causal Link Between Appellants' Bonuses And The Transactions At Issue.

NYAG failed to submit evidence supporting a causal relationship between the alleged wrongdoing and the amounts it seeks to disgorge. Such a causal link is required because disgorgement aims to "eliminate profit from wrongdoing while avoiding . . . the imposition of a penalty." Restatement (Third) of Restitution and Unjust Enrichment § 51(4) (2011); *id.* § 51 cmt. *i* ("Disgorgement does not impose a general forfeiture: defendant's liability in restitution is not the whole of the gain from a tainted transaction, but *the amount of the gain that is attributable to the underlying wrong.*" (emphasis added)); *id.* ("If the claimant's evidence will not yield even a reasonable approximation, the claim of unjust enrichment is merely speculative, and disgorgement will not be allowed."). The requirement of a causal link between targeted funds and wrongdoing ensures that only wrongful benefits are disgorged. *See Diamond v. Oreamuno*, 24 N.Y.2d 494, 498-99 (1969) (disgorgement targets only "profits which . . . [defendants] derived solely from exploiting" their positions). *See also Jim Beam Brands Co. v. Tequila Cuervo La Rojena S.A. de C.V.*, No. 600122/2008, 2011 N.Y. Slip Op.

34181(U), at *7 (Sup. Ct. N.Y. County July 12, 2011) ("Jim Beam's expert's reliance on a disgorgement theory also fails because there is *no causal link* between any increase in profits during the period of the breach, which is still continuing." (emphasis added)).[23]

Against this clear legal backdrop, NYAG conceded at oral argument on summary judgment that it must prove a causal nexus between Appellants' alleged wrongdoing and the funds to be disgorged (R. 527) ("So basically, what we will have to establish . . . is that there is a nexus between the frauds that Mr. Greenberg and Mr. Smith committed on behalf of AIG or AIG committed at their direction, and a segment of the bonuses they received.").

Nevertheless, and despite its acknowledgement of its burden, NYAG did not even attempt to meet these causation requirements in opposing Appellants' summary judgment motion. There simply is no evidence in the record to suggest that any part of Appellants' bonuses resulted from their alleged participation in the two transactions remaining at issue. To the contrary, there is affirmative evidence that Appellants did *not* receive any funds as a result of the two allegedly wrongful transactions: AIG never

[23] The Second Circuit has also held that disgorgement can be "ordered only with respect to those [profits] that were illegally derived." *SEC v. Razmilovic*, 738 F.3d 14, 31 (2d Cir. 2013); *CFTC v. British Am. Commodity Options Corp.*, 788 F.2d 92, 93 (2d Cir. 1986) ("Generally, where benefits result from both lawful and unlawful conduct, the party seeking disgorgement must distinguish between the legally and illegally derived profits.").

sought to claw back Appellants' bonuses after their departure, and released any such claims on November 25, 2009, when AIG settled with Appellants and AIG paid Appellants $150 million. *See supra* Sections III. A, IV.A; (R. 142-52).

D. NYAG's Belated Attempt To Pursue Disgorgement Violates Principles Of Due Process.

Foundational federal and state due process principles prevent the State from threatening the livelihood and reputation of a citizen by pursuing a suit on one theory of liability and remedy, and years into the litigation, altering that theory. *See Mullane v. Cent. Hanover Bank & Tr. Co.*, 339 U.S. 306, 314-15 (1950). Yet, as discussed above, only in May 2013 (eight years after this action was commenced and after discovery was completed) did NYAG begin to *consider* whether it had a claim for disgorgement after NYAG was compelled to withdraw its claim for money damages as a result of Appellants' settlement of a federal securities class action. *See supra* Statement of the Case II.C; (R. 221-22). This Court should reaffirm the constitutional limitations on the State's power to arbitrarily determine and then impose penalties on its citizens, and reject NYAG's attempt to revive its long-abandoned disgorgement claim to evade the impact of *Applied Card* on this action.

V. NYAG IS NOT ENTITLED TO THE TYPE OF PERMANENT INJUNCTIVE RELIEF IT SEEKS UNDER NEW YORK LAW OR THE FACTS OF THIS CASE.

During the May 28, 2013 oral argument on the prior appeal in this action, the Solicitor General told this Court that NYAG seeks a sweeping injunction preventing Appellants from participating in the securities industry or "serving as officers and directors of public companies." (R. 220.) The demand thus significantly expands upon the injunctive relief sought in NYAG's Amended Complaint, which requests only a prohibition against ongoing or future fraudulent conduct. (R. 140.)

In its June 25, 2013 Opinion, this Court expressed skepticism about the possibility of NYAG obtaining the permanent injunctive relief it now seeks, and expressly stated that "there is no doubt room for argument about whether the lifetime bans that the Attorney General proposes would be a justifiable exercise of a court's discretion," but directed the lower courts to consider "in the first instance" whether NYAG could proceed with this expanded demand for injunctive relief. *Greenberg II*, 21 N.Y.3d at 448. Contrary to this Court's directive, neither of the courts below analyzed: (a) whether the injunctive relief sought was authorized by the Martin Act or the Executive Law; (b) whether NYAG could obtain a permanent injunction against Appellants in the absence of a genuine threat of irreparable harm or a

reasonable expectation that the alleged wrong will reoccur; or (c) whether the "lifetime bans" sought by NYAG were "a justifiable exercise" of discretion. *See id.*

The courts below should have dismissed NYAG's claims for permanent injunctive relief on the grounds that the relief sought is not authorized by the Martin Act or Executive Law § 63(12) and is not appropriate under the undisputed facts of this case.

A. The Injunctive Relief NYAG Seeks Is Not Authorized By The Martin Act Or Executive Law § 63(12).

Neither the Martin Act nor Executive Law § 63(12) authorizes NYAG to seek: (1) an unlimited injunction against service as an officer or director of a public company; or (2) a lifetime ban on participation in the securities industry. N.Y. Gen. Bus. Law § 353(1); N.Y. Exec. Law § 63(12). To the contrary, the Martin Act expressly limits available injunctive relief to a prohibition against selling or offering securities within or from New York State:

> "[I]f the attorney-general should believe from such evidence that such person, partnership, corporation, company, trust or association actually has or is engaged in any such fraudulent practice, he may include in such action *an application to enjoin permanently* such person, partnership, corporation, company, trust or association, and such other person or persons as may have been or may be concerned with or in any way participating in such fraudulent practice, *from selling or offering for sale to*

> *the public within this state, as principal, broker or agent, or otherwise, any securities issued or to be issued*."

N.Y. Gen. Bus. Law § 353(1) (emphasis added).

Similarly, Executive Law § 63(12) authorizes injunctions only against future fraudulent or illegal actions, and does not authorize restrictions on a defendant's otherwise legal business activities:

> "Whenever any person shall engage in repeated fraudulent or illegal acts or otherwise demonstrate persistent fraud or illegality in the carrying on, conducting or transaction of business, the attorney general may apply, . . . *for an order enjoining the continuance of such business activity or of any fraudulent or illegal acts*, directing restitution and damages and, in an appropriate case, cancelling any certificate filed under and by virtue of the provisions of section four hundred forty of the former penal law or section one hundred thirty of the general business law, and the court may award the relief applied for or so much thereof as it may deem proper."

N.Y. Exec. Law § 63(12) (emphasis added).[24]

As discussed fully in Argument Section II.B, *supra*, the New York Legislature's decision to include certain remedies but not others in the Martin Act and Executive Law § 63(12) is a conclusive indication that

[24] In contrast, the federal securities laws, such as the Securities Exchange Act of 1934, expressly authorize federal courts to bar individuals from serving as officers or directors of a publicly traded company upon application by the SEC. *See* 15 U.S.C. § 78u(d)(2). With respect to Appellants, who entered into consent judgments with the SEC, dated August 7, 2009, the SEC did not pursue such a bar against Mr. Greenberg, and only sought a three-year bar against Mr. Smith. Those choices, made under statutory authorization as part of a comprehensive nationwide regulatory scheme governing the national securities markets, should not be disturbed by a state court proceeding by NYAG or any of the other 49 state attorneys general, let alone under statutes which do not permit NYAG to seek such relief.

NYAG cannot pursue the injunctive relief it seeks in this case. Neither the Martin Act nor the Executive Law provides a basis for NYAG's attempt to obtain a permanent injunction enjoining Appellants from participating in the securities industry or from acting as officers and directors of a public company.

The bar on service as an officer or director of a publicly traded company is not authorized by the language of the Martin Act, which only permits injunctions "from selling or offering for sale to the public" "any securities issued or to be issued." N.Y. Gen. Bus. Law § 353(1). Nor is an officer or director bar authorized by Executive Law § 63(12), which permits only injunctions of "fraudulent or illegal acts." N.Y. Exec. Law § 63(12).

In permitting NYAG to proceed with its pursuit of injunctive relief not authorized by those statutes, the motion court purported to rely on this Court's decision in *People v. McCann*, 3 N.Y.2d 797 (1957). But *McCann* – which has not been cited or discussed in any reported decision in the more than half century since it was decided, and was merely an affirmance[25] – does not hold that officer and director bars are permissible under the Martin

[25] *McCann* does not contain any analysis of the issue and simply states "Judgment affirmed." *Id*. at 800. Likewise, the Fourth Department decision was a mere affirmance and similarly devoid of written analysis. *See People v. McCann*, 2 A.D.2d 644 (4th Dep't 1956). And the unreported decision of the Erie Equity Term affirmed by the Fourth Department merely recited an order and did not analyze the legal issues. *See People v. McCann*, No. B60296, slip op. (Sup. Ct. Erie County June 23, 1955).

Act.[26] The decision did not examine the statutory language of the Martin Act, but instead merely rejected the argument that a prohibition on participating in the New York securities industry unconstitutionally denied the appellant the right to work. 3 N.Y.2d at 797-98. The *McCann* parties do not appear to have raised the question of whether the relief at issue was statutorily authorized, and the Court did not decide that issue.

B. The Injunctive Relief Sought By NYAG Constitutes An Impermissible Penalty.

Injunctive relief is not available in a Martin Act or Executive Law action where such relief constitutes an impermissible penalty. The "only legitimate aim" of a Martin Act injunction "is to secure the investing public against injury through *possible future fraudulent practices on the part of the defendant*." *People v. Riley*, 188 Misc. 969, 972 (Sup. Ct. N.Y. County 1946) (emphasis added). "Martin Act injunctions are granted, not as punishment to the individual but as a protection to the public . . . ." *Lexington Sixty-First Assocs.*, 38 N.Y.2d at 597.

[26] The three dissenting judges in *McCann* suggested that the majority erred by not explicitly examining the statutory framework of the Martin Act, objecting that "the appellant should have been *restrained from engaging in fraudulent practices*," and that the injunction at issue was so "universal in scope that it seems to us that it should not be approved by this court without modification." 3 N.Y.2d at 798 (emphasis added). The dissent further observed that the injunction at issue was improper because it was so "sweeping" that it failed to "'clearly inform a defendant of the acts he is forbidden to commit'" and "'the injunction forbids defendant to engage in activities which are altogether lawful.'" *Id.* at 799 (quoting *May's Furs & Ready-to-Wear, Inc. v. Bauer*, 282 N.Y. 331, 343 (1940)).

NYAG's requested injunction would constitute an improper penalty because it is superfluous. The SEC has already sought and obtained the relief requested by NYAG in the form of consent judgments entered into between the SEC and each Appellant.[27] *See supra* Statement of the Case III.A; (R.102-116). NYAG has not presented any evidence of past or threatened non-compliance by Appellants with the federal injunctions.

Because the existing injunctions address any legitimate sovereign interest in precluding "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person," *see* 17 C.F.R. § 240.10b-5(c) (2013), further injunctive relief is wholly unnecessary and would not serve any valid public purpose. *See State v. Holiday Inns, Inc.*, 656 F. Supp. 675, 678 (W.D.N.Y. 1984) (NYAG lacks a valid sovereign interest where "broad injunctive relief" covering same subject matter was sought by private litigants); *cf. Envtl. Conservation Org. v. City of Dallas*, 529 F.3d 519, 523-24, 529-30 (5th Cir. 2008). As the United States Supreme Court has noted, "one injunction is as effective as 100" and

[27] The Appellate Division's decision stated that the "existence of a federal consent judgment imposing a similar but more lenient injunctions, and not providing for any acknowledgment of guilt does not preclude the injunction sought here by the State." (R. 588) (internal citations omitted). In support, the court cited *SEC v. Citigroup Global Markets, Inc.*, 827 F. Supp. 2d 328 (S.D.N.Y. 2011), *vacated and remanded*, 752 F.3d 285 (2d Cir. 2014), a decision that was overturned by the Second Circuit and did not discuss the propriety of overlapping state and federal injunctions.

"100 injunctions are no more effective than one." *Hawaii v. Standard Oil Co. of Cal.*, 405 U.S. 251, 261 (1972).

Because Mr. Greenberg (as a control person) and Mr. Smith are already bound by federal injunctions that fully address any plausible sovereign interest (R. 86-97, 102-116), and NYAG has not proffered any admissible evidence establishing the elements necessary to obtain injunctive relief, the only conceivable purpose for the continued pursuit of permanent injunctive relief would be to punish Appellants, which as this Court held in *Lexington Sixty-First Associates*, 38 N.Y.2d at 597, is not a permissible goal of a Martin Act proceeding.

C. NYAG Is Not Entitled To An Injunction Based On The Undisputed Facts Of This Case.

It is hornbook New York law that the party seeking a permanent injunction must show "that there is a danger of *irreparable injury* unless the injunction is entered and that there is an *inadequacy of other remedies* to afford just and equitable relief, and it is a cardinal rule of equity that without these factors a permanent injunction will not be issued." 67A N.Y. Jur. 2d *Injunctions* § 45 (2010) (emphasis added) (footnotes omitted). These settled rules of equity apply to NYAG's claims under the Martin Act and Executive Law. *See State v. Fine*, 72 N.Y.2d 967, 968-69 (1988) (the Martin Act did

not supplant longstanding requirements for injunctive relief because the Martin Act does not specify differing standards).

Moreover, in determining whether to grant a permanent injunction, the court looks to the facts as they exist at the time of trial, not as they are alleged to have existed when the complaint was filed. *Dickinson v. Springer*, 246 N.Y. 203, 211 (1927) ("The courts of this State . . . would deny injunctive relief if it appeared that though a basis for injunctive relief may have existed at the time the suit was begun, it no longer existed at the time of the trial."); *accord*, 67A N.Y. Jur. 2d *Injunctions* § 45 (2010) ("[A] court will deny such relief, even though it appears that a basis for such relief may have existed at the time the action began, if it no longer exists at the time of trial.").

In support of their motion for summary judgment, Appellants submitted sworn statements making a *prima facie* showing that no such likelihood of irreparable harm or recurrent illegality exists.[28] *See supra*

[28] In fact, the conduct that NYAG seeks to enjoin – serving as an officer or director of a publicly traded company and participating in the securities industry – is not even illegal conduct. NYAG lacks any sovereign interest in protecting New York State residents from *legal* conduct. *See State v. Magley*, 105 A.D.2d 208, 210 (3d Dep't 1984) (affirming denial of injunction under Executive Law § 63(12) because "[s]ubdivision 12 of section 63 was intended to prevent the perpetration of ongoing fraud or illegality, but where the act sought to be enjoined is not a violation of law, subdivision 12 of section 63 does not confer the required authority for an inquiry as to such act"); *see Assured Guaranty II*, 18 N.Y.3d 341, 349 (the Martin Act "authorizes the Attorney General to investigate and enjoin fraudulent practices in the marketing of stocks, bonds and other

Statement of the Case IV; *infra* Argument Section VII.B. In response, NYAG trial counsel provided only rank speculation from a news article regarding Appellants' possible future conduct. (R. 332-35.) Such speculation cannot create a triable issue of fact sufficient to defeat summary judgment. *See, e.g.*, *Espinal v. Trezechahn 1065 Ave. of the Ams., LLC*, 94 A.D.3d 611, 613 (1st Dep't 2012); *Ellen v. Lauer*, 210 A.D.2d 87, 90 (1st Dep't 1994).

Despite this failure by NYAG, the motion court nonetheless concluded that "the scope and nature of the permanent injunction" "pose issues of fact, including the credibility of defendants, which are not appropriate for summary resolution." (R. 22.) In so doing, the motion court relied on inapposite federal cases involving credibility determinations concerning whether defendants would violate the securities laws in the future.

Here, the relevant facts (Appellants' ages, the scope of the existing federal injunctions, and the nature of their activities over the past decade) do not require any credibility determinations. (R. 35-36, 86-89, 98-101, 102-16.) Moreover, nearly fifteen years have passed since AIG entered into the

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securities within or from New York" (internal quotation marks omitted)); *McCann*, 3 N.Y.2d at 799 (Van Voorhis, J., dissenting) (arguing that the Martin Act injunction was improper because "the injunction forbids defendant to engage in activities which are altogether lawful" (internal quotation marks omitted)).

two transactions remaining at issue in this case took place (R. 125-28, 130-35), and there is no allegation of any misconduct involving either Appellant in the ensuing period (R. 37, 99-100). This lengthy interlude without additional incident further demonstrates that there is no reasonable likelihood of future harm.[29] *See Lee v. Tetra Tech, Inc.*, 14 Misc. 3d 1235(A), 2007 NY Slip Op. 50312(U), at *10 (Sup. Ct. Monroe County 2007) (denying permanent injunction when "in view of the passage of [time] after the commencement of the action without evidence of further incident," there is no actual or imminent threat sufficient to sustain a claim for permanent injunctive relief).[30]

[29] It also renders NYAG's claim for permanent injunctive relief moot. *See State v. Carvel Corp.*, No. 42126/79, 1979 WL 3896, at *2 (Sup. Ct. N.Y. County Dec. 24, 1979) (summary judgment granted dismissing NYAG's request for an injunction due to lack of an "imminent" injury); *see also State v. Grecco*, 21 A.D.3d 470, 478 (2d Dep't 2005) (dismissing Executive Law § 63(12) cause of action that did not allege "'repeated fraudulent or illegal acts'" or "'persistent fraud or illegality in the carrying on, conducting or transaction of business'"); *People v. Volkswagen of Am., Inc.*, 47 A.D.2d 868, 868 (1st Dep't 1975) (injunctive relief not granted "in view of the immediate correction of the advertisement and the passage of almost three years without repetition of the offense"). *People v. Alexanders Dep't Store, Inc.*, 42 A.D.2d 532, 532 (1st Dep't 1973) (rejecting claim for injunction where the violation to be enjoined was "a single offense unlikely to be repeated by the respondent" and the claim for an injunction "was not commenced until seven months after the offending conduct" and "in the absence of any indication of threatened or probable repetition, no useful purpose will be served by granting injunctive relief."). Under established law, then, NYAG should not be permitted to proceed with its claim for permanent injunctive relief, because no remedy is available and the matter is moot, Absent a remedy, any judicial decision "can have no immediate effect and may never resolve anything." *N.Y. Pub. Interest Research Grp. v. Carey*, 42 N.Y.2d 527, 531 (1977) (internal quotation marks omitted).

[30] Notably, even when a permanent injunction is warranted, New York law expressly contemplates dissolution of the injunction after five years in the absence of evidence of

Significantly, NYAG has *never* sought any preliminary injunctive relief since commencing this action over a decade ago, effectively conceding that there is no genuine threat of irreparable harm or likelihood of future harm. *Cf. SEC v. Monarch Fund*, 608 F.2d 938, 943-44 (2d Cir. 1979) (reversing injunction, in part, because "judgment below was not entered until more than seven years after the alleged violations" and "the SEC conceded that at no time during those seven years did it attempt to expedite the requested injunctive relief").

Considered together, these factors establish that NYAG's claim for injunctive relief should be dismissed. *See, e.g.*, *SEC v. Jones*, 476 F. Supp. 2d 374, 384 (S.D.N.Y. 2007) (dismissing SEC's request for injunction where "the Commission has adduced no positive proof aside from Defendants' past alleged wrongdoing to suggest 'some cognizable danger of recurrent violation,'" and several incident-free years had passed since defendants' alleged misconduct); *see also SEC v. Nat'l Student Mktg. Corp.*, 360 F. Supp. 284, 300 (D.D.C. 1973) (granting summary judgment to certain defendants on SEC's request for injunction because, even assuming defendants had violated securities laws, "there is no reasonable likelihood of

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misconduct. *See* N.Y. Gen. Bus. Law § 359-g(3). Here, nearly three times the statutorily mandated five-year period has passed since the transactions at issue took place, and there is no allegation or evidence in this case of any misconduct or threat of imminent irreparable harm during that period.

a similar violation since these defendants are not, and are not expected to be directors or insiders of any public company"). These cases comport with New York State law, which supports dismissal of claims seeking declaratory relief where the relief requested concerns circumstances that may never occur. *See Sutton Madison, Inc. v. 27 E. 65th St. Owners Corp.*, 68 A.D.3d 512, 512-13 (1st Dep't 2009).[31]

VI. NYAG'S CLAIMS FOR DISGORGEMENT AND INJUNCTIVE RELIEF ARE BARRED BY THE SUPREMACY CLAUSE OF THE UNITED STATES CONSTITUTION.

The Supremacy Clause of the United States Constitution "invalidates state laws that 'interfere with or are contrary to' federal law." *Hillsborough Cty., Fla. v. Automated Med. Labs., Inc.*, 471 U.S. 707, 712 (1985); *Air Transp. Ass'n of Am. v. Cuomo*, 520 F.3d 218, 220 (2d Cir. 2008) (preempting New York statute that conflicted with federal statutory scheme). Congress can preempt state laws either by express terms or through implication where the federal scheme is comprehensive and leaves no room for state regulation. *Air Transp. Ass'n*, 520 F.3d at 220-21.

[31] For the same reason, NYAG lacks an ongoing sovereign interest in the injunctive relief it seeks and therefore has no standing to pursue it. *See Grasso*, 54 A.D.3d at 207 (describing "minimal constitutional standing requirements" that must be met for NYAG to continue prosecution of action as: "'a distinct and palpable injury' to the plaintiff 'that is likely to be redressed if the requested relief is granted'"); *see also id.* at 194-95 (NYAG "no longer has the authority to prosecute" action where it would "vindicate only the interests of private parties, not any public interest"); *id.* at 192 n.7 ("[T]he Attorney General no longer has a legitimate interest in these causes of action.").

Appellants in this case previously entered into consent judgments with the SEC (under statutes in which disgorgement is *expressly* authorized by Congress)[32] to settle allegations that included the transactions remaining at issue in this action and disgorged a total of $8.25 million. (R. 86-97, 102-16.) Thus, the federal securities regulator, the SEC, has already determined what disgorgement is appropriate for Appellants with respect to the transactions at issue here, and that judgment has been accepted by a court of competent jurisdiction.

A. If This Case Is Brought To Benefit AIG Or Its Shareholders, NYAG's Claim For Disgorgement Is Impliedly Preempted By Federal Law Because It Frustrates Federal Objectives For National Standards Governing Securities Law Actions.

There is a paramount federal interest "in protecting the integrity and efficient operation of the market for nationally traded securities." *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 78 (2009). To protect that interest, Congress enacted a framework of federal securities laws intended to provide uniform standards in that area. *Lander v. Hartford Life & Annuity Ins. Co.*, 251 F.3d 101, 111 (2d Cir. 2001) (Congress enacted "SLUSA, NSMIA, and PSLRA . . . to provide national, uniform standards

[32] Unlike the Martin Act or Executive Law § 63(12), federal securities laws authorize disgorgement. *See* 15 U.S.C. § 78u(d)(3)(A)-(B); 15 U.S.C. § 78u-2(e); 15 U.S.C. § 78u-6(4); 15 U.S.C. § 7246.

for the securities markets and nationally marketed securities"); *see also Dabit*, 547 U.S. at 87 (Congress intended to create "national standards for securities class action lawsuits involving nationally traded securities" (citation omitted) (internal quotation marks omitted)). Indeed, the legislative history of the federal securities laws demonstrates the congressional desire to designate the federal government as the "exclusive regulator" of the national securities markets. H.R. Rep. No. 104-622, at 16. Congress did this to eliminate the "dangers of maintaining differing federal and state standards of liability for nationally-traded securities." S. Rep. No. 105-182, at 3 (noting that no single state should "impose the risks and costs of its peculiar litigation system on all national issuers" (internal quotation marks omitted)).

As stated in the legislative history of the National Securities Markets Improvement Act of 1996 ("NSMIA"): "The legislation preempts authority that would allow the States to employ the regulatory authority they retain to reconstruct in a different form the regulatory regime for covered securities that Section 18 has preempted." H. Rep. No. 104-622, at 34. Accordingly, NSMIA preempts state Blue Sky Laws, such as the Martin Act, except for

"enforcement actions" "with respect to fraud or deceit." 15 U.S.C. § 77r(c)(1).[33]

NYAG here seeks to encroach on the federal securities regulatory framework and obstruct the Congressional intent by applying state law standards that are easier to overcome than federal law standards. (*See* R. 504) ("Simply put, the Attorney General brings these cases to recover damages suffered by many, sometimes tens of thousands or more, investors. The actions are not duplicative of similar class actions *brought under different* [*federal*] *statutes imposing higher standards of proof.*" (emphasis added)). The United States Supreme Court has specifically cautioned against parallel cases proceeding under different evidentiary standards. *Dabit*, 547 U.S. at 86-87 ("That prospect, which exists to some extent in this very case, *squarely conflicts with the congressional preference for 'national standards for securities class action lawsuits involving nationally traded securities.'*" (footnote omitted) (emphasis added)); *accord Guice v. Charles Schwab & Co.*, 89 N.Y.2d 31, 48 (1996). This Court should not permit

[33] Earlier this month, a New York federal court struck down an attempt to improperly encroach into regulated areas. *N.Y. Bankers Ass'n v. City of New York*, No. 1:15-cv-04001-KPF, 2015 WL 4726880 (S.D.N.Y. Aug. 7, 2015). In that decision, the court ruled that a law passed by the New York City Council in 2012 – The Responsible Banking Act ("RBA") – infringed on state and federal regulatory powers and was preempted. The court found that the RBA's authorization to collection data and information and use that information to influence the behavior of the banks was preempted as an impermissible attempt to regulate within an area already occupied by federal and state laws. *Id.* at *24, *29-32.

NYAG to pursue a case that would lead to such a federal-state conflict here.[34]

B. NYAG's Claim For Injunctive Relief Is Preempted By The Supremacy Clause Of The United States Constitution.

NYAG's claim for injunctive relief also is preempted by federal law. Unlike the Martin Act or Executive Law § 63(12), the Securities Act of 1933 ("Securities Act") and Securities Exchange Act of 1934 ("Exchange Act")

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[34] To the extent that NYAG continues to pursue disgorgement as a proxy for money damages on behalf of the AIG investors that NYAG previously claimed to represent, the pursuit of those private interests directly conflicts with the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), Pub. L. No. 105-353, 112 Stat. 3227, which prohibits any lawsuit in which "damages are sought on behalf of more than 50 persons" or "one or more named parties seek to recover damages on a representative basis." 15 U.S.C. § 78bb(f)(5)(B)(i)(I)-(II).

The mere fact that NYAG is the nominal plaintiff would not inoculate the suit from preemption by SLUSA. When a State acts to "pursue the interests of a private party," courts recognize that "the State is no more than a nominal party" and the private party or parties on whose behalf the State is suing is the "real party in interest." *Alfred L. Snapp & Son, Inc. v. Puerto Rico*, 458 U.S. 592, 602 (1982); *see also, e.g.*, *In re Baldwin-United Corp.*, 770 F.2d 328, 340-42 (2d Cir. 1985) (the real parties in interest were the "plaintiffs-investors in the federal action," not the state attorneys general); *State v. Operation Rescue Nat'l*, 80 F.3d 64, 71-72 (2d Cir. 2012); *accord Pennsylvania v. New Jersey*, 426 U.S. 660, 665-66 (1976). And where, as here, the real parties-in-interest may be the private beneficiaries of any recovery by the State, *see supra* Argument Section IV.B, courts apply the standards applicable to a suit directly litigated by those private parties. *See Louisiana ex. rel. Caldwell v. Allstate Ins. Co.*, 536 F.3d 418, 428-29 (5th Cir. 2008); *see also Ohio v. GMAC Mortgage, LLC*, 760 F. Supp. 2d 741, 750 (N.D. Ohio 2011). If NYAG has no sovereign or quasi-sovereign interest in this action, but rather brought this action on behalf of private parties, who are the real parties in interest, then this suit is preempted. *See Seneci*, 817 F.2d at 1017; *see also Pennsylvania v. Mid-Atl. Toyota Distrib., Inc.*, 704 F.2d 125, 129-30 (4th Cir. 1983).

Nor would this suit fall within the SLUSA exclusion for state "enforcement" actions, 15 U.S.C. § 77p(e), as a suit advanced on behalf of private interests is not considered an enforcement action. *See Seneci*, 817 F.2d at 1017 ("Where the complaint only seeks to recover money damages for injuries suffered by individuals, the award of money damages will not compensate the state for any harm done to its quasi-sovereign interests"); *cf. In re Exxon Valdez*, 1993 WL 735037, at *2 (D. Alaska, July 8, 1993).

expressly authorize courts to bar offenders from serving as either officers or directors upon application by the SEC. *See* 15 U.S.C. § 78u(d)(2). The Acts further prevent enforcement of a state regulatory scheme that "directly or indirectly prohibit[s], limit[s] or impose[s] conditions" on the offer or sale of a covered security. 15 U.S.C. § 77r(a)(3). New York thus may not impose forward-looking injunctive relief that does not remedy past harm and that would burden issuers of securities. This Court's prior decisions recognize this distinction. *See Lexington Sixty-First Assocs.*, 38 N.Y.2d at 595.

NYAG seeks a far-reaching permanent injunction with no nexus to the conduct alleged,[35] a demand which would impose substantive state regulatory obligations on national issuers of public securities. This conflict with the federal securities regulatory scheme is particularly relevant where, as here, the SEC has considered these very Appellants and transactions and concluded that no director and officer bar was appropriate for Mr. Greenberg and that only a limited (and now-expired) bar was appropriate for Mr. Smith. (R. 36, 86-97, 99, 102-16.)

[35] NYAG seeks a permanent injunction barring Appellants from: (a) serving as directors or officers of a public company, which they have not done for over a decade and have sworn they have no intention of doing; and (b) selling securities to members of the public, which they have never done and have sworn they have no intention of doing. (R. 37, 100.)

The federal securities regime also comprehensively addresses reporting requirements for public companies. *See* Regulation S-K, 17 C.F.R. pt. 229 (2013). In particular, federal regulations set out what information must be disclosed regarding executive officers and candidates for the board of directors of public companies, including disclosure of any involvement by those individuals in regulatory enforcement litigation. *See id.* § 229.401 (2013). In circumstances where the SEC concludes that disclosure is insufficient, because an individual is "unfit" to serve in such a capacity, the agency has the express legislative authority to seek a bar order forbidding an individual from serving as a director or officer. *See* 15 U.S.C. § 77t(e) (authorizing director and officer bar for violations of 15 U.S.C. § 77q(a)(1) (Section 17(a) of the Securities Act)); *id.* § 78u(d)(2) (authorizing director and officer bar for violations of 15 U.S.C. § 78j(b) (Section 10(b) of the Exchange Act) and rules promulgated thereunder).

By seeking an order barring Appellants from serving as officers or directors of a public company or from participating in the securities industry, NYAG seeks to frustrate the carefully crafted scheme that Congress devised. Accordingly, the injunctive relief NYAG seeks in this action is barred by the Supremacy Clause of the United States Constitution. U.S. Const. art. VI, cl. 2.

VII. THE COURTS BELOW ERRED BY FAILING TO RECOGNIZE THAT THE BURDEN OF PROOF HAD SHIFTED FROM APPELLANTS TO NYAG, WHO AS PLAINTIFF WILL HAVE THE BURDEN OF PROOF AT TRIAL.

While the movant has the initial burden of proof on a summary judgment motion, *GTF Marketing, Inc. v. Colonial Aluminum Sales, Inc.*, 66 N.Y.2d 965, 967 (1985), after the initial burden is satisfied, the burden shifts, and the opponent of the motion must come forward with admissible evidence to rebut the *prima facie* showing that the claim has no merit. *Ramos v. Howard Indus., Inc.*, 10 N.Y.3d 218, 224 (2008); *Alvarez v. Prospect Hosp.*, 68 N.Y.2d 320, 326-27 (1986). *See supra* Argument Section I.

As shown below, the Appellate Division's failure to find that Appellants made a *prima facie* showing of their right to summary judgment – thereby shifting the burden to NYAG – will, unless reversed, result in a lengthy and unnecessary trial in which NYAG cannot prevail on its claims for disgorgement and permanent injunctive relief.

A. Although Appellants Demonstrated The Absence Of Any Issues Of Material Fact Concerning NYAG's Disgorgement Claim, The Appellate Division Incorrectly Concluded That The Burden Had Not Shifted To NYAG.

In their motion for summary judgment, Appellants demonstrated that NYAG cannot prevail on its claim for disgorgement because there is no

evidence to support a causal link between the two transactions remaining at issue in this litigation and any bonuses received by Appellants. *See* Statement of the Case III.A.

In response, NYAG did not submit any evidence, but suggested instead that if NYAG establishes liability at trial, it should *then* be entitled to take discovery to establish a nexus between liability and its disgorgement claim. (R. 327.) But that argument fails because discovery in this matter closed long ago and the motion court denied NYAG's application to bifurcate the trial. (R. 566-67.) The Appellate Division appeared to incorrectly assume that discovery was still open, noting that it would have been appropriate for the motion court to have granted a protective order precluding discovery relating to the disgorgement remedy "prior to an adjudication of liability." (R. 588.) However, all discovery (with limited inapplicable exceptions) closed in 2009. The "Certificate of Readiness for Trial" filed by NYAG as part of its Note of Issue on January 20, 2011 expressly affirmed that "discovery proceedings now known to be necessary" had been completed (R. 168), and NYAG's counsel affirmed in submitting the Note of Issue that "[a]ll applicable discovery orders have been complied with." (R. 169.)

NYAG also argued that in order to prevail on summary judgment, Appellants were required to disprove that their bonuses resulted from the alleged fraudulent transactions. That is incorrect. NYAG had the burden to rebut Appellants' *prima facie* showing by demonstrating the existence of an issue of fact as to the causal connection between the bonuses received by Appellants and the challenged conduct. *See Prospect Plaza Tenant Ass'n v. N.Y.C. Hous. Auth.*, 11 A.D.3d 400, 401 (1st Dep't 2004) (unjust enrichment claim failed on motion to dismiss where there was not "even a perfunctory showing as to what benefit was conferred upon defendant"). NYAG failed to meet its burden in this regard by failing to produce any evidence connecting Appellants' bonuses to the allegedly improper conduct.

NYAG's failure to proffer evidence in opposition to Appellants' summary judgment motion should have resulted in the entry of judgment dismissing the action. *See Ramos*, 10 N.Y.3d at 224; *Alvarez*, 68 N.Y.2d at 326-27; *IDX Capital, LLC v. Phoenix Partners Grp. LLC*, 19 N.Y.3d 850, 851-52 (2012) (affirming a grant of summary judgment because the opponent "failed 'to produce evidentiary proof in admissible form sufficient to establish the existence of material issues of fact'"); *Brandy B. v. Eden Cent. Sch. Dist.*, 15 N.Y.3d 297, 302 (2010) ("Summary judgment *must* be granted if the proponent makes 'a prima facie showing of entitlement to

judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact,' and the opponent fails to rebut that showing" (emphasis added)); *Ferluckaj v. Goldman Sachs & Co.*, 12 N.Y.3d 316, 319 (2009) (granting summary judgment to defendants where "no evidence in the record" supported plaintiff's theory).

The Appellate Division erred in ruling that Appellants had failed to make a *prima facie* showing "demonstrating the lack of incentive compensation paid to defendants as a result of the sham transactions . . . ." (R. 587-88.) That holding improperly reversed the burden of proof on a summary judgment motion by ignoring NYAG's admission that it had no evidence to support its disgorgement claim, thereby requiring Appellants to affirmatively prove a negative.[36]

The sole case relied on by the Appellate Division to support its holding that Appellants failed to satisfy their *prima facie* burden, *William J. Jenack Estate Appraisers & Auctioneers, Inc. v. Rabizadeh*, 22 N.Y.3d 470

[36] The Appellate Division ignored its own precedent that a summary judgment movant does not have to prove a negative to make a *prima facie* showing on a motion for summary judgment. *See, e.g., Martinez v. Hunts Point Coop. Mkt., Inc.*, 79 A.D.3d 569, 570-71 (1st Dep't 2010) ("[O]ur jurisprudence does not 'require a defendant [moving for summary judgment] to prove a negative on an issue as to which [it] does not bear the burden of proof." (second and third alterations in original)); *Strowman v. Great Atl. & Pac. Tea Co., Inc.*, 252 A.D.2d 384, 385 (1st Dep't 1998) ("He is not, as the dissent holds, required 'definitively [to] deny actual or constructive notice of the banana peel.' Such a requirement would, in effect, require a defendant to prove a negative on an issue as to which he does not bear the burden of proof." (alteration in original)).

(2013), actually supports a finding that Appellants did, in fact, meet their *prima facie* burden. In that case, this Court held that "To successfully establish his entitlement to summary judgment," the movant "must show that the record is bereft of documentation" substantiating plaintiff's claim. *Id.* at 475-76. Here, Appellants satisfied the *Rabizadeh* standard by demonstrating that the record is "bereft" of evidence establishing a causal connection between Appellants' bonuses and the acts complained of.

Moreover, shifting the trial burden on to Appellants defeats the goals of the summary judgment procedure. *See Andre v. Pomeroy*, 35 N.Y.2d 361, 364 (1974) ("[W]hen there is no genuine issue to be resolved at trial, the case should be summarily decided, and an unfounded reluctance to employ the remedy will only serve to swell the Trial Calendar and thus deny to other litigants the right to have their claims promptly adjudicated.").

Indeed, placing an elevated burden on a moving defendant at the summary judgment phase contravenes the goal of the CPLR "to secure the just, speedy and inexpensive determination" of actions. CPLR 104. *Cf. Janos v. Peck*, 21 A.D.2d 529, 531 (1st Dep't 1964) ("Broad and liberal use of the partial summary judgment procedure is in furtherance of the general objectives of CPLR."), *aff'd*, 15 N.Y.2d 509 (1964). As this Court has made clear: "The burden of a party moving for summary judgment is to 'make a

prima facie showing of entitlement to judgment as a matter of law.' *The moving party need not specifically disprove every remotely possible state of facts on which its opponent might win the case*." *Ferluckaj*, 12 N.Y.3d at 320 (emphasis added) (citation omitted). The burden then shifts to the other party "to produce evidentiary proof . . . sufficient to establish the existence of material issues of fact."[37] *Id*. (omission in original) (internal quotation marks omitted).

As defendants in this action, Appellants do not bear the burden at trial, and satisfied their *prima facie* burden by demonstrating that, after discovery had been closed and a Note of Issue was filed by NYAG certifying that all discovery "now known to be necessary" had been completed (R. 168), the Solicitor General acknowledged to this Court that NYAG had no evidence to support its claim for disgorgement. (R. 222-24.) The burden should then have shifted to NYAG to produce *some* evidence that its disgorgement claim can be sustained at trial, by demonstrating a causal connection between the two transactions at issue and the bonuses that NYAG seeks to disgorge.

[37] Where a motion for summary judgment is made by the party without the burden of proof on the issue at trial, the motion "without more, [should put] an opposing party with the burden of proof to the task of producing evidence sufficient to sustain a favorable verdict." David P. Currie, *Thoughts on Directed Verdicts and Summary Judgments*, 45 Univ. Chi. L. Rev. 72, 29 (1977).

Because NYAG failed to produce any such evidence, Appellants should have been granted summary judgment on NYAG's claim for disgorgement.

B. Although Appellants Demonstrated The Absence Of Any Issues Of Material Fact Concerning The Availability Of Injunctive Relief, The Appellate Division Incorrectly Concluded That The Burden Had Not Shifted To NYAG.

As with disgorgement, Appellants made a *prima facie* showing that NYAG could not establish a claim for permanent injunctive relief. Under New York law, a claim for permanent injunctive relief is moot where there is no genuine threat of irreparable harm or reasonable expectation the alleged wrong will recur. *See Mallinckrodt v. Barnes*, 272 A.D.2d 651, 652-53 (3d Dep't 2000) (injunctive relief claim was moot where it was "entirely likely that these circumstances will not recur") (Graffeo, J.); *see also State v. N.Y.C. Conciliation & Appeals Bd.*, 123 Misc. 2d 47, 48 & n. 2 (Sup. Ct. N.Y. County 1984) (same). Appellants demonstrated on summary judgment that there is no likelihood of irreparable harm and no reasonable expectation that Appellants will engage in any future wrongdoing. *See supra* Statement of the Case Section IV.

This evidence makes a *prima facie* showing that there is no reasonable possibility of harm that would justify a permanent injunction against Appellants. *See supra* Argument Section V.C. *See also, e.g., SEC v. Brown*, 878 F. Supp. 2d 109, 119 (D.D.C. 2012) (granting defendant summary

judgment on SEC's motion for injunctive relief where SEC did not adduce any evidence defendant was "seeking employment in securities-related positions or that she [was] currently or prospectively capable of committing any securities violations").

NYAG has not produced any competent evidence contradicting Appellants' evidence, let alone evidence sufficient to create a triable issue of material fact. NYAG submitted only a single affidavit by one of NYAG's trial counsel that offered solely baseless press speculation about possible future conduct by Appellants. (R. 332-35.) Such speculation is insufficient to satisfy NYAG's burden in opposing Appellants' summary judgment motion. *See Alvarez*, 68 N.Y.2d at 327 ("neither is that burden met by the unsubstantiated assertions or speculations of plaintiff's counsel that a defendant may have breached a possible duty of care"); *GTF Mktg.*, 66 N.Y.2d at 967-68 (attorney affidavit insufficient to resist summary judgment); *Breytman v. Olinville Realty, LLC*, 46 A.D.3d 484, 486 (1st Dep't 2007) (speculation not sufficient to raise a triable issue).[38]

[38] Moreover, at oral argument in the motion court on Appellants' summary judgment motion, NYAG effectively conceded it cannot meet the normal requirements for permanent injunctive relief. NYAG argued that a permanent injunction is necessary solely because Appellants have failed to show "contrition," and not because NYAG has satisfied the traditional equitable grounds for a permanent injunction. (R. 557-59.) This unprecedented position is unsupported by New York law and is in tension with basic constitutional principles.

As with Appellants' disgorgement claim, the Appellate Division held without analysis that Appellants failed to "demonstrate conclusively" that an injunction was not warranted "under the circumstances." (R. 588.) The Appellate Division failed to recognize that the burden had shifted from Appellants to NYAG, and posited the existence of issues of fact as to the "imminence of harm," even though NYAG had not submitted any evidence on that subject. (R. 588.) The Appellate Division thus again effectively shifted the burden of proof to Appellants to prove a negative, rather than requiring NYAG to provide evidence to support its case.

In evaluating whether a movant has presented a *prima facie* case, this Court considers the proof each party is reasonably expected to produce at trial and counsels against demanding proof that cannot be provided. *Travelers' Ins. Co. v. Pomerantz*, 246 N.Y. 63, 69 (1927). Appellants here have done all they can be expected to do, by presenting sworn affidavits that NYAG failed to rebut, thereby satisfying their burden of establishing a *prima facie* case.

CONCLUSION

Appellants respectfully request that this Court enter summary judgment in Appellants' favor and dismiss this action. In the alternative, this Court should reverse the decisions below and remand the action to the motion court with a direction to follow the procedure set forth in this Court's June 25, 2013 Order by reviewing the evidence submitted on summary judgment and issuing a new decision considering that evidence.

Dated: New York, New York
August 21, 2015

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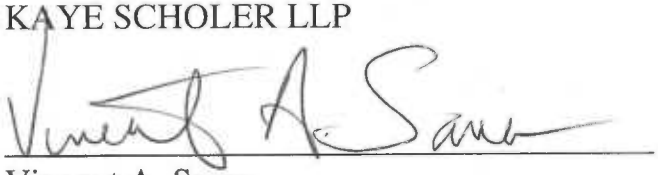

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ADDENDUM

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: JEFFREY K. OING J.S.C. Justice

PART 48

Index Number : 451586/2010
PEOPLE OF THE STATE OF NEW
vs
ERNST & YOUNG LLP
Sequence Number : 002
DISMISS

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____

The following papers, numbered 1 to _____, were read on this motion to/for _____

Notice of Motion/Order to Show Cause — Affidavits — Exhibits _____ | No(s). _____
Answering Affidavits — Exhibits _____ | No(s). _____
Replying Affidavits _____ | No(s). _____

Upon the foregoing papers, it is ordered that this motion is

"Motion is decided on the record.
Transcript to be So Ordered.
Parties to submit transcript
to the Court forthwith."

Movant directed to order
the transcript & bear the costs.

Δ to move/answer pursuant to
the directives set forth on
the record.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
FOR THE FOLLOWING REASON(S):

Dated: 12/12/12

JEFFREY K. OING, J.S.C.
J.S.C.

1. CHECK ONE: ..... ☐ CASE DISPOSED ☒ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: .....MOTION IS: ☐ GRANTED ☐ DENIED ☐ GRANTED IN PART ☒ OTHER
3. CHECK IF APPROPRIATE: ..... ☐ SETTLE ORDER ☐ SUBMIT ORDER
☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: CIVIL TERM PART 48

- X

THE PEOPLE OF THE STATE OF NEW YORK by ERIC T. SCHNEIDERMAN, Attorney General of the State of New York,

Plaintiff,

- against -

INDEX NUMBER: 451586/10

ERNST & YOUNG LLP,

Defendant.

- X

60 Centre Street
New York, New York
December 12, 2012

BEFORE:

HONORABLE JEFFREY K. OING, Justice.

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Margaret Baumann
Official Court Reporter

Proceedings

THE COURT: Court has before it the matter of the People of the State of New York versus Ernst & Young, Index Number 451456 of 2012.

This is defendant's Motion Sequence Number 2 which is a motion, it's a very limited motion. It is a motion seeking to dismiss that part of the plaintiff's damages seeking disgorgement of profits as a result of the underlying transaction heard in this case.

Parties, enter appearances for the record.

For the plaintiff.

MR. ELLENHORN: For the plaintiff, David Ellenhorn, of the Attorney General's office, Mr. Morian, Ms. Trakht are two of my colleagues with me. I will be arguing.

THE COURT: For the defendant.

MR. RUTHBERG: Miles Ruthberg, for the defendant, and also I have some of my colleagues here.

THE COURT: Terrific.

Okay. This is your motion to dismiss this disgorgement claim, and let me just get the complaint for one second.

There are in this complaint four causes of action, and just to set them out.

The first cause of action is under the Martin Act Securities Fraud, General Business Law Sections 353 to 353.

The second cause of action is also Martin Act

Securities Fraud, General Business Law Section 352-c.

The third cause of action is the Martin Act Securities Fraud, General Business Law Section 352-c.

And the fourth cause of action is for Persistent Fraud and Illegality, Executive Law Section 63.

And, the bone of contention here is in the wherefore clause where they are seeking disgorgement, right, and you are looking to get rid of that branch of the damages.

So, tell me why I should dismiss that.

MR. RUTHBERG: Yes, sir, thank you.

The complaint in this case, your Honor, attempts to go beyond the ample remedies that are provided on the face of the Martin Act in the Executive Law. Those statutes expressly provide for injunctive relief, damages and restitution. And, the complaint here seeks all of those.

But, the complaint also goes beyond that and seeks disgorgement, and that is not provided in the statutes and it should be dismissed.

The result is compelled by the New York Statutory Construction Law. At some level this motion is actually quite simple, your Honor, and it would also be helpful to your Honor, but we attempted to boil down the extensive authorities that are cited, both sides, to this very small notebook, which is the authorities cited in the briefs that

we think are the most helpful and dispositive.

THE COURT: Let me ask you a question.

They claim in their complaint there, Ernst & Young, in Paragraph 5, which reaped over $150 million in fees from Lehman must be held accountable for its role in this fraud.

And, then they go on say in Paragraph 71, E&Y permitted Lehman to engage in an accounting fraud while reaping over $150 million in fees. Ernst & Young as a purported independent auditor was obligated instead to insure that Lehman's financial statements disclose the Repo 105 transactions. Financial statements said not a word about Repo 105 falsely represented that Lehman was treating all Repo transactions as financing, and Ernst & Young accordingly must be held accountable for the consequences of this fraud.

Let me ask you a question, that $150 million, where did that money come from? Was that, is it a fee for the services you rendered, or was that part of an investment that you were sort of getting money as an investor or some sort of stakeholder?

MR. RUTHBERG: That's the key point, your Honor. It came from Lehman. The alleged foster. It did not come from consumers. It did not come from investors.

THE COURT: Or from the State. Did it come from the State?

MR. RUTHBERG: It did not come from the State.

THE COURT: You know where I'm going with this question then?

MR. RUTHBERG: Yes, sir.

And so restitution does not fit here very easily, and I think the Attorney General recognizes that, and has sought damages, and has sought extensive damages, your Honor.

THE COURT: Yes.

MR. RUTHBERG: Very extensive damages. So, it is not a case where the Attorney General does not have a form of relief provided by the legislature which is quite significant.

And, our point, your Honor, is that under the maxim of expressio unius est exclusio alterius, the case is actually quite simple.

The legislature has expressly provided for certain remedies, including the equitable remedy of restitution by the way expressly provided for that.

THE COURT: The biggest part is the injunctive relief aspect.

MR. RUTHBERG: Yes, sir.

THE COURT: But no where in the statute in the General Business Law that we're talking about is there a disgorgement provision.

However, the courts have held that disgorgement may be possible in limited circumstances, and that is when the consumers have put in money, investors have put in money or the State has put in money. That is where disgorgement may be probable or possible in those circumstances. Okay.

MR. RUTHBERG: Yes, sir. And, that's where it overlaps with restitutionary principles, and that's really the thrust of the statute on its face.

THE COURT: Got it. Thank you. Yes.

MR. RUTHBERG: I'm sorry, your Honor?

THE COURT: I got it, great. Thank you.

Is there anything else?

MR. RUTHBERG: I would just point your Honor to the language of the statute. Your Honor is already obviously extremely well prepared. I won't waste your time.

THE COURT: Thank you.

MR. RUTHBERG: And, perhaps, I should sit down at this point.

THE COURT: If you want to respond, I will let you respond.

MR. RUTHBERG: Thank you, your Honor.

THE COURT: Counsel, I mean, the two cases that I am looking at they are really compatible because I know each side cited the case separately. The one side cited one case; the other side cited the other case. When I read

it, they are compatible.

And, one of them is the People of the State of New York by Elliot Spitzer vs. Direct Revenue, and that is 19 Misc. 3d 1124A, and then the other case, Matter of People vs. Applied Card System, 11 NY3d 105, by the Court of Appeals in 2008. The first case is by Justice Cahn and that was in 2008.

And they are really compatible because they're saying -- although Justice Cahn said that there is no disgorgement, he actually said why there was no disgorgement. He said, disgorgement, there is no allegations in the complaint that the respondent received anything of value from the petitioner or consumers.

And that, and that he goes on -- excuse me.

The statutes do not authorize general disgorgement of profits received from sources other than the public.

And the Court of Appeals basically said the same thing when it said that the Martin Act protects consumers and the State. It does not protect -- and if the State is starting to collect money or recover money, and Justice Cahn says this:

If the State is trying to recover money, it becomes punitive in a sense because there was no state money involved, and any money you collect on a disgorgement principle theory is punitive in that regard.

Proceedings

So, why shouldn't I grant this motion to dismiss the disgorgement claim?

MR. ELLENHORN: You are running against centuries of law as as follows.

THE COURT: Oh --

MR. ELLENHORN: As follows, as follows:

It is absolutely well established that in a fraud case, whether it's a consumer fraud or security fraud or whole range of other cases where the Court has the power to grant equitable relief, which it does here --

THE COURT: Yes, no doubt.

MR. ELLENHORN: -- it has an inherent power to cause the defendant to receive money that the defendant received through fraudulent practices or for other reasons or ill-gotten gains to disgorge that money to the State or a plaintiff, and I have never seen a case that made the distinctions or imposed the kind of limitations certainly, no authoritative case, centuries of other cases that you are suggesting exists.

Now let me go on, please.

THE COURT: Okay.

MR. ELLENHORN: This is very fundamental to the powers of this office.

THE COURT: I am not discounting that.

MR. ELLENHORN: I understand that, and I can't

decide that case, but you shouldn't decide that case based on one line in one decision that is against all the law in this State and the United States.

Disgorgement is not a penalty. The courts have universally said that disgorgement is not -- Judge, please let me make my argument.

THE COURT: I just have a question.

Go ahead, finish then.

MR. ELLENHORN: Go ahead, I'll answer your question.

THE COURT: I was going to say what monies did the State expend? What monies did Ernst & Young get from the State?

MR. ELLENHORN: Didn't get any monies from the State.

THE COURT: Okay.

MR. ELLENHORN: And that's completely irrelevant.

THE COURT: Okay. What monies did Lehman -- did Ernst & Young get from consumers and the public?

MR. ELLENHORN: This is not a consumer fraud case. It's a securities fraud case.

THE COURT: Isn't the Martin Act designed to protect consumers and the public?

MR. ELLENHORN: The Martin Act is designed and, in fact, does protect the public. It's an anti-securities

fraud. It's a Blue Sky law, and it entitles the government where there has been a securities fraud to obtain a variety of forms of relief.

One is damages to the victims. The people who invested in Lehman based on what we claim are false financial statements, which were certified wrongly by the defendant. That is one form of relief.

THE COURT: Damages to the victim, or damages to the victims.

MR. ELLENHORN: Yes, damages to the victim.

One form -- let's leave aside injunctive relief.

Another form of relief is penalties, which are very minimal or limited by statute.

THE COURT: Like $2,000.

MR. ELLENHORN: It's not much. It's not what this case is about.

THE COURT: It's a hand slap.

MR. ELLENHORN: It's not what the case is about.

And, the third, which is not listed in the statute and clearly does not have to be, but for centuries courts have issued disgorgement relief in federal court, state court, securities cases, consumer where it is not listed in the statute.

THE COURT: In those cases that you are relying on centuries of cases --

MR. ELLENHORN: Right.

THE COURT: -- where disgorgement was proper, and I think I looked at it, those cases involve situations where consumers actually suffered a loss, or they were actually participating, or the state put in money and actually was recovering money for the state.

There is no cases that I saw that had a situation where, in this complaint that you have here that I'm looking at, where there is no allegation where the money that they claimed to have gotten, Ernst & Young, the $150 million in fees, was somehow tied to the investors putting money into Lehman or somehow tied to any other consumer putting money into it because the allegations, and I read the complaint.

MR. ELLENHORN: What you're saying is correct.

THE COURT: Thank you.

MR. ELLENHORN: But, with all due respect, you are making the same -- you are possibly making the same error I believe was made in the one case they are relying on, and that is confusing.

THE COURT: So, the centuries of cases that you are relying on, you're saying that my reading of the facts are pretty okay.

MR. ELLENHORN: I can't say every case you've read, but what I'm saying is the following.

You are confusing, with all due respect,

restitutionary damages, which is designed to make a victim whole. People invested in Lehman stock. They were injured they are entitled to damages.

THE COURT: But the State was not an investor.

MR. ELLENHORN: The State that has nothing to do with it, with all due respect. Actually the State --

THE COURT: Counsel, that phrase doesn't really turn me on, with all due respect.

MR. ELLENHORN: I apologize.

The State may or may not have been an investor through a state pension plan.

THE COURT: Okay.

MR. ELLENHORN: Disgorgement serves a different purpose. It's clearly delineated.

THE COURT: I'm glad you said that because I didn't see that in the papers here. If, in fact --

MR. ELLENHORN: I think it is.

THE COURT: If, in fact, there is a pension plan that is involved here, you're saying that the State invested, had a pension plan that invested in Lehman.

MR. ELLENHORN: I don't know. It may have.

THE COURT: Don't say something you don't --

MR. ELLENHORN: We're not relying on it.

THE COURT: Don't say that if you don't know. That's a critical fact then that may change the dynamics of

this.

MR. ELLENHORN: I don't know.

THE COURT: Okay.

MR. ELLENHORN: I believe it's likely. I don't think it's a critical fact. I don't think it's relevant. If it's relevant to your Honor, and it seems to be, and we need to determine whether the State was a victim or an investor, we will do so, but that is not the theory of our case.

We are not suing on behalf of the State to get money for the State because it may have lost money in Lehman. Disgorgement is a remedy that is designed to prevent the wrongdoer from obtaining ill-gotten gains. Please, that is the purpose of it.

And the cases are clear, many of them are in the federal courts, under analogous laws, federal securities law, which the courts have routinely issued disgorgement orders even against Ernst & Young, and this goes to your points you raised, the courts have said, that that money is being disgorged.

THE COURT: All right.

MR. ELLENHORN: That money is being disgorged if I may, not, not to compensate the victims whether they be -- whoever they may be, not to punish the defendant as a statutory penalty, but to, as an incentive to prevent people

from wrongdoing.

In other words, you got money you shouldn't have gotten. You are going to have to disgorge it. And, the courts have laid out in case after case, mostly many federal securities cases directly analogous here, and having said that, where that money goes will be decided by the judge or the SEC or the Attorney General's office.

THE COURT: You see, that's the problem. If you get a disgorgement claim -- if I let it go forward and you prevail and you get a disgorgement claim, you are asking the Court to decide where the money goes.

What if, at the end of the day, it doesn't go anywhere?

MR. ELLENHORN: Well, first of all --

THE COURT: What happens then?

MR. ELLENHORN: It has to go somewhere.

THE COURT: What if at the end of the day there is a situation where we find out the consumers aren't effected by what happened, these investors aren't effected by what happened, and ultimately there is nobody to give the money to.

MR. ELLENHORN: Yes, there is.

THE COURT: Who then?

MR. ELLENHORN: The State Treasurer. That's exactly what I am saying.

Proceedings

It doesn't mean the State was a victim.

THE COURT: That becomes punitive. It's not disgorgement.

MR. ELLENHORN: That's not what the case law says.

THE COURT: You could take that position, fine.

MR. ELLENHORN: That's not what the case law says.

THE COURT: I'm not going to argue about it. That is fine.

MR. ELLENHORN: It isn't what the case law says. The case law makes it very clear. I want to talk about Applied Card for a moment.

Applied Card was an extremely important case to this office. It was in the New York Court of Appeals, it was litigated at great length, and that case dealt with the powers of this office under the Martin Act and the Executive Law. That is what the case was all about.

THE COURT: It was preemption case.

MR. ELLENHORN: It was many things.

THE COURT: It primarily --

MR. ELLENHORN: It was --

THE COURT: -- a preemption case.

MR. ELLENHORN: Well, this is the way we viewed the case. What was important about that case was this, we deal with this every day, and it's going to play and animate this entire litigation no matter what happens.

Proceedings

THE COURT: Right.

MR. ELLENHORN: In that case, a settlement had been reached in an a class action --

THE COURT: Correct.

MR. ELLENHORN: -- in which money was available for the investors. There is a pending federal class case here before Judge Kaplan. Okay.

Now, what the Court of Appeals held was that where the federal class action was settled, and the investors released the defendants, the New York Attorney General's office was, therefore -- I don't the word is preemption, but were, therefore, bound by principles of res judicata, we couldn't get money from the people because they had already settled with the plaintiffs.

THE COURT: The Court of Appeals said, that's not accurate, you can do that. Court of Appeals allows you to do what you did.

MR. ELLENHORN: This is what I'm saying, Judge, the Court of Appeals says we cannot get money for the victims who have been satisfied and given relief.

THE COURT: Right.

MR. ELLENHORN: But, the Court goes on to say that, as an exercise of the equity powers, the court may order wrongdoers to disgorge their fraudulently obtained profits, and it doesn't say the New York Court of Appeals is saying

that we could get disgorgement.

THE COURT: Wait a minute, you just quoted a phrase, "the court may order wrongdoers to disgorge their fraudulently obtained profits."

MR. ELLENHORN: Yes.

THE COURT: Did you know you just quoted a federal court?

MR. ELLENHORN: I'm quoting the New York Court of Appeals quoting a federal court.

THE COURT: Thank you. Because it wasn't really quoting. What they did was they put is as a "see," and said right here, Compare CF, Securities and Exchange Commission vs. Fischbach Corporation, 133 F 3d, 170 at 175 Second Circuit 1997, and they quoted that language that you cited.

But, before that language, there was this whole paragraph that they put in, and I'll read it for the record:

"Our holding does not, however, substantially prejudice the public interest served by the Attorney General in pursuing this action. Indeed, respect for the finality of the *Allec* settlement," which you have mentioned, "still permits the Attorney General to seek restitution on behalf of those not bound by the settlement and for the time periods not embraced therein."

Clearly, that's right on point.

"In addition, the claims for injunctive relief,

civil penalties, and costs remain undisturbed. And, as Supreme Court noted, the Attorney General might be able to obtain disgorgement, an equitable remedy distinct from restitution of profits that respondents derive from all New York consumers whether within the *Allec* settlement class or not."

MR. ELLENHORN: Yes.

THE COURT: Again I ask you, who are the consumers in this case in your complaint that you have alleged have been harmed by the acts of Ernst & Young?

MR. ELLENHORN: The people who were harmed by the actions of Ernst & Young and Lehman where hundreds of thousands of investors in Lehman stock.

THE COURT: Counsel, that would be fine, but if you had made that allegation, and the allegations could have taken the form of Ernst & Young which reaped over $150 million in fees that were derived from investors and consumers putting money in Lehman because of the misleading financial statements that generated such huge amounts such that Ernst & Young can earned $150 million, that would be a different story. I don't have those allegations.

MR. ELLENHORN: I have never heard -- this case, Applied Card wasn't a consumer fraud case. There are cases, consumer fraud cases where we get disgorgement of profits, separate, and we may or may not give it to the consumers.

Proceedings

This is a securities fraud case. It's a slightly different case. If we are stripped of this power, we will have less power than the Securities and Exchange Commission under statutes that are exactly alike, and, in fact, less liberal than the Martin Act, that have the Securities and Exchange Commission that has been getting disgorgement of profits in securities fraud cases for money that wasn't necessarily paid by investors.

And they have been keeping the money in the United States Treasury or they have been giving it to the investors as a matter of discretion, and they have that discretion.

THE COURT: I understand that.

MR. ELLENHORN: No court has ever suggested that we don't have that same power.

THE COURT: You are relying on the principle then in federal court where they permit disgorgement under the Federal Securities Act, and you are asking me to use that as the basis now to extend the Martin Act --

MR. ELLENHORN: No.

THE COURT: -- beyond what it's saying.

MR. ELLENHORN: No. No, I am not.

The federal courts have -- I absolutely am not.

The federal courts have been saying for decades, literally decades, that in federal courts can order disgorgement in securities fraud cases without any statutory

authority whatsoever.

There were later some statutes adopted that used the word disgorgement. They were ordering disgorgement in comparable circumstances to this one, including by accountants before the statutes ever mentioned the word disgorgement.

THE COURT: Let me remind you and I remind the folks in the other motion I argued, I am in state court, and unless you have a Court of Appeals case from the New York State Court of Appeals that says exactly what the federal courts say, I am less inclined to agree with that statement.

MR. ELLENHORN: I understand that. But we are not talking about federal rules of procedure here.

THE COURT: I'm talking about --

MR. ELLENHORN: We're talking about power.

THE COURT: I'm talking about substantive procedure here. I'm glad you mentioned that. This is power. This disgorgement. This is nothing to take lightly. This is an extreme remedy that you are asking to pursue.

MR. ELLENHORN: I don't want to mention, I'm a little embarrassed to say this, but one of the cases we didn't bring to your attention, I just didn't think of it, I'm embarrassed, it's a case that I tried about 20 yards away here across the hall before Justice Ramos this last summer, and it was a case involving our claim for

disgorgement of certain fees that an appraising company had gotten, and it was no intention to give that money to the people who paid the money for practical reasons and many, many reasons. Justice Ramos held that we had the power to get disgorgement.

THE COURT: I am glad you mentioned that because you said something very critical. You said it was an appraisal fee, that there were consumers that actually paid fees.

MR. ELLENHORN: In that case there were.

THE COURT: So, whether or not you are going to distribute to consumers that, to me, is irrelevant.

But, the fact that there are actual bodies that have been injured as a result of the defendant's conduct is sufficient to provide disgorgement.

I don't have anything in this complaint, and I've read this complaint even though I was -- I did read it very carefully.

MR. ELLENHORN: I'm sure you did.

THE COURT: I didn't see any allegations other than Lehman and Ernst & Young having this sort of like, okay, we changed the accounting principle, now you could post these transactions as sales rather than loans so that we could look really good on our balance sheets. That we're getting rid of -- we're lowering our leverage. We're looking rosy

to investors. We're liquid and all that. But, no one knows, you know, wink-wink, that in actuality tomorrow, even though we get a hundred million dollars, tomorrow we got to pay it back with interest.

So, you know, I don't see those allegations.

MR. ELLENHORN: A couple of responses.

THE COURT: In the Ramos case you just conceded or admitted to me.

MR. ELLENHORN: I want to clarify what I said in the Ramos case.

THE COURT: I'm listening to what you're saying, that's why. Okay.

MR. ELLENHORN: The fees were actually paid by the banks which made the mortgage loans, and they were not the victims. It was a scheme by a bank and mortgage lenders and First American to render inflated appraisals which led, as you know, to the collapse of the housing market, and the fees that were being disgorged where paid by the banks, the wrongdoers, Great Western or Country Wide. They were not fees being paid by any consumers.

THE COURT: Who was paying the fees? The banks were paying the fees.

MR. ELLENHORN: The banks were directly paying the fees to First American.

THE COURT: To First American who was being sued,

right, they were the defendants?

MR. ELLENHORN: We were suing them.

THE COURT: You were suing First American?

MR. ELLENHORN: Yes.

THE COURT: In other words, there was somebody other than -- there was a consumer of sorts paying the fees. Okay. Here, in this case, Lehman is not a consumer. Lehman is sort of the -- what is the word?

MR. ELLENHORN: They're the wrongdoer.

THE COURT: I understand they're the wrongdoer, but they're paying a fee for services rendered.

In your case, it's multiple people paying these mortgage fees to First American.

MR. ELLENHORN: All I'm saying is that I don't believe the law limits. If you do, then, obviously, I am fighting against you. I don't want -- I don't enjoy that.

THE COURT: I want to hear the arguments.

MR. ELLENHORN: I am saying, yes, many of the cases -- this is an unusual case, it's the first time the Attorney General's office, I'll acknowledge that, I'm happy to acknowledge it, proud to acknowledge it, it's the first time --

THE COURT: And you walked in here. I guarantee you it's going uptown.

MR. ELLENHORN: It's the first time the Attorney

General's office probably has sued an accounting firm. It's neither here, nor there. It's a major fraud or established to be a major fraud.

Now, it's true, therefore, that many of the cases, the run-of-the-mine cases where we get disgorgement or seek disgorgement are consumer fraud cases. I'm not going to dispute that. So, what?

I don't know of any case law that says that the fundamental principle is that if someone has aided and abetted or taken part or specifically in a fraud, a securities fraud or a consumer fraud or some other financial fraud, and they have been enriched as a result of their misconduct, the court, in its discretion, depending on the facts, can order disgorgement as a way of denying them.

It is in the public interest. It is a prophylactic measure, but not deemed to be a penalty as such, but it is in the nature of a prophylactic measure. It has simply nothing to do with helping the victims.

The separate relief is sought for them. This is a discreet form of relief. It is designed to prevent unjust enrichment or people from profiting from wrongdoing.

I agree with you that many, if not most, I haven't combed them carefully, of the cases that come through the courts in which we get disgorgement involve consumers, but it's not limited to that.

Proceedings

THE COURT: Let me ask you this:

Other than disgorgement, that doesn't mean you are not going to be able to recover other monies or damages?

MR. ELLENHORN: Well, let me tell you about that because there's a very interesting subtext going on here or may be going on. It may or may not eliminate it as well.

We are seeking in the main, as I said, two types of relief. One in the main, let's leave out injunctions, penalties for the moment, which are incidental penalties.

We are seeking money. It could be hundreds of millions of dollars, if not billions, to be determined for people who invested in Lehman stock, particularly in 2007 and 2008, got severe losses. If we have to prove that, that is a fundamental part of our relief.

The second part it's severed.

Now, in the federal court, in the federal court, the private plaintiffs' class action, major class action, actually they don't have the power, the private plaintiffs don't have the power to get disgorgement under the securities laws, the SEC does. What they're seeking is money damages for the victims of the alleged fraud.

THE COURT: Right.

MR. ELLENHORN: In that sense, we're in the same shoes they're in. We are seeking additional relief disgorgement as the SEC does all the time.

Now, if they settle that case at some point -- and may settle it, I don't know, 99.9 of these cases settle, this may be the one-tenth of one percent, it isn't -- when they settle that case, if they settle that case, probably a couple of years from now, they will then, without any question, if we have not resolved our case, first by settlement or trial or whatever, they'll come in and say they may well be right.

Sorry, fellows, you have wasted your time because we have settled. Over in the federal court, you can't, under Applied Card, now get damages for the people except for a few people might opt out. All right. That's part of the life. That's what the Applied Card case was about.

But it is for that reason, among others, among others, that our ability to get disgorgement of some or all of the fees that they received in doing a non-audit, an improper audit, that we have that power and that right. That's not effected by Applied Card. In fact, it's preserved by Applied Card.

All, I could say, Judge, very respectfully -- you don't like people to say with respect -- I'm not going to say with respect.

THE COURT: Thank you.

MR. ELLENHORN: But it is with respect, I believe that my colleagues want me to say something.

Okay, I thank you.

Good suggestion. I don't want to put it that way.

THE COURT: Okay.

MR. ELLENHORN: I think when you delve a little further into the cases it becomes very clear that disgorgement is simply a different form of animal. It is designed -- it is not designed to punish in a legal sense, but it is designed to deter people who receive money they shouldn't get, and where it goes is a totally separate question.

THE COURT: Right.

MR. ELLENHORN: Whether it goes to the consumer, we could give it to the victims. I believe and the SEC has done it all the time, that we could.

THE COURT: Your time is up. That's what I was to tell you.

MR. ELLENHORN: I don't mind if you say so.

THE COURT: He's your colleague. He's telling you your time is up.

MR. ELLENHORN: He tries to do that to me in the office all the time.

THE COURT: I need to do that though.

MR. ELLENHORN: These are very serious matters.

THE COURT: Absolutely. You are right, and I think I got a handle on it.

MR. ELLENHORN: What I'm saying is the case is very clear, the federal cases are very clear, there's no reason they don't apply fully here. In fact, our courts said we look to federal cases when we're dealing with the Martin Act because they're parallel types of proceedings.

The cases are very clear that if we get disgorgement, whatever it might be, you might give us half, it becomes your decision, by the way. It's not a jury matter. That's what Judge Ramos ruled in First American, that's why we fought about disgorgement.

If you say at the end of the day, I think Ernst & Young should give back half of the fees because you did a bad audit, they did an improper audit, if you reach that conclusion, and the fair thing is for them they shouldn't profit from a fraudulent audit. Then that money can, in fact, be given to people who were victimized by this fraud. It could theoretically be given to Lehman creditors that went into bankruptcy. It could be kept by the State. That's not the issue.

THE COURT: All right. Mr. Ellenhorn, I have to cut you off.

MR. ELLENHORN: Thank you very much.

THE COURT: You want to respond briefly, counsel, very briefly.

MR. RUTHBERG: Very briefly. Just for the record,

your Honor, Mr. Ellenhorn has said that fraud has somehow been established in this case. That is what this case is about. The SEC did not seek disgorgement because there was no fraud by Ernst & Young here. And so we will, in due course, we will present to your Honor the facts on that. I am not going to, obviously, do that today. With that, I will sit down, your Honor.

THE COURT: All right.

This is my decision with respect do the defendant's motion here.

I heard the arguments here, and I know the reliance is on a lot of the federal cases with respect to disgorgement there.

There is an understanding, and I can't ignore the fact that, yes, on the federal side, disgorgement seems to be routinely a remedy that is applied against the defendant in those securities actions.

It is not to say disgorgement is not applied here in the state court. The only condition is, and I read those two cases that I have here, the People vs. Applied Card, as well as People vs. Direct Revenue.

The courts there, one Court of Appeals and one Supreme Court trial court decision, they are not saying disgorgement is not in the zone or realm of possibility. They are saying if you want disgorgement, there are going to

be conditions seeking disgorgement. One of the impacts it has to impact the consumers. There has to be some sort of showing or allegation that the consumers who are putting in money. For example, in the Direct Revenue case, there the consumers weren't putting any money in. Those were the advertisers themselves that were putting the money in. And, in the Court of Appeals case, they make the same motion that as long as you have respondents or consumers putting in money, disgorgement may be possible.

Here, in this case, and I know plaintiff's counsel is arguing that the fact that there are no consumers or no allegations in this complaint that consumers that have been impacted or the public has been impacted, that it still should not prevent a disgorgement remedy.

I disagree with that. I believe that while we are -- while the courts do look at disgorgement, it is done in the very careful and very thoughtful manner, and that is, in this case, the allegations in this complaint fail to allege anything with respect to consumers or the public at large,

Now, the argument then goes plaintiff's counsel says that we don't necessarily need to have consumers, we don't necessarily need to have the public affected. The State Attorney General is permitted to go and recover these monies on behalf of the consumers.

Proceedings

My question then becomes is where is the allegation in here that the State actually invested money or lost money as a result of the purported action or conduct of defendants. That allegation is missing too. When those allegations are not met or made, then what happens is that disgorgement remedy or vehicle that the plaintiff is seeking and if they actually prevail, it becomes a penalty. It becomes punitive. Disgorgement is not designed as a punitive measure because punitive damages in treble damages are a whole separate area of law.

Disgorgement is exactly that, restitution to give back or pay back somebody a value that they put in when they shouldn't have. And in this case, these allegations in this complaint fail to set forth sufficiently --

(Pause).

THE COURT: You have one. I have one.

MR. ELLENHORN: I'm sorry?

THE COURT: You have someone telling you.

LAW SECRETARY: Sorry.

THE COURT: Okay.

MR. ELLENHORN: I would like to say something.

THE COURT: Hold on one second.

MR. ELLENHORN: After you finish.

THE COURT: I'll give you a second. Hang on a second.

(Continuing) -- exactly what the public injury is, what the consumer's injury is, what the injury is to the State.

Disgorgement, one, is restitution to recover, disgorgement is to deter conduct, and in this sense it is not there.

So, that is my decision and order with respect to the motion.

I find that based on these two cases I have here and based on the insufficiency of the allegations set forth in the complaint that a disgorgement remedy has not been stated here, and, accordingly, I am going to grant the defendant's motion to dismiss that aspect of the complaint seeking disgorgement against it.

Counsel, you have something you want to add?

MR. ELLENHORN: You made your ruling, and I am not going to try to persuade you otherwise. I would like to clarify something for the record because this is, obviously, going to take this up.

THE COURT: Yep.

MR. ELLENHORN: The complaint is very clear that investors in Lehman stock suffered massive injury. It is true that they suffered massive injury from a fraud which we contend was --

THE COURT: Facilitated.

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MR. ELLENHORN: -- more than facilitated by Ernst & Young.

It is true that, obviously, a stockholder in Lehman didn't pay their auditing fees, that's a fact. They wouldn't pay them. The company pays their auditing fees.

But, it is not true, not even remotely true that the victims of the fraud did not suffer huge financial losses.

THE COURT: I'm not disputing that. I'm just saying that the allegations --

MR. ELLENHORN: I want to be clear about that.

THE COURT: The allegations are insufficient.

MR. ELLENHORN: Your Honor's ruling, I believe, is that because the fees were not actually paid by a stockholder, they were paid by the company, you know, somehow they could keep them even if they acted wrongly.

THE COURT: I did not say that. I said the disgorgement vehicle is not available.

MR. ELLENHORN: Well, but there is no other way to get the fees. There is no other way to get the fees.

And by the way, New York's interests, I should also note, although I didn't make this argument as such, I didn't think it was necessary, New York's interest is not simply those of a party that might through its State pension plan have invested in Lehman. New York has an interest, and the

courts have recognized it for about 75 years, in maintaining the integrity of the financial markets of which New York is the world center, and that's an interest.

THE COURT: Okay, Mr. Ellenhorn.

MR. ELLENHORN: All right, enough.

THE COURT: Thank you. I think I made my point.

MR. ELLENHORN: I'm sorry, I know you made your point. I wanted to clarify our position.

THE COURT: You could clarify for the record.

Counsel, you want to make any clarification with respect to what was said?

MR. RUTHBERG: No, sir.

Before I forget, I want to tell your Honor, we did reach agreement on a stipulation and order regarding scheduling of discovery in this case. I want to hand that up your Honor.

(Handing).

THE COURT: When do you want to do a compliance conference then? I'm going to sign it. You talk to my Part Clerk.

THE CLERK: Come over with me, and we will give you a future date. Okay.

THE COURT: I need to know before you leave, folks. Hold on one second.

Have you served an answer in this case? Has an

answer been served? I guess not.

MR. RUTHBERG: No.

MR. ELLENHORN: Only two and a half years, we still don't have an answer.

MR. RUTHBERG: Well, to correct the record, it was in federal court and came it back.

MR. ELLENHORN: It was in federal court, came back and the motion.

THE COURT: What I want is I want to direct you to serve an answer, today is December 12th, serve an answer or move. Well, you've already moved with respect to the complaint. Serve an answer by January 9th. Okay. So that we have that, so we could have the issue joined before we go forward.

Having said all that, that is my decision and order with respect to this motion.

Counsel, you are the moving party. Order the transcript, please. I will so order it. You have it for your records, and have a very good afternoon.

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MR. RUTHBERG: Thank you, your Honor.

(Proceedings are recessed).

So Ordered

JEFFREY K. OING J.S.C.

CERTIFIED TO BE A TRUE
AND CORRECT TRANSCRIPT

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Mtn Seq No. 002

Margaret Baumann

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OFFICIAL COURT REPORTER