

Trump's NY Civil Fraud Trial Spotlights Long-Criticized Law

By **Mark Kelley and Lois Ahn** (April 5, 2024, 3:33 PM EDT)

In late 2023 and early 2024, Justice Arthur F. Engoron of the New York Supreme Court held a bench trial on claims brought by New York Attorney General Letitia James against former President Donald Trump relating to allegedly fraudulent financial statements submitted to banks and insurers.

Justice Engoron entered a judgment that is likely to cost Trump over \$450 million.

In October, Trump lambasted the law used against him — New York Executive Law Section 63(12) — as "VERY UNFAIR" on his Truth Social platform.[1]

It is no surprise that Trump, who has been sued many times for fraud, would take aim at Section 63(12), since the law specifically targets "repeated fraudulent or illegal acts" and "persistent fraud or illegality in the carrying on, conducting or transaction of business."

But Trump is not Section 63(12)'s only critic. Since its inception, Section 63(12) has been denounced as too vague and too potent. Indeed, the law has been used aggressively against entities like Exxon Mobil Corp. and Juul Labs Inc., and powerful individuals like "Pharma Bro" Martin Shkreli. Powerful legal tools make powerful enemies.

But these criticisms have both a historical and substantive basis. After all, Section 63(12) is a strikingly broad law with several major departures from the traditional and familiar elements of common law fraud.

This article answers a few simple questions about the law, providing its history, its major differences from the traditional fraud elements and a brief summary of some of the criticisms it has drawn since Trump's case brought it back into the limelight. The article concludes with a few consideration points for parties in receipt of an investigative subpoena by the attorney general's office.

History of Section 63(12)

Section 63(12) was enacted in 1956. The New York Times reported at the time that then-New York Attorney General Jacob Javits said the law was among "powerful new weapons in his fight to prevent frauds against the public." [2] The Better Business Bureau also supported the law, stating it would be "most helpful in combating fraudulent practices" that deceive or defraud New York consumers. [3]

As codified today, Section 63(12) grants the attorney general broad powers to regulate state businesses "in the interest of securing an honest marketplace," as the New York Appellate Division said in its 2008 decision in *People v. Coventry First LLC*. [4] The attorney general can bring actions under the statute against any person engaging in "repeated fraudulent or illegal acts" or otherwise "demonstrat[ing] persistent fraud or illegality in the carrying on, conducting or transaction of business." [5]

When originally enacted, however, Section 63(12) did not define the terms "fraud" or "fraudulent." [6]



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The New York State Bar Association's Committee on State Legislation disapproved of the bill for this very reason, arguing it had been "drawn in too loose a manner," and asking, "[w]ho is to state what 'repeated fraudulent or illegal acts or otherwise demonstrate persistent fraud or illegality' means?"[7]

That issue was later addressed in a 1965 amendment, which defined "fraud" and "fraudulent" to mean "any device, scheme or artifice to defraud and any deception, misrepresentation, concealment, suspension, false pretense, false promise or unconscionable contractual provisions." [8]

But the 1965 amendment gave rise to additional concerns. The New York State Department of Commerce argued that it went "well beyond the common law concept of a fraud" and "does not require a fraud to be an intentional act." [9]

The New York State Council of Retail Merchants Inc. argued that it would "[give] an 'unconscionable' degree of power to the enforcement arm of the government" — "a degree of power capable of swinging from enforcement to harassment." [10]

Notwithstanding these criticisms, the New York Attorney General's Office has used Section 63(12) for decades. Early enforcement actions included cases against the Waldorf-Astoria Hotel for billing its customers a 2% charge for sundries "without any explanation, itemization or identification," [11] and against companies for engaging in sweepstakes scams against consumers. [12]

More recent cases brought under Section 63(12) include actions against Juul, [13] Exxon Mobil, [14] Shkreli [15] and Amazon.com Inc. [16]

Common Law Fraud Versus Section 63(12)

One basis for criticism of Section 63(12) is the relatively lax pleading requirements compared to common law fraud. Section 63(12) does not require all of the traditional elements of common law fraud, which are essentially the same as those for a claim of securities fraud under Section 10(b) of the Securities Exchange Act and Rule 10b-5. [17]

Those elements are: (1) a false representation, (2) of material fact, (3) with intent to defraud, (4) a reasonable reliance on the representation, (5) causing damages to the plaintiff. [18]

A common law fraud claim must also be brought within six years of the date the cause of action accrued, or two years of when the fraud was or should have been discovered. [19]

Fraud is typically difficult to prove. Three of the toughest elements are materiality, intent and reasonable reliance. Materiality usually requires proof that a reasonable investor would be misled. [20] *Scienter* — a classic stumbling block for plaintiffs — typically requires allegations sufficient to show either motive and opportunity to defraud, or strong circumstantial evidence of conscious misbehavior or recklessness. [21]

And the "always nettlesome" [22] inquiry, in the words of the U.S. Court of Appeals for the Second Circuit in its 1997 *Schlaifer Nance & Co. v. Estate of Warhol* decision, into reasonable reliance takes a plaintiff's experience and knowledge into account, such that the element is not met if the nature of the risk assumed could have been ascertained. [23]

But Section 63(12) does not require any of these things — as noted by the New York Supreme Court in

its 1971 decision in *State v. Interstate Tractor Trailer Training Inc.*, "[g]ood faith or lack of fraudulent intent is not in issue."^[24] In fact, in the highly publicized decision following Trump's trial, Judge Engoron noted that "intent, scienter, and reliance are not elements of a stand-alone §63(12) claim."^[25]

While materiality is relevant in a Section 63(12) case, it is not necessary, since the law is "meant to protect not only the average consumer, but also 'the ignorant, the unthinking and the credulous,'" as the New York Appellate Division noted in its 2003 decision in *People v. General Electric Co. Inc.*^[26]

Moreover, Section 63(12) applies to a broader range of conduct than common law fraud claims cover. In its *People v. GE* decision, the New York Appellate Division noted that under the law, "the test for fraud is whether the targeted act has the capacity or tendency to deceive, or creates an atmosphere conducive to fraud."^[27] That scope dramatically expands Section 63(12)'s coverage.

Yet, notwithstanding all of these differences with its common law cousin, a fraud claim under Section 63(12) enjoys the same six-year statute of limitations.^[28]

Section 63(12) and Its Critics

For many of the same reasons, Section 63(12) has faced some disapproval. Without attempting to resolve these ongoing debates, we conclude by briefly summarizing a few of the more recent criticisms and providing a few points for consideration in the event of a state attorney general inquiry.

One common critique following Trump's recent case is that Section 63(12) punishes "victimless crimes." For example, Northwestern University Pritzker School of Law professor and co-chairman of the Federalist Society's Board of Directors Steven Calabresi raised this concern in a criticism of the case against Trump, calling the trial "Kafkaesque," a "Stalinist nightmare," and "truly a victimless crime."^[29]

In a blog post responding to Calabresi that took no position on the propriety of Trump's case, University of California, Berkeley School of Law professor Orin Kerr pointed out that a statute prohibiting driving while intoxicated might also be enforced even if a drunk driver happens to get home safe.^[30]

Relatedly, the Associated Press studied nearly 150 cases brought under Section 63(12), and found that "nearly every previous" time a business was dissolved as a result of a case brought under the law, "victims and losses were key factors."^[31] It thus appears that, in the majority of such cases, the underlying fraud was not victimless.

Another, related criticism of Section 63(12) — at least as it was applied to Trump — relates to the availability of disgorgement as a remedy. The statute provides for an injunction against continuation of a business, restitution and damages, and cancellation of a business certificate. It also allows "the court [to] award the relief applied for or so much thereof as it may deem proper."^[32]

The legal premise for an award of disgorgement is well established. The New York Court of Appeals affirmed the availability of that relief in its 2016 decision in *People v. Greenberg*, involving claims brought against Maurice Greenberg by then-Attorney General Eric Schneiderman.^[33]

However, the award of disgorgement in Trump's case has struck some as inappropriate given that the counterparties to the fraud — banks and insurance companies — chose to continue dealing with him, notwithstanding his reputation.^[34]

Finally, Trump and others have complained that Section 63(12) is too potent a tool for a politically motivated attorney general.[35] Whether or not these critics are correct that the New York state attorney general is politically motivated, it is certainly true that Section 63(12) is a powerful law with a long track record of major cases.

But the attorney general has many tools at her disposal to investigate deceptive conduct, including the Martin Act and General Business Law Sections 349 and 350. In other words, that criticism is not a criticism of Section 63(12), but of the New York Attorney General's Office generally, no matter who inhabits it.

These laws are a reminder, not only of the awesome power exercised by the New York state attorney general, but also that the receipt of an investigative subpoena from the attorney general's office warrants serious care and attention.

A party receiving a subpoena should immediately issue a hold notice to relevant personnel to avoid spoliation issues.

They should contact the attorney general's office to learn what they can about what prompted the investigation, its scope, their role in the potential charges, whether the inquiry is part of a single-state or multistate investigation, and any federal enforcement agency involvement.

And should efforts to resolve procedural or substantive issues with the subpoena fail, that party may consider moving to modify or even quash the subpoena.

The broad authority Section 63(12) provides New York's attorney general to investigate and pursue enforcement proceedings against fraud highlights the importance of judicious exercise of discretion by that office.

The absence of certain procedural safeguards normally present in the civil fraud context — such as the need to prove scienter or reliance — and the tendency to use the law against powerful entities guarantee that Section 63(12) will be the subject of criticism and further discussion for years to come.

The attorney general's extensive powers under the law also underscore the importance for counsel representing a party faced with the threat of an enforcement action to consider all options, including potential constitutional challenges, as part of a defense strategy.

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[1] @realDonaldTrump, Truth Social (Oct. 3, 2023, 8:42 AM), <https://truthsocial.com/@realDonaldTrump/posts/111171136822383110>.

[2] Leo Egan, Anti-Fraud Bills Hailed by Javits, *The New York Times*, Mar. 26, 1956, at 26.

[3] New York Bill Jacket, 1956 S.B. 3289, Ch. 592.

See https://ag.ny.gov/sites/default/files/appeal_brief_and_addendum.pdf.

[4] People ex rel. Cuomo v. Coventry First LLC, 861 N.Y.S.2d 9, 11 (1st Dep't 2008).

[5] N.Y. Exec. Law §63(12).

[6] See People ex rel. Schneiderman v. Credit Suisse Sec. (USA) LLC, 47 N.Y.S.3d 236, 237 (1st Dep't 2016).

[7] New York Bill Jacket, 1956 S.B. 3289, Ch. 592.

[8] New York Bill Jacket, 1965 S.B. 1219, Ch. 666.

[9] Id.

[10] Id.

[11] State ex rel. Lefkowitz v. Hotel Waldorf-Astoria Corp., 323 N.Y.S.2d 917, 919 (Sup. Ct. 1971).

[12] People ex rel. Lefkowitz v. Prestige Video Stores, Inc., 299 N.Y.S.2d 955, 956-57 (Sup. Ct. 1969).

[13] People ex rel. James v. JUUL Labs, Inc., 181 N.Y.S.3d 537 (1st Dep't 2023).

[14] People ex rel. James v. Exxon Mobil Corp., 119 N.Y.S.3d 829 (Sup. Ct. 2019).

[15] Fed. Trade Comm'n v. Vyera Pharms., LLC, No. 20-CV-00706, 2021 WL 4392481 (S.D.N.Y. Sept. 24, 2021).

[16] New York ex rel. James v. Amazon.com, Inc., 550 F. Supp. 3d 122 (S.D.N.Y. 2021).

[17] Serova v. Teplen, No. 05-CV-6748, 2006 WL 349624, at *8 (S.D.N.Y. Feb. 16, 2006).

[18] Lama Holding Co. v. Smith Barney Inc., 668 N.E.2d 1370, 1373 (N.Y. 1996).

[19] N.Y. C.P.L.R. §213(8).

[20] Acacia Nat'l Life Ins. Co. v. Kay Jewelers, Inc., 610 N.Y.S.2d 209, 213 (1st Dep't 1994).

[21] Eternity Glob. Master Fund Ltd. v. Morgan Guar. Tr. Co. of N.Y., 375 F.3d 168, 187 (2d Cir. 2004) (applying New York law).

[22] Schlaifer Nance & Co. v. Est. of Warhol, 119 F.3d 91, 98 (2d Cir. 1997).

[23] HSH Nordbank AG v. UBS AG, 941 N.Y.S.2d 59, 66 (1st Dep't 2012).

[24] State ex rel. Lefkowitz v. Interstate Tractor Trailer Training, Inc., 321 N.Y.S.2d 147, 151 (Sup. Ct. 1971); see also Matter of People ex rel. Schneiderman v. Trump Entrepreneur Initiative LLC, 26 N.Y.S.3d 66, 72 (1st Dep't 2016).

[25] Decision and Order at 5, *James v. Trump*, No. 452564/2022 (N.Y. Sup. Ct. Feb. 16, 2024), NYSCEF Doc. No. 1688.

[26] *People v. Gen. Elec. Co.*, 756 N.Y.S.2d 520, 523 (1st Dep't 2003) (quoting *Guggenheimer v. Ginzburg*, 372 N.E.2d 17, 19 (N.Y. 1977)).

[27] *People ex rel. Spitzer v. Gen. Elec. Co.*, 756 N.Y.S.2d 520, 523 (1st Dep't 2003).

[28] N.Y. C.P.L.R. § 213(9).

[29] Steven Calabresi, President Trump's Kafkaesque Civil Trial in New York State, *The Volokh Conspiracy* (Feb. 18, 2024), <https://reason.com/volokh/2024/02/18/president-trumps-kafkaesque-civil-trial-in-new-york-state/>.

[30] Orin S. Kerr, Thoughts on Judge Engoron's Opinion, A Response to Calabresi, *The Volokh Conspiracy* (Feb. 19, 2024), <https://reason.com/volokh/2024/02/19/thoughts-on-judge-engorons-opinion-a-response-to-calabresi/>.

[31] Bernard Condon, Dissolving Trump's Business Empire Would Stand Apart in History of NY Fraud Law, *Associated Press* (Jan. 29, 2024), <https://apnews.com/article/trump-fraud-business-law-courts-banks-lending-punishment-2ee9e509a28c24d0cda92da2f9a9b689>.

[32] N.Y. Exec. Law §63(12).

[33] *People ex rel. Schneiderman v. Greenberg*, 54 N.E.3d 74, 77 (N.Y. 2016).

[34] Steven M. Cohen, Trump's \$355 Million Fine Fits With New York Law, *Wall St. J.* (Feb. 19, 2024), <https://www.wsj.com/articles/trumps-355-million-fine-fits-with-new-york-law-but-will-we-regret-it-business-fraud-5c0e7850>.

[35] See, e.g., Ben Protess et al., Trump Is Battling a New York Law Used to Take on Corporate Giants, *The New York Times* (Sept. 22, 2022) <https://www.nytimes.com/2022/09/23/nyregion/donald-trump-letitia-james-lawsuit.html>.