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Expert Analysis

Private Right of Action Under the Martin Act—Does It Exist?

By Erica F. Buckley

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Question: We are a group of unit owners in a new construction condominium in New York City. The sponsor has not completed all that was promised under the offering plan and there are construction defects. Can we sue under the Martin Act?

Answer: The offer and sale of new construction condominium units is governed by the Martin Act—New York's blue-sky law. The Martin Act is primarily a disclosure statute, which empowers the attorney general to determine disclosure requirements for the offer and sale of real estate securities (such as new construction condominium units).

The Martin Act also empowers the attorney general to commence investigations and enforcement actions against any individual or business for the use of "any device, scheme or artifice to defraud or for obtaining money or property by means of any false pretense, representation or promise, or . . . any deception, misrepresentation, concealment, suppression, fraud, false pretense or false promise[.]" *See* General Business Law §352(1).

In addition to broad enforcement powers, the Martin Act also empowers the attorney general to promulgate suitable rules and regulations governing disclosure materials for prospective purchasers. Gen. Bus. Law§ 352-e(6). The Martin Act and applicable governing regulations require, among other things, the sponsor to file an offering plan with the attorney general that includes a detailed description of the property being sold. *See* 13 N.Y.C.R.R. §20.7 (condominiums); §21.7 (cooperatives); §22.7 (homeowners associations); and §24.7 (timeshares). But for the Martin Act, prospective purchasers would likely not receive such detailed information before purchasing a condominium unit.

Erica F. Buckley

This is why there is no private right of action under the Martin Act. This is well settled based on decisions rendered by the New York Court of Appeals—the highest court of the state. Only the attorney general can sue if the disclosure requirements of the statute and governing regulations are not met, *because* but for the Martin Act, there was no legal duty to otherwise describe in such detail the property being sold. *See, e.g., Kerusa Co. v. W10Z/515 Real Estate Ltd. Partnership*, 12 N.Y.3d 236 (2009); *Kralik v. 239 E. 79th St. Owners*, 5 N.Y.3d 54 (2005); *CPC Int'l v. McKesson*, 70 N.Y.2d 268 (1987); *Anwar v. Fairfield Greenwich*, 728 F.Supp.2d 354 (S.D.N.Y. 2010).

The lack of private right of action under the Martin Act doesn't mean purchasers are without remedies. In fact, buyers are *not* preempted from filing a lawsuit based on the sponsor's misrepresentation or omission of an aspect or detail of the condominium merely because the misrepresentation or omission relates to, or partially involves, a required disclosure.

As the Court of Appeals wrote, "[a]n injured investor may bring a common-law claim (for fraud or otherwise) that is not *entirely dependent* on the Martin Act for its

viability. Mere overlap between the common law and the Martin Act is not enough to extinguish common-law remedies." *Assured Guaranty (UK) v. J.P. Morgan Inv. Mgmt.,* 18 N.Y.3d 341, 353 (2011) (emphasis added)*; CMMF v. J.P. Morgan Inv. Mgmt*, 78 A.D.3d 562, 564 (1st Dep't 2010) ("The key therefore, is whether the causes of action in question 'fit within a cognizable legal theory' without relying wholly on the provisions of the Martin Act.").

The Martin Act might prevent a unit owner or non-sponsor-controlled board from suing a sponsor if the claims are predicated solely on the sponsor's obligations under the Martin Act and governing regulations.

In other words, if the Martin Act and governing regulations are the sole source of the requirement that the sponsor must disclose a specific aspect or detail of the property and the buyer wishes to sue the sponsor because of a misrepresentation or omission of the specific aspect or detail made in that disclosure, the sponsor could potentially argue that the plaintiff doesn't have standing to sue.

An example of such a condition might be the type of roof warranty that comes with the purchase of a condominium unit. Under New York Law, there is no requirement to disclose to a purchaser the type or scope of roof warranty applicable to your building, and but for the Martin Act, you as a purchaser of a condominium unit may not have otherwise received that information.

Therefore, if the sponsor fails to include material information on the type or scope of roof warranty in the offering plan, then the suing party may be facing Martin Act preemption arguments if they try to sue.

Regardless of the above, there could be situations where the Martin Act and governing regulations would not preempt a plaintiff from suing the sponsor. For example, if the lawsuit alleges a fraud that is not entirely dependent on the disclosure requirements of the Martin Act and governing regulations, or if the purchaser was suing under a non-fraud common-law cause of action that is not entirely dependent on the Martin Act and governing regulations (e.g., breach of contract).

Let's take another example. Say there was a city code that requires sponsors of new construction condominium offerings to follow detailed specifications when constructing a building. In the offering plan, the sponsor describes what they are required by code to build, or they undertake to comply with the code when they construct the building. After moving in, unit owners discover that the sponsor didn't comply with the city code. Therefore, a purchaser or non-sponsor-controlled board could arguably sue for a violation of the code or for a misrepresentation. *See* Assured Guaranty.

Given the complexity of bringing these types of claims, many purchasers and boards may seek redress from the attorney general. While the Office of the Attorney General has exclusive jurisdiction under the Martin Act, it also has broad prosecutorial discretion (along with limited resources). This means that many unit owners or non-sponsor-controlled boards are often left to explore what their remedies are. This generally means looking at whether a unit owner or board has enough information to explore common-law fraud claims, which, unlike Martin Act fraud, require the plaintiff to prove intent and reliance.

In addition to common-law fraud, many unit owners or non-sponsor-controlled boards (or groups) will explore breach of contract claims, which can often be successful, especially if the sponsor's attorney fails to assert Martin Act preemption.

Given the complexity of these issues, it is generally always preferable to try to resolve such claims through non-litigation means such as alternative dispute resolution. But if that is not successful, then a unit owner or a non-sponsor-controlled board may be left with no choice but to sue the sponsor, and if this is the case, it would be wise to ensure that all claims can stand on their own from Martin Act claims.

Erica F. Buckley *is the former chief of the Real Estate Finance Bureau. She leads Nixon Peabody's Cooperatives & Condominiums and State Attorneys General practices. This column is for informational purposes only and is not a substitute for agency guidance.*