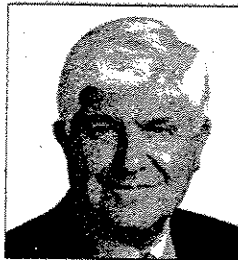


BY JOHN F.X. PELOSO AND BEN A. INDEK

Appellate Court Ratchets Up State Role in Securities Law Prosecution

OVER THE LAST several years, the securities industry has witnessed an expansion of the role of state authorities in the enforcement of the securities laws. This phenomenon has been most evident in New York, where the State Attorney General has been noisily aggressive in investigating and prosecuting alleged abuses in the research, investment banking and mutual fund areas. At the same time, New York County District Attorney, Robert M. Morgenthau, has continued to pursue his long-standing interest in initiating charges against alleged corporate and securities malfeasance. Last month, in *People v. Cohen*, the Appellate Division, First Department, affirmed New York State's interest in securities industry investigations in upholding a perjury conviction stemming from testimony given by the defendants in a National Association of Securities Dealers (NASD) investigation.¹ This decision further evidences the growing involvement of state authorities in what has historically been the domain of federal securities law enforcement.



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eral officers, the State's perjury charges could not be brought in New York State court. Defendants also argued that because the NASD is charged with enforcing the federal securities laws, the United States government's interests are affected rather than those of New York State. In response, the State argued that the NASD is a private corporation and not a federal tribunal (making *Loney* inapplicable) and that in any event, the State is affected by perjury committed before the NASD involving a New York securities firm. After reviewing the background, responsibilities and oversight of the NASD, the court concluded that the NASD is a private, self-regulatory organization rather than a federal agency, and that while the NASD is primarily concerned with the enforcement of the federal securities laws, it also has responsibility for compliance with other laws, rules and regulations, including state securities provisions.

The defense also argued that the perjury charges did not fall within the perjury statute, which provides that an individual is guilty of perjury when he provides false testimony in

a "proceeding before any court, body, agency, public servant or other person authorized by law to conduct such proceeding and to administer the oath or cause it to be administered." *Id.* at *124 quoting Section 210.15 of the New York Penal Law. According to the defendants, there was no proceeding before a New York State tribunal or officers of the state, and interviews before the NASD are not a "proceeding" within the ambit of the perjury statute. The court disagreed, finding that the perjury statute encompasses an on-the-record interview held in New York. Key to this finding was the court's observation that the NASD was "authorized by law" to conduct its investigation and to administer an oath pursuant to SEC approval of the self-regulatory organization's investigatory rule that provides that the NASD may require an individual subject to its jurisdiction to testify under oath.

Thus, the court rejected both the jurisdictional and statutory scope arguments and denied defendants' motions to dismiss the perjury counts. The case proceeded to trial, and after a jury conviction (and a subsequent motion to set aside the perjury verdicts and to dismiss those counts in the indictment, which was denied), Cohen and three other defendants appealed. On March 18, 2004, the appellate division, first department, affirmed. According to an attorney involved in the case, defendants intend to seek an appeal.³

First Department's

On appeal, defendants reiterated the arguments against New York's jurisdiction, that the matter concerned a federal investigation by U.S. governmental agency, asserted that New York's jurisdiction contravenes the principles of federalism and challenged the evidentiary bases underlying the convictions. Central to these arguments was the *Loney* case, which defendants urged precluded state prosecution for perjury before a body whose activities involved exercising authority conveyed by federal statutes.

Background

People v. Cohen arose out of an NASD investigation of a brokerage firm and the role played by Stanley Cohen in the activities of that firm. Almost 30 years before the NASD's investigation, the Securities and Exchange Commission had barred Cohen from the securities industry for two years and imposed a lifetime prohibition against his exercising supervisory responsibilities at any firm. In 1994, the NASD permitted Cohen to return to the industry in a non-supervisory capacity. In the late 1990's, the NASD began an investigation into Cohen's role at a registered firm in light of concerns that he might be violating his lifetime prohibition. In connection with that investigation, Cohen and others testified under oath before the NASD enforcement staff.² Cohen and four others were later charged in a 27-count indictment, which included 21 counts of perjury.

In 2000, defendants moved to dismiss the perjury counts, arguing that New York did not have jurisdiction over a prosecution for perjury committed in connection with an NASD investigation and that New York's perjury statute did not encompass perjury before the NASD. These were novel issues, which impelled the State Supreme Court Justice to observe in his opinion that "... this is the first prosecution, anywhere, for perjury before the NASD" *People v. Cohen*, 187 Misc2d 117, *119 (Nov. 16, 2000).

Relying on a century-old U.S. Supreme Court decision, *Thomas v. Loney*, 134 US 372, 375 (1890), holding that federal courts have exclusive jurisdiction over perjury that is committed "in a case pending in a court or other judicial tribunal of the United States," defendants argued that because the NASD acts in many respects as a federal tribunal and that its employees are, in essence, fed-

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Loney involved a contested Congressional election as to which the United States House of Representatives had authority and responsibility to oversee. As part of that power, Congress regulated the use of depositions taken in connection with disputes concerning an election and provided that an individual who had falsely testified under an oath administered by U.S. law was guilty of perjury. In *Loney*, as part of this federal scheme, a witness testified before a state appointed notary public and was later charged with perjury by the State of Virginia. On appeal from the granting of a writ of habeas corpus, the Court rejected the jurisdiction of the Virginia court to hear the perjury charges, observing that the oath administered by the state notary public was not required by Virginia law, but rather was an oath authorized by federal law. Thus the federal government, not the State of Virginia, maintained exclusive jurisdiction to deal with the alleged perjury.

The appellate division summarily dismissed *Loney* as irrelevant, observing that it essentially involved a federal election; and the happenstance that the oath sought to be enforced had been administered by a state notary, was inconsequential because the statute requiring the oath was a federal one. It is interesting to note that the court apparently gave substantial weight to the fact that the authority to administer the oath stemmed from federal not state law.

The court next rejected defendants contention that the case involved a federal investigation by a federal entity from which exclusive federal jurisdiction flows. It adopted the reasoning of several federal court decisions which hold (in other circumstances) that the NASD is a private organization, albeit, with the responsibility to enforce not only the federal securities laws, but also state securities law.

Finally, the court dealt with what it called a "nuanced" argument apparently made for the first time on appeal. Defendants asserted that New York State does not have the power to regulate perjury committed in an NASD proceeding because the NASD's authority to enforce New York's broker registration requirements stems from federal law (the Maloney Act), 15 U.S.C. §780-3, et seq. According to the court, defendants argued that *Loney* "... compels the conclusion that the jurisdictional issue is governed by the source of

the authority pursuant to which the oath is administered rather than just the particular forum in which the oath is administered..." Under this line of reasoning, defendants urged that even if the court were to conclude that the NASD is not a federal agency, its power delegated under the federal securities laws to require an oath creates exclusive federal jurisdiction for perjury committed in an NASD proceeding.

The court brushed these arguments aside. While remarking that "*Loney* is easily distinguishable" and calling defendants' application of *Loney* "unduly elastic" and "ultimately sophistic," the court stated that "whatever the ultimate authority allowing the NASD to take testimony under oath, the NASD does not

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serve exclusively federal interests, but also references state law, most notably enjoying delegated authority to enforce New York's broker registration requirements [citation omitted] and serves the interests of its constituent members. Thus, the power delegated to the NASD to enforce compliance with state securities regulations is substantive and not merely procedural."

Here it would seem, the court is grounding its jurisdiction in the law of the governmental entity whose laws are being enforced and the ultimate interest of the State in the outcome. While that is not inconsistent with *Loney*, it would appear to not deal with that aspect of the Supreme Court's decision in *Loney* where the Court rejected state jurisdiction to prosecute perjury given to a state notary in "a proceeding where the authority to administer the oath came from federal not state law." Justice Gray in *Loney* wrote:

"But the power of punishing a witness for testifying falsely in a judicial proceeding belongs peculiarly to the government in whose tribunal that proceeding is had."

Now it may be that the NASD is not a federal tribunal. But neither is it a state tribunal. If it is a tribunal at all, it is one created under the federal securities laws whose rules, including the power to administer oaths, come from federal law, a fact recognized by the appellate division in holding that an NASD examination qualified for application of the perjury statute. Indeed, the Virginia perjury statute pursuant to which the witness in *Loney* was indicted and which was rejected by the Supreme Court as a basis for state jurisdiction, was substantially the same as the New York Penal Law under which the *Cohen* defendants were prosecuted. The Virginia statute, as quoted by the U.S. Supreme Court reads:

"... if any person to whom an oath is lawfully administered, on any occasion, willfully swears falsely on such occasion touching any material matter or thing, he shall be guilty of perjury." Code VA 1887, Section 3741.

Thus, it would seem, the appellate division has not squarely met the defendants' argument that *Loney* compels the conclusion that the jurisdictional issue is governed not by the law being enforced by, but the entity by whose authority the oath is administered.

It will be interesting to see if this decision is appealed and, if so, how the issue is resolved. As a practical matter, whether a perjurious testifier before the NASD is prosecuted by the state or federal authorities may be more a matter of which prosecutor's office is more zealous in pursuing the case, contrasting state and federal perjury statutes and perhaps the influence of sentencing guidelines.

In any event, one thing is clear: the state and local authorities have been, and undoubtedly will continue to be, very aggressive in extending their jurisdiction with respect to violations of the securities laws and tangential matters. Additionally, we are likely to see defense lawyers' tasks continue to become more complicated by federal/state parallel proceeding issues.

1. The appellate division's March 11, 2004 decision was published in the New York Law Journal on March 18, 2004.

2. At the criminal trial and on appeal, Mr. Cohen contended that an oath was never administered at his NASD testimony and that perjury had not occurred. Both the trial court and appellate division rejected Mr. Cohen's claims.

3. "State Perjury Charges Loom for Brokers Who Lie to NASD, Panel Says," Tom Perrotta, NYLJ, (March 16, 2004).