

Using the Martin Act to Bring Fraudulent Practices in Dark Pool Promotion to Light: An Analysis of the Martin Act's Applicability to Misrepresentations Regarding the Operation of Dark Pools

BROOKE SGAMBATI*

In June 2014, New York Attorney General Eric Schneiderman filed a complaint against Barclays Capital in the Supreme Court of the State of New York, alleging that Barclays made material misrepresentations to its clients regarding the operation of its dark pool, Barclays LX. Schneiderman's complaint relied on the Martin Act, a New York state securities law that grants the Attorney General broad power to combat fraud in the purchase or sale of securities, to bring the action against Barclays. This Note will address an issue of first impression that is central to Schneiderman's case: does the Martin Act authorize the Attorney General to exercise broad oversight over the operation of dark pools (which are best described as platforms for securities transactions) or must actions brought by the Attorney General under the Martin Act relate to specific securities transactions that occur within dark pools? A broad reading of the Attorney General's authority under the Martin Act would allow his office to investigate and prosecute misrepresentations like those that Barclays allegedly made to persuade customers to use its dark pool. A narrow conception of his power would limit his office's ability to regulate the operation of dark pools and likely would require dismissal of the case against Barclays. This Note will also discuss whether a broad reading of the Martin Act, which would permit the Attorney General to use the statute to require more transparency in the operation of dark pools, would be beneficial from a

* Managing Editor, Colum. J.L. & Soc. Probs., 2015–2016. J.D. Candidate 2016, Columbia Law School. The author would like to thank Professor James Fanto for his comments on early drafts of this Note and the staff of the *Columbia Journal of Law and Social Problems* for all their assistance in editing and revision.

public policy standpoint, or if such a reading is an impermissible expansion of a law that has already been criticized for granting the Attorney General an extraordinary amount of power.

I. INTRODUCTION

“Dark pools” are widely and increasingly complex platforms for securities transactions that serve as alternatives to traditional public exchanges. They are essentially private stock exchanges that are owned and operated by large financial institutions. These private exchanges allow investors to complete securities transactions without having to reveal their identities or report their trading activities in real time.¹ When an investor places an order to buy or sell stock on a public exchange, the exchange typically makes information regarding that order publicly available before the order is executed.² As a result, when an investor places an order for a large block of shares on a public exchange, the trade may cause market movements that are disadvantageous for the investor.³ Dark pools, in contrast, report transaction data only after a trade’s completion.⁴ Thus, dark pools allow investors to trade without alerting their competitors, which minimizes the market impact of their actions.⁵ Executing trades “in the dark” can be beneficial to investors with large orders because these in-

1. See Michael Lewis, *The Wolf Hunters of Wall Street: An Adaptation From “Flash Boys: A Wall Street Revolt,”* by Michael Lewis, N.Y. TIMES MAG. (Mar. 31, 2014), <http://www.nytimes.com/2014/04/06/magazine/flash-boys-michael-lewis.html> [<https://perma.cc/PCC6-RLDL>] (noting dark pools are “private exchanges created by banks and brokers that did not have to report in real time what trading activities took place within them”).

2. See *Strengthening the Regulation of Dark Pools*, U.S. SEC. AND EXCH. COMM’N (Oct. 21, 2009), <https://www.sec.gov/news/press/2009/2009-223-fs.htm> [<https://perma.cc/PCC6-RLDL>] (“When investors place an order to buy or sell on an exchange, the exchange typically makes that order available for the public to view.”).

3. See Chris Wright, *What Is A Dark Pool And What Does Barclays’ Misuse Of It Mean For Bank Shares?*, FORBES (June 27, 2014), <http://www.forbes.com/sites/chriswright/2014/06/27/what-is-a-dark-pool-and-what-does-barclays-misuse-of-them-mean-for-bank-shares> [<https://perma.cc/VB44-S6E3>] (“[A] big institutional investor who wants to make a significant trade [knows] that doing so in public markets is going to create such waves that [they] lose out from the market movements that follow.”).

4. See GARY SHORTER & RENA S. MILLER, CONG. RESEARCH SERV., R43739, DARK POOLS IN EQUITY TRADING: POLICY CONCERNS AND RECENT DEVELOPMENTS 2 (2014) (“[D]ark pools[]’ do not provide quotes into the pre-trade public quote stream as is generally required of trades on the NASDAQ, the stock exchanges, and ECNs. They publish trade data only after transactions occur.”).

5. See Christopher Mercurio, Note, *Dark Pool Regulation*, 33 REV. BANKING & FIN. L. 69 (2013) (“This arrangement minimizes price movements in the public market and allows participants to trade without alerting competitors to their actions.”).

vestors may disguise their trading activity, which reduces the risk that other market participants, including predatory high frequency traders, will notice and take advantage of the investors' positions.⁶

While the benefits to investors who trade "off-exchange" seem clear, these investors may be subject to predatory behavior within dark pools.⁷ This is largely due to the fact that dark pools are opaque and under-regulated.⁸ Although dark pools are subject to SEC regulations that impose various registration and operational requirements,⁹ those rules were created with the intent of "allow[ing] developing systems with low volumes to operate under a minimal regulatory burden."¹⁰ As a result, dark pools are usually exempt from the more stringent quotation dissemination and fair access standards that these regulations impose on other types of alternative trading systems.¹¹

Furthermore, brokers operating dark pools are not required to disclose critical information about various aspects of the dark

6. See John McCrank, *Dark markets may be more harmful than high-frequency trading*, REUTERS (Apr. 6, 2014), <http://www.reuters.com/article/us-dark-markets-analysis-idUSBREA3508V20140406> [<https://perma.cc/3ZSC-WUZZ>] ("Investors with large orders can [] more easily disguise what they are doing, reducing the danger that others will hear what they are doing and take advantage of them."); Jared Bernstein, *The Importance of Shedding Some Light on Dark Pools*, N.Y. TIMES (July 22, 2014), <http://www.nytimes.com/2014/07/23/upshot/the-importance-of-shedding-some-light-on-dark-pools.html> [<https://perma.cc/R9VD-52F5>] ("[T]he dark pools are private clubs, initially used by large institutional investors that wanted to execute a large sale in a dark place. One reason for such a move is that sales on the more transparent public exchanges risk falling prey to 'front-running' by high-frequency traders.").

7. See Rupert Neate, *Barclays and Credit Suisse pay biggest ever fines for dark pool trading*, GUARDIAN (Jan. 31, 2016, 2:58 PM), <http://www.theguardian.com/business/2016/jan/31/barclays-and-credit-suisse-to-pay-biggest-ever-fines-for-dark-pool-trading> [<https://perma.cc/MEG5-R3X3>] ("Barclays and Credit Suisse has been fined \$154m . . . following an investigation into the banks' 'dark pools' private trading exchanges exploited by 'predatory, high-frequency traders' at the expense of the bank's traditional customers.").

8. Bernstein, *supra* note 6.

9. See SHORTER & MILLER, *supra* note 4, at 5 ("Under Reg ATS, dark pools are required to register either as exchanges with the SEC or as broker-dealers with the Financial Industry Regulatory Authority (FINRA), the frontline regulator of SEC-registered broker-dealers.").

10. JOHN C. COFFEE, JR. & HILLARY A. SALE, *SECURITIES REGULATION: CASES AND MATERIALS* 38, 598 (12th ed. 2012).

11. See *id.* at 598; Nicholas Crudele, *Dark Pool Regulation: Fostering Innovation and Competition While Protecting Investors*, 9 BROOK. J. CORP. FIN. & COM. L. 569, 577 (2015) ("Only when an ATS exceeds five percent of the daily volume of a security does it have to disseminate its best price quotes to the national exchanges."); SHORTER & MILLER, *supra* note 4, at 8 ("Dark pools are generally not subject to . . . [the fair access standard] requirement, which means that their liquidity is not made available to the investing public on terms that 'are not unfairly discriminatory.'").

pools' operations to their customers — including the identities of the parties that trade on their systems, information about what types of orders are available on their platforms and the sources of their pricing data.¹² Thus, it is nearly impossible for investors to know what really happens when their orders are filled within these private exchanges.¹³ Most brokers claim that they will only execute customers' trades in their dark pools when the best prices are available there.¹⁴ However, it appears as though they have little incentive to honor this guarantee, as no rule prohibits brokers from trading against their own customers within their dark pools.¹⁵ The majority of customer orders that are sent to the typical dark pool are filled there, but it is unlikely that a single dark pool could offer the best price available for such a high proportion of transactions.¹⁶ If brokers were truly acting in their customers' best interests, then more trades that were initially routed to a broker's proprietary dark pool would eventually be executed elsewhere.¹⁷ In his recent book *Flash Boys*, Michael Lewis posits that traders may actually trade against their clients within their

12. See Dave Michaels & Nick Baker, *Stricter Dark Pool Rules Said to Be Under Consideration at the SEC*, BLOOMBERG BUSINESS (Jan. 12, 2015, 3:43 PM), <http://www.bloomberg.com/news/articles/2015-01-12/stricter-dark-pool-rules-said-to-be-under-consideration-at-sec> [<https://perma.cc/S9WR-PWR7>] (“Under consideration are requirements that address two key areas of concern for critics of dark pools: the disclosure of the types of orders available on the platforms and the source of pricing data . . .”).

13. See MICHAEL LEWIS, *FLASH BOYS: A WALL STREET REVOLT* 86 (2015) (“[B]ecause the dark pool was not required to say exactly when it had sent an order, and the broker did not typically tell his investors where it had executed a trade, much less the market conditions at the moment of execution, the customer lived in darkness.”).

14. *Id.* (“In theory, the brokers were meant to find the best price for their customers. If the customer wanted to buy shares in Chevron, and the best price happened to be on the New York Stock Exchange, the broker was not supposed to stick the customer with a worse price inside its own dark pool.”).

15. *Id.* (“It was entirely possible that a broker's own traders were trading against the customers in its dark pool: There were no rules against doing that.”).

16. *Id.* at 85–86 (2015) (“[W]hile the brokers often protested that there were no conflicts of interest inside their dark pools, all the dark pools exhibited the same strange property: A huge percentage of the customer orders sent into a dark pool were executed inside the pool. . . . Most of the brokers' dark pools constituted less than 1 percent of the entire market, and yet somehow those brokers found the best price for their customers between 15 and 60 percent of the time.”).

17. See *id.* at 86 (“[A]ll the dark pools had the same strange property: A huge percentage of the customer orders sent into a dark pool were executed inside the pool. . . . It was hard to explain. A broker was expected to find the best possible price in the market for his customer. The Goldman Sachs dark pool — to take one example — was less than 2 percent of the entire stock market. So why did nearly 50 percent of the customer orders routed into Goldman's dark pool end up being executed inside that pool — rather than out in the wider market?”).

banks' dark pools, a practice that is not per se illegal.¹⁸ Similarly, while many financial institutions promote their dark pools as safe havens from high-frequency traders, they may in fact permit such high volume traders to buy access to their dark pools.¹⁹ For example, in a recent complaint filed against Barclays, New York Attorney General Eric Schneiderman alleged that Barclays operated its dark pool to favor high-frequency traders and "actively sought to attract them by giving them systematic advantages over others trading in the pool" despite contrary representations to customers.²⁰ Investors who utilize dark pools must simply trust that their brokers are not engaged in dishonest behavior, because they do not have access to information about the dark pools' operation beyond what the banks choose to reveal.

Today there are approximately forty-five dark pools operating within the United States, in addition to thirteen public exchanges.²¹ While early dark pool customers were predominantly large institutional investors interesting in buying or selling large blocks of stock, banks have been executing smaller transactions for individual investors off-exchange with increasing frequency.²² This trend is evidenced by the current similarity in size between the average dark pool and public exchange orders.²³ Even more striking is the fact that nearly all orders from "mom and pop" investors are currently executed off-exchange.²⁴ The group of cli-

18. *Id.* ("It was entirely possible that a broker's own traders were trading against the customers in its dark pool [W]hile the brokers often protested that there were no conflicts of interest inside their dark pools, all the dark pools exhibited the same strange property: A huge percentage of the customer orders sent into a dark pool were executed inside the pool. . . . Most of the brokers' dark pools constituted less than 1 percent of the entire market, and yet somehow those brokers found the best price for their customers between 15 and 60 percent of the time.")

19. *See id.* ("Goldman Sachs and Credit Suisse ran the most prominent dark pools, but every brokerage firm strongly encouraged investors who wanted to buy or sell big chunks of stock to do so in that firm's dark pool.")

20. Press Release, N.Y. Att'y Gen., *A.G. Schneiderman Announces Fraud Charges Against Barclays In Connection With Marketing And Operation Of Its Dark Pool* (June 25, 2014), <http://www.ag.ny.gov/press-release/ag-schneiderman-announces-fraud-charges-against-barclays-connection-marketing-and> [https://perma.cc/K7WS-A5Y6].

21. McCrank, *supra* note 6.

22. *See id.* ("The pools were originally created for institutions to trade large blocks of stock without creating a large impact in the market.")

23. *See id.* ("[T]he average size of orders in dark pools has shrunk to around 200 shares, similar to levels on public exchanges.")

24. *See id.* ("Around 40 percent of all U.S. stock trades, including almost all orders from 'mom and pop' investors, now happen 'off exchange,' up from around 16 percent six years ago.")

ents trading within dark pools is much larger and more diverse today than it was just a few years ago.²⁵

As the numbers of dark pool trades and customers have increased in recent years, regulators have called for greater oversight and regulation of dark pools²⁶ because of their increasing concerns that the unchecked growth of off-exchange trading has been harmful to investors.²⁷ For example, in June 2014, Securities and Exchange Commission Chair Mary Jo White announced that the agency was examining whether the present high volume of off-exchange trading undermines the quality of the U.S. stock market and cited the lack of transparency within dark pools as a particular area of concern.²⁸ Similarly, the chief executive of the Financial Industry Regulatory Authority, the largest self-regulatory organization for the U.S. securities industry, announced that his agency was exploring options for increasing its regulatory surveillance of dark pools in 2013.²⁹

While most proposals for increased oversight of dark pools have come from federal agencies, one notable move to expand regulatory authority over off-exchange trading has occurred at the state level. In March 2014, New York Attorney General Eric Schneiderman announced that his office had launched an investigation into the relationships between dark pools and high frequency traders as part of its “Insider Trading 2.0 Initiative.”³⁰ During its investigation, Schneiderman’s office scrutinized Barclays’ dark pool and discovered that Barclays had made misrep-

25. Bernstein, *supra* note 6 (“While once a scant few institutional investors quietly soaked in the dark pools, that’s no longer the case.”).

26. See Mercurio, *supra* note 5, at 70 (“As dark pool market share (and its concomitant market-wide influence) increases, so do the calls for regulation and oversight from regulators and industry leaders.”).

27. See Scott Patterson, Jean Eaglesham & Bradley Hope, “Dark Pools” Face New SEC Probe, WALL ST. J. (June 9, 2014), <http://www.wsj.com/articles/dark-pools-face-new-sec-probe-1402356915> [<https://perma.cc/NT4L-626J>] (“After years of unchecked growth in off-exchange trading, regulators are increasingly concerned that the level of activity in dark pools is harming investors.”).

28. See *id.*

29. Scott Patterson & Caitlin Nish, *Finra Seeks to Shine Light on Dark Pools*, WALL ST. J. (May 22, 2013), <http://blogs.wsj.com/moneybeat/2013/05/22/finra-seeks-to-shine-light-on-dark-pools> [<https://perma.cc/V48V-V8WL>] (“Rick Ketchum, chief executive of the Financial Industry Regulatory Authority . . . said Finra was . . . looking generally at the question about how to shed at least more surveillance light and perhaps public light on dark pools.”).

30. Eric T. Schneiderman, N.Y. Att’y Gen., Remarks on “Insider Trading 2.0 — A New Initiative to Crack Down on Predatory Practices” at New York Law School (Mar. 18, 2014), http://www.ag.ny.gov/pdfs/HFT_and_market_structure.pdf [<https://perma.cc/U5DJ-AF5E>].

representations regarding its operation to its customers.³¹ Specifically, Barclays allegedly “falsified marketing material purporting to show the extent and type of high frequency trading in its dark pool,” “falsely marketed the percentage of aggressive high frequency trading activity in its dark pool,” “made a series of false representations to clients about its ‘Liquidity Profiling’ service” by claiming that the service provided protection from predatory trading, “falsely represented that it routed client orders for securities to trading venues in a manner that did not favor [its] own dark pool,” and “secretly gave high frequency trading firms informational and other advantages over other clients trading in the dark pool.”³² Schneiderman subsequently filed a lawsuit against Barclays in June 2014, which was the first legal action in which he attempted to crack down on unscrupulous practices in the operation of dark pools.³³

Several of Schneiderman’s claims against Barclays were grounded in the Martin Act, a New York state law that empowers the Attorney General to investigate, regulate and bring enforcement actions against securities fraud.³⁴ His reliance on the Martin Act was immediately controversial, as that law has traditionally been used to prosecute alleged fraud that is tied to specific securities transactions.³⁵ Schneiderman’s critics argued that he

31. Complaint at 4, *People v. Barclays Capital, Inc.*, 1 N.Y.S.3d 910 (N.Y. Sup. Ct. 2015); Press Release, N.Y. Att’y Gen., *supra* note 20.

32. Complaint at 2–4, *People v. Barclays*, 1 N.Y.S.3d 910.

33. See A.G. Schneiderman Announces Landmark Resolutions with Barclays and Credit Suisse for Fraudulent Operation of Dark Pools; Combined Penalties and Disgorgement to State of New York and SEC of Over \$154 Million, N.Y. STATE OFFICE OF THE ATTY GEN. (Feb. 1, 2016), <http://www.ag.ny.gov/press-release/ag-schneiderman-announces-landmark-resolutions-barclays-and-credit-suisse-fraudulent> (“These cases mark the first major victory in the fight to combat fraud in dark pool trading and bring meaningful reforms to protect investors from predatory, high-frequency traders,’ Attorney General Schneiderman said. ‘This effort . . . began when we first sued Barclays.’”).

34. See *New York State’s Martin Act: A Primer*, DECHERT LLP (Jan. 15, 2004), http://www.dechert.com/files/Publication/a4def5dd-77bf-48ae-bead-491bfc9142c/Presentation/PublicationAttachment/dbeb2852-2e00-49d6-971f-4c2db9674658/FS_2004-04.pdf [<https://perma.cc/6WKL-EEZ7>] (“Sections 352 and 353 of the Act taken together, give the Attorney General the power to regulate, investigate and take enforcement action against securities fraud, including seeking equitable and monetary remedies.”).

35. See, e.g., Memorandum of Law in Support of its Motion to Dismiss Defendant’s Complaint at 1–2, *People v. Barclays*, 1 N.Y.S.3d 910 (“[I]n seeking to extend its regulatory authority to trading platforms, the NYAG ignores that the Martin Act — on which the NYAG’s claims are predicated — is limited to actions for fraud in the purchase or sale of ‘securities,’ and simply does not extend to all actions related to finance. Here, the allegations concern the functioning of LX as a trading platform, and do not identify any misstatements concerning any ‘security.’”); *NY Attorney General Going too Far?*, THE SEC. L. BLOG (Oct. 8, 2014), <http://seclaw.blogspot.com/2014/10/ny-attorney-general-going-too>

was extending the Martin Act beyond its current bounds, since he was using the law to prosecute fraudulent misrepresentations regarding the operation of an entire trading platform (Barclays' dark pool) without tying those allegations to any specific securities transaction.³⁶ The issue was not fully litigated in the case against Barclays, which settled before going to trial.³⁷ However, when ruling on Barclays' motion to dismiss, Justice Kornreich of the New York Supreme Court appeared to accept the Attorney General's argument that fraudulent misrepresentations regarding the operation of trading platforms could be actionable under the Martin Act.³⁸

This Note will analyze whether the New York Attorney General may use the Martin Act to prosecute fraud in the operation of proprietary trading platforms, thereby increasing his office's regulatory oversight of dark pools. It will also address the policy implications of a broad interpretation of the Martin Act, which grants the Attorney General this extended power. Part II of the Note will provide further information about the Martin Act and outline the New York Attorney General's powers under that law. Part III will then assess whether the New York Attorney General may use the Martin Act to investigate and regulate dark pools. Part IV will discuss the Barclays case in greater detail, summa-

far.html [<https://perma.cc/BR4C-GCY3>] ("I agree with the legal argument — allegations that the workings of a 'dark pool' were misrepresented is NOT a fraud 'engaged in to induce or promote the issuance, distribution, exchange, sale, negotiation or purchase of securities' which is the requirement for a claim under the Martin Act.").

36. See, e.g., Reply Brief of Defendant at 1, *People v. Barclays*, 1 N.Y.S.3d 910 ("The NYAG's reading of the Martin Act would render the Act virtually unlimited in scope. His sweeping interpretation would improperly reach *any* purported misstatement that could possibly have an effect on a securities transaction."); Christopher Faille, *Footnote 13: Barclays Did "Change the Number,"* ALLABOUTALPHA (Oct. 7, 2014) <http://allaboutalpha.com/blog/2014/10/07/footnote-13-barclays-did-change-the-number> [<https://perma.cc/6RRL-LJQP>] (stating the Barclays case revealed "the NYAG's continuing desire . . . to expand the scope of the Martin Act").

37. See A.G. Schneiderman Announces Landmark Resolutions with Barclays and Credit Suisse for Fraudulent Operation of Dark Pools; Combined Penalties and Disgorgement to State of New York and SEC of Over \$154 Million, *supra* note 33 ("Attorney General Eric T. Schneiderman today announced that Barclays Capital Inc. and Credit Suisse Securities (USA) LLC will pay a combined \$154.3 million to the State of New York and the SEC to settle investigations into false statements and other omissions made in connection with the marketing of their respective dark pools and other high-speed electronic equities trading services.").

38. *People v. Barclays*, 1 N.Y.S.3d at 917 ("[T]o the extent the applicability of the Martin Act to representations about trading venues can be considered a close call . . . this court views the Court of Appeals' guidance on the Martin Act to be that doubts in favor of the Martin Act's applicability should be resolved in the NYAG's favor.").

rizing both the Attorney General's arguments concerning the legitimacy of his broad interpretation of the Martin Act and Barclays' counterargument that the Attorney General's office overreached its authority under the law by bringing the suit. This Part will analyze the relative strength of each argument by addressing both the relevant case history and Justice Kornreich's treatment of each argument in her decision denying Barclays' motion to dismiss the Attorney General's Martin Act claims in *New York v. Barclays Capital*. Finally, Part V will consider policy arguments both in favor of and against interpreting the Martin Act broadly to allow the Attorney General to prosecute fraudulent misrepresentations regarding the operation of dark pools.

II. THE MARTIN ACT: ONE OF THE NEW YORK ATTORNEY GENERAL'S MOST POWERFUL LEGAL WEAPONS

The Martin Act is a New York state law that was passed in 1921 in an effort to prevent fraud in the purchase and sale of securities.³⁹ It empowers the New York Attorney General to investigate, regulate and bring enforcement actions against alleged securities fraud.⁴⁰ The Martin Act is New York's "blue sky" law,⁴¹ one of a series of antifraud laws adopted by various states before the first federal securities laws were passed in 1933 and 1934.⁴² However, the Martin Act is unique relative to the securities laws of other states in several respects. For example, it grants en-

39. David Voreacos, *The Martin Act — QuickTake*, BLOOMBERG VIEW (Aug. 25, 2014, 3:26 PM), <http://www.bloombergvew.com/quicktake/martin-act> [https://perma.cc/TQT3-94AJ].

40. *New York State's Martin Act: A Primer*, *supra* note 34.

41. While scholars are uncertain about the origin of the term "blue sky laws", "[t]he most plausible explanation . . . is that the term referred to the fact that . . . fly-by-night operators [who were targeted by early blue sky legislation] . . . operated so blatantly that they would 'sell building lots in the blue sky in fee simple.'" Jonathan R. Macey & Geoffrey P. Miller, *Origin of the Blue Sky Laws*, 70 TEX. L. REV. 347, 359 n.59 (1991). Nearly every state has its own blue sky legislation. B. Rogers, Annotation, *Blue Sky Laws*, 87 A.L.R. 42 (1933) ("Blue [s]ky [l]aws [have] been adopted in practically every state in the Union. . . . While the statutes differ widely in detail, the underlying purpose of them is . . . to protect the investing public.").

42. Robert A. McTamane, Commentary, *New York's Martin Act: Expanding Enforcement in an Era of Federal Securities Regulation*, 8 ANDREWS ENRON LITIG. & REG. REP. 19, 20 (2003). Congress did not intend for federal securities legislation to preempt state antifraud laws. Instead, "Congress envisioned a dual system of regulation" in which the states retained jurisdiction over securities transactions within their borders. Christopher R. Lane, *Halting the March Toward Preemption: Resolving Conflicts Between State and Federal Securities Regulators*, 39 NEW ENG. L. REV. 317, 325 (2005).

forcement powers directly to the Attorney General, while other states' laws typically allocate enforcement duties to securities commissioners.⁴³ Additionally, the Act allows the Attorney General to bring both civil and criminal actions against parties accused of violating the law.⁴⁴ Finally, the Martin Act permits the Attorney General exceptionally wide latitude to issue subpoenas and gather evidence before filing suit. According to § 354 of the statute, the Attorney General may easily obtain an order from a New York Supreme Court justice directing persons under investigation to answer questions or produce documents concerning allegedly fraudulent activities by “simply show[ing] upon his information and belief that the testimony of such person or persons is material and necessary.”⁴⁵ If he satisfies this requirement, then “it shall be the duty of the justice . . . to grant such application.”⁴⁶

The scope of the New York Attorney General's enforcement power under the Martin Act is the most significant difference between that law and similar statutes in other states. Under the Martin Act, the Attorney General has “the broadest and most easily triggered investigative and prosecutorial powers of any securities regulator, state or federal.”⁴⁷ The only elements required to establish a violation of the Martin Act are “a misrepre-

43. See Frank C. Razzano, *The Martin Act: An Overview*, 1 J. BUS. & TECH L. 125 (2006) (“Unlike the ‘blue sky’ laws of most states, which follow the Uniform Securities Act by establishing state securities commissions administering a regulatory scheme, New York’s Martin Act eschews state regulation of securities and adopts a broad civil and criminal enforcement model that empowers New York’s Attorney General to enjoin and prosecute conduct that is deemed detrimental to the investing public.”).

44. See Kulbir Walha & Edward E. Filusch, Recent Development, *Eliot Spitzer: A Crusader Against Corporate Malfeasance, or a Politically Ambitious Spotlight Hound? A Case Study of Eliot Spitzer and Marsh & McLennan*, 18 GEO. J. LEGAL ETHICS 1111, 1116 (2005) (“[T]he Martin Act became not just a vehicle for civil penalties, but also placed the sword of potential criminal penalties in the hand of the Attorney General.”).

45. N.Y. GEN. BUS. LAW § 354 (McKinney 2016).

46. *Id.*

47. *State v. 7040 Colonial Rd. Assocs. Co.*, 671 N.Y.S.2d 938, 941–42 (N.Y. Sup. Ct. 1998) (quoting David J. Kaufmann, *Introduction and Commentary Overview*, in 19 MCKINNEY’S CONSOLIDATED LAWS OF NEW YORK ANNOTATED 8, 9 (1996)). For example, “the Act empowers the Attorney General to commence an investigation even *before* the commission of a fraudulent act or practice,” and “the Attorney General may pursue his investigative goals either through confidential investigations conducted under compulsion of subpoena or through public investigations conducted pursuant to court order.” *Id.* at 942. See also Eric Dinallo, *Prosecuting Securities Fraud from a New York Perspective*, 5 N.Y.U.J. LEGIS. & PUB. POL’Y 41, 43 (2001) (Dinallo, the former Bureau Chief of the Investor Protection Bureau of the New York Attorney General’s Office, acknowledges the extraordinary scope of the Martin Act and states that it “is one of the broadest anti-fraud statutes ever devised, at least in a democratic society”).

sentation or omission of material fact when engaged in to induce or promote the issuance, distribution, exchange, sale, negotiation or purchase of securities.”⁴⁸ New York courts have declared that the term “fraud” as used in the Martin Act should be broadly defined to include “all deceitful practices contrary to the plain rules of common honesty.”⁴⁹ Furthermore, the Attorney General does not have to prove that the accused had a specific intent to commit fraud in order to bring a successful action under the Martin Act, as the statute lacks a scienter requirement.⁵⁰ Nor is he required to show that fraud actually occurred or to prove reliance or damages.⁵¹ As a result, the Martin Act has been described as imposing “virtually *per se* . . . liability” for securities fraud; if the Attorney General can prove that the accused made a material misrepresentation or omission during a securities transaction, then the accused has violated the Martin Act.⁵²

The jurisdictional scope of the Martin Act is similarly far-reaching. The Act has been construed to permit the prosecution of securities fraud “that takes place in New York, that is directed to New York from outside the state, and that emanates from New York.”⁵³ Because nearly all U.S. public companies are traded on the New York Stock Exchange or NASDAQ, the Martin Act’s broad jurisdictional reach grants the Attorney General authority

48. *New York State’s Martin Act: A Primer*, *supra* note 34.

49. Aaron M. Tidman, Note, *Securities Law Enforcement in the Twenty-First Century: Why States Are Better Equipped Than the Securities and Exchange Commission to Enforce Securities Law*, 57 SYRACUSE L. REV. 379, 391 (2007) (quoting *People v. Federated Radio Corp.*, 154 N.E. 655, 657 (N.Y. 1926)).

50. See Wendy N. Davis, *Up Against Wall Street: New York’s Business Laws Make It There, But Can They Make It Everywhere?*, 88 A.B.A.J. 30 (2002) (“Unlike federal securities laws, the Martin Act does not require the government to prove a specific intent to defraud. Instead, a person can commit fraud under the Martin Act simply by making representations about the future ‘beyond reasonable expectations’ to persuade a buyer to purchase stock.”).

51. See *New York State’s Martin Act: A Primer*, *supra* note 34 (“Later cases have further clarified that the common law fraud elements of . . . reliance and damages are not required in order to demonstrate a violation of the Martin Act.”).

52. See *McTamaney*, *supra* note 42, at 21 (“So, in several key respects, the Martin Act arguably is hardly a fraud statute at all, but rather it specifies virtually *per se* criminal and civil liability if the designated acts occur.”). In contrast, § 10b-5 of the 1934 Securities Exchange Act requires showings of reliance, damages and scienter. See Katya Jestin & Matthew Cipolla, *Reimposing a Scienter Requirement in the Martin Act*, N.Y. L.J. (2013).

53. Tidman, *supra* note 49, at 391.

over the vast majority of securities transactions executed in the United States.⁵⁴

Additionally, New York courts often describe the Martin Act's jurisdictional reach in expansive terms and exhibit a favorable disposition toward the Act. The Fourth Department has instructed that the Martin Act should "be liberally construed [so] that its beneficent purpose may, so far as possible, be attained."⁵⁵ Similarly, the New York Court of Appeals has repeatedly "observed that the Martin Act was enacted to create a statutory mechanism in which the Attorney General would have broad regulatory and remedial powers to prevent fraudulent practices by investigating and intervening at the first indication of securities fraud on the public."⁵⁶ Commentators have cited these factors when arguing that the Martin Act provides the New York Attorney General with more power than other states' securities regulators and with an edge over the SEC.⁵⁷

Although the Martin Act may be described as "one of the legal weapons most feared on Wall Street" today,⁵⁸ that wasn't always the case. Despite the Act's broad allocation of power to the Attorney General, most office holders did not exercise that power aggressively.⁵⁹ Furthermore, until recently, Martin Act investigations and prosecutions were rarely directed at Wall Street.⁶⁰ Instead, former Attorneys General used the law to target con men and to shut down run-of-the-mill frauds like Ponzi schemes and

54. See *id.* ("Almost all public companies are traded in New York on the NYSE or the NASDAQ, so almost all securities touch the state and fall within the Martin Act's jurisdiction.")

55. *People v. Lexington Sixty-First Assocs.*, 38 N.Y.2d 588, 595 (N.Y. 1976).

56. *Assured Guar. (UK) Ltd. v. J.P. Morgan Inv. Mgmt., Inc.*, 962 N.E.2d 765, 768 (N.Y. 2011).

57. Tidman, *supra* note 49, at 390; *New York State's Martin Act: A Primer*, *supra* note 34.

58. Michael J. de la Merced, *In JPMorgan Case, the Martin Act Rides Again*, N.Y. TIMES (Oct. 2, 2012), http://dealbook.nytimes.com/2012/10/02/in-jpmorgan-case-the-martin-act-rides-again/?_r=0 [<https://perma.cc/5PEX-Q9HL>].

59. See Ashby Jones, *Cuomo to E&Y: Let Me Introduce You to My Good Friend, Martin*, WALL ST. J. L. BLOG (Dec. 21, 2010, 4:39 PM), <http://blogs.wsj.com/law/2010/12/21/cuomo-to-ey-let-me-introduce-you-to-my-good-friend-martin> [<https://perma.cc/L3C6-GWW3>] ("The law dates to 1921, but wasn't widely used until the middle of 2001.")

60. See Nicholas Thompson, *The Sword of Spitzer*, LEGAL AFFAIRS (May–June 2004), http://www.legalaffairs.org/issues/May-June-2004/feature_thompson_mayjun04.msp [<https://perma.cc/68DQ-3VCH>] ("For three-quarters of a century, an unspoken gentleman's agreement bound the moneymen of Wall Street and the New York attorney general's office.")

boiler rooms.⁶¹ The Martin Act was very rarely employed to investigate the questionable dealings of legitimate financial institutions.⁶² Thus, “an unspoken gentleman’s agreement bound the moneymen of Wall Street and the New York [A]ttorney [G]eneral’s office,” whereby the Attorney General would refrain from using the Martin Act to prosecute powerful players in the banking industry.⁶³

All of this changed when Eliot Spitzer was elected Attorney General. Spitzer resurrected the Martin Act as part of his effort to clean up the financial following the stock market crash of 2000 and the Enron scandal of 2001.⁶⁴ He first used the statute to target Merrill Lynch and Salomon Smith Barney, where he uncovered evidence that the firms’ analysts recommended subpar stock to their clients in order to secure benefits for their investment banking divisions.⁶⁵ Spitzer eventually persuaded each institution to agree to a large settlement.⁶⁶ He then launched an investigation into New York’s entire investment banking industry: working with both federal securities regulators and state regulators from California, Massachusetts, Alabama, Texas, New Jersey, Illinois and Utah, Spitzer exacted a total of \$1.4 billion in fines from the ten largest investment banking firms.⁶⁷ In so do-

61. *See id.* (“Acceptable targets through the years included shady pharmacists, Ponzi schemes, and peddlers of fraudulent Salvador Dali lithographs.”).

62. *See id.* (“The AG got to use an astonishingly powerful state securities law called the Martin Act, but not against the big boys.”).

63. *Id.*

64. *See* Walha & Filusch, *supra* note 44, at 1114 (“In 2000, as the stock market began to collapse and news of the excesses of Wall Street spread through the media, Spitzer began to investigate the industry that would make him a national (and international) figure [by using] the Martin Act.”); McTamane, *supra* note 42, at 19 (“Since Enron, New York’s Attorney General Eliot Spitzer and Manhattan District Attorney Robert Morgenthau have made well-publicized use of New York’s 1921 Martin Act.”).

65. *See* Walha & Filusch, *supra* note 44, at 1114 (“Spitzer’s first high profile use of the Martin Act was against Merrill Lynch for conflicts of interest among its stock analysts. . . . Following the settlement with Merrill Lynch, Spitzer announced an investigation into Jack Grubman, an analyst with Solomon Smith Barney.”).

66. *See id.* (“These damning emails and the publicity surrounding them when they were released eventually forced Merrill Lynch into a settlement with Spitzer . . .”). Following the settlement with Merrill Lynch, Spitzer announced an investigation into Jack Grubman, an analyst with Solomon Smith Barney.

67. Thompson, *supra* note 60 (“Spitzer used the Martin Act to bring a [] public case . . . against the entire investment banking industry. New York’s 10 biggest investment firms were forced to pay a total of \$1.4 billion in fines.”); *see also* McTamane, *supra* note 42 (referencing “[t]he settlement being negotiated with New York’s major brokerage firms agreeing to pay more than \$1.4 billion for allegedly biased ratings on stocks to help win investment banking business” as one of the most prominent Martin Act proceedings. “The ten firms would pay fines, sever links between research and investment banking, and fund

ing, Spitzer used the Martin Act to prosecute securities fraud cases that the SEC and the U.S. Attorney's Office had previously declined to pursue.⁶⁸

Spitzer's utilization of the Martin Act to go after the biggest players in the banking industry "rocked the financial world."⁶⁹ However, Spitzer was criticized for overreaching his jurisdiction by acting as a regulator instead of a prosecutor.⁷⁰ Still, Spitzer's use of the Martin Act was effective in inducing change on Wall Street.⁷¹ Moreover, Spitzer's successors were not deterred from exercising their power under the Act in a similar manner.⁷² Andrew Cuomo continued to use the Martin Act to aggressively combat fraud within the financial services industry while serving as Attorney General from 2007 to 2010, and Eric Schneiderman has done the same since he entered office in 2011.⁷³

III. CAN THE MARTIN ACT BE USED TO PROSECUTE MISREPRESENTATIONS REGARDING THE OPERATION OF DARK POOLS?

While the Martin Act grants the New York Attorney General extraordinary authority to investigate and prosecute securities

independent stock research for investors. Regulators in California, Massachusetts, Alabama, Texas, New Jersey, Illinois and Utah all took parts of the investigation, and each will take part of the recovery").

68. See Jeff Izant, Note, *Mens Rea and the Martin Act: A Weapon of Choice for Securities Fraud Prosecutions?*, 2012 COLUM. BUS. L. REV. 913, 917 (2012) ("Spitzer used . . . the Martin Act to hold financial executives and their companies accountable for criminal securities fraud when the SEC or the U.S. Attorney's Office did not pursue the cases themselves.").

69. Richard Pérez-Peña & Patrick McGeehan, *Assault on Wall St. Misdeeds Lifts Spitzer's U.S. Profile and Makes Enemies*, N.Y. TIMES (Nov. 4, 2002), <http://www.nytimes.com/2002/11/04/nyregion/assault-on-wall-st-misdeeds-lifts-spitzer-s-us-profile-and-makes-enemies.html> [<https://perma.cc/BPN6-5HCC>].

70. See Walha & Filusch, *supra* note 44, at 1117–18 ("One of the charges often levied against Spitzer is that he has acted, not as a prosecutor, but rather as a regulator.").

71. See Tidman, *supra* note 49, at 381 ("[T]he attorney general has proven that state securities law enforcement has been more effective than federal securities law enforcement in the twenty-first century.").

72. See, e.g., Jones, *supra* note 59 ("Spitzer wielded the law aggressively . . . Cuomo has largely followed suit."); Miles Mogulescu, *The Man Who May Bring the Banksters to Justice (If They Don't Break His Knees First)*, HUFFINGTON POST BLOG (Aug. 29, 2011, 9:43 AM), http://www.huffingtonpost.com/miles-mogulescu/eric-schneiderman-new-york_b_940004.html [<https://perma.cc/R7E7-M7PA>] ("Cuomo has largely followed suit, using the [Martin Act] to sue Bank of America.").

73. See Jones, *supra* note 59 ("Spitzer wielded the law aggressively . . . Cuomo has largely followed suit."); Mogulescu, *supra* note 72 ("Schneiderman seems intent on using the formidable weapons on his office to investigate possible financial crimes.").

fraud, there are limits to its scope. One of these limits is that Martin Act cases have traditionally concerned allegations of fraud that can be tied to specific securities transactions.⁷⁴ If the Martin Act indeed requires this type of nexus between a material misstatement or omission and an investor's decision to purchase or sell a security, then Attorney General Schneiderman will have difficulty using the Act to prosecute misrepresentations regarding dark pools, as most misrepresentations that a broker would make to persuade a client to use its dark pool would probably concern the operation of the trading platform as a whole.⁷⁵

In his investigation and prosecution of Barclays, Schneiderman attempted to use the Martin Act to crack down on questionable activity within dark pools by targeting brokers' misrepresentations about the functioning of their proprietary exchanges.⁷⁶ One of Barclays' main arguments in its defense was that actions under the Martin Act must concern the purchase or sale of securities and that, because the alleged misrepresentations at issue concerned the general operations of Barclays' dark pool, they were not actionable.⁷⁷ If the New York courts had accepted this argument, it would have made it more difficult for Schneiderman to increase his office's regulatory oversight of dark pools and to prosecute fraud in the operation of proprietary trading platforms.

Lack of precedent addressing the specific argument that the Martin Act requires a close connection between actionable misrepresentations and specific securities transactions makes it difficult to determine how courts will decide the issue.⁷⁸ On one

74. See, e.g., Barclays' Memorandum of Law in Support of its Motion to Dismiss the Complaint at 12, *People v. Barclays Capital Inc.*, 1 N.Y.S.3d 910 (N.Y. Sup. Ct. 2015) ("Because the alleged misrepresentations related solely to the manner in which Barclays processed trades for clients — not to any investment decision regarding a security — the alleged misrepresentations fall outside the Martin Act.")

75. See, e.g., The State of New York's Memorandum of Law in Opposition to Barclays' Motion to Dismiss at 7–8, *People v. Barclays*, 1 N.Y.S.3d 910 ("Since at least 2011, Barclays has made false representations in marketing materials, sales meetings, presentations, and elsewhere regarding how it treated client orders entrusted to it for routing and execution . . . The above misrepresentations were part of an overarching scheme: Barclays sought to make investors believe that its brokerage services and dark pool were operated to offer meaningful protection from predatory or aggressive high frequency trading, when in truth, Barclays was exposing its clients to predatory high frequency traders.")

76. *Id.*

77. See Barclays' Memorandum of Law in Support of its Motion to Dismiss the Complaint at 7–8, *People v. Barclays*, 1 N.Y.S.3d 910.

78. See, e.g., *People v. Barclays*, 1 N.Y.S.3d at 916 ("This is a novel issue. The cases cited by the NYAG and Barclays are inapposite. They . . . do not address this specific issue.")

hand, New York's highest court has instructed that the Martin Act is to "be liberally construed in order that its beneficent purpose may, so far as possible, be attained" for decades.⁷⁹ New York courts have also held that "[t]he purpose of the law is to prevent all kinds of fraud in connection with the sale of securities."⁸⁰ This emphasis on broad scope and liberal construction seems to weigh in favor of interpreting the law to allow the Attorney General to apply it to fraudulent misstatements regarding the operation of trading platforms, including dark pools. After all, when a broker's misrepresentations persuade a customer to authorize trading on his behalf within a dark pool, the misrepresentations can be said to "induce or promote" the "exchange, sale, negotiation or purchase" of securities,⁸¹ which the Martin Act provides as grounds for application of the statute. While the Attorney General has never before used the Martin Act to prosecute fraud that occurs in this context,⁸² courts may still adopt a novel interpretation of the law because doing so would further its purpose and benefit consumers.⁸³ Schneiderman's office has relied heavily on these arguments in its case against Barclays.⁸⁴

On the other hand, Barclays has argued that reading the Martin Act broadly so as to give effect to its purpose interprets the law so expansively as to essentially rewrite it: in its reply brief in support of its motion to dismiss the Attorney General's Martin Act claims, Barclays argued that accepting the Attorney General's argument "would render the Martin Act virtually unlimited in scope."⁸⁵ If the court were to find that a broker's misrepresentations regarding the operation of a dark pool did not influence investors' decisions to buy or sell specific securities but rather

79. *People v. Lexington Sixty-First Assocs.*, 38 N.Y.2d 588, 595 (N.Y. 1976). *See also* *People v. Charles Schwab & Co., Inc.* 971 N.Y.S.2d 267, 270 (N.Y. App. Div. 2013) ("[T]he statute is remedial and should be broadly construed in order to attain its beneficent purpose.").

80. *People v. Federated Radio Corp.*, 244 N.Y. 33, 38 (N.Y. 1926).

81. N.Y. GEN. BUS. LAW § 352-c(1)(c) (McKinney 1982).

82. *People v. Barclays*, 1 N.Y.S.3d at 916 (describing the question of the Martin Act's applicability to fraudulent misrepresentations concerning the operation of trading platforms as "a novel issue.").

83. *See, e.g.*, The State of New York's Memorandum of Law in Opposition to Barclays' Motion to Dismiss at 10, *People v. Barclays*, 1 N.Y.S.3d 910 ("The [New York] Court of Appeals has held consistently that the Martin Act should be liberally construed, in order that its beneficent purpose may, so far as possible, be attained.").

84. *See, e.g., id.* at 10–11; Transcript of Oral Argument at 17–18, *People v. Barclays*, 1 N.Y.S.3d 910.

85. *Id.* at 8.

affected their choice of trading platform, it may conclude that the plain language of the Martin Act does not reach the misrepresentations at issue.⁸⁶

Additionally, Barclays cited cases supporting its argument that the Martin Act “cannot be reasonably extended to cover a purchaser who does not make his purchase from the misrepresenter” to argue that the Attorney General’s Martin Act claims should be dismissed.⁸⁷ In these cases, the courts dismissed Martin Act claims despite the fact that the plaintiffs entered into securities transactions as a result of the defendants’ fraudulent misrepresentations, because the defendants were not parties to the transactions and thus not subject to Martin Act liability with respect to them.⁸⁸ This principle provides support for dismissal of the Attorney General’s Martin Act claims, unless he is able to show that Barclays’ misrepresentations persuaded investors to purchase securities from *Barclays* within its dark pool.

In February 2015, Justice Kornreich of the New York Supreme Court denied Barclays’ motion to dismiss the Attorney General’s Martin Act claims in *New York v. Barclays Capital*.⁸⁹ In so doing, Justice Kornreich accepted the Attorney General’s argument that fraudulent misrepresentations regarding the operation of trading platforms are actionable under the Martin Act. While Justice Kornreich acknowledged the novelty of the issue before the court and the lack of relevant precedent,⁹⁰ she rejected Barclays’ argument that statements about a trading platform are too far removed from investors’ trading decisions to qualify as “investment decisions” under the Martin Act.⁹¹ Instead, she found that “the choice of trading platform can have a significant

86. See, e.g., *All Seasons Resorts Inc. v. Abrams*, 497 N.E.2d 33, 35 (N.Y. 1986) (stating that the purpose of the Martin Act is to “protect[] the public from fraudulent exploitation in the offer and sale of securities”) (emphasis added).

87. Barclays’ Reply Memorandum of Law in Further Support of its Motion to Dismiss the Complaint at 4, *People v. Barclays*, 1 N.Y.S.3d 910 (quoting *Kaufman v. Chase Manhattan Bank, N.A.*, 581 F. Supp. 350, 355 (S.D.N.Y. 1984)).

88. See *Kaufman*, 581 F. Supp. 350 (where misrepresentations made by bank officers were not actionable under the Martin Act when they caused the plaintiff to buy shares of a corporation from a third party); *Herdegen v. Paine, Webber, Jackson & Curtis*, 220 N.Y.S.2d 459 (1961) (where misrepresentations made by a broker were not actionable under the Martin Act when they caused the plaintiff to purchase securities from another broker).

89. *People v. Barclays*, 1 N.Y.S.3d 910.

90. See *id.* at 916 (“This is a novel issue. The cases cited by the NYAG and Barclays are inapposite. They . . . do not address this specific issue.”).

91. *Id.*

impact on the outcome of a trade,” and that “where it is alleged that . . . investors chose to execute their trades in the Dark Pool because trading on that platform was thought to directly impact the outcome of the trades, their decision to trade in the Dark Pool is very much an investment decision.”⁹² Justice Kornreich conceded that “Barclays’ arguments [were] not entirely unreasonable” but noted that precedent counseled that doubts about the applicability of the Martin Act should be resolved in the Attorney General’s favor.⁹³

While Justice Kornreich’s decision is not a definitive ruling, it is the only clear judicial statement regarding the Martin Act’s applicability to misrepresentations concerning the operation of dark pools. As such, it gives powerful support to the argument that the Attorney General may use the law to police fraudulent statements made by brokers while promoting their firms’ dark pools to investors.

IV. POLICY CONSIDERATIONS REGARDING THE USE OF THE MARTIN ACT TO PROSECUTE MISREPRESENTATIONS CONCERNING THE OPERATION OF DARK POOLS

This Part discusses various policy considerations that ultimately support a broad reading of the Martin Act, which would allow the New York Attorney General to use the law to prosecute misrepresentations concerning trading platforms such as dark pools. There is room for disagreement about the policy implications of such an expansive interpretation of the Martin Act. On one hand, it is easy to see how permitting the Attorney General to use the Martin Act to crack down on banks’ unscrupulous practices in promoting their dark pools would be beneficial for consumers and would further the purpose of the law. On the other hand, such a broad reading of the Martin Act may be an impermissible expansion of the scope of a law that is already criticized for the extraordinary amount of power that it grants the Attorney General. Furthermore, allowing the Attorney General to use the Martin Act to police private exchanges could exacerbate certain administrability problems that some attorneys and lawmak-

92. *Id.*

93. *Id.* at 917 (“[T]his court views the Court of Appeals’ guidance on the Martin Act to be that doubts in favor of the Martin Act’s applicability should be resolved in the NYAG’s favor.”).

ers have criticized the law for creating.⁹⁴ Specifically, the Attorney General's aggressive use of the Martin Act to regulate the financial industry may create friction with federal regulators.⁹⁵ While state blue sky laws and federal securities regulations necessarily overlap, a state prosecutor who uses a powerful state law to influence national capital market regulatory policy arguably infringes on the jurisdiction and mandate of the SEC.⁹⁶ If each state enforced its blue sky law as aggressively as Schneiderman seeks to enforce the Martin Act, the financial industry could find itself in an untenable situation, in which various regulators with overlapping authority imposed conflicting standards on industry participants.

Since Eliot Spitzer began using the Martin Act to aggressively police the financial industry, both industry insiders and lawmakers have criticized what they consider to be the inappropriate application of state law to problems that are essentially national in scope.⁹⁷ They find fault with the extraordinary authority that the Martin Act grants the New York Attorney General, arguing that it allows him to exert more influence on the nation's financial industry than is appropriate for any state officer. For example, in a June 2002 letter to the editor of the New York Times, Representative Michael Oxley expressed concern that the New York Attorney General's activism in policing the financial industry threatened to usurp the authority of the SEC and the industry's self-regulatory organizations.⁹⁸ He warned that if every state attorney general were to apply its securities laws as aggressively as the New York Attorney General enforces the Martin Act, then

94. See, e.g., Davis, *supra* note 50, at 30 (summarizing concerns expressed by former Representative Michael Oxley and Jan Handzlik, the former chair of the White Collar Crime Committee of the ABA Criminal Justice Section, regarding administrability problems created by the Martin Act).

95. See Michael G. Oxley, Letter to the Editor, *Who Should Police the Financial Markets?*, N.Y. TIMES (June 9, 2002), <http://www.nytimes.com/2002/06/09/business/1-who-should-police-the-financial-markets-447650.html> [<https://perma.cc/4BEU-JV55>] (arguing the SEC is better positioned to undertake this regulation than the New York Attorney General).

96. See *id.* (arguing that "setting policy for our national capital markets is properly the duty and responsibility of the Securities and Exchange Commission" and that the role of state attorneys general should be limited to enforcing state laws).

97. See Davis, *supra* note 50, at 30 ("[O]pinion remains mixed on the wisdom of using a New York state law to address a problem with national implications.").

98. See Oxley, *supra* note 95 ("What we are witnessing is nothing less than a regulatory coup that would usurp the proper role of the S.E.C. and the self-regulatory organizations.").

“balkanization” of securities laws could result, in which “every firm would have to answer to [the different legal requirements imposed by] every attorney general.”⁹⁹ The two concerns articulated by Representative Oxley — the potential usurpation of the SEC’s authority and overregulation by multiple government actors — are shared by many of the Martin Act’s opponents.¹⁰⁰

Federal lawmakers are aware of the possibility for conflict between state and federal securities regulation, and Congress has considered bills that would prevent states from imposing their own legal standards on businesses that are already subject to oversight by the SEC.¹⁰¹ For example, the proposed Securities Fraud Deterrence and Investor Restitution Act contains provisions that would ban states from passing laws or reaching settlements with requirements that “differ from or are in addition to the requirements in those areas established by the [SEC or] by a national securities exchange or self regulatory organization.”¹⁰² The bill engendered significant controversy when it was proposed; it was supported by the SEC and many House Republicans and opposed by state securities regulators and many Democrats.¹⁰³ While federal legislation has preempted state securities laws in specific areas,¹⁰⁴ the provisions of the proposed Securities Fraud Deterrence and Investor Restitution Act were the closest that Congress has come to completely preempting states’ authori-

99. Davis, *supra* note 50, at 30.

100. See, e.g., *id.* at 30 (“It’s certainly unusual to have a state attorney general take action that has such broad-based impact,” says Boston lawyer Stanley Keller, chair of the ABA Business Law Section’s Federal Regulation of Securities Committee. Investment firms’ conduct, Keller says, is ‘a national market phenomenon’ best handled by the Securities and Exchange Commission.”).

101. See *id.* (“[A]mendments were proposed to both House and Senate bills that would prevent states from imposing laws over businesses subject to the SEC.”).

102. Tidman, *supra* note 49, at 404; Amendment to H.R. 2179 offered by Mr. Baker, available at <http://financialservices.house.gov/media/pdf/108cmhr2179am1p1.pdf> [<https://perma.cc/MD2X-F843>] (last visited July 31, 2016).

103. Mindy Olson, Note, *The Securities Fraud Deterrence and Investor Restitution Act: More Effective than Current Regulation?*, 30 J. CORP. L. 425, 437 (2005) (“As the bill stood in 2003, which included the preemption provision, there were parties who supported the bill and parties who opposed it. In general, the SEC supports it, as do several House Republicans. It is, of course, opposed by state securities regulators, including New York Attorney General Spitzer [and] congressional Democrats.”).

104. See, e.g., Jennifer O’Hare, *Preemption Under the Securities Litigation Uniform Standards Act: If It Looks Like a Securities Fraud Claim and Acts Like a Securities Fraud Claim, Is It a Securities Fraud Claim?*, 56 ALA. L. REV. 325, 325 (2004) (“In the Securities Litigation Standards Act of 1998 (SLUSA), Congress took the unusual step of preempting state law, deciding that federal courts should be the exclusive venue for many securities fraud class actions.”).

ty to enforce their blue sky laws.¹⁰⁵ The fact that “Congress has generally left the states’ securities law enforcement [power] untouched” indicates that both state and federal agencies may properly exercise overlapping law enforcement authority in the securities industry.¹⁰⁶

A final argument against an expansive interpretation of the Martin Act is that by using the Martin Act to aggressively increase his oversight of the securities industry, the Attorney General acts more like a regulator than a prosecutor.¹⁰⁷ According to this argument, the Attorney General’s role should be to enforce state law within the boundaries of the state.¹⁰⁸ He should not use state law to “set[] policy for our national capital markets,” as that policy-making role is “properly the duty and responsibility of the Securities and Exchange Commission and the self-regulatory organizations.”¹⁰⁹ However, interpreting the Martin Act broadly to allow Schneiderman to investigate and prosecute fraudulent misrepresentations concerning the operation of trading platforms would not necessarily allow him to assume a more regulatory role over dark pools. Even if Schneiderman undertook the investigation and prosecution of Barclays with the goal of “chang[ing] the dark pool business” in mind,¹¹⁰ his actions in that matter were those of a law enforcement officer, not those of a regulator. The Barclays case may have drawn attention to the need for greater regulatory oversight of dark markets, but Schneiderman’s use of the Martin Act was limited to targeting fraud committed by Barclays — an act that is prosecutorial, rather than regulatory, in nature.

Other arguments weigh in favor of adopting an interpretation of the Martin Act that would allow the New York Attorney General to investigate and prosecute fraudulent practices in the pro-

105. Tidman, *supra* note 49, at 398 (“Representative Baker’s proposed provisions in the Securities Fraud Deterrence and Investor Restitution Act was the closest that Congress has come to preempting state authority to enforce securities law.”).

106. *See id.* (discussing “the need for overlap in a dual system” of federal and state regulatory authority).

107. *See* Walha & Filusch, *supra* note 44, at 1117 (“One of the charges often levied against Spitzer is that he has acted, not as a prosecutor, but rather as a regulator.”).

108. *See* Oxley, *supra* note 95 (“I appreciate the important role of the state attorneys general, who have the duty of enforcing state laws.”).

109. *Id.*

110. *See* Charlie Gasparino, *NY AG Preps Case Against Credit Suisse Dark Pool*, FOX BUS. (July 27, 2015), <http://www.foxbusiness.com/features/2015/07/27/ny-ag-preps-case-against-credit-suisse-dark-pool.html> [<https://perma.cc/ZGK7-DKPB>].

motion and operation of dark pools. First, the Martin Act allows the New York Attorney General to prosecute alleged fraud more easily than federal regulators can.¹¹¹ This is largely due to the Martin Act's lack of a scienter requirement and its expansive definition of the term "fraud."¹¹² As there is widespread consensus that dark pools are underregulated,¹¹³ it makes sense to encourage the efforts of agencies that are willing and able to investigate and prosecute fraudulent activity in that area of the financial industry — regardless of whether those agencies are federal regulators or the offices of state attorneys general.

Next, the New York Attorney General can use his power under the Martin Act to work cooperatively with the SEC to further common goals rather than to usurp that agency's authority. When Congress passed federal securities legislation the 1930s, it intended federal investigations and prosecutions to supplement those of the states, not preempt them.¹¹⁴ The SEC has also acknowledged the advantages of federal-state enforcement cooperation in recent years.¹¹⁵ Consequentially, it is appropriate for state officers to target areas of the securities industry that they

111. See Cyrus Sanati, *Cuomo and the Broad Power of the Martin Act*, N.Y. TIMES: DEALBOOK (May 13, 2010, 2:28 PM), <http://dealbook.nytimes.com/2010/05/13/cuomo-and-the-broad-power-of-the-martin-act> [<https://perma.cc/X8YG-JNRH>] (noting the Martin Act "makes it easier for Mr. Cuomo to prosecute a case than the standards that federal regulators follow in their investigations" because "the burden of proof needed to obtain a conviction is lower").

112. See *supra* Part I; Tidman, *supra* note 49, at 392 ("The Martin Act's . . . broadly interpreted definition of "fraud," and lack of scienter, give the New York State Attorney General more authority to enforce securities laws than any other state regulator . . ."). See also *Federated Radio Corp.*, 154 N.E. at 657 (In the context of the Martin Act, "[t]he words 'fraud' and 'fraudulent practice' . . . should be given a wide meaning, so as to include all acts, although not originating in any actual evil design or contrivance to perpetuate fraud or injury upon others, which do by their tendency to deceive or mislead the purchasing public come within the purpose of the law.").

113. See *supra* Part I.

114. See Tidman, *supra* note 49, at 398 ("When Congress passed the Securities and Exchange acts, it intended federal securities regulation and enforcement to supplement state securities regulation and enforcement and to serve as an interstate gap filler.").

115. See Elisse B. Walter, Commissioner, U.S. Sec. and Exch. Comm'n., Remarks Before the North American Securities Administrators Association 2011 Annual Conference (Sept. 12, 2011), available at <https://www.sec.gov/news/speech/2011/spch091211ebw.htm> [<https://perma.cc/7NXZ-EPAM>] ("[F]ederal-state cooperation can go a long way towards ensuring that investors remain confident in our markets. . . . The SEC's enforcement division and [state] agencies view activities that run afoul of our securities laws from different vantage points, meaning more effective scrutiny of suspicious participants and trends. Each agency has its own advantages . . . that can come together to make stronger cases. We each benefit from the tips and complaints that we pass each other's way. The coordination of state and federal action maximizes the reach of our resources and can allow each of us to do more for investors within all-too-tight budgets.").

perceive to be under-regulated within their jurisdictions. Over the past fifteen years, there have been several occasions when the New York Attorney General has used the Martin Act to fill a “regulatory vacuum” by cracking down on fraudulent activity that the SEC had previously overlooked.¹¹⁶ For example, during the late 1990s, the SEC was “a timid, poorly managed bureaucracy at a time when the markets it police[d] and frauds it [sought] to prevent were increasingly complex.”¹¹⁷ Its relative inertia during this period opened the door for Attorney General Spitzer to use the Martin Act to combat fraudulent practices in the securities industry that had flown under the SEC’s radar.¹¹⁸ Spitzer’s investigation of Merrill Lynch provides one example of his office’s efforts to fill a regulatory void left open by the SEC.¹¹⁹ Conflicts of interest between the research analysts and investment banking divisions of Wall Street firms were rampant during this period;¹²⁰ analysts routinely recommended subpar stock to their clients in order to gain the stock issuers’ business for their firms’ investment bankers.¹²¹ However, the SEC did nothing to address this problem until after the New York Attorney General’s Office took action.

When the New York Attorney General uses his power under the Martin Act to target fraudulent activity that has not been addressed by federal regulators, his investigations often spur the federal agencies to action.¹²² For example, after federal regulators became aware of Spitzer’s investigation of Merrill Lynch,

116. See Tidman, *supra* note 49, at 381 (“The New York State Attorney General saw an area of the law where federal regulators had failed, and he filled that regulatory vacuum. With the Martin Act as his sword, Mr. Spitzer induced change in industries that had been cheating the rules for years under the inefficacy and complacency of federal regulators.”).

117. Mark Maremont & Deborah Solomon, *Missed Chances: Behind SEC’s Failings: Caution, Tight Budget, ‘90s Exuberance*, WALL STREET J. (Dec. 24, 2003), <http://www.wsj.com/articles/SB107223513870781900> [<https://perma.cc/V55V-HYC6>].

118. See Lane, *supra* note 42, at 329 (“The number of enforcement actions initiated by the SEC dropped from 525 in 1999 to 484 in 2001. This combination of factors provided an opening for assertive state officials such as Spitzer to act when the wave of financial scandals broke in 2002.”).

119. See *supra* Part II.

120. See John Cassidy, *The Investigation: How Eliot Spitzer humbled Wall Street*, NEW YORKER (Apr. 7, 2003), <http://www.newyorker.com/magazine/2003/04/07/the-investigation> [<https://perma.cc/XPU6-CUFU>] (“The problems were structural. . . . Everybody had permitted analysts to become appendages of the investment-banking system.”).

121. See Walha & Filusch, *supra* note 44, at 1114 (“Spitzer found several examples of [one analyst] bashing stocks within Merrill Lynch that he was publicly touting.”).

122. See Tidman, *supra* note 49, at 381 (“The New York State Attorney General’s actions eventually woke-up Congress and the SEC, and federal regulators began working with Mr. Spitzer to more effectively tackle securities fraud.”).

“the S.E.C., the New York Stock Exchange . . . , and the National Association of Securities Dealers . . . quickly launched a joint investigation into Wall Street research practices.”¹²³

While aggressive law enforcement by a state attorney general in a field that is also subject to federal regulation may sometimes cause friction,¹²⁴ state and federal agencies may be able to combat illegal practices on Wall Street more effectively by working together.¹²⁵ Allowing federal regulators and state attorneys general to exercise concurrent jurisdiction over under-regulated areas of the securities industry (such as dark pools) is probably the most effective way to protect investors, which is the ultimate goal of both state and federal securities legislation.

Finally, fears concerning the “balkanization” of securities laws are likely overstated, at least insofar as they relate to the topic of this Note. While the Martin Act is unique compared to other states’ blue sky laws in that it grants the New York Attorney General extraordinary investigatory and prosecutorial powers, similar standards for fraud exist across most other securities statutes at both the state and federal level.¹²⁶ As a result, critics of the existing dual regulatory system for securities law enforcement “exaggerate when they complain of an unjustified need to comply with fifty or more conduct standards.”¹²⁷ Balkanization is most likely to occur, if at all, with respect to enforcement policies and practices rather than as a result of conflicting legal standards.¹²⁸ Even if banks must take additional measures to comply

123. Cassidy, *supra* note 120, at 65 (“The regulators divvied up the top dozen firms. At the national level, the S.E.C., the N.Y.S.E., and the N.A.S.D. took several firms each to examine. At the local level, New York and California each took two firms, and eight other states . . . took one each . . . [so that] every big firm on Wall Street was being scrutinized by two sets of investigators.”); *see also* Tidman, *supra* note 49, at 393 (“The New York State Attorney General’s settlement with Merrill Lynch forced other securities regulators out of their comfort zones.”).

124. *See, e.g.*, Cassidy, *supra* note 120, at 68 (describing deteriorating relations between Spitzer and SEC Chairman Harvey Pitt around the time of the Merrill Lynch settlement).

125. *See* Tidman, *supra* note 49, at 381 (“The New York State Attorney General’s actions eventually woke-up Congress and the SEC, and federal regulators began working with Mr. Spitzer to more effectively tackle securities fraud.”).

126. *See* Renee M. Jones, *Dynamic Federalism: Competition, Cooperation and Securities Enforcement*, 11 CONN. INS. L.J. 107, 127 (2005) (“Contrary to the assertions of preemption advocates, similar standards for fraud do exist across all securities regimes, state and federal.”).

127. *Id.*

128. *See id.* (“The problem of ‘balkanization,’ if it exists, relates mainly to enforcement policies and practices, and is not caused by contradictory or conflicting legal standards.”).

with the Martin Act's standards, it may be both appropriate and desirable for that law to help shape national antifraud policy. It is appropriate for the New York Attorney General to assume a prominent role in ensuring fair dealing within the financial industry, as a vast number of these transactions take place in New York.¹²⁹ While balkanization may be cause for concern in some areas of securities regulation, Schneiderman's use of the Martin Act to prosecute fraud relating to dark pools is unlikely to create the types of problems that proponents of the balkanization argument fear. This is because the conduct Schneiderman has targeted — Barclays' fraudulent misrepresentations regarding the operation of its dark pools — violates federal securities laws in addition to various state blue sky laws.¹³⁰ As a result, a desire to avoid increased balkanization in securities regulation carries little weight in restricting the New York Attorney General from using the Martin Act to crack down on unscrupulous practices in the promotion of dark pools.

V. CONCLUSION

An analysis of the relevant law and policy considerations supports Justice Kornreich's interpretation of the Martin Act, which allows the Attorney General to use his authority under the law to prosecute fraudulent misrepresentations regarding the operation of trading platforms. Dark pools are widely acknowledged to be under-regulated, which weakens the arguments that critics of the Martin Act typically make against broad interpretations of the law. For example, interpreting the Martin Act to allow the Attorney General to crack down on fraudulent practices relating to the promotion of dark pools is unlikely to impede SEC regulation, as the SEC does not exercise much oversight in this area. Furthermore, it is unlikely to lead to overregulation, which can result from the balkanization of securities laws. Finally, accepting a

129. See, e.g., *People v. Barclays Capital, Inc.*, 1 N.Y.S.3d 910 (N.Y. Sup. Ct. 2015) (“New York, the center of the financial universe, benefits greatly from having powerful blue sky laws.”).

130. See Press Release, U.S. Sec. and Exch. Comm'n, Barclays, Credit Suisse Charged With Dark Pool Violations (Jan. 31, 2016), available at <https://www.sec.gov/news/pressrelease/2016-16.html> [<https://perma.cc/7MMV-C98P>] (“The SEC's order finds that Barclays violated Section 17(a)(2) of the Securities Act, Securities Exchange Act Section 15(c)(3), Rules 15c3-5(c)(1)(i) and 15c3-5(b) of the SEC's Market Access Rule, and Rules 301(b)(2) and (10).”).

broad reading of the Martin Act that allows the Attorney General to hold brokers accountable when they make misrepresentations concerning the operation of their dark pools serves the primary goal of both the Martin Act and the federal securities laws — protecting investors from securities fraud.