

New Enforcement Powers for NYDFS? More Sanctions and More Defendants

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Legislation proposed as part of Gov. Andrew Cuomo's executive budget for 2021 would substantially expand the enforcement powers of the superintendent of the New York State Department of Financial Services, as well as the categories of firms and individuals against whom those powers may be leveled.

If enacted, this legislation could seriously impact many types of life insurance, annuity, and securities products and services that are offered or sold in New York.

Broader Penalties for Unlicensed Persons

The proposed legislation would dramatically increase the potential consequences for any individual or entity (each a "person") that fails to comply with any requirement to obtain a license (including any registration, accreditation, authority, charter, etc.) that is imposed by the New York financial services, banking, or insurance laws. Specifically, all conduct of such unlicensed persons would be subject to any penalties those laws provide for properly licensed persons engaging in the same conduct. (This would be in addition to the sanctions for being unlicensed.)

This amendment to the New York financial services law would greatly increase the risks attendant to, for example, failing to obtain any required licenses under the New York insurance law (but not such failures under New York securities law). The impact of this would be further magnified by the below-mentioned ten-fold increase proposed for penalties under the insurance law.

Ten-Fold Increase in Insurance Law Penalties

The administrative penalty that section 109 of the New York insurance law authorizes the DFS superintendent to impose for willful violations of the insurance law or regulations would be increased from \$1,000 to \$10,000 per offense.

Expanded Financial Services Law Civil Penalties

The proposed legislation would in several ways broaden section 408(a) of the New York financial services law, which currently authorizes the superintendent to levy a civil penalty of (i) up to \$5,000 per offense for fraud (including intentional material misrepresentations) involving a "financial product or service"; or (ii) up to \$1,000 for certain other violations of the financial services law or regulations thereunder. Specifically:

- The foregoing fraud component of current section 408(a) would be greatly broadened to cover "any fraud, misrepresentation [which no longer need be intentional or material], or unfair, deceptive, or abusive act or practice." This language theoretically could authorize administrative penalties for almost any conduct of which the superintendent disapproves.
- The current reference to \$1,000 would be eliminated, and the maximum sanction would be expanded so as to be, for the whole of section 408(b), the greater of (i) \$5,000 "for each offense"; (ii) twice the damages attributable to the offense; or (iii) twice the economic gain attributable to the offense. Accordingly, the penalty for each type of offense covered by section 408(b) would be potentially much increased.
- Language would be added that could make it easier for the superintendent to (i) sanction persons who offer financial products and services based on misconduct by their service providers; or (ii) sanction such service providers directly.

Nevertheless, immediately following its authorization of these penalties, section 408(b) would continue to provide that

“penalties for regulated persons under the insurance law shall be as provided for under the insurance law” and that the superintendent shall not impose “any penalty under this section in addition to any penalty or fine for the same act or omission that is imposed under the insurance law.”

This proviso, and similar language that appears for persons regulated under the banking law, could in many cases limit the impact of the proposed changes to section 408(b) for persons regulated under the insurance or banking laws. Nevertheless, persons regulated under the insurance laws would in any event potentially be subject to the above-mentioned proposed increase in the authorized penalties under section 109 of the insurance law.

Sweeping New Restitution Remedy

The proposed legislation would add a provision to the New York financial services law that would authorize the superintendent “[i]n any administrative proceeding or judicial action” under the financial services, banking, or insurance laws to “order the individual or entity subject to such proceeding or action to make restitution to all consumers harmed by such individual or entity’s conduct.” The language of this new provision, which is stated to be “in addition to any other penalty or sanction imposed by law,” does not prescribe any limits on the types of conduct or misconduct that may give rise to such restitution or any limits on the categories of persons that the superintendent may require to make such restitution.

Adding Securities to “Financial Product or Service”

Currently, the New York financial services law’s definition of “financial product or service” excludes, among other things, financial products or services “regulated for the purpose of consumer or investor protection by any other state agency, state department or state public authority.” The proposed legislation would remove this exclusion and would include within the definition “the sale or provision to a consumer or small business of any security, investment advice, or money management device.”

The proposed legislation would, nevertheless, exclude from the definition “financial products or services where the rules or regulations promulgated by the superintendent on such financial products or services would be preempted by federal law.” Subject to such federal preemption, therefore, securities sales and advice provided, for example, by broker-dealers or investment advisers would fall within the definition, notwithstanding that those securities activities may also be subject to regulation for the protection of consumers and investors by the New York attorney general pursuant to New York securities law.

This means that such securities-related activities could be in jeopardy, among other things, to the above-discussed expanded penalties under section 408(a) and the new restitution remedy.