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## MUNICIPAL LAW

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### *The City as Plaintiff: The Affirmative Litigation Division*

**I**N MY PREVIOUS columns, I described the role of the Office of the Corporation Counsel's approximately 650 lawyers in defending New York City's legal interests across a wide array of subjects. In the great majority of cases, the city is a defendant. For example, approximately 8,000 tort cases were contested in the last year alone.

Today, I focus on the Law Department's affirmative litigation division, whose task is to advance the interests of the city and its citizens through affirmative legal action in which the city assumes the role of plaintiff. Though far smaller in number of attorneys than the Law Department's defensive side, the city's "plaintiffs' bar" litigates a wide range of issues with substantial impact on the people of the city. While a number of other divisions in the Law Department regularly initiate affirmative claims in their areas of responsibility, the affirmative litigation division is the only division devoted entirely to this function.

The lawsuits brought by attorneys of the affirmative litigation division seek to protect public health and safety, protect city financial interests, and compel other levels of government (New York State and the federal government) to live up to their obligations to the city. Recent cases illustrate the scope of interesting matters handled by the division.

#### **Internet Cigarette Litigation**

• *Internet Cigarette Litigation:* The explosive growth of Internet commerce has given rise to Internet-based businesses that exploit the wide differences in cigarette prices created by uneven local, state and foreign cigarette taxation by permitting smokers in jurisdictions such as New York to purchase cigarettes over the Internet from low-tax jurisdictions. The purchases appear to "save" the buyer from having to pay the amount of the New York cigarette tax that is included in the purchase price at New York stores, a misimpression fostered by Internet sellers who deceptively tout their products as "tax-free." But the tax applies to cigarettes possessed in New York by any consumer, regardless of where purchased. Internet cigarette sellers actively thwart the collection of the tax by refusing to report purchases to state tax authorities, as required under the federal Jenkins Act.<sup>1</sup> Losses of state and local cigarette taxes nationally from this form of cross-border smuggling are estimated to exceed half a billion dollars a year, of which New York city's share is substantial.

Federal case law dating from the early 1970s, developed in response to cross-border cigarette smuggling transacted by telephone, holds cigarette mailings unaccompanied by Jenkins Act filings to be a scheme or artifice to defraud the taxing jurisdiction, in violation of federal mail and wire fraud statutes. City attorneys have



adapted this earlier case law to the civil Racketeer Influenced and Corrupt Organizations Act (RICO) statute, commencing RICO actions against approximately 30 Internet cigarette sellers.<sup>2</sup> These actions include first-time claims under New York's Public Health Law 1399-ll, which bars any Internet cigarette sales into New York State. The constitutionality of this statute was recently upheld by the U.S. Court of Appeals for the Second Circuit.<sup>3</sup>

The city's claims implicate an issue of RICO law that has divided New York's lower federal courts: Can a RICO plaintiff (here, the city) allege the predicate offenses of mail or wire fraud based on misrepresentations made not to the plaintiff but

to a government agency (here, New York State), where the regulatory or enforcement consequence of the misrepresentation injures the plaintiff?<sup>4</sup> The Second Circuit recently suggested that its prior decisions endorse this theory of liability.<sup>5</sup>

#### **Firearms Litigation**

• *Firearms Litigation:* In recent years, a significant number of municipal governments have brought suit against firearms manufacturers on the strength of data establishing that the marketing and distribution practices of the industry contribute substantially to the proliferation of illegal firearms in urban centers.<sup>6</sup> Building on the recent findings of a federal district court in Brooklyn in a suit brought by the National Association for the Advancement of Colored People (NAACP),<sup>7</sup> New York City's pending action against firearms manufacturers and distributors<sup>8</sup> may proceed to trial this year. Utilizing data showing that firearms industry practices result in a secondary illegal market for guns in the city, the city's complaint rests on the police power authority of a municipality to abate public nuisances, defined as conditions that substantially affect public health and safety and the public's right to free access to public places. The trial of the NAACP's action, recently completed in federal court, resulted in findings that the firearms industry could adopt sales practices to limit the proliferation of illegal guns. The NAACP court ultimately ruled, however, that the NAACP did not establish the unique injury required in a private plaintiff's public nuisance action. As a public plaintiff, the city need not have suffered unique injury and, by offering evidence comparable to that offered by the NAACP, the city seeks to prove that firearms manufacturing and distribution practices create a public nuisance.

A significant legal issue requiring resolution before the city case proceeds is whether dismissal of a similar public nuisance action against many of the same defendants brought by New York's attorney general forecloses the city's action as a matter of res judicata, as the defendants contend. The state's public nuisance claim against certain firearms manufacturers, brought in 2000, was dismissed by the Appellate Division, First Department in *People of State of New York v. Sturm Ruger*, 309 AD2d 91 (1st Dept.), appeal dismissed, 2003 NY LEXIS 3291 (2003). Whether different levels of government may be deemed to be in privity for res judicata purposes is

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an issue with profound implications for state and local governments that does not seem to have been addressed previously by New York courts. If the city is successful in resisting defendants' contention, it will be able not only to maintain its lawsuit against firearms manufacturers, but to initiate claims in the future where the state has not prevailed in a similar claim.

• **Securities Litigation:** The New York City pension funds are among the largest public holders of securities in the nation. At a time of highly publicized cases involving allegations of massive fraud by managers of global corporations, the city's interests in this area must be vigorously represented. The affirmative litigation division pursues claims against issuers of securities when fraudulent activity by company management impairs the value of city pension fund holdings. On behalf of the city pension funds, the division is participating in the securities fraud actions against Enron, WorldCom and Adelphia. In the *Cendant* securities litigation, division attorneys, working with attorneys from the Law Department's appeals division, persuaded the U.S. Court of Appeals for the Third Circuit to overturn a \$262 million fee award and send the issue back to the district court, where a settlement resulted in a savings to the class of \$207 million.<sup>9</sup> Of the three public pension funds sharing the duties of lead plaintiff, only New York City acted against what it viewed as an excessive award by a federal district court in derogation of a negotiated fee agreement.

## Product Liability

• **Product Liability Actions:** The affirmative litigation division has for many years led the city's effort to recover for the property damage sustained by city agencies caused by the lead-based paint and asbestos-containing materials used in schools, other city buildings and housing owned by the New York City Housing Authority. Asbestos property damage litigation, initially commenced in state court, has required city attorneys to gain expert-

ise in bankruptcy law as the cases moved into that forum, and to litigate within the unfamiliar terrain of the various asbestos settlement trusts. To date, Law Department attorneys have recovered over \$80 million in asbestos property damage claims for the city. This year, city attorneys obtained a favorable decision, now on appeal, from the Bankruptcy Court in Florida; it was worth an additional \$40 million.

• **Insurance Litigation:** Although the city of New York does not purchase third-party liability insurance for itself, it is frequently covered as an "additional insured" on the insurance policies of those who enter into contracts with the city. Because contractors may expose the city to tort liability whether or not the city is the primary provider of a particular service — such as, for example, foster care, road maintenance, transportation and the management of cultural and entertainment facilities — contractors are required to procure insurance coverage protecting the city in the event of claims against the city arising out of the contractor's city-related activities. The insurance coverage mandates defense of the city and indemnification for damages.

However, when the city tenders claims to the liability carriers it shares with its contractors, the city's status as "merely" an additional insured (rather than a premium-paying client) appears to invite coverage denials that are not well-founded in law. The affirmative litigation division has therefore ventured into the realm of insurance coverage declaratory judgments by instituting hundreds of cases seeking declarations of coverage. In response, the carriers routinely acknowledge their policies, saving the city \$24 million in judgments and settlements over the past 15 months.

## City Versus the State

• **Litigation Against the State:** Sometimes it proves necessary for the city to initiate litigation against

the state or the federal government to secure payments due to the city of New York under applicable statutes or regulations. In one such case, this summer, attorneys from the affirmative litigation division tried an action in the Court of Claims to recover damages resulting from the state's breach of its contractual and court-ordered obligation to place mentally retarded children served by the city's foster care system into appropriate facilities run by the State Office of Mental Retardation and Developmental Disabilities (OMRDD). OMRDD's ongoing unresponsiveness to the needs of this population has delayed or denied OMRDD services to thousands of children over the years and has imposed on the city the expensive burden of caring for and providing intensive and costly services to mentally retarded children for whom OMRDD services have been deemed appropriate by both the state Legislature and OMRDD itself.

In an earlier lawsuit the city sought to compel OMRDD to fulfill its responsibility under the State Mental Health Law to this population.<sup>10</sup> The city's lawsuit was settled by a consent decree (the "Webb Stipulation"), dated May 1, 1991, in which the state agreed to place 200 such children into OMRDD care in each of four years from priority lists submitted by the city. When, in the city's view, the state agency fell short of its Webb Stipulation obligations, the affirmative litigation division brought a contempt motion against the state in 1994. The trial court found that the state had violated the consent decree and awarded the city more than \$9 million in damages.<sup>11</sup> The Appellate Division reversed on grounds that the Supreme Court could not award contractual damages against the state and that the matter should properly be tried in the Court of Claims as a breach of contract action.<sup>12</sup>

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In the recent Court of Claims trial, city attorneys presented evidence at trial that the city's cost of caring for the number of mentally retarded children who ought to have been in state care for the full four years covered by the stipulation totaled \$18 million. The court's decision is pending.

## Conclusion

The matters discussed above are only a small part of the caseload of the affirmative litigation division. Other matters being handled by the division include an action under the RICO statute to recover kickbacks paid to a nonprofit organization that was filing false claims for public assistance payments, litigation with certain Westchester communities over the quantity of city water they can use and the rates they must pay, and an action to recover pay telephone franchise payments.

(1) 15 USC §375-378 (1949). The Jenkins Act provides that all interstate shipments of cigarettes must be reported to the taxing authority of the state into which the cigarettes are shipped.

(2) *City of New York v. Cyco.net, Inc.*, 03 cv 0383 (DAB) (SDNY); *City of New York v. A.E. Sales, Inc.*, 03 cv 7715 (DAB) (SDNY); *City of New York v. Esmokes, Inc.*, 03 cv 10091 (SDNY). The RICO statute is found at 18 USC §1961 et seq.

(3) *Brown & Williamson Tobacco Corp. v. Pataki*, 320 F3d 200 (2d Cir. 2003).

(4) *Compare Ideal Steel Supply Corp. v. Anza*, 254 FSupp2d 464 (SDNY 2003) with *Trautz v. Weisman*, 819 FSupp 282, 286 (SDNY 1993).

(5) *Transcript of oral argument, Ideal Steel Supply Corp. v. Anza*, 03-7381 (2d Cir. Dec. 16, 2003).

(6) See, e.g., *City of Chicago v. Beretta U.S.A. Corp.*, 337 Ill. App. 3d 1 (2002), appeal granted, 203 Ill. 2d 544 (April 2, 2003).

(7) *NAACP v. American Arms, et al.* 99 Civ. 3999 (JBW) (EDNY).

(8) *City of New York v. B.L. Jennings, et al.*, 00 CV 3641 (JBW) (EDNY).

(9) *In re Cendant Corp. Litigation*, 264 F3d 201 (3d Cir. 2001).

(10) *City of New York, et al. v. Webb*, Index No. 40313/86 (Supreme Ct. N.Y. County).

(11) *City of New York, et al. v. Maul*, Index No. 40313/86, Decision and Order dated Aug. 15, 1995 (Supreme Ct. N.Y. County) (Collazo, J.).

(12) *City of New York, et al. v. Maul*, Index No. 40313/86, Decision and Order dated May 15, 1997 (App. Div. 1st Dept.).

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