No. 18-1501

IN THE
Supreme Court of the United States

CHARLES C. LIU AND XIN WANG A/K/A LISA WANG,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF FOR PETITIONERS

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INTRODUCTION

Nowhere has Congress explicitly empowered the SEC to obtain disgorgement in judicial proceedings. The relevant statutes explicitly authorize the SEC to pursue other forms of relief, including civil monetary penalties (within stated limits) and equitable relief. But they never mention disgorgement.

The SEC's sole legal argument here is thus that disgorgement is "an equitable remedy." Opp. 5. But this Court held, in *Kokesh v. SEC*, 137 S. Ct. 1635 (2017), "that SEC disgorgement constitutes a penalty" and cannot be considered an equitable remedy. *Id.* at 1642. Accordingly, the SEC's legal claim rests on the wholly unsupported proposition that the exact same remedy that the Court concluded was a penalty for purposes of the SEC's statute of limitations is not a penalty for purposes of the SEC's remedial authority. To state that proposition is to refute it.

Review of this important legal issue is especially warranted because, as the SEC's filing confirms, this issue has arisen repeatedly and the lower courts, including the Ninth Circuit, have not aligned their precedents with this Court's analysis in *Kokesh*. As a result, the SEC collects huge sums of money by pursuing a penalty that it does not have the power to seek in federal court. Beyond that, other agencies, like the Federal Trade Commission ("FTC"), have followed the SEC's lead to seek disgorgement penalties despite lacking statutory authorization to do so.

Petitioners have been assessed a $26 million, unauthorized penalty. They directly raised the issue of the SEC's statutory authority to pursue such a penalty in proceedings below. The Ninth Circuit addressed and rejected that argument. The petition thus gives this Court a clear opportunity to address

this significant, frequently litigated issue of law as to which the lower courts need guidance.

ARGUMENT

I. THE COURT SHOULD GRANT THIS PETITION TO STOP THE SEC FROM ROUTINELY PURSUING A FORM OF RELIEF THAT CONGRESS NEVER AUTHORIZED

A. Congress Did Not Give the SEC Power To Seek Disgorgement Penalties

It is common ground that there is no explicit statutory authority for the SEC to obtain disgorgement in federal court. That is why in *Kokesh* no fewer than five Justices questioned the statutory source of this asserted authority, and it is why counsel for the SEC in *Kokesh* could not cite any such source. *See* Oral Arg. Tr. 7-9, 13, 31, 52, *Kokesh v. SEC*, No. 16-529 (U.S. Apr. 18, 2017). It is also why the SEC failed to invoke any statutory authority to seek disgorgement in the district court proceeding below. *See* Compl. at 27, Prayer for Relief ¶ V, *SEC v. Liu*, No. SACV 16-00974-CJC (AGRx), ECF #1 (C.D. Cal. May 26, 2016); SEC Mem. in Support of Summ. J. at 20-23, *SEC v. Liu*, No. SACV 16-00974-CJC (AGRx), ECF #199-1 (C.D. Cal. Jan. 4, 2017); SEC Supp. Br., *SEC v. Liu*, No. SACV 16-00974-CJC (AGRx), ECF #220 (C.D. Cal. Feb. 8, 2017).

Faced with this lack of explicit authorization, the SEC argues to this Court (at 5-6) that, by granting the agency the authority to "enjoin" statutory violations and otherwise grant "equitable relief," Congress implicitly authorized a disgorgement remedy. *See* 15 U.S.C. §§ 77t(b) (authorizing the SEC to "bring an action in any district court of the United States . . . to enjoin such acts or practices, and upon a proper showing, a permanent or temporary injunction or

restraining order shall be granted"), 78u(d)(1) (same), 78u(d)(5) ("[T]he [SEC] may seek, and any Federal court may grant, any equitable relief that may be appropriate or necessary for the benefit of investors.").

Congress, however, specified that the SEC could seek several enumerated forms of relief, including civil monetary damages, but never suggested that, on top of those damages (which are explicitly limited by statute, *see id.* §§ 77t(d)(2), 78u(d)(3)), the agency could also obtain unlimited disgorgement relief. *See FTC v. Credit Bureau Ctr., LLC*, Nos. 18-2847 & 18-3310, 2019 WL 3940917, at *15 (7th Cir. Aug. 21, 2019) (reviewing this Court's jurisprudence to hold that courts should not "presum[e] that Congress authorizes the judiciary to supplement express statutory remedies"). It makes no sense for Congress to enact specific provisions to limit the amount of civil monetary penalties available while leaving monetary penalties through disgorgement entirely up to a court's discretion.

Notably, moreover, in contrast to district court proceedings, Congress expressly authorized disgorgement in certain SEC *administrative* proceedings. *See* 15 U.S.C. § 78u-2(e) (allowing the SEC to "enter an order requiring accounting and disgorgement" in an administrative proceeding); Pet. 9 n.4. Congress thus plainly knows how to authorize disgorgement when it wants to do so. *See Nken v. Holder*, 556 U.S. 418, 430 (2009) ("[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.") (citation omitted).

Under this Court's analysis in *Kokesh*, statutes allowing the SEC to seek injunctions and other equitable relief do not authorize disgorgement. *Kokesh* establishes that disgorgement is a penalty because it is imposed for violating a public law, has a punitive purpose, and is not compensatory. *See* 137 S. Ct. at 1643-44. These characteristics are not consistent with the "'*solely*'" remedial purpose of equity, which is to restore the status quo, not punish a wrongdoer. *Id.* at 1645 (quoting *Austin v. United States*, 509 U.S. 602, 610 (1993)) (italics added by Court in *Kokesh*). *See Tull v. United States*, 481 U.S. 412, 424 (1987) ("[A] court in equity . . . may not enforce civil penalties."); *Hecht Co. v. Bowles*, 321 U.S. 321, 329-30 (1944) (explaining that equity is an "instrument for nice adjustment and reconciliation," not punishment); *see generally* Dan B. Dobbs & Caprice L. Roberts, *Law of Remedies* § 4.3, at 397 (3d ed. 2018). Indeed, even the seminal case affirming the SEC's right to seek broad equitable relief makes clear that the agency may not impose penalties. *See SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1308 (2d Cir. 1971) ("SEC may seek other than injunctive relief in order to effectuate the purposes of the Act, so long as such relief is remedial relief and is not a penalty assessment.").

None of the cases upon which the SEC relies (at 8-9) suggests that the disgorgement at issue here is not a penalty under the Court's analysis in *Kokesh*. Nor does any provide any substantive explanation why the *exact same disgorgement* remedy that the Court held is a penalty for purposes of a statute of limitations would not be a penalty for determining the SEC's remedial authority. *Compare* Opp. 8.

Far from justifying the disgorgement authority claimed by the SEC, the Supreme Court cases upon

which the SEC relies assumed that the remedy at issue merely put the parties back in the position they were in before the actions at issue. *See Tull*, 481 U.S. at 424 (cited at Opp. 6) (explaining that civil penalties were not equitable because they were not "limited to restoration of the status quo"); *Porter v. Warner Holding Co.*, 328 U.S. 395, 402 (1946) (cited at Opp. 5) (focusing on "the return of that which rightfully belongs" to victims as equitable, and *not* payment of "penalties which go to the United States Treasury"); *Mitchell v. Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 292-93 (1960) (cited at Opp. 5) (holding that returning unlawfully withheld wages to employees is equitable); *Chauffeurs, Teamsters & Helpers v. Terry*, 494 U.S. 558, 570-72 (1990) (cited at Opp. 6) (also explaining that returning unlawfully withheld wages to employees is equitable).

But that assumption is not tenable for SEC disgorgement, which this Court has said "bears all the hallmarks of a penalty." 137 S. Ct. at 1644. As in *Kokesh*, the disgorgement at issue here was imposed for violating public laws; it was imposed for punitive purposes; and it was not compensatory. As the *Kokesh* Court stressed, the SEC is not even required to return any money to the alleged victims. In this context, disgorgement is intended not to restore the status quo, but instead to "deter violations of the securities laws." *Id.* (emphasis added). The SEC's cases are thus irrelevant.[1]

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[1] The other cases the SEC cites come from vastly different contexts than an agency's ability to extrapolate the power to seek monetary penalties from authority to seek equitable relief. For instance, *Kansas v. Nebraska*, 135 S. Ct. 1042 (2015), held in an original-jurisdiction proceeding that equitable relief is available

The SEC also cites statutory language that it claims demonstrates that Congress contemplated disgorgement relief. Those provisions, however, are wholly consistent with petitioners' argument. None purports to ratify judicial decisions granting disgorgement authority where it has not otherwise been authorized. To the contrary, most encompass administrative proceedings where Congress did expressly give the SEC some disgorgement authority. They therefore can reasonably be understood to apply where Congress explicitly authorized some form of disgorgement. For example, 11 U.S.C. § 523(a)(19) contemplates disgorgement payments, among a list of several categories of relief that include penalties (which are authorized in federal court cases) and restitutionary payments, from "any court or administrative order." *See* Opp. 7. Similarly, the whistleblower statute cited by the SEC refers generally to monetary sanctions like disgorgement "with respect to any judicial or administrative action." 15 U.S.C. § 78u-6(a)(4); *see* Opp. 7.

In all events, whatever else these provisions contemplate, they do not suggest that the form of disgorgement at issue here and in *Kokesh* are permissible. As this Court explained, that form of disgorgement is a penalty because "[i]t is imposed as a consequence of violating a public law and it is intended to deter, not to compensate." 137 S. Ct. at 1644. Nothing in the statutes suggests that Congress intended to authorize penal, non-compensatory disgorgements.

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to enforce a water-rights compact between two sovereign States when legal damages are inadequate.

B. Review Is Especially Warranted Because This Issue Arises Frequently and Circuit Courts Continue To Rely on an Erroneous Pre-*Kokesh* Understanding

The Court's analysis in *Kokesh* undermined the prior understanding of the lower federal courts that SEC disgorgement was remedial and therefore a permissible equitable remedy. *See* Pet. 17. As then-Judge Kavanaugh stated, *Kokesh* "overturned a line of cases from [the D.C. Circuit] that had concluded that disgorgement was remedial and not punitive." *Saad v. SEC*, 873 F.3d 297, 305 (D.C. Cir. 2017) (Kavanaugh, J., concurring). Other judges have likewise understood that *Kokesh* cuts the analytical legs out from under prior decisions approving disgorgement authority as remedial. For example, Judge O'Scannlain agreed with the panel that existing Ninth Circuit case law supported disgorgement, but separately requested en banc consideration to correct the Ninth Circuit's analysis in the wake of *Kokesh*. *See FTC v. AMG Capital Mgmt., LLC*, 910 F.3d 417, 429 (9th Cir. 2018) (O'Scannlain, J., specially concurring) ("Because our interpretation wrongly authorizes a power that the statute does not permit, we should rehear this case en banc to relinquish what Congress withheld.").[2] Judge Merritt similarly stated that disgorgement "may not even be applicable in SEC contexts for much longer in light of" *Kokesh*. *Osborn v. Griffin*, 865 F.3d 417, 470 n.1 (6th Cir. 2017) (Merritt, J., dissenting); *see also* Stephen M. Bainbridge, Kokesh *Footnote Three Notwithstanding: The Future*

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[2] The disgorgement award sought in *AMG Capital Management* shares the same characteristics as that sought by the SEC under similar statutory provisions. *See AMG Capital Mgmt.*, 910 F.3d at 433-34 (O'Scannlain, J., specially concurring).

of the Disgorgement Penalty in SEC Cases, 56 Wash. U. J.L. & Pol'y 17, 27-30 (2018).[3]

Nevertheless, lower courts have continued to rely on pre-*Kokesh* precedents. *See* Pet. 17 (collecting cases from circuit courts that had awarded disgorgement as equitable relief on the basis that it was remedial, not punitive). The very uniformity of the lower courts in reflexively relying on outdated analysis to approve disgorgement by the SEC (and other agencies) warrants review here. The Court should grant certiorari so that the lower courts will align their case law with the Court's decisions.

In this regard, the SEC's brief notably does not dispute that these issues arise frequently and are of tremendous financial consequence. The scope of equitable relief broadly impacts the enforcement authority of several significant agencies, including the FTC, the Environmental Protection Agency, and the Consumer Financial Protection Bureau, which rely on equity to collect what *Kokesh* revealed to be disgorgement penalties. *See* Pet. 20-21. The SEC alone collects billions of dollars in disgorgement penalties annually. *See* Pet. 14-15. If the SEC has no statutory authority to do so, surely that is an issue of immediate importance for this Court to address.

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[3] The SEC's discussion (at 9-11) misses the point of these comments, which is not to claim a conflict based on concurring and dissenting opinions, but to show that numerous jurists and scholars have recognized that *Kokesh* has undermined the analysis that courts had previously relied upon in concluding that disgorgement is remedial.

II. THIS CASE SQUARELY PRESENTS A PURELY LEGAL ISSUE

This case cleanly presents a single and wholly legal question, making it an excellent vehicle for this Court's review. Petitioners raised the issue below, and the Ninth Circuit expressly ruled on it.

A. Petitioners Raised Their Challenge to the Disgorgement Penalty Below

Contrary to the SEC's argument (at 11-12), petitioners expressly challenged the SEC's disgorgement award below. *See* Pet'rs C.A. Br. 3 ("Did the district court . . . have authority to award disgorgement as equitable restitution?"), 25 ("Whether the district court had authority to award disgorgement is a legal issue also reviewed de novo."), 26 ("The court doubly penalized Liu and Wang by imposing . . . statutorily unauthorized disgorgement as a penalty . . . ."), 48 ("First, the court lacked statutory authority to award disgorgement."), 49 ("[T]he court in fact awarded [disgorgement] as a penalty, not an equitable remedy."), 49-53.[4]

Moreover, and again contrary to the SEC's contention (at 11-12), the Ninth Circuit directly resolved petitioners' challenge, holding that its pre-*Kokesh* precedent was binding and applied to the disgorgement award. App. 6a-7a ("Relying on *Kokesh*, the Appellants argue that the district court lacked the

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[4] Even had petitioners agreed that one variety of disgorgement could be equitable, that is not close to waiving their argument that a punitive variety of disgorgement is unauthorized. *See* Opp. 12. In fact, after the sound bite clipped by the SEC, petitioners immediately explained the disgorgement award against petitioners was punitive, not equitable relief. Oral Arg. at 29:15, *SEC v. Liu*, No. 17-55849 (9th Cir. Oct. 11, 2018), https://go.usa.gov/xVYgU.

power to order disgorgement in this amount. But *Kokesh* expressly refused to reach this issue so that case is not 'clearly irreconcilable' with our longstanding precedent on this subject.") (citations omitted). This Court's power to review a question of law actually decided by the court below is irrefutable. *See Yee v. City of Escondido*, 503 U.S. 519, 534 (1992).

B. Petitioners Present a Question of Law, Not Fact

The SEC mischaracterizes the question of law petitioners present about the equitable nature of a disgorgement penalty. Whether the exact same form of relief characterized as a penalty by *Kokesh* qualifies as equitable relief is hardly fact-bound. Instead, it is a quintessential question of law considered by the Ninth Circuit de novo and ripe for this Court's review. *See* App. 1a-3a.

The facts of this case, which petitioners do not challenge, are relevant only to show that the disgorgement award sought by the SEC is of the same type as the one this Court determined to be a penalty in *Kokesh*. Whether, contrary to past practice, the SEC might ultimately determine to send the disgorged funds to the investors rather than the U.S. Treasury has no impact on the justiciability of the legal question presented and ruled upon below, any more than it did in *Kokesh*. Nor does the SEC explain how petitioners would obtain review by this Court if they had to wait for the agency finally to resolve the destination of the awards sought. *See* Opp. 13-14.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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