No. 18-1501

IN THE

Supreme Court of the United States

CHARLES C. LIU, ET AL.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

BRIEF OF AMICUS CURIAE NEW ENGLAND LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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Dated: December 20, 2019

BATEMAN & SLADE, INC. STONEHAM, MASSACHUSETTS

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INTEREST OF AMICUS CURIAE[1]

The New England Legal Foundation (NELF) is a nonprofit, nonpartisan, public-interest law firm incorporated in Massachusetts in 1977 and headquartered in Boston. Its membership consists of corporations, law firms, individuals, and others who believe in NELF's mission of promoting balanced economic growth in New England and the nation, protecting the free-enterprise system, and defending individual economic rights and the rights of private property. In fulfillment of its mission, NELF has filed numerous amicus briefs in this Court in a great variety of cases.

NELF appears as an amicus in the present case because this case raises serious questions about the power of a federal court to exercise its equitable powers to award the Securities and Exchange Commission "disgorgements" of the kind described by this Court in *Kokesh v. Securities and Exchange Commission*, 137 S.Ct. 553 (2017). Consistent with its mission, NELF has long opposed the exercise of power over property or businesses by a court or agency when that power has not been clearly lawfully delegated. For the reasons set forth in this brief, such appears to be the case here.

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[1] Pursuant to Supreme Court Rule 37.6, NELF states that no party or counsel for a party authored this brief in whole or in part and that no person or entity, other than NELF, made any monetary contribution to its preparation or submission.

Pursuant to Supreme Court Rule 37.3(a), NELF has obtained the consent of all parties. On November 19, 2019 Petitioners filed a blanket consent to the filing of amicus briefs in support of either or neither party, and by letter dated December 17, 2019, the Solicitor General granted his consent to the filing of this brief.

SUMMARY OF THE ARGUMENT

Equity abhors penalties. Because in *Kokesh* the disgorgement typically sought by the SEC in enforcement actions was ruled to be a penalty, a court may not grant disgorgement as equitable relief.

That ruling of the *Kokesh* Court is not limited to limitations of actions. While the ruling was used to identify a limitations period, it was arrived at by analyzing the character and purpose of disgorgement as a form of relief in securities enforcement actions such as this one. The Court explicitly stated that the ruling was made in the context of such actions, and the SEC has repeatedly treated this case too as an enforcement action, without distinguishing it in any relevant way from the one in *Kokesh*. Hence the ruling made in *Kokesh* applies here.

The SEC relies on a few earlier decisions of this Court that, at most, recognized non-punitive, restitutionary disgorgement as equitable. The canon of prior construction is not applicable, either. No specific words of a securities statute were construed authoritatively by this Court and then reenacted by Sarbanes-Oxley in 2002. The cases cited by the SEC were either decided after Sarbanes-Oxley or, if they were decided earlier and used the word "disgorge," they understood it to mean equitable restitution and distinguished it from a penalty.

ARGUMENT

I. In *Kokesh* This Court Ruled That Disgorgement Is A Penalty Under Securities Law. From That Ruling It Follows That Disgorgement May Not Be Granted By A Court As An Equitable Remedy.

In *Kokesh* this Court ruled that "[d]isgorgement in the securities-enforcement context is a 'penalty' within the meaning of [28 U.S.C.] § 2462, and so disgorgement actions must be commenced within five years of the date the claim accrues." *Kokesh v. Securities and Exchange Commission*, 137 S.Ct. 1635, 1639 (2017). That predicate ruling on the punitive nature of securities disgorgement compels the conclusion that a federal court may not grant the SEC disgorgement as equitable relief.

In *Kokesh* the Court reasoned that disgorgement is a remedy the SEC seeks for a violation "committed against the United States rather than an aggrieved individual," with the SEC acting "'to remedy harm to the public at large, rather than standing in the shoes of particular injured parties.'" *Id.* at 1643 (quoting SEC's brief in that case). It also observed that these disgorgements are "imposed for punitive purposes" of "protect[ing] the investing public by providing an effective deterrent to future violations." *Id.* (further citation and quotation marks omitted). "Sanctions imposed for the purpose of deterring infractions of public laws are," the Court noted, "inherently punitive because 'deterrence [is] not [a] legitimate nonpunitive governmental objectiv[e].'" *Id.* (quoting *Bell v. Wolfish*, 441 U.S. 520, 539 n.20 (1979)). As a final factor, the Court emphasized that, at best, only on occasion are any of the funds disgorged to the

SEC distributed in turn to investors as restitution. *Id.* at 1644

In short, "[w]hen an individual is made to pay a noncompensatory sanction to the Government as a consequence of a legal violation, the payment operates as a penalty." *Id.* "SEC disgorgement," the Court concluded, "thus bears all the hallmarks of a penalty." *Id.*

May a federal court grant the SEC such relief then?

Since the time of the leading case *Securities and Exchange Commission v. Texas Gulf Sulphur Company*, 312 F. Supp. 77 (S.D.N.Y. 1970), the SEC's argument in favor of court-ordered disgorgement has invoked the federal courts' "'inherent equity power to grant relief ancillary to an injunction.'" *Kokesh*, 137 S.Ct. at 1640 (quoting *Texas Gulf*). *See also* SEC's Brief for the Respondent in Opposition (BIO) at 8.

The extent of the equitable powers of a federal court are delimited, however, by the "principles of the system of judicial remedies which had been devised and were being administered by the English Court of Chancery at the time of the separation of the two countries." *Grupo Mexicano de Desarrollo S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308, 318 (1999) (further citation and quotation marks omitted). *See also Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 210 (2002) (equitable relief limited to "categories of relief that were typically available in equity") (further citation and quotation marks omitted; emphasis removed).

Traditionally courts sitting in equity aimed to restore the status quo after wrongdoing and not to

punish the wrongdoer. *See* Dan B. Dobbs & Caprice L. Roberts, *Law of Remedies* § 4.3 at 397 (3d ed. 2018). As this Court has observed, "[r]emedies intended to punish culpable individuals, as opposed to those intended simply to extract compensation or restore the status quo, were issued by courts of law, not courts of equity." *Tull v. United States*, 481 U.S. 412, 422 (1987). *See Feltner v. Columbia Pictures Television, Inc.*, 523 U.S. 340, 352–53 (1998) (quoting *Tull*); *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 255 (1993) (equitable relief does not include "punitive damages"); *Brown v. Swann*, 35 U.S. (10 Pet.) 497, 503 (1836) (equity will not assist to enforce penalty; "enforcement of a penalty . . . has never been its province"); *United States v. Parkinson*, 240 F.2d 918, 921 (9th Cir. 1956) (in traditional equity, "Penalties were abominated."); 2 Joseph Story, *Commentaries on Equity Jurisprudence* at 748 ("It is a universal rule, in Equity, never to enforce either a penalty or a forfeiture.") (2d ed. 1846).

It is not surprising, therefore, that nothing in 18th century English Courts of Chancery resembled the punitive disgorgements sought and obtained by the SEC over the past fifty years since *Texas Gulf*. *See* Francesco A. DeLuca, *Sheathing Restitution's Dagger Under the Securities Acts: Why Federal Courts Are Powerless to Order Disgorgement in SEC Proceedings*, 33 Rev. Banking & Fin. L. 899 (2014).

Neither "disgorge" nor "disgorgement" appear as entries in any of the following 18th century law dictionaries: Thomas Blount, *A Law-Dictionary and Glossary* (1717); Giles Jacob, *A New Law Dictionary* (1739); 1 Timothy Cunningham, *A New and Complete Law-Dictionary* (1765); 1 Giles Jacob, *The Law Dictionary* (1797). DeLuca, *supra*, shows that a remedy like modern American securities

"disgorgements" did not exist in Chancery under that name or any other.

Hence, because *Kokesh* established that the disgorgements that the SEC has long sought and obtained from federal courts are penalties and because penalties are foreign to traditional principles of equity, a court may not award disgorgement as equitable relief to the SEC.

II. *Kokesh's* Characterization Of SEC Disgorgements As Penalties Is Not Confined To Limitations Of Actions. It Also Applies To Disgorgements Considered As A Form Of Court-Ordered Relief.

In its response to the Petition, the SEC argued that *Kokesh* does not apply here. It noted that *Kokesh's* analysis was conducted for purposes of answering a question concerning the timeliness of disgorgement actions brought by the SEC, and so it urged the Court to conclude that the *Kokesh* analysis has no bearing on the question before the bench now. The SEC's reasoning lacks any basis in the text of the decision. The *Kokesh* analysis, although not conducted specifically for the present purpose, turns out to be in fact highly relevant to it anyway.

Nowhere in *Kokesh* did the Court's penalties analysis so much as allude to 28 U.S.C. § 2462 (the statute of limitations being considered there), or to the law of limitations of actions in general, or even to any public policy underlying such laws, as we have seen. *See supra* pp. 3-4. Every step of the analysis was taken without any regard or reference to such considerations. *See Kokesh*, 137 S.Ct. at 1643-44. Certainly, in its response the SEC did not identify

any such connection. *See* BIO at 7-8. As the Court summarized its reasoning in *Kokesh*:

> SEC disgorgement thus bears all the hallmarks of a penalty: It is imposed [i] as a consequence of violating a public law and it is [ii] intended to deter, [iii] not to compensate. The 5-year statute of limitations in §2462 therefore applies when the SEC seeks disgorgement.

137 S.Ct. at 1644 (enumeration added).

That passage illustrates the point being made here. All three of the factors identified by the Court are what they are independently of the law of limitations of actions entirely. Their sole connection with § 2462 comes only at the conclusion of the Court's tripartite reasoning. Having determined that disgorgements are penalties, the Court concluded that, as such, disgorgements come within the plain terms of the statute. *Id*. *See* § 2462 ("any civil fine, penalty, or forfeiture"). And that is the first and last connection made by the *Kokesh* Court between disgorgements as penalties and the law of the limitations of actions. Manifestly, the Court's determination that securities disgorgements are penalties was simply *applied to* § 2462; it did not *arise out of* § 2462, nor out of any other law or policy relating to the limitations of actions.

In fact, the Court itself stated explicitly that the "context" of its disgorgement analysis is "securities-enforcement," *Kokesh*, 137 S.Ct. at 1639, and that of course is exactly the legal "context" of the question before the Court now.

So it is doubly difficult to understand how the SEC can deny the relevance of *Kokesh* while itself

openly, repeatedly, and without demur treating this securities case as an "enforcement" action. *See* BIO *passim* (using "enforcement" sixteen times; e.g., "SEC enforcement actions," "civil enforcement actions," etc.). The SEC even volunteered its own Question Presented, in which it chose to add the contextual phrase "in a civil enforcement action." *See id.* at i. How then does the "securities-enforcement context" of *Kokesh* differ relevantly from the present one? We are not told.

There is yet another compelling reason for rejecting the SEC's attempt to distinguish *Kokesh*. While the Court emphasized that its decision in no way addressed the question of a court's authority to order disgorgements in enforcement actions, 137 S.Ct. at 1642 n.3, the three "hallmarks" of a disgorgement penalty identified by the Court can now be seen to go to the very heart of the kind of relief securities disgorgements provide (i.e., non-compensatory) and to the rationale for a court's awarding them as relief (i.e., to vindicate the public interest and deter future violations). In other words, contrary to the SEC's view, the Court's reasoning there bears directly on the question before the Court now, which concerns whether that is the kind of relief that a court is authorized to provide to fulfil an equitable purpose.

There simply is no textual support for the SEC's attempt to limit the reach of *Kokesh*. On the contrary, the text of that decision is decisive evidence to the contrary.

III. The Court's Hands Are Not Tied Either By Its Own Precedents Or By Sarbanes-Oxley.

In its response to the petition, the SEC also made two other, intertwined arguments. BIO at 5-7.

First, the SEC invoked the inherent equitable powers of a court to grant all needed relief that is adjunct to an injunction. For this expansive conception of the "inherent" equitable powers of a federal court to do "complete rather than truncated justice," it relied on *Porter v. Warner Holding Co.*, 328 U.S. 395, 398, 400 (1946), a case which is pretty much the *locus classicus* for an enlarged view of equity jurisdiction.[2] But it is worth taking a look at the relief *Porter* allowed, before we consider the expansive language upon which the SEC so much relies as a basis for awards of punitive disgorgements.

Porter dealt with rent overcharges under the Emergency Price Control Act of 1946. While the word "disgorge" is applied once to the relief in that case, *id.* at 398, the relief sought was in fact restitution based on a court's statutory power to issue an "other order" in addition to an injunction, *see id.* at 396 ("we are concerned with the power of a federal court . . . to order restitution of rents collected by a landlord in excess of the permissible maximums"), 397 ("other order"), 399 (same). In fact, so far was that case from being concerned with anything like the punitive disgorgements at issue here that the Court wrote, "Restitution, which lies within that equitable jurisdiction, is consistent with

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[2] A second case that the SEC cites, BIO at 5, relies on *Porter*. *See Mitchell v. Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 290-92 (1960).

and differs greatly from the damages and *penalties* which may be awarded under [another section of the act which granted a personal right of action at law plus treble damages]." *Id.* at 402 (emphasis added).

Hence, all money awarded in *Porter* was intended to be returned to the tenants who had overpaid it, relief that clearly had no punitive purpose. *Id.* (court asked to "restor[e] the status quo and order[] the return of that which rightfully belongs to the purchaser or tenant"). "Such action," as the Court aptly observed, "is within the recognized power and within the highest tradition of a court of equity." *Id.*

The restitution to be "disgorge[d]" in *Porter*, then, was strikingly unlike the disgorgements considered in *Kokesh*, where the Court noted that there exists no statutory "command" that funds disgorged to the SEC be paid to victims and that they only sometimes are. *See* 137 U.S. at 1644. Any more expansive language found in *Porter* would nowadays be read in light of this Court's renewed and more cautious emphasis on traditional principles of equity. *See Grupo Mexicano*, 527 U.S. at 322 ("equity is flexible; but in the federal system, at least, that flexibility is confined within the broad boundaries of traditional equitable relief"); *Great-West Life & Annuity Inc. Co. v. Knudson*, 534 U.S. 204 (2002), and *Sereboff v. Mid Atlantic Medical Servs., Inc.*, 547 U.S. 356 (2006). *See also supra* pp. 4-5.

Moreover, it would scarcely be reasonable to quote *Porter's* broader language in order to justify a form of relief (i.e., punitive disgorgement) inconsistent with *Porter's* own discussion of the relief it actually awarded, which it distinguished specifically from punitive relief. That, however, is

exactly how the SEC selectively seeks to use certain language in *Porter* now. *See* BIO at 5.

The SEC's second argument says that Congress has in effect ratified punitive disgorgement as equitable relief by enacting certain provisions of the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002). The provisions were enacted against a supposedly settled "backdrop" of decisions in which this Court had "repeatedly characterized disgorgement as an equitable remedy," as the SEC puts it. BIO at 5-6. The SEC claims that the canon of prior construction applies to this situation, *see* Antonin Scalia and Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts* 322-26 (2012), and that the Court's supposed recognition of equitable "disgorgement" in past cases is now essentially baked into the securities statutes.

The prior-construction canon applies only when (i) specific words of a statute have received an authoritative interpretation by a court and then (ii) a later reenactment "perpetuat[es] the wording." Scalia, *supra*, at 322, 325 (wording of statute "repeated"). *See Lightfoot v. Cedant Mortgage Corp.*, 137 S.Ct. 553, 563 (2017) (later provision "mirrors" statutory wording interpreted earlier); *Armstrong v. Exceptional Child Center, Inc.*, 135 S.Ct. 1378, 1386 (2015) ("repetition of the same language" interpreted in earlier statute). Only when these two defining conditions are met does the canon arguably apply.

What is striking is that the SEC invokes the canon without identifying either which specific words of a particular securities statute received an earlier authoritative interpretation or how Sarbanes-Oxley reenacted those specific words.

Instead, the SEC paints a vague decisional "backdrop," but the four cases of this Court cited by the SEC do not support the existence of a settled "backdrop" any more than does *Porter*, on which three of them in fact rely. *See* BIO at 5-6.

The first case was decided under a provision of the Fair Labor Standards Act and ruled that the law permitted an injunction against the employer to be accompanied by an order to "reimburse" workers for unlawfully detained wages. *See Mitchell v. Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 296 (1960). Relying on *Porter*, the Court left no doubt that it regarded the reimbursement as restitutionary and not punitive. *See id.* at 293 ("restitution," "not rendered thereby punitive," "compensatory only"). That is also how the three dissenting justices understood it. *See id.* at 298 n.1 (Whittaker, Black, Clark, JJ., dissenting) (discussing "restitution" in *Porter*), 301 (arguing 1949 amendment banned such "restitution order"). *See also Chauffeurs, Teamsters & Helpers v. Terry*, 494 U.S. 558, 571 (1990) (*Mitchell* backpay "restitutionary"). As it happens, the words "disgorge" and "disgorgement" do not even appear in *Mitchell*.

The second case was decided thirteen years *after* Sarbanes-Oxley was enacted and so it could scarcely have been "backdrop" to the legislation. *See Kansas v. Nebraska*, 574 U.S. 445 (2015).

The third case dealt with civil penalties, distinguishing them from what it called "disgorgement," which it explicitly understood to mean the restorative, equitable "restitution" described in *Porter*. *See Tull*, 481 U.S. at 424.

The fourth case dealt with the legal remedy of backpay, which it distinguished from the equitable

remedy of "disgorgement," again equated expressly with the restitution described in *Porter* and now also in *Tull*. *See Chauffeurs*, 494 U.S. at 570-71.

These cases simply do *not* show that, before the enactment of Sarbanes-Oxley in 2002, this Court had reached a clear, settled view that *punitive* securities disgorgement, like that described in *Kokesh* — or any other kind of punitive disgorgement, for that matter — is relief available under the equitable powers of a federal court.

Moreover, if the specific word in question here is "disgorgement," *see* BIO at 5, we note that in none of the cases of this Court cited by the SEC was the word construed as part of *any* statute, let alone a securities statute, nor did the cases involve a statute later reenacted by Sarbanes-Oxley.[3]

Rather, what we have seen in those cases is that this Court sometimes used the word "disgorgement" before 2002 in a *non-punitive* sense, synonymously with restorative restitution. *See Kokesh*, 137 S.Ct. at 1645 ("disgorgement serves compensatory goals in some cases," as opposed to when it is used to punish). As the *Porter* Court said, restorative restitution is relief that "is within the recognized power and within the highest tradition of a court of equity." 328 U.S. at 402. The punitive disgorgement

[3] NELF agrees with the Petitioners on Sarbanes-Oxley. *See* Brief for Petitioners at 35-40. The provisions of Sarbanes-Oxley cited by the SEC rest, at most, on an acknowledgement of the view taken by lower courts on the question of the availability of "equitable" disgorgements of the *Kokesh* kind. None of the provisions can remotely be understood either to substitute a congressional command for the judicial practice or to put Congress's mandatory seal of ratification on it, thereby placing the practice beyond judicial review by this Court.

described in *Kokesh* and put at issue here clearly is not that kind of relief.

It is readily apparent that the SEC has labored to create an aura of authoritativeness around awards of punitive securities disgorgements and that it has done so by misguidedly trying to shoehorn this relief into the canon of prior construction. *See Armstrong*, 135 S.Ct. at 1386-87 (rejecting not dissimilar use of canon). The Court should not permit a misuse of the canon to tie its hands and to place beyond its reach the correction of the lower courts on this important question of law. The correction is long overdue.

CONCLUSION

For the reasons stated above, the Court should rule that punitive disgorgements are not relief a federal court may award the SEC.

Respectfully submitted,
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Dated: December 20, 2019