No. 23-987

IN THE

Supreme Court of the United States

SHALINI AHMED,

Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

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

REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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INTRODUCTION

Certiorari is warranted because the Second Circuit has transformed disgorgement into a penalty and has stripped the Relief Defendants of their constitutional ownership rights in their assets based on infirm findings made on an erroneous basis of law. That decision clashes with this Court's precedents and those of other appeals courts, as well as has interfered with the Relief Defendants' constitutional property rights. The decision below is not only wrong but also enormously consequential, as it impacts thousands of defendant *and* relief defendant litigants in SEC proceedings.

Review of these important legal issues is especially warranted because this issue will arise repeatedly and the court of appeals' decision does not align with this Court's holdings in *Liu v. SEC,* 140 S. Ct. 1936 (2020). As a result, the SEC will collect a huge sum of money under the guise of "equitable" relief, though that relief is in reality a penalty, which is impermissible.

Disgorgement is $64.1 million, despite no "gain" in the two Company C transactions for which $14.4 million disgorgement has been assessed, and despite the alleged victim seizing an additional $35 million for the same underlying alleged conduct. Disgorgement here is a penalty of nearly $50 million, a significant sum of money.

In addition, the SEC seeks to collect that disgorgement from the Relief Defendants, based on infirm findings made on an erroneous basis of law under

the nominee doctrine. This is impermissible under this Court's precedents which reverse and remand when infirm findings are made on an erroneous basis of law. This is also against other court of appeals' decisions which utilize a multi-factor approach, and not just one factor, on the determination of nominee status.

The petition should be granted so the Court can confirm the correct standard on disgorgement to ensure it remains equitable under its holding in *Liu*, and so that constitutional property rights, especially of innocent Relief Defendants, are upheld.

ARGUMENT

Despite the SEC's blanket statement to the contrary, Opp. 8, the court of appeals did not apply the correct legal standard, and its' decision conflicts with multiple decisions of this Court.

I. The Court Should Grant the Petition to Ensure that Lower Courts Apply the Correct Standard on Disgorgement as this Court Mandated in *Liu*.

A. This Court Has Held that to Remain Equitable, Disgorgement Must Not Exceed Net Profits *And* Be Awarded for Victims.

This Court limited the vast unchecked reach of disgorgement in *Liu*, holding that "a disgorgement award that does not exceed a wrongdoer's net profits *and* is awarded for victims is equitable relief permissible." *Liu* at 1940. (emphasis added). Thus, the Court mandated that *both* requirements must be satisfied

for disgorgement to remain permissible equitable relief. The SEC instead attempts to bifurcate this requirement by arguing that the issue of disgorgement being "awarded for victims . . . is a separate question from how disgorgement is *calculated.*" Opp. 10. But disgorgement is not even authorized as equitable relief when there are no alleged victims. Indeed, it is only when "an investor has suffered pecuniary harm [that] bring[s] the investor into the category of victims." *SEC v. Govil*, 86 F.4th 89, 105 (2d Cir. 2023).[1]

Here, no investor suffered pecuniary harm in both the C1 and C2 transactions, and there are no alleged victims; thus, there is nothing to disgorge for these two transactions, and the order of disgorgement is punitive. Pet. 11-13.

Liu also defines "net profits" as "the gain made upon any business or investment, *when both the receipts and payments are taken into the account.*" *Liu* at 1945. (emphasis added) (citation omitted).[2] Yet, the SEC blatantly ignores *Liu's* clear definition. Here,

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1. Nor is there any merit to the SEC's argument that *Govil* "does not cast doubt on the correctness of the [appellate] decision here." Opp. at 10, n.* In fact, *Govil* explicitly held that "'[e]quitable relief' requires that the relief be 'awarded for victims,' *Liu*, 140 S.Ct. at 1940, and that in turn requires a finding of pecuniary harm." *Govil* at 106 (citing *Liu*). Nor will this tension be resolved, as the Second Circuit denied the SEC's petition for rehearing to address this issue. *SEC v. Govil*, 2d Cir. 22-1658, Doc. 78, Order dated January 24, 2024.

2. The district court did not apply *Liu* in its 2018 decision as *Liu* was decided in 2020. At minimum, the Court should reverse and remand with instructions to apply *Liu* to disgorgement in the first instance.

the shares in the C1 transaction were valued by the market and tendered at $10.9 million for the receipt of $10.9 million, thus there is no "gain" or "net profit" to disgorge because the *receipt* of $10.9 million is exactly equal to the value of shares *given* at $10.9 million. In other words, "when both the receipts and payments are taken into the account" the "net profits" is zero, and the alleged victim got shares worth what it paid at the market price.

Similar in the C2 transaction, where the *receipt* of $7.5 million was *less* than the value of shares *given* to the alleged victim. Indeed, the alleged victim immediately *wrote up* those shares to a value of $10.1 million. Thus, there is no "gain" or "net profit" to disgorge in this transaction, and it was the alleged victim who reaped a bargain at the time of transaction by $2.6 million.

The SEC's argument ignores this Court's holding that *both* receipts *and* payments must be accounted for in calculating net profit. Faced with this conundrum, the SEC tries to instead argue that the value of *payment* in the form of shares given does not matter. The SEC is wrong.

Another equitable limitation identified in *Liu* is that disgorgement must be "awarded for victims." *Liu* at 1940. Here, in the two Company C transactions, there is no victim, as there is no pecuniary harm, because shares were tendered at the prevailing market price in the C1 transaction and were tendered at below market price in the C2 transaction, where the alleged victim reaped a substantial bargain.

Requiring disgorgement of a further $14.4 million from these two transactions does not return the defendant to status quo, but rather confers a windfall on the alleged victim and takes the disgorgement remedy outside of the "heartland of equity." *Liu* at 1943.

The SEC's statement that "Petitioner has not disputed [C1 and C2 transactions] caused pecuniary harm . . . and that the disgorgement judgment will be distributed to . . . victims" is wrong. Opp. 10. Petitioner *has* disputed that these two transactions have caused any pecuniary harm and *has* disputed that there are any alleged victims from these two transactions. Indeed, that is what her Petition argues. Pet. 11–13.

The court of appeals' affirmation of disgorgement in both the C1 and C2 transactions conflicts with this Court's precedent and holding in *Liu*.

B. This Court Did Not Give the SEC Power to Determine Disgorgement That Would Translate into An Impermissible Penalty.

This Court has similarly held that disgorgement that "restor[es] the status quo . . . situate[s] the remedy squarely within the heartland of equity." *Liu* at 1943. (internal quotation marks omitted) (citation omitted). Here, the alleged victim has unilaterally seized an additional $35 million of assets for the same underlying conduct in this case that has not been offset against disgorgement. The SEC attempts to circumvent this Court's holding mandating disgorgement remain equitable by arguing that the Seized Assets are not "ill-gotten gain[s]" and "[were] not derived directly from [defendant's] fraud." Opp. 10.

But the SEC's argument proves the punitive nature of the disgorgement order. These Seized Assets were lawfully earned, and it is backwards to suggest that an offset would only be permissible if the Seized Assets were unlawfully earned, as the SEC argues. Here, the court of appeals not only affirmed disgorgement of $64.1 million but also affirmed denial of a credit for the forfeiture of an *additional* $35 million of Seized Assets *for the same underlying conduct.* This gives the alleged victim a prohibited "double recovery," does not restore the status quo before any alleged wrongdoing, and permits "more than a fair compensation to the person wronged." *Liu* at 1943. This also contravenes the calculation of "net profits" defined by this Court as taking into account "*both* the receipts and *payments*." *Liu* at 1945. (emphasis added in both) (citation omitted). The court of appeals' affirmance of this forfeiture without a corresponding offset has turned disgorgement into an impermissible penalty.

The SEC tries to salvage its position by attempting to differentiate other cases that permit an offset by stating that these "carried interest[s] had no concrete value." Opp. 11. Besides the fact that the alleged victim itself valued these Seized Assets at over $35 million, and was quick to seize these and other valuable assets (that have also since provided liquid distributions that have also not been offset), these assets had "value in [Petitioner and Defendant's] hands . . . the relevant inquiry at this point is not the value of the shares; it is whether the shares had value at all." *Govil* at 108. The SEC's stance simply ignores that these Seized Assets had and continue to have significant value, indeed seized by the alleged victim at the first instance.

Also, the district court never even addressed the issue of value because it reasoned that the alleged victim seized not ill-gotten gains, but rather *lawfully-earned assets* "forfeited" because of "Disabling Conduct" – the same alleged underlying conduct at issue in this case. Pet. App. 89. The denial of an offset for these Seized Assets cannot be squared with *Liu* and has turned disgorgement into an impermissible penalty.

Contrary to the SEC's argument, the Petitioner is entitled to raise these issues because the SEC is seeking to take all of Petitioner's and Relief Defendants' assets in satisfaction of its judgment, wherein disgorgement is punitive, in violation of this Court's holdings.

II. The Court Should Grant the Petition to Ensure Relief Defendants' Constitutional Ownership Rights are Upheld.

The appellate court found that the district court "erroneously shifted the burden to the Relief Defendants to show that [Defendant] is *not* the equitable owner of assets to which the Relief Defendants hold legal title." Pet. App. 49. (italics in original). This erroneous shifting of burden also included the three assets at issue: the minor children's Family Trust, their MetLife insurance policy, and Petitioner's Fidelity x7540 account.

This Court holds that "where findings [of the district court] are infirm because of an erroneous view of the law, a remand is the proper course . . . " and that "[in this situation] the court of appeals is not relieved of the usual requirement of remanding for further

proceedings to the tribunal charged with the task of factfinding in the first instance." *Pullman-Standard v. Swint*, 456 U.S. 273, 292 (1982). Here, the district court's findings are infirm, not legally sufficient, and based on an erroneous view of the law.

Contrary to the SEC's misstatement, the district court did not find that Defendant had "funded th[e] Trust" using money obtained from any alleged fraud, but only that the SEC *alleged* so, specifically stating "Relief Defendants argue that . . . the SEC has not shown [Trust] w[as] funded by Defendant's illicit gains . . . [t]he SEC *counters* that the [$9 million Trust] was funded with Defendant's money, including [from two frauds totaling $3.577 million] . . . Because the *evidence establishes only that Defendant funded this Trust* . . . the [Trust] was funded and created using Defendant's money and therefore can be used to satisfy a judgment against him." Pet. App. 83 n.21. (emphasis added in both). The district court based its ruling solely on the fact that the Trust was "funded and created" by Defendant.

This one factual finding is "infirm" and not legally sufficient to strip the minor children of their constitutional ownership rights in their Trust and MetLife insurance policy and is contrary to this Court's holdings in *Pullman*. The district court did not find that the Trust was funded with any proceeds of fraud, and only claimed that the Trust could be used for the Defendant's judgment because it "was funded and created using Defendant's money." App. Pet. 83 n.21. The district court simply mentioned control as it related to the Trust's interest in another asset, but because it

applied the wrong law, it never engaged with the fact that the Trust is not even a named relief defendant, was controlled by an independent third-party Trustee, and *only* benefitted the minor children, who have an unquestionable equitable stake in the Trust's assets. Pet. 16. Instead, the district court based the nominee status of the Trust on this one infirm finding on an erroneous view of the law and the appellate court's affirmance stands against this Court's precedents of remanding for further fact-finding in these situations.

Because it applied the wrong law, the district court also did not engage with the fact that Petitioner *controlled* her Fidelity x7540 account, which was, *inter alia*, opened for her by her ex-employer and where she transferred and invested funds.

The district court's reliance on one finding on the Trust and two preliminary-injunction findings on Petitioner's Fidelity x7540 account go against other circuit cases where courts have adhered to multi-factor nominee findings, especially at the judgment stage. Pet. 17-18. Here, the district court cited the six-factor nominee rule but did not even apply it (let alone erroneously), because it wrongly deemed the burden of proof to be the Relief Defendants' responsibility. The district court's finding that it could take the (i) Trust solely because it "was funded and created using Defendant's money." App. Pet. 83 n.21, (ii) MetLife insurance policy because it was owned by the Trust, *id.*, and (iii) Petitioner's Fidelity x7540 account based on preliminary-injunction findings App. Pet. 82 n.19, are not legally sufficient to strip the Relief Defendants

from their constitutional ownership rights in these assets worth over $30 million.

Nor is this harmless error, as constitutional ownership rights are implicated, and the Relief Defendants are prejudiced by the infirm findings made on an erroneous basis of law. The district court's legal error has affected the substantial rights of the Relief Defendants. Indeed, upon remand, the district court would have applied the correct legal standard on these three assets and considered the Relief Defendants' evidence, including those relating to control and benefit. This is critical, as "[t]h[ese] factual issue[s] [are] dispositive of the case . . . the Court of Appeals should not have resolved in the first instance this factual dispute which had not been considered by the District Court." *Demarco v. U.S.*, 415 U.S. 449, 450 (1974).

III. Review is Especially Warranted on These Legal Questions to Ensure that Disgorgement Remains Equitable and that Relief Defendants' Constitutional Rights Are Upheld.

The questions here are substantial and important and impact all defendants and relief defendants in SEC cases, as the SEC aggressively seeks disgorgement and aggressively goes after innocent Relief Defendants' assets to satisfy the Defendant's judgment.

The SEC mischaracterizes the questions of law petitioner presents about the mandatory equitable nature of disgorgement and the requirement to remand when the wrong law is applied. These questions are

hardly fact-bound and are instead quintessential questions of law that are ripe for this Court's review and that will give much-needed guidance to courts after *Liu*.

The facts of this case are relevant only to show that disgorgement is punitive and that the three assets cannot be deemed nominees based on infirm findings made on an erroneous basis of law. The facts have no impact on the justiciability of the legal questions presented and ruled upon below. These legal questions are not fact-bound. The parties have a legal dispute on if equity permits disgorgement when there is no pecuniary loss; legal dispute if equity permits disgorgement if value has been returned to the alleged victim through shares given and also through the seizure of many millions of dollars of additional assets from the alleged wrongdoer; legal dispute if Relief Defendant assets can be taken for a Defendant's judgment even if infirm findings not legally sufficient were made on an erroneous basis of law; and legal dispute if their assets can be taken at judgment-stage on preliminary-injunction findings. All these present legal issues that warrant further review.

And while the parties dispute the value of the Seized Assets and disgorgement calculation in the two Company C transactions, the district court committed *legal* error when it did not offset disgorgement by the value of the Company C shares and Seized Assets. Pet. 7-13.

Similarly, while the parties dispute the extent of control and benefit that Defendant allegedly had over

Relief Defendants' assets, when the district court ruled that Relief Defendants' assets could be taken simply because Defendant "funded and created" the asset, or based on preliminary-injunction findings, it committed *legal* error by making infirm findings on an erroneous basis of law. Pet. 13-19.

The two-court rule does not limit review in cases like this, where two courts have deviated from this Court's holdings by affirming disgorgement as punitive and stripping Relief Defendants from their constitutional ownership rights in their assets based on infirm findings made on an erroneous basis of law, both which warrant further legal review. Nor does the two-court rule preclude this Court from independently examining any factual issues that implicate constitutional rights. *See, e.g., Napue v. Illinois,* 360 U.S. 264, 271-272 (1959); *Fiske v. Kansas,* 274 U.S. 380, 385-386 (1927).

The SEC collects billions of dollars in disgorgement annually. Under *Liu*, this Court has mandated these amounts be equitable. If the SEC can circumvent this Court's holdings to collect penalties under the guise of "equitable" disgorgement, surely that is an issue of immediate importance for this Court to address.

Granting certiorari would ensure that courts adhere to this Court's holding that disgorgement must remain within equitable limits and cannot be punitive; and that Relief Defendants' assets cannot be taken for a Defendant's judgment without proper analysis using the correct law. This impacts many defendants and relief defendants in SEC proceedings, now and in future.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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