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

BRIEF FOR PARKER R. HALLAM AND FREDERICK A. VOIGHT AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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TABLE OF CONTENTS

Page

TABLE OF CITED AUTHORITIES iii

INTEREST OF *AMICI CURIAE* 1

SUMMARY OF ARGUMENT 2

ARGUMENT 2

I. DISGORGEMENT IS NOT A REMEDY AUTHORIZED BY CONGRESS AND MAY NOT BE IMPOSED IN CIVIL ENFORCEMENT ACTIONS 3

A. Evolution of the "Disgorgement" Remedy 4

B. Statutory Amendments Enacting A Comprehensive Remedies Scheme Displaced Common-Law Equitable Disgorgement 7

C. *Central Bank of Denver* Precludes Claims and Remedies Not Expressly Authorized by Securities Statutes 11

D. *Great-West* Forecloses the Imposition of "Disgorgement" as an Equitable Remedy 15

Table of Contents

Page

E. *Kokesh* Confirms that "Disgorgement" is a Penalty, Not an Equitable Remedy 20

CONCLUSION 25

TABLE OF CITED AUTHORITIES

Page

CASES

Astoria Fed. Sav. & Loan Ass'n v. Solimino,
501 U.S. 104 (1991) 8

Bowen v. Massachusetts,
487 U.S. 879 (1988) 16

Cent. Bank of Denver v. First Interstate Bank of Denver,
511 U.S. 164 (1994) 11-12

Cent. States, Se. & Sw. Areas Health & Welfare Fund ex rel. Bunte v. Health Special Risk, Inc.,
756 F.3d 356 (5th Cir. 2014) 18-19

City of Milwaukee v. Illinois & Michigan,
451 U.S. 304 (1981) 7-8, 10

Cleary v. Perfectune, Inc.,
700 F.2d 774 (1st Cir. 1983) 11

Page

Dirks v. SEC,
681 F.2d 824 (D.C. Cir.), *rev'd on other grounds*, 463 U.S. 646 (1983) 11-12

Edmonson v. Lincoln Nat. Life Ins. Co.,
777 F. Supp. 2d 869 (E.D. Penn. 2011) 22

Erie R. Co. v. Tompkins,
304 U.S. 64 (1938)...7

Fairfax's Devisee v. Hunter's Lessee,
11 U.S. (7 Cranch) 603 (1812) 8

Farlow v. Peat, Marwick, Mitchell & Co.,
956 F.2d 982 (10th Cir. 1992)...............................11

Fazaga v. Fed. Bureau of Investigation,
916 F.3d 1202 (9th Cir. 2019)...............................10

Fine v. Am. Solar King Corp.,
919 F.2d 290 (5th Cir. 1990).................................11

Great-West Life & Ann. Ins. Co. v. Knudson,
534 U.S. 204 (2002)...15-19

Horvath v. Keystone Health Plan E., Inc.,
333 F.3d 450 (3d Cir. 2003) 22

Page

IIT v. Cornfeld,
619 F.2d 909 (2d Cir. 1980) 11

Isbrandtsen Co. v. Johnson,
343 U.S. 779 (1952) 8

K & S P'ship v. Cont'l Bank, N.A.,
952 F.2d 971 (8th Cir. 1991) 11

Kokesh v. SEC,
137 S. Ct. 1635 (2017) 1, 14, 20-22

Levine v. Diamanthuset, Inc.,
950 F.2d 1478 (9th Cir. 1991) 11

Mobil Oil Corp. v. Higginbotham
436 U.S. 618 (1993) 8

Monsen v. Consol. Dressed Beef Co.,
579 F.2d 793 (3d Cir. 1978) 11

Moore v. Fenex, Inc.,
809 F.2d 297 (6th Cir.), *cert. denied sub nom. Moore v. Frost*, 483 U.S. 1006 (1987) 11

Reich v. Cont'l Cas. Co.,
33 F.3d 754 (7th Cir. 1994) 17

Page

Sandoz Inc. v. Amgen Inc.,
137 S. Ct. 1664 (2017) 9-10

Schatz v. Rosenberg,
943 F.2d 485 (4th Cir. 1991) 11

Schlifke v. Seafirst Corp.,
866 F.2d 935 (7th Cir. 1989) 11

Schneberger v. Wheeler,
859 F.2d 1477 (11th Cir. 1988) 11

SEC v. Amerifirst Funding, Inc.,
No. 3:07-CV-1188-D, 2008 WL 1959843
(N.D. Tex. May 5, 2008) 21-22

SEC v. Blatt,
583 F.2d 1325 (5th Cir. 1978) 14

SEC v. Clark,
915 F.2d 439 (9th Cir. 1990) 21

SEC v. Contorinis,
743 F.3d 296 (2d Cir. 2014) 21

SEC v. ETS Payphones, Inc.,
408 F.3d 727 (11th Cir. 2005) 21-22

Page

SEC v. Halek,
537 F. App'x 576 (5th Cir. 2013) ... 18

SEC v. Kahlon,
873 F.3d 500 (5th Cir. 2017) ... 14

SEC v. Seghers,
298 F. App'x. 319 (5th Cir. 2008) ... 18

SEC v. Texas Gulf Sulphur Co.,
446 F.2d 1301 (2d Cir. 1971) ... 5, 23

SEC v. Texas Gulf Sulphur Co.,
312 F. Supp. 77 (S.D.N.Y. 1970),
aff'd in part and rev'd in part,
446 F.2d 1301 (2d Cir. 1971) ... 4-5

SEC v. Warde,
151 F.3d 42 (2d Cir. 1998) ... 21

Texas v. Pankey,
441 F.2d 236 (10th Cir. 1971) ... 10

TVA v. Hill,
473 U.S. 153 (1978) ... 10

Page

United States v. Am. Commercial Lines, L.L.C. 759 F.3d 420 (5th Cir. 2014) 9

United States v. Hudson & Goodwin, 11 U.S. (7 Cranch) 32 (1812) 7

United States v. Texas, 507 U.S. 529 (1993) 8

Zoelsch v. Arthur Andersen & Co., 824 F.2d 27 (D.C. Cir. 1987) 12

STATUTES AND OTHER AUTHORITIES

1 T. Hazen, LAW OF SECURITIES REGULATION § 1:37 (7th ed., rev. 2016) 4

15 U.S.C. § 77h-1(e) 6

15 U.S.C. § 77t(d) 15, 24

15 U.S.C. § 78j 12

15 U.S.C. § 78q-2 6

15 U.S.C. § 78t(e) 12

Page

15 U.S.C. § 78u(d)(3)(B) 15, 24

15 U.S.C. § 78u(d)(5) 13

15 U.S.C. § 78u-2...6

15 U.S.C. § 78u-2(e)...6

15 U.S.C. § 78u-3...6

15 U.S.C. § 78u-3(e)...6

Annual Report, Division of Enforcement, U.S. Securities and Exchange Comm'n (2018) 5

Employee Retirement Income Security Act of 1974 § 502(a)(3), 29 U.S.C. § 1132(a)(3)........15-16, 18-19

Oil Pollution Act of 1990, 33 U.S.C. § 2701 *et. seq.*..9

Securities Enforcement Remedies and Penny Stock Reform Act. Pub. L. 101-429, Oct. 15, 1990, 104 Stat. 931 (1990)...6

Securities Exchange Act of 1934 § 21(d)(5), 15 U.S.C. § 78u(d)(5)...........................2-3, 13-15, 19

INTEREST OF *AMICI CURIAE*[1]

Nowhere in the comprehensive provisions of the federal securities statutes did Congress provide the Securities and Exchange Commission ("SEC") with authority to obtain disgorgement from defendants in federal district court cases. Moreover, this Court recently concluded that the remedy of disgorgement in SEC enforcement actions is a penalty, *Kokesh v. SEC*, 137 S. Ct. 1635, 1639 (2017), raising the further issue of whether awards of disgorgement—especially when coupled with a civil money penalty—exceed statutory penalty caps.

Parker R. Hallam and Frederick A. Voight are defendants in separate pending civil enforcement actions in which the SEC seeks judgments of disgorgement in addition to statutory monetary penalties. As victims of attempted SEC and judicial overreach on the very issue facing the Court, *amici* have a substantial interest in supporting Petitioners' appeal in this case, and specifically in establishing that the SEC has no legal basis, in law or equity, to seek the remedy of disgorgement in district court actions.

[1] This brief is submitted under Federal Rule of Appellate Procedure 29(a) with the consent of all parties. Petitioner's blanket consent is on file with this Court. Respondent's consent was received by letter on December 20, 2019. Undersigned counsel for *amici curiae* certify that no counsel for a party authored this brief in whole or in part; no party or their counsel have made a monetary contribution intended to fund the preparation or submission of this brief; and no one other than *amici curiae* and their counsel made any monetary contribution intended to fund the preparation and submission of this brief.

SUMMARY OF ARGUMENT

Congress has enacted a comprehensive and detailed enforcement scheme to address violations of federal securities laws, including a specific set of remedies available in district court actions. In disregard of the prerogatives of the legislative branch, the courts in every circuit have nevertheless crafted their own remedial scheme, imposing judgments of "disgorgement" against defendants, a remedy never authorized by Congress.

The purported remedy of disgorgement in securities law actions cannot survive scrutiny under common law notions of "inherent" or "ancillary" authority or under the very terms of the applicable statutes, here the Securities Act and Exchange Act. The comprehensive legislative enforcement scheme vitiates the old common law rationale for judicially-created remedies under the doctrine of displacement.

The Court has long held litigants—including the government—to the clear and express terms of these statutes, precluding resort to claims not directly and explicitly authorized under the plain language of the securities laws. The SEC justifies disgorgement under the general grant of equitable power contained in Exchange Act § 21(d)(5), which restricts district courts to equitable relief fashioned for the benefit of the investors. Disgorgement fails under that section for two reasons: First, because there is no res, there is no basis for the exercise of equitable power. Second, the Court in *Kokesh* has held SEC disgorgement to be a penalty, which removes any argument that disgorgement qualifies as an equitable remedy.

The *Kokesh* Court also noted that disgorgement in SEC enforcement actions commonly goes to the U.S. Treasury, not to any defrauded investors, further removing it from the purview of § 21(d)(5).

The continued imposition of judicially-created "disgorgement" awards, despite the comprehensive enforcement scheme enacted by Congress, allows for recoveries over and above statutory penalty caps set by statute and cannot be reconciled with the Court's separation of powers jurisprudence and the respect the Article III courts are obliged to accord the authority and role of the legislative branch.

The so-called remedy of disgorgement as fashioned and embellished by the lower courts suffers from these multiple fatal infirmities. The Court should therefore rule that the remedy of disgorgement is not authorized in civil enforcement actions.

ARGUMENT

I. DISGORGEMENT IS NOT A REMEDY AUTHORIZED BY CONGRESS AND MAY NOT BE IMPOSED IN CIVIL ENFORCEMENT ACTIONS

Despite the SEC's routinely seeking and collecting disgorgement awards in federal district court cases—apparently with little challenge over the years—the federal securities laws do not authorize disgorgement as a remedy in district court enforcement cases. The Petitioners were charged

with, *inter alia*, violations under the Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act"). Neither statute provides disgorgement as a remedy in an injunctive proceeding in district court cases. Recent decisions by this Court establish beyond peradventure that the SEC has no authority to seek, and a district court has no authority to impose, a judgment of "disgorgement" against a defendant in a civil enforcement action.

A. Evolution of the "Disgorgement" Remedy

For decades after the Depression-era enactment of modern securities legislation, the only statutory remedy available to the SEC in an enforcement action was an injunction barring future violations of securities laws.[2] In the absence of statutory authorization for monetary remedies, the Commission urged courts to order what it called "disgorgement" of "ill-gotten gains" as an exercise of their "inherent equity power to grant relief ancillary to an injunction." In 1970, the agency first found success in *SEC v. Texas Gulf Sulphur Co.,* 312 F.

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[2] *See* 1 T. Hazen, LAW OF SECURITIES REGULATION § 1:37 (7th ed., rev. 2016). Subsequent amendments to the Securities Exchange Act of 1934 and additional legislation including the Investment Advisers Act of 1940, the Securities Enforcement Remedies and Penny Stock Reform Act, the Sarbanes-Oxley Act, and, most recently, the Dodd-Frank Wall Street Reform and Consumer Protection Act, specifically empowered the agency to seek injunctions, administrative cease-and-desist orders, monetary penalties, and bars and suspensions from certain types of employment in the securities industry. None of this legislation ever authorized a remedy of "disgorgement" by federal courts in SEC enforcement actions.

Supp. 77, 91 (S.D.N.Y. 1970), *aff'd in part and rev'd in part*, 446 F.2d 1301 (2d Cir. 1971). The circuit court upheld the disgorgement remedy under that premise while admonishing that "the 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." 446 F.2d at 1308.

In the half century since the *Texas Gulf Sulphur* decision, the authority of federal courts to order disgorgement has been expanded and accepted as doctrine. The SEC and the courts have made these orders routine in enforcement practice. The SEC has employed the sanction of disgorgement to recoup billions of dollars from defendants in enforcement cases – often more than the amount recouped in congressionally-authorized monetary penalties. For example, in 2018, the SEC obtained $2.5 billion in disgorgement judgments as compared to about $1.4 billion in penalty assessments.[3] The agency's ability to achieve such large recoveries is attributable to the breadth of activity to which disgorgement can apply. Under shifting and inconsistent standards fashioned exclusively by the courts, defendants have been required to disgorge funds that they never possessed, but that instead went to an unrelated third party, so long as those funds can be traced to the alleged violation. Further, the amount of disgorgement need only be a

[3] Annual Report, Division of Enforcement, U.S. Securities and Exchange Comm'n (2018), available at https://www.sec.gov/files/enforcement-annual-report-2018.pdf, last visited December 20, 2019.

"reasonable approximation of profits causally-connected to the violation."[4]

The rationale allowing the SEC to extract these massive and unpredictable awards from defendants, solely under the "ancillary" notion of common law equitable power—without any express grant of legislative authority—was fueled by a statutory enforcement framework that provided no monetary consequence for securities violators, much less an orderly penalty scheme. But that rationale was dealt a series of blows starting in 1990, when Congress first authorized the SEC to seek civil monetary penalties generally, inaugurating the multi-tiered penalty regime in place today.[5] In addition to the new civil penalty scheme, Congress expressly, and for the first time, created a disgorgement remedy, but *limited the imposition of that remedy to administrative proceedings only*, conspicuously not authorizing the remedy in federal court actions.[6]

The continuing vitality of the disgorgement remedy in Article III courts was further emasculated by a series of decisions by this Court, particularly in three pivotal cases which, both alone and together, establish that the SEC has no legal authority to

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[4] *See* discussion *infra*, at pp. 21-22.

[5] Securities Enforcement Remedies and Penny Stock Reform Act. Pub. L. 101-429, Oct. 15, 1990, 104 Stat. 931 (1990) (relevant sections codified as amended at 15 U.S.C. §§ 78q–2, 78u–2, 78u–3).

[6] *See* 15 U.S.C. §§ 77h-1(e), 78u-2(e), and 78u-3(e).

seek, and a district court has no authority to impose, any amount of so-called "disgorgement" in an SEC enforcement action.

B. Statutory Amendments Enacting A Comprehensive Remedies Scheme Displaced Common-Law Equitable Disgorgement

The old "equitable" remedy of disgorgement was displaced by the enactment of a comprehensive scheme of remedies in the federal securities statutes. The federal "common law" was the original font of "ancillary" disgorgement authority, starting with the *Texas Gulf Sulphur* decision in 1970. But the doctrine of displacement precludes continuing resort to common law equitable remedies when Congress has acted to create a comprehensive statutory enforcement scheme, as Congress did beginning with its overhaul of the federal securities statutes in 1990.

The Court has long recognized that federal common law can exist only in the absence of statutory mandates. "Federal courts, unlike state courts, are not general common-law courts and do not possess a general power to develop and apply their own rules of decision." *City of Milwaukee v. Illinois & Michigan*, 451 U.S. 304, 312–13 (1981) (citing *Erie R. Co. v. Tompkins*, 304 U.S. 64, 78 (1938) and *United States v. Hudson & Goodwin*, 11 U.S. (7 Cranch) 32 (1812)). Although sometimes "[f]ederal common law is a 'necessary expedient,'" it is also true that "when Congress addresses a question previously governed by a decision rested on federal common law the need for such an unusual

exercise of lawmaking by federal courts disappears." *Id.* at 314.

Although this Court has also acknowledged that statutes invading the common law are to be read with a presumption favoring retention of existing law, that longstanding principle does not apply when a statutory purpose to the contrary is evident. *United States v. Texas*, 507 U.S. 529, 534 (1993); *Isbrandtsen Co. v. Johnson*, 343 U.S. 779, 783 (1952); *Astoria Fed. Savings & Loan Ass'n. v. Solimino*, 501 U.S. 104, 108 (1991). To effectively abrogate a labyrinth of developed common law, Congress need not "affirmatively proscribe" the common law doctrine at issue. *City of Milwaukee*, *supra*, at 315. The doctrine of displacement serves to nullify applicable common law principles so long as the supervening legislation "speak[s] directly" to the question addressed by the common law. *Id. at* 315; *Mobil Oil Corp. v. Higginbotham*, 436 U.S. 618, 625 (1993).

Modern displacement analysis assumes that "it is for Congress, not the federal courts, to articulate the appropriate standards to be applied as a matter of federal law." *City of Milwaukee, supra, at* 316–17 (holding that federal common law applies only "[u]ntil the field has been made the subject of comprehensive legislation or authorized administrative standards"). *Cf.*, *Fairfax's Devisee v. Hunter's Lessee*, 11 U.S. (7 Cranch) 603, 623 (1812) ("The common law, therefore, ought not to be deemed to be repealed, unless the language of a statute be clear and explicit for this purpose.").

The Fifth Circuit's recent analysis in *United States v. Am. Commercial Lines, L.L.C.*, is instructtive and consistent with the Court's current displacement jurisprudence. 759 F.3d 420 (5th Cir. 2014). The government brought an action against the party responsible for an oil spill to recover amounts paid from Oil Spill Liability Trust Fund to contractors who had been engaged to clean-up the oil spill. *Id*. at 422-23. The responsible party then filed a third-party complaint against the contractors under federal common law. *Id*. at 423-24. The Fifth Circuit held that Oil Pollution Act of 1990 (OPA), 33 U.S.C. § 2701—which imposed strict liability on responsible parties and had no allowance for third-party claims—displaced the responsible party's common law claims against the contractors. *Id*. at 426. Noting first that when Congress enacts a carefully-calibrated liability scheme with respect to specific remedies, "the structure of the remedies suggests that Congress intended for th[e] statutory remedies to be exclusive," *id.* at 424, the court held that "federal common law has been preempted as to every question to which the legislative scheme spoke directly, and every problem that Congress has addressed." *Id*. at 425 (internal quotes and citations omitted). The Fifth Circuit concluded that the OPA's "balanced and comprehensive remedial scheme' provides the exclusive remedy for a claimant to recover statutory removal costs from a responsible party and forecloses a responsible party from bringing a [common law] third-party complaint against a spill responder." *Id.*

In *Sandoz Inc. v. Amgen Inc.*, the Court was more recently presented with a patent infringement action

by a drug manufacturer under the Biologics Price Competition and Innovation Act against an applicant for a biosimilar drug. 137 S. Ct. 1664, 1675 (2017). The Court concluded that common law injunctive relief was not available because the Act did not provide that remedy. *Id.*

When confronting other displacement claims, the lower courts have held consistently that once "the field has been made the subject of comprehensive legislation or authorized administrative standards," federal common law no longer applies. *Fazaga v. Fed. Bureau of Investigation*, 916 F.3d 1202, 1230 (9th Cir. 2019) (quoting *Texas v. Pankey*, 441 F.2d 236, 241 (10th Cir. 1971)). Here, the continued imposition of the common-law remedy of disgorgement in SEC enforcement actions is precluded by the enactment of a comprehensive and elaborate statutory scheme which imposes a well-calibrated construct of remedies, even if the agency or the courts may find the wisdom of that remedial structure wanting. "Our 'commitment to the separation of powers is too fundamental' to continue to rely on federal common law "by judicially decreeing what accords with 'common sense and the public weal' when Congress has addressed the problem.'" C*ity of Milwaukee, supra*, 451 U.S. at 314–15, quoting *TVA v. Hill*, 473 U.S. 153, 195, (1978).

Because the federal securities statutes provide a comprehensive scheme of regulation and enforcement, detailing all available causes of action and remedies, the doctrine of displacement wholly vitiates the "equitable" remedy of disgorgement to

the extent it remains grounded in common law notions of inherent or ancillary equitable authority.

C. *Central Bank of Denver* Precludes Claims and Remedies Not Expressly Authorized by Securities Statutes

Deference to the constitutional prerogatives of Congress led the Court to the same result a quarter century ago when considering the continued prosecution of a common law claim of aiding-and-abetting under the federal securities laws. The 1994 ruling in *Central Bank of Denver v. First Interstate Bank of Denver* makes clear that the statutory text governs strictly the scope of authority conferred by the federal securities statutes and that claims cannot be manufactured by implication. 511 U.S. 164 (1994). At issue in *Central Bank of Denver* was the legal viability of the long-sanctioned claim for aiding-and-abetting liability in securities fraud cases under § 10(b) of the Exchange Act, a "secondary liability" claim that had been accepted and enforced by every circuit[7] since at least 1966. *Id.* at 169. The statutory

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[7] *See, e.g.*, *Cleary v. Perfectune, Inc.*, 700 F.2d 774, 777 (1st Cir. 1983); *IIT v. Cornfeld,* 619 F.2d 909, 922 (2d Cir. 1980); *Monsen v. Consol. Dressed Beef Co.*, 579 F.2d 793, 799–800 (3d Cir. 1978); *Schatz v. Rosenberg,* 943 F.2d 485, 496–97 (4th Cir. 1991); *Fine v. Am. Solar King Corp.*, 919 F.2d 290, 300 (5th Cir. 1990); *Moore v. Fenex, Inc.*, 809 F.2d 297, 303 (6th Cir.), *cert. denied sub nom. Moore v. Frost*, 483 U.S. 1006 (1987); *Schlifke v. Seafirst Corp.*, 866 F.2d 935, 947 (7th Cir. 1989); *K & S Partnership v. Cont'l Bank, N.A.*, 952 F.2d 971, 977 (8th Cir. 1991); *Levine v. Diamanthuset, Inc.*, 950 F.2d 1478, 1483 (9th Cir. 1991); *Farlow v. Peat, Marwick, Mitchell & Co.*, 956 F.2d 982, 986 (10th Cir. 1992); *Schneberger v. Wheeler,* 859 F.2d 1477, 1480 (11th Cir. 1988). The only court

language in question proscribed the violation of securities laws "directly or indirectly,"[8] but did not expressly authorize causes of action for aiding-and-abetting. The Court held that the statutory text was controlling and refused to permit the imposition of aiding and abetting liability by implication, striking down thirty years of jurisprudence and rejecting the claim because the statute did not expressly authorize it.[9] *Id*. The Court did so over the dissent's protestation that aiding-and-abetting liability was "settled law" with "a long pedigree in civil proceedings brought by the SEC under § 10(b) and Rule 10b–5, and ha[d] become an important part of the SEC's enforcement arsenal."[10]

Central Bank of Denver clarified that federal securities statutes are to be strictly construed as meaning only what they say; if an enforcement tool is not expressly provided by Congress in the statutory scheme, it does not exist. There is no such thing as

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not to have squarely recognized aiding and abetting in private § 10(b) actions had done so in an action brought by the SEC, *see Dirks v. SEC*, 681 F.2d 824, 844 (D.C. Cir.), *rev'd on other grounds*, 463 U.S. 646 (1983), and had suggested that such a claim was available in private actions, *see Zoelsch v. Arthur Andersen & Co.,* 824 F.2d 27, 35–36 (D.C. Cir. 1987).

[8] Section 10(b) is codified at 15 U.S.C. § 78j.

[9] Congress responded by later expressly authorizing the SEC to bring civil actions against aiders and abettors of violations of the Exchange Act by enacting 15 U.S.C. § 78t(e), as part of the Private Securities Litigation Reform Act of 1995.

[10] 511 U.S. at 200 (Stevens, J., dissenting).

an "implied" claim or remedy under the federal securities statutes.

The statutory language from which the "disgorgement" remedy allegedly derives suffers from the same infirmity as the § 10(b) language addressed by the Court in *Central Bank of Denver*. Since the precise and comprehensive architecture of the securities laws have now displaced the old open-ended common law rationale, the sole potential source for the imposition of "disgorgement" derives from the qualified reference to "equitable relief" found only in Section 21(d)(5) of the Exchange Act. Although the Exchange Act does provide sanction for legitimate equitable remedies in district court cases, that legislative authorization is expressly and uniquely circumscribed, precluding resort to a district court's "inherent" or "ancillary" authority in matters of equity:

> In any action or proceeding brought or instituted by the Commission under any provision of the securities laws, the Commission may seek, and any Federal court may grant, any equitable relief that may be appropriate or necessary *for the benefit of investors*.[11]

Thus only equitable remedies specifically fashioned "for the benefit of investors" are available under the Exchange Act. This precludes the pursuit

[11] 15 U.S.C. § 78u (d)(5) (emphasis added). There is no parallel provision for equitable relief under the Securities Act, Investment Company Act of 1940 or Investment Advisers Act of 1940.

or imposition of any amount of disgorgement in this case because the purpose of disgorgement in SEC cases is *not* to compensate the victims of a securities fraud, but to deprive the wrongdoer of his "ill-gotten" gain. *See Kokesh v. SEC,* 137 S. Ct. 1635, 1639 (2017); *SEC v. Kahlon*, 873 F.3d 500, 509 (5th Cir. 2017) ("purpose of disgorgement is not to compensate the victims of the fraud, but to deprive the wrongdoer of his ill-gotten gain.") (quoting *SEC v. Blatt*, 583 F.2d 1325, 1335 (5th Cir. 1978)). This alone establishes conclusively that disgorgement—which normally is paid to the U.S. Treasury—is not "for the benefit of investors."[12] Under *Central Bank of Denver,* a district court may only enforce remedies expressly authorized in the plain language of the federal securities statutes; since disgorgement is not an equitable remedy expressly authorized by Section 21(d)(5), there is not any amount of disgorgement that may be sought by the SEC or imposed by an Article III court in this case.

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[12] Disgorgement in SEC enforcement actions is a separate and additional remedy from receiverships, which are appointed as an exercise of statutorily-authorized equitable authority performed directly "for the benefit of investors" under § 21(d)(5). Even in cases where the court has appointed a receiver to marshal assets and collect additional funds through litigation "claw-backs" for restitution to investors, the separate monetary judgment against the defendant for disgorgement transcends the receiver's function and imposes personal liability upon a defendant or "relief defendant" for amounts not dependent upon any res identified and administered by a receiver. This precludes the "disgorgement" award from characterization as "equitable" relief. *See* discussion *infra* at pp. 17-18.

In civil enforcement actions under the federal securities laws, Congress has decided to empower courts to impose penalties under a detailed three-tier structure, but has said nothing of disgorgement. In this case, the statutory scheme only permits the imposition of penalties under the formulation codified in 15 U.S.C. § 77t(d) (Securities Act) and 15 U.S.C. § 78u(d)(3)(B) (Exchange Act), all under specified penalty caps.

The remedy of disgorgement cannot be justified as emanating from the federal common law, and must survive, if it can, only as a statutory remedy authorized by the qualified grant of equitable power found in § 21(d)(5) of the Exchange Act. But as decisions subsequent to *Central Bank of Denver* have demonstrated, disgorgement cannot survive scrutiny as a statutorily-sanctioned equitable remedy either.

D. *Great-West* Forecloses the Imposition of "Disgorgement" as an Equitable Remedy

That disgorgement is no longer available as a statutory equitable remedy under the Securities Act or the Exchange Act is further demonstrated by the Court's 2002 seminal holding in *Great-West Life & Ann. Ins. Co. v. Knudson*, where, like here, the availability of a similar remedy was rejected as falling outside an express statutory grant of equitable power. 534 U.S. 204, 218, 221 (2002). At issue in *Great-West* was an ERISA plan's insurance carrier's suit to recoup anticipated proceeds from a future judgment against a third-party tortfeasor, a

claim grounded in § 502(a)(3) of ERISA.[13] That section authorized claims "(A) to enjoin any act or practice which violates ... the terms of the plan, or (B) to *obtain other appropriate equitable relief* (i) to redress such violations or (ii) to enforce any provisions of ... the terms of the plan." 29 U.S.C. § 1132(a)(3) (emphasis added). Because "§ 502(a)(3), by its terms, only allows for *equitable* relief," the Court analyzed the nature of the claim as either *legal* or *equitable* to determine whether it fell within Congress's legislative authorization of remedies for "other appropriate equitable relief." *Great-West*, 534 U.S. at 221.

The *Great-West* Court noted that "suits seeking (whether by judgment, injunction, or declaration) to compel the defendant to pay a sum of money to the plaintiff are suits for 'money damages,' as that phrase has traditionally been applied, since they seek no more than compensation for loss resulting from the defendant's breach of legal duty." *Id.* at 210 (quoting *Bowen v. Massachusetts,* 487 U.S. 879, 918–19 (1988) (Scalia, J., dissenting)). Of course, money damages are "the classic form of *legal* relief." *Id.* On the other hand, for a restitution-type claim to lie in equity, "the action generally must seek not to impose personal liability on the defendant, but to restore to the plaintiff *particular funds or property in the defendant's possession*." *Id.* at 214 (emphasis added).

Using these time-honored canons, the *Great-West* Court held that the claim against the plan

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[13] Employee Retirement Income Security Act of 1974 (ERISA) § 502(a)(3), 29 U.S.C. § 1132(a)(3).

beneficiary for the wrongfully-withheld proceeds—although essentially a claim for restitution—was legal and not equitable. The Court rejected the argument that claims for restitution traditionally sound in equity, holding that "whether it is legal or equitable depends on 'the basis for [the plaintiff's] claim' and the nature of the underlying remedies sought." *Id.* at 213 (quoting *Reich v. Cont'l Cas. Co.,* 33 F.3d 754, 756 (7th Cir. 1994)). The Court explained that restitution claims are legal where judgment is sought "imposing a merely personal liability upon the defendant to pay a sum of money." *Id*.

Historically, the Court explained, "[i]n cases in which the plaintiff 'could *not* assert title or right to possession of particular property, but in which nevertheless he might be able to show just grounds for recovering money to pay for some benefit the defendant had received from him,' the plaintiff had a right to restitution *at law* through an action derived from the common-law writ of assumpsit." *Id.* In contrast, "a plaintiff could seek restitution *in equity,* ordinarily in the form of a constructive trust or an equitable lien, where money or property identified as belonging in good conscience to the plaintiff could clearly be traced to particular funds or property in the defendant's possession." In *Great-West*, as in this case, the subject funds "are not in [defendant's] possession," precluding the categorization of the claim as one in equity. *Id.* at 214.

Finally, the *Great-West* Court tackled the argument advanced by the insurance company and the government that foreclosing relief was

inconsistent with the basic purpose of the statutory scheme providing for enforcement of the terms of ERISA plans. Just as the Securities Act and Exchange Act in the instant case are intended generally to provide redress and recovery from violators, the Court countered that "vague notions of a statute's 'basic purpose' are nonetheless inadequate to overcome the words of its text regarding the *specific* issue under consideration." *Id.* at 220. Adhering to the same constitutional respect for legislative prerogatives and strict construction as it exhibited earlier in *Central Bank of Denver*, the Court concluded that it would "not attempt to adjust the 'carefully crafted and detailed enforcement scheme' embodied in the text that Congress has adopted." *Id.* at 221.

Since the statutory reference to "equitable relief" only permits "those categories of relief that were *typically* available in equity," the Court held that § 502(a)(3) did not authorize the claim: "Respecting Congress's choice to limit the relief available under § 502(a)(3) to "equitable relief" requires us to recognize the difference between legal and equitable forms of restitution. Because petitioners seek only the former, their suit is not authorized by § 502(a)(3)." *Id.* at 218. The lower courts have recognized the continuing vitality of the *Great-West* holding in subsequent cases, the Fifth Circuit recently reiterating that the threshold "requirement that the res be traceable" to characterize a claim for restitution or damages as equitable "is still very much intact." *Cent. States, Se. & Sw. Areas Health & Welfare Fund ex rel. Bunte v. Health Special Risk, Inc.*, 756 F.3d 356, 366 (5th Cir. 2014). The court in that case

dismissed an action under § 502(a)(3) as legal and not equitable because there was no "specifically identified . . . particular fund distinct from [Defendants'] general assets." *Id.* A specified res is the threshold requirement for such an exercise of equitable power.

The similar grant of remedial authority afforded by the Exchange Act—§ 21(d)(5)—is even more narrowly drawn than ERISA's § 502(a)(3) "appropriate equitable relief," allowing the SEC to seek only "equitable relief that may be appropriate or necessary for the benefit of investors." Just as in *Great-West*, the SEC's disgorgement claim does not trace investor monies to a particular res or identifiable funds *in the violator's possession* for which the SEC can seek an equitable lien or constructive trust—it simply seeks a lump sum disgorgement judgment for the amount to be paid, often without regard to the profit made by the wrongdoer or the expenses paid by the wrongdoer in determining the amount of funds to be returned. Just as in *Great-West,* the SEC seeks to recover funds not necessarily in the defendant's possession (and in some cases, never even attributable to the defendant.) Just as in *Great-West*, the SEC here has not, and cannot, even identify "particular funds or property in the [Petitioners'] possession" which actually belong to the SEC or, for that matter, to any injured investors. Instead, the SEC's disgorgement claim seeks a sum of money upon which to "impose personal liability on the defendant," a factor which alone disqualifies the remedy as one in equity under *Great-West*.

E. *Kokesh* Confirms that "Disgorgement" is a Penalty, Not an Equitable Remedy

The long-held understanding about the purpose of disgorgement in SEC cases—intended not to benefit the investors but to punish the violator—recently led the Court to rule that disgorgement is a *penalty*. As Petitioners correctly argue, the Court in *Kokesh v. SEC* determined that disgorgement, as sought by the SEC, is subject to the penalty-sanction 5-year statute of limitations, because in the context of SEC enforcement actions disgorgement constitutes an "action, suit or proceeding for the enforcement of a civil fine, penalty, or forfeiture, pecuniary or otherwise," as opposed to the equitable remedy the SEC had always claimed it was. 137 S. Ct. 1635, 1639 (2017).

The *Kokesh* Court began its analysis by evaluating whether disgorgement as sought by the SEC was punitive in nature, concluding categorically that SEC disgorgement is a remedy for breaking public laws against the United States—not for specifically harming an individual. *Id.* at 1643. "When the SEC seeks disgorgement, it acts in the public interest, to remedy harm to the public at large, rather than standing in the shoes of particular injured parties." *Id.* The Court then noted that because the SEC focuses on the deterrent nature of disgorgement, it employs disgorgement as a penalty. *Id.* Finally, the *Kokesh* Court determined that the remedy of disgorgement was punitive because, as sought and implemented by the SEC, disgorgement is not compensatory—the profits are paid to the govern-

ment, not necessarily returned to the aggrieved investors. *Id.*[14]

Further, in response to the SEC's argument that its use of disgorgement is "remedial" rather than "punitive," the Court noted that the SEC's longstanding use of the remedy is without regard to the effect on the wrongdoer—often the SEC seeks disgorgement of "not only the unlawful gains that accrue to the wrongdoer directly, but also the benefit that accrues to third parties whose gains can be attributed to the wrongdoer's conduct." *Id.* at 1644–45.[15] Further, the *Kokesh* Court noted that the SEC sometimes moves for disgorgement without regard to the actual expenses of the wrongdoer—that is, the SEC seeks entitlement to a disgorgement amount exceeding the wrongdoer's actual profit. *Id.* at 1645.[16]

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[14] The Court also described frequent scenarios where disgorgement awards obtained by the SEC went necessarily to the United States Treasury because "no party before the court was entitled to the funds and … the persons who might have equitable claims were too dispersed for feasible identification and payment." *Kokesh, supra,* at 1644.

[15] Examples include instances where insider trading defendants have been ordered to "disgorge" the profits of the parties to whom they provided the information—even though they did not profit from the transaction. *Kokesh, supra,* at 1644-45. (citing *SEC v. Contorinis*, 743 F.3d 296, 302 (2d Cir. 2014); *SEC v. Warde*, 151 F.3d 42, 49 (2d Cir. 1998); *SEC v. Clark*, 915 F.2d 439, 454 (9th Cir. 1990)).

[16] Despite the agency's expansive view, in many courts disgorgement was limited to illegally-derived "profits" that the SEC could forensically prove. *See, e.g., SEC v. ETS Payphones, Inc.*, 408 F.3d 727, 735 (11th Cir. 2005) ("the power to order disgorgement extends only to the amount with interest by

Because the ultimate issue was not briefed by the parties, the *Kokesh* Court expressly reserved for another day the seemingly obvious conclusion that what it termed "SEC disgorgement" could not be imposed at all.[17] But *Kokesh* necessarily dictates that the remedy of disgorgement as employed in SEC enforcement actions is a *legal* remedy in the form of a civil penalty, a conclusion reached by some courts well in advance of *Kokesh* and necessarily overruling *sub silentio* circuit court opinions to the contrary.[18] *See Horvath v. Keystone Health Plan E., Inc.*, 333 F.3d 450, 457 n.3 (3d Cir. 2003) (disgorgement likely a remedy at law because "there are no funds readily traceable to [the plaintiff] over which a constructive trust or other equitable remedy may be imposed"); *Edmonson v. Lincoln Nat. Life Ins. Co.*, 777 F. Supp. 2d 869, 891 (E.D. Penn. 2011) ("disgorgement is a legal remedy where the plaintiff cannot assert title or right to possessing particular property"). The very nature of disgorgement in SEC enforcement cases is legal, as the SEC seeks *in personam* liability for monetary payment. Indeed, in the very first case to

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which the defendant profited from his wrongdoing"); *SEC v. Amerifirst Funding, Inc.*, No. 3:07-CV-1188-D, 2008 WL 1959843, at *2 (N.D. Tex. May 5, 2008) (disgorgement represents "the amount of profits connected to the violation").

[17] The Court reserved the issues "whether courts possess authority to order disgorgement in SEC enforcement proceedings or on whether courts have properly applied disgorgement principles in this context." 137 S. Ct. at 1642 n.3.

[18] *See e.g.*, *SEC v. Halek*, 537 F. App'x 576 (5th Cir. 2013) (disgorgement is equitable); *SEC v. Seghers*, 298 F. App'x. 319, 336 (5th Cir. 2008) (same).

impose disgorgement in 1970, under the premise of common law "ancillary" authority, the circuit court embraced this expansion of remedial power only "so long as such relief is remedial relief and is not a penalty assessment." *Texas Gulf Sulphur, supra,* 446 F.2d at 1308.

The *Kokesh* Court held that SEC's disgorgement claims are not remedial or compensatory, and are instead simply damages in the form of a penalty, not traced to specific property or the rightful ownership of individual investors. The *Great-West* Court held that claims for damages to hold an individual personally liable, or not traceable to identified assets in the possession of wrongdoers, are legal claims and cannot be pursued under the rubric of a statutory grant of equitable claims authority. *Central Bank of Denver* established the supremacy of express statutory language in defining available remedies, precluding claims not clearly authorized by Congress.

As reflected in that case, it makes no difference that claims like disgorgement may be "settled law" with a "long pedigree."[19] So was "aiding-and-abetting" liability, "an important part of the SEC's enforcement arsenal," until the Court applied the terms of the statute and took it away.

The judicial imposition of remedies excluded by Congress from comprehensive statutory enforcement

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[19] Indeed, the invalidity of statutory "SEC disgorgement" as compelled by the *Kokesh/Great-West/Central Bank of Denver* trilogy appears to be a question of first impression.

schemes is not consistent with the requirements of due process, respect for the separation of powers, the terms of the applicable statutes, or the constitutional limitations on the reach of Article III authority. In its common form, the penalty of disgorgement also flouts the legislative penalty caps crafted by Congress in §§ 77t(d) and 78u(d)(3)(B); routinely obtaining judgments for both statutorily-authorized penalties *and* for the judicially-created penalty of disgorgement effectively allows the SEC and the courts to evade those caps altogether by "double-dipping."[20]

If Congress wishes to vest the SEC with authority to seek some form of disgorgement as a legal remedy—and the courts with power to impose it—the Congress is free to do so, in clear and express terms, as the Court now clearly demands. But in the absence of legislative action and under the controlling authority of *Kokesh*, *Great-West* and *Central Bank of Denver*, the SEC is vested with no

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[20] Pursuant to the parallel penalty schemes in 15 U.S.C. §§ 77t(d) and 78u(d)(3)(B), the district court may impose a penalty on individual defendants such as Petitioners up to $5,000, $50,000, or $100,000 under the first, second and third penalty tiers respectively, or "the gross amount of pecuniary gain to such defendant as a result of the violation," and no more. But under the current disgorgement regime as implemented in all the circuits, defendants can be penalized for the full "amount of pecuniary gain" as authorized by Congress and then simultaneously penalized *again* under the rubric of "disgorgement" for the same "amount of pecuniary gain," and often for additional amounts, depending on the circuit. Obviously, this renders meaningless the statutory penalty limits chosen by the legislative branch and underscores that the statutory remedies scheme was intended by Congress to be exclusive.

statutory authority to seek disgorgement against Petitioners and the district court was without the power to impose any amount of disgorgement in this case.

CONCLUSION

The Court should hold that disgorgement is not an allowed remedy in SEC enforcement actions and accordingly reverse the judgment of the Court of Appeals for the Ninth Circuit.

Respectfully Submitted,

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