No. 18-1501

IN THE
# Supreme Court of the United States

CHARLES C. LIU, ET AL., *Petitioners,*

v.

SECURITIES AND EXCHANGE COMMISSION, *Respondent*.

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

**BRIEF OF SECURITIES LAW PROFESSORS AS *AMICI CURIAE* IN SUPPORT OF RESPONDENT**

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## INTEREST OF *AMICI CURIAE*[1]

*Amici* are scholars at American law schools whose research and teaching focus on federal securities regulation. Amici have no financial stake in the outcome of this litigation but are interested in federal courts retaining their historical ability to order disgorgement as an equitable remedy in appropriate cases, particularly in enforcement actions instituted by the Securities and Exchange Commission (the SEC or Commission). A full list of amici, who joined this brief as individuals and not representatives of any institutions with which they are affiliated, is set forth in the Appendix to this brief.

## SUMMARY OF ARGUMENT

Federal district courts have inherent powers to impose ancillary equitable remedies in properly instituted federal agency enforcement actions, and disgorgement has long been regarded as an equitable remedy. The fact that this Court has categorized disgorgement as a penalty for a statute of limitations purpose does not remove the disgorgement remedy from its traditional equitable realm.

Moreover, this Court need not look solely to the inherent equitable powers of federal courts to determine whether district courts, in enforcement actions by the SEC, may order the disgorgement of ill-gotten gains acquired through a violation of the

[1] The parties have consented to the filing of this brief. No counsel for any party authored this brief in whole or in part, and no person other than amici or its counsel made a monetary contribution to the preparation or submission of this brief.

federal securities laws. Nearly two decades ago, Congress amended the Securities Exchange Act of 1934 to add an express provision authorizing the SEC to seek, and federal courts to grant, "any equitable relief that may be appropriate or necessary for the benefit of investors." Exchange Act § 21(d)(5); 15 USC 78u(d)(5).

The statutory text of multiple disgorgement-related provisions in the federal securities laws and the voluminous legislative record from decades of lawmaking leave no doubt that Congress has legislated based on the understanding that district courts have the authority to order disgorgement as one form of equitable relief in SEC enforcement actions. And because the availability of court-ordered disgorgement is one of the blocks at the foundation of what has become an increasingly tall tower of congressionally authorized express securities law remedies, a decision by this Court to remove that block would frustrate the workings of everything built on top of it.

Finally, a decision by this Court to prohibit district courts from ordering disgorgement in SEC enforcement actions would allow fraudsters to retain stolen funds, and thus weaken the SEC's efforts to secure fair and efficient capital markets and to compensate victims of securities law violations.

## ARGUMENT

### I. DISTRICT COURTS HAVE INHERENT AUTHORITY TO ORDER EQUITABLE REMEDIES, INCLUDING DISGORGEMENT, IN PROPERLY INSTITUTED AGENCY ENFORCEMENT ACTIONS

Petitioners seek to reverse a longstanding presumption that district courts in federal agency enforcement actions may order appropriate ancillary equitable relief, including disgorgement, unless Congress has explicitly revoked that authority. If petitioners' position is accepted, this radical about-face would thwart the effective enforcement of federal law in countless areas. As petitioners recognize, the SEC is only one of many federal agencies operating under "[n]early 100 statutes [that] allow courts to fashion relief through their equitable powers." Pet. for Writ of Certiorari 20–21 (citation omitted). *See, e.g.*, *California v. Am. Stores Co.*, 495 U.S. 271, 279-80 (1990) (courts have equitable authority to order divestitures under an antitrust statute permitting the government to "institute proceedings in equity to prevent and restrain [antitrust] violations" through petitions "praying that such violation shall be enjoined or otherwise prohibited"). Petitioners' untenable claim that the holding in *Kokesh v. SEC*, 137 S. Ct. 1635 (2017), renders disgorgement for all purposes as something other than an equitable remedy is likewise far reaching and would impose sweeping new restrictions on federal courts' authority.

### A. Federal Courts' Equitable Powers Are Particularly Broad and Flexible When the Public Interest in the Enforcement of Federal Law is Involved

Federal courts of original jurisdiction are charged with overseeing "all suits of a civil nature at common law or in equity," unless Congress has specified otherwise. Judiciary Act of 1789, § 11, 1 Stat. 73, 78; *see also* U.S. Constitution Art. III, §§ 1, 2 (vesting "judicial power of the United States" in a Supreme Court and "such inferior Courts as the Congress may from time to time ordain" for "all Cases, in Law and Equity"). In statutes administered by federal agencies, Congress frequently includes jurisdictional language echoing these broad grants of equitable jurisdiction, *see infra* at 14 (quoting provisions in the four principal federal securities acts), and at times expressly authorizes courts to grant "equitable relief," *see infra* at 17 (quoting § 21(d)(5) of the Exchange Act, 15 USC 78u(d)(5)). But even absent such language, the background presumption is that Congress intends district courts to exercise their inherent equitable authority when overseeing agency enforcement actions. *Porter v. Warner Holding Co.*, 328 U.S. 395, 398–402 (1946).

A court's authority to order ancillary equitable remedies in government enforcement actions is particularly important because although agency efforts often benefit victims of a wrongdoer's illegal conduct, agencies' mandates are broader than simply vindicating those individuals' interests (who often can and do bring suit on their own behalves). *See, e.g.*, *Gen. Tel. Co. v. EEOC*, 446 U.S. 318, 326 & n.8 (1980) ("When the EEOC acts, albeit at the behest of and for the benefit of specific individuals, it also acts to vindicate the public interest in preventing employment discrimination.") (citing *Porter*, 328 U.S. at 397–98). Violators' conduct can also inflict diffuse harm such that victims may be difficult to identify, but violations of federal law harm the public interest in and of themselves, even if that harm is hard to quantify or to allocate.

This Court has thus long held, as forcefully articulated in *Porter*, that, absent clear instruction from Congress, courts in properly instituted agency enforcement actions may draw upon equitable remedies to redress proven violations. At issue in *Porter* was "the power of a federal court, in an enforcement proceeding under section 205(a) of the Emergency Price Control Act of 1942, to order restitution of [excessive] rents collected by a landlord." *Porter*, 328 U.S. at 396. The Act permitted the government to seek from an "appropriate court" a "permanent or temporary injunction, restraining order, or other order"—language which the defendant argued was insufficient to confer on the court "jurisdiction under the statute to order restitution." *Id.* at 397.

The Court disagreed, noting that "[i]t is readily apparent … that a decree compelling one to disgorge profits, rents or property acquired in violation of the [law] may properly be entered by a District Court once its equity jurisdiction has been invoked under § 205(a)." *Id.* at 398–99. Notably, the majority and the dissent agreed on the baseline presumption that:

> Unless otherwise provided by statute, all the inherent equitable powers of the District Court are

> available for the proper and complete exercise of that jurisdiction. *And since the public interest is involved in a proceeding of this nature, those equitable powers assume an even broader and more flexible character than when only a private controversy is at stake.*

*Id.* at 398 (emphasis added) (citation omitted); *see also id.* at 408 (Rutledge, J., dissenting) ("When Congress is silent in formulating remedies for rights which it has created, courts of equity are free to use these creative resources.").

The *Porter* Court divided over whether the Emergency Price Control Act specifically prohibited a district court from exercising its inherent authority to order the most appropriate equitable remedy. Although the dissent maintained that equitable restitution to victims was impermissible because Congress had already provided private plaintiffs with a right of action under a different provision—§ 205(e), *see id.* at 405-06 (Rutledge, J., dissenting), the Court concluded otherwise, refusing to draw such a speculative inference, *id.* at 398.

As the Court explained, "either of two theories" justified its holding that courts retain implied authority to order equitable restitution, even under an elaborately constructed remedial scheme. *Id.* at 399. First, the Court read the catch-all phrase of "other order" as an invocation of courts' equitable authority, and restitution was clearly "an equitable adjunct to an injunction decree." *Id.* Second, an order that clawed back ill-gotten gains and disbursed them to victims was "appropriate and necessary to enforce compliance with the Act." *Id.* at 400. After all, "[f]uture compliance may be more definitely assured if one is compelled to restore one's illegal gains," *id.,* and it is "within the highest tradition of a court of equity" to "act in the public interest by restoring the status quo," *id.* at 402.

The *Porter* Court thus already *rejected* arguments raised by petitioners in the present case. It declined to hold that courts' equitable authority in a properly instituted enforcement action could be implicitly revoked because Congress provided for an analogous remedy elsewhere in the statute (let alone in statutes administered by other federal agencies). *See id.* at 398–99. And it refused to accept the dissent's view that the Act's ample "[l]egal, equitable and criminal sanctions"—the government's "powerful battery of weapons"—implicitly barred the district court from "reinforc[ing] with armor not provided in the Act." *Id.* at 404–05 (Rutledge, J., dissenting). Moreover, *neither* the dissent nor the majority took issue with equitable authority extending to disgorgement orders in general—only whether the government could take any recovered money "and give it to persons whose right to recover it the Act has cut off." *Id.* at 407–08 (Rutledge, J., dissenting).

Petitioners try to distinguish *Porter*. They contend that the statutory language at issue authorized both injunctive relief as well as "any 'other order,'" and it was "[t]hat explicit language [that] was the *Porter* Court's basis" for concluding the District Court could exercise its "equitable discretion." Pet. Br. 34. But petitioners fail to address the multiple rationales for *Porter*'s holding and provide no basis for reading the vague phrase "other orders" as authorizing equitable restitution, while construing the federal securities laws' multiple references specifically to "equity" and "equitable relief" as *prohibiting* a district court from ordering equitable disgorgement.

Petitioners' strained reading of *Porter* mirrors the one that this Court rejected in *Mitchell v. Robert De Mario Jewelry, Inc.*, 361 U.S. 288, 291–92 (1960) (concluding that *Porter* was not to be distinguished based on finding in some "language of the statute affirmative confirmation of the power to order reimbursement," because in crafting regulatory frameworks "Congress … must be taken to have acted cognizant of the historic power of equity to provide complete relief in the light of statutory purposes"). As in *Porter*, the *Mitchell* majority and dissent disagreed over statutory construction, and once again, the Court refused to construe the statute narrowly, recognizing a district court's equitable jurisdiction in a Fair Labor Standards Act case to "order reimbursement for loss of wages caused by an unlawful discharge or other discrimination." *Id.* at 289.

This Court recently relied on *Porter* when acting as a court of original jurisdiction in adjudicating two states' dispute regarding a water rights compact with the force of federal law. *Kansas v. Nebraska*, 135 S. Ct. 1042, 1051–53 (2015). In *Kansas*, the parties agreed that Nebraska violated the law, which "resulted in a $3.7 million loss to Kansas; and Nebraska ha[d] agreed to pay those damages." *Id.* at 1053. The parties disagreed, however, as to "whether Nebraska's conduct warrant[ed] additional relief," such as "an additional monetary award." *Id.* at 1056. The majority accepted the Special Master's recommendation that Nebraska be subject to partial disgorgement because "Nebraska's reward" for its violation "was 'much larger than Kansas' loss, likely by more than several multiples.'" *Id.* at 1056.

Importantly, the *Kansas* Court was unanimous in concluding that it had equitable authority to order disgorgement, with the dissent from the disgorgement order disagreeing only with respect to its appropriateness for the case.[2] These opinions are therefore fatal to petitioners' claim that "[d]isgorgement was never part of the historical understanding of equity." Pet. Br. 27.

As the majority explained, the Court's non-compensatory disgorgement order was within "its full authority to remedy violations of and promote compliance with the agreement, so as to give complete effect to public law." *Id.* at 1053. This was particularly so because, "'[w]hen federal law is at issue and 'the public interest is involved,' a federal court's 'equitable powers assume an even broader and more flexible character than when only a private controversy is at stake.'" *Id.*, quoting *Porter*, 328 U.S. at 398. The Court therefore had the authority to order disgorgement given its "broad remedial powers" when "such cases

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[2] *See id.* at 1057 (describing the "disgorgement order [as] a 'fair and equitable' remedy"); *id.* at 1064 (Roberts, C.J., concurring in part and dissenting in part) (joining majority in ordering disgorgement pursuant to the Court's "equitable power"); *id.* at 1070 (Thomas, J., joined by Scalia, J., and Alito, J., concurring in part and dissenting in part) ("Disgorgement is strong medicine, and as with other forms of equitable power, we should impose it against the States 'only sparingly.'") (quoting Missouri v. Jenkins, 515 U.S. 70, 131 (1995)).

involve not private parties' private quarrels, but States' clashes over federal law." *Id.* at 1056.[3] It also described *Porter* as standing for the exercise of "equitable power to *disgorge* profits gained from violating a federal statute." *Id.* at 1057 (emphasis added); *see also id.* at 1062-63 (stating that "our equitable authority to grant remedies is at its apex when public rights and obligations are thus implicated") (citing *Porter*, 328 U.S. at 398).

Although the dissent endorsed the majority's description of equitable disgorgement authority, it distinguished its precedent because the states' dispute was "not the same as the flexibility *Porter* claimed for courts engaged in supervising the administration of a federal regulatory program." *Id.* at 1067 (Thomas, J., concurring in part and dissenting in part). The dissent also acknowledged that "the involvement of 'public interests' might augment the Court's equitable powers in the context of disputes involving regulated parties and their regulators," *id.*—the very situation at issue in petitioners' case.

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[3] Petitioners rely on a series of cases that fit into the category the *Kansas* Court distinguished here: litigation involving private disputes between private parties. For example, petitioners repeatedly cite *Great-West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204 (2002)—a case in which the Court gave a narrow construction of the term "equitable relief" in the ERISA. Even further afield is petitioners' reliance on cases like *Alexander v. Sandoval*, 532 U.S. 275 (2001), that deal with implied private rights of action (not available remedies)—a situation clearly not at issue in the present matter.

With its broad equitable authority in mind, the *Kansas* Court explained that "actual damages" would be "inadequate" because they could incentivize a violator's conduct "as long as it [wa]s willing to pay that amount" of damages." *Id.* at 1057 (internal quotation omitted). "[D]isgorgement of gains" was thus "needed" because it "appropriately reminds [the violator] of its legal obligations, *deters future violations*, and promotes the [law's] successful administration." *Id.*, citing *Porter*, 328 U.S. at 400 (emphasis added). The Court concluded, however, that "disgorgement need not be all or nothing." *Id.* at 1058. Rather, "flexibility [is] inherent in equitable remedies" and should be "award[ed] … with reference to the facts of the particular case." *Id.* (internal quotations omitted).

### B. Disgorgement is an Equitable Remedy, Even in Instances When it Constitutes a Penalty Under the *Kokesh* Criteria

Petitioners only feebly attempt to distinguish this line of cases, failing to even mention *Kansas*. Instead they argue that this Court classified SEC disgorgement as a penalty and thus the terms "equity" and "equitable" in the federal securities laws must be read to *prohibit* court-ordered disgorgement. Petitioners' support for disregarding nearly a century of case law is *Kokesh*, a decision narrowly holding that SEC disgorgement constitutes a "penalty" for statute of limitations purposes. 137 S. Ct. at 1642 n.3. It was that holding in *Kokesh* that led petitioners to the following faulty syllogism: (1) penalties are not available in equity; (2) disgorgement in SEC enforcement actions is a penalty; thus (3) for all intents and purposes, SEC disgorgement is a penalty and cannot serve as an equitable remedy.

For a syllogism to be useful, however, the meaning of its elements cannot vary depending on context. But, as this Court has explained, "'[p]enalty' is a term of varying and uncertain meaning." *Life & Cas. Ins. Co. v. McCray*, 291 U.S. 566, 574 (1934). Thus, depending on context, a remedy sought primarily to punish can be treated differently from a remedy sought as equitable relief in an agency enforcement action. That same remedy can be treated as a penalty for some purposes but not for others. This is true even if experiencing the remedy feels like a "penalty" and operates as a deterrent to the defendant and third-parties.[4]

The decision in *Kansas v. Nebraska*, 135 S. Ct. 1042 (2015), provides a recent illustration that

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[4] Whether Congress or courts are within their constitutional bounds when permitting or ordering remedies they deem equitable is not a question currently before this Court, and would benefit from a more adequate exploration than is available in this litigation. *See* Theresa A. Gabaldon, *Equity, Punishment, and the Company You Keep: Discerning a Disgorgement Remedy under the Federal Securities Laws*, 105 Cornell L. Rev. __ (forthcoming 2020), at https://ssrn.com/abstract=3441432 (differentiating the question of whether a remedy is equitable for constitutional purposes—in particular the jury-trial right under the Seventh Amendment). *Cf. Lebron v. National R.R. Passenger Corp.*, 513 U.S. 374, 392 (1995) (Congress can designate a corporation as a non-governmental entity "for purposes of matters that are within Congress's control," while that same entity may be considered a governmental entity "for purposes of determining the constitutional rights of citizens affected by its actions.").

disgorgement can be an equitable remedy even if a defendant is "penalized" when ordered to disgorge ill-gotten gains from a violation of federal law. As one of the *amici* has written, "the equitable disgorgement that was ordered in *Kansas,*" in the words of *Kokesh*, "'bears all the hallmarks of a penalty: It [was] imposed as a consequence of violating a public law and [was] intended to deter, not to compensate.'" Donna M. Nagy, *The Statutory Authority for Court-Ordered Disgorgement in SEC Enforcement Actions*, 71 SMU L. Rev. 895, 925 (2018) (quoting *Kokesh*, 135 S.Ct. at 1644). *Cf. Tull v. United States*, 481 U.S. 412, 424 (1987) (describing disgorgement as a "limited form of penalty" while at the same time observing that "disgorgement of improper profits [is] traditionally considered an equitable remedy").

## II. CONGRESS HAS LEGISLATED BASED ON THE UNDERSTANDING THAT COURTS WILL USE THEIR EQUITABLE POWERS TO GRANT APPROPRIATE SEC REQUESTS FOR DISGORGEMENT

Petitioners may be correct in observing that Congress "'deliberately omitted'" an express remedy of court-ordered disgorgement from the federal securities laws, Pet. Br. 15 (quoting *Massachusetts Mut. Life Ins. Co. v. Russell*, 473 U.S. 134, 147 (1985)), but there is a simple explanation for the omission that undercuts their assumption that Congress "'did *not* intend to authorize'" that remedy. *Id.* Namely, Congress viewed the explicit authorization of court-ordered disgorgement as unnecessary because, at least from 1983 onwards, Congress took it as a given that district courts could and would use their statutorily authorized equitable powers, in properly instituted SEC enforcement actions, to grant appropriate requests for the disgorgement of a securities law violator's ill-gotten gains.

### A. Congress Has Crafted a Comprehensive Statutory Scheme Containing SEC "Enforcement Tools" Predicated on the Availability of Court-Ordered Disgorgement as an Equitable Remedy

The ability to seek equitable relief from a district court in a properly instituted enforcement action is one of the SEC's oldest "enforcement tools." *Kokesh*, 137 S.Ct. at 1640. Indeed, in each of the four principal securities acts, Congress included a provision that explicitly grants district courts jurisdiction over "all suits in equity and actions at law brought to enforce any liability or duty created by" the act. § 22(a) of the Securities Act of 1933 (the Securities Act), 15 U.S.C. 77v(a); § 27(a) of the Securities Exchange Act of 1934 (the Exchange Act), 15 U.S.C. 78aa(a); § 44 of the Investment Company Act of 1940 (the Inv. Company Act), 15 U.S.C. 80a-43; and § 214(a) of the Investment Advisers Act of 1940 (the Inv. Advisers Act), 15 U.S.C. 80b-14(a).

Traditionally and still typically, the SEC institutes enforcement actions in district courts pursuant to its authority to seek permanent or temporary injunctions, or restraining orders, "[w]henever it shall appear to the Commission that any person is engaged or is about to engage" in a securities law violation. *See, e.g.*, § 20(b) of the Securities Act, 15 U.S.C. 77t(b) (with analogues in the Exchange Act, Inv. Company Act, and Inv. Advisers Act). But beginning in 1984 for insider trading cases, and after 1990 for other securities law violations, the SEC may also (or alternatively) initiate enforcement actions in district courts to seek civil monetary penalties. *See* Exchange Act § 21A(a), 15 U.S.C. 78u-1(a) (insider trading violations) and § 21(d)(3), 15 U.S.C. 78u(d)(3) (other violations) (with analogues in the Securities Act, Inv. Company Act, and Inv. Advisers Act). In addition, since 1975, Exchange Act § 21(e), 15 U.S.C. 78u(e), has authorized the SEC to apply to district courts for "writs of mandamus, injunctions, and orders commanding [ ] any person to comply with" any Exchange Act provision, rule, or regulation.

Once the SEC properly institutes an enforcement action in a district court and proves a violation of the federal securities laws, it can seek a host of enforcement remedies, including ancillary equitable relief that orders a securities law violator to disgorge any ill-gotten gains.

### *1. This Court Has Recognized That District Courts May Use Their Inherent Equitable Powers to Order Ancillary Relief in Federal Securities Cases, and Every Circuit Has Held that Such Powers Extend to Court-Ordered SEC Disgorgement*

This Court in *Deckert v. Indep. Shares Corp.*, 311 U.S. 282 (1940), recognized the power of a district court to order ancillary equitable relief in a federal securities case within its jurisdiction. *See id.* at 288 (quoting the reference in Securities Act § 22(a), 15 U.S.C. 77v(a), to "all suits in equity and actions at law brought to *enforce* any liability" and emphasizing that the "power to *enforce* implies the power to make effective the right of recovery afforded by the Act").

*Deckert* involved private plaintiffs seeking rescission and restitution pursuant to the express right of action in what is now § 12(a)(2) of the Securities Act, 15 U.S.C. 77l(a)(2). But this Court nonetheless held that the plaintiffs' claims also "state[d] a cause for equitable relief" in the form of a temporary injunction and an appointment of a receiver. *Deckert,* 311 U.S. at 288.

Years later, in an SEC enforcement action seeking an injunction, the Ninth Circuit cited *Deckert* and concluded that the agency had "similar rights as a litigant" to seek the appointment of a receiver based on "the broad equitable powers of the federal courts" to order ancillary relief. *Los Angeles Trust Deed & Mortg. Exch. v. SEC*, 285 F.2d 162, 181 (9th Cir. 1960) (citing as well as this Court's ancillary equity relief holdings in *Porter* and *Mitchell*). *See* Roberta S. Karmel, "*Will Fifty Years of the SEC's Disgorgement Remedy Be Abolished*," 71 SMU L. Rev. 799, 800 (2018) (citing other lower court decisions upholding "the appointment of a receiver as an appropriate exercise of a court's equity power").

As this Court recognized in *Kokesh*, court-ordered disgorgement of a securities law violator's ill-gotten gains became a standard ancillary remedy sought by the SEC in most enforcement actions subsequent to the decision in *Texas Gulf Sulphur*. *See Kokesh*, 137 S.Ct. at 1640; *SEC v. Texas Gulf Sulphur*, 446 F.2d 1301, 1307-08 (2d Cir. 1971) (finding "little doubt that § 27 of the [Exchange] Act confers general equity power upon the district courts" and describing disgorgement "as an ancillary remedy in the exercise of the courts' general equity powers to afford complete relief") (citing decisions including *Porter* and

*Mitchell*). Every circuit court has since consistently upheld disgorgement as a valid exercise of a district court's equitable power. *See* Resp. Br. 12-13 (citing cases).

### 2. *Exchange Act § 21(d)(5)'s Explicit Authorization of "Equitable Relief" Confirms the Broad Scope of Courts' Equitable Powers*

Beginning in 2002, district courts no longer had to rely solely on their inherent powers to grant equitable relief in SEC enforcement actions. Instead, these courts can now look to the express provision in § 21(d)(5) of the Exchange Act, which Congress enacted as part of the Sarbanes-Oxley Act, Pub. L. No. 107-204, 116 Stat. 745, in the wake of the Enron and WorldCom scandals. Section 21(d)(5) provides in full:

> Equitable Relief.—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.

15 U.S.C. 78u(d)(5).

Petitioners incorrectly assume that this provision imposes a silent "condition" requiring such equitable relief to be used as restitution for injured investors. Pet. Br. 30 n.14. But Congress did no such thing. Section 21(d)(5) plainly authorizes remedies that can be used as compensation for investors, but it is hardly limited to restitutionary relief. Indeed, all securities law enforcement remedies—including disgorgement that is paid to the Treasury—ensue to "the benefit of investors," as the statute commands. *See Kokesh*, 137 S. Ct. at 1643 (observing that disgorgement deters future securities law violations and thereby "'further[s] the Commission's *public policy mission of protecting investors and safeguarding the integrity of the markets*'") (internal quotation omitted) (emphasis added); S. Rep. 107-205, at 27 (2002) (observing that § 21(d)(5) authorizes "any equitable relief necessary or appropriate to protect, and mitigate harm to, investors").

### B. Congress Repeatedly Has Ratified, and in Several Instances Expressly Codified, the Equitable Remedy of Court-Ordered SEC Disgorgement

Petitioners perceive "congressional silence," Pet. Br. 39, only because they ignore numerous occasions, over the span of more than 35 years, when Congress ratified, and in several instances expressly codified, court-ordered disgorgement as a securities law enforcement remedy. Depicting such codification as merely "scattered references to 'disgorgement' in the U.S. Code," Pet. Br. 14, overlooks the forest for the trees. Each textual reference to court-ordered disgorgement—in one Securities Act provision, three Exchange Act provisions, and in a twice-enacted "Fair Funds" provision of the U.S. Code—was part of a broader congressional effort to enhance securities law enforcement, and each reflects the congressional understanding that court-ordered disgorgement, as a type of equitable relief, is a statutorily authorized remedy. *See* Nagy, *supra*, at 903-19. In addition to the multiple references to court-ordered disgorgement in the text of the federal securities laws, several

Congressional Committee Reports contain extensive evidence of disgorgement's congressional ratification.

#### *1. Evidence from the 1980s—ITSA and ITSFEA*

Congress's first statutory reference to court-ordered SEC disgorgement appeared in the Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, 120 Stat. 4677. ITSFEA augmented the civil monetary penalty provision in the Insider Trading Sanctions Act of 1984 (ITSA), Pub. L. No. 98-376, 98 Stat. 1264, which authorized the SEC to seek, and federal courts to order, the payment of up to three times the profit gained or loss avoided by a person found liable for illegal insider trading or tipping.[5] ITSFEA also added a new § 20A to the Exchange Act, which provides an express private right of action for investors who traded contemporaneously with such unlawful traders or tippers, and includes subsection (b)(2) that reads:

> Offsetting *Disgorgements* Against Liability.—The total amount of damages imposed against any person [found liable for illegal tipping or trading] shall be diminished by the amounts, if any, that such person *may be required to disgorge, pursuant to a court order obtained at the instance of the Commission*, in a proceeding brought under § 21(d) of [the Exchange Act] relating to the same transaction or transactions.

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[5] ITSA's civil penalty provision initially was codified as Exchange Act § 21(d(2), but ITSFEA amended the provision and shifted it to Section 21A of the Exchange Act, 15 U.S.C. 78u-1.

15 U.S.C. 78t-1(b)(2) (emphasis added). Congress's inclusion of the term "disgorgement" in a subsection caption, and its reference to "amounts … disgorge[d] pursuant to a court order," constitute codification; such textual references can hardly be explained away as a noncommittal acknowledgment "that some courts were entering disgorgement orders." Pet. Br. 37.

The Report of the House Committee on Energy and Commerce that accompanied ITSFEA likewise negates petitioners' unfounded claims of congressional agnosticism. The ITSFEA Report is replete with references to the remedy of court-ordered disgorgement. *See* H.R. Rep. 100-910 (1988) at 11 (twice), 12 (four times), 20 n.16 (twice). Notably, the ITSFEA Report explains that the "civil penalty [in insider trading cases] was intended *to go beyond disgorgement of illegal profits to add the imposition of a significant fine* as a needed deterrent." *Id.* at 11 (emphasis added).

More than four years prior, the House Committee Report that accompanied ITSA mentioned disgorgement a total of eight times, H.R. Rep. 98-355 (1983) at 7 (three times), 8, 10, 11 (twice), 12. One such reference rooted the statutory source for court-ordered disgorgement in the jurisdictional provisions of the federal securities laws:

> Once the equity jurisdiction of a court has been invoked on a showing of a securities violation, the court possesses the necessary power to fashion an appropriate remedy. Thus, the Commission may request that the court order certain equitable relief, such as the disgorgement (giving up) of illegal profits.

H.R. Rep. 98-355 at 7.

The ITSA Report also emphasized the House Committee's conclusions that the then-existing insider trading remedies of an injunction and disgorgement amounted to an "insufficient deterrent," and that the new monetary penalty would result in greater deterrence because it would do more than "merely restore[ ] a defendant to his original position." *Id.* at 7. Specifically, a sanction of up to three times the illicit gain or loss avoided would extract "*a real penalty* for [an insider trading defendant's] illegal behavior." *Id.* (emphasis added). ITSA's text explicitly stated that such monetary penalty actions "may be brought in addition to any other actions that the Commission or the Attorney General are entitled to bring." ITSA § 2A (subsequently amended and codified at Exchange Act § 21A(d)(3), 15 U.S.C. 78u-1(d)(3), and captioned "Remedy Not Exclusive").

Most important for purposes of the issue before this Court, the ITSA Report underscores not only that civil monetary penalties were not intended to displace court-ordered disgorgement but also that courts "may" —as opposed to must—disburse such disgorged funds to victims harmed by illegal insider trading. As stated in the ITSA Report:

> The new penalty may be used *in addition to* existing remedies available to the Commission. Thus, in appropriate insider trading cases, the Commission may seek: (1) a court order enjoining the violator from breaking the law again; (2) *disgorgement of ill-gotten gains which may, if appropriate*, be paid into an escrow fund so that traders or other private parties damaged by the

> insider trading can obtain compensation for their losses; and (3) the imposition of the new civil money penalty payable to the U.S. Treasury.

H.R. Rep. 98-355 at 8 (emphasis added).

### 2. *Evidence from the 1990s—the Remedies Act and the PSLRA*

Congress's next statutory references to court-ordered disgorgement came in the Private Securities Litigation Reform Act of 1995, Pub. L. 104-67, 109 Stat. 737, which amended the federal securities laws to provide:

> Prohibition of Attorneys' Fees Paid From *Commission Disgorgement Funds*.—Except as otherwise ordered by the court upon motion by the Commission, or, in the case of an administrative action, as otherwise ordered by the Commission, *funds disgorged as the result of an action brought by the Commission in Federal court*, or as a result of any Commission administrative action, shall not be distributed as payment for attorneys' fees or expenses incurred by private parties seeking distribution of the disgorged funds.

PSLRA § 103(b) (codified at Securities Act § 20(f), 15 U.S.C. 77t(f); Exchange Act § 21(d)(4), 15 U.S.C. 78u(d)(4)) (emphasis added).

These PSLRA provisions not only constitute a second codification of court-ordered disgorgement as an available enforcement remedy. They also evidence congressional respect for a district court's equitable determinations. That is, although Congress as a general matter decided that funds disgorged by defendants in SEC enforcement actions should not be used to offset expenses incurred by private parties seeking a share of those proceeds, it nonetheless granted courts (and the SEC in administrative proceedings) the authority to trump that default principle when circumstances warrant.

The Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat. 931 (the Remedies Act), provides additional evidence that Congress regards court-ordered disgorgement as a statutorily authorized equitable remedy. Although not in the text of the Remedies Act itself, references to court-ordered disgorgement appear throughout the House and Senate Committee Reports accompanying the legislation. *See* H.R. Rep. 101-616 (1990) at 13, 17 (three times), 22, 31 (three times), 35; S. Rep. 101-337 at 6 (twice), 8 n.7, 9 (twice), 10 (five times), 13, 16. Several of these references explicitly categorize court-ordered disgorgement as "equitable" or "ancillary" relief. *See, e.g*. H.R. Rep. 101-616 at 31 (referencing "equitable relief, including disgorgement"); S. Rep. at 10 (referencing "ancillary relief (especially disgorgement of ill-gotten gains)"). Moreover, in discussing the Act's new authorization for the SEC to order "accounting and disgorgement" in administrative proceedings, both Committees observed that the SEC already had the authority to seek disgorgement relief in district court. *See* S. Rep. at 16; H.R. Rep. 101-616 at 35.

In justifying what was then the controversial decision to extend court-ordered monetary penalties to offenses beyond insider trading, the Reports also observed that the existing remedy of "disgorgement merely requires the return of wrongfully obtained profits" and does not impose any "meaningful" or "actual" economic penalty. *See* H.R. Rep. 101-616 at 17; S. Rep. at 10. Accordingly, both Committees concluded "that authority to seek or impose substantial monetary penalties, in addition to disgorgement of profits, is necessary for the deterrence of securities law violations that otherwise may provide great financial returns to the violator." H.R. Rep. 101-616 at 17; S. Rep. at 10. To that end, and at the SEC's suggestion, the text of the Remedies Act includes a provision specifying that its three-tiered civil penalty remedy is "not exclusive." *See* §§ 101 (codified at Securities Act § 20(d)(3)(C), 15 U.S.C. 77t(d)(3)(C), with analogues in the Exchange Act, Inv. Company Act, and Inv. Advisers Act).

A decision by this Court to prohibit district courts from ordering disgorgement in SEC enforcement actions would therefore frustrate the very workings of the express statutory remedies that Congress so carefully designed. For example, absent a court's entry of a disgorgement order, a securities law violator who is required under § 20(d)(2) of the Securities Act to pay a civil monetary penalty equal to the "gross amount of pecuniary gain to such defendant as a result of the violation" could satisfy such a judgment with ill-gotten profits. 15 U.S.C. § 77t(d)(2). That result is precisely the one that Congress sought to foreclose by expanding enforcement remedies—first in ITSA and ITSFEA and then in the Remedies Act—to provide for "real," "actual," and "meaningful" economic penalties that go beyond redress available through disgorgement.

### 3. *Evidence from 2002 to 2010—the Sarbanes-Oxley Act and the Dodd-Frank Act*

The text of the Sarbanes-Oxley Act's "Fair Funds" provision reveals yet another instance of court-ordered disgorgement's codification and adds to the quantum of evidence demonstrating Congress's intent for courts to order both civil penalties and equitable disgorgement relief in appropriate cases. The provision states:

> Civil Penalties Added to *Disgorgement Funds* for the Relief of Victims.—If in any *judicial* or administrative action brought by the Commission under the securities laws … the Commission *obtains an order requiring disgorgement against any person for a violation of such laws or the rules or regulations thereunder*, … and the Commission also obtains pursuant to such laws a civil penalty against such person, the amount of such civil penalty shall, on the motion or at the direction of the Commission, *be added to and become part of the disgorgement fund* for the benefit of the victims of such violation.

Sarbanes-Oxley Act § 308(a), codified at 15 U.S.C. § 7246 (emphasis added). Previously, civil penalties imposed in SEC enforcement actions could be paid only to the Treasury. *See supra* at 15 (citing civil penalty provisions). Petitioners' implausible contention that § 7246 is "best understood to reflect Congress's decision to authorize disgorgement in administrative proceedings, but not federal court actions," Pet. Br. 2, asks this Court to disregard its textual canon that every word in a statute should carry meaning. Moreover, in 2002, the SEC's authority to order civil penalties in administrative proceedings extended only to regulated entities and their associated persons. Thus, for § 7246 to have impacted victims of securities law violations more than marginally, court-ordered penalties had to be placed into court-ordered disgorgement funds.

The Senate Committee Report accompanying the Sarbanes-Oxley Act also referenced court-ordered disgorgement in its discussion of Exchange Act § 21(d)(5)'s new express authorization for "equitable relief." *See* S. Rep. 107-205, at 27 (2002) (explaining that the provision was intended to authorize "additional relief in enforcement cases" beyond "orders to disgorge funds" received as a result of a law violation).

Eight years later, in the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. 111-203, 124 Stat. 1376, Congress re-codified court-ordered disgorgement when it amended the text of § 7246's fair-funds provision to eliminate a disgorgement order as a condition precedent for a fund's creation. It did so, at the behest of the SEC, in order to allow distribution of civil penalties to victims, even in instances when a securities law violator did not reap any profits, and thus could not be ordered to pay disgorgement. But the amended text retains § 7246(a)'s initial reference to "a disgorgement fund" in a "judicial or administrative action" brought by the SEC. *Id.* at § 929B.

The second explicit reference to court-ordered SEC disgorgement in the Dodd-Frank Act amended the Exchange Act to authorize the payment of bounty awards to qualified whistleblowers based on "any monies, including penalties, disgorgement, and interest ordered to be paid" in "any judicial or administrative action." Dodd-Frank Act § 922 (codified at Exchange Act § 21F(a)(4), 15 U.S.C. 78u-6(a)(4)). By including in the statute another explicit reference to disgorgement paid in judicial actions, Congress once again codified its decades-old understanding that court-ordered disgorgement is a statutorily authorized form of equitable relief.

## III. COURT-ORDERED DISGORGEMENT ADVANCES THE SEC's MISSION TO PROTECT INVESTORS AND MAINTAIN FAIR, ORDERLY, AND EFFICIENT CAPITAL MARKETS

Court-ordered disgorgement is an enormously important remedy in securities enforcement. In the aggregate, defendants were ordered to pay $14.5 billion in disgorgement (and $5.8 billion in civil penalties) in fiscal years 2015 to 2019. *See* SEC, Div. of Enforcement, *2019 Annual Report* 16. Some disgorgement orders were deemed satisfied with payments in parallel criminal or civil actions, but most—$9.9 billion—were not. Of that amount, 66% was imposed in civil enforcement actions instituted in district courts.[6]

Despite petitioners' assertions to the contrary, the SEC could not easily substitute court-ordered

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[6] Where a factual statement does not include a citation, the statement is based on a database of SEC enforcement actions developed and maintained by one of the *amici*. *See* Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 Cornell L. Rev. 901 (2016).

disgorgement with disgorgement in administrative proceedings. Pet. Br. 17, 28. In a settled action, defendants usually prefer an administrative to a judicial resolution. Defendants in *contested* actions, like the one against petitioners, almost always face the SEC in court. In FY 2018 and 2019, only 3% of cases that were not settled during the investigation were filed as administrative proceedings. The reason is that in contested cases the SEC typically seeks remedies that only a district court can impose, such as a temporary restraining order, an asset freeze, and a receiver—all remedies that the district court ordered against petitioners. In addition, defendants who violate a court's order may be found in contempt and be subject to additional fines or imprisonment. Forcing the SEC to bring a second case in an administrative proceeding to obtain disgorgement would unnecessarily duplicate the cost of the process and was not what Congress intended.

Petitioners cite to *Kokesh* for the factual proposition that *all* SEC disgorgement is punitive, Pet. Br. 22, but the reality is much more nuanced. The SEC's Division of Economic and Risk Analysis has developed systems to ensure that disgorgement calculations are consistent across similar violations. In insider trading cases not involving tipping, the SEC seeks as disgorgement trading profits—the difference between purchase and sale price. *See* Verity Winship, *Disgorgement in Insider Trading Cases: FY2005-2015*, 71 SMU L. Rev. 999, 1003–04 (2018). In foreign bribery cases, the SEC seeks as disgorgement the amount by which the contracts obtained through bribes "unjustly enriched" the defendant, not gross revenues. *See, e.g.*, Order, *Deutsche Bank AG*, Exch.

Act Rel. 86,740, at 6. In cases against rogue investment advisers who overcharge clients for their services, the SEC routinely seeks only the amount of the overcharge as disgorgement. *See, e.g.,* Order, *State Street Bank and Trust Company*, Inv. Company Act Rel. 33,534, at 7.

A principal exception is cases where the scheme is fraudulent from the outset, like the one by petitioners. In such cases, the SEC typically seeks as disgorgement gross receipts raised from investors. Such a request is akin to a rescission coupled with restitution, and is designed to restore the status quo before the fraud took place. If petitioners were allowed to offset the costs spent marketing their fraud, as they contend, Pet. Br. 9, they would effectively profit from it. As the *Liu* district court found, petitioners misappropriated investors' funds to market the fraudulent offering through companies they controlled. *See* Order Granting Plaintiff's Motion for Summary Judgment Against Defendants Liu and Wang, SEC v. Liu, No. SACV 16-00974-CJC, ECF No. 238, at 5–7 (C.D. Cal. Apr. 20, 2017). If petitioners were allowed to offset the millions they spent concealing the fraud, the effect would be to subsidize securities violations. In the kind of scenario presented in petitioners' case, typical of offering frauds, any payment received from defrauded investors is a payment that would not have been made but for the fraud. Expenses in petitioners' and like schemes are incurred not in furtherance of a legitimate business, they are instead in furtherance of a fraud. They may not be profits in the accounting sense, but they are receipts by co-conspirators produced by the fraudulent scheme that would not have existed but for the fraud.

Under those circumstances, such receipts are the ill-gotten gains from the violation and their return is essential to restore the status quo.

Tipper-tippee insider trading cases implicate a another exception, which is based on Congress's *express* directive that district courts in SEC enforcement actions have broad authority to recoup *all* illicit profits that resulted from an unlawful communication. *See* H.R. Rep. 100-910 (1988) at 20 n.16 (emphasizing "the Commission's ability to obtain the full scope of equitable and other relief available in appropriate cases" and observing that "if a tipper's communication resulted in profits to his direct tippee and to remote tippees as well, the Commission could obtain disgorgement from the tipper of the profits of both the direct and remote tippees, and could seek an ITSA penalty of up to three times that amount"). Although such joint-and-several liability is often viewed as distinct from the longstanding equitable remedy of disgorgement, *see* Brief of Remedies and Restitution Scholars as Amici Curiae in Support of Neither Side at 6–7, Congress did not regard courts' equitable authority in SEC enforcement actions as constrained by the net-profit tradition for disgorgement that developed through the centuries in private disputes.

A refusal to recognize court-ordered disgorgement will also drastically diminish the SEC's ability to compensate defrauded investors, in particular those investors who have no other recourse. *See* Urska Velikonja, *Public Compensation for Private Harm: Evidence from the SEC's Fair Fund Distributions*, 67 Stan. L. Rev. 331, 373 tbl.4 (2015) ("Velikonja, *Fair Funds*"). Private lawsuits are rarely filed and almost never succeed in the sorts of cases that result in large disgorgement orders: offering fraud, misappropriation by investment advisers, and conflicted transactions that benefit market professionals at the expense of investors in violations of securities laws. *See id.*

To be able to compensate investors, the SEC must not only be granted disgorgement relief but also must *collect* it, identify defrauded investors, and pay the distribution agents and tax administrators. Historically, the SEC is often unable to collect monetary judgments imposed on individual defendants like petitioners. On average, the SEC collects just over half of the ordered monetary penalties (53% in FY 2009-2013 and 58% for FY 2014-2018). *See* SEC, *FY 2018 Annual Performance Report* 127. That includes penalties paid by public companies and their subsidiaries, predominantly in settlements with the SEC. Although accurate figures are not publicly available, the collection rate for disgorgement is considerably lower than that for civil penalties. A large share of disgorgement is imposed on individuals who contest charges, and who frequently pay cents on the dollar. *See* Urska Velikonja, *Public Enforcement After* Kokesh: *Evidence from SEC Actions*, 108 Geo. L.J. 389, 428 tbl.7 (2019) ("Velikonja, *Kokesh*").

Petitioners suggest that the SEC distributes court-ordered disgorgement only in the rare cases. Pet. Br. 7. In reality, most collected disgorgement is distributed. In cases resolved in FY 2010 to 2018, courts and the SEC ordered defendants to pay a combined $13.8 billion in disgorgement in 3,714 cases.[7] The SEC created a distribution fund in 425 cases (11.4%) to distribute $3.7 billion in disgorgement. While that is only 27% of aggregate disgorgement ordered during the period, it represents close to 75% of collected disgorgement. *See* Velikonja, *Fair Funds* 334. But for SEC compensation, most of these investors would recover nothing.

The SEC typically recommends to courts that disgorgement be paid to the Treasury only in cases in which no distribution to investors appears possible. These include cases with no obvious harmed investors (for example, in foreign bribery cases), with investors who cannot easily be identified (for example, in insider trading cases), or with costs of distribution that are high relative to the collected amount. *See* Velikonja, *Kokesh* 400. In petitioners' case, the SEC has yet to collect anything and has not made a recommendation about where to direct paid disgorgement.

If the Court eliminates court-ordered disgorgement, the decision will hurt those most vulnerable, reward those most cunning, and weaken fair, orderly, and efficient capital markets.

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[7] The amount does not include orders that were deemed satisfied with payments in parallel actions, so it is lower than the figures that the SEC reports. Velikonja, *Kokesh* 408, 424 tbl.6.

## CONCLUSION

For these reasons, the Court should affirm the judgment below.

Respectfully submitted,

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