

White Collar Criminal Defense

November 5, 2019

Supreme Court to Review the SEC's Right to Seek Disgorgement

By **H. Gregory Baker** and **Alexandra S. Droz**

On Friday, the Supreme Court agreed to hear a long-anticipated case challenging the SEC's authority to seek disgorgement, in a case which could significantly and permanently diminish the SEC's enforcement powers.¹ The SEC's right to seek monetary penalties and injunctions is authorized by Congress, but its ability to seek disgorgement is an equitable form of relief provided for by courts since the 1970s. Although not statutorily sanctioned, disgorgement is one of the SEC's most powerful enforcement tools. In fiscal year 2018, the SEC won disgorgement orders totaling \$2.5 billion, compared with a total of \$1.4 billion for all other types of monetary penalties.² The co-director of the SEC's Division of Enforcement, Steven Peikin, recently noted that "disgorgement is a central component of meaningful relief and often the surest way to restore at least a portion of investors' losses."³

The Supreme Court granted a writ of certiorari in *Charles C. Liu, et al. v. SEC*, No. 18-1501, a case in which the Ninth Circuit upheld an almost \$35 million judgment against a husband and wife who allegedly defrauded Chinese investors out of millions in an EB-5 immigrant visa scheme involving a cancer treatment center that was never built.⁴ The SEC sued in May 2016, claiming that Charles Liu and Xin Wang misappropriated investors' money for personal use and funneled millions to Chinese marketing firms. The district

court for the Central District of California granted summary judgment for the SEC, ordering the couple to pay \$8.2 million in monetary penalties and to disgorge the nearly \$27 million in ill-gotten gains they took from EB-5 visa-seeking Chinese investors.

After the Ninth Circuit affirmed the judgment and denied a subsequent petition for re-hearing, petitioners Liu and Wang asked the Supreme Court to decide "[w]hether the Securities and Exchange Commission may seek and obtain disgorgement from a court as 'equitable relief' for a securities law violation even though this Court has determined that such disgorgement is a penalty."⁵ The petitioners argue that under the reasoning in the Supreme Court's 2017 *Kokesh v. SEC* decision, disgorgement is no longer available as a form of equitable relief.

In *Kokesh v. SEC*, the Supreme Court held that disgorgement constitutes a penalty, and consequently that SEC claims for disgorgement are subject to the five-year statute of limitations.⁶ The Supreme Court explained its reasoning that disgorgement "bears all the hallmarks of a penalty: it is imposed as a consequence of violating a public law and it is intended to deter, not to compensate."⁷ However, the Court explicitly noted that "[n]othing in this opinion should be interpreted as an opinion on whether

¹ *Charles C. Liu, et al. v. SEC*, No. 18-1501, 2019 WL 5659111 (U.S. Nov. 1, 2019).

² See Supreme Court to consider challenge to SEC disgorgement powers, Investment News, Nov. 1, 2019, available at <https://www.investmentnews.com/article/20191101/FREE/191109985/supreme-court-to-consider-challenge-to-sec-disgorgement-powers>.

³ Remedies and Relief in SEC Enforcement Actions, PLI White Collar Crime 2018: Prosecutors and Regulators Speak, Oct. 3, 2018, available at <https://www.sec.gov/news/speech/speech-peikin-100318>.

⁴ *SEC v. Liu*, 754 F. App'x 505, 509 (9th Cir. 2018).

⁵ May 31, 2019 Petition for a Writ of Certiorari, *Charles C. Liu, et al. v. SEC*, No. 18-1501.

⁶ *Kokesh v. SEC*, 137 S. Ct. 1635, 1644 (2017). A five-year statute of limitations applies to any "action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise." 28 U.S.C. § 2462.

⁷ *Kokesh*, 137 S. Ct. at 1644.

courts possess authority to order disgorgement in SEC enforcement proceedings or on whether courts have properly applied disgorgement principles in this context.”⁸

Since the *Kokesh* decision was issued in 2017, scholars and legal practitioners in the area of securities law have anticipated that a defendant would challenge the SEC’s ability to seek disgorgement. With the Supreme Court’s decision to grant the petition to hear the case in

Liu v. SEC, that moment has finally arrived. Given that disgorgement is one of the most significant remedies available to the SEC’s enforcement division, the Supreme Court’s decision in the case could significantly curtail the Commission’s enforcement authority, should the Court decide to strip it of its disgorgement power.

⁸ *Id.* at 1642, fn. 3.

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