No. 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 a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF THE *AMICUS CURIAE* NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC., IN SUPPORT OF RESPONDENT

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[January 22, 2020]

QUESTION PRESENTED

Whether a district court, in a civil enforcement action brought by the Securities and Exchange Commission, may order disgorgement of money acquired through fraud.

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STATEMENT OF INTEREST[1]

The North American Securities Administrators Association, Inc. ("NASAA") is the non-profit association of state, provincial, and territorial securities regulators in the United States, Canada and Mexico. NASAA has 67 members, including the securities regulators in all 50 states,[2] the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. Formed over a century ago in 1919, NASAA is the oldest international organization devoted to protecting investors from fraud and abuse in the offer and sale of securities.

NASAA's U.S. members are responsible for regulating transactions under state securities laws, commonly known as "Blue Sky Laws."[3] The principal activities of NASAA's U.S. members include registering certain securities offerings, licensing the broker-dealers and investment advisers who sell securities or provide investment advice, and initiating enforcement actions to address fraud and other misconduct. NASAA's members are intimately

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[1] Pursuant to U.S. Sup. Ct. Rule 37.6, counsel for *amicus* affirms that no party other than *amicus* and its counsel authored this brief, in whole or in any part, and that no person or entity other than *amicus* or *amicus's* counsel has made a monetary contribution to the preparation and submission of this brief. The parties have provided their written consent for the filing of this amicus brief.

[2] Laura Posner, partner at Cohen Milstein Sellers & Toll PLLC and a co-author of this brief, served as the Bureau Chief of the New Jersey Bureau of Securities for approximately three years and as the Chair of Enforcement for NASAA for two years.

[3] *See generally* 1 LOUIS LOSS ET AL., SECURITIES REGULATION 55-251 (5th ed. 2014).

familiar with the securities markets and the fraud and other abuses victimizing their state residents.

The overriding mission of NASAA and its members is to protect investors, particularly retail investors, from fraud and abuse. NASAA supports the work of its members and the investing public by, among other things, promulgating model rules, providing training and professional education opportunities, coordinating multi-state enforcement actions and examinations, and commenting on proposed legislation and rulemaking. NASAA also offers its legal analysis and policy perspective to state and federal courts as *amicus curiae* in important cases involving the interpretation of state and federal securities laws, securities regulation, and investor protection. This is one of those cases.

NASAA and its members have an interest in this appeal because they, like their federal counterpart, the Securities Exchange Commission ("SEC"), have a strong interest in enforcing the securities laws to protect investors from fraud and abuse. In order to effectively address the many varieties of investment fraud in an increasingly complex market, securities regulators must have the flexibility to obtain all appropriate remedies, including disgorgement. NASAA and its members regularly encounter a wide variety of frauds in which disgorgement is essential to providing compensation to fraud victims and to deterring fraud.

NASAA members and the SEC regularly work together to address widespread and complex frauds, including frauds arising out of the EB-5 Immigrant Investor Program. For example, in 2014, the Vermont Department of Financial Regulation ("DFR") began

an investigation into an EB-5 fraud involving Jay Peak Inc., a ski resort operated by two residents of Florida and Vermont ("Jay Peak"). After working closely with DFR, in April 2016, the SEC charged the developers of Jay Peak with 52 counts of fraud and the misuse of approximately $200 million in funds from hundreds of investors in 74 countries. Ultimately, DFR and the SEC together obtained nearly $81 million in disgorgement for the benefit of investors from the perpetrators of the Jay Peak fraud.

Similar to the Jay Peak defendants, Petitioners here engaged in an EB-5 Immigrant Investor Program fraud in which they induced fifty investors to invest a total of nearly $27 million dollars (Pet. App. at 12a-13a), telling investors that the money would fund the constructions of a cancer treatment center. *Id.* at 2a. Petitioners, in direct violation of the terms of the offering documents, then misappropriated and funneled that money to themselves and used it to pay for personal expenses (*id.* at 16a n.9; 17a-18a; 33a), exhausted all but a couple hundred thousand of the money raised, and never even obtaining the required permits to break ground for the cancer treatment center. *Id.* at 2a-3a; 21a. The District Court ordered the disgorgement of $26.7 million (*id.* at 40a), less than the amount that Petitioners fraudulently took from innocent investors, since – in the court's opinion – there were no legitimate business expenses incurred by Petitioners. *Id.* at 18a. The court of appeals concurred with this assessment. *Id.* at 7a.

SUMMARY OF ARGUMENT

As this Court made clear just last year: "Congress intended to root out all manner of fraud in the securities industry. And it gave to the Commission the tools to accomplish that job." *Lorenzo v. SE*C, 139 S. Ct. 1094 (2019). For more than half a century, the Courts and Congress consistently agreed that one of those "tools" was the SEC's ability to seek disgorgement in Court.

More than fifty years ago, the Second Circuit first recognized that district courts may require defendants in SEC actions to disgorge their illicit gains "as an ancillary remedy in the exercise of the courts' general equity powers to afford complete relief." *Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1307 (1971), *cert. denied*, 404 U.S. 1005 (1971). Since then, the circuits have uniformly held that disgorgement is an available remedy in the SEC's enforcement actions.[4] Following this Court's *Kokesh* decision[5],

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[4] *See SEC* v. *Happ*, 392 F.3d 12, 31 (1st Cir. 2004); *SEC* v. *Cavanagh*, 445 F.3d 105, 116 (2d Cir. 2006); *SEC* v. *Hughes Capital Corp.*, 124 F.3d 449, 455 (3d Cir. 1997); *SEC* v. *Gotchey*, 981 F.2d 1251, 1992 WL 385284, at *2 (4th Cir. 1992) (unpublished table decision), cert. denied, 509 U.S. 927 (1993); *SEC* v. *Huffman*, 996 F.2d 800, 803 (5th Cir. 1993); *SEC* v. *Blavin*, 760 F.2d 706, 713 (6th Cir. 1985) (per curiam); *SEC* v. *Lipson*, 278 F.3d 656, 662-663 (7th Cir. 2002); *SEC* v. *Ridenour*, 913 F.2d 515, 517-518 (8th Cir. 1990); *SEC* v. *Rind*, 991 F.2d 1486, 1493 (9th Cir.), cert. denied, 510 U.S. 963 (1993); *SEC* v. *Maxxon, Inc.*, 465 F.3d 1174, 1179 (10th Cir. 2006), cert. denied, 550 U.S. 905 (2007); *SEC* v. *Calvo*, 378 F.3d 1211, 1217 (11th Cir. 2004); *SEC v. First City Fin. Corp., Ltd.*, 890 F.2d 1215, 1230 (D.C. Cir. 1989).

[5] In *Kokesh*, this Court cautioned that "[n]othing in this opinion should be interpreted as an opinion on whether courts possess authority to order disgorgement in SEC enforcement

every court of appeals and every district court that considered the issue also uniformly determined that nothing in that decision called into question the availability of disgorgement in SEC enforcement actions. *See SEC* v. *Weaver*, 773 Fed. Appx. 354, 356-357 (9th Cir. 2019).[6]

This is unsurprising given that the disgorgement of profits is a "historic equitable remedy." *SEC v. Commonwealth Chem. Securities, Inc.*, 574 F.2d 90, 95 (2d Cir. 1978) ("Disgorgement of profits in an action brought by the SEC . . . appears to fit" the description of "[a] historic equitable remedy" because "the court is not awarding damages to which plaintiff is legally entitled but is exercising the chancellor's discretion to prevent unjust enrichment").[7]

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proceedings or on whether courts have properly applied disgorgement principles in this context." *Kokesh v. SEC*, 137 S. Ct. 1635, 1642 n.3 (2017).

[6] *See also SEC* v. *Metter*, 706 Fed. Appx. 699, 702 (2d Cir. 2017); *United States SEC* v. *Ahmed*, 343 F. Supp. 3d 16, 26-27 (D. Conn. 2018); *SEC* v. *Flowers*, No. 17-cv-1456, 2018 WL 6062433, at *2 (S.D. Cal. Nov. 19, 2018); *SEC* v. *Present*, No. 14-cv-14692, 2018 WL 1701972, at *2 (D. Mass. Mar. 20, 2018); *SEC* v. *Revolutions Med. Corp.*, No. 1:12-CV-3298, 2018 WL 2057357, at *2-*3 (N.D. Ga. Mar. 16, 2018); *SEC* v. *Arcturus Corp.*, No. 3:13-CV-4861, 2018 WL 1701998, at *1-*3 (N.D. Tex. Jan. 10, 2018); *SEC* v. *Sample*, No. 3:14-CV-1218-B, 2017 WL 5569873, at *1-*2 (N.D. Tex. Nov. 20, 2017); *SEC* v. *Jammin Java Corp.*, No. 2:15-cv-8921, 2017 WL 4286180, at *2-*3 (C.D. Cal. Sept. 14, 2017); *SEC* v. *Brooks*, No. 07-61526-CIV, 2017 WL 3315137, at *6-8 (S.D. Fla. Aug. 3, 2017).

[7] *See also SEC v. Jones*, 155 F. Supp. 3d 1180, 1184 (D. Utah 2015) (disgorgement is equitable because "the primary purpose of disgorgement is not to compensate victims" but "to prevent wrongdoers from unjustly enriching themselves through

Congress has also repeatedly and expressly recognized court authority to order disgorgement in SEC enforcement actions. *See, e.g.*, Sarbanes-Oxley Act of 2002, § 308(b), 15 U.S.C. 7246(a)(separate civil penalties assessed against securities wrongdoers may "be added to and become part of a disgorgement fund or other fund established for the benefit of the victims of such violation."); Private Securities Litigation Reform Act of 1995, Pub. L. 104-67, § 103(b), 109 Stat. 737 (codified at Securities Act of 1933 ("1933 Act") § 20(f), 15 U.S.C. § 77t(f)); Securities Exchange Act of 1934 ("1934 Act") § 21(d)(4), 15 U.S.C. § 78u(d)(4)) (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.).

The Courts and Congress are correct. Without the remedy of disgorgement, regulators would lose a "tool" necessary to deter wrongdoing and compensate victims of fraud. Disgorgement is most often imposed on individual fraudsters and investment advisers who prey on small, unsophisticated retail investors. These

violations, which has the effect of deterring subsequent fraud") (citations and quotation marks omitted); *SEC v. Seibald*, No. 95 Civ.2081 (LLS), 1997 WL 605114, at *7 (S.D.N.Y. Sept. 30, 1997) ("The SEC does not sue for common-law damages: it has suffered no loss. The basis of the action [for disgorgement], against all defendants, is equitable").

retail investors typically lack not only the capacity and resources to monitor their investments, but also to bring suit to recover their losses when they fall victim to fraud. The SEC thus serves an important role in bringing securities enforcement actions that private litigants will not fill. Accordingly, in many circumstances, disgorgement is the primary vehicle through which funds are returned to investors.

Every dollar that is lost to a fraudulent investment is a dollar that is not invested in a legitimate business or market. Requiring disgorgement of these dollars puts the funds back into the hands of investors for future investment. When disgorged funds cannot be returned to investors, they are used by the SEC in ways that benefit the markets and investors, including, compliance and examinations of registrants, investigations of fraudulent schemes, and investor education outreach. Disgorged funds, regardless of whether they flow to identifiable investors (as is typically the case) or the U.S. Treasury, thus further the purpose of the federal securities laws: protecting investors and maintaining market integrity. If the "tool" of disgorgement was suddenly unavailable, the hundreds of millions of dollars returned to fraud victims every year by the SEC would escheat to fraudsters at the direct expense of their victims, and wrongdoers would be emboldened to engage in misconduct in violation of the federal securities laws.

ARGUMENT

I. THE DISGORGEMENT REMEDY IS CRITICAL TO REGULATORS' ABILITY TO ENFORCE SECURITIES LAWS AND THE RECOUPLEMENT OF FUNDS BY DEFRAUDED INVESTORS.

A. Regulators Play an Essential Role in Enforcing the Securities Laws.

Our capital markets function and grow in large part due to the trust investors place in the regulators who are charged with policing the conduct of market participants. Maintaining that trust is essential to the continued primacy of the U.S. markets in an ever-increasingly competitive global marketplace. The essential work securities regulators – both state and federal – do to investigate suspected investment fraud, and, where warranted, pursue enforcement actions, is integral to maintaining investor trust. Moreover, enforcing the securities laws serves not only the interests of investors, but the businesses that rely on markets to raise capital.

The 1933 Act, 48 Stat. 74, as amended, 15 U.S.C. § 77a *et seq.*, is designed to provide investors with full disclosure of material information concerning public offerings of securities in commerce, to protect investors against fraud and, through the imposition of specified civil liabilities, to promote ethical standards of honesty and fair dealing. *See* H.R. REP. No. 73-85, at 1-5 (1933). The 1934 Act, 48 Stat. 881, as amended, 15 U.S.C. § 78a *et seq*. (together with the 1933 Act, the "Acts"), is intended principally to protect investors against manipulation of stock prices through regulation of

transactions upon securities exchanges and in over-the-counter markets, and to impose regular reporting requirements on companies whose stock is listed on national securities exchanges. *See* S. REP. No. 73-792, at 1-5 (1934).

As this Court explained more than 40 years ago in *Ernst & Ernst*, "[a]lthough the Acts contain numerous carefully drawn express civil remedies and criminal penalties, Congress recognized that efficient regulation of securities trading could not be accomplished under a rigid statutory program." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 195 (1976). Accordingly, as part of the 1934 Act, "Congress created the [Securities and Exchange] Commission, which is provided with an arsenal of flexible enforcement powers." *Id.*; *see, e.g.,* 1933 Act §§ 8, 19, 20, 15 U.S.C. §§ 77h, 77s, 77t; 1934 Act §§ 9, 19, 21, 15 U.S.C. §§ 78i, 78s, 78u.

In addition to the federal regulatory framework, every state has its own securities laws – commonly referred to as "Blue Sky Laws" – designed to protect investors against fraudulent sales practices and activities.[8] Pursuant to these laws, state securities regulators have protected investors for the past 100 years, longer than any other securities regulator. While certain provisions of the Blue Sky Laws vary from state to state, most state Blue Sky Laws require companies making offerings of securities to register their offerings before they can be sold in a particular state (unless a specific exemption from registration is available), and grant the state

[8] Currently, 43 states have adopted the Uniform Securities Act. The Uniform Securities Act was developed by the Uniform Law Commission for adoption by the states.

securities regulator the authority to investigate and pursue enforcement actions in cases of securities fraud that occurs, or targets, investors in their states.

This interlocking system of state and federal securities laws was expressly designed "to root out all manner of fraud in the securities industry" (*Lorenzo v. SEC*, 139 S. Ct. 1094, 1104 (2019)) and "to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits" (*id.* at 1103 (citing *SEC v. W. J. Howey Co.*, 328 U.S. 293, 299, 66 S. Ct. 1100, 90 L. Ed. 1244 (1946))), by providing regulators with "the tools to accomplish that job." *Id*. at 1104.

While this Court has "long recognized that meritorious private actions to enforce federal antifraud securities laws are an essential supplement to criminal prosecutions and civil enforcement actions brought [by regulators and law enforcement]", *see, e.g., Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308 (2007), they are a supplement. Both this Court and Congress have made clear that regulators and law enforcement have a unique and distinct role in enforcing the securities laws that is different – and oftentimes broader – than that afforded to private litigants. *See, e.g., Transamerica Mortg. Advisors, Inc. (TAMA) v. Lewis*, 444 U.S. 11 (1979) (declining to recognize a private right of action under both Section 17(a) of the 1934 Act, and Section 206 of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-6(1)); *Central Bank, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994) (declining to recognize a private right of action of action to bring claims for aiding and abetting under Section

10(b));[9] *Stoneridge Inv. Partners v. Scientific-Atlanta, Inc.,* 552 U.S. 148 (2008) (holding that private plaintiffs could not bring a Section 10(b) suit against companies that were suppliers of an entity committing fraud, because (even though the suppliers' conduct was deceptive) investors did not rely on their statements or representations)[10];

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[9] As the Court explained:

> In § 10(b), Congress prohibited manipulative or deceptive acts in connection with the purchase or sale of securities. It envisioned that the SEC would enforce the statutory prohibition through administrative and injunctive actions. Of course, a private plaintiff now may bring suit against violators of § 10(b). But the private plaintiff may not bring a 10b-5 suit against a defendant for acts not prohibited by the text of § 10(b).

See also Janus Capital Grp., Inc. v. First Derivative Traders, 564 U.S. 135, 143 (2011) (explaining that *Central Bank* held that, "Rule 10b-5's private right of action does not include suits against aiders and abettors. . . . Such suits--against entities that contribute "substantial assistance" to the making of a statement but do not actually make it--may be brought by the SEC, *see* 15 U.S.C. § 78t(e), but not by private parties."). The decision in *Central Bank* led to calls for Congress to create an express cause of action for aiding and abetting within the 1934 Act. Then-SEC Chairman Arthur Levitt, testifying before the Senate Securities Subcommittee, cited *Central Bank* and recommended that private aiding and abetting liability be established. S. Hearing No. 103-759, 13-14 (1994). Congress did not follow this course. Instead, in § 104 of the Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 757, it directed prosecution of aiders and abettors to the SEC. 15 U.S.C. § 78t(e).

[10] The Court expressed concern that an extension of the cause of action would lead to increased private litigation and undermine "Congress' specific response to *Central Bank* in § 104 of the PSLRA." *Id.* at 162. "Congress amended the securities laws to provide for limited coverage of aiders and abettors. Aiding and

Morrison v. National Australia Bank, 561 U.S. 247 (2010) (holding that Section 10(b) did not provide a private cause of action against foreign and American defendants for misconduct in connection with securities traded on foreign exchanges).[11]

Regulators, thus, fulfill a unique and critical role in ensuring fairness in our markets, compensation to victims, and protection to investors. To carry out this role, regulators must have access to the tools and remedies necessary to punish wrongdoers, deter future violative conduct, and recover funds for defrauded investors. Disgorgement is one of those essential tools.

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abetting liability is authorized in actions brought by the SEC but not by private parties." *Id*. The Court explained that because "[s]econdary actors are subject to criminal penalties, *see e.g.,* 15 U.S.C. § 78ff, and civil enforcement by the SEC, *see*, *e.g.,* § 78t(e)," the "enforcement power is not toothless." *Id*. at 166.

[11] Following *Morrison,* Congress distinguished between the SEC and private plaintiffs. In Section 929P(b), 124 Stat. 1862, of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), 15 U.S.C. § 78u-6, Congress confirmed the SEC's authority to enforce Section 10(b) in cases involving transactions outside the United States. Pub. L. No. 111-203, 124 Stat. 1376, 1864–65 (2010) (codified at 15 U.S.C. §§ 77v(c) & 78aa(b)). *See also SEC v. Scoville*, 913 F.3d 1204 (10th Cir. 2019), *cert. denied*, No. 18-1566, 2019 WL 5686461 (U.S. Nov. 4, 2019). In contrast, for private rights, in Section 929Y, 124 Stat. 1871, Congress required the SEC to solicit public comment and conduct a study to determine the extent to which private rights under the antifraud provisions of the 1934 Act should be extended across international boundaries, and submit a report of the study to Congress by early 2012. *Study on the Cross-Border Scope of the Private Right of Action Under Section 10(b) of the Securities Exchange Act of 1934*, SEC (2012), https://www.sec.gov/news/studies/2012/929y-study-cross-border-private-rights.pdf.

B. The Remedy of Disgorgement Plays a Pivotal Role in Regulators' Ability to Deter Fraud and Bring Wrongdoers to Justice.

"The magnitude of the federal interest in protecting the integrity and efficient operation of the market for nationally traded securities cannot be overstated." *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 78 (2006). In order to effectively police the securities markets, regulators must have the necessary tools to deter future violations, as well as redress frauds that have already occurred. When properly applied, disgorgement of ill-gotten gains is a vital and effective tool for addressing and deterring financial misconduct. Equitable remedies often have a deterrent effect: "[t]he historic injunctive process was designed to deter." *Hecht Co. v. Bowles*, 321 U.S. 321, 329 (1944).

Federal courts consistently recognize the importance of disgorgement to deter violations of the securities laws. *See*, *e.g.*, *SEC v. Rind*, 991 F.2d 1486, 1491 (9th Cir. 1993) ("Disgorgement plays a central role in the enforcement of the securities laws."); *SEC v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1104 (2d Cir. 1972) ("The deterrent effect of an SEC enforcement action would be greatly undermined if securities law violators were not required to disgorge illicit profits."); *SEC v. Texas Gulf Sulphur Co.*, 446 F.2d 1301, 1308 (2d Cir. 1971) ("It would severely defeat the purposes of the [Securities Exchange Act of 1934] if a violator of Rule 10b-5 were allowed to retain the profits from his violation.").

Relatedly, federal courts, including this Court, also recognize the key role of disgorgement in the

enforcement of other federal regulatory schemes. *See, e.g.*, *Porter v. Warner Holding Co.*, 328 U.S. 395, 400 (1946) ("Future compliance [with the Emergency Price Control Act of 1942[12]] may be more definitely assured if one is compelled to restore one's illegal gains"); *United States v. Rx Depot, Inc.*, 438 F.3d 1052, 1061 (10th Cir. 2006) (recognizing deterrent effect of disgorgement in enforcement of the Food, Drug, and Cosmetic Act[13]) (citing *SEC v. Fischbach Corp.*, 133 F.3d 170, 175 (2d Cir. 1997)); *FTC v. Gem Merchandising Corp.*, 87 F.3d 466, 470 (11th Cir. 1996) (recognizing the importance of disgorgement to enforcement of the Federal Trade Commission Act[14]); *CFTC v. Co Petro Mktg. Grp., Inc.*, 680 F.2d 573, 583-84 (9th Cir. 1982) (concluding "that it would frustrate the regulatory purposes of the [Commodity Exchange Act[15]] to allow a violator to retain his ill-gotten gains.").

While the SEC commonly uses disgorged funds to compensate investors, another "primary purpose of disgorgement as a remedy for violation of the securities laws is to deprive violators of their ill-gotten gains, thereby effectuating the deterrence objectives of those laws." *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1474 (2d Cir. 1996). Permitting wrongdoers to profit from their violations would only incentivize further fraud and other misconduct.

Petitioners contend that "[n]ot much" would change if the SEC were suddenly – after half a

[12] Emergency Price Control Act of 1942, 50 App. U.S.C. § 901.

[13] Food, Drug, and Cosmetic Act, 21 U.S.C. § 301.

[14] Federal Trade Commission Act, 15 U.S.C. § 41.

[15] Commodity Exchange Act, 7 U.S.C. § 1.

century – banned from obtaining disgorgement in civil proceedings, since according to Petitioners, the SEC is authorized to obtain penalties in amounts that are "commensurate with those that [the SEC] has sought using the . . . disgorgement remedy." Brief for Petitioners ("Pet. Br.") at 2, 42. *See also* Brief of Andy Altahawi as Amicus Curiae in Support of Petitioners ("Altahawi") at 15 ("The SEC has numerous statutory remedies at its disposal to enforce the federal securities laws. If this Court holds that the SEC does not have the power to seek or obtain disgorgement from federal courts it would not diminish the effectiveness of the SEC's enforcement program."). Respectfully, this is wrong. The Acts authorize the imposition of civil penalties not to exceed "the greater of (i) [a specified dollar amount, depending on the nature of the violation], or (ii) the gross amount of pecuniary gain to [the] defendant as a result of the violation." 1933 Act, 15 U.S.C. § 77t(d)(2); 1934 Act, 15 U.S.C. § 78u(d)(3)(B). By requiring wrongdoers to give up their ill-gotten gains, disgorgement prevents the use of those ill-gotten gains to pay or offset any penalties assessed pursuant to the Acts. If wrongdoers were permitted to use ill-gotten gains to offset penalties in this manner, the deterrent effect of the penalties would be entirely lost. Indeed, if an ill-gotten gain were greater than a penalty, it would actually incentivize a rational actor to violate the Acts, a terrible public policy consequence. Without the possibility of disgorgement, in conjunction with the other available civil penalties, there would be much less downside to committing fraud or other misconduct. Wrongdoers "could continue to re-offend safe in the knowledge that the most they would ever lose would be the amount of their improper gains."

United States v. Prochnow, No. 07-10273, 2007 WL 3082139 at *5 (11th Cir. Oct. 22, 2017).

The fact that disgorgement successfully aids deterrence does not serve to transform it into a penalty. *See* Brief of Amicus Curiae Securities Industry and Financial Markets Association in Support of Petitioners ("SIFMA") at 12. The Court has "emphasized 'the fact that sanctions frequently serve more than one purpose.'" *Kokesh*, 137 S. Ct. at 1645 (quoting *Austin v. United States*, 509 U.S. 602, 610 (1993)). The traditional purpose of disgorgement is to restore the status quo, rather than to punish. It is not a punishment for wrongdoers to give up their unlawful gains, because the wrongdoer was never entitled to that money or property in the first place. Properly applied, disgorgement achieves deterrence through its unmistakably equitable purpose of depriving wrongdoers of the gains resulting from their violations and restoring those funds to victims.

Finally, even if the Court were to hold that disgorgement is not available in civil proceedings, it would not resolve Petitioners' objections to the manner in which disgorgement has historically been applied in SEC enforcement proceedings. As Petitioners and their *amici* acknowledge, the SEC also has express authority to order disgorgement in its administrative enforcement proceedings. 15 U.S.C. § 77h-1(e).[16] If the SEC is unable to obtain complete relief in court proceedings, it may, by necessity, adjudicate more of its most complex and

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[16] *See, e.g.*, Pet. Br. 40-41; Brief of the Chamber of Commerce of the United States of America as Amicus Curiae in Support of Petitioners at 22; Amicus Curiae Brief of the New Civil Liberties Alliance in Support of Petitioners at 10, 16.

consequential matters in the administrative forum. Given that certain of these same *amici* continue to claim – without justification[17] – that the SEC administrative proceedings are unfair and should be abolished,[18] this argument amounts to nothing more than an effort by wrongdoers to avoid being forced to disgorge their ill-gotten gains at all.

C. The Remedy of Disgorgement Fulfills the Vital Need to Compensate Victims.

While equitable remedies need not be compensatory, disgorgement does – contrary to Petitioners' assertion (Pet. Br. 7) – typically provide essential compensation to victims of fraud. *Stoneridge Investment Partners, LLC*, 552 U.S. at 166 (2008) ("SEC enforcement actions have collected * * *

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[17] *See* Memo from Inspector General Carl Hoeckler to SEC Chair Mary Jo White, Transmittal of Report of Investigation: 15-ALJ-0482-I, 4 of 5 (Aug. 7, 2015), https://www.sec.gov/oig/reportspubs/oig-sec-interim-report-investigation-admin-law-judges.pdf (SEC Inspector General did not "develop[] any evidence to support the allegations of bias in ALJs' decisions in the Commission's administrative proceedings").

[18] *See*, *e.g.,* Brief of the Chamber of Commerce of the United States of America as Amicus Curiae Supporting Petitioners (Aug. 25, 2017) at 8-11, *Lucia v. SEC*, 138 S. Ct. 2044 (2018) (No. 17-130) (arguing that "[t]he Commission's increased use of in-house administrative proceedings before SEC ALJs . . . materially and adversely affects the rights and interests of businesses and individuals subject to SEC enforcement actions and to SEC regulation more generally"); Brief of the New Civil Liberties Alliance as Amicus Curiae in Support of Petitioners (Feb. 28, 2018), *Lucia v. SEC*, 138 S. Ct. 2044 (2018) (No. 17-130) (arguing generally that SEC administrative adjudication is ineffective and "violate[d] procedural rights guaranteed by the Constitution").

billion[s] in disgorgement and penalties, much of it for distribution to injured investors.").

Disgorgement is an important and common remedy: more than half of SEC enforcement actions result in some disgorgement. When disgorgement is ordered, it represents almost 80% of all monetary penalties imposed.[19] According to a forthcoming article to be published in the Georgetown Law Journal, entitled *Public Enforcement After Kokesh: Evidence from SEC Actions*, between 2010-2018, in cases where the SEC was the only public enforcement agency to bring an action, it secured $22.8 billion in aggregate monetary relief, of which $13.8 billion (or 61%) was disgorgement. *See also* SEC, Div. of Enforcement, 2019 Annual Report at 16 (In the aggregate, defendants were ordered to pay $14.5 billion in disgorgement in fiscal years 2015 to 2019).

Petitioners suggest that the SEC does not typically distribute court-ordered disgorgement to harmed investors. Pet. Br. 7. In reality, the overwhelming majority of disgorged funds the SEC obtains are distributed to investors through fair funds. 15 U.S.C. § 7246. Between 2002 and 2012, the SEC created 243 fair funds, and those funds distributed $14.46 billion in civil monetary penalties and disgorgement to defrauded investors.[20] Moreover, in those cases resolved in fiscal years 2010 to 2018, courts and the SEC ordered defendants to

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[19] Urska Velikonja, forthcoming article, *Public Enforcement After Kokesh: Evidence from SEC Actions,* 108 GEO. L.J. 389, 395 (2019).

[20] Urska Velikonja, *Public Compensation for Private Harm: Evidence from the SEC's Fair Fund Distributions*, 67 STAN. L. REV. 331, 333 (2015).

pay a combined $13.8 billion in disgorgement. The SEC created a distribution fund in 425 cases of those cases, and distributed approximately 75% of the disgorgement it was able to collect through those funds.[21]

Distribution of these disgorged funds to harmed investors fulfills an essential role – compensation to victims – that otherwise would not be available. Private lawsuits cannot substitute in full for SEC enforcement. *Stoneridge*, 552 U.S. at 167 (invoking the availability of disgorgement in SEC suits as a reason to give a "narrow" scope to the investors' private right of action). The vast majority of successful private lawsuits stem from class actions arising from disclosure fraud by public companies.[22] Private plaintiffs are far less successful in actions against public-firm subsidiaries and financial intermediaries,[23] even where the SEC also brings a suit.[24] Furthermore, there is virtually no private litigation against individuals that the SEC targets for offering fraud or insider trading,[25] the types of cases where the majority of disgorgement is ordered. In *Public Compensation for Private Harm: Evidence*

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[21] *Id.* at 334 n.12.

[22] *See* Cornerstone Research, Accounting Class Action Filings and Settlements 1, 8, 9 (2019), https://www.cornerstone.com/Publications/Reports/2018-Accounting-Class-Action-Filings-and-Settlements [https://perma.cc/LU9D-NB8T] (reporting that in FY 2018, 53% of private securities settlements and 88% of settlement dollars were from class actions alleging accounting fraud).

[23] Velikonja, *Public Enforcement After Kokesh* at 433.

[24] *Id.*; Velikonja, *Public Compensation for Private Harm* at 373 & tbl.4.

[25] *See* Velikonja, *Public Enforcement After Kokesh* at 433.

from the SEC's Fair Fund Distributions, Georgetown University Law Center Professor Urska Velikonja demonstrates that "[t]he rise of public compensation, such as the SEC's distribution funds, fills a void in securities laws that leaves many victims with no private remedy."[26] Velikonja's study reveals that, "[s]uccessful class actions accompany 46.3% of fair funds distributions overall and 28.1% of distributions in cases not associated with issuer reporting and disclosure violations."[27] Because the majority of SEC cases are not accompanied by successful class actions, "the SEC's fair fund distribution is often the only source of compensation for defrauded investors."[28] Accordingly, "traditional compensation schemes, in particular private litigation, fail to compensate victims for large classes of harms."[29]

Contrary to the assertions of Petitioners' *amici*, the SEC also does not have substitute remedies. *See* SIFMA at 25 ("In the securities enforcement context, disgorgement is never "necessary" or "appropriate" because the SEC has statutory authority to collect civil penalties, which are an equivalent, if not stronger, form of relief."); Altahawi at 16 ("funds collected by the SEC as civil penalties can also be distributed by the agency to harmed investors pursuant to the "fair funds" provision in § 308 of the Sarbanes–Oxley Act of 2002"). While the securities laws provide for treble civil fines for insider trading and allows for civil fines to substitute for

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[26] Velikonja, *Public Compensation for Private Harm* at 331.

[27] *Id*. at 391.

[28] *Id*.

[29] *Id*. at 338.

disgorgement if necessary,[30] there is no easy replacement for other violations that make up the bulk of SEC disgorgement orders. Eliminating disgorgement as a remedy in court cases will, thus, primarily benefit individual defendants, who are the most difficult class to deter, and whose violations are often more difficult to prosecute. For the same reason, equitable disgorgement, notwithstanding the availability of civil penalties, does not "effectively expose defendants to double-disgorgement: once as a civil penalty, and again as 'equitable relief.'" SIFMA at 26-27 (emphasis omitted).

Restitution is also an imperfect substitute for disgorgement. Restitution is measured "by the defendant's wrongful gain" and requires that the defendant return wrongful gains "properly attributable to the defendant's interference with the claimant's legally protected rights."[31] Missing or inaccurate recordkeeping and commingled assets – a common occurrence in fraudulent schemes – can significantly impede efforts to identify funds subject to restitution. Even if the rules of restitution were relaxed for public enforcement, restitution could substitute for disgorgement only when the violator was unjustly enriched at the expense of identifiable investors. In many types of fraud, there are no identifiable defrauded investors who either lost money to the fraudster or can receive compensation for their losses.

Last, while it is true, as this Court noted in *Kokesh*, that there have been several instances where

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[30] 15 U.S.C. § 78u-1(a)(2) (2012).

[31] Restatement (Third) of Restitution and Unjust Enrichment § 51 cmt. a (Am. Law Inst. 2010).

the amount recovered by the SEC through disgorgement "exceed[ed] the profits gained as a result of the violation,"[32] that is not typically the case. The vast majority of disgorgement awards require the defendant to only return wrongfully-obtained property to victims, and do not have penalty-like attributes. *See*, *e.g.*, *SEC v. Bhagat*, No. C-01-21073, 2008 WL 4890890, at *1 (N.D. Cal. Nov. 12, 2008) ("[A] general practice of awarding disgorged funds to the victims of the illegal conduct appears to have emerged."); *SEC v. Andes*, No. 82-1659, 1986 WL 1212, at *3 (E.D. Pa. Jan. 23, 1986) ("[M]ost courts do order that disgorged proceeds be distributed among injured investors."). While Petitioners and their *amici* criticize the SEC for purported overreach, the discretion in the amount and type of money awarded lies with the courts. While, of course, it is possible for courts to award erroneous or excessive disgorgement awards, that is not a reason to suddenly bar the SEC from utilizing the essential tool of disgorgement.

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[32] *Kokesh*, 137 S. Ct. at 1644 (citing *SEC v. Contorinis,* 743 F.3d 296 (2d Cir. 2014), a case where the SEC recovered third party profits from an insider trader who never received the profits, and *SEC v. Warde*, 151 F.3d 42 (2d Cir. 1998), a case where the SEC recovered disgorgement from a tipper when the ill-gotten gains were in fact earned by the person he tipped).

CONCLUSION

For all of the foregoing reasons, *amicus curiae* respectfully submits that the judgment of the court of appeals should be affirmed.

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Dated: January 22, 2020