

[Securities Regulation Daily Wrap Up, ENFORCEMENT—U.S.: Merits briefing begins in Liu case challenging SEC disgorgement power, \(Dec. 18, 2019\)](#)

Securities Regulation Daily Wrap Up

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By [Mark S. Nelson, J.D.](#)

Charles Liu argued in his merits brief that the SEC would still have adequate enforcement tools even if it were to lose the authority to seek disgorgement.

Charles Liu and Xin Wang have filed their merits brief challenging the authority of the SEC to seek, and of federal courts to award, disgorgement in civil enforcement proceedings. The case highlights the importance of footnotes in Supreme Court opinions and the context of Supreme Court precedents. Here, the Supreme Court in [Kokesh](#) left open the question of federal court authority to award disgorgement in SEC cases via footnote, but that opinion also appeared to limit its reach to the specific question presented regarding whether disgorgement was a penalty for purposes of the general federal limitations period. Regardless of the outcome, Congress has begun the process of advancing legislation that, if enacted, would clarify the SEC's disgorgement authorities. The justices are [scheduled](#) to hear oral argument in Liu's case on March 3, 2020 ([Liu v. SEC](#), December 16, 2019).

Government's equity theory disputed. By way of background, the Supreme Court in *Kokesh* limited its opinion there to the specific question presented about whether the SEC must abide by the federal limitations period contained in 28 U.S.C. §2462 when it seeks disgorgement. Said the court in footnote three: "Nothing in this opinion should be interpreted as an opinion on whether courts possess authority to order disgorgement in SEC enforcement proceedings or on whether courts have properly applied disgorgement principles in this context[.] The sole question presented in this case is whether disgorgement, as applied in SEC enforcement actions, is subject to §2462's limitations period."

Liu's merits brief opens by positing that the SEC lacks statutory authority to seek and the federal courts likewise lack such authority to award disgorgement. Liu asserts that the federal securities laws are devoid of explicit authorization for the SEC to obtain disgorgement in federal court. Liu also points to changes made by the Dodd-Frank Act that explicitly allowed the CFTC and the Consumer Financial Protection Bureau to seek disgorgement but which did not speak to the SEC's ability to seek this type of remedy. Elsewhere in the brief, Lui argues that the SEC still has potent tools for enforcement cases even if it were found to lack authority to seek disgorgement.

One area of especially strong dispute between Liu and the government is the reach of Exchange Act Section 21(d). Specifically, Section 21(d)(5) states: "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."

Liu argues this provision, with respect to disgorgement, should be understood to apply only to administrative proceedings, not federal court cases. Liu also asserts that the Supreme Court in *Kokesh* was clear that disgorgement "bears all the hallmarks of a penalty," while also suggesting that penalties are beyond a court's equitable powers. Thus, according to Liu, it is impermissible to read the SEC's injunctive authority to include disgorgement.

The government's [certiorari-stage brief in opposition](#) in *Liu*, by contrast, argued that disgorgement was consistent with *Kokesh*. The government noted multiple statutory sources for the SEC's authority to seek, and for federal courts to grant, disgorgement, including as injunctive relief allowed by the Securities Act and the Exchange Act (i.e., "enjoin" would include disgorgement). The government also said that the Sarbanes-Oxley

Act amended Exchange Act Section 21(d) to permit courts to order equitable relief and that related Supreme Court precedent suggests that disgorgement is equitable. The government also noted additional securities law provisions that refer to "disgorgement funds" and laws governing still other practice areas that provide for special treatment of disgorgement.

Moreover, the government theorized that "penal" and "penalty" (similar to the terms of the general federal limitations period statute,) can be "elastic in meaning" such that a remedy can be both equitable or penal depending on the circumstance. The government further disputed a reference in Liu's certiorari petition suggesting that Justice Kavanaugh, while he was still a D.C. Circuit judge, had concurred in a case involving the SEC to suggest limits on disgorgement. The government said the Kavanaugh [conurrence](#) did not suggest that disgorgement was beyond the authority of the SEC to seek, or a federal court to grant, such remedy in enforcement cases.

Potential for legislative reversal. Congress can legislatively reverse Supreme Court opinions in cases where the court's interpretation of a statute does not match lawmakers' intentions. In the current session to Congress, for example, legislation has been introduced to reverse the Supreme Court's decision limiting Dodd-Frank Act whistleblowers and to clarify the SEC's authority to obtain disgorgement. With respect to disgorgement, the bills introduced to date would explicitly authorize the SEC to seek, and for a federal court to order, disgorgement in SEC enforcement cases. The House bill would allow for a generous 14-year limitations period. The Senate version, by contrast, would also authorize the SEC to seek restitution in enforcement cases within a limitations period far more generous than the five-year limitations period it would apply to disgorgement ([S. 799](#)). The House [passed](#) its disgorgement bill by a vote of 314-95, while the Senate bill awaits further action.

Given that the disgorgement bills have broad bi-partisan support, it is at least remotely possible that Congress could enact such legislation before the Justices decide Liu's case, which, as mentioned, will not be argued until March 2020, and which could be decided as late as June 2020. If a disgorgement law were enacted before a Supreme Court decision, the court could dismiss the case as moot. Several terms ago the court had been presented with the question of whether the government was entitled to a warrant to access Microsoft's non-U.S. servers. The court would eventually order the case [dismissed as moot](#) after Congress enacted the CLOUD Act, which clarified the government's authorities. Even if the court issues an opinion in Liu's case and Congress has not acted at that time, lawmakers could later statutorily reverse a decision that curbs the SEC's authority.

The case is [No. 18-1501](#).

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