

In Unanimous Decision, Supreme Court Faults Major SEC Enforcement Rule

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Government lawyers had argued that disgorgement was not a punishment because the goal is to prevent those who break the law from being unjustly enriched.

The U.S. Supreme Court put sharp new limits on a favorite tool used by securities regulators to recoup money from people found to have violated federal laws.

The unanimous ruling found that disgorgement is essentially a penalty and is thus bound by the five-year statute of limitations already in place for any "civil fine, penalty or forfeiture".

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But in delivering the opinion of the court, Justice Sonia Sotomayor said SEC disgorgement "bears all the hallmarks of a penalty" for which a 5-year statute of limitations applies: "It is imposed as a outcome of violating a public law and it is meant to deter, not to compensate".

The high court took on the issue of the SEC's disgorgement policy as a result of the SEC's legal action against Charles R. *Kokesh*, which began in October 2009. The agency collected more than \$4 billion in disgorgement actions and other penalties in the 2016 fiscal year. Some \$29.2 million of the disgorgement was charged against activities predating the inception of the 5-year statute of limitations. The limitations period will also change the dynamics of the settlement process, as potential defendants will be facing far less risk exposure and the division will have far less leverage. The First, Tenth, and D.C. Circuits were of the opinion that the statute did not apply because disgorgements were not a penalty. Laroe, Sherman's investor, filed to intervene when the court of appeals remanded the case.

"Allowing the SEC to pursue stale claims would actually weaken the enforcement of the securities laws", the Cato Institute said in its brief.

The 10th Circuit had said disgorgement was not a penalty and therefore not subject to the statute of limitations.

The Government's primary argument against categorizing disgorgement as a penalty was that SEC disgorgement is merely remedial and returns the defendant to the position he would

have operated prior to the violation. The power of such authorities was shrunken down so much so that they have an even more restricted time to recover ill-gotten profits.