January 17, 2017

U.S. Supreme Court to Review Whether Statute of Limitations Applies to SEC Disgorgement Claims

On January 13, 2017, the Supreme Court granted certiorari in *Kokesh* v. *Securities and Exchange Commission* (U.S. Jan. 13, 2017) (No. 16-529) to determine whether disgorgement claims are subject to the five-year statute of limitations applicable to enforcement proceedings seeking civil penalties. The decision would resolve a split between the Tenth Circuit, which held in *Kokesh* that the five-year limitations period does not apply, and the Eleventh Circuit, which has held that it does.

Notably, courts, including the Eleventh Circuit, have held that there is no statute of limitations for injunctive and other equitable relief. The law has, until now, been mixed as to whether disgorgement is a form of equitable relief immune from the five-year statute of limitations.

Relevant Background

SEC proceedings are governed by 28 U.S.C. § 2462, which provides that "an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued." The catch-all statute of limitations has also been applied to certain other regulatory agencies, such as the Commodities and Futures Trading Commission ("CFTC"), and Federal Energy Regulatory Commission ("FERC"), as well as the SEC.

In *Gabelli* v. *Securities and Exchange Commission*, 133 S. Ct. 1216 (2013), the Supreme Court held that, under § 2462, enforcement actions seeking civil penalties must be brought within five years from the date when the defendant's allegedly fraudulent conduct occurs, and not when the fraud is discovered. *Kokesh* addresses a question left open by *Gabelli*: whether claims for disgorgement are subject to the same rule. *See* 133 S. Ct. at 1220 n.1.

The Split Between the Tenth and Eleventh Circuits[1]

Last year, in *Securities and Exchange Commission* v. *Graham*, 823 F.3d 1357, 1363 (11th Cir. 2016), the Eleventh Circuit held that a claim for disgorgement is "an action, suit or proceeding for . . . forfeiture"

[1] In opinions that pre-dated the Supreme Court's decision in *Gabelli*, the First and D.C. Circuits have held, like the Tenth Circuit, that the five-year limitations period does not apply to actions for disgorgement. *See Riordan* v. *SEC*, 627 F.3d 1230, 1234 (D.C. Cir. 2010); *SEC* v. *Tambone*, 550 F.3d 106, 148 (1st Cir. 2008).

Since *Gabelli*, at least two district courts in the Second Circuit have held that § 2462 does not apply to disgorgement claims. *See SEC* v. *Ahmed*, No. 3:15cv675 (JBA), 2016 WL 7197359, at *5 (D. Conn. Dec. 8, 2016); *SEC* v. *Saltsman*, No. 07-CV-4370 (NGG), 2016 WL 4136829, at *24-29 (E.D.N.Y. Aug. 2, 2016).

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within the meaning of § 2462 and subject to its five-year statute of limitations. The court reasoned that, under their ordinary meaning, there is "no meaningful difference in the definitions of disgorgement and forfeiture." The court interpreted both concepts to apply to losing or being forced to turn over property because of a crime or wrongdoing. Alternatively, the court found that disgorgement "can be considered a subset of forfeiture" because disgorgement "only includes direct proceeds from wrongdoing," whereas "forfeiture can include both ill-gotten gains and any additional profit on those ill-gotten gains (i.e., secondary profits)." It therefore concluded that "for the purposes of § 2462 the remedy of disgorgement is a 'forfeiture,' and § 2462's statute of limitations applies." (Our client alert on *Graham* can be found here.)

More recently, in *Securities and Exchange Commission* v. *Kokesh*, 834 F.3d 1158 (10th Cir. 2016), the Tenth Circuit disagreed with the Eleventh Circuit and adopted a narrower interpretation of "forfeiture" as used in § 2462. Specifically, the Tenth Circuit viewed the term "forfeiture" in § 2462 as denoting civil forfeitures, which historically referred to "actions against property that either facilitated or was acquired as a result of criminal activity." The court found that, although "some [modern] federal forfeiture statutes have been expanded to include disgorgement-type remedies," the meaning of the word "forfeiture" did not encompass the disgorgement of ill-gotten gains when § 2462 was enacted. Moreover, the court explained that "forfeitures," "civil fines" and "penalties," all are "undoubtedly punitive." By contrast, following Tenth Circuit precedent, the court found that disgorgement is "remedial" and not intended to "inflict punishment." The court likewise held that "disgorgement is not a penalty under § 2462."

Analysis

If the Supreme Court decides that § 2462 applies to disgorgement claims, following the five-year statute of limitations would provide individuals and companies facing enforcement actions greater certainty as to the potential liability. Moreover, in some cases, the five-year limitations period would curtail the monetary value of disgorgement remedies available to the SEC and other regulatory agencies, or result in disgorgement being unavailable entirely. For example, in *Kokesh*, the district court entered a $34.9 million disgorgement order based on securities-law violations dating back to 1995. The SEC did not bring charges until 2009. Under the five-year statute of limitations, the amount of disgorgement would have been limited to $5 million, representing a fraction of the district court's judgment.

We currently expect the Supreme Court to hear oral argument in *Kokesh* by the spring, and issue an opinion by the end of June.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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