No. 16-529

In the Supreme Court of the United States

CHARLES R. KOKESH,

Petitioner,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF FOR THE AMERICAN INVESTMENT COUNCIL AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF *AMICUS CURIAE*[1]

The American Investment Council ("AIC") is an advocacy, communications, and research organization devoted to advancing access to capital, job creation, retirement security, innovation, and economic growth in the United States by promoting responsible long-term investment. Formerly known as the Private Equity Growth Capital Council, the AIC was established in 2007, and its members include the world's leading private equity and growth capital firms. The AIC's members are united by their commitment to growing and strengthening the businesses in which they invest. Pursuant to its mission, the AIC develops, analyzes, and distributes information about the private equity and growth capital industry and its contributions to the U.S. and global economy. The AIC advocates for sound public policies before the Securities and Exchange Commission ("SEC"), Congress, and the courts, including by submitting amicus curiae briefs in cases raising legal issues important to the private investment industry.

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1 No counsel for a party authored this brief in whole or in part, and no entity or person, aside from *amicus curiae*, its members, and its counsel, made a monetary contribution intended to fund the preparation or submission of this brief. All parties to this matter have consented to submission of this brief.

The issue presented in this case—whether the five-year statute of limitations period imposed by 28 U.S.C. § 2462 for "an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture" includes disgorgement actions brought by the SEC—is of particular importance to the AIC and its members. Private equity funds and their portfolio companies are subject to extensive regulations under the federal securities laws. In order to conduct business responsibly and make appropriate investments on behalf of their investors, AIC members have an interest in repose and require certainty about the potential liabilities that they and their portfolio companies may face in the future. The applicability of 28 U.S.C. § 2462 to the SEC's disgorgement actions promotes that certainty.

Therefore, the AIC respectfully submits that the Circuit Court's decision should be reversed, as it grants the SEC inappropriately expansive powers to extract "fine[s], penalt[ies], and forfeiture[s]" in contravention to 28 U.S.C. § 2462 and is inconsistent with the Court's decision in *Gabelli v. SEC*, 133 S. Ct. 1216 (2013). Moreover, because the Circuit Court's decision would give the SEC the power to extract punitive disgorgement against a party for conduct no matter how far in the past, it also upsets private parties' settled expectations and creates potentially chilling uncertainty as to the finality of transactions.

INTRODUCTION AND SUMMARY OF THE ARGUMENT

Pursuant to 28 U.S.C. § 2462, "an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture" is subject to a five-year statute of limitations period. Four years ago, in *Gabelli v. SEC*, 133 S. Ct. 1216 (2013), this Court addressed the question of whether this limitations period ran from the date the defendant's conduct occurred, or whether—as the SEC argued—the limitations period began at some later, undefined date when the SEC "discovered" the underlying conduct. In a unanimous opinion, the Court rejected the SEC's argument, emphasizing that the SEC's reading of § 2462 would violate the core purpose of statutes of limitations: to provide certainty that parties will not be liable for stale claims, particularly where the evidence needed to prove such claims may no longer exist. *Gabelli*, 133 S. Ct. at 1221.

In *Gabelli*, the Court recognized that where the plaintiff was a "defrauded victim" herself, the "discovery rule" would apply. *Id.* at 1221. However, it refused to extend that exception to SEC enforcement actions, where the SEC's role is not to ensure that the "injured receive recompense," but to "punish[] and label defendants [as] wrongdoers" and to deter others from violating the law. *Id.* at 1223. In this context—where the SEC is neither a victim nor standing in the shoes of a victim, but rather "a prosecutor seeking penalties"—the Court recognized the necessity of time limits so as to create certainty and avoid exposing parties "to Government enforcement action not only for five years after their misdeeds, but for an additional uncertain period into the future." *Id.* at 1223-24.

So it is here. The SEC does not exercise its disgorgement powers solely, or even primarily, to recover a loss to itself or to injured victims. Rather, "the SEC's purpose in seeking disgorgement of ill-gotten profits has always been deterrence," not the compensation of victims. *Official Comm. of Unsecured Creditors of WorldCom, Inc. v. SEC*, 467 F.3d 73, 83 (2d Cir. 2006) (Sotomayor, J.). In recent years, disgorgement has proven to be an ever-more powerful weapon in the SEC's enforcement arsenal. It has been utilized at a rate that outstrips the civil penalties that the SEC also levies. Consistent with its punitive character, the SEC's disgorgement power is not limited in the manner that traditional equitable remedies brought by private plaintiffs are limited: the SEC need not (1) identify any victims at all (indeed, no victims need even exist), (2) trace the disgorged funds to any unlawfully-obtained assets, or (3) prove that the defendant ever actually possessed the assets the SEC is requiring them to disgorge. Moreover, because the true purpose of its disgorgement power is not to compensate victims, but rather to deter, the SEC has discretion to determine how to dispose of disgorged assets, and it frequently transfers those assets to the U.S. Treasury and not to any victim at all.

To allow the SEC to wield this extraordinary power for conduct that occurred at "any distance of time"—not to compensate victims, but "to punish, and label defendants [as] wrongdoers," *Gabelli*, 133 S. Ct. at 1223 (citation omitted)—would be detrimental to the just and timely enforcement of our securities laws and the functioning of our nation's securities markets. Allowing the SEC to punish aged conduct would undermine faith in those markets by unsettling parties' expectations about the finality of their transactions—including transactions which conformed to market standards at the time—increasing uncertainty as to counterparties' future liabilities, and raising the specter of open-ended prosecution for past conduct. The SEC would be empowered to present market participants with a Hobson's choice: pay whatever penalty the SEC seeks, or face monetary sanctions (including disgorgement) for conduct going back as far as the SEC desires. The SEC could threaten that if the defendant failed to "pay up," it would face a damaging, costly, and lengthy investigation extending back years, including into conduct as to which the exonerating or mitigating evidence had vanished due to the passage of time. Just as with sanctions formally styled "penalties," the disgorgement power the SEC exercises allows it to extract a "fine, penalty, or forfeiture" and should, therefore, be constrained by 28 U.S.C. § 2462's five-year limitations period.

ARGUMENT

I. 28 U.S.C. § 2462 PROTECTS PARTIES' SETTLED EXPECTATIONS AGAINST GOVERNMENTAL ENFORCEMENT ACTIONS SEEKING TO PUNISH CONDUCT FROM TIME IMMEMORIAL.

In refusing to weaken the five-year limitations period in 28 U.S.C. § 2462, the Court's opinion in *Gabelli* reaffirmed Chief Justice Marshall's warning that "it 'would be utterly repugnant to the genius of our laws' if actions for penalties could 'be brought at any distance of time.'" S. Ct. at 1223 (quoting *Adams v. Woods*, 2 Cranch 336, 342 (1805)). The Court cautioned about the potential abuses and disruptions that would occur if "defendants [were] exposed to Government enforcement action not only for five years after their misdeeds, but for an additional uncertain period into the future." *Id.* at 1223.

For one, if the government could hold defendants liable for events that have long since passed, their settled expectations would be disrupted. Statutes of limitations serve a salutary purpose. As the Court explained, "even wrongdoers are entitled to assume that their sins may be forgotten," and defendants' ability to do so lends "security and stability to human affairs." *Id.* at 1221 (citations omitted). Further, absent appropriate limitations periods, targets of government enforcement actions would be disabled from defending themselves, being "surprise[d] through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared." *Id.* (quoting *Order of R.R. Telegraphers v. Ry. Express Agency, Inc.*, 321 U.S. 342, 348-49 (1944)). Thus, by interpreting § 2462 to bar the SEC's claims, the Supreme Court "set[] a fixed date when exposure to the specified Government enforcement efforts ends, advancing 'the basic policies of all limitations provisions: repose, elimination of stale claims, and certainty about a plaintiff's opportunity for recovery and a defendant's potential liabilities.'" *Id.* (quoting *Rotella v. Wood*, 528 U.S. 549, 555 (2000)).

The *Gabelli* decision highlighted the difference between government enforcement actions to promote adherence to law and private actions to compensate injured victims. The Court explained that a "discovery rule" lengthening the limitations period may be appropriate for suits by *victims,* who generally "do not live in a state of constant investigation" and therefore may delay in discovering a fraud perpetrated against them. *Id.* at 1222. In contrast, "a central 'mission' of the [SEC] is to 'investigat[e] potential violations of the federal securities laws,'" and "it has many legal tools at hand to aid in that pursuit," including powers to compel the production of information, award whistleblowers, and enter into cooperation agreements. *Id.* (quoting SEC, Div. of Enforcement, *Enforcement Manual* (2012)).

Moreover, the SEC "is not only a different kind of plaintiff, it seeks a different kind of relief." *Id.* at 1223. When victims bring suit, they seek compensation from a defendant to "restore the status quo" that existed prior to their injury, and extending the statute of limitations in those cases may help to "ensure that the injured receive [that] recompense." *Id.* (citations omitted). However, the purpose of governmental enforcement actions necessarily goes beyond "ensur[ing] that the injured receive recompense." They are designed to deter and to "punish, and label defendants wrongdoers." *Id.*

In short, § 2462 rests upon fundamental concerns underlying all statutes of limitations, including the need to respect settled expectations and the loss of evidence. As used by the SEC, disgorgement goes "beyond compensation," serving primarily as a tool to punish wrongdoing—not to return victims to their status quo. It is therefore precisely the type of "fine, penalty, or forfeiture" that concerned the Court in *Gabelli*.

II. THE GOVERNMENT'S POSITION WOULD GIVE THE SEC VIRTUALLY LIMITLESS POWER TO EXTRACT PERPETUAL FINES, PENALTIES, OR FORFEITURES.

The SEC's disgorgement power is an extraordinary punitive remedy in the character of a "fine, penalty, or forfeiture," and the SEC's interpretation of § 2462 would allow it to extend the use of that remedy back through time, gutting *Gabelli's* exhortations against perpetual penalties. The SEC's position should therefore be rejected.

A. SEC Disgorgement Is an Extraordinary Punitive Power Akin to a "Fine, Penalty, or Forfeiture" and Is Not Subject to Limits on Traditional Restitution Remedies.

Courts have repeatedly recognized that "the SEC's purpose in seeking disgorgement of ill-gotten profits has always been deterrence," not the compensation of victims. *Official Comm. of Unsecured Creditors of WorldCom, Inc. v. SEC*, 467 F.3d 73, 83 (2d Cir. 2006) (Sotomayor, J.); *see also, e.g.*, *SEC v. Frohling*, __ F.3d __, No. 13-3191, 2016 WL 7093925, at *4 (2d Cir. Dec. 6, 2016) ("The 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.") (quotation marks and citation omitted); *SEC v. Commonwealth Chem. Sec., Inc.*, 574 F.2d 90 (2d Cir. 1978) (Friendly, J.) ("[T]he primary purpose of disgorgement is not to compensate investors.").

Likewise, the SEC itself has repeatedly acknowledged that its disgorgement power is not "intended to make investors whole," but rather "to deprive the wrongdoer of their ill-gotten gain." SEC, *Report Pursuant to Section 308(C) of the*

Sarbanes Oxley Act of 2002, at 3 n.2 (2003). In fact, the SEC has consistently relied on this point throughout decades of litigation—including to argue that investors have no standing to challenge an SEC decision not to distribute disgorged funds to victims. *See, e.g.*, Br. of SEC at *24, *SEC v. Custable*, 796 F.3d 653 (7th Cir. 2015) (No. 15-1442), 2015 WL 3383280 ("The purpose of disgorgement . . . is depriving wrongdoers of their ill-gotten gains—*not* satisfying creditors or repaying investors.") (quotation marks and citation omitted); Br. of SEC at *4, *Martin v. SEC*, 734 F.3d 169 (2d Cir. 2013) (No. 11-3011), 2012 WL 8126225 ("Compensation to injured investors is 'a distinctly secondary goal.'") (citation omitted); *see also* Br. of SEC at *41, *SEC v. Smyth*, 420 F.3d 1225 (11th Cir. 2005) (No. 04-11985), 2004 WL 4802488 ("In contrast to the compensatory purpose of damages in private actions, . . . the purpose of disgorgement in [SEC] actions is to prevent unjust enrichment and to deter future violations."); Br. of SEC at *13, *SEC v. AMX Int'l, Inc.*, 7 F.3d 71 (5th Cir. 1993) (No. 92-1376), 1992 WL 12127856 ("[T]he purpose [of disgorgement] is to remove ill-gotten gains from wrongdoers, and deter future violations."); *see also* Press Release, SEC, Enforcement Director Andrew J. Ceresney to Leave SEC (Dec. 8, 2016) (referring to $13.8 billion in disgorgements and civil penalties as "monetary sanctions").[2]

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[2] https://www.sec.gov/news/pressrelease/2016-259.html.

Consistent with this punitive and non-compensatory intent, when the SEC sues for disgorgement, it does not stand in the shoes of an injured party, subjecting itself to the burdens and defenses of a person in that position. Rather, the SEC's disgorgement power is designed for law enforcement, and is thus unbound by many of the traditional limits of equitable actions for restitution to which injured private parties are subject.

No tracing required. For instance, "[f]or restitution to lie in equity, the action generally must seek not to impose personal liability on the defendant, but to restore to the plaintiff particular funds or property in the defendant's possession." *Great-W. Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 214 (2002). Thus, when seeking equitable restitution, a plaintiff may only recover money or property that can "*clearly be traced* to particular funds or property" possessed by the defendant. *Id.* at 213 (emphasis added); *see also Restatement (3d) of Restitution & Unjust Enrichment* § 51, cmt. e (Am. Law Inst. 2011) (accounting and traditional disgorgement require showing "what portion of the defendant's assets or income is properly attributable to the underlying wrong to the claimant"); *id.* § 55(1) (constructive trust allows recovery of "identifiable property . . . and its traceable product"). In contrast, the SEC's power to disgorge is "not limited to specific assets traced back to a violation." *SEC v. Quan*, 817 F.3d 583, 594 (8th Cir. 2016); *see also SEC v. Contorinis*, 743 F.3d 296, 303 n.3 (2d Cir. 2014) ("[W]e have long deemed specific tracing unnecessary in ordering disgorgement for securities fraud.") Because the primary goal of SEC disgorgements is to deter future violations, not to return assets to victims, there need not be a precise connection between the disgorged assets and any victims' loss.

No need to identify any victims. In contrast to a traditional restitution action—which would be brought by a party that suffered a loss, or someone acting directly on their behalf—the SEC does not need to identify any specific victim who suffered a loss, or even that there are victims at all, when seeking disgorgement. *See, e.g.*, *FTC v. Bronson Partners, LLC*, 654 F.3d 359, 373 (2d Cir. 2011) ("[A] regulatory agency seeking disgorgement need not identify specific victims to whom payment is due . . . , as it would be required to do if seeking to impose a constructive trust."). For example, the SEC has disgorged millions of dollars from defendants for violations of the Foreign Corrupt Practices Act without even alleging that anyone was harmed by those violations. *See, e.g.*, *In the Matter of Total, S.A.*, Exch. Act Release No. 39654 (May 29, 2013) (disgorging $153 million for FCPA violation); *In the Matter of General Cable Corp.*, Exch. Act Release No. 79703 (Dec. 29, 2016) ($51 million disgorgement). Likewise, the SEC has ordered disgorgements in insider trading cases without alleging that investors lost money due to the relevant violations. *See, e.g.*, *In the Matter of Artis Capital Mgmt., L.P. & Michael W. Harden*, Inv. Advisers Act Release No. 4550 (Oct. 13, 2016)

($5.1 million disgorgement amount for insider trading).

Funds need not be returned to victims. The SEC need never return disgorged funds to victims, either because the SEC has not identified any individual who has suffered a harm, or because the SEC determines that, in its opinion, the cost of distributing the funds to victims is too high. *See* 17 C.F.R. § 201.1102(b); *see also, e.g.*, *Total*, Exch. Act Release No. 39654, at 11 (disgorged amount paid to "the United States Treasury"); *Artis Capital*, Inv. Advisors Release No. 4550, at 9 (same); *In the Matter of Itg Inc. & Alternet Sec., Inc.*, Admin. Proc. File No. 3-16742, Sec. Act Release No. 9887 (Aug. 12, 2015) (ordering $2 million disgorgement to the Treasury for misuse of customer information). Indeed, the SEC may establish a Fair Fund to compensate victims with disgorged amounts only if it "also assess[es] a civil money penalty." 17 C.F.R. § 201.1100.[3] As a result, many of the funds disgorged by the SEC are never used to compensate victims; for instance, between 2013 and 2015, the SEC collected $6.8 billion in disgorgement and penalties, but only distributed $833 million in Fair Funds to investors. SEC, *FY 2015 Annual*

[3] Civil monetary penalties, like disgorgements, may be distributed to victims, 15 U.S.C. § 7246(a), which provides further evidence that disgorgements are not intended to be any more compensatory or any less punitive than civil penalties.

Performance Report, at 40-41, https://www.sec.gov/about/reports/sec-fy2015-fy2017-annual-performance.pdf.

Defendants not necessarily enriched. Further, the SEC can disgorge funds from defendants who were not themselves enriched. Thus, the SEC requires insider traders to disgorge profits realized by others as a result of the traders' unlawful trading or tipping. *See, e.g.*, *Contorinis*, 743 F.3d at 301-02 (holding insider trader responsible to disgorge profits he did not personally realize); *SEC v. Warde*, 151 F.3d 42, 49 (2d Cir. 1998) ("A tippee's gains are attributable to the tipper, regardless whether benefit accrues to the tipper."). The SEC can also require wrongdoers to disgorge the profits of their collaborators in a fraud, irrespective of whether the defendant ever possessed those profits personally. *See, e.g.*, *SEC v. Pentagon Capital Mgmt. PLC*, 725 F.3d 279, 288 (2d Cir. 2013) (finding "no statutory requirement that a disgorgement award be measured as to each individual defendant" and that "joint and several liability for combined profits on collaborating . . . parties is appropriate") (citation and quotation marks omitted); *SEC v. Monterosso*, 756 F.3d 1326, 1337-38 (11th Cir. 2014) ("'[A] personal financial benefit' is not a 'prerequisite for joint and several liability.'") (per curiam) (quoting *SEC v. Platforms Wireless Int'l Corp.*, 617 F.3d 1072, 1098 (9th Cir. 2010)).

Laches may not apply. Finally, restitution and other equitable actions available to private victims respect the settled expectations of the wrongdoer and victim alike through the principle of laches. *See Holmberg v. Armbrecht*, 327 U.S. 392, 396 (1946); *see also Halstead v. Grinnan*, 152 U.S. 412, 416 (1894) (laches "prevents the breaking up of relations and situations long acquiesced in"). Therefore, the private law honors the finality of transactions and provides "security and stability to human affairs," *Gabelli*, 133 S. Ct. at 1221, by treating as settled the allocation of rights that have been openly and knowingly acquiesced to by the parties. By contrast, the SEC claims its disgorgement power is not subject to laches. *See, e.g.*, Br. of SEC at *19-20, *SEC v. Silverman*, 328 F. App'x 601 (11th Cir. 2009) (No. 08-16710-FF), 2009 WL 1674430. Thus, under the SEC's theories, the SEC could reach back far in time to strip a party of property which it believed to be ill-gotten even if the party that parted with the property knowingly acquiesced to its taking years earlier. Indeed, under its theories, the SEC could pursue disgorgement and unsettle transactions even if the putatively injured victim did not want the property, knowingly disclaimed any interest in the property, or simply did not believe it was victimized.

Thus, the power the SEC claims to exercise in this case goes far beyond what it would have been permitted to use if it were standing in the shoes of an injured victim. Its function is not "recompense" of an "injured victim"; rather, it is law enforcement.

Gabelli, 133 S. Ct. at 1224. Just like the remedy styled a penalty in *Gabelli*, disgorgement functions as a "fine, penalty or forfeiture" and is subject to the limitations imposed on fines, penalties, and forfeitures. *See supra* at 7-8; *see also Reynolds Metals Co. v. Ellis*, 202 F.3d 1246, 1248 (9th Cir. 2000) ("[I]t is clear that a court must look to the substance of the remedy sought, . . . rather than the label placed on that remedy.") (quotation marks and citation omitted).

B. Left Unchecked by § 2462, the SEC's Disgorgement Power Is Subject to Governmental Overreach and Would Allow the SEC to Extract Enormous Penalties in Perpetuity.

Even when constrained by a five-year statute of limitations, the SEC's existing disgorgement power—unchecked by traditional limitations on equitable restitution—is an extraordinarily punitive remedy. The breadth of the disgorgement power has allowed the SEC to disgorge enormous sums from individual defendants, often dwarfing the civil penalties that are applied. *See, e.g.*, *SEC v. Wyly*, No. 10-05760 (S.D.N.Y. Feb. 26, 2015) ($100 million disgorgement to Treasury with no penalty); *SEC v. Mantria Corp.*, No. 09-02676, 2011 WL 3439348 (D. Colo. Aug. 5, 2011) ($37 million disgorgement to the SEC with a $500,000 penalty).

Taken in the aggregate, the SEC has collected billions of dollars in disgorged funds annually, and in recent years, the SEC's total disgorgement awards have been more than twice the total amounts of its civil penalties. *See, e.g.*, *Select SEC and Market Data Fiscal 2016* (Jan. 18, 2017) at 2 (reporting disgorgement of $2.8 billion and civil penalties of $1.3 billion for fiscal year 2016);[4] *Select SEC and Market Data Fiscal 2015* (Feb. 5, 2016) at 2 (reporting disgorgement of $3.0 billion and civil penalties of $1.2 billion for fiscal year 2015).[5] Moreover, in the years since *Gabelli*, the growth in disgorgement awards has outstripped the growth of civil monetary penalties, which grew at over 24% and 9%, respectively, between 2013 and 2016.[6]

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4 https://www.sec.gov/reportspubs/select-sec-and-market-data/secstats2016.pdf.

5 https://www.sec.gov/reportspubs/select-sec-and-market-data/secstats2015.pdf.

6 *Compare Select SEC and Market Data 2013* (Feb. 7, 2014) at 2, https://www.sec.gov/reportspubs/select-sec-and-market-data/secstats2013.pdf (reporting disgorgement of $2.257 billion and penalties of $1.167 billion) *with Select SEC and Market Data 2016* (Jan. 18, 2017) at 2, https://www.sec.gov/reportspubs/select-sec-and-market-data/secstats2016.pdf (reporting disgorgement of $2.809 billion and penalties of $1.273 billion). By contrast, a comparison of fiscal years 2009 and 2012—the years between the 2008 financial crises and the *Gabelli* decision—reveal a threefold increase in penalty awards, while disgorgement stayed flat. *Compare Select SEC and Market Data 2009* (Nov. 16, 2009) at 2, https://www.sec.gov/about/secstats2009.pdf (disgorgement of $2.09 billion and penalties of $345 million) *with Select SEC and Market Data 2012* (Feb. 6, 2013) at 2,

If the Court were to hold that 28 U.S.C. § 2462 does not apply to SEC disgorgement actions at all, this already extraordinary power would be rendered even more extraordinary, giving the SEC the power to pursue putative wrongdoers' profits and to unsettle transactions going back decades or more, simply because it saw a law enforcement interest in doing so. Such a result would not only be inimical to what Chief Justice Marshall described as the "genius of our laws," *Adams v. Woods*, 2 Cranch 336, 342 (1805), but it would effectively gut *Gabelli* by allowing the government to investigate (or threaten to investigate) and sue on aged conduct to which the parties have long since acquiesced.

The SEC itself has acknowledged that the federal securities laws are at their most effective and fair when administrated quickly. Delay undermines both the deterrence value and the public perception that enforcement is fair. *See Strengthening the SEC's Vital Enforcement Responsibilities: Hearing Before the Subcomm. on Sec., Ins. & Inv. of the Senate Comm. on Banking, Housing & Urban Affairs*, 111th Cong. 46 (2009) (former Director of the SEC's Enforcement Division noting that "[a] sense of urgency is critical. If cases are unreasonably delayed, if there is a wide gap between conduct and atonement, then the message

https://www.sec.gov/about/secstats2012.pdf (disgorgement of $2.083 billion and penalties of $1.021 billion).

[] to the investing public that the SEC is vigilant is . . . diluted."); *see also* SEC Div. of Enforcement, *Enforcement Manual* §3.1.1 (2016), https://www.sec.gov/divisions/enforce/enforcementmanual.pdf ("Swift investigations generally are most effective and enhance the public interest.").

The rule the SEC now proposes, however, would not only dilute the perceptions that the securities laws are administered fairly, but would give the government overwhelming leverage to force putative defendants to settle claims as to which they have good defenses, or otherwise settle on unfair terms. The SEC could reach back and use the threat of disgorgement to extract settlements with higher penalties or more serious charges, or alternatively agree to lower penalties in exchange for higher disgorgement amounts. The SEC could also use this power simply to extract monetary sanctions for long-past conduct. Few defendants would be able to resist an SEC settlement related to more recent conduct, even if they never violated the law or had good and viable defenses, if the alternative was an open-ended SEC investigation into their entire operating history. The SEC could simply deliver the message to the intransigent defendant: pay, or else.

And, because the SEC—unlike the threatened private party—has as its "central 'mission'" the task of collecting and maintaining (often in secret) evidence of potential securities law violations, *Gabelli*, 133 S. Ct. at 1222, its threat would be real.

The SEC "has many legal tools at hand to aid in that pursuit," including powers to compel the production of information, award whistleblowers, and enter into cooperation agreements. *Id.* ("[E]ven without filing suit, it can subpoena any documents and witnesses it deems relevant . . . ."). It thus would be able to take advantage of the passage of time to bring actions when "evidence has been lost, memories have faded, and witnesses have disappeared." *Id.* at 1221 (quotation marks and citation omitted).

Indeed, under the SEC's theory, without any current or recent violation at all, it could reach back indefinitely to punish conduct that at one time was acquiesced in or was widely known and accepted but later fell out of favor, simply because it wanted to or felt media or political pressure to do so. Courts have warned against just such a possibility. *See, e.g.*, *Morrison v. Olson*, 487 U.S. 654, 728 (1988) (Scalia, J., dissenting) ("Therein is the most dangerous power of the prosecutor: that he will pick people that he thinks he should get, rather than cases that need to be prosecuted.") (citation omitted); *see also FDIC v. Maxxam, Inc.*, 523 F.3d 566, 571-573 (5th Cir. 2008) (describing intense political pressure placed on the FDIC to file an action against the executive of a failed savings-and-loan).

Even setting aside the fairness of such an approach to defendants, the SEC's proposed enforcement power would not be to the benefit of investors. Market participants would be perpetually uncertain as to whether the SEC would reconsider the validity of specific market practices years after the fact. Indeed, *Gabelli* is an example of the SEC undertaking just such a retroactive determination. That case alleged illegal "market timing" of mutual funds, *Gabelli*, 133 S. Ct. at 1219, which had been a widespread practice that the SEC had previously chosen not to prosecute.[7] *See* Mark T. Roche et al., *Will the SEC Have Forever to Pursue Securities Violations? SEC v. Gabelli*, 44 Sec. Reg. & L. Rep. 1415, at 2 n.3 (2012) (quoting SEC's stipulation in *SEC v. O'Meally*, Trial Tr. at 2186-87, No. 06-06483 (S.D.N.Y. Jan. 9, 2012), ECF No. 185, that "[b]eginning in the mid 1990's, the SEC knew about the practice of market timing in mutual funds, and the decision was to let the marketplace regulate itself"); *see also Upton v. SEC*, 75 F.3d 92, 98 (2d Cir. 1996) (vacating SEC

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[7] However, following an announcement that the New York State Attorney General was investigating the practice, the SEC changed its mind, bringing investigations and ultimately a number of actions against alleged market timers many years after the fact. *See* Mark T. Roche et al., *Will the SEC Have Forever to Pursue Securities Violations? SEC v. Gabelli*, 44 Sec. Reg. & L. Rep. 1415, at 2 n.3 (July 23, 2012); *see also In the Matter of Bear, Stearns & Co., Inc.*, Sec. Act Release No. 8668 (Mar. 16, 2006) (settling administrative proceeding concerning market timing practices arising in the late 1990s and early 2000s); *SEC v. Pimco Advisors Fund Mgmt. LLC*, 341 F. Supp. 2d 454, 461 (S.D.N.Y. 2004) (refusing to dismiss SEC suit for market timing violations).

order because the SEC knew the relevant practice "well before the underlying events in this action took place and yet did not publicly condemn it").

More recently, the SEC has turned its attention to conduct in the private equity industry originating more than five years ago. In 2016, the SEC's then-Director of Enforcement tacitly acknowledged this change of focus when dismissing arguments that "it is unfair to charge advisers for disclosure failures in fund organizational documents that were drafted long before the SEC began its focus on private equity" and, indeed, before the 2010 Dodd-Frank Act even required such advisers "to register" with the SEC. Andrew Ceresney, Director of Enforcement, *Securities Enforcement Forum West 2016 Keynote Address: Private Equity Enforcement* (May 21, 2016).[8] The Enforcement Director provided examples of recent SEC actions against private equity firms totaling \$59.2 million in disgorgement and \$22.3 million in civil penalties, which included conduct well outside the five-year period. *See id.* At the same time, the SEC acknowledged that affected investors could have but chose not to seek relief and recognized that those firms, in fact, provided benefits to their (putatively harmed) investors. *See id.* n.8 (citing example); *see also id.* ("Many investors have invested in private equity based on their

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[8] https://www.sec.gov/news/speech/private-equity-enforcement.html.

expectation that private equity returns would be uncorrelated with and/or exceed public equity market returns, and in certain cases, they have been proven correct.”).

But under the SEC’s theory, the SEC would have the discretion to seek disgorgement not just for conduct in the past five years but as far back as it wished—even if investors were unharmed by the charged conduct (and, indeed, may have believed they were benefited by it). That authority would confer extraordinary powers on the SEC, permitting it to extort settlements and effectively ending the benefit of repose. That power is particularly concerning in the private equity context where the nature of investments are long-term and liability may turn, in part, on disclosures to investors long ago—including those conveyed orally or in emails. *See id.* n.8 (settled action concerning disclosures dating back to 1997). Given this passage of time, the deterioration of evidence would significantly handicap firms in their ability to defend against an SEC action. The application of the *Gabelli* doctrine to SEC disgorgement actions protects market participants by permitting them to invest free from the fear that the government will reach back in time to unsettle transactions on which they relied and as to which there may be no injured party or no one entitled to recompense.

Of course, the rights of injured parties should be respected, and the government is entitled to change its enforcement priorities over time, for example, to reflect new threats to the securities markets. However, it would not serve those ends to allow the SEC—merely by labeling its practice as equitable disgorgement—to reach back to time immemorial. Rather, this would risk unsettling investors' long-held and relied-upon expectations about any given transactions while simultaneously creating the specter of never-ending liability, harming both the fair administration of the securities laws and the efficient workings of the markets.

CONCLUSION

For the foregoing reasons, the American Investment Council urges the Court to reverse the judgment of the Circuit Court.

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