KILPATRICK TOWNSEND

July 14, 2017

Kokesh v. SEC: The U.S. Supreme Court Limits SEC Disgorgement Powers

and John I. Sanders

Since the 1970s, courts have regularly ordered disgorgement of ill-gotten gains in SEC enforcement proceedings.[1] According to the SEC, this was done as a means to both "deprive . . . defendants of their profits in order to remove any monetary reward for violating" securities laws and "protect the investing public by providing an effective deterrent to future violations."[2] Disgorgement has been one of the SEC's most powerful tools in recent years.[3] Earlier this week, the Supreme Court issued an opinion that significantly limits the SEC's ability to disgorge ill-gotten gains.[4]

The question before the Supreme Court in *Kokesh v. SEC* was whether disgorgement, as it has been used by the SEC, constitutes a "penalty." [5] Under federal law, a 5-year statute of limitations applies to any "action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise."[6] The SEC has long argued that disgorgement does not constitute a "penalty" and, therefore, is not subject to a 5-year statute of limitations. The Supreme Court unanimously rejected the SEC's position by holding that disgorgement constitutes a "penalty." [7] As a result, the SEC will be precluded from collecting ill-gotten gains obtained by the defendant more than five years before the date on which the SEC files its complaint.[8]

In the Kokesh case, the Supreme Court's decision means that the defendant may retain $29.9 million of the $34.9 million in allegedly ill-gotten gains because that amount was received outside of the 5-year state of limitations.[9] The Kokesh decision is also likely to have a significant long-term impact on SEC enforcement proceedings by reducing the leverage the SEC can apply while negotiating settlements.

Paul Foley *is a partner with* ***Kilpatrick Townsend & Stockton****'s Winston-Salem and New York offices.* ***John I. Sanders*** *is an associate based in the firm's Winston-Salem office.*

[1] *SEC* v. *Texas Gulf Sulphur Co.*, 312 F. Supp. 77, 91 (SDNY 1970), aff 'd in part and rev'd in part, 446 F. 2d 1301 (CA2 1971).

[2] *Id*. at 92.

[3] SEC, *SEC Announces Enforcement Results for FY 2016* (Oct. 11, 2016), *available at* https://www.sec.gov/news/pressrelease/2016-212.html (illustrating that the SEC has obtained more than $4 billion in disgorgements and penalties in each of the three most recent fiscal years).

[4] *Kokesh v. SEC*, available at www.supremecourt.gov.

[5] *Id*. ("This case presents the question whether [28 U.S.C.] §2462 applies to claims for disgorgement imposed

as a sanction for violating a federal securities law.").

[6] 28 U.S.C. §2462 (2017).

[7] *Kokesh v. SEC, supra* note 4*, available at* www.supremecourt.gov. ("SEC disgorgement thus bears all the hallmarks of a penalty: It is imposed as a consequence of violating a public law and it is intended to deter, not to compensate.").

[8] *Id*.

[9] *Id*.