

June 1, 2016

## Eleventh Circuit Limits SEC's Ability to Seek Disgorgement and Declaratory Relief in Agency Actions

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### **Holds That Disgorgement and Declaratory Relief Claims Are Subject to 28 U.S.C. § 2462's Five-Year Statute of Limitations**

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#### **SUMMARY**

On May 26, 2016, the United States Court of Appeals for the Eleventh Circuit issued an important decision in *SEC v. Graham*, no. 4:13-cv-110011, holding that SEC claims for disgorgement in civil actions are subject to the five-year statute of limitations on suits to enforce “any civil fine, penalty, or forfeiture” under 28 U.S.C. § 2462. The Court also held that declaratory relief in SEC civil actions is subject to the five-year statute of limitations, but that injunctive relief is not. As a result of this ruling, the SEC’s ability to seek disgorgement and declaratory relief—including in connection with enforcement actions brought under the Securities Act of 1933, the Securities Exchange Act of 1934, and the Foreign Corrupt Practices Act—is substantially circumscribed and limited to putative violations that occur within five years of the initiation of the SEC action.

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#### **BACKGROUND AND DISCUSSION**

*Graham* involved an SEC civil enforcement action against several individual defendants who allegedly violated the registration and anti-fraud provisions of the Securities Act of 1933 and Securities Exchange Act of 1934. The SEC alleged that the defendants sold condominium investments that functioned as

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unregistered securities, and failed to pay the returns that defendants had guaranteed to investors.<sup>1</sup> The SEC sought relief including: (i) a declaration that the defendants violated federal securities laws, (ii) a permanent injunction prohibiting the defendants from future violations of federal securities laws, (iii) disgorgement of all profits from the defendants' alleged violations, (iv) an order that the defendants repatriate any funds held outside the district court's jurisdiction, and (v) a civil monetary penalty.<sup>2</sup>

Several of the defendants moved for summary judgment on the grounds that (i) the condominium sales in question were not governed by the federal securities laws, and (ii) the SEC's claims were barred by 28 U.S.C. § 2462's five-year statute of limitations "for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise," which applies to all actions brought by the United States government, including the SEC.<sup>3</sup> The defendants argued that none of the SEC's claims, filed on January 30, 2013, was timely under § 2462's five-year limitations period, which is triggered on the date on which the last act giving rise to the government's cause of action occurs.<sup>4</sup> The SEC filed a cross-motion for summary judgment.<sup>5</sup>

On May 12, 2014, the district court held that § 2462's five-year statute of limitations applied to all forms of relief sought by the SEC. Rejecting the SEC's argument that the limitations period did not apply to its claims because "the words 'declaratory relief,' 'injunction,' and 'disgorgement' do not appear in § 2462," the district court concluded that the relief requested by the SEC fell within the ambit of § 2462 because "[p]enalties, 'pecuniary or otherwise,' are at the heart of all forms of relief sought."<sup>6</sup> With respect to disgorgement specifically, the district court reasoned that "the disgorgement of all ill-gotten gains realized from the alleged violations of the securities laws—*i.e.*, requiring defendants to relinquish money and property—can truly be regarded as nothing other than a forfeiture (both pecuniary and otherwise), which remedy is expressly covered by § 2462."<sup>7</sup> Finding that the SEC failed to meet its burden of "point[ing] to any act of offering or sale of alleged securities by any of the defendants . . . after January 30, 2008," or within five years of the SEC's commencement of the action on January 30, 2013, the district court dismissed the SEC's claims with prejudice.<sup>8</sup>

On appeal to the Eleventh Circuit, the SEC conceded that § 2462 barred its claim for civil monetary penalties, but challenged the district court's ruling that § 2462 applies to injunctive relief, declaratory

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<sup>1</sup> *SEC v. Graham*, 21 F. Supp. 3d 1300, 1302-03 (S.D. Fla. 2014).

<sup>2</sup> *Id.* at 1304-05.

<sup>3</sup> *Id.* at 1305, 1307-08.

<sup>4</sup> *Id.* at 1305, 1308.

<sup>5</sup> *Id.* at 1301.

<sup>6</sup> *Id.* at 1310.

<sup>7</sup> *Id.* at 1310-11.

<sup>8</sup> *Id.* at 1312, 1316.

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relief, and disgorgement.<sup>9</sup> Strictly construing the statute of limitations in favor of the government as required under established law, the Eleventh Circuit reversed only the district court's holding that the SEC's claim for injunctive relief was barred, and affirmed the district court's holding that the SEC's claims for declaratory relief and disgorgement were barred by § 2462.<sup>10</sup>

Most significantly, the Eleventh Circuit affirmed the district court's holding that § 2462's statute of limitations applies to the SEC's claims for disgorgement, agreeing with the district court that disgorgement constitutes a "forfeiture" as that term is used in the statute. In so holding, the Court rejected the SEC's argument that disgorgement cannot be considered to be forfeiture within the meaning of § 2462 because "disgorgement only includes direct proceeds from wrongdoing, whereas forfeiture can include both ill-gotten gains and any additional profit earned on those ill-gotten gains."<sup>11</sup> The Court reasoned that there is "no indication that in enacting section 2462's widely applicable statute of limitations, Congress meant to adopt the technical definitions . . . the SEC urges over the words' ordinary meanings," "[p]articularly because section 2462 applies to a wide variety of agency actions and contexts."<sup>12</sup> Rather, the Court determined that, for the purposes of § 2462, "there is no meaningful difference in the definitions of disgorgement and forfeiture," and "forfeiture includes disgorgement."<sup>13</sup> Because the Court found that disgorgement is subject to § 2462 as a form of "forfeiture," it declined to reach the defendants' alternative argument that disgorgement is a "penalty" within the meaning of § 2462.<sup>14</sup>

The Eleventh Circuit similarly agreed with the district court's conclusion that declaratory relief "is backward-looking and thus would operate as a penalty under § 2462."<sup>15</sup> The Court was "unpersuaded" by the SEC's argument that declaratory relief should be exempted from § 2462 "because the SEC may use findings of past violations of securities laws to obtain other remedies."<sup>16</sup> The Court did, however, reject the district court's conclusion that the injunctive relief sought by the SEC was a penalty within the ambit of § 2462, citing Eleventh Circuit precedent expressly holding that "[s]ection 2462 does not apply to

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<sup>9</sup> *SEC v. Graham*, No. 414-13562, slip op. at 11-12 (11th Cir. May 26, 2016) ("Op.").

<sup>10</sup> *See id.* at 14-15. The SEC had also challenged the district court's conclusion that § 2462 is jurisdictional in nature, but the Eleventh Circuit declined to reach the question of whether "§ 2462's time bar is a jurisdictional requirement or only an affirmative defense," finding that it had no impact on the Court's conclusion that the SEC's claims for declaratory relief and disgorgement were barred by § 2462's five-year limitations period, while its claim for injunctive relief was not. *Id.* at 4 n.1.

<sup>11</sup> *Id.* at 13.

<sup>12</sup> *Id.* at 14.

<sup>13</sup> *Id.* at 12, 14.

<sup>14</sup> *Id.* at 13 n.3.

<sup>15</sup> *Id.* at 9.

<sup>16</sup> *Id.* at 10.

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equitable remedies.”<sup>17</sup> The Court noted that, even absent binding precedent, § 2462 would not apply to injunctive relief because an injunction does not fall within the “ordinary meaning” of the word “penalty,” which “addresses a wrong done in the past,” while an injunction “typically look[s] forward in time” and is “nonpunitive.”<sup>18</sup>

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### IMPLICATIONS

The Eleventh Circuit’s decision in *Graham* substantially circumscribes the government’s ability to obtain disgorgement by limiting the circumstances in which it can seek this relief to situations where the conduct supporting the alleged violations occurred within five years of the filing of the action. The decision is also important because it will impact SEC actions beyond those alleging violations of the Securities Act of 1933 and Securities Exchange Act of 1934 (under which the SEC brought its enforcement action in *Graham*). As the *Graham* court recognized, § 2462 “applies to a wide variety of agency actions and contexts” and thus *Graham* will also limit the SEC’s ability to seek disgorgement and declaratory relief in actions brought under *all* federal securities laws, including the FCPA. This is a notable development because the SEC has frequently sought (and obtained) significant disgorgement orders against entities charged with violating the FCPA.

It is important to note, however, that the *Graham* decision applies only within the Eleventh Circuit and appears to create a split among the circuit courts regarding the applicability of § 2462’s limitations period to the SEC’s claims for disgorgement.<sup>19</sup> The D.C. Circuit is expected to revisit the issue in *Timbervest v. SEC*, No. 15-1416 (filed Nov. 13, 2015), where the appellants are challenging, among other things, the SEC’s disgorgement claim brought more than five years after the allegedly violative conduct in question.

The SEC has not yet indicated whether it is considering pursuing further appellate review. Consideration of the case by the full Eleventh Circuit appears unlikely, as the Court typically sits *en banc* only rarely. The government could, however, seek discretionary review by the U.S. Supreme Court, which may be more inclined to exercise its discretionary review in order to resolve the circuit split.

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<sup>17</sup> *Id.* at 5-6 (citing *United States v. Banks*, 115 F.3d 916, 919 (11th Cir. 1997)).

<sup>18</sup> *Id.* at 5-8.

<sup>19</sup> See *Riordan v. SEC*, 627 F.3d 1230, 1234 (D.C. Cir. 2010) (holding that § 2462’s five-year limitations period does not apply to disgorgement actions, and summarizing D.C. Circuit precedent holding the same); *SEC v. Rind*, 991 F.2d 1486, 1492 (9th Cir. 1993) (holding that § 2462’s limitations period does not apply to SEC civil enforcement actions, including those seeking disgorgement).

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