Securities Litigation and Enforcement
Investigations, Compliance and Defense

Recent Legislation Expands SEC's Ability to Pursue Disgorgement

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On January 1, 2021, Congress made several important changes to the US securities laws that will impact the Securities and Exchange Commission's (SEC) ability to pursue and recover funds through disgorgement.

Specifically, Congress, as part of its vote to enact the National Defense Authorization Act (NDAA) over President Trump's veto, passed a provision titled "Investigations and Prosecution of Offenses for Violations of the Securities Laws." This section amended certain disgorgement-related provisions of the Securities Exchange Act of 1934 to: (1) expressly grant the SEC statutory authority to pursue disgorgement as a remedy for civil enforcement actions in federal court; (2) extend the statute of limitations for all disgorgement actions involving fraud and scienter from five years to ten years; and (3) direct courts to apply a ten-year statute of limitations for all other claims seeking equitable remedies, such as injunctions, bars, suspensions, and cease and desist orders.

The amendments in the NDAA are likely Congress's response to the US Supreme Court's decisions in *Kokesh* (2017) and *Liu* (2020). In *Kokesh*, the Court held that disgorgement was a "penalty" and thus was subject to a five-year statute of limitations. At the time, however, the Court did not address whether, if disgorgement was a "penalty," the SEC could still seek disgorgement pursuant to its power to obtain an "equitable remedy" under Section 21(d)(5) of the Securities and Exchange Act. The Court in *Liu* answered this question, holding that disgorgement could be considered an equitable remedy, but only if subject to certain limitations, such as ensuring the disgorged funds come from the wrongdoer and ensuring the recovered funds benefit the wronged investors. With this legislation, Congress's actions have greatly expanded the timeframe during which the SEC can seek disgorgement. By doing so, it has also increased the total amount of disgorgement the SEC could collect. While the new law does not explicitly address the equitable restrictions the Court acknowledged in *Liu*, the SEC may point to this legislation as additional authority that allows it to seek disgorgement not tied directly to equitable claims for the benefit of wronged investors. Additionally, although the bill includes language providing that it applies to any action pending or filed after the date of the NDAA, litigants may have grounds to challenge any retroactive application of the statute. These issues will likely have to be resolved by the courts going forward.

This alert is an update to our previous alert, "Practical Implications of Supreme Court's Decision Related to SEC's Disgorgement Remedy," which was published on June 30, 2020 and is available here.

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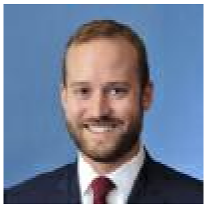

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