

## Securities Litigation and Enforcement

# Two Circuits Hold Statute of Limitations Does Not Apply To SEC Employment, Officer, and Director Bars

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On November 6, 2020, the Court of Appeals for the DC Circuit held that *Kokesh v. SEC*, 137 S. Ct. 1635 (2017)—in which the court applied the five-year limitations period under 28 U.S.C. § 2462 to SEC claims seeking disgorgement—did not apply to Financial Industry Regulatory Authority (FINRA)'s imposition of an employment, officer, or director bar. In *Saad v. SEC*, No. 19-1214 (DC Cir. 2020), the court narrowly construed *Kokesh*, finding that it arose in a context and on facts distinguishable from Saad's case. The *Saad* decision follows the Third Circuit's earlier decision that also held that *Kokesh* did not time bar the SEC from prohibiting a defendant from serving as an officer or director.

Is a trend brewing? And, if so, will that trend hold? Or are these cases merely outliers that arose in unique circumstances? The answers remain to be seen. In the meantime, litigants should watch closely to see how other courts apply Section 2462 in the context of injunctions that prevent an individual from being employed in the securities industry or serving as an officer or director of a public company.

### ***Kokesh* Applied Section 2462 to Disgorgement.**

In *Kokesh*, the SEC brought claims seeking “civil monetary penalties, disgorgement, and an injunction barring Kokesh from violating securities laws in the future.” The district court found that Section 2462—which imposes a five-year limitations period on government actions seeking “any civil fine, penalty, or forfeiture”—applied to the SEC's claims for civil money penalties but not to the SEC's claims for so-called equitable relief. The Tenth Circuit affirmed, but the US Supreme Court reversed. The Supreme Court concluded that “SEC disgorgement constitutes a penalty within the meaning of §2462” thereby subjecting the SEC to the five-year limitations period for three main reasons. First, “[t]he violation for which the remedy is sought is committed against the United States rather than an aggrieved individual.” Second, “disgorgement is imposed for punitive purposes”—often to “label defendants wrongdoers’ as a consequence of violating public laws” and to deter future violations—and “[s]anctions imposed for the purpose of deterring infractions of public laws are inherently punitive.” Third, “in many cases, SEC disgorgement is not compensatory” because the disgorged funds are frequently not returned to victims. As a result, the Supreme Court explained, “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. The five-year statute of limitations in § 2462 therefore applies when the SEC seeks disgorgement.”

### **Does *Kokesh* Apply to Employment, Officer, or Director Bars?**

While *Kokesh* specifically addressed SEC requests for disgorgement, the Supreme Court's reasoning was not necessarily limited to disgorgement. As such, it was not immediately clear whether Section 2462 applies to SEC requests for injunctions, including those that bar defendants from employment in the securities industry or from service as an officer or director in a public company. Stated simply, are those bars a penalty under Section 2462?

The DC Circuit's ruling in *Saad* addressed this open question. In *Saad*, an employee misappropriated his employer's funds and repeatedly attempted to cover up his wrongdoing. His efforts failed, and FINRA “imposed a bar that permanently forbade Saad from associating with any FINRA member firm in any capacity.” The SEC eventually “affirmed the permanent bar finding it to be ‘remedial, not punitive.’” In 2017, the DC Circuit vacated that decision in part and remanded “for the Commission to determine in

the first instance whether [*Kokesh*] has any bearing on Saad’s case.” 873 F.3d 297 (DC Cir. 2017). In doing so, then-Judge Kavanaugh and Judge Millet issued dueling opinions—the former explaining why employment bars are a penalty under *Kokesh*, and the latter taking the opposite view. See “After *Kokesh*, Does The SEC Have A New Time Limit For Claims Seeking An Officer Or Director Bar?” [ABA Sec. Lit. J.](#) (Aug. 25, 2018).

Last week, the DC Circuit sided with Judge Millet and held that *Kokesh* had no bearing on Saad’s case. In reaching this conclusion, the court noted that *Kokesh* applies to SEC disgorgement requests and enforcement actions. In contrast, the court explained, *Saad* involved a different sanction, statute, and proceeding; a FINRA regulatory proceeding barring Saad from associating with any FINRA member firm. The court further recognized that the SEC sustained Saad’s bar “not as a penalty but as a means of protecting investors,” and concluded the injunction “was not ‘excessive or oppressive’ in any other respect.” Slip op. 10. In so ruling, the DC Circuit rejected an overly broad reading of *Kokesh* and suggested that future questions about the scope of *Kokesh* would similarly be addressed case-by-case.

The DC Circuit was not the first to reach that conclusion. In September 2019, in *SEC v. Gentile*, the Third Circuit distinguished *Kokesh* and held that a valid, preventive injunction is not a penalty subject to Section 2462. 939 F.3d 549 (3d Cir. 2019), *cert. denied*, 140 S. Ct. 2669 (2020). In reversing the district court’s decision finding an injunction barring the owner of a broker-dealer from the penny stock industry was untimely under Section 2462, the Third Circuit explained that “Injunctions may not be supported by the desire to punish the defendant or deter others, so courts abuse their discretion when they issue or broaden injunctions for those reasons.” As such, the court held “SEC injunctions that are properly issued and valid in scope are not penalties and thus are not governed by § 2462. If an injunction cannot be supported by a meaningful showing of actual risk of harm, it must be denied as a matter of equitable discretion—not held time barred by § 2462.”

While the guidance from *Saad* and *Gentile* is useful as far as it goes, it does not definitively resolve the question of whether Section 2462 applies to SEC requests for injunctions, including employment, officer, or director bars. As a result, what (if anything) *Kokesh* means for those circumstances will likely continue to be a point of contention. Securities lawyers and defendants should thus keep watching to see whether other courts reach a similar conclusion based on the specific facts and circumstances, or follow the lead of *Kokesh* itself (and the Supreme Court’s earlier decision in *Gabelli v. SEC*, 568 US 442 (2013)) in categorically holding that certain relief is subject to a five-year limitations period. Securities lawyers should also be mindful to raise the statute of limitations defense when defending SEC claims for injunctions, including employment, officer, or director bars.

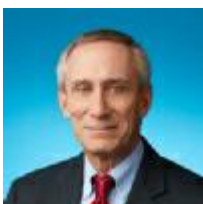
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