

Client Alert: Court Adopts SEC's New Unregistered Dealer Theory, Creates Risk of Disgorgement and Penalties for Anyone Trading Securities As Part of A Business

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By: Anthony Barkow, Gabriel K. Gillett, Charles D. Riely, Grace C. Signorelli-Cassady

A broad array of financial market participants—mutual funds, private funds, insurers, pension funds, family offices, individuals, and more—may be at risk after the Securities and Exchange Commission (SEC) secured summary judgment in a case alleging an individual and an affiliated entity acted as unregistered securities dealers when they bought and sold securities for their own account.^[1]

As a recent article explained, as a result of decisions like this one, a “Sword of Damocles now hangs over ... just about anyone making a dime in almost any market.”^[2] That is because, under the new theory the SEC advanced in this case and other recent enforcement actions, many market participants could be required to register as dealers, disgorge profits and pay interest and penalties earned from trading activity years ago that seemed perfectly legal at the time. The decision thus serves as a red flag for a wide range of entities that buy and sell securities—and in theory could ensnare *any* entity that trades or invests for its own account.

The Securities Exchange Act of 1934 requires those who act as securities dealers to register with the SEC. The Exchange Act defines a “dealer” as “any person engaged in the business of buying and selling securities ... for such person’s own account,” but exempts from that definition those who buy and sell securities “not as a part of a regular business.”^[3] For nearly nine decades, that has meant that those who do not have customers, and thus cannot transact with their own customers, are not dealers. The SEC also published guidance highlighting various factors that indicate when someone is acting as a dealer.^[4]

However, in a series of recent enforcement cases filed across the country, the SEC has been advocating a new and broad view—that a dealer can be *anyone* who is engaged in the business of buying and selling securities regardless of having customers and the presence of any factors.^[5] In *SEC v. Fierro*, for example, the SEC alleged defendants acted as unregistered dealers when they bought convertible notes from corporate issuers, held them for at least six months, then converted

the debt into equity and sold the resulting shares at a profit.^[6] The district court granted summary judgment for the SEC. Relying largely on two recent district court decisions from Florida, the court held that because “Defendants were engaged in the business of buying and selling securities” they were “required to register with the SEC as dealers.”^[7]

The defendants in *Fierro* offered reasons why the SEC’s theory should be rejected as contrary to the Exchange Act. For example, the definition of dealer historically has been understood as only applying to entities that buy and sell securities to execute customer orders—not traders or investors who take on risk—and that is how Congress understood the definition when adopting it in 1934.^[8] Defendants also highlighted that they were not required to register as a dealer based on the SEC’s own rules and the SEC’s own guidance describing the relevant factors for dealer status.^[9]

Still, the district court in *Fierro* agreed with the SEC and adopted its expansive interpretation of “dealer.” Whether that decision and others will hold up, and whether courts in other jurisdictions will follow suit, remains to be seen. But unless and until the SEC reverts to its prior and longstanding interpretation—voluntarily or via court order—traders, investors, and other participants in the financial markets would be wise to gauge the risk that their activities could be deemed to require dealer registration and disgorgement of past profits.

Jenner & Block represents amici curiae that are encouraging courts to reject the SEC’s new theory for those reasons and others, including because courts are the wrong forum for the SEC to seek to alter its rules or to amend the statutory definition of dealer.^[10]

Footnotes

[1] *SEC v. Fierro*, No. 20-cv-2104 (D. NJ June 29, 2023), ECF No. 50.

[2] Brandon Kochkodin, Forbes, The Government Is Quietly Suing Its Way To Broader Powers Over Traders (July 12, 2023), <https://tradingmarketsproject.com/wp-content/uploads/2023/07/The-Government-Is-Quietly-Suing-Its-Way-To-Broader-Powers-Over-Traders.pdf>.

[3] 15 U.S.C. § 78c(a)(5).

[4] SEC, *Guide to Broker-Dealer Registration* (April 2008; revised Dec. 12, 2016), <https://www.sec.gov/about/reports-publications/investor-publications/guide-broker-dealer-registration>.

[5] See, e.g., *SEC v. Auctus Fund Management, LLC*, No. 23-cv-11233 (D. Mass. filed June 1, 2023); *SEC v. LG Capital Funding, LLC*, No. 22-cv-03353 (E.D.N.Y. filed June 7, 2022); *SEC v. Carebourn Cap., L.P.*, No. 21-cv-02144 (D.M.N. filed Sept. 24, 2021); *SEC v. GPL Ventures LLC*, No. 21-cv-06814 (S.D.N.Y. filed Aug. 13, 2021); *SEC v. Morningview Financial, LLC*, No. 22-cv-8142 (S.D.N.Y. filed Sept. 23, 2022); *SEC v. Fife*, No. 20-cv-5227 (N.D. Ill. filed Sept. 3, 2020); *SEC v. Keener*, No. 20-cv-21254 (S.D. Fla. filed Mar. 24, 2020); *SEC v. Fierro*, No. 3:20-cv-2104 (D.N.J. filed Feb. 26, 2020); *SEC v. River N. Equity LLC*, No. 1:19-cv-1711 (N.D. Ill. filed Mar. 11, 2019).

[6] Slip op. 1-3.

[7] Slip op. 15 (relying on *SEC v. Almagarby*, 479 F. Supp. 3d 1266 (S.D. Fla. 2020), *appeal pending*, No. 21-13755 (11th Cir.); *SEC v. Keener*, 2020 WL 4736205 (S.D. Fla. Aug. 14, 2020), *appeal pending*, No. 22-14237 (11th Cir.)).

[8] See Defs.' Opp. to MSJ at 6-10.

[9] See Defs.' Opp. to MSJ at 11-14.

[10] See Mot. for Leave to File Amicus Curiae Brief, *SEC v. LG Capital Funding, LLC*, No. 22-cv-3353 (E.D.N.Y. July 13, 2023), ECF No. 39; Brief of Amici Curiae, *SEC v. Morningview Financial, LLC*, No. 22-cv-8142 (S.D.N.Y. July 6, 2023), ECF No. 33; Unopposed Mot. for Leave to File Amicus Curiae Brief, *SEC v. Almagarby*, No. 21-13755 (11th Cir. July 13, 2023), ECF No. 60-1; Brief of Amicus Curiae, *SEC v. Keener*, No. 22-14237 (11th Cir. June 7, 2023), ECF No. 36.

Related Attorneys



Anthony Barkow

Managing Partner, New York
abarkow@jenner.com
+1 212 891 1662



Gabriel K. Gillett

Partner
ggillett@jenner.com
+1 312 840 7220



Charles D. Riely

Partner

criely@jenner.com

+1 212 891 1686



Grace C. Signorelli-Cassady

Associate

gsignorelli@jenner.com

+1 312 840 7281

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