Public Enforcement After *Kokesh*: Evidence from SEC Actions

Urska Velikonja*

Disgorgement of ill-gotten gain, similar to an unjust enrichment claim, is a common remedy in United States Securities and Exchange Commission (SEC) enforcement. In June 2017, the Supreme Court held in Kokesh *v. SEC that disgorgement is a penalty. As such, the statute of limitations in section 28 U.S.C. § 2462 for any "fine, penalty, or forfeiture" bars the SEC from seeking disgorgement for any violation committed more than five years before suit.*

The Kokesh *decision has reverberated through federal enforcement. Most directly, it bars SEC disgorgement claims for long-running frauds, costing the Agency $1.1 billion to date. As is typical for Supreme Court decisions,* Kokesh *also raised more questions than it answered. If disgorgement is a penalty, then most other enforcement remedies are also penalties and are thus time limited to five years. Moreover, disgorgement in SEC civil actions is not expressly authorized in any statute. If disgorgement is a penalty, then the SEC cannot seek disgorgement in court actions at all. More than two years after the* Kokesh *decision, its impact remains uncertain.*

Using a unique dataset of over eight thousand SEC enforcement actions filed between 2010 and 2018, this Article unravels the impacts of Kokesh. *Depending on how broadly lower courts interpret* Kokesh*, anywhere between twenty and eighty percent of SEC disgorgement is at risk. At the same time, and contrary to claims advanced by SEC leadership,* Kokesh *does not substantially undermine the Agency's abilities to compensate investors or to deter misconduct, but it will certainly change the incentives at work during settlement negotiations. However* Kokesh *is interpreted, one group of defendants—individuals running long-standing frauds targeting small-scale investors—clearly benefits. Many of them will be able to fleece ordinary people of their nest eggs and then keep the money they stole. Even if such defendants cannot be deterred, the result is corrosive because it offends basic notions of fairness and thus undermines the rule of law.*

* Professor of Law, Georgetown University Law Center. I would like to thank Alejandro J. García for his research assistance with this Article. For helpful conversations and suggestions, I thank Adam Feibelman, Jonathan Macey, Randall Thomas, Bob Thompson, David Vladeck, Andrew Vollmer, and participants of the 2018 Corporate & Securities Litigation Workshop at the University of Richmond, the Business Law Workshop at the University of Texas, Austin, the 2019 Tulane Corporate and Securities Law Roundtable, and the 2019 Yale Journal on Regulation Symposium.

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INTRODUCTION

In June 2017, in *Kokesh v. SEC*,[1] the Supreme Court decided a seemingly uncontroversial technical question: whether disgorgement in SEC enforcement actions is a penalty and thus subject to a five-year statute of limitations in 28 U.S.C. § 2462 applicable to any "fine, penalty, or forfeiture" in a government-enforcement action.[2] The Court answered the question in the affirmative.[3] After the bruising oral argument,[4] the ultimate decision was not surprising—but its implications have been.

Kokesh is the second decision in four years to interpret section 2462. Its 2013 counterpart, *Gabelli v. SEC*,[5] held that although the provision is a statute of limitations and not a statute of repose,[6] time for the imposition of penalties in a government action is measured from the date of the violation, not from the date the violation is discovered (as is typical for limitations provisions).[7] As a result, if the government does not discover misconduct within five years of the violation, the statute of limitations in section 2462 operates as an absolute bar on liability, much like a statute of repose.[8]

Section 2462 bars the imposition of penalties after the five-year period has expired, but it does not bar the imposition of remedies that are not penalties. At the time of *Gabelli*, only civil fines in SEC enforcement actions were understood to be penalties and thus potentially time barred.[9] Other remedies, including disgorgement, injunctions, and officer and director bars were understood to be

1. 137 S. Ct. 1635 (2017).

2. "Except as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon." 28 U.S.C. § 2462 (2012).

3. *See Kokesh*, 137 S. Ct. at 1645.

4. *See* David J. Lynch, *Supreme Court Justices Question SEC Enforcement Tool*, FIN. TIMES (Apr. 18, 2017), https://www.ft.com/content/268d002a-244c-11e7-8691-d5f7e0cd0a16; Dave Michaels, *Justices Grill SEC Over Limiting Power to Make Wrongdoers Give Back Gains*, WALL ST. J. (Apr. 18, 2017, 3:45 PM), https://www.wsj.com/articles/justices-grill-sec-over-limiting-power-to-make-wrongdoers-give-back-gains-1492537032.

5. 568 U.S. 442 (2013).

6. *See generally* CTS Corp. v. Waldburger, 573 U.S. 1, 7–8 (2014) (distinguishing statutes of limitation from statutes of repose). Typically, time in a statute of limitations is measured from the date that the violation is discovered or should have been discovered, whereas time in a statute of repose is measured from the date of the violation. *Id.*

7. *Gabelli* creates a legal fiction that the government has such substantial investigative powers that it reasonably should discover every violation at the time it is committed. *See* 568 U.S. at 451.

8. *See generally CTS Corp.*, 573 U.S. at 13 (noting that the term "statute of limitations" is not always formally applied and can refer more generally to "any provision restricting the time in which a plaintiff must bring suit").

9. *See Gabelli*, 568 U.S. at 444, 447 n.1.

equitable remedies and remedial measures, not penalties, and thus not time barred after five years.[10] *Kokesh* changed that. In *Kokesh*, the Court held that disgorgement of ill-gotten gains obtained through misconduct was a penalty, and thus the SEC could not seek disgorgement of profits wrongfully obtained more than five years before filing suit.[11] The Court developed a three-part test to decide the issue. It held, first, that sanctions are penalties when they address wrongs to the public, not to the individual; second, that sanctions are penalties when they seek to deter misconduct, rather than to compensate; and third, that sanctions are penalties unless used exclusively to compensate injured investors.[12]

The holding meant that the petitioner and adjudged fraudster Charles Kokesh could keep most of the $35 million that he misappropriated from his investors. But, as is typical for Supreme Court decisions, *Kokesh* also raised additional questions. First, the Court in *Kokesh* distinguished between penalties and compensatory relief. Compensatory relief, sought to redress private harms and not primarily to deter violations, is not deemed a penalty and is thus not subject to the limitations period in section 2462.[13] Restitution that is paid to the aggrieved party is deemed compensatory and thus not a penalty.[14] Disgorgement sought to compensate injured investors arguably would satisfy the test. But *Kokesh* itself equivocates on when relief can be considered compensatory, and appears categorically to disqualify disgorgement because no statute commands that disgorgement be distributed to the victims of fraud.[15] The distinction between penalties and compensatory relief also does not appear to leave any room for remedial and forward-looking measures, such as obey-the-law injunctions or officer-and-director bars. Thus, it is possible that, under the Court's vague three-part test, disgorgement and most other enforcement remedies may be penalties.[16] Because section 2462 is a catchall statute of limitations, applicable to any federal civil enforcement action whenever the enabling statute does not provide a specific limitations period, the *Kokesh* decision potentially affects federal enforcement agencies other than

10. *See id.* at 447 n.1.

11. 137 S. Ct. 1635, 1645 (2017). The language of *Kokesh* suggests that a claim for restitution of wrongful profits to be distributed to injured investors might not be considered a "penalty," but only if the SEC brings the claim in order to compensate investors and not to further public goals, such as deterrence. Because the goal of SEC enforcement is deterrence, any SEC remedy is arguably a penalty, including restitution. *See id.* at 1643–44.

12. *See id.* at 1643–44.

13. *See id.* at 1642–44.

14. *See id.* at 1644 (citing Porter v. Warner Holding Co., 328 U.S. 395, 402 (1946)).

15. *See id.* Section 922 of the Dodd–Frank Act authorizes the SEC to distribute disgorged funds to investors but does not require distribution. Dodd–Frank Wall Street Reform and Consumer Protection Act § 922, 15 U.S.C. § 78u-6(g)(3)(A) (2012).

16. *See, e.g.*, Gabriel K. Gillett, Howard S. Suskin & Adam G. Unikowsky, *After* Kokesh*, Does the SEC Have a New Time Limit for Claims Seeking an Officer or Director Bar?*, ABA (Aug. 25, 2018), https://www.americanbar.org/groups/litigation/committees/securities/articles/2018/summer2018-after-kokesh-does-the-sec-have-a-new-time-limit-for-claims-seeking-an-officer-or-director-bar/ (arguing that officer-and-director bars can be time barred).

the SEC. That includes at least some of the statutes enforced by the Commodity Futures Trading Commission (CFTC),[17] the Federal Trade Commission (FTC),[18] the Consumer Financial Protection Bureau (CFPB),[19] banking regulators,[20] the Federal Election Commission (FEC),[21] and the Environmental Protection Agency (EPA).[22]

Second, because disgorgement of wrongfully obtained profits in SEC actions has long been considered an equitable remedy that courts have the inherent right to order, it is not expressly authorized in any statute. Penalties cannot be imposed unless authorized by statute. If disgorgement is a penalty, then—the argument goes—the SEC cannot seek disgorgement in court actions at all,[23] at least until securities laws are amended to add disgorgement as a legal remedy.

Two years after *Kokesh*, none of these questions have been definitively answered and the impact of the decision remains uncertain. Soon after the decision, some practitioners argued that nothing would change in SEC enforcement,[24]

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17. *See* CFTC v. Reisinger, No. 11-C-8567, 2013 WL 3791691, at *7 (N.D. Ill. July 18, 2013) (holding that "§ 2462 governs the CFTC's civil penalty claims").

18. *See* M. Sean Royall, Richard H. Cunningham & Ashley Rogers, *Are Disgorgement's Days Numbered?:* Kokesh v. SEC *May Foreshadow Curtailment of the FTC's Authority to Obtain Monetary Relief*, 32 ANTITRUST 94, 94 (2018); Jennifer Kim, Note, *Is Disgorgement a Penalty in the Antitrust-Enforcement Realm?: Exploring Mediation as the FTC's Response to* Kokesh *in the Context of Reverse Payment Settlements*, 20 CARDOZO J. CONFLICT RESOL. 163, 180 (2018).

19. Letter from Lawrence DeMille-Wagman, Senior Litigation Counsel at the Consumer Financial Protection Bureau, to Mark Langer, Clerk of the Court of the United States Court of Appeals for the District of Columbia Circuit (June 7, 2017) (conceding that § 2462 applies to civil penalties and disgorgement in administrative proceedings brought by the CFPB).

20. *See* Matthew T. Martens et al., *Implications of the Supreme Court's* Kokesh *Decision*, WILMERHALE (June 19, 2017), https://www.wilmerhale.com/en/insights/client-alerts/2017-06-19-implications-of-the-supreme-courts-kokesh-decision [https://perma.cc/8YHF-EMWZ] (discussing that § 2462 arguably applies to 12 U.S.C. § 1818(b)(6), which authorizes the Federal Reserve, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation to order banking institutions to take "affirmative action," including providing restitution or reimbursement).

21. *See* FEC v. Williams, 104 F.3d 237, 240 (9th Cir. 1996) (holding that "§ 2462 applies to FEC actions for the assessment or imposition of civil penalties under FECA").

22. *See* Douglas Edward Pittman, *Is Time Up for Equitable Relief? Examining Whether the Statute of Limitations Contained in 28 U.S.C. § 2462 Applies to Claims for Injunctive Relief*, 70 WASH. & LEE L. REV. 2449, 2453 & n.22 (2013).

23. *Compare* Liu v. SEC, 2019 WL 5659111 (2019) (mem.) (casting doubt on the SEC's authority to grant disgorgement in civil actions by granting certiorari), *and* Stephen M. Bainbridge, Kokesh *Footnote Three Notwithstanding: The Future of the Disgorgement Penalty in SEC Cases*, 56 WASH. U. J. L. & POL'Y 17, 30 (2018) (arguing that the SEC does not have the authority to order disgorgement without statutory authorization), *with* Roberta S. Karmel, *Will Fifty Years of the SEC's Disgorgement Remedy Be Abolished?*, 71 S.M.U. L. REV. 799, 800 (2018) (contending that the SEC does have a right to seek equitable disgorgement).

24. *See, e.g.*, Russell G. Ryan, *The Equity Façade of SEC Disgorgement*, 4 HARV. BUS. L. REV. ONLINE, Nov. 15, 2013, at 12, http://www.hblr.org/2013/11/the-equity-facade-of-sec-disgorgement/ [https://perma.cc/926T-2G73] (arguing that losing disgorgement "would not raise an alarm in the realm of SEC enforcement"); Dixie L. Johnson et al., *King & Spalding Discusses Potential Effects of SEC Disgorgement as a Penalty*, CLS BLUE SKY BLOG (June 21, 2017), http://clsbluesky.law.columbia.edu/2017/06/21/king-spalding-discusses-potential-effects-of-sec-disgorgement-as-penalty/ [https://perma.

while others countered that everything would.[25] There is currently no reliable estimate of *Kokesh*'s bite. The SEC's leadership estimates that in the two years since *Kokesh*, the decision has barred the SEC from ordering about $1.1 billion in disgorgement,[26] and that this number grows by the day. One empirical study found that *Kokesh* has had a statistically significant negative impact on stock prices, suggesting that investors in publicly traded companies value enforcement.[27] Another empirical study suggested that few violations older than five years result in disgorgement orders, but its findings were limited to enforcement of insider trading violations.[28] There has been no thorough empirical investigation into the impact of *Kokesh* on enforcement generally, and in particular, none that distinguishes cases based on the characteristics of the defendant, the charged violations, or the case resolution.

To shed light on the decision's likely impact, this Article conducts a comprehensive analysis of nine years of SEC enforcement, beginning with fiscal year (FY) 2010, when the SEC first sued Charles Kokesh, and ending with FY 2018, the last complete fiscal year. This Article does not study observed changes in enforcement since the *Kokesh* decision or market responses to the decision. Rather, this Article offers predictions based on a careful parsing of enforcement actions filed during the period. The Article offers suggestive answers to the question of what would have happened had *Kokesh* been the law during the study period, proceeding on the assumption that everything else would remain constant.[29] This information is important both for the SEC and for Congress, which is currently considering bills to undo *Kokesh* for SEC enforcement.[30]

cc/JC3F-CH2D] (suggesting that *Kokesh* would have a minor effect on SEC enforcement because the SEC often pursues claims within five years of the misconduct).

25. *See, e.g.*, Kathryn Barry et al., *The Catch with* Kokesh*: Insurers Refusing to Cover Disgorgement to SEC*, JD SUPRA (Oct. 24, 2018), https://www.jdsupra.com/legalnews/the-catch-with-kokesh-insurers-refusing-10747/ [https://perma.cc/3UMK-JHTT] (noting that *Kokesh* has had substantial unanticipated consequences).

26. SEC, ANNUAL REPORT: DIVISION OF ENFORCEMENT 21 (2019) [hereinafter 2019 ENFORCEMENT REPORT], https://www.sec.gov/files/enforcement-annual-report-2019.pdf [https://perma.cc/V8A4-49A2]. That figure almost certainly overstates the amount of foregone disgorgement. Unlike private plaintiffs, the SEC does not always seek maximum monetary penalties. It frequently waives payment for, or even refuses to impose, monetary penalties when the defendant: cannot pay (*see, e.g.*, SEC v. Summit Tr. Co., No. 15-cv-05843-JCJ, slip op. at 7 (E.D. Pa. Nov. 6, 2015), ECF No. 3); is bankrupt (*see, e.g.*, SEC v. Quadrant 4 Sys. Corp., No. 17-cv-04883, slip op. at 5 (N.D. Ill. Sept. 28, 2017), ECF No. 37); or cooperates with an SEC investigation (*see, e.g.*, CVR Energy, Inc., Exchange Act Release No. 80039, 2017 WL 605041, at *6 (Feb. 14, 2017)).

27. *See* Nerissa C. Brown, Brian T. Gale & Adrienna A. Huffman, *Kokesh v. SEC*: The Market Impact of Reducing SEC Enforcement Powers 30 (Feb. 2019) (unpublished manuscript), https://ssrn.com/abstract=3292548 [https://perma.cc/6D57-2J5H] (conducting an event study of six important dates around the *Kokesh* decision and finding a statistically significant negative impact on stock prices).

28. *See* Verity Winship, *Disgorgement in Insider Trading Cases: FY2005–FY2015*, 71 SMU L. REV. 999, 1011 (2018) (estimating that only 2% of disgorgement was for insider trading violations outside the five-year limitations period).

29. That is a strong but necessary assumption for this study. The assumption is relaxed in Parts IV and V, which discuss possible responses and implications.

30. *See, e.g.*, STAFF OF H. COMM. ON FIN. SERVS., 116TH CONG., DISCUSSION DRAFT B. TO AMEND THE SECURITIES EXCHANGE ACT OF 1934 TO ALLOW THE SECURITIES AND EXCHANGE COMMISSION TO SEEK AND FED. COURTS TO GRANT RESTITUTION TO INVESTORS AND DISGORGEMENT OF UNJUST

This Article reviews 8,197 discrete enforcement cases and reports several observations of note. Disgorgement represents the bulk of monetary penalties imposed.[31] Importantly, almost $10 billion of the $22.8 billion in monetary penalties imposed during the study period is court-ordered disgorgement, much of it for fraudulent offers of securities by individual offenders.[32] Disgorgement is also a common remedy: more than half of SEC enforcement actions result in some disgorgement. When disgorgement is ordered, it represents almost 80% of all monetary penalties imposed.[33]

Disgorgement is also often ordered in cases that allege violations older than five years. Charging documents in 37% of cases allege violations older than the five-year limitations period.[34] The share has increased from less than 30% in 2010 to almost 50% in 2018, suggesting that the statute of limitations has a more significant impact on SEC enforcement today than in the past.[35] The impact of the five-year bar on disgorgement orders varies considerably by case characteristics. Insider trading and market manipulation are typically detected, investigated, and prosecuted during the five-year period, whereas other violations are not. Foreign bribery cases, in particular, are almost always prosecuted outside the limitations period.[36]

This study also suggests that the SEC might be able to moderate the impact of *Kokesh* in settled cases, where it should be able to negotiate a tolling agreement to stop the limitations clock during its investigation. A large majority of actions against public companies and large financial firms settle, muting the impact of *Kokesh* on enforcement of foreign bribery or other violations by Wall Street firms. By contrast, individual offenders and smaller private firms that prey on retail investors are more likely to avoid full sanctions unless *Kokesh* is undone.[37]

SEC leadership has asserted that *Kokesh* would impair the SEC's ability to deter misconduct and to compensate investors. The research reported in this Article suggests that the impact on deterrence and compensation should be relatively limited. *Kokesh* bars only enforcement of violations older than five years, not those prosecuted more quickly. *Ex ante*, offenders cannot count on evading prosecution within five years, and thus they would not discount substantially the expected cost of misconduct. However, once offenders have been able to keep their scheme going undetected for five years, their incentives to continue breaking the law *do change*. Moreover, some groups of defendants—individuals in

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ENRICHMENT (Jun. 6, 2019) (introduced by Rep. Ben McAdams), https://financialservices.house.gov/uploadedfiles/bills-116pih-sea34.pdf [https://perma.cc/BVG8-8YEM]. For a compilation of draft bills seeking to undo *Kokesh* for SEC enforcement, see *Putting Investors First: Examining Proposals to Strengthen Enforcement Against Securities Law Violators*, U.S. H. COMM. ON FIN. SERVS., https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403833 [https://perma.cc/WC5W-WGJD] (last visited Sept. 25, 2019).

31. *See infra* Section III.A.
32. *See infra* Section III.B.3; *see also infra* Table 6.
33. *See infra* Section III.A & Table 6.
34. *See infra* Section II.C.1.
35. *See infra* Section II.C.1 & Table 1.
36. *See infra* Section II.C.2 & Table 3.A.
37. *See infra* Section II.D.

particular—do not respond substantially to marginal reductions or increases in sanctions and are thus unlikely to change their behavior in the wake of *Kokesh*.[38] SEC leadership has also suggested that by limiting disgorgement, *Kokesh* impairs the SEC's ability to compensate investors, including in cases where no private action was filed or a filed action was unsuccessful. This Article suggests that the impact on SEC compensation should be relatively minor.[39]

This does not imply that Congress should not codify disgorgement and extend the limitations period for SEC enforcement. To the contrary, Congress must intervene because the status quo allows fraudsters who are caught to keep the money they stole under a legal technicality (that is, a statute of limitations that is short relative to how long it takes to detect, investigate, and prosecute the average SEC case). That reality undermines the credibility of the federal enforcement program and is inconsistent with the rule of law notion that just laws should deprive lawbreakers of their profits.[40]

This Article proceeds as follows. Part I sets the stage by supplying information on securities enforcement and the statute of limitations provision in question. Part II describes in more detail the broad and deep empirical approach adopted in this Article and provides an overview of its findings. Additionally, Part II considers whether *Kokesh* suggested that *all* disgorgement constitutes a penalty subject to the five-year limitations period. It assesses the implications of that holding, including the availability of tolling agreements as a mitigation technique.

Part III discusses the importance of disgorgement for SEC enforcement and evaluates the consequences of a broader reading. More generally, how far exactly does *Kokesh* go in limiting disgorgement as a remedy in SEC enforcement actions? Does footnote 3, included as an aside in *Kokesh*, ban *all* court-ordered disgorgement in civil actions, regardless of the limitations period?[41] Does *Kokesh* ban only disgorgement as a penalty, leaving disgorgement as restitution untouched? Does it limit all remedies that are "punitive" and thus subject to the five-year time bar?

The availability of substitute remedies and substitute enforcers would mute the impact of *Kokesh*. To the extent that civil fines, restitution, compensation

38. *See infra* Section IV.A.2.

39. If, however, the holding in *Kokesh* expands in subsequent cases and impedes the SEC's ability to trade disgorgement in settlements for more serious sanctions, such as professional bars or registration revocations, then the impact on the ability of the SEC to enforce the law and compensate investors will be substantial.

40. *See generally* Brian Z. Tamanaha, *The History and Elements of the Rule of Law*, 2012 SING. J. LEGAL STUD. 232, 241–42 (observing that the rule of law requires that rules be predictable and just).

41. Footnote 3 says:

> Nothing in this opinion should be interpreted as an opinion on whether courts possess authority to order disgorgement in SEC enforcement proceedings or on whether courts have properly applied disgorgement principles in this context. The sole question presented in this case is whether disgorgement, as applied in SEC enforcement actions, is subject to § 2462's limitations period.

Kokesh v. SEC, 137 S. Ct. 1635, 1642 n.3 (2017).

agreements, and professional bars could substitute for the no-longer-available disgorgement, the impact will be less consequential. The same is true if other enforcement agents, public and private, can substitute for missing SEC enforcement. Part IV concludes that such meaningful substitution is unlikely because public and private enforcers already have ample incentives to jump on the SEC bandwagon in parallel actions, and because when they do, they typically piggyback on the SEC's investigative work. But incentives to settle persist, and the SEC should be able to continue compensating investors even after *Kokesh*. Part V discusses a way forward with and without congressional intervention based on the analysis offered in Parts II, III, and IV.

I. ENFORCEMENT AND SECTION 2462

Kokesh arose from an SEC enforcement action but interprets section 2462, a catchall statute of limitations for civil penalties in federal enforcement. Despite high levels of public interest, the enforcement process continues to be poorly understood. This Part first explains the typical process for SEC enforcement and discusses delays that may be involved. Although the discussion is limited to the SEC, the Agency's enforcement techniques are similar to those of other civil enforcement agencies. This Part follows with an analysis of *Gabelli* and *Kokesh*, two recent Supreme Court decisions that interpret section 2462.

A. SEC ENFORCEMENT

Unlike injured investors who can sue only under select liability provisions, the SEC can bring an enforcement action for any violation of the federal securities laws.[42] That is both a feature, because jurisdictional questions about the SEC's right to sue are rare, and a bug, because the workload is overwhelming. Many securities violations go undetected, uninvestigated, and unprosecuted.[43]

Fraudsters usually cover their tracks, so a considerable amount of time sometimes passes between the violation and detection of that violation. Once SEC staff learns of a possible violation, they can open a matter under inquiry (MUI)[44] followed by an investigation if the initial inquiry suggests that the matter is worth pursuing.[45] There is no data on how much time typically passes between violation and detection or between detection and opening an investigation. In cases that the

42. *See, e.g.*, Securities Exchange Act of 1934 § 21(d), 15 U.S.C. § 78u(d) (2012).

43. *Cf.* SEC DIV. OF ENF'T, ENFORCEMENT MANUAL § 2.3.2 (2017) [hereinafter ENFORCEMENT MANUAL] (discussing the many requisite considerations and procedures before opening an investigation).

44. *See* ENFORCEMENT MANUAL, *supra* note 43, § 2.3.1, at 12.

45. *See id.* § 2.3.2 (listing several factors relevant for deciding whether to investigate a potential violation). The SEC staff closes about 45% of MUIs without opening an investigation. *See* SEC OFFICE OF INSPECTOR GEN., CASE NO. OIG-567, REPORT OF INVESTIGATION: DESTRUCTION OF RECORDS RELATED TO MATTERS UNDER INQUIRY AND INCOMPLETE STATEMENTS TO THE NATIONAL ARCHIVES AND RECORDS ADMINISTRATION REGARDING THAT DESTRUCTION BY THE DIVISION OF ENFORCEMENT 2 (2011), https://www.sec.gov/foia/docs/oig-567.pdf [https://perma.cc/83YA-A2DC] (reporting that SEC staff opened 23,289 MUIs between October 1, 1992 and July 20, 2010, and of those, it closed 10,468 without opening an investigation or another MUI).

SEC prosecutes, it takes on average about two years from opening an investigation to filing a complaint in court or an order instituting proceedings (OIP) in an administrative proceeding, but the variance is quite high.[46] Foreign bribery (FCPA) cases take more than four years on average to investigate.[47] Complex disclosure violations by public companies can likewise take years to investigate.[48] Insider trading cases, on the other hand, can be filed within weeks of the alleged trading.[49]

A two-year investigation may strike those familiar with securities litigation as relatively long because class actions are often filed within weeks of the first disclosure.[50] But class actions are filed before discovery has taken place, whereas the SEC files an enforcement action only after it has completed a substantial investigation.[51] Because of this distinction, short limitations periods cause substantially more trouble in government actions than in private lawsuits. During an SEC investigation, enforcement staff compile a record of alleged violations, hear testimony, collect documentary evidence, and test their legal and factual theories internally to make sure they only bring cases they believe they can win.[52] This is perhaps the most important, yet least appreciated, due process protection that defendants in public enforcement actions enjoy. An enforcement action can put a defendant's business under a dark cloud, so the SEC's internal procedures require enforcement staff to convince different superiors—including their immediate bosses, the Director of Enforcement, directors of other relevant divisions, and finally the politically appointed Commissioners—in order to file an enforcement action.[53] That process takes time.

46. *See* SEC, FY 2011 PERFORMANCE AND ACCOUNTABILITY REPORT 62 (2011), https://www.sec.gov/about/secpar/secpar2011.pdf [https://perma.cc/J4HJ-4EWN] (reporting that in FY 2007 to 2010, between 54% and 70% of enforcement actions were filed within two years of opening an MUI); Memorandum from Carl W. Hoecker, Inspector Gen., SEC, to Jay Clayton, Chairman, SEC, 4 (Oct. 5, 2018) [hereinafter Hoecker Memorandum], https://www.sec.gov/Inspector-Generals-Statement-on-the-SECs-Mgt-and-Performance-Challenges-Oct-2018.pdf [https://perma.cc/HU54-ZL5D] (reporting that 52% of actions were filed within two years of opening an MUI in FY 2017, compared with 53–64% in 2012).

47. *The Gray Cloud of FCPA Scrutiny Lasted Too Long in 2017*, FCPA PROFESSOR (Jan. 4, 2018), http://fcpaprofessor.com/gray-cloud-fcpa-scrutiny-lasted-long-2017/.

48. *See, e.g.*, Memorandum Concerning SEC's Volkswagen Investigation 2–4, SEC v. Volkswagen AG, No. 3:19-cv-01391-CRB (N.D. Cal. July 8, 2019) (explaining that due to defendants' stonewalling and delayed responses, the SEC investigated for almost three and a half years before filing a complaint).

49. *See infra* note 151. The median lag time for insider trading is substantially longer than that. *See* Michael A. Perino, *Real Insider Trading*, ST. JOHN'S SCH. L. LEGAL STUD. RES. PAPER SERIES 30, Feb. 20, 2019, https://ssrn.com/abstract=3338536 [https://perma.cc/4MX3-89B3] (reporting that the median lag time is just over three years between the violation and enforcement action).

50. *See* CORNERSTONE RESEARCH, SECURITIES CLASS ACTION FILINGS: 2018 YEAR IN REVIEW 26 (2019), https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2018-Year-in-Review [https://perma.cc/3HYB-VL5D] (reporting a median filing lag of eleven days in 2018 and a median filing lag of twenty-three days in years 1997 to 2017).

51. *See* Stephen J. Choi & A. C. Pritchard, *SEC Investigations and Securities Class Actions: An Empirical Comparison*, 13 J. EMPIRICAL LEGAL STUD. 27, 28 (2016).

52. *See* ENFORCEMENT MANUAL, *supra* note 43, §§ 2.5.1, 3.2.9.7, 3.3.1–.7.

53. In other words, the Division of Investment Management must sign off on any enforcement action against investment advisers and funds, and the Division of Corporation Finance must approve any enforcement action for accounting misrepresentations. *See id.* § 2.5.1.

Of the actions that are filed, about 45% are settled during the investigation and are filed as settled actions.[54] About half of initially contested cases are settled during the legal proceedings, so three-quarters of the cases the SEC brings are ultimately settled, and the rest are decided by default: on motion to dismiss, by summary disposition, or after trial.[55]

If the defendant is found to have violated securities laws, the SEC can impose a panoply of sanctions and remedies: injunctions and cease-and-desist orders, monetary penalties (including fines and disgorgement), and the most fearsome of them all: professional bars and registration revocations.[56] The SEC can also ask the court to appoint a receiver, freeze assets, or require an accounting. The Commission has the opportunity to be more creative in settlements, where it has asked defendants to compensate investors,[57] to pay for an independent monitor,[58] and to review and revise internal policies and procedures.[59] Perhaps most famously, the SEC required Tesla, a public company, to preclear the CEO's Twitter activity when it became clear that Elon Musk could not be trusted to tweet without adult supervision.[60]

When adopted in the 1930s, the securities laws did not authorize the SEC to obtain any monetary relief—only injunctions, registration revocations, and professional bars. The SEC sometimes obtained compensatory relief in settlements, but it did not seek monetary relief in court until the 1960s.[61] Beginning in the 1960s, the SEC asked courts for relief ancillary to injunctions, including disgorgement and accounting, to deprive fraudsters of their wrongful gains and to bolster its enforcement effort.[62] The measure of the disgorgement remedy is the somewhat vaguely defined ill-gotten gain, which is similar to but not coextensive with restitution, and includes any "tangible profit causally connected" to the

54. Of 8,197 cases in the dataset, 3,662 settled during the investigation. In recent years, the percentage of settled actions has increased to more than half (869 of 1678 cases filed between January 20, 2017 and September 30, 2018—51.8%—were settled during the investigation).

55. *See* Urska Velikonja, *Are the SEC's Administrative Law Judges Biased? An Empirical Investigation*, 92 WASH. L. REV. 315, 346 & n.204, 347 & tbl.3 (2017).

56. *See* Securities Exchange Act of 1934 § 21(d), 15 U.S.C. § 78u(d) (2012).

57. *See* WL Ross & Co. LLC, Investment Advisers Act Release No. 4494, 2016 WL 11467650, at *6 (Aug. 24, 2016).

58. *See* Lovelock & Lewes, Exchange Act Release No. 64184, 2011 WL 1295803, at *23–26 (Apr. 5, 2011).

59. *See id*. at *20–22.

60. *See* SEC v. Tesla, Inc., No. 1:18-cv-8947-AJN-GWG, slip op. at 1–2 (S.D.N.Y. Apr. 30, 2019), ECF No. 17.

61. *See* John D. Ellsworth, *Disgorgement in Securities Fraud Actions Brought by the SEC*, 1977 DUKE L.J. 641, 642–43 (describing SEC settlements from 1943 and 1945 that resulted in investor compensation despite the lack of statutory authority to order monetary relief).

62. In 1965, the SEC sued Texas Gulf Sulphur Co. and its insiders for accounting fraud and insider trading, seeking restitution. *See* SEC v. Texas Gulf Sulphur Co., 258 F. Supp. 262, 275 (S.D.N.Y. 1966). In 1971, the Second Circuit decision in *SEC v. Texas Gulf Sulphur Co*. recognized that the SEC had authority to seek court-ordered disgorgement of illegal trading profits from corporate insiders who traded on material nonpublic information. *See* 446 F.2d 1301, 1307–08 (2d Cir. 1971).

securities violation.[63] Unlike restitution, which aims to make investors whole, disgorgement aims to deprive the wrongdoer of ill-gotten gain.[64] The SEC has sought disgorgement when there are no obvious investors who lost out (for example, in FCPA cases), where investors cannot easily be identified (for example, in insider trading cases), or where the SEC has no intention of distributing collected monies to investors (for example, in cases where the costs of distribution are high relative to the collected amount).[65] Also, the SEC has sought to hold one party liable for disgorgement of the improper profits of defendant and non-defendant third parties.[66] But much of the time, the SEC seeks disgorgement of the defendant's profits in order to distribute that disgorgement to harmed investors.[67]

The SEC did not have express statutory authority to order disgorgement in administrative proceedings until 1990.[68] There is currently no statutory provision that expressly gives the SEC the power to seek disgorgement in court, nor one that gives courts the power to order disgorgement. But since 1984, Congress has enacted six securities statutes that recognize court-ordered disgorgement as a remedy in SEC enforcement actions.[69] Thus, the conspicuous omission of disgorgement as a legally authorized remedy does not imply that Congress intended for the SEC to obtain disgorgement only in administrative proceedings. Rather, courts had "routinely ordered disgorgement" in SEC actions well before 1990,[70] so both the SEC and lawmakers discussing the then-proposed Securities Enforcement Remedies and Penny Stock Reform Act assumed that the SEC did not need statutory authorization to seek equitable relief such as disgorgement.[71] Most recently, the Dodd–Frank Act in 2010 amended the Commodity Exchange Act to specifically authorize the CFTC to obtain equitable restitution and

63. SEC, REPORT PURSUANT TO SECTION 308(C) OF THE SARBANES OXLEY ACT OF 2002, at 33, https://www.sec.gov/news/studies/sox308creport.pdf [https://perma.cc/4WN6-JNNM].

64. *See* SEC v. Blavin, 760 F.2d 706, 713 (6th Cir. 1985) ("The purpose of disgorgement is to force 'a defendant to give up the amount by which he was unjustly enriched' rather than to compensate the victims of fraud." (quoting SEC v. Commonwealth Chem. Sec., Inc., 574 F.2d 90, 102 (2d Cir. 1978))).

65. *See* Urska Velikonja, *Public Compensation for Private Harm: Evidence from the SEC's Fair Fund Distributions*, 67 STAN. L. REV. 331, 340–41, 351–56 (2015).

66. *See, e.g.*, SEC v. First Jersey Sec., Inc., 101 F.3d 1450, 1475 (2d Cir. 1996).

67. *See* Velikonja, *supra* note 65, at 334 (estimating that "[b]etween 2004 and 2012, the SEC used fair funds to distribute more than 75% of all collected monetary penalties," which included disgorgement).

68. *See* Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, §§ 202(a), 203(e), 104 Stat. 931, 937–40 (codified at 15 U.S.C. §§ 78u-2(e), 78u-3(e) (2012)).

69. *See* Donna M. Nagy, *The Statutory Authority for Court-Ordered Disgorgement in SEC Enforcement Actions*, 71 SMU L. REV. 895, 903 (2018) (discussing "the Insider Trading Sanctions Act of 1984 (ITSA); the Insider Trading and Securities Fraud Enforcement Act of 1988 (ITSFEA); the Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (Remedies Act); the Private Securities Litigation Reform Act of 1995 (PSLRA); the Sarbanes–Oxley Act of 2002; and the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd–Frank Act)" (footnotes omitted)).

70. *See id.* at 910–11 & n.94 (citing *Hearings on S. 647 Before the Subcomm. on Securities, Insurance, and Investment of the Comm. on Banking, Housing, and Urban Affairs*, 101st Cong. 426 (1990) (written responses of Richard Breeden, Chairman, SEC)).

71. *See id.*

disgorgement.[72] No such authorization appeared necessary for the SEC: section 922 of the Dodd–Frank Act authorized the SEC to reward whistleblowers based on "any monies, including penalties, disgorgement, and interest" ordered in "any judicial or administrative action."[73]

B. *KOKESH*, *GABELLI*, AND THE STATUTES OF LIMITATIONS IN SECURITIES ENFORCEMENT

Statutes of limitations and statutes of repose impose time limits on agency enforcement actions. Some agencies enforce statutes that include specific limitations provisions for the violations they prosecute.[74] SEC enforcement, on the other hand, is subject to section 2462, the federal catchall five-year statute of limitations, which applies to any "action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise."[75] Many of the criminal securities violations have longer statutes of limitations: fraud against a financial institution comes with a ten-year limitations period,[76] and other securities crimes have a six-year limitations period.[77] Unlike criminal courts, which can toll statutes of limitations for up to three years in cases with foreign evidence or when the defendant avoids capture, there is no parallel statutory tolling provision in civil enforcement actions.[78] As a statute of limitations, section 2462 is in theory subject to equitable tolling in the event of fraudulent concealment, that is, when a "defendant takes steps beyond the challenged conduct itself to conceal that conduct from the plaintiff."[79] However, that defense has rarely been advanced successfully.

Until recently, section 2462 did not pose much of an obstacle to enforcement. It was understood to be a statute of limitations that does not begin to run until the Agency discovers or reasonably should have discovered the misconduct instead of from the moment the violation was committed.[80] That changed in February 2013 when the Supreme Court held in *Gabelli v. SEC* that the statute of limitations under section 2462 begins to run when the violation is committed, not when

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72. Dodd–Frank Wall Street Reform and Consumer Protection Act § 744, 7 U.S.C. § 13a-1(d) (2012).

73. *Id.* § 922, 15 U.S.C. § 78u-6(a)(1), (a)(4)(a), (g)(3)(A) (2012).

74. *See* Nikhil Gore, Kokesh v. SEC *and Implications for Consumer and Financial Regulatory Agencies*, COV FIN. SERVS. (June 9, 2017), https://www.covfinancialservices.com/ 2017/06/kokesh-v-sec-and-implications-for-consumer-and-financial-regulatory-agencies/ [https://perma.cc/HU77-XJ7Q] (noting that UDAAP laws (prohibiting unfair, deceptive, or abusive acts or practices) and most consumer financial-protection laws include clear statutes of limitations for the CFPB).

75. 28 U.S.C. § 2462 (2012).

76. 18 U.S.C. § 3293 (2012).

77. *See* 18 U.S.C. § 3301 (2012) (providing a six-year limitations period for certain securities fraud offenses).

78. *See* CHARLES DOYLE, CONG. RESEARCH SERV., R 31253, STATUTE OF LIMITATION IN FEDERAL CRIMINAL CASES: AN OVERVIEW 8–11 (2017), https://fas.org/sgp/crs/misc/RL31253.pdf [https://perma.cc/KVW2-KJ28] (explaining the conditions for tolling in federal criminal law).

79. Gabelli v. SEC, 568 U.S. 442, 447 n.2 (2013); *see also* SEC v. Geswein, 2 F. Supp. 3d 1074, 1084–85 (N.D. Ohio 2014) (affirming that *Gabelli* did not prohibit equitable tolling of the statute of limitations and denying a motion to dismiss because equitable tolling was available to the SEC).

80. *See* SEC v. Gabelli, 653 F.3d 49, 58–60 (2d Cir. 2011).

the SEC discovers the violation.[81] The Court offered two justifications. First, the SEC's immense investigative powers mean that the SEC reasonably should be able to discover any violation from the moment it is committed.[82] And second, a limitations period predicated on discovery would introduce legal uncertainty and unjustly deny a defendant repose.[83]

At the time of *Gabelli*, it was understood that section 2462 applied only to penalties, which included civil fines and forfeiture orders, but not to remedial measures, imposed to redress a private injury, such as restitution or an injunction.[84] As a result, if the SEC did not discover misconduct until it was too late to impose a civil fine, it could still bring an action to seek remedies that were not penalties, including disgorgement, which was understood as necessary to prevent offenders from profiting from fraud and thus as an equitable or remedial measure.[85]

Precedent distinguishes penalties imposed to punish infractions of public law from remedial measures that compensate injured parties and redress a private injury.[86] Polar cases are easy to identify—a fine on the one hand and restitution on the other—but disgorgement does not fit neatly in either category because its goal is not compensation but preventing profiteering. Although collected disgorgement is often distributed to investors, according to the SEC, the primary purpose of disgorgement is not compensation.[87]

In 2017, the Supreme Court was asked to decide in *Kokesh v. SEC* whether disgorgement was a penalty. The Court developed a three-part test to decide the issue. It held that: (1) sanctions are penalties when they address wrongs to the public, not to the individual; (2) sanctions are penalties when they seek to deter misconduct, rather than to compensate; and (3) sanctions are penalties unless used exclusively to compensate injured investors.[88] That disgorgement is sometimes used to compensate victims was not relevant.[89] Rather, the Court held, disgorgement is imposed to deter violations, which is "inherently punitive."[90]

81. *See* 568 U.S. at 448, 454.

82. *See id.* at 450–51.

83. *See id.* at 452.

84. *See, e.g.*, Meeker v. Lehigh Valley R.R. Co., 236 U.S. 412, 423 (1915) (discussing § 2462's precursor statute).

85. *See, e.g.*, Timbervest LLC, Investment Company Act Release No. 31830, 2015 WL 5472520, at *15 & n.69 (Sept. 17, 2015) [hereinafter Timbervest Release] (opining that professional bars, cease-and-desist orders, and disgorgement are all equitable remedies, not punishments).

86. *See* Kokesh v. SEC, 137 S. Ct. 1635, 1642–43 (2017).

87. *See id.* at 1643 (quoting several cases finding that the purpose of disgorgement is deterrence, including: SEC v. Fischbach Corp., 133 F.3d 170, 175 (2d Cir. 1997); SEC v. First Jersey Sec., Inc., 101 F.3d 1450, 1474 (2d Cir. 1996); SEC v. Rind, 991 F.2d 1486, 1491 (9th Cir. 1993); and SEC v. Texas Gulf Sulphur Co., 312 F. Supp. 77, 92 (S.D.N.Y. 1970), *aff'd in part, rev'd in part*, 446 F.2d 1301 (2d Cir. 1971)).

88. *See id.* at 1643–44.

89. *See id.* at 1644 ("Although disgorged funds may often go to compensate securities fraud victims for their losses, such compensation is a distinctly secondary goal." (quoting *Fischbach Corp.*, 133 F.3d at 175) (internal quotation marks omitted)).

90. *Id.* at 1643. This is neither the time nor the place to discuss this particular point, but the observation proves too much: any sanction imposed by the government for violating laws will inevitably deter. That the government has the right to investigate at all will deter some violators.

In developing the test, the Court pushed the line between penalties and remedial measures far in favor of penalties, leaving little room for measures that are remedial (as opposed to compensatory) in nature.[91] Under *Kokesh*, a measure is either entirely compensatory or else a penalty. Thus understood, all remedies in SEC enforcement actions, with the exception of restitution to be paid entirely to injured investors,[92] can be construed as punitive. If so, as several district courts have reasoned,[93] then the SEC cannot prosecute violations older than five years.

The case of Charles Kokesh illustrates the problems that *Gabelli* and *Kokesh* pose for securities enforcement. Charles Kokesh owned and controlled two registered investment-advisory firms.[94] From 1995 until 2007 when the funds were dissolved, Kokesh took illegal distributions, paid himself unearned performance fees, and reimbursed unauthorized expenses—ultimately misappropriating $45 million from more than 21,000 investors who put money in the funds he managed.[95] Kokesh "specifically targeted smaller investors (those investing $5,000 or less) because they would be less likely to sue if they discovered his schemes."[96] To conceal his misappropriation, Kokesh distributed false proxy statements to his investors and filed false reports with the SEC.[97]

Evidence of misconduct was discovered during the dissolution proceedings. After a relatively brief investigation, the SEC filed suit against Kokesh in 2009, some two years after the last violation.[98] After six years of legal wrangling and a five-day jury trial, the SEC prevailed on all counts, and the district court entered final judgment against Kokesh.[99] The district court ordered Kokesh to pay nearly $35 million in disgorgement of wrongfully obtained profits, plus more than $18 million in prejudgment interest and a $2,354,593 civil fine.[100] The civil fine imposed on Kokesh was relatively small because, under *Gabelli*, only violations that took place within the five years before suit could be the basis for a civil

91. Toward the end of the opinion, the Court equivocates, suggesting that disgorgement of illegal gains net of "marginal costs incurred in producing the revenues" could be remedial and thus not subject to a limitations period. *Id*. at 1644–45 (quoting RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 51 cmt. h (AM. LAW INST. 2010)). But the Court reverses course in the following paragraph, stating that disgorgement orders are "intended to punish, and label defendants wrongdoers," and thus fall within the limitations period in § 2462. *Id*. at 1645 (quoting Gabelli v. SEC, 568 U.S. 442, 452 (2013)) (internal quotation marks omitted).

92. *See id*. at 1643–44.

93. *See, e.g*., SEC v. Cohen, 332 F. Supp. 3d 575, 592–95 (E.D.N.Y. 2018) (finding SEC's request for injunctive relief would function to punish defendants and was therefore a penalty); SEC v. Jones, 300 F. Supp. 3d 312, 318 (D. Mass. 2018) (finding SEC's request for injunctive relief "would simply admonish Jones to obey the federal securities laws" in the future, and thus would constitute a penalty).

94. *Kokesh*, 137 S. Ct. at 1641.

95. Complaint at 1, 4, SEC v. Kokesh, No. 6:09-cv-1021 (D.N.M. Oct. 27, 2009) [hereinafter *Kokesh* Complaint].

96. SEC v. Kokesh, No. 09-cv-1021-SMV/LAM, 2015 WL 11142470, at *5 (D.N.M. Mar. 30, 2015).

97. *Kokesh* Complaint, *supra* note 95, at 1–2.

98. *See id*. at 14.

99. *Kokesh*, 2015 WL 11142470, at *1, *11.

100. *Id*. at *10. The civil fine equaled "the amount of funds that [Kokesh] himself received during the limitations period." *Id*. at *5.

fine.[101] In the case of Charles Kokesh, that included violations committed between October 2004 and July 2007—when his funds were dissolved—but not violations committed between 1995 and October 2004.[102]

If—as the Supreme Court held—disgorgement operates as a penalty, the implication of *Kokesh* coupled with *Gabelli* is that the SEC can only seek disgorgement of ill-gotten gains obtained up to five years before the SEC files suit, and no more. It does not matter that the fraudulent scheme lasted for over a decade, nor does it matter that the defendant concealed his violations. Thus, the disgorgement order against Kokesh was ultimately reduced to $5 million; in similar cases, *Kokesh* has barred the SEC from ordering more than $1.1 billion in disgorgement.[103]

More consequential is the yet unanswered question of what other remedies might be "penalties" under the Supreme Court's reasoning. So far, two district courts have opined that obey-the-law injunctions are also subject to the five-year limitations period,[104] and a circuit court has suggested the same about professional bars.[105] If *Kokesh* is interpreted as broadly as it has been by the two district courts, section 2462 operates as an absolute bar on enforcement of violations older than five years.

II. DISGORGEMENT AFTER *KOKESH*

More than two years after the *Kokesh* decision, its impact remains speculative. The only two serious empirical studies to date are limited in their approach and samples. Brown, Gale, and Huffman find a small but statistically significant negative impact of the *Kokesh* decision on the value of common stock in the average public firm.[106] The finding is interesting but limited: public firms are only 6% of SEC defendants and pay just 3.5% of total disgorgement.[107] Individual defendants like Charles Kokesh, on the other hand, constitute almost 60% of SEC defendants and are ordered to pay over 90% of all disgorgement.[108]

Verity Winship extends her research to include all SEC defendants, but limits its scope to insider trading violations.[109] Using prejudgment interest to estimate

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101. *See* Gabelli v. SEC, 568 U.S. 442, 444, 448 (2013).

102. *See Kokesh* Complaint, *supra* note 95, at 1 (noting that Kokesh's fraud took place from "at least 1995 through July 2007").

103. *See* 2019 ENFORCEMENT REPORT, *supra* note 26, at 21.

104. *See* cases cited *supra* note 93.

105. *See* Saad v. SEC, 873 F.3d 297, 304 (D.C. Cir. 2017) (remanding to the SEC to determine whether a permanent bar on defendant's FINRA registration was "impermissibly punitive" in light of *Kokesh*).

106. *See* Brown, Gale & Huffman, *supra* note 27, at 3–4.

107. *See infra* Section III.B.2; Appendix, Table A. Public firms paid only $5.1 billion of the total $144.9 billion of disgorgement ordered (including cases where part of the amount is credited with payments in parallel proceedings). Data on file with author.

108. *See infra* Section III.B.2; Appendix, Table A. The figures include disgorgement ordered in SEC proceedings and credited with payments in parallel proceedings. If parallel proceedings are excluded, individuals and their shell companies pay 58% of all disgorgement. *See infra* Section III.B.2.

109. *See generally* Winship, *supra* note 28.

the time periods for which disgorgement was ordered, Professor Winship estimates that about 2% of disgorgement imposed in insider trading cases is for violations older than five years.[110] She acknowledges that her calculations *understate* the extent of the *Kokesh* problem because the SEC does not always ask for full prejudgment interest and judges do not always order it.[111] As shown in more detail in this Part, approximately 12% of insider trading cases allege violations older than five years, making it the category most commonly prosecuted within the five-year period.[112] On average, 37% of SEC cases charge violations older than five years.[113]

Instead of relying on indirect proxies such as stock prices and prejudgment interest orders, this Article reviews charging documents to provide an estimate of how often the SEC attempts to enforce violations older than five years. Like all approaches, the one adopted in this Article has drawbacks, as discussed in the following section describing the methodology. The remainder of this Part analyzes the impact of the specific holding in *Kokesh* that extended the five-year statute of repose in section 2462 to disgorgement claims.

Whether time bars reduce potential monetary penalties is a difficult question to answer empirically even if, in theory, the answer has to be "yes." There are at least three reasons for this. First, the SEC can take the bite out of the statute of limitations by securing an agreement with the defendant to toll the limitations period pending the investigation.[114] Without a tolling agreement, the SEC could seek to impose only preventive and compensatory sanctions for violations entirely outside the five-year period, such as an injunction or restitution, but could still bring the case. Second, if there are ready substitutes to disgorgement that the SEC could impose, the impact of the limitations period will be muted.[115] Third, if the SEC cannot bring an action, other public and private enforcement agents can sometimes step up in its place and make up for the shortfall.[116] This Part analyzes the first question in more detail, whereas Part IV delves into the latter two.

A. DESCRIPTION OF APPROACH

The data reported and studied in this Article was hand-collected from *Select SEC and Market Data Reports* (Reports) that the SEC prepares annually and publishes on its website.[117] The Reports include a list of all enforcement actions filed

110. *See id.* at 1011.

111. *See id.* at 1012 n.74.

112. *See infra* Table 3.A.

113. *Id.*

114. *See* Mike Koehler, *Foreign Corrupt Practices Act Continuity in a Transition Year*, 70 S.C. L. REV. 143, 201–02 (2018) ("[S]tatute of limitations issues are meaningless when, as often occurs, issuers under FCPA scrutiny waive statute of limitations defenses or agree to toll the statute of limitations.").

115. *See infra* Section IV.A.1 (suggesting that the feasibility of substitute remedies is uncertain given the lack of clarity whether noncompensatory remedial measures are considered penalties).

116. *See generally* Amanda M. Rose, *The Multienforcer Approach to Securities Fraud Deterrence: A Critical Analysis*, 158 U. PA. L. REV. 2173 (2010) (discussing the advantages and disadvantages of overlapping enforcement regimes); *see also infra* Section IV.A.1.

117. *See Reports and Publications*, SEC, https://www.sec.gov/reports [https://perma.cc/F54D-J3YD] (last visited Sept. 27, 2019).

during the fiscal year, organized by subject matter and date. The dataset includes all independent enforcement actions[118] filed in FY 2010 to the end of FY 2018 (that is, from October 1, 2009 to September 30, 2018) and resolved by September 30, 2018. The period includes three fiscal years before the Court decided *Gabelli* (on February 27, 2013) and ends almost sixteen months after the Supreme Court decided *Kokesh*. The period was selected to include the enforcement action against Charles Kokesh—filed on October 27, 2009—and to end with the last full fiscal year for which data is available.

In order to determine whether the *Gabelli* and *Kokesh* decisions potentially impact enforcement, I analyzed charging documents to record the allegations against each defendant.[119] If the complaint or the OIP included allegations of specific violations that took place more than five years before filing, the case was coded as either partly or entirely outside the limitations period, depending on when the alleged violations took place.[120]

The approach is imperfect. Many violations are not completed on a single day. Some are ongoing, where some elements of a claim occur before the limitations period and others after. Some securities violations are so-called continuing, rather than discrete, violations.[121] Where possible, I took these factors into account. Unfortunately, charging documents do not always provide sufficient detail and errors are inevitable. Moreover, allegations in complaints are sometimes untested. The SEC might not be able to prove all alleged violations in contested litigation, and if it can prove them, might not seek civil fines and disgorgement for some or all violations.[122] These shortcomings notwithstanding, complaints and OIPs are typically the only source of facts that is consistently made available in SEC enforcement actions. Where other sources are available—news stories

118. *Id.* In a given year, the SEC files a variety of cases. These include: (1) delinquent filing actions against reporting companies for failure to file periodic reports; (2) follow-on actions barring previously convicted or sanctioned brokers, investment advisers, transfer agents, and other market participants from operating in financial markets, and barring auditors and attorneys from appearing before the Commission; and (3) contempt proceedings to enforce prior orders—all of these were excluded from this analysis because the SEC or another agency already established the violation in an earlier action. This analysis includes only so-called standalone or independent actions, in which the SEC seeks to establish that a defendant violated the securities laws. *See* Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 CORNELL L. REV. 901, 933–40 (2016) (outlining the methodology). In its annual enforcement reports, the SEC adopts the same distinctions and methodology. *See* SEC, Annual Report: Division of Enforcement 9 (2018) [hereinafter 2018 Enforcement Report], https://www.sec.gov/files/enforcement-annual-report-2018.pdf [https://perma.cc/9RRG-A922].

119. Charging documents in district court cases were retrieved from Bloomberg Law. Charging documents in cases filed in administrative proceedings were retrieved from either the SEC's website or Westlaw.

120. *See infra* Section II.C.1.

121. *See generally* SEC v. Kokesh, 884 F.3d 979, 981–85 (10th Cir. 2018) (distinguishing continuing violations, such as failure to supervise or omissions to act in compliance with a duty, from a series of repeated violations).

122. The SEC sometimes waives monetary penalties because the defendant cannot afford to pay. *See, e.g.*, Nob Hill Capital Mgmt., Inc., Exchange Act Release No. 73108, 2014 WL 4571396, at *3 (Sept. 16, 2014).

and company press releases, for example—they may be less reliable than the SEC's charging documents, which go through several layers of internal review.

In addition to collecting information on the timing of violations, I also collected information on defendant characteristics (whether the defendant is a firm or an individual; whether it is a public firm or a subsidiary of a public firm; whether it is a registered broker–dealer, investment adviser, transfer agent, accountant, etc.), case characteristics (the type of violation, litigation venue, etc.), case resolution (who prevailed; whether the case was settled or decided by default, summary judgment, or after trial; sanctions imposed), and information on any parallel proceedings where a portion of monetary penalties may have been credited.

A final caveat. The study can only analyze and report what is publicly available. Much of securities enforcement is confidential. One can observe actions that are filed, but not cases that the SEC declines to investigate or to prosecute,[123] including those declined due to expired limitations periods. Reported data may understate the scale of the problem created by the short limitations period to the extent that the SEC refuses to investigate and prosecute older violations. Moreover, resolutions in reported cases depend on factors such as defendants' willingness to settle, ability to pay, cooperation, and parallel actions, burying any signal in plenty of noise. As a result, the study is not designed to advance causal claims about either *Gabelli* or *Kokesh*—only informed estimates and educated guesses.

B. SUMMARY OBSERVATIONS

The entire dataset includes 8,197 individual defendants targeted in SEC enforcement actions filed in FYs 2010 to 2018. Of those, 2,850 were sued before February 27, 2013 when the Supreme Court decided *Gabelli*; 3,975 were sued after *Gabelli* and on or before June 5, 2017 when *Kokesh* was decided; and 1,372 defendants in the dataset were sued after *Kokesh*. A combined 6,825 defendants in the dataset were sued before *Kokesh*.

Just over 40% of defendants are firms (3,328 or 40.6%), and 9.5% (782) are public firms or subsidiaries of public firms.[124] Many defendant firms were registered in some capacity at some point during the violation or proceedings: 32.5% of firms (1,080) were federal- or state-registered broker–dealers, investment advisers, exchanges, NRSROs, transfer agents, PCAOB-registered auditors, or banks.

Almost two-thirds of defendants were sued in court (5,255 or 64.1%) and fewer than 36% were sued in administrative proceedings. A total of 44.7% (3,662 defendants) agreed to settle the enforcement action during the investigation and so the legal proceeding against them was filed as a settlement. Cases filed in

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123. *See* ENFORCEMENT MANUAL, *supra* note 43, §§ 2.2.1, 2.3.2, 3.1.2, (reminding SEC enforcement staff to "[c]onsider the statute of limitations issue early in the investigation").

124. The count of public firms and subsidiaries does not include firms whose stock trades in over-the-counter markets (OTC) but did not register under the Securities Exchange Act § 12(b). There are 47 such OTC firms in the sample.

administrative proceedings are much more likely to be settled than cases filed in court: 80.9% of administrative cases are filed as settled actions (2,381 of 2,942) compared with only 24.4% of cases filed in court (1,281 of 5,255 court cases are filed as settled). Additional summary statistics are reported in Table A in the Appendix.

Of 8,197 defendants in the dataset, as of September 30, 2018, 6,833 (83.4%) had resolved the SEC's enforcement proceeding completely as to liability and as to all remedies and sanctions. The SEC prevailed on at least one claim and obtained at least one kind of relief in 6,606 cases (96.7%). In 5,455 cases (79.8% of resolved cases and 82.6% of cases in which the SEC prevailed), the SEC obtained some form of monetary relief. That includes civil fines and disgorgement, as well as receivership and asset seizure. In 3,714 cases (54.4% of resolved cases and 56.2% of cases in which the SEC prevailed), the SEC obtained some disgorgement.[125] Only injunctions, cease-and-desist orders, and civil fines were imposed more often than disgorgement.[126]

C. DISGORGEMENT UNDER A TIME BAR

The Supreme Court's holding in *Kokesh* is somewhat difficult to follow, but it suggested that all disgorgement constitutes a penalty and is thus subject to the five-year limitations period.[127] This Part proceeds with that understanding. Because this reading potentially overstates the impact of the Court's holding, the observations in this section report the outer bound of the *Kokesh* holding.

1. General Observations

Of 8,197 cases in the dataset, 5,167 (63%) are cases where all alleged violations took place entirely within the five-year limitations period. In 2,802 cases (34.2%), some violations took place outside the limitations period and in 228 cases (2.8%), *all* alleged violations took place *outside* the five-year limitations period. In all, in 37% of cases at least one alleged violation took place outside the limitations period. The relative share of cases that allege violations *entirely inside* the five-year limitations period has gradually declined during the study period, from 71% in FY 2010 and 2011 to 51% in FY 2018.[128]

It is not clear why the SEC is increasingly charging older violations. It could be due to a change in the SEC's charging practices, its settlement rate,

125. The tally includes individual and joint-and-several liability, and disgorgement ordered by the SEC but deemed satisfied with payments in a parallel proceeding.

126. An injunction or a cease-and-desist order is imposed in almost every case resolved in favor of the SEC. Civil fines were imposed in 4,182 cases (61.2% of resolved cases and 63.3% of cases in which SEC prevailed).

127. The Court explained that although "district courts may distribute the [disgorged] funds to the victims, they have not identified any statutory command that they do so." Kokesh v. SEC, 137 S. Ct. 1635, 1644 (2017). Because disgorgement can but does not have to be paid as compensation, arguably all disgorgement is a penalty and thus subject to the five-year statute of repose.

128. The share of cases entirely inside the five-year SOL is as follows: FY 2010 (70.5%); FY 2011 (71.3%); FY 2012 (68.4%); FY 2013 (69.1%); FY 2014 (66.2%); FY 2015 (59.9%); FY 2016 (56.5%); FY 2017 (59.4%); FY 2018 (51.5%).

investigation delays, or changes in the mix of cases that the staff brings. In cases settled before initiation, the SEC and defendants can negotiate over not only sanctions and remedies, but also over which violations will be charged.[129] An increase in the relative share of settlements could be driving the trend, but the data do not appear to support that hypothesis. The relative share of settlements has increased over the years, but so has the share of older allegations in both settled and contested cases, as shown in Table 1 below.[130]

TABLE 1: PERCENTAGE OF CASES ENTIRELY INSIDE THE SOL

	Settled cases	**Contested cases**
Pre-*Gabelli*	57.9% (586)	75.2% (1,383)
Post-*Gabelli* & Pre-*Kokesh*	53.4% (1,025)	68.7% (1,412)
Post-*Kokesh*	48.1% (351)	63.8% (410)

Older violations in charging documents can either be the product of detection delays, investigation delays, or both. The average time from opening an MUI to enforcement action has increased marginally during the study period, from twenty-one months to two years,[131] so the increase could be partly due to investigation delays. Moreover, the SEC might be prosecuting cases of longer duration or reporting such older violations (or both) in charging documents with greater frequency. After Bernard Madoff's Ponzi scheme came to light and the financial crisis drained capital markets of liquidity, it became apparent that many asset managers were stealing from their investors. The federal government brought several hundred cases,[132] sometimes targeting misconduct that occurred a decade or more before filing the complaint.[133] That flood slowed to a trickle by FY 2012,[134]

129. *See* Roy Shapira, *A Reputational Theory of Corporate Law*, 26 STAN L. & POL'Y REV. 1, 52 (2015) (observing that the language used to describe the misconduct in the settled enforcement action against Citigroup did not allege intentionality and used a lower measure of investor losses than a parallel enforcement action for the same misconduct filed against an employee).

130. In a series of additional tests, I took into account defendant characteristics (is the defendant a public firm or subsidiary of a public firm?), professional registration, types of violations (that is, relying on SEC categorization in Reports), litigation venue, whether the case was settled before filing, and whether the case was filed before or after *Kokesh*—the disparity remains statistically significant. Even after controlling for case and defendant characteristics, settled cases are significantly more likely to include charges outside of the limitations period and the timing of the filing continues to matter: the SEC includes charges that extend beyond the five-year statute of limitations more often since *Kokesh* than before.

131. *See* Hoecker Memorandum, *supra* note 46, at 4 (reporting that 52% of cases were filed within two years of opening an MUI in FY 2017, compared with 64% in FY 2012).

132. *See* Press Release No. 10-1390, DOJ, Financial Fraud Enforcement Task Force Announces Results of Largest-Ever Nationwide Operation Targeting Investment Fraud (Dec. 6, 2010), https://www.justice.gov/opa/pr/financial-fraud-enforcement-task-force-announces-results-largest-ever-nationwide-operation [https://perma.cc/69BE-QP39].

133. *See, e.g.*, Charles Riley, *Prosecutors: Madoff Fraud Started in 1970s*, CNN (Oct. 2, 2012, 8:47 AM), https://money.cnn.com/2012/10/01/investing/madoff-fraud/ [https://perma.cc/96SP-P36W] (reporting that Bernard Madoff's fraud may have started more than 30 years before his indictment).

134. *Compare* SEC, SELECT SEC AND MARKET DATA FISCAL 2009, at 3 tbl.2 (2009) (reporting that the SEC filed 141 securities offering cases (21% of total actions filed)), *with* SEC, SELECT SEC AND

but the SEC has continued to file older cases. Under SEC Chair Jay Clayton (appointed on May 4, 2017, one month before the Court decided *Kokesh*), the SEC has focused on fraud against retail investors, including misappropriation by investment advisers that often takes a long time to discover and to prosecute.[135]

The SEC might also be including older allegations to demonstrate that the statute of limitations is a challenge for enforcement. Since *Kokesh*, SEC Chair Clayton has on multiple occasions testified in Congress about the negative impact of the *Kokesh* decision.[136] When asked about his wish list for the SEC, Commissioner Rob Jackson responded that a legislative fix to *Kokesh* was right at the top.[137] In recently filed complaints, the SEC has explicitly asked district courts for disgorgement, but has limited the demand to five years before filing.[138] Several settlements filed after *Kokesh* order payment of disgorgement within the five-year limitations period but also report the amount of disgorgement the SEC could not seek because of *Kokesh*.[139]

Whatever the reason for the increase in the relative share of cases that allege violations outside the limitations period, it appears that the SEC is often unable to detect and investigate violations fully within five years. There is no evidence to suggest that the SEC unreasonably delays detection or investigation of violations,[140] though it can delay prosecution through the use of tolling agreements.

With these caveats acknowledged, Table 2 below breaks out disgorgement potentially impacted by the *Kokesh* decision. Except in a handful of recently filed cases, the SEC does not disaggregate the portions of disgorgement inside and outside the five-year limitations period. The dataset associates monetary penalties with each case and produces tallies by summing all cases in a category. As a result, in Table 2 the aggregate amounts for cases *entirely inside* the limitations period and those *entirely outside* the limitations period report accurate figures. Aggregate statistics for cases with charges *partly outside* the limitations period include all disgorgement ordered, and thus overstate total disgorgement amounts

MARKET DATA FISCAL 2012, at 3 tbl.2 (2012) (reporting that the SEC filed only 89 securities offering cases (12.1% of total actions filed)).

135. *See* David J. Lynch, *SEC Boss Clayton Touts His Populist Shift*, FIN. TIMES (July 26, 2017), https://www.ft.com/content/5f77d784-721c-11e7-aca6-c6bd07df1a3c.

136. *See Oversight of the U.S. Securities and Exchange Commission: Hearing Before the S. Comm. on Banking, Housing, & Urban Affairs*, 115th Cong. 37–38 (2018) (statement of Jay Clayton, Chair, SEC); *Oversight of the U.S. Securities and Exchange Commission: Hearing Before the H. Comm. on Fin. Servs.*, 115th Cong. 66 (2018) (statement of Jay Clayton, Chair, SEC).

137. *See* Peter Rasmussen, *As* Lucia *Fades Away, the SEC Struggles to Deal with* Kokesh, BLOOMBERG L. (Nov. 15, 2018, 1:47 PM), https://news.bloomberglaw.com/bloomberg-law-analysis/analysis-as-lucia-fades-away-the-sec-struggles-to-deal-with-kokesh.

138. *See, e.g.*, Complaint at 1, 3, SEC v. AmeraTex Energy, Inc., No. 4:18-cv-00129, 2019 WL 3430276 (E.D. Tex. July 30, 2019).

139. *See, e.g.*, SEC v. Hall, No. 15-23489-CIV-ALTONAGA/O'Sullivan, 2017 WL 3635108, at *4 (S.D. Fla. June 29, 2017) (ordering Hall to pay $4,703,300.51 in disgorgement and prejudgment interest and adding that an additional $2,259,068 in ill-gotten gains was outside the five-year statute of limitations).

140. Nor is there evidence that the SEC *does not* unreasonably delay prosecution.

affected by *Kokesh*.[141] The study cannot allocate the amounts of disgorgement attributable to violations outside the limitations period because detailed information is not available. In some cases, such as the action against the Wyly brothers, who were ordered to pay $187 million in disgorgement for accounting fraud and insider trading that took place over 18 years, the bulk of the ordered disgorgement is outside the limitations period.[142] In others, only a small portion would be outside the limitations period. Reported figures thus overstate the significance of the five-year limitations period, but they are the best approximation available.

TABLE 2: DISGORGEMENT ORDERS (2010–2018)

	Including Parallel Cases	**Without Parallel Cases**
Entirely Inside SOL	$6.57 billion	$5.63 billion
Partly Outside SOL	$136.37 billion	$6.45 billion
Entirely Outside SOL	$2.00 billion	$1.72 billion

About 41% of disgorgement in cases without parallel enforcement proceedings is ordered in cases where all allegations are *inside* the limitations period, and 12% is ordered in cases where all allegations are *outside* the limitations period. The balance, $6.45 billion or 47%, is ordered in cases that straddle the five-year limit. In the aggregate, between $1.7 and $8.2 billion in disgorgement ordered in cases filed in FY 2010 to 2018 (of $13.8 billion) would have been potentially at risk if *Kokesh* were in place during the study period.

2. Variation by Type of Violation

Not all securities violations are created equal. Some are regularly detected much more quickly than others. It is relatively easy for an alert observer to catch a pump-and-dump scheme in the act. Computers can be programmed to detect unusual trading patterns and flag insider trading. Foreign bribery, on the other hand, may never come to light without a whistleblower complaint or a report by the company itself.[143]

141. Only the portion outside the limitations period is time barred under *Kokesh*. To use Charles Kokesh as an example, the tables and figures below include all $53 million as "disgorgement affected" by the *Kokesh* decision, even though he was ultimately ordered to pay $5 million (not zero, as the numbers used would imply).

142. *See* Final Form Brief for Appellants at 1, 33, SEC v. Wyly, 117 F. Supp. 3d 381 (S.D.N.Y. 2015), *appeal docketed* No. 15-2821-cv (2d Cir. Apr. 8, 2016).

143. *See* Alexander Dyck, Adair Morse & Luigi Zingales, *Who Blows the Whistle on Corporate Fraud?*, 65 J. FIN. 2213, 2225 (2010) (presenting data on entities that detect corporate fraud).

Once detected, some violations take longer to investigate than others.[144] Insider trading is usually detected quickly, but it can take a long time to establish a link between the trading account and the source of the information. Scienter is a key element of insider trading prosecutions and can be difficult to establish,[145] introducing delays. When going after remote fourth- or fifth-tier tippees, the SEC staff must meticulously build the case to prove that the trader trading knew that the source breached her fiduciary duties by passing along material non-public information.[146] That ordinarily requires cooperating witnesses and defendants who flip—and sometimes it even includes wiretapping.[147] By contrast, illegal trading by friends and family of corporate insiders often requires little more than a couple of Internet searches to identify the source of the information and their personal connection to the trader.[148]

On the other hand, foreign bribery takes a long time to detect and to investigate. The evidence is regularly voluminous and often located outside the United States.[149] When available, the evidence might not be sufficient to implicate the U.S. parent. The SEC might wait for the U.S. parent to complete an internal investigation. Targeting individuals responsible for the violation further delays the investigation.

As a result of these differences in detection and investigation delays, one would expect that the *Kokesh* decision would have a disparate impact on different types of enforcement actions, depending on the nature of the violation. Tables 3.A and 3.B below provide an overview of time-barred violations depending on the type of violation.

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144. Little is known about the possible delay between detection and opening an investigation. In the late 1990s and early 2000s, the SEC failed to investigate two multi-billion-dollar Ponzi schemes, perpetrated by Bernard Madoff and R. Allen Stanford, even after both were flagged by examinations staff and outside whistleblowers on multiple occasions. *See* SEC OFFICE OF INVESTIGATIONS, REPORT NO. OIG-509, INVESTIGATION OF FAILURE OF THE SEC TO UNCOVER BERNARD MADOFF'S PONZI SCHEME 21–22 (2009), https://www.sec.gov/about/offices/oig/reports/investigations/2009/oig-509.pdf [https://perma.cc/M8GV-7QFP] (reporting that the SEC received multiple specific complaints about Madoff's possible Ponzi scheme between 1992 and 2008, when Madoff's funds collapsed); SEC OFFICE OF INSPECTOR GENERAL, INVESTIGATION OF THE SEC'S RESPONSE TO CONCERNS REGARDING ROBERT ALLEN STANFORD'S ALLEGED PONZI SCHEME 16–28 (2010), https://www.sec.gov/about/offices/oig/reports/investigations/2010/oig-526.pdf [https://perma.cc/UV6A-JALM] (reporting that the SEC first received information about a possible Ponzi scheme operated by Allen Stanford in 1997, then opened and closed several MUIs before finally bringing an action in 2009).

145. *See, e.g.*, United States v. Newman, 773 F.3d 438, 447–55 (2d Cir. 2014) (discussing the high bar for establishing *mens rea* liability and the scant evidence available in the government's case).

146. *See, e.g.*, Salman v. United States, 137 S. Ct. 420, 423 (2016) (noting that the "tippee acquires the tipper's duty to disclose or abstain from trading if the tippee knows the information was disclosed in breach of the tipper's duty").

147. *See* SEC v. Galleon Mgmt., LP, 274 F.R.D. 120, 124–25 (S.D.N.Y. 2011) (compelling defendant to comply with the SEC's motion to produce wiretapped conversations that defendants provided to federal prosecutors as part of a parallel criminal investigation into the same alleged insider trading).

148. *See, e.g.*, Litigation Release No. 23780, SEC, Security Professional Charged with Insider Trading (Mar. 15, 2017), https://www.sec.gov/litigation/litreleases/2017/lr23780.htm [https://perma.cc/JCZ3-32PL] (reporting that Todd David Alpert learned of material non-public information while working as a security guard for a board member).

149. *See The Gray Cloud of FCPA Scrutiny Lasted Too Long in 2017*, *supra* note 47.

TABLE 3.A: SOL BY TYPE OF VIOLATION

	Cases Entirely Inside SOL	Cases Partly Outside SOL	Cases Entirely Outside SOL
Insider Trading	708 (87.8%)	82 (10.2%)	16 (2.0%)
Market Manipulation	736 (76.3%)	215 (22.3%)	13 (1.3%)
Miscellaneous	77 (76.2%)	22 (21.8%)	2 (2.0%)
Securities Offering	1,737 (67.1%)	820 (31.7%)	32 (1.2%)
Public Finance Abuse	212 (65.4%)	96 (29.6%)	16 (4.9%)
Issuer Reporting	657 (53.6%)	522 (42.6%)	47 (3.8%)
Investment Adviser, Transfer Agent & SRO	733 (51.5%)	642 (45.1%)	48 (3.4%)
Broker–Dealer	301 (48.9%)	296 (48.1%)	18 (2.9%)
FCPA	6 (4.0%)	107 (71.8%)	36 (24.2%)
All	5,167 (63.0%)	2,802 (34.2%)	228 (2.8%)

TABLE 3.B: DISGORGEMENT ORDERS BY TYPE OF VIOLATION

	Disgorgement Ordered (% cases)[a]	Disgorgement Inside SOL (% amount)[b]	Amount Potentially Affected (in $M)[c]
Insider Trading	89.4%	89.4%	59.3
Market Manipulation	66.1%	82.2%	80.2
Miscellaneous	13.5%	12.6%	10.3
Securities Offering	71.1%	55.5%	2,616.8
Public Finance Abuse	19.4%	12.6%	126.4
Issuer Reporting	28.2%	61.5%	418.1
Investment Adviser, SRO & Transfer Agent	49.0%	29.0%	1,494.3
Broker–Dealer	54.4%	23.5%	514.4
FCPA	64.6%	0%	2,848.0

[a] Includes all completely resolved cases in which the SEC prevailed.
[b] Aggregates disgorgement orders in cases in which all charges are inside the five-year limitations period, and does not include disgorgement ordered and deemed satisfied in a parallel action.
[c] Aggregates disgorgement in cases in which charges are partly or entirely outside the five-year limitations period, and does not include disgorgement ordered and deemed satisfied in a parallel action.

Insider trading and, to a somewhat lesser extent, market manipulation tend to be prosecuted much more quickly than the average case. Only 12.2% of insider trading and 23.6% of market manipulation cases allege violations older than five years, compared with 37% of cases overall.[150] In fact, it is not uncommon for the SEC to file an enforcement action for insider trading within days of the violation.[151] One might posit that larger disgorgement awards are correlated with violations of longer duration and delayed detection, but that does not appear to be the case for insider trading and market manipulation.

At the other end of the spectrum, FCPA cases frequently include violations that are not only partly, but rather entirely outside the limitations period (24.2% of FCPA cases).[152] Not a single dollar of disgorgement in FCPA cases was ordered in cases with violations entirely inside the limitations period. Defendants in FCPA investigations are typically large, public firms with international operations that face not only SEC investigations, but also criminal investigations by the U.S. Department of Justice (DOJ) and its international counterparts. FCPA defendants expect to settle with enforcement agencies and so they regularly sign tolling agreements with the SEC and the DOJ.[153] FCPA investigations usually take a long time, but tolling agreements reduce the pressure to investigate the matter quickly, so the average time to investigate an FCPA case is substantially longer than for most other kinds of cases.[154] As a result, reported figures overstate the statute of limitations problem somewhat—at least for FCPA cases.[155]

Securities offering cases and accounting fraud cases include a mix of violations that can lead to enforcement. Some violations take a long time to uncover, while others are detected quickly. Among the longer are the disclosure fraud and abuse of inside information by Samuel and Charles Wyly that took eighteen years from the first violation to the filing of the complaint.[156] Among the quicker is Elon Musk's tweet on August 7, 2018 announcing that he had secured funding to take

150. Data on file with author.

151. *See, e.g.*, Complaint for Violations of the Federal Securities Laws at 2–6, SEC v. Alda Ltd., No. 2:17-cv-01287-CCC-LDW (D.N.J. Feb. 24, 2017) (alleging that traders bought shares between February 10 and 14, 2017 and sold them on February 14 and 15, 2017 after Fortress acquisition was announced); Complaint and Jury Demand at 2, SEC v. Zhou, No. 1:15-cv-8796-TPG (S.D.N.Y. Nov. 9, 2015) (alleging that Zhou sold shares on announcement of a merger on November 2, 2015, one week before the SEC filed the complaint).

152. Data on file with author.

153. *See* Koehler, *supra* note 114, at 201–02.

154. *Compare id.* at 203 (reporting a four-and-a-half year median investigation period), *with* Hoecker Memorandum, *supra* note 46, at 4 (reporting a twenty-four month average investigation period for all enforcement actions in FY 2017).

155. *See infra* Section II.D. Individual defendants in FCPA cases have been more successful in avoiding tolling agreements. Two Och-Ziff executives prevailed against the SEC when the district court construed tolling agreements they had signed narrowly. *See* SEC v. Cohen, 332 F. Supp. 3d 575, 590 (E.D.N.Y. 2018).

156. *See* Complaint at 10, SEC v. Wyly, 950 F. Supp. 2d 547 (S.D.N.Y. 2013) (No. 10-cv-5760) (alleging in a 2010 complaint that the Wylys began trading on inside information in 1992).

Tesla private, when in fact there was no such commitment. The SEC filed a complaint against Musk a mere seven weeks after the tweet.[157]

Cases against financial intermediaries, including broker–dealers, investment advisers, transfer agents, and SROs are more likely than the average securities case to include older charges. Their violations consist of long-lasting customer-abuse schemes like those by Charles Kokesh,[158] Bernard Madoff,[159] and Allen Stanford,[160] and also well-concealed violations by sophisticated Wall Street firms.[161] Financial intermediaries are regularly ordered to disgorge and to compensate investors for losses from conflicted transactions such as cherry-picking, violations of suitability rules, receipts of kickbacks, charges of unwarranted fees and expenses to the fund, and even asset misappropriation—54.4% of cases against broker–dealers and 49% of cases against investment advisers included some disgorgement, and only 23.5% and 29% of total disgorgement ordered, respectively, was for violations entirely inside the limitations period.[162]

There is an important distinction between cases that target accounting fraud (that is, issuer reporting violations) and those that target financial intermediaries. As explained in more detail in Part III, accounting fraud cases rarely result in any disgorgement, except where executives traded on inside information while lying to public investors. Because disgorgement is so often ordered for insider trading that accompanied accounting manipulation, such violations are more likely to be prosecuted entirely within the limitations period. As a result of these characteristics, relatively few accounting fraud cases involve disgorgement orders—only 28.2%—and 61.5% of the aggregate disgorgement amount is ordered in cases entirely inside the limitations period.[163] (The aggregate amount at risk is also relatively small, in particular because a single action accounts for 45% of that amount.)[164]

157. *See* Complaint at 1, SEC v. Musk, No. 1:18-cv-8865 (S.D.N.Y. Sept. 27, 2018).

158. Litigation Release No. 23228, SEC, Federal Court Imposes $55 Million Final Judgment Against Investment Adviser CEO (Apr. 2, 2015), https://www.sec.gov/litigation/litreleases/2015/lr23228.htm [https://perma.cc/ZG2Q-LUKP].

159. Press Release No. 2008-293, SEC, SEC Charges Bernard L. Madoff for Multi-Billion Dollar Ponzi Scheme (Dec. 11, 2008), https://www.sec.gov/news/press/2008/2008-293.htm [https://perma.cc/N8EQ-FG58].

160. Press Release No. 2009-26, SEC, SEC Charges R. Allen Stanford, Stanford International Bank for Multi-Billion Dollar Investment Scheme (Feb. 17, 2009), https://www.sec.gov/news/press/2009/2009-26.htm [https://perma.cc/AKP4-QRHZ].

161. For example, in 2016, Merrill Lynch was ordered to pay $415 million in monetary penalties, including $57 million in disgorgement and prejudgment interest, because it used cash in custodial accounts "to fund its own business activities through a series of increasingly complex trades" and allowed "clearing banks to hold general liens over tens of billions of dollars of securities owned by its customers," contrary to clear prohibitions. Merrill Lynch, Pierce, Fenner & Smith Inc., Exchange Act Release No. 78141, 2016 WL 4363431, at *1, 19 (June 23, 2016).

162. *See supra* Table 3.B.

163. Data on file with author.

164. The judgment against the Wyly brothers accounts for $188 million of the $418 million in accounting fraud disgorgement potentially affected by *Kokesh*.

These deviations produce important disparate impacts that arise from the *Kokesh* decision. The relative alacrity in charging those who trade on inside information or manipulate markets in publicly traded securities is not (only) due to the hardworking staff who prosecute insider trading, but is also because the SEC, the Financial Industry Regulatory Authority (FINRA), and stock exchanges actively monitor the public markets.[165] Most insider trading prosecutions are initiated after an announcement of a tender offer that is accompanied by unusual trading patterns.[166] Once the SEC secures trading information from brokerages, it is only a matter of time before the enforcement staff finds informed traders, freezes their accounts when necessary, and serves them with a complaint. Similarly, unusual increases in trading volumes and in the prices of otherwise obscure pink-sheet stocks allow the staff to identify pump-and-dump schemes early and to prosecute perpetrators quickly.

Small-time offering frauds are also often discovered quickly, but for a different reason. Without much capital or a network of deep-pocket investors, offering frauds promising outlandish returns (for example, 10% per month) tend to unravel quickly.[167] That is good for the SEC because none of the violations are time barred. But investors rarely recover because the perpetrator has often already spent the funds he raised on otherwise unaffordable luxuries.[168]

3. Variation by Defendant Characteristics

Private firms are rarely charged with disclosure or accounting fraud, and public firms rarely trade on inside information. All types of defendants appear in cases associated with detection and investigation delays, as shown in Table 4.A below. About one-third of cases against individuals and the private shells they control include charges of violations older than five years. That share is higher for public firms and public-firm subsidiaries, at 47% and 55%, respectively.

165. *See* Perino, *supra* note 49, at 28 & tbl.3.

166. *See id*. at 47 tbl.12 (showing that 67% of insider trading prosecutions involve announcements of M&A activity).

167. *See* Complaint at 2, SEC v. Meli, No. 1:17-cv-00632 (S.D.N.Y. Jan. 27, 2017) (showing that the SEC filed suit only two years after the fraud started). On the other hand, however, the largest offering frauds can last a long time.

168. *See, e.g.*, Press Release No. 2018-141, SEC, SEC Charges Failed Fyre Festival Founder and Others with $27.4 Million Offering Fraud (July 24, 2018), https://www.sec.gov/news/press-release/2018-141 [https://perma.cc/E7SP-EAWK] (reporting that Billy McFarland used investor funds to pay for a penthouse apartment in Manhattan, travel by private plane, and socialize with celebrities); Press Release No. 2018-89, SEC, SEC Charges Owner of Alternative Investment Firm in Belize Airport Financing Scam, Release No. 2018-89 (May 16, 2018), https://www.sec.gov/news/press-release/2018-89 [https://perma.cc/LWD6-FPTN] (reporting that the perpetrator spent investor funds on "mortgage and property tax payments on his family's Florida mansion, multiple luxury automobiles, private school tuition for his children, $36,000 for his family's beach club membership, and almost $2.7 million to pay off credit cards").

TABLE 4.A: SOL BY TYPE OF DEFENDANT

	Cases Entirely Inside SOL	Cases Partly Outside SOL	Cases Entirely Outside SOL
OTC[169]	39 (83.0%)	8 (17.0%)	-
Government & NGO	66 (68.8%)	28 (29.2%)	2 (2.1%)
Individual	3,139 (64.5%)	1,603 (32.9%)	127 (2.6%)
Private Firm	1,532 (63.8%)	841 (35.0%)	30 (1.2%)
Public Firm	257 (52.7%)	197 (40.4%)	34 (7.0%)
Public Subsidiary	134 (45.6%)	125 (42.7%)	35 (11.9%)
All	5,167 (63.0%)	2,802 (34.2%)	228 (2.8%)

TABLE 4.B: DISGORGEMENT ORDERS BY TYPE OF DEFENDANT

	Any Disgorgement Ordered (% cases)[a]	Disgorgement Inside SOL (% amount)[b]	Amount Potentially Affected (in $M)[c]
OTC	40.5%	72.3%	5.6
Government & NGO	2.1%	100%	0
Individual	61.9%	51.6%	2,755.2
Private Firm	53.3%	73.5%	727.2
Public Firm	30.0%	7.0%	3,120.5
Public Subsidiary	58.6%	19.2%	1,559.3

[a] Includes all completely resolved cases in which the SEC prevailed.
[b] Aggregates disgorgement orders in cases in which all charges are inside the five-year limitations period, and does not include disgorgement ordered and deemed satisfied in a parallel action.
[c] Aggregates disgorgement in cases in which charges are partly or entirely outside the five-year limitations period, and does not include disgorgement ordered and deemed satisfied in a parallel action.

But the real differences emerge when looking at disgorgement orders only. Individuals are more likely than other types of defendants to be ordered to disgorge ill-gotten gains (in 61.9% of cases compared with 56.2% of cases overall). And when they are ordered to disgorge ill-gotten gains, more than half of disgorgement in the aggregate is imposed in cases where all violations are *inside* the limitations period (51.6%). The total amount of disgorgement potentially outside the five-year limitations period is nevertheless large: $2.75 billion.

Public firms and public-firm subsidiaries are ordered to disgorge ill-gotten gains at lower rates than individuals (in 30.0% and 58.6% of cases, respectively), but the bulk of the disgorgement they pay is for violations *outside* the limitations period. Only a combined 11% of aggregate disgorgement imposed on public firms and public-firm subsidiaries is ordered in cases where all violations are *inside* the limitations period. The total amount of disgorgement potentially outside the limitations period amounts to more than $4.7 billion.

When individuals are ordered to pay disgorgement for older violations, it is primarily for offering fraud (57% of the total amount). When public firms are ordered to pay disgorgement for older violations, it is primarily for FCPA violations (90.7% of the total amount). By contrast, public-firm subsidiaries are ordered to pay disgorgement for older violations in a wider variety of cases, for example, investment adviser violations (47.4% of total disgorgement) and mortgage-securities offering fraud (44.6% of total disgorgement).

D. THE IMPACT OF TOLLING AGREEMENTS

That a portion or all of the allegations in the complaint or the OIP are outside the five-year limitations period does not imply that any disgorgement will be affected. The SEC can secure a tolling agreement to stop the limitations clock and thus obtain penalties for violations older than five years at the time it files the enforcement action. Persons under investigation agree to sign tolling agreements because they hope to convince the staff not to sue. The chance that the SEC will sue increases considerably if a person refuses a tolling agreement and the staff already has sufficient information to bring a good-faith claim.[170] Because contested enforcement actions are so costly, large-firm defendants in particular regularly agree to toll the statute.

A typical SEC tolling agreement will stop the limitations clock for "any action or proceeding against [the defendant] . . . arising out of the investigation."[171] But tolling agreements are not a cure for short statutes of limitation or repose. Although the clock is stopped only for violations described in the agreement, time keeps running for later-discovered violations.[172] A tolling agreement can stop the clock but does not turn back time. For any violations that predate the tolling agreement by more than five years, the SEC's action is time barred.[173]

Little is known about the prevalence of tolling agreements. SEC enforcement actions rarely disclose tolling agreements.[174] They are reportedly common in

169. OTC firms, used as shorthand for firms whose stock trades in the over-the-counter market, are firms that are not listed on any exchange but are also not private because their stock trades freely. They are typically subject to periodic reporting requirements under § 13 of the Exchange Act. Securities Exchange Act of 1934 § 13, 15 U.S.C. § 78m (2012).

170. Conversation with Andrew Vollmer, former Deputy General Counsel, SEC, former partner in the securities enforcement practice, Wilmer Cutler Pickering Hale & Dorr LLP (June 2019) (on file with author).

171. SEC v. Cohen, 332 F. Supp. 3d 575, 589 (E.D.N.Y. 2018).

172. *See id.* at 590 ("By their plain terms, those agreements only tolled the statute of limitations applicable to actions arising out of the SEC's LIA investigation—not actions arising out of investigations that themselves arose out of the LIA investigation.").

173. *See id.* at 589, 592.

174. Among limited exceptions are Complaint at 3, SEC v. Proctor, 1:16-cv-00437-UNA (D. Del. June 14, 2016) (noting that defendant entered a tolling agreement "for the period from November 1, 2014 through June 15, 2016"); Complaint at 3, SEC v. Hall, 1:15-cv-23489-CMA (S.D. Fla. Sept. 17, 2015); Arthur Kaplan, Securities Act Release No. 10500, 2018 WL 2387360, at *1 (May 24, 2018).

FCPA cases.[175] Cooperating defendants regularly agree to toll the statute of limitations while they help the SEC bring their counterparts to justice.[176] Defendants sometimes disclose their agreements to toll the statute of limitations in their annual reports.[177] But without consistent disclosure, it is impossible to study the impact of tolling agreements directly.

Instead, I resort to an indirect proxy to study the prevalence of tolling agreements: I look at the subset of cases with allegations entirely outside the limitations period where the order imposing civil fines was issued after *Gabelli*. The dataset contains 156 cases that include allegations of violations entirely outside the limitations period and that were resolved after *Gabelli*. *Gabelli* did not bar enforcement of older violations, but it did bar a particular type of sanction: a civil fine.[178] After *Gabelli*, the SEC could initiate an action to seek an injunction or a cease-and-desist order, disgorgement, and professional bars, but could not obtain any civil fines for violations that occurred more than five years before filing.[179] So, under *Gabelli*, the SEC should not have been able to obtain a civil fine in any of the 156 cases—yet that is not what happened. The vast majority of these cases were settled (138 of 156, or 88%). Seventy-three percent of settled cases (and 79% of settlements that included non-zero monetary penalties) included civil fines, which could not be imposed but for a tolling agreement. Of the eighteen cases that were not settled, eight were dismissed because the district court held that the statute of limitations barred prosecution.[180] In five contested cases the SEC obtained civil fines, suggesting that the defendant signed a tolling agreement (that is, five of eighteen contested cases included a tolling agreement).[181]

175. *See* Koehler, *supra* note 114, at 201.

176. *See, e.g.*, Charles Loveless, Securities Act Release No. 3726, Exchange Act Release No. 76633, 2015 WL 8731726, at *3–4 (Dec. 14, 2015) (showing a cooperator who was charged in 2015 for violations that occurred in 2003 and 2004); Complaint at 6, SEC v. Slaine, No. 1:10-cv-00754-DAB (S.D.N.Y. Feb. 2, 2010) (showing a cooperator who was charged eight years after the last violation).

177. *See, e.g.*, Newmont Mining Corp., Annual Report (Form 10-K), at 171 (Feb. 21, 2017) ("We are conducting an investigation, with the assistance of outside counsel . . . . The investigation includes a review of compliance with the requirements of the U.S. Foreign Corrupt Practices Act and other applicable laws and regulations. The Company is working with the U.S. Securities and Exchange Commission ('SEC') and the U.S. Department of Justice with respect to the investigation. In March 2016, the Company entered into a one-year agreement with the U.S. SEC tolling the statute of limitations relating to the investigation, and in April 2016, entered into a similar agreement with the U.S. Department of Justice.")

178. *See* Gabelli v. SEC, 568 U.S. 442, 445, 447 n.1 (2013) (holding that the SEC must file an action to impose a civil fine "within five years 'from the date'" the violation occurred, quoting 28 U.S.C. § 2462 (2012), and noting that whether § 2462 applies to claims for disgorgement or injunctive relief were issues "not before us").

179. *See* Timbervest Release, *supra* note 85, at *15–16 (noting civil fines cannot be imposed where the "proceeding was not brought within five years of the violations," but finding this restriction does not apply to equitable remedies).

180. *See* SEC v. Cohen, 332 F. Supp. 3d 575, 595 (E.D.N.Y. 2018) (dismissing case against two defendants); SEC v. Gentile, No. 16-1619 (JLL), 2017 WL 6371301, at *1 (D.N.J. Dec. 13, 2017) (dismissing case against Gentile); SEC v. Graham, 21 F. Supp. 3d 1300, 1316–17 (S.D. Fla. 2014), *aff'd in part, rev'd in part*, 823 F.3d 1357 (11th Cir. 2016) (dismissing case against five defendants).

181. Only five Timbervest defendants avoided a civil fine as time-barred. *See* Timbervest Release, *supra* note 85, at *15–16.

This allows us to conclude that tolling agreements appear remarkably common in *settled* SEC enforcement actions and can soften the impact of a short limitations period. *Kokesh* potentially raises the price of signing a tolling agreement to the person under SEC investigation (as compared with the pre-*Kokesh* status quo), but so long as the person believes she has a decent chance of persuading the staff not to sue, she will sign the tolling agreement.

Although tolling agreements may be a standard feature of cases that are moving towards a settlement, they are less common in contested cases. As a result, contested cases present a challenge for the SEC after *Kokesh*. In such cases, the SEC can no longer obtain civil fines or disgorgement of ill-gotten gains for violations that predate the filing of the complaint by more than five years. The SEC will sometimes rush and file the case just before the five-year deadline,[182] but that is not always possible because the SEC does not yet have sufficient evidence to file suit.

As shown in Table 1, contested cases are less likely than settled cases to include older charges. Further, some types of cases are more likely to result in a settlement than others: cases involving public firms and public-firm subsidiaries are more likely to settle. For example, 80.3% of public firms and subsidiaries settled during the investigation, compared with 40.6% of individuals. Relatedly, some types of violations more frequently result in a settlement during the investigation than others. This is partly due to the type of defendants targeted—public companies are charged with FCPA and accounting fraud—but even individual defendants are more likely to settle FCPA and accounting fraud charges than they are to settle securities offering charges.[183]

Tables 5.A and 5.B below report on the number of contested cases and total disgorgement ordered in cases that included charges partly or entirely outside the five-year limitations period. These cases are less likely to have included a tolling agreement than settled cases. They include disgorgement orders in cases without parallel enforcement actions (that is, SEC-only cases), similar to the one imposed on Charles Kokesh, and are thus most at risk after *Kokesh*.

The method is imperfect in that it both overstates the size of the problem in contested cases because not all disgorgement is outside the limitations period, and understates the size of the risk posed by *Kokesh* because it excludes settled cases. Not all settled cases include a tolling agreement and, more importantly, *Kokesh* changes the calculus for defendants to toll the limitations period.[184] On net, the tables below provide a reasonable overview of the types of cases most likely to be affected by *Kokesh*.

182. In at least nine cases in the dataset, the SEC filed the enforcement action on the last day before the five-year limitations period expired. In a dozen more cases, the SEC filed the enforcement action less than a week before the limitations period expired. *See, e.g.*, Complaint at 3, SEC v. Villena, No. 1:18-cv-04309 (S.D.N.Y. May 15, 2018) (filing complaint one day before limitations period expired); Alexander v. Rekeda, Securities Act Release No. 9340, Exchange Act Release No. 67455, Investment Company Act Release No. 30140, 2012 WL 2920988, at *2 (July 18, 2012) (same).

183. Twenty-five percent (346/1408) of individuals settled during the investigation in securities offering fraud cases and more than 60% of individuals settled during the investigation in accounting fraud and FCPA (529/875) cases. Data on file with author.

184. Winship tries to deal with the problem by looking at prejudgment interest on disgorgement orders and calculates that approximately 2% of all interest payments in insider trading cases date longer

TABLE 5.A: DISGORGEMENT AT RISK (BY VIOLATION)

	Disgorgement at Risk (in $M)	Number of Contested Cases[a]
Securities Offering	1,751.9	253
Investment Adviser, SRO & Transfer Agent	311.1*	86
Issuer Reporting	268.4**	44
Broker–Dealer	31.0	35
Market Manipulation	29.4	28
Insider Trading	27.7	20
FCPA	13.5	2
Public Finance Abuse	7.3	10
Miscellaneous	0.2	1
Total	2,440.5	479

*The total includes $53 million imposed on Charles Kokesh.
** Of that total, $187.7 million was ordered in one action against brothers Samuel and Charles Wyly, whose appeal to the federal court of appeals was stayed pending *Kokesh* and will presumably succeed in partly avoiding payment of the ordered amount.
[a] The count includes all cases that included an order of disgorgement (that is, SEC-only disgorgement), that were not settled during the investigation, and that alleged at least some violations outside the limitations period.

TABLE 5.B: DISGORGEMENT AT RISK (BY DEFENDANT)

	Disgorgement at Risk (in $M)	Number of Contested Cases Affected[a]
Individuals	1,990.3*	319
Private Firms (incl. shell companies)	244.9	145
Public Subsidiaries	135.6	5
Public Firms	64.0	8
OTC Firms	5.6	2
Total	2,440.5	479

* The total includes $240.7 million imposed on Kokesh and the Wyly brothers—all affected by the *Kokesh* decision.
[a] The count includes all cases that included an order of disgorgement (that is, SEC-only disgorgement), that were not settled during the investigation, and that alleged at least some violations outside the limitations period.

than five years. *See* Winship, *supra* note 28, at 1011. But Winship herself acknowledged that her calculations *understate* the extent of the problem because the SEC does not always ask for full interest and judges do not always order it. *See id*. at 1012 & n.74.

As shown in Table 5.A, securities offering and investment adviser cases are disproportionately affected by the *Kokesh* decision. Over 71% of all disgorgement that is at risk and 52% of cases are for offering violations. Another 13% of at-risk disgorgement and 18% of cases involve asset misappropriation and fee overcharges of assets by investment advisers like Charles Kokesh.[185] What both categories have in common is that they include long-lasting schemes in which: (1) offenders manage large amounts of investor money typically raised in favorable (and less careful) market conditions, (2) the schemes are difficult to uncover, and (3) individual defendants regularly contest the charges. Relatedly, 82% of at-risk disgorgement is imposed on individual defendants, and another 10% is imposed on private firms, most of which are shell companies controlled by individuals. In other words, the main beneficiaries of *Kokesh* are individuals who offer fraudulent securities or steal from investors in the funds they control.

In some of these cases, the SEC could have uncovered misconduct sooner through regular examinations, but discovery within the five-year limitations period is unlikely given the limited resources that are available for ongoing examinations.[186] The SEC's Office of Compliance Inspections and Examinations (OCIE) aims to examine newly registered investment advisers, as well as those that have been registered for several years but have not been recently examined.[187] But a lot can happen in the period between examinations. Moreover, only registered advisers are subject to exams, not those who offer investment services without bothering to register. Without a periodic exam, evidence of violations may not surface until the tide goes out, revealing who—like Charles Kokesh—has been swimming naked.[188] Barring disgorgement of profits obtained more than five years before suit invites evasion and delays.[189]

185. The original order against Kokesh is in the dataset ($53 million) and it certainly was affected by the Supreme Court's decision.

186. In FY 2018, the SEC's Office of Compliance Inspections and Examinations (OCIE) examined approximately 17% of the more than 13,200 registered investment advisers, an increase from approximately 15% in 2017, but less than 10% of broker–dealers. *See* SEC OFFICE OF COMPLIANCE INSPECTIONS & EXAMINATIONS, 2019 EXAMINATION PRIORITIES 1 (2019), https://www.sec.gov/files/OCIE%202019%20Priorities.pdf [https://perma.cc/HAX2-UD27] [hereinafter OCIE, EXAMINATION PRIORITIES].

187. *See id.* at 7.

188. The quote "[i]t's only when the tide goes out that you know who's been swimming naked" has been attributed to Warren Buffett reflecting on the financial crisis. *See* Alex Crippen, *Warren Buffett Wearing "Belt and Suspenders" As Tide Went Out*, CNBC (June 29, 2009, 9:46 PM), https://www.cnbc.com/id/31617055 [https://perma.cc/N2FK-LJ5T].

189. *Cf.* Hoecker Memorandum, *supra* note 46, at 4 (listing several cases in which targets of SEC investigations provided false testimonies and obstructed investigations); *see also* DOYLE, *supra* note 78, at 3–5, 10–11 (discussing suspensions of statutes of limitation when the defendant conceals bankruptcy assets or flees).

III. THE IMPORTANCE OF DISGORGEMENT FOR SEC ENFORCEMENT

In footnote 3 of the *Kokesh* decision, the Court ominously remarked that it was not taking a position "on whether courts possess authority to order disgorgement in SEC enforcement proceedings."[190] That footnote has been widely understood to threaten court-ordered disgorgement in SEC actions. As explained in sections I.A–B, disgorgement in administrative proceedings is expressly authorized by statute, but it is time limited after *Kokesh*. Court-ordered disgorgement, on the other hand, is not expressly authorized by statute. That arguably means that courts may not order disgorgement at all. That would represent a major setback to SEC enforcement.

A. DISGORGEMENT IN THE AGGREGATE

As shown in Table 6 below, total disgorgement represents the bulk of monetary penalties imposed during the study period. In cases where the SEC was the only public enforcement agency to bring an action, it secured $22.8 billion in aggregate monetary penalties, of which $13.8 billion (or 61%) was disgorgement. Almost $10 billion of aggregate disgorgement was ordered in court cases.

The SEC refers the most serious cases to criminal authorities (that is, the DOJ). In these cases, the SEC usually brings an action but then moves to stay the civil or administrative proceeding while it waits for the resolution of the parallel criminal action. Once the defendant has been convicted or pleads guilty, the SEC moves for summary judgment on liability and secures civil fines and disgorgement, but is satisfied with payments in the parallel criminal case or agrees to credit payments in the parallel case. But the DOJ is not the only agency that brings cases alongside the SEC. FINRA, the CFTC, foreign criminal authorities and securities regulators, and private parties also order substantial monetary penalties for securities violations; the SEC sometimes deems its civil fine and disgorgement orders satisfied with payments to these other agencies and authorities. If all monetary penalties in SEC cases are included, disgorgement represents $144.9 billion of $154.7 billion in monetary penalties imposed during the nine fiscal years studied. Note that only two disgorgement orders represent 88% of the total. In enforcement actions against Madoff employees Eric Lipkin and Enrica Cotellessa-Pitz, the SEC secured a combined $128 billion in disgorgement.[191] Both orders were deemed satisfied with restitution and forfeiture in the corresponding criminal cases against Lipkin and Cotellessa-Pitz.[192]

190. Kokesh v. SEC, 137 S. Ct. 1635, 1642 n.3 (2017).

191. *See* SEC v. Cotellessa-Pitz, 1:11-cv-09302-LTS, slip op. at 3 (S.D.N.Y. Jan. 5, 2016), ECF No. 16 (ordering $97.3 billion in disgorgement); SEC v. Lipkin, No. 1:11-cv-03826-LTS, slip op. at 6 (S.D. N.Y. Jan. 5, 2016), ECF No. 10 (ordering $30.6 billion in disgorgement).

192. *See Cotellessa-Pitz*, slip op. at 3; *Lipkin*, slip op. at 6.

TABLE 6: DISGORGEMENT ORDERS (FY 2010–2018)

Total Monetary Penalties	$154.7 billion
Civil Fines	$9.8 billion
Disgorgement	$144.9 billion
Total Monetary Penalties (without credits in parallel cases)	$22.8 billion
Civil Fines (without credits in parallel cases)	$9.0 billion
Disgorgement (without credits in parallel cases)	$13.8 billion
In Court	$9.9 billion
In Administrative Proceedings	$3.9 billion
Median Disgorgement[a]	$379,841 ($337,832 for SEC-only cases)
Median Disgorgement as % of Monetary Penalties[a,b]	78.1%

[a] Includes only cases where some disgorgement was ordered.
[b]Calculated per defendant. Includes cases with credited disgorgement in a parallel action.

Disgorgement represents the bulk of monetary penalties not only in the aggregate but also in individual cases. The median defendant who is ordered to pay some disgorgement faces $379,841. Defendants do not pay disgorgement in every case where they are ordered to pay monetary penalties. But where a defendant is ordered to pay disgorgement, disgorgement represents 78.1% of monetary penalties ordered (using the median amount).

B. DISGORGEMENT VARIATIONS

The harm to enforcement in a world without disgorgement would not be evenly distributed. Some violations generate more substantial illegal profits than others, and some types of defendants are more likely to be ordered to pay disgorgement than others.

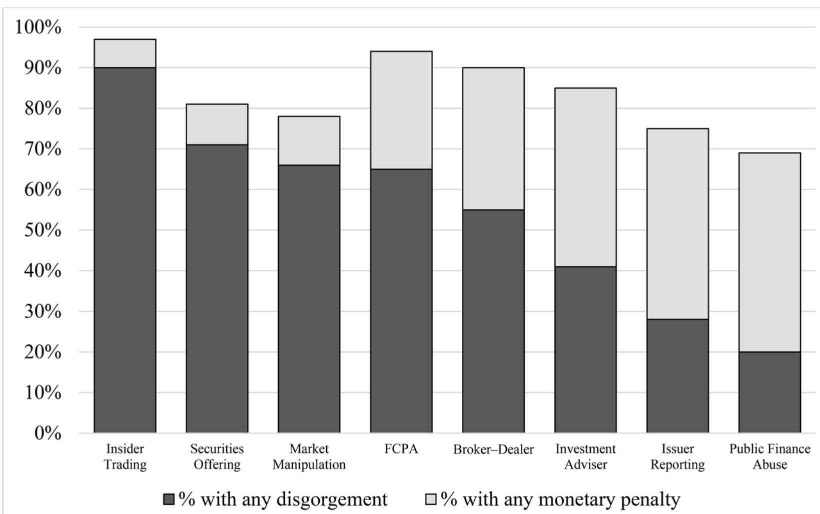
1. Variation by Type of Violation

The SEC typically orders disgorgement where the defendant obtains ill-gotten gains from the violation. That includes offering fraud where the defendant misappropriates invested funds or obtains funds on the basis of false statements; an investment adviser reimburses unauthorized expenses; and insider trading and foreign bribery. Firms charged with accounting fraud, typically exchange-listed companies, rarely pay disgorgement because accounting manipulation harms the public markets without a direct benefit to the firm.[193]

193. To be fair, fraud often inflates firms' stock prices. During the period of manipulation, firms issue new stock, acquire companies using their stock as consideration, and borrow at lower interest rates. *See* Monsanto Co., Securities Act Release No. 10037, Exchange Act Release No. 77087, 2016 WL 537943, at *10 (Feb. 9, 2016) (noting that Monsanto issued securities during the period of manipulation). *See generally* Urska Velikonja, *The Cost of Securities Fraud*, 54 WM. & MARY L. REV. 1887, 1903 n.64 (2013) (discussing several ways in which a company can benefit from false disclosures even when not offering new securities to investors).

Disgorgement is also rare in public and municipal finance abuse cases because qualified immunity bars the SEC from obtaining money judgments against towns, counties, and states.[194] Figure 1 provides an overview of the frequency of monetary penalties and disgorgement for various violations.

Figure 1: Frequency of Monetary Penalties and Disgorgement by Violation Type (FY 2010–2018)



As shown in Figure 1, in cases in which the SEC prevailed, more than two thirds of cases in each category resulted in some monetary penalties. Because the objective of this section is to evaluate the importance of the SEC's disgorgement authority to its enforcement activities, Figures 1 and 2 include SEC-only disgorgement orders for which there was no secondary basis for recovery. It thus excludes disgorgement and fines that were deemed satisfied or credited in a parallel proceeding.[195] This approach is

194. That has not stopped the SEC from imposing money judgments on city officials and public utilities. *See* Maggie Guidotti, Note, *Seeking "the SEC's Full Protection": A Critique of the New Frontier in Municipal Securities Enforcement*, 82 U. CHI. L. REV. 2045, 2062 (2015).

195. For example, in September 2018, the SEC settled an enforcement action for FCPA violations with Petrobras. Petróleo Brasileiro S.A. – Petrobras, Securities Act Release No. 10561, Exchange Act Release No. 84295, 2018 WL 4628173, at *1 (Sept. 27, 2018) [hereinafter Petrobras Release]. It ordered Petrobras to pay $853.2 million in civil fines and $933.5 million in disgorgement and prejudgment interest. *Id.* at *8–9. The settlement provides that disgorgement will "be reduced and deemed satisfied by the amount of any payment" in the parallel securities class action, and that Petrobras would "receive a dollar-for-dollar credit" for payments to the DOJ and Brazilian authorities. *Id.* at *8–9.

predicated on the idea that other legal bases for recovery could and would supplement or substitute for disgorgement if it became unavailable, whether entirely or partly as time barred. That idea is often true, but not always. Usually, the parallel action is a criminal action by U.S. federal authorities. Prosecutors can seek forfeiture and restitution, and they can benefit from longer limitations periods; in such cases, the predicate assumption is quite appropriate. Parallel actions, of course, also include enforcement actions by foreign regulators, enforcement actions by the CFTC and FINRA, and parallel private suits. The Commodity Exchange Act authorizes the CFTC to seek disgorgement as an equitable remedy,[196] but FINRA relies on securities laws for its enforcement and remedy authority.[197] If the SEC cannot obtain disgorgement, neither can FINRA.

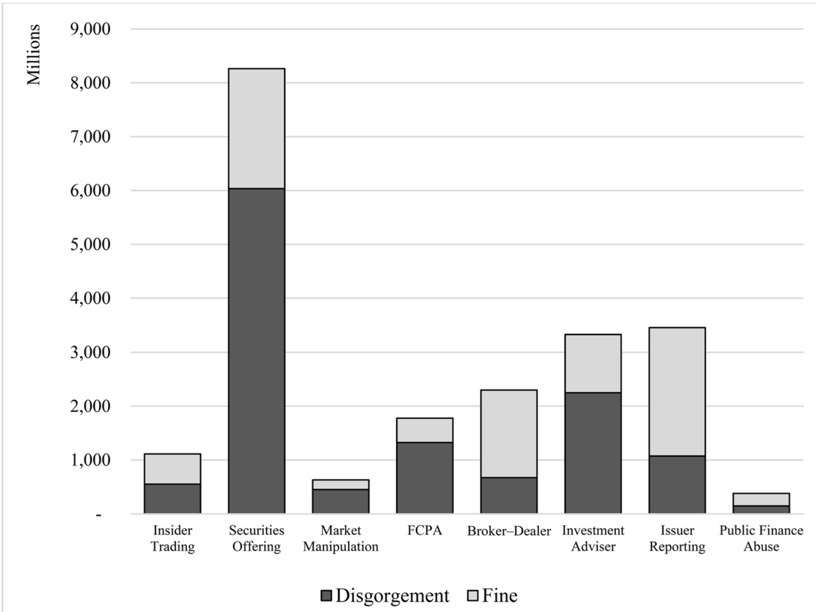
The incidence of monetary penalties—the share of resolved cases in which some monetary penalty is ordered—is between 68.2% in public finance abuse cases at the low end and 96.6% in insider trading cases at the high end. The range in the frequency of disgorgement orders is substantially greater. Fewer than 20% of cases against self-regulatory organizations (SROs)—a category that includes FINRA, stock exchanges, and rating agencies—and public finance abuse cases result in a disgorgement order, whereas almost 90% of insider trading cases result in at least some disgorgement.

Figure 2 reports the aggregate amount of disgorgement imposed, another measure of the importance of the disgorgement remedy. Unsurprisingly, almost half of all (non-parallel) disgorgement is ordered in securities offering cases, predominantly filed in court, followed by FCPA cases as a distant second, and investment adviser cases as a closer third. In all, nearly 60% of disgorgement is imposed on fraudsters who offered individual securities or investments in funds, and who either made material misrepresentations or misappropriated invested monies for their own use. The SEC categorizes cases as against investment advisers when the perpetrator was registered or should have been registered as an investment adviser. Where no such obligation under the securities laws exists, the SEC categorizes such cases as securities offering cases.

196. 7 U.S.C. § 13a-1(d)(3)(B) (2012).

197. *See* Saad v. SEC, 873 F.3d 297, 299, 304 (D.C. Cir. 2017) (remanding to the lower court to consider whether *Kokesh* applies to FINRA-imposed bars).

Figure 2: Aggregate Amounts of Monetary Penalties and Disgorgement by Violation Type (FY 2010–2018)



[*] Monetary penalties are reported in $M (i.e., $1,000 = $1 billion).
[**] Categories in Figure 2 track categories in Figure 1. Insider trading cases, as the first-listed category, have the highest *rate* of disgorgement imposed, but the aggregate amount is relatively small.
[***] SROs & Transfer Agents are included in the Investment Adviser category. The chart omits the Miscellaneous category. There are only ninety-six cases in the Miscellaneous category, and total monetary penalties amount to less than $200 million, including over $11 million in disgorgement.

Disgorgement is both appropriate and necessary where the offender obtained investors' money under false pretenses. More importantly, substitute remedies are not readily available,[198] and certainly not ones as flexible as disgorgement. Securities laws provide for treble civil fines for insider trading and allows for civil fines to substitute for disgorgement if necessary.[199] However, there is no easy stop gap for other violations, which is where the bulk of disgorgement is ordered.

2. Variation by Defendant Characteristics

SEC enforcement varies by target as well. Blockbuster civil fines are ordinarily imposed on large public firms and Wall Street firms—which are often organized as subsidiaries of public holding companies—but our understanding of how the burden of monetary penalties is otherwise distributed is extremely limited.

198. *See infra* Section IV.A.
199. 15 U.S.C. § 78u-1(a)(2) (2012).

Despite the hype, public firms and public-firm subsidiaries represent a small share of defendants in SEC enforcement actions: 9.6% of defendants and 11.1% of completely resolved cases in the dataset (because public-firm defendants tend to settle at higher rates than other defendants). The bread and butter of securities enforcement actions are against individuals and private firms—usually shell companies controlled by individual defendants. Combined, they represent 88.7% of defendants and 87% of completely resolved cases in the dataset.

Public firms and public-firm subsidiaries paid a substantial amount in monetary penalties during the study period: $14.4 billion or $11.8 billion, depending on whether we include the amounts ordered by the SEC but credited for payments in parallel actions. Public firms and their subsidiaries were ordered to pay over two-thirds of civil fines and—excluding cases with parallel enforcement proceedings —just over half of aggregate monetary penalties (52%).

But individuals and private firms pay the balance, which is a staggering amount. If all orders of monetary penalties are included, including those deemed satisfied with payments in parallel proceedings, the SEC ordered individuals and private firms to pay $140.3 billion in monetary penalties; if orders in cases with parallel proceedings are excluded, they paid $11 billion, an amount similar to monetary penalties imposed on public firms and public-firm subsidiaries. The important difference between public companies and individual defendants is in disgorgement orders: depending on whether orders with parallel proceedings are included, individuals and shell companies paid either 95% (included) or 58% (not included) of disgorgement, considerably more than public firms and their subsidiaries.

TABLE 7: MONETARY PENALTIES BY TYPE OF DEFENDANT (2010–2018)

	Public Firm & Public Subsidiary*	**Individual & Private Firm***
Total Penalties	$14.4	$140.3
Civil Fines	$6.8	$3.0
Disgorgement	$7.6	$137.3
Total Penalties (w/o parallel)	$11.8	$11.0
Civil Fines (w/o parallel)	$6.0	$4.6
Disgorgement (w/o parallel)	$5.8	$8.0

*All dollar figures are in $B.

Disgorgement is a remedy most often imposed on individual fraudsters and investment advisers who prey on retail investors. They peddle everything, from get-rich-quick schemes[200] to what at first blush appears like honest asset

200. *See, e.g.*, SEC v. Meli, No. 1:17-cv-632, 2017 WL 9916833, at *1 (S.D.N.Y. Jan. 30, 2017).

management services[201] that ultimately leave retail investors holding the bag. Not only do retail investors tend to lack the capacity and the resources to monitor their investments, but they also have a limited capacity to bring a private suit to recover their losses. Their individual losses may be comparatively small, but they often feel large to an individual retail investor, who has lost her nest egg and now lacks the financial resources to bring a suit. Even if an investor has the resources and the gumption to sue, the perpetrator's remaining assets may have been frozen by the SEC and prosecutors, leaving nothing for the investor to pursue outside of the government action.

3. Court-Ordered Disgorgement

Disgorgement in administrative proceedings is expressly authorized by statute,[202] but court-ordered disgorgement is not. If disgorgement is a penalty, as the Court held in *Kokesh*, then courts arguably have no authority to impose disgorgement.

Scholars have ably argued that the Supreme Court's sweeping language in *Kokesh* is overbroad, and will likely be curtailed by lower courts, Congress, and perhaps the Supreme Court itself in subsequent decisions. Relying on the Court's recent precedent on disgorgement, Donna Nagy advances a convincing case that courts have capacious equitable powers that are "particularly broad and flexible when the public interest in the enforcement of a federal law is involved."[203] If so, disgorgement of unjust enrichment or compensatory disgorgement may nevertheless be legally permissible, even if not expressly authorized by statute. Listwa and Seidell go further, suggesting that equitable "penalties" do exist, and thus it is incorrect to conclude that *Kokesh* bars disgorgement in court.[204] Former SEC Commissioner Roberta Karmel explains that equitable disgorgement differs from disgorgement as a penalty, in particular for cases where the SEC's goal is to distribute ill-gotten gains to investors.[205]

The reasoning in *Kokesh* suggests that where disgorgement is distributed to investors, courts arguably continue to have the right to impose it—but that right is uncertain. Moreover, even if permitted, courts could only impose disgorgement up to the amount of unjust enrichment, that is, revenues net of marginal costs necessary to generate them. Remedial disgorgement that is not distributed to investors appears to be on shaky ground after *Kokesh*.

Even if the Supreme Court had drawn a clean line between punitive and non-punitive disgorgement, it would be impossible to identify which portions of

201. *See* Kokesh v. SEC, 137 S. Ct. 1635, 1641 (2017).

202. 15 U.S.C. §§ 78u-2(e), 78u-3(e) (2012).

203. Nagy, *supra* note 69, at 895 (referencing Kansas v. Nebraska, 574 U.S. 445 (2015), where the Court exercised its original jurisdiction and ordered Nebraska to disgorge its unlawful gains, in addition to ordering compensatory damages for Kansas's losses).

204. *See* Daniel B. Listwa & Charles Seidell, *Penalties in Equity: Disgorgement After* Kokesh v. SEC, 35 YALE J. ON REG. 667, 679 (2018) (citing Tull v. United States, 481 U.S. 412 (1987)).

205. *See* Karmel, *supra* note 23, at 799, 806 (arguing that federal courts possess the authority to order equitable disgorgement to deter unjust enrichment).

historically ordered disgorgement were punitive, compensatory, or remedial. Judgments do not distinguish between different types of disgorgement,[206] and case documents do not make these distinctions possible. The SEC's calculations are typically offered as a single figure, and the Agency is given wide discretion to estimate appropriate disgorgement.[207]

Thus, Table 8.A below includes all disgorgement orders issued by courts in cases that have been completely resolved as to liability and monetary penalties, and in which the SEC prevailed. As noted above in Table 6, the SEC obtained $9.9 billion in court-ordered disgorgement (and $3.9 billion in administrative proceedings) in all cases, including those still ongoing.

TABLE 8.A: COURT-ORDERED DISGORGEMENT BY TYPE OF VIOLATION (FY 2010–2018)

	No. of Cases	Cases with Disgorgement[a]	Aggregate Amount in Disgorgement (in $M)[b]
Securities Offering	1,568	79%	5,456
Insider Trading	538	89%	554
Market Manipulation	511	61%	377
Issuer Reporting	491	38%	991
Investment Adviser, SRO & Transfer Agent	424	72%	829
Broker–Dealer	89	36%	62
FCPA	69	64%	1,372
Public Finance Abuse	59	59%	80
Miscellaneous	17	53%	5

[a] All cases with disgorgement orders, including those deemed satisfied in a parallel action.
[b] SEC-only disgorgement.

As shown in Table 8.A, disgorgement is commonly imposed. It is ordered in more than half of all cases except for broker–dealer violations and issuer reporting cases. Disgorgement is overall more commonly imposed in court cases than in administrative proceedings, and that is true for every category listed except for market manipulation.

206. *See, e.g.*, SEC v. Kokesh, No. 09-cv-1021-SMV/LAM, 2015 WL 11142470, at *10 (D.N.M. Mar. 30, 2015) (ordering $34,927,329 in disgorgement without distinguishing the "type" of disgorgement).

207. *See* SEC v. First City Fin. Corp., 890 F.2d 1215, 1231 (D.C. Cir. 1989) ("[D]isgorgement need only be a reasonable approximation of profits causally connected to the violation.").

TABLE 8.B: COURT-ORDERED DISGORGEMENT BY TYPE OF DEFENDANT (FY 2010–2018)

	No. of Cases[a]	Cases with Disgorgement[b]	Aggregate Amount in Disgorgement (in $M)[c]
Individual	2,550	73%	5,115
Private Firm	955	69%	2,208
Public Firm	188	39%	1,651
Public Subsidiary	33	79%	734
OTC	32	37%	20

[a] The dataset includes eight cases against a government and nonprofit defendants who were not ordered to pay any disgorgement.
[b] All cases with disgorgement orders, including those deemed satisfied in a parallel action.
[c] SEC-only disgorgement.

Table 8.B shows that individuals and private (typically shell) companies pay 75% of court-ordered disgorgement. Eliminating disgorgement as a remedy in court cases will primarily benefit individual defendants, who are the most difficult class to deter, and whose violations are often more difficult to prosecute because individuals are less likely to settle.

IV. DETERRENCE AND COMPENSATION AFTER *KOKESH*

The analysis thus far has proceeded on the assumption of *ceteris paribus*: except for *Kokesh*, all else will remain equal in SEC enforcement. But surely enforcement will change in response to *Kokesh*. The SEC will move expediently and file enforcement proceedings more quickly,[208] perhaps after investigating cases somewhat less thoroughly than before *Kokesh*. It will certainly rely more heavily on technology and analytics,[209] perhaps at the expense of prosecuting violations that are not amenable to computerized oversight.[210] The SEC's limited resources mean that it cannot be everywhere at all times, so *Kokesh* might push the Agency to look for misconduct under the street light. That will benefit the most sophisticated players who ply their trade in dark pools, buy and sell opaque instruments, and occupy corrupt boardrooms, as well as some of the least sophisticated fraudsters, who prey on retail investors' lust for quick returns, but stay under the radar because of good luck or canny deception. The SEC Enforcement Manual urges staff to consider statute-of-limitations concerns when opening investigations, and *Kokesh* will sharpen their

208. *See* Hoecker Memorandum, *supra* note 46, at 4 (urging quick investigations, but not at the expense of quality).

209. The SEC has already built predictive models and algorithms for accounting fraud, insider trading, and cherry picking by broker–dealers. The FY 2019 budget allocates $45 million for additional information-technology enhancements. *See* Press Release No. 2018-14, SEC, Investor Protection, Capital Formation and Market Integrity Are Top Priorities in SEC Budget Request (Feb. 12, 2018), https://www.sec.gov/news/press-release/2018-14 [https://perma.cc/4LJB-YJVK].

210. For most offering frauds, the securities sold are not registered or traded in public markets, so visibility is low.

attention.[211] Staff might refer longer lasting frauds for criminal prosecution more readily than before *Kokesh*. They might insist more strongly on tolling agreements in exchange for any cooperation credit, and signed tolling agreements will include more sweeping language. These shifts will take time and may be subtle, so we may never know the actual and full extent of *Kokesh*'s impact on SEC enforcement.

For what it is worth, SEC leadership has asserted that *Kokesh* would impair the SEC's ability to pursue the twin goals of enforcement: deterrence and compensation.[212] This Part suggests that the impact of *Kokesh* on deterrence and compensation will likely be less substantial than feared. The first section considers the implications of *Kokesh* on deterrence. The second section discusses the impact of *Kokesh* on investor compensation.

A. DETERRING SECURITIES VIOLATIONS

1. Substitute Remedies and Enforcement Agents

In *Kokesh*, the Supreme Court opined that sanctions are penalties when they address wrongs to the public, not to the individual, and when they seek to punish, rather than to compensate.[213] Even disgorgement that the SEC chooses to distribute to injured investors as compensation is a penalty because "no statute commands" the SEC to distribute disgorgement to investors.[214] Remedial disgorgement that deprives the offender of profit, and nothing more, would likewise be treated as a penalty under *Kokesh*, at least according to *Kokesh* dicta.[215]

Moreover, in *Kokesh* the Supreme Court did not carve out a third category of sanctions that are neither penalties nor statutory damages, so it is currently unclear whether noncompensatory remedial measures such as injunctions, officer-and-director bars, penny-stock bars, and professional bars are also penalties. District courts have reasoned that injunctions are penalties,[216] and if they are right, the SEC can no longer prosecute violations older than five years.

That the SEC cannot prosecute violations older than five years does not imply that such violations will not be adequately deterred. The answer depends on whether other enforcement agents, public and private, can substitute for missing SEC enforcement of older violations.[217] Securities fraud is a crime subject to a six-year limitations period and tolling for concealment, so criminal prosecution

211. *See* ENFORCEMENT MANUAL, *supra* note 43, §§ 2.3.1, 2.3.2, 3.1.1 (reminding SEC enforcement staff to "[c]onsider the statute of limitations issue early in the investigation").

212. *See* 2018 ENFORCEMENT REPORT, *supra* note 118, at 6 (describing deterrence and compensation as two goals of SEC enforcement).

213. *See* Kokesh v. SEC, 137 S. Ct. 1635, 1642 (2017).

214. *Id.* at 1644.

215. *Kokesh* quotes *Texas Gulf Sulphur Co.* for the proposition that disgorgement deprives defendants "of their profits in order to . . . provid[e] an effective deterrent to future violations." *Id.* at 1640 (quoting SEC v. Tex. Gulf Sulphur Co., 312 F. Supp. 77, 92 (S.D.N.Y. 1970), *aff'd in part, rev'd in part*, 446 F.2d 1301 (2d Cir. 1971)).

216. *See supra* text accompanying note 93.

217. The SEC can also respond by working to expedite investigations of older violations.

could substitute for SEC enforcement.[218] However, effective substitution is likely limited. The SEC has plenary authority to enforce securities laws, but criminal prosecutors do not.[219] Only intentional securities violations are crimes; reckless or negligent ones are not. The SEC already refers over 100 cases per year for criminal prosecution;[220] thus, the cases most severely impacted by *Kokesh* are the ones where prosecution would not be appropriate.[221] Like the SEC, federal and state prosecutors must prioritize their limited resources.

Private litigants are also unlikely to substitute for SEC enforcement. Their claims are subject to three- and five-year statutes of repose,[222] no longer than the SEC's limitations period. Moreover, like criminal prosecutors, private litigants' enforcement authority is limited. The Securities Act includes several express private rights of action in sections 11,[223] 12,[224] and 15,[225] and the Securities Exchange Act includes five more in sections 9,[226] 16,[227] 18,[228] 20,[229] and 20A.[230] Some of these causes of action allow litigants to prevail without showing any *mens rea*, such as in suits to rescind sales of unregistered securities under Securities Act section 12(a)(1),[231] and in suits for damages for misrepresentations in the registration statement under section 11(b).[232] Others impose a lower negligence standard, including suits that target insiders, underwriters, and other gatekeepers involved in preparing a materially misleading registration statement under section 11.[233] But the most significant liability provision used by private litigants is the implied right of action under Exchange Act section 10(b),[234] which requires a showing of scienter, among other elements.[235]

218. *See* 18 U.S.C. § 3301(b) (2012) (providing a six-year limitations period for certain securities fraud offenses); DOYLE, *supra* note 78, at 10–11 (describing tolling for concealment under federal criminal law).

219. 15 U.S.C. § 77t(a)–(b) (2012) ("Whenever it shall appear to the Commission . . . [that] any rule or regulation . . . ha[s] been or [is] about to be violated, it . . . may investigate such facts.").

220. SEC, FISCAL YEAR 2020 CONGRESSIONAL BUDGET JUSTIFICATION ANNUAL PERFORMANCE PLAN & FISCAL YEAR 2018 ANNUAL PERFORMANCE REPORT 127 (2019), https://www.sec.gov/files/secfy20congbudgjust_0.pdf [https://perma.cc/R93B-5FFW] (reporting 107 criminal investigations in FY 2018 related to conduct under investigation by the SEC).

221. *See supra* Section II.D.

222. Securities Act of 1933 § 13, 15 U.S.C. § 77m (2012); 28 U.S.C. § 1658(b) (2012).

223. Securities Act of 1933 § 11(a), (b)(3), (c), 15 U.S.C. § 77k(a)–(c).

224. *Id.* § 12(a)(1)–(2), 15 U.S.C. § 77l.

225. *Id.* § 15(a), 15 U.S.C. § 77o(a).

226. Securities Exchange Act of 1934 § 9(f), 15 U.S.C. § 78i(f) (2012).

227. *Id.* § 16(b), 15 U.S.C. § 78p(b).

228. *Id.* § 18(a), 15 U.S.C. § 78r(a).

229. *Id.* § 20(a), 15 U.S.C. § 78t(a).

230. *Id.* § 20A(a), 15 U.S.C. § 78t-1(a).

231. Securities Act of 1933 § 12(a)(1), 15 U.S.C. § 77l(a)(1) (2012).

232. *Id.* § 11(b), 15 U.S.C. § 77k(b).

233. *Id.* § 11(c), 15 U.S.C. § 77k(c). The burden of proof for negligence is shifted to the defendant to show that she took reasonable care. 15 U.S.C. § 77k(c).

234. *See* Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b).

235. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976).

But private litigants cannot substitute for SEC enforcement for another, more important reason. The vast majority of successful private settlements result from class action litigation that prosecutes disclosure fraud by public companies.[236] Private plaintiffs are far less successful in actions against public-firm subsidiaries and financial intermediaries,[237] even where the SEC also brings a suit.[238] Private litigation against individuals that the SEC targets for offering fraud or insider trading is rare to nonexistent.[239]

There is some overlap between the various enforcement agencies, most notably for violations of the antifraud provisions of the securities laws. But there is also considerable space in which the SEC and state securities regulators alone have the right to prosecute. Where jurisdiction is concurrent, public enforcers sometimes join forces in parallel actions.[240]

2. Deterring Violations

There is little doubt that *Kokesh* has reduced the potential sanctions for a subset of enforcement actions—in particular, long-lasting offering fraud and investment adviser misappropriation—and thus arguably lowered the deterrent effect of securities enforcement, at least in theory. But that does not imply that in practice, it has increased offenders' propensity for securities violations.

Deterrence has been the most powerful argument in favor of public enforcement, favored by regulators and policymakers from every color of the political rainbow.[241] But deterrence has a dark secret: although compelling in theory, the evidence that larger sanctions reduce the rates of misconduct is limited.[242] When coupled with increased and visible enforcement, increased sanctions have been shown to deter financial crimes such as tax evasion, as well as speeding and

236. *See* CORNERSTONE RESEARCH, ACCOUNTING CLASS ACTION FILINGS AND SETTLEMENTS: 2018 REVIEW AND ANALYSIS 1, 8, 9 (2019), https://www.cornerstone.com/Publications/Reports/2018-Accounting-Class-Action-Filings-and-Settlements [https://perma.cc/LU9D-NB8T] (reporting that in FY 2018, 53% of private securities settlements and 88% of settlement dollars were from class actions alleging accounting fraud).

237. *See infra* Section IV.B.

238. In a study of SEC fair fund distribution, I showed that private plaintiffs often file successful parallel actions in accounting fraud cases. In other cases, they file suits less often, and when they do, they succeed at far lower rates. *See* Velikonja, *supra* note 65, at 373 & tbl.4.

239. *See id.* To illustrate this point, take the following example: no private suit in federal court has been filed against Charles Kokesh.

240. *See, e.g.*, Press Release No. 14-884, Office of Pub. Affairs, DOJ, Bank of America to Pay $16.65 Billion in Historic Justice Department Settlement for Financial Fraud Leading Up to and During the Financial Crisis (Aug. 21, 2014), http://www.justice.gov/opa/pr/bank-america-pay-1665-billion-historic-justice-department-settlement-financial-fraud-leading [https://perma.cc/3K8K-VXJ4] (reporting that Bank of America reached a settlement with DOJ, the Federal Housing Administration, the Government National Mortgage Association, the Federal Deposit Insurance Corporation, the SEC, and several state attorneys general).

241. *See* Dan M. Kahan, *The Secret Ambition of Deterrence*, 113 HARV. L. REV. 413, 416–18 (1999).

242. *See* Michael Tonry, *Learning from the Limitations of Deterrence Research*, 37 CRIME & JUST. 279, 279 (2008) (reporting that three-strike laws, mandatory minimum sentences, and even the death penalty do not affect crime rates).

illegal parking.[243] At least some securities fraud, in particular fraud by repeat players such as Wall Street firms, probably follows the same pattern.[244]

But there is no evidence that individuals who commit securities violations are typically aware of punishment levels beyond knowing that some white-collar criminals are jailed. In addition to public enforcement, most people comply with the law because of self-respect, personal obligations, social norms, and organizational rules that control behavior—and those influences have not changed after *Kokesh*.[245] Those who do not obey the law offend primarily because it is in their self-interest to do so, laws notwithstanding. They are driven by internal motivations, overconfidence, and superiority, and they respond little to sanction levels.[246] Securities violators are frequently recidivists,[247] apparently immune to general or special deterrence.[248]

This evidence suggests that different types of defendants may respond differently to the change in potential sanctions. Nickel-and-dime fraudsters who prey on naïve retirees or pre-retirees may not respond at all to the lesser threat of large disgorgement awards. Even somewhat more sophisticated violators may not respond because *Kokesh* impacts only older violations. On the other hand, public firms and public-firm subsidiaries with well-informed legal and compliance departments might respond more aggressively to *Kokesh* than individual fraudsters. Compliance is a cost center for which its value is measured against its returns. If potential sanctions are lower, public firms and their subsidiaries might invest less in compliance. The SEC will continue to use tolling agreements,[249] but *Kokesh* will impact settlement dynamics for detected and prosecuted violations.

243. *See id.*

244. *See* Andrew Ceresney, Dir., Div. of Enf't, SEC, Keynote Address at the Securities Enforcement Forum West 2016: Private Equity Enforcement (May 12, 2016), https://www.sec.gov/news/speech/private-equity-enforcement.html [https://perma.cc/4QP9-T4WS] (opining that the Commission's "private equity actions have led to significant change in the private equity industry, all to the benefit of investors").

245. *See* Tonry, *supra* note 242, at 291 (referencing Robert Ellickson's observations of cattle rancher dispute resolution in Shasta County, which fostered his five-level model of social control characterized by self-control, obligations to others, social norms, organizational controls, and government enforcement (citing ROBERT C. ELLICKSON, ORDER WITHOUT LAW: HOW NEIGHBORS SETTLE DISPUTES 131 (1991))).

246. *See* Jayne W. Barnard, *Securities Fraud, Recidivism, and Deterrence*, 113 PENN. ST. L. REV. 189, 193 (2008) (arguing that many securities offenders are "unlikely to be deterred by monetary penalties or injunctions").

247. *See* Mark Egan, Gregor Matvos & Amit Seru, *The Market for Financial Adviser Misconduct*, 127 J. POL. ECON. 233, 251 (2019) (reporting that 27% of registered investment advisers that engage in misconduct are repeat offenders); Julia Dimitriadis, Securities Violations, Recidivism, and Deterrence: An Econometric Approach 29, 33 (Apr. 29, 2019) (unpublished paper, Georgetown University Law Center) (on file with author) (reporting an overall recidivism rate of 15%, and finding a much higher recidivism rate for broker–dealer violations than insider trading).

248. *See generally* Paul H. Robinson & John M. Darley, *The Role of Deterrence in the Formulation of Criminal Law Rules: At Its Worst When Doing Its Best*, 91 GEO. L.J. 949, 955 (2003) (defining "special deterrence" as "the degree to which a punishment, once experienced, reduces the likelihood of the person who experienced the punishment risking a similar punishment by offending again in the future").

249. *See supra* Section II.D.

A somewhat larger share of investigations may not settle and may result in litigation.

As a result, although in theory *Kokesh* should significantly reduce the deterrent threat of enforcement, in practice it might not. That does not imply that *Kokesh* causes no harm. Laws reinforce social norms, but unfair laws undermine the rule of law. Statutes of limitations "are by definition arbitrary."[250] They deprive the plaintiff of a remedy if she does not bring suit within the period, even if she could not have discovered the violation, which strikes most people as unfair and inconsistent with the rule of law.[251]

Statutes of limitation and repose have a long history because they serve compelling social goals. They provide repose, that is, "certainty about a plaintiff's opportunity for recovery and a defendant's potential liabilities."[252] They "promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared."[253] They promote certainty in legal affairs[254] and reduce "the danger of official punishment because of acts in the far-distant past."[255]

Those are arguments in favor of some period after which enforcement should be barred, but the actual time limit imposed depends on balancing the costs and the benefits. Typically, less serious violations are associated with shorter limitations periods, and vice versa. There is no statute of limitations for murdering a member of Congress,[256] for example, but there is a one-year statute of repose for criminal contempt.[257]

Securities fraud is somewhere in between. Although it is not the most serious crime, it is often difficult to discover when the violation is committed. Whichever limitations period is chosen, it ought to strike a balance between worthy goals of repose and error reduction, and equally worthy goals of punishment, retribution, and even compensation. *Kokesh* allows fraudsters who manage to conceal their fraud for more than five years to keep the money. Charles Kokesh funded an extravagant lifestyle with monies stolen from small investors, "including by purchasing a gated mansion, buying and renovating a private polo ground, and keeping a personal stable of more than 50 horses."[258] It offends basic notions of justice that he should get to keep the money he stole just because he was clever

250. Chase Sec. Corp. v. Donaldson, 325 U.S. 304, 314 (1945).

251. *See* Tyler T. Ochoa & Andrew J. Wistrich, *The Puzzling Purposes of Statutes of Limitation*, 28 PAC. L.J. 453, 511–12 (1997).

252. Gabelli v. SEC, 568 U.S. 442, 448 (2013) (quoting Rotella v. Wood, 528 U.S. 549, 555 (2000)).

253. *Id.* (quoting R.R. Telegraphers v. Ry. Express Agency, 321 U.S. 342, 348–49 (1944)).

254. *See id.* at 448–49 (explaining that statutes of limitation provide "security and stability to human affairs" and are thus "vital to the welfare of society" (quoting Wood v. Carpenter, 101 U.S. 135, 139 (1879))).

255. Toussie v. United States, 397 U.S. 112, 114–15 (1970).

256. 18 U.S.C. § 351 (2012).

257. 18 U.S.C. § 3285 (2012).

258. Lynch, *supra* note 4.

enough to "target [] smaller investors" who were "less likely to sue."[259] That, and not deterrence, is the strongest argument in favor of amending section 2462.

B. INVESTOR COMPENSATION WITHOUT DISGORGEMENT

The SEC leadership regularly highlights compensation as an important goal of enforcement in publications, speeches, and testimony, and the data bear that out.[260] Excluding receiverships, the SEC ordered some form of compensation in 10.8% of cases with monetary penalties (587 of 5,457).[261] That figure includes types of compensation that *Kokesh* would not affect directly, such as clawbacks of executive compensation in the event of an accounting restatement,[262] and "voluntary" offers to reimburse or compensate investors as part of a settlement with the SEC.[263] Yet the bulk involves SEC distribution funds, where the SEC distributes to harmed investors monetary penalties that it extracted from defendants, as reported in Table 9. The figures exclude cases in which injured investors may have been compensated through a parallel criminal action.

To discuss the impact of *Kokesh* on the SEC's ability to compensate investors, this Article reviews distribution funds established in the cases in the dataset. Because the SEC does not have a monopoly on investor compensation, this section also reviews an older set of distribution funds to determine how successfully parallel private suits could supplement SEC compensation.

1. Fair Funds and Other SEC Compensation

The SEC set up distribution funds in 533 cases in the dataset. In those cases, it ordered defendants to pay $7.4 billion, of which $3.6 billion was disgorgement. A minor share of that total was for violations entirely inside the limitations period: 43.9% of cases but only 26.8% of disgorgement dollars ordered for distribution to investors.

259. SEC v. Kokesh, No. 09-cv-1021-SMV/LAM, 2015 WL 11142470, at *5 (D.N.M. Mar. 30, 2015).

260. No statute authorizes the SEC to recover investor losses (that is, restitution), and the SEC's compensation effort is derivative of its authority to recover other types of financial sanctions (that is, fines and disgorgement).

261. Including cases with receivers and parallel criminal restitution would double that figure. Data on file with author.

262. *See* Sarbanes–Oxley Act of 2002 § 304(a), 15 U.S.C. § 7243(a) (2012).

263. *See, e.g.*, AXA Rosenberg Grp. LLC, Securities Act Release No. 9181, Investment Company Act Release No. 29574, Investment Advisers Act Release No. 3149, 2011 WL 334789, at *8 (Feb. 3, 2011) (taking into account, during settlement, the defendants' agreement to compensate investors $216 million); State St. Bank & Tr. Co., Securities Act Release No. 9107, 2010 WL 421154, at *10 (Feb. 4, 2010) (acknowledging that State Street paid and agreed to pay a total of $550 million to compensate investors).

TABLE 9: SEC DISTRIBUTION FUNDS AND SOL

Any Compensation	587 (10.8% of cases with monetary penalties)
Distribution Fund	533
Disgorgement Fund	399 (10.7% of cases with disgorgement)
Fund Amounts	$7,434 million
Civil Fine	$3,905 million
Disgorgement	$3,634 million
Affected Disgorgement Funds	224 (56.1% of cases with disgorgement funds)
Affected Disgorgement	$2,659 million (73.2% of fund disgorgement)

That does not imply that *Kokesh* will doom the SEC's compensation efforts. A large majority of affected funds were created in cases that settled during the investigation (177 of 224, or 79%), and all but eight of such cases settled after some initial skirmishing before a judge. Remedies imposed in settled actions are negotiated, and settling defendants regularly agree to pay monetary penalties to avoid more substantial sanctions, such as a bar or a more serious injunction.[264] More than a quarter of cases and over 90% by amount of affected disgorgement ($2.4 billion) resulted from settlements with public companies and subsidiaries of public companies, which continue to face strong disincentives to litigate. In such cases, the SEC could demand that the defendant fully compensate injured investors in order to settle the case, like it sometimes did in the 1940s, long before it had the right to impose monetary penalties.[265] Finally, without the authority to order full disgorgement, the SEC could order restitution of the full amount in appropriate cases.

Unless *Kokesh* is interpreted to limit all enforcement for violations older than five years or public companies begin to push back harder, tolling agreements and substitute compensation remedies could mitigate the impact of *Kokesh* on the SEC's compensation effort.

2. Parallel Compensation: Evidence from Earlier Fair Funds

If we relax the assumption that defendants' willingness to settle and to sign tolling agreements will remain constant after *Kokesh*, the SEC's ability to compensate investors could deteriorate substantially. That does not imply that investors will not be compensated, because another agency could step in or investors themselves could sue.

264. *Compare* Complaint at 3, SEC v. Musk, No. 1:18-cv-08865 (S.D.N.Y. Sept. 27, 2018) (seeking an officer-and-director bar), *with* Final Judgment as to Defendant Elon Musk, SEC v. Musk at 2, 4, No. 1:18-cv-08865-AJN-GWG (S.D.N.Y. Oct. 16, 2018) (agreeing ultimately to a limited bar and a $20 million civil fine).

265. *See* Ellsworth, *supra* note 61, at 642–43 (reporting that SEC defendants in the 1940s agreed to compensate investors to avoid an injunction, even though the SEC had no authority to impose monetary penalties).

The data described above deliberately exclude orders of restitution in parallel criminal cases, reporting SEC-only compensation funds. The SEC does not have exclusive jurisdiction to prosecute securities violations. In a limited subset of cases, FINRA and the CFTC punish violations, but only the CFTC can create a distribution fund to compensate investors.[266] As noted, criminal authorities can prosecute securities crimes, but it is implausible that Assistant United States Attorneys would ramp up criminal enforcement for the primary purpose of compensating harmed investors in ill-fated investment schemes. That leaves state securities regulators. As Carlos Berdejó has shown in recent work, a handful of states have established investor restitution funds, but aggregate amounts are small and recoveries are limited.[267]

The Securities Investor Protection Corporation (SIPC) offers investor protection against the loss of cash and securities held at a financially troubled SIPC-member brokerage firm.[268] Compensation is capped at $500,000, including up to $250,000 for cash, and availability is limited to failed brokerages and to missing assets.[269] When Bernard Madoff's Ponzi scheme unraveled, only investors with accounts with Bernard L. Madoff Investment Securities LLC (BLMIS) were eligible for compensation, and not investors in feeder funds that invested in BLMIS. Moreover, investors could recover only the difference between cash deposited with BLMIS—less any withdrawals—and could not recover any returns, appreciation, fee overcharges, churning, or losses from conflicted investment advice.[270]

A more substantial obstacle to investors who lose money to securities fraud is that few SEC defendants are failed SIPC-registered brokerages. As reported in Part II, a majority of cases and disgorgement amounts affected by *Kokesh* involve unregistered offers of securities for which SIPC funds would not be available.[271]

Similarly, FINRA arbitration and private litigation would be of limited use. FINRA has jurisdiction over brokers and brokerages, who represent a small share of SEC defendants and pay an even smaller share of disgorgement: 6% of all potentially time-barred disgorgement was imposed against broker–dealers[272] and 1.3% of disgorgement in time-barred contested cases was imposed on broker–dealers.[273]

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266. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-05-670, SEC AND CFTC PENALTIES: CONTINUED PROGRESS MADE IN COLLECTION EFFORTS, BUT GREATER SEC MANAGEMENT ATTENTION IS NEEDED 5 (2005).

267. *See* Carlos Berdejó, *Small Investments, Big Losses: The States' Role in Protecting Local Investors from Securities Fraud*, 92 WASH. L. REV. 567, 602–08 (2017) (reporting that Florida, Indiana, and Montana have created investor restitution funds that can typically compensate no more than a quarter or less of investors' losses).

268. *See What SIPC Protects*, SEC. INV'R. PROTECTION CORP., https://www.sipc.org/for-investors/what-sipc-protects [https://perma.cc/PTE9-X8KN] (last visited Oct. 4, 2019).

269. *See id.*

270. *Claims*, MADOFF RECOVERY INITIATIVE, https://www.madofftrustee.com/claims-03.html [https://perma.cc/3H6R-SUSZ] (last visited Oct. 4, 2019) (describing net-equity methodology).

271. *See supra* Section II.D and Table 5.A.

272. *See supra* Table 3.B.

273. *See supra* Table 5.A.

Finally, SEC enforcement does not bar investors from bringing parallel private lawsuits so long as they ultimately recover no more than their actual losses.[274] For example, in September 2018 the SEC settled with Brazilian oil company Petrobras for FCPA violations and ordered the company to pay over $1.8 billion in monetary penalties, including $933 million in disgorgement and prejudgment interest.[275] It created a fair fund for the disgorgement and prejudgment interest,[276] and directed that payments be distributed in a parallel class action that had already settled for $3 billion.[277] In addition, the SEC agreed to reduce the disgorgement obligation for any payments to the class action settlement fund.[278] As a result, investors will receive no more than the $3 billion that Petrobras already agreed to pay in the class action.

But Petrobras is the exception. As I have shown in prior work, private litigation is not an important source of compensation for securities violations, except for accounting fraud.[279] And as discussed in section II.D, accounting fraud is among the categories least affected by *Kokesh*.[280] Private litigation is rare in the types of cases and against the types of defendants who benefit most from *Kokesh*: offering fraud by individual defendants.

Private cases take a long time to resolve, so I rely on an earlier dataset to reinforce this point. The dataset includes enforcement actions filed in FY 2005 to FY 2012 for which the SEC set up a distribution fund. Under the rules in force during that time, the SEC could not distribute any funds unless it included some disgorgement, so all funds in the sample include at least some disgorgement.[281] From FY 2005 to FY 2012, the SEC set up at least 171 distribution funds in cases that collectively set out to distribute $8.7 billion, of which $3.85 billion was disgorgement.

Less than half of those cases, 78 of 171, charged violations entirely within the limitations period. Seventy-five charged at least some violations outside the limitations period and eighteen charged violations entirely outside the limitations period. If *Kokesh* were in force at the time, more than half of disgorgement set aside for distribution, $2.4 billion of $3.85 billion, would potentially be at risk.[282]

274. That is, investors can recover the full extent of their losses and no more. *See* Velikonja, *supra* note 65, at 364–65 (explaining that courts and the SEC consider parallel compensation proceedings when distributing funds to investors).

275. *See* Petrobras Release, *supra* note 195, at *8–9.

276. *See id.* at *10.

277. *See In re* Petrobras Sec. Litig., 317 F. Supp. 3d 858, 862, 879 (S.D.N.Y. 2018).

278. *See* Petrobras Release, *supra* note 195, at *8–9.

279. *See* Velikonja, *supra* note 65, at 373–74.

280. Table 5.A suggests that issuer reporting cases are the third most affected category by *Kokesh*, but the bulk of disgorgement is in a single action. Whether the case is included or not, securities-offering and investment-adviser violations result in substantially more and larger disgorgement orders.

281. *See* Sarbanes–Oxley Act of 2002 § 308(a), 15 U.S.C. § 7246(a) (2012).

282. $462 million in disgorgement was ordered and set aside for distribution in cases entirely outside the limitations period, and $1.9 billion was ordered in cases partly outside the limitations period. Data on file with author.

Parallel securities class actions were filed in fifty-nine of the ninety-three cases that included violations outside the limitations period (63.4%). Forty of these actions were successful. The rest were dismissed for the typical reasons: failure to plead scienter with sufficient specificity;[283] failure to plead "loss causation"[284]—a causal connection between the fraud and the economic loss;[285] failure to bring the claim within the applicable limitations period;[286] and finally, failure to assert a recognized private right of action.[287]

Aggregate damages in the forty successful class actions total $9.9 billion, a large amount, but also a misleading amount. Twenty-six of the forty settlements were in accounting fraud cases that produced 85% ($8.43 billion) of the total damages awarded. Those same accounting fraud cases produced minimal disgorgement awards—only $67 million.[288] Cases where *Kokesh* threatens disgorgement are not always accompanied by parallel class actions, and when an action is filed, it often fails. Overall, a minority of class actions in cases with parallel SEC enforcement actions succeed, and these cases typically yield small recoveries, with the exception of accounting fraud cases.

This result supplements the findings in my earlier work, in which I showed that class actions do not substitute for the SEC's compensation efforts.[289] Securities class action target different defendants for different misconduct.

V. A WAY FORWARD

In the end, this Article cannot answer the most pressing question that *Kokesh* poses: which remedies are penalties and thus time barred? Scholars have ably argued that the Supreme Court's sweeping language in *Kokesh* is overbroad, and likely will be curtailed by lower courts.[290] Former SEC Commissioner Roberta Karmel explains that equitable disgorgement differs from disgorgement as a

283. *See, e.g.*, *In re* Biogen Idec, Inc. Sec. Litig., No. 05-10400-WGY, 2007 WL 9602250, at *12, *14 (D. Mass. Oct. 25, 2007).

284. Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 342 (2005) (citing 15 U.S.C. § 78u-4(b)(4)).

285. *See, e.g.*, Wilamowsky v. Take-Two Interactive Software, Inc., 818 F. Supp. 2d 744, 759 (S.D.N.Y. 2011).

286. *See, e.g.*, *In re* MBIA Inc. Sec. Litig., No. 05-Civ-03514-LLS, 2007 WL 473708, at *9 (S.D.N.Y. Feb. 14, 2007).

287. *See, e.g.*, Stipulation of Dismissal, With Prejudice, of Claims Asserted Under Sections 34(b), 36 (a) and 48(a) of the Investment Company Act of 1940 at 1–2, *In re* Hartford Mut. Funds Fee Litig., No. 04-cv-00344-AWT (D. Conn. Dec. 6, 2007) (concluding that there is no private cause of action for undisclosed revenue sharing between investment advisers and the inferior investment funds they were promoting, or for receiving kickbacks for such promotions).

288. The twenty-six actions that yielded 85% of the total damages yielded only 6% of the disgorgement orders in the forty-case sample. By contrast, all other cases that produced 94% of the disgorgement awards produced either no class action settlement or a settlement with minimal damages (15% of total damages).

289. *See generally* Velikonja, *supra* note 65.

290. *See* Karmel, *supra* note 23, at 799–800 (arguing that "federal courts have authority to order [equitable] disgorgement to prevent unjust enrichment"); Nagy, *supra* note 69, at 922–26 (describing Kansas v. Nebraska, 574 U.S. 445 (2015), where the Court exercised its original jurisdiction and ordered Nebraska to disgorge its unlawful gains, in addition to ordering compensatory damages for Kansas's losses).

penalty, and suggests there is life to disgorgement after *Kokesh*, in particular for cases where the SEC's goal is to distribute ill-gotten gains to investors.[291] Finally, even according to *Kokesh*, the SEC possesses the right to order restitution.[292]

But these proposals are, at most, second-best solutions. Restitution is an imperfect substitute for disgorgement. Restitution is measured "by the defendant's wrongful gain" and requires that the defendant return wrongful gains "properly attributable to the defendant's interference with the claimant's legally protected rights."[293] Poor recordkeeping and commingled assets can impede efforts to identify funds subject to restitution. Even if the rules of restitution were relaxed for public enforcement, restitution could substitute for disgorgement only when the violator was unjustly enriched at the expense of identifiable investors. In FCPA, accounting-fraud, and even insider-trading cases there are no identifiable defrauded investors who either lost money to the fraudster and or can receive compensation for their losses.

Many of the SEC's distribution funds are created in cases where investors clearly suffered losses, but those losses are not easily traceable to the fraudster's gain. Offering frauds are the exception, but often the amounts collected from violators are so small that it makes little economic sense for the SEC to set up a distribution fund.[294] If restitution (or equitable disgorgement) is predicated on the payment of collected funds to investors, then fraudsters in smaller schemes that do not justify the cost of a distribution fund may avoid sanction.

The proposals are also second-best solutions because they rely on subsequent judge-made law. Judges, as Chief Justice Roberts (in)famously explained during his nomination hearing, "call balls and strikes" and do not "pitch or bat."[295] Judges can, at best, supply answers to questions before them, on specific facts. Their interpretations inevitably produce "disparities and inconsistencies."[296] As shown in this Article, *Kokesh* may be good law but is bad policy because it produces uncertainty and impedes "full justice."[297] As noted throughout this Article, *Kokesh* leaves many questions unanswered. Leaving answers up to the courts will

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291. *See* Karmel, *supra* note 23, at 799, 806.

292. *See* Kokesh v. SEC, 137 S. Ct. 1635, 1644–45 (2017).

293. RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 51 cmt. a (AM. LAW INST. 2010).

294. *See* Velikonja, *supra* note 65, at 351 (reporting that the SEC does not set up a distribution fund when the amount is small because of the high costs associated with distribution).

295. *Confirmation Hearing on the Nomination of John G. Roberts, Jr. to Be Chief Justice of the United States: Hearing Before the S. Comm. on the Judiciary*, 109th Cong. 56 (2005) (statement of John G. Roberts, Jr., Nominee for Chief Justice of the United States Supreme Court).

296. *Putting Investors First: Reviewing Proposals to Hold Executives Accountable: Hearing Before the Subcomm. on Inv'r Prot., Entrepreneurship, and Capital Mkts. of the H. Comm. on Fin. Servs.*, 116th Cong. (2019) (statement of John C. Coffee, Jr., Adolf A. Berle Professor of Law, Columbia University Law School) (referencing the law of insider trading as largely judge-made).

297. For a discussion of competing views on statutes of limitation, see Yair Listokin, *Efficient Time Bars: A New Rationale for the Existence of Statutes of Limitations in Criminal Law*, 31 J. LEGAL STUD. 99, 100 (2002).

produce years of uncertainty.[298] Congressional intervention is a more efficient, democratic, and just solution to the problems that *Kokesh* presents.

A variety of approaches would be consistent with the results reported in this Article. First and foremost, Congress must expressly authorize judicial disgorgement, ideally as both a penalty (that is, forfeiture) and an equitable remedy (that is, compensatory disgorgement and restitution), like it did for the CFTC in the Dodd–Frank Act.[299]

Disgorgement as a penalty is not tax deductible,[300] nor is it covered by directors' & officers' insurance policies.[301] This consequence of the *Kokesh* decision has generated considerable unrest among potential targets of enforcement. By contrast, compensatory disgorgement and restitution are not considered penalties, so they would continue to be both tax-deductible and covered by most directors' and officers' insurance policies. If Congress were to codify disgorgement as an equitable remedy or remedial sanction, and not a penalty, then disgorgement would be both deductible and insurable.

Second, many securities violations take a long time to detect, investigate, and prosecute. The SEC's job is immense, and it does not typically delay investigations unnecessarily. There are currently more than 13,000 registered investment advisers in the United States,[302] not dissimilar to the two firms that Charles Kokesh used to perpetrate his fraud. The SEC is not currently funded to review them, even periodically. Limitations provisions should thus strike a reasonable balance between defendants' interest in accuracy and repose and the public interest in investor protection and attractive capital markets, where offenders do not regularly get to keep their ill-gotten gains.

One such proposal that balances the costs and benefits would be to have no statute of limitations for compensatory disgorgement and disgorgement of unjust enrichment—that is, revenues net of the marginal costs necessary to generate such revenues. Neither punish and both put the defendant back in the position he was in before the violation.

There are several standard policy arguments in favor of limitations periods, but none undermine this proposed amendment. The first argument is that limitations

298. See, for example, the disruptive impact of *Lucia v. SEC* on administrative adjudication. 138 S. Ct. 2044 (2018). After *Lucia*, the SEC reopened and reassigned 160 cases for new trials before new ALJs. *See In re* Pending Administrative Proceedings, Administrative Proceedings Rulings Release No. 5955, at 1–3 (ALJ Sept. 12, 2018). Because the constitutionality of removal protections remains uncertain, the SEC filed only three contested cease-and-desist actions (against seven defendants) before ALJs between March 2018 and July 2019. Data on file with author.

299. *See* Dodd–Frank Wall Street Reform and Consumer Protection Act § 744, 7 U.S.C. § 13a-1(d)(3) (2012).

300. *See* Johnson et al., *supra* note 24; Scott M. Levine & Sean E. Jackowitz, Kokesh v. SEC*: A Tax Case in Sheep's Clothing?*, TAXNOTES (May 1, 2017), https://www.taxnotes.com/editors-pick/kokesh-v-sec-tax-case-sheeps-clothing [https://perma.cc/89R5-P2VK].

301. *See* J.P. Morgan Sec., Inc. v. Vigilant Ins. Co., 84 N.Y.S.3d 436, 438, 444 (N.Y. App. Div. 2018) (holding that disgorgement as a penalty is not covered by insurance that excludes penalties from coverage); Barry et al., *supra* note 25.

302. OCIE, EXAMINATION PRIORITIES, *supra* note 186, at 1.

periods provide repose, that is, "certainty about a plaintiff's opportunity for recovery and a defendant's potential liabilities."[303] A longer or even unlimited limitations period provides as much certainty as a five-year limitations period. In fact, the more precise definition of penalties provides more certainty than the imprecise definition of "penalties" offered in *Kokesh*.

The second policy argument in favor of limitations periods is that they "promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared."[304] To the extent that evidence deteriorates over time, a shorter limitations period is favorable to a longer one, but that is typically balanced against the policy goals of deterrence and retribution. There is no statute of limitations for murder, for example, even though unreliable eyewitness evidence is often used to prove murder. Documentary evidence, which is predominantly used in securities enforcement actions,[305] typically does not deteriorate with time, although the ability to explain the document's context may.

However, if fresh evidence is the reason for a short limitations period, then statutes are a poor mechanism for achieving that objective. There is no rule of evidence that bars the SEC from using older evidence to prove more recent violations. Fraudulent schemes that the SEC prosecutes are often long-lasting. Charles Kokesh, for example, began to steal from his clients fourteen years before the SEC sued him, and he continued to do so until about two years before the suit.[306] Bernard Madoff's and Allen Stanford's schemes also lasted for several decades.[307] When the SEC sets out to prosecute long-lasting schemes, it can present to the judge and the jury evidence of when the defendant began stealing and how he stole funds over time. In the case against Kokesh, the limitations period became relevant only when the district court set out to calculate monetary penalties.[308] Only then did the court choose to ignore financial statements and receipts showing embezzlement that was older than five years at the time the SEC filed suit. Moreover, if the objective of a limitations period is to ensure fresh evidence at the time of sanctioning, it fails. The initiation of a legal proceeding tolls the statute of limitations. As long as enforcement proceedings begin within the limitations period, the age of evidence at sanctioning is irrelevant. In the case against Charles Kokesh, the district court set monetary penalties in 2015, almost six years after the SEC filed suit.[309] By that point, the court considered evidence that was almost eleven years old to set civil fines and disgorgement.

Finally, limitations periods are designed to prevent unreasonable delay. In *Gabelli*, the Supreme Court explained that limitations periods exist because

303. Gabelli v. SEC, 568 U.S. 442, 448 (2013) (quoting Rotella v. Wood, 528 U.S. 549, 555 (2000)).
304. *Id.* (quoting R.R. Telegraphers v. Ry. Express Agency, Inc., 321 U.S. 342, 348–49 (1944)).
305. Witnesses lie and dissemble; documents typically do not.
306. *See Kokesh* Complaint, *supra* note 95, at 1, 14.
307. *See supra* note 144.
308. *See* SEC v. Kokesh, No. 09-cv-1021-SMV-LAM, 2015 WL 11142470, at *10 (D.N.M. Mar. 30, 2015).
309. *See id.*

"even wrongdoers are entitled to assume that their sins may be forgotten."[310] Over time, offenders may have self-rehabilitated and could be prejudiced by the late-filed action.[311] Statutes of limitations promote certainty in legal affairs[312] and reduce "the danger of official punishment because of acts in the far-distant past."[313] But that is not what the five-year limitations period for SEC actions does. The SEC does not typically prosecute old violations. Few SEC enforcement actions are dismissed for being entirely outside the limitations period.[314] Instead, in a vast majority of cases in which the limitations period applies, liable wrongdoers pay reduced monetary penalties. Moreover, compensatory and remedial disgorgement do not punish old sins—they merely put the defendant in the position before the violation.

An alternative to a longer limitations period would be the SEC's more aggressive invocation of equitable tolling doctrines, such as fraudulent concealment. But *Gabelli* all but forecloses the use of equitable tolling for section 2462. The *Gabelli* Court suggested that the doctrine would be available when "defendant takes steps beyond the challenged conduct itself to conceal that conduct from the plaintiff."[315] But if that language requires actions or conduct that are not also an element of the violation, the list of cases where the doctrine could be successful will be short indeed. One of the charges levied against Charles Kokesh was that he distributed false proxy statements to his investors and filed false reports with the SEC to conceal his fraud.[316] False filings with the Commission and false proxy statements are securities violations prohibited under sections 13 and 14 of the Exchange Act.[317] But it would appear under *Gabelli* that the SEC could not rely on such evidence to seek equitable tolling, even if the defendant's purpose of filing false reports was to conceal his fraud from the SEC.

Finally, at least some violations could certainly be detected more quickly if the SEC had more resources to conduct examinations and investigations. An additional alternative to a longer limitations period is a budget increase.[318]

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310. Gabelli v. SEC, 568 U.S. 442, 449 (2013) (quoting Wilson v. Garcia, 471 U.S. 261, 271 (1985)).

311. *See* Ochoa & Wistrich, *supra* note 251, at 464–66 (opining that "[a]t some point, the psychological—and perhaps even moral—balance begins to tip in favor of the defendant"); Note, *The Statute of Limitations in Criminal Law: A Penetrable Barrier to Prosecution*, 102 U. PA. L. REV. 630, 634 (1954) (arguing that "the pursuit of only more recent criminals is consistent with that aim of criminal law which seeks to rehabilitate wrongdoers and serves to free the citizen from vexatious fear of prosecution for old crimes").

312. *See Gabelli*, 568 U.S. at 448–49 (explaining that statutes of limitations provide "security and stability to human affairs" and are thus "vital to the welfare of society" (quoting Wood v. Carpenter, 101 U.S. 135, 139 (1879))).

313. Toussie v. United States, 397 U.S. 112, 114–15 (1970).

314. Only .12% of completed cases in the dataset (8 of 6,833) were dismissed for being outside the limitations period. Data on file with author.

315. *Gabelli*, 568 U.S. at 447 n.2. *See also* SEC v. Geswein, 2 F. Supp. 3d 1074, 1084–85 (N.D. Ohio 2014) (affirming that *Gabelli* did not prohibit equitable tolling of the statute of limitations).

316. *See Kokesh* Complaint, *supra* note 95, at 1–2.

317. Securities Exchange Act of 1934 §§ 13(a), 14(a)(1), 15 U.S.C. §§ 78m(a), 78n(a)(1) (2012).

318. *See Putting Investors First: Examining Proposals to Strengthen Enforcement Against Securities Law Violators: Hearing Before the Subcomm. on Inv'r Prot., Entrepreneurship, and Capital Mkts. of the*

CONCLUSION

Charles Kokesh is typical of the SEC defendants who pay disgorgement. *Kokesh* bars the SEC from collecting ill-gotten gains that resulted from long-lasting, but ongoing schemes. The standard arguments in favor of statutes of limitation—repose and evidence quality—are harder to sustain when the defendant violated securities laws recently. As this Article shows, deterrence of securities violations and efforts to compensate investors may not suffer as much as feared after *Kokesh*. But *Kokesh* produced uncertainty and unjust results. Congress must both authorize disgorgement in civil actions and extend the limitations period for disgorgement.

H. Comm. on Fin. Servs., 116th Cong. (2019) (statement of Stephen J. Crimmins, Partner, Murphy & McGonigle PC) (arguing for a budget increase).

APPENDIX

TABLE A: SUMMARY STATISTICS (2010–2018)

Defendants	
Individuals	4,869 (59.4%)
Private Firm (incl. shell company)	2,403 (29.3%)
Public Company	488 (6.0%)
Subsidiary of Public Company	294 (3.6%)
OTC Firm	47 (0.6%)
Government & NGO	96 (1.2%)
Registered Entity (as broker–dealer, investment adviser, auditor, bank)	1,080 (32.5% of firms)
Resolutions	
Court	5,255
Settled	1,281 (24.4%)
Contested	3,974 (75.6%)
Administrative Proceeding	2,942
Settled	2,381 (80.9%)
Contested	561 (19.1%)
Case Status	
All Cases	8,197
Fully Resolved	6,833
SEC Prevailed	6,606 (96.7%)
Any Monetary Relief	5,455 (79.8%)
Disgorgement	3,714 (54.4%)
SOL	
Entirely Inside SOL	5,167 (63%)
Partly Outside SOL	2,802 (34.2%)
Entirely Outside SOL	228 (2.8%)

TABLE B: TOP TEN SEC-ONLY DISGORGEMENT ORDERS IN CONTESTED CASES (2010–2018)

	Defendant Type	Violation Type	> SOL	Disgorgement (USD $)
Edwin Fujinaga	Individual	Securities Offering	Y	544,359,364
CR Intrinsic Investor, LLC (i.e., SAC Capital)	Private Registered Firm	Insider Trading	N	326,774,922
Liping Zhu	Individual	Issuer Reporting	N	302,486,988
Nikolai S. Battoo	Individual	Securities Offering	N	290,129,197
Management Solutions Inc. (controlled by Wendell Jacobson)	Private Firm	Securities Offering	N	241,361,188
Milowe Allen Brost	Individual	Securities Offering	Y	210,159,622
Louis V. Schooler	Individual	Securities Offering	Y	147,610,280
Samuel E. Wyly	Individual	Issuer Reporting	Y	123,836,959
Bank of America N.A.	Public Firm	Securities Offering	Y	115,840,000
Marlon Quan	Individual	Securities Offering	Y	96,191,673