FEDERAL ELECTION COMMISSION
WASHINGTON D.C. 20463

SENSITIVE

SUBMITTED LATE

September 27, 1999

MEMORANDUM

TO: The Commission

FROM: Lawrence M. Noble
General Counsel

BY: Lois G. Lerner ZGZ by AAS
Associate General Counsel

SUBJECT: MUR 4250
Applicability of 28 U.S.C. § 2462 to "Disgorgements"

During discussion at the Executive Session of September 22, 1999 of the effect of FEC v. Williams on MUR 4250 (*see* the Office of the General Counsel's Memorandum of September 20, 1999), a question arose as to whether the use of the term "forfeiture" in prescribing the type of legal actions subject to the five year statute of limitations at 28 U.S.C. § 2462 encompassed actions seeking disgorgements.

This issue posses two interrelated questions: 1) whether disgorgement is the type of legal relief contemplated by the term "forfeiture" and, thus, subject to the five year statute of limitations; and 2) whether disgorgement to the United States Treasury, as distinct from disgorgement to the original contributor, is material to the conclusion in the first question. As is discussed below, both the historical interpretation of the forfeitures and the application of disgorgement remedies in the District of Columbia Circuit firmly establish that disgorgement is an equitable remedy distinct from the legal forfeiture actions. Less directly addressed by the courts has been the question of whether the recipient of the disgorgement changes the nature of the remedy from an equitable one to a legal one. However, the available judicial opinions suggest that the recipient of the disgorgement is not material to its characterization as an equitable remedy.

Forfeiture as a Punitive Legal Action

In a 1993 decision, Austin v. United States, 509 U.S. 602 (1993), the Supreme Court provided an exhaustive analysis of the historically punitive nature of forfeiture actions. In discussing the applicability of the Excessive Fines Clause of the Eighth Amendment to *in rem* forfeitures, the Court turned to a historical review of the term to determine "whether it was punishment." *Id* at 610. The court noted that "sanctions

frequently serve more than one purpose [and] need not exclude the possibility that a forfeiture serves some remedial purposes to conclude that it is subject to the limitations of the Excessive Fines Clause." *Id.* Tracing the origin of forfeiture remedies to the American Colonies, and before then to English law, the Court noted that "examination of those laws suggests that the First Congress viewed forfeiture as punishment" and that "forfeit was the term Congress used for fine." *Id.* at 613 and 614 (citations omitted). Turning to a review of American jurisprudence, the Court consistently noted that "[i]n these cases, forfeiture has been justified on two theories – that the property itself is 'guilty' of the offense, and that the owner may be held accountable for the wrongs of others to whom he entrusts his property. Both theories rest, at bottom, on the notion that the owner has been negligent in allowing his property to be misused and that he is properly punished for that negligence." *Id.* at 615 (citations omitted). "We conclude, therefore, that forfeiture generally and statutory *in rem* forfeiture in particular historically have been understood, at least in part, as punishment." *Id.* at 618.

Consistent with this historical analysis, Black's Law Dictionary defines forfeiture as "[s]omething to which the right is lost by the commission of a crime or fault or the losing of something by way of penalty." Black's Law Dictionary 584 (5th ed. 1979).

Disgorgement as Equitable Remedial Action

By contrast, courts have traditionally treated disgorgement as an equitable remedy designed to return the parties to the status quo by divesting the wrongdoer of ill-gotten gains. The district court in the Southern District of New York, in the first published opinion addressing the applicability of § 2462 to governmental disgorgement actions, found such a determination "to turn on whether disgorgement constitutes a 'fine, penalty, or forfeiture,'" and that "the determining consideration concerns whether the amount . . . serves a remedial or punitive function." SEC v. Lorin, 869 F.Supp. 1117, 1121-1122 (S.D.N.Y. 1994) (citation omitted). In determining the remedial nature of disgorgement, the court turned principally to the Supreme Courts' decision in Meeker v. Lehigh Valley R.R. holding § 2462's predecessor, "which referred to suits seeking a 'penalty or forfeiture,'" to not bar an action by private parties to recover damages (pursuant to §16 of the Interstate Commerce Act) resulting from unreasonable rates and unjust discrimination by transportation providers "because those terms 'refer to something imposed in a punitive way for an infraction of a public law, and do not include a liability imposed solely for the purpose of redressing a private injury, even though the wrongful act be a public offense, and punishable as such.'" *Id.* at 1123 (citing Meeker, 236 U.S. 412, 423 (1915)). The district court reasoned that Meeker "allows for the conclusion that disgorgement does not constitute a fine, penalty, or forfeiture" in holding "that 'strictly remedial' liabilities do not fall under the 'catch-all' statute because they are not 'punitive,'" hence, "disgorgement is similar to the redressing of a private injury in that both serve to return affected parties to the status quo before the lawful activity at issue had taken place. That goal appears, by definition, to be remedial." *Id.* (citing Meeker, 236 U.S. at 423) (additional citations omitted). Accordingly, the district court concluded that it would "not label disgorgement a fine, penalty, or forfeiture in light of the operation of disgorgement, which merely deprives one of wrongfully obtained

proceeds. As such, disgorgement merely returns the wrongdoer to the status quo before any wrongdoing had occurred." *Id.* at 1122 (citations omitted).

This reasoning has been adopted in SEC v. Williams, a Massachusetts district court addressing a direct § 2462 challenge to an SEC suit seeking injunctive relief and disgorgement of ill-gotten profits. 884 F.Supp. 28 (D. Mass. 1995). SEC v. Williams held that § 2462 "does not appl[y] to every action by any government agency. By the terms of the statute, the five year limitations period applies only to suits or proceeding for the enforcement of any civil fine, penalty or forfeiture, pecuniary or otherwise." *Id.* at 30 (citations omitted). The court found that SEC disgorgement "like all disgorgement actions, is designed to deprive a defendant of ill gotten gains . . . a defining feature of the disgorgement action is that the amounts disgorged may not exceed the amount of illicit gain . . . this marked limitation in the court's authority emphasizes the remedial nature of the disgorgement action." *Id.* (citations omitted).

The D.C. Circuit has also upheld this reasoning in two actions directly implicating § 2462. In Johnson v. SEC, involving a petition by respondent for review of an SEC censure and suspension, the court found the censure and suspension to constitute a penalty under § 2462 because they were "certainly not 'remedial' in the sense the term is used in Meeker and its progeny, for they are not directed toward correcting or undoing the effects of Jonhson's allegedly faulty supervision." 87 F.3d 484, 491-492 (D.C. Cir. 1996) (emphasis added). Like the court in Lorin, the D.C. Circuit, in dicta, found Meeker to apply to governmental remedial actions: "Similarly, where the effect of the [] actions is to restore the status quo ante, such as through a proceeding for restitution or disgorgement of ill-gotten profits, § 2462 will not apply." *Id.* at 491. This same conclusion was reached by the appellate court in SEC v. Sprecher, wherein respondent challenged the disgorgement as time bared. In an unpublished memorandum opinion, the court held that "[d]isgorgement is an equitable remedy, not punishment like a fine." No. 94-5006, 1996 WL 175216, at *4 (D.C. Cir. Apr. 9, 1996).

The only two the D.C. Circuit opinions directly addressing the applicability of § 2462 to actions for disgorgement of ill-gotten gains found such actions not be subject to the limitations at § 2462.[1] Similarly, concerning whether disgorgement to the U.S. Treasury, as distinct from disgorgement to the contributor in the FECA context, impacts on the remedial nature of disgorgement, both the reasoning and language used by various courts addressing the remedial nature of disgorgement indicate that the recipient source of the disgorgement is of little consequence to its remedial function.

---

[1] For purposes of bankruptcy proceedings, courts have held disgorgement awards to be penalties, thus protecting them from discharge. *See* Cisneros v. Cost Control Marketing & Sales Management of Virginia, Inc., 862 F.Supp. 1531 (W.D. Va. 1994), *aff'd sub nom*, 64 F.3d 920 (4th Cir. 1995); SEC v. Telsey, 144 B.R. 563 (Bnkr.S.D.Fla. 1992). However, as the court in Williams explained, these bankruptcy cases "stand for the limited proposition that the deterrent effects of disgorgement, whatever these may be, implicate the non-dischargeability provision of the bankruptcy code." 884 F.Supp. at 31, *see also* Lorin, 869 F.Supp. at 1124.

The N.Y. district court in Lorin noted that "SEC actions seeking disgorgement differ slightly from [the cause of action in Meeker] in that they do not attempt to redress a private injury, but rather aim to separate the securities law violator from him or her unlawfully obtained funds," yet adopted Meeker, holding the SEC disgorgement action remedial and not subject to § 2462. Lorin, 869 F.Supp. at 1123. Similarly, the D.C. Circuit in Johnson, although at times speaking in terms of "remedying the damage caused to the harmed parties" and restoring "the stolen funds to their rightful owner," in characterizing the SEC censure and suspension at issue as punitive noted that, unlike disgorgements, "they are not directed toward correcting or *undoing* the effects of [the illegality]." Johnson, 87 F.3d at 488 and 491-492 (emphasis added). In SEC v. Bilzerian, the D.C. Circuit in finding that disgorgement did not violated the Double Jeopardy Clause because it did not constitute punishment, noted that "[t]he primary purpose of disgorgement is not to refund others for losses suffered but rather to deprive the wrongdoer of his ill-gotten gain." Bilzerian, 29 F.3d 689, 697 (D.C. Cir. 1994) (citations omitted). The D.C. Circuit again in SEC v. First City Financial Corp., in finding disgorgement an appropriate remedy for violations of certain securities reporting requirements, defined disgorgement "as an equitable remedy designed to deprive a wrongdoer of his unjust enrichment and to deter others from violating the securities laws". 890 F.2d 1215, 1230 (D.C. Cir. 1998) (citations omitted).

Other courts have also viewed the divestiture of the ill-gotten gains as a remedial action, separate and apart from redressing private injuries. In SEC v. Williams, the district court noted that disgorgement "is designed to deprive a defendant of ill-gotten gains. A defining feature of the disgorgement action is that the amounts disgorged may not exceed the amount of illicit gain." 884 F.Supp. at 30 (citation omitted). In Crude Co. v. FERC, the district court, in denying a challenge to a Department of Energy refund order based on a claim that the payments to DOE would not serve to restore the status quo because the restitution was not going to the injured parties, succinctly held that "[a] wrongdoer must disgorge ill-gotten gains." 923 F.Supp. 222, 240 (D.D.C. 1996) (citations omitted), *aff'd*, 135 F3d. 1445 (Fed. Cir. 1998).

Conclusion

These opinions form a strong basis for the argument that the recipient of a disgorgement is of less consequence to the relief's characterization as remedial than that the disgorgement be proportional to the ill-gotten gains so as not to contain punitive aspects. This is especially true in the FECA context where the source of the illegal funds, the contributors, are often not similarly situated to the traditional victim. Accordingly, it would appear that a disgorgement to the U.S. Treasury in this matter, equal to the amount of the loan proceeds, would not be subject to the statute of limitations at § 2462.[3]

---

[3] Of course, the Commission will still have to address the issue raised in Fireman v. United States, (No. 99-17 C, United States Court of Federal Claims), regarding who the disgorgement should go to.