SHEATHING RESTITUTION'S DAGGER UNDER THE SECURITIES ACTS: WHY FEDERAL COURTS ARE POWERLESS TO ORDER DISGORGEMENT IN SEC ENFORCEMENT PROCEEDINGS

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"Beneath the cloak of restitution lies the dagger to compel the conscious wrongdoer to disgorge his gains."[1]

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[1] GRAHAM DOUTHWAITE, ATTORNEY'S GUIDE TO RESTITUTION § 8.1, at 324 (1977).

Abstract

When the Securities and Exchange Commission ("SEC") brings an action in federal court, it typically seeks disgorgement. The SEC's disgorgement remedy requires an individual who has violated a securities law to pay a money judgment in the amount of the profits attributable to the underlying violation. As the securities acts do not explicitly authorize a federal court to order disgorgement in an SEC enforcement proceeding, federal courts award the remedy pursuant to their equity jurisdiction.

Under Supreme Court precedent, a remedy falls within a federal court's equity jurisdiction if, but only if, the English High Court of Chancery ordered a functionally equivalent remedy in 1789. However, the Chancery did not award money judgments measured by the amount of a wrongdoer's profit attributable to his wrong except in cases involving an abuse of a fiduciary relationship. Because the SEC's disgorgement remedy does not require a fiduciary relationship, the remedy has no analog in 1789 Chancery decisions. Accordingly, federal courts may not award the SEC's disgorgement remedy pursuant to their equity jurisdictions.

The United States Securities and Exchange Commission ("SEC") frequently resorts to the federal courts to deprive those who have transgressed the securities acts of the gains realized from their malfeasance.[2] The mechanism through which the SEC seeks to do so is the remedy of disgorgement.[3] Though the securities acts do not expressly provide for disgorgement, the SEC has persuaded federal courts to grant it pursuant to their equity jurisdiction.[4] Interestingly,

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[2] *See, e.g.*, SEC v. CMKM Diamonds, Inc., 729 F.3d 1248, 1260–62 (9th Cir. 2013) ($409,638.11); SEC v. Pentagon Capital Mgmt. PLC, 725 F.3d 279, 280 (2d Cir. 2013) ($38,416,500); SEC v. Boock, No. 09 Civ. 8261 (DLC), 2013 WL 4828571, at *2 (S.D.N.Y. Sept. 9, 2013) ($1,050,000); SEC v. Simone, No. 07–cv–3928 (JG), 2013 WL 4495664, at *1 (E.D.N.Y. Aug. 19, 2013) ($543,497); SEC v. Reynolds, No. 3:08–CV–0438–B, 2013 WL 3778830, at *7 (N.D. Tex. July 19, 2013) ($10,531,225); SEC v. Graulich, No. 2:09–cv–04355 (WJM), 2013 WL 3146862, at *7 (D.N.J. June 19, 2013) ($5,592,102); SEC v. Bass, No. 1:10–CV–00606 (LEK/DRH), 2012 WL 5334743, at *2–3 (N.D.N.Y. Oct. 26, 2012) ($4,557,632).

[3] SEC v. Cavanagh, 445 F.3d 105, 117 (2d Cir. 2006).

[4] Russell G. Ryan, *The Equity Façade of Disgorgement*, 4 HARV. BUS. L. REV. ONLINE 1, 2–3 (2013), http://hblr.org/wp-content/uploads/2013/11/Ryan__The-Equity-Fa%C3%A7ade-of-SEC-Disgorgement.pdf ("Congress has never explicitly included disgorgement among the remedies the SEC can seek in federal court. . . . Over time, courts came to accept as a truism the notion that disgorgement is inherently an ancillary equitable remedy."); LOUIS LOSS & JOEL SELIGMAN, FUNDAMENTALS OF SECURITIES REGULATION 1054 (5th ed. 2004); Comment, *Equitable Remedies in SEC Enforcement Actions*, 123 U. PA. L. REV. 1188, 1188 (1975); *see, e.g.*, SEC v. Lipson, 278 F.3d 656, 662–63 (7th Cir. 2002); SEC v. Manor Nursing Ctrs., Inc., 458 F.2d 1082, 1103 (2d Cir. 1972); SEC v. Chester Holdings, Ltd., 41 F. Supp. 2d 505, 528 (D.N.J. 1999); SEC v. R. J. Allen & Assocs., Inc., 386 F. Supp. 866, 880 (S.D. Fla. 1974). Though this note focuses on disgorgement's applications under the securities acts, its conclusions have broader applicability, as ninety-nine federal statutes contain provisions enabling federal courts to resort to their equitable powers in fashioning relief. Ten federal statutes contain the same language—"all suits in equity"—conferring equitable jurisdiction on district courts as the securities acts under Section 22(a) of the Securities Act of 1933, 15 U.S.C. § 77v(a) (2012), and Section 27(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa(a). Also, eighty-nine federal statutes contain "equitable relief," which is contained in Section 21(d)(5) of the Securities Exchange Act of 1934. 15 U.S.C. § 78u(d)(5). Furthermore, in some contexts, the "general" equitable jurisdiction of federal courts, absent specific statutory authorization to invoke such jurisdiction, has been sufficient to uphold a

only one case, *SEC v. Cavanagh*, has attempted to demonstrate that a federal court may award disgorgement to the SEC pursuant to the court's equity jurisdiction.[5] Specifically, *Cavanagh* concluded that, because eighteenth-century English chancellors effectively ordered disgorgement, the federal courts may award disgorgement to the SEC under their equitable powers.[6]

This note contends that *Cavanagh* failed to show that a federal court's equity jurisdiction encompasses the SEC's disgorgement remedy and that the federal courts are powerless to order disgorgement in SEC enforcement proceedings. *Cavanagh* makes a diligent effort to show that the liability to surrender ill-gotten gains was a standard part of eighteenth-century English equity jurisprudence,[7] but it succeeds only in showing that such liability was the consequence of a breach of fiduciary duty or knowing participation in such a breach.[8] Though the conclusion that fiduciaries and those involved in a breach of fiduciary duties are liable to disgorge ill-gotten gains is indisputable,[9] it does not support *Cavanagh*'s ambitious claim that eighteenth-century English chancellors ordered disgorgement of ill-gotten gains in the absence of a fiduciary relationship.[10]

Part I provides an introduction to the SEC's disgorgement remedy, classic disgorgement, and the equity jurisdiction of the federal judiciary. Next, Part II discusses the history of the SEC's disgorgement remedy. Part III then analyzes *Cavanagh*'s conclusion that disgorgement was an available remedy in the High Court of Chancery in England in 1789 by examining the analogous remedies, binding precedents, and persuasive precedents on which the opinion relied. After analyzing *Cavanagh*, Part IV argues that the SEC's

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disgorgement order. George P. Roach, *A Default Rule of Omnipotence: Implied Jurisdiction and Exaggerated Remedies in Equity for Federal Agencies*, 12 FORDHAM J. CORP. & FIN. L. 1, 75 n.253 (2007) (citing CFTC v. Am. Metals Exch. Corp., 991 F.2d 71, 76 n.9 (3d Cir. 1993)).

[5] *See Cavanagh*, 445 F.3d at 118–20.

[6] *Id.* at 120 ("Because chancery courts possessed the power to order equitable disgorgement in the eighteenth century, we hold that contemporary federal courts are vested with the same authority by the Constitution and the Judiciary Act.").

[7] *Id*. at 118–20.

[8] *See infra* Part IV.

[9] *See* Sarah Worthington, *Reconsidering Disgorgement for Wrongs*, 62 MOD. L. REV. 218, 225 (1999).

[10] *See id.* at 218.

disgorgement remedy is not equitable. Part V discusses the implications of this conclusion. Finally, Part VI concludes that disgorgement is beyond the equitable powers of the federal courts.

I. First Principles: A Primer on the SEC's Disgorgement Remedy, Classic Disgorgement, and the Equity Jurisdiction of the Federal Courts

A. "Disgorgement" in the Securities Context

As described and granted in modern SEC cases, such as *Cavanagh*, the remedy of disgorgement consists of three elements.[11] First, it is a money judgment.[12] Second, it is measured by a defendant's profits acquired through wrongful behavior.[13] Third, it is awarded as an equitable remedy.[14]

When granting the SEC its disgorgement remedy, courts frequently bolster their decisions to grant the remedy with a discussion of its purpose.[15] "The primary purpose of disgorgement as a remedy for violation of the securities laws," according to a 2013 Second Circuit opinion, "is to deprive violators of their ill-gotten gains, thereby effectuating the deterrence objectives of those laws."[16] By deterring violations of the securities laws, the SEC's disgorgement remedy in turn promotes "the purpose of the federal securities laws to maintain investor confidence in the integrity of our capital markets."[17]

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[11] *Cavanagh*, 445 F.3d at 116 ("Defendant Hantges argues that the District Court exceeded its *equity powers* by imposing a 'disgorgement' remedy. The remedy consists of factfinding by a district court to determine the *amount of money acquired through wrongdoing* . . . and an order compelling the wrongdoer to *pay that amount* plus interest to the court.") (emphasis added).

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] *See, e.g.*, SEC v. Cioffi, 868 F. Supp. 2d 65, 70 (E.D.N.Y. 2012); SEC v. One or More Unknown Traders, 853 F. Supp. 2d 79, 83 (D.D.C. 2012); SEC v. Verdiramo, 907 F. Supp. 2d 367, 372 (S.D.N.Y. 2012).

[16] SEC v. Razmilovic, 738 F.3d 14, 36 (2d Cir. 2013).

[17] Ronald L. Cheney & Daniel M. Sibears, *Disgorgement in SEC Insider Trading Cases: Toward a New Measure of Disgorgement*, 26 BOS. BAR J. 5, 7–8 (1982); *accord* Ryan, *supra* note 4, at 5 (acknowledging deterrence rationale); Roach, *supra* note 4, at 30–31 (discussing deterrence and

B. Classic Disgorgement

"Classic disgorgement" is a traditional response to unjust enrichment against a wrongdoer that seeks to make illegal conduct unprofitable.[18] In this sense, "disgorgement" simply means "that the defendant must yield up gains that it cannot justly retain."[19] Though the term "disgorgement" is new to Anglo-American law,[20] the concept of classic disgorgement is not.[21] Historically, classic disgorgement occurred at law and in equity, as a claimant could

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consumer-confidence rationale). *But see* James R. Farrand, *Ancillary Remedies in SEC Civil Enforcement Suits*, 89 HARV. L. REV. 1779, 1802–05 (1976) (questioning applicability of consumer-confidence rationale absent compensatory component).

[18] RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 51(4), at 203 (2011) ("[T]he unjust enrichment of a conscious wrongdoer, or of a defaulting fiduciary without regard to notice or fault, is the net profit attributable to the underlying wrong. The object of restitution in such cases is to eliminate profit from wrongdoing while avoiding, so far as possible, the imposition of a penalty. Restitution remedies that pursue this object are often called 'disgorgement' or 'accounting.'").

[19] Colleen P. Murphy, *Misclassifying Monetary Restitution*, 55 SMU L. REV. 1577, 1625 (2002); *accord* BLACK'S LAW DICTIONARY 536 (9th ed. 2009) (defining "disgorgement" as "[t]he act of giving up something (such as profits illegally obtained) on demand or by legal compulsion").

[20] Roach, *supra* note 4, at 49 ("As applied in any context, 'disgorgement' was used in less than a dozen federal or state case opinions from 1800 to 1960. Perhaps more startling is the fact that the term was used so often between 1960 and 2000 even though the first proposed definitions only began to appear around 2000. The term was not used or defined in the Restatement First and was only defined in a draft of the Restatement Third as of 2000. Black's Law Dictionary only offered a definition after 2000 and, while many of the foundation articles on restitutionary remedies have mentioned the term, few ascribe any consensus to its meaning."); *see also* SEC v. R. J. Allen & Assocs., Inc., 386 F. Supp. 866, 880 (S.D. Fla. 1974) (recognizing that the term "disgorgement" is "a term of modern vintage").

[21] *See* Daniel Friedmann, *Restitution of Benefits Obtained Through the Appropriation of Property or the Commission of a Wrong*, 80 COLUM. L. REV. 504, 505 & nn.6–8 (1980) (citing Lightly v. Clouston, (1808) 127 Eng. Rep. 774 (C.P.); 1 Taunt. 112; Lamine v. Dorrell, (1705) 92 Eng. Rep. 303 (K.B.); 2 Ld. Raym. 1216; Howard v. Wood, (1679) 83 Eng. Rep. 540 (K.B.); 2 Lev. 245; Arris v. Stukely, (1677) 86 Eng. Rep. 1060 (Ex.); 2 Mod. 260).

recover a defendant's wrongfully obtained profits in a court of either jurisdiction.[22]

1. Classic Disgorgement at Law

Generally, when a claimant sought to recover a money judgment measured by a wrongdoer's profits, his action was at law.[23] To reach a wrongdoer's profits at law, a claimant had to waive the underlying wrong—namely, a tort—and bring an action for *indebitatus assumpsit*.[24] By waiving the tort, the claimant relinquished any claim to damages and instead opted to have his recovery measured by "the gains resulting to the defendant from his tort."[25] By bringing an action for *indebitatus assumpsit*, the claimant had to allege counterfactually that the tortfeasor owed the claimant a debt that the tortfeasor promised to repay.[26] Modern authorities use the term "quasi contract" to refer to the basis of liability in such cases, but the underlying idea and procedure are the same.[27]

Interestingly, one of the earliest cases involving classic disgorgement at law involved securities.[28] In *Lamine v. Dorrell*,[29] the tortfeasor took the claimant's securities and subsequently sold

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[22] Murphy, *supra* note 19 ("[O]btaining the defendant's gains could be accomplished both at law and equity, depending on the circumstances of the case."); Graham Douthwaite, *Profits and Their Recovery*, 15 VILL. L. REV. 346, 347 (1970) ("In our common law jurisprudence, profits, as such, are recoverable on the basis of a constructive trust in a suit brought in equity. At times, as will be seen, the same result has been reached in a suit at law on the basis of a quasi contract.").

[23] 1 DAN B. DOBBS, THE LAW OF REMEDIES § 4.1(2), at 556 (2d ed. 1993) ("Restitution claims for money are usually claims 'at law.'"); 1 GEORGE E. PALMER, THE LAW OF RESTITUTION § 2.12, at 157 (1978) ("When the victim of a tort or other wrong seeks a money judgment for the benefit obtained by the tortfeasor, the appropriate remedy frequently will be quasi contract.").

[24] *See* Friedmann, *supra* note 21. Literally, "indebiatus assumpsit" means "being indebted, he undertook." BLACK'S LAW DICTIONARY 142 (9th ed. 2009).

[25] 1 DOBBS, *supra* note 23, § 4.2(3), at 585.

[26] *Id.* at 578–79.

[27] *See id.* § 4.2(1), at 571–72; 1 PALMER, *supra* note 23, § 1.2, at 6–9; *see, e.g.*, Douthwaite, *supra* note 22 (acknowledging that profits are sometimes recoverable at law through quasi contract).

[28] *See* 1 PALMER, *supra* note 23, at 53.

[29] (1705) 92 Eng. Rep. 303 (K.B.); 2 Ld. Raym. 1216.

them.[30] Hence, the underlying tort was conversion.[31] Waiving his suit for conversion, the claimant sought the proceeds of the tortfeasor's sale of the securities on a theory of quasi contract.[32] The King's Bench ruled in the claimant's favor and awarded him the proceeds of the tortfeasor's sale of his securities.[33]

2. Classic Disgorgement in Equity

Courts of law did not have exclusive authority to order classic disgorgement, as courts of equity forced wrongdoers to give up ill-gotten gains in two situations.[34] First, a court of equity could order disgorgement as legal relief incidental to an award of equitable relief "such as an injunction, specific performance, or reformation or cancelation of an instrument."[35] In these situations, classic disgorgement was technically legal, not equitable.[36] Second, courts of equity ordered classic disgorgement where a claimant could show a fiduciary relationship between himself and the defendant.[37] Only in this latter category is classic disgorgement equitable.[38]

Thus, history reveals three distinct categories of classic disgorgement: (1) legal disgorgement at law; (2) legal disgorgement in equity; and (3) equitable disgorgement in equity. The SEC's disgorgement remedy claims to be a species of this last genus of

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[30] 1 PALMER, *supra* note 23, § 2.2, at 53.
[31] *Id.*
[32] *Id.*
[33] *Id.*
[34] *See* Douthwaite, *supra* note 22, at 350 (recognizing equity's ability to order disgorgement where such an order was incidental to an award of equitable relief and where there were substantive grounds in equity to require disgorgement).
[35] *Id.* (footnotes omitted); *accord* 1 DOBBS, *supra* note 23, § 2.7, at 180.
[36] *See* 1 DOBBS, *supra* note 23, § 2.7, at 180–81 ("Before the merger of law and equity, the rule developed that in certain instances, if equity obtained jurisdiction because of some equitable matter in the case, then equity might proceed to dispose of the entire controversy, and for this purpose might decide legal as well as equitable issues.").
[37] *See* Worthington *supra* note 9 (analyzing English cases and concluding that "disgorgement . . . is available *only* when the defendant has breached an obligation of 'good faith or loyalty'").
[38] *See* 1 DOBBS, *supra* note 23, § 4.3(5), at 610–11.

disgorgement.[39] To understand why the SEC must advance this position requires a brief introduction to federal equity jurisprudence.

C. The Equity Jurisdiction of the Federal Courts

If a claimant could recover a wrongdoer's profits at law or in equity, then why does it matter whether the SEC styles its disgorgement remedy as legal or equitable? The answer lies in the securities acts.[40] Nothing in the securities acts authorizes the SEC to seek legal disgorgement.[41] However, three separate provisions—Section 22(a) of the Securities Act of 1933, Section 21(d)(5) of the Securities Exchange Act of 1934, and Section 27 of the Securities Exchange Act of 1934—permit the agency to invoke the federal judiciary's equity jurisdiction.[42] Accordingly, federal courts may award disgorgement to the SEC only if disgorgement falls within the bounds of the federal courts' equity jurisdiction.[43]

Though the SEC's entitlement to equitable relief is clear from the face of the securities acts,[44] determining the extent of the federal judiciary's equity jurisdiction requires rigorous legal analysis.[45] The analysis necessarily begins with Article III of the United States Constitution and Section 11 of the Judiciary Act of 1789, which bestow equity jurisdiction upon the federal courts.[46]

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[39] *See supra* note 14 and accompanying text.

[40] Ryan, *supra* note 4, at 12.

[41] *Id.*

[42] *Id.* at 4 n.22 (discussing applicability of Section 21(d)(5) of the Securities Exchange Act of 1934); LOSS & SELIGMAN, *supra* note 4 (discussing reliance on Section 27 of the Securities Exchange Act of 1934); Comment, *supra* note 4, at 1188 & n.3 (discussing reliance on Section 27 of the Securities Exchange Act of 1934 and Section 22(a) of the Securities Act of 1933). For a case relying on Section 21(d)(5) of the Securities Exchange Act of 1934, see *SEC v. Lipson*, 278 F.3d 656, 662–63 (7th Cir. 2002). For a case relying on Section 27 of the Securities Exchange Act of 1934 and Section 22(a) of the Securities Act of 1933, see *SEC v. Chester Holdings, Ltd.*, 41 F. Supp. 2d 505, 528 (D.N.J. 1999).

[43] *See* Ryan, *supra* note 4, at 4 (stating that disgorgement "can lawfully be ordered only if it in fact constitutes *equitable* relief rather than legal relief").

[44] *See supra* note 42 and accompanying text.

[45] *See* Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999) (Scalia, J.) (setting forth test for equity jurisdiction).

[46] U.S. CONST. art. III, § 2, cl. 1 ("The judicial power shall extend to all Cases, in Law and Equity . . . ."); Judiciary Act of 1789, ch. 20, § 11, 1 Stat.

Whether a federal court possesses the power to grant a particular remedy pursuant to its equity jurisdiction depends on whether that remedy passes the test that the Supreme Court set forth in *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.*[47] Under *Grupo*, a remedy is within a federal court's equitable powers if, but only if, the remedy was granted "by the High Court of Chancery in England at the time of the adoption of the Constitution and the enactment of the original Judiciary Act, 1789."[48] In *Cavanagh*, the Second Circuit applied *Grupo* and concluded that the High Court of Chancery had the authority to order disgorgement in 1789.[49]

II. Disgorgement's History Under the Securities Acts

Since the Second Circuit decided *SEC v. Texas Gulf Sulphur Co.*[50] in 1971, the SEC's disgorgement remedy has played an integral role in enforcing the provisions of the securities acts.[51] The remedy is largely the brainchild of SEC lawyers of the late 1960s and early

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73, 78 (Sept. 24, 1789) ("[T]he circuit courts shall have original cognizance, concurrent with the courts of the several States, of all suits of a civil nature at common law or in equity.").

[47] *Grupo*, 527 U.S. at 318 (citing A. DOBIE, HANDBOOK OF FEDERAL JURISDICTION AND PROCEDURE 660 (1928)).

[48] *Id.*

[49] SEC v. Cavanagh, 445 F.3d 105, 120–21 (2d Cir. 2006) ("[F]ederal courts possess authority under the Constitution and the Judiciary Act to impose the equitable remedy of disgorgement.").

[50] 446 F.2d 1301, 1307–08 (2d Cir. 1971).

[51] LOSS & SELIGMAN, *supra* note 4 ("Beginning with *SEC v. Texas Gulf Sulphur Co.* in 1971, the courts have ordered restitution or disgorgement of profits in several Commission injunctive actions for trading while in possession of material nonpublic information."); Barbara Black, *Should the SEC Be a Collection Agency for Defrauded Investors?*, 63 BUS. LAW. 317, 320 (2008) ("*SEC v. Texas Gulf Sulphur Co.* was the first case in which an appellate court recognized the disgorgement remedy and required corporate insiders who traded on material nonpublic information to disgorge their illegal trading profits."); John D. Ellsworth, *Disgorgement in Securities Fraud Actions Brought by the SEC*, 1977 DUKE L.J. 641, 641–42 & nn.1–2 (1977) (identifying *Texas Gulf Sulphur* as the first time the SEC sought and received disgorgement); Comment, *supra* note 4, at 1194 ("Since *Texas Gulf Sulphur*, disgorgement of profits derived from illegal insider trading has become a 'regular' in the arsenal of enforcement remedies.").

1970s.[52] Stanley Sporkin, the Deputy Director of the SEC's Enforcement Division when courts began granting disgorgement, argued that courts could grant disgorgement pursuant to their equitable powers.[53] Specifically, Sporkin argued "that an equity court traditionally has been able to mold the kinds of remedies that are required to do justice."[54] Adopting Sporkin's argument, early courts ordering disgorgement in SEC enforcement proceedings premised their disgorgement orders on their equitable authority to grant relief that would effectuate the purposes of the securities acts as incidental to the grant of an injunction.[55] However, by the late 1970s and early 1980s, courts had begun ordering disgorgement in the absence of an injunction.[56] Under this modern approach, federal courts order the SEC's disgorgement remedy as an equitable remedy pursuant to their

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[52] *See* Ellsworth, *supra* note 51, at 641 n.1 (identifying 1966 as the first year in which the SEC argued that it could seek disgorgement in court); Stanley Sporkin, *SEC Developments in Litigation and the Molding of Remedies*, 29 BUS. LAW. 121, 122–23 (1974) (summarizing SEC's early argument for disgorgement); *see also* SEC v. R. J. Allen & Assocs., Inc., 386 F. Supp. 866, 880 (S.D. Fla. 1974) ("The word 'disgorgement' appears to be a term of modern vintage utilized in connection with Commission suits seeking to deprive the defendants of the gains from their wrongful conduct as an ancillary remedy to fully effect the deterrent force that is essential to adequate enforcement of the federal securities laws."). Various agencies have piggybacked on the SEC's efforts to convince courts that they may order disgorgement to secure disgorgement orders of their own. *See, e.g.*, FTC v. Bronson Partners, LLC, 654 F.3d 359, 372–75 (2d Cir. 2011) (FTC); CFTC v. Wilshire Inv. Mgmt. Corp., 531 F.3d 1339, 1344 (11th Cir. 2008) (CFTC); US v. Rx Depot, Inc., 438 F.3d 1052, 1061 (10th Cir. 2006) (FDCA). Nevertheless, authorities still associate the remedy with the SEC. *See, e.g.*, Rebecca Gross, Lauren Britsch, Kirk Goza & Jaclyn Epstein, *Securities Fraud*, 49 AM. CRIM. L. REV. 1213, 1271 (2012) ("Disgorgement is an equitable remedy that returns profits obtained by a defendant through securities fraud to the victim(s) of the fraud. The primary purposes of this remedy are to discourage securities law violations . . . .").

[53] Sporkin, *supra* note 52.

[54] *Id.* at 123.

[55] Ryan, *supra* note 4, at 3; *see, e.g.*, *R. J. Allen & Assocs., Inc.*, 386 F. Supp. at 880–81.

[56] LOSS & SELIGMAN, *supra* note 4, at 1056 ("Disgorgement may be granted even when an injunction is denied . . . ." (citing SEC v. Commonwealth Chem. Sec., Inc., 574 F.2d 90, 103 n.13 (2d Cir. 1978); SEC v. Lund, 570 F. Supp. 1397, 1404 (C.D. Cal. 1983))).

equity jurisdiction.[57] Syllogistically, modern courts reason as follows: under the securities acts, courts may grant equitable remedies; disgorgement is an equitable remedy; therefore, courts may grant disgorgement.[58] The syllogism is incontestably valid.[59] Whether it is sound is a different question.[60]

Before *Cavanagh*, the soundness of the courts' syllogistic reasoning was presumed, as courts and academics concluded that disgorgement was an equitable remedy with little or no reflection.[61]

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[57] SEC v. Cavanagh, 445 F.3d 105, 120 (2d Cir. 2006) ("Because chancery courts possessed the power to order equitable disgorgement in the eighteenth century, we hold that contemporary federal courts are vested with the same authority by the Constitution and the Judiciary Act.").

[58] *See, e.g.*, SEC v. First City Fin. Corp., 890 F.2d 1215, 1230 (D.C. Cir. 1989) ("Disgorgement is an equitable remedy designed to deprive a wrongdoer of his unjust enrichment and to deter others from violating the securities laws . . . . Unless otherwise provided by statute, all the inherent equitable powers of the District Court are available for the proper and complete exercise of that jurisdiction . . . . Disgorgement, then, is available simply because the relevant provisions of the Securities Exchange Act of 1934, sections 21(d) and (e), 15 U.S.C. §§ 78u(d) and (e), vest jurisdiction in the federal courts.") (internal citations and quotations omitted).

[59] IRVING M. COPI & CARL COHEN, INTRODUCTION TO LOGIC 13 (12th ed. 2005) ("A deductive argument is *valid* when, if its premises are true, its conclusion *must* be true.").

[60] *Id.* at 19 ("When an argument is valid, *and* all of its premises are true, we call it sound.").

[61] Ryan, *supra* note 4, at 1 ("The SEC commonly describes disgorgement as an equitable remedy, and courts similarly begin their disgorgement analyses by assuming as axiomatic the equitable nature of disgorgement."); *see, e.g.*, SEC v. Blavin, 760 F.2d 706, 713 (6th Cir. 1985) ("Once the Commission has established that a defendant has violated the securities laws, the district court possesses the equitable power to grant disgorgement . . . ."); 11A EDWARD N. GADSBY, BUSINESS ORGANIZATIONS § 9.03(2) (1984) ("Disgorgement is an equitable remedy designed to deprive defendants of all gains flowing from their wrong, rather than to compensate the victims of the fraud . . . ."), *quoted in* Thomas C. Mira, Comment, *The Measure of Disgorgement in SEC Enforcement Actions Against Inside Traders Under Rule 10b-5*, 34 CATH. U. L. REV. 445, 445 n.1 (1985). Some judges, however, were less credulous. *See* SEC v. MacDonald, 699 F.2d 47, 55 (1st Cir. 1983) (Coffin, J., dissenting in part) ("I concede that there is no case or other authority clearly sanctioning full disgorgement as 'equitable'."). Others explicitly recognized the *assumption* that disgorgement was an equitable remedy. *See* SEC v. Lipson, 278 F.3d 656, 662 (7th Cir. 2002)

Though *Cavanagh* valiantly attempted to show that the SEC's disgorgement remedy was equitable, its analysis is, nonetheless, misguided.

III. An Analysis of Cavanagh

In *Cavanagh*, the Second Circuit purportedly dispelled any doubts as to the soundness of the syllogism justifying disgorgement, legitimizing over three decades of disgorgement orders.[62] Applying the Supreme Court's test for equitable jurisdiction set forth in *Grupo*,[63] the Second Circuit saw the question before it as "whether the remedies available at chancery in 1789 included disgorgement."[64]

(Posner, J.) ("Disgorgement in SEC cases has been *assumed* to be an equitable remedy.") (emphasis added).

[62] *Cavanagh*, 445 F.3d at 116–17 ("[T]his case is the first to present squarely the question whether this remedy survives the Supreme Court's teachings in *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308, 119 S.Ct. 1961, 144 L.Ed.2d 319 (1999), on the proper scope of equitable remedies in the federal courts. We hold that it does.").

[63] Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999).

[64] *Cavanagh*, 445 F.3d at 118. Roughly a month after the Second Circuit decided *Cavanagh*, the Supreme Court decided *Sereboff v. Mid Atlantic Med. Servs., Inc.*, 547 U.S. 356 (2006). In *Sereboff*, the Court announced that when determining whether a particular type of relief was legal or equitable, it would look to authorities from "the days of the divided bench." *Id.* at 362 (citation omitted). As the Federal Rules of Civil Procedure merged law and equity in 1938, FED. R. CIV. P. 2, *Sereboff* ostensibly widens the inquiry and provides courts with nearly 150 years of additional case law to support their conclusions. *See Sereboff*, 547 U.S. at 362. According to Professor George Roach, the Supreme Court in *Sereboff* "either made a mistake or has introduced a substantial change in the analysis detailed in *Grupo*." Roach, *supra* note 4, at 39; *see also* George P. Roach, *Counter-Restitution for Monetary Remedies in Equity*, 68 WASH. & LEE L. REV. 1271, 1310 n.205 (2011) (calling *Sereboff* a "slightly different standard" from *Grupo*). However, Professor Anthony DiSarro views *Grupo* as setting the standard "to determine the scope of federal court equitable jurisdiction conferred under the Judiciary Act of 1789" and *Sereboff* as governing the determination of "whether a particular claim qualified as 'equitable' for purposes of statutory relief." Anthony DiSarro, *Freeze Frame: The Supreme Court's Reaffirmation of the Substantive Principles of Preliminary Injunctions*, 47 GONZ. L. REV. 51, 92–95 (2011). Whether *Sereboff* changes the *Grupo* standard is of academic interest but is beyond the scope of this note. The focus of this note is not on determining the

Given that the term "disgorgement" was unlikely to appear in the English Reports, the Second Circuit adopted a functional analysis that focused on how the High Court of Chancery handled a defendant who profited from his illegal behavior.[65] *Cavanagh* concluded that eighteenth-century English chancellors ordered remedies that were functionally identical to the SEC's disgorgement remedy.[66] In support of its conclusion, *Cavanagh* cited allegedly analogous equitable remedies, two eighteenth-century English cases, and two colonial American decisions.[67] After careful analysis, *Cavanagh*'s three-headed argument fails to show that the High Court of Chancery granted remedies resembling the SEC's disgorgement remedy in 1789. Thus, the seemingly imposing argument is nothing more than a Chimera.

A. Analysis of Allegedly Analogous Equitable Remedies

In finding that disgorgement is an equitable remedy, *Cavanagh* relied heavily upon disgorgement's superficial similarities to the equitable remedies of "accounting, constructive trust, and restitution."[68] Even before *Cavanagh*, courts and academics brusquely concluded that disgorgement was analogous to remedies whose equitable nature was uncontroversial.[69] Perhaps this implies

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applicable standard but on analyzing *Cavanagh*'s application of the relatively straightforward *Grupo* standard.

[65] *Cavanagh*, 445 F.3d at 118 ("[O]ur inquiry concerns not the name used by equity courts and commentators for historical remedies but rather their specific actions and the resulting practical consequences. This note does not take issue with the Second Circuit's functional approach. After all, "[w]hat's in a name? that which we call a rose [b]y any other name would smell as sweet." WILLIAM SHAKESPEARE, ROMEO AND JULIET act 2, sc. 2, ll. 43–44 (Brian Gibbons ed., Routledge 1980) (1599).

[66] *Cavanagh*, 445 F.3d at 120.

[67] *Id.* at 118–20.

[68] *Id.* at 119.

[69] *See, e.g.*, SEC v. Commonwealth Chem. Sec., Inc., 574 F.2d 90, 96 (2d Cir. 1978) (Friendly, J.) ("[The SEC's seeking disgorgement] is decidedly more *analogous* to the traditional jurisdiction of equity to award restitution.") (emphasis added); SEC v. R. J. Allen & Assocs., Inc., 386 F. Supp. 866, 880 (S.D. Fla. 1974) ("[T]his Court *equates* disgorgement with restitution and recoupment which are equity remedies of ancient origin.") (emphasis added); Mira, *supra* note 61, at 445 ("[Disgorgement is] *akin* to

that disgorgement has always lacked a foundation in history and could only be justified through an analogy.[70] In any event, *Cavanagh*'s application of the *Grupo* standard deserves careful consideration to determine whether it withstands scrutiny. Because *Cavanagh* relied on an argument from analogy, this section of the note will focus on the similarities and differences between the SEC's disgorgement remedy and the allegedly analogous equitable remedies.[71] In the end, the disanalogies between disgorgement, on one hand, and the remedies of accounting, constructive trust, and restitution, on the other, vitiate *Cavanagh*'s analogical arguments.[72]

1. A Comparison of the SEC's Disgorgement Remedy and the Remedy of Accounting

The first equitable remedy to which *Cavanagh* analogized disgorgement is the remedy of accounting.[73] In his seminal work on the remedy of accounting, Professor Joel Eichengrun defined the accounting as a "general equitable remedy to recover the income from another's property wrongfully retained by [a] fiduciary."[74] A

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the ancient principle of restitution whereby an unjustly enriched party must restore benefits received to an aggrieved party.") (emphasis added); Comment, *supra* note 4, at 1195 ("The remedies employed to grant monetary relief are *basically* the historical ones of restitution and rescission.") (emphasis added).

[70] Naturally, if modern courts could find clear examples of disgorgement in the pages of the English Reports, they would not need to resort to an argument from analogy to justify their disgorgement orders. As Justice Holmes acknowledged, "[a] page of history is worth a volume of logic." New York Trust Co. v. Eisner, 256 U.S. 345, 349 (1921) (Holmes, J.).

[71] "[D]isanalogies are the primary weapon against an analogical argument." COPI & COHEN, *supra* note 59, at 454.

[72] *See id*. at 13, 443 (stating that analogical arguments can have varying degrees of strength but cannot be "valid" or "invalid"); *see also infra* Part IV (concluding that *Cavanagh*'s analogies lend no support to *Cavanagh*'s conclusion that the SEC's disgorgement remedy is equitable).

[73] *Cavanagh*, 445 F.3d at 119.

[74] Joel Eichengrun, *Remedying the Remedy of Accounting*, 60 IND. L.J. 463, 467 (1985). Eichengrun labels this accounting the "true accounting." *Id.* at 463. He identifies other remedies that courts of equity had labeled as "accounting," but states that these other "accounting[s]" did not come into existence until the nineteenth century. *Id.* at 467. As this focuses on *Cavanagh*'s application of the *Grupo* standard, such nineteenth-century

plaintiff who established a right to an accounting received a money judgment against the defendant measured by the amount of the defendant's ill-gotten gains.[75] Insofar as the accounting remedy results in a money judgment, it is unique amongst equitable remedies.[76]

Given that the SEC's disgorgement remedy and the remedy of accounting result in money judgments measured by the amount of a defendant's ill-gotten gains, they are similar in their *outcome*.[77] However, they are different in their *application*.[78] The SEC's disgorgement remedy applies to wrongdoing, namely, transgressions of the securities laws.[79] It does not require a fiduciary relationship.[80] In stark contrast, the remedy of accounting does not extend to wrongdoing but applies only to breaches of fiduciary relationships.[81]

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developments are irrelevant. *See* Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999); *Cavanagh*, 445 F.3d at 117–18. Hence, when this note uses the term "accounting," it refers exclusively to Eichengrun's "true accounting."

[75] Eichengrun, *supra* note 74, at 463.

[76] JOHN P. DAWSON, UNJUST ENRICHMENT: A COMPARATIVE ANALYSIS 37–38 (1951) ("[The accounting] was and is a restitutionary remedy ending, unlike the other equitable remedies, in a simple money decree.").

[77] *Compare* LOSS & SELIGMAN, *supra* note 4 (stating that disgorgement "is a method of forcing a defendant to give up the amount by which he was unjustly enriched"), *with* Eichengrun, *supra* note 74 (stating that an accounting results in "an order directing payment of the sum of money found due").

[78] *Compare Cavanagh*, 445 F.3d at 117 ("[D]isgorgement has been used by the SEC and courts to prevent wrongdoers from unjustly enriching themselves through violations . . . ."), *with* Eichengrun, *supra* note 74 ("The accounting thus evolved into a general equitable remedy to recover the income from another's property wrongfully retained by the fiduciary.").

[79] *Cavanagh*, 445 F.3d at 117 ("[D]isgorgement has been used by the SEC and courts to prevent wrongdoers from unjustly enriching themselves through violations . . . .").

[80] *See supra* Part I.A (summarizing requirements for SEC's disgorgement remedy without reference to a fiduciary relationship).

[81] 1 DOBBS, *supra* note 23, § 4.3(5), at 610–11; Eichengrun, *supra* note 74, at 468; Christopher C. Langdell, *A Brief Survey of Equity Jurisdiction* (pt. 2), 2 HARV. L. REV. 241, 248 (1889).

Thus, there is a distinction between the equitable remedy of accounting and the SEC's disgorgement remedy.[82]

Furthermore, the distinction between the accounting and the SEC's disgorgement is not a mere nicety.[83] The presence of a fiduciary relationship between the claimant and the wrongdoer was essential to empower a court of equity to grant a money judgment in the form of an accounting.[84] In 1882, and again in 1906, the United States Supreme Court recognized the importance of a fiduciary relationship to the accounting and declined to extend the remedy from fiduciaries to wrongdoers.[85] Doing so, the Court wrote, "would extend the jurisdiction of equity to every case of tort, where the wrong-doer had realized a pecuniary profit from his wrong."[86] Similarly, writing on the accounting in 1889, Christopher C. Langdell stated: "[T]here must be a fiduciary relation between the plaintiff and the defendant . . . . This requirement disposes at once of all cases in which the defendant has acquired his possession wrongfully . . . ."[87] Finally, in 1951, Professor John P. Dawson commented that, under traditional equity jurisprudence, the holding of a 1927 New York Court of Appeals case that had ordered an accounting against a wrongdoer was "not to be accepted."[88] Hence, the fiduciary-wrongdoer distinction between the accounting and the SEC's disgorgement remedy undermines *Cavanagh*'s analogy to the accounting.[89]

Moreover, the fiduciary-wrongdoer distinction not only damages *Cavanagh*'s analogy between the two remedies but also undermines *Cavanagh*'s entire mission.[90] The SEC's disgorgement

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[82] *See supra* notes 78–81 and accompanying text (showing that the accounting remedy requires a fiduciary relationship, whereas the SEC's disgorgement remedy does not).
[83] *See* Langdell, *supra* note 81.
[84] 1 DOBBS, *supra* note 23, at 610–11; Eichengrun, *supra* note 74.
[85] *See* Eichengrun, *supra* note 74, at 482 n.83 (citing United States v. Bitter Root Dev. Co., 200 U.S. 451 (1906); Root v. Lake Shore & Mich. S. Ry. Co., 105 U.S. 189 (1882)).
[86] *Id.* (quoting *Root*, 105 U.S. at 214).
[87] Langdell, *supra* note 81.
[88] DAWSON, *supra* note 76, at 38 & 156 n.26 (citing Fur & Wool Trading Co. v. Fox, 245 N.Y. 215 (1927)).
[89] *See supra* notes 78–88 and accompanying text (demonstrating the existence of a difference between the accounting and the SEC's disgorgement remedy and the significance of that difference).
[90] *See* Langdell, *supra* note 81; Worthington, *supra* note 9.

remedy purports to be an equitable remedy that results in a money judgment.[91] However, only one equitable remedy resulted in a money judgment: the accounting.[92] As shown earlier, the accounting and the SEC's disgorgement remedy are not analogous, let alone synonymous.[93] Therefore, the fiduciary-wrongdoer distinction between the accounting and the SEC's disgorgement remedy forecloses the possibility that *Cavanagh* could show that the High Court of Chancery awarded claimants money judgments measured by a wrongdoer's profits in 1789.[94] Nevertheless, this note will continue its analysis.

2. A Comparison of the SEC's Disgorgement Remedy and the Constructive Trust

As a preliminary matter, Cavanagh introduces ambiguity when it likens the SEC's disgorgement remedy to the constructive trust.[95] The term "constructive trust" can refer to the *remedial* constructive trust or the *institutional* constructive trust.[96] A remedial constructive trust is a remedy for unjust enrichment that requires a defendant to relinquish "identifiable property . . . and its traceable product" to a claimant.[97] It is not a trust but an "analogy or

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[91] *See supra* Part I.A (defining SEC's disgorgement remedy).
[92] *See supra* note 76 and accompanying text.
[93] *See supra* notes 78–88 and accompanying text (recognizing fiduciary-wrongdoer distinction between the accounting and the SEC's disgorgement remedy).
[94] *See* Langdell, *supra* note 81.
[95] *See* H. Jefferson Powell, *"Cardozo's Foot": The Chancellor's Conscience and Constructive Trusts*, 56 LAW & CONTEMP. PROBS. 7, 10 (1993) ("Although both U.S. and English lawyers are familiar with the term 'constructive trust,' as is so often the case similar language disguises substantive differences.").
[96] *Id.* ("English law has always thought of the constructive trust as an institution . . . as opposed to the American attitude that the constructive trust is purely a remedial device.") (internal quotations omitted).
[97] RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 55(1) & (2), at 296 (2011); *accord* 3 AUSTIN WAKEMAN SCOTT, THE LAW OF TRUSTS § 462.1, at 2315 (1939) ("A constructive trust arises where a person who holds title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it.").

metaphor."[98] On the other hand, an institutional constructive trust is "a substantive principle of liability normally imposed where a fiduciary relationship exists,"[99] which permits beneficiaries to recover trust assets and their traceable product from express trustees in breach of their duties or from "takers with notice of an express trust."[100] Each conception of the constructive trust poses its own unique problem for *Cavanagh*'s analogy, and they share a common feature that distinguishes them from the SEC's disgorgement remedy.

First, if *Cavanagh* intended to analogize the SEC's disgorgement remedy to the institutional constructive trust, it runs into problems similar to those it encountered with its accounting analogy.[101] This is because the institutional constructive trust, like the accounting, requires a fiduciary relationship for liability.[102] In contrast, the SEC's disgorgement remedy sweeps more broadly and seeks to impose a liability to surrender ill-gotten gains on those who have violated the securities laws irrespective of the presence of fiduciary obligations.[103] Hence, the SEC's disgorgement remedy's breadth of application nullifies an analogy to the institutional constructive trust.[104]

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[98] 1 DOBBS, *supra* note 23, § 4.3(2), at 590. In this sense, the constructive trust is the equitable equivalent of the quasi contract. *See id.* ("The quasi-contract is imposed by courts to prevent unjust enrichment, not generated by contract. The constructive trust is likewise imposed by court to prevent unjust enrichment, and not generated by any trust."); *accord* SCOTT, *supra* note 97, at 2316 ("A constructive trust bears much the same relation to an express trust that a quasi-contractual obligation bears to a contract. In the case of a constructive trust, as in the case of quasi contract, an obligation is imposed not because of the intention of the parties but in order to prevent unjust enrichment.").

[99] Powell, *supra* note 95, at 11 (quoting Avondale Printers & Stationers Ltd. v. Haggie [1979] 2 NZLR 124, 147 (Mahon, J.)); *accord* 1 PALMER, *supra* note 23, § 1.3, at 11–12.

[100] DAWSON, *supra* note 76, at 27.

[101] *See supra* Part III.A.1 (discussing problem of fiduciary-wrongdoer distinction associated with *Cavanagh*'s analogizing the SEC's disgorgement remedy to the accounting remedy).

[102] *Compare supra* text accompanying note 81 (accounting), *with supra* text accompanying note 100 (institutional constructive trust).

[103] *See supra* Part I.A (explaining SEC's disgorgement remedy).

[104] *See supra* text accompanying notes 99–100 (stating that a fiduciary relationship is necessary to find an institutional constructive trust).

Second, an analogy to the remedial constructive trust fares no better.[105] Because *Grupo* requires a court to analyze the practices of the English Chancery in 1789 to determine whether a federal court may grant a remedy under its equity jurisdiction, the remedial constructive trust must survive its own *Grupo* analysis before an analogy to it will have any legitimacy.[106] Because *Grupo* is a functional inquiry, merely finding Chancery opinions that employ the terms "constructive trust" will not do.[107] Poring over the pages of the English Reports in search of evidence of a remedial constructive trust would be an exercise in futility because English precedent is clear: there is no remedial constructive trust.[108] Hence, an analogy to the remedial constructive trust lends no support to *Cavanagh*'s

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[105] Ryan writes: "In the securities law context, true disgorgement should . . . mean that the defendant in fact possesses or at least has access to the asset being disgorged." Ryan, *supra* note 4, at 10. He goes on to state that disgorgement is equitable only when there is a "specific pool of money that can be turned over to the SEC." *Id.* at 11. Thus, according to Ryan, the SEC's disgorgement remedy is equitable only when it is the byproduct of a remedial constructive trust. *Compare id.* at 10–11, *with supra* text accompanying note 97. There are two problems with Ryan's conclusion. First, the constructive trust was not the only equitable remedy that a claimant could use as a stepping-stone to a defendant's profits, as an accounting was available to certain claimants. *See supra* notes 74–76 and accompanying text. Second, given that Ryan neglects any discussion of a fiduciary relationship in connection with his notion of the SEC's disgorgement remedy, he is referring to a remedial constructive trust, which must be subjected to its own *Grupo* analysis. *See infra* notes 106–09 and accompanying text.

[106] *See* Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999).

[107] *See* SEC v. Cavanagh, 445 F.3d 105, 118 (2d Cir. 2006).

[108] Powell, *supra* note 95, at 11 ("The court's primary focus, under the traditional English approach, must be on the presence or absence of evidence showing the existence of a quasi-fiduciary relationship and its abuse, not on the overall equities between plaintiff and defendant."); 1 PALMER, *supra* note 23, § 1.3, at 11–12 ("As one English writer has said, 'the fiduciary relationship is clearly wed to the constructive trust over the whole, or little short of the whole, of the trust's operation in English law.' The great development of constructive trust as a remedy aimed at unjust enrichment has taken place in [the United States], for most of our courts have freed the remedy of any necessary connection with fiduciary relationship.").

conclusion that the SEC's disgorgement remedy finds historical support in eighteenth-century English equity jurisprudence.[109]

Finally, regardless of whether the Second Circuit had the institutional or remedial constructive trust in mind when crafting its analogy, both conceptions differ from the SEC's disgorgement remedy in a significant way. A claimant who is entitled to a constructive trust, in any sense of the word, may recover identifiable property and its traceable product.[110] Unlike any conception of the constructive trust, the SEC's disgorgement remedy "involves no claim to particular assets and no requirement of tracing."[111] Instead, when the SEC seeks profits via its disgorgement remedy, it need only show a "causal relationship between [the violation of the securities laws] and the property to be disgorged."[112] Hence, the SEC's disgorgement remedy is different from the institutional and remedial constructive trusts. Accordingly, *Cavanagh*'s analogy to the "constructive trust" cannot support a conclusion that the English Chancery was awarding disgorgement in 1789.[113]

3. A Comparison of the SEC's Disgorgement Remedy and "Restitution"

None of the remedial analogies in *Cavanagh* is more confusing, and confused, than the analogy to "restitution."[114] As the Third Restatement of Restitution and Unjust Enrichment explains, "when . . . the word 'restitution' refers to a remedy, the fact that restitution can take such different forms may leave its meaning uncertain."[115] Literally, "restitution restores something to someone,

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[109] *See supra* text accompanying notes 106–08.

[110] *Compare supra* text accompanying note 97 (remedial constructive trust), *with supra* text accompanying note 100 (institutional constructive trust).

[111] *Cf.* RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 51 cmt. b, at 205 (2011) (discussing disgorgement); *accord* Ryan, *supra* note 4, at 8–9 ("[D]isgorgement is an equitable obligation to return a sum equal to the amount wrongfully obtained, rather than a requirement to replevy a specific asset . . . ." (quoting SEC v. Banner Fund Int'l, 211 F.3d 602, 617 (D.C. Cir. 2000))).

[112] Ryan, *supra* note 4, at 9 (quoting *Banner Fund Int'l*, 211 F.3d at 617).

[113] *See supra* notes 111–12 and accompanying text.

[114] *See* SEC v. Cavanagh, 445 F.3d 105, 119 (2d Cir. 2006).

[115] RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 1 cmt. e(1), at 8 (2011).

or restores someone to a previous position."[116] The means through which a claimant may receive "restitution" are restitution's "characteristic remedies."[117] Some of these remedies are legal; others are equitable.[118] Whether a particular remedy that results in restitution "is legal or equitable depends on 'the basis for [the plaintiff's] claim' and the nature of the underlying remedies sought."[119] However, this is the precise question *Cavanagh* purports to answer when analogizing disgorgement to "restitution."[120] Therefore, the analogy to "restitution" is circular and unhelpful.[121]

B. Analysis of Binding Precedents

After analogizing disgorgement to traditional equitable remedies, *Cavanagh* cites two eighteenth-century decisions of the High Court of Chancery: *Garth v. Cotton* and W*illoughby v. Willoughby*.[122] Because the *Grupo* standard requires federal courts to look to the High Court of Chancery's practices in 1789 to determine their equitable jurisdiction, these cases are critical to *Cavanagh*'s

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[116] *Id.*

[117] *Id.* § 1 cmt. e(3), at 9.

[118] *Id.* § 4(1); *accord* 1 DOBBS *supra* note 23, § 4.1(1), at 556. Many courts and authorities incorrectly assert that "restitution is exclusively an equitable remedy." Murphy, *supra* note 19, at 1579 ("[D]ue to a misreading of history and precedents, some courts have suggested that restitution is exclusively an equitable remedy."); *accord* Caprice L. Roberts, *The Restitution Revival and the Ghosts of Equity*, 68 WASH. & LEE L. REV. 1027, 1038 & n.69 (2011) (criticizing *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 255–56 (1993) for "describing restitution—incompletely—as 'a remedy traditionally viewed as 'equitable'"").

[119] Great-W. Life & Annuity Ins. Co. v. Knudson, 534 U.S. 204, 213 (2002) (Scalia, J.) (citing Reich v. Continental Casualty Co., 33 F.3d 754, 756 (7th Cir. 1994) (Posner, J.)).

[120] SEC v. Cavanagh, 445 F.3d 105, 119 (2d Cir. 2006).

[121] *See* COPI & COHEN, *supra* note 59, at 116 (defining circular definitions); *cf.* Murphy, *supra* note 19, at 1637 ("With respect to a statutory authorization of 'equitable relief,' labeling the remedy as restitution is beside the point because ultimately, the question comes down to how courts interpret the meaning of 'equitable relief.'").

[122] *Cavanagh*, 445 F.3d at 120 (citing Garth v. Cotton, (1756) 27 Eng. Rep. 1182 (Ch.) 1196; 1 Ves. Sen. 524, 546; Willoughby v. Willoughby, (1756) 99 Eng. Rep. 1366 (Ch.) 1366; 1 Term. Rep. 763, 763).

analysis.[123] However, these cases, much like Cavanagh's analogical arguments, lend no support to the conclusion that the High Court of Chancery awarded a remedy akin to the SEC's disgorgement remedy in 1789.[124] Thus, these cases do not empower a federal court to order the SEC's disgorgement remedy pursuant to its equitable powers.[125]

1. *Garth v. Cotton*

The first case on which *Cavanagh* relies in attempting to show that the SEC's disgorgement remedy has historical foundations in the practices of the English High Court of Chancery is *Garth*.[126] Though to paint a clear picture of the entire dispute in *Garth* would be nearly impossible, the relevant facts are straightforward.[127] D.M. Kerly recounts them as follows:

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[123] *See* Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999).

[124] *See infra* Part III.C.1-2 (showing that the remedies granted in *Garth* and *Willoughby* differ from the SEC's disgorgement remedy because *Garth* and *Willoughby* involved breaches of trust).

[125] *See Grupo*, 527 U.S. at 318–19.

[126] *Cavanagh*, 445 F.3d at 120 (citing *Garth,* 27 Eng. Rep. at 1196; 1 Ves. Sen. at 546). *Garth* was reported several times. *See, e.g.*, (1753) 26 Eng. Rep. 1231 (Ch.); 3 Atk. 751; (1753) 27 Eng. Rep. 1182 (Ch.); 1 Ves. Sen. 524; (1753) 28 Eng. Rep. 510 (Ch.); 1 Ves. Sen. 233; (1753) 21 Eng. Rep. 239 (Ch.); 1 Dickens 183. The reports are largely consistent with each other. *See* Tara Helfman, *Land Ownership and the Origins of Fiduciary Duty*, 41 REAL PROP. PROB. & TR. J. 651, 661 n.27 (2006).

[127] According to Tara Helfman, "the facts of [Garth] are so convoluted as to merit a separate essay . . . ." Helfman, *supra* note 126, at 658. *Cavanagh* summarizes the facts of *Garth* as follows: "[C]ontingent remaindermen sought relief in equity when a life tenant and trustees conspired to defraud the remaindermen by selling timber from the relevant estate and dividing the proceeds among themselves. The plaintiff remainderman, who lacked a remedy at law for now-obscure reasons related to English land law of the time, sought an order compelling the wrongdoers to give him the proceeds of the asserted waste of the land's assets." 445 F.3d at 120. The opinion in *Cavanagh* slightly misstates the facts of the case, as the trustees were not part of the conspiracy; they merely failed to prevent it. *See Garth*, 21 Eng. Rep. at 246; 1 Dickens at 201 ("[H]ere is no positive act of the trustees, but only a laches, or neglect in not performing their trust, and bringing a bill for an injunction to stop this waste."); *Garth*, 26 Eng. Rep. at 1232; 3 Atk. at 754 ("But in this case the trustees have not acted . . . ."). This is not surprising, as *Cavanagh* cites only to a report of the arguments presented in

> [A] settlement had been made on the tenant for life, for 99 years, if he should so long live, with remainder to trustees to preserve contingent remainders, with remainder to the eldest son in tail and other remainders, and with remainder over to the Defendant's testator. The tenant for life was impeachable for voluntary waste, but, before any son was born, he made an arrangement with the Defendant's testator to cut the timber and divide the proceeds. The Plaintiff, the eldest son of the tenant for life, now sued to recover the money paid under this arrangement.[128]

After hearing the parties' arguments, Lord Chancellor Hardwicke held that the defendant must account for the profits derived from the sale of the timber and prejudgment interest.[129] Hardwicke rested his conclusion on the following argument. First, Hardwicke acknowledged that the trustees could have brought suit to enjoin the collusion between the plaintiff's father and the defendant but that they had, for reasons unknown, failed to do so.[130] Second, Hardwicke posited the general rule that a stranger to a trust will be liable under the trust for profits derived from its breach if he (1) purchased trust property with notice of the trust, or (2) received, without providing valuable consideration, trust property without notice of the trust.[131] Third, Hardwicke established a formula to find a "nominal or imputed breach of trust on the part of the trustees."[132] Such a breach is the sum of notice of the trust on behalf of the plaintiff's father and the defendant, and the trustees' negligence in failing to enjoin the breach of the trust.[133] Hence, there was a breach

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the case, not a report of the chancellor's decision. *See* 445 F.3d at 120 (citing *Garth*, 27 Eng. Rep. 1182; 1 Ves. Sen. 524).

[128] D. M. KERLY, AN HISTORICAL SKETCH OF THE EQUITABLE JURISDICTION OF THE COURT OF CHANCERY 260 (1890).

[129] *Garth*, 26 Eng. Rep. at 1234–235; 3 Atk. at 758; *Garth*, 21 Eng. Rep. at 239; 1 Dickens at 183.

[130] KERLY, *supra* note 128; *Garth*, 21 Eng. Rep. at 245; 1 Dickens at 198.

[131] *Garth*, 21 Eng. Rep. at 245; 1 Dickens at 200.

[132] *See* Root v. Lake Shore & M.S. Ry. Co., 105 U.S. 189, 216 (1881).

[133] *Id.*; *see also Garth*, 21 Eng. Rep. at 246; 1 Dickens at 201.

of trust to which the defendant was a party. Therefore, the defendant was required to account for profits derived from that breach.[134]

Hardwicke's opinion in *Garth* garnered significant attention,[135] as it is the first case to establish a claim for equitable waste.[136] "Waste," as Black's Law Dictionary defines the term, is "[p]ermanent harm to real property committed by a tenant (for life or for years) to the prejudice of the heir, the reversioner, or the remainderman."[137] "Equitable waste" is that species of "[w]aste that abuses a privilege of nonimpeachability at common law, for which equity will restrain the commission of willful, destructive, malicious, or extravagant waste."[138] A "privilege of nonimpeachability" arises when the instrument creating the tenancy grants the tenant the land "without impeachment of waste" or similar language.[139] At law, such language shielded a tenant from any liability for waste because it gave the tenant a legal right to commit acts of waste.[140] Chancellors believed themselves to be equally as powerless to provide a remedy for waste where the instrument creating the tenancy contained a nonimpeachability clause—until *Garth*.[141]

Additionally, before *Garth*, the High Court of Chancery would grant an accounting in a case of legal waste but only as relief incidental to its granting an injunction.[142] *Garth* held that the Chancery could grant an accounting, absent any other form of equitable relief, in a case of equitable waste.[143] This has led some authorities to characterize equitable waste as an exception to the general rule that the Chancery will not grant an accounting for waste

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[134] *See supra* text accompanying note 129.

[135] *See, e.g.*, Tate v. Field, 56 N.J. Eq. 35, 38 (1897) (identifying *Garth v. Cotton* as a "famous case"); KERLY, *supra* note 128, at 259 (identifying *Garth v. Cotton* as a "celebrated judgment").

[136] 1 HENRY WILMOT SETON, FORMS OF JUDGMENTS AND ORDERS 540 (6th ed. 1901).

[137] BLACK'S LAW DICTIONARY 1727 (9th ed. 2009).

[138] *Id.* at 1728.

[139] 1 JOHN NORTON POMEROY, A TREATISE ON EQUITABLE REMEDIES § 489, at 811 (1905).

[140] *Id.*

[141] SETON, *supra* note 136.

[142] 1 POMEROY, *supra* note 139, at 814–15.

[143] *See supra* note 129 and accompanying text.

absent a grant of some other type of equitable relief.[144] However, given Hardwicke's express reliance on a breach of trust and dicta stating that "a tenant for years [is] a kind of fiduciary for the lessor, or the remainder man, who stands in his place,"[145] equitable waste is nothing more than an application of the general rule that equity will grant an accounting in cases involving breaches of trust.[146]

From this analysis of *Garth*, one can see that it does not support *Cavanagh*'s holding. First, even if *Garth* is the lone exception to the rule that equity will not grant an accounting for waste absent an injunction, one cannot shoehorn *Cavanagh*'s facts into that narrow exception only for equitable waste.[147] Second, *Garth* involved a breach of a trust, over which English courts of equity had exclusive jurisdiction.[148] Third, in light of Hardwicke's dicta proclaiming that all tenants are fiduciaries for their remaindermen, equitable waste necessarily entails a breach of fiduciary obligations, which serves as an independent justification for granting an accounting.[149] Unlike Hardwicke's accounting remedy for equitable waste, SEC's disgorgement remedy is a remedy for wrongdoing and is not linked to a breach of fiduciary obligations.[150] Accordingly, *Garth* does not support a disgorgement award absent a fiduciary relationship.[151]

2. *Willoughby v. Willoughby*

The only other binding precedent Cavanagh cites is *Willoughby*,[152] another one of Hardwicke's influential decisions.[153]

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[144] H. Tomas Gomez-Arostegui, *Prospective Compensation in Lieu of A Final Injunction in Patent and Copyright Cases*, 78 FORDHAM L. REV. 1661, 1731 & n.265 (2010).

[145] *Garth*, 21 Eng. Rep. at 241; 1 Dickens at 189.

[146] *See* Eichengrun, *supra* note 74, at 482.

[147] Gomez-Arostegui, *supra* note 144.

[148] John H. Langbein, *The Contractarian Basis of the Law of Trusts*, 105 YALE L.J. 625, 648 (1995) ("In England and in most leading American jurisdictions, the law of trusts had been the province of separate equity courts or equity divisions.").

[149] Eichengrun, *supra* note 74, at 482.

[150] *See supra* Part I.A (explaining components of SEC's disgorgement remedy).

[151] *See supra* notes 147–49 and accompanying text.

[152] There are two separate accounts of this case in the reporters. For a truncated version, see *Willoughby v. Willoughby*, (1756) 28 Eng. Rep. 437

In *Willoughby*, George entered into a marriage settlement with his wife, Jane, to provide her with income after his death.[154] Under the settlement, Jane was to receive an annual jointure from the land for the duration of her life, with the remainder going to any sons from the marriage.[155] To protect her jointure, the marriage settlement created a mortgage on the land in Jane's favor, and trustees held this mortgage.[156] After George's death, his and Jane's eldest son, Henry, used antiquated legal mechanisms to obtain title to the land.[157] Next, he borrowed money from Jane, and provided her with a mortgage on the land as security.[158] He then borrowed money from Jeffery Cripps, and mortgaged the land to him as security as well.[159] On the same day, Henry directed the trustees who held the original mortgage in Jane's favor to assign that mortgage to Alexander Boote as trustee for Cripps.[160] Cripps was aware of the marriage settlement when he entered into these transactions.[161]

In reasoning reminiscent of *Garth*, Hardwicke stated: "I take it to be just upon the same foot as the case of a trustee to preserve contingent remainders. If such a trustee join in a conveyance to a purchaser for a valuable consideration, and the purchaser has notice of that trust, the latter is affected with the trust . . . ."[162] Not surprisingly, Hardwicke ordered that the defendants—Henry, Cripps, and Boote—account for the profits they derived from this breach of trust.[163]

Willoughby stands for the proposition that where a purchaser of trust property has notice of the trust, he "becomes a trustee, and liable in the same manner as the person from whom he

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(Ch.); 2 Ves. Sen. 684. For a more detailed report, see *Willoughby v. Willoughby*, (1787) 99 Eng. Rep. 1366 (Ch.); 1 Term Rep. 763.

[153] 4 JAMES KENT, COMMENTARIES ON AMERICAN LAW 87 (2d ed. 1832) (recognizing *Willoughby* as the "Magna Carta" of the law of attendant terms).

[154] 99 Eng. Rep. at 1366; 1 Term Rep. at 763.

[155] *Id.*

[156] *Id.*

[157] *Id.*

[158] *Id.*

[159] 99 Eng. Rep. at 1366; 1 Term Rep. at 764.

[160] *Id.*

[161] *Id.*

[162] 99 Eng. Rep. at 1370; 1 Term Rep. at 771.

[163] 99 Eng. Rep. at 1372; 1 Term Rep. at 775.

purchased."[164] As the High Court of Chancery would have required the breaching trustee to account for profits, the purchaser-with-notice must have accounted as well.[165] Thus, *Willoughby*, like *Garth*, involved a person who wrongfully acquired trust property, thereby making him liable as though he were a trustee. An accounting for profits was the traditional remedy for breaches of trust.[166] A breach of trust is noticeably absent from *Cavanagh* and the requirements for the SEC's disgorgement remedy.[167] Thus, *Willoughby* is inapposite and does not support a finding that the SEC's disgorgement remedy has equitable ancestors.

C. Analysis of Persuasive Precedents

In addition to *Garth* and *Willoughby*, *Cavanagh* cites two early American decisions for the proposition that disgorgement is an equitable remedy: *Haldane v. Fisher*[168] and *Cadwallader v. Mason*.[169] Because a remedy is equitable under *Grupo* only if the English High Court of Chancery had the power to grant it in 1789, these cases are not binding for two reasons.[170] As these cases were decided post-1789, they temporally fail the *Grupo* standard.[171] More significantly, *Grupo* does not direct, or even permit, courts to look to the decisions of state courts when determining the propriety of a federal court's granting a particular equitable remedy.[172] The reason for this is that *Grupo* requires an analysis of the English Chancery's practices, and the decisions of the English Chancery were not binding on the states.[173] In 1821, Justice Joseph Story, a leading

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[164] 2 JARIUS WARE PERRY, A TREATISE ON THE LAW OF TRUSTS AND TRUSTEES § 828, at 517 n.4 (5th ed. 1899) (citing *Willoughby*, 99 Eng. Rep. 1366; 1 Term. Rep. 771).
[165] *See* Eichengrun, *supra* note 74, at 482.
[166] *Id.*
[167] *See supra* Part I.A.
[168] 2 U.S. (2 Dall.) 176, 1 Yeates 121 (Pa. 1792).
[169] Wythe 188 (Va. High Ct. Ch. 1793).
[170] *See* Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 332 (1999).
[171] *Id.*
[172] *See id.*
[173] Kristin A. Collins, *"A Considerable Surgical Operation": Article III, Equity, and Judge-Made Law in the Federal Courts*, 60 DUKE L.J. 249, 266–72 (2010); *see also* Fontain v. Ravenel, 58 U.S. 369, 393 (1854).

commentator in the field of early-American equity jurisprudence,[174] acknowledged that the states' equity decisions had deviated from principles of English equity to such an extent "that it would be somewhat hazardous for a lawyer at the chancery bar of Westminster to form an opinion as to the authority to give, or to deny relief."[175] Thus, even before reading *Haldane* and *Cadwallader*, a student of colonial equity jurisprudence would have reason to question *Cavanagh*'s citations to those opinions. A thorough analysis of the facts of those opinions validates this skeptical attitude.[176]

1. *Haldane v. Fisher*

Subsequent authorities have cited *Haldane* for various propositions for which it does not stand.[177] Hence, a thorough explanation of the case is warranted. Hester Duche had been receiving rents from a piece of land in Philadelphia up until her death in June 1779.[178] When she died, her husband, James Duche, became the executor of her estate.[179] Elizabeth Haldane was Hester's heir-at-law and acquired title to the profit-generating land upon Hester's death.[180] However, Elizabeth did not learn that she had acquired title to the land until 1785.[181] In 1786, Elizabeth sold the land to John Duffield, who brought a successful action for ejectment against the tenants.[182] James later died, and Elizabeth brought suit against his

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[174] DiSarro, *supra* note 64, at 62.

[175] Collins, *supra* note 173, at 268 (2010) (quoting Joseph Story, Justice, United States Supreme Court, Address Delivered Before the Members of the Suffolk Bar, at Their Anniversary, at Boston (Sept. 4, 1821), in 1 Am. Jurist 1, 22 (1829)).

[176] *See infra* Part III.D.1-2 (arguing *Haldane* and *Cadwallader* are irrelevant to a *Grupo* analysis and do not support to proposition for which *Cavanagh* cited them).

[177] Haldane involved an action for account. Haldane v. Fisher, 2 U.S. (2 Dall.) 176, 178, 1 Yeates 121 (Pa. 1792). However, subsequent authorities have incorrectly cited it as a case involving indebtiaus assumpsit. *See, e.g.*, Lowell v. Strahan, 145 Mass. 1, 6 (1887); Travellers' Ins. Co. v. Heath, 95 Pa. 333, 337 (1880); Vandenheuvel v. Storrs, 3 Conn. 203, 206–07 (1819).

[178] *Haldane*, 2 U.S. (2 Dall.) at 176.

[179] *Id.* at 177.

[180] *Id.* at 176.

[181] *Id.* at 177.

[182] *Id.*

executor for the rents received by James after Hester's death.[183] Chief Justice M'Kean thought the case was simple.[184] He acknowledged that, under the doctrine of *actio personalis moritur cum persona*,[185] Elizabeth could not maintain an action for James's trespass against his executor.[186] Thus, the only route to James's profits was an accounting against James's executor.[187] M'Kean held Elizabeth was entitled to an accounting of James's profits derived from the land.[188]

Haldane's relevance to a *Grupo* analysis is questionable. First, *Haldane*'s similarity to English equity jurisprudence in 1789 is doubtful, as the case expressly avoided the question of "whether such an action as the present, could be maintained in England."[189] Second, James, as executor of Hester's, stood in a fiduciary relation with respect to Elizabeth, Hester's heir-at-law.[190] Therefore, Elizabeth could have brought an action for an accounting against James in his capacity as executor—an action over which eighteenth-century English chancellors would have entertained jurisdiction.[191] Hence, there was a fiduciary relation between James and Elizabeth sufficient to support an action for an accounting.[192] Accordingly, this case does not support the proposition that the Chancery would have awarded a wrongdoer's profits to a claimant absent a fiduciary relationship. Hence, this case does not support *Cavanagh*'s conclusion that the SEC's disgorgement remedy is equitable.

2. *Cadwallader v. Mason*

Cadwallader is a paradigmatic example of an eighteenth-century equity decision by an American chancellor that would baffle

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[183] *Id.*
[184] *Id.* at 178 ("This does not appear to me to be a hard or difficult case.").
[185] *Actio personalis moritur cum persona* translates to "a personal action dies with the person." BLACK'S LAW DICTIONARY, app. B at 1816 (9th ed. 2009).
[186] *Haldane*, 2 U.S. (2 Dall.) at 178.
[187] *Id.*
[188] *Id.*
[189] *Id.*
[190] Since 1527, English law has held that executorships are "office[s] de trust." Maurizio Lupoi, *The New Law of San Marino on the "Affidamento Fiduciario,"* 25 TRUST L. INT'L, no. 2, 2011, at 51, 51 n.4.
[191] *See* Eichengrun, *supra* note 74, at 466.
[192] *See id.* at 469.

a contemporary English barrister. In *Cadwallader*, a mortgagee sought an accounting of a mortgagor's profits that the mortgagor had acquired while wrongfully possessing the land.[193] The mortgagee came into equity without having utilized applicable legal remedies to retain possession.[194] Chancellor George Wythe conceded that he was unable to locate a case that had granted an accounting to a mortgagee against a mortgagor for profits made while the mortgagor wrongfully possessed the land and acknowledged that earlier cases had denied such accountings.[195] Nevertheless, Wythe explicitly rejected those precedents on the grounds that legal remedies, though available, were cumbersome and held that the mortgagee was entitled to an accounting against the mortgagor for profits realized during the mortgagor's unlawful possession.[196]

As a Virginia chancellor, Wythe could disregard English practices as he saw fit.[197] Wythe did not hesitate to exercise his broad powers to do so.[198] At least by 1740, the rule in England had been established: "Where the mortgagor has been permitted to remain in possession, the mortgagee is not entitled to an account of past rents and profits."[199] The rule rested on the premise that a mortgagee had adequate legal remedies to retake possession of the land,[200] and where a plaintiff had adequate legal remedies, he could not resort to equity.[201] Hence, *Cadwallader*, by providing a mortgagee with an accounting, an equitable remedy, in this situation, flew in the face of

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[193] Cadwallader v. Mason, Wythe 188, 188 (Va. High Ct. Ch. 1793).
[194] *Id.*
[195] *Id.* Chancellor Wythe discussed precedents but failed to provide any citations.
[196] *Id.*
[197] *See* sources cited *supra* note 173.
[198] *Cadwallader*, 1 Wythe at 188.
[199] HENRY WILMOT SEATON, FORMS OF DECREES IN EQUITY AND OF ORDERS CONNECTED WITH THEM *141 (1831) (citing *Ex parte* Wilson, (1813) 35 Eng. Rep. 315 (Ch.) 315; 2 Ves. & Beames 252, 252; 1 Rose 444, 444; Drummond v. Duke of St. Albans, (1800) 31 Eng. Rep. 667 (Ch.) 670; 5 Ves. Jun. 433, 438; Colman v. Duke of St. Albans, (1796) 30 Eng. Rep. 874 (Ch.) 877; 3 Ves. Jun. 25, 32; Mead v. Lord Orrery, (1745) 26 Eng. Rep. 937 (Ch.) 941; 3 Atk. 235, 244; Higgins v. York Buildings Company, (1740) 26 Eng. Rep. 467 (Ch.) 467; 2 Atk. 107, 107). Editor's Note: Author Henry Wilmot Seaton is more frequently published as Henry Wilmot Seton.
[200] *Mead*, 26 Eng. Rep. at 941; 3 Atk. at 244.
[201] Thomas O. Main, *Traditional Equity and Contemporary Procedure*, 78 WASH. L. REV. 429, 451 (2003).

decisions of the English chancery. Hence, *Cadwallader* rejected English practices and is consequently irrelevant to a *Grupo* analysis, which requires an analysis of those very practices.[202] *Cadwallader*, then, does not support the contention that the SEC's disgorgement remedy is equitable.[203]

IV. The SEC's Disgorgement Remedy Is Not an Equitable Remedy

The foregoing analysis demonstrates that *Cavanagh* fell short. The authorities cited in *Cavanagh* show that the High Court of Chancery ordered disgorgement only in cases involving fiduciary obligations.[204] The SEC's disgorgement remedy is not so limited.[205] Therefore, *Cavanagh* failed to demonstrate that a remedy resembling the SEC's disgorgement remedy was available in the High Court of Chancery in 1789.[206]

As *Cavanagh* failed in its mission, one might conclude that the future looks bleak for the continued viability of the SEC's disgorgement remedy. Such a conclusion is overly optimistic, as the remedy's future is hopeless. Professor Sarah Worthington analyzed English law seven years before the Second Circuit decided *Cavanagh* and concluded that "disgorgement . . . is available only when the defendant has breached an obligation of 'good faith or

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[202] Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999).

[203] *See id.*

[204] *See supra* Part III.C.

[205] *See supra* Part I.A.

[206] For an example of an accurate *Grupo* analysis involving the concept of disgorgement, see *Newby v. Enron Corp.*, 188 F. Supp. 2d 684, 702–07 (S.D. Tex. 2002) (Rosenthal, J.). In *Newby*, Judge Rosenthal concluded that disgorgement was available to claimants appearing before the High Court of Chancery in 1789. *Id.* at 702. Unlike the conclusion in *Cavanagh*, the conclusion in *Newby* rested its conclusion on indisputable premises. First, in *Newby*, there was a breach of a fiduciary duty. *Id.* Second, this breach would have permitted the High Court of Chancery to grant an accounting or a constructive trust. *Id.* at 703–07. Accordingly, an eighteenth-century claimant could have received disgorgement as a byproduct of either of those remedies *Id.* at 702. Though its analysis is accurate, *Newby* does not answer the question of whether the remedy of disgorgement was available in the chancery.

loyalty.'"[207] Therefore, the SEC's disgorgement remedy cannot be an equitable remedy under *Grupo*.[208] Hence, federal courts are powerless to order disgorgement in SEC enforcement proceedings.[209]

V. Implications

Given the conclusion that the federal courts are powerless to order disgorgement in SEC enforcement proceedings[210] and the SEC's disgorgement remedy's deterrent purposes,[211] the conclusion that the SEC will be powerless to deter violations of the securities acts seems inescapable. Considering that disgorgement delivered $7.9 billion to the SEC from 2009 to 2012, whereas courts awarded the SEC $3.273 billion in penalties during that period, only seems to strengthen the certainty of this conclusion.[212] This seemingly inevitable conclusion, however, is far from preordained.

First, the SEC's disgorgement remedy is not *sufficient* to deter violations of the securities acts. Though "Congress has never explicitly included disgorgement among the remedies the SEC can seek in federal court,"[213] it recognized that the "authority to seek or impose substantial money penalties, in addition to disgorgement of profits, is necessary for the deterrence of securities law violations."[214] If disgorgement were the only remedy available for securities act violations, violators "would run no risk of liability . . . beyond that of returning what they wrongfully obtained."[215] Recent

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[207] Worthington, *supra* note 9.
[208] *See Grupo*, 527 U.S. at 318–19.
[209] *See supra* Part I.C. The SEC could choose to limit the application of its disgorgement remedy to breaches of fiduciary obligations. SEC v. Lipson, 278 F.3d 656, 662–63 (7th Cir. 2002) (Posner, J.) (recognizing that SEC's disgorgement remedy is equitable when linked to breach of fiduciary duty).
[210] *See supra* Part IV.
[211] *See supra* Part I.A.
[212] Ryan, *supra* note 4, at 1 n.1.
[213] *Id.* at 2.
[214] *See* H.R. REP. NO. 101-616, at 1384 (1990), *quoted in* Official Comm. of Unsecured Creditors of WorldCom, Inc. v. SEC, 467 F.3d 73, 81 (2d Cir. 2006) (Sotomayor, J.).
[215] RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 51 cmt. k, at 233 (2011) (quoting Ward v. Taggart, 336 P.2d 534, 538 (Cal. 1959) (Traynor, J.)).

scholarship applying game theory to disgorgement only confirms this painfully obvious reality.[216]

Second, the SEC's disgorgement remedy is not *necessary* to deter violations of the securities acts.[217] The SEC has two options that can render violations unprofitable without resorting to the equitable jurisdiction of the federal courts. The SEC has statutory authority to require disgorgement in an administrative proceeding.[218] Administrative disgorgement has not been the SEC's preferred method of depriving wrongdoers of their ill-gotten gains,[219] presumably because injunctions are unavailable in administrative proceedings.[220] Though inconvenient, the SEC may seek an injunction in federal court and disgorgement in an administrative proceeding.[221] To avoid this inconvenience while functionally achieving disgorgement, "[t]he SEC can . . . ask federal courts, when imposing statutory penalties against a defendant, to calculate that penalty as an amount equal to 'the gross amount of pecuniary gain to [the] defendant as a result of the violation.'"[222]

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[216] *Cf.* Elias Pete George, *Using Game Theory and Contractarianism to Reform Corporate Governance: Why Shareholders Should Seek Disincentive Schemes in Executive Compensation Plans*, 42 GOLDEN GATE U. L. REV. 349, 379–80 (2012) (finding that disgorgement is insufficient to deter wrongdoing in the corporate governance context because the probability of apprehension is low). George's findings are equally applicable to violations of the securities laws because the certainty of prosecution is relatively low. *See* Jayne W. Barnard, *Securities Fraud, Recidivism, and Deterrence*, 113 PENN ST. L. REV. 189, 220 (2008) ("Retail securities fraud is said to be a 'low-risk crime' (for its perpetrators) because it is so difficult to detect and prosecute.").

[217] Ryan, *supra* note 4, at 3 ("Today, however, there are no compelling reasons to stretch disgorgement beyond its limits. In recent decades, Congress has granted the SEC and the courts a vast array of options to impose harsh monetary and other sanctions against wrongdoers in virtually all kinds of securities cases, regardless of whether disgorgement is available as an additional remedy.").

[218] *Id.* at 13 (citing 15 U.S.C. §§ 77h-1(e), 78u-2(e)-3(e) (2012)).

[219] Ryan, *supra* note 4, at 11 n.63.

[220] *See How Investigations Work*, SEC, http://sec.gov/News/Article/Detail/Article/1356125787012#.UzhAifldVIF (last visited Apr. 16, 2014).

[221] *Id.*

[222] *Id.* (second alteration in original) (quoting 15 U.S.C. § 78u(d)(3)(B)); *see also* Official Comm. of Unsecured Creditors of WorldCom, Inc. v. SEC, 467 F.3d 73, 82 (2d Cir. 2006) ("The Remedies Act permits the SEC, in addition to seeking disgorgement of ill-gotten profits, to seek civil penalties

VI. Conclusion

Cavanagh's holding that the SEC's disgorgement remedy is an equitable remedy under *Grupo* is the fallout of decades of neglect of equitable jurisprudence in American law schools[223] and years of relaxed judicial scrutiny of SEC arguments for disgorgement in the federal courts.[224] A straightforward application of the *Grupo* standard reveals that the SEC's disgorgement remedy is not an equitable remedy.[225] Therefore, a federal court may not order the SEC's disgorgement remedy pursuant to the court's equitable powers.[226]

Some might argue that the conclusion that disgorgement is not available as a remedy in the SEC enforcement context may "frustrate the purposes of the regulatory scheme."[227] However, these concerns are overblown, as the SEC's disgorgement remedy is neither necessary nor sufficient for deterrence.[228] Moreover, the undesirability of a conclusion cannot affect its truth. Because the equity jurisdiction of the federal courts cannot support a disgorgement order in the SEC enforcement context, the SEC must look elsewhere for support if it continues to seek disgorgement.[229]

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of generally up to the amount of the gross pecuniary gain from the securities fraud.").

[223] *See* Andrew Kull, *Common-Law Restitution and the Madoff Liquidation*, 92 B.U. L. REV. 939, 966 (2012) (describing "the gradual process by which the elimination of a separate equity jurisdiction would lead first to the disappearance of equity from the law school curriculum, then to an ebb tide in professional awareness, as lawyers who had never learned these rules gradually took over from those who had").

[224] *See* Ryan, *supra* note 4, at 1 (acknowledging that courts typically begin their disgorgement analyses by "assuming as axiomatic" that disgorgement is an equitable remedy).

[225] *See supra* Part III.

[226] *See* Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308, 318–19 (1999).

[227] *See* Roach, *supra* note 4, at 75 n.253 (quoting CFTC v. Am. Metals Exch. Corp., 991 F.2d 71, 76 n.9 (3d Cir. 1993)).

[228] *See supra* Part V.

[229] Professor Barbara Black has suggested that the Securities Enforcement Remedies and Penny Stock Reform Act of 1990's "legislative history makes clear that Congress assumed that disgorgement was already available as a remedy in judicial proceedings." Black, *supra* note 51, at 321 (citing S. REP. NO. 101-337, at 8 (1990)). In response, Ryan has argued that "the fact that Congress has explicitly granted the SEC, an independent *executive* branch agency, the power to order disgorgement administratively as part of

its law enforcement functions, weighs heavily against any presumption that disgorgement is a remedy in equity." Ryan, *supra* note 4, at 2 n.12. Whether either of these arguments is persuasive is beyond the scope of this note.