

11th Circuit Rules Against SEC Penny-Stock Ban

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In a 2-1 opinion issued on February 14, 2024, an Eleventh Circuit panel partially reversed a lower court ruling that would have barred a defendant from participating in future penny-stock offerings. The majority found it was an abuse of discretion for the district court to impose a permanent bar where the defendant voluntarily ceased the unlawful activity and had not already exhibited his unlikeliness to comply with the law going forward.

As part of a wider crackdown on “toxic lending” in microcap markets, the SEC accused Ibrahim Almagarby of flooding the markets with converted penny-stock debt without first registering as a dealer. The district court ordered Almagarby to disgorge \$885,126.30 in total net profits and \$182,150.69 in prejudgment interest, for a total of \$1,067,276.99. It also permanently enjoined him from selling unregistered securities and from any future participation in penny-stock offerings. In contesting the SEC’s request for a permanent injunction, Almagarby argued that because he had voluntarily ceased the conduct at issue, there was no risk of future misconduct. *SEC v. Almagarby, et. al*, 479 F.Supp.3d 1266, 1273–74 (2020). The district court rejected Almagarby’s argument, citing cases by the Eleventh^[1] and Second Circuits^[2] for the proposition that voluntary cessation is neither dispositive nor preclusive of an injunction enjoining the unlawful activity “because, absent an injunction, there is little to stop Defendants from resuming their unlawful activity.” *Id.* at 1274.

In the majority opinion, the Eleventh Circuit held that the district court did not abuse its discretion in permanently enjoining Almagarby from transacting in securities without registering as a dealer or associating with a registered broker-dealer. However, the Eleventh Circuit disagreed with the district court with respect to the imposition of the penny-stock bar, which prohibited both unlawful and lawful penny-stock transactions. The Eleventh Circuit majority concluded that the Eleventh Circuit has not “to the best of our knowledge, approved of enjoining a defendant from participating in otherwise lawful behavior when that defendant had not already exhibited his unlikeliness to comply with the law going forward — either through prior adjudicated securities violations or through conduct bordering on (if not amounting to) criminal.”

Chief Judge William Pryor issued a partial dissent, disagreeing that the penny-stock bar would have been an abuse of discretion where “voluntary cessation is the only impediment to Almagarby’s recidivism.” However, the majority’s reasoning may have created an opening in Eleventh Circuit jurisprudence for defendants contesting penny-stock bars. Similarly, a defendant could argue against other types of bars sought by the SEC, including those against serving as an officer or director of a public company.

The case is *SEC v. Almagarby et al.*, case number 21-13755, in the U.S. Court of Appeals for the Eleventh Circuit.

[1] See, e.g., *SEC v. Carriba Air, Inc.*, 681 F.2d 1318, 1322 (11th Cir. 1982) (this circuit has stated that assertions on the part of the defendant that he would cease his wrongful conduct are by no means dispositive.). See also *SEC v. Ginsburg*, 362 F.3d 1292, 1305 (11th Cir. 2004).

[2] *SEC v. Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1101 (2d Cir. 1972).

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