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The Trump Administration's Move Against SEC Judges

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The Trump administration's new position on the constitutionality of the U.S. Securities and Exchange Commission's administrative law judges is more far-reaching and potentially consequential than is generally understood. On Nov. 29, the U.S. solicitor general, who speaks for the federal government before the U.S. Supreme Court, filed a brief urging the court to review the case of Raymond J. Lucia v. SEC. Lucia is seeking to overturn an SEC fine and professional bar based on the argument that the ALJ in his case was not properly appointed. In an about-face, the solicitor general now agrees with Lucia that the SEC's ALJs are "officers" subject to the appointments clause of the Constitution, not mere employees, as the SEC had argued.

What has received less attention is that the administration's brief urges the court to go beyond the requirements for *appointing* ALJs (an issue that has divided many federal judges and is ripe for Supreme Court review) and consider also the restrictions on *removing* them from office — an issue that was not passed on below and on which there is no judicial disagreement. Nevertheless, citing the Supreme Court's 2010 decision in Free Enterprise Fund v. Public Company Accounting Oversight Board, the solicitor general all but states that the traditional system of tenure protections for ALJs is unconstitutional — even though no court has adopted that view.

Were the Supreme Court to do so, it could undermine protections not just for ALJs at the SEC and other agencies, but also for senior civil servants in a range of federal agencies, who by design are insulated from political and other forms of reprisal. The administration's position is likely a product of the "unitary executive" theory popular among some conservative theorists, which holds that the president should have relatively unfettered control of executive branch agencies, and is skeptical of restrictions on his power to remove officials in them.

Historically, the SEC's ALJs were hired through a competitive civil service system, without involvement from the SEC's politically appointed chairman and other commissioners. Lucia (like others in recent years who have been charged in the SEC's administrative tribunal) has argued that this hiring practice violated the appointments clause.

The appointments clause is designed to preserve political accountability and the separation of powers among the three branches of government. It requires the government's senior-most "officers" to be

presidentially appointed and Senate-confirmed, and provides that certain other officials — referred to as "inferior officers" — can be appointed by the head of an executive branch agency if Congress allows.[1] The term "inferior officers" can be confusing: their stature is high relative to most federal workers, who are considered mere employees and are outside the scope of the appointments clause altogether. Lucia argues that the SEC's ALJs have enough authority and responsibility to be considered "inferior officers." If so, the argument goes, then the proceedings involving the ALJs were void because the ALJs were not actually appointed by the commissioners atop the SEC.

Whether the SEC's ALJs are subject to the appointments clause has sharply divided many judges of the federal courts of appeals. In August of 2016, a D.C. Circuit panel held in Lucia's case that the ALJs are mere employees.[2] Four months later, in David F. Bandimere v. SEC, a Tenth Circuit panel, by a 2-1 vote, reached the opposite conclusion — that the ALJs are "inferior officers" subject to the appointments clause.[3]

Until the Lucia filing, the Trump administration had maintained the position of the Obama administration that the ALJs are not subject to the appointments clause.[4] But the solicitor general's new brief, which was not signed by SEC lawyers — presumably they objected — abandons the SEC's historic position, and agrees that the SEC's ALJs have to be directly appointed by the SEC's commissioners. (With Lucia and the government now aligned, the Supreme Court will have to appoint amicus counsel to defend the judgment below.)

On one level, this arcane issue is likely to be relatively inconsequential for future cases. On Nov. 30, in response to the solicitor general filing the day before, the SEC's commissioners formally ratified the appointment of the ALJs. (This move does not impact those, like Lucia, whose cases have concluded within the SEC.[5]) The ratification, and the prospect of future commission-level approval of ALJ hires, arguably weakens the ALJs' appearance of independence, but only slightly.

The larger issue is that the solicitor general's brief encourages the court to go out of its way to "reframe the question presented or add a question presented to address the issue of removal."[6] In so doing, the administration is taking aim at one of the foundations of the administrative state. ALJs have been around since the Administrative Procedure Act of 1946 (APA). In order to remove an ALJ, a proceeding must be instituted before a separate agency known as the Merit Systems Protection Board, and there must be "cause," meaning a showing of misconduct. This congressionally-established framework insulates ALJs from at-will removal, ensuring that they can perform their fact-finding function with independence, even as their decisions are ultimately reviewable by senior agency officials who are closer to the political process. (Put differently, Congress did not want ALJs to worry that they could lose their jobs if they rule against the agency.) Similar protections exist for many career civil servants whose independence and expertise is valued.

The 2010 Free Enterprise Fund decision relied on by the solicitor general concerned the constitutionality of the Public Company Accounting Oversight Board. The board, created by the 2002 Sarbanes-Oxley legislation, regulates auditors of public companies. The board is supervised by the SEC, and its members are selected by the SEC's commissioners. The Supreme Court held, by a 5-4 vote along familiar ideological lines, that the framework for removing members of the board encroached too much on presidential prerogative. In particular, the accounting board members were "officers" insulated from the president's removal power by two layers of "only for cause" protection. The board members by statute were removable only for cause, not at the will of the SEC commissioners, and the SEC commissioners are assumed to be removable only for cause, not at the will of the president. Chief Justice John G. Roberts Jr.'s opinion for the court held that the board members must be removable at the will of the SEC

commissioners.

The ALJs at the SEC and other agencies also enjoy at least two layers of protection against being fired at the will of the president — in that both the ALJs and the MSPB enjoy "only for cause" protection.[7] However, the chief justice added a footnote to his Free Enterprise Fund opinion to make clear that the court was not speaking to the ALJ system. He did so in part because it was not clear whether ALJs are "inferior officers" and in part because they often "perform adjudicative rather than enforcement or policymaking functions."[8] The first of these grounds may not be available for much longer, depending on what happens in the Lucia case. But the second ground is key: As Justice Stephen G. Breyer explained in dissent, a long-standing tradition protects the "personal independence" of officials who adjudicate disputes by ensuring that they cannot be fired at will.[9]

The solicitor general's Lucia brief challenges that tradition. It calls on the Supreme Court to take the unusual step of addressing an issue not passed on below, and questions "whether the statutory restrictions on [SEC ALJs'] removal are consistent with separation-of-powers principles."[10] If the Supreme Court agrees to reach this issue, presumably the administration would argue for the ALJs to be removable at the will of the officials atop their agencies, or for another change that weakens their independence — potentially making SEC enforcement proceedings, and other proceedings across the government, less fair. As two judges in the Tenth Circuit pointed out in Bandimere's case, "ALJ insulation from agency control and coercion was a primary goal of the APA."[11]

Also significant is that decades-old protections for senior civil servants in many agencies — the so-called Senior Executive Service — could be impaired if the Supreme Court follows the administration's lead. This is a foreseeable consequence of extending the Free Enterprise decision that Justice Breyer warned of in his dissent.[12] Most, if not all, SES members are arguably "inferior officers," and at least in independent agencies like the SEC, they are insulated by two layers of "only-for-cause" protection. However, as with the ALJs, the Free Enterprise Fund majority did not opine on the status of civil servants in independent agencies.[13]

The Supreme Court observed in the seminal 1935 case of Humphrey's Executor v. United States that "one who holds his office only during the pleasure of another cannot be depended upon to maintain an attitude of independence against the latter's will."[14] The court — which could grant certiorari next month — should decline the administration's invitation to reach the removal issue, and should preserve the traditions of independence and tenure for ALJs and the civil service.

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[1] The clause reads in relevant part as follows: "The Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." U.S. Const. Art. 2 § 2 cl. 2.

[2] Raymond J. Lucia Cos. v. SEC, 832 F.3d 277 (D.C. Cir. 2016).

[3] Bandimere v. SEC, 844 F.3d 1168 (10th Cir. 2016). On Feb. 16, 2017, the full D.C. Circuit agreed to review Lucia's case en banc, but on June 26, 2017, the court, with Chief Judge Merrick Garland recused, split 5-5, which by operation of the D.C. Circuit's rules automatically affirmed the panel's decision. Raymond J. Lucia Co., 868 F.3d 1021 (D.C. Cir. 2017); D.C. Cir. R. 35(d). Meanwhile, on March 13, 2017, the SEC asked the full Tenth Circuit to rehear the Bandimere case en banc. On May 3, 2017, the court declined to do so by a 9-2 vote. Bandimere v. SEC, 855 F.3d 1128 (10th Cir. 2017).

[4] The SEC's petition for rehearing in the Bandimere case — arguing that the ALJs are mere employees — was authorized by the new administration's solicitor general's office, following deliberation and consultation within the government. See Unopposed Motion for Extension of Time, Bandimere v. SEC, No. 15-9586 (10th Cir. Jan. 31, 2017).

[5] Some commentators have questioned whether the Supreme Court would or could accept the case given that the SEC has probably mooted the issue on a going-forward basis. But the issue is not moot as to Lucia himself — he is currently subject to SEC sanctions. That suffices for an Article III "case or controversy." Also, the SEC's ratification is not before the Supreme Court.

[6] Br. for Respondent, Lucia v. SEC, No. 17-130, at 26 (U.S. Nov. 29, 2017) ("SG brief").

[7] See 5 U.S.C. §§ 1202(d), 7521(a).

[8] 561 U.S. 477, 507 n.10.

[9] 561 U.S. at 530.

[10] SG brief, at 20.

[11] 855 F.3d at 1131 (Lucero, J., dissenting from denial of rehearing en banc).

[12] 561 U.S. at 540-42.

[13] 561 U.S. at 506-08.

[14] 295 U.S. 602, 629 (1935).