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SEC's Appointments Clause Dilemma Gets Worse

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On January 12, the Supreme Court granted certiorari in *SEC v. Lucia*, which will decide whether the Securities and Exchange Commission's (SEC) administrative law judges (ALJs) are appointed consistently with the Constitution's Appointments Clause. Unfortunately for the SEC, at least right now, no one is arguing that the SEC's process is constitutional. What the Court does in this case will potentially upend not only the SEC's ALJ process but other agencies' as well. As this blog has explained here and here, there is a clear circuit split on whether the way that the SEC hires its ALJs comports with the Appointments Clause. The Appointments Clause provides:

> [The President] shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the Supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but 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.

There is no doubt that the SEC's five ALJs are not treated as "inferior officers" that are appointed pursuant to the Appointments Clause because they are not appointed by the President, a court of law, or the head of a department (even if the SEC was considered a department). Instead, they are hired through the government's civil service process overseen by the Office of Personnel Management just like other federal government employees. In the D.C. and Tenth Circuits, respondents in SEC administrative enforcement actions before ALJs challenged the constitutionality of the administrative forum as violating the Appointments Clause. The outcome of those two cases has created a circuit split, which the Supreme Court decided Friday to address. First, the D.C. Circuit, in *Raymond J. Lucia Companies, Inc. v. SEC*, concluded that SEC ALJs need not be appointed pursuant to the Appointments Clause because they were simply employees rather than "inferior officers." According to its own precedent, whether a government official was an employee or an "inferior officer" depended on three factors:

- the significance of the matters resolved by the official;
- the discretion the official exercised in reaching his or her decisions; and
- the finality of those decisions.

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The Court concluded that SEC ALJs were not "inferior officers" because they did not render final decisions on behalf of the Commission (even though a substantial majority of ALJ decisions are affirmed, often without opinion). The D.C. Circuit later re-heard the panel's decision, and then split evenly 5-5 (with Chief Judge Merrick Garland not participating) in February 2017, thus leaving the panel's decision in place. The Tenth Circuit, on the other hand, in a 2-1 decision, reached the opposite conclusion in *Bandimere v. SEC*. The *Bandimere* court concluded that an SEC ALJ was an "inferior officer" who must be appointed consistent with the Appointments Clause. In doing so, the Court relied heavily on *Freytag v. Comm'r of Internal Revenue*, in which the Supreme Court concluded that inferior officers were those:

- whose positions were "established by law";
- whose duties, salary and means of appointment were specified by statute; and
- who exercised significant discretion in carrying out important functions.

Using those criteria, the Tenth Circuit majority had little trouble concluding that SEC ALJs were "inferior officers." Under the Administrative Procedures Act (APA), SEC ALJs (and other ALJs) preside over and take evidence at administrative hearings, determine the scope and form of evidence, subpoena parties, examine witnesses, prepare initial decisions with factual findings and legal conclusions, and rule on both dispositive and procedural motions. As a result, the court concluded that SEC ALJs exercised significant discretion in carrying out important functions. The majority also noted that the Commission allows an ALJ's initial decision to become final in approximately 90 percent of cases, which means that, most of the time, an ALJ decision is effectively final. Because SEC ALJs were "inferior officers" who had not been appointed pursuant to the Appointments Clause, the majority set aside the ALJ and the SEC's decision. The SEC, of course, sought rehearing *en banc*, which a majority of the Tenth Circuit denied in May of 2017. Perhaps of relevance, Judge Gorsuch was on the Court when the SEC filed its petition for rehearing *en banc* but ultimately did not participate in the vote to deny rehearing *en banc*. This is when things got interesting. As expected, Lucia petitioned for certiorari. Then, in September 2017, the SEC half-heartedly petitioned for certiorari in *Bandimere*. Whereas the SEC had previously argued in the Tenth Circuit that the panel decision was wrong, in the Supreme Court (with the Solicitor General's office doing the principal drafting), the SEC argued that the Supreme Court should address the Appointments Clause issue for reasons it would explain more in its forthcoming response to the *Lucia* petition. The SEC also said that: (1) *Lucia* was probably a better vehicle to decide the issue (because now-Justice Gorsuch had been on the Tenth Circuit when the petition for rehearing was filed though he did not vote on it); and (2) if the Supreme Court denied the *Lucia* petition, it should deny the SEC's petition in *Bandimere* – though that would obviously leave in place the decision that SEC ALJs are hired in violation of the Appointments Clause. In October, the SEC filed a highly unusual response to the *Lucia* petition. First, contrary to all the prior briefing in *Bandimere* and *Lucia*, no SEC attorneys were on the brief. It was authored exclusively by the Solicitor General's office. Second, it completely abandoned the SEC's prior position and flatly conceded that SEC ALJs are officers of the United States, not employees. On behalf of the government (though presumably not the SEC), the Solicitor General agreed that the D.C. Circuit was wrong, the petition for certiorari should be granted and suggested that

the Court “appoint an amicus curiae to defend the judgment below.” Then, and finally, and perhaps most ominously, the Solicitor General raised two additional issues. First, the Solicitor General agreed with the *Bandimere* dissent that this case has implications for ALJs in numerous other federal agencies who conduct adversarial administrative proceedings. The Solicitor General cited the FDIC, the Department of Agriculture, the CFPB, the NLRB, the FERC, and the EPA as examples of other agencies whose ALJs might be appointed or hired in violation of the Appointments Clause. And second, the Solicitor General, injected another reason why SEC ALJs might currently be constitutionally defective – because they cannot be removed by the President, relying on the *Free Enterprise* case. Since all parties submitting briefs supported granting certiorari, the Court’s decision to grant certiorari perhaps comes as no surprise. What happens from here though is anyone’s guess. Since the Solicitor General now essentially is another advocate for Lucia, presumably someone else will need to argue the SEC’s position. Most likely this will be the SEC itself. This will not be the first time this term an agency and the Solicitor General have argued opposite sides of a case before the Supreme Court. The Solicitor General and the NLRB were at odds before the Court in October. But, most importantly, this case is likely to have enormous repercussions which – if the Solicitor General is right – may potentially reshape numerous federal agencies, not simply the SEC.