

PUBLICATIONS

The Supreme Court Considers The Fate of SEC ALJs

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The fate of SEC Administrative Law Judges (“ALJ”) – and perhaps those at other federal agencies – hung in the balance as oral argument was held before the Supreme Court on Monday, April 23, 2018. The question being considered is whether the ALJs held their positions in contravention of the Constitution’s Appointments Clause. In *Raymond J. Lucia v. SEC*, No. 17-130 repeated questions from the Justices probed the positions of the advocates, reflecting a skepticism of claims by each sides that the Court’s prior decisions supported the rule of decision each advocated. During the arguments the Justices as times stated they were unclear as to the proper test to be applied. Concern was repeatedly expressed regarding the impact of the decision on the federal government.

The question being debated centered on the Appointments Clause of the Constitution and whether SEC ALJs are Officers within the meaning of the Clause. The parties agree that the Clause creates three categories of federal civil servants: Principal Officers, Inferior Officers and employees. Principal Officers are appointed by the President with the advice and consent of the Senate; Inferior Officers (usually referred to as Officers) can be appointed under law by the President, a department head or an agency; employees can simply be hired. While SEC ALJs traditionally were viewed as employees when *Lucia* reached the Supreme Court after the D.C. Circuit rejected challenges to that practice, the agency and Solicitor General switched sides, adopting Petitioner’s view that they are Officers. The SEC offered a ratification process to try and correct the error confessed.

Briefs for each of the parties – Petitioner, Solicitor General and Court appointed *Amicus* who defended the decision below – all discussed the Court’s prior decisions at length (summarized and analyzed here). While each side adopted different views of what the

Clause required to be an Officer, each claimed its view was consistent with the Court's jurisprudence. The arguments did not seem to yield any clear consensus on the appropriate resolution of the dispute.

Petitioners

Petitioner, began by stating the rule he advocated: "SEC ALJs have been invested with the sovereign power to preside over formal adjudications. They are officers under all of this Court's precedents, particularly Freytag [*Freytag v. Comm'r* , 501 U.S. 868 (1991)] and Edmond [*Edmond v. U.S.*, 520 U.S. 651 (1997)], and any textually and historically accurate construction of the Appointments Clause." In exercising that authority under the tutelage of the SEC, those ALJs have "independence in their decisional functions, their hearing functions, and their evidentiary functions." And, the decision of the ALJ is final unless the agency decides to review it.

Justice Kennedy raised one of the points that would reoccur throughout the arguments - the impact of the Court's decision on other agencies: "[I]f we follow your theory of the case and – and you prevail, what effect, if any will that have on ALJs in other agencies, Social Security ALJs?" Petitioner noted that this case is limited to adversarial proceedings subject to Sections 556 and 557 of the Administrative Procedure Act ("APA"): "There are approximately 150 ALJs who fit that definition, which is not Social Security ALJs, by the way, in the federal government, in 25 agencies." Indeed, the APA provides that "an on-the record adjudication . . . can be done by three people only: The agency, a member of the agency, or an ALJ. And words are known by the company they keep. These are all officers."

Justice Kagan turned the discussion to the question of Petitioner's overall position which she termed "odd" since he claimed to have suffered through a bias proceedings but now wants to correct that by making the ALJs directly accountable to the agency under the Appointments Clause: "See, there's something that strikes me as – as a little bit odd about this argument because . . . if we just take a step back a little bit. I mean, you have some real complaints about this process and how it happened and the bias that you think the ALJ showed. And if that's a problem, it's a hard context in which to think that the solution to the problem is . . . the greater political accountability that comes from the Appointments Clause" and having the ALJs directly accountable to the agency.

Petitioner responded by returning to the APA, noting that the statute gives the characteristics of an Officer as detailed in their brief. Justice Kennedy stepped in, however, stating "So then you're saying assume, as Justice Kagan's question indicates, that it's important to the perception of justice that the adjudicator be independent. Which way does that cut as to your argument?" As time expired, Petitioner responded that "it's important for regulated entities, the Commission, the judges, and the courts that review their decisions to know that they are structurally independent, that they are structurally dependent even if they have statutory decisional independence."

Solicitor General

The Solicitor began by summarizing its position on the critical question regarding the test for determining who is an Officer within the meaning of the Clause: "Under Buckley [*Buckley v. Valeo*, 424 U.S. 1 (1976)] and Freytag, a constitutional officer occupies a continuing position that's been vested by law with significant discretion to do one of two things: Either to bind the government or third-parties on important matters or to undertake other important sovereign functions. Here, the Commission's ALJs have been vested by statute with both powers. They adjudicate disputes that impose liability . . . and they can and do issue binding decisions."

Justice Breyer then began a series of questions on issues ranging from whether ALJ's are protected from dismissal if they decide a case in a manner that does not conform to agency policy to what the impact of adopting Petitioner's proposed rule would be on the civil

service while stating that he is unclear how to decide the case. At one point, for example, the Justice stated: “And I think frankly, I don’t know how do decide this case for the following reason: I don’t think it would make much difference but for the decision in the PCAOB case, *Free Enterprise [Free Enter. Fund v. PCAOB]*, 561 U.S. 477 (2010)]. When I read that decision and combine it with this, then I think if I adopt your approach, good-bye to the merit civil service at the higher levels and good-bye to independence of ALJs . . . So how do I decide this case?”

After discussing the Justice’s dissent in *Free Enterprise* the Solicitor noted: “I think the way to decide this case. . . I think what you’d say is Freytag sets up a two-part test for when you’re an officer of the United States. ALJs satisfy both. So you don’t even need to decide whether one or the other is sufficient or necessary.”

Subsequently, Justice Kennedy returned to the issue of the perception of fairness: “Assume that the perception and fact of fairness and – impartiality are enhanced by independence. How does that factor into what you’re arguing, and is it a proper consideration for us in this case?” The Solicitor noted that this is a proper consideration, stating that fairness was a key issue when the APA was enacted. Continuing he stated that “The idea behind the Appointments Clause is you’ve got to have a clear line of accountability. And this Court said in Freytag and *Free Enterprise*, when you diffuse the appointment power, you diffuse accountability.”

As the Solicitor’s time came to an end, Justice Gorsuch posed the first question about remedies: “What is the effect of the SEC’s remedial order purporting to ratify the appointment of the . . . ALJs?” The Solicitor allowed that it is consistent with prior decisions on the question in contrast to Petitioner’s contention that the SEC’s approach “repeats the problem.”

Court appointed Amicus:

Amicus began with a reiteration of his test for determining who is an Officer within the meaning of the Clause: “[A]n officer of the United States is someone with the power to bind the government or private parties in the name of his own office. In contrast, someone whose acts have no binding effect without the sanction of an officer is not himself an officer of the United States.”

Chief Justice Roberts immediately turned to the Court’s decision in *Frytag* -- the Court held that Special Trial Judges at the Tax Court who could in some instances enter a final decision but not in others were Officers – and how it fit into the proposed test: “If I were trying to figure out who an officer is, I think I might have started with Freytag. And your test that you just proposed doesn’t seem similar to what Freytag talked about . . .” *Amicus* responded by point to the fact that the Special Trial Judges in that case had the power to hold a person in contempt, authority which is consistent with the proposed test, although he allowed that Freytag has two branches of which this is only one. Justice Kagan followed-up, noting that “it’s hard to think . . . that Frytag really thought that that as all important.”

Amicus responded by agreeing that “you could read Freytag broadly, obviously, much more broadly than the rule we’re proposing, but you don’t have to read it that way. I’m not making a claim about what was in the Court’s mind. . .” In the end however the judges in that case have “the power to bind” which is crucial.

Justice Breyer then returned to the question of other agencies and statutory schemes: “The problem I have with this, the whole thing, is I have no idea of what the nature of jobs are throughout the civil service. . . I don’t know that anyone in this case has methodically gone through civil service positions to tell me whether or not, if we decide one way or the other and on the theory, we are driving wedges of dependence into what was to be since Chester Alan Arthur a merit-based civil service.” *Amicus* agreed: “I completely agree with you, Justice Breyer, that that is a concern, which is why our test doesn’t turn on importance [of the functions performed].”

The Chief Justice then returned to the question of the Court’s prior precedents: “Counsel . . . [Petitioner] said in his reply brief, ‘This

Court has never held that an adjudicatory official is not an officer.' Do you agree with that?" *Amicus* responded "Yes, but an adjudicatory official is somebody that gets to decide a case . . . to bind the parties at the end of the day . . ." which is key to his proposed rule.

Later the Chief Justice turned to the question of the accountability of the Officer, noting: "One of the principles that caused the drafters to give the authority to appoint officers to the President was the important one of accountability." *Amicus* responded: "Exactly. . . I think the Commission [SEC] is going to be held 100 percent accountable for every single decision. . ." which again is one of the predicates for his proffered rule.

Finally, Justice Kagan queried the source of *Amicus*' proposed rule while allowing that she liked it. *Amicus* noted that it traced in part to an early state court decision in 1822 and "the second part of our test, which asks whether somebody's authorized to act in the name of their own office or only in the name of somebody else's office, just reflects that principle, which I think is, as we've talked about, ubiquitous in actual government practice."

Petitioner's rebuttal

The argument concluded with a brief rebuttal by Petitioner. First, Petitioner claimed that the test proposed by *Amicus* applies to Principal Officers but not Inferior Officers. Second, SEC ALJs lack the authority to make final decisions. Finally, if the case is reversed the proceeding below should be viewed as a nullity and dismissed because of the significant Constitutional error.

Comment

While each side claimed the prior decisions of the Court were in accord with its position, as the questioning from the bench demonstrated, that determination, at best, depends on how those decisions are read and interpreted. While there were questions and points during the argument which suggested that the Court may view *Freytag* and perhaps its other decisions as controlling, clearly the Justices are troubled by the proposed tests. One key point is the impact on the federal government and the civil service. Justice Breyer, for example, repeatedly returned to this issue throughout the argument as did other members of the Court. Another critical issue concerned the overall fairness of the process as well as the perceived fairness, as Justice Kennedy repeatedly noted.

Finally, the issue of remedies is key. Although this topic was little discussed, it was clear that the potential impact of the decision on not just the SEC but other federal agencies and perhaps even terminated cases – a point only very briefly mentioned by the Solicitor -- are issues which concern the Court. In the end, perhaps the clearest point is that a case which many once viewed as a foregone conclusion in view of the confession of error is anything but that. A decision will be handed down by the end of June.