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## The Shadow of Free Enterprise: The Unconstitutionality of the Securities & Exchange Commission's Administrative Law Judges

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# The Shadow of Free Enterprise: The Unconstitutionality of the Securities & Exchange Commission’s Administrative Law Judges<sup>Ψ</sup>

By Linda D. Jellum<sup>\*</sup> and Moses M. Tincher<sup>\*\*</sup>

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## ABSTRACT

Six years ago, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), for the first time giving the Securities and Exchange Commission (SEC) the power to seek monetary penalties through its in-house adjudication. The SEC already had the power to seek such penalties in federal court. With the Dodd-Frank Act, the SEC's enforcement division could now choose between an adjudication before an SEC Administrative Law Judge (ALJ) or a civil action before an Article III judge. With this new choice, the SEC realized a significant home-court advantage. For example, in 2014, the SEC's enforcement division prevailed in 100% of its administrative proceedings, while it prevailed in only 61% of the cases it brought in federal court. With these statistics, it is no surprise that potential respondents to SEC enforcement actions soon challenged the constitutionality of the SEC's new choice.

In this Article, we explain why the SEC ALJs' appointment and removal processes violate the United States Constitution. The SEC ALJs are inferior officers of the United States. As such, they must be appointed by the President, a court of law, or the head of a department. Instead, they are appointed by the head SEC ALJ. Additionally, in *Free Enterprise Fund v. Public Company Accounting Oversight Board*,<sup>1</sup> the

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Supreme Court held that dual for-cause removal provisions violate separation of powers because such clauses prevent the President from faithfully executing the law. The SEC ALJs are subject to multiple for-cause removal protections. Possibly, the Supreme Court will refuse to extend its holding in *Free Enterprise*— that multiple levels of tenure protection violate separation of powers—to ALJs. However, if the Court meant what it said and if the case is to have any relevance beyond the agency involved in that case, then the multiple for-cause removal provisions affecting the SEC ALJs specifically, and all ALJs generally, will need to be reconsidered.

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<sup>1</sup> 561 U.S. 477, 483–84 (2010).

## I. INTRODUCTION

In 2016, the Securities and Exchange Commission (SEC) brought a record number of enforcement actions.<sup>2</sup> The SEC's new Chair, Mary Jo White, credited changes in the agency's approach for the uptick: "Over the last three years, we have changed the way we do business on the enforcement front by using new data analytics to uncover fraud, enhancing our ability to litigate tough cases, and expanding the playbook bringing novel and significant actions to better protect investors and our markets."<sup>3</sup> Others credit White's policy that "there's no violation or potential violation that's too small to go after," for the increase.<sup>4</sup> While the truth likely lies somewhere in between, Congress played a significant role in the agency's transformation. Six years ago, Congress enacted the Dodd-Frank Act,<sup>5</sup> for the first time giving the SEC the power to seek monetary penalties in its in-house adjudications. The SEC already had the power to seek such penalties in federal court.<sup>6</sup> With the Dodd-Frank Act, the SEC's enforcement division could choose which forum to use: an adjudication before an SEC Administrative Law Judge (ALJ) or a civil action before an Article III judge.<sup>7</sup>

With this new forum, the SEC soon realized it had a significant home-court advantage. A recent Wall Street Journal study found that from October 2010 to March 2015, the SEC's enforcement division

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<sup>2</sup> 2.P.J. D'Annunzio, No Violation 'Too Small' as SEC Sets Enforcement Record, Law.Com (Oct.11, 2016), [http://www.law.com/sites/almstaff/2016/10/11/no-violation-too-small-as-sec-sets-enforcement-record/?kw=No%20Violation%20Too%20Small%20as%20SEC%20Sets%20Enforcement%20Record&et=editorial&bu=Daily%20Report&cn=20161013&src=EMC-Email&pt=Morning%20News&slreturn=20160930151208\[https://perma.cc/MV3J-ASZU\]](http://www.law.com/sites/almstaff/2016/10/11/no-violation-too-small-as-sec-sets-enforcement-record/?kw=No%20Violation%20Too%20Small%20as%20SEC%20Sets%20Enforcement%20Record&et=editorial&bu=Daily%20Report&cn=20161013&src=EMC-Email&pt=Morning%20News&slreturn=20160930151208[https://perma.cc/MV3J-ASZU]) (noting that "[t]here were 868 enforcement actions this fiscal year compared with 807 in 2015 and 755 in 2014").

<sup>3</sup> Id.

<sup>4</sup> Id.

<sup>5</sup> See generally Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, 1376–2223 (2010) (codified in scattered sections of U.S.C. tits. 7, 12, 15, 22, and 42).

<sup>6</sup> See *Bebo v. SEC*, 799 F.3d 765, 768 (7th Cir. 2015).

<sup>7</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 1055(a)(1).

prevailed in 86% of the proceedings it brought in-house, while it prevailed in 70% of the cases it brought in federal court.<sup>8</sup> Indeed, from October 2013 to January 2015, the SEC won 219 in-house adjudications in a row.<sup>9</sup> In fiscal year 2014, the SEC's enforcement division prevailed in 100% of its administrative proceedings, while it prevailed in only 61% of the cases it brought in federal court.<sup>10</sup> Perceiving these statistics to be accurate, it is no surprise that potential respondents to SEC enforcement actions soon challenged the constitutionality of the SEC's new choice.<sup>11</sup> Relatedly, the Federal Trade Commission (FTC) was recently impacted by similar challenges. On March 23, 2016, the House passed a bill that would strip the FTC's power to adjudicate antitrust cases through its administrative process following a court's denial of an FTC preliminary injunction request.<sup>12</sup> Assuming this bill becomes law, all antitrust cases will have to be brought in federal court.

The first constitutional challenges plaintiffs filed in the SEC cases raised equal protection and due process claims.<sup>13</sup> In these challenges, the plaintiffs alleged that the SEC's administrative proceedings do not provide the same degree of procedural protections and fairness that are afforded in federal court.<sup>14</sup> These challenges

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<sup>8</sup> Jean Eaglesham, Fairness of SEC Judges Is in Spotlight, Wall St. J. (Nov. 22, 2015, 9:25 PM), <http://www.wsj.com/articles/fairness-of-sec-judges-is-in-spotlight-1448236970> [<https://perma.cc/2Y3H-8GV9>].

<sup>9</sup> Ryan Jones, The Fight over Home Court: An Analysis of the SEC's Increased Use of Administrative Proceedings, 68 SMU L. Rev. 507, 509 (2015).

<sup>10</sup> See Nate Raymond, U.S. Judge Criticizes SEC Use of In-House Court for Fraud Cases, Reuters (Nov. 5, 2014, 1:37 PM), <http://www.reuters.com/article/2014/11/05/sec-fraud-rakoff-idUSL1N0SV2LN20141105> [<https://perma.cc/L9DT-HUG2>].

<sup>11</sup> At least one academic believes that the SEC statistics are being used inaccurately and that the SEC is no more likely to prevail before an ALJ than in court. See generally Urska Velikonja, Reporting Agency Performance: Behind the SEC's Enforcement Statistics, 101 Cornell L. Rev. 901 (2016).

<sup>12</sup> Standard Merger and Acquisition Reviews Through Equal Rules Act of 2015, H.R. 2745, 114th Cong. § 4 (2016).

<sup>13</sup> See Bebo v. SEC, 799 F.3d 765, 768 (7th Cir. 2015); see also Chau v. SEC, 72 F. Supp. 3d 417, 420 (S.D.N.Y. 2014); Gupta v. SEC, 796 F. Supp. 2d 503, 514 (S.D.N.Y. 2011).

<sup>14</sup> See generally, 799 F.3d at 768; see also Chau, 72 F. Supp. 3d 417 at 420; Gupta, 796 F. Supp. 2d at 507

have so far proved unsuccessful. Hence, a new round of challenges has now begun as a result of the Supreme Court's 2010 holding in Free Enterprise Fund v. Public Company Accounting Oversight Board.<sup>15</sup> In Free Enterprise, the Court held that dual for-cause removal provisions violate separation of powers because the President is prevented from faithfully executing the law.<sup>16</sup> The SEC ALJs are subject to multiple for-cause removal protections; therefore, plaintiffs added Free Enterprise removal claims to their legal challenges.<sup>17</sup>

The plaintiff in Bebo v. SEC was the first plaintiff to raise a removal claim.<sup>18</sup> On March 3, 2015, Laurie Bebo filed suit in the Eastern District Court of Wisconsin, arguing, among other things, that the SEC ALJs' removal structure violated separation of powers.<sup>19</sup> The court in Bebo found plaintiff's claims to be "compelling and meritorious;" however, the court held that it lacked subject matter jurisdiction to hear them.<sup>20</sup> With this ruling, the court effectively required the plaintiff to raise her claim before the very tribunal she alleged was unconstitutional.<sup>21</sup> The Seventh Circuit affirmed.<sup>22</sup>

Several months later, the plaintiff in Tilton v. SEC filed a similar challenge in the Southern District Court of New York, alleging that the removal scheme for the SEC ALJs was unconstitutional.<sup>23</sup>

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<sup>15</sup> See generally 561 U.S. 477 (2010).

<sup>16</sup> Id. at 496; cf. Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd., 684 F.3d 1332–40 (D.C. Cir. 2012) (holding that the Copyright Royalty Board members are similarly unconstitutionally subject to dual for-cause removal protection).

<sup>17</sup> See Bebo, 799 F.3d at 768; Chau, 72 F. Supp. 3d at 437; Gupta, 796 F. Supp. 2d at 514.

<sup>18</sup> Bebo v. SEC, No. 15-C-3, 2015 U.S. Dist. LEXIS 25660, at \*1 (E.D. Wis. Mar. 3, 2015).

<sup>19</sup> Id. at \*2–3.

<sup>20</sup> Id. at \*3–4 (concluding that the claims were "subject to the exclusive remedial scheme set forth in the Securities Exchange Act").

<sup>21</sup> After Bebo was affirmed by the Seventh Circuit, the Supreme Court denied certiorari. Bebo v. SEC, 799 F.3d 765, 767 (7th Cir. 2015), cert denied, 136 S. Ct. 1500 (2016).

<sup>22</sup> Bebo, 799 F.3d at 767.

<sup>23</sup> Tilton v. SEC, No. 12-CV-2473, 2015 U.S. Dist. LEXIS 85015, at \*1–2 (S.D.N.Y. June 30, 2015), aff'd, 824 F.3d 276, 279 (2d Cir. 2016). Tilton recently

Plaintiff Tilton, however, added a new constitutional claim: not only are SEC ALJs subject to unconstitutional removal provisions, they are inferior officers who are not appointed by the SEC Commissioners, the President, or a court of law.<sup>24</sup> Thus, their appointment violates the Appointments Clause of the United States Constitution.<sup>25</sup> Just like the court in Bebo, the district court in Tilton also dismissed the case for lack of subject matter jurisdiction.<sup>26</sup>

Shortly after Tilton was decided, two federal district courts rejected both Tilton and Bebo's holdings regarding subject matter jurisdiction. The Southern District Court of New York and the Northern District Court of Georgia both concluded that federal courts had jurisdiction to hear these constitutional challenges.<sup>27</sup> Because the plaintiffs sought preliminary injunctions and declaratory relief, these courts next addressed the likelihood that the plaintiffs would succeed on the merits of their constitutional claims.<sup>28</sup> In doing so, both courts addressed the appointment claim, finding that because the SEC ALJs are inferior officers, and because they were not appointed as required,

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filed a new complaint with the U.S. District Court for the Southern District of New York, seeking declaratory and injunctive relief. Complaint at 1–2, Tilton v. SEC, No. 1:16-cv-07048 (S.D.N.Y. Sept. 9, 2016). The complaint challenges the SEC's decision not to apply its new procedural rules in Tilton's pending administrative case. Id. at 2

<sup>24</sup> Tilton, 2015 U.S. Dist. LEXIS 85015, at \*5–6.

<sup>25</sup> Id.

<sup>26</sup> Id. at \*36–37. (“Congress has carefully delineated the distinct roles of the Commission and the courts in cases such as this. It rests first with the Commission to determine whether to commence an action at all . . . [T]here is no basis to allow Plaintiffs to bypass this congressionally created remedial scheme. Accordingly, this Court lacks subject matter jurisdiction over this action.”). The Second Circuit recently affirmed, over a strong dissent, the district court's decision that the case was impliedly precluded. Tilton v. SEC, 824 F.3d 276, 279 (2d Cir. 2016) (holding that Congress implicitly precluded federal district court jurisdiction over the plaintiffs' constitutional claims).

<sup>27</sup> See Timbervest, LLC v. SEC, No. 1:15-CV-2106-LMM, 2015 U.S. Dist. LEXIS 132082, at \*20 (N.D. Ga. Aug. 4, 2015); Gray Fin. Grp., Inc. v. SEC, 166 F. Supp. 1335, 1343, 1349 (N.D. Ga. 2015), vacated and remanded, Hill v. SEC, 825 F.3d 1236, 1252 (11th Cir. 2016); Hill v. SEC, 114 F. Supp. 3d 1297, 1306, 1310 (N.D. Ga. 2015), vacated and remanded, Hill v. SEC, 825 F.3d 1236, 1252 (11th Cir. 2016); Duka v. SEC, 103 F. Supp. 3d 382, 385, 392 (S.D.N.Y. 2015).

<sup>28</sup> See Timbervest, 2015 U.S. Dist. LEXIS 132082, at \*22; Gray, 166 F. Supp. at 1349–50; Hill, 114 F. Supp. 3d at 1319; Duka, 103 F. Supp. 3d at 392–93.



their appointment likely violates the Constitution.<sup>29</sup> As for the removal claim, neither court believed that multiple layers of for-cause removal protection were problematic.<sup>30</sup> The plaintiffs, however, lost these arguments on appeal.<sup>31</sup> Collectively, these cases raise difficult questions regarding the constitutionality of the SEC ALJs. These cases could potentially dismantle the entire formal administrative system.

In this Article, we examine the validity of the claims that the SEC ALJs' appointment and removal process violates Article II of the United States Constitution and the separation of powers principle.<sup>32</sup> The importance of the resolution of these issues cannot be overstated. If the above-discussed plaintiffs' claims are valid, the SEC ALJ system will need to be revised and the legitimacy of hundreds of past, pending, and future SEC adjudications will be in doubt. This concern may explain the SEC's reluctance to correct the appointments issue with a relatively simple fix.<sup>33</sup> In addition, if the removal structure violates the Constitution, then the legitimacy of thousands of federal adjudications held before all ALJs may be at risk because all federal ALJs are subject to at least dual for-cause removal protections.<sup>34</sup> The

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<sup>29</sup> *Duka v. SEC*, 124 F. Supp. 3d 287, 289 (S.D.N.Y. 2015); *Timbervest*, 2015 U.S. Dist. LEXIS 132082, at \*35; *Gray*, 166 F. Supp. at 1354; *Hill*, 114 F. Supp. 3d at 1319

<sup>30</sup> See *Hill*, 114 F. Supp. 3d at 1319 n.12 (noting that the court "has serious doubts that . . . ALJs likely occupy 'quasi-judicial' or 'adjudicatory' positions, and thus these two-layer protections likely do not interfere with the President's ability to perform his duties"); *Duka*, 103 F. Supp. 3d at 395 (noting that the statutory restrictions on the removal of SEC ALJs do not "infringe the President's constitutional authority").

<sup>31</sup> *Hill v. SEC*, 825 F.2d 1236, 1237–38, 1252 (11th Cir. 2016) ("[T]he district court[s] [in *Gray* and *Hill*] erred in exercising jurisdiction. We vacate . . . and remand with instructions to dismiss each case for lack of jurisdiction."). *Duka* was effectively abrogated by *Tilton v. SEC*, 824 F.3d 276, 279 (2d Cir. 2016).

<sup>32</sup> U.S. Const. art. II.

<sup>33</sup> *Duka v. SEC*, 15 Civ. 357 (RMB) (SN), 2015 U.S. Dist. LEXIS 124444, at \*18 n.7 (The court gave the SEC the opportunity to cure any violation of the Appointments Clause; however, the SEC advised the court that "[a]lthough the Commission in its adjudicatory capacity may decide in due course whether the SEC ALJs' appointments violate the Constitution[,] . . . the Commission has not issued a decision or otherwise taken any public action on these questions.").

<sup>34</sup> See *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 478, 487 (2010). But see *Kent H. Barnett, Avoiding Independent Agency*

appointment procedure used by other federal agencies is less clear, but it is likely that the SEC is not alone in bypassing the constitutionally valid appointment procedure.<sup>35</sup>

We proceed as follows: Part II explains the history of the SEC and its expanding powers, and Part III describes ALJs generally and their role in the SEC's in-house adjudications. These parts provide background for the remainder of the Article.

Part IV is the heart of the Article. In Subsection A, we first turn to the question of whether SEC ALJs are inferior officers, because resolution of the appointments and removal claims depends on a finding that the SEC ALJs are inferior officers, not employees. Although the SEC claims its ALJs are merely employees, we disagree. The SEC ALJs are inferior officers. Because the SEC ALJs are inferior officers, and because the SEC admits that its ALJs are not appointed by its commissioners, the President, or a court of law, in Subsection B, we explain why the SEC ALJ appointment process violates the Constitution. Resolving this legal question is easy; fixing the process is more difficult. Whether the SEC Commissioners can retroactively appoint its current ALJs without casting doubt on existing decisions and pending cases is unclear. Indeed, the recent aftermath of NLRB v. Noel Canning suggests that these administrative decisions may be invalid.<sup>36</sup> In any event, whether this type of post-hoc "appointment" truly comports in spirit with the constitutional requirements of the Appointments Clause is uncertain.<sup>37</sup>

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Armageddon, 87 Notre Dame L. Rev. 1349 (2012) (suggesting courts adopt a three tiered approach to for-cause removal provisions to preserve both agency independence and the President's removal power).

<sup>35</sup> Id. at 542–43 (Breyer, J., dissenting) ("My research reflects that the Federal Government relies on 1,584 ALJs to adjudicate administrative matters in over 25 agencies."); see also John F. Duffy, Are Administrative Patent Judges Unconstitutional?, 77 Geo. Wash. L. Rev. 904, 904–05 (2009) (concluding that administrative patent judges are likely unconstitutional due to their method of appointment).

<sup>36</sup> See 134 S. Ct. 2550, 2553–56 (2014).

<sup>37</sup> See generally Ronald J. Krotoszynski, Jr., Transcending Formalism and Functionalism in Separation-of-Powers Analysis: Reframing the Appointments Power after Noel Canning, 64 Duke L.J. 1513, 1516 (2015) (suggesting that a workable account of the federal appointments process requires blending both a formalist and functionalist legal analysis); John M. Greabe, Noel Canning and

In Subsection C, we turn to the harder question: whether the multiple for-cause removal provisions of the SEC ALJs violate separation of powers. After exploring the conflicting and confusing case law in this area,<sup>38</sup> we offer a framework for determining when for-cause removal provisions violate separation of powers. We then apply that framework to conclude that the multiple for-cause removal provisions protecting the SEC ALJs likely violate separation of powers. Specifically, the SEC ALJ's first level of for-cause removal protection is problematic under Morrison v. Olsen.<sup>39</sup> And the SEC ALJ's second level of for-cause removal protection is problematic under Free Enterprise. Because the second level for-cause removal provisions apply to most ALJs,<sup>40</sup> the implications are potentially staggering. And, again, there does not appear to be an easy fix.

Possibly, the Supreme Court will refuse to extend its holding in Free Enterprise—that multiple levels of tenure protection violate separation of powers—to ALJs.<sup>41</sup> To extend the holding could significantly disrupt the administrative state. However, if the Court meant what it said in Free Enterprise, and if that case is to have any relevance beyond the agency involved in it, then the multiple for-cause removal provisions affecting the SEC ALJs specifically, and all ALJs generally, will need to be reconsidered.

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Remedial Obligation Under the Constitution, 100 Va. L.R. Online 47 (2014) (arguing that the remedy for the wrong in Noel Canning should be decided in a manner that is akin to harmless- and plain-error review).

<sup>38</sup> Because most of the cases address the distinction between principal and inferior officers and not inferior officers and employees, guidelines can be difficult to discern.

<sup>39</sup> 487 U.S. 654 (1988).

<sup>40</sup> Whether Social Security ALJs are inferior officers is an open question given the nature of their authority.

<sup>41</sup> Free Enter. Fund, 561 U.S. at 477.

## II. THE BIRTH OF THE SEC, ALJs, AND SEC ADJUDICATIONS

### A. *The Birth of the SEC*

As a direct response to the Great Depression, Congress created the SEC pursuant to Section 4 of the Exchange Act.<sup>42</sup> The Exchange Act authorized the SEC to enforce the federal securities laws by proposing securities rules and regulations and by regulating the securities industry, which includes the nation's stock and options exchanges.<sup>43</sup> According to its current website, the SEC's mission is to "protect investors;" "maintain fair, orderly, and efficient markets;" and "facilitate capital formation."<sup>44</sup> The SEC is an independent agency<sup>45</sup> with five commissioners, all of whom the President appoints, subject to Senate approval.<sup>46</sup> No more than three commissioners can be members of the same political party.<sup>47</sup> The Exchange Act does not expressly address the President's power to remove the SEC commissioners.<sup>48</sup> Hence, it is unclear whether the President has the power to remove them at will; however, many

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<sup>42</sup> 15 U.S.C. § 78d(a) (2012).

<sup>43</sup> 15 U.S.C. § 78d-1(a) (2012). The SEC also enforces the Securities Act of 1933, the Trust Indenture Act of 1939, the Investment Company Act of 1940, the Investment Advisers Act of 1940, the Sarbanes–Oxley Act of 2002, and other statutes.

<sup>44</sup> The Role of the SEC, Investor.gov, <http://investor.gov/introduction-investing/basics/role-sec> [<https://perma.cc/S4UD-KB6H>].

<sup>45</sup> See Free Enter. Fund, 561 U.S. at 510–11 (noting that four Justices would find the SEC to be an independent agency because it is a "free-standing, self-contained entity in the Executive Branch") (internal quotation marks omitted); Kirti Datla & Richard L. Revesz, Deconstructing Independent Agencies (and Executive Agencies), 98 Cornell L. Rev. 769, 771 (2013) (noting that independent agencies are generally "defined as entities whose heads enjoy (or are believed to enjoy) for-cause removal protection," and they include the "Securities and Exchange Commission (SEC)").

<sup>46</sup> 15 U.S.C. § 78d(a).

<sup>47</sup> § 78d(a)

<sup>48</sup> In contrast, the Federal Trade Commission Act gave the President the power to remove Federal Trade Commission commissioners for "inefficiency, neglect of duty, or malfeasance in office" (i.e., not "at will"). See 15U.S.C. § 41 (2012).

assume that the President may remove the Commissioners only “for cause.”<sup>49</sup>

The SEC’s powers have increased with time and need. For example, in 1984, Congress granted the SEC the power to seek civil monetary penalties in district court in insider trading cases.<sup>50</sup> In 1990, Congress, for the first time, authorized the SEC to pursue any person for Exchange Act violations through an administrative cease-and-desist adjudication.<sup>51</sup> Prior to 1990, such actions had to be brought in federal district court.<sup>52</sup> Through this in-house adjudication, the SEC enforcement division could obtain an order enjoining anyone found to be violating the Exchange Act.<sup>53</sup> Congress also gave the SEC limited authority to seek civil monetary penalties in these enforcement adjudications against regulated entities.<sup>54</sup> However, the SEC’s enforcement division had to file in federal district court to seek monetary penalties against an entity who was either not a regulated entity<sup>55</sup> or was not associated with a regulated entity.<sup>56</sup> In federal court, the defendants could invoke their Seventh Amendment right to a jury trial, file pretrial motions, and seek discovery,<sup>57</sup> options that are unavailable in the SEC’s in-house adjudications.<sup>58</sup>

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<sup>49</sup> The only time the Supreme Court has addressed this issue, the parties stipulated that SEC Commissioners “cannot themselves be removed by the President except [for] ‘inefficiency, neglect of duty, or malfeasance in office’” Free Enter. Fund, 561 U.S. at 487 (citing Humphrey’s Executor v. United States, 295 U.S. 602, 620 (1935)). The Court “decide[d] the case with that understanding.” Id.

<sup>50</sup> Insider Trading Sanctions Act of 1984, Pub. Law No. 98-376, § 2, 98 Stat. 1264, 1264–65 (1984) (codified as amended in various sections of 15 U.S.C.).

<sup>51</sup> Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, §§ 102, 203, 104 Stat. 931, 933–35, 939–40 (1990).

<sup>52</sup> See H.R. 975—Securities Law Enforcement Remedies Act, of 1990: Summary Reported to House amended (07/23/1990), Congress.gov, <https://www.congress.gov/bill/101st-congress/house-bill/975> [<https://perma.cc/2D2A-2YPP>] (This bill was not enacted).

<sup>53</sup> See 15 U.S.C. § 78u-3 (2012).

<sup>54</sup> See Securities Enforcement Remedies and Penny Stock Reform Act § 203.

<sup>55</sup> Registered entities primarily include broker-dealers and investment advisers. See id. §§ 301, 401.

<sup>56</sup> Id.

<sup>57</sup> Fed. R. Civ. P. 12; Fed. R. Civ. P. 26; Fed. R. Civ. P. 38.

<sup>58</sup> See 17 C.F.R. §§ 201.233–234 (2016).

Twenty years later, and in direct response to the financial crisis of 2009, Congress passed the Dodd-Frank Act, which authorized the SEC to seek civil monetary penalties from “any person” suspected of violating the Exchange Act—both those registered and unregistered with the SEC— after an administrative hearing, subject to judicial review on the administrative record in the court of appeals.<sup>59</sup> Importantly, the Dodd-Frank Act gave the SEC the discretion to decide whether to bring an enforcement action in federal court or in an administrative proceeding.<sup>60</sup> Because respondents in administrative proceedings have no right to a jury trial, no right to file pretrial motions, and little right to obtain discovery, the level playing field tilted in the SEC’s favor.

### *B. The Birth of ALJs*

The Administrative Procedure Act (APA)<sup>61</sup> authorizes agencies, including the SEC, to conduct formal, in-house administrative proceedings, or adjudications, before an ALJ.<sup>62</sup> When the APA was originally enacted, ALJs were called “hearing examiners” because they were expected to oversee hearings and compile the record for the agency to review *de novo*.<sup>63</sup> The name change is historically

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<sup>59</sup> Section 929P of the Dodd-Frank Act, amended Section 8A of the Securities Act, Section 21B(a) of the Securities Exchange Act, Section 9(d)(1) of the Investment Company Act, and Section 203(i)(1) of the Investment Advisers Act to permit the imposition of civil monetary penalties in administrative proceedings, in addition to the cease-and-desist orders previously available to the SEC. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929P, 124 Stat. 1376, 1862–65 (2010). Additionally, for cease-and-desist proceedings instituted under the Securities Act, where there was no pre-existing provision for SEC-imposed penalties because that act did not address regulated entities, the Dodd-Frank Act adopts the three-tiered penalty grid already contained in the Securities Exchange Act, the Investment Company Act and the Investment Advisers Act. Compare Dodd-Frank Wall Street Reform and Consumer Protection Act § 929P with Securities Enforcement Remedies and Penny Stock Reform Act §§ 202, 301, 401.

<sup>60</sup> See 15 U.S.C. §§ 78u(d), 78u-1, 78u-2, 78u-3 (2012).

<sup>61</sup> 5 U.S.C. § 551, et seq. (2012).

<sup>62</sup> 5 U.S.C. § 3105 (2012) (authorizing agencies to conduct hearings before ALJs).

<sup>63</sup> 5 U.S.C. § 557(b) (2012).

significant. At the beginning of the nineteenth century, “examiners”<sup>64</sup> presided over most agency proceedings.<sup>65</sup> Agencies hired examiners directly.<sup>66</sup> These examiners were not independent, in the sense that the agencies for which they worked controlled their assignments, their compensation, their promotions, and their retention.<sup>67</sup> Indeed, some examiners served completely at the pleasure of their superiors and had no job security whatsoever.<sup>68</sup> Hence, judicial “independence” and “impartiality” were not an assured part of the administrative equation.<sup>69</sup>

By the 1930s, legal commentators began to raise serious concerns about the status of these examiners, as well as about the examiners’ ability to decide cases fairly, independently, and impartially.<sup>70</sup> For example, in 1934, the American Bar Association’s (ABA) Special Committee on Administrative Law criticized the fact that some

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<sup>64</sup> The term “examiners” came into use in 1906. 3 Kenneth Culp Davis, *Administrative Law Treatise* § 17.11, at 313 (2d ed. 1978).

<sup>65</sup> Russell L. Weaver, *Management of ALJ Offices in Executive Departments and Agencies*, 47 *Admin. L. Rev.* 303, 303 (1995).

<sup>66</sup> *Id.*

<sup>67</sup> See Malcolm Rich, *Adapting the Central Panel System: A Study of Seven States*, 65 *Judicature* 246, 246 (1981) (“The agencies controlled the compensation and job tenure of their hearing officers and could ignore their decisions and enter de novo rulings instead.”).

<sup>68</sup> See *id.*

<sup>69</sup> See *Ramspeck v. Fed. Trial Exam’rs Conference*, 345 U.S. 128, 131 (1953) (noting that hearing examiners were “mere tools of the agency concerned and subservient to the agency heads in making their proposed findings of fact and recommendations”).

<sup>70</sup> An ABA Report concluded that: [A]ppointments to administrative tribunals are all too generally classed as patronage and, it is to be feared, the decisions of some of them are occasionally dealt with as a form of patronage. It is not easy to maintain judicial independence or high standards of judicial conduct when a political sword of Damocles continually threatens the judge’s source of livelihood. While a few federal administrative tribunals have, in spite of all obstacles, preserved a high degree of independence from political pressure and political considerations, unfortunately there are others which have yielded and as a result the cause of justice has suffered. Report of the Special Committee on Administrative Law, 57 *Annu. Rep. A.B.A.* 539, 546 (1934) [hereinafter ABA Special Report]; see also Jeffrey S. Lubbers, *Federal Administrative Law Judges: A Focus on Our Invisible Judiciary*, 33 *Admin. L. Rev.* 109, 111 (1981).

examiners exercised both prosecutorial and adjudicative functions.<sup>71</sup> However, separation of functions and status were not the only concerns. Even had examiners been functionally separate from their agencies, their decisions were not final and could be overruled by agency superiors.<sup>72</sup>

During the debate on enacting the APA, many suggestions were offered regarding how to reform the system. Some argued that Congress should create a federal administrative court that would hear only administrative cases.<sup>73</sup> Others suggested that Congress should create an independent administrative judiciary—a central panel of

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<sup>71</sup> ABA Special Report, supra note 70, at 545. One member of the Committee summed up the concerns as follows: If there is anything of which we can be relatively sure after some hundreds, even thousands, of years of experience with judicial machinery, it is that no man can be trusted to be judge in his own case. And he is a judge in his own case if he is also the prosecutor or if he is also the legislator who made the rule he is asked to interpret and apply. Agency after agency in our federal government is authorized to wield all three powers of government at once. Wearing its legislative toga, a commission makes a regulation, on compliance with which John Doe's right to continue in business may depend. Having reason to believe that John Doe is guilty of violating the regulation, the commission doffs the toga and, taking up the executive scepter, investigates and prosecutes him. With the scepter still in its hand, the commission hurriedly dons the judicial ermine and proceeds to present itself at least two scintillas of evidence to prove that it was right in the first place. While care is sometimes taken to preserve the form of placing the burden of proof on the prosecutor, all the form in the world cannot disguise the fact that the burden is usually on John Doe to prove himself innocent before a commission that at least strongly suspects he is guilty. If John or his lawyer construes the regulation differently than does the commission, that is just unfortunate for John. The commission made the regulation and is confident that it knows just what it meant to say. And it is always free to change its mind. John is in the position of a man whose wife changes her system of bidding in the middle of a bridge game without notice. He is sure to lose and is equally sure to get blamed for it. Louis G. Caldwell, A Federal Administrative Court, 84 U. Pa. L. Rev. 966, 973–74 (1936) (emphasis in original). See also Wong Yang Sung v. McGrath, 339 U.S. 33, 36–38, 41–42 (1950).

<sup>72</sup> Lubbers, supra note 70, at 111 (“Furthermore, the role of the presiding officer in an agency's decisional process was often unclear; many agencies would ignore the officer's decisions without giving reasons, and enter their own de novo decisions.”).

<sup>73</sup> John D. O'Reilly, Jr., The Federal Administrative Court Proposal: An Examination of General Principles, 6 Fordham L. Rev. 365, 365–66 (1937); see also Attorney General's Committee on Administrative Procedure—Majority and Minority Reports, 27 A.B.A. J. 91, 93 (1941).



judges—to adjudicate administrative matters.<sup>74</sup> Congress ultimately rejected both of these suggestions.<sup>75</sup>

In 1946, with the passage of the APA, Congress opted for a third approach, which included a number of protective components. First, Congress sought to prevent agency officials from acting as lawmaker, investigator, prosecutor, and jury in the same case.<sup>76</sup> To further this point, the APA provided that ALJs could not be responsible to, or subject to supervision by anyone performing investigative or prosecutorial functions for an agency.<sup>77</sup> The APA, thus, required an agency to separate its prosecuting functions from its adjudicating functions.<sup>78</sup> Any agency employee who investigated or prosecuted a case could not supervise or direct the work of those individuals who adjudicated the same case.<sup>79</sup> Additionally, those individuals who investigated or prosecuted a case could not be part of the decision-making process.<sup>80</sup> And, the APA restricted some *ex parte*

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<sup>74</sup> See generally Rich, *supra* note 67, 246–47 (describing these alternatives).

<sup>75</sup> See generally 5 U.S.C. § 551 et seq. (2012).

<sup>76</sup> 5 U.S.C. § 554 (d)(2) (2012).

<sup>77</sup> See § 554(d)(2). Indeed, Congress created a unique system because of its concern about separating the adjudicatory function from other conflicting agency functions. In 1970 and 1977 respectively, Congress created the Occupational Safety and Health Review Commission (OSHRC) and the Federal Mine Safety and Health Review Commission (FMSHRC). Robin J. Arzt, Recommendations for a new Independent Adjudication Agency to Make the Final Administrative Adjudications of Social Security Act Benefits Claims, 23 J. Nat'l Ass'n Admin. L. Judges 267, 281 (2003). Both are independent, Executive Branch agencies located outside the Department of Labor. *Id.* Importantly, they have adjudicative authority only. *Id.* (“OSHRC determines whether regulations promulgated and enforced by the Occupational Safety and Health Administration have been violated. FMSHRC adjudicates violations of standards promulgated and enforced by the Mine Safety and Health Administration.”).

<sup>78</sup> 5 U.S.C. § 554(d).

<sup>79</sup> § 554(d).

<sup>80</sup> § 554(d). There were, however, some exceptions. The APA provides that Section 554(d) “does not apply . . . to the agency or a member or members of the body comprising the agency.” § 554(d)(2)(C). As a result, “a member or members of the body comprising the agency” could be involved in prosecutorial, investigatory, and adjudicatory functions. § 554(d)(2)(c).

communications.<sup>81</sup> In short, the APA altered the prior practice to mirror more closely the federal judicial process.

In addition, the APA altered the prior treatment of examiners to more closely mirror the status of Article III judges. The centerpiece of the APA reform involved strengthening the job protections and status of some of the examiners,<sup>82</sup> or as they would soon be called, ALJs,<sup>83</sup> by giving these hearing examiners job protections designed to bolster their independence.<sup>84</sup> So, the APA gave the role of hiring to the Office of Personnel Management (OPM).<sup>85</sup> The OPM was exclusively responsible for examining, certifying, and compensating these hearing examiners.<sup>86</sup> The OPM determined the minimum experience needed for an individual to be an ALJ and evaluated applicants for the position (by conducting interviews, by

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<sup>81</sup> § 554(d). Congress later amended the APA to add another section designed to address ex parte communications. 5 U.S.C. § 557(d)(2012).

<sup>82</sup> William S. Jordan, III, Chevron and Hearing rights: An Unintended Combination, 61 Admin. L. Rev. 249 at 270 (2009) (citing Kenneth Culp Davis, Administrative Law 309 (1951)); Attorney General's Committee on Administrative Procedure, 77th Cong., Final Report on Administrative Procedure in Government Agencies 45–46 (1941) (noting that the securing of fair and competent hearing personnel was viewed as “the heart of formal administrative adjudication”).

<sup>83</sup> Marvin H. Morse, The Administrative Law Judge: A New Direction for the Corps?, 30 Fed. B. News & J. 398, 401 n.2 (1983) (“The APA . . . initially referred to presiding officers as examiners, colloquially referred to as hearing examiners. This title was administratively standardized to Administrative Law Judge by the Civil Service Commission in August 1972. The ALJ title was ratified by the Act of March 27, 1978, Pub. [L. No.] 95-251, 92 Stat. 183.”); see also Paul R. Verkuil et al., The Federal Administrative Judiciary, 1992 A.C.U.S. 771, 798 (1992). In 1978, Congress amended the APA to officially change the term from hearing examiners to administrative law judges. Pub. L. No. 95-251, 92 Stat. 183, 183–84 (1978).

<sup>84</sup> See also Rich, supra note 67, at 246 (“Congress, in its 1946 Administrative Procedure Act (APA), sought to establish a corps of federal hearing officers that were more independent of the agencies. Hearing officers were to be given career appointments and compensation was to be managed by the Office of Personnel Management. Yet, the hearing officers were not granted complete independence from the agencies, for the APA allowed them to be assigned exclusively to particular agencies.”).

<sup>85</sup> OPM has been “exclusively responsible for the initial examination, certification for selection, and compensation of ALJs.” Lubbers, supra note 70, at 112.

<sup>86</sup> Id.

administering a test to evaluate writing ability, by evaluating the experience of applicants, and by ranking eligible applicants).<sup>87</sup> Despite these changes, however, agencies retained control over the ALJ they selected from the OPM's register and over the ALJ they hired.<sup>88</sup> In other words, while the agencies retained control over who worked for them, the pool of available candidates, which the OPM now controlled, shrunk.

Once hired, ALJs enjoyed increased job protections and independence vis-a-vis pre-APA examiners. Although the APA did not grant ALJs the life tenure granted to Article III judges, the APA provided that ALJs could be removed only for cause or due to a reduction in workforce.<sup>89</sup> In addition, the APA required that ALJs be assigned cases in rotation and that ALJs not perform duties inconsistent with their role as ALJs.<sup>90</sup> Additionally, the APA required that ALJ compensation be determined based on length of service, rather than based on performance evaluations.<sup>91</sup> As the Supreme Court later concluded, these changes made a significant difference in the status of ALJs:

There can be little doubt that the role of the modern federal hearing examiner or administrative law judge within this framework is "functionally comparable" to that of a judge. His powers are often, if not generally, comparable to those of a trial judge: He may issue subpoenas, rule on proffers of evidence, regulate the course of the hearing, and make or recommend decisions. See § 556(c). More importantly, the process of agency adjudication is currently structured so as to assure that the hearing examiner exercises his independent judgment on the evidence before him, free from pressures by the parties or other officials within the agency.<sup>92</sup>

As others have pointed out,<sup>93</sup> the APA system is hardly perfect. There are criticisms of the OPM's selection criteria and of agencies'

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<sup>87</sup> Id.

<sup>88</sup> Id. at 113.

<sup>89</sup> 5 U.S.C. § 7521 (2012); 5 C.F.R. § 1201.131 (2007).

<sup>90</sup> 5 U.S.C. § 3105 (2012); 5 C.F.R. § 930.212 (2007).

<sup>91</sup> See generally 5 U.S.C. § 5372 (2012); 5 U.S.C. § 4301(2)(D) (2012).

<sup>92</sup> *Butz v. Economou*, 438 U.S. 478, 513 (1978).

<sup>93</sup> See generally Michael Asimow & Jeffrey S. Lubbers, The Merits of "Merits" Review: A Comparative Look at the Australian Administrative Appeals

inability to conduct performance evaluations.<sup>94</sup> Indeed, ALJs are removable “only” for “good cause,” which must be “established and determined” by the Merit Systems Protection Board (MSPB) after a formal adjudication.<sup>95</sup> Members of the MSPB, who determine whether “good cause” exists to remove an ALJ, are themselves protected; the President may remove them “only for inefficiency, neglect of duty, or malfeasance in office.”<sup>96</sup> Hence, all ALJs are protected by at least two dual for-cause layers.

### *C. SEC Adjudications*

Like other federal agencies, the SEC is required to appoint and compensate all of its officers, including ALJs.<sup>97</sup> The SEC selects ALJs from the OPM’s list of eligible candidates, based on the agency’s need.<sup>98</sup> More specifically, the SEC’s Office of Administrative Law Judges, with input from the Chief Administrative Law Judge, human resources, and OPM, identifies

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Tribunal, 28 Windsor Y. B. Access Just. 261 (2010) (discussing improvements to the ALJ system).

<sup>94</sup> See Verkuil, *supra* note 83, at 1011 n.1199 (noting that the 1978 Civil Service Reform Act “explicitly exempted ALJs from the performance appraisals required under that system” to maintain “the present system of providing protection for [ALJs]”).

<sup>95</sup> 5 U.S.C. § 7521(a) (2012).

<sup>96</sup> 5 U.S.C. § 1202(d) (2012).

<sup>97</sup> 15 U.S.C. § 78d(b)(1) (2012).

<sup>98</sup> See 5 U.S.C. § 3105 (2012); 5 C.F.R. § 930.204 (2014).

and selects SEC ALJs.<sup>99</sup> The SEC Commissioners are not involved in the appointment process in any way.<sup>100</sup>

By statute, the SEC may delegate adjudicatory functions to its ALJs.<sup>101</sup> Pursuant to that statutory authority,<sup>102</sup> the SEC, like many agencies, has delegated significant authority to its ALJs to conduct administrative proceedings.<sup>103</sup> Specifically, during these hearings, ALJs may:

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<sup>99</sup> See Second Amended Complaint for Declaratory and Injunctive Relief and Demand for Jury Trial ¶ 52, *Gray Fin. Grp., Inc. v. SEC*, 166 F. Supp. 3d 1335 (N.D. Ga. 2015) (No. 1:15-cv-0492-AT), 2015 WL 4185313 [hereinafter *Gray Complaint*] (“SEC ALJs may be appointed by the SEC’s Office of Administrative Law Judges, with input from the Chief Administrative Law Judge, human resource functions and the Office of Personnel Management.”); see also 5 C.F.R. § 930.204(a) (“An agency may appoint an individual to an administrative law judge position only with prior approval of OPM, except when it makes its selection from the list of eligibles provided by OPM. An administrative law judge receives a career appointment and is exempt from the probationary period requirements under part 315 of this chapter.”).

<sup>100</sup> A federal district judge enjoined the SEC from proceeding with an enforcement hearing because the assigned ALJ was not appointed by the SEC Commissioners. *Hill v. SEC*, 114 F. Supp. 3d 1297, 1303, 1319 (N.D. Ga. 2015) (noting that “SEC ALJs are ‘not appointed by the President, the Courts, or the [SEC] Commissioners’” and that “[t]he SEC concede[d] that Plaintiff’s ALJ . . . was not appointed by an SEC Commissioner”).

<sup>101</sup> 15 U.S.C. § 78d-1(a) (2012) (“[T]he [SEC] shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission . . . including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter.”).

<sup>102</sup> 17 C.F.R. § 200.14 (2016).

<sup>103</sup> Under the SEC Rules of Practice, an SEC ALJ may, within his or her discretion, perform the following actions: take testimony, 17 C.F.R. § 201.111 (2016); conduct trials, *id.*; rule on admissibility of evidence, 17 C.F.R. §§ 201.111(c), 201.320 (2016); order production of evidence, 17 C.F.R. §§ 201.230(a)(2), 201.232 (2016); issue orders, including show-cause orders, *see, e.g.*, 17 C.F.R. 201.141(b) (2016); *China Everhealth Corp.*, 109 S.E.C. Docket 2274, Release No. 1639 (July 22, 2014); rule on requests and motions, including pre-trial motions for summary disposition, *see, e.g.*, 17 C.F.R. § 201.250(b) (2016); grant extensions of time, 17 C.F.R. § 201.161 (2016); dismiss for failure to meet deadlines, 17 C.F.R. § 201.155(a) (2016); reconsider decisions, 17 C.F.R. § 201.111(h); reopen any hearing prior to the filing of a decision, 17 C.F.R. § 201.111(j); amend the SEC’s OIP, 17 C.F.R. § 201.200(d)(2) (2016); impose sanctions on parties for contemptuous conduct, 17 C.F.R. § 201.180(a) (2016); reject filings that do not comply with the SEC’s Rules of Practice, 17 C.F.R. § 201.180(b); dismiss the case, decide a particular matter against a party, or prohibit

(1) Administer oaths and affirmations; (2) Issue subpoenas; (3) Rule on offers of proof; (4) Examine witnesses; (5) Regulate the course of a hearing; (6) Hold pre-hearing conferences; (7) Rule upon motions; and (8) Unless waived by the parties, prepare an initial decision containing the conclusions as to the factual

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introduction of evidence when a person fails to make a required filing or cure a deficient filing, 17 C.F.R. § 201.180(c); enter orders of default and rule on motions to set aside default, 17 C.F.R. § 201.155 (2016); consolidate proceedings, 17 C.F.R. § 201.201(a) (2016); grant law enforcement agencies of the federal or state government leave to participate, 17 C.F.R. § 201.210(c)(3) (2016); regulate appearance of amici, 17 C.F.R. § 201.210(d); require amended answers to amended OIPs, 17 C.F.R. § 201.220(b) (2016); direct that answers to OIPs need not specifically admit or deny, or claim insufficient information to respond to, each allegation in the OIP, 17 C.F.R. § 201.220(c); require the SEC to file a more definite statement of specified matters of fact or law to be considered or determined, 17 C.F.R. § 201.220(d); grant or deny leave to amend an answer, 17 C.F.R. § 201.220(e); direct the parties to meet for prehearing conferences and preside over such conferences as the ALJ “deems appropriate,” 17 C.F.R. § 201.221(b) (2016); order any party to furnish prehearing submissions, 17 C.F.R. § 201.222(a) (2016); issue subpoenas, 17 C.F.R. § 201.232 (2016); rule on applications to quash or modify subpoenas, 17 C.F.R. § 201.232(e); order depositions and act as the “deposition officer,” 17 C.F.R. §§ 201.233, 201.234 (2016); regulate the SEC’s use of investigatory subpoenas after the institution of proceedings, 17 C.F.R. § 201.230(g) (2016); modify the Rules of Practice with regard to the SEC’s document production obligations, 17 C.F.R. § 201.230(a)(1); require the SEC to produce documents it has withheld, 17 C.F.R. § 201.230(c); disqualify himself or herself from considering a particular matter, 17 C.F.R. § 201.112(a) (2016); order that scandalous or impertinent matter be stricken from any brief or pleading, 17 C.F.R. § 201.152(f) (2016); order that hearings be stayed while a motion is pending, 17 C.F.R. § 201.154(a) (2016); stay proceedings “pending Commission consideration of offers of settlement,” 17 C.F.R. § 201.161(c)(2) (2016); modify the Rules of Practice as to participation of parties and amici, 17 C.F.R. § 201.210(f) (2016); allow the use of prior sworn statements for any reason and limit or expand the parties’ intended use of the same, 17 C.F.R. § 201.235(a), (a)(5) (2016); express views on offers of settlement, 17 C.F.R. § 201.240(c)(2) (2016); grant or deny leave to move for summary disposition, 17 C.F.R. § 201.250(a) (2016); order that hearings not be recorded or transcribed, 17 C.F.R. § 201.302(a) (2016); grant or deny the parties’ proposed corrections to hearing transcript, 17 C.F.R. § 201.302(c); issue protective orders governing confidentiality of documents, 17 C.F.R. § 201.322 (2016); take “official notice” of facts not appearing in the record, 17 C.F.R. § 201.323 (2016); regulate the scope of cross-examination, 17 C.F.R. § 201.326 (2016); and certify issues for interlocutory review and determine whether proceedings should be stayed during pendency of review, 17 C.F.R. § 201.400(c), (d) (2016).

and legal issues presented, and issue an appropriate order.<sup>104</sup>

Although the APA requires that ALJs be assigned by rotation “so far as is practicable,”<sup>105</sup> SEC Rules provide that the Chief Administrative Law Judge selects the ALJ for each hearing.<sup>106</sup> The selected ALJ then presides over the hearing and issues an initial decision.<sup>107</sup>

As noted earlier, procedures in SEC administrative proceedings vary greatly from the procedures in federal court.<sup>108</sup> For example,

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<sup>104</sup> 17 C.F.R. § 200.14(a) (2016); see also 17 C.F.R. § 200.30–9 (2016) (authorizing ALJs to make initial decisions). These statutes are similar to the authority in the APA. See 5 U.S.C. § 556(c)(2012).

<sup>105</sup> 5 U.S.C. § 3105 (2012).

<sup>106</sup> 17 C.F.R. § 201.110 (2016).

<sup>107</sup> 17 C.F.R. § 201.360(a)(1) (2016).

<sup>108</sup> David Zaring, Enforcement Discretion at the SEC, 94 Tex. L. Rev. 1155, 1165–70 (2016) (discussing the ALJ process). Administrative proceedings in general differ in several critical ways from federal court proceedings. In the case of SEC proceedings, those differences include: (1) In administrative proceedings, an SEC ALJ serves as finder of both fact and of law; (2) Administrative proceedings do not afford juries to litigants, unlike federal court; (3) The Federal Rules of Civil Procedure, which apply in federal court, do not apply in an administrative proceeding; (4) The Federal Rules of Evidence, together with their associated protections, which apply in federal court, do not apply in an administrative proceedings—any evidence that “can conceivably throw any light upon the controversy,” including unreliable hearsay testimony, “normally” will be admitted in an administrative proceeding. In the Matter of Jay Alan Ochanpaugh, Securities Exchange Act Release No. 54363, 2006 SEC LEXIS 1926, at \*23 n.29 (Aug. 25, 2006); (5) Defendants’ ability to conduct discovery is limited in administrative proceedings. For example, pre-trial depositions are generally not allowed in administrative proceedings; they are allowed in federal court (17 C.F.R. §§ 201.233–201.234); (6) The SEC Rules of Practice do not provide respondents the opportunity to challenge the SEC’s legal theories before trial dispositive motions; dispositive motions are available in federal court; (7) The SEC Rules of Practice do not allow respondents to assert counterclaims against the SEC. Federal court defendants may assert counterclaims against their adversaries; (8) The SEC Rules of Practice require the hearing to take place, at most, approximately four months from the issuance of the SEC’s Order Instituting Proceedings (OIP). In its discretion, the SEC can require the hearing to occur as early as one month after the OIP is issued. While the SEC can allow itself years of investigation and research to prepare an administrative case, the SEC does not need to start making available the limited discovery afforded to administrative proceeding respondents until seven days after the OIP is issued; and (9) Administrative proceedings are private, closed

respondents have no right to a jury trial.<sup>109</sup> The Federal Rules of Civil Procedure and Evidence do not apply; instead, the SEC uses its own Rules of Practice.<sup>110</sup> Pursuant to these rules, respondents generally cannot take depositions or obtain documents.<sup>111</sup> Counterclaims are not permissible.<sup>112</sup> And the SEC's rules do not allow for the equivalent of a Rule 12(b) motion to test the sufficiency of the SEC's allegations.<sup>113</sup> Moreover, while the SEC may on its own motion, or at the request of a party, order interlocutory review during a proceeding, "[p]etitions by parties for interlocutory review are disfavored."<sup>114</sup>

SEC administrative proceedings also occur, in theory at least, much more quickly than federal court actions. Following an Order Instituting Proceeding's (OIP) issuance, a hearing must occur within four months; however, the SEC may schedule the evidentiary hearing as early as one month following the OIP's issuance.<sup>115</sup> At the conclusion of the hearing, the ALJ issues an initial decision.<sup>116</sup> Either the litigant or the SEC's enforcement decision can appeal that decision.<sup>117</sup> If neither party appeals,<sup>118</sup> the ALJ's decision is "deemed

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to the public and the news media, unlike federal court proceedings. As noted, many of these differences apply in all administrative proceedings.

<sup>109</sup> 17 C.F.R. § 201.110 (2016).

<sup>110</sup> 17 C.F.R. § 201.100(a) (2016). Ochanpaugh, *supra* note 108, at \*24 n.29 ("[Any] evidence that 'can conceivably throw any light upon the controversy,' at hand should, normally be admitted.") (quoting Jesse Rosenblum, 47 S.E.C. 1065, 1072 (1984)).

<sup>111</sup> 17 C.F.R. §§ 201.232–201.234 (2016). Recently, on July 13, the SEC amended its Rule of Practice governing administrative proceedings. The most significant amendments are that the length of the prehearing period is extended and parties now have the right to limited discovery-type depositions in complex cases. Daniel V. Ward, Jon A. Daniels, & Alexandria Perrin, *Inside SEC's New In-House Court Rules*, Law360 (Aug. 1, 2016, 11:54 AM), <http://www.law360.com/articles/823479/inside-sec-s-new-in-house-court-rules> [<https://perma.cc/G6J6-XPBA>]. The rules take effect for all cases filed after September 27, 2016.

<sup>112</sup> See generally 17 C.F.R. §§ 201.100–201.250 (2016) (Rules of Practice).

<sup>113</sup> § 201.220 (describing content of answers to allegations).

<sup>114</sup> § 201.400(a).

<sup>115</sup> § 201.360(a)(2).

<sup>116</sup> § 201.360(a)(2).

<sup>117</sup> § 201.410. In addition, the SEC can review the matter "on its own initiative." § 201.411(c).

<sup>118</sup> And the SEC does not review an initial order.



the action of the Commission,”<sup>119</sup> and the SEC issues an order making the ALJ’s initial order final.<sup>120</sup>

If either party appeals, the SEC’s review is essentially de novo.<sup>121</sup> If a majority of the participating Commissioners do not agree with the ALJ’s initial decision, the ALJ’s initial decision “shall be of no effect, and an order will be issued in accordance with this result.”<sup>122</sup> If, instead, a majority agree with the ALJ, the SEC will adopt the ALJ’s initial order as its final order.<sup>123</sup> An appealed ALJ decision is not final until the SEC adopts it as final.<sup>124</sup>

If a respondent loses before the SEC, the respondent may petition the appropriate federal court of appeals to review the SEC’s final order.<sup>125</sup> Once an appeal is filed, the court of appeals has “exclusive” jurisdiction “to affirm or modify and enforce or to set aside the order in whole or in part.”<sup>126</sup> For judicial review, the SEC’s findings of facts are “conclusive” “if supported by substantial evidence.”<sup>127</sup>

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<sup>119</sup> 15 U.S.C. § 78d-1(c) (2012).

<sup>120</sup> 17 C.F.R. § 201.360(d)(2) (2016).

<sup>121</sup> §§ 201.411(a), 201.452. Additionally, the Commissioners can allow the parties to submit additional evidence. *Id.* While review is de novo, the SEC accepts the ALJ’s “credibility finding, absent overwhelming evidence to the contrary.” *In re Clawson*, Exchange Act Release No. 48143, 2003 WL 21539920, at \*2 (July 9, 2003); *see also In re Pelosi*, Securities Act Release No. 3805, 2014 WL 1247415, at \*2 (Mar. 27, 2014) (“The Commission gives considerable weight to the credibility determination of a law judge since it is based on hearing the witnesses’ testimony and observing their demeanor. Such determinations can be overcome only where the record contains substantial evidence for doing so.”) (footnote and internal quotation marks omitted).

<sup>122</sup> 17 C.F.R. § 201.411(f) (2016).

<sup>123</sup> 5 U.S.C. § 557(b) (2012).

<sup>124</sup> § 557(b).

<sup>125</sup> 15 U.S.C. § 78y(a)(1) (2012).

<sup>126</sup> § 78y(a)(3).

<sup>127</sup> § 78y(a)(4). The court of appeals may also order additional evidence to be taken before the SEC and remand the action for the SEC to conduct an additional hearing with the new evidence. § 78y(a)(5). The SEC then files its new findings of facts based on the additional evidence with the court of appeals which will be taken as conclusive if supported by substantial evidence. *Id.*

### III. THE CONTROVERSY

Respondents raise two claims under Article II of the U.S. Constitution: (1) the SEC ALJs' appointment violates the Appointments Clause because the ALJs are not appointed by the President, a court of law, or a department head; and (2) the SEC ALJs' multiple for-cause tenure protection violates Article II and separation of powers<sup>128</sup> because the President is not able to faithfully exercise the laws and remove incompetent executive officials. Both of these claims require a court to first find that the SEC ALJs are officers, not employees.<sup>129</sup> If the SEC ALJs are merely employees, neither their appointment nor their removal violates the Constitution.

#### *A. Inferior Officers*

The Appointments Clause of the U.S. Constitution identifies the appointment procedure for two types of officers: principal officers, who are selected by the President with the advice and consent of the Senate, and inferior officers, whom "Congress may allow to be appointed by the President alone, by the heads of departments, or by the Judiciary."<sup>130</sup> No one argues that the ALJs are principal officers;<sup>131</sup> rather, the dispute is whether the SEC ALJs are inferior officers or employees.<sup>132</sup>

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<sup>128</sup> Separation of powers is implied by "the opening sections of Articles I, II, and III of the Constitution, [which] separately and respectively vest 'all legislative Power' in Congress, the 'executive Power' in the President, and the 'judicial Power' in the Supreme Court (and such 'inferior Courts as Congress may from time to time ordain and establish'). In doing so, these provisions imply a structural separation-of-powers principle." *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 515 (2010) (Breyer, J., dissenting) (citing *Miller v. French*, 530 U.S. 327, 341–342 (2000)).

<sup>129</sup> *See, e.g., Gray Fin. Grp., Inc. v. SEC*, 166 F. Supp. 3d 1335 (N.D. Ga. 2015); *Hill v. SEC*, 114 F. Supp. 3d 1297 (N.D. Ga. 2015).

<sup>130</sup> *Buckley v. Valeo*, 424 U.S. 1, 132 (1976); U.S. Const. art. II, § 2, cl. 2.

<sup>131</sup> *See Edmond v. United States*, 520 U.S. 651, 664 (1997) (holding that military appellate judges are inferior officers, not principal officers).

<sup>132</sup> *Hill*, 114 F. Supp. 3d at 1316 (noting that "[t]he issue of whether the SEC ALJ is an inferior officer or employee for purposes of the Appointments Clause depends on the authority he has in ('Whether administrative law judges are necessarily 'Officers of the United States' is disputed.').

## 1. The Supreme Court's Appointment Cases<sup>133</sup>

While there is no bright-line rule dividing principal and inferior officers,<sup>134</sup> the difference between an officer and a non-officer employee depends on whether the employee exercises significant authority pursuant to the laws of the United States.<sup>135</sup> Initially, the Supreme Court divided government employees into two categories: principal officers and inferior officers.<sup>136</sup> The Supreme Court now recognizes a third category: lesser functionaries, or employees.<sup>137</sup> Employees do not exercise significant authority; officers do.<sup>138</sup> When determining whether individuals exercise significant authority pursuant to the laws of the United States, courts consider a variety of factors, including the manner in which Congress created the position, the appointment process, the responsibilities of the position, the tenure and duration of the position, the amount and manner of pay, the level of supervision, and the identity of the supervisor.<sup>139</sup> No one factor is determinative.<sup>140</sup>

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<sup>133</sup> The Supreme Court case law in this area focuses on the difference between principal and inferior officers, rather than the difference between inferior officers and officers. This point makes the analysis difficult.

<sup>134</sup> See Memorandum from Steven G. Bradbury, Acting Assistant Attorney General, Office of Legal Counsel, to the General Counsels of the Executive Branch: Officers of the United States Within the Meaning of the Appointments Clause 3 (Apr. 16, 2007), <https://www.justice.gov/sites/default/files/olc/opinions/2007/04/31/appointmentsclause10.pdf> [<https://perma.cc/7RPQ-L463>] (“[T]he Supreme Court has not articulated the precise scope and application of the [Inferior Officer] Clause’s requirements.”); Eric J. Konecke, The Appointments Clause and Military Judges: Inferior Appointment to a Principal Office, 5 Seton Hall Const. L.J. 489, 492 (1995); John M. Burkoff, Appointment and Removal Under the Federal Constitution: The Impact of Buckley v. Valeo, 22 Wayne L. Rev. 1335, 1347–64 (1976) (describing Supreme Court precedent as “circular” and “not particularly useful”).

<sup>135</sup> Edmond, 520 U.S. at 662 (noting that exercising “significant authority” on behalf of the United States is “the line between [an] officer and non-officer”).

<sup>136</sup> Ex parte Hennen, 38 U.S. 230, 235 (1839) (holding that a law clerk was an inferior officer).

<sup>137</sup> Freytag v. Comm’r, 501 U.S. 868, 881 (1991).

<sup>138</sup> Id. at 881 (quoting Buckley v. Valeo, 424 U.S. 1, 126 n.162 (1976)).

<sup>139</sup> Id. at 880–82; see also Moses Tinchler, Note, Timber! The SEC Falls Hard as the Georgia District Court in Timbervest v. SEC Finds the Appointment of the

Three cases are particularly illustrative. Two consider the status of hearing officers similar to the SEC ALJs; however, the cases reached opposite and inconsistent results.<sup>141</sup> The third directly addressed SEC ALJs.<sup>142</sup> First is the Supreme Court's 1991 decision in Freytag v. Commissioner.<sup>143</sup> Second is the D.C. Circuit Court's 2000 decision in Landry v. FDIC.<sup>144</sup> Third is the D.C. Circuit Court's decision in Raymond J. Lucia Co., Inc. v. SEC.<sup>145</sup>

Freytag was decided first and is, arguably, the most important case because it came from the Supreme Court.<sup>146</sup> In that case, the Supreme Court determined that Tax Court special trial judges (STJ) were inferior officers.<sup>147</sup> The Tax Court is an Article I court with judges who are appointed for limited terms.<sup>148</sup> Congress authorized the Chief Judge of the Tax Court to appoint STJs to hear specific tax cases.<sup>149</sup> For some of these cases the STJ could resolve the case directly, but for other cases, the STJ could only make recommended decisions.<sup>150</sup> In the latter situation, a judge from the Tax Court would review the STJ's recommended decision and make a final decision.<sup>151</sup> Freytag's case was one of the latter, requiring review and adoption by a Tax Court judge.<sup>152</sup>

Freytag challenged the validity of the judgment against him, arguing that the appointment of the STJs by the chief judge of the Tax Court violated the U.S. Federal Constitution's Appointments

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SEC ALJs "Likely Unconstitutional" 67 Mercer L. Rev. 459, 468–70 (2016) (noting that courts use the four-factors test in Morrison, as well as the level of supervision test in Edmond, to determine whether an officer exercises significant authority).

<sup>140</sup> Freytag, 501 U.S. at 880–82.

<sup>141</sup> See id. at 868; Landry v. FDIC, 204 F.3d 1125, 1134 (D.C. Cir. 2000).

<sup>142</sup> Raymond J. Lucia Co., Inc. v. SEC, 832 F.3d 277, 296 (D.C. Cir. 2016).

<sup>143</sup> Freytag, 501 U.S. at 868–922.

<sup>144</sup> 204 F.3d at 1134.

<sup>145</sup> 832 F.3d at 296 (reh'g granted Feb. 16, 2017).

<sup>146</sup> 501 U.S. at 868.

<sup>147</sup> Id. at 881–82.

<sup>148</sup> Id. at 871.

<sup>149</sup> Id. at 870.

<sup>150</sup> Id. at 873.

<sup>151</sup> Id.

<sup>152</sup> Freytag, 501 U.S. at 872.

Clause.<sup>153</sup> The government responded by arguing that the STJs were merely employees who did “no more than assist the regular Tax Court judge in taking the evidence and preparing proposed findings and opinion.”<sup>154</sup> The Justices unanimously rejected this argument and held that the STJs were inferior officers.<sup>155</sup> To hold that the STJs were inferior officers and not merely employees, the Court considered several factors. First, the Court noted that “the office of a special trial judge is ‘established by Law’”<sup>156</sup> and that the statute lays out the “duties, salary, and means of appointment for that office.”<sup>157</sup> The Court noted that “[t]hese characteristics distinguish special trial judges from special masters, who are hired by Article III courts on a temporary, episodic basis, whose positions are not established by law, and whose duties and functions are not delineated in a statute.”<sup>158</sup> In other words, STJs serve more permanently.

Second, the Court focused on the types of duties and level of discretion the STJs had. The STJs “perform more than ministerial tasks. They take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders.”<sup>159</sup> In the course of performing these tasks, the STJs “exercise significant discretion.”<sup>160</sup>

Third, the Court added that “[e]ven if the duties of [STJs] were not as significant as we . . . have found them to be,” there are circumstances where they “exercise independent authority,” and they

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<sup>153</sup> *Id.* at 872.

<sup>154</sup> *Id.* at 880.

<sup>155</sup> The Justices sharply disagreed as to why the appointment process was valid. *See id.* Five justices reasoned that the STJ was an “inferior Officer” whose appointment was proper because the Tax Court could properly appoint an inferior officer as one of “the Courts of Law” under Article II, Section 2, Clause 2. *Id.* at 890–92. The remaining four justices reasoned that the STJ was an “inferior Officer,” but that the Tax Court’s power to make such appoints derived from the fact that it was a Department within the meaning of Article II, Section 2, Clause 2. *Id.* at 892–93 (Scalia, J., concurring).

<sup>156</sup> *Id.* at 881 (citing *Burnap v. United States*, 252 U.S. 512, 516–17 (1920)); *United States v. Germaine*, 99 U.S. 508, 511–12 (1879)).

<sup>157</sup> *Id.* at 880–82 (citing *Burnap*, 252 U.S. at 516-17; *Germaine*, 99 U.S. at 511–512.).

<sup>158</sup> *Freytag*, 501 U.S. at 881.

<sup>159</sup> *Id.* at 881–82.

<sup>160</sup> *Id.* at 882.

cannot be “inferior officers” for some purposes and not others.<sup>161</sup> Fourth, and almost as an aside, the Court pointed out that the STJs were authorized to decide cases in some instances, even if in other instances the STJs only proposed findings and orders, while the regular Tax Court judge rendered the final decision.<sup>162</sup> Notably, the Court specifically rejected the argument that officials who “lack authority to enter into a final decision” must be employees and not inferior officers, because that argument “ignores the significance of the duties and discretion that special trial judges possess.”<sup>163</sup> In sum, the Court held that the STJs could not be inferior officers in some situations and employees in others, finding that the STJs’ limited, final decision-making authority was not determinative.<sup>164</sup>

Despite this relatively clear finding, the D.C. Circuit Court in Landry v. FDIC focused on this factor to distinguish Freytag’s holding from the case that came before that court.<sup>165</sup> In Landry, the D.C. Circuit Court held that Federal Deposit Insurance Corporation (FDIC) ALJs were employees and not inferior officers.<sup>166</sup> The plaintiff in Landry challenged the constitutionality of the FDIC ALJ appointment process.<sup>167</sup> Landry argued that the FDIC ALJ was an inferior officer who could only be appointed by the President, the courts, or the head of a department pursuant to the Appointments Clause.<sup>168</sup> The FDIC ALJ had been appointed by a federal banking agency.<sup>169</sup>

In resolving the inferior officer issue, the court noted that “[t]he line between ‘mere’ employees and inferior officers is anything but bright . . . . In fact, the earliest Appointments Clause cases often

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<sup>161</sup> Id.

<sup>162</sup> Id.

<sup>163</sup> Id. at 881.

<sup>164</sup> Freytag, 501 U.S. at 882.

<sup>165</sup> Landry v. FDIC, 204 F.3d 1125, 1125–44 (D.C. Cir. 2000).

<sup>166</sup> Id. at 1134.

<sup>167</sup> Id. at 1130.

<sup>168</sup> “[The President] . . . shall appoint . . . 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.” U.S. Const. art. II, § 2, cl. 2.

<sup>169</sup> Landry, 204. F.3d at 1130.

employed circular logic, granting officer status to an official based in part upon his appointment by the head of a department.”<sup>170</sup> Next, the court examined and distinguished Freytag, claiming, erroneously, that the Court in that case had “laid exceptional stress on the STJs’ final decision[-]making power.”<sup>171</sup> The Landry majority noted that the STJs had “authority to render the final decision of the Tax Court in declaratory judgment proceedings and in certain small-amount tax cases.”<sup>172</sup> The majority contrasted the FDIC ALJs’ decision-making authority with that of the STJs, noting that the FDIC ALJs issue recommended, not initial, decisions.<sup>173</sup> The FDIC Board of Directors then renders a final decision based on a de novo review of the entire record.<sup>174</sup> Because the FDIC ALJs could only issue recommended decisions, and because final decisions were reserved to the FDIC, the majority held that the FDIC ALJs were employees, not officers.<sup>175</sup>

Judge Randolph concurred in the result, but strongly criticized the majority’s finding that the FDIC ALJs were not inferior officers.<sup>176</sup> He reasoned that the FDIC ALJs were indistinguishable from the STJs based on the reasoning provided in Freytag.<sup>177</sup> Quoting Freytag extensively, Judge Randolph noted that the Supreme Court had placed no particular emphasis on the fact that the STJs had final decision-making authority.<sup>178</sup> Indeed, “the fact that an ALJ cannot render a final decision and is subject to the ultimate supervision of the FDIC shows only that the ALJ shares the common characteristic

<sup>170</sup> Id. at 1132 (citations omitted).

<sup>171</sup> Id. at 1134.

<sup>172</sup> Id. at 1133 (citing Freytag, 501 U.S. at 882) (emphasis in original).

<sup>173</sup> Id. (citing 12 C.F.R. § 308.38).

<sup>174</sup> Id. (citing 12 C.F.R. § 308.40).

<sup>175</sup> Landry, 204 F.3d at 1133.

<sup>176</sup> Id. at 1140 (Randolph, J., concurring).

<sup>177</sup> Id. at 1140–41 (finding that Freytag “cannot be distinguished” because “[t]here are no relevant differences between the ALJ in this case and the [STJ] in Freytag”) (emphasis in original).

<sup>178</sup> Id. at 1142 (noting that the majority’s “first distinction of Freytag is thus no distinction at all”) (emphasis in original). The Supreme Court stated that Tax Court Rule 183, which established the deferential standard, was “not relevant to [its] grant of certiorari,” and noted that it would say no more about the rule than to say that the STJ did not have final authority to decide Petitioner’s case. Freytag v. Comm’r, 501 U.S. 868, 874 n.3 (1991); see also Landry, 204 F.3d at 1142 (Randolph, J., concurring).

of the ‘inferior Officer,’ [because] ‘inferior officers’ are officers whose work is directed and supervised at some level by others who were appointed by Presidential nomination.”<sup>179</sup> Judge Randolph also pointed out that the decisive fact for the majority in Landry—that the FDIC ALJs lack authority to enter final orders—was based on an “alternative holding” from Freytag; the Supreme Court had already determined the STJs were inferior officers before it provided the final-order-authority analysis.<sup>180</sup>

In short, Landry’s holding that the FDIC ALJs were not officers is inconsistent with Freytag and other cases addressing this issue.<sup>181</sup> The Landry majority acknowledged that the FDIC ALJs, like the STJs, were established by law; that their “duties, salary, and means of appointment” were specified by statute; and that they conduct trials, take testimony, rule on evidence admissibility, and enforce discovery compliance.<sup>182</sup> Even though the Supreme Court in Freytag found that the STJs’ exercise of these powers constituted the exercise of “significant authority,” the Landry majority concluded the FDIC ALJs’ exercise of these powers was less important than whether the ALJs had the authority to render a final decision.<sup>183</sup> Despite recognizing that the Supreme Court had “introduced mention of the STJs’ power to render final decisions with something of a shrug,” the D.C. Circuit held that FDIC ALJs were not inferior officers solely

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<sup>179</sup> Landry, 204 F.3d at 1142 (quoting Edmond v. United States, 520 U.S. 651, 663 (1997)).

<sup>180</sup> Id. Despite finding that FDIC ALJs are inferior officers, Judge Randolph also noted there was no violation of the Appointments Clause because (1) the FDIC ALJs were properly appointed by the Office of Thrift Supervision—which may constitute the “head of department” under Article II, and (2) because of the FDIC’s de novo review process, the plaintiff had suffered no prejudice. Id. at 1143.

<sup>181</sup> See, e.g., Edmond v. United States, 520 U.S. 651, 665–66 (1997) (examining a number of factors to hold that judges of Coast Guard Court of Criminal Appeals were inferior officers); Ryder v. United States, 515 U.S. 177, 187–88 (1995) (examining a number of factors to hold that appellate military judges from the Coast Guard Court of Military Review were inferior officers subject to the appointment provisions).

<sup>182</sup> Landry, 204 F.3d at 1133–34 (internal quotations omitted).

<sup>183</sup> Id. at 1133.



because they did not have the power to render final decisions in certain cases.<sup>184</sup>

More recently, the D.C. Circuit compounded its error and gave employer-agencies the power to determine whether its ALJ were employees or inferior officers. In Raymond J. Lucia Co., Inc. v. SEC,<sup>185</sup>—the first of these SEC cases to reach the courts—the D.C. Circuit identified the “main criteria for drawing the line between inferior Officers and employees . . . [as] (1) the significance of the matters resolved by the officials, (2) the discretion they exercise in reaching their decisions, and (3) the finality of those decisions.”<sup>186</sup> The court repeated that the FDIC ALJs in Landry were not inferior officers because they did not meet the third criterion.<sup>187</sup> The court then reasoned that its holding in Landry required it to hold that the SEC ALJs are employees because they too, it concluded, cannot issue final decisions.<sup>188</sup> This holding is incorrect because, as shown above, this reasoning is inconsistent with Freytag; yet, the court suggested that it was bound to follow its precedent regardless of whether Landry and Freytag were consistent.<sup>189</sup>

However, even if the court is correct that the finality of the decision-making authority is the only relevant criterion, this decision is wrong for another reason. As the petitioners argued, the relevant statute specifically provides that an SEC ALJ’s decision “shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission.”<sup>190</sup> Thus, the statutory language provides that the SEC ALJs have statutory authority to make final decisions.

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<sup>184</sup> Id. at 1134; cf. Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd., 684 F.3d 1332, 1339 (D.C. Cir. 2012) (reasoning that the Copyright Royalty Board’s “nonremovability and the finality of its decision[-making] made the officers inferior officers”).

<sup>185</sup> See generally 832 F.3d 277, 277 (D.C. Cir. 2016) (reh’g granted Feb. 16, 2017).

<sup>186</sup> Id. at 284 (quoting Tucker v. Comm’r, 676 F.3d 1129, 1132 (D.C. Cir. 2012) (internal quotation marks omitted)).

<sup>187</sup> Id.

<sup>188</sup> Id. at 285.

<sup>189</sup> Id. (arguing that “to the extent petitioners contend that the approach required by Landry is inconsistent with Freytag or other Supreme Court precedent, this court has rejected that argument and Landry is the law of the circuit”).

<sup>190</sup> 15 U.S.C. § 78d-1(c) (2012).

In other words, Congress authorized the SEC ALJs to have final decision-making authority, and it is congressional intent regarding the status of these officers that is relevant.

In Raymond J. Lucia Co., Inc., the government acknowledged that the statute authorized the SEC ALJs to make final decisions; however, the government countered that the SEC, by rule, chose not to give ALJs this finality decision-making power.<sup>191</sup> The D.C. Circuit adopted this argument noting that, first, the SEC's rules provide that the SEC can take additional time to decide whether it will review an ALJ decision, even when no one requests such review.<sup>192</sup> Second, the SEC's rules provide that when deciding not to order review, the Commission will issue an order indicating that it has decided not to review the ALJ's decision and set a date when any sanctions will take effect.<sup>193</sup> Yet, it is unclear how either of these actions alone, or combined, robs the ALJ's decision of finality. Regardless, even if they did, these are the SEC's rules, not congressional statutes.<sup>194</sup> The SEC simply has no power to turn an inferior officer into an employee by issuing a procedural rule or two.<sup>195</sup> The decision of whether an officer is a principal officer, an inferior officer, or an employee was constitutionally left to Congress, not the agency employing that officer.<sup>196</sup> The D.C. Circuit flipped the power.

In sum, the D.C. Circuit in both Landry and Raymond J. Lucia Co., Inc. misapplied Freytag by concluding that final decision-making authority was the sole criterion for distinguishing between an inferior officer and an employee.<sup>197</sup> The court's holding in both cases is not consistent with Freytag. Moreover, the D.C. Circuit compounded its erroneous reasoning. Even if the court were correct that final decision-making authority alone were the deciding factor,

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<sup>191</sup> 832 F.3d at 285–86.

<sup>192</sup> Id. at 286 (citing 17 C.F.R. § 201.411(c)).

<sup>193</sup> Id. (citing 17 C.F.R. § 201.360(d)(2)).

<sup>194</sup> See generally 17 C.F.R. §201.100.

<sup>195</sup> Cf. Whitman v. Am. Trucking Ass'n, 531 U.S. 457, 486 (2001) (rejecting the lower court's holding that an agency could cure a delegation issue by narrowly interpreting its governing statute).

<sup>196</sup> See U.S. Const. art. 2, § 2, cl. 2.

<sup>197</sup> See Raymond J. Lucia Co., Inc. v. SEC, 832 F.3d 227, 284–85 (reh'g granted Feb. 16, 2017) (citing Landry v. FDIC, 204 F.3d 1125, 1134–35 (D.C. Cir. 2000); Freytag v. Comm'r, 501 U.S. 868, 881 (1991)).

Congress gave such authority to the SEC ALJs.<sup>198</sup> It is immaterial that the SEC may have tried to cabin that authority by issuing procedural rules; the SEC simply has no power to determine what type of officer it hires. In short, these decisions should not control the outcome of whether the SEC ALJs are inferior officers.

In late 2016, the United States Court of Appeals for the Tenth Circuit decided Bandimere v. SEC.<sup>199</sup> Bandimere involved an appeal from an SEC administrative enforcement proceeding presided over by an SEC ALJ. The plaintiff in the case had argued in the underlying enforcement proceeding that the SEC ALJ was an inferior officer and unconstitutionally appointed; however, the SEC rejected that argument.<sup>200</sup> The SEC conceded that if the SEC ALJ were an inferior officer, he would be unconstitutionally appointed.<sup>201</sup> However, the SEC argued that its SEC ALJs are merely employees, not inferior officers.<sup>202</sup>

On appeal, the Tenth Circuit disagreed with the SEC and held that because the SEC ALJ was an inferior officer who was not appointed as the Constitution required, he “held his office unconstitutionally when he presided over Mr. Bandimere’s hearing.”<sup>203</sup> In its reasoning, the majority explained that “[a]lthough the Supreme Court has not stated a specific test for determining whether an employee has inferior officer status, ‘[e]fforts to define [‘inferior Officers’] inevitably conclude that the term’s sweep is unusually broad.’”<sup>204</sup>

Importantly, the majority noted that the Supreme Court’s opinion in Freytag v. Commissioner<sup>205</sup> controlled the result in Bandimere.<sup>206</sup> In Freytag, a unanimous Court had held that the Tax Court’s special trial judges (STJs) were inferior officers and not employees.<sup>207</sup> As

<sup>198</sup> See 15 U.S.C. § 78d-1(c).

<sup>199</sup> --- F.3d ---, No. 15-9586, 2016 WL 7439007 (10th Cir. Dec. 27, 2016).

<sup>200</sup> Id. at \*2.

<sup>201</sup> Id. at \*3 (citing SEC Release No. 9972, 2015 WL 6575665, at \*19).

<sup>202</sup> See id. at \*10.

<sup>203</sup> Id. at \*15.

<sup>204</sup> Id. at \*4 (quoting Free Enterprise Fund, 561 U.S. 477, 539 (2010) (Breyer, J., dissenting)).

<sup>205</sup> 501 U.S. 868 (1991).

<sup>206</sup> Bandimere, 2016 WL 7439007, at \*4.

<sup>207</sup> Id., at \*4-6; Freytag v. Comm’r, 501 U.S. 868 (1991).

noted above, the Court identified three factors for courts to consider when determining whether an employee is an inferior officer: First, whether the position was “established by law;” second, whether “the duties, salary, and means of appointment for that office are specified by statute”; and third, and most importantly, whether the employee exercises significant duties and discretion.<sup>208</sup> Applying those factors to the SEC ALJs, the Bandimere majority concluded that SEC ALJs were inferior officers because the position was established by the Administrative Procedures Act, statutes set forth the SEC ALJs’ duties, salaries, and hiring process, and the “SEC ALJs exercise significant discretion in performing ‘important functions’ commensurate with the STJs’ functions described in Freytag.”<sup>209</sup> The majority concluded:

In sum SEC ALJs closely resemble the STJs described in Freytag. Both occupy offices established by law; both have duties, salaries, and means of appointment specified by statute; and both exercise significant discretion while performing “important functions” that are “more than ministerial tasks.” Further, both perform similar adjudicative functions as set out above. We therefore hold that the SEC ALJs are inferior officers who must be appointed in conformity with the Appointments Clause.<sup>210</sup>

The majority then explicitly rejected the SEC’s argument that Freytag had relied on the STJs’ “final decision-making power” to decide STJs were inferior officers.<sup>211</sup> In doing so, the majority criticized the D.C. Circuit’s decision in Landry v. FDIC,<sup>212</sup> upon which the SEC had relied. The majority noted that the majority

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<sup>208</sup> Id. at \*5 (citing Freytag, 501 U.S. at 881).

<sup>209</sup> Id. at \*8-9 (noting that the SEC ALJs’ exercise of authority included making credibility findings to which the SEC gives “considerable weight;” “shap[ing] the administrative record by taking testimony;” ruling on discovery, admissibility of evidence and dispositive motions; entering default judgments; and issuing initial decisions that publicly “declare respondents liable and impose sanctions”).

<sup>210</sup> Id. at \*9 (citing Freytag, 501 U.S. at 881–82; Samuels, Kramer & Co. v. Comm’r, 930 F.2d 975, 986 (2d Cir. 1991)).

<sup>211</sup> Id. at \*10.

<sup>212</sup> Id.

opinion in Landry misinterpreted Freytag by placing undue weight on final decision-making authority of the STJs.<sup>213</sup>

In contrast, the Bandimere dissent argued that the SEC ALJs' lack of "final decision-making authority," should be determinative. The dissent expressed concern about "the probable consequences" of the majority's holding, in that "all federal ALJs are at risk of being declared inferior officers."<sup>214</sup>

The Tenth Circuit's decision in Bandimere has caused a circuit split, with the decision from the three-judge panel of the D.C. Circuit in Raymond J. Lucia Co., Inc. v. SEC.<sup>215</sup> In that case, the D.C. Circuit applied Landry, rather than Freytag, to hold that because the SEC ALJs do not have final decision making authority, they are employees.<sup>216</sup>

The circuit split may not last long. The D.C. Circuit recently granted the petitioner's petition for rehearing en banc in Raymond J. Lucia Co., Inc. v. SEC.<sup>217</sup> The parties have been directed to brief two issues: (1) whether the SEC administrative law judge who handled the hearing is an inferior officer rather than an employee, and (2) whether the court should overrule Landry.<sup>218</sup> Moreover, on the same date it granted en banc review in Raymond J. Lucia Co., Inc., the D.C. Circuit also granted en banc review in the case of PHH Corp. v. CFPB.<sup>219</sup> In PHH Corp., the

D.C. Circuit had held that an independent agency with a single director head violates Article II of the Constitution.<sup>220</sup> Importantly, one issue to be briefed is what the court should do if it decides in Raymond J. Lucia Co., Inc. that ALJs are inferior officers.<sup>221</sup>

It thus appears likely that the D.C. Circuit will reverse Raymond J. Lucia Co., Inc. and hold that the SEC ALJs are inferior officers. Assuming that the court does so, the SEC will have to reappoint its

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<sup>213</sup> Id.

<sup>214</sup> Id. at \*25 (McKay, C.J., dissenting).

<sup>215</sup> 832 F.3d 277, 283 (D.C. Cir. 2016) (reh'g granted Feb. 16, 2017).

<sup>216</sup> Id. at 283–89.

<sup>217</sup> Id.

<sup>218</sup> Order docketed, No. 15-1345 (D.C. Cir. Feb. 16, 2017).

<sup>219</sup> 839 F.3d 1 (D.C. Cir. 2016) (reh'g granted Feb. 16, 2017).

<sup>220</sup> Id. at \*9.

<sup>221</sup> Order docketed, No. 15-1345 (D.C. Cir. Feb. 16, 2017).

ALJs, this time constitutionally. But two questions remain. First, are the multiple for-cause removal restrictions constitutional, and second, how can the SEC fix the “thousands of [invalid] administrative actions” its unconstitutional ALJs have issued.<sup>222</sup>

Less directly analogous, but still relevant, are the Supreme Court decisions in the military tribunal cases. The Supreme Court issued three opinions, following Freytag but preceding Landry, addressing the Appointments Clause as it relates to judges presiding in military tribunals.<sup>223</sup> The holdings in these cases suggest that officials (other than Article III judges) who preside over government adjudications are inferior officers of the United States.

First, in Weiss v. United States, the plaintiff challenged the appointment of military trial judges who were appointed by the President to be military officers, but who were never appointed to be military trial judges.<sup>224</sup> The Court unanimously held that because the initial appointment of those officers serving as judges was consistent with the Appointments Clause, no reappointment was required.<sup>225</sup> This case did not examine the inferior officer distinction, but merely assumed that the military judges were inferior officers.<sup>226</sup>

Second, in Ryder v. United States, the plaintiff challenged his criminal conviction because the intermediate appellate court (named at that time the Coast Guard Court of Military Review) included two civilian judges whose appointments did not comply with the Appointments Clause.<sup>227</sup> Unlike the trial judges in Weiss, these

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<sup>222</sup> Id., at \*25 (McKay, C.J., dissenting).

<sup>223</sup> Edmond v. United States, 520 U.S. 651, 651 (1997); Ryder v. United States, 515 U.S. 177, 177 (1995); Weiss v. United States, 510 U.S. 163, 163 (1994).

<sup>224</sup> Weiss, 510 U.S. at 170. The parties apparently stipulated that “military judges, because of the authority and responsibilities they possess, act as ‘Officers’ of the United States.” Id. at 169, 173 (stating prior cases “undoubtedly establish the analytical framework upon which to base the conclusion that a military judge is an ‘officer of the United States’—a proposition to which both parties agree”).

<sup>225</sup> Id. at 176. The justices disputed the issue of whether the military judges were “inferior Officers” or “principal officers,” not whether they were employees. See id. at 182–94 (Souter, J., concurring).

<sup>226</sup> Because both parties did not dispute whether military trial judges were officers, the Court simply assumed they were and focused on “whether these officers needed another appointment pursuant to the Appointments Clause before assuming their judicial duties.” Id. at 170.

<sup>227</sup> Ryder, 515 U.S. at 179.

judges were not first appointed as military officers; hence, they were never appointed to a military office in a manner that was consistent with the Appointments Clause.<sup>228</sup> Without further explanation, the Court seemingly agreed with the determination of the Court of Military Appeals that the judges serving on the Coast Guard Court of Military Review were inferior officers who needed to be appointed in accordance with the Appointments Clause.<sup>229</sup> Significantly, the Court made this presumption while disregarding the de facto officer doctrine<sup>230</sup> as well as the fact that the decisions of the appellate judges in question were subject to review by a higher appellate court.<sup>231</sup>

Following the Weiss decision, the Secretary of Transportation corrected the appointments infirmity by “adopting” the civilian judges as his own “judicial appointments.”<sup>232</sup> A few years later, this retroactive adoption-appointment was challenged in Edmond v. United States.<sup>233</sup> In Edmond, the issue was whether military trial judges were principal or inferior officers.<sup>234</sup> The Court concluded these judges were “inferior officers,” because “[g]enerally speaking, the term ‘inferior officer’ connotes a relationship with some higher ranking officer or officers below the President: Whether one is an ‘inferior’ officer depends on whether he has a superior.”<sup>235</sup> Notably, the fact that the military judges’ decisions were subject to reversal on further appeal demonstrated that these judges “have no power to render a final decision on behalf of the United States unless permitted to do so by other Executive officers,” thus making them inferior

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<sup>228</sup> Id. at 187–88.

<sup>229</sup> See id. at 180 (noting that the Court of Military Appeals had relied on its holding in U.S. v. Carpenter, 37 M.J. 291, that military judges are inferior officers).

<sup>230</sup> The de facto officer doctrine is a doctrine that allows courts to validate “acts performed by a person acting under the color of official title even though it is later discovered that the legality of that person’s appointment or election to office is deficient.” Id.

<sup>231</sup> Id. at 187–88.

<sup>232</sup> Edmond v. United States, 520 U.S. 651, 654 (1997).

<sup>233</sup> Id. at 655–56.

<sup>234</sup> Id. at 660–61.

<sup>235</sup> Id. at 662.

officers.<sup>236</sup> In effect, determining the inferior officer status requires more than just looking at whether one holds a “[lower] rank” or “responsibilities of a [lesser] magnitude;” the key is whether one is “directed and supervised at some level by others who were appointed by presidential nomination with the advice and consent of the Senate.”<sup>237</sup> Edmonds provides the litmus test for distinguishing between principal and inferior officers.<sup>238</sup>

## 2. The Department of Justice Opinions

In addition to the case law just described,<sup>239</sup> another relevant source, the Office of Legal Counsel of the Department of Justice (DOJ), has addressed this issue, most recently in April 2007.<sup>240</sup> After extensive analysis, the DOJ concluded that a government employee is a federal officer when that employee has a “continuing position” established by law that involves the application of the sovereign powers of the federal government.<sup>241</sup> “The question for purposes of [this continuing position] is simply whether [the] position possesses delegated sovereign authority to act in the first instance, whether or not that act may be subject to direction or review by superior officers.”<sup>242</sup> According to the DOJ, it is not necessary that employees

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<sup>236</sup> Id. at 665. Justice Souter’s concurrence argued that more factors should be considered in determining whether these judges were principal or inferior officers, but in the end agreed “that the judges . . . are inferior officers within the meaning of the Appointments Clause.” Id. at 667-70 (Souter, J., concurring).

<sup>237</sup> Id. at 663.

<sup>238</sup> See, e.g., Ass’n of Am. R.R. v. United States DOT, 821 F.3d 19, 38 (D.C. Cir. 2016) (relying on Edmond to hold that because the arbitrator is not directed or supervised by anyone, she is a principal officer who must be appointed by the president with the advice and consent of the Senate).

<sup>239</sup> See also Butz v. Economou, 438 U.S. 478, 513 (1978) (“There can be little doubt that the role of the . . . administrative law judge . . . is ‘functionally comparable’ to that of a judge. His powers are often, if not generally, comparable to those of a trial judge: He may issue subpoenas, rule on proffers of evidence, regulate the course of the hearing, and make or recommend decisions.”).

<sup>240</sup> See Bradbury, supra note 134, at 3.

<sup>241</sup> Bradbury, supra note 134, at 1 (“That is, a position, however labeled, is in fact a federal office if (1) it is invested by legal authority with a portion of the sovereign powers of the federal Government, and (2) it is ‘continuing.’”).

<sup>242</sup> Bradbury, supra note 134, at 19.



have discretion or independent authority to be principal or inferior officers.<sup>243</sup> “[T]reating discretion as necessary for the existence of an office conflicts with the original understanding of ‘office,’ early practice, and early precedents.”<sup>244</sup> Citing historic authority, the memo notes that officers “were persons holding sovereign authority delegated from the King that enabled them in conducting the affairs of government to affect the people ‘against [their] will, and without [their] leave.’”<sup>245</sup> In contrast, a person whose position is “purely advisory” or who “provid[es] goods and services” is not an officer.<sup>246</sup>

In addition, in 1991, the DOJ concluded that the Department of Education (DOE) ALJs were inferior officers because of their executive policy-making role.<sup>247</sup> “By deciding a series of cases, the ALJ presumably would develop interpretations of the statute and regulations and fill statutory and regulatory interstices comprehensively with his own policy judgments.”<sup>248</sup> Indeed, to ensure that the DOE ALJs were not principal officers, DOJ reasoned that ALJ “final opinions” must be reviewable by the Secretary.<sup>249</sup>

### 3. The SEC ALJs are Inferior Officers

With this legal background, there should be little doubt that the SEC ALJs are inferior officers. First, like the STJs in *Freytag*, the office of the SEC ALJ and the duties, salary, and means of appointment are all established by law.<sup>250</sup> Moreover, ALJs are permanent employees—unlike special masters.<sup>251</sup>

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<sup>243</sup> Bradbury, *supra* note 134, at 19. (“If it is not necessary to the existence of delegated sovereign authority (and thus to the existence of an office) that a position include the exercise of discretion, all the more is it not necessary that a position include some sort of ‘independent’ discretion in carrying out sovereign functions.”).

<sup>244</sup> Bradbury, *supra* note 134, at 18.

<sup>245</sup> Bradbury, *supra* note 134, at 8 (citing *King v. Burnell*, Carth. 478 (K.B. 1700)) (alteration in original).

<sup>246</sup> Bradbury, *supra* note 134, at 4.

<sup>247</sup> *Sec’y of Educ. Review of Admin. Law Judge Decisions*, 15 U.S. Op. Off. Legal Counsel 8, 14 (1991) [hereinafter *Sec’y of Educ. Review*].

<sup>248</sup> *Id.* at 8, 14.

<sup>249</sup> *Id.* at 15–16.

<sup>250</sup> *See* 5 U.S.C. §§ 556, 557, 3105, 5311; 15 U.S.C. § 78d-1 (establishing ALJs and their duties, salary, and means of appointment). The SEC has argued that

Second, like the STJs, the SEC ALJs perform more than ministerial tasks: they regulate the course of proceedings, control the record of the case, preside over the testimony of witnesses, determine credibility issues, rule on the admissibility of evidence, issue subpoenas, issue sanctions, exclude people (including attorneys)

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the SEC ALJs are employees because the APA does not require the SEC to use the ALJs. *Gray Fin. Grp., Inc. v. SEC*, 166 F. Supp. 3d 1335, 1353 (N.D. Ga. 2015), vacated and remanded, *Hill v. SEC*, 825 F.3d 1236, 1252 (11th Cir. 2016). Likely, the SEC made this argument because Judge Kavanaugh noted this fact in his dissent in *Free Enterprise*. *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 537 F.3d 667, 699 n.8 (D.C. Cir. 2008) (Kavanaugh, J., dissenting) (“[T]here are good reasons the Board and the United States did not cite ALJs as a precedent [for the argument that dual for-cause removal provisions violate separation of powers]. First, an agency has the choice whether to use ALJs for hearings . . . Congress has not imposed ALJs on the Executive Branch.”). However, Judge Kavanaugh made this point to respond to the issue of whether the dual for-cause removal provisions were problematic, not to address whether SEC ALJs were inferior officers. *Id.* And this point does not appear to be relevant to the issue of whether the ALJs exercise significant authority. *See Freytag v. Comm’r*, 501 U.S. 868, 871 (finding STJs to be inferior officers even though the Chief Judge of the Tax Court was not required to use them). The SEC also argued that deference should be given to Congress’s view that the ALJ removal process is constitutional. *Gray*, 166 F. Supp. 3d at 1353–54. However, no deference should be given to congressional choices that violate separation of powers, regardless of whether they are longstanding. *See INS v. Chadha*, 462 U.S. 919, 944–45 (1983) (holding legislative veto to be unconstitutional despite its longstanding use). “[C]ongressional pronouncements are not dispositive . . . for purposes of separation of powers analysis under the Constitution.” *Dep’t of Transp. V. Ass’n of Am. R.R.*, 135 S. Ct. 1225, 1231 (2015). Whether Congress had a longstanding belief that ALJs were employees should not be relevant to this Court in deciding the issues before it. Lastly, the SEC suggested that ALJs are employees because they are placed in the competitive service system. *Gray*, 166 F. Supp. 3d at 1353–54. However, placement in the competitive service system is similarly irrelevant because that system includes all positions in “the Government of the United States . . . including [principal officers] subject to Senate confirmation.” *Free Enter. Fund*, 561 U.S. at 537–38 (Breyer, J., dissenting) (citing 5 U.S.C. §§ 2101, 2102(a)(1)(B), 2014); *cf.* *Com. of Pa., Dept. of Health and Human Services*, 80 F.3d 796, 804 (3d Cir. 1996) (noting that title is not determinative of officer status; rather it is the nature of a position that must be considered). The factors courts consider in making the decision of inferior officer status are identified in *Edmond v. United States*, 520 U.S. 651, 663 (1997); *Freytag*, 501 U.S. at 881–82; *Ryder v. United States*, 515 U.S. 177, 187–88 (1995); *Burnap v. United States*, 252 U.S. 512, 516 (1920); *United States v. Germaine*, 99 U.S. 508, 511–12 (1878). None of these courts considered placement in the civil service system.

<sup>251</sup> *See* 15 U.S.C. § 78d-1(a).

from hearings, enter default judgments, and make substantive rulings and findings.<sup>252</sup> Indeed, the SEC has specifically chosen to give its ALJs as much power as possible under the APA.<sup>253</sup> The SEC ALJs are not merely compiling a hearing record for some higher entity to resolve.

Third, like the STJs, the SEC ALJs exercise significant discretion when carrying out their duties.<sup>254</sup> In short, the SEC ALJs have significant authority and substantial discretion in executing the laws of the United States. Moreover, the SEC ALJs may formulate executive policy because as they decide a series of cases, they interpret statutes and regulations, fill statutory and regulatory interstices, and comprehensively make policy judgments.<sup>255</sup> This finding was essential to the DOJ's conclusion that DOE ALJs were inferior officers.<sup>256</sup>

Fourth, like the STJs, the SEC ALJs exercise powers of the government and have significant discretion in adjudicating enforcement proceedings involving major sanctions. The SEC ALJs' initial decisions regularly can and do become final, although the SEC must act to make them final.<sup>257</sup> Rightly or wrongly, this factor was held to be determinative in Landry.<sup>258</sup> By regulation, the SEC ALJ's initial decision becomes the SEC's final order when there is no review of the initial decision.<sup>259</sup> In fact, in the majority of SEC administrative enforcement proceedings there is no review; thus, the SEC ALJ's initial decision regularly becomes the final order. For

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<sup>252</sup> 17 C.F.R. § 201.111 (authority); 17 C.F.R. § 200.14 (powers); 17 C.F.R. § 201.180 (sanctions).

<sup>253</sup> 17 C.F.R. § 201.111 (“No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. 556, 557.”).

<sup>254</sup> See, e.g., 17 C.F.R. § 201.111 (“The hearing officer shall have the authority to do all things necessary and appropriate to discharge his or her duties.”); 17 C.F.R. § 201.232 (discretion to issue subpoenas); 17 C.F.R. § 201.320 (discretion to receive and exclude evidence); 17 C.F.R. § 201.360 (duty to prepare an initial decision, including “findings and conclusion, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record”).

<sup>255</sup> Sec’y of Educ. Review, supra note 247, at 14.

<sup>256</sup> Id.

<sup>257</sup> See 17 C.F.R. § 201.360; 17 C.F.R. § 201.411.

<sup>258</sup> Landry v. FDIC, 204 F.3d 1225, 1134 (2000).

<sup>259</sup> See 17 C.F.R. § 201.360; 17 C.F.R. § 201.411.

example, in 2014, the SEC ALJs issued 186 initial decisions, of which 174 (approximately 94%) became the SEC's final order.<sup>260</sup> Further, the SEC ALJ decisions are subject to review directly by principal officers, the SEC Commissioners.<sup>261</sup> Although these orders are subject to review by the SEC, case law suggests that being subject to reversal does not render an inferior officer a non-officer employee.<sup>262</sup> Indeed, in the words of Justice Scalia in Edmond, “[W]e think it evident that ‘inferior officers’ are officers whose work is directed and supervised at some level by others who were appointed by presidential nomination with the advice and consent of the Senate.”<sup>263</sup>

In short, the DOJ's opinion, coupled with the Supreme Court decisions in Freytag and the military cases, strongly suggest that the SEC ALJs are “inferior officers.” They appear indistinguishable from military judges, the STJs, and even U.S. magistrates.

In Free Enterprise Fund v. Public Company Accounting Oversight Board, the Supreme Court's majority opinion suggested that whether SEC ALJs were inferior officers was an unresolved, disputed issue.<sup>264</sup> However, “the Court has held that district-court

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<sup>260</sup> See ALJ Initial Decisions: Administrative Law Judges, Securities and Exchange Commission (May 12, 2016), <http://www.sec.gov/alj/aljdec/aljdecarchive/aljdecarc2014.shtml>. [<https://perma.cc/N8DZ-ATV5>].

<sup>261</sup> See 17 C.F.R. § 201.360(d).

<sup>262</sup> See Freytag v. Comm'r, 501 U.S. 868, 881–82 (1991).

<sup>263</sup> Edmond v. United States, 520 U.S. 651, 663 (1997).

<sup>264</sup> 561 U.S. 477, 507 n.10 (2010) (“[O]ur holding does not address that subset of independent agency employees who serve as administrative law judges . . . Whether administrative law judges are necessarily ‘Officers of the United States’ is disputed.”) (citing Landry, 204 F.3d at 1125); accord, Free Enter. Fund, 537 F.3d at 699 n.8 (Kavanaugh, J., dissenting) (stating that “many ALJs are employees, not officers) (citing Landry v. FDIC, 204 F.3d 1125, 1132–34 (D.C. Cir. 2000) (“ALJs in FDIC are employees because they possess only recommendatory powers that are subject to de novo review by agency.”)). Both Justice Roberts and Judge Kavanaugh cite only one case to support their assertions on this issue: Landry. Kavanaugh cites Landry to support his conclusion that “many ALJs are employees, not officers,” Free Enter. Fund, 537 F.3d at 699 n.8 (Kavanaugh, J., dissenting), and Roberts cites Landry to support his assertion that “[w]hether administrative law judges are necessarily ‘Officers of the United States’ is disputed,” Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 507 n.10 (2010). Neither judge cited the Supreme Court's most relevant holding that special trial judges for the tax court

clerks, thousands of clerks within the Treasury and Interior Departments, an assistant surgeon, a cadet-engineer, election monitors, federal marshals, military judges, Article I [Tax Court special trial] judges, and the general counsel for the Transportation Department are inferior officers.”<sup>265</sup> It would not be a stretch to include the SEC ALJs, or all ALJs for that matter, to this list.

### *B. Appointments*

#### 1. The SEC ALJs are Unconstitutionally Appointed

The Constitution provides that “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.”<sup>266</sup> Pursuant to this language, Congress must identify which of these three entities will appoint the SEC ALJs,<sup>267</sup> who are inferior officers.<sup>268</sup> By statute, Congress has identified that each agency or department head shall appoint its ALJs.<sup>269</sup> The SEC is a “Department” of the United States and its Commissioners function collectively as its “Head.”<sup>270</sup> Therefore, the SEC Commissioners must appoint the SEC ALJs.

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are inferior officers. See *Freytag v. Comm’r*, 501 U.S. 868, 869–922 (1991). While neither judge thus suggests that *Landry* resolves this issue, anyone asserting the SEC ALJs are “inferior officers” will need to explain why the reasoning in *Landry* either was wrong or is not relevant to SEC ALJs.

<sup>265</sup> Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 812 (2013) (citing *Free Enter. Fund*, 561 U.S. at 540 (Breyer, J., dissenting) (citing cases)); see also *General Counsel*, Central Intelligence Agency, <https://www.cia.gov/offices-of-cia/general-counsel> [<https://perma.cc/HHC7-WPPF>] (suggesting that the CIA General Counsel is an inferior officer).

<sup>266</sup> U.S. Const. art. II, § 2, cl. 2.

<sup>267</sup> The Appointments Clause applies to all agency officers, including those whose functions are “predominately quasi-judicial and quasi-legislative,” and regardless of whether the agency officers are “independent of the Executive in their day-to-day operations.” *Buckley v. Valeo*, 424 U.S. 1, 133 (1976) (quoting *Humphrey’s Ex’r v. United States*, 295 U.S. 602, 625–26 (1935)).

<sup>268</sup> U.S. Const. art. II § 2, cl. 2.

<sup>269</sup> 5 U.S.C. § 3105 (2012).

<sup>270</sup> *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 511 (2010) (noting that “the common, near-contemporary definition of a ‘department’ as a ‘separate allotment or part of business’ and that even though the SEC was

However, the SEC Commissioners do not appoint the SEC ALJs.<sup>271</sup> Because the SEC ALJs are not appointed pursuant to the identified procedure in Article II, their appointment is unconstitutional.<sup>272</sup> Even the SEC does not dispute that if the SEC ALJs are inferior officers, then the current appointment process likely violates the Constitution.<sup>273</sup> The SEC argues that its ALJs are not inferior officers but mere employees.<sup>274</sup>

## 2. Why the SEC Will Not Fix the Unconstitutional Appointments

There may be a relatively “easy cure” to this constitutional infirmity—the SEC Commissioners could simply appoint the current ALJs directly, as the Secretary of Transportation did after Weiss.<sup>275</sup> However, the SEC has so far refused to take this simple corrective measure.<sup>276</sup> It is unclear why; however, it is possible that the SEC is

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created as an independent agency, “[b]ecause the Commission is a freestanding component of the Executive Branch, not subordinate to or contained within any other such component, it constitutes a ‘Departmen[t]’ for the purposes of the Appointments Clause.”).

<sup>271</sup> Timbervest, LLC v. SEC, No. 1:15-CV-2106-LMM, 2015 U.S. Dist. LEXIS 132082, at \*35 (N.D. Ga. Aug 4, 2015); Transcript of Oral Argument at 25–26, Tilton v. SEC, No. 15-CV-2472 (RA), 2015 U.S. Dist. LEXIS 85015 (S.D.N.Y. June 30, 2015), aff’d 824 F.3d 276 (2d Cir. 2016) (No. 15-CV-2472-RA) [hereinafter Tilton Transcript] (The SEC’s attorney “acknowledge[d] that the commissioners were not the ones who appointed [the ALJ presiding in that case].”).

<sup>272</sup> See Timbervest, 2015 U.S. Dist. LEXIS 132082, at \*35.

<sup>273</sup> Tilton Transcript, supra note 271, at 29 (The judge asked the SEC’s attorney, “If I find that the ALJs are inferior officers, do you necessarily lose?” To which the attorney responded, “We acknowledge that, your Honor, if this Court were to find ALJ Foelk to be an inferior officer, that would make it more likely that the plaintiffs can succeed on the merits for the Article II challenge . . .”).

<sup>274</sup> Hill v. SEC, 114 F. Supp. 3d 1297, 1317 (N.D. Ga. 2015), vacated and remanded 825 F.3d 1236 (11th Cir. 2016) (“[T]he SEC contends ALJs are ‘mere employees’ based upon Congress’s treatment of them and the fact that they cannot issue final orders and do not have contempt power.”); but see Hill v. SEC, 825 F.3d 1236, 1252 (11th Cir. 2016) (“vacat[ing] the district court’s preliminary injunction orders and remand[ing] with instructions to dismiss each case for lack of jurisdiction” because Congress intended “to channel all objections to a final Commission order . . . into the administrative forum.”).

<sup>275</sup> See id. at 1320; Edmond v. United States, 520 U.S. 651, 654 (1997).

<sup>276</sup> Duka v. SEC, No. 15 Civ. 357 (RMB)(SN), 2015 U.S. Dist. LEXIS 124444, at \*65 (S.D.N.Y. Sept. 17, 2015) (referencing its previous decision in

concerned that such an action would be tantamount to an admission that the appointment process was unconstitutional. With such an admission, pending and existing SEC orders could be subject to challenge.

The SEC's concern may have validity. In 2014, the Supreme Court decided NLRB v. Noel Canning.<sup>277</sup> In that case, the Supreme Court held that President Obama improperly appointed three commissioners to the National Labor Relations Board (NLRB) using the recess process.<sup>278</sup> The Court held that the commissioners' appointments were invalid, because the Senate was not in recess when the appointments were made.<sup>279</sup> The Court's decision immediately affected Noel Canning by invalidating the NLRB's decision that that company had engaged in an unfair labor practice.<sup>280</sup> But the Court's holding had a much more significant impact. All the cases the NLRB had resolved in the eighteen-month period between January 4, 2012, (the day the President made the invalid recess appointments) and August 5, 2013, (the day the Senate confirmed nominees for the vacancies) were potentially invalid.<sup>281</sup>

The NLRB's response was swift. The same day the Supreme Court issued its decision, the chair of the NLRB issued a statement noting that the agency would "analyz[e] the impact that the Court's decision has on Board cases in which the January 2012 recess appointees participated."<sup>282</sup> He further emphasized that the NLRB

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Duka v. SEC, No. 15 Civ. 357 (RMB)(SN), 2015 U.S. Dist. LEXIS 100999, at \*8 (S.D.N.Y. Aug. 3, 2015), where the SEC refused to cure the Appointments Clause violation).

<sup>277</sup> 134 S. Ct. 2550, 2550 (2014).

<sup>278</sup> Id. at 2556–57.

<sup>279</sup> Id. (holding that a three day vacancy was too short to be considered a recess).

<sup>280</sup> Mark L. Shapiro et al., The Supreme Court's Noel Canning Decision and the NLRB's Response, Mondaq (July 17, 2014), <http://www.mondaq.com/unitedstates/x/328048/employee+rights+labour+relations/The+Supreme+Courts+Noel+Canning+Decision+and+the+NLRBs+Response> [<https://perma.cc/KSG9-ECMN>] [hereinafter Noel Canning Decision].

<sup>281</sup> Noel Canning Decision, supra note 280.

<sup>282</sup> Statement of NLRB Chairman Mark Gaston Pearce on the Supreme Court's Noel Canning Decision, NLRB Office of Public Affairs (June 26, 2014), <https://www.nlr.gov/news-outreach/news-story/statement-nlr-chairman-mark-gaston-pearce-supreme-courts-noel-canning/> [<https://perma.cc/X528-H5GK>].

“[was] committed to resolving any cases affected by [the Court’s] decision as expeditiously as possible.”<sup>283</sup> Shortly thereafter, the NLRB modified or set aside orders in forty-three cases pending in federal court and filed motions to vacate orders on appeal in forty-nine other pending cases.<sup>284</sup> Additionally, the NLRB promised to reexamine all orders not yet appealed to federal court.<sup>285</sup> Finally, the NLRB had to evaluate whether its appointment of some regional directors and the actions of those regional directors were valid.<sup>286</sup> In sum, the short-term and long-term consequences of the Noel Canning decision were far more complex than the Court likely anticipated when it claimed that its holding would not “render illegitimate thousands of recess appointments reaching all the way back to the founding era.”<sup>287</sup> Moreover, the aftermath of Noel Canning was not the first time the NLRB had to revisit the validity of its orders. In 2010, in New Process Steel, L.P. v. NLRB, the Supreme Court held that the NLRB lacked authority to issue orders without a quorum.<sup>288</sup> In response, the NLRB simply re-issued all of the orders that had been issued by the two-member panels.<sup>289</sup>

In these two instances, the timeframes and, hence, the number of affected orders, were relatively small. If a court concludes that the SEC is appointing its ALJs in a manner that violates the Constitution, the impact will likely be more substantial. It is unclear how long the SEC has been appointing its ALJs in this manner and, thus, how many orders pending and issued would be potentially invalid.<sup>290</sup> Thus, the SEC may rightly be concerned with appearing to concede

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<sup>283</sup> Id.

<sup>284</sup> Noel Canning Decision, supra note 280.

<sup>285</sup> Id.

<sup>286</sup> Id.

<sup>287</sup> NLRB v. Noel Canning, 134 S. Ct. 2550, 2577 (2014).

<sup>288</sup> 560 U.S. 674, 676 (2010).

<sup>289</sup> Noel Canning Decision, supra note 280.

<sup>290</sup> The SEC has so far refused to answer discovery regarding how long it has been appointing its ALJs in such manner and how many orders these potentially unconstitutional ALJs have issued. See Why the SEC’s Proposed Changes to Its Rules of Practice Are Woefully Inadequate—Part III, Securities Diary (Nov. 18, 2015), <https://securitiesdiary.com/2015/11/18/why-the-secs-proposed-changes-to-its-rules-of-practice-are-woefully-inadequate-part-iii/> [https://perma.cc/2LAH-W9FH].



that its appointment process is unconstitutional or even trying to fix something the SEC does not believe to be broken; the potential impact could be staggering.<sup>291</sup>

### C. Removal

While the Constitution explicitly provides for the appointment of principal and inferior officers, it does not explicitly provide for their removal in most situations.<sup>292</sup> Rather, the Constitution contains only one removal provision. That provision states that “all civil Officers of the United States shall be removed from Office on Impeachment for,

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<sup>291</sup> Alternatively, the SEC Commissioners may take another approach. In *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 684 F.3d 1332 (D.C. Cir. 2012), the D.C. Circuit held that three copyright royalty judges who comprised the Copyright Royalty Board were unconstitutionally appointed. The court resolved the unconstitutionality problem by severing the statutory provision that authorized the Librarian of Congress power to remove the judges. *Id.* at 1336–37, 1340. Because the judges were not validly appointed at the time they issued the challenged determination, the court vacated and remanded without reaching the merits of *Intercollegiate's* challenge. *Id.* at 1332. After remand, the Librarian appointed new copyright royalty judges, who reviewed the existing, written record to resolve the remanded case. *Intercollegiate Broad. Sys., Inc. v. Copyright Royalty Bd.*, 796 F.3d 111 (D.C. Cir. 2015). The new judges refused to reopen that record, allow additional submissions, or conduct new hearings because The Board decided not to hold new evidentiary hearings because *Intercollegiate* had “fail[ed] . . . to point to any instance of an exclusion of relevant evidence that affected the outcome of the proceeding, or to any portion of the Final Determination that turned on witness credibility.” *Id.* at 116. The D.C. Circuit found “nothing in the proceedings leading up to and including the new Board's determination that suggests a lack of independence from the previous, constitutionally defective determination” and held that review of the existing, written record by the properly-appointed panel was sufficient in this case. *Id.* at 123. Cf., *Doolin Sec. Sav. Bank v. Office of Thrift Supervision*, 139 F.3d 203, 212-14 (D.C. Cir. 1998) (holding that the temporary director of OTS, who was validly appointed, ratified an order issued by an improperly appointed “acting director”); *FEC v. Legi-Tech, Inc.*, 75 F.3d 704, 709 (D.C. Cir. 1996) (holding that the remedy of dismissal was not warranted by FEC’s unconstitutional composition when the FEC reconstituted itself after the finding of unconstitutionality and potentially “rubberstamp[ed]” its prior decision).

<sup>292</sup> *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 516 (2010) (Breyer, J., dissenting) (“[W]ith the exception of the general ‘vesting’ and ‘take care’ language, the Constitution is completely ‘silent with respect to the power of removal from office.’”) (quoting *Ex parte Hennen*, 38 U.S. 230, 258 (1839)).

and Conviction of, Treason, Bribery, or other high Crimes and Misdemeanors.”<sup>293</sup> The impeachment process is seldom used.<sup>294</sup> Officers are removed other than by impeachment.<sup>295</sup> How is removal possible? Because the Constitution did not “expressly take[] away” the removal power from the President, the President is presumed to have this power to oversee executive officers.<sup>296</sup>

Because the President’s ability to remove an officer is an important means of controlling that officer,<sup>297</sup> the removal power compliments the appointment power.<sup>298</sup> The power is not absolute; Congress may limit the President’s removal power to ensure an officer’s independence.<sup>299</sup> The clash between the executive’s desire for unfettered removal power and the legislature’s desire to limit such power impacts separation of powers—the doctrine that helps to ensure that each governmental branch maintains its own separate function.<sup>300</sup> Congress has limited the President’s ability to remove the

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<sup>293</sup> U.S. Const. Art. II, § 4.

<sup>294</sup> William F. Funk & Richard H. Seamon, *Administrative Law* 60–61 (5th ed. 2016).

<sup>295</sup> *Id.* at 61.

<sup>296</sup> *Free Enter. Fund*, 561 U.S. at 492 (citing Letter from James Madison to Thomas Jefferson (June 30, 1789), in 16 *Documentary History of the First Federal Congress of the United States of America, June-August 1789*, 893 (Charlene Bangs Bickford ed., 2004)).

<sup>297</sup> Funk & Seamon, *supra* note 294, at 60.

<sup>298</sup> Long ago in *Myers v. United States*, the Court struck down a statute that required the President to obtain the advice and consent of the Senate prior to removing the postmaster general. 272 U.S. 52, 107–08, 118, 176 (1926). According to the Court, the power to remove a federal officer necessarily accompanied the constitutionally granted power to appoint that officer. *Id.* at 122, 126–27, 163–64. The power to remove did not flow from the constitutionally granted power to advise on and consent to that appointment. *Id.*

<sup>299</sup> The Court in *Humphrey’s Executor v. United States*, for example, upheld a removal provision limiting the President’s ability to remove a commissioner of the Federal Trade Commission (FTC) for “inefficiency, neglect of duty, or malfeasance in office,” in part because the FTC was designed to be independent and free from domination and control of the President. 295 U.S. 602, 619, 629, 632 (1935); *accord* *Morrison v. Olson*, 487 U.S. 654, 693 (1988) (noting that “the congressional determination to limit the removal power of the Attorney General was essential . . . to establish the necessary independence of the office”).

<sup>300</sup> M. Elizabeth Magill, *The Real Separation in Separation of Powers Law*, 86 *Va. L. Rev.* 1127, 1132–33 (2000).

SEC ALJs by providing for multiple levels of for-cause removal protection. The question is whether Congress can do so without violating separation of powers.

### 1. The Supreme Court's Removal Cases

Likely because the Constitution does not explicitly define the executive's power to remove officers, the Supreme Court has proffered conflicting direction in the cases it has examined since Marbury v. Madison.<sup>301</sup> The Supreme Court<sup>302</sup> first addressed the validity of executive removal in 1839 in Ex parte Hennen.<sup>303</sup> In Hennen, an inferior officer sought mandamus after he was removed from his position as a district court clerk.<sup>304</sup> The Court rejected the clerk's argument that his removal was unconstitutional under Article II.<sup>305</sup> The relevant statute contained no removal limitation, and the Court refused to imply one.<sup>306</sup> Silence, the Court held, meant that the executive retained full removal power.<sup>307</sup> The Court reasoned that when Congress fails to provide for removal of inferior officers,

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<sup>301</sup> 5 U.S. 137, 162 (1803) (“[A]s the law creating the office [of justice of the peace] gave the officer a right to hold it for five years, independent of the executive, the appointment was not revocable; but vested in the officer legal rights, which are protected by the laws of this country.”). The Court subsequently rejected this statement as obiter dictum in Myers v. United States, 272 U.S. 52, 141 (1926).

<sup>302</sup> While state supreme courts had addressed this issue, this case is the first where the U.S. Supreme Court discussed executive removal. See, e.g., Avery v. Inhabitants of Tyringham, 3 Mass. 160, 176–77 (1807).

<sup>303</sup> Ex parte Hennen, 38 U.S. 230 (1839).

<sup>304</sup> Id. at 256.

<sup>305</sup> Id. at 261–62.

<sup>306</sup> See id. at 258–59 (While the 1st section of the Act of May 18, 1820, 3 Story, 1790 did limit the tenure of certain officers to a four-year term: “[C]lerks of Courts are not included within this law, and there is no express limitation in the Constitution, or laws of Congress, upon the tenure of the [clerks’] office.” Thus, because the tenure for the office of clerks is not fixed, these officers are “removable at pleasure.”).

<sup>307</sup> See id. at 258–59 (maintaining that because “[t]he Constitution is silent with respect to the power of removal from office, where the tenure is not fixed,” the tenure of the clerks’ office “must be held at the will and discretion of some department of the government, and subject to removal at pleasure,” and “although no power to remove is expressly given, yet there can be no doubt, that these clerks hold their office at the will and discretion of the head of the department”).

because (1) the Constitution likely does not intend those officers to hold term for life,<sup>308</sup> (2) the power of removal is incidental to the power of appointment,<sup>309</sup> and (3) “[t]he appointment of clerks of the court properly belongs to the courts of law,” the courts would also have removal power.<sup>310</sup> Hence, Hennen was out of luck.

Similarly, in Parsons v. United States, the Court again refused to imply a removal limitation in a statute that did not contain one.<sup>311</sup> In this case, the Court held that Congress had not intended to limit the President’s power to remove an inferior officer, a district attorney.<sup>312</sup> The relevant statute provided that “[d]istrict attorneys shall be appointed for a term of four years” and did not contain any provision addressing removal.<sup>313</sup> Like it had in Hennen,<sup>314</sup> the Court refused to imply a removal limitation.<sup>315</sup> In refusing to imply the removal limitation, the Court iterated the long understanding of both Congress and the executive that the removal power was an inherent power of the executive.<sup>316</sup> The Court then described the well-known battle over the first Tenure of Office Act, which had prohibited the executive from exercising any removal without the advice and consent of the Senate.<sup>317</sup> Despite the fact that the Tenure of Office Act had been repealed before Parsons was appointed,<sup>318</sup> the Court examined the statute’s drafting history and applied the constitutional avoidance canon, refusing to imply any limitation on the executive’s removal power.<sup>319</sup>

In the statutes at issue in Hennen and Parsons, Congress did not expressly limit the removal power of the entity appointing the

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<sup>308</sup> Id. at 259.

<sup>309</sup> Hennen, 38 U.S. at 259.

<sup>310</sup> Id. at 258.

<sup>311</sup> Parsons v. United States, 167 U.S. 324, 338–39 (1897).

<sup>312</sup> Id.

<sup>313</sup> See id. at 327–28.

<sup>314</sup> See Hennen, 38 U.S. at 258–59.

<sup>315</sup> Parsons, 167 U.S. at 343.

<sup>316</sup> Id.

<sup>317</sup> With first Tenure of Office Act, Congress attempted to prevent the President from removing officers “friendly to the views of congress.” Id. at 339 (citing Tenure of Office Act, ch. 154, 14 Stat. 430 (1867)).

<sup>318</sup> Id. at 342.

<sup>319</sup> Id. at 343.

inferior officers; hence, the Supreme Court refused to imply such a limitation in either statute. In contrast, in United States v. Perkins, the Court reviewed a statute in which Congress had included a removal limitation in the statute.<sup>320</sup> In Perkins, a naval cadet, an inferior officer, was honorably discharged because his services were no longer required during peacetime.<sup>321</sup> He sued for accrued salary.<sup>322</sup> The relevant statutes barred his peacetime discharge except “for misconduct.”<sup>323</sup> The issue for the Court was whether Congress could limit the executive’s removal authority in this way when appointment was vested in the head of a department rather than in the President.<sup>324</sup> The Court held that Congress could impose removal limits under these circumstances.<sup>325</sup> According to the Court, when Congress “vests the appointment of inferior officers in the heads of departments, it may limit and restrict the power of removal as it deems best for the public interest.”<sup>326</sup> In other words, Congress’s power to vest appointments in an entity other than the executive provided Congress with the concomitant power to limit that entity’s removal capabilities.<sup>327</sup> Notably, the President retained removal power over the department head: the Secretary of the Navy.<sup>328</sup>

These early cases provided a framework for removal: the Court’s holdings in Hennen and Parsons suggest that because the power to remove accompanies the power to appoint, the Court will not imply removal limitations in statutes that do not contain them. In other words, Congress must provide a clear statement that the executive’s

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<sup>320</sup> 116 U.S. 483, 483–84 (citing Army Appropriation Act of July 13, 1866, ch. 176, 14 Rev. Stat. 90 (1866)).

<sup>321</sup> See id. at 483.

<sup>322</sup> Id.

<sup>323</sup> Id. at 485 (citing Act of Aug. 5, 1882, §§ 1229, 1525, 22 Rev. Stat. 219).

<sup>324</sup> Id. at 484 (“Whether or not Congress can restrict the power of removal incident to the power of appointment of those officers who are appointed by the President by and with the advice and consent of the Senate, under the authority of the Constitution (article 2, section 2) does not arise in this case, and need not be considered.”).

<sup>325</sup> Id. at 485.

<sup>326</sup> Perkins, 116 U.S. at 485.

<sup>327</sup> Id.

<sup>328</sup> Id. (the head of the department is the Secretary of the Navy); see Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 494, 494 n.3 (2010).

removal power is limited because no limitation will be implied. In addition, the Court's holding in Perkins suggests that when Congress explicitly includes removal limitations, the Court will uphold them, at least when someone other than the executive holds appointment power. Notably, in all of these cases, the Court examined the legitimacy of removal restrictions regarding inferior officers; the Court had yet<sup>329</sup> to address the legitimacy of removal limitations regarding principal officers.

In 1926, in Myers v. United States, the Court addressed that issue: whether the President has unfettered power under the Constitution to remove officers "whom he has appointed by and with the advice and consent of the Senate."<sup>330</sup> Plaintiff Myers was appointed to be a postmaster in Portland, Oregon, for a four-year term.<sup>331</sup> Before the term's conclusion, the President removed him.<sup>332</sup> Myers sued for his salary from the date of removal.<sup>333</sup> The relevant statute provided, "Postmasters of the first, second, and third classes shall be appointed and may be removed by the President by and with the advice and consent of the Senate, and shall hold their offices for four years unless sooner removed or suspended according to law."<sup>334</sup> The Senate had not consented to Myers's removal.<sup>335</sup> The issue for the Court was whether the removal limitation (requiring the advice and consent of the Senate) was constitutional.<sup>336</sup> But a threshold issue also had to be addressed: was Myers a principal or inferior officer?

The Court suggested, without really deciding, that Myers was a principal officer.<sup>337</sup> The Court reasoned that because Congress vested appointment of postmasters in the President with the advice and

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<sup>329</sup> In United States ex rel. Goodrich v. Guthrie, the issue of whether the President had the power to remove a territorial judge was argued but not decided. 58 U.S. 284, 302–03 (1845).

<sup>330</sup> Myers v. United States, 272 U.S. 52, 106 (1926).

<sup>331</sup> Id.

<sup>332</sup> Id.

<sup>333</sup> Id.

<sup>334</sup> Id. at 107 (citing Act of July 12, 1876, ch. 179, 19 Stat. 78, 80, 81).

<sup>335</sup> Id. at 107–08.

<sup>336</sup> Myers, 272 U.S. at 107–08.

<sup>337</sup> Id. at 158–65.

consent of the Senate, the postmaster must be a principal officer.<sup>338</sup> This circular reasoning is likely incorrect. Like principal officers, Congress has the power to vest the appointment of inferior officers in the President subject to the Senate's advice and consent.<sup>339</sup> Unlike principal officers, Congress also has the power to vest the appointment of inferior officers in courts of law and heads of departments instead.<sup>340</sup> Hence, the method of appointment should not dictate whether an officer is principal or inferior. Regardless, the Court understood Myers to be a principal officer.

The Court then held that Congress could not limit the executive's removal power to remove officers exercising executive powers.<sup>341</sup> To reach its holding, the Court examined in excruciating detail<sup>342</sup> the views of the first Congress<sup>343</sup> regarding the nature of the executive power and the importance of the take care clause.<sup>344</sup> The Court concluded that for the President to have "confidence in the intelligence, ability, judgment or loyalty of [his executive subordinates,] he must have the power to remove him without delay."<sup>345</sup> To require the President to file for-cause charges and submit those charges to the Senate "might make impossible that unity

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<sup>338</sup> *Id.* at 163 (quoting *Shurtleff v. United States*, 189 U.S. 311, 315 (1903) ("Congress has regarded the office as of sufficient importance to make it proper to fill it by an appointment to be made by the President and confirmed by the Senate. It has thereby classed it as appropriately coming under the direct supervision of the President and to be administered by officers appointed by him (and confirmed by the Senate) with reference to his constitutional responsibility to see that the laws are faithfully executed. Art. 2, sec. 3.") (internal quotation marks omitted)).

<sup>339</sup> U.S. Const. art. II, § 2, cl. 2.

<sup>340</sup> *Id.*

<sup>341</sup> *Myers*, 272 U.S. at 163–64.

<sup>342</sup> Or, as noted in a later case, "These opinions examine at length the historical, legislative, and judicial data bearing upon the question, beginning with what is called 'the decision of 1789' in the first Congress and coming down almost to the day when the opinions were delivered. They occupy 243 pages of the volume in which they are printed." *Humphrey's Ex'r v. United States*, 295 U.S. 602, 626 (1935).

<sup>343</sup> Compare *Myers*, 272 U.S. at 109–35, with *Parsons v. United States*, 167 U.S. 324, 327–34 (1897) (describing the same history in fewer pages).

<sup>344</sup> *Myers*, 272 U.S. at 108–09. The Court also cited the Commander in Chief Clause, the Appointments Clause, the Impeachment Clause, and the Faithfully Execute Clause. *Id.* at 108–09 (citing U.S. Const. art. II, §§ 2, 3, 4).

<sup>345</sup> *Id.* at 134.

and coordination in executive administration essential to effective action.”<sup>346</sup>

But the Court did not stop there. Expansively, the Court extended its reasoning to officers exercising quasi-adjudicatory powers as well:

Of course, there may be duties so peculiarly and specifically committed to the discretion of a particular officer as to raise a question whether the President may overrule or revise the officer’s interpretation of his statutory duty in a particular instance. Then there may be duties of a quasi-judicial character imposed on executive officers and members of executive tribunals whose decisions after hearing affect interests of individuals, the discharge of which the President cannot in a particular case properly influence or control. But even in such a case he may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised. Otherwise he does not discharge his own constitutional duty of seeing that the laws be faithfully executed.<sup>347</sup>

According to the majority, the President’s unfettered removal power thus flowed from the President’s “constitutional duty of seeing that the laws be faithfully executed.”<sup>348</sup> Hence, even in the case of quasi-judicial officers, the President must retain the power to remove those below him.

The Court’s reliance on the Take Care Clause gave the dissent pause. As if foreshadowing the current controversy regarding the SEC ALJs, Justice Holmes warned that “arguments drawn from the executive power of the President, and from his duty to appoint officers of the United States (when Congress does not vest the appointment elsewhere), to take care that the laws be faithfully

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<sup>346</sup> Id.

<sup>347</sup> Id. at 135.

<sup>348</sup> Id.



executed, and to commission all officers of the United States, seem to [be] spider's webs inadequate to control the dominant facts."<sup>349</sup>

The Court's holding and reasoning in Myers was consistent with the Court's holdings and reasoning in Hennen and Parsons, in which the Court had refused to imply removal restrictions because of the inherent power of the executive to remove officers. However, the Court's holding and reasoning in Myers was inconsistent with the Court's holding and reasoning in Perkins, in which the Court had upheld an express removal provision. To explain the different outcome, the Court could have distinguished the plaintiff in Perkins because he was an inferior officer. Indeed, Justice Roberts later suggested in Free Enterprise that the nature of the officer's status was determinative in these early removal cases.<sup>350</sup> Justice Roberts was incorrect.<sup>351</sup>

Instead, the Myers Court distinguished Perkins not by focusing on the inferior nature of the officer in that case, but by focusing on who held the removal power.<sup>352</sup> In Myers, Congress had retained some removal power for itself; in contrast, in Perkins, Congress merely placed "incidental" restrictions (for-cause removal during peacetime) on the head of a department's ability to remove an officer.<sup>353</sup> Such incidental restrictions on the executive were legitimate, the Court reasoned, because Congress did not aggrandize its own power at the expense of the Executive.<sup>354</sup> The Court underscored that it had never allowed Congress "to draw to itself, or

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<sup>349</sup> Id. at 177 (Holmes, J., dissenting).

<sup>350</sup> Free Enter. Fund. v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 510 (2010) (holding that "the Board members are inferior officers," because the Commission has the power to remove Board members "at will").

<sup>351</sup> See generally, Peter L. Strauss, On the Difficulties of Generalization - Pcaobi N the Footsteps of Myers, Humphrey's Executor, Morrison, and Freytag, 32 Cardozo L. Rev. 2255 (2011) (criticizing Free Enterprise).

<sup>352</sup> According to the Court in Myers, whether an officer is principal or inferior should have no bearing on whether the limitation on the President's removal power is constitutional; rather, the focus should turn to who holds this power in compliance with the Constitution. See Myers, 272 U.S. at 164–76. So even though the Court may have incorrectly held that the postmaster in that case was a principal officer, when in all likelihood he was inferior, this difference did not matter to the Court. See id. at 160–61.

<sup>353</sup> Myers, 272 U.S. at 161.

<sup>354</sup> Id.

to either branch of it, the power to remove or the right to participate in the exercise of [the removal] power. To do this would be to go beyond the words and implications of that clause, and to infringe the constitutional principle of the separation of governmental powers.”<sup>355</sup> Hence, when Congress vests appointment power in an entity other than the President, Congress can place for-cause restrictions on that entity’s power to remove an officer. However, when Congress gives itself a role in the President’s power to remove an officer, Congress crosses the line.

The majority’s holding in Myers soon proved to be too broad. In 1935 in Humphrey’s Executor v. United States, the Court retreated from this broad description of the President’s removal power.<sup>356</sup> The relevant act in Humphrey’s Executor established the Federal Trade Commission (FTC), an independent agency, and contained a for-cause removal provision.<sup>357</sup> That provision limited the President from removing an FTC Commissioner unless for “inefficiency, neglect of duty, or malfeasance in office.”<sup>358</sup> The FTC Commissioners are principal officers.<sup>359</sup> Like it did in Myers, however, the Court ignored the distinction between principal and inferior officers.

Despite the language in Myers suggesting that the President’s removal power was sacrosanct, the Court upheld the for-cause removal limitation in Humphrey’s Executor.<sup>360</sup> In doing so, the Court acknowledged that the language quoted above regarding quasi-judicial officers might suggest that the for-cause removal provision was unconstitutional.<sup>361</sup> But the Court rejected the language as dicta.<sup>362</sup> Instead, Myers, the Court said, was distinguishable in a

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<sup>355</sup> Id.

<sup>356</sup> Humphrey’s Ex’r v. United States, 295 U.S. 602, 632 (1935).

<sup>357</sup> The Federal Trade Commission Act, ch. 311, 38 Stat. 717 (1914) (codified as amended at 15 U.S.C. §§ 1, 41).

<sup>358</sup> Humphrey’s Ex’r, 295 U.S. at 620 (quoting The Federal Trade Commission Act, c. 311, 38 Stat. 717 (1914) (codified as amended at 15 U.S.C. §§ 1, 41)).

<sup>359</sup> While the Court did not expressly state that the FTC Commissioners are principal officers, it was implied because under The Federal Trade Commission Act, 15 U.S.C. §§ 41, 42, all Commissioners must be appointed by the President with the advice and consent of the Senate. See id. at 619–20

<sup>360</sup> Id. at 632.

<sup>361</sup> Id. at 632; see supra text accompanying note 347.

<sup>362</sup> Humphrey’s Ex’r, 295 U.S. at 627–28.

number of ways.<sup>363</sup> The most critical difference between the two cases was the type of power the officers exercised.<sup>364</sup> The Court noted that the postmaster in Myers had performed purely executive functions and, therefore, had to be responsive to the President.<sup>365</sup> Myers had no quasi-legislative or quasi-judicial power.<sup>366</sup>

In contrast, the FTC Commissioners in Humphrey's Executor performed both quasi-legislative and quasi-judicial powers.<sup>367</sup> The Court reasoned that the power the FTC Commissioners exercised required that they be independent from the President.<sup>368</sup> Thus, the Court expressly limited Myers, saying that Myers did not apply to “an officer who occupies no place in the executive department and who exercises no part of the executive power vested by the Constitution in the President.”<sup>369</sup>

In addition to considering the nature of the officer's powers, the Court highlighted two other important differences between Myers and Humphrey's Executor. First, the Court pointed out that Congress had intended the FTC and its Commissioners to be independent from the President, unlike the post office and postmasters.<sup>370</sup> Second, the Court noted that the FTC Commissioners' tenure was limited to seven years.<sup>371</sup> Both factors further supported the legitimacy of the

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<sup>363</sup> Id. at 627.

<sup>364</sup> Id. at 631–32.

<sup>365</sup> Id.

<sup>366</sup> Id. at 627.

<sup>367</sup> Id. at 626, 628 (expressly “disapprov[ing]” statements in Myers that suggested that the President had an inherent constitutional power to remove members of quasi-judicial bodies).

<sup>368</sup> Humphrey's Ex'r, 295 U.S. at 627–28 (“A postmaster is an executive officer restricted to the performance of executive functions. He is charged with no duty at all related to either the legislative or judicial power. The actual decision in the Myers case finds support in the theory that such an officer is merely one of the units in the executive department and, hence, inherently subject to the exclusive and illimitable power of removal by the Chief Executive, whose subordinate and aid he is.”).

<sup>369</sup> Id. at 628.

<sup>370</sup> Id. at 628–30.

<sup>371</sup> Id. at 623–34; but see Shrutteliff v. United States, 189 U.S. 311, 316 (1903) (holding that while an inferior officer had limited tenure, Congress had not explicitly intended to limit the President's general removal power). Note that the

removal limitations. Thus, the Court limited the Myers holding: no longer did the President have unfettered authority to remove all officers. After Humphrey's Executor, the President had unfettered authority to remove "all purely executive officers."<sup>372</sup> Pursuant to what we will call the Myers/Humphrey's distinction, Congress may not limit a President's power to remove purely executive officers, but Congress may limit his power to remove quasi-legislative and quasi-judicial officers, especially when such officers' tenure is time-limited.<sup>373</sup>

The Myers/Humphrey's distinction held firm for half a century. For example, in 1958, the Court applied this distinction in Wiener v. United States, to hold that Congress could limit the President's power to remove a member of the War Claims Commission.<sup>374</sup> Wiener refused to resign when asked to do so by President Eisenhower.<sup>375</sup> Wiener filed suit in the Court of Claims to recover his unpaid salary.<sup>376</sup> The relevant act provided that the commissioners had very limited tenure (three years).<sup>377</sup> The act did not have an explicit removal provision.<sup>378</sup> The issue for the Court was whether the act contained an implied for-cause removal provision.<sup>379</sup> You will recall that the Court had refused in Hennen and Parsons to imply for-cause

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limited tenure of the officer had also played no role in the Court's decision in Hennen, Parsons, and Myers.

<sup>372</sup> Humphrey's Ex'r, 295 U.S. at 628.

<sup>373</sup> Id. at 631–32; Myers v. United States, 272 U.S. 52, 127–28 (1926). Some commentators have suggested that the Court in Humphrey's Executor used a functionalist approach. See, e.g., Steven G. Calabresi & Joan L. Larsen, One Person, One Office: Separation of Powers or Separation of Personnel?, 79 Cornell L. Rev. 1045, 1109 n.321 (1994). We are not so sure. At best, the Court may have approached the separation of powers question from a functionalist approach (asking how it could uphold the limitation), then crafted a formalist bright-line rule for future cases. However, the Court based its distinction of the legitimacy of the removal restriction on the type of power the officer exercised. Myers, 272 U.S. at 134–35. Such a distinction is classically formalist.

<sup>374</sup> Wiener v. United States, 357 U.S. 349, 356 (1958).

<sup>375</sup> Id. at 350.

<sup>376</sup> Id.

<sup>377</sup> Id.

<sup>378</sup> Id.

<sup>379</sup> Id. at 351 (noting that the issue was a "variant of the constitutional issue decided in [Humphrey's Executor]").

removal limitations, but upheld an express removal provision in Perkins.<sup>380</sup> Had the Court followed those three cases, the Court would have required Congress to limit removal expressly.<sup>381</sup> However, the Court did not cite Hennen, Parsons, or Perkins. Additionally, the Court did not discuss whether the War Claims Commissioners were principal or inferior officers and whether this difference mattered to its holding.<sup>382</sup>

Instead, the Court cited Myers and Humphrey's Executor.<sup>383</sup> The Court noted that Humphrey's Executor had limited Myers's holding to apply only to “purely executive officers.”<sup>384</sup> The War Claims Commission was a quasi-adjudicatory body, and Congress intended for the commissioners to be “‘entirely free from the control or coercive influence, direct or indirect,’ of either the Executive or the Congress.”<sup>385</sup> The Court assumed that Congress, when it enacted the relevant statute,<sup>386</sup> had been aware that the holding in Humphrey's Executor rested on the purely- executive-power distinction; thus, the Court reasoned that Congress’s “failure of explicitness” in providing for removal was telling.<sup>387</sup> By failing to provide a removal limitation, Congress actually meant to include one, the Court reasoned.<sup>388</sup> The Court held that the President had neither the constitutional nor statutory power to remove a War Claims Commissioner, who is a “member of an adjudicatory body.”<sup>389</sup> In short, without distinguishing, let alone mentioning, Hennen, Parsons, or Perkins, the Court relied on the Myers/Humphrey's distinction to imply a removal

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<sup>380</sup> See supra text accompanying notes 305–306, 313, 315, 320, 325.

<sup>381</sup> Id.

<sup>382</sup> The War Claims Commissioners are similar to ALJs, in that both have limited quasi-adjudicatory power. See infra text accompanying note 389.

<sup>383</sup> Wiener, 357 U.S. at 351–52.

<sup>384</sup> Id. at 352.

<sup>385</sup> Id. at 355–56 (quoting Humphrey's Ex'r v. United States, 295 U.S. 602, 629 (1935)).

<sup>386</sup> The relevant statute was the War Claims Act of 1948, Pub. L. No. 80-896, 62 Stat. 1240, whereby Congress created the War Claims Commission but did not include a provision for the removal of commissioners in successive legislation. Id. at 349–50.

<sup>387</sup> Id. at 352.

<sup>388</sup> See id. at 353–54.

<sup>389</sup> Id. at 356.

limitation, even though Congress provided no clear statement that it intended any such limitation. With Wiener, the pendulum on the President's removal powers swung completely in the opposite direction of Myers.

Similarly, in 1986, the Court applied the Myers/Humphrey's distinction in Bowsher v. Synar.<sup>390</sup> In Bowsher, the Court analyzed the constitutionality of the Gramm-Rudman-Hollings Act.<sup>391</sup> That Act authorized the comptroller general, a principal officer,<sup>392</sup> to (1) determine whether the President and Congress were abiding by federal deficit caps, and (2) implement cuts when necessary.<sup>393</sup> The Act provided that the comptroller general could be removed by a joint resolution of Congress, which was subject to presidential veto.<sup>394</sup> The reasons Congress could offer for removal included permanent disability, inefficiency, neglect of duty, malfeasance, committing a felony, or committing other conduct involving moral turpitude.<sup>395</sup> Like it had in the statute at issue in Myers, Congress had again aggrandized itself by inserting itself into the removal process.

The Court struck down the Act, finding the removal provision to be unconstitutional.<sup>396</sup> According to the Court, the comptroller general's functions were the "very essence" of executing the law.<sup>397</sup> The Court reasoned that Congress could not vest authority to execute the laws in the comptroller general precisely because Congress retained the power to remove him.<sup>398</sup> According to the Court, the legislative history was very clear that Congress had included the removal provision specifically so that "[i]f [the comptroller general] does not do his work properly, [Congress], as practically his

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<sup>390</sup> Bowsher v. Synar, 478 U.S. 714, 724–25 (1986).

<sup>391</sup> Also known as the Balanced Budget and Emergency Deficit Control Act of 1985, Pub. L. No. 99- 177, 99 Stat. 1038 (codified as amended at 2 U.S.C. § 901 et. seq.).

<sup>392</sup> See Bowsher, 478 U.S. at 722–23 (quoting the Constitutional provision for principal officer appointment).

<sup>393</sup> Id. at 732–33.

<sup>394</sup> Id. at 728, 728 n.7 (citing 31 U.S.C. § 703(e)(1)B (1995)).

<sup>395</sup> Id. at 728, 728 n.7 (quoting 31 U.S.C. § 703(e)(1)B (1995)).

<sup>396</sup> Id. at 734.

<sup>397</sup> Id. at 733.

<sup>398</sup> Bowsher, 478 U.S. at 726–27, 733–34.

employers, ought to be able to discharge him from his office.”<sup>399</sup> Although the dissent believed that the “for cause” removal limitations effectively limited Congress’s removal power, making the Act constitutional, the majority disagreed.<sup>400</sup> The for- cause standard was too broad and vague to limit Congress’s power.<sup>401</sup> The Court explained that after Congress passes a law, Congress can influence the execution of that law only by passing new legislation or by impeachment.<sup>402</sup> “The structure of the Constitution does not permit Congress to execute the laws; it follows that Congress cannot grant to an officer under its control what it does not possess.”<sup>403</sup> In Bowsher, as in Myers, the Court held that Congress did not have the authority to retain for itself any ability to remove an executive officer.<sup>404</sup> Rather, because the officer exercised executive authority, the President’s removal power could not be limited.<sup>405</sup> As it had in Wiener, the Court again ignored Hennen, Parsons, and Perkins. Perhaps the Court did so because the relevant officer was a principal rather than an inferior officer, although the Court did not mention this distinction.

After Bowsher, the law seemed clear. The President needs the ability to control executive officers that work for him so that he can faithfully execute the laws; however, the President has less need to control those who exercise quasi-adjudicative and quasi-legislative powers. Hence, pursuant to the Myers/Humphrey’s distinction, Congress cannot limit the President’s ability to remove “purely executive officers,” but can limit the President’s ability to remove quasi- legislative and quasi-adjudicative officers. Additionally, under Perkins, Myers, and Bowsher, Congress cannot reserve for itself any power over the removal of executive officers, but can limit the removal powers of the heads of departments when they hold appointment power. Whether an officer was inferior or principal appeared irrelevant to the analysis.

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<sup>399</sup> Id. at 728–29 (quoting 58 Cong. Rec. 7136 (1921)).

<sup>400</sup> Id. at 729–32.

<sup>401</sup> Id. at 729–30.

<sup>402</sup> Id. at 726.

<sup>403</sup> Id.

<sup>404</sup> Bowsher, 478 U.S at 726–27.

<sup>405</sup> Id.

Just two years after Bowsher, in Morrison v. Olson, the Court abruptly changed course and rejected the Myers/Humphrey's distinction in the case of a "purely executive" inferior officer.<sup>406</sup> The act at issue in Morrison was the Ethics in Government Act.<sup>407</sup> In that Act, Congress established the office of independent counsel, whose function was to "investigate and, if appropriate, prosecute certain high-ranking Government officials" involved in criminal activity.<sup>408</sup> The Act provided that the attorney general, a principal officer, could remove the independent counsel, an inferior officer, only "for good cause."<sup>409</sup> The Court examined whether the good cause limitation on the Attorney General's power to remove independent counsel, by itself, violated separation of powers and whether the act as a whole "impermissibly interfere[d]" with the President's ability to faithfully execute the law.<sup>410</sup>

Under Perkins, when Congress vests the appointment of an officer in someone other than the President, Congress can expressly limit the removal of that officer.<sup>411</sup> Because Congress vested appointment authority in the Attorney General, the good cause limitation was constitutional under Perkins. Relegating Perkins to a "see also" footnote,<sup>412</sup> the Court turned instead to its holdings in Bowsher, Myers, Humphrey's Executor, and Wiener.<sup>413</sup> The Court noted that Humphrey's Executor was clear that the Constitution did not give the President "illimitable power of removal" over all executive officers.<sup>414</sup> And the Court stressed that "[u]nlike both Bowsher and Myers, [Morrison did] not involve an attempt by Congress itself to gain a role in the removal of executive officials other than its established powers of impeachment and conviction."<sup>415</sup>

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<sup>406</sup> Morrison v. Olson, 487 U.S. 654, 689–91 (1988).

<sup>407</sup> Id. at 659 (citing 28 U.S.C. §§ 49, 591 et seq. (Supp. V 1982)).

<sup>408</sup> Id. at 660 (citing 28 U.S.C. §§ 591–99 (Supp. V 1982)).

<sup>409</sup> Id. at 663 (citing 28 U.S.C. § 596(a)(1) (Supp. V 1982)).

<sup>410</sup> Id. at 685.

<sup>411</sup> See supra text accompanying notes 325–327.

<sup>412</sup> Morrison, 487 U.S. at 689, n.27.

<sup>413</sup> Id. at 685–88.

<sup>414</sup> Id. at 687 (quoting Humphrey's Ex'r v. United States, 295 U.S. 602, 629 (1935)).

<sup>415</sup> Id. at 686.



The Court acknowledged that the independent counsel performed a “core executive function[.]”<sup>416</sup>The Myers/Humphrey’s distinction would thus suggest that the removal provision was unconstitutional. Rejecting the Myers/Humphrey’s distinction as determinative for inferior officers, the Court stated, “the determination of whether the Constitution allows Congress to impose a ‘good cause’-type restriction on the President’s power to remove an official cannot be made to turn on whether or not that official is classified as ‘purely executive.’”<sup>417</sup> While the type of functions an officer performs was relevant to the analysis,<sup>418</sup> the Court concluded that the more important question was whether the removal restriction “impede[d] the President’s ability to perform his constitutional duty [to ensure that the laws are faithfully executed].”<sup>419</sup>

The Court then turned to the question of whether the Act interfered with the President’s ability to take care that the laws be faithfully executed under Article II.<sup>420</sup> You will recall that the Court in Myers had reasoned that limits on the President’s ability to remove an officer, especially an executive officer, interfered with his ability to faithfully execute the laws.<sup>421</sup> In other words, executive removal provisions are prima facie evidence that the President is unable to fulfill his constitutional obligations. In Morrison, the Court rejected

<sup>416</sup> Id. at 669.

<sup>417</sup> Id. at 689.

<sup>418</sup> Id. at 691.

<sup>419</sup> Id. The Court said:

[O]ur present considered view is that the determination of whether the Constitution allows Congress to impose a “good cause”-type restriction on the President’s power to remove an official cannot be made to turn on whether or not that official is classified as “purely executive.” The analysis contained in our removal cases is designed not to define rigid categories of those officials who may or may not be removed at will by the President, but to ensure that Congress does not interfere with the President’s exercise of the “executive power” and his constitutionally appointed duty to “take care that the laws be faithfully executed” under Article II.

Id. at 689–90 (footnotes omitted).

<sup>420</sup> Id. at 693.

<sup>421</sup> Myers v. United States, 272 U.S. 52, 163–64 (1926).

this prima facie approach and analyzed whether the President's ability to faithfully execute the law actually was impeded.<sup>422</sup> Rejecting the conclusion that the President's ability to faithfully execute the law actually was impeded under this statute, the Court reasoned that the independent counsel (1) was an inferior officer, (2) had limited jurisdiction, (3) did not have tenure, (4) lacked policymaking power, and (5) did not have significant administrative authority.<sup>423</sup> Moreover, the Court noted that President retained the ability to remove the attorney general without cause even if he could not remove the independent counsel.<sup>424</sup> Hence, the good cause limitation was a reasonable restriction on the President's removal authority.<sup>425</sup>

Because the inferior officers in Morrison were subject to only one level of "for-cause" removal, this case left open the question of whether more than one level of for-cause removal would be constitutional.<sup>426</sup> In 2010, the Supreme Court answered this question in the negative in Free Enterprise Fund v. Public Company Accounting Oversight Board.<sup>427</sup> The Court framed the issue as whether "the President [may] be restricted in his ability to remove a principal officer, who is in turn restricted in his ability to remove an inferior officer, even though that inferior officer determines the policy and enforces the laws of the United States?"<sup>428</sup> The answer, the Court held, was no.<sup>429</sup> Dual for-cause removal provisions are contrary to Article II's "vesting of the executive power in the President" since "[t]he President cannot 'take Care that the Laws be faithfully executed' if he cannot oversee the faithfulness of the officers who execute them."<sup>430</sup>

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<sup>422</sup> See Morrison, 487 U.S. at 689–90.

<sup>423</sup> Id. at 691–92.

<sup>424</sup> Id. at 692 (observing that the President retains "ample authority" by being able to remove the Attorney General at-will).

<sup>425</sup> Id. at 689.

<sup>426</sup> Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 495 (2010).

<sup>427</sup> Id. at 483–84.

<sup>428</sup> Id.

<sup>429</sup> Id. at 484.

<sup>430</sup> Id.

The Court in Free Enterprise examined the validity of a for-cause removal provision in the Sarbanes–Oxley Act of 2002 (the Act).<sup>431</sup> With the Act, Congress created a private, non-profit corporation,<sup>432</sup> the Public Company Accounting Oversight Board (Board), “[a]fter a series of celebrated accounting debacles.”<sup>433</sup> Congress sought to tighten regulation of the accounting industry to prevent any further such debacles.<sup>434</sup> Pursuant to the Act, the SEC appoints five members to the Board for staggered five-year terms<sup>435</sup> and oversees their functions, “particularly with respect to the issuance of rules or the imposition of sanctions (both of which are subject to Commission approval and alteration).”<sup>436</sup> The Act provided that the SEC Commissioners could remove individual members of the Board “only ‘for good cause shown.’”<sup>437</sup> The plaintiff, a non-profit entity representing accounting firms, sued, claiming, among other things, that the dual for- cause removal provisions violated separation of powers in light of the Board’s “wide-ranging executive power.”<sup>438</sup>

Under Perkins and Morrison, a single for-cause removal provision on inferior officers who lack policy-making power and do not exercise significant administrative authority is constitutional.<sup>439</sup> So long as the President retains unfettered power to remove the principal officers (here the SEC Commissioners), the President’s ability to faithfully execute the laws is not unconstitutionally

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<sup>431</sup> Sarbanes–Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002).

<sup>432</sup> According to the statute, Board members are not Government “officer[s] or employee[s].” Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 484 (2010) (citing 15 U.S.C. §§ 7211(a), (b) (2006 & Supp. IV 2010)). Although the Board members are not Government officials for statutory purposes, the Board is “part of the Government” for constitutional purposes. Id. at 485–86.

<sup>433</sup> Id. at 484.

<sup>434</sup> Id.

<sup>435</sup> Id.

<sup>436</sup> Id. at 486 (citing 15 U.S.C. §§ 7217(b)–(c) (2006)).

<sup>437</sup> Id.

<sup>438</sup> Free Enter. Fund, 561 U.S. at 487.

<sup>439</sup> Id. at 494–95, 508 (noting that “restricting certain officers to a single level of insulation from the President . . . would have no effect, absent a congressional determination to the contrary, on the validity of any officer’s continuance in office”).

impeded. However, the parties had stipulated that the SEC Commissioners themselves were also removable only for cause.<sup>440</sup>

Notably, this stipulation may be wrong. There is no statute limiting the SEC Commissioners' removal, as there was in Humphrey's Executor, likely because the statute establishing the SEC was enacted at a time when Congress assumed that for-cause removal provisions would violate the Constitution.<sup>441</sup> Without an explicit removal limitation in the statute, possibly a president would have the ability to remove a Commissioner for any reason because under Hennen and Parsons removal provisions are generally not implied.<sup>442</sup> Because the parties stipulated that the SEC Commissioners were only removable for cause, however, the Court presumed that the members of the Board had dual for-cause removal protection; these inferior officers could only be removed for-cause by principal officers who also could only be removed for cause.<sup>443</sup> In dissent, Justice Breyer noted that whether the SEC Commissioners have tenure protection was such a critical finding to the majority's holding that it should not have been based on the parties' stipulation.<sup>444</sup>

Although the majority should not have accepted the stipulation, the second for-cause level of protection proved to be the Act's undoing. In finding that dual for-cause removal protections impeded the President's ability to faithfully execute the laws, the majority returned to the Myers/Humphrey's distinction it had recently rejected in Morrison.<sup>445</sup> The Court noted that "the power of appointing, overseeing, and controlling those who execute the laws" is a

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<sup>440</sup> Id. at 487 ("The parties agree that the Commissioners cannot themselves be removed by the President except under the Humphrey's Executor standard of 'inefficiency, neglect of duty, or malfeasance in office.'") (citation omitted). One wonders why the Court did not apply the constitutional avoidance doctrine and interpret the statute to not include for-cause removal, thereby avoiding the removal question. It appears that the majority was set on reviewing the constitutionality of this very powerful board.

<sup>441</sup> See id.; see also id. at 518 (Breyer, J., dissenting).

<sup>442</sup> But see Wiener v. United States, 357 U.S. 349, 356 (1958) (holding that the President's power to remove a War Claims Commissioner was impliedly limited even though the statute was silent regarding removal).

<sup>443</sup> Free Enter. Fund, 561 U.S. at 487.

<sup>444</sup> Id. at 545–46 (Breyer, J., dissenting).

<sup>445</sup> See supra text accompanying footnotes 416–419.

quintessential executive act.<sup>446</sup> Myers, the majority noted, reaffirmed the principle that the President must have some power to remove those officers for whom he is responsible.<sup>447</sup> Pointing to Humphrey's Executor, the majority noted that Congress could confer good-cause tenure on officers who acted in a “quasi-legislative and quasi-judicial” capacity, rather than in a “purely executive” capacity.<sup>448</sup> But here, the majority concluded, the Board members exercised executive power.<sup>449</sup>

After resurrecting the defunct Myers/Humphrey's distinction, the majority examined whether the Board members were principal or inferior officers. The majority interpreted Humphrey's Executor as holding that Congress could confer good-cause tenure on quasi-legislative and quasi-judicial principal officers.<sup>450</sup> Notably, the majority explained, the Court in “Humphrey's Executor did not address the removal of inferior officers.”<sup>451</sup> The majority pointed out that pursuant to the Constitution, Congress can vest the appointment of inferior officers in the heads of departments.<sup>452</sup> When Congress does so, the majority continued, then the department head—rather than the President—holds removal power, and Congress can limit the department head's removal power, under Perkins.<sup>453</sup>

(1)The majority then turned to Morrison which, you will recall, had rejected the Myers/Humphrey's distinction for inferior officers.<sup>454</sup> In Morrison, the Court examined factors to determine when removal provisions would impede a President's ability to faithfully execute the laws.<sup>455</sup> Removal provisions do not impede a President's power when the officer (1) is inferior, has limited jurisdiction, (3) does not have tenure, (4) lacks policymaking power,

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<sup>446</sup> Free Enter. Fund, 561 U.S. at 480 (quoting 1 Annals of Cong. 486 (Joseph Hales ed., 1834)).

<sup>447</sup> Id. at 492–93.

<sup>448</sup> Id. at 493 (quoting Humphrey's Ex'r v. United States, 295 U.S. 602, 627–29 (1935)) (internal quotation marks omitted).

<sup>449</sup> Id. at 498.

<sup>450</sup> Id. at 493 (quoting Humphrey's Ex'r, 295 U.S. at 627–29).

<sup>451</sup> Id. (emphasis added).

<sup>452</sup> Free Enter. Fund, 561 U.S. at 493.

<sup>453</sup> Id.; United States v. Perkins, 116 U.S. 483, 485 (1886).

<sup>454</sup> See supra text accompanying footnotes 416–419.

<sup>455</sup> Morrison v. Olson, 497 U.S. 654, 691–92 (1988).

and (5) lacks significant administrative authority.<sup>456</sup> In other words, the less important the officer, the more likely that a removal limitation will be valid. Examining these factors, the Free Enterprise majority noted that the Board members were inferior officers; thus, the first factor was met.<sup>457</sup> However, the majority did not examine any of the four remaining Morrison factors, at least not clearly.<sup>458</sup>

Instead, the Court focused on the ability of the President to supervise and control the Board members in light of the multiple removal provisions.<sup>459</sup> The majority noted that one level of for-cause removal on executive inferior officers would be constitutional, because the President retained the power to remove the principal officers if they failed to remove an incompetent inferior officer.<sup>460</sup> However, the added layer of tenure protection in the case of the Board was problematic, because the President would be unable to remove either the incompetent Board members or the SEC Commissioners who failed to remove the incompetent Board members.<sup>461</sup> The Court seemed particularly troubled because, not only were there two levels of for-cause removal protection, but for one of them, Congress had enacted “an unusually high standard that must be met before Board members [could] be removed.”<sup>462</sup> In sum, one for-cause removal limitation on a purely executive inferior office is constitutional. More than one is not.

Then, as if foreshadowing the controversy regarding the SEC ALJs, the Court questioned: if two levels of for-cause tenure

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<sup>456</sup> Id.

<sup>457</sup> Free Enter. Fund, 561 U.S. at 510.

<sup>458</sup> The majority noted in a footnote that its option did not address ALJs specifically. The majority distinguished ALJs from Board members because many ALJs “perform adjudicative rather than enforcement or policymaking functions . . . or possess purely recommendatory powers.” Id. at 507 n.10. The footnote suggests that Board members have policymaking power, though the footnote is not clear on this point.

<sup>459</sup> Id. at 495.

<sup>460</sup> Id.

<sup>461</sup> Id. at 496.

<sup>462</sup> Id. at 503 (“A Board member cannot be removed except for willful violations of the Act, Board rules, or the securities laws; willful abuse of authority; or unreasonable failure to enforce compliance . . . .”). Id. at 505 (describing the Board’s for-cause standard as “a sharply circumscribed definition” that requires “rigorous procedures that must be followed prior to removal”).

protection were constitutional, “why not a third?”<sup>463</sup> Where, the majority wondered, does the Constitution draw the line?<sup>464</sup> The majority criticized the potential “Matryoshka doll of tenure protections” that would “exercise[] power in the people’s name” if multiple for-cause removal provisions were valid.<sup>465</sup> In sum, the majority concluded that dual for-cause tenure protections “subvert[] the President’s ability to ensure that the laws are faithfully executed—as well as the public’s ability to pass judgment on his efforts. The Act’s restrictions are incompatible with the Constitution’s separation of powers.”<sup>466</sup> Minimizing the potential effects of its holding, the majority simply severed “the unconstitutional tenure provisions . . . from the remainder of the statute.”<sup>467</sup>

Justice Breyer dissented.<sup>468</sup> He criticized the majority for “fail[ing] to create a bright-line rule [which would cause] uncertainty about the scope of its holding.”<sup>469</sup> He worried that a broad application of Free Enterprise’s holding could dismantle the entire administrative state by putting the “job security” of “thousands of high-level Government officials . . . and their administrative actions and decisions constitutionally at risk.”<sup>470</sup> He specifically cautioned that if all dual for- cause removal provisions violate the Constitution, then the removal of more than 1,584 ALJs in over twenty-five agencies would be unconstitutional.<sup>471</sup>

The majority responded to Breyer’s concern by suggesting that it was unlikely that its holding would apply to ALJs, because “unlike members of the Board, many administrative law judges . . . perform adjudicative rather than enforcement or policymaking functions or

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<sup>463</sup> Free Enterprise Fund, 561 U.S. at 497.

<sup>464</sup> See id.

<sup>465</sup> Id.

<sup>466</sup> Id. at 498.

<sup>467</sup> Id. at 508.

<sup>468</sup> Id. at 514 (Breyer, J., dissenting).

<sup>469</sup> Free Enterprise Fund, 561 U.S. at 536.

<sup>470</sup> Id. at 540–41.

<sup>471</sup> Id. at 542–43.

possess purely recommendatory powers.”<sup>472</sup> Returning again to the Myers/Humphrey’s distinction, the majority said:

[O]ur holding also does not address that subset of independent agency employees who serve as administrative law judges . . . . Whether administrative law judges are necessarily “Officers of the United States” is disputed. [See Landry v. FDIC, 204 F.3d 1125 (D.C. Cir. 2000).] And unlike members of the Board, many administrative law judges of course perform adjudicative rather than enforcement or policymaking functions . . . or possess purely recommendatory powers. The Government below refused to identify either “civil service tenure-protected employees in independent agencies” or administrative law judges as “precedent for the PCAOB.”<sup>473</sup>

The majority thus distinguished ALJs from the members of the Board based on their quasi-judicial role and limited powers. It is unclear whether Roberts was trying to apply the Myers/Humphrey’s distinction (executive versus quasi-legislative or quasi-judicial), was referring to some of the Morrison factors (lacking policymaking power and lacking significant administrative authority), or was combining the two in a removal test mash-up. Regardless, he was incorrect. The members of the Board performed adjudicative functions.<sup>474</sup> Additionally, many ALJs have more than recommendatory powers and have “important administrative duties beyond pure adjudication.”<sup>475</sup> As noted earlier, ALJs affect policy when they adjudicate, which is one reason why the DOJ had concluded that ALJs are inferior officers.<sup>476</sup>

Trying to make sense of this footnote, Professor Kevin Stack has suggested that Justice Roberts may have been trying to distinguish

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<sup>472</sup> Id. at 507 n.10 (majority opinion).

<sup>473</sup> Id.

<sup>474</sup> Id. at 531 (Breyer, J., dissenting).

<sup>475</sup> Free Enter. Fund, 561 U.S. at 535.

<sup>476</sup> See generally Sec’y of Educ. Review, supra note 247, at 14.



Board members from ALJs by suggesting that Board members perform adjudicative functions as well as executive and legislative functions, while ALJs perform only adjudicative functions.<sup>477</sup> Possibly. But if so, Roberts expanded the Myer/Humphrey's distinction to apply to removal limitations placed on inferior officers (ALJs).

If this was what Justice Roberts intended, then he has seemingly resurrected the formalistic Myers/Humphrey's distinction: if any officer performs purely adjudicative, as opposed to purely executive, functions, then additional removal insulation does not violate separation of powers. None of the Supreme Court cases that applied the Myers/Humphrey's distinction up to that time had done so in the case of an inferior officer. In any event, the Court's response is dicta at best and confusing at worst.

In sum, the Free Enterprise majority reasoned that dual for-cause removal provisions violate the Constitution precisely because the President is unable to remove either an inferior officer who fails in her job or the principal officers who oversee her.<sup>478</sup> Rather, the President would have to rely on both inferior and principal officers always acting lawfully, competently, and faithfully. Pursuant to Morrison and Humphrey's Executor, each layer of for-cause removal would have been constitutional by itself; however, under Free Enterprise, when Congress combines the two layers of for-cause removal, the dual layers become unconstitutional.<sup>479</sup> As the D.C. Circuit Court in Association of American Railroads v. U.S. Department of Transportation recently noted, "[J]ust because two structural features raise no constitutional concerns independently does not mean Congress may combine them in a single statute."<sup>480</sup>

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<sup>477</sup> Kevin M. Stack, Agency Independence After PCAOB, 32 *Cardozo L. Rev.* 2391, 2412, 2411 n.117 (2011).

<sup>478</sup> Free Enter. Fund, 561 U.S. at 496.

<sup>479</sup> See, e.g., Ass'n of Am. R.R. v. U.S. Dep't. of Transp., 721 F.3d 666, 673 (D. C. Cir. 2013) vacated on other grounds 135 S. Ct. 1225 (2015), remanded to 821 F.3d 19 (D.C. Cir. 2016).

<sup>480</sup> Id. at 673.

## 2. A Removal Framework

The nine removal cases described provide conflicting guidance, but offer the following removal framework. The Court applies a different test depending on whether the removal limitations affect principal or inferior officers. For principal officers, the Court crafted the Myers/Humphrey's distinction: a formalist test based on the type of acts the officer performed.<sup>481</sup> Under the Myers/Humphrey's distinction, Congress cannot limit the President's authority to remove purely executive officers.<sup>482</sup> However, Congress can limit the President's ability to remove quasi-legislative and quasi-adjudicative officers.<sup>483</sup> The Court has never, however, considered whether multiple levels of tenure protection for quasi-legislative and quasi-adjudicative principal officers would be constitutional. And that issue does not arise in regard to the SEC ALJs, who are not principal officers.

Instead, the issue that arises with SEC ALJs is whether multiple levels of for-cause removal on inferior officers are constitutional. Recall that removal limitations for inferior officers are not implied; that is the rule from Hennen and Parsons.<sup>484</sup> Next, Perkins tells us that Congress can expressly limit the executive's removal power when Congress vests appointment in an entity other than the President.<sup>485</sup> But Myers and Bowsher caution that Congress can limit the removal power of that entity so long as Congress does not keep for itself a role in the removal process and so long as the President's ability to faithfully execute the laws is not impeded.<sup>486</sup>

One method the Court has used to determine whether a removal provision impedes the President's ability to faithfully execute the laws is to examine the Morrison factors: whether the officer (1) is

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<sup>481</sup> See supra Part III.C.1.

<sup>482</sup> See, e.g., Myers v. United States, 272 U.S. 52, 135 (1926). Additionally, the Court rejected Congress's attempt to assume removal authority over executive officers. Bowsher v. Synar, 478 U.S. 714, 726–27 (1986). But see Morrison v. Olson, 487 U.S. 654, 686 (1988).

<sup>483</sup> See, e.g., Wiener v. United States, 357 U.S. 349, 356 (1958); Humphrey's Ex'r v. United States, 295 U.S. 602, 631–32 (1935).

<sup>484</sup> See supra Part III.C.1.

<sup>485</sup> Id.

<sup>486</sup> Myers, 272 U.S. at 161; Bowsher, 478 U.S. at 726–27, 733–34.

inferior, (2) has limited jurisdiction, (3) lacks tenure, (4) lacks policymaking power, and (5) lacks significant administrative authority.<sup>487</sup> The less significant the official and her responsibilities, the more likely that the removal provision will be upheld. No one of these factors is determinative; rather, the Court's concern, as explained in Free Enterprise, is that the President's ability to execute the laws not be impeded.<sup>488</sup> And the President's ability to execute the laws is impeded when there are multiple for-cause removal provisions. The President must retain some ability to remove a recalcitrant inferior officer, whether the President has the power to remove that inferior officer directly or the ability to remove the principal officer overseeing the recalcitrant.

### 3. The SEC ALJ Removal Provisions Violate Separation of Powers

Assuming the Supreme Court applies this removal framework to the SEC ALJs, it should conclude that the SEC ALJ removal limitations violate separation of powers. As noted earlier, the SEC ALJs are inferior officers, not employees, because they exercise significant authority and decision-making power pursuant to the laws of the United States.<sup>489</sup>

Because the SEC ALJs are inferior officers, the appropriate approach, under Perkins, is for a court to ask first whether Congress vested appointment power in an entity other than the executive and, second, whether Congress expressly limited that entity's power to remove the inferior officer without taking on removal power for itself.<sup>490</sup> For the SEC ALJs, Congress vested their appointment in the OPM.<sup>491</sup> Further, Congress provided that the SEC, like all agency heads, may remove its ALJs only for cause.<sup>492</sup> Thus, Congress vested

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<sup>487</sup> Morrison, 487 U.S. at 691–92.

<sup>488</sup> Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 496 (2010).

<sup>489</sup> See supra Part III.A.3.

<sup>490</sup> See supra Part III.C.1.

<sup>491</sup> See Gray Complaint, supra note 99, at ¶ 52 (“SEC ALJs may be appointed by the SEC’s Office of Administrative Law Judges, with input from the Chief Administrative Law Judge, human resource functions and the Office of Personnel Management.”).

<sup>492</sup> 5 U.S.C. § 7521(a) (2012).

appointment authority in an entity other than the President, limited the removal power of that entity, and did so without retaining removal power for itself. So far, so good.

Next, under Morrison removal provisions on inferior officers are valid so long as the officer (1) has limited jurisdiction, (2) lacks tenure, (3) lacks policymaking power, and (6) lacks significant administrative authority.<sup>493</sup> And under Free Enterprise, in order to be valid, these express removal provisions cannot actually interfere with the President's ability to faithfully execute the laws.

Here is where problems arise. A court examining the five factors identified in Morrison— whether the officer (1) is inferior, (2) has limited jurisdiction, (3) does not have tenure, (4) lacks policymaking power, and (5) lacks significant administrative authority<sup>494</sup>—should find that the SEC ALJs meet only two of them. The SEC ALJs are inferior officers,<sup>495</sup> and they have somewhat limited jurisdiction, because they can adjudicate only certain types of SEC cases.<sup>496</sup> However, a court would likely find that the SEC ALJs do not meet the other three factors. When the SEC ALJs adjudicate cases, they inevitably make policy, albeit their policy-making authority may be more limited than purely executive officials.<sup>497</sup> Moreover, they hold significant adjudicatory authority (it is unclear whether adjudicatory authority is the same as administrative authority; Morrison did not define administrative authority)<sup>498</sup> and have for-cause tenure.<sup>499</sup> Arguably, because the Morrison factors suggest that the SEC ALJs are inferior officers with significant authority, the first level for-cause protection provided to the SEC ALJs may well be unconstitutional.

This conclusion may seem unnecessarily formalist. A functionalist would note that ALJs have served as the cornerstone of the administrative system for many years. The ALJ system has

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<sup>493</sup> Morrison, 487 U.S. at 691–92.

<sup>494</sup> Morrison v. Olson, 487 U.S. 654, 691–92 (1988).

<sup>495</sup> See supra Part III.A.3.

<sup>496</sup> See generally Sonia A. Steinway, Comment, SEC “Monetary Penalties Speak Very Loudly.” But What Do They Say? A Critical Analysis of the SEC’s New Enforcement Approach, 124 Yale L.J. 209 (2014) (providing a list of enforcement actions that the SEC brings).

<sup>497</sup> Sec’y of Educ. Review, supra note 247, at 14.

<sup>498</sup> See supra note 455 and accompanying text.

<sup>499</sup> 5 U.S.C. § 7521(a) (2012).

worked for years and affects a huge number of litigants who interact with a huge number of agencies. The implications of finding the current removal process for ALJs to be unconstitutional are staggering. To take just one example, the Social Security Administration (SSA) ALJs hear thousands of cases each year dealing with social security benefits.<sup>500</sup> To shut down the process would have dramatic impact. In short, because ALJs have served important functions for so long, it may seem counterintuitive to find their appointment and removal unconstitutional now.

Yet, this argument is classically functionalist: if the system is not broken and has worked thus far, why fix it? A similar argument was raised in INS v. Chadha, in which the plaintiff challenged the constitutionality of the legislative veto.<sup>501</sup> Justice White, in dissent, warned that without the legislative veto, Congress would have to “either [] refrain from delegating the necessary authority . . . or . . . abdicate its law-making function to the Executive Branch and independent agencies.”<sup>502</sup> He worried that choosing the former would “leave[] major national problems unresolved” while choosing the latter would create the risk of “unaccountable policymaking” by those who were not elected to perform that function.<sup>503</sup> Rejecting these concerns, the Supreme Court nevertheless found the power arrangement unconstitutional.<sup>504</sup> Despite Justice White’s fears, the majority’s holding proved not to be “destructive,” nor did it cause the administrative world to fall apart.<sup>505</sup> Similarly, here, the longstanding nature of the ALJs’ multiple for-cause removal procedures alone cannot be the basis for finding an unconstitutional removal process constitutional. Disrupting a system that is largely working should factor into the solution, but should not be determinative as to whether that system violates the Constitution.

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<sup>500</sup> Social Security Disability Benefits: Hearing Before the S. Comm. on Homeland Sec. & Gov’t Affairs, 113th Cong. (2013) (statement of Debra Bice, Chief Administrative Law Judge, Social Security Administration) (discussing the hearings process).

<sup>501</sup> INS v. Chadha, 462 U.S. 919, 928 (1983).

<sup>502</sup> Id. at 968 (White, J., dissenting).

<sup>503</sup> Id.

<sup>504</sup> Id. at 955–58 (majority opinion).

<sup>505</sup> Id. at 1002 (White, J., dissenting).

Additionally, quasi-adjudicators, like the SEC ALJs, are arguably protected from executive removal for good reason: to promote ALJ independence. Before the APA was enacted, there was considerable concern that hearing examiners could not exercise independent judgment both because they were required to perform prosecutorial and investigative functions in addition to their judicial work,<sup>506</sup> and because they were subordinate to the agency heads.<sup>507</sup> So, Congress included within the APA a number of provisions to help ensure the independence of these hearing examiners, later ALJs. For example, when conducting a hearing, an ALJ cannot be “responsible to or subject to the supervision or direction” of employees or agents who perform investigative or prosecutorial functions for the agency.<sup>508</sup> Nor may an ALJ “consult [any] person or party,” including other agency officials, concerning a “fact at issue” in the hearing, “unless on notice and opportunity for all parties to participate.”<sup>509</sup> Moreover, and at issue here, ALJs can be removed only for good cause established and determined by the MSPB after a formal adjudication.<sup>510</sup> Finally, Congress ensured that ALJ compensation is also free from executive control.<sup>511</sup> In sum, Congress rightly concluded that effective adjudication requires that litigants believe the process to be fair and the decision-maker to be impartial.<sup>512</sup> ALJs must be free to adjudicate without threat of retaliation.<sup>513</sup> Protecting

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<sup>506</sup> See, e.g., *Wong Yang Sung v. McGrath*, 339 U.S. 33, 36–41 (1950).

<sup>507</sup> *Butz v. Economou*, 438 U.S. 478, 514 (1978) (citing *Ramspeck v. Fed. Trial Exam’rs Conference*, 345 U.S. 128, 131 (1953)).

<sup>508</sup> 5 U.S.C. § 554(d)(2) (2012).

<sup>509</sup> *Id.* § 554(d)(1).

<sup>510</sup> *Id.* § 7521(a).

<sup>511</sup> See generally 5 U.S.C. § 4301(2)(D) (2012); 5 U.S.C. § 5372 (2012).

<sup>512</sup> *Withrow v. Larkin*, 421 U.S. 35, 47 (1975) (stating that biased decision-making is “constitutionally unacceptable,” especially in a system that “endeavor[s] to prevent even the probability of unfairness”); *Town of Winthrop v. FAA*, 535 F.3d 1, 14 (1st Cir. 2008). After all, due process “demands impartiality on the part of those who function in judicial or quasi-judicial capacities.” *Schweiker v. McClure*, 456 U.S. 188, 195 (1982) (citing *Marshall v. Jerrico, Inc.*, 446 U.S. 238, 242–43, 243 n.2 (1980)).

<sup>513</sup> A former ALJ alleged she felt pressured to rule in favor of the SEC and that she was told to work under the presumption that the defendants were guilty until proven innocent. Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J.

ALJs from arbitrary and retaliatory removal promotes independence and impartiality.<sup>514</sup> Moreover, agencies can review de novo the ALJ decision and reverse it if they disagree. Hence, again from a functionalist standpoint, this one level of removal protection may not only be constitutional, but welcomed. Justice Breyer certainly seemed to think so.<sup>515</sup>

Nevertheless, even if the initial for-cause layer of removal protection is constitutional, it is very unlikely that the second for-cause layer is constitutional under Free Enterprise. Focusing on the two for-cause layers, the Court in Free Enterprise examined whether multiple removal provisions actually impeded the President's ability to supervise and control the Board members.<sup>516</sup> What was particularly problematic to the majority in Free Enterprise was the second for-cause removal layer; this layer prevented the President from removing the overseeing principal officer of an underperforming inferior officer. In short, the President could exercise neither direct nor indirect control over an underperforming inferior officer.

Like the Board members in Free Enterprise, the SEC ALJs are protected by a second, and possibly a third, level of removal protection. First, all ALJs, including the SEC ALJs, are protected by statute from removal absent good cause.<sup>517</sup> Second, to remove an SEC ALJ, the SEC Commissioners must first bring a good-cause formal proceeding before the MSPB.<sup>518</sup> However, these SEC Commissioners may themselves be protected from removal absent "inefficiency, neglect of duty, or malfeasance in office."<sup>519</sup> Third,

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(May 6, 2015, 10:30 PM), <http://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803> [<https://perma.cc/J3X2-TS7X>].

<sup>514</sup> *Butz v. Economou*, 438 U.S. 478, 514 (1978) (considering whether agency employees had immunity from prosecution for allegedly ultra vires acts).

<sup>515</sup> *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 522 (2010) (Breyer, J., dissenting).

<sup>516</sup> *Id.* at 495–96 (majority opinion); *but see* Zaring, *supra* note 108, at 1191–95 (arguing that whatever the doctrinal problems with removal, ALJs are too traditional to find unconstitutional now).

<sup>517</sup> 5 U.S.C. § 7521(a) (2012).

<sup>518</sup> *Id.* While other civil servants also receive hearings before dismissal, only the ALJs receive formal hearings. *See* 5 U.S.C. § 4303(b)(1) (2012).

<sup>519</sup> *See, e.g.*, *Free Enter. Fund*, 561 U.S. at 487 (internal quotation marks omitted); *MFS Sec. Corp. v. SEC*, 380 F.3d 611, 619–20 (2d Cir. 2004).

members of the MSPB, who determine whether sufficient “good cause” exists to remove an SEC ALJ, are also protected from removal.<sup>520</sup> In sum, for an incompetent SEC ALJ to be removed, first the SEC Commissioners must refer the ALJ to the MSPB and establish cause, then the MSPB must agree that cause existed. Hence, presumably three levels of for-cause removal are present.

Assuming the above analysis is correct, the world of ALJs, and the SEC ALJs specifically, must change. Because if the SEC ALJs’ removal provisions violate separation of powers, then likely all ALJs’ removal provisions violate separation of powers. In Free Enterprise, the majority remedied the constitutional infirmity simply by severing the unconstitutional language.<sup>521</sup> Severing the unconstitutional for-cause removal provisions for the SEC ALJs will not be so simple. The statute that includes the first level of for-cause removal protection applies to all ALJs, not just the SEC ALJs.<sup>522</sup> If all dual for-cause removal provisions violate the Constitution, then the removal of more than 1,584 ALJs in over twenty-five agencies would be unconstitutional.<sup>523</sup> In short, the potential repercussions of finding the ALJs’ for-cause removal provision to be unconstitutional are significantly greater than were the repercussions for invalidating a removal provision that applied to a Board with just five members.

However, there is an additional concern in the case of the SEC ALJs specifically. The members of the MPRB and the SEC Commissioners also have for-cause tenure.<sup>524</sup> Severing the SEC ALJ for-cause removal limitation addresses only one of these potentially problematic, multiple for-cause tenure protections. The Court would still need to evaluate the intersection of these two remaining for-cause removal provisions to ensure the two acting in concert do not impede the President’s ability to faithfully execute the law.

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<sup>520</sup> They are removable “by the President only for inefficiency, neglect of duty, or malfeasance in office.” 5 U.S.C. § 1202(d) (2012).

<sup>521</sup> Free Enter. Fund, 561 U.S. at 509.

<sup>522</sup> Id. at 540–41 (Breyer, J., dissenting).

<sup>523</sup> Id. at 542–43 (Breyer, J., dissenting).

<sup>524</sup> Id. at 487 (majority opinion) (“The parties agree that the Commissioners cannot themselves be removed by the President except under the Humphrey’s Executor standard of ‘inefficiency, neglect of duty, or malfeasance in office.’”).



Justice Breyer expressed concern about the dismantling of the ALJ system in his dissent in Free Enterprise.<sup>525</sup> Broad application of Free Enterprise's holding, he warned, could dismantle the entire administrative state by putting the job security of "thousands of high-level Government officials . . . and their administrative actions and decisions constitutionally at risk."<sup>526</sup> For Justice Breyer, multiple levels of removal protection serve a legitimate role in protecting the integrity of agency adjudications and should be upheld.<sup>527</sup> And the majority appeared to concede as much in footnote ten when it responded to Justice Breyer's concern.<sup>528</sup>

However, if Justice Breyer is right, then Free Enterprise is meaningless; its holding would apply only to those cases in which Congress creates an agency within an independent agency and tenure protects both levels.<sup>529</sup> To our knowledge, Congress has created this unusual agency structure only once in our Nation's history, and is unlikely to do so again. Indeed, ALJs seem quite different from the PCAOB members. We cannot imagine that the Supreme Court intended to issue such a narrow opinion.<sup>530</sup> However, the

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<sup>525</sup> Id. at 540–41 (Breyer, J., dissenting).

<sup>526</sup> Id.

<sup>527</sup> Id. at 536 (Breyer, J., dissenting).

<sup>528</sup> Id. at 507 n.10 (majority opinion).

<sup>529</sup> Recently, the D.C. Circuit cited Free Enterprise to support its holding that it was unconstitutional for the CFPB to be headed by a single director whom the President could not remove except for cause. PHH Corp. v. Consumer Fin. Protection Bureau, 839 F.3d 1 (D.C. Cir. 2016) (reh'g granted Feb. 16, 2017).

<sup>530</sup> In any event, at least one court has agreed with Justice Breyer. The United States District Court for Southern District of New York in Duka v. SEC, suggested that the SEC ALJ's dual for-cause removal protections are likely constitutional. 103 F. Supp. 3d 382, 393–96 (S.D.N.Y. 2015). The court issued its ruling in response to a motion for a preliminary injunction, so the court's analysis is preliminary and short on explanation. In its reasoning, the court returned to the Myers/Humphrey Executor's distinction. Id. at 394. The court noted that limiting the removal of "quasi-judicial" agency adjudicators [is] unlikely to interfere with the President's ability to perform his executive duties." Id. at 395. Because the Duka court applied the principal officer framework rather than the inferior officer framework—specifically finding the SEC ALJs' quasi-adjudicatory nature to be determinative—the court's conclusion lacks persuasiveness. Additionally, the United States District Court for Northern District of Georgia noted that because ALJs "likely occupy 'quasi-judicial' or 'adjudicatory' positions," it had "serious doubts" that the two-layer protections are unconstitutional. See Timbervest, LLC v.

composition of the Supreme Court has changed with the passing of Justice Antonin Scalia. The conservative majority that decided Free Enterprise is no more. Very likely, resolution of this important issue hinges on the identity of the next President and that leader's appointment to the Supreme Court.

#### IV. CONCLUSION

The SEC ALJs current structure likely violates the Constitution in two ways. First, as inferior officers, the SEC ALJs must be appointed by the President, courts of law, or a department. However, the SEC ALJs are appointed by the OPM and the SEC Chief ALJ. This appointment process violates the Constitution. How the SEC will remedy this constitutional infirmity is not clear. Perhaps the Commissioners will simply appoint the already-serving SEC ALJs to their current positions, as the DOT did after Weiss v. United States.<sup>531</sup> Regardless of whether such a retroactive process would allow for meaningful appointment as the Constitution contemplates, there is a more fundamental concern. What about the validity of the pending and issued SEC ALJ orders?<sup>532</sup> The effects from Noel Canning<sup>533</sup> suggest that such an approach may have a staggering impact.<sup>534</sup>

Second, as inferior officers, the SEC ALJs cannot be subject to multiple levels of for-cause removal protection without violating separation of powers. And unlike the statute at issue in Free Enterprise, severing the unconstitutional provision will not be an easy fix. The statute that includes the first level of for-cause removal protection applies to more than 1,500 ALJs in twenty-five different agencies, not just to the SEC ALJs. Hence, the repercussions of such a holding would be significantly greater than were the repercussions for invalidating a

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SEC, No. 1:15-CV-2106-LMM, 2015 U.S. Dist. LEXIS 132082, at \*35 n.10 (N.D. Ga. Aug 4, 2015); Gray Fin. Grp., Inc. v. SEC, 166 F. 3d 1335, 1354 n.10 (N.D. Ga. Aug. 4, 2015), vacated and remanded, Hill v. SEC, 825 F.3d 1236, 1252 (11th Cir. 2016); Hill v. SEC, 114 F. Supp. 3d 1297, 1319 n.12 (N.D. Ga. 2015), vacated and remanded 825 F.3d 1236, 1252 (11th Cir. 2016).

<sup>531</sup> See Edmond v. United States, 520 U.S. 651, 654 (1997) (discussing Weiss v. United States, 510 U.S. 163 (1994)).

<sup>532</sup> See supra Part III.B.2.

<sup>533</sup> NLRB v. Noel Canning, 134 S. Ct. 2550 (2014).

<sup>534</sup> See supra Part III.B.2.

removal provision that applied to a Board with just five members. Moreover, severing the SEC ALJ for- cause removal limitation addresses only one problematic for-cause layer. Two more would remain.

Hence, the constitutional challenges raised in these cases are far from inconsequential. Thousands of ALJs may be subject to unconstitutional appointment and removal provisions. And there is no easy fix. The shadow of Free Enterprise looms large.