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CLIENT ALERT

Supreme Court Ruling Invalidates Staff-Appointed SEC Administrative Law Judges

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Yesterday, the Supreme Court issued its much-anticipated decision in *Lucia v. SEC*, No. 17–130, holding that administrative law judges (ALJs) at the Securities and Exchange Commission are "Officers of the United States" for purposes of the Constitution's Appointments Clause—and therefore must be appointed by the President, "Courts of Law," or "Heads of Departments." In practice, the ruling means that the five current ALJs who have been hired by SEC staff, rather than by the SEC commissioner, were unconstitutionally appointed and that their rulings to date are invalid.

The case was brought by Raymond Lucia, best known for the marketing of his "Buckets of Money" retirement savings plan. Lucia challenged the validity of an SEC proceeding in which an ALJ charged him with violating certain securities laws. Citing *Freytag v. Commissioner*—a 1991 Supreme Court decision holding that "special trial judges" ("STJs") of the United States Tax Courts are "Officers of the United States"—Lucia argued that the SEC's ALJs should likewise be treated as officers, given the similar powers and responsibilities of the two sets of judges. The D.C. Circuit rejected Lucia's argument, holding that SEC ALJs are "mere employees—officials with lesser responsibilities who are not subject to the Appointments Clause." The Supreme Court granted certiorari and reversed by a 7–2 vote.

Justice Kagan's opinion for seven Justices rejected the D.C. Circuit's view, holding that SEC ALJs are "near-carbon copies" of the STJs that were held to be "Officers" in *Freytag*. Traditionally, the Court has set forth two factors for delineating "Officers": they (1) must hold a "continuing and permanent" office established by law, and (2) must wield "significant authority." The majority found it "unnecessary" to elaborate on this traditional framework on account of the close factual parallels with *Freytag*. The Court reasoned that, like the STJs in *Freytag*, SEC ALJs (1) "take testimony," (2) "conduct trials," (3) "rule on the admissibility of evidence," and (4) "have the power to enforce compliance with discovery orders." Indeed, SEC ALJs exercise even more autonomy than STJs, in that major ALJ decisions need not always be reviewed by a higher judge or commission. Thus, the Court reversed the D.C. Circuit decision and remanded the case for further proceedings under a properly appointed ALJ.

Justice Thomas concurred, joined by Justice Gorsuch, noting that the SEC ALJs "easily qualify" as "Officers" under the Founders' understanding of "Officers" as "all federal civil officials with responsibility for an ongoing statutory duty."

Justice Breyer concurred in part and dissented in part, concluding that the ALJ's appointment violated the Administrative Procedure Act, as the SEC unlawfully delegated the appointment power to its staff. In Justice Breyer's view, before deciding whether ALJs are "Officers," the Court should first "decid[e] . . . what effect that holding would have on the statutory 'for cause' removal protections that Congress provided for [ALJs]." If being an "Officer" means ALJs could be fired at will, Breyer would not conclude that they are "Officers."

Justice Sotomayor dissented, joined by Justice Ginsburg. She explained that one should not be deemed an "Officer" under federal law if she lacks "the ability to make final, binding decisions on behalf of the Government." Because ALJs can issue only "initial" rulings subject to the SEC's review, she reasoned, ALJs should not be considered "Officers."

Yesterday's decision may make SEC ALJs somewhat more accountable to the President, who ultimately answers to the electorate, rather than to the non-political SEC staff. But the Court side-stepped a second question that the Solicitor General had urged it to address—"whether the statutory restrictions on removing the Commission's ALJs are constitutional." (Interestingly, the SEC-appointed judge in Lucia's case did not rule against the SEC a single time in his first 50 cases and adopted a bright-line rule of banning employment in the investment industry for any defendant who contested proceedings against the SEC.) Further, the Court's decision will prompt a close look at the responsibilities and appointment procedures for some 1,930 ALJs throughout the federal government—which some estimate are presiding in well over a million pending cases.
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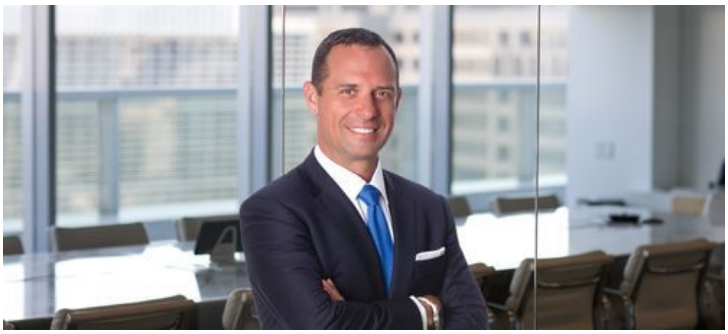

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