No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA, ET AL.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

BRIEF FOR THE CATO INSTITUTE AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Can an executive agency's officers investigate, prosecute, and adjudicate disputes without oversight from the chief executive?

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INTEREST OF THE *AMICUS CURIAE*[1]

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Robert A. Levy Center for Constitutional Studies was established in 1989 to promote the principles of limited constitutional government that are the foundation of liberty. Toward those ends, Cato publishes books and studies, conducts conferences, issues the annual *Cato Supreme Court Review*, and files *amicus* briefs.

This case is important to Cato because it concerns core separation-of-powers issues and the democratic accountability of executive officers.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Constitution created three branches of government. The legislative and executive branches are controlled by the electorate. The president is vested with all executive power, and therefore controls the executive branch. 1 Annals of Cong. 481 (James Madison, June 16, 1789) ("[I]f any power whatsoever is in its nature executive, it is the power of appointing, overseeing, and *controlling* those who execute the laws.") (emphasis added). The president has a duty to see that the law is faithfully executed. To do this he must be able to remove those officers who fail in their duties.

And yet, the SEC's administrative law judges (ALJs) are protected from control by the electorate.

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[1] Rule 37 statement: All parties lodged a blanket consent with the Clerk. No party's counsel authored any of this brief. No person other than *amicus* funded its preparation and submission.

The president lacks the ability to remove ALJs should they abuse their powers or fail to use their discretion to act intelligently or wisely.

The D.C. Circuit ruled that ALJs need not be subject to presidential removal because they are not executive officers. When the case was reheard *en banc*, the court deadlocked 5–5, leaving in place the panel's earlier characterization of ALJs as something less than the category of officers subject to the removal power. But ALJs' duties are similar to Special Trial Judges (STJs) and court clerks, positions the Court has previously determined to be officers. If anything, ALJs have more power and exercise their duties with greater discretion and independence than STJs or court clerks.

The similarities between ALJs and court clerks or STJs are alone enough to show that ALJs are officers. Even more, ALJs fit the definitions of an "executive officer" established by legal and historical precedent. Chief Justice John Marshall articulated a test for distinguishing an officer from an employee. In *United States v. Maurice*, 26 F. Cas. 1211 (C.C.D. Va. 1823), he explained that if a position did not require a contract because the government had prescribed duties of the position independent of a specific position-holder—and that successive holders' duties would not change—then that position is an office, and thereby its holder an officer. The Court later expanded on Marshall's criterion by setting parameters for the tenure, duration, compensation, and duties of an officer. Parameters that distinguish an officer from an employee. Evaluating the ALJ role against these parameters demonstrates that ALJs are officers, not employees. Most im-

portantly, ALJs have significant discretion and perform more than ministerial duties, which, based on the Court's definitions, makes them ALJs officers.

Both Congress and the SEC have recognized that ALJs are officers. Considering how much more closely the ALJ position aligns with the definition of an officer than that of an employee, this should not be a surprise.

The quasi-judicial nature of an ALJ's role does not change their status as officers. The Court established that presidential accountability applies to officers with a quasi-judicial function over 90 years ago. It held that, even for a quasi-judicial executive officer, the president "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." *Myers v. United States*, 272 U.S. 52, 135 (1926). Precedent going back to the Founding also supports the notion that SEC ALJs must be subject to executive oversight. The Comptroller of the Treasury was then considered quasi-judicial for the same reasons an ALJ should be so considered today, yet still removable by the president. The president has also removed territorial judges, demonstrating that the judicial character of an executive-branch officer does not change the president's authority to remove that officer.

This case presents an important application of the Appointments Clause. Accepting arguments like those presented here, the Tenth Circuit rightly concluded that ALJs are officers in *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016). The Court should similarly hold that ALJs are officers who must be appointed in accordance with Article II, ensuring proper accountability and adherence to basic constitutional principles.

ARGUMENT

I. SEC ALJS ARE EXECUTIVE OFFICERS BECAUSE OF THEIR DISCRETION AND POWER

ALJs are officers, not employees, because of the discretion they wield and the power they exercise. The close similarities between ALJs and STJs or court clerks—positions that the Court has deemed to be offices—are sufficient proof that ALJs are officers. Moreover, ALJs fit multiple legal and historical definitions of officers. On this, the D.C. Circuit erred.

A. ALJs Have Duties and Powers Similar to Other Positions That the Court Has Held to Be Offices

ALJs perform many important functions, including, critically, shaping the evidentiary record, evaluating witness credibility, and rendering decisions and findings of fact after contested trial-like proceedings. 17 C.F.R. §201.111. These factors alone are more than enough to render them officers, as *Freytag v. C.I.R.* makes abundantly clear 501 U.S. 868 (1991).

In *Freytag*, the Court determined that STJs are executive officers because of their discretion and power. *Id*. at 881-82. There is no material difference between the discretion and power STJs and SEC ALJs exercise. Like the *Freytag* STJs, SEC ALJs "perform more than ministerial tasks." *Id.* at 881. They too "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-82; 17 C.F.R. §201.111. And, like STJs, ALJs "exercise significant discretion in the course of carrying out their duties." *Freytag*, 501 U.S. at 881-82; 17 C.F.R. §201.111. ALJs notably use

their discretion to make findings as to the credibility of witnesses and the SEC defers to ALJs' "credibility finding, absent overwhelming evidence to the contrary." *In re Clawson*, Exchange Act Release No. 48143, 2003 WL 21539920, at *2 (July 9, 2003); *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."); *Universal Camera Corp. v. N.L.R.B.*, 340 U.S. 474, 496 (1951). Moreover, the opinions ALJs issue are final unless appealed and *Freytag* emphasized the importance of STJs' power to issue opinions. 5 U.S.C. § 557(b); *Freytag*, 501 U.S. at 882 (noting that the fact that the STJ can "render the decisions of the Tax Court" in some cases is enough to be considered an officer).

The ALJs' authority also mirrors that of court clerks, which, under the Court's determination, rendered them officers. *See Ex parte Hennen*, 38 U.S. 230, 260 (1839) ("These clerks fall under that class of inferior officers, the appointment of which the Constitution authorizes Congress to vest in the head of the department."). This despite the fact that clerks have no power to make final decisions for the court outside of default judgments (which can be rescinded by the court). FRCP 77(2); FRCP 55(b)(1)—as can ALJs, 17 C.F.R. § 201.155, who can also reject deficient filings as some clerks can, 17 C.F.R. § 201.180 (b), (c). Clerks can administer oaths and affirmations, 28 U.S.C. § 953, as can ALJs. 17 CFR 201.111(a). There is no power or discretion that clerks have that ALJs do not.

Since these powers make a clerk an "officer of the United States," they have the same effect on ALJs.

The panel below ruled that SEC ALJs are not officers because their decisions are not final (in that they are appealable to the Commission). *Raymond J. Lucia Cos., Inc. v. SEC*, 832 F. 3d 277, 285 (D.C. Cir. 2016). This argument fails in the face of respondents' actual experience appearing before SEC ALJs. Although ALJs' rulings on questions of law are subject to review, their findings of fact are nearly unassailable and are given great deference by the Commission. That is, of course, assuming that a respondent proceeds so far as to obtain an appealable decision. As many as half of SEC enforcement actions result in settlement with up to 80 percent of those settlements being concluded during administrative proceedings. Urska Velikonja, *Securities Settlements in the Shadows*, 126 Yale L.J. Forum 124 (2016). The tenor of administrative proceedings, set in the SEC almost exclusively by the ALJs, inform both respondents' decisions and their counsels' admonitions regarding the wisdom of settlement. If most respondents never make their case before the Commission and if those who do are almost irretrievably bound by the factual determinations of ALJs, it is difficult to see how the existence of such limited review can be controlling. If it is true that "[w]ise observers have long understood that the appearance of justice is as important as its reality," it must also be true that appearance of justice does not trump actual injustice in practice. *J.E.B. v. Ala. ex rel. T.B.*, 511 U.S. 127, 161 n.3 (1994) (Scalia, J., joined by Rehnquist, C. J., and Thomas, J., dissenting).

B. SEC ALJs Fit Legal Precedents and Historical Definitions of Officers

There are also important historical precedents for considering ALJs to be officers. At the Founding, jurists understood that a position's holder must be an officer if executing the duties of that position entailed exercising coercive authority over others. "It is a rule, that where one man hath to do with another's affairs against his will, without his leave, that is an office, and he who is in it, an officer." Giles Jacob, A New Law Dictionary 641 (10th ed. 1773).

The first Supreme Court justice to consider the characteristics that distinguish officers from employees was Chief Justice John Marshall, in *United States v. Maurice*, 26 F. Cas. 1211 (C.C.D. Va. 1823). That case required the Court to determine if an agent for fortifications was an officer of the United States. The opinion in that case established general criteria for determining whether a position is or is not an office:

> An office is defined to be "a public charge or employment," and he who performs the duties of the office, is an officer. If employed on the part of the United States, he is an officer of the United States. Although an office is "an employment," it does not follow that every employment is an office. A man may certainly be employed under a contract, express or implied, to do an act, or perform a service, without becoming an officer. But if a duty be a continuing one, which is defined by rules prescribed by the government, and not by contract, which an individual is appointed by government to perform, who enters on the duties appertaining to his station, without any contract defining them, if those duties continue, though the person be changed; it seems very difficult to distinguish such a

> charge or employment from an office, or the person who performs the duties from an officer.

Id. at 1214.

To Marshall, it was the lack of a contract to perform a service in which different people may consecutively hold the same position that distinguishes an "office" from employment. *Maurice*, 26 F. Cas. at 1214. The Court cited Marshall's definition of an office in a later case regarding the status of a merchant appraiser. *Auffmordt v. Hedden*, 137 U.S. 310, 327 (1890). Marshall's definition applies to an SEC ALJ, who is not under contract to perform a service but rather "enters on the duties appertaining to his [or her] station" and that "those duties continue, though the person be changed." The criteria the Court applied in *Auffmordt* provides even more support for classifying SEC ALJs as the officers they are. *See Id.* 5 U.S.C. § 3105.

In *United States v. Hartwell*, the Court issued another, more comprehensive definition of "office," which ALJs fit absolutely. 73 U.S. 385 (1867). "[A]n office is a public station, or employment, conferred by the appointment of government" and "[t]he term embraces the ideas of tenure, duration, emolument, and duties." *Id.* at 393. The Court applied these requirements and found that n officer is someone "appointed pursuant to law, and his compensation was fixed by law." *Id.* An ALJ is likewise appointed pursuant to law and the compensation is fixed by law. 5 U.S.C. § 3105; 5 U.S.C. § 5372. The Court then noted that "[v]acating the office of his superior would not have affected the tenure of his place," *Hartwell*, 73 U.S. at 393, underlining the independent nature of an office. An ALJ's tenure is likewise unaffected by the removal of another person

from office. Finally, the Court recognized that an officer's "duties were continuing and permanent, not occasional or temporary," *id.*, accurately describing an ALJ's duties. 5 U.S.C. § 7521.

The Court expanded on that definition to require that one must be "exercising significant authority" to be considered an officer. *Buckley v. Valeo*, 424 U.S. 1, 126 (1976). This expansion was not meant to challenge prior understandings of officer status, but to crystalize the reasoning that led the Court to determine district court clerks and postmasters first class to be inferior officers. *Id. Buckley's* definition of officer included "all appointed officials exercising responsibility under the public laws of the Nation." *Id.* at 131. The panel's reliance on *Buckley* was thus misplaced.

In *Buckley*, the Court distinguished employees from officers by describing them as "lesser functionaries subordinate to officers of the United States." *Id.* The Court's decision in *Freytag* reflected this distinction, as it determined that special trial judges are officers because they "perform more than ministerial tasks" and exercise "significant discretion." *Freytag*, 501 U.S. at 881-82. *Buckley's* emphasis on the relative independence of a position and its organizational relationship to other officers closely pertains to SEC ALJs. The statutory framework governing the authority of ALJs ensures that they are not directly controlled by any other officer. 5 U.S.C. § 7521(a).

Considering the independence of and discretion wielded by the SEC's ALJs in the context of relevant historical and legal precedents, it is clear why Congress considers ALJs to be officers. The SEC's enabling statute provides that ALJs' authority to hold hearings is predicated upon their status as officers. 15 U.S.C. §

77u ("All hearings shall be public and may be held before the Commission or an *officer or officers* of the Commission designated by it.") (emphasis added); *see also* 17 C.F.R. § 201.111 (SEC regulation referring to an ALJ as a "hearing officer").

II. ADMINISTRATIVE LAW JUDGES' PROTECTION FROM REMOVAL IS UNCONSTITUTIONAL UNDER THE APPOINTMENTS CLAUSE

The Constitution guarantees that even officers who are appointed (not elected) are nonetheless accountable to the people. Although the Constitution offers no explicit guidance on removals, jurists have understood that removals "empower the President to keep these officers accountable" including through the removal of the officers if necessary. *Free Enter. Fund v. Pub. Co. Acc'ting Oversight Bd.*, 561 U.S. 477, 483 (2010).

A. ALJs Must Be Removable by the President to Ensure Democratic Accountability for Executive Officers

Since the Founding, jurists have understood that the president, to fulfill his constitutional duty to ensure that the laws be faithfully executed, must have the power to remove executive officers. The Constitution does not specify how an officer can be removed (other than impeachment), and so a debate occurred in the First Congress over the presidential power to remove officers. Some felt that impeachment was the only proper method of removal because it was the only one specifically mentioned. James Madison disagreed, declaring that "it is absolutely necessary that the President should have the power of removing from office; it will make him, in a peculiar manner, responsible for

their conduct, and subject him to impeachment himself, if he suffers them to perpetrate with impunity high crimes or misdemeanors against the United States, or neglects to superintend their conduct, so as to check their excesses." 1 Annals of Congress 387 (1789). Such a power to remove officers was seen at the time as "incident to the power of appointment." *Myers*, 272 U.S. at 110 (1926).

Madison did not consider this power to remove to be absolute, but "because Congress may establish offices by law," Congress could decide if the officer's tenure was "either during good behavior or during pleasure." 1 Annals of Congress 389 (1789). In the end of the debate, the First Congress by a "considerable majority" resolved "the power of removal to be in the President." *Id.* at 399.

Despite Congress's authority to grant tenure for good behavior, as of 1903 "no civil officer [had] ever held office by a life tenure since the foundation of the government" with the exception of Article III judges. *Shurtleff v. United States*, 189 U.S. 311, 316 (1903). When Congress attempted to condition the removal of a postmaster on congressional approval, the Court held that to be an unconstitutional limitation on the power of the president. *Myers*, 272 U.S. at 176.

If a limitation on the president's removal power is unconstitutional, it is immaterial which entity exercises the limitation. If it is unconstitutional to condition the president's removal power on the Senate's consent, it is equally unconstitutional to condition the removal power on the consent of the Merit Systems Protection Board (MSPB). As Madison said, if the executive officer "shall not be displaced but by and with the advice and consent of the senate, the President is no

longer answerable for the conduct of the officer; all will depend on the senate. You here destroy a real responsibility without obtaining even the shadow." 1 Annals of Congress 394-95. Likewise, the president is not fully answerable for the conduct of ALJs who cannot be removed without the advice and consent of the MSPB (which also cannot be removed but for cause). When an ALJ goes beyond the powers of that office, but the MSPB refuses to exercise its removal power, which elected official are the American people to blame?

B. SEC ALJs Are Not Democratically Accountable, Because Their Removal Involves Two Layers of Protection

SEC ALJs are inferior officers that are protected from presidential removal by at least two layers of for-cause removal protection. Permitting an executive officer to enjoy such insulation from removal unconstitutionally prevents the president from exercising the necessary control to be politically accountable for the actions of the officer. *Free Enter. Fund*, 561 U.S. at 477.

The first layer of protection exists at the SEC level. The SEC can only remove an ALJ "for cause." 5 U.S.C. § 7521(a). Second, that determination of cause must be confirmed by the MSPB. MSPB members themselves can only be removed "for cause." *Id.*; 5 U.S.C. § 1202. Therefore, the judgment that an SEC ALJ should be removed for cause is "committed to another officer, who may or may not agree with the president's determination, and whom the President cannot remove simply because that officer disagrees with him." *Free Enter. Fund*, 561 U.S. at 484. Moreover, *Free Enterprise Fund* established that SEC commissioners themselves are only removable for

cause, *id.* at 487. Assuming that the Court was correct in *Free Enterprise Fund,* there exist in fact three layers of insulation between SEC ALJs and the president because commissioners themselves must initiate the removal proceedings against ALJs. 5 U.S.C. § 7521(a).

C. Even Officers in Quasi-Judicial Roles Like ALJs Must Be Removable by the President

Historical precedent going back to the Founding and this Court's direct on-point holdings show that even federal officials serving "quasi-judicial" roles like the ALJ position must be removable by the president.

The Court has held that even executive officers with a quasi-judicial role must not be beyond the president's power to remove any officer who fails to exercise the discretion required of the office intelligently or wisely. As it said in *Myers*:

> 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.

272 U.S. at 135.

The president's power to remove quasi-judicial officers is not absolute like the power to remove purely executive officers; Congress can limit the removal of such quasi-judicial officers to "for-cause" reasons. *Humphrey's Executor v. United States*, 295 U.S. 602, 629 (1935). The removal for-cause still allows the president to see that the laws "be faithfully executed" but only so long as the president exercises direct authority to remove the officer for cause, or the power is exercised by an individual the president can remove without cause. *Free Enter. Fund*, 561 U.S. at 495-96.

History also shows that quasi-judicial executive officers must be subject to the presidential removal power. The first discussion of a quasi-judicial executive officer's removal occurred during the First Congress when considering the removal of the Comptroller of the Treasury. The Comptroller, due to his authority to decide claims between the United States and individual citizens, exercised power that was "not purely executive" but also included a "judicial quality." 1 Annals of Congress 635-36 (1789). Because of the quasi-judicial character of the office, Madison proposed that the tenure of the office be for "good behavior," but even so "the Comptroller would be dependent upon the President, because he can be removed by him." *Id.* Tenure based only on "good behavior" was necessary to "secure his impartiality," but even the need for impartiality was not sufficient to shield the officer entirely from the president's removal power. *Id.* This for-cause protection was too much for many of the other members of the First Congress and Madison eventually withdrew his motion. *Id.* at 637-39. The Court revived Madison's position in *Humphrey's Executor*, implementing his idea of limiting the removal of quasi-judicial executive

officers. Still, the president retained the power to remove the quasi-judicial officer for cause.

ALJs fulfill a more purely judicial function than either members of the Federal Trade Commission or the Comptroller of the Treasury. Their role may be more properly analogous to other non-Article III federal judges. While the president has never removed an Article III judge—the Constitution insulates them from such action—the president has removed many Article I judges without even giving cause and without congressional authorization. The power to remove these judges is essential to the president's ability to fulfill his duty. Before the Civil War, Attorney General John J. Crittenden was specifically asked about the presidential power to remove territorial judges, even without congressional authorization. He concluded:

> The President of the United States is not only invested with authority to remove the Chief Justice of the Territory of Minnesota from office, but it is his duty to do so if it appear that he is incompetent and unfit for the place. . . . Being civil officers, appointed by the President, by and with the advice and consent of the Senate, and commissioned by the President, they are not exempted from that executive power which, by the constitution, is vested in the President of the United States over all civil officers appointed by him.

5 U.S. Op. Atty. Gen. 288, 290 (1851). Crittenden opined that this removal power "has been long since settled, and . . . has ceased to be a subject of controversy or doubt." *Id.*

Then in *McAllister v. United States*, the Court interpreted the general statutory provisions for removal and replacement of "any civil officer . . . except judges of the courts of the United States" by the president as allowing the president to remove territorial judges. 141 U.S. 174 (1891). The quasi-judicial character of the office did not change the president's power to remove such executive officers.

When considering Congress's removal of the Comptroller General, the Court stated that "[i]nterpreting a law enacted by Congress to implement the legislative mandate" and "exercis[ing] judgment concerning facts that affect the application of the Act" are "[d]ecisions of that kind are typically made by officers charged with executing a statute." *Bowsher v. Synar*, 478 U.S. 714, 733 (1986).

The D.C. Circuit, in *Kuretski v. C.I.R*, also considered the presidential removal of tax judges. In that case, the court held: "A tribunal may be considered a 'Court of Law' for purposes of the Appointments Clause notwithstanding that its officers may be removed by the President. The *Freytag* Court's treatment of territorial courts confirms the point." *Kuretski v. C.I.R.*, 755 F.3d 929, 941 (D.C. Cir. 2014), *cert. denied*, 135 S. Ct. 2309 (2015).

These examples include executive officers who exercise quasi-judicial functions as well as Article I judges that preside over a "court of law." ALJs sit somewhere in the middle of this continuum. That it is well-settled that the president must have the power to remove officers sitting at both ends of this spectrum, however, confirms that he must at least have the power to remove officers in the middle of it for cause.

* * *

In sum, ALJs are located squarely within the executive branch and remain executive officers who should be subject to control by superior officers (here the Commission) and ultimately the president. The Appointments Clause serves to control these officers at the front end, and the removal clause the back, as the Court has made clear in the series of cases that culminated in *Free Enterprise Fund*. The Court in that case simply set the question of ALJs aside, *Free Enter. Fund*, 561 U.S. at 507 n.10, but there is no constitutional basis to consider any type of executive officer in any way "immune" from the requirement of removability inherent in the separation of powers. If the Court were to recognize ALJs as a class of officers immune from removal by virtue of their quasi-judicial function, it would in effect be manufacturing a fourth branch of government.

CONCLUSION

Our Constitution requires that our government remain democratically accountable, so *amicus* asks the Court to reverse the D.C. Circuit and find that ALJs are officers of the United States and thus removable by the president.

Respectfully submitted,

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