

No. 08-861

THE MORRIS TYLER MOOT COURT OF APPEALS AT YALE

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FREE ENTERPRISE FUND, et al.,

Petitioners,

v.

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD, et al.,

Respondents.

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

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BRIEF FOR THE PETITIONERS

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## QUESTIONS PRESENTED<sup>1</sup>

In response to a series of highly publicized corporate accounting scandals in 2001 and 2002, Congress passed the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745. Title I of that Act established an independent Public Company Accounting Oversight Board to oversee the auditing of public companies throughout the United States. Two questions are presented for this Court's consideration:

- 1) Does the Securities and Exchange Commission's appointment of Board members, who exercise substantive policymaking and enforcement functions without ongoing direction and supervision by a superior officer, violate the Constitution's Appointments Clause?
- 2) Does the Act, by vesting appointment and removal authority over Board members in another independent agency and providing that those members may only be removed for cause, interfere with the President's constitutionally appointed duty to ensure the faithful execution of the laws in contravention of separation of powers?

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<sup>1</sup> The petitioners in this action are Free Enterprise Fund and Beckstead & Watts, LLP. The respondents are the Public Company Accounting Oversight Board and the United States of America.

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## OPINIONS BELOW

The opinion of the U.S. District Court for the District of Columbia is available at *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 2007 WL 891675 (D.D.C. 2007) [hereinafter *PCAOB I*]. The opinion of the panel of the U.S. Court of Appeals for the District of Columbia Circuit affirming the district court's judgment is reported at *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 537 F.3d 667 (2008) [hereinafter *PCAOB II*].

## STATEMENT OF JURISDICTION

The judgment of the D.C. Circuit panel was entered on August 22, 2008. A request for rehearing en banc was denied on November 17, 2008. A petition for a writ of certiorari was filed on January 5, 2009. This Court subsequently granted the petition for a writ of certiorari. This Court's jurisdiction rests on 28 U.S.C. § 1254(1).

## CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The following is a list of the constitutional and statutory provisions involved in this case. For the full text of the constitutional and statutory provisions, please see the attached appendix.

U.S. Const. art. II, §§ 1-3  
SOX § 101(a), (c), (e), 15 U.S.C. § 7211(a), (c), (e)  
SOX § 103(a)(1), 15 U.S.C. § 7213(a)(1)  
SOX § 104, 15 U.S.C. § 7214  
SOX § 105(a), (c), (e), 15 U.S.C. § 7215(a), (c), (e)  
SOX § 107, 15 U.S.C. § 7217  
SOX § 109(a), (c), (d), 15 U.S.C. § 7219(a), (c), (d)

## STATEMENT OF FACTS

### **I. The Public Company Accounting Oversight Board**

In response to several highly publicized accounting scandals at corporations including Enron and WorldCom, Congress hastily passed into law the Sarbanes-Oxley Act of 2002 ("SOX" or "Act"), Pub. L. No. 107-204, 116 Stat. 745 (codified as amended at 15 U.S.C. §§

7201 *et seq.*). A central feature of the Act was the creation of the Public Company Accounting Oversight Board (“PCAOB” or “Board”), an independent agency tasked with “oversee[ing] the audit of public companies that are subject to the securities laws.” SOX § 101(a), 15 U.S.C. § 7211(a). This independent Board was designed to be insulated from the influence of the largely self-regulated accounting industry, which had brought an “extraordinary amount of political pressure” to bear on the Securities and Exchange Commission (“SEC” or “Commission”) when it attempted to impose new accounting standards. *See Hearing on Enron Accounting and Investor Issues Before the S. Comm. on Banking, Housing, and Urban Affairs*, 107th Cong. 44 (2002) (statement of Arthur Levitt, former SEC Chairman). The Board was thus organized “to minimize as much as possible any potential unhealthy public or private pressure on the setting of accounting standards,” *id.* at 13 (statement of Sen. Dodd), including pressures emanating from Congress and the SEC itself.

Congress had initially considered a number of arrangements that would have housed these oversight functions within the SEC, including a law requiring the SEC to establish an Office of Audit Review, H.R. 5184, 107th Cong. (2002), and a law delegating to the SEC authority to promulgate regulations to promote auditor independence, S. 2056, 107th Cong. § 2 (2002). Congress, however, rejected these alternatives and chose to vest the new rulemaking and oversight authority in an independent Board that would, in the words of one of its supporters, wield “massive . . . unchecked power, by design.” 148 Cong. Rec. S6334 (daily ed. July 2, 2002) (statement of Sen. Gramm).

The resulting arrangement, the PCAOB, consists of five members who are appointed by the SEC to staggered five-year terms. SOX § 101(e), 15 U.S.C. § 7211(e). It possesses four principle powers under the Act, in addition to a catch-all authorization to “perform such other

duties or functions as the Board . . . determines are necessary or appropriate . . . to carry out this Act, in order to protect investors, or to further the public interest.” *Id.* § 101(c)(5), 15 U.S.C § 7211(c)(5).

First, the Board possesses broad rulemaking powers affecting all publicly traded companies in the country, along with their auditing firms. The Act commands the Board to establish binding auditing rules and independence standards regulating the preparation of audit reports for public companies, “as may be necessary or appropriate in the public interest or for the protection of investors.” *Id.* § 103(a)(1), 15 U.S.C. § 7213(a)(1). Violations of these rules are treated as violations of the Securities Exchange Act of 1934 and carry severe consequences, including revocation of a firm’s ability to conduct audits of public companies, imposition of up to \$15 million in fines, and up to twenty years’ imprisonment. *Id.* § 105(c)(4), 15 U.S.C. § 7215(c)(4); 15 U.S.C. § 78ff (as made applicable by SOX § 3(b), 15 U.S.C. § 7202(b)).

Second, the Board has the power to enforce its regulations by conducting inspections of accounting firms at will. Although the statute provides a mandatory initial inspection schedule, the Board may alter that schedule by rule and conduct “special inspections” of any firm at any time. SOX § 104(b)(2), 15 U.S.C. § 7214(b)(2). During an inspection, the Board can test a firm’s auditing procedures to whatever extent it determines is “necessary and appropriate.” *Id.* § 104(d)(3), 15 U.S.C. § 7214(d)(3). It may also demand production of “any record in the possession, custody, or control of such firm or person” that it deems relevant. Board Rule 4006, [http://www.pcaobus.org/Rules/Rules\\_of\\_the\\_Board/Section\\_4.pdf](http://www.pcaobus.org/Rules/Rules_of_the_Board/Section_4.pdf) (last visited Apr. 25, 2009).

Third, the Board has the authority to conduct formal investigations “of any act or practice, or omission to act” by an accounting firm that “may violate” the Act, Board rules, relevant securities laws, or professional standards. *Id.* § 105(b)(1), 15 U.S.C. § 7215(b)(1). As

part of an investigation, the Board has complete discretion to compel testimony and the production of documents. *Id.* § 105(b)(2), 15 U.S.C. § 7215(b)(2). If the Board finds a violation, it may impose a wide range of sanctions “as it determines appropriate.” *Id.* § 105(c)(4), 15 U.S.C. § 7215(c)(4).

Fourth, the Board has authority to support its operations by levying a tax — called an “accounting support fee” — on any publicly traded company in the United States. SOX § 109(d), 15 U.S.C. § 7219(d). The statute does not limit or cap the amount of funds the Board can raise through such fees, which are now levied on about 15,000 companies, *see* List of Issuers with No Outstanding Past-Due Share of the Accounting Support Fee (2009), [http://www.pcaob.org/Support\\_Fees/Issuers\\_Paid.pdf](http://www.pcaob.org/Support_Fees/Issuers_Paid.pdf) (last visited Apr. 25, 2009), and which, along with other Board-imposed fees, fund the entirety of the Board’s operations. SOX § 109(c)(1), 15 U.S.C. § 7219(c)(1). The funds are exclusively for the Board’s use and cannot be siphoned by the SEC, as they are not considered “public monies of the United States.” *Id.* The Board also wields the authority to set its own budget, which is not subject to any statutory cap. *Id.* § 109(b), 15 U.S.C. § 7219(b).

Reflecting Congress’s intention to create a Board independent from outside control, the Act provides for only the most limited oversight by the Commission. Thus, while the Board’s rules and standards cannot take effect without SEC approval, the SEC is obligated to approve any rule “if it finds that the rule is consistent with the requirements of this Act and the securities laws, *or* is necessary or appropriate in the public interest or for the protection of investors.” *Id.* § 107(b)(3), 15 U.S.C. § 7217(b)(3) (emphasis added). The SEC may amend Board rules and rescind the Board’s enforcement authority, *id.* § 107(d)(1), 15 U.S.C. § 7217(d)(1), but only through cumbersome and time consuming notice-and-comment procedures. 15 U.S.C. § 78s(c)

(made applicable by SOX § 107(b)(5), 15 U.S.C. § 7217(b)(5)). The SEC may also censure or impose limitations on the Board's activities but only upon showing, "on the record" and "after notice and opportunity for a hearing" that the Board "violated or is unable to comply" with the Act or "without reasonable justification or excuse, has failed to enforce compliance" with the Act or rules promulgated thereto. *Id.* § 107(d)(2), 15 U.S.C. § 7217(d)(2).

The Board's independence is even greater with respect to its enforcement functions. Thus, the SEC exercises no control over which firms the Board investigates or inspects and with what frequency. *Id.* § 105(b)(1), 15 U.S.C. § 7215(b)(1). Nor can it manage the Board's methods of conducting these inspections. *Id.* § 105(b)(2), 15 U.S.C. § 7215(b)(2). The SEC lacks any authority whatsoever to affirmatively order the Board to investigate certain firms or recommend sanctions. *Id.* § 107(c)(3) (limiting the SEC's authority to altering only existing Board-imposed sanctions).

Finally, the Board is further shielded from any meaningful SEC oversight by exceptionally strong tenure protections. Its members can only be removed if the majority of the Commissioners find, "on the record, after notice and opportunity for a hearing" that a member (1) "*willfully* violated any provision of this act, the rules of the Board, or the securities laws," (2) "*willfully* abused [her] authority" or (3) "without reasonable justification or excuse, has failed to enforce compliance" with any provision, rule, or professional standard promulgated under the Act. *Id.* § 107(d)(3), 15 U.S.C. § 7217(d)(3).

## **II. Procedural History**

Beckstead & Watts, LLP, is a small Nevada accounting firm that was the subject of a Board inspection in 2004 and a Board investigation beginning in 2005. *PCAOB II*, 537 F.3d at 670; *PCAOB I*, 2007 WL 891675, at \*2. It joined with the Free Enterprise Fund, a non-profit

public interest organization representing Beckstead & Watts and other firms affected by the Board's activities, to bring this suit in the U.S. District Court for the District of Columbia. Petitioners sought an order enjoining the Board from taking further action against Beckstead & Watts and a judgment declaring that the provisions of the Act establishing the Board violate the appointments clause and separation of powers. *PCAOB II*, 537 F.3d at 670; *PCAOB I*, 2007 WL 891675, at \*2.

The district court rejected petitioners' constitutional claims and granted respondents' motion for summary judgment, concluding that Board members were inferior officers who were properly appointed by the Commission, and that the President exercised sufficient control over the Board, through the SEC, to defeat a separation of powers challenge. *PCAOB I*, 2007 WL 891675, at \*4-5. On appeal, a divided panel of the District of Columbia Circuit affirmed the judgment of the district court for substantially the same reasons. *PCAOB II*, 537 F.3d at 669. The D.C. Circuit denied a petition for rehearing en banc, and petitioners subsequently filed a petition for a writ of certiorari. This Court's review is de novo. See *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 465 n.10 (1992).

### **SUMMARY OF ARGUMENT**

“If there is a principle in our Constitution . . . more sacred than another, it is that which separates the Legislative, Executive, and Judicial powers.” 1 Annals of Congress 603 (Joseph Gales ed., 1834) (remarks of James Madison). Indeed, this Court has always protected this separation of powers “even when . . . no immediate threat to liberty is apparent,” for “[w]hen structure fails, liberty is always in peril.” *Pub. Citizen v. U.S. Dep't of Justice*, 491 U.S. 440, 468 (1989) (Kennedy, J., concurring). This division of powers is not a matter of etiquette or form. Rather, the Framers understood that only a clear assignment of power to the branches would

ensure that the public would know who to reward for that power's proper deployment or punish for its misuse.

To ensure accountability in the Executive Branch, Article II does two things: First, it vests executive power in a single President and gives him the duty — and power — to ensure the faithful execution of the laws. Second, it requires that the President appoint, with the advice and consent of the Senate, the principle officers to whom he entrusts executive authority. The Sarbanes-Oxley Act flagrantly defies these mandates. Notwithstanding their vast policymaking and enforcement powers, the Board's members are appointed and removed (only for cause) by *another independent agency*. The Board thus constitutes an unprecedented “Fifth Branch” of government that is purposefully insulated from meaningful oversight—either in the initial choice of its officers or its ongoing functions—by any public official whom the people can influence through the ballot box. Rather than uphold the Board and countenance the proliferation of such novel statutory creatures, this Court should reverse the opinion of the Circuit Court and declare the Board unconstitutional.

The Act violates the Appointments Clause. That Clause divides all federal officers into two classes: principal officers, who must be appointed by the President and confirmed by the Senate, and inferior officers, who can be appointed solely by the President, the courts, or the “Heads of Departments.” This framework ensures that a democratically elected President will be responsible for important appointments, allowing the people to hold him accountable for the actions of his appointees. Knowing that the voters are watching, the President is motivated to exercise great care and deliberation in the selection of powerful federal officials.

The Sarbanes-Oxley Act trammels upon this carefully crafted constitutional structure by establishing an extraordinarily powerful new agency whose members are appointed not by any

democratically elected official, but rather by another independent agency purposefully shielded from public accountability. This new Board exercises tremendous authority over all publicly traded companies in the United States, with broad authority to promulgate binding rules for accounting firms, to levy taxes, and to conduct wide-ranging inspections and investigations resulting in harsh sanctions. Yet voters incensed at the Board's policies would have no idea which elected officials — if any — to blame at the ballot box; the Act has severed the carefully crafted lines of accountability between the government and its citizens.

The Board members' status as principal officers is confirmed by this Court's precedents and the history of the Appointments Clause, which make plain that the defining characteristic of principal officers is their freedom from the continuous managerial direction of a superior. This is the lesson of *Edmond v. United States*, 520 U.S. 651 (1997), which held that Coast Guard judges subject to ongoing direction and supervision were inferior officers, even though their decisions were subject only to limited review. This principle is also reflected in the accepted principal officer status of ambassadors and consuls — each of whom had significant operational freedom at the time of the Constitution's ratification, although their final decisions were subject to broad after-the-fact review. The same is true of federal judges, who enjoy enormous day-to-day independence and are considered principal officers, despite the fact that their rulings are also subject to extensive review.

The Act guarantees the Board complete independence to conduct inspections, investigations, and enforcement actions. Although the statute provides the SEC with a number of oversight powers, these are all after-the-fact mechanisms of reviewing final Board decisions — not a means to intervene in or direct the Board's ongoing functions. Indeed, the Act purposefully insulates the Board from external interference by allowing the SEC to remove Board members or

limit the operations of the Board only upon meeting extraordinarily high statutory hurdles, and by requiring the SEC to defer to the Board's proposed rules. These flimsy levers of control are insufficient to provide the kind of active, continuous, and comprehensive direction and supervision that rendered the Coast Guard judges inferior in *Edmond*.

Respondents' reliance on this Court's decision in *Morrison v. Olson*, 487 U.S. 654 (1988), is misplaced. *Morrison* did not purport to establish a definitive test for distinguishing principal from inferior officers, as *Edmond* did. But even if *Morrison* were controlling here, the factors deemed relevant to the principal-inferior distinction in that case would plainly indicate that Board members — who exercise sweeping authority, are members of a permanent agency, and are protected by a powerful for-cause restriction on their removal — are principal officers.

Even if Board members were inferior officers, their appointment by the Commissioners would still violate the Appointments Clause, because the Commissioners are not collectively the "Head" of a "Department." This Court has consistently interpreted the term "Department" in the Constitution to refer to the Cabinet-level agencies, which — unlike the SEC — are directly accountable to the President. Moreover, the SEC Chairman exercises all the incidents of executive administration and control over the Commission; it is the Chairman, not the Commissioners as a whole, who heads the agency.

The Act's violation of the separation of powers doctrine is equally clear. The Constitution vests power in a single President to ensure the faithful execution of the laws and this Court has repeatedly found that the Executive's removal power is an indispensable implement in carrying out his constitutionally mandated functions. While the Court has allowed Congress to impose *some* restrictions on the President's authority to remove executive officers, it has been unequivocal that Congress may not "completely strip[]" the President of his removal authority.

*Morrison*, 487 U.S. at 692. Yet the Act does precisely that. Only the SEC — itself insulated from presidential oversight and public accountability by its “for cause” removal protections — may remove a Board member, and only upon a finding by a majority of its Commissioners that the member has willfully violated the Act or unreasonably failed to enforce compliance. The President can no more order the SEC to make that determination than he can order the Federal Reserve Chairman to lower interest rates. Nor could he realistically deploy his own limited removal authority over the Commissioners to cajole them into making such a determination. Even if he could remove the unyielding Commissioners, the Senate would have to confirm their replacements. But those new Commissioners, having been chosen for the willingness to terminate the Board member, would have to recuse themselves from the removal proceedings or else run afoul of the due process dictate that disciplinary adjudicators be impartial. Few Presidents would venture down such a politically costly and uncertain path.

This complete divesture of the President’s removal power should mark the end of this Court’s inquiry. Indeed, it need not—and should not—adopt a nebulous “totality of the factors” test to divine whether the remaining provisions of the Act, when cobbled together, provide other informal avenues for the exercise of presidential influence. The lower court erred in engaging in this type of ad hoc inquiry, which is as perilous as it is contrary to existing precedent. In *Morrison*, this Court was explicit that the President — or his alter ego — must retain at least some direct removal authority. Only *after* it determined that the President retained significant removal authority did it consider whether the rest of the statute provided the *additional* mechanisms necessary to exercise adequate control.

There are sound reasons for requiring direct removal authority, the first of which is the need to ensure executive accountability. The Framers placed responsibility in a unitary executive

because they understood that diffusing such powers would give the President a scapegoat for his failures. They further understood that only where the lines of responsibility were direct and clearly defined could the public identify the blameworthy officials and hold them accountable through the ballot box. But the Sarbanes-Oxley Act is anathema to these dual precepts. It divests the President of his single most visible lever of control — his removal authority — and leaves him only with a hazy set of informal and circuitous conduits through which he can exert influence. Should the President be guilty of negligent inaction in policing Board policy, he may plausibly claim—and the public could not confute—that responsibility lies with a derelict SEC over whom he has limited control. But where the President has removal authority and neglects to properly deploy it, he alone may be blamed. Put differently, this is a case where functionalism is a vice and formalism a constitutional mandate.

Upholding the PCAOB under a “totality of factors” analysis would also be an open invitation for Congress to disperse existing agency powers across a “Fifth Branch” of similarly designed, unaccountable boards. The damage of green-lighting the legislature to fundamentally restructure the Executive branch is substantially enhanced by the lack of any bright-line standard that delimits Congress’ authority to design boards that resemble the PCAOB but deviate in the details. Not only does this leave future policymakers legislating blind, it deprives the courts of any principled standard to assess whether these boards are in compliance with Article II. Mandating the preservation of removal powers provides that bright-line standard.

But even taken as a whole, the Act leaves the President destitute of his necessary oversight powers. Respondents cannot identify a single *direct* tool by which the President can ensure that a Board member is “competently performing his or her statutory responsibilities in a manner that comports with” the Sarbanes-Oxley Act. *Morrison*, 487 U.S. at 692. The lower

court’s assertion that he may influence the SEC, which “in turn” controls the Board is utterly unavailing, 537 F.3d at 680, because it overstates the President’s control over the SEC, the SEC’s control over the Board, and critically, the President’s ability to wield the former to effect the latter. That phrase — “in turn” — is the Board’s constitutional graveman, for it is an effective concession that contrary to the mandates of Article, neither the President nor his alter ego has any unobstructed mechanism to police the Board’s execution of its functions.

## ARGUMENT

### I. THE APPOINTMENT OF BOARD MEMBERS BY THE COMMISSION VIOLATES THE KEY STRUCTURAL SAFEGUARDS OF THE APPOINTMENTS CLAUSE

As an integral part of the Constitution’s separation of powers scheme, the Appointments Clause protects the fundamental principle that those who appoint powerful federal officers must be accountable to the people. The Clause provides that the President:

shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

U.S. Const. art. II, § 2, cl. 2.<sup>2</sup> This Clause was meant, above all, “to ensure public accountability for both the making of a bad appointment and the rejection of a good one.” *Edmond v. United States*, 520 U.S. 651, 660 (1997). It “preserves [an] aspect of the Constitution’s structural integrity by preventing the diffusion of the appointment power,” guaranteeing that appointments

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<sup>2</sup> Respondents concede that the Board members are “Officers of the United States” within the meaning of the Appointments Clause, rather than mere governmental employees. This is a wise concession, for Board members undoubtedly exercise “significant authority pursuant to the laws of the United States” and are thus officers who “must . . . be appointed in the manner prescribed by” the Appointments Clause. *Buckley v. Valeo*, 424 U.S. 1, 126 (1976) (per curiam).

will be made by easily identifiable officials who can be held responsible for their appointees' actions. *See Ryder v. United States*, 515 U.S. 177, 182 (1995) (internal quotation marks omitted).

This carefully designed framework is “more than a matter of ‘etiquette or protocol’; it is among the significant structural safeguards of the constitutional scheme.” *Edmond*, 520 U.S. at 659 (quoting *Buckley v. Valeo*, 424 U.S. 1, 125 (1976) (per curiam)). By vesting the power to appoint principal officers in a single, highly visible President, whose decision must be confirmed by the Senate, the Framers ensured that the people would know who to blame for a poor appointment. *See Freytag v. Comm’r*, 501 U.S. 868, 884 (1991). Likewise, the Clause decrees that the only executive branch officials who may appoint inferior officers are the “Heads of Departments,” who answer directly to the President.

The Board operates in direct contravention of these foundational constitutional principles. Its members exercise wide-ranging authority with no operational oversight whatsoever, but they are appointed by the Commissioners of the SEC — itself an independent agency purposefully insulated from accountability to elected officials. Board members are thus quintessential examples of what the Appointments Clause was designed to protect *against*: extraordinarily powerful and independent bureaucrats who owe their positions not to any democratically elected official, but to *other bureaucrats*. Voters incensed by Board policies would have great difficulty venting their anger at the ballot box: the President, though the head of the executive branch, arguably bears less responsibility for the Board members' actions than the unelected, independent Commissioners — or the members of Congress who created the whole scheme.

Board members are principal officers, who must be nominated by the President and confirmed by the Senate. The Act's provisions establishing the Board are therefore unconstitutional. These provisions would still be unconstitutional even if the Board members

were inferior officers, however, because the Commission is not a “Department,” and the Commissioners are not collectively its “Head.”

**A. Principal Officers Are Those Whose Ongoing Operations Are Not Subject to Managerial, Day-to-Day Supervision and Direction by Superior Officers**

Although the particular characteristics distinguishing principal from inferior officers have often been “far from clear,” *Morrison v. Olson*, 487 U.S. 654, 671 (1988), this Court has long characterized inferior officers as “the mere aids and subordinates of the heads of departments.” *See United States v. Germaine*, 99 U.S. 508, 511 (1879). Both the text of the Appointments Clause and this Court’s precedents recognize that inferior officers are those whose ongoing operations are subject to the managerial control of principal officers. By contrast, the availability of after-the-fact review of an officer’s actions is irrelevant to the determination whether that officer is principal.

These principles underlay this Court’s most recent decision addressing the Appointments Clause in *Edmond v. United States*, 520 U.S. 651 (1997). At issue in *Edmond* was the constitutional status of civilian judges appointed to the Coast Guard Court of Criminal Appeals, an intermediate tribunal that reviewed the judgments of courts-martial. *Id.* at 653, 655. That court was, in turn, subject to the oversight of the Coast Guard’s Judge Advocate General and the United States Court of Appeals for the Armed Forces. *Id.* at 664. This Court concluded that the Court of Criminal Appeals judges were inferior officers because they could be removed without cause, lacked the ability to formulate their own policies and procedures, and were unable to issue binding judgments on behalf of the United States. *Id.* at 664-65.

Generally, under the *Edmond* analysis, an inferior officer must have “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.” *Id.* at 662. But “[i]t is not enough” that an allegedly

inferior officer have a relationship with an officer who possesses greater responsibilities, or a formally higher rank. *Id.* at 662-63. Instead, the *Edmond* test focuses on the *degree of independence* with which the officer in question operates:

[I]n the context of a Clause designed to preserve political accountability relative to important Government assignments, we 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.

*Id.* at 663 (emphasis added). Of particular relevance in this analysis is the ability of other officials to remove the officer in question. This Court has repeatedly recognized that at-will removal authority “is a powerful tool for control,” ensuring that an officer’s day-to-day operations will reflect the wishes of his superiors. *See id.* at 664; *see also Bowsher v. Synar*, 478 U.S. 714, 726 (1986) (“[I]t is only the authority that can remove [an officer] . . . that he must fear and, *in the performance of his functions, obey.*” (emphasis added)).

The *Edmond* Court explicitly rejected the notion that the Coast Guard judges’ status under the Appointments Clause should turn on the degree of after-the-fact review exercised by their superiors. *Id.* at 665. Instead, “[w]hat is significant is that the judges . . . have no power to render a final decision on behalf of the United States unless permitted to do so by other executive officers.” *See id.* Unlike rulings of an ordinary court, the decisions of the Court of Criminal Appeals were not binding and effective unless pre-approved by another official: the Judge Advocate General. The Judge Advocate General, in turn, could not order that a judgment of the Court of Criminal Appeals become effective until he determined that “there is to be [no] further action” by a host of actors — including the President, the Secretary of Transportation, and this Court. 10 U.S.C. § 866(e).

The judges in *Edmond* were thus subjected to an extraordinary degree of operational oversight. They had no authority to formulate policy or procedure, lacked the ability to issue binding judgments without pre-approval, and were removable at will. These powerful forms of control explain why the *Edmond* Court concluded that the Judge Advocate General's inability to interfere in individual cases was irrelevant, *see Edmond*, 520 U.S. at 664; the judges were already subject to their superiors' commanding influence through diverse other mechanisms.

*Edmond* neatly comports with long-settled constitutional understandings and the text of the Appointments Clause itself. Article III judges, for instance, are considered principal officers under the Appointments Clause, according to both this Court's precedent, *see Freytag v. Comm'r*, 501 U.S. 868, 884 (1991), and longstanding constitutional tradition, *see Weiss v. United States*, 510 U.S. 163, 191-92 & n.7 (1994) (Souter, J., concurring). Yet the decisions of lower federal court judges are subject to extensive review and reversal at the hands of higher courts. As in *Edmond*, their status under the Appointments Clause turns not on the availability of after-the-fact review, but rather on the degree to which their ongoing operations are subject to outside direction. Federal judges are principal officers because their activities are strongly insulated from such outside direction through constitutional provisions guaranteeing them life tenure without reductions in salary. *See* U.S. Const. art. III, § 1.

Similarly, the Appointments Clause specifically provides that ambassadors and consuls are principal officers, even though the First Congress considered them subordinates of the Secretary of State and thus subject to the Secretary's oversight and review. *See In re Sealed Case*, 838 F.2d 476, 483 (D.C. Cir.) (citing early congressional materials and statute), *rev'd sub nom. Morrison v. Olson*, 487 U.S. 654 (1988); *Marsh v. Chambers*, 463 U.S. 783, 790 (1983) (accorded special weight to constitutional interpretations of the First Congress). The Framers

presumably understood that ambassadors and consuls would nevertheless often be stationed in distant nations, where the difficulty of reliable and quick communications with the Secretary would give them substantial independence in conducting their day-to-day affairs. Their status as principal officers thus reflects *Edmond*'s understanding of the principal-inferior distinction as concerned not with the scope or availability of after-the-fact review, but rather with the operational independence an officer enjoys.

**B. Board Members Are Principal Officers, Because They Possess Complete Independence in Conducting Ongoing Inspection and Investigation Functions**

The Sarbanes-Oxley Act guarantees the Board complete independence in conducting its day-to-day investigatory and enforcement functions. For instance, the Board is empowered to conduct inspections of public accounting firms at will. SOX § 104(b)(2), 15 U.S.C. § 7214(b)(2). During such inspections, the Board is authorized to examine and test a firm's accounting procedures to whatever degree it, in its sole discretion, deems "necessary or appropriate." *Id.* § 104(d)(3), 15 U.S.C. 7214(d)(3). Yet firms under investigation cannot even *request* Commission review of the Board's actions until the Board has either issued a final report or declared that a firm has failed to resolve accounting problems during the twelve months following a Board inspection report. *Id.* § 104(h)(1), 15 U.S.C. § 7214(h)(1). Similarly, although the Board has tremendous discretion to conduct investigations, compel testimony and document production, and impose a wide variety of sanctions, *see id.* § 105(b), (c)(4), 15 U.S.C. § 7215(b), (c)(4), the Commission has no authority to intervene in Board investigation or enforcement actions. Only *after* the Board has imposed a final sanction — that is, after the Board has completed its investigation and, for its purposes, closed the case — can the Commission institute review. *See id.* § 107(c), 15 U.S.C. § 7217(c).

The Board thus exercises the executive branch’s “core power” to enforce the laws, *see Printz v. United States*, 521 U.S. 898 (1997), with no supervision or direction whatsoever. It is deliberately insulated from Commission review until it has completed its work on each particular inspection or investigation. Indeed, the Board’s complete operational independence is guaranteed by the Act’s text, which provides that “[t]he Board shall . . . set the budget and *manage the operations of the Board and the staff of the Board*,” subject only to limited after-the-fact SEC review. *See* SOX § 101(c)(7), 15 U.S.C. § 7211(c)(7) (emphasis added).

This operational independence has far-reaching consequences. The Board has unfettered and unreviewable discretion to investigate any public accounting firms (or firm personnel) that it determines “may” have violated securities-related laws or rules, or professional standards. *See id.* § 105(b)(1), 15 U.S.C. § 7215(b)(1). Its decision to compel testimony or the production of documents during an investigation is similarly unconstrained and unreviewable. *See id.* § 105(b)(2), 15 U.S.C. § 7215(b)(2). It has unilateral power to conduct “special inspections” of any firm it chooses, for any reason. *See id.* § 104(b)(2), 15 U.S.C. 7214. This unconstrained power to conduct inspections and investigations is highly significant because even inadvertent violations of the Board’s complex and lengthy rules can lead to harsh penalties including fines up to \$2 million for firms and \$100,000 for individuals. *See id.* § 105(c)(4)(D)(i), 15 U.S.C. § 7215(c)(4)(D)(i). Indeed, a firm’s efforts simply to comply with an intrusive, ongoing Board investigation could be enormously expensive.

The Board thus lacks the kind of comprehensive day-to-day managerial control this Court found decisive in *Edmond*. Unlike the judges at issue in *Edmond*, Board members are protected by an extraordinarily powerful for-cause restriction on their removal. *See id.* § 107(d)(3)(A)-(C), 15 U.S.C. § 7217(d)(3)(A)-(C). The Board is also given primary responsibility under the Act for

formulating its own rules of procedure. *See, e.g.*, § 105(a), 15 U.S.C. § 7215(a) (“*The Board shall establish, by rule, . . . fair procedures for the investigation and disciplining of registered public accounting firms and associated persons of such firms.*” (emphasis added)). The Commission cannot promulgate rules for the Board; it is given only the power to amend Board rules already in effect. *See id.* § 107(b)(5), 15 U.S.C. § 7217(b)(5). Finally, unlike the judges in *Edmond*, Board members have the capacity to issue final, binding judgments on behalf of the United States. *See, e.g., id.* § 107(c)(1), 15 U.S.C. § 7217(c)(1) (discussing “the review by the Commission of *final disciplinary sanctions* imposed by the Board” (emphasis added)). Indeed, the statute explicitly provides for Board sanctions to take immediate effect, and only to be stayed upon the Commission’s decision to review the case or receipt of an application for review. *See id.* § 105(e)(1), 15 U.S.C. § 7215(e)(1).<sup>3</sup>

**C. The Commission’s Limited Oversight Authority Is Insufficient To Provide the Supervision and Direction Necessary To Render Board Members Inferior Officers**

Section 107 of the Act gives the Commission authority to review certain final judgments of the Board, to remove Board members, to rescind the Board’s enforcement authority, and to approve and amend Board rules. Respondents’ reliance on this section is misplaced, however, because it does not provide the Commission with power to direct the ongoing operations of the Board — the crucial test under this Court’s case law. Instead, the SEC’s authority under section 107 consists largely of after-the-fact review, particularly with respect to the Board’s investigatory and inspection functions. These review mechanisms are both deferential and limited. For example, the Commission can only amend Board rules and rescind the Board’s

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<sup>3</sup> The Board has *voluntarily* decided, by rule, to impose a stay on its rulings until the period during which the Commission may institute review has expired. *See* 69 Fed. Reg. 29,150-01 (May 20, 2004); Pub. Co. Accounting Oversight Bd., Bylaws and Rules of the Public Company Accounting Oversight Board 88 (2008). The Board still maintains the legal capacity to issue final, effective judgments without the pre-approval of a higher officer, however, because the statute does not require an automatic stay, and the Board has discretion to promulgate a new rule allowing for its judgments to have immediate effect.

enforcement authority after cumbersome notice-and-comment rulemaking procedures that make continuous, day-to-day direction and supervision impossible. *See* 15 U.S.C. § 78s(c) (made applicable by SOX § 107(b)(5), 15 U.S.C. § 7217(b)(5)).

Upon close examination, the provisions requiring Commission approval of Board rules turn out to be nothing more than paper tigers. The Act requires that “[t]he Commission *shall* approve a proposed rule, *if it finds that the rule is consistent with the requirements of this Act*, or is necessary or appropriate in the public interest or for the protection of investors.” *Id.* § 107(b)(3), 15 U.S.C. § 7217(b)(3) (emphasis added). Thus, the Commission *must* approve a rule if the rule is consistent with the Act *or* furthers the public interest. This provision makes perfect sense as part of a statute designed to give the Board a significant degree of independence from Commission oversight. Proposed rules consistent with the Act must receive Commission approval, while rules not necessarily contemplated by the Act but nevertheless potentially in furtherance of the public interest may receive a greater degree of Commission scrutiny. These provisions combine with the statute’s sweeping grants of discretion to the Board to produce a regime in which the Commission has no choice but to approve Board rules if they do not contravene the expansive language of the statute.

The Commission’s power to amend the Board’s rules is similarly toothless. The Commission can only pass amendments that “further the purposes of that Act.” *Id.* § 107(b)(5), 15 U.S.C. § 7217(b)(5). Because one of the central purposes of the Act was plainly the creation of a Board with sufficient operational independence to ensure effective and unbiased regulation of the accounting industry, there is a core of operational functions with which the Commission cannot interfere. The Commission may amend Board rules relating to ministerial or minor administrative matters, but it cannot use its amendment power to interfere with or insert itself

into the day-to-day conduct of Board inspections and investigations. To do so would be to undermine, rather than further, a central aim of the Act.

Respondents next point to the Commission’s authority to remove Board members. The statute, however, imposes an extraordinarily high bar to such removals: Board members can only be removed by the Commission if it finds, after notice and opportunity for a hearing, that they have willfully violated a statutory provision or Board rule, willfully abused their authority, or failed to enforce compliance with legal provisions or Board rules without any reasonable justification or excuse.<sup>4</sup> *Id.* § 107(d)(3)(A)-(C), 15 U.S.C. § 7217(d)(3)(A)-(C). Apparently aware that the provisions allowing removal only for *willful* abuses of power impose a high bar to Commission action, respondents rely heavily on the final removal provision, which allows for a Board member’s dismissal if the member “without reasonable justification or excuse, has failed to enforce compliance with any such [statutory] provision or [Board] rule, or any professional standard by any registered public accounting firm or any associated person thereof.” *Id.* This provision does not bear the weight respondents place on it, because it only protects against lax enforcement. It provides no protection whatsoever against the far more serious threat of *overly aggressive* enforcement.

Moreover, the Act and the Board’s rules are couched in such expansive language that it would be nearly impossible for the Commission to determine that a member’s failure to enforce a particular provision in a particular way was “unreasonable.” For instance, the Act provides that the Board may impose any sanction “it determines appropriate,” *id.* § 105(c)(4), 15 U.S.C. §

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<sup>4</sup> A comprehensive canvassing of other “for cause” restrictions reveals none with comparable stringency. The only other removal provisions include: (i) “for cause.” *See, e.g.*, 12 U.S.C. 242 (1980) (Board of Governors of the Federal Reserve); (ii) “inefficiency, neglect of duty, or malfeasance in office.” *See, e.g.*, 15 U.S.C. § 41 (Federal Trade Commission); 29 U.S.C. § 661(b) (Occupational Safety and Health Review Commission); 42 U.S.C. § 5841(e) (Nuclear Regulatory Commission); (iii) “neglect of duty or malfeasance in office.” *See, e.g.*, 15 U.S.C. § 2053(a) (Consumer Products Safety Commission); 29 U.S.C. § 153(a) (National Labor Relations Board); and (iv) implicit for cause restrictions. *See, e.g.*, 7 U.S.C. § 4a (Commodity Futures Trading Commission); 47 U.S.C. § 154 (Federal Communications Commission).

7215(c)(4), may conduct an investigation of “any act or practice, or omission to act” that may violate any provision of the Act, the rules of the Board, or the securities laws, *id.* § 105(b)(1), 15 U.S.C. § 7215(b)(1), and may “do any and all other acts and things necessary, appropriate, or incidental to the conduct of its operations and the exercise of its obligations, rights, and powers” under the Act, *id.* § 101(f)(6), 15 U.S.C. § 7211(f)(6). The broad, general language of these provisions enhances the Board’s tremendous operational discretion while severely restricting the Commission’s ability to find that a Board member has acted in accordance with an “unreasonable” interpretation of the relevant statutes or rules.<sup>5</sup>

The fact that the Board’s budget is subject to approval by the Commission, *id.* § 109(b), 15 U.S.C. § 7219(b), does not provide the Commission with the kind of managerial control necessary to render Board members inferior officers. The budgetary approval process occurs only once a year, seriously limiting its usefulness as a mechanism for controlling the Board’s ongoing functions. Moreover, the Commission has shown itself to be extremely deferential to the Board’s budget requests — perhaps unsurprisingly, since the Board is spending its own funds, and not those of the SEC.<sup>6</sup>

Finally, respondents assert that the Commission’s authority to relieve the Board of its enforcement responsibilities, *see id.* § 107(d)(1), 15 U.S.C. § 7217(d)(1), establishes robust

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<sup>5</sup> Respondents assert that this Court should construe the Commission’s amendment and removal powers broadly, in accordance with the canon of constitutional avoidance. But this canon “has no application in the absence of statutory ambiguity.” *United States v. Oakland Cannabis Buyers’ Cooperative*, 532 U.S. 483, 494 (2001). Because the Act’s text places explicit limits on the Commission in accordance with the clear legislative purpose, reliance on the avoidance canon is inappropriate here. *See Boumediene v. Bush*, 128 S. Ct. 2229, 2271 (2008) (“The canon of constitutional avoidance does not supplant traditional modes of statutory interpretation. . . . We cannot ignore the text and purpose of a statute in order to save it.”).

<sup>6</sup> The SEC’s remarkable deference to the Board’s budget proposals is perhaps most evident in its approval of the Board members’ enormous salaries. Board members pay themselves annual salaries of \$531,995, with the Chairman receiving \$654,406 — a salary far higher than that of any other single federal officer, including the President of the United States, and exceeding the salaries of four SEC Commissioners, including the SEC Chairman, *combined*. *See* Paul S. Atkins, Comm’r, Sec. & Exch. Comm’n, Statement at Open Meeting To Consider PCAOB’s Proposed 2008 Budget (Dec. 18, 2007); Sarah Johnson, *SEC Commissioner Rails Against PCAOB Salary Hikes*, CFO, Dec. 18, 2007, <http://www.cfo.com/article.cfm/10327975>.

Commission control over the Board. This view is highly unrealistic for three reasons. First, the adjoining provision, *id.* § 107(d)(2), 15 U.S.C. § 7217(d)(2), bars the Commission from limiting “the activities, functions, and operations of the Board” unless the Commission determines after a hearing that the Board has violated relevant laws or its own rules, or has failed to enforce compliance with such provisions without any reasonable excuse. Thus, while the Commission may relieve the Board of enforcement responsibilities, it cannot limit the Board’s ongoing operations or activities unless it can fulfill significant statutorily mandated conditions. Second, the Commission’s authority to rescind the Board’s enforcement responsibilities is not plenary; the Commission can only do so consistently with the purposes of the Act — including the creation of a strong and independent Board. *See id.* § 107(d)(1), 15 U.S.C. § 7217(d)(1).

Finally, even if the Commission did have plenary authority to revoke the Board’s enforcement responsibilities, it is doubtful that knowledge of this potential check would alter the Board members’ behavior. Even if the Commission invoked this power, section 107(d)(2) plainly contemplates that the Board would still operate, and its members would continue to occupy their positions for the duration of their terms. It is, moreover, highly doubtful that their activities will be swayed by a remedy so drastic it is unlikely to be invoked. Although Congress has the power to abolish or limit the jurisdiction of a federal court or administrative agency, for example, those bodies are not normally considered to be subject thereby to day-to-day congressional supervision and direction. The Commission has been given a sledgehammer where it needed a scalpel.

**D. *Morrison v. Olson* Did Not Create a Definitive Test for Distinguishing Between Principal and Inferior Officers, but Even Under *Morrison*’s Analysis, Board Members Are Principal Officers**

Respondents rely heavily on this Court’s ruling in *Morrison v. Olson*, 487 U.S. 654 (1988), to support their conclusion that Board members are inferior officers. But as this Court

noted in *Edmond*, “*Morrison* did not purport to set forth a definitive test for whether an office is ‘inferior’ under the Appointments Clause.” *Edmond*, 520 U.S. at 661. *Edmond*, however, did purport to establish such a definitive test, and *Edmond* therefore controls the instant case.

In *Morrison*, this Court held that the Independent Counsel created by the Ethics in Government Act of 1978, 28 U.S.C. §§ 591-599, was an inferior officer. The *Morrison* Court articulated four factors relevant to the principal-inferior distinction, all supporting its conclusion that the Independent Counsel was an inferior officer: the Independent Counsel could be removed by the Attorney General, and had limited duties, jurisdiction, and tenure. *Morrison*, 487 U.S. at 671-72. Although the *Edmond* Court recognized that two of the *Morrison* factors indicated that the judges at issue in *Edmond* were *principal* officers, the Court concluded that the judges were inferior officers anyway. *See Edmond*, 520 U.S. at 661. *Edmond* thus strongly signaled that the *Morrison* test was limited to an isolated situation and would not be generally applicable.

Even if *Morrison* were decisive here, however, the four factors articulated in that case uniformly indicate that the Board members are principal rather than inferior officers. First, unlike the Independent Counsel, the Board members are protected by a super-strong for-cause removal provision. The Independent Counsel, by contrast, could be removed “for good cause” or for “any . . . condition that substantially impairs the performance of such independent counsel’s duties.” *Morrison*, 487 U.S. at 663. This malleable standard is far less onerous than the procedure for removing Board members, who must *willfully* violate relevant statutes or regulations, or fail to enforce extremely amorphous standards with no reasonable excuse. *See supra* Section I.C. Second, the Independent Counsel’s duties were limited to investigation and prosecution — she had no “authority to formulate policy for the Government or the Executive Branch.” *Morrison*, 487 U.S. at 671. Board members, by contrast, possess the power to issue accounting rules and

standards that substantially affect the entire national economy, with only cursory and deferential review by the Commission, in addition to their sweeping authority to inspect, investigate, and enforce. For instance, the Board’s interpretation of a vague provision of the Act in 2004 was estimated to cost public companies \$35 billion annually — expenses that had a disproportionate and sometimes devastating effect on small- and medium-sized businesses. *See* Am. Elecs. Ass’n, Sarbanes-Oxley Section 404, at 19 (2005).

Third, while the Independent Counsel operated within an extraordinarily limited and tightly controlled jurisdiction, the Board is not nearly so constrained. Board members are charged with exercising a wide range of powers affecting the entire accounting industry — and through it, the entire economy of the United States. The Independent Counsel, by contrast, was “appointed essentially to accomplish a single task,” an investigation of a particular person or transaction, and could only operate within the limited jurisdiction granted by a special court. *Morrison*, 487 U.S. at 672. Fourth, and perhaps most importantly, the Board is not a “temporary” entity like the Office of the Independent Counsel. *Id.* After her particular investigation had concluded, the Independent Counsel’s office simply ceased to exist. The Independent Counsel’s status as an inferior officer was thus consistent with this Court’s longstanding rule that officers who would otherwise be principal are rendered inferior *simply by virtue of their temporary status*. *See United States v. Eaton*, 169 U.S. 331, 343 (1898) (holding that a “vice-consul” appointed during a consul’s temporary absence was an inferior officer, who because he “is charged with the performance of the duty of the superior for a limited time and under special and temporary conditions . . . is not thereby transformed into the superior and permanent official”), *cited with approval in Morrison*, 487 U.S. at 672. The Board, by contrast, is a *permanent* governmental entity, whose wide jurisdiction is set by statute.

*Morrison* did not create a nebulous, all-encompassing “functional” test for dividing principal from inferior officers, as respondents contend in an apparent effort to cherry-pick favorable statutory provisions to support their claims of inferior officer status. Instead, it explicitly rested its holding on four factors that it recognized were well-grounded in this Court’s Appointments Clause jurisprudence. The *Morrison* Court, for instance, relied on this Court’s 130-year-old decision in *United States v. Germaine*, which held that officer status “embraces the ideas of tenure, duration, . . . and duties.” *Germaine*, 99 U.S. 508, 511 (1879), *quoted in Morrison*, 487 U.S. at 672. *Morrison* carefully defined the relevant factors in its principal-inferior officer test; it did not embrace respondents’ amorphous all-things-considered approach.

**E. Even If Board Members Were Inferior Officers, Their Appointment Would Still Be Unconstitutional Because They Were Not Appointed by the “Head” of a “Department”**

Even if the Board’s members were inferior officers, their appointments would only be valid if made by “the President alone, . . . the Courts of Law, or . . . the Heads of Departments.” U.S. Const. art. II, § 2, cl. 2. Respondents contend that the Commissioners are a department head for Appointments Clause purposes. This approach is supported neither by constitutional text nor by this Court’s precedents.

**i. The SEC Is Not a “Department” Within the Meaning of the Appointments Clause**

Reading “Departments” to include independent agencies like the Commission below the Cabinet level would contradict the settled meaning of the term “Department” elsewhere in the Constitution. This Court noted in *Freytag* that the Opinions Clause, which provides that the President “may require the Opinion, in writing, of the principal Officer in each of the Executive Departments,” U.S. Const. art. II, § 2, cl. 1, is applicable only to the Cabinet members. *Freytag*, 501 U.S. at 886. This interpretation of the Opinions Clause dates back more than a century, as

does this Court’s determination that the word “department” has the same meaning in the Appointments Clause as it does in the Opinions Clause. *See id.*; *Germaine*, 99 U.S. at 511; *see also Burnap v. United States*, 252 U.S. 512, 515 (1920) (“The term head of a Department means . . . the Secretary in charge of a great division of the executive branch of the Government, like the State, Treasury, and War, who is a member of the Cabinet.”). Likewise, this Court has established that the Twenty-fifth Amendment’s reference to the “principal officers of the executive departments,” U.S. Const. amend. XXV, § 4, encompasses only the principal officers of “Cabinet-level entities.” *Freytag*, 501 U.S. at 887.

Moreover, allowing appointments of inferior officers by independent agencies would undermine the principles of political accountability at the heart of the Appointments Clause. This Court noted in *Freytag* that “[t]he Cabinet-level departments are limited in number and easily identified. Their heads are subject to the exercise of political oversight and share the President’s accountability to the people.” *Id.*, 501 U.S. at 886. The same cannot be said of an independent agency like the Commission, which is purposely insulated from democratic accountability. Appointments by such an insulated entity run the risk of diffusing the power to appoint, undermining the Clause’s purpose of “ensur[ing] that those who wielded [such power] were accountable to political force and the will of the people.” *Id.*, 501 U.S. at 884.

## **ii. The SEC Chairman — and Not the Commissioners as a Whole — Is the Commission’s “Head”**

Even if the Commission were a “Department,” however, the Board members’ appointments would still be invalid because the Commissioners as a whole do not constitute the Commission’s “Head.” This Court has never held that a multimember body can constitute the head of a department. Indeed, it is the Commission’s Chairman who exercises all the incidents of administrative and executive control over the Commission. In 1950, Congress mandated that the

SEC Chairman be given control over “the executive and administrative functions of the Commission,” including “the appointment and supervision of personnel,” the “distribution of business” among personnel and administrative units, and “the use and expenditure of funds.” Reorganization Plan No. 10 of 1950 § 1, 64 Stat. 1265, 1266. At the same time, Congress stripped the Commission of its ability to select the Chairman, instead vesting that power in the President. *Id.* Indeed, the Commission’s own Web site describes the Chairman as “the SEC’s top executive.” Current SEC Commissioners, <http://www.sec.gov/about/commissioner.shtml> (last visited Apr. 18, 2009).

The district court agreed that the Chairman is the proper head of the Commission, but denied relief due to lack of standing. Since the Chairman concurred with the Commission in the selection of each Board member, the court concluded, petitioners had not shown that they were harmed by the constitutional violation. *PCAOB I*, 2007 WL 891675, at \*5. This ruling contravenes the commonsensical notion that an individual’s decision-making in a group context will often be different than it would have been if the individual had exercised unilateral authority. Indeed, the Framers vested primary appointment authority in the President because they believed that an individual would act much differently — and much more judiciously — than a group motivated by its manifold “private and party likings and dislikes, partialities and antipathies, attachments and animosities.” *The Federalist No. 76*, at 485 (Alexander Hamilton) (Robert Scigliano ed., 2000). Even if this were untrue, petitioners would still have standing because there is clear evidence that the Chairman’s views on the initial Board appointments in 2002 were swayed considerably by pressure from other Commissioners. *See U.S. Gen. Accounting Office, Actions Needed To Improve Public Company Accounting Oversight Board Selection Process 7-10, 20-21 (2002)*. This pressure was so intense that in late 2002 the

Chairman withdrew his support for his preferred candidate for the Board’s chairmanship when the candidate encountered strong resistance from other Commissioners. *See id.* at 9-10. Because the Board’s membership would likely have differed if the SEC Chairman had exercised sole appointment authority, petitioners have standing to challenge the Commission’s unconstitutional use of the appointments power.

## **II. THE PCAOB VIOLATES THE SEPARATION OF POWERS**

The Constitution vests all of the “executive Power . . . in a President,” U.S. Const. art. II, § 1, and provides that he “shall take Care that the Laws be faithfully executed.” *Id.* § 3. The Framers’ decision to concentrate this power in a single executive was not the product of haphazard compromise or happenstance. Rather, they understood that a unitary executive was crucial to effective, democratic governance. The Framers adjudged that only “a single magistrate” would give the necessary “energy, dispatch, and responsibility to the office.” 1 Max Farrand, *Records of the Federal Convention of 1787*, at 65 (1911) (remarks of James Wilson). They recognized that the unique status of the Presidency as “the only [office] for whom the entire Nation votes” rendered him a crucial counterweight to the corrosive effect of regional and interest-based factions. *Clinton v. Jones*, 520 U.S. 681, 711 (1997) (Breyer, J., concurring). Most important, the Framers understood that only by concentrating executive power in a unitary entity could it be ensured that the public would know who to reward for its proper exercise and who to punish for its abuse. “One of the weightiest objections to a plurality in the executive . . . is that it tends to conceal faults and destroy responsibility.” *The Federalist No. 70*, at 427 (Alexander Hamilton) (C. Rossiter ed., 1961). Thus, the Framers decided “to vest Executive authority in one person rather than several . . . in order to focus, rather than to spread, Executive responsibility thereby facilitating accountability.” *Clinton*, 520 U.S. at 712 (Breyer, J., concurring).

To safeguard these values, this Court — through its separation of powers doctrine — has painstakingly guarded against legislative encroachments on Executive powers, even those that appear at first glance to be “innocuous.” *Metro. Wash. Airports Auth. v. Citizens for the Abatement of Aircraft Noise, Inc.*, 501 U.S. 252, 277 (1991) [hereinafter *MWAA*]. But “if any power whatsoever is in its nature executive it is the power of appointing, overseeing, and controlling those who execute the laws.” 1 Annals of Congress 463 (Gales & Seaton eds., 1789) (remarks of James Madison). The Sarbanes-Oxley Act divests the President of the totality of these powers over the Board. Not only does it interpose an unprecedented second layer of “for cause” removal restrictions between the President and officers wielding tremendous executive authority—it interposes one whose stringency is unparalleled in the world of independent agencies. By further placing appointment and removal authority over the Board solely in the hands of the SEC, itself an independent agency “specifically designed *not* to have the quality . . . of being subject to the exercise of political oversight and sharing the President's accountability to the people,” *Freytag v. Comm'r*, 501 U.S. 868, 916 (1991) (Scalia, J., concurring in part), the Act creates a wholly novel creature: an independent agency within an independent agency, shielded from any meaningful presidential influence and unaccountable to any publicly elected official. In so doing, the Act constitutes the fragmentation of the Executive that Article II was designed to prevent.

#### **A. The PCAOB’s Removal Restrictions Taken Alone Violate Separation of Powers**

Under *Morrison*, any statutory scheme that “interfere[s] with the President's exercise of the executive power and his constitutionally appointed duty to take care that the laws ‘be faithfully executed’” is unconstitutional. 487 U.S. at 690. Whatever uncertainty inheres in that statement, one thing is certain: Congress may not “completely strip[] from the President” “the

power to remove an executive official.” *Id.* at 692. The Sarbanes-Oxley does precisely that, “thus providing no means for the President to ensure the [Board’s] ‘faithful execution’ of the laws.” *Id.*

The constitutional imperative of maintaining the executive’s removal powers is well established. Indeed, it has been understood since the earliest days of the Republic that Article II’s grant “include[es] the power of appointment *and removal* of executive officers.” *Myers v. United States*, 272 U.S. 52, 163-164 (1926) (emphasis added). The First Congress’ so-called “Decision of 1789” provides clear evidence of this understanding. *Id.* at 111-32. The controversy at hand was a proposed bill establishing certain Executive Branch offices with language providing that the officers were to be “removable by the President.” *Id.* at 109, 111. James Madison strenuously opposed the language on the grounds that it falsely implied that the President’s removal power could “be exercised by virtue of a legislative grant only.” *Myers*, 272 U.S. at 112 (quoting 1 *Annals of Congress* 579). The President, he argued, must possess inherent removal authority, for only this could assure “that great principle of unity and responsibility in the executive department, which was intended for the security of liberty and the public good.” *Myers*, 272 U.S. at 131 (quoting 1 *Annals of Congress* 499 (Madison)). After “one of the ablest constitutional debates which has taken place in Congress since the adoption of the Constitution,” *Parsons v. United States*, 167 U.S. 324, 329 (1897), the House concurred with Madison’s understanding and deleted the removal language from the bill. This debate and the resulting consensus that the President possessed inherent removal authority over all executive officers is not some piece of historical trivia. This Court has recognized that the Decision of 1789 “provides contemporaneous and weighty evidence of the Constitution’s meaning since many of the Members of the First Congress had taken part in framing that instrument.” *Bowsher v. Synar*, 478 U.S. 714, 723-24 (1986); *see also Myers*, 272 U.S. at 149 (“[T]he construction given to the Constitution in 1789 . .

. [is] considered as firmly and definitely settled, and there is good sense and practical utility in the construction.”).

Since then, this Court has repeatedly affirmed the centrality of removal power in ensuring the “faithful execution of the laws.” When this Court in *Myers* struck down a statute conditioning the President’s removal of a postmaster on the advice and consent of the Senate, it explained that the President’s “power of removing those [executive officers] is *essential* to the execution of the laws by him.” 272 U.S. at 117 (emphasis added). In *Bowsher*, this Court emphasized that “[o]nce an officer is appointed, it is only the authority that can remove him . . . that he must fear and, in the performance of his functions, obey.” 478 U.S. at 726 (1986). And in *Morrison*, this Court recognized that to “completely strip[]” the President of removal authority would leave him with “no means . . . to ensure the ‘faithful execution’ of the laws.” 487 U.S. at 692.

To be clear, this Court has authorized Congress to impose broadly worded “for cause” restrictions on removal. But this Court has never sanctioned a “for cause” removal as strict as the Board’s, *see* SOX § 107(d)(3), 15 U.S.C. § 7217(d)(3), much less a provision eliminating *all* presidential removal authority. The court below relied on *Humphrey’s Executor v. United States*, 295 U.S. 602 (1935), *United States v. Perkins*, 116 U.S. 483 (1886), and *Morrison* to suggest otherwise, but none of these cases remotely support its conclusion. All these cases upheld substantially weaker “for cause” restrictions which “put[] the removal power squarely in the hands of the [President]” or his alter ego.<sup>7</sup> *Morrison*, 487 U.S. at 686. Thus, in *Humphrey’s Executor*, the President himself could remove the Federal Trade Commission (“FTC”) Chairman for “inefficiency, neglect of duty, or malfeasance in office.” *See* 15 U.S.C. § 41. In *Perkins*, the President — through his alter-ego, the Secretary of the Navy — could dismiss the officer in

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<sup>7</sup> Courts have recognized that there is no difference from a removal authority standpoint between the President and his alter egos who serve at his pleasure. *See, e.g., In re Sealed Case*, 838 F.2d 476, 528 n.30 (D.C. Cir. 1988) (R.B. Ginsburg, J., dissenting).

question for “deficient examination,” “misconduct,” or by court-martial sentence. 116 U.S. at 484. Similarly, in *Morrison*, the President — through his alter ego, the Attorney General — could remove the Independent Counsel for “physical disability, mental incapacity, any other condition that substantially impairs [her] performance” or an undefined “good cause.” 487 U.S. at 663. But these express the outermost boundaries of Congress’ authority to restrict removal powers. Never has there been an independent agency whose heads were only removable by another independent agency for cause, rather than by the President or his alter ego.

Undaunted by the lack of favorable precedent, the lower court interpreted the language in *Perkins* that Congress “may limit and restrict the power of removal [of inferior officers] as it deems best for the public interest” to mean that Congress may impose *complete* removal restrictions on *any* inferior executive officer. *PCAOB II*, 537 F.3d 674, 683 (quoting *Perkins*, 116 U.S. at 485). But that four-paragraph opinion cannot sustain the weight the lower court places on it for several reasons. First, that language referred to inferior officers, which the Board members are not. *See supra* Part I(A)-(D). Second, this Court has never extended *Perkins*’ sprawling dicta to officers — even inferior ones — who wield executive powers as extensive as the Board members’, nor should it.<sup>8</sup> “[A]s room for policy formulation increases, congressional limitations upon presidential influence become problematic.” *In re Sealed Case*, 838 F.2d at 497 (quoting Daniel Gifford, *The Separation of Powers Doctrine and the Regulatory Agencies After Bowsher v. Synar*, 55 Geo. Wash. L. Rev. 441, 467 (1987)). But *Perkins* himself was a cadet engineer with none of the rulemaking and enforcement authority that the PCAOB exercises.

Third, the Circuit Court’s interpretation of *Perkins* conflicts with this Court’s clear statement that

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<sup>8</sup> Indeed, the Court has only invoked *Perkins* thrice: to uphold removal restrictions on an Air Force employee, *Nixon v. Fitzgerald*, 457 U.S. 731, 787 (1982), a landscape architect, *Burnap v. United States*, 252 U.S. 512, 516 (1920), and the Independent Counsel, *Morrison*, 487 U.S. at 691 nn.27 & 29. And even in upholding the independent counsel, the Court relied heavily on the fact that she “lack[ed] policymaking or significant administrative authority.” *Id.* at 691.

Congress may not “completely strip[]” the President of his removal authority over *any* executive officer—inferior or otherwise. *Morrison*, 487 U.S. at 692.

Respondents suggest that the President is not actually stripped of his authority to remove Board members because he can direct the Commission — under threat of removal — to terminate Board members. But that suggestion does not square with two features of the statutory scheme. First, it ignores the unusually stringent “for cause” restriction that protect Board members’ tenure. The SEC is prohibited *by law* from firing a Board member absent a finding, “on the record [and] after notice and opportunity for a hearing” that such member “*willfully*” violated the Act or , “without *reasonable* justification or excuse,” failed to enforce compliance. *See* SOX § 107(d)(3), 15 U.S.C. § 7217(d)(3) (emphasis added). The President can no more force the SEC to make that legal finding than he can force the Federal Reserve Chairman to lower interest rates. Second, removal authority is vested in the Commission as a whole, rather than its Chairperson, which means that the President’s only recourse if the Commission fails to find a removal offense is to remove a *majority* of the noncompliant Commissioners and replace them with individuals handpicked for their willingness to execute the removal. But even if the Senate confirmed these new Commissioners, they would likely be disqualified from participating in the removal proceedings. *See, e.g., Cinderella Career & Finishing Sch., Inc. v. FTC*, 425 F.2d 583, 591 (D.C. Cir. 1970) (“The test for disqualification [is] . . . whether a disinterested observer may concluded that [a decision-maker] has in some measure adjudged the facts as well as the law of a particular case in advance of hearing it.”). And, having clearly prejudged the outcome of the proceedings, if they participated anyway the removal could easily be invalidated on due process grounds. *See Goldberg v. Kelly*, 397 U.S. 254, 271 (1970) (holding that an impartial decision maker is an essential due process requirement in administrative proceedings).

## **B. The Court Below Erred in Considering the Act “Taken as a Whole” Rather Than Striking It Down Based on Its Removal Restrictions**

Unable to articulate a realistic scenario in which the President could effect the removal of a Board member, the lower court retreated to the position that removal authority is not “the be-all and end-all of Executive authority” and that this Court’s precedent requires “a more nuanced approach that examines the myriad means of Executive control.” *See PCAOB II*, 537 F.3d at 669. Three considerations militate against adopting this approach. First, resort to an ad hoc, “totality of factors” analysis is inconsistent with this Court’s approach in *Morrison*. Second, it discounts the need to preserve clear lines of responsibility for executive action and, in so doing, risks severe corrosion of executive accountability. Third, it invites Congress to replicate Board-like entities while leaving policymakers and judges bereft of a clear standard to evaluate their constitutionality. This is a recipe for creeping legislative encroachment into executive powers.

The lower court commits a basic error by reading *Morrison* to suggest that a statutory scheme stripping the President of his removal authority may nonetheless be constitutional when taken as a whole. The first inquiry in *Morrison* was whether the good cause restriction, “*taken by itself*, impermissibly interfere[d] with the President’s” execution of his duties. 487 U.S. at 685 (emphasis added). Contrary to the interpretation of the lower court, this Court did not say that removal authority was just one of many equally potent and independently adequate levers of executive control — it said it was the “*most important*[.]” lever. *Id.* at 696 (emphasis added). Only after the Court satisfied itself that the President was not “completely stripped” of his removal authority, did it proceed to consider the second question: whether — notwithstanding the qualified removal powers — the statute “taken as a whole” still impermissibly diminished the President’s ability to control the Independent Counsel. *Id.* at 685.

To argue the reverse — that a statutory scheme can flunk the first test, yet survive by passing the second — makes little sense in context for two reasons. First, if the other mechanisms for asserting presidential control were sufficient to preserve presidential oversight, it would be wholly unnecessary to inquire specifically into the removal power. The Circuit Court’s approach thus renders a third of this Court’s opinion in *Morrison* utterly superfluous. Second, the issue in *Morrison* was how a prosecutor who exercised “a core executive function,” could survive under *Humphrey’s Executor*’s holding that Congress could only restrict the removal authority of officers exercising “quasi-legislative” or “quasi-judicial” functions. *Id.* at 604. The Independent Counsel was the first purely executive officer that the President (or his alter ego) could neither appoint, countermand, nor remove at will. Thus, the issue confronting the Court was: how, given this package of novel restrictions, could the President ensure the faithful execution of the law with only his limited removal authority? It was to answer *this* question that the Court considered the rest of the statute and proffered additional means by which the President could control the prosecutor.

The second reason to reject the lower court’s approach centers on accountability: only clearly defined, direct removal authority can ensure that the public understands where to assign blame for the PCAOB’s failures. “‘If there be one principle clearer than another, it is this: [in government], somebody must be trusted, in order that when things go wrong it may be quite plain who should be punished. . . . Power and strict accountability of its use are the essential constituents of good government.’” *Bowsher v. Synar*, 478 U.S. 714, 738 (1986) (Stevens, J., concurring). But there can be no accountability unless “a clear assignment of power . . . allows the citizen to know who may be called to answer for making, or not making, those delicate and necessary decisions essential to governance.” *Loving v. United States*, 517 U.S. 748, 758 (1996).

On the other hand, “where lines of responsibility are obscured by complex and diffusive apportionments of Executive power, the resulting arrangement tends to conceal faults and destroy responsibility.” The Federalist No. 70, at 427 (Hamilton). “It often becomes impossible, amidst mutual accusations, to determine on whom the blame or punishment of a pernicious measure . . . ought really to fall. It is shifted from one to another with so much dexterity, and under such plausible appearances, that the public opinion is left in suspect about the real author.” *Id.* at 426. The Framers understood the perils that governance could become “so complicated” as to render it “impracticable to pronounce” who is to blame, and for this reason they vested executive power in a single, unitary President — to ensure that despite the functional complexity of government, people would know where to channel their grievances. *Id.*

The PCAOB is anathema to this arrangement. The threat of even a single layer of “for cause” removal restrictions is evident: as demonstrated in the last elections, it is difficult enough for the public to tell whether the fault for lax regulation lay with a wayward SEC shielded from presidential control, or with a derelict Executive who failed to make appropriate use of his removal authority. *See, e.g., McCain’s Scapegoat*, Wall St. J., Sept. 19, 2008. That problem is multiplied exponentially where the President is completely divested of any direct removal authority and left only with the most indirect and attenuated means to nudge the SEC into policing PCAOB enforcement of the law. If the Board’s policies prove disastrously unpopular, he has precisely what Hamilton feared: a plausible claim that responsibility lay elsewhere— either with an SEC that failed to exercise its oversight functions or a Congress that cabined the Board from presidential control.

Given these considerations, it is utterly irrelevant that the President *could*, in theory, use his “less direct and generally more subtle” means to cajole the SEC into properly overseeing the

Board. *See PCAOB II*, 537 F.3d at 680-681. Nor does it matter that the SEC *could* adopt a permissive reading of the PCAOB’s byzantine enabling statute. If the President negligently failed to exercise this oversight, the public would have no means of knowing that blame lie with him. What may be obvious to a court after considered study is far from obvious to the public. “Bureaucracy is the ultimate black box of government — the place where exercises of coercive power are most unfathomable and thus most threatening.” Elena Kagan, *Presidential Administration*, 114 Harv. L. Rev. 2245, 2332 (2001). It is precisely for this reason that maintaining accountability in executive agencies is so paramount. But “a fundamental precondition of accountability in administration [is] the degree to which the public can understand the sources and levers of bureaucratic action.” *Id.* Only a lever as clearly defined and easily ascertainable as the removal power can ensure that the public is properly able to hold the executive accountable for its officers’ actions.

The third reason for rejecting the lower court’s approach is the overriding need for a manageable bright-line rule so as to forestall fragmentation of the Executive. The Kavanaugh dissent correctly noted that upholding the Board would “green-light Congress to create a host of similar entities,” such as an “Energy Price Enforcement Board appointed by and removable only for cause by FERC” or “an Indecency Enforcement Board appointed by and removable only for cause by the FCC.” 537 F.3d at 699. The lower court’s protestation that this “parade of horrors . . . ignores the [PCAOB’s specific] statutory scheme,” 537 F.3d at 685 n.15, misses the point because its decision is devoid of any standard delimiting how far Congress can stray from that specific statutory scheme before it runs afoul of Article II. The “totality of factors” test provides no guidance as to whether a hypothetical Indecency Enforcement Board that is identical in all respects to the PCOAB minus the FCC’s ability amend its existing rules, would be constitutional.

*Cf.* SOX § 107(d)(1), 15 U.S.C. § 7217(d)(1). Or whether such an entity would be constitutional if the FCC could manage its ongoing investigations but lacked review over its final sanctions. *Cf.* SOX 107(c), 15 U.S.C. § 7217(c). In short, the lower court’s ad hoc test leaves future policymakers legislating blind.

The lack of standards further invites the very sort of legislative encroachment that the separation of powers doctrine is meant to protect against.<sup>9</sup> As Justice Scalia precisely recognized in *Morrison*, the problem with the “totality of the circumstances” approach is that the tendency is to conclude after “taking all things into account . . . that the power taken away from the President is not really *too* much.” 487 U.S. at 733 (Scalia, J., dissenting). Proper maintenance of judicial vigilance requires that this Court establish a clear rule that Congress may not completely divest the President of his removal authority.

**C. Even Under a “Totality of Factors” Analysis the Board Is Unconstitutional Because It Leaves the President Without Any Means to Ensure Its Faithful Execution of the Laws**

Even if this Court were to opt for a “totality of factors” analysis, the Board cannot withstand constitutional scrutiny. Under *Morrison*, this second question asked whether the statute, “taken as a whole,” impermissibly “reduc[es] the President’s ability to control the [executive power] wielded by” executive officials, or otherwise “deprives the President of control over the [exercise of executive power so as] to interfere impermissibly with his constitutional obligation to ensure the faithful execution of the laws.” *Morrison*, 487 U.S. at 685,

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<sup>9</sup> The court below inaccurately suggests in passing that the PCAOB does not represent a constitutionally suspect encroachment because it does not “aggrandiz[e]” Congress’ powers. 537 F.3d at 679. But this Court has made clear one branch may affect an unconstitutional encroachment *either* by “interfere[ing] impermissible with the other’s performance of its constitutionally assigned functions” *or* by “assum[ing] a function that more properly is entrusted to another.” *INS v. Chadha*, 462 U.S. 919, 963 (1983) (Powell, J., concurring); *Loving v. United States*, 517 U.S. 748, 757 (1996) (“Even when a branch does not arrogate power to itself . . . the separation-of-powers doctrine requires that a branch not impair another in the performance of its constitutional duties.”).

693. But in enacting the Sarbanes-Oxley Act, Congress deliberately engineered a statutory scheme that divests the President of *any* meaningful ability to control the Board.

The lower court downplayed the significance of this unprecedented stripping of the President's appointment, removal, and supervisory authority by asserting that "the President possesses significant influence over the Commission, which in turn possesses comprehensive control over the Board." *See PCAOB II*, 537 F.3d at 681. This assertion is both factually incorrect and legally irrelevant. It is factually incorrect in that it greatly exaggerates both the President's influence over the SEC and the SEC's control over the Board. It is legally irrelevant because Article II vests Executive power in the *President*, not in the independent agencies which "cannot in any proper sense be characterized as an arm or an eye of the executive." *Humphrey's Executor*, 295 U.S. at 628. Thus, either the President or his alter ego must have at least some unobstructed oversight authority over executive officers.

The lower identified several purportedly "significant additional levers of influence" that the President has over the SEC, but not a single one translates into an ability to influence the Board itself. These levers include: (1) control over the SEC Chairman, who is appointed by and serves at the pleasure of the President, and who "often dominate[s] commission policymaking," *PCAOB II*, 537 F.3d at 680; (2) the President's ability to appoint "[l]ike-minded Commissioners" who may, in turn, appoint compliant Board members, *id.* at 682; (3) the President's ability to provide or withhold the "presidential good will . . . generally require[d]" to secure congressional budgetary support, *id.* at 680; and (4) an assortment of other tools like "centralization of contracting, personnel requirements, and property allocations." *Id.* (citing Peter L. Strauss, *The Place of Agencies in Government: Separation of Powers and the Fourth Branch*, 84 Colum. L.

Rev 573, 587 (1984)). However much influence these levers generally afford the President, they provide almost none in this case.

With respect to the first, Congress deliberately designed the PCAOB in a way that frustrates the typical dominance enjoyed by agency chairpersons. Thus, while the Chairman has exclusive authority to appoint all “heads of major administrative units” within the SEC, *see* Reorganization Plan No. 10 of 1950, § 1(b)(2), the Act vests the power to appoint Board members in the Commission as a whole. SOX § 101(e)(4), 15 U.S.C. § 7211(e)(4). Furthermore, while it is certainly true that chairpersons “often” possess disproportionate influence within their agencies, that generic proposition has not applied in practice with respect to the SEC’s relationship with the Board. *See, e.g.*, U.S. Gen. Accounting Office, *Securities and Exchange Commission* 7-10, 20-21 (describing a Commissioner mutiny when the SEC Chairman attempted to dominate the PCAOB appointment process).

The second suggestion — that the President can simply appoint “[l]ike-minded Commissioners,” *PCAOB II*, 537 F.3d at 682 — is startlingly oblivious to the realities of the SEC’s appointment scheme. Because SEC Commissioners serve staggered five-year terms, the majority of Commissioners may be holdovers from the previous administration for the entirety of a President’s first term. For example, at present, four of the five sitting Commissioners are Bush appointees. The term of one of these four expires in 2011 and the terms of the other three expire in 2013— *after* the next presidential election. *See* <http://www.sec.gov/about/commissioner.shtml> (last visited Apr. 24, 2009). The President has no means to ensure that these holdovers, many of whom may be hostile to his agenda, do not stack the Board with equally defiant officers. And absent a willful breach of the law that *a majority* of the Commission deems a removable offense, the President will be helpless in replacing rogue Board members.

The third supposed lever — the agency’s reliance on “presidential good will” to obtain congressional budgetary approval, *PCAOB II*, 537 F.3d at 680 — is yet another general rule inapplicable to the specific agency at hand. In practice, the SEC has not been overly dependent on presidential backing to secure congressional support. On the contrary, Congress has repeatedly given the SEC *more* funding than requested in the White House proposed budget. *See, e.g., Six Months Later, New Audit Board Holds First Talk*, N.Y. Times, Jan. 10, 2003.

The fourth means of influence appears to be a throwaway point. Neither the court below, nor the law review article which casually references, explains how tools as feeble as control over property allocations and personnel requirements translate into substantive and continuing influence over the policymaking and enforcement functions of an independent agency.

This is because they do not. Indeed, the lower court’s conclusion that independent agencies do not “differ significantly or systematically” from other executive agencies with respect to their “relationships with the rest of government,” *PCAOB II*, 537 F.3d at 680 (quoting Strauss, at 596) flatly contradicts this Court’s repeated recognition that agencies like the SEC are “specifically designed *not* to have the quality . . . of being subject to the exercise of political oversight and sharing the President’s accountability to the people.” *See Freytag*, 501 U.S. at 916 (1991) (Scalia, J., concurring in part); *Humphrey’s Executor*, 295 U.S. at 628 (noting that independent agencies “cannot in any proper sense be characterized as an arm or an eye of the executive”).

But even if the lower court was correct in its assessment of the President’s influence over the SEC, it would only demonstrate why the *Commission* — not the Board — is consistent with Article II. The President possesses none of these levers of influence with respect to the PCAOB itself. Divested of his appointment power, he has no way of ensuring that the Board members

share his general policy outlook. Where an officer “is appointed by persons who are themselves not politically accountable . . . ongoing supervision by a politically accountable official, whether by the President or by someone serving at the President’s pleasure, seems particularly important.” Laurence H. Tribe, 1 American Constitutional Law § 4-8, at 684 (3d ed. 2000). Given this lack of “political accountability at the front end for the choice of that officer, a ‘for cause’ limitation on removal that renders political supervision impossible” is doubly troubling. *Id.* Worse, the Act eliminates the President’s ability to use his “good will” as leverage to influence Board policy because by giving the Board tax-levying authority, the Act removed it from the congressional appropriations process. *See* SOX § 109, 15 U.S.C. § 7219.

Given the sum of these restrictions — the inability to appoint or remove Board members, the lack of countermand authority, and the loss of budgetary leverage — the PCAOB, “taken as a whole,” unquestionably fails the test outlined in *Morrison*. Several factors necessitate this conclusion. First, the Board members exercise powers vastly greater than the Independent Counsel, a matter of overriding significance because the question of whether restrictions on executive control “impede the President’s ability to perform his constitutional duty . . . must be analyzed in . . . light” of “the functions of the officials in question.” *Morrison*, 487 U.S. at 691. Thus, in upholding the Independent Counsel, the Court relied heavily on her “limited jurisdiction and tenure and lack[] of policymaking or significant administrative authority.” *Id.* Her jurisdiction was limited by statute to the uppermost echelon of executive officials, *id.* at 659, n.2, and in the office’s twenty-one year lifespan, only a few dozen individuals were subject to its inquiry. *See* Gerald S. Greenberg, *Historical Encyclopedia of U.S. Independent Counsel Investigations* (2000). Nor did the Independent Counsel possess any policymaking authority. On the contrary, she was obligated by statute to “comply with the written or otherwise established

policies of the Department of Justice” governing prosecutions except where impossible. 28 U.S.C. § 594(f); *Morrison*, 487 U.S. at 662. By contrast, the PCAOB’s jurisdiction includes “all accountants and everybody they work for, which directly or indirectly is every breathing person in the country.” 148 Cong. Rec. at S6334 (statement of Sen. Gramm). The Board also promulgates the very regulations which govern their inspections and investigations.

Second, the President’s control over the Board pales in comparison to his control over the Independent Counsel. In a bizarre move, the court below compared the President’s control over the Independent Counsel with the *Commission’s* control over the PCAOB, 537 F.3d at 681-82, to conclude that the PCAOB passes constitutional muster. But Article II protects the ability of the President to faithfully execute the laws, not that of an independent agency. The proper comparison asks how much control the *President* possesses, and under that comparison the Board flunks the *Morrison* test. As discussed above, the President — through his Attorney General — possessed the single “most important[.]” lever of control: direct removal authority. 487 U.S. at 696. Moreover, by giving the Attorney General “unreviewable discretion” to refrain from recommending appointment of an Independent Counsel, the Ethics in Government Act granted the President exclusive authority to initiate an investigation. *Id.* at 696. Furthermore, unlike the Board’s unconstrained jurisdiction to inspect or investigate any auditing firm for any violation, “the jurisdiction of the independent counsel [was] defined with reference to the facts submitted by the Attorney General.” *Id.* at 696. Finally, the President retained the equivalent of at-will removal authority over the Independent Counsel because “[i]f the President truly disagrees with the Independent Counsel, the President can make the Counsel vanish with one stroke of the presidential pardon pen: no underlying targets of prosecution, no prosecutor.” Akhil Amar, *Intratextualism*, 112 Harv. L. Rev. 747, 803 (1999). While the rarity of independent

prosecutions enabled the President to use his pardon power surgically and sparingly, *see id.* (discussing President Ford’s Nixon pardon and President Bush’s Weinberger pardon), the sheer volume of audit inspections and investigations render it impossible for the President to wield his pardon power with any such precision. *See PCAOB 2007 Annual Report 3*, [www.pcaobus.org/About\\_the\\_PCAOB/Annual\\_Reports/2007.pdf](http://www.pcaobus.org/About_the_PCAOB/Annual_Reports/2007.pdf) (last visited Apr. 24, 2009).

In other words, the President does not possess *a single one* of the numerous mechanisms of control that, in combination, led this Court to uphold the Independent Counsel statute. Thus, the PCAOB fails even the Circuit Court’s permissive “totality of the factors.”

### **CONCLUSION**

For the foregoing reasons, petitioners respectfully request that the judgment of the Court of Appeals for the District of Columbia Circuit be reversed.

Respectfully submitted,

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Counsel for Petitioners  
April 27, 2009

## **APPENDIX: CONSTITUTIONAL AND STATUTORY PROVISIONS**

### **U.S. Const. art. II, § 1 provides in relevant part:**

The executive Power shall be vested in a President of the United States of America.

### **U.S. Const. art. II, § 2, cl. 2 provides in relevant part:**

[The President] shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

### **U.S. Const. art. II, § 3 provides in relevant part:**

[The President] shall take Care that the Laws be faithfully executed. . .

### **SOX § 101(a), 15 U.S.C. § 7211(a) provides in relevant part:**

There is established the Public Company Accounting Oversight Board, to oversee the audit of public companies that are subject to the securities laws . . . .

### **SOX § 101(c), 15 U.S.C. § 7211(c) provides in relevant part:**

Duties of the Board. The Board shall, subject to action by the Commission under section 7217 of this title, and once a determination is made by the Commission under subsection (d) of this section--

- (1) register public accounting firms that prepare audit reports for issuers, in accordance with section 7212 of this title;
- (2) establish or adopt, or both, by rule, auditing, quality control, ethics, independence, and other standards relating to the preparation of audit reports for issuers, in accordance with section 7213 of this title;
- (3) conduct inspections of registered public accounting firms, in accordance with section 7214 of this title and the rules of the Board;
- (4) conduct investigations and disciplinary proceedings concerning, and impose appropriate sanctions where justified upon, registered public accounting firms and associated persons of such firms, in accordance with section 7215 of this title;
- (5) perform such other duties or functions as the Board (or the Commission, by rule or order) determines are necessary or appropriate to promote high professional standards among, and improve the quality of audit services offered by, registered public accounting firms and associated persons thereof, or otherwise to carry out this Act, in order to protect investors, or to further the public interest;

- (6) enforce compliance with this Act, the rules of the Board, professional standards, and the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, by registered public accounting firms and associated persons thereof; and
- (7) set the budget and manage the operations of the Board and the staff of the Board.

**SOX § 101(e), 15 U.S.C. 7211(e) provides in relevant part:**

(1) Composition. The Board shall have 5 members, appointed from among prominent individuals of integrity and reputation who have a demonstrated commitment to the interests of investors and the public, and an understanding of the responsibilities for and nature of the financial disclosures required of issuers under the securities laws and the obligations of accountants with respect to the preparation and issuance of audit reports with respect to such disclosures.

...

(4) Appointment of Board members

(A) Initial Board. Not later than 90 days after July 30, 2002, the Commission, after consultation with the Chairman of the Board of Governors of the Federal Reserve System and the Secretary of the Treasury, shall appoint the chairperson and other initial members of the Board, and shall designate a term of service for each.

(B) Vacancies. A vacancy on the Board shall not affect the powers of the Board, but shall be filled in the same manner as provided for appointments under this section.

(5) Term of service

(A) In general. The term of service of each Board member shall be 5 years, and until a successor is appointed, except that--

(i) the terms of office of the initial Board members (other than the chairperson) shall expire in annual increments, 1 on each of the first 4 anniversaries of the initial date of appointment; and

(ii) any Board member appointed to fill a vacancy occurring before the expiration of the term for which the predecessor was appointed shall be appointed only for the remainder of that term.

...

(6) Removal from office. A member of the Board may be removed by the Commission from office, in accordance with section 7217(d)(3) of this title, for good cause shown before the expiration of the term of that member.

**SOX § 103(a)(1), 15 U.S.C. § 7213(a)(1) provides:**

In general. The Board shall, by rule, establish, including, to the extent it determines appropriate, through adoption of standards proposed by 1 or more professional groups of accountants designated pursuant to paragraph (3)(A) or advisory groups convened

pursuant to paragraph (4), and amend or otherwise modify or alter, such auditing and related attestation standards, such quality control standards, and such ethics standards to be used by registered public accounting firms in the preparation and issuance of audit reports, as required by this Act or the rules of the Commission, or as may be necessary or appropriate in the public interest or for the protection of investors.

**SOX § 104, 15 U.S.C. § 7214 provides in relevant part:**

(a) In general. The Board shall conduct a continuing program of inspections to assess the degree of compliance of each registered public accounting firm and associated persons of that firm with this Act, the rules of the Board, the rules of the Commission, or professional standards, in connection with its performance of audits, issuance of audit reports, and related matters involving issuers.

(b) Inspection frequency

(1) In general. Subject to paragraph (2), inspections required by this section shall be conducted--

(A) annually with respect to each registered public accounting firm that regularly provides audit reports for more than 100 issuers; and

(B) not less frequently than once every 3 years with respect to each registered public accounting firm that regularly provides audit reports for 100 or fewer issuers.

(2) Adjustments to schedules. The Board may, by rule, adjust the inspection schedules set under paragraph (1) if the Board finds that different inspection schedules are consistent with the purposes of this Act, the public interest, and the protection of investors. The Board may conduct special inspections at the request of the Commission or upon its own motion.

(c) Procedures. The Board shall, in each inspection under this section, and in accordance with its rules for such inspections--

(1) identify any act or practice or omission to act by the registered public accounting firm, or by any associated person thereof, revealed by such inspection that may be in violation of this Act, the rules of the Board, the rules of the Commission, the firm's own quality control policies, or professional standards;

(2) report any such act, practice, or omission, if appropriate, to the Commission and each appropriate State regulatory authority; and

(3) begin a formal investigation or take disciplinary action, if appropriate, with respect to any such violation, in accordance with this Act and the rules of the Board.

(d) Conduct of inspections. In conducting an inspection of a registered public accounting firm under this section, the Board shall--

(1) inspect and review selected audit and review engagements of the firm (which may include audit engagements that are the subject of ongoing litigation or other controversy between the firm and 1 or more third parties), performed at various offices and by various associated persons of the firm, as selected by the Board;

(2) evaluate the sufficiency of the quality control system of the firm, and the manner of the documentation and communication of that system by the firm; and

(3) perform such other testing of the audit, supervisory, and quality control procedures of the firm as are necessary or appropriate in light of the purpose of the inspection and the responsibilities of the Board.

...

(f) Procedures for review. The rules of the Board shall provide a procedure for the review of and response to a draft inspection report by the registered public accounting firm under inspection. The Board shall take such action with respect to such response as it considers appropriate (including revising the draft report or continuing or supplementing its inspection activities before issuing a final report), but the text of any such response, appropriately redacted to protect information reasonably identified by the accounting firm as confidential, shall be attached to and made part of the inspection report.

...

(h) Interim Commission review

(1) Reviewable matters. A registered public accounting firm may seek review by the Commission, pursuant to such rules as the Commission shall promulgate, if the firm--

(A) has provided the Board with a response, pursuant to rules issued by the Board under subsection (f) of this section, to the substance of particular items in a draft inspection report, and disagrees with the assessments contained in any final report prepared by the Board following such response; or

(B) disagrees with the determination of the Board that criticisms or defects identified in an inspection report have not been addressed to the satisfaction of the Board within 12 months of the date of the inspection report, for purposes of subsection (g)(2) of this section.

(2) Treatment of review. Any decision of the Commission with respect to a review under paragraph (1) shall not be reviewable under section 78y of this title, or deemed to be "final agency action" for purposes of section 704 of Title 5.

**SOX § 105, 15 U.S.C. § 7215 provides in relevant part:**

(a) In General.--The Board shall establish, by rule, subject to the requirements of this section, fair procedures for the investigation and disciplining of registered public accounting firms and associated persons of such firms.

(b) Investigations.--

(1) Authority.-- In accordance with the rules of the Board, the Board may conduct an investigation of any act or practice, or omission to act, by a registered public accounting firm, any associated person of such firm, or both, that may violate any provision of this Act, the rules of the Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under this Act, or professional standards, regardless of how the act, practice, or omission is brought to the attention of the Board.

(2) Testimony and document production.-- In addition to such other actions as the Board determines to be necessary or appropriate, the rules of the Board may—

(A) require the testimony of the firm or of any person associated with a registered public accounting firm, with respect to any matter that the Board considers relevant or material to an investigation;

(B) require the production of audit work papers and any other document or information in the possession of a registered public accounting firm or any associated person thereof, wherever domiciled, that the Board considers relevant or material to the investigation, and may inspect the books and records of such firm or associated person to verify the accuracy of any documents or information supplied;

(C) request the testimony of, and production of any document in the possession of, any other person, including any client of a registered public accounting firm that the Board considers relevant or material to an investigation under this section, with appropriate notice, subject to the needs of the investigation, as permitted under the rules of the Board; and

(D) provide for procedures to seek issuance by the Commission, in a manner established by the Commission, of a subpoena to require the testimony of, and production of any document in the possession of, any person, including any client of a registered public accounting firm, that the Board considers relevant or material to an investigation under this section.

(3) Noncooperation with investigations.----

(A) In general.--If a registered public accounting firm or any associated person thereof refuses to testify, produce documents, or otherwise cooperate with the Board in connection with an investigation under this section, the Board may--

(i) suspend or bar such person from being associated with a registered public accounting firm, or require the registered public accounting firm to end such association;

(ii) suspend or revoke the registration of the public accounting firm; and

(iii) invoke such other lesser sanctions as the Board considers appropriate, and as specified by rule of the Board.

(B) Procedure.--Any action taken by the Board under this paragraph shall be subject to the terms of section 107(c).

...

(c) Disciplinary Procedures.—

(1) Notification; recordkeeping.-- The rules of the Board shall provide that in any proceeding by the Board to determine whether a registered public accounting firm, or an associated person thereof, should be disciplined, the Board shall—

(A) bring specific charges with respect to the firm or associated person;

(B) notify such firm or associated person of, and provide to the firm or associated person an opportunity to defend against, such charges; and

(C) keep a record of the proceedings.

...

(4) Sanctions.-- If the Board finds, based on all of the facts and circumstances, that a registered public accounting firm or associated person thereof has engaged in any act or practice, or omitted to act, in violation of this Act, the rules of the

Board, the provisions of the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, including the rules of the Commission issued under this Act, or professional standards, the Board may impose such disciplinary or remedial sanctions as it determines appropriate, subject to applicable limitations under paragraph (5), including--

- (A) temporary suspension or permanent revocation of registration under this title;
- (B) temporary or permanent suspension or bar of a person from further association with any registered public accounting firm;
- (C) temporary or permanent limitation on the activities, functions, or operations of such firm or person (other than in connection with required additional professional education or training);
- (D) a civil money penalty for each such violation, in an amount equal to—
  - (i) not more than \$ 100,000 for a natural person or \$ 2,000,000 for any other person; and
  - (ii) in any case to which paragraph (5) applies, not more than \$ 750,000 for a natural person or \$ 15,000,000 for any other person;
- (E) censure;
- (F) required additional professional education or training; or
- (G) any other appropriate sanction provided for in the rules of the Board.

...

(e) Stay of Sanctions.--

(1) In general.-- Application to the Commission for review, or the institution by the Commission of review, of any disciplinary action of the Board shall operate as a stay of any such disciplinary action, unless and until the Commission orders (summarily or after notice and opportunity for hearing on the question of a stay, which hearing may consist solely of the submission of affidavits or presentation of oral arguments) that no such stay shall continue to operate.

(2) Expedited procedures.-- The Commission shall establish for appropriate cases an expedited procedure for consideration and determination of the question of the duration of a stay pending review of any disciplinary action of the Board under this subsection.

**SOX § 107, 15 U.S.C. § 7217 provides in relevant part:**

(a) General Oversight Responsibility.--The Commission shall have oversight and enforcement authority over the Board, as provided in this Act. The provisions of section 17(a)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78q(a)(1)), and of section 17(b)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78q(b)(1)) shall apply to the Board as fully as if the Board were a "registered securities association" for purposes of those sections 17(a)(1) and 17(b)(1).

(b) Rules of the Board.--

(1) Definition.-- In this section, the term "proposed rule" means any proposed rule of the Board, and any modification of any such rule.

(2) Prior approval required.-- No rule of the Board shall become effective without

prior approval of the Commission in accordance with this section, other than as provided in section 103(a)(3)(B) with respect to initial or transitional standards.

(3) Approval criteria.-- The Commission shall approve a proposed rule, if it finds that the rule is consistent with the requirements of this Act and the securities laws, or is necessary or appropriate in the public interest or for the protection of investors.

(4) Proposed rule procedures.-- The provisions of paragraphs (1) through (3) of section 19(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78s(b)) shall govern the proposed rules of the Board, as fully as if the Board were a "registered securities association" for purposes of that section 19(b), except that, for purposes of this paragraph--

...

(5) Commission authority to amend rules of the board.-- The provisions of section 19(c) of the Securities Exchange Act of 1934 (15 U.S.C. 78s(c)) shall govern the abrogation, deletion, or addition to portions of the rules of the Board by the Commission as fully as if the Board were a "registered securities association" for purposes of that section 19(c), except that the phrase "to conform its rules to the requirements of this title and the rules and regulations thereunder applicable to such organization, or otherwise in furtherance of the purposes of this title" in section 19(c) of that Act shall, for purposes of this paragraph, be deemed to read "to assure the fair administration of the Public Company Accounting Oversight Board, conform the rules promulgated by that Board to the requirements of title I of the Sarbanes-Oxley Act of 2002, or otherwise further the purposes of that Act, the securities laws, and the rules and regulations thereunder applicable to that Board".

(c) Commission Review of Disciplinary Action Taken by the Board.--

(1) Notice of sanction.-- The Board shall promptly file notice with the Commission of any final sanction on any registered public accounting firm or on any associated person thereof, in such form and containing such information as the Commission, by rule, may prescribe.

(2) Review of sanctions.-- The provisions of sections 19(d)(2) and 19(e)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78s (d)(2) and (e)(1)) shall govern the review by the Commission of final disciplinary sanctions imposed by the Board (including sanctions imposed under section 105(b)(3) of this Act for noncooperation in an investigation of the Board), as fully as if the Board were a self-regulatory organization and the Commission were the appropriate regulatory agency for such organization for purposes of those sections 19(d)(2) and 19(e)(1), except that, for purposes of this paragraph--

(A) section 105(e) of this Act (rather than that section 19(d)(2)) shall govern the extent to which application for, or institution by the Commission on its own motion of, review of any disciplinary action of the Board operates as a stay of such action;

(B) references in that section 19(e)(1) to "members" of such an organization shall be deemed to be references to registered public accounting firms;

(C) the phrase "consistent with the purposes of this title" in that section 19(e)(1) shall be deemed to read "consistent with the purposes of this title and title I of the Sarbanes-Oxley Act of 2002";

(D) references to rules of the Municipal Securities Rulemaking Board in that section 19(e)(1) shall not apply; and

(E) the reference to section 19(e)(2) of the Securities Exchange Act of 1934 shall refer instead to section 107(c)(3) of this Act.

(3) Commission modification authority.-- The Commission may enhance, modify, cancel, reduce, or require the remission of a sanction imposed by the Board upon a registered public accounting firm or associated person thereof, if the Commission, having due regard for the public interest and the protection of investors, finds, after a proceeding in accordance with this subsection, that the sanction--

(A) is not necessary or appropriate in furtherance of this Act or the securities laws; or

(B) is excessive, oppressive, inadequate, or otherwise not appropriate to the finding or the basis on which the sanction was imposed.

(d) Censure of the Board; Other Sanctions.--

(1) Rescission of board authority.-- The Commission, by rule, consistent with the public interest, the protection of investors, and the other purposes of this Act and the securities laws, may relieve the Board of any responsibility to enforce compliance with any provision of this Act, the securities laws, the rules of the Board, or professional standards.

(2) Censure of the board; limitations.-- The Commission may, by order, as it determines necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act or the securities laws, censure or impose limitations upon the activities, functions, and operations of the Board, if the Commission finds, on the record, after notice and opportunity for a hearing, that the Board--

(A) has violated or is unable to comply with any provision of this Act, the rules of the Board, or the securities laws; or

(B) without reasonable justification or excuse, has failed to enforce compliance with any such provision or rule, or any professional standard by a registered public accounting firm or an associated person thereof.

(3) Censure of board members; removal from office.-- The Commission may, as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act or the securities laws, remove from office or censure any member of the Board, if the Commission finds, on the record, after notice and opportunity for a hearing, that such member—

(A) has willfully violated any provision of this Act, the rules of the Board, or the securities laws;

(B) has willfully abused the authority of that member; or

(C) without reasonable justification or excuse, has failed to enforce compliance with any such provision or rule, or any professional standard by any registered public accounting firm or any associated person thereof.

**SOX § 109, 15 U.S.C. § 7219 provides in relevant part:**

(a) In General.--The Board, and the standard setting body designated pursuant to section 19(b) of the Securities Act of 1933, as amended by section 108, shall be funded as provided in this section.

(b) Annual Budgets.--The Board and the standard setting body referred to in subsection (a) shall each establish a budget for each fiscal year, which shall be reviewed and approved according to their respective internal procedures not less than 1 month prior to the commencement of the fiscal year to which the budget pertains (or at the beginning of the Board's first fiscal year, which may be a short fiscal year). The budget of the Board shall be subject to approval by the Commission. The budget for the first fiscal year of the Board shall be prepared and approved promptly following the appointment of the initial five Board members, to permit action by the Board of the organizational tasks contemplated by section 101(d).

(c) Sources and Uses of Funds.--

(1) Recoverable budget expenses.-- The budget of the Board (reduced by any registration or annual fees received under section 102(e) for the year preceding the year for which the budget is being computed), and all of the budget of the standard setting body referred to in subsection (a), for each fiscal year of each of those 2 entities, shall be payable from annual accounting support fees, in accordance with subsections (d) and (e). Accounting support fees and other receipts of the Board and of such standard-setting body shall not be considered public monies of the United States.

(2) Funds generated from the collection of monetary penalties.-- Subject to the availability in advance in an appropriations Act, and notwithstanding subsection (i), all funds collected by the Board as a result of the assessment of monetary penalties shall be used to fund a merit scholarship program for undergraduate and graduate students enrolled in accredited accounting degree programs, which program is to be administered by the Board or by an entity or agent identified by the Board.

(d) Annual Accounting Support Fee for the Board.--

(1) Establishment of fee.-- The Board shall establish, with the approval of the Commission, a reasonable annual accounting support fee (or a formula for the computation thereof), as may be necessary or appropriate to establish and maintain the Board. Such fee may also cover costs incurred in the Board's first fiscal year (which may be a short fiscal year), or may be levied separately with respect to such short fiscal year.

(2) Assessments.-- The rules of the Board under paragraph (1) shall provide for the equitable allocation, assessment, and collection by the Board (or an agent appointed by the Board) of the fee established under paragraph (1), among issuers, in accordance with subsection (g), allowing for differentiation among classes of issuers, as appropriate.