

No. 08-861

In The
Supreme Court of the United States

FREE ENTERPRISE FUND AND
BECKSTEAD AND WATTS, LLP,
Petitioners,

v.

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD
AND UNITED STATES OF AMERICA,
Respondents.

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

Brief of *Amicus Curiae* The Claremont Institute
Center for Constitutional Jurisprudence
In Support of Petitioners

John C. Eastman
Counsel of Record
Karen J. Lugo
Center for Const'l Juris.
c/o Chapman Univ. Sch. of Law
One University Dr.
Orange, CA 92866
(714) 628-2500

*Counsel for Amicus Curiae The Claremont Institute
Center for Constitutional Jurisprudence*

QUESTIONS PRESENTED

1. Whether the Sarbanes-Oxley Act violates the Constitution's separations of powers by vesting members of the Public Company Accounting Oversight Board ("PCAOB") with far-reaching executive power while completely stripping the President of all authority to appoint or remove those members or otherwise supervise or exercise control over that power, or whether, as the court of appeals held, the Act is constitutional because Congress can restrict the President's removal in any way it "deems best for the public interest."
2. Whether the court of appeals erred in holding that, under the Appointments Clause, PCAOB members are "inferior officers" directed and supervised by the Securities and Exchange Commission ("SEC") merely because the SEC may review some of the members' work product, where the SEC lacks any authority to supervise those members personally, to remove the members for any policy-related reason or to influence the members' key investigative functions.
3. If the Court of Appeals correctly determined that Act's provision for their appointment by the SEC violates the Appointments Clause either because the SEC is not a "Department" under *Freytag v. Commissioner*, 501 U.S. 868 (1991), or because the five commissioners are not the "Head" of the SEC.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	ii
TABLE OF AUTHORITIES	v
INTEREST OF <i>AMICUS CURIAE</i>	1
SUMMARY OF ARGUMENT	2
ARGUMENT	4
I. THE FOUNDERS FOLLOWED A RICH TRADITION IN POLITICAL PHILOSOPHY WHEN INCORPORATING SEPARATION OF POWERS PRINCIPLES INTO THE CONSTITUTION.....	4
II. THE FRAMERS INTENDED EXECUTIVE OVERSIGHT AND CONTROL OVER PCAOB-TYPE AGENCIES.....	9
A. PCAOB (Deconstructed).....	12
III. THE POWER OF APPOINTMENT WAS GIVEN TO THE EXECUTIVE TO AID IN EXECUTION OF PRESIDENTIAL DUTIES.	16
A. Executive was to have unitary authority to speak on behalf of government.....	16
B. The President was given appointment powers for purpose of delegating some administrative duties while retaining accountability	19

IV. REMOVAL POWER IS AN INTEGRAL PART OF EXECUTIVE AUTHORITY.....	21
A. Removal power derives from Section II authority	22
B. Separation of powers precludes distance between executive and administrative agencies.....	25
V. PCAOB ALSO SUFFERS FROM SERIOUS NON-DELEGATION PROBLEMS.....	27
VI. POLICY ARGUMENTS AGAINST PCAOB TYPE AGENCIES	30
CONCLUSION.....	32

TABLE OF AUTHORITIES

CASES

<i>A.L.A. Schechter Poultry Corp. v. United States</i> , 295 U.S. 495 (1935).....	27
<i>Bowsher v. Synar</i> , 478 U.S. 714, 721-22 (1986).....	26
<i>Buckley v. Valeo</i> , 424 U.S. 1 (1976)	20
<i>Cunningham v. Neagle</i> , 135 U.S. 1 (1980)	19
<i>Edmond v. United States</i> , 520 U.S. 651 (1997).....	11
<i>Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.</i> , 537 F.3d 667 (D.C. Cir. 2008)	25
<i>Humphrey’s Executor v. United States</i> , 295 U.S. 602 (1935).....	23
<i>INS v. Chadha</i> , 462 U.S. 919 (1983)	26
<i>J.W. Hampton, Jr. & Co. v. United States</i> , 276 U.S. 394 (1928).....	27, 28
<i>Lebron v. National Railroad Passenger Corp.</i> , 513 U.S. 374 (1995).....	10
<i>Mistretta v. United States</i> , 488 U.S. 361 (1989). 26, 27	
<i>Myers v. United States</i> , 272 U.S. 52 (1926)16, 19, 21, 24	
<i>Panama Ref. Co. v. Ryan</i> , 293 U.S. 388 (1935).....	22
<i>Russell Motor Car Co. v. United States</i> , 261 U.S. 514 (1923).....	19
<i>United States v. Eliason</i> , 41 U.S. (16 Pet.) 291 (1842)19	
<i>Wash. Airports Auth. v. Citizens for Abatement of Aircraft Noise, Inc.</i> , 501 U.S. 252 (1991)	21
<i>Wilcox v. Jackson ex dem. McConnel</i> , 13 U.S. (13 Pet.) 498 (1829)	19
<i>Williams v. United States</i> , 42 U.S. (1 How.) 290 (1843).....	19

STATUTES

15 U.S.C.A. § 7211(a)	12, 13
15 U.S.C.A. § 7214(b)(1)(B).....	13
15 U.S.C.A. § 7215(b)(2)(D)	14
15 U.S.C. § 7251(c)(4)(D)(i)	12, 15
15 U.S.C.A. § 7215(c)(4)(F)	14

OTHER AUTHORITIES

Adams, Samuel, Letter to Henry H. Lee (Aug. 29, 1789), <i>available at</i> http://press-pubs.uchicago.edu/founders/documents/a2_2_2-3s47.html	23
Amar, Akhil, AMERICA'S CONSTITUTION (Random House 2005)	6, 14
American Electronics Association, <i>Sarbanes-Oxley Section 404: The 'Section' of Unintended Consequences and Its Impact on Small Businesses</i> , February 2005, <i>available at</i> http://www.aeanet.org/governmentaffairs/AeASOXPaperFinal021005.asp	14
Dawson, John, Virginia Convention Speech (June 1788), <i>reprinted in</i> 2 THE DEBATE ON THE CONSTITUTION 746 (Bernard Bailyn ed., Library of America 1993)	6
Kent, James, COMMENTARIES ON AMERICAN LAW (1873) (Oliver Wendell Holmes ed., Rothman & Co. 12 th ed., 1989).....	14
Nagy, Donna M., <i>Playing Peekaboo with Constitutional Law: The PCAOB and Its Public/Private Status</i> . 80 Notre Dame L. Rev. 971 (2005).....	12, 13

- Prakash, Saikrishna, *New Light on the Decision of 1789*, 91 Cornell L. Rev. 1021 (2006) 17, 18, 21, 22
- Starr, Kenneth W., *The PCAOB: An Obstacle to President Obama's Success*, The Wall Street Journal, May 13, 2009, available at <http://online.wsj.com/article/SB124216925017912671.html> 25
- Story, Joseph, *Commentaries on the Constitution of the Untied States* (Willian S. Hein & Co., Inc. 1994) (1891) 7, 17
- Story, Joseph, *A Familiar Exposition of the Constitution of the United States* (Regnery Gateway 1986) (1865) 7, 17
- Taub, Steven, *Oxley: I'm Not Happy with Sarbox*, CFO.com, April 6, 2007, available at http://www.cfo.com/article.cfm/8985156/c_8985869 15
- The Federalist No. 51 (James Madison) (The Modern Library 1980) 5,6
- Thornton, Bruce, *GREEK WAYS: HOW THE GREEKS CREATED WESTERN CIVILIZATION* (Encounter Books 2000) 3
- Tucker, St. George, *BLACKSTONE'S COMMENTARIES* (Law Book Exchange 1996) (1803) 4, 19, 20
- Tucker, St. George, *VIEW OF THE CONSTITUTION OF THE UNITED STATES* (The Liberty Fund 1999) (1803) 4, 5, 6, 21
- Washington, George, Letter to Bushrod Washington (Nov. 1787), in *George Washington: Writings* 661 (John H. Rhodehamel ed., Library of America 1997) 4
- Washington, George, Letter to Marquis de Lafayette (Feb. 1788), in *George Washington: Writings* 668

viii

(John H. Rhodehamel ed., Library of America
1997)..... 5

INTEREST OF *AMICUS CURIAE*¹

The Claremont Institute for the Study of Statesmanship and Political Philosophy is a non-profit educational foundation whose stated mission is to “restore the principles of the American Founding to their rightful and preeminent authority in our national life,” including the principle, at issue in this case, that the power of the Executive, as articulated in the Constitution and codified in the separation of powers doctrine and the Appointments Clause, does not allow government to create rogue agencies of far-reaching power outside the accountability owed to the people. The Institute pursues its mission through academic research, publications, scholarly conferences and, via its Center for Constitutional Jurisprudence, the selective appearance as *amicus curiae* in cases of constitutional significance.

The Claremont Institute Center for Constitutional Jurisprudence has participated as *amicus curiae* before this Court in several other cases of constitutional import, including *Elk Grove Unified School District v. Newdow*, No. 02-1624; *Zelman v. Simmons-Harris*, 536 U.S. 639 (2002), *Solid Waste Agency of Northern Cook County v. U.S. Army Corps of Engineers*, 531 U.S. 159 (2001); *Boy*

¹ The Claremont Institute Center for Constitutional Jurisprudence files this brief with the consent of all parties. The letters granting consent have been filed previously. Counsel for a party did not author this brief in whole or in part. No person or entity, other than *amicus curiae*, its members, or its counsel made a monetary contribution specifically for the preparation or submission of this brief.

Scouts of America v. Dale, 530 U.S. 640 (2000); and *United States v. Morrison*, 529 U.S. 598 (2000).

SUMMARY OF ARGUMENT

The creation and operation of the Public Company Accounting Oversight Board (PCAOB) unconstitutionally violates the separation-of-powers doctrine by vesting Executive powers in a public corporation that is largely immune from Executive oversight. Because policymaking convenience and complicity between Congress and the President does not excuse unconstitutional legislation, we ask the Court to strike down the PCAOB.

Part I closely examines the historical record to prove that the Founding generation clearly would have viewed a body with the powers of the PCAOB as providing an inherently governmental function of a distinctly executive nature. Consequently, the Constitution they crafted would regard the PCAOB as an Executive agency requiring presidential oversight. Part II demonstrates the importance of the President's powers of appointment to his constitutional duty to control the Executive Branch. Part III examines the importance of the appointment power from the perspective of the removal power.

Part IV explains that Congress violated the nondelegation doctrine by delegating powers that it does not possess and therefore may not legally delegate—namely, the Executive powers of appointment and oversight. Finally, Part V delineates the potential pitfalls that may result from

3

disabling government's oversight of its operations,
and therefore government's accountability to the
governed.

ARGUMENT

I. THE FOUNDERS FOLLOWED A RICH TRADITION IN POLITICAL PHILOSOPHY WHEN INCORPORATING SEPARATION OF POWERS PRINCIPLES INTO THE CONSTITUTION

Our Founding Fathers established a constitutional republic based upon the rule of law, expressly not the rule of shadowy committees beyond the scrutiny and reach of the citizenry. The very structure of the PCAOB with its attenuated oversight violates both the spirit and the letter of the Founders carefully crafted tripartite system of government designed according to a transcendent rule of law.

Beginning with ancient Greece there was a sense that political power should originate from a body of law that was above men who had potential for corruption and capture. “Political power must . . . reside in institutions, offices, laws and procedures that transcend any one man or group of men, . . . These compose a ‘common thing’ (*koinonia*) in which each citizen is a partner, and they function not through brute force but through reason and persuasion. The institutions of government must be available and beneficial to all citizens.” Bruce Thornton, *Greek Ways: How the Greeks Created Western Civilization* 121 (Encounter Books 2000). As Aristotle observed “governments which regard only

the interest of the rulers are all defective and perverted forms, for they are despotic.” *Id.*

When constitutional constraints are side-stepped and the mandated linkage between government agency and its assigned authority is broken, the result renders the law questioned and without authority. When George Washington discussed ratifying-era constitutional controversies with eventual Supreme Court Justice Bushrod Washington, he affirmed that “the power under the Constitution will always be with the people” when correcting power “exercised contrary to their interests.” Letter from George Washington to Bushrod Washington (Nov. 1787), *in George Washington: Writings* 661 (John H. Rhodehamel ed., Library of America 1997).

The Founders wisely designed a system of separated power with final authority residing in the “censorial power of the people, which is in effect a branch of the sovereign power itself. St. George Tucker, *View of the Constitution of the United States* 48 (The Liberty Fund 1999). However, this citizen oversight is contingent upon the constitutionally prescribed connection between the people and government officials. Blackstone described government “ministers” as “trustees or agents” of the people since the people “ought to do, themselves, whatever they conveniently can; [and] that, what they can not do of themselves, must be committed to the management of ministers chosen by themselves; . . .” 2 St. George Tucker, *Blackstone’s Commentaries* 174 (Law Book Exchange 1996).

Yet, when these “ministers” abuse power, the citizenry have as their rightful recourse elective leverage. Therefore, the Chief Executive, as the official in charge of subordinate appointees, must have direct and unobstructed ability to review and correct the activities of committees fulfilling the roles of appointed agents. Tucker knew the necessity of citizen oversight, even if through the Executive, when he called the representative who dared to openly violate his duty “bold and desperate” when “he knows himself amenable to the people for such a breach of trust.” Tucker, *View of the Constitution, supra*, at 48.

In creating the PCAOB Committee Congress worked to produce an opaque and unaccountable body removed from proper Executive correction and citizen scrutiny. St. George Tucker warned that if the people were to remain sovereign, the citizenry must have the ability to censor the agent “that forgets his responsibility.” *Id.* He predicted that where the vigilance and attention of the people is wanting, “usurpation is often as little perceived as that of a star, rising in the east whilst the sun is in the meridian.” Tucker anticipated incremental power transfers, but found them particularly insidious because they are difficult to detect and easy to rationalize. *Id.* at 49.

Beyond citizen vigilance, the Founders realized the need for “auxiliary precautions” as taught by mankind’s experience with what Washington delicately called the “defect of better motives.” “[O]pposite and rival interests” were thus introduced

to “divide and arrange the several offices in such a manner as that each may be a check on the other; . . .” *The Federalist No. 51*, at 337 (James Madison) (The Modern Library 1980). Justice Story wrote that “free institutions [have] ever been found essentially to depend . . . [on] a system of checks and balances.” He endorsed the corrective influence of “distributing the power among different branches, each having a check upon the other.”¹ Joseph Story, *Commentaries on the Constitution of the United States* 378 (William S. Hein & Co., Inc. 1994) (1891). George Washington was confident that the separated powers were “so distributed among the Legislative, Executive, and Judicial Branches . . . that it can never be in danger of degenerating into any [other] despotic or oppressive form.” Letter from George Washington to Marquis de Lafayette (Feb. 1788), *in Washington, supra*, at 668.

The Framers of our Constitution thus paid heed to the wisdom of Baron de Montesquieu and organized a separated, balanced, and accountable government structure designed to expose the people’s business to citizen judgment. Through the tripartite system of government they designed, they intentionally inhibited the exercise, and therefore the abuse of power: “But constant experience shows us that every man invested with power is apt to abuse it, and to carry his authority as far as it will go. Is it not strange, though true, to say that virtue itself has need of limits? To prevent this abuse, it is necessary from the very nature of things that power should be a check to power.” Baron de Montesquieu,

The Spirit of the Laws 150 (Thomas Nugent trans., Hafner Pub. Co. 1949). “No man is a warmer advocate for *proper* restraints and *wholesome* checks in every department of government than I am.” Washington, *supra*, at 662 (emphasis in original). “That the Legislative, Executive, and Judicial powers, should be separate and distinct, in all free governments, is a political fact, so well established, . . . that no country ever did, or ever can long remain free, where they are blended.” John Dawson, June 1788 Virginia Convention Speech, *reprinted in* 2 THE DEBATE ON THE CONSTITUTION 746 (Bernard Bailyn ed., Library of America 1993).

The Founders knew that a successful constitutional republic must rise above ministerial lawmaking. They understood that for liberty to thrive, power must be diffused and counterweighted. Thomas Jefferson recommended that “powers of government should be so divided and balanced among several bodies of magistracy, as that no one could transcend their legal limits, without being effectually checked and restrained by the others.” Letter from Thomas Jefferson to Benjamin Rush (Sept. 23, 1800), *in* Akhil Amar, *America’s Constitution* 60 (Random House 2005). Indeed, Madison argued that “the constant aim” of our Constitution is to vest each member of our government with a personal interest in preventing encroachment by members of opposing branches so that “the private interest of every individual may be a sentinel over the public rights.” *The Federalist No. 51*, at 337 (James Madison) (The Modern Library

1980). Ultimately, power had to be “divided, subdivided, and distributed into so many separate channels” so that it would not rush down “in one single torrent, overwhelming and sweeping away whatever it encounters in its passage.” Tucker, *View of the Constitution*, supra, at 48.

II. The Framers Intended Executive Oversight and Control over PCAOB-Type Agencies.

The Public Company Accounting Oversight Board (PCAOB) was established “in order to protect the interests of investors and further the public interest in preparation of informative, accurate, and independent audit reports for companies the securities of which are sold to, and held by and for, public investors.” 15 U.S.C.A. § 7211(a) (West Supp. 2004). With this language PCAOB was established as a watchdog agency to combat accounting fraud and management negligence, the revelation of which resulted in the demise of Enron and WorldCom. However, this oversight agency’s structure essentially creates an ironic environment for oversight since the Board whose mission is to restore accountability to America’s business market is not itself accountable to the chief executive. Without any accountability, the PCAOB may be susceptible to abuse of its rulemaking and disciplinary functions. Even worse, if not checked this model will surely serve as a prototype for similar agencies.

Created by the Sarbanes-Oxley Act of 2002, the PCAOB sets auditing standards for the auditors of

public companies. The PCAOB functions as a rule maker, adjudicator and disciplinarian. While functioning like an executive agency that also has legislative and judicial powers, the committee's five members are not appointed by the President but by five commissioners of the Securities and Exchange Commission (SEC), which is in turn significantly independent of the President. Another feature of this committee, causing it to function like an *independent* executive committee, is that the five members are removable only for cause by the SEC, and not at will. This organizational characteristic causes PCAOB to be two steps removed from accountability to the Chief Executive.

Even with Congress labeling PCAOB as a "private nonprofit corporation," rather than the government agency it seems to be, it is likely that under this court's holding in *Lebron v. National Railroad Passenger Corp.*, 513 U.S. 374 (1995), Congress's best efforts to keep PCAOB private will be unavailing. In *Lebron*, the court introduced a three-prong test to determine whether a private entity was indeed the government itself. The three-prong test involves an inquiry into: (1) whether the government created the entity, (2) whether the government created the entity to further governmental objectives, and (3) whether the government retains permanent authority to appoint a majority of the directors.

There is little analysis necessary to determine that PCAOB satisfies all three-prongs in *Lebron*. PCAOB was created by Congress in Title I of

Sarbanes-Oxley. The objectives of the PCAOB are far more governmental than those of the entities involved in any of the prior cases presented to the courts. The language of the statute that created the PCAOB describes that PCAOB's mission is to protect "the interests of investors and furthering the public interest in the preparation of reliable audit reports." Additionally, PCAOB's rulemaking, enforcement, and adjudicative powers are quintessentially governmental powers. Finally, Title I additionally grants the SEC (a government agency) the power to appoint all five members so long as PCAOB is in existence. Therefore, despite Congress' best efforts to label PCAOB as a private entity, available case law indicates otherwise.

Additionally, although the Court of Appeals held that the PCAOB board members were considered "inferior officers," the holding in *Edmond v. United States*, 520 U.S. 651 (1997), strongly suggests otherwise. Although this court did not firmly establish a set of criterion in analyzing whether an individual should be considered an "inferior officer," the court did indicate that the level of supervisory authority should be the primary indicia. *Id.* at 1583. Unlike *Edmond*, where the court found military judges to be "inferior officers," the PCAOB operates under far less supervisory control. The PCAOB board members are not removable without cause,²

² The court stated that "the power to remove officers...is a powerful tool for control. *Id.* at 1581. As has been stated so many times, the SEC is unable to remove PCAOB board members without cause, thus stripping the SEC of this "powerful tool for control."

are able to initiate investigations and make rulings without the consent of the SEC and were vested with vast regulatory powers. This lack of SEC supervisory control over the PCAOB makes the ruling below that the PCAOB board members are “inferior officers” at odds with *Edmond*.

A. PCAOB (Deconstructed)

Section 101 of Title 1 establishes and delineates the Board’s principal responsibilities. It states:

- (a) ESTABLISHMENT OF BOARD.- There is established the Public Company Accounting Oversight Board, to oversee the audit of public companies that are subject to the securities laws, and related matters, *in order to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports* for companies the securities of which are sold to, and held by and for, public investors. The Board shall be a body corporate, operate as a nonprofit corporation, and have succession until dissolved by an Act of Congress.

15 U.S.C.A. § 7211(a) (West Supp. 2004) (emphasis added).

Upon a reading of this section it becomes apparent that Congress intended that this “private

non-profit corporation” would also be vested with an inherently government mission. In order to accomplish this government mission, PCAOB was granted far-reaching power that it has exercised since its inception without any accountability to the chief executive.³

PCAOB’s extensive power is evidenced upon a review of their rulemaking and disciplinary functions. Section 103 of Title I establishes the PCAOB as the primary standard-setter for auditors, requiring the PCAOB to promulgate rules establishing the auditing and related attestation standards, quality control standards, and ethics standards to be used by registered firms. *Id.* The PCAOB has used this power to complicate compliance requirements with vague language and statutory additions that add nothing to investor security aside from burdening auditors and their associated individuals.

Included in the PCAOB’s power to create rules and standards for auditors is its broad authority to grant exemptions to any person, issuer, public accounting firm, or transaction. 15 U.S.C.A. §

³ Even supporters of the bill like Senator Phil Gramm recognized the significant governmental powers that were being bestowed upon PCAOB: “This board is going to have massive power, unchecked power, by design... We are setting up a board with massive power that is going to make decisions that affect all accountants and everybody they work for, which directly or indirectly is every breathing person in the country. They are going to have massive unchecked powers.” Donna M. Nagy, *Playing Peekaboo with Constitutional Law: The PCAOB and Its Public/Private Status*, 80 Notre Dame L. Rev. 971, 1003 (2005) (quoting 148 Cong. Rec. S6334 (Sen. Gramm)).

7214(b)(1)(B). The only qualifier to the PCAOB's exemption power is the requirement that "the exemption is necessary or appropriate in the public interest." *Id.*

Section 105 of Title 1 grants the PCAOB broad authority to conduct investigations and impose discipline. This includes an authorization to investigate any act, practice, or failure to act, by any registered firm, or its associated persons that may violate Sarbanes-Oxley, rules of the Board or provisions of the securities laws. *Id.* § 7215(b)(1). Pursuant to its investigatory powers, the PCAOB may require testimony or production of documents from both registered firms and their associated persons as well as the clients themselves. Should there be a refusal to cooperate the Board can elect to seek a subpoena or levy fines. *Id.* § 7215(b)(2)(D).

Should the PCAOB find a violation, the PCAOB has a wide array of disciplinary actions at their disposal, including: censure, required additional professional education, temporary suspension, permanent revocation, limitation on activities and civil monetary penalties (this includes fines for both intentional and un-intentional violations). *Id.* § 7215(c) (4)(F).

In addition to the costs imposed by disciplinary actions, Congress authorized PCAOB to fund itself through the assessment of "accounting support fees" paid by public companies, imposing even more direct costs. Moreover, in addition to these fees and fines, PCAOB's constant tightening of the rules and regulations have imposed high compliance and

regulatory costs on both registered firms and individuals. A recent study performed by the University of Rochester, estimates that the annual costs of the Board's rules are over \$35 billion. American Electronics Association, *Sarbanes-Oxley Section 404: The 'Section' of Unintended Consequences and Its Impact on Small Businesses*, February 2005, Available at <http://www.aeanet.org/governmentaffairs/AeASOXPaperFinal021005.asp>.

These high costs to the public have been attributed to the mountain of red tape that the PCAOB is charged with creating and its broad interpretation of Sarbanes-Oxley's rules on what constitutes "internal controls." It is these powers that have caused the PCAOB to reward the big accounting firms with unreasonably complex and costly compliance regulations that only they can handle. This has essentially made small accounting firms irrelevant and unable to compete. Even former Congressman Michael Oxley (one of the namesakes of Sarbanes-Oxley) has recognized the problem, noting that the original bill "was two paragraphs long, but by the time the PCAOB was done, it was 330 pages of regulations. It was far too prescriptive and [more] expensive than anyone anticipated." Steven Taub, *Oxley: I'm Not Happy with Sarbox*, CFO.com, April 6, 2007, available at http://www.cfo.com/article.cfm/8985156/c_8985869.

As presently organized, with massive budgets and far-reaching powers, PCAOB is the type of government agency that the Founders intended to be

directly overseen by the Executive. Any branch that can level penalties upwards of \$2 million for unintentional violations and over \$15 million for intentional violations, *see* 15 U.S.C. § 7251(c)(4)(D)(i), has too much power without any accountability to the public upon which is imposing such burdensome time and financial costs.⁴ As Senator Gramm so bluntly stated, PCAOB affects “every breathing person” in the United States and should therefore be held accountable to the Executive and thus to the public.

III. The Power of Appointment was Given to the Executive to Aid in Execution of Presidential Duties.

A. Executive was to have unitary authority to speak on behalf of government.

The Framers understood the need for a “strong executive” in the areas of both foreign affairs and domestic administration. “[A]fter a controversial discussion the executive power of the government was vested in one person and many of his important functions were specified so as to avoid the

⁴ It is also worth noting that in 2008, PCAOB Chairman Mark Olson earned an annual salary of \$654,406 with the remaining four members receiving \$531,995 annually. These salaries are significantly higher than those earned by members of Congress as even by the President of the United States, further demonstrating the necessity of accountability to the chief executive and through him to the public.

humiliating weakness of the Congress during the Revolution and under the Articles of Confederation.” *Myers v. United States*, 272 U.S. 52, 117-18 (1926), quoting 1 Max Farrand, *Records of the Federal Convention of 1787* 66-97 (1911). Because the President was to speak with a voice of authority on foreign policy matters and to lead in setting domestic priorities, Article II simply begins with a simple but comprehensive assignment of executive power to the President: “The executive Power shall be vested in a President of the United States of America.” U.S. Const., Art. II, Sec. 1.

Several states had experimented with executive councils and abandoned the idea in favor of a single executive magistrate. They recognized, as Justice Story would later note, that “a council often becomes the means, either of shifting off all effective responsibility from the chief magistrate, or of intrigues and oppositions, which destroy his power, and supplant his influence.” Story, *Commentaries, supra*, at 288. Legal commentator James Kent also noted the failed experience in states that tried to govern by council:

Unity increases not only the efficacy, but the responsibility, of the executive power. Every act can be immediately traced and brought home to the proper agent. There can be no concealment of the real author, nor, generally, of the motives of public measures, when there are no associates to divide or to mask responsibility. There will be much less temptation to depart from duty, and much

greater solicitude for reputation, when there are no partners to share the odium, or to communicate confidence by their example. The eyes of the people will be constantly directed to a single conspicuous object; and, for these reasons, De Lolme (a) considered it to be a sound axiom of policy, that the executive power was more easily confined when it was one. "If the execution of the laws," he observes, "be entrusted to a number of hands, the true cause of public evils is hidden.

James Kent, COMMENTARIES ON AMERICAN LAW 291 (Oliver Wendell Holmes ed., Rothman & Co. 12th ed., 1989) (1873).

The Framers vested executive authority in the President for purposes of unity, consistency, and accountability. The President may choose to delegate some responsibilities to agencies over which he has direct oversight but it is clear that the Framers did not intend that boards and committees fulfill Executive functions while entirely removed from Executive supervision. This practice results in exactly the "government by council or committee" that the Framers expressly rejected. *See Amar, supra*, at 197 ("What Article II did make emphatically clear from start to finish was that the president would be personally responsible for his branch.")

B. The President was given appointment powers for the purpose of delegating some administrative duties while retaining accountability.

The president as Chief Executive is charged in Section 2, with the power of appointing superior officers: He shall have Power, . . . and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, . . . and all other Officers of the United States.” U.S. Const., Art. II, Sec. 2. Justice Story called the power of appointment “one of the most important and delicate in a republican government” and warned that it could become “one of the most dangerous engines to destroy private independence and public liberty, which can assail the public.” While Story spoke of these dangers he also commended the Framers for installing safeguards against the abuse of power like the Senatorial advice and consent feature. Joseph Story, *A Familiar Exposition of the Constitution of the United States* 218 (Regnery Gateway 1986) (1865).

This Court evaluated the Framers’ words and intentions when contemplating presidential appointment duties in *Myers v. United States*. Chief Justice Taft’s exhaustive study led him to conclude, for the Court, that although the President was obliged to “faithfully execute the laws,” he could not personally attend to all aspects of his duties, so “the reasonable implication, even in the absence of express words, was that as part of his executive

power he should select those who were to act for him under his direction in the execution of the laws.” Myers, 272 U.S. at 118-119. See also *Wilcox v. Jackson ex dem, McConnel*, 38 U.S. (13 Pet.) 498, 513 (1839); *United States v. Eliason*, 41 U.S. (16 Pet.) 291, 302 (1842); *Williams v. United States*, 42 U.S. (1 How.) 290, 297 (1843); *Cunningham v. Neagle*, 135 U. S. 1, 63 (1890); *Russell Motor Car Co. v. United States*, 261 U. S. 514, 523 (1923); and Blackstone (“The constitution of the United States has made ample provision for [the Executive’s] aid in these respects, by assigning to him ministers to whom the conduct of each of the executive departments may be committed . . .” Tucker, *Blackstone, supra*, at 319.

The very idea of creating a regulatory board to monitor compliance with federal laws, yet operating two steps removed from Executive authority, would have been completely inconsistent with founding era aims to institutionally frustrate isolated and opaque power centers. Blackstone cautioned that power and authority should be delegated with an eye to accountability and trust writing “that the choice of ministers may be made, either, personally, by the whole body of the people; or by their deputies, chosen for that especial purpose, and in whom they can repose a proper confidence.” *Id.*

Blackstone accurately and presciently identified the exact issue presented in the PCAOB executive-in-nature, but not executive-in-accountability, committee when he exposed the due concern given “numerous boards” resulting in “divided responsibility” until “it is entirely lost, and where the

chance of unanimity lessens in geometrical proportion to the number that compose it.” *Id.* What Blackstone, Justice Story and the Framers recognized was that the lessening of unanimity, or unity, resulted in the attendant lessening of accountability since spotting a person designated with responsibly to the electorate is obviously more difficult for each layer of decision-making and each additional horizontal committee member.⁵

IV. Removal Power is an Integral Part of Executive Authority

Records reflecting founding and ratifying era discussions on presidential power to *remove* appointees are scarce. The logical reason for the attention to appointment protocols but not the same emphasis on removal procedures is that Framers expected executive removal power to stem from the President’s authority to appoint superior officers.

⁵ As to the claim that PCAOB officers are inferior or that their duties do not rise to a level requiring Executive direction. We think its fair import is that any appointee exercising significant authority pursuant to the laws of the United States is an “Officer of the United States,” *Buckley v. Valeo*, 424 U.S. 1, 126 (1976). They may, therefore, properly perform duties only in aid of those functions that Congress may carry out by itself, or in an area sufficiently removed from the administration and enforcement of the public law as to permit their being performed by persons not “Officers of the United States.” *Id.* at 139]

A. Removal power derives from Section II authority.

The construction of PCAOB so that officers are removed, not by the Executive, but by appointed members of the SEC who are themselves significantly insulated from presidential oversight, is the most glaring violation of constitutional intent at issue in this case. This organizational feature contradicts the monumental ruling in *Myers v. United States*, 272 U.S. 52 (1926), where the court held that the President possesses a constitutional right under Article II to remove executive officials without cause.

One congressional debate is recorded that reveals early understanding of the Executive's removal power. According to Professor Saikrishna Prakash, who investigated the removal question for the authoritative Documentary History of the First Federal Congress, the seminal congressional "Decision of 1789" vindicates exclusive Presidential authority to remove appointees. Saikrishna Prakash, *New Light on the Decision of 1789*, 91 Cornell L. Rev. 1021, 1022 (2006).

While the final vote on the source of Executive Removal Power was split between a group that found the authority as emanating from the President's Executive Office and those that recognized a power reciprocal to the Appointment Power, the discussion in 1789 reveals that "the first Congress concluded that the Constitution's grant of executive power authorized the President to remove executive

officers” according to the actions and writing of men like:

Alexander Hamilton, writing as: Pacificus in 1793, had no doubt that the first Congress had endorsed the executive-power theory. Similarly, Chief Justice John Marshall, in his biography of George Washington, claimed that the Decision ‘has ever been considered as a full expression of the sense of the legislature’ that the Constitution granted the executive removal authority. William Howard Taft, the only Chief Justice to have also served as Chief Executive, read the Decision of 1789 in a similar vein. *Id.* at 1023-1024.

Professor Prakash offers additional proof in the actions of subsequent Presidents who demonstrated confidence that they had the power to remove officers by virtue of the Constitutional authority. Washington removed 23 officers, Adams 27, and Jefferson 124. These Presidents apparently did not cite the Decision of 1789 as the basis for these removals, so it is possible that each of them concluded that they had a constitutional removal power independent of the Decision of 1789. In any event, there is no evidence that anyone challenged these Presidents' removals despite the fact that no statute authorized them. *Id.* at 1066-1067.

At least one clear reference to the presumptive nature of executive removal authority was made during the ratification debates: “If there is a total Silence in the Constitution, is it not natural to conclude that an Officer holding during Pleasure is removable by the same Power which appointed him,

whether vested in a single Person, or a joint Number? . . . But in the Removal of Officers the President has not a Constitutional Council. *He must therefore be solely accountable.* Letter from Samuel Adams to Henry H. Lee (Aug. 29, 1789), *available at* http://press-pubs.uchicago.edu/founders/documents/a2_2_2-3s47.html (emphasis added).

When Justice Story wrote on the removal power he also cited the practice of President George Washington. Acknowledging the Constitution's silence on the subject, he attributed the doctrine of Executive removal to "just deference" to the "great man" and he observed that the practice of the President exercising the power of removal prevailed "without any restraint from the Senate." Story, *Familiar Exposition, supra*, at 219.

While the Court of Appeals' majority opinion viewed the removal issue in this case in a rather simple light under existing precedent, as Judge Kavanaugh correctly noted in his eloquent dissent, there is actually a great deal of difference between the present case and *Humphrey's Executor v. United States*, 295 U.S. 602 (1935). Mainly, the difference lies in the fact that the officials of the independent agencies at issues in *Humphrey's Executor* were removable for cause *by the President*, whereas members of the PCAOB are removable for cause only *by another independent agency*. It is this essential difference that places the President two levels of for-cause removal away from the PCAOB's Board members, a previously unheard of restriction on the

President's authority over executive officers. Therefore, rather than being *Humphrey's Executor* redux, as the majority below claimed, this case should rather be referred to as *Humphrey's Executor* squared. It is this unique characteristic of PCAOB's organization that places it beyond the bounds of *Humphrey's Executor* and instead into a realm all its own.

B. Separation of powers precludes distance between executive and administrative agencies.

The Founders created a government divided into three branches of accountable power: each checking the other and each responsible to the people. Within those branches, there was expressly not to be separation between officials and the people.

When this Court astutely analyzed and applied founding philosophy and constitutional debates in *Myers v. United States*, 272 U.S. 52 it performed the most comprehensive historical treatment ever given to legal analysis of the Executive's appointment and removal power. *See, generally, Myers*, 272 U.S. at 106-239. In *Myers* the Court found that legislative power was encroaching on Presidential prerogatives to unilaterally remove an executive branch official. This reasoning was then applied in *Springer v. Government of Philippine Islands* when the Court defined the distinction between legislative and executive delegation functions as follows:

Legislative power, as distinguished from executive power, is the authority to make laws, but not to enforce them or appoint the agents charged with the duty of such enforcement. The latter are executive functions.

Springer v. Government of Philippine Islands, 272 U.S. 189, 202 (1928).

The reason for this clear distinction cannot be lost in the vagueries of classifications and job titles. The Founders feared one thing above all else and that was tyranny. This theme is found repeatedly in early separation of powers discussions and attention to it remains an important aspect of our constitutional system of government. For the Founders, liberty was only as safe as the protections installed to resist tyranny. “[T]he Court has explained time after time that the separation of powers protects not simply the office and the officeholders, but also individual rights. As Justice Kennedy has stated, ‘Liberty is always at stake when one or more of the branches seek to transgress the separation of powers.’” *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 537 F.3d 667, 714 (D.C. Cir. 2008) (Kavanaugh, J., dissenting), quoting *Clinton v. City of New York*, 524 U.S. 417, 450 (1998) (Kennedy, J., concurring).

See also *Wash. Airports Auth. v. Citizens for Abatement of Aircraft Noise, Inc.*, 501 U.S. 252, 272 (1991) (“The ultimate purpose of this separation of

powers is to protect the liberty and security of the governed.”); *Mistretta v. United States*, 488 U.S. 361, 380 (1989) (separation of powers is “essential to the preservation of liberty”); *Bowsher v. Synar*, 478 U.S. 714, 721-22, 730 (1986) (separation of powers is “critical to preserving liberty”); *INS v. Chadha*, 462 U.S. 919, 963 n.4 (1983) (Powell, J., concurring in judgment) (discussing concern that “Congress is exercising unchecked judicial power at the expense of individual liberties” and stating it was “precisely to prevent such arbitrary action that the Framers adopted the doctrine of separation of powers”); see also Tucker, *View of the Constitution*, *supra*, at 48 (noting that the people had a responsibility, through their governmental agents, to “be sure to take part against those who would usurp either the rights of the people, or the proper functions of another agent:...as it is also the people who will ‘preserve the several branches of the government within their due limits’”).

V. PCAOB Also Suffers From Serious Non-delegation Problems.

Creation of the PCAOB has also violated the non-delegation doctrine because the agency it created represents a congressional delegation of a power Congress does not possess. Specifically, Congress has delegated executive power to a public corporation, yet it has deprived the President of his Constitutional mandate to appoint and supervise this *de facto* executive agency. Although the Court

rarely finds a non-delegation doctrine problem, it has recognized that Congress may not delegate powers it does not possess.

This Court has long held that the primary criterion for congressional delegation of decision-making authority to federal agencies requires enumeration of “an intelligible principle to which the person or body authorized to [act] is directed to conform.” *J.W. Hampton, Jr. & Co. v. United States*, 276 U.S. 394, 409 (1928). Congress has historically faced little difficulty complying with this elastic standard because all but two delegations of its powers have survived judicial scrutiny. See *Panama Ref. Co. v. Ryan*, 293 U.S. 388 (1935); and *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

However, this broad rule presupposes that Congress actually possesses the power it wishes to delegate. This Court has recognized that Congress may not delegate powers it does not possess. For example, the Court would not have upheld the delegation of sentencing guidelines to the Judicial Branch if Congress had trespassed against another Branch’s constitutional powers. The Court held that “Congress may delegate to the Judicial Branch non-adjudicatory functions that *do not trench upon the prerogatives of another Branch* and that are appropriate to the central mission of the Judiciary.” *Mistretta*, 488 U.S. at 388 (emphasis added).

Indeed, the Court has made it clear that delegations of authority may not usurp the powers constitutionally vested in other branches. Chief

Justice Taft wrote for the Court in *J.W. Hampton* that a delegation is unconstitutional “if by law it attempts to invest itself or its members with either executive power or judicial power.” *J.W. Hampton*, 276 U.S. at 406. Faithful extension of this doctrine also prevents Congress from creating a nongovernmental agency vested with Executive power, yet unsusceptible to Executive oversight. Moreover, the Court stated in *Loving v. United States* that “it remains a basic principle of our constitutional scheme that one branch of the government may not intrude upon the central prerogatives of another.” 517 U.S. 748, 757 (1996), citing *Plaut v. Spendthrift Farms, Inc.*, 514 U.S. 211, 225—26 (1995).

Contrary to this long established rule, Congress has “trenched upon the prerogatives of” the Executive Branch by insulating the Board members—who are performing an executive task—from presidential scrutiny. The Constitution explicitly states that the executive power is vested in the President, so Congress lacks the authority to restrict presidential oversight of this *de facto* executive agency.

This case therefore uniquely implicates the non-delegation doctrine not through the typical avenue of Congress granting too much legislative power to the Executive, but rather by depriving the President of his constitutional authority to manage the Executive Branch. This is precisely the delegatory “trench[ing] upon the prerogatives of another Branch” that *Mistretta* forbids, 488 U.S. at 388; and the delegatory

“invest[ment] of Executive powers that *J.W. Hampton* prohibits. 276 U.S. at 406.

This transgression yields the same substantive result as a textbook separation of powers problem, but is cloaked in the form of a seemingly benign delegation. Congress purportedly provides a new means of financial regulation replete with Executive power, yet it lacks any genuine accountability to the Executive. In this sense, the PCAOB delegation is a Trojan horse that promises executive power, yet deprives the executive of oversight.

VI. Policy Arguments Against PCAOB-Type Agencies.

The creation of PCAOB has essentially established a previously unknown realm of regulators. The new public/private regulator is public for purposes of rights, liberties and structures protected by the Constitution and private for purposes of accountability. By labeling PCAOB a private agency, Congress was able to circumvent the statutory obligations and protections that apply to the federal government. This in turn has made private/public regulators less accountable to the public, their actions less transparent and their policy less legitimate than their purely public counterparts. Further, a private/public regulator with policy making power such as PCAOB possesses significantly lessens Congress’ and the President’s own accountability to the public because it blurs

responsibility for unpopular or unsuccessful decision-making.

PCAOB's lack of an accountable structure has likely contributed to what members of both parties see as its policy failures. For example, as U.S. Senator John Kerry (D-MA) has noted, during most of the six years since its creation, PCAOB has hurt legitimate entrepreneurial companies by stretching the term "internal control" in Sarbanes-Oxley's section 404 to company minutiae that had no relevance to investors.

The massive amounts of red tape imposed by PCAOB have both parties expressing dismay at the increased costs of smaller companies going public, especially at a time when growth capital is so hard to come by. In an effort to cure these concerns over PCAOB policy, Senator Kerry has called for a task force to "make it easier for small businesses to comply with the Sarbanes-Oxley by reducing their regulatory burden." Kenneth W. Star, *The PCAOB: An Obstacle to President Obama's Success*, The Wall Street Journal, May 13, 2009, available at <http://online.wsj.com/article/SB124216925017912671.html>. But that problem is merely a symptom of the separation of powers problems that lie at the root of PCAOB, and for that, we already had a brilliant task force: the constitutional convention of 1787. Compliance with *that* task force's report, the Constitution, would cure the root problem rather than merely tinkering at symptomatic edges.

CONCLUSION

Our framers bequeathed to us a brilliant constitutional structure, designed to allow government to function within separation of powers constraints that would at the same time prevent it from becoming tyrannical. The structure of PCAOB so clearly violates those most basic of constitutional constraints that it should be held to be unconstitutional.

John C. Eastman
Counsel of Record

Karen J. Lugo
Center for Const'l Juris.

c/o Chapman Univ. Sch. of Law
One University Dr.
Orange, CA 92866
(714) 628-2500