SEPARATION OF POWERS, INDEPENDENT AGENCIES, AND FINANCIAL REGULATION: THE CASE OF THE SARBANES-OXLEY ACT

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INTRODUCTION

"[T]he most important separation-of-powers case regarding the President's appointment and removal powers to reach the courts in the last 20 years,"[1] as one dissenting Court of Appeals judge described it, will come before the Supreme Court in the 2009 Term. The case also involves one of the most significant pieces of financial regulation Congress had enacted this decade before the current financial crisis, the Sarbanes-Oxley Act of 2002 (the "Act," "SOX," or the "SOX Act").[2] That Act, adopted with overwhelming, bipartisan sup-

* Sudler Family Professor of Constitutional Law, New York University School of Law. This Article began with, but substantially expands upon, two *amici curiae* briefs that I filed, one before the District Court, the other before the Court of Appeals, on behalf of seven former Chairmen of the Securities and Exchange Commission ("SEC"). Those former Chairmen reflect four decades of SEC leadership under Presidents of both political parties: G. Bradford Cook (1973), Roderick M. Hills (1975-77), Harold M. Williams (1977-81), David S. Ruder (1987-89), Arthur Levitt, Jr. (1993-2001), Harvey L. Pitt (2001-03) and William Donaldson (2003-05). Collectively, they represent decades of experience in the administration of the federal securities laws, including oversight of the numerous self-regulatory and private-sector regulatory bodies that function under the SEC's authority. Five (Chairmen Hills, Williams, Ruder, Levitt, and Pitt) testified during hearings that led to the adoption of the Sarbanes-Oxley Act ("the Act") of 2002, and members of Congress cited their testimony frequently to support and explain the Act's response to the corporate abuses and financial reporting frauds that made the Act necessary. Two (Chairmen Pitt and Donaldson) were directly responsible for implementing the Act's requirements, including the creation and staffing of the Public Company Accounting Oversight Board. I am particularly grateful for the research assistance of Joshua Stillman, Laura Trice, and Genevieve Lakier. For helpful comments, I thank Rachel Barkow and Cass Sunstein.

1. Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 537 F.3d 667, 685 (D.C. Cir. 2008) (Kavanaugh, J., dissenting), *cert. granted*, 77 U.S.L.W. 3632 (2009).

2. Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified at 15 U.S.C. §§ 7201-7266).

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port[3] in the aftermath of the Enron, WorldCom, and similar corporate and accounting scandals of the 1990s, was designed to repair the perceived gap in financial-market regulation that facilitated these corporate debacles. The centerpiece of the Act is the Public Company Accounting Oversight Board (the "PCAOB" or the "Board"), a regulatory body the Act created and located within the Securities and Exchange Commission ("SEC"). The Board was designed to be the initial entity charged with the task of overseeing the professional accounting industry in ways designed to restore integrity and confidence in the United States' capital and securities markets. But the way in which this new administrative entity, the Board, is structured, particularly its relationship to the SEC and the President, has led critics to challenge the Act as a novel assault on the constitutionally enshrined system of separated powers.

To its constitutional critics, the Act violates, in several ways, the required degree of control the President must have over administrative agencies. The way in which Board members are appointed is said to violate the Appointments Clause of the Constitution.[4] The extent to which Board members are insulated from the President's effective, ongoing control—because the President cannot easily remove Board members (or those who supervise Board members, the SEC Commissioners) with whose policy decisions he disagrees—is said to violate the constitutionally required degree of control the President must have over those who implement federal law.[5] Finally, in addition to these specific constitutional defects, in the view of the critics, the overall structure of this new regulatory entity, taken as a whole, violates basic separation of powers principles.[6]

The challengers to the Act present this constitutional struggle as the latest battlefront over the "unitary executive branch" theory of the Constitution. According to that theory, the Constitution requires that all those who implement and

3. The House of Representatives approved the bill with a vote of 423-3. 148 CONG. REC. H5480 (daily ed. July 25, 2002). The Senate voted 99-0 in favor of the bill. 148 CONG. REC. 57365 (daily ed. July 25, 2002).

4. Michael A. Carvin, Noel J. Francisco & Christian G. Vergonis, *Massive, Unchecked Power by Design: The Unconstitutional Exercise of Executive Authority by the Public Company Accounting Oversight Board*, 4 N.Y.U. J.L. & BUS. 199, 229 (2007).

5. *Id.* at 216.

6. *Id.* at 215.

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execute federal law must be effectively subordinate to the President; the President must have the ability to effectively control and influence the administration of federal law.[7] Indeed, many of the lawyers leading the challenge to the constitutionality of the Sarbanes-Oxley Act have been, for many years, among the leading proponents and advocates for the unitary executive branch theory.[8] According to these proponents, even if the Constitution does not require all elements of a complete unitary executive branch understanding, surely the Sarbanes-Oxley Act is a bridge too far. To put it most colorfully, critics of the Act characterize the case as involving an independent agency inside an independent agency.[9] It follows that even if the Constitution tolerates the existence of independent agencies, the challengers argue that what they see as a Russian-doll approach to independent agencies must exceed the limits of what the Constitution permits.

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7. A recent major book provides a broad historical perspective on the unitary executive branch vision of the Constitution. *See* STEVEN G. CALABRESI & CHRISTOPHER S. YOO, THE UNITARY EXECUTIVE (2008). Important work preceding this book includes Steven G. Calabresi & Christopher S. Yoo, *The Unitary Executive During the Second Half-Century*, 26 HARV. J.L. & PUB. POL'Y 667 (2003); Steven G. Calabresi & Saikrishna B. Prakash, *The President's Power To Execute the Laws*, 104 YALE L.J. 541 (1994); Steven G. Calabresi & Kevin H. Rhodes, *The Structural Constitution: Unitary Executive, Plural Judiciary*, 105 HARV. L. REV. 1153 (1992); Stephen L. Carter, *Constitutional Improprieties: Reflections on* Mistretta, Morrison, *and Administrative Government*, 57 U. CHI. L. REV. 357 (1990); Stephen L. Carter, *The Independent Counsel Mess*, 102 HARV. L. REV. 105 (1988); Gary Lawson, *The Rise and Rise of the Administrative State*, 107 HARV. L. REV. 1231 (1994); Lee S. Liberman, Morrison v. Olson*: A Formalistic Perspective on Why the Court Was Wrong*, 38 AM. U. L. REV. 313 (1989); Geoffrey P. Miller, *Independent Agencies*, 1986 SUP. CT. REV. 41. *See* Lawrence Lessig & Cass R. Sunstein, *The President and the Administration*, 94 COLUM. L. REV. 1, 47-55, 118-19 (1994), for the principal work rejecting the unitary executive branch theory.

8. Among the lawyers representing the plaintiffs are Kenneth W. Starr, Viet D. Dinh, Michael A. Carvin, Noel J. Francisco & Christian G. Vergonis. In addition, the Washington Legal Foundation and the Mountain States Legal Foundation filed briefs amicus curiae in the lower courts supporting the constitutional challenge. *See* Brief of Appellants, Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 537 F.3d 667 (D.C. Cir. 2008) (No. 07-5127); Brief of Amicus Curiae Wash. Legal Found. in Support of Plaintiffs-Appellants Free Enterprise Fund, et al. Urging Reversal, Free Enter. Fund, 537 F.3d 667 (No. 07-5127); Brief of Amicus Curiae Mountain States Legal Found., Free Enter. Fund, 537 F.3d 667 (No. 07-5127).

9. *E.g.*, Carvin, Francisco & Vergonis, *supra* note 6, at 226.

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That the Act and the structure of the Board raise less familiar questions related to the unitary executive branch theory is of no doubt. In designing the Board, Congress was seeking to achieve a variety of aims simultaneously: to ensure the independence of the Board from the regulated industry in order to avoid the problem of capture; to reduce the risk of future congressional interference with the Board; to give the Board stature, legitimacy, and competence, including the ability to attract talented members through payment of substantial compensation; to avoid interagency turf wars by putting the Board under the authority of the SEC; and to avoid having the SEC's problems with resources and staffing affect the Board by giving the Board an independent basis of funding. The effort to realize these various aims led to the creation of a structure for the Board, within the SEC, that is not common. While the United States Court of Appeals for the District of Columbia Circuit upheld the Act in a 2-1 decision, the constitutional issues provoked a long, passionate, intensely argued dissent from Judge Kavanaugh,[10] and that Court then declined to rehear the case *en banc* in another closely divided, 5-4, vote.[11] Given this sharp division, the nature of the constitutional challenges being made to the administrative structure, and the controversial nature of the Sarbanes-Oxley Act itself today as a matter of policy,[12] the Supreme Court's decision to tackle these issues is hardly surprising.

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10. Free Enter. Fund, 537 F.3d at 685-715 (Kavanaugh, J., dissenting).

11. Free Enterprise Fund v. Public Company Accounting Oversight Board, No. 07-5127 (D.C. Circ. Nov. 17, 2008) (petition for rehearing en banc denied).

12. For academic debate on the effects and desirability of the Sarbanes-Oxley Act as a policy matter, the leading critical article is Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521 (2005). Other important works on this debate include Robert P. Bartlett, III, *Going Private But Staying Public*, 76 U. CHI. L. REV. 7 (2009); Robert C. Clark, *Corporate Governance Changes in the Wake of the Sarbanes-Oxley Act: A Morality Tale for Policymakers Too*, 22 GA. ST. U. L. REV. 251 (2005); Donald C. Langevoort, *The Social Construction of Sarbanes-*Oxley, 105 MICH. L. REV. 1817(2007); Kate Litvak, *Sarbanes-Oxley and the Cross-Listing Premium*, 105 MICH. L. REV. 1857 (2007); Robert A. Prentice & David B. Spence, *Sarbanes-Oxley as Quack Corporate Governance: How Wise is the Received Wisdom?*, 95 GEO. L.J. 1843 (2007); Larry E. Ribstein, *Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002*, 28 J. CORP. L. 1 (2002).

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In this Article, I argue that despite the rhetoric and fervor of the Act's constitutional critics, their challenges amount to little more than thinly disguised attacks on the constitutionality of independent administrative agencies per se. But, at least since *Humphrey's Executor v. United States*,[13] the Supreme Court has consistently affirmed the constitutionality of independent agencies.[14] I suggest this challenge is particularly inappropriate in the context of national regulation of the U.S. capital markets, where the SEC has served since the 1930s as the congressionally designated regulatory overseer over an array of private, public, and mixed public-private regulatory structures, including entities such as the New York Stock Exchange ("NYSE"), the Chicago Board of Options Exchange ("CBOE"), and the Financial Industry Regulatory Authority ("FINRA"), the successor to the National Association of Securities Dealers ("NASD"). This unique and integrated regulatory system, working collaboratively but subject to the plenary power of the SEC, has assured investors worldwide of the integrity of U.S. capital markets, at least until the financial crisis that started in 2008. The reasons Congress designed the Board as it did reflect this overall structure of the regulatory state's longstanding approach to capital-market oversight. In light of these reasons and a clear understanding of separation-of-powers principles applied to the administrative state, the Act is constitutional.

In the wake of the massive corporate accounting and auditing scandals of the last decade, Congress determined that the auditing function in this regulatory system had become compromised through excessive dependency on the regulated entities, the accounting firms. As a result, and building on the history of regulatory institutions in this field, Congress enacted the Sarbanes-Oxley Act in 2002. As its foundation, the Act created a regulatory body, the Public Company Accounting Oversight Board, modeled on the NYSE and NASD (whose regulatory functions have since been consolidated into FINRA), to help supervise the accounting and auditing profession under the direct legal oversight and control of the SEC.

13. 295 U.S. 602 (1935).

14. *See, e.g.*, Morrison v. Olson, 487 U.S. 654 (1988); Bowsher v. Synar, 478 U.S. 714, 725 n.4 (1986).

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Congress considered a number of institutional alternatives to restore the credibility and reliability of public company financial statements. Ultimately, with bipartisan and virtually unanimous support, Congress and the President concluded that the most effective way to do so was to create the PCAOB as an entity that was not beholden to the accounting profession and that would function under the oversight of the SEC. Nothing in the Constitution denies Congress and the President the power to make that choice.

The Act does not give Congress any power to appoint Board members. The Act does not give Congress any power to remove Board members. Members of Congress do not sit on the Board, nor does Congress directly participate in making or vetoing Board policy. In no way does the Act give Congress itself the power to participate directly in the execution and implementation of federal law. Most importantly, the SEC, in law and fact, exercises pervasive control over the Board. For purposes of constitutional law, as I will show below, that is the end of the matter. Neither the separation of powers nor the Appointments Clause requires any more. Absent impermissible congressional participation *itself* in one of these constitutionally prohibited ways, Congress has ample constitutional power to create independent agencies, like the SEC, as well as subunits, such as the Board, that operate under the control and oversight of the SEC.

Properly understood, an attack on the constitutionality of the PCAOB is not a complaint about the PCAOB per se. It is an attack on the Supreme Court decisions that for generations have recognized the constitutionality of the numerous independent agencies that Congress has created. Because Congress has the power to create independent agencies, like the SEC, it has the lesser power of creating units within these agencies that function under the control and oversight of the SEC and that are staffed by employees or inferior officers whom the SEC appoints.

The Constitution permits Congress to create administrative agencies with diverse structures, including entities that function under the control and authority of these agencies. The separation of powers and the Appointments Clause limit Congress in only one particular way: Congress cannot retain any legal right to participate *itself* directly in the appointment or removal of officials who execute and implement federal law,

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nor can Congress retain any right to veto (or in any other way directly participate in) an agency's policymaking or adjudication decisions. Because Congress has granted itself none of these powers over the Board or the SEC, the Act is constitutional.

The attacks on the constitutionality of the Board, as will be shown below, invoke abstract and general propositions about the separated powers system, but ignore this essential principle, as well as the express terms of the Act and the way the Act functions in practice. The Supreme Court has rarely invalidated the structure of administrative agencies. In each and every case, the Court did so because Congress had attempted to insert *itself* directly into the appointment or removal process or to directly control the agency's decisions through a veto-like power. No Supreme Court decision exists that constitutionally invalidates an administrative agency structure when Congress has not directly inserted itself into the administrative process in one of these specific ways. For this fundamental reason, the courts have been correct thus far in rejecting the constitutional challenges to the Board's design.

In addition, Board members are, at most, "inferior officers" of the United States. As will be shown below, the Board functions under the direct and full legal oversight and control of the SEC. The SEC has plenary power over both Board rules and sanctions. Neither Board rules nor Board disciplinary sanctions have any legal effect unless and until the SEC adopts them. Beyond these specific powers, the SEC has broad authority over the Board's functions, including the power to relieve the Board of any responsibility to enforce compliance with the Act or the securities laws. The SEC appoints Board members and may censure or remove them from office. The Board's budget cannot take effect unless and until the SEC approves it. Similarly, the SEC must also approve Board-proposed subpoenas and the Board must obtain SEC permission to litigate in court. Given the array of powers the SEC has over the Board, Board members are at most "inferior officers" of the United States.

Moreover, the President has all the power over the SEC itself that is constitutionally required. The President nominates the SEC Commissioners, who are principal officers of the United States, and the President can remove them for justified cause. The Commissioners serve fixed terms of office,

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after which the President again has the power to nominate new Commissioners. This President-principal-inferior structure—with no direct congressional participation in appointment or removal of Board or SEC members—has long been constitutional.

In light of these principles and the structure of the Act, attacks on the Board's constitutionality are without constitutional foundation. First, to the extent the Board's opponents claim that the President must have more direct power over Board members,[15] the Constitution provides no basis for such a claim. The "separation of powers" most emphatically does not require that the President have personal removal power over all the inferior officers who exercise administrative authority in the United States. Congress, which creates these offices, can define the terms under which inferior officers serve and the conditions upon which they can be removed.[16] The Constitution requires only that Congress itself not participate in the removal process. To the extent the Board's opponents instead complain that the SEC itself does not have enough power to oversee the Board,[17] the structure and text of the Act belie such a claim.

Second, the Appointments Clause permits Congress to give independent agencies, such as the SEC, the power to appoint their inferior officers. No court has held otherwise. Were the law to the contrary, much of the organizational structure of the independent agencies would be unconstitutional. By statute, numerous independent agencies appoint their inferior officers. Nothing in the Constitution or Supreme Court decisions require the illogical conclusion that Congress cannot give an agency the power to appoint its own legal subordinates. The SEC is a "Department" within the meaning of U.S. Const. Art II., § 2, cl. 2 (and the SEC Commissioners are properly the "Head" of this Department).

Part I provides a history of the Sarbanes-Oxley Act and situates the creation of the PCAOB within the broader history

15. Carvin, Francisco & Vergonis, *supra* note 6, at 216.

16. *See, e.g.*, United States v. Perkins, 116 U.S. 483, 483 (1886) (first recognizing this principle); *see also* Morrison v. Olson, 487 U.S. at 689 n.27 (holding there is "no specific constitutional impediment to congressionally imposed restrictions on the President's removal powers [over inferior officers]").

17. Carvin, Francisco & Vergonis, *supra* note 6, at 221-22.

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of the regulatory structures that have governed United States financial markets since the 1930s. Part II explains why, particularly in light of this history, the independence of the Board from direct presidential control and the relationship of the Board to the SEC are consistent with longstanding separation of powers principles. Part III then addresses a question the Supreme Court has never resolved: whether independent agencies are "departments" within the meaning of Art. II of the Constitution and, hence, whether Congress can place the power to appoint inferior officers in the heads of the independent agencies. Although aspects of the Board's structure are less familiar, the structure of the Board and of the Sarbanes-Oxley Act are fully consistent with separation of powers principles.

I.
HISTORY AND STATUTORY BACKGROUND OF THE PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD

The structure that Congress and the President chose for the PCAOB is best understood in light of the overall regulatory system that made regulation of the U.S. securities markets perhaps the greatest regulatory success in modern administrative governance for many decades, at least until more recent years.[18] Since the 1930s, the SEC has sat atop that system. Under the umbrella authority of the SEC, Congress and the SEC have relied on an innovative array of institutional arrangements—some involving purely private self-regulatory bodies ("SROs"), some involving more mixed public-private governance structures, and some involving direct SEC regulation—that, working together, have collectively succeeded in ensuring investor confidence in the integrity of U.S. markets. The PCAOB is the logical outgrowth of these prior structures, as

18. *See, e.g.*, CHARLES R. MORRIS, MONEY, GREED, AND RISK: WHY FINANCIAL CRISES AND CRASHES HAPPEN 78 (1999) ("The securities regulatory system that evolved through the 1930s . . . has proven itself the most successful in the world."). Indeed, nearly all European countries today are attempting to replicate the structure and function of the SEC. *See* Robert A. Prentice, *The Inevitability of a Strong SEC*, 91 CORNELL L. REV. 775, 833 (2006) ("In recent years, every E.U. member has created its own version of the SEC, not because of requirements, but because of the obvious success of American capital markets operating under the SEC's protective umbrella.").

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Congress responded to the accounting scandals and financial crises of the last decade.

A. *The Regulatory Regime for U.S. Securities Markets*

In the wake of the 1929 market crash, Congress concluded that the absence of reliable corporate financial reports and adequate regulatory oversight of capital markets required legislative response. Over the next decade, Congress enacted the six core statutes that comprised the original federal securities laws: the Securities Act (1933), the Securities Exchange Act (1934), the Public Utility Holding Company Act (1935), the Trust Indenture Act (1939), and the Investment Company and Investment Advisors Acts (1940). Reliable accounting and auditing is at the foundation of this system. These acts require, and give the SEC the power to compel, "that financial statements filed with the Commission by public companies, investment companies, broker/dealers, public utilities, investment advisors, and others, be certified (or audited) by independent public accountants."[19]

From the outset, private SROs, such as the NYSE and the NASD (now FINRA) have played a central role in this regulatory regime. These SROs have broad reach; for example, by statutory mandate all broker-dealers must be registered with the NASD. Pursuant to the Securities Exchange Act, as amended in 1975, all rulemaking and disciplinary actions of these SROs take place under the umbrella of the SEC.[20] By statute, these SROs "exercise authority subject to SEC oversight" and "have no authority to regulate independently of the SEC's control."[21] These SROs must file notice of any proposed rule with the SEC; after publishing the rule for public comment, the SEC must then approve or reject it, subject to judi-

19. Commission Statement of Policy on the Establishment and Improvement of Standards Related to Auditor Independence, Release No. 33-7507, 66 S.E.C. Docket 1110 (Feb. 18, 1998), *available at* http://www.sec.gov/rules/policy/33-7507.htm.

20. *See* Gordon v. NYSE, 422 U.S. 659, 667 (1975).

21. S. Rep. No. 94-75, at 23 (1975), *reprinted in* 1975 U.S.C.C.A.N. 179, 202. These 1975 Amendments to the Exchange Act of 1934 were designed to ensure the SEC had general power "to review and to amend *all* self-regulatory organization rules." Business Roundtable v. S.E.C., 905 F.2d 406, 409 (D.C. Cir. 1990) (emphasis added).

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cial review.[22] The SEC may also, on its own initiative, abrogate, add to, or delete any SRO rule.[23] Precisely because the SEC must approve the rules of these SROs before they become effective, SRO rules are federal law that preempt conflicting state law.[24]

Similarly, federal law requires SROs to discipline those over whom they exercise regulatory powers for violations of SRO rules, SEC rules, or the securities laws. As with rulemaking, SRO disciplinary actions take place under the umbrella of "plenary" or *de novo* SEC review.[25] Once an SRO imposes a final disciplinary sanction, it must file notice with the SEC, which on its own motion or application may or must review the sanction. The SEC must make an independent determination of whether a violation occurred and may remit or cancel any sanction that is "excessive or oppressive."[26] Again, judicial review of the SEC's decision is available. Thus, as the D.C. Circuit recently noted, "[t]he authority [NASD] exercises ultimately belongs to the SEC . . . ."[27] So complete is the SEC's "scrutiny and approval" of SROs that the Supreme Court has held SRO rules exempt from the antitrust laws.[28] Other SROs under the umbrella of the SEC include the Municipal Securities Regulatory Board ("MSRB"), which the Securities Acts Amendments of 1975 directed the SEC to establish. As it later did with the PCAOB, Congress authorized the MSRB to write rules, conduct inspections, and fund its operations through a fee it imposed on members.[29]

The Sarbanes-Oxley Act drew directly on these prior congressional structures in creating the PCAOB and defining the SEC's legal authority and power over the Board.

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22. 15 U.S.C. § 78s(b)(1) (2006); *see also* Business Roundtable, 905 F.2d at 408 (discussing this structure).

23. 15 U.S.C. § 78s(c) (2006).

24. Credit Suisse First Boston Corp. v. Grunwald, 400 F.3d 1119, 1121 (9th Cir. 2005).

25. *See* Nat'l Assoc. of Sec. Dealers, Inc. v. S.E.C., 431 F.3d 803, 804 (D.C. Cir. 2005); Schultz v. S.E.C., 614 F.2d 561, 568 (7th Cir. 1980).

26. 15 U.S.C. § 78s(e)(1)-(2) (2006).

27. Nat. Assoc. of Sec. Dealers, Inc., 431 F.3d at 806.

28. Gordon v. NYSE, 422 U.S. at 689.

29. 15 U.S.C. § 78o-4(b)(1)-(2) (2006).

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B. *Defects in Auditing Regulation*

The regulatory structures and relationships in the accounting and auditing arena drew on a somewhat different mix of institutions, given the absence of pre-existing entities in this arena with the status of the NYSE. The initial securities laws authorized the SEC to dictate how financial statements filed with it should be prepared and audited. But the SEC quickly determined to defer, instead, to authoritative private sector bodies in the first instance. By the time of the corporate scandals of the last decade, however, the regulatory oversight system of the accounting profession was viewed as an ineffective, confusing, and inefficient mix of state, SEC, and private-sector standard setters. Experts testified that the system had become a "positively Byzantine structure of accounting disciplinary bodies which generally lack adequate and assured financial support, clear and undivided responsibility for discipline, and an effective system of SEC oversight."[30] Other witnesses described it as "a veritable alphabet soup of organizations provid[ing] governance" and "a bewildering array of monitoring groups."[31]

For accounting standards, the SEC initially deferred to a private board created by the American Institute of Certified Public Accountants ("the Institute"), the main group representing a majority of the accounting profession. In 1973, the SEC supported the establishment of the Financial Accounting Services Board ("FASB"), a private-sector, standard-setting body, and announced that the SEC would treat FASB accounting "principles, standards, and practices" as having "substantial authoritative support," while those contrary to FASB would be

30. *Accounting Reform and Investor Prot.: Hearings Before the S.Comm. on Banking, Hous., and Urban Affairs*, 107th Cong. (2002) (statement of Joel Seligman, Dean & Ethan A.H. Shepley Univ. Professor, Wash. Univ. Sch. of Law in St. Louis), cited in LEGISLATIVE HISTORY OF THE SARBANES-OXLEY ACT OF 2002, Vol. II, 532 (Gov. Printing Office 2003) [hereinafter LEGISLATIVE HISTORY].

31. *Id.* at 723 (statement of Shaun O'Malley, Chairman, 2000 Public Oversight Bd. Panel on Audit Effectiveness; Former Chairman, Price Waterhouse LLP); *id.* at 376 (statement of John Biggs, Chairman, President, and CEO, TIAA-CREF).

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treated as lacking such support.[32] Nonetheless, FASB's funding mechanism was insecure and, in the wake of the corporate scandals of the last decade, came to be viewed as compromising FASB's integrity. FASB received two-thirds of its funding from subscriptions and sales of FASB publications and one third from voluntary industry contributions. As a leading expert testified to Congress during the Sarbanes-Oxley hearings, this funding mechanism caused FASB to be "less than optimally independent or objective" because it constantly placed FASB "in the role of a hat-in-hand supplicant soliciting the industry for charity."[33]

For auditing standards, the SEC deferred for many years to the Auditing Standards Board ("ASB"), a private-sector, standard-setting body that the Institute created, funded, and whose members the Institute selected. Overseen by the SEC, the ASB was the primary actor responsible for setting and interpreting the General Accepted Auditing Standards ("GAAS"). But ASB members were predominantly practicing accountants, many of them partners in the major accounting firms. "The self-interest endemic to the ASB's structure drew particularly harsh criticism during the Enron congressional hearings."[34] As a former Chief Accountant at the SEC testified, for example, the standards tended "to be written to protect the accounting firms in case they get in trouble on an audit . . . it's not drafted with the public interest in mind."[35]

Finally, while governance of the accounting profession had been a focus of the securities laws since the 1930s, the setting of auditing standards for the accounting profession did not become a major public concern until the 1970s. Massive financial scandals at companies like Penn Central Railway prompted congressional hearings and demands for more ef-

32. Statement of Policy on Establishment and Improvement of Accounting Principles and Standards, Accounting Series Release No. AS-150 (Dec. 20, 1973), 39 Fed. Reg. 1260 (Jan. 20, 1974).

33. *The Financial Accounting Standards Board Act: Hearing Before the H. Subcomm. on Commerce, Trade and Consumer Protection of the H. Energy & Commerce Comm.*, 107th Cong. 52 (2002) (prepared statement of John C. Coffee, Jr., Adolf A. Berle Professor of Law, Columbia Univ. Law Sch.).

34. Donna M. Nagy, *Playing Peekaboo with Constitutional Law: The PCAOB and its Public/Private Status*, 80 NOTRE DAME L. REV. 975, 990 (2005).

35. LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 217 (statement of Lynn Turner, former Chief Accountant, Sec. & Exch. Comm'n).

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fective oversight of auditing, which Congress concluded at that time should remain a system of self-regulation. In response, the private sector, in consultation with the SEC, created the Public Oversight Board ("POB"), with peer review of one accounting firm by another as its foundation. But the POB lacked sanctioning authority and was funded by the Institute, which made the POB dependent on voluntary contributions from the firms it was overseeing. By 1999, in its Annual Reports to Congress, the SEC reported that it no longer considered the POB system effective. Indeed, the next year the Institute refused to increase the POB's funding in the wake of the POB's announced decision to examine the major accounting firms' compliance with the relevant standards for auditor independence.

When Congress revisited this system in the Sarbanes-Oxley hearings in 2002, numerous witnesses, including former and current SEC Chairmen, testified that the system of peer review itself was fundamentally flawed and that the design of the POB had numerous structural flaws. Experts characterized peer review as "too incestuous,"[36] because it involved "competitors reviewing competitors"[37] and had "not produced a credible result."[38] Indeed, one former SEC Chairman testified that "to my knowledge, there has never been a negative review of a major firm."[39] Thus matters stood on the eve of the Enron collapse.

C. *The Sarbanes-Oxley Act of 2002: The Legislative Process*

During 2002, as the crisis in U.S. capital markets mounted, the process that led to SOX began with Representative Oxley's introduction of a bill in the House of Representatives.[40] That bill envisioned a Public Regulatory Organization

36. *Id.* at 24 (statement of Harold M. Williams, Former Chairman, Sec. & Exch. Comm'n).

37. LEGISLATIVE HISTORY, *supra* note 32, Vol. II, at 533 (statement of Joel Seligman, Dean, and Ethan A. H. Shepley Univ. Professor, Washington Univ. Sch. of Law).

38. LEGISLATIVE HISTORY, *supra* note 32, Vol. III, at 1116 (prepared statement of Harvey L. Pitt, Chairman, Sec. & Exch. Comm'n).

39. LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 76 (prepared statement of Harold M. Williams, Former Chairman, Sec. & Exch. Comm'n).

40. Oxley's bill was entitled "The Corporate and Auditing Accountability, Responsibility and Transparency Act," H.R. 3763, 107th Cong. (2002). Oxley

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("PRO") very different from what eventually emerged from Congress. Representative Oxley's bill called for a new regulatory agency but it provided almost no conception of what form that agency should take. Indeed, the bill did not legislate the specific form of the new entity at all. Instead, the Oxley bill required the SEC to create the new regulatory agency through a process of agency rulemaking.[41] Although the bill specified some of the PRO's features (for example, that the PRO be composed of five members, only two of whom could be licensed accountants),[42] Oxley's bill left final control of most of the details of the Board's structure to the discretion of the SEC. His bill also imposed no restrictions on the SEC's appointment or removal power.[43] Oxley's bill thus envisaged the details of the new regulatory structure to be far more a creation of the SEC than of Congress.[44]

Although the House ultimately approved Oxley's bill by a vote of 334 to 90, opponents harshly criticized it for delegating responsibility to the SEC for creation of the new regulatory organization. By making the PRO a creature of agency rulemaking rather than legislation, Oxley's bill, some critics argued, would undermine the institutional credibility of the new regulatory organization and allow the scope of the regulator's authority to be weakened by an SEC that some suggested might be unduly captured by corporate interests.[45] Others

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introduced it to the House on Feb. 14, 2002. It was subsequently referred to the Committee on Financial Services, which by a vote of 49 to 12 recommended it to the full House, which voted in favor of it (334-90) on April 25, 2002. *Bill Tracking Report*, H.R. 3763 (Cong. Info. Service 2004).

41. H.R. 3763 §2(b).

42. *Id.* §2(b)(1)(a).

43. *Id.*

44. Rep. Oxley repeatedly emphasized the "flexibility" his bill gave the SEC "to deal with problems without legislating every time" and argued that Congress had created the SEC "to deal precisely with situations like this" and that there was no need to "t[ie] the hands" of the SEC by creating legislatively a new regulatory body. 148 Cong. Rec. H1545 (daily ed. Apr. 24, 2002). Nineteen witnesses testified before the House Committee on Financial Services.

45. Rep. LaFalce, for example, warned that Oxley's bill was a "woefully inadequate" response to the Enron crisis which simply "pretend[ed] to bring about reform" by "punt[ing] overhaul to just where the industry would like it—the Securities and Exchange Commission." 148 Cong. Rec. H1544 (daily ed. Apr. 24, 2002). The minority report in the Committee Report to accompany Oxley's bill similarly warned that by "delegating decisions on [the new

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questioned whether the SEC had sufficient statutory authority to create the kind of regulatory authority that Oxley's bill required.[46] Some, such as Representative Kucinich, wanted Congress to create a new independent agency.[47] Others, such as Representative LaFalce, wanted to vest appointment power jointly in the SEC and the Comptroller General, rather than in the SEC alone, in order to give the new entity *more* independence from the SEC.[48] That proposal was dropped once constitutional problems with that appointment structure were raised.[49]

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agency's] duties and powers to the SEC" the bill "provide[d] an opportunity for the authority of the new regulator to be weakened." H. R. Rep. No. 107-414, Minority Views of John J. LaFalce, Paul E. Kanjorski, Bernard Sanders, Luis V. Gutierrez, and Janice D. Schakowsky.

46. Three law professors sent a letter to Senator Sarbanes expressing "serious doubts as to the SEC's powers" to create a new oversight board by agency rule-making procedures and warning of the legal challenges that could result from any attempt to require the SEC to do so. Letter from John C. Coffee, Jr., Bevis Longstreth, and Joel Seligman to Senator Paul S. Sarbanes (July 1, 2002), *in* LEGISLATIVE HISTORY, *supra* note 32, Vol. II, at 670. Although the letter was specifically a response to a recent SEC proposal to establish a regulatory body by agency rulemaking procedures, rather than a critique of Oxley's bill, the concerns raised by the letter apply equally to both; *see also,* 148 Cong. Rec. S6327 (daily ed. July 8, 2002) (statement of Sen. Sarbanes) (arguing that "others have raised questions about the adequacy of the authority the SEC has to accomplish all of this by regulation alone . . . clearly, a firmer base would be established, a stronger reference point, if the board were established by statute, and the potential of litigation that might arise with respect to some of these disciplinary and fee-imposing powers if they were created solely by the SEC by regulation [were] avoided . . . ").

47. 148 Cong. Rec. H1567 (daily ed. Apr. 24, 2002) (Amendment in the Nature of a Substitute No. 4, Offered by Mr. Kucinich). In Kucinich's alternative bill, members of the agency he envisioned would have been nominated by the President and confirmed by the Senate. Yet his bill also stated, confusingly, that this entity should be established "within" the SEC. It also vested the SEC with the power to establish and revise the standards this entity would use to conduct audits. *Id.* Kucinich's bill was defeated by the vote of 381 to 38.

48. Comprehensive Investor Protection Act, H.R. 3818, 10th Cong. (2002).

49. After David Walker, the Comptroller General of the United States, pointed to the possible constitutional problems posed by the bill's requirement that the Comptroller General play a role in Board appointment, Rep. LaFalce agreed to take this section out of his bill. *Hearings on H.R. 3763 Before the H. Comm. on Financial Services,* 107th Cong. 146 (2002) (colloquy between Comptroller General Walker and Rep. LaFalce).

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During this same period, the Senate Committee on Banking, Housing and Urban Affairs conducted hearings on accounting reform. Many who testified in this initial phase of Senate consideration supported creating an entity that would have separate staffing and funding from the SEC and that would be designed by statute to be independent of the accounting industry, instead of the vague administrative structure the House had adopted.[50] This testimony was critical, according to the eventual Senate Committee Report, in shaping the final structure of the SEC-Board relationship.[51]

When the process resumed in the Senate several months later, support for giving the SEC power to design the new entity apparently had evaporated (in the interim, the WorldCom scandal had also emerged). Senator Sarbanes, Chair of the Senate Committee on Banking, Housing, and Urban Affairs, introduced a bill that proposed creation of the new PCAOB. Title I of the Sarbanes bill, which laid out the structure of the PCAOB and its relationship to the SEC, is nearly identical to what ultimately emerged as Title I of the enacted SOX Act.[52] The Senate Committee on Banking, Housing, and Urban Af-

50. *See, e.g.*, LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 11 (testimony of Paul Volcker, former Chairman of the Federal Reserve Board) (cautioning against housing the new regulatory agency within the SEC, given his concerns that the SEC was insufficiently funded and did not have "sufficient staff to do the review process that is needed."); *id.* at 38 (testimony of Arthur Levitt, former Chairman of the SEC) (cautioning that the SEC was "pretty stretched right now in terms of resources" and calling for a "truly independent oversight body that has the power not only to set the standards by which audits are performed, but also to conduct timely investigations that cannot be deferred for any reason and to discipline accountants"); *id.* at 21 (testimony of David Ruder, former Chairman of the SEC) (arguing that "oversight of the audit system should become truly independent" and that "a new, separate audit supervisory board should be modeled on the private sector Financial Accounting Standards Board").

51. S. Rep. 107-205, at 5, 7, 20 (2002).

52. *Compare* (Sen. Sarbanes') Public Accounting Reform and Investor Protection Act of 2002, S. 2673 107th Cong. (2002) *with* 15 USC §§ 7211-19 (2008). The only apparent differences between Title I of Sarbanes' bill and Title I of the Sarbanes Oxley Act are relatively minor and relate to the initial set-up of the Board. *Compare e.g.*, S. 2673 § 101(d) *with* USC § 7211(d) (adding a sentence specifying that "[t]he Commission shall be responsible, prior to the appointment of the Board, for the planning for the establishment and administrative transition to the Board's operation."). The only substantive change between S. 2673 and Title I of the enacted bill appears to occur in the funding section. 15 USC § 7219(f) limits the fees that can be

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fairs then heard testimony from thirty-six witnesses over ten days. This testimony centered on "the systemic and structural weaknesses affecting our capital markets which were revealed by repeated failures of audit effectiveness and corporate and financial and broker-dealer responsibility in recent months and years."[53] Among those testifying were five former SEC Chairmen and the then-current SEC Chairman; Paul Volcker, Chairman of the Trustees of the International Accounting Standards Board; the Comptroller General of the United States; three former SEC Chief Accountants; members of the Public Oversight Board ("POB"); representatives of the accounting profession; and academic experts on corporate and securities regulation.

The discussion that ensued requires careful attention because, perhaps unsurprisingly, members of Congress and witnesses used the term "independent" or "independence" in a number of different ways. For this reason also, it is important not to take individual sentences out of context. Most often, "independent" meant that the new regulatory entity should be autonomous from the accounting industry, in contrast to its predecessor. At times, those who spoke used "independence" to mean that the new entity should have a source of funding and staffing that was separate from the chronically underfunded and understaffed SEC, even though the new entity would be under the SEC's full authority and control. Occasionally, some used "independence" to argue that the new entity should be insulated from partisan or personal congressional pressures. To an even lesser extent, there were a few who suggested that Congress should create a new, conventional New Deal-style "independent" agency for the task.

Nearly all of those testifying concluded that the system of accounting industry self-regulation required major revision. Most supported creation of a new, more effective entity to oversee auditing that would not be dependent on the accounting profession for financing. As one former SEC Chairman testified: "[w]e need a truly independent oversight body that has the power not only to set the standards by which audits are performed, but also to conduct timely investigations that can-

collected by PCAOB to the Board's recoverable budget expenses, while Sarbanes' bill did not.

53. S. Rep. No. 107-205, at 2 (2002).

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not be deferred for any reason and to discipline accountants."[54] Even the POB, which had been established to oversee the prior self-regulatory process, concluded by early 2002 that it could not effectively perform this role. As the POB Chairman testified, "a new regulatory structure" was "essential," but to be effective, "it must be totally independent of the accounting profession and it must be based on the foundation of congressional action . . . ."[55] The central theme in this testimony was that, in order to avoid the problem of industry capture, which had plagued the system, the new entity had to be as independent as possible of the accounting industry.

At the same time, Congress was advised, by former SEC Chairmen and others, not to create an entirely new, independent agency for this role. An entirely new independent agency would run the risk of creating jurisdictional turf wars, such as those that had infected relationships between the SEC and the Commodity Futures Trading Commission ("CFTC"). To ensure unified, effective, and efficient regulatory oversight, Congress was advised that it should create an entity that would function under SEC control and oversight.[56] This testimony suggested that Congress should build on the SEC relationship with the SROs. Experienced financial regulators, in particular, urged Congress to look for institutional models, not to New Deal-style independent agencies, but to the distinct self-regulating institutions of the financial system, such as the then-NASD, that functioned under SEC control.[57]

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54. *Id.* at 10 (quoting Arthur Levitt, Jr.).

55. LEGISLATIVE HISTORY, *supra* note 32, Vol. II, at 898 (prepared statement of Charles A. Bowsher, Chairman, Pub. Oversight Bd. and former Comptroller Gen. of the United States).

56. For example, Richard Breeden, Chairman of the SEC from 1989 to 1993, adamantly opposed establishing the new regulatory agency as an independent institution and instead supported placing the agency within the SEC. The SEC, he argued, was the only institution "with the integrity, the institutional strength, the experience, and the determination to get the job done." Breeden warned that a new, independent agency might not have "adequate teeth to get the job done" and warned of possible jurisdictional fights if the new agency was not placed under its control. LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 18 (testimony of Richard Breeden).

57. *See, e.g.*, LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 21 (testimony of David Ruder, Chairman of the SEC 1987-1989) (urging that the creation of a "new separate audit supervisory board should be modeled on the private sector Financial Accounting Standards Board—FASB—and perhaps on the self-regulatory system of the NASD"); *id.*, Vol. II, at 528 (testimony of Robert

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In the Senate committee, several proposals emerged for how this structure should be designed. For example, a proposal from Senators Gramm and Enzi would have vested appointment power over the new Board not in the SEC alone (as in the bill Senator Sarbanes had introduced) but jointly in the SEC, the Federal Reserve Board, the CFTC (each of which would be empowered to appoint two members of the Board) and the President (who was given the authority to appoint the Chairman of the Board). While acknowledging that the SEC had to have authority over the Board for constitutional purposes, they sought a structure to make the Board *more* independent of the SEC than in the Sarbanes bill.[58] Senators Gramm and Enzi argued that the right appointment structure would help ensure the Board's "prestige" and "public image," thus making it easier to attract a higher caliber of Board members, and that the Board should be more independent of the SEC than in the Sarbanes bill.[59] As Senator Sarbanes later explained on the Senate floor, his committee had moved away from the administrative structure of the Oxley bill after concluding that the Board needed a "clear statutory underpinning" to avoid legal questions about the SEC's authority to create the Board itself.[60]

Both supporters and critics in the Senate urged that the Board should be highly professional, independent of the accounting industry, and insulated from congressional pressures as a means of guarding *against* excessive regulation and undue political interference with capital markets. They defended the need to make the source of PCAOB funding separate from the

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R. Glauber, Chairman of NASD) (asserting that "the history of the NASD is to a large degree the history of successful self-regulation in the United States" and suggesting that "if properly designed, a new private-sector regulator can make a major contribution by tapping industry resources and insights not available to the Government.")

58. 148 Cong. Reg. S6334 (daily ed. July 8th, 2002).

59. *Id.* As Sen. Gramm explained:

> The substitute that I offered in committee with Senator Enzi has an independent board. I think it is better, but you can argue that the two boards are pretty similar. Ours is a little more independent of the SEC; though, in the end, to meet the constitutional test, the SEC has to have authority over it. We went a little further in terms of independence and appointing members, and I have already talked about that.

60. 148 Cong. Rec. S6331 (daily ed. July 8th, 2002).

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SEC to further ensure that the Board would attract effective and professional regulators. Indeed, many Senators, including Senator Gramm, were concerned that Congress not be pushed into adopting substantive legislative mandates; they believed that giving more flexibility to an agency, rather than enacting substantive rules into law, would produce better regulation, but that this made it all the more important that the new entity attract the highest quality professionals in order to be credible and strong.[61] At the same time, Senator Sarbanes and others repeatedly made clear that the Board would remain subject to SEC oversight and that this oversight was "important."[62]

In addition, supporters of the Sarbanes bill emphasized that the Board needed to be able to secure the personnel and funding critical to its effectiveness. The Senate Committee Report, for example, argued that by providing PCAOB with a guaranteed source of funding in the form of the annual "accounting support fees" the Act required public companies to pay to the agency, the bill helped ensure both the Board's professionalism and its independence from the regulated industry; in addition, by allowing the Board to pay its employees at salaries commensurate with those available in the private sector, the Board would be able to attract a "strong, well-trained and experienced staff, of sufficient size to carry out the Board's responsibilities."[63] This was in implied contrast to the

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61. In floor debate on the Sarbanes bill, Sen. Gramm expressed at significant length his displeasure with what he perceived to be the media push for "legislative mandates." He stated:

> Now, I don't buy the idea that legislating something instead of setting up a reasoned system to make decisions is a tougher approach; and if it is, I don't want it . . . . What I believe we should do is set up the best and strongest board we can, make it independent, give it independent funding, and put competent people on it. . . . One of the advantages of setting up an independent board, giving them a mandate to look at these areas, but not chiseling it into stone in legislation, is because they can then say, well, here is the principle and if you are General Motors, here is how it applies, but if you are XYZ Paint Company in Montana, or Wyoming, or wherever, you might only have one accounting firm operating in the town that you are domiciled in . . . . Now, I know it is not a mandate in the same sense as writing it into law, but I think the result would end up being better.

148 Cong. Rec. S6335 (daily ed. July 8th, 2002) (statement of Sen. Gramm).

62. 148 Cong. Reg. S6334.

63. S. Rep. No. 107-205, at 7 (2002).

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SEC, which during both the committee hearings and floor debate was repeatedly depicted as being chronically underfunded, understaffed and thus unable to adequately carry out its regulatory responsibilities.[64] Hence, the Board's staffing and funding base was to be separate from that of the SEC.

Indeed, the fact that the Sarbanes bill provided the Board with guaranteed funding, in the form of the annual "accounting support fees" the Act required all registered public companies to pay,[65] was promoted as an important safeguard against both the chronic underfunding that plagued the SEC *and* the corporate control that witnesses at the Senate hearings on accounting blamed for the regulatory failure of private organizations like the FASB that up until then had been responsible for setting standards for the accounting industry.[66] Independence, as articulated in the Senate floor debate on the Sarbanes proposal, thus meant autonomy from the regulated industry, unlike in the past, and separateness from the SEC for purposes of staffing and funding, given the SEC's resource constraints. This structure was promoted as a means by which Congress could ensure that the new regulatory authority had sufficient resources, and perhaps also sufficient "prestige," to

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64. *See, e.g.*, GAO Report, *SEC Operations, Increased Workload Creates Challenges*, reprinted in LEGISLATIVE HISTORY, *supra* note 32, Vol. II, at 594 (finding that "although industry officials said that they respect SEC as a regulator [the] SEC's limited staff resources have resulted in substantial delays in SEC regulatory and oversight processes . . . "); LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 511 (testimony of David Walker, Comptroller General) (pointing to the "growing mismatch between the SEC's responsibilities and their resources.")

65. S. 2673 § 109 (codified as 15 USC § 7219(g)).

66. *See, e.g.*, LEGISLATIVE HISTORY, *supra* note 32, Vol. I, at 22 (testimony of David Ruder) (arguing that "when businesses do not like the FASB's standards or its process for creating them, they sometimes withdraw financial support or fail to provide it in the first place" and that "[t]he problem with delays in promulgation of [FASB] rules comes in part because of pressure from the business community."); *id.* at 25 (testimony of Harold Williams, Chairman of the SEC 1977-1981) ("The functioning of the FASB could be significantly enhanced if its independence could be protected, to withstand the pressures of the business community, the profession, and even the Congress. A source of funding that is dependable and not beholden to the profession or the corporate community would increase the ability of the Board to address more difficult and critical issues and do so in a timely manner."); *id.* at 56 (prepared statement of Arthur Levitt, Chairman SEC 1993-2000 calling for other sources of funding for the FASB).

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regulate effectively without having to accommodate to corporate pressure and economic control.

A Conference Committee reconciled the House-Senate differences largely by adopting and strengthening the Senate version.[67] When the reconciled bill returned to the House (containing, almost without alteration, Title I of the original Sarbanes bill), members endorsed the new administrative structure as a sound means of ensuring that the Board would be less likely to be captured by the regulated interests and less prone to partisan congressional manipulation via the funding process.[68]

With overwhelming bipartisan support, the Sarbanes-Oxley Act of 2002 then passed: 423-4 in the House and 99-0 in the Senate. In signing the bill into law, President George W. Bush endorsed the legislation as some of "the most-far reaching reforms of American business practices since the time of Franklin Delano Roosevelt."[69] President Bush, not known to be reticent to issue signing statements flagging potential constitutional issues with legislation that arguably interfered with the President's Article II powers, expressed no concern that the Act interfered constitutionally with the Executive Branch in *any* of the many ways the Board's opponents asserted.[70]

In all this history, I have found no meaningful discussion or debate of the "for-cause" removal provision concerning the SEC's power over the Board. That absence suggests two points. First, Congress did not consider the removal power a particularly significant element in the overall SEC-Board relationship. A great deal of Congress' focus centered on how to structure the Board and the SEC-Board relationship, yet in all this discussion, the removal power did not come up. That is not sur-

67. H.R. Conf. Rep. No. 107-610 (2002).

68. Rep. Oxley expressed his support for the independence the reconciled bill provided to the new regulatory agency and attempted to minimize the differences between his original bill and the reconciled version by claiming that his bill had also called for an independent oversight authority. 148 Cong. Rec. H5474 (daily ed. July 25, 2002). Rep. Maloney asserted during debate that the reconciled bill adopted what she called the "Sarbanes-LaFalce proposal for the strongest possible new independent accounting oversight board." 148 Cong. Rec. H5463 (daily ed. July 25, 2002).

69. 38 Weekly Comp. Pres. Doc. 1284 (Aug. 5, 2002).

70. Statement by President George W. Bush Upon Signing H.R. 3763, 2002 U.S.C.C.A.N. 543 (July 30, 2002).

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prising, given that Congress otherwise focused on giving the SEC pervasive power and control over the Board. Second, although the Act's challengers present the removal power provision as if it were the key to Congress' design, the history of the Act belies that view. Congress did not seem particularly invested in this provision's structure. In all the various administrative structures Congress considered, and all the specific discussion of the Board itself, there is no indication that the for-cause removal provision was of any great significance. It might be that Congress simply borrowed the SRO removal restrictions already in the Exchange Acts, without any particular attention or focus on those provisions.

As confirmation, the critical Senate Committee Report ("the Report"), the most authoritative document explaining the version of the Act adopted, emphasized at the outset that "[t]he successful operation of the Board depends upon its independence and professionalism."[71] The Report went on to list the array of provisions designed to ensure these aims, which make it clear that "independence" meant autonomy from the regulated industry. Thus, the Report noted the appointment process, the qualifications for Board service, the ban on other business activities of Board members or payments from any accounting firms, and a "cooling off" period at the end of Board service that prohibited employment for any Board-registered accounting firm.[72] But in this long opening catalogue of features designed to ensure the Board's independence and professionalism, the Report makes no mention of the removal provision.[73]

D. *The Public Company Accounting Oversight Board*

A centerpiece of the Act was the creation of the PCAOB to be located, like numerous other entities in the securities-regulation regime, under the legal authority and control of the SEC. Congress concluded that the "successful operation of the Board depends upon its independence and professionalism."[74] By independence, Congress meant independence from the entities being regulated, the accounting firms. Thus, Con-

71. S. Rep. No. 107-205, at 6.
72. *Id.*
73. The Report does mention the removal provision later. *Id.* at 12, 49.
74. *Id.* at 6.

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gress paid close attention to structuring the conditions, constraints, and appointments methods for members of the Board.

Congress required that each of the five Board members "must have a demonstrated commitment to the interests of investors and the public, and an understanding of the financial disclosures required of" public companies, and the responsibilities for those disclosures under the federal securities laws.[75] Board members serve full-time, for five-year staggered terms, with a two-term limit.[76] To further assure their independence, the Act stipulates that Board members may not engage in other business activities of any nature or receive any payments from any accounting firms (except for standard retirement payments) during Board service.[77] For one year after their terms end, Board members may not practice before the Board.[78] Further, Congress specified that two members, neither more nor less, should be or have been certified public accountants ("CPA"s), and, to ensure sufficient distance from the regulated firms, that the Chair, if a CPA, should not have been a practicing CPA for at least five years prior to Board service.[79] To attract the highest quality personnel, the Act also "makes it plain" that "the Board is to provide for staff salaries that are fully competitive with those for comparable private-sector self-regulatory, accounting, technical, supervisory, or related staff or management positions."[80] The SEC appoints the five Board members after consultation with the Chairman of the Board of Governors of the Federal Reserve System and the Secretary of the Treasury.[81]

Pursuant to the Act, the Board has four principal duties: (1) to register public accounting firms; (2) to adopt rules ensuring "informative, accurate, and independent" audit reports; (3) to conduct inspections of registered public accounting firms; (4) to conduct investigations and disciplinary proceedings concerning such firm and associated persons and to im-

75. 15 U.S.C. § 7211(e)(1).
76. *Id.* § 7211 (e)(5).
77. *Id.* § 7211 (e)(3).
78. *Id.* § 7211 (g)(3).
79. *Id.* § 7211 (e)(2).
80. *Id.* § 7211 (f)(4); *see* S. Rep. No. 107-205, at 7.
81. *Id.* § 7211 (e)(1), (4).

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pose appropriate sanctions when justified.[82] As with the SROs, the Board exists under the umbrella of the SEC and is subject to even more extensive SEC oversight and control. Section 107 of the Act provides several pages of provisions governing SEC oversight of the Board, provisions that draw directly from, and even expand upon, Congress' long-established provisions for SEC oversight of other independent bodies under the SEC's authority. As the Senate Committee Report specifically states, the "rules for SEC oversight of the Board are generally the same as those that apply to SEC oversight of the National Association of Securities Dealers, under section 19 of the Securities Exchange Act."[83]

Board rules and disciplinary actions have no legal effect unless and until the SEC approves them. Before Board proposed rules take effect, they must be filed with the SEC, published by the SEC for public comment, and approved by the SEC. The SEC may directly abrogate, amend, or disapprove Board rules. Similarly, for proposed disciplinary action by the Board, an application to the SEC for review, or the institution of review by the SEC itself, automatically stays such disciplinary action, unless and until the SEC determines to dissolve the stay.[84] The SEC may "enhance, modify, cancel, reduce, or require the remission of a sanction imposed by the Board."[85] More broadly, the SEC "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."[86] The Board cannot issue subpoenas on its own but may seek SEC issuance of a subpoena; similarly, the Board cannot bring or defend litigation without SEC approval.[87] The SEC also has the power to appoint and remove Board members.

Congress also concluded that the two entities that, under the SEC, oversee the accounting profession should not have

82. *Id.* § 7211(a), (c).

83. S. REP. No. 107-205, at 12. *See* 15 U.S.C. § 7217(a) (2003); Nagy, *supra* note 36, at 1018 ("Section 107 establishes a system of SEC oversight for the PCAOB that parallels the record keeping, rulemaking, and disciplinary review procedures currently in place for the NASD and other SROs.").

84. 15 U.S.C. § 7215(e)(1) (2002).

85. *Id.* § 7217(c)(3).

86. *Id.* § 7217(d)(1).

87. *Id.* § 7215 (b)(2)(D).

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their budgets and operations held hostage to the willingness of the profession to make voluntary financial contributions.[88] Thus, the Act requires that the primary funding for *both* the Board and the private body, FASB, come from "accounting support fees" paid by public companies.[89] Both the Board and FASB are required to allocate these fees based on a congressionally mandated formula that rests on a public company's market capitalization.[90] The Board's budget must be approved by the SEC,[91] and the SEC must also approve the Board-assessed fees.[92]

In sum, Congress concluded that the prior system of profession-dependent self-regulation of auditing had contributed to the corporate financial scandals and debacles of the recent past. Rather than continue to rely on purely private self-regulation, Congress chose to create a Board independent of the accounting profession, characterized as a nonprofit, private corporation, that functions under even more extensive SEC legal oversight and control than the SROs that have long played a major role, under the SEC's oversight and control, in regulating the securities markets. As Part II now shows, nothing in the Constitution denies Congress the power to make the policy judgments reflected in the Act's design of the Board-SEC relationship.

II.
CONGRESS' CREATION OF A REGULATORY UNIT THAT FUNCTIONS UNDER THE PERVASIVE CONTROL AND OVERSIGHT OF THE SEC, SUCH AS THE PCAOB, DOES NOT VIOLATE THE SEPARATION OF POWERS

A. *Board Members Are "Inferior Officers" of the United States*

For purposes of this Article, I assume that the Board is a governmental body under the Appointments Clause, even

88. *See, e.g.*, S. REP. No. 107-205, at 13 ("The Committee's witnesses overwhelmingly agreed that both the Board and the FASB required guaranteed sources of funding, in order to protect their independence.").

89. 15 U.S.C. § 7219(c)(1) (2002).

90. *Id.* § 7219(g)(1).

91. *Id.* § 7219(b).

92. *Id.* § 7219(d)(1). Unlike the legal requirement that the SEC "approve" Board-assessed fees, the SEC "reviews" FASB-assessed fees. *Id.* § 7219(e)(1).

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though Congress expressly created the Board to be a nongovernmental, nonprofit corporation.[93] Even so, Board members are, at most, "inferior officers" under the Constitution.[94] "Inferior officers" are those "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."[95]

Board members are indeed subordinate to the SEC Commissioners, who are themselves principal officers appointed by presidential nomination and Senate confirmation. The Board has no legal power to enact rules or impose sanctions itself. The Board, in essence, proposes rules and sanctions to the SEC. For proposed rules, the Act provides that no Board proposal "shall become effective without prior approval of the Commission."[96] The Act authorizes the SEC to approve proposed rules only if the SEC finds that "the rule is consistent with the requirements of this Act and the securities laws" or that the rule "is necessary or appropriate in the public interest or for the protection of investors."[97] The courts review the rules and orders of the SEC, because only these have binding legal effect—not the rules or orders of the Board itself.[98]

For proposed Board sanctions, the SEC has the power to "enhance, modify, cancel, reduce or require the remission" of the sanction if the SEC determines the sanction is not "necessary or appropriate" or if it is "excessive, oppressive, inadequate, or otherwise not appropriate to the finding or the basis on which the sanction was imposed."[99] Upon judicial review, it is the findings of fact of the SEC—not the Board—that are conclusive if supported by substantial evidence.[100]

In addition, the SEC has the power to rescind or limit any of the Board's powers. The SEC 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

93. 15 U.S.C. § 7211(b) (2006).

94. "Employees" are "lesser functionaries subordinate to officers of the United States." Buckley v. Valeo, 424 U.S. 1, 126 n.162 (1976).

95. Edmond v. United States, 520 U.S. 651, 662-63 (1997).

96. 15 U.S.C. § 7217(b)(2) (2003).

97. *Id.* § 7217(b)(3).

98. *See* 15 U.S.C. 78y (2006).

99. § 7217(c)(3).

100. § 78y(a)(4).

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standards."[101] The SEC also has the power to "censure or impose limitations upon the activities, functions, and operations of the Board" under specific circumstances.[102] The SEC, of course, appoints Board members. In addition, the SEC must approve the budget of the Board. The SEC must approve a "reasonable annual accounting support fee" that the Board proposes "as may be necessary or appropriate to establish and maintain the Board."[103] In practice, the SEC has actively overseen the Board's budget and fees.[104] The SEC must also approve Board decisions to seek subpoenas,[105] as well as to "sue and be sued, complain and defend" in the courts.[106] In addition, the Act makes explicit that nothing in it "shall be construed to impair or limit" the authority of the SEC to "regulate the accounting profession, accounting firms, or persons associated with such firms for purposes of enforcement of the securities laws," among other matters.[107]

This array of statutory provisions in the Act governing SEC oversight of the Board must also be read in conjunction with the history and past practice of the SEC's oversight of the various SROs. With respect to proposed rules and sanctions of the Board, the Act directly borrows from the Securities Exchange Act of 1934 to give the SEC the same oversight and control that the SEC has over rules and sanctions of the various SROs that function under the SEC umbrella. The courts of appeals have characterized these powers as "plenary."[108]

The Board is designed to be independent of the accounting industry but subordinate to the SEC's legal authority. The fact that the Board is authorized by statute to impose "accounting support fees" on public companies, under a congressionally mandated formula, gives the Board no more power than has the FASB, which has similar congressional authoriza-

101. § 7217(d)(1).

102. § 7217(d)(2).

103. § 7219(d)(1) (2006).

104. *See* Order Approving PCAOB Budget and Annual Support Fee for Calendar Year 2006, Securities Act Release No. 8676, Exchange Act Release No. 53641 (Apr. 13, 2006).

105. 15 U.S.C. § 7215(b)(2)(D) (2006)

106. *Id.* § 7211(f)(1).

107. *Id.* § 7202(c).

108. *See* Nat'l Ass'n Sec. Dealers v. S.E.C., 431 F.3d at 804; Schultz v. S.E.C., 614 F.2d at 568.

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tion.[109] Yet no one would contend that members of the FASB are "inferior officers" of the United States.

The Supreme Court has issued few decisions clarifying the distinction between "employees," whose appointment Congress can assign at will, and "inferior officers," whose appointment Congress must assign in accordance with Art. II., § 2, cl. 2, of the Constitution.[110] This issue need not be fully resolved, however, in the context of recognizing that the structure of the PCAOB is constitutional. For at most, Board members are inferior officers. Based on the array of powers the SEC exercises over the Board, the Board members are certainly actors "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."[111] The Board is legally subordinate to the SEC. If Board members are "employees," even the Board's opponents do not challenge the constitutionality of the Act. But even if Board members are considered "inferior officers," the Act is constitutional, as the next Sections demonstrate.

B. *The SEC-Board Structure Does Not Violate the Separation of Powers*

The Board's opponents' primary claim is that the PCAOB violates the separation of powers.[112] As a starting point, this claim is somewhat difficult even to decipher, because the claim appears to vacillate between two different concerns. At times, the claim appears to be that the President must *himself* have the power directly to remove PCAOB members for cause.[113] At other times, the claim appears to be that the *SEC* must have more expansive powers than the Act purportedly provides to remove Board members.[114] Regardless of this confusion, Supreme Court precedent has resoundingly rejected both of these theories for many decades.

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109. *See* 15 U.S.C. § 7219(d)(1).

110. *See* Note, *Congressional Restrictions on the President's Appointment Power and the Role of Longstanding Practice in Constitutional Interpretation,* 120 Harv. L. Rev. 1914, 1916 (2007).

111. Edmond v. United States, 520 U.S. at 662-63.

112. *E.g.*, Carvin, Francisco & Vergonis, *supra* note 6, at 215.

113. *See, e.g., id.* at 216.

114. *See, e.g., id.* at 221.

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First, the only cases in which the Supreme Court has held the structure of an administrative agency unconstitutional are rare cases in which Congress has attempted to insert itself directly into the appointment or removal process or to control directly an agency's decisions through a veto-like power.[115] None of those features is present here. The Supreme Court has never held the design of an administrative agency unconstitutional when Congress has *not* inserted itself directly into the administrative process in one of these three specific ways.[116] The Act does not insert Congress directly into the appointment or removal process for Board members or in any other way insert Congress directly into the administration of the Act.

The claim that the President must have direct, "for cause" removal power over Board members is the claim that the President must have "for cause" removal power over all government officials who act as "inferior officers" of the United States. But such a principle would be radically inconsistent with longstanding political practice, as well as Supreme Court precedent. Indeed, such a principle is at odds with the basic practice and legal understanding of the administrative state. This claim goes well beyond even an attack on independent agencies alone: it is an attack on the structure of nearly all administrative agencies, both those whose heads serve at the pleasure of the President (purely executive agencies) and those whose heads the President can remove only for cause (independent agencies). For generations, the President has not had, and has not been constitutionally required to have, the direct power to remove inferior officers of the United States for cause or under any other standard.

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115. *See, e.g.*, Metro. Wash. Airports Auth. v. Citizens for Abatement of Aircraft Noise, Inc., 501 U.S. 252 (1991) (direct congressional participation in agency decision-making); Bowsher v. Synar, 478 U.S. at 714 (direct congressional involvement in removal process); INS v. Chadha, 462 U.S. 919 (1983) (direct congressional veto over agency decisions); Buckley v. Valeo, 424 U.S. at 1 (direct congressional participation in appointment process); Myers v. United States, 272 U.S. 52 (1926) (direct Senate participation in removal).

116. *See, e.g.*, Morrison v. Olson, 487 U.S. at 686 (upholding office of independent counsel because, "[u]nlike both *Bowsher* and *Myers*, this case does not involve an attempt by Congress itself to gain a role in the removal of executive officials other than its established powers of impeachment and conviction.").

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The independent agencies, for example, appoint numerous inferior officers. As Justice Scalia has noted, Congress has given the Federal Communications Commission ("FCC") the power to appoint its managing director; the SEC, the power to appoint "such officers . . . as may be necessary;" the Federal Trade Commission ("FTC"), the power to appoint its secretary; the Commodity Futures Trading Commission ("CFTC"), the power to appoint its general counsel.[117] Nearly all other independent agencies have similar powers, by statute, to select their own inferior officers. Thus, the Consumer Product Safety Commission appoints its general counsel and various executive and associate executive directors,[118] the Federal Election Commission appoints its general counsel,[119] the Federal Maritime Commission ("FMC")[120] and Federal Mine Safety and Health Review Commission[121] appoint key agency officials, the Nuclear Regulatory Commission appoints the heads of its various administrative units,[122] and so on.[123] Executive agencies, like the Environmental Protection Agency or the Internal Revenue Service, are statutorily empowered to appoint their own inferior officers as well, as are other agencies throughout the government.

None of these statutes authorizes or permits the President directly to remove any of these inferior officers for cause or under any other standard. In *Freytag v. Commissioner of Internal Revenue*,[124] for example, the Court held that special trial judges of the Tax Court were "inferior officers" of the United States.[125] Congress gave the Chief Judge of the Tax Court the power to appoint and remove these special trial judges. Neither the statute nor the Court's opinion suggested the President has the power himself to remove special trial judges for cause or any other reason—let alone that the Constitution

117. Freytag v. Comm'r, 501 U.S. 868, 918 (1991) (Scalia, J., concurring).
118. 15 U.S.C. § 2053(g)(1)(A) (2006).
119. 2 U.S.C. § 437c(f)(1) (2006).
120. 46 C.F.R. § 501.5(a) (2007).
121. 30 U.S.C. § 812(a)-(c).
122. 42 U.S.C. § 5841(a)(4) (2006).
123. *See generally* Marshall J. Breger & Gary J. Edles, *Established By Practice: The Theory and Operation of Independent Federal Agencies*, 52 ADMIN. L. REV. 1111, 1236-1282 (2000).
124. 501 U.S. at 868.
125. *Id.*

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requires that the President have such power. Indeed, no court has suggested such a presidential power is constitutionally required.

Instead, for over a century the Supreme Court has made clear that Congress has the constitutional power to set the terms under which inferior officers of the United States hold their positions. As the Court held in *United States v. Perkins*:

> We have no doubt that when Congress, by law, vests the appointment of inferior officers in the heads of departments it may limit and restrict the power of removal as it deems best for the public interest. The constitutional authority in Congress to thus vest the appointment implies authority to limit, restrict, and regulate the removal by such laws as Congress may enact in relation to the officers so appointed.[126]

In *Perkins*, Congress had provided that naval officers could be dismissed only under specified conditions. The Secretary of Navy, who had the power to appoint such officers, claimed that the congressional restriction on removal violated the "constitutional prerogative of the executive [branch]."[127] The Court firmly rejected that position. In doing so, *Perkins* reflected principles suggested years earlier in *Ex Parte Hennen*,[128] which had also made clear that Congress has the power to define the conditions under which inferior officers serve and can be removed.[129]

Here, Congress gave the power to the SEC to appoint Board members, as well as the power to remove them. That is the common and longstanding practice by which inferior officers in administrative agencies, independent as well as purely executive, are appointed and removed. The Constitution hardly denies Congress the power to create such familiar structures.

The basic structure of administrative government is that principal officers of the United States must be nominated by the President and confirmed by the Senate. Even with respect

126. United States v. Perkins, 116 U.S. at 485 (quoting Perkins v. United States, 20 Ct. Cl. 438, 444 (1885)).

127. *Id.* at 484.

128. 38 U.S. (13. Pet.) 230 (1839).

129. *See, e.g., id.* at 260 (noting that "the President has certainly no power to remove" inferior officers in the face of congressional constraints).

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to these principal officers, Congress can decide to limit the President to a good-cause removal power.[130] Congress can also choose, instead, to permit the President to remove such officers at will. With respect to inferior officers, Congress can vest the appointment power in the President, the Courts of Law, or in the Heads of Departments,[131] and Congress can fix the terms on which those inferior officers hold their positions, including by denying the President the power to remove those officers at will or for cause. Even *Myers* itself, in which the Board's opponents invest so much weight,[132] expressly recognized this principle: the authority of Congress "to vest the appointment of such inferior officers in the heads of departments carries with it authority incidentally to invest the heads of department with power to remove."[133] *Myers* held the removal scheme at issue unconstitutional only because Congress had given *itself* the right to participate in the removal of the inferior officers involved.[134]

Here, the President can remove SEC Commissioners under what the courts consider a "for cause" standard.[135] In turn, the SEC appoints, oversees, controls, and has removal power over its inferior officers, such as members of the Board. For separation of powers purposes, this is sufficient. Congress is free to decide that such a structure best protects investor confidence and most effectively ensures proper regulation of the capital markets.

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130. *See* Wiener v. United States, 357 U.S 349, 351-56 (1958); Humphrey's Ex'r v. United States, 295 U.S. at 629-32. The Board's opponents note that "the Supreme Court has never endorsed a restriction on the President's removal power [over principal officers] more intrusive than 'for cause.'" Carvin, Francisco & Vergonis, *supra* note 6, at 220. They do not, however, put this assertion in context by acknowledging that the Supreme Court has *never* been *asked* to uphold a more intrusive restriction, nor has the Court ever actually *invalidated* a restriction on presidential removal power for being more intrusive than good cause. Of course, the issue is irrelevant to this case, since Board members are, at most, inferior officers of the United States, not principal ones.

131. U.S. CONST. art. II, § 2, cl.2.

132. *See, e.g.*, Carvin, Francisco & Vergonis, *supra* note 6, at 217.

133. Myers v. United States, 272 U.S. at 161.

134. *See id.* (noting that the Constitution does not permit Congress to "draw to itself, or to either branch of it, the power to remove or the right to participate in the exercise of that power.").

135. *See* S.E.C. v. Blinder, Robinson & Co., 855 F.2d 677, 681 (9th Cir. 1988).

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Were it otherwise, the President would have the power to remove for cause every inferior officer in the United States: agency general counsels, FTC investigators, special trial judges in the Tax Court, and all others. The Constitution has never been understood to require that the President have direct removal power over all the inferior officers of the United States.

The particular history and structure of governmental regulation of the capital markets makes this the least apt arena to create a new constitutional rule that the President must have for-cause removal power over inferior officers, such as Board members. As noted above, this system has relied for decades on a unique combination of public-private institutional relationships under the umbrella and oversight of the SEC. In conjunction with the SEC, the various SROs exercise a form of governmental power. Rules of FINRA (previously, the NASD) approved by the SEC, for example, are federal law and preempt conflicting state law. Yet the President has no power to appoint or remove FINRA directors or, similarly, the head of the NYSE. In determining that more effective regulation of accounting and auditing was necessary to restore confidence in the markets in the wake of the corporate scandals of the last decade, Congress similarly could have given those powers to the preexisting private organizations, FASB or ASB. As with the NYSE and FINRA, had Congress done so, the President would not have had inherent constitutional power to remove the heads of FASB or ASB. Instead, Congress determined to replace the industry-controlled self-regulatory system of auditing with a new Board located, like the SROs, under the umbrella and oversight of the SEC. Indeed, the SEC has far *more* power over the Board than it does over the NYSE or FINRA or than it did over the Board's predecessors, such as ASB. The SEC, for example, appoints Board members. The SEC must approve the Board's budget but not that of the SROs. It would be perverse to conclude that Congress, by creating a subunit of the SEC under even greater SEC control than other parts of this integrated regulatory system, such as the SROs, was then constitutionally barred from authorizing the SEC to remove Board members only for specified reasons. Nothing in the Constitution or Supreme Court decision requires such a nonsensical result.

The Board's opponents try to avoid the force of all this history and doctrine by misrepresenting a pre-New Deal

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case.[136] That so much of the Board's opponents' argument rests on *Myers* is telling. Perhaps wishfully, but with great inaccuracy, the Board's opponents characterize *Myers* as a "seminal" decision.[137] But as is well known, *Humphrey's Executor*—truly the seminal decision of the modern administrative state—long ago limited *Myers* to the latter's specific holding and facts.[138] As the Court recently emphasized yet again, it "expressly disapprove[s] of any statements in *Myers* that 'are out of harmony' with the views expressed in *Humphrey's Executor*."[139] *Myers* involved a postmaster whom Congress had precluded the President from removing without the Senate's consent. Because the Senate directly participated in the removal process, and because a postmaster exercised nothing more than "purely executive" functions, *Myers* held this statute unconstitutional. But in limiting *Myers* to the specific context of statutes in which Congress seeks to insert itself directly into the removal process, *Humphrey's Executor* expressly concluded that *Myers* "cannot be accepted as controlling" when it comes to modern administrative agencies.[140] Referring to the FTC, the Court characterized the agency as "an administrative body created by Congress to carry into effect legislative policies embodied in the statute in accordance with the legislative standard therein prescribed . . . ."[141]

Similarly, the SEC and the Board are administrative bodies created by Congress to carry into effect legislative policies embodied in statute. As *Humphrey's Executor* makes clear, *Myers* has no application to such administrative agencies.[142] *Myers* assuredly does not stand for the proposition that the President, in defiance of congressional statute, has inherent constitutional power to remove for cause all inferior officers of the

136. Myers v. United States, 272 U.S. at 53.

137. *See* Carvin, Francisco & Vergonis, *supra* note 6, at 217.

138. *See* Humphrey's Ex'r v. United States, 295 U.S. at 602.

139. Morrison v. Olson, 487 U.S. at 687 n.24.

140. Humphrey's Ex'r, 295 U.S. at 627; *see also* Morrison, 487 U.S. at 687 n.24 ("We recognized that the only issue actually decided in *Myers* was that 'the President had power to remove a postmaster of the first class, without the advice and consent of the Senate as required by act of Congress.'").

141. *Id.*

142. *See also* FEC v. NRA Political Victory Fund, 6 F.3d 821, 826 (D.C. Cir. 1993) (holding there is no "vitality to the claim" that Congress cannot restrict the President's removal power over even principal officers of independent agencies, such as the Federal Election Commission).

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United States, including those throughout the government who exercise administrative powers in the agencies.

The final prop in the Board's opponents' argument is an attempt to turn the Court's decision upholding the Independent Counsel Act in *Morrison v. Olson*[143] on its head.[144] *Morrison* limited *Myers* even further. Some had suggested that the statute invalidated in *Myers* had two relevant flaws, not one. In addition to inserting the Senate into the removal process, *Myers* had also suggested there might be some narrow category of officials, who, unlike administrative agency officials, exercised only "core" executive branch functions and thus were constitutionally required to serve at the President's will. *Morrison* put this latter notion to rest. If any official exercises "core" executive functions, it was the independent counsel, whose function was solely to investigate and prosecute federal crimes. But even so, *Morrison* held that Congress had sufficient justification to insulate the independent counsel from the President's direct control and removal power. In so holding, *Morrison* dispensed with the scholastic effort to categorize an official's functions as "executive," or "core executive," or "quasi-legislative," or "quasi-judicial."[145]

Regardless of these labels, Congress can insulate officials from removal at the President's will, as long as Congress does not itself participate in the removal process. As *Morrison* put it, "the essence of the decision in *Myers*" was that Congress cannot participate in the removal process.[146] The Sarbanes-Oxley Act does not permit Congress to do so. Thus, the Act is clearly constitutional, under *Morrison*, *Humphrey's Executor*, and *Perkins*—indeed, even under *Myers* itself[147]—although the Act

143. 487 U.S. 654.

144. *See, e.g.*, Carvin, Francisco & Vergonis, *supra* note 6, at 223.

145. *Id.* at 689-91.

146. *Id.* at 686.

147. Even *Myers* itself, in which the Board's opponents invest so much weight, expressly recognized the following principle: the authority of Congress "to vest the appointment of such inferior officers in the heads of departments carries with it authority incidentally to invest the heads of departments with power to remove." Myers v. United States, 272 U.S. at 161. *Myers* held the removal scheme at issue unconstitutional only because Congress had given *itself* the right to participate in the removal of the inferior officers involved. *See id.* (stating that the Constitution does not permit Congress to "draw to itself, or to either branch of it, the power to remove or the right to participate in the exercise of that power").

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does not give the President the direct power to remove Board members.

At other times, the Board's opponents' "separation of powers" challenge seems to rest on the theory that the Act is unconstitutional because Congress has given the SEC too little power to remove Board members.[148] But for two reasons at least, this theory misunderstands the Act and has no legal support in the statute's text or history.

First and most importantly, as explained in detail above, the SEC has a broad array of oversight authority and control over the Board. To the extent the specific design of the SEC's removal power is relevant, those removal provisions cannot be assessed, constitutionally or practically, by abstracting them from the rest of the statutory structure. The removal power is one *means* through which a superior can exercise effective control over an inferior, but the ultimate question that is relevant is whether the principal can exercise effective control. In this case, the SEC has numerous means of control and oversight of the Board, in addition to the removal power. Taken as a whole, these powers leave no doubt that the SEC has ample legal authority and power to effectively control the Board.

Apart from "plenary" power over the most important legal actions of the Board—the issuances of rules or sanctions—the SEC has general powers far more expansive than the mere power to remove Board members. Even assuming the Constitution would require the SEC to have effective oversight powers over every other action of the Board, in addition to Board rules and sanctions, the Act gives the SEC the practical power to do just that. The SEC's powers to rescind fully the Board's authority and to approve the Board's budget, as well as to take over the regulatory process itself at any moment, for example, give the SEC effective, practical control over all of the Board's activities. The SEC can also leverage its power over Board rules and sanctions to supervise the Board's other activities. These are far greater powers, in fact, than the SEC has over the SROs that also function under its supervision. On top of all this, the SEC also has power to remove Board members.[149] Though the

148. *See* Carvin, Francisco & Vergonis, *supra* note 6, at 215-16.

149. In the face of all these other sources of power that effectively give the SEC the ability to oversee and control the Board, the precise legal standard under which the SEC is empowered to remove Board members is not critical

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Board's opponents try to present the Board as a free-wheeling, unchecked agent, the Act makes clear that the Board, like SROs and related entities in the securities regulatory regime, functions under the legal authority and control of the SEC.[150]

Second, the Board's opponents misrepresent the legal relationship between the SEC and the Board. The text of the Act, its legislative history, and the history of SEC oversight of SROs, upon which Congress based the analogous provisions in the Act, do not support the Board's opponents' positions.

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to the Act's constitutionality. Section 101(e)(6) of the Act authorizes the SEC to remove Board members for "good cause." 15 U.S.C. § 7211 (e)(6). Section 101 also states that this removal must be done "in accordance with section 107(d)(3)." The latter specifies the required *procedures* for both censure and removal: the SEC must make the required findings on the record after notice and opportunity for a hearing. 15 U.S.C. § 7217(d)(3). But § 107(d)(3), which applies to *both* censure and removal, also states that the SEC can "remove or censure" for three specific reasons, including willful violation of the Act, of the rules of the Board, or of the securities laws; or willful abuse of authority; or failure to enforce compliance with various legal provisions and rules. *Id.* The Senate Committee Report, the most authoritative Committee report from the legislative process, given the Senate's role in creation of the Board, states that the SEC can remove Board members "for cause." *See* S. Rep. No. 107-205, at 12 (2002) ("The SEC can relieve the Board of any responsibility to enforce any provision of the bill, or censure or limit operations of the Board, or remove a Board member, for cause.") (describing Section 107 of the Act). The proper reconciliation of these provisions, as well as the proper meaning of "willful" violations or abuses of authority, should await a concrete case in which they are actually at issue. To the extent these removal provisions are ambiguous, Chevron U.S.A. Inc. v. Nat'l Res. Def. Council, Inc., 467 U.S. 837 (1984), would require the courts to defer to the SEC's reasonable construction of the Act. Moreover, if the constitutionality of the Act were to turn on the specific standard for removal the Act creates, the courts would be obligated to interpret the Act to avoid such constitutional concerns, to the extent the text of the Act so permits. Edward J. DeBartolo Corp. v. Fla. Gulf Coast Bldg. & Constr. Trades Council, 485 U.S. 568, 575 (1988) ("[W]here an otherwise acceptable construction of a statute would raise serious constitutional problems, the Court will construe the statute to avoid such problems unless such construction is plainly contrary to the intent of Congress."). Particularly in facial challenges to Acts of Congress on separation of powers grounds, "it is the duty of federal courts to construe a statute in order to save it from constitutional infirmities." Morrison v. Olson, 487 U.S. at 682.

150. With respect to the SROs, the SEC has censured the NASD, for example, for its failure to regulate properly the quotation practices of NASD market makers. *See* In the Matter of Nat'l Assoc. of Sec. Dealers, Exch. Act Release No. 37,538, [1996-1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,825 (Aug. 8, 1996).

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They assert, without foundation, that the SEC must give *Chevron*-type deference to the Board's construction of the Act.[151] But nothing in the Act, past SEC practice, or general administrative law and practice, supports this odd claim. No Board rule or sanction has legal effect unless and until the SEC approves it; in essence, the Board proposes rules and sanctions, which only the SEC has the legal authority to adopt. The Act specifies that the courts review the Commission's rules and orders, not those of the Board. Thus, the agency that implements the Act, and to which the courts would give *Chevron* deference, is the SEC, not the Board.[152] Nor has the SEC given *Chevron*-style deference to the legal interpretations of the SROs or similar entities it has overseen for many years.[153]

Yet the SEC has even greater statutory power over Board sanctions, for example, than it does over those of the NASD. For the latter, the SEC has no power to enhance an NASD-proposed penalty but is limited to affirming, remanding, or, in certain circumstances, modifying it.[154] But the SEC has the additional statutory power to "enhance" any Board-proposed sanction[155] and can disapprove a Board-proposed sanction because, among other factors, it is "inadequate."[156]

Similarly, the Board's opponents assert that the SEC exercises only "appellate-like review" of the Board's final decisions, even though, as the D.C. Circuit concluded, the Act makes the

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151. Carvin, Francisco & Vergonis, *supra* note 6, at 209.

152. *See, e.g.*, Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 545 U.S. 967, 980 (2005) (noting that *Chevron* requires courts to defer to "the implementing agency's [reasonable] construction [of a statute]") (citing *Chevron*, 467 U.S. at 843-44 & n.11); Business Roundtable v. SEC, 905 F.2d 406, 408 (D.C. Cir. 1990) (deferring to the SEC under *Chevron*); Belenke v. SEC, 606 F.2d 193, 197, 199 (7th Cir. 1979) (deferring to SEC's interpretation of the securities laws, not to that of the SRO, the CBOE, whose proposed rule change the SEC approved).

153. *See, e.g.*, Sorrell v. SEC, 679 F.2d 1323, 1326 n.2 (9th Cir. 1982) (holding that SEC engages in "independent" and "*de novo*" "review of NASD decisions"); Todd & Co. v. S.E.C., 557 F.2d 1008, 1012-13 (3d Cir. 1977) (holding that SEC engages in "full review" of NASD rules and "must base its [the SEC's] decision on its own findings"); Belenke, 606 F.2d at 198 (stating that the SEC makes an independent determination that an SRO's proposed rules are consistent with the securities laws); *see also* R.H. Johnson & Co. v. S.E.C., 198 F.2d 690, 694-95 (2d Cir. 1952) (same), *cert. denied*, 344 U.S. 855 (1952).

154. *See* 15 U.S.C. § 78s(e).

155. *Id.* § 7217(c)(3).

156. *Id.*

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Board's adjudications subject to the SEC's *de novo* review upon an immediate stay either when an application for review is filed or *sua sponte* by the SEC.[157] In addition, the SEC has the power, among others, to "enhance, modify, cancel, reduce, or require the remission of" any Board sanction, as well as to rescind the Board's authority altogether or to take over regulating areas the Board regulates. It is the findings of the SEC as to facts that the Act makes conclusive if supported by substantial evidence.[158] Unlike the relationship of an administrative agency to a court, the Board functions as a subunit under the legal authority and control of its parent, the SEC.

Moreover, even if the SEC *were* limited to appellate-like review over certain aspects of Board proceedings, such as Board sanctioning decisions, the Constitution would not be violated. Like Board members, for example, special trial judges in the Tax Court are inferior officers of the United States.[159] Yet these special trial judges have even greater legal powers than do Board members. Special trial judges have the power to issue legally binding, final decisions in certain classes of cases,[160] and in addition, their superiors, the Tax Court judges, cannot overturn special trial judge findings of fact unless those findings are clearly erroneous.[161] The relationship between the Tax Court and special trial judges *is* akin to appellate-like review. Nonetheless, though the President has no direct removal power over special trial judges, and the Chief Judge of the Tax Court appoints these inferior officers, this structure poses no threat to the separation of powers.[162] By contrast to special trial judges in the Tax Court, Board mem-

157. For this assertion, see Carvin, Francisco & Vergonis, *supra* note 6, at 226. For the D.C. Circuit's contrary analysis, see Free Enter. Fund, 537 F.3d at 670. For the relevant statutory provisions, see 15 U.S.C. §§ 7217(c)(2), 7215(e)(1), and 7217(c)(2)(A). The D.C. Circuit relied on its earlier interpretation of analogous review provisions for SEC oversight over adjudications by the SROs in Nat'l Ass'n of Sec. Dealers, Inc. v. SEC, 431 F.3d at 804.

158. 15 U.S.C. § 78y(a)(4); R.H. Johnson & Co., 198 F.2d at 694 (holding that under the 1934 Securities Exchange Act, courts review orders of the Commission only, not those of the NASD, which the SEC must approve before they have legal effect).

159. *See* Freytag v. Comm'r, 501 U.S. at 882.

160. *Id.*

161. *See* Stone v. Comm'r, 865 F.2d 342, 344 (D.C. Cir. 1989).

162. *See* Freytag, 501 U.S. at 888-92.

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bers do not have even the power to enter final, legally binding decisions of the SEC in *any* class of case.

Finally, the Board's opponents apparently claim that, over and above their challenges to the Act's removal and appointments provisions, the Act somehow violates the "separation of powers" when "taken as a whole."[163] But this rhetoric adds nothing to the Board's opponents' other claims. If the structure by which Board members can be appointed and removed is constitutional, as it is, then how an agency's structure could still, nonetheless, violate the separation of powers is mysterious. The Board's opponents offer no theory, nor any coherent principle, over and above their removal and appointments challenges as to what Congress would have to do to correct any such nebulous constitutional violation as one resting on the structure of the Act "taken as a whole." The President-principal officer-inferior officer structure is routine and fully suffices for separation of powers purposes. Nothing more about an Act of Congress, "taken as a whole," is constitutionally required.

The Board's opponents rely only on *Morrison*[164] for their language about the Act "taken as a whole." But this language has meaning, if at all, only in that exceptional context, not in the context of administrative agencies in general. In *Morrison*, Congress had created an independent counsel's office, tasked with investigating and potentially prosecuting the President and the President's closest aides.[165] These independent counsels performed the most core executive functions—the investigation and prosecution of criminal cases—in the areas most sensitive to separation of powers issues, where the ability of the President and his top aides to function effectively was at stake. Even so, the Court upheld the statute in an 8-1 decision. But *Morrison*'s understandable concern for the separation of powers risks involved when Congress creates a mechanism to prosecute criminally the President and his closest aides has little bearing on Congress' routine creation of independent administrative agencies or subunits, such as the Board, that function under the oversight and control of such agencies. As long as the appointments and removal structure for an independent agency and its subunits are constitutional, there is nothing fur-

163. Carvin, Francisco & Vergonis, *supra* note 6, at 223.
164. Morrison v. Olson, 487 U.S. at 685, 693 (1988).
165. *See id.* at 660 n.2.

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ther about the enabling Act, "taken as a whole," that is relevant for separation of powers analysis.

C. *Judge Kavanaugh's Dissenting Views*

The strongest challenge to the constitutionality of the Act has come from Judge Kavanaugh's dissent in the D.C. Circuit. In his view, the Act has two constitutional flaws: (1) it violates the Appointments Clause because Board members should be considered "principal officers," rather than inferior ones; and (2) it violates the President's Article II authority "to remove executive officials, and thereby exercise the executive power and take care that the laws be faithfully executed."[166]

1. *The Principal/Inferior Officer Distinction*

Despite the arguments above, Judge Kavanaugh concluded that Board members should be considered principal officers. If so, the Act would indeed be unconstitutional, because Article II would then clearly require Presidential nomination and Senate confirmation. Surprisingly, there is less judicial precedent than one might think, in the Supreme Court or lower federal courts, on the line between principal and inferior officers. Indeed, in every case in which the Court has decided whether an officer was inferior or principal, the Court has found the officer to be of inferior status;[167] put another way, the Court has never rejected, as far as I am aware, Congress' implicit judgment (through the statutory appointment structure) that some officer is "inferior" for Article II purposes.[168]

166. Free Enter. Fund, 537 F.3d at 686 (Kavanaugh, J., dissenting).

167. The Court has found, for example, the following offices to be inferior: a district court clerk, Ex parte Hennen, 38 U.S. (13 Pet.) 225, 258 (1839); an election supervisor, Ex parte Siebold, 100 U.S. 371, 397-98 (1880); a vice consul charged temporarily with the duties of the consul, United States v. Eaton, 169 U.S. 331, 343 (1898); a "United States commissioner" in district court proceedings, Go Bart Importing Co. v. United States, 282 U.S. 344, 352-54 (1931); a Special Trial Judge in the Tax Court, Freytag v. Commissioner, 501 U.S. 868 (1991); and the Independent Counsel, Morrison v. Olson, 487 U.S. 654 (1988).

168. Buckley v. Valeo held the appointments structure of the original Federal Election Commission unconstitutional on the ground that the Commissioners were clearly "officers of the United States," 424 U.S. at 126, and the structure Congress had chosen was unconstitutional whether the Commissioners were principal or inferior officers. *See id.* at 143.

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The absence of extensive case law partly stems from the fact that Congress has historically used the "principal officer" structure for many appointments that do not necessarily involve principal officers in the constitutional sense. United States Attorneys, for example, are appointed through Presidential nomination and Senate confirmation, even though they serve under the control and authority of the Attorney General; despite this appointment structure, the Office of Legal Counsel has consistently concluded that United States Attorneys are "inferior officers," as have two lower federal courts.[169] Similarly, Congress historically has required Senate confirmation for a number of high-level Department of Justice officials, even though most of those officials, such as the Deputy Attorney General, are clearly subordinate to the Attorney General.[170] So, too, the 240,000 or so active military officers

169. The Office of Legal Counsel concluded many years ago that "inferior officer" entails amenability to supervision by the superior "in whom the power of appointment is vested." United States Attorneys—Suggested Appointment Power of the Attorney General—Constitutional Law (Article 2, § 2, cl. 2), 2 Op. Off. Legal Counsel 58, 58-59 (1978) (quoting Collins v. United States, 14 Ct. Cl. 568, 574 (1878)); *see also* United States v. Gantt, 194 F.3d 987, 999 (9th Cir. 1999) (concluding that United States Attorneys are inferior officers), *overruled on other grounds by* United States v. Grace, 526 F.3d 499, 506 (9th Cir. 2008) (en banc). *Compare* David Weiss, *Nothing Improper? Examining Constitutional Limits, Congressional Action, Partisan Motivation, and Pretextual Justification in the U.S. Attorney Removals*, 107 MICH. L. REV. 317, 342 (2008) (arguing that *Edmond* "in combination with courts of appeals opinions, the executive branch's repeated arguments for such an interpretation, and the agreement of the Congressional Research Service and commentators counsels strongly for the determination that USAs constitute inferior officers"), *with* Ross E. Wiener, *Inter-Branch Appointments After the Independent Counsel: Court Appointment of United States Attorneys*, 86 MINN. L. REV. 363, 420 (2001) (finding "compelling reasons to consider U.S. Attorneys principal officers," and arguing that "[i]n its simplicity, the *Edmond* test would ignore the complex reality of federal law enforcement, the tension between local autonomy and central control that characterizes the relationship between U.S. Attorneys and Main Justice, and the pervasive role of the U.S. Attorneys in shaping and implementing policy on behalf of the United States").

170. For example, the Office of Legal Counsel has concluded that deputy assistant secretaries, who are subject to direction by an assistant secretary, are "unquestionably" inferior officers. Department of Housing and Urban Development—Delegations of Authority—42 U.S.C. § 3533, 3535, 2 Op. Off. Legal Counsel 87, 89 (1978). Interesting questions might be presented by the role of the Solicitor General, given the relative autonomy in fact that office has garnered by tradition. Moreover, there are further puzzles the Court has not come close to working out. For example, federal district

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are appointed through the principal officer method of Presidential nomination and Senate confirmation, but they are not all principal officers in the constitutional sense.[171]

The most authoritative doctrinal treatment is the relatively short analysis in the recent 8-1 *Edmond* decision. There, the argument was that civilian appellate judges on the Coast Guard Court of Criminal Appeals, an executive branch body within the Department of Transportation that reviews decisions of courts-martial, and whose members are appointed by the Secretary of Transportation, were principal officers. The Court rejected this argument on the ground that "[w]hether one is an 'inferior officer' depends on whether he has a superior" (other than the President) who was nominated by the President and confirmed by the Senate.[172] The Court went on to say: "'[I]nferior 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."[173]

Though appellate judges are obviously subordinate to their "supreme court"—in this case, the Court of Appeals for the Armed Forces ("COFA")—we do not necessarily conceive of the work of appellate judges as "directed and supervised" by others beyond the fact that such judges are structurally subordinate to their supreme court. Thus, we might conclude that intermediate judges are inferior officers precisely because of their structural position. But the Court went on to point out that (1) the COFA had review power over decisions of the

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judges are appointed through the principal-officer structure of Presidential nomination and Senate confirmation. Is this longstanding practice constitutionally required? Is the fact of appellate review enough to make district judges "inferior officers"? As Justice Souter has noted, the Court has never addressed this issue, but from early on, the general understanding has been that district judges are principal officers. Weiss v. United States, 510 U.S. 163, 191 n.7 (1994) (Souter, J., concurring); *see also* In re Sealed Case, 838 F.2d 476, 483 (D.C. Cir. 1988) (suggesting that "lower federal judges . . . are principal officers" because they are "not subject to personal supervision"), *rev'd sub nom.* Morrison v. Olson, 487 U.S. 654 (1988).

171. *See* Weiss v. United States, 510 U.S. at 182 (Souter, J., concurring) (noting that "Congress has simply declined to adopt the less onerous appointment process for inferior officers" when it comes to active military officers).

172. 520 U.S. at 662.

173. *Id.* at 663.

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Coast Guard Court of Criminal Appeals, albeit a more limited review power than that of the Supreme Court over the Federal Courts of Appeals and (2) the Coast Guard Judge Advocate General could remove these judges at will and prescribed the rules of procedure for the court.[174]

Edmond arguably remains ambiguous in two respects. First, to the extent "direction and supervision" by a superior is required, must there be *de facto* actual direction and supervision in practice or is the superior's *de jure* supervisory authority sufficient, even if the superior exercises that authority only rarely? Surely the answer must be the latter, as even Judge Kavanaugh recognizes.[175] The analysis of structural constitutional issues such as these must turn on the facial characteristics of the legal relationships that statutes create, not on the peculiarities of how individual government actors actually exercise their power—an empirical inquiry that would be, in any event, daunting for courts to undertake. From an *ex ante* perspective, Congress creates these offices based on formal, legal relationships of authority set out by statute; it would be a destabilizing regime of law were Congress to create an "inferior officer" by statute, only to have that officer somehow transmute into a principal. Even if the Court of Appeals for the Armed Forces never reversed the Court of Criminal Appeals, the judges on the latter court would remain inferior officers. Thus, the legal authority to direct and supervise must be the critical focal point.

The more significant ambiguity concerns the meaning of "supervision and control."[176] *Edmond* contemplates that more

174. *Id.* at 664-65.

175. *See* Free Enter. Fund, 537 F.3d at 706 n.14 (Kavanaugh, J., dissenting) (noting that "the analysis of whether an officer is 'directed and supervised' depends on the express language of the statutes governing the officer in question," and not on "the vagaries of particular supervisory relationships or personalities that might result in different degrees of actual supervision and direction").

176. For academic analysis, see, for example, Tuan Samahon, *Are Bankruptcy Judges Unconstitutional? An Appointments Clause Challenge*, 60 HASTINGS L.J. 233 (2008) (arguing, controversially, that bankruptcy judges have accumulated "accoutrements of principal officer status" such that they should now be considered principal officers and their appointment by the courts of appeals unconstitutional); Akhil Reed Amar, *Intratextualism*, 112 HARV. L. REV. 747, 802-12 (1999) (arguing that inferior officers must be subordinate to a superior officer or entity).

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is required than merely being a formal subordinate in a hierarchical chain of command, though such status contributes significantly to inferior officer status. But in addition, there must be a superior (other than the President) who has the legal power to exercise some degree of actual supervision and control. The Office of Legal Counsel's most extensive analysis of this question concludes, with only slightly greater precision, that "the most important issues are the extent of the officer's discretion to make autonomous policy choices and the location of the power to supervise and remove the officer."[177]

Judge Kavanaugh asserted that the Board failed this test, and hence was composed of principal officers, because the Act limits the SEC to removing Board members only "for cause." But in fixating so intently on this single element, Judge Kavanaugh confused the forest for a single tree, as the D.C. Circuit majority essentially pointed out. The SEC has such comprehensive, commanding, and pervasive powers over the Board that the content of the SEC's removal power is of no meaningful relevance to whether the Board's work is "directed and supervised" by the SEC. Put another way, *Edmond* makes powers like removal relevant *means* in assessing the ultimate legal question of whether the nominal superior has the power to "direct and supervise." Instead, Judge Kavanaugh *equated* removal power with "direction and supervision"; in doing so, he treated unconstrained removal power as an end in itself, rather than a means to effective direction and supervision. If the *only* way a superior could exercise control over another official was through the threat of removal, then a constrained, for-cause removal power would be a substantial limit on the superior's effective control. But that is far from the case with the SEC-Board relationship, just as it has been far from the case for years with the SEC's relationships with the SROs that function under SEC oversight and control.

The D.C. Circuit majority catalogued the exceptional repertoire of powers the SEC possesses, many of which were noted above.[178] The SEC approves all Board rules and may abrogate, delete, or add to them. All Board sanctions are subject to plenary review by the Commission, and the Commission "may en-

177. The Constitutional Separation of Powers Between the President and Congress, 20 Op. Off. Legal Counsel 124, 1996 WL 876050, at *16 (1996).

178. 537 F.3d at 672.

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hance, modify, cancel, reduce, or require the remission of a sanction imposed by the Board."[179] The Commission both appoints and removes Board members. The SEC may impose limitations upon Board activities, and relieve the Board of its enforcement authority altogether. Just as with the SROs, the Board's disciplinary authority "ultimately belongs to the [Commission], and the legal views of the [Board] must yield to the Commission's view of the law."[180] As the D.C. Circuit noted, the SEC has substantially more power and oversight authority over the Board than the COFA and Coast Guard Judge Advocate General had over Coast Guard judges in *Edmond* or than the Attorney General had over the Independent Counsel in *Morrision*.[181]

Two reasons might explain Judge Kavanaugh's confusion about the proper role of SOX's removal provision in the constitutional analysis. First, in nearly all the Supreme Court cases that address "for cause" removal constraints, the statutes involve the relationship between the President and an agency—not between an agency and another entity.[182] In the context of Presidential power over agencies, the removal power is a critical factor precisely because the President lacks the power to take over the rulemaking or sanctioning function of the agency or otherwise to dictate how the agency exercises its power.[183] But the SEC has exactly the coercive legal power over the Board that the President lacks over independent agencies. Thus, the language in Court opinions involving the critical role of removal power, upon which Judge Kavanaugh relies so heavily, arises from a context in which, without an

179. 15 U.S.C. § 7217(c)(3).

180. Nat. Assoc. of Sec. Dealers, Inc., 431 F.3d at 806; *see also* Gold v. SEC, 48 F.3d 987, 990 (7th Cir. 1995) (noting that disciplinary sanctions imposed by the NYSE are subject to "full and independent review" by SEC); Shultz v. SEC, 614 F.2d at 568 (noting that, in reviewing a decision of the Chicago Board Options Exchange, "the Commission makes a de novo determination of the facts and the law").

181. 537 3.Fd at 672-73.

182. *See, e.g.*, Morrison v. Olson, 487 U.S. 654 (1988); Humphrey's Executor v. United States, 295 U.S. 602 (1935); Myers v. United States, 272 U.S. 52 (1926).

183. For an excellent recent summary and analysis of the extent to which the President does or does not have the power to supplant agency decisionmaking, see Peter L. Strauss, *Overseer, or "the Decider"? The President in Administrative Law*, 75 GEO. WASH. L. REV. 696 (2007).

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unconstrained removal power, the President lacks other effective means of dictating agency policy.[184] That is exactly opposite of the SEC-Board relationship.

Second, there is no doubt something odd about the fact that SOX grants the SEC such all-encompassing power over the Board, but then turns around and permits the SEC to remove Board members only for cause. Tension exists between the overall thrust of the Act's design for the SEC-Board relationship and the presence of this for-cause removal constraint. The legislative history reveals no clear reason Congress included the for-cause removal provision. Nonetheless, it is clear from the text of the statute that emerged that the SEC has more than enough authority to ensure its capacity to "direct and supervise" the Board.

Though the constitutional focus must be on the SEC's formal legal authority to direct and control the Board, the SEC does, as a practical matter, exercise this authority over the Board and similar entities in profound ways. Recall that Congress built the SEC-Board structure on the SEC's longstanding relationship with the SROs, though the SEC has far more power over the Board. But even with respect to the SROs, the SEC has long had the power to force management changes. For example, Chairman Arthur Levitt successfully insisted on new management for the NASD and the Nasdaq during a period of troubles with those entities.[185] This was so even though the SEC can remove the heads of NASD and Nasdaq only for cause as an enforcement sanction.[186] Nonetheless, the other

184. In the President-agency context, for-cause removal restrictions have significant practical significance. *See* Freytag v. Comm'r of Internal Revenue, 501 U.S. at 916 (Scalia, J., concurring in part) ("[I]ndependent regulatory agencies such as the Federal Trade Commission and the Securities and Exchange Commission" 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 . . . .") (internal quotation marks and alteration omitted); Mistretta v. United States, 488 U.S. at 411 (noting that good-cause provisions were "specifically crafted to prevent the President from exercising 'coercive influence' over independent agencies"). But in the context of the SEC's relationship with the Board, they do not.

185. JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET: A HISTORY OF THE SECURITIES AND EXCHANGE COMMISSION AND MODERN CORPORATE FINANCE 702 (3d ed. 2003).

186. *See* Section 19(h)(4) of the Securities Exchange Act of 1934, 15 U.S.C. 78s(h)(4). As that Section states:

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powers the SEC has over these entities gives the SEC the power, practically speaking, to dictate management. With respect to the Board, there is ample evidence, even in the formal record, of the pervasive SEC control over the Board's actions.[187]

Judge Kavanaugh caricatured the case as "*Humphrey's Executor* squared."[188] This phrase is rhetorically catchy, but factually wrong. The PCAOB simply is not an independent agency

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(4) The appropriate regulatory agency for a self-regulatory organization is authorized, by order, if in its opinion such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, to remove from office or censure any officer or director of such self-regulatory organization, if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such officer or director has willfully violated any provision of this chapter, the rules or regulations thereunder, or the rules of such self-regulatory organization, willfully abused his authority, or without reasonable justification or excuse has failed to enforce compliance—

(A) in the case of a national securities exchange, with any such provision by any member or person associated with a member;

(B) in the case of a registered securities association, with any such provision or any provision of the rules of the Municipal Securities Rulemaking Board by any member or person associated with a member; or

(C) in the case of a registered clearing agency, with any provision of the rules of the clearing agency by any participant.

187. As the public record demonstrates, there is extensive staff-to-staff interaction between the SEC and the Board. For example, the Board has amended proposed rules in response to informal recommendations from the SEC's staff in order to secure approval by the SEC. *See* Audio Webcast: PCAOB Open Meeting (Nov. 22, 2005), http://www.pcaobus.org/News_and_Events/webcasts_archive.aspx#33; *see also*, SEC, ANNUAL REPORT 2003, at 28 (2004), *available at* http://www.sec.gov/pdf/annrep03/ar03full.pdf (noting that the SEC's Office of International Affairs "worked with the [Board] to address the concerns of foreign authorities regarding the international implications of the PCAOB's system for registering accounting firms"); *id.* at 66 (SEC's Office of Chief Accountant "[p]rovided extensive oversight of the formation and start-up activities of the [Board]"); *id.* at 68 (SEC's Office of Chief Accountant "worked closely . . . to develop the PCAOB's support fee and budget"); *id.* at 69 (describing collaborative effort to develop certain Board standards); Office of the Chief Accountant, http://www.sec.gov/about/offices/oca.htm ("The Professional Practice group works closely with the [Board] to develop auditing policies and procedures that promote . . . reliable financial reporting information.") (last visited June 25, 2009).

188. Free Enter. Fund, 537 F.3d at 686 (Kavanaugh, J., dissenting).

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inside an independent agency (the SEC). Unlike the President's power over a true independent agency, the SEC has an arsenal of legal powers that gives it full authority to supervise and direct the Board, and the SEC does in fact exercise those powers. The extent of the SEC's removal power, given this arsenal, is of absolutely no practical difference. Any notion that the SEC lacks the power to supervise and direct the Board is fanciful. Thus, notwithstanding Judge Kavanaugh's assertions, Board members are inferior, not principal, officers.

Judge Kavanaugh's dissent also seems to argue that, even if Board members are inferior officers, the Act is still unconstitutional because of the for-cause removal provisions. Part II of his dissent is devoted entirely to an argument, separate from the Appointments Clause, that the removal structure independently leads the Act to violate the Constitution.[189] Of course there is no "Removal Clause" in the Constitution (if there were, it would have spared both courts and political branches some 200 years of still unsettled debate). Thus, Judge Kavanaugh's argument is made under the "Take Care Clause."[190] As I understand it, the argument is that, even though the SEC is constitutional despite the degree to which the for-cause removal constraint insulates it from Presidential control, the President's control over execution of the laws becomes too attenuated when the Board is also protected from SEC removal by a second for-cause constraint.

Let me begin by unpacking this argument and some of its consequences, before turning to why it should be rejected in the context of the specific SEC-Board relationship. First, notice that this argument would appear to require a major constitutional distinction, with significant potential effects on policymaking, between executive and independent agencies. On this view, Congress would have power to insulate inferior officers in the Department of Justice, such as an Inspector General, for example, by permitting the Attorney General to remove them only for cause. Because the Attorney General serves at the President's pleasure, this structure would not involve two "for-cause" constraints. But Congress could not create an Inspector General in the SEC whom the SEC could re-

189. *Id.* at 692.

190. U.S. Const. Art. II Sec. 3 (stating that the President "shall take care that the laws be faithfully executed . . . .").

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move only for cause. Yet is there any sound functional reason that Congress is required to make an Inspector General in the SEC subject to SEC control in a way not required for an Inspector General in the Department of Justice ("DOJ")? If there are good reasons to have independent Inspector Generals in government agencies, because doing so will hold an agency more accountable, should the Constitution be understood to permit that option for executive but not independent agencies?

Put another way, at its core, Judge Kavanaugh's argument would require a fundamental constitutional distinction regarding the permissible internal design of independent and executive agencies. But the Court has never embraced such a distinction in any other context, and there would be a variety of further ramifications in holding that Article II requires different internal structures for independent and executive agencies.[191] The Court's most vehement critic of independent agencies, Justice Scalia, has wisely recognized that "adjusting the remainder of the Constitution to compensate for *Humphrey's Executor* is a fruitless endeavor."[192] If the SEC itself is constitutional, then the SEC can be given the same power to

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191. Judge Kavanaugh quotes from a speculative passage in Professor Tribe's treatise:

> [I]n the particular situation in which an inferior 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. In such circumstances, where there is little or no political accountability at the front end for the choice of that officer, a 'for cause' limitation on removal that renders political supervision impossible appears troubling from an accountability perspective.

LAURENCE H. TRIBE, 1 AMERICAN CONSTITUTIONAL LAW § 4-8, at 684 (3d ed. 2000). Professor Tribe wrote this while discussing the special panel of judges that appointed the Independent Counsel, the structure at issue in *Morrison*. Of course, there is no form of political accountability for the Art. III judges who did the appointing there, unlike the SEC Commissioners, over whom Congress, for example, exercises oversight powers. But in addition, Professor Tribe was not addressing a situation, as in the SEC-Board context, in which the principal exercises pervasive, comprehensive powers over the inferior. The special panel of judges, of course, had exceedingly narrow powers over the Independent Counsel.

192. *Id.* at 921.

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appoint its independent inferior officers as the DOJ. Judge Kavanaugh paid too little heed to Justice Scalia's admonition.

Perhaps the response would be to conclude that Congress cannot insulate inferior officers in *any* agency, executive or independent. This would be a quite different argument than the one Judge Kavanaugh makes, of course. *Morrison* would also undermine it to a large extent, since *Morrison* expressly upheld for-cause removal constraints on officers inferior to the Attorney General. I recognize that there were other specific structural factors involved (limited tenure, limited focus of the office) and that, in any event, *Morrison* might not be as healthy a decision today as when the 8-1 decision first came down. But *Perkins* and *Hennen*, long-established precedents, would be inconsistent with this position as well. *Hennen* dates to the early nineteenth century and was endorsed in early Attorney General Opinions.[193] And modern Office of Legal Counsel opinions conclude that *Hennen* and *Perkins* "remain good law."[194]

But none of these issues are necessary to resolve regarding the Board, for the reasons canvassed earlier. In the context of the SOX Act, the issue over the removal provision is a chimera. It makes no practical difference to the SEC's power over the Board, given all the other powers of the SEC. If the Court were to hold that the Constitution required the SEC to be able to remove Board members at will, to protect the President's power, nothing at all would change in practice. The SEC's effective power over the Board would be no more than it is already.

III.
THE CONSTITUTION PERMITS CONGRESS TO CHOOSE TO VEST IN AN INDEPENDENT AGENCY, SUCH AS THE SEC, THE POWER TO APPOINT THAT AGENCY'S INFERIOR OFFICERS

A. *Independent Agencies Are "Departments" Under the Appointments Clause*

The Board's opponents argue that because the SEC is an independent administrative agency, Congress cannot choose to give the SEC the power to appoint its own inferior of-

193. The President and Accounting Offices, 1 Op. Att'y Gen. 624 (1823).

194. 20 Op. Off. Legal Counsel 124, 138 (1996), *reprinted in* 63 LAW AND CONTEMP. PROBS. 513, 557 (2000) ("Dellinger Memo").

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ficers.[195] The Supreme Court has never decided whether the independent agencies of the United States, such as the FCC, FTC, FMC, Federal Reserve Banks ("FRB"), Interstate Commerce Commission ("ICC"), National Labor Relations Board ("NLRB"), Nuclear Regulatory Commission ("NRC"), Federal Energy Regulatory Commission ("FERC"), and the SEC, are "Departments" within the meaning of the Appointments Clause.[196] But all other sources of legal authority, the long-standing practices and traditions of American government, the enactments of Congress in numerous statutes, and common sense support the principle that independent agencies are such "Departments" in the same way that the purely executive agencies are as well.

First, no federal court has ever held, as far as I am aware, that an independent agency's appointment of an inferior officer within that agency violates the Appointments Clause. The Board's opponents do not point to any such case. However, the Supreme Court and lower courts have held that the appointments power can be given to Article I courts, such as the Tax Court,[197] to the Governors of the Postal Service,[198] and to a special division of a court of appeals created for the purpose of appointing independent counsels.[199]

Second, in a comprehensive and recent analysis, the DOJ's Office of Legal Counsel ("OLC") concluded that independent agencies are Departments for purposes of the Appointments Clause.[200] That 1996 OLC memorandum itself drew directly upon an important, earlier formal opinion of the Attorney General.[201] In that opinion, the Attorney General concluded that Congress could authorize the Civil Service Commission to appoint an inferior officer. The 1996 OLC opinion found the earlier Attorney General's analysis "persuasive" and reaffirmed it. At least four Justices on the Court have expressly adopted the understanding of the Appointments

195. Carvin, Francisco & Vergonis, *supra* note 6, at 229.

196. *See* Freytag, 501 U.S. at 887 n.4 (1991) (reserving the question); *id.* at 916-17 (Scalia, J., concurring in part and concurring in the judgment).

197. *Id.* at 892.

198. Silver v. U.S. Postal Serv., 951 F.2d 1033, 1038 (9th Cir. 1991).

199. Morrison, 487 U.S. at 655 (1988).

200. "Dellinger Memo," *supra* note 196, at 543.

201. *See* Authority of Civil Service Commission to Appoint a Chief Examiner, 37 Op. Att'y Gen. 227 (1933).

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Clause laid out in the 1933 Attorney General's opinion.[202] No Justice has taken issue with this 1933 opinion, let alone rejected it.

Third, in addition to this longstanding DOJ understanding of the Appointments Clause, Congress has acted for many decades with the understanding that independent agencies are "Departments" and that the heads of these agencies can be assigned the power to appoint their inferior officers. As Justice Scalia has catalogued, many statutes give the independent agencies the power to do so. As noted above, there are many other inferior officers whom the heads of independent agencies appoint beyond the ones Justice Scalia used as examples. A well established, systemic practice of the political branches of government, like this one, to which neither Congress nor the Executive has objected, is yet an additional reason for the courts to recognize the constitutionality of such a practice. With respect to the separation of powers and issues concerning the structure of government, the Supreme Court has recognized that longstanding political practice should play a significant role in determining the meaning of the Constitution. This judicial recognition has played a major role in some of the most important cases involving the structure and organization of governmental powers in constitutional history.[203]

Fourth, the practical consequences of concluding that the Constitution permits Congress to create independent agencies, but forbids Congress from assigning to these agencies the power to appoint their inferior officers, argue against any such illogical conclusion. Not only would such a principle require dismantling longstanding structures of administrative organization, it could create a system of administration organized at

202. *See* Freytag, 501 U.S. at 919 (Scalia, O'Connor, Kennedy, & Souter, JJ., concurring in part and concurring in the judgment).

203. *See, e.g.*, McCulloch v. Maryland, 17 U.S. 316, 401 (1819) (noting that, where the structure of government is at issue, any constitutional issues "if not put at rest by the practice of the government, ought to receive a considerable impression from that practice"); *see also* Youngstown Sheet v. Sawyer, 343 U.S. 579, 610-11 (1952) (Frankfurter, J., concurring) ("[A] systematic, unbroken, executive practice, long pursued to the knowledge of the Congress and never before questioned, engaged in by Presidents who have also sworn to uphold the Constitution, making as it were such exercise of power part of the structure of our government, may be treated as a gloss on 'executive power' vested in the President by § 1 of Art. II.").

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cross-purposes with itself. Congress created the PCAOB to function under the oversight and control of the SEC, much as the SEC oversees many other entities, including the SROs. This system enables the SEC to bring its expertise to bear on a comprehensive and integrated system of regulating the securities and capital markets. If Congress could not lodge the appointments power for Board members in the SEC, but instead were constitutionally required to place it elsewhere, Congress would be obligated to locate the appointments power with, for example, the Secretary of the Treasury. But the Secretary of Treasury has no legal power to oversee the SEC, nor would he or she have any further, ongoing power to oversee the acts of Board members. It is the SEC, not the Secretary, that can remove or censure Board members, abolish functions of the Board, and that must approve Board rules or sanctions to give them legal effect. If the Secretary appointed Board members who did not share the legal understandings and policy positions of the SEC, this system would be a recipe for institutional paralysis and constant internal institutional conflict.[204]

The courts should require such a nonsensical organization of government only if the Constitution's text, history, past political practices, and judicial precedent unequivocally requires it. But far from requiring such a bizarre structure, these sources have long been understood to permit Congress to do the obvious: to conclude that government will function more efficiently and effectively if the heads of administrative agencies, including the independent agencies, are permitted to appoint their inferior officers, such as PCAOB members.

The Board's opponents' arguments to the contrary rest on two sources. First, the Board's opponents quote from a few late nineteenth century cases that, in passing, refer to "Heads of Departments" as "members of the cabinet."[205] These cases arose before Congress created the first major administrative agency, the ICC, in 1887, and hence before the basic structures of modern administrative government.[206] It is unsurpris-

204. Indeed, the Appointments Clause frowns upon "interbranch appointments," precisely because of the various distortions in government functioning that would ensue. *See* Freytag, 501 U.S. at 883; Morrison, 487 U.S. at 675-77.

205. Carvin, Francisco & Vergonis, *supra* note 6, at 239.

206. *See* STEPHEN BREYER, RICHARD STEWART, CASS SUNSTEIN & ADRIAN VERMEULE, ADMINISTRATIVE LAW AND REGULATORY POLICY 16 (6th ed. 2006).

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ing, therefore, that these late nineteenth century cases would invoke cabinet members as exemplary heads of departments.

But even this language merely recognized cabinet status as sufficient, not necessary, for "Department" status. None of these cases (or any other) invalidated a statute's appointment structure on the grounds that *only* members of the cabinet were "Heads of Departments."[207] These cases merely held that the phrase "Heads of Departments" does not include "the inferior commissioners and bureau officers, who are themselves the mere aids and subordinates of the heads of the departments."[208] But the SEC Commissioners are not subordinate to the head of any *other* department; SEC Commissioners are not "within" some other department. They are principal officers of the United States, nominated by the President and confirmed by the Senate. For several reasons, then, the passing language in these nineteenth century cases has no bearing on whether independent agencies, or even purely executive agencies not part of the Cabinet, are "Departments" under the Appointments Clause.

Second, the Board's opponents argue that *Freytag* should be read to preclude Congress from vesting the appointments power in independent agencies.[209] The Board's opponents are wrong, but this issue requires more extensive discussion. *Freytag* upheld Congress' power to give the Tax Court the right to appoint its inferior officers, much like the power the SEC has here. But the Court differed 5-4 over whether the Tax Court should be considered one of the "Courts of Law" or one of the "Departments."[210] The Court also expressly reserved the question whether the SEC and other independent agencies were Article II "Departments."[211]

207. *See* United States v. Mouat, 124 U.S. 303 (1888); United States v. Germaine, 99 U.S. 508 (1878).

208. Germaine, 99 U.S. at 511.

209. Carvin, Francisco & Vergonis, *supra* note 6, at 235-37.

210. *See* Freytag, 501 U.S. at 888-92 (stating that the Tax Court is one of the "Courts of Law"); *id.* at 901-22 (Scalia, J., concurring) (stating that the Tax Court is a "Department").

211. *See id.* at 887 n.4.

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The five-member majority concluded that the Tax Court could not be a Department because it was a Court of Law: "The Tax Court exercises judicial power to the exclusion of any other function. It is neither advocate nor rulemaker."[212] As the majority put it, the Tax Court's powers are "quintessentially judicial in nature" and "the Tax Court exercises its judicial power in much the same way as the federal district courts exercise theirs."[213] Indeed, Congress had specifically transformed the Tax Court *from* an executive agency, as were its predecessors, *to* a court.[214] Congress' intent to create the Tax Court as a court was critical to the Supreme Court's analysis.[215] For these reasons, the majority concluded the Tax Court was not a "Department," but rather a "Court of Law," under the Appointments Clause.

None of this reasoning, of course, applies to the SEC. Far from being a court exercising nothing but judicial power, the SEC is a classic administrative agency that exercises the conventional agency mix of rulemaking, investigative, and adjudicatory powers. The SEC is not a "Court of Law," nor, conversely, are the reasons that the Tax Court *is* a "Court of Law" and *not* a "Department" applicable to the SEC.

Beyond this holding, the majority made a number of additional statements, upon which the Board's opponents attempt to build a case, to explain further why the Tax Court is not a "Department." These statements emphasize concern that the appointments power not become excessively diffused to "every organ in the Executive Branch."[216] But it is crucial not to misunderstand these statements, as numerous administrative law scholars have cautioned.[217] First, the majority would not limit "Departments" in Article II to only Cabinet-level departments.

212. *Id.* at 891.
213. *Id.*
214. *Id.* at 887-88.
215. *See Id.*
216. *Id.* at 885.
217. *See, e.g.*, PETER L. STRAUSS, TODD D. RAKOFF & CYNTHIA R. FARINA, GELLHORN AND BYSE'S ADMINISTRATIVE LAW: CASES AND COMMENTS 174 (rev. 10th ed. 2003) (noting that, if misread, *Freytag* would "unsettle[ ] a broad range of existing agency appointments practices"). The courts of appeals have resisted misreading *Freytag* in this way, rejecting claims that *Freytag* makes unconstitutional agency appointment of inferior officers. *Id.* at 175-76 (citing Landry v. FDIC, 204 F.3d 1125 (D.C. Cir. 2000)); Silver v. Postal Serv., 951 F.2d 1033.

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Such a position would make little sense, given that the Constitution does not create or recognize a Cabinet and that Congress can move, and historically has moved, departments inside and outside the Cabinet. Instead, the majority recognized (as do the Board's opponents)[218] that at least entities the majority characterized as "like the Cabinet-level departments" can be given appointments power.[219] Second, at the same time, the majority provided no guidance as to what makes an administrative agency "like" the Cabinet-level departments. Third, the majority also expressly reserved the question whether the SEC, and similar independent agencies, met whatever standard might be used to judge this question.[220]

Writing for himself and Justices O'Connor, Kennedy, and Souter, Justice Scalia—a former administrative law scholar—concluded that "Departments" had to be understood expansively. In the view of these Justices, Article II uses the word "Departments" "not to connote size or function (much less Cabinet status), but separate organization."[221] Put in other terms, "Departments" includes "all independent establishments" and "all independent executive establishments."[222] As these Justices explained concisely, "the chain of appointment and supervision that [Article II] envisions" is clear. "Principal officers could be permitted by law to appoint their subordinates. That should subsist, however much the nature of federal business or of federal organizational structure may alter."[223] There is no doubt that the SEC is a "separate organization" and an "independent establishment." It has final authority to adopt rules and issue orders that have the full effect of federal law without the further approval of any other department. There is also no doubt that SEC Commissioners are principal

218. Carvin, Francisco & Vergonis, *supra* note 6, at 234.

219. *See* Freytag, 501 U.S. at 886; *see also* Plaintiffs' Memorandum of Points and Authorities in Support of Motion for Summary Judgment, 2006 WL 2688932 at *37, Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., No. 06-0217, 2007 WL 891675 (D.D.C. Mar. 21, 2007) (accepting that "Department" is not confined to the Cabinet, but includes "those agencies that resemble a cabinet department"). The EPA, the CIA, and the Federal Reserve Banks, for example, "have long appointed personnel that surely qualify as 'inferior officers' . . . ." Strauss, Rakoff, & Farina, *supra* note 219, at 175.

220. *See* Freytag, 501 U.S. at 887 n.4.

221. *Id.* at 920 (Scalia, J., concurring).

222. *Id.* at 918-19.

223. *Id.* at 920.

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officers. Under this analysis, then, the SEC is a "Department" to which Congress may give the power to appoint the SEC's inferior officers.

Though the majority reserved express judgment on whether independent agencies were "Departments," the four concurring Justices strongly suggested that these agencies must be so considered.[224] Justice Scalia, in particular, has long been concerned about the existence of independent agencies and the correctness of *Humphrey's Executor*. But as long as *Humphrey's Executor* remains the law, even Justice Scalia accepts that it follows that independent agencies must have the power, if Congress so decides, to appoint their inferior officers—and that independent agencies are therefore "Departments."[225] As he put it, "adjusting the remainder of the Constitution to compensate for *Humphrey's Executor* is a fruitless endeavor."[226] That is precisely the principle upon which the Board's opponents' Appointments Clause claim must fall: given the constitutionality of independent agencies, they necessarily are "Departments," permitted to appoint their own inferior officers.

Not only would any other conclusion unsettle decades of administrative government, by denying Congress the logical power to permit principal officers the power to appoint their inferiors, but such a conclusion would also create administrative and regulatory dysfunction and inefficiency by requiring that inferior officers be appointed by someone *other than* their superiors. For these reasons, the Board's opponents' misunderstanding of *Freytag* must be rejected. The SEC is clearly not a "Court of Law." Instead, the SEC must be understood as a "Department" under the Appointments Clause.

B. *Congress Can Choose to Define the SEC Commissioners as the "Head" of the SEC*

The Board's opponents also claim that, even if the SEC is a Department, only the SEC Chairman, not the five-member Commission, can be the "Head" of that Department under the Appointments Clause.[227] The Board's opponents' standing to raise this claim in a court of law on behalf of the Chairman of

224. *See id.* at 918-21.
225. *See id.* at 920-21.
226. *Id.* at 921.
227. Carvin, Francisco & Vergonis, *supra* note 6, at 240.

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the SEC is questionable.[228] But in any event, the lack of constitutional logic in this position is clear. Congress can choose whether to create independent agencies at all. It can create an independent agency with a single head or, as Congress has in fact done, independent agencies structured as multi-headed commissions, like the SEC. Congress need not create the position of Commission Chair at all. Thus, Congress has the power to decide that the SEC acting as a Commission is the "Head" of the SEC. Given that the legal position of "Chair" exists only to the extent Congress creates and recognizes it, and that Congress could abolish the position of Chair at any time, no other conclusion makes sense of the Constitution's structural provisions.

Similarly, Congress can decide that only the Commissioners, acting as a whole, can remove any SEC inferior officer. Congress has complete power to determine the conditions for removal of inferior officers.[229] Under the Board's opponents' view, the Constitution would require Congress to give the Chair appointment power, while permitting Congress to authorize the Commission to turn around and remove those whom the Chair appointed. The Constitution does not require such an illogical and dysfunctional system of administrative organization. That is why the courts and the Department of Justice have understood the "Head" of a Department to include multi-member bodies.[230]

Once again, the Board's opponents' real complaint is with the existence of independent agencies per se. Once Congress is recognized to have constitutional power to create independent agencies at all, headed by multi-member commissions, it follows that Congress has the discretion to treat those commissions as "Heads" of the agencies Congress has created.

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228. *See* FEC v. NRA Political Victory Fund, 6 F.3d at 825.

229. *See* United States v. Perkins, 116 U.S. at 485; *see also* Morrison v. Olson, 487 U.S. at 689 n.27 (citing *Perkins*).

230. *See* Morrison, 487 U.S. at 661 n.3 (describing the "head" of the Special Division under title VI of the Ethics in Government Act, 28 U.S.C. § 49 (1982 ed., Supp. V), as a three member panel of circuit court judges); Silver v. U.S. Postal Serv., 951 F.2d at 1035-41 (finding a nine-member group of governors to be the head of the U.S. Postal Service); 37 Op. Att'y Gen. 227, 231 (1933).

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CONCLUSION

The Sarbanes-Oxley Act of 2002 does not amount to "*Humphrey's Executor* squared." Rhetorically charged phrases like that aside, the Act does not involve an independent agency inside an independent agency. Such a structure might raise interesting constitutional issues, but that is not the structure of the SEC-Board relationship. Instead, the SEC has pervasive, comprehensive powers of control and oversight over the Board. In other contexts, such as Presidential power over an independent agency, a for-cause removal provision combines with an array of other limits on the superior's powers. In SOX, the opposite is true: the SEC has virtually every power other than at-will removal over the Board. In this context, the removal power is, constitutionally speaking, a red herring. The Board is not legally independent of the SEC in a way that tests the constitutionality of an independent agency inside an independent agency.

Practically, as well, the removal provision makes little or no difference in fact. If the SEC could remove Board members at will, rather than for cause, it is difficult to identify any basis for concluding that the SEC would have more capacity to influence or control Board decisions. Given that the SEC has so many other weapons at its disposal to control the Board, the removal power—critical in other contexts, where these other weapons are lacking—is of no practical consequence.

In creating the Board, Congress built upon a longstanding, integrated system of regulation for U.S. financial markets that relies on SEC oversight of numerous entities, public and private, including the Board, all of which function under SEC control. Congress judged that this structure is the best means to combine the advantages of SEC expertise and experience with the benefits of a specialized entity, subordinate to the SEC, to focus on the accounting industry. Superficially, the administrative structure of the Board and its relationship to the SEC looks different than more common administrative governance structures. But from a constitutional perspective, this difference is indeed only superficial. Applying the foundational principles of constitutional law that have governed the structure of the administrative state for decades, the Sarbanes-

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Oxley Act and the Board that is its centerpiece are consistent with the essential structure of the system of separation of powers.

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