

High Court Ruling Won't Upend SOX Oversight Board

By Erin Fuchs

Law360, New York (June 28, 2010) -- While the U.S. Supreme Court on Monday eased restrictions on removing members of an auditing oversight board created by the Sarbanes-Oxley Act of 2002, the ruling isn't likely to have a sweeping impact on the watchdog's ability to enforce SOX, securities attorneys say.

The high court's 5-4 decision rejected a constitutional bid to do away with the Public Company Accounting Oversight Board, sparing an entity created to oversee auditors in the wake of the Enron Corp. scandal.

"The industry has been very interested in this case because the board has overwhelming authority to micromanage all aspects of the accounting industry," said Jonathan Cohn, a partner at Sidley Austin LLP who worked on the case when he headed the appellate staff of the Civil Division at the U.S. Department of Justice.

Libertarian lobbyist group Free Enterprise Fund and Nevada accounting firm Beckstead & Watts LLP argued in their Jan. 5, 2009, petition challenging the PCAOB that it violates the separation of powers and appointments clauses in the U.S. Constitution.

In its Monday decision, a majority of the high court ruled that the PCAOB's removal restrictions — which allow board members to be removed only for good cause — violate the separation of powers doctrine.

Under the high court's decision, the U.S. Securities and Exchange Commission may remove the PCAOB's board members at will. But the decision won't affect the board's appointments, and the PCAOB will continue to function as before.

Jones Day partner Michael Carvin, who represented the Free Enterprise Fund, hailed the Supreme Court ruling as a victory even though the majority opted not to dismantle the PCAOB.

"We think this will put the agency on the proper constitutional footing," he said. His client is "very happy" about the decision despite having "asked for a different form of remedy which was to stop the board from going forward."

Despite Carvin's claims of victory, there's disagreement among experts as to what a victory in this instance would entail, especially since several attorneys, including Carvin himself, predict the ruling won't stop the PCAOB from functioning.

McGuireWoods LLP partner Christopher Cutler, a former attorney for the PCAOB, described the ruling as a win for the board because the high court's majority severed the removal restrictions of SOX from the statute while leaving the rest of it intact.

"I think there are some folks at the PCAOB that are fairly happy right now," he said. "The PCAOB lives on."

Cutler viewed the PCAOB challenge as an unsuccessful attempt to invalidate Section 404 of SOX, a controversial part of the post-Enron law that concerns procedures for internal control over financial reporting.

"Their motivations were very clear. The internal control provisions were seen as overly burdensome. Plaintiffs hopped on this and said, 'We've got to rewrite SOX,'" Cutler said.

Carvin, the lawyer for the petitioners, denied that his clients' aim was to strike down SOX, though he acknowledged that if the opinion had been "written differently," SOX would have been more vulnerable to attack.

In its Monday opinion, the majority of the high court found it could sever the removal provisions from SOX while allowing the PCAOB to continue operating because the board's very existence doesn't violate the separation of powers doctrine.

John Neiman, a partner at Bradley Arant Boult Cummings LLC, described the high court's decision as moderate and pragmatic.

"All the court did here was judicially erase a single provision from Sarbanes-Oxley," he said.

While the high court's decision might not have an appreciable impact on SOX, some lawyers predict that it could prompt challenges to removal procedures for officers or employees of other federal boards or agencies — particularly as more federal entities are created in the wake of financial and health care reform.

Mayer Brown LLP's David Gossett, who's been following the PCAOB case closely, said, "I have a feeling we're going to see a heck of a lot of litigation on these grounds over the next couple of years."

--Additional reporting by Shannon Henson, Jacqueline Bell and Jocelyn Allison