ADMINISTRATIVE LAW — APPOINTMENTS CLAUSE — D.C. CIRCUIT HOLDS THAT THE SEC CHAIRMAN IS NOT THE "HEAD" OF THE SEC. — *Free Enterprise Fund v. Public Co. Accounting Oversight Board*, 537 F.3d 667 (D.C. Cir. 2008), *cert. granted*, 77 U.S.L.W. 3431 (U.S. May 18, 2009) (No. 08-861).

The Appointments Clause of the Constitution grants the President the sole power to appoint officers of the United States with the advice and consent of the Senate.[1] But there is an exception for so-called "inferior Officers," whose appointment Congress may vest in "Heads of Departments."[2] Although there has been much litigation trying to distinguish inferior from principal officers,[3] the definition of "Heads of Departments" has received much less attention. Recently, in *Free Enterprise Fund v. Public Co. Accounting Oversight Board*,[4] the D.C. Circuit upheld the constitutionality of the Sarbanes-Oxley Act of 2002[5] against a facial challenge that it violated the Appointments Clause and separation of powers principles.[6] In rejecting the Appointments Clause challenge, the D.C. Circuit held that the Chairman of the Securities and Exchange Commission (SEC) is not the "Head" of the SEC for Appointments Clause purposes.[7] But a contextual analysis of the Chairman's powers shows otherwise, and the majority's holding undermines the purposes of the Appointments Clause by diffusing appointment power to the less politically accountable multimember Commission.

In the wake of the Enron and WorldCom accounting scandals, Congress passed the Sarbanes-Oxley Act to improve the regulation of accounting firms.[8] The Act created a Public Company Accounting Oversight Board with the power to supervise and sanction accounting companies.[9] The five SEC commissioners oversee the Board[10] and collectively appoint the Board's five members,[11] who are removable by the Commission "for good cause shown."[12] Commission members are

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1 U.S. CONST. art. II, § 2, cl. 2.

2 *Id.*

3 *See, e.g.*, Edmond v. United States, 520 U.S. 651 (1997); Morrison v. Olson, 487 U.S. 654 (1988); Buckley v. Valeo, 424 U.S. 1 (1976).

4 537 F.3d 667 (D.C. Cir. 2008), *cert. granted*, 77 U.S.L.W. 3431 (U.S. May 18, 2009) (No. 08-861).

5 Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

6 *Free Enter. Fund*, 537 F.3d at 669.

7 *See id.* at 678.

8 *See id.* at 669.

9 *See* 15 U.S.C. § 7211(c) (2006).

10 *Id.* § 7217.

11 *Id.* § 7211(e)(4).

12 *Id.* § 7211(e)(6).

themselves appointed by the President with the advice and consent of the Senate[13] and can only be removed by the President for cause.[14]

The Free Enterprise Fund, a public interest organization, and Beckstead & Watts, an accounting firm, filed a complaint in the U.S. District Court for the District of Columbia alleging that the creation of the Board violated the nondelegation doctrine, the Appointments Clause, and separation of powers principles.[15] The district court awarded summary judgment to the Board on all counts.[16]

The plaintiffs claimed that Board members were principal, not inferior, officers under the Appointments Clause, and could therefore only be appointed by the President.[17] Because it allowed the Commission to appoint the Board's members, the Act was facially unconstitutional. The district court disagreed, holding that Board members were inferior officers because they were subject to oversight and removal by the Commission.[18] The plaintiffs argued in the alternative that the SEC could not be vested with appointment power because it was not a "Department" under the Appointments Clause, and even if it was a department, the Chairman and not the multimember Commission was the "Head."[19] The district court disagreed in part, holding that the SEC was a department, but agreed with the plaintiffs that only the SEC Chairman, and not the Commission, was the head with the power to appoint inferior officers.[20] But since the Chairman had voted for each of the Board members, the district court held that the plaintiffs lacked standing to pursue this claim.[21]

The plaintiffs also argued that the Board violated separation of powers principles. Given the Board's ability to exercise "wide-ranging, core executive power," the plaintiffs maintained that the Act unconstitutionally "undermines the President's ability to perform his constitu-

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13 Securities Exchange Act of 1934 § 4(a), 15 U.S.C. § 78d(a).

14 Although the Securities Exchange Act of 1934 does not explicitly state that the President can only remove a Commissioner for good cause, courts have generally assumed this to be true. *See, e.g.*, SEC v. Blinder, Robinson & Co., 855 F.2d 677, 681 (10th Cir. 1988) ("[I]t is commonly understood that the President may remove a commissioner only for 'inefficiency, neglect of duty or malfeasance in office.'"). In *Wiener v. United States*, 357 U.S. 349 (1958), the Supreme Court held that a for-cause removal limitation could be inferred without an explicit statutory removal provision. *Id.* at 356.

15 Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., No. 06-0217, 2007 WL 891675, at *1 (D.D.C. Mar. 21, 2007).

16 *Id.* at *6. The district court easily disposed of the nondelegation claim, holding that the Board was governed by sufficiently "intelligible principles." *Id.* at *5 (citing Whitman v. Am. Trucking Ass'ns, 531 U.S. 457, 474 (2001)).

17 Complaint at 21–22, *Free Enter. Fund*, 2007 WL 891675 (No. 06-0217), 2006 WL 5503861.

18 *Free Enter. Fund*, 2007 WL 891675, at *4.

19 *Id.*

20 *See id.*

21 *Id.* at *5.

tional duties"[22] due to the Act's "double for-cause limitation on removal."[23] This limitation means the President's ability to influence the Board through removal is separated by two levels: the President can only remove Commission members for cause, and the Commission members can only remove Board members for cause. The district court rejected this claim, holding that the removal limitations were not "unduly severe in all circumstances."[24]

The D.C. Circuit affirmed.[25] Writing for the majority, Judge Rogers[26] rejected the Appointments Clause claim. Applying the test from *Edmond v. United States*,[27] in which an inferior officer was defined as someone who is "directed and supervised at some level" by a principal officer,[28] the majority held that Board members are inferior officers because they are subject to "comprehensive control by the Commission."[29] The majority also held that the SEC is a "Department" for purposes of the Appointments Clause.[30] Relying on *Freytag v. Commissioner*,[31] which equated "Departments" with "the Cabinet-level departments,"[32] the majority ruled that the SEC is sufficiently "Cabinet-like" because the SEC "exercises executive authority over a major aspect of government policy."[33] Although reaching the same result, the majority then disagreed with the district court's holding that the Chairman, and not the Commission, constitutes the head of the SEC. Instead, it held that the Commission exercises the same authority as is vested in other department heads;[34] emphasizing the limitations on the Chairman's powers, the majority concluded she is "simply one commissioner who has additional administrative functions."[35] Noting that "[a]ll three branches of government are in agreement that the head of an agency can be a multi-member body," the majority held that the Commission is the SEC head.[36]

In determining whether double for-cause removal limitations violate the separation of powers, the majority relied on *Humphrey's Ex-*

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[22] Complaint, *supra* note 17, at 20.

[23] *Free Enter. Fund*, 537 F.3d at 679.

[24] *Free Enter. Fund*, 2007 WL 891675, at *5.

[25] *Free Enter. Fund*, 537 F.3d at 669. The Fund dropped its nondelegation claim on appeal. *Id.* at 670 n.2.

[26] Judge Rogers was joined by Judge Brown.

[27] 520 U.S. 651 (1997).

[28] *Id.* at 663.

[29] *Free Enter. Fund*, 537 F.3d at 676.

[30] *Id.*

[31] 501 U.S. 868 (1991).

[32] *Id.* at 886.

[33] *Free Enter. Fund*, 537 F.3d at 677.

[34] *Id.* at 677–78.

[35] *Id.* at 678.

[36] *Id.* at 677.

ecutor v. United States,[37] in which the Supreme Court first upheld a for-cause removal limitation on the head of an independent agency.[38] The majority defined the Board as simply a "heavily controlled component of an independent agency, . . . fully congruent with the paradigm laid out in *Humphrey's Executor*."[39] The majority held that the President's "significant influence over the Commission," which oversees the Board, allows the President to exercise sufficient control over the Board despite the double for-cause removal limitation.[40]

Judge Kavanaugh dissented.[41] He argued that since Board members cannot be removed at will by the Commission, they should presumptively be considered principal officers, and therefore the Act violates the Appointments Clause.[42] On the separation of powers issue, Judge Kavanaugh called *Humphrey's Executor* one of the "outermost constitutional limits of permissible congressional restrictions on the President's removal power,"[43] arguing that a double for-cause removal limitation impedes Presidential control far more than the typical single for-cause provisions upheld in *Humphrey's Executor*.[44] The Board's "unprecedented"[45] insulation "completely stripped" the President of control and therefore violated separation of powers principles.[46]

Because Judge Kavanaugh argued that Board members are principal officers, making the Act unconstitutional, he did not address the majority's claim that the Commission is the SEC head.[47] But that holding is necessary to uphold the Act on its face, and the majority's conclusion undermines the precedent interpreting the Appointments Clause and the purpose of the clause. Determining who is the head requires a contextual analysis, and the Chairman's plenary powers indicate that she must be the head. Moreover, vesting the appointment power in the multimember Commission violates the Appointment Clause's intent by not reserving the appointment power in the SEC's most politically accountable actor, the Chairman.

In defining the "Heads" of departments, the Supreme Court has said they are "what are now called the members of the Cabinet."[48]

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[37] 295 U.S. 602 (1935).

[38] *Id.* at 629–30.

[39] *Free Enter. Fund*, 537 F.3d at 680.

[40] *Id.* at 681.

[41] *Id.* at 685 (Kavanaugh, J., dissenting).

[42] *See id.* at 707–09.

[43] *Id.* at 698.

[44] *Id.* at 701; *see also id.* at 686 ("[T]he majority opinion views this case as *Humphrey's Executor* redux. But this case is *Humphrey's Executor* squared.").

[45] *Id.* at 700.

[46] *Id.* at 701 (quoting Morrison v. Olson, 487 U.S. 654, 692 (1988)) (internal quotation marks omitted).

[47] *Id.* at 712 n.24.

[48] United States v. Mouat, 124 U.S. 303, 307 (1888).

Freytag expanded this construction beyond just Cabinet members when the Court held that "Departments" should be defined as "executive divisions *like* the Cabinet-level departments."[49] If "Departments" are "like" the Cabinet departments, it follows that "Heads" must be "like" the Cabinet department heads. The Ninth Circuit applied this functional test in *Silver v. United States Postal Service*.[50] Relying on a "contextual appreciation" of the Postal Service's organizational structure, the Ninth Circuit concluded that the postal powers rested exclusively with the Postal Service Governors, not the individual Postmaster General.[51] Therefore, the Ninth Circuit held that the Governors were the head of the Postal Service.[52]

A similar contextual appreciation of the SEC's organizational structure yields the conclusion that the Chairman is the head of the SEC. The majority attempted to minimize the powers of the Chairman by arguing that she is simply a commissioner with "additional administrative functions."[53] But this is misleading. While the Securities Exchange Act of 1934[54] only created a multimember Commission,[55] the Reorganization Plan No. 10 of 1950[56] formalized the position of Chairman and transferred to it all of the "*executive* and administrative functions of the Commission."[57] These functions include the power to allocate duties among the different SEC divisions, to spend agency funds, and to delegate authority to lower-level officers or employees.[58]

The majority's claim that the Chairman is simply a commissioner with extra duties is contradicted by its own reasoning. During its discussion of the separation of powers issue, the majority argued that the President possesses influence over the Commission due to his control over the Chairman, whom the majority described as having significant powers because she "dominate[s] commission policymaking" and "directs 'the administrative side of commission business, select[s] most

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[49] Freytag v. Comm'r, 501 U.S. 868, 886 (1991) (emphasis added).

[50] 951 F.2d 1033 (9th Cir. 1991).

[51] *Id.* at 1038. The Ninth Circuit noted that the Governors appoint and can remove the Postmaster General, making it "impossible to conclude that the [Postmaster General] is the head of the department." *Id.* at 1038–39.

[52] *Id.* at 1038.

[53] *Free Enter. Fund*, 537 F.3d at 678.

[54] 15 U.S.C. §§ 78a–78mm (2006).

[55] *Id.* § 78d(a).

[56] 3 C.F.R. 1006 (1949–1953), *reprinted in* 5 U.S.C. app. at 567–68 (2006).

[57] *Id.* § 1(a) (emphasis added). Prior to 1950, the Commission elected a Chairman annually. *See* Donna M. Nagy, *Playing Peekaboo with Constitutional Law: The PCAOB and Its Public/Private Status*, 80 NOTRE DAME L. REV. 975, 1051 n.424 (2005) (providing background on the creation of the Chairman position).

[58] Reorganization Plan No. 10 of 1950 §§ 1(a), 2, 3 C.F.R. 1006, *reprinted in* 5 U.S.C. app. at 568.

staff, set[s] budgetary policy, and as a consequence command[s] staff loyalties.'"[59] As the Tenth Circuit has also noted, the SEC Chairman "exerts far more control than [her] one vote would seem to indicate" because she "controls key personnel, internal organization, and the expenditure of funds."[60]

According to the SEC's website, the Chairman is "the agency's chief executive."[61] Every important position in the SEC is appointed by the Chairman.[62] This includes the General Counsel, the Chief Accountant, and the Chief Economist,[63] all of whom are probably inferior officers under the Appointments Clause and must be appointed by the department head.[64] The majority tried to reconcile this conflict by arguing that the Chairman does not have "sole appointment authority" with respect to those officers because the Commission as a whole must approve all major appointments.[65] But requiring subsequent *approval* from the Commission does not mean the Chairman is not the one exercising the appointment power.

The majority pointed out that the Reorganization Act of 1949[66] requires an agency "head" to be either a civil service position or subject to presidential appointment with Senate approval and claimed the Chairman is neither.[67] But the Chairman is subject to Senate approval as a Commissioner, and while the title of agency "head" for statutory purposes may be instructive, it is not determinative for constitutional purposes. Moreover, the majority's point is undercut by other statutory schemes, which define the Chairman as the "head." For example, the Inspector General Act of 1978[68] (IG Act) created an Inspector General office in each federal agency and defines the SEC as a "designated Federal entity."[69] The "head" of this entity appoints the agency's Inspector General.[70] The IG Act requires the Director of the

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[59] *Free Enter. Fund*, 537 F.3d at 680 (alterations in original) (quoting Peter L. Strauss, *The Place of Agencies in Government: Separation of Powers and the Fourth Branch*, 84 COLUM. L. REV. 573, 591 (1984)).

[60] SEC v. Blinder, Robinson & Co., 855 F.2d 677, 681 (10th Cir. 1988).

[61] U.S. Sec. & Exch. Comm'n, The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation, http://sec.gov/about/whatwedo.shtml (last visited May 15, 2009).

[62] *See* Reorganization Plan No. 10 of 1950 § 1(a), 3 C.F.R. 1006, *reprinted in* 5 U.S.C. app. at 568.

[63] *See* U.S. Sec. & Exch. Comm'n, *supra* note 61.

[64] These appointees exercise "significant authority pursuant to the laws of the United States," Buckley v. Valeo, 424 U.S. 1, 126 (1976), and would likely be deemed inferior officers subject to the Appointments Clause.

[65] *Free Enter. Fund*, 537 F.3d at 678.

[66] Pub. L. No. 81-109, 63 Stat. 203 (1949).

[67] *Free Enter. Fund*, 537 F.3d at 678 (citing 5 U.S.C. § 904 (2006)).

[68] 5 U.S.C. app. at 466–98 (2006).

[69] *Id.* at 483, § 8G(a)(2) (internal quotation marks omitted).

[70] *Id.* at 484, § 8G(c).

Office of Management and Budget to consult with the Comptroller General to determine the "head" of each entity and publish that list annually.[71] Since 1989, the first year this list was published, until the most recent publication of January 21, 2009, every single list has designated the Chairman as the "head" of the SEC.[72] But the majority overlooked this fact.

The majority might argue that none of these points proves beyond a shadow of a doubt that the Chairman is the head. Therefore, given that Congress and the President have explicitly approved the Act, one might prefer to minimize the Chairman's powers and disregard the Board's unusual appointment method rather than overrule the Act on technical grounds. But even if the contextual analysis is not dispositive, because the Chairman is the department's most politically accountable actor, the purpose of the Appointments Clause weighs strongly in favor of concluding that she is the head.

According to the historian Gordon Wood, the Framers considered "the power of appointment" to be "the most insidious and powerful weapon of eighteenth-century despotism."[73] The Supreme Court has held that the clause protects the "structural interests . . . of the entire Republic"[74] by preventing Congress from "distributing power too widely [and] by limiting the actors in whom Congress may vest the power to appoint."[75] The rationale is simple: "[W]idely distributed appointment power subverts democratic government."[76] Resting power in a limited number of heads promotes political accountability. According to the Supreme Court, appointment power can be vested in department heads because they are "subject to the exercise of political oversight and share the President's accountability to the people."[77]

The holding that the Commission is the department head violates this principle. Although the majority is right that a multimember commission *can* satisfy the Appointments Clause, this makes sense only when such a commission is the most politically accountable actor in the department.[78] In the case of the SEC, not only has Congress

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[71] *Id.* at 485, § 8G(h)(1).

[72] *See, e.g.*, 2008 and 2009 List of Designated Federal Entities and Federal Entities, 74 Fed. Reg. 3656, 3656 (Jan. 21, 2009); List of Designated Federal Entities and Federal Entities, 54 Fed. Reg. 47,158, 47,158 (Nov. 9, 1989).

[73] GORDON S. WOOD, THE CREATION OF THE AMERICAN REPUBLIC, 1776–1787, at 143 (1998).

[74] Freytag v. Comm'r, 501 U.S. 868, 880 (1991).

[75] *Id.* at 885.

[76] *Id.*

[77] *Id.* at 886.

[78] This was true in the two examples the majority cites to show that multimember commissions can be department heads. In *Silver*, the Ninth Circuit properly held that the Postal Service is headed by the Governors since they are appointed by the President, whereas the Postmaster General is appointed by the Governors. *See* Silver v. U.S. Postal Serv., 951 F.2d 1033, 1037–39

approved the delegation of significant executive authority away from the Commission and to the Chairman, but it also has granted this extra authority with the understanding that the Chairman would be subject to more presidential control. While the President can remove members of the Commission only for cause, "the [C]hairman serves at the pleasure of the President."[79] This removal power is critical for political accountability, for "it is only the authority that can remove him . . . that [an officer] must fear and, in the performance of his functions, obey."[80] The majority itself noted that the President's ability to appoint and remove the Chairman is the most effective way for the President to hold the SEC accountable.[81]

The Chairman's high degree of political accountability is corroborated by recent events. During the 2008 presidential campaign, a major response by Senator John McCain to the financial crisis was to promise to "fire" SEC Chairman Christopher Cox.[82] After the 2008 election, one of President-elect Obama's most high-profile nominations was that of Mary Schapiro to head the SEC.[83] These anecdotes suggest that in terms of public perception, the SEC Chairman is the most important and politically visible member of the Commission.

Vesting the appointment power exclusively in a department's most politically accountable actor, rather than in multiple different actors, avoids the diffusion of responsibility that the Framers sought to avert through the Appointments Clause. Allowing the Commission to appoint some officers and the Chairman to appoint others opens the door for Congress to vest the appointment of officers within the same department to a clutter of overlapping entities, each with varying degrees of presidential accountability.[84] The Appointments Clause sought to avoid just such a state of affairs. The Sarbanes-Oxley Act fails to do so and should have been held unconstitutional.

(9th Cir. 1991). In the case of the Civil Service Commission, the governing statute did not provide for a chairman. *See* Civil Service (Pendleton) Act, ch. 27, 22 Stat. 403 (1883) (amended 1978).

79 SEC v. Blinder, Robinson & Co., 855 F.2d 677, 681 (10th Cir. 1988).

80 Bowsher v. Synar, 478 U.S. 714, 726 (1986) (quoting Synar v. United States, 626 F. Supp. 1374, 1401 (D.D.C. 1986)) (internal quotation mark omitted).

81 *See Free Enter. Fund*, 537 F.3d at 680 ("[T]he President possesses significant additional levers of influence. Most obviously, by appointment of the Commission chairman, who serves at the pleasure of the President[,] . . . the President can influence Commission policy . . . .").

82 Stephen Braun & Noam N. Levey, *Seizing on Wall Street's Woes*, L.A. TIMES, Sept. 19, 2008, at A18. Although there was some debate over whether Senator McCain had cause to "fire" Cox, Senator McCain could have demoted Cox from the chairmanship without showing cause. *See For the Record: SEC Chairman*, L.A. TIMES, Oct. 3, 2008, at A2 (*Los Angeles Times* correcting its initial assertion that the President could not fire the Chairman).

83 *See* Jim Puzzanghera & Peter Nicholas, *Obama To Pick Mary Schapiro as SEC Head*, L.A. TIMES, Dec. 18, 2008, at C1.

84 *Cf.* Elena Kagan, *Presidential Administration*, 114 HARV. L. REV 2245, 2336 (2001) ("Take the President out of the equation and what remains are individuals and entities with a far more tenuous connection to national majoritarian preferences and interests . . . .").