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3rd UPDATE: US Supreme Court Invalidates Part Of Accounting Board

(Adds comment from Sen. Leahy, Rep. Kanjorski and the Cato Institute.)

By Brent Kendall and Fawn Johnson Of DOW JONES NEWSWIRES

WASHINGTON (Dow Jones)--A divided U.S. Supreme Court on Monday struck down some federal provisions that created a private regulatory body to inspect and discipline public-company accountants, but the decision doesn't dismantle the accounting board or invalidate the 2002 Sarbanes-Oxley Act as some critics would have liked.

The high court, in a 5-4 opinion by Chief Justice John Roberts, found fault with some parts of the Public Company Accounting Oversight Board, which was created as part of Sarbanes-Oxley to combat corporate accounting scandals in the wake of collapses at Enron and WorldCom.

Congress had given the five-member board, a not-for-profit corporation, broad regulatory authority over accounting firms that audit publicly traded companies.

Roberts said the structure of the accounting board violated constitutional separation-of-powers principles because it was too difficult for the president to remove board members.

"The president cannot take care that the laws be faithfully executed if he cannot oversee the faithfulness of the officers who execute them," Roberts wrote.

The court, however, refused to strike down the accounting board in its entirety, saying the board's mere existence didn't violate the Constitution.

PCAOB said it will continue to run all programs as usual, and no legislation will be needed to bring it in line with the Constitution. "We are pleased that the decision allows the PCAOB to continue without interruption to carry out its important mission of overseeing public company audits," said PCAOB Acting Chairman Daniel L. Goelzer.

Roberts said Sarbanes-Oxley "remains fully operative as a law." He said the unconstitutional provisions governing the board could be severed from the rest of the law.

Roberts said the Securities and Exchange Commission will now have the authority to remove board members at will. Previously, the SEC could only remove members for good cause.

"I am pleased that the court has determined that the board's operations may continue and the Sarbanes-Oxley Act, with the board's tenure restrictions excised, remains fully in effect," said SEC Chairman Mary Schapiro. "The PCAOB is a cornerstone of the Sarbanes-Oxley Act and serves a critical role in promoting investor protection and audit quality."

The accounting industry also applauded the ruling. "This is the least disruptive decision," said Center for Audit Quality Executive Director Cindy Fornelli. "We're pleased the court made it clear the PCAOB could continue to function....It's important for investors."

Barry Melancon, president of the American Institute of CPAs, said, "The court rejected a transparent attempt to undermine the post-Enron reforms that have served our financial markets well."

The decision could be considered a setback for those looking to get rid of accounting rules. "They could have struck down the whole [Sarbanes-Oxley] law and they obviously did not do that. For critics of the law, that means much narrower relief," said Hans Bader, an attorney at the Competitive Enterprise Institute, which was co-counsel for the plaintiffs in the case.

But Bader posited that the ruling could call into question previous rulings from the PCAOB because it wasn't accountable to higher-ups in the administration at the time it made those rules.

Free-market advocates who don't like Sarbanes-Oxley saw some good in the decision. PCAOB now is "tied more closely with the administration," said Cato Institute Senior Fellow Ilya Shapiro. "It removes the ability of the president or the administration to say, 'We don't control these guys.'"

The court's ruling fell along its ideological fault lines, with the conservatives in the majority and the liberal justices in dissent.

Justice Stephen Breyer, writing for the dissenters, said the accounting board raised no constitutional concerns.

"The court's contrary holding threatens to disrupt severely the fair and efficient administration of the laws," Breyer wrote.

Citing Breyer's dissent, Senate Judiciary Committee Chairman Patrick Leahy (D., Vt.) said he is "very disappointed" in the decision because it could call into question agencies created by Congress to combat fraud and inefficiency.

"Congress has established dozens of agencies which serve as indispensable corporate watchdogs and whose oversight provides a check on the power of Wall Street," Leahy said.

Rep. Paul Kanjorski (D., Pa.) said he is disappointed in the Supreme Court in some regards, he is glad the PCAOB will be able to continue its work.

A free-enterprise group and a Nevada accounting firm had challenged the legality of the board, arguing that it violated constitutional separation-of-powers principles.

The challengers argued that Congress vested the accounting board with widespread and unsupervised government power that couldn't be checked by the president or the head of a government department.

The case is Free Enterprise Fund v. Public Company Accounting Oversight Board, 08-861.

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