

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-85090; File No. PCAOB-2019-01)

February 11, 2019

Public Company Accounting Oversight Board; Notice of Filing of and Immediate Effectiveness of Proposed Bylaw and Rule Amendments to Provide that the Board's Appointment and Removal of Hearing Officers Are Subject to Commission Approval

Pursuant to Section 107(b) of the Sarbanes-Oxley Act of 2002 (the "Act"), 15 U.S.C. 7217(b), notice is hereby given that on January 29, 2019, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "SEC" or the "Commission") the proposed amendments described in items I and II below, which items have been prepared by the Board. The Commission is publishing this notice to solicit comments on the proposed amendments from interested persons.

I. Board's Statement of the Terms of Substance of the Proposed Amendments

On December 20, 2018, the Board adopted amendments to its bylaws and rules (collectively, the "proposed amendments") to provide that the PCAOB's appointment and removal of PCAOB hearing officers are subject to Commission approval and to make related clarifying and conforming changes to the PCAOB's rules. Specifically, the Board is amending Article VI of its bylaws and PCAOB Rules 1001(h)(i), 5200, and 5402. The proposed amendments are concerned solely with the administration of the PCAOB in that they relate to the employment relationship between the Board and its hearing officers, its interaction with the Commission in the Commission's performance of oversight of the PCAOB, and the clarification of the delegations of authority by the Board to PCAOB hearing officers.

The text of the proposed amendments appears in the Board’s SEC Form 19b-4 filing and is available on the Board’s website at <https://pcaobus.org/Rulemaking/Pages/Docket045> and at the Commission’s Public Reference Room.

II. Board’s Statement of the Purpose of, and Statutory Basis for, the Proposed Amendments

In its filing with the Commission, the Board included statements concerning the purpose of, and basis for, the proposed amendments and stated that the amendments are concerned solely with the administration of the PCAOB. The text of these statements may be examined at the places specified in Item IV below. The Board has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Board’s Statement of the Purpose of, and Statutory Basis for, the Proposed Amendments

1. Purpose

The Board’s duties under the Act include acting on registration applications of public accounting firms that prepare audit reports for issuers, brokers, or dealers,<sup>1</sup> and conducting disciplinary proceedings concerning, and imposing appropriate sanctions where justified upon, registered public accounting firms and their associated persons.<sup>2</sup> In carrying out these duties, the Board may direct that a PCAOB hearing officer preside

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<sup>1</sup> The PCAOB has oversight authority with respect to audits of brokers and dealers that are registered with the SEC. *See* Sections 110(3) and (4) of the Act, 15 U.S.C. 7220(3) and (4).

<sup>2</sup> *See, e.g.*, Sections 101(c)(1) & (4), 102(c), 105(a) & (c)(1)-(3) of the Act, 15 U.S.C. 7211(c)(1) & (4), 7212(c), 7215(a) & (c)(1)-(3).

over a disciplinary or other proceeding.<sup>3</sup> The Board’s authority to do so derives from Section 101(f)(4) of the Act, permitting the Board, subject to Commission oversight under Section 107 of the Act, “to appoint such employees, accountants, attorneys, and other agents as may be necessary or appropriate, and to determine their qualifications, define their duties, and fix their salaries or other compensation.” Section 101(g)(2) of the Act further authorizes that “[t]he rules of the Board shall, subject to the approval of the Commission . . . permit, as the Board determines necessary and appropriate, delegation by the Board of any of its functions to an . . . employee of the Board, . . . including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any matter.” In 2004, the Commission approved the Board’s proposed rules relating to investigations and adjudications, authorizing creation of the PCAOB’s hearing officer position.<sup>4</sup>

On June 21, 2018, the U.S. Supreme Court held in *Lucia v. SEC* that SEC Administrative Law Judges (ALJs) are inferior officers under the Appointments Clause of the U.S. Constitution and that accordingly SEC ALJs are required to be appointed by “the President, a court of law, or a head of department,” such as the Commission.<sup>5</sup> Since the *Lucia* decision, the Commission has taken various actions, including issuance of an order reiterating its November 30, 2017 approval of the prior appointments of its ALJs by

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<sup>3</sup> See, e.g., Sections 101(f)(4) and 101(g)(2) of the Act, 15 U.S.C. 7211(f)(4) & (g)(2); PCAOB Rules 5200 (Commencement of Disciplinary Proceedings), 5500 (Commencement of Hearing on Disapproval of a Registration Application).

<sup>4</sup> See *Order Approving Proposed Rules Relating to Investigations and Adjudications*, SEC Rel. No. 34-49704, 2004 WL 1439833 (May 14, 2004).

<sup>5</sup> 138 S. Ct. 2044, 2050-51 (2018).

its staff as the Commission's own under the Constitution.<sup>6</sup> In light of the *Lucia* litigation, other federal government agencies have taken similar measures as to their ALJs or like officials, also out of an abundance of caution and for avoidance of doubt.<sup>7</sup>

The *Lucia* case did not involve a challenge to PCAOB hearing officers, only to SEC ALJs. Nor has any court, the Commission, or the Board adjudicated whether a PCAOB hearing officer is, like an SEC ALJ, an inferior officer under the Appointments Clause.<sup>8</sup> Indeed, there are a number of differences between the position of an SEC ALJ and the position of a PCAOB hearing officer.<sup>9</sup>

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<sup>6</sup> See *In re Pending Administrative Proceedings*, SEC Rel. No. 34-83907, 2018 WL 4003609, \*1 (Aug. 22, 2018).

<sup>7</sup> See, e.g., USITC, The Appointment of the Commission's Administrative Law Judges for Section 337 Investigations, 83 Fed. Reg. 45,678-01 (Sept. 10, 2018); FMSHRC, Ratification Notice (Apr. 3, 2018), available at [www.fmshrc.gov/about/news/commission-ratification-notice](http://www.fmshrc.gov/about/news/commission-ratification-notice); FDIC, Resolution of Board of Directors (July 19, 2018), available at <https://www.fdic.gov/news/board/2018-07-19-085152.pdf>; CFTC, Ratification and Reconsideration Order, *In re Pending Administrative Proceedings*, 2018 WL 1966116 (Apr. 6, 2018); Letter from Sec'y R. Alexander Acosta, Dep't of Labor, to Hon. Paul R. Almanza, Admin. Law Judge, Dep't of Labor (Dec. 21, 2017), available at [https://www.oalj.dol.gov/PUBLIC/FOIA/Frequently\\_Requested\\_Records/ALJ\\_Appointments/Secretarys\\_Ratification\\_of\\_ALJ\\_Appointments\\_12\\_21\\_2017.pdf](https://www.oalj.dol.gov/PUBLIC/FOIA/Frequently_Requested_Records/ALJ_Appointments/Secretarys_Ratification_of_ALJ_Appointments_12_21_2017.pdf); FTC, *P130500 Federal Trade Commission Minute: Ratification of Appointment of Administrative Law Judge and Chief Administrative Law Judge* (Sept. 11, 2015), attached as Ex. A to FTC, Order Denying Respondent LabMD, Inc.'s Motion to Dismiss, *In re LabMD Inc.*, No. 9357 (Sept. 14, 2015), available at <https://www.ftc.gov/system/files/documents/cases/150914labmdmotion.pdf>.

<sup>8</sup> An attempt was made to challenge the constitutionality of a PCAOB hearing officer's appointment in *Kabani v. SEC*, but the court held that the argument had not been timely raised and was forfeited. 733 F. App'x 918, 2018 WL 3828524, \*1 (9<sup>th</sup> Cir. Aug. 13, 2018).

<sup>9</sup> For example, an SEC ALJ may administer oaths and affirmations; issue, revoke, quash, or modify subpoenas; issue protective orders; and punish contemptuous conduct; a PCAOB hearing officer does not have that authority. Compare 17 CFR 200.14(a)(1) & (2), 200.111(b), 180(a), 232(e), 322 with PCAOB Rules 5103, 5105, 5200(b)(1), 5424.

Nevertheless, out of an abundance of caution and to eliminate any uncertainty about the status of PCAOB hearing officers that might distract from the PCAOB's mission, including its important registration and disciplinary functions, the Board is adopting certain amendments to its bylaws and rules. These amendments modify the PCAOB's processes to appoint and remove its hearing officers to provide that such appointments and removals shall be subject to the approval of the Commission, a head of department under the Appointments Clause.

The amendments to Article VI of the Board's bylaws and PCAOB Rule 1001(h)(i), the language of which rule is changed to cross-reference the bylaw amendment, specify that the PCAOB's appointment and removal of any PCAOB hearing officer are subject to Commission approval. These changes are consistent with the Commission's broad authority to oversee the Board under Section 107 of the Act, *see* Sections 101(c) & (f) and 107 of the Act, 15 U.S.C. 7211(c) & (f), 7217, and the Commission's authority to "appoint . . . officers, attorneys, economists, examiners, and other employees" under Section 4(b) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. 78d(b).

As contemplated by these amendments, when the PCAOB's Governing Board, as defined by the bylaws,<sup>10</sup> has reached a decision on the appointment or removal of any PCAOB hearing officer, that decision shall be submitted to the Commission for

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<sup>10</sup> *See* Articles IV and VI of the PCAOB's bylaws (stating that "[t]he Governing Board shall consist of those persons appointed thereto by the Securities and Exchange Commission, pursuant to Section 101 of the Act" and that "[t]he Chairman of the Governing Board . . . shall also be the President and Chief Executive Officer of the Corporation"). In *Free Enterprise Fund v. PCAOB*, 561 U.S. 477, 510 (2010), the Supreme Court held that PCAOB Governing Board members are inferior officers under the Appointments Clause.

consideration. The proposed appointment or removal of a hearing officer by the PCAOB cannot be effectuated until Commission approval has been given. The Commission's approval of a PCAOB hearing officer's appointment will result in the hearing officer being appointed in the manner of an inferior officer for purposes of the Appointments Clause.<sup>11</sup>

The Board is also adopting certain clarifying and conforming amendments to its adjudications rules in light of the rule changes discussed above. Specifically, the Board is adding a new subsection to Rule 5200 to summarize the framework within which the hearing officer functions under the Act and the Board's rules. That new subsection explains that all proceedings shall be presided over by the Board, which is the entity empowered to act on registration applications and to conduct disciplinary proceedings.<sup>12</sup> Alternatively, the Board may order that the proceedings be conducted in the first instance by a hearing officer to whom the Board has, under certain conditions, delegated adjudicatory responsibilities.<sup>13</sup> The new subsection makes even more explicit the manner in which current PCAOB rules, such as Rules 5200(b)(10), 5201(d)(2), 5204(b), and 5445, situate the hearing officer within PCAOB adjudication processes.<sup>14</sup>

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<sup>11</sup> See *Free Enterprise Fund*, 561 U.S. at 512 n.13 (noting examples of precedents in which “[w]e have previously found that the department head’s approval [of the appointment of personnel] satisfies the Appointments Clause”).

<sup>12</sup> See, e.g., Sections 101(c)(1) & (4) of the Act, 15 U.S.C. 7211(c)(1) & (4) (“the Board shall . . . register public accounting firms . . . [and] conduct . . . disciplinary proceedings . . .”) (emphasis added).

<sup>13</sup> See Section 101(g)(2) of the Act, 15 U.S.C. 7211(g)(2) (permitting, under specified conditions, “delegation by the Board of any of its functions to an . . . employee of the Board . . . , including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any matter”).

<sup>14</sup> The provision is also analogous to SEC Rule of Practice 110, 17 CFR 201.110.

Additionally, the amendments make clarifying and conforming edits to the heading of current PCAOB Rule 5200(b) and to the heading and text of PCAOB Rule 5402(b). Specifically, the words “appointment” and “appoint” in these current rules are replaced with “assignment” and “assign,” and current Rule 5200(b) is renumbered Rule 5200(c) and cross-referenced to new Rule 5200(b). These changes avoid any confusion between the actions of the Board and the Commission in appointing, and approving the appointment of, a hearing officer, and the PCAOB Secretary’s ministerial act of assigning a specific hearing officer to a specific proceeding pursuant to a Board order.

The above-described, targeted amendments seek to dispel any legal uncertainty arising from *Lucia* about the PCAOB hearing officer, who, as noted, may be tasked with presiding over a disciplinary or other proceeding. This will facilitate and make more efficient the Board’s performance of its duties under the Act to take “[a]ction on [a]pplications” for the “regist[r]ation [of] public accounting firms that prepare audit reports for issuers, brokers, and dealers”; to “conduct . . . disciplinary proceedings concerning, and impose appropriate sanctions where justified upon, registered public accounting firms and associated persons of such firms”; and to “enforce compliance with th[e] Act, the rules of the Board, professional standards, and the securities laws relating to the preparation and issuance of audit reports and the obligations and liabilities of accountants with respect thereto, by registered public accounting firms and associated persons thereof.”<sup>15</sup> These functions are part of the Board’s responsibility “to oversee the audit of companies that are subject to the securities laws, and related matters, in order to

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<sup>15</sup> See, e.g., Sections 101(c)(1), (4) & (6), 102(c), 105(a) & (c)(1)-(3) of the Act, 15 U.S.C. 7211(c)(1), (4) & (6), 7212(c), 7215(a) & (c)(1)-(3).

protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports.”<sup>16</sup>

Moreover, additional benefits will flow from the amendments because the Appointments Clause serves an important public purpose. The Supreme Court has described the Clause’s requirements as “among the significant structural safeguards of the constitutional scheme,” “designed to preserve political accountability relative to important government assignments.”<sup>17</sup> The Board has chosen to remedy the uncertainty caused by *Lucia* by conforming the appointment and removal of its hearing officers to those requirements. Thus, the Appointments Clause’s benefits and protections are explicitly extended to respondents in PCAOB proceedings, and to the public more broadly.

## 2. Statutory Basis

The statutory basis for the proposed amendments is Title I of the Act. Specifically, Section 101(f)(2) of the Act empowers the Board, subject to Commission oversight under Section 107 of the Act, “to conduct its operations and maintain offices, and to exercise all other rights and powers authorized by this Act.” Section 101(f)(4), as discussed, empowers the Board, subject to Commission oversight under Section 107 of the Act, to appoint personnel. Section 101(g)(1) directs the Board, “subject to the approval of the Commission . . . [to] provide for the operation and administration of the Board, the exercise of its authority, and the performance of its responsibilities under th[e] Act.” And Section 101(g)(2), as discussed, permits the Board, “subject to the approval of the Commission,” to delegate its hearing functions within the PCAOB. Furthermore, the

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<sup>16</sup> See Section 101(a) of the Act, 15 U.S.C. 7211(a).

<sup>17</sup> *Edmond v. United States*, 520 U.S. 651, 659, 663 (1997).



amendments directly relate to statutory duties of the Board and purposes for its establishment that are discussed above.

B. Board's Statement on Burden on Competition

Not applicable. The proposed amendments are concerned solely with the administration of the PCAOB, as discussed in Item I above.

C. Board's Statement on Comments on the Proposed Amendments Received from Members, Participants or Others

Written comments were neither solicited nor received. The proposed amendments are concerned solely with the administration of the PCAOB, as discussed in Item I above.

III. Date of Effectiveness of the Proposed Amendments and Timing for Commission

The foregoing proposed amendments have become effective pursuant to Section 19(b)(3)(A) of the Securities Exchange Act of 1934<sup>18</sup> and paragraph (f)(3) of Rule 19b-4 thereunder.<sup>19</sup> At any time within 60 days of the filing of the proposed amendments, the Commission summarily may temporarily suspend such amendments if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Act.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed amendments are consistent with the requirements of Title I of the Act. Comments may be submitted by any of the following methods:

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<sup>18</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>19</sup> 17 CFR 240.19b-4(f)(3).

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/pcaob.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include PCAOB-2019-01 on the subject line.

Paper comments:

- Send paper comments in triplicate to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to PCAOB-2019-01. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/pcaob.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed amendments that are filed with the Commission, and all written communications relating to the proposed amendments between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549-1090, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing will also be available for inspection and copying at the principal office of the PCAOB. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make

available publicly. All submissions should refer to PCAOB-2019-01 and should be submitted on or before [insert 21 days from publication in the Federal Register].

For the Commission, by the Office of the Chief Accountant, pursuant to delegated authority.<sup>20</sup>

Eduardo A. Aleman  
Deputy Secretary

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<sup>20</sup> 17 CFR 200.30-11(b)(2).