

2009

## Beyond Economics: The U.S. Recognition of International Financial Reporting Standards as an International Subdelegation of the SEC's Rulemaking Authority

Jacob L. Barney

Follow this and additional works at: <https://scholarship.law.vanderbilt.edu/vjtl>



Part of the [Administrative Law Commons](#), and the [Securities Law Commons](#)

---

### Recommended Citation

Jacob L. Barney, Beyond Economics: The U.S. Recognition of International Financial Reporting Standards as an International Subdelegation of the SEC's Rulemaking Authority, 42 *Vanderbilt Law Review* 579 (2021)

Available at: <https://scholarship.law.vanderbilt.edu/vjtl/vol42/iss2/5>

This Note is brought to you for free and open access by Scholarship@Vanderbilt Law. It has been accepted for inclusion in Vanderbilt Journal of Transnational Law by an authorized editor of Scholarship@Vanderbilt Law. For more information, please contact [mark.j.williams@vanderbilt.edu](mailto:mark.j.williams@vanderbilt.edu).

# NOTES

## **Beyond Economics: The U.S. Recognition of International Financial Reporting Standards as an International Subdelegation of the SEC's Rulemaking Authority**

### ABSTRACT

*A final rule promulgated by the Securities and Exchange Commission (SEC) in 2008 allowing foreign private securities issuers to prepare SEC-required financial disclosures under international financial reporting standards (IFRS) as promulgated by the International Accounting Standards Board (IASB) is a highly significant event for U.S. and global capital markets. However, surprisingly few questions have been asked regarding the SEC's legal authority to take such an unprecedented step.*

*This Note assesses the recent SEC action with regard to IASB from two perspectives—traditional administrative law, with particular emphasis on delegations by government entities to private parties, and international law, with particular emphasis on the ability of a national government to delegate some portion of its sovereignty to international bodies. This Note concludes that the SEC does not currently possess the authority necessary to recognize IASB as an official accounting standard-setter, and that Congress must take the lead on any proposed agency action which would function as an international delegation of authority.*

## TABLE OF CONTENTS

I.	INTRODUCTION .....	581
II.	THE HISTORY OF ACCOUNTING RULEMAKING UNDER U.S. SECURITIES LAWS.....	584
	A. <i>The History of the SEC and Its Role as Accounting Standard-Setter</i> .....	584
	B. <i>The History and Standard-Setting Procedures of FASB</i> .....	587
	C. <i>The History and Standard-Setting Procedures of IASB</i> .....	589
III.	SUBDELEGATION.....	592
	A. <i>General Limitations on the Ability of Government Branches and Agencies to Subdelegate Their Authority to Private Parties</i> .....	592
	1. Delegation and Subdelegation in Administrative Law .....	592
	2. <i>U.S. Telecom Ass'n v. FCC: Legal         Limitations on Subdelegation</i> .....	593
	B. <i>Recognition of Industry Standards Established by a Nongovernmental Entity as a Form of Subdelegation</i> .....	595
	1. Recognition of Externally Created Accounting Standards as a Subdelegation of the SEC's Authority.....	596
	a. "Passing of Power" .....	596
	b. Previous Scholarly Work .....	597
	c. Comparisons to Other Delegations.....	597
	2. Delegation vs. Incorporation.....	598
	C. <i>Specific Limitations on the SEC's Ability to Subdelegate Accounting Rulemaking Authority</i> .....	601
IV.	INTERNATIONAL DELEGATION.....	604
	A. <i>Constitutional Limitations on Delegations of Power to International Organizations</i> .....	604
	B. <i>Policy Considerations Regarding International Delegations</i> .....	610
	1. Accounting as an Expression of National and Financial Forces.....	610
	a. National Forces .....	611
	b. Financial Forces.....	612
	2. The Effect of Accounting System Choice on Capital Formation .....	614

V.	RECOMMENDATIONS AND PROPOSALS FOR FUTURE ACTION.....	616
A.	<i>A Path Forward for Congress</i> .....	616
B.	<i>Judicial Review of the SEC's Recognition of IFRS</i> .....	618
VI.	CONCLUSION.....	620

In the U.S. capital markets many . . . are anxious to capitalize on the benefits of having a widely used set of accounting standards accepted and in place. I am excited about this opportunity, but I also want to make sure we get it right.<sup>1</sup>

## I. INTRODUCTION

The prevailing regime of financial accounting and reporting for publicly held companies in the U.S. is currently undergoing significant changes. Almost since its inception, the U.S. Securities and Exchange Commission (SEC) has “outsourced” its statutory authority to promulgate financial accounting rules<sup>2</sup> applicable to companies that must make financial disclosures under the federal securities laws.<sup>3</sup> The SEC currently recognizes the Financial Accounting Standards Board (FASB) as the organization empowered to promulgate such accounting rules.<sup>4</sup> Although several organizations have been recognized by the SEC as officially establishing generally accepted accounting principles (GAAP) since the 1930s,<sup>5</sup> all of these organizations (in their role as standard-setters) have worked exclusively toward the goal of establishing rules and practices for U.S. companies—or, at least, for those companies wishing to access U.S. capital markets.<sup>6</sup>

---

1. Donald T. Nicolaisen, *A Securities Regulator Looks at Convergence*, 25 NW. J. INT'L L. & BUS. 661, 662 (2005).

2. See Securities Act of 1933 § 19(a), 15 U.S.C. § 77s(a) (2008) (“[T]he Commission shall have authority . . . to prescribe . . . the methods to be followed in the preparation of accounts . . .”). This Note uses the terms “rules,” “principles,” and “standards” interchangeably to refer to those substantive accounting guidelines which are or may soon be controlling under the federal securities laws.

3. Andrew F. Kirkendall, Comment, *Filling in the GAAP: Will the Sarbanes-Oxley Act Protect Investors from Corporate Malfeasance and Restore Confidence in the Securities Market?*, 56 SMU L. REV. 2303, 2306–07 (2003).

4. *Id.* at 2307–08.

5. See *id.* (providing a brief chronology of the SEC’s delegation to various accounting organizations).

6. See Concept Release on Allowing U.S. Issuers to Prepare Financial Statements in Accordance with International Financial Reporting Standards, Securities Act Release No. 8831, Exchange Act Release No. 56,217, Investment

Recently, however, the SEC has considered allowing companies, both foreign and U.S.-based, to disclose financial information in accordance with the International Financial Reporting Standards (IFRS) promulgated by the International Accounting Standards Board (IASB).<sup>7</sup> In 2006, the SEC began allowing foreign-based securities issuers to file with the SEC financial statements prepared in accordance with IFRS and containing a conversion or “reconciliation” from IFRS to U.S. GAAP<sup>8</sup> (as opposed to financial statements prepared entirely in accordance with GAAP). SEC Chairman Christopher Cox publicly stated that he wanted the SEC to “eliminate, by 2009 at the latest, the SEC requirement for foreign private issuers to reconcile IFRS-based financial statements to US GAAP.”<sup>9</sup> However, in the most recent and arguably most important development in the U.S. shift toward the use of international accounting standards, the SEC promulgated a final rule in January 2008 that allowed foreign private securities issuers to file IFRS-based financial statements with the SEC without including a reconciliation to U.S. GAAP.<sup>10</sup> This development comes despite the fact that many in business and academia hold reservations against recognizing IFRS without a corresponding IFRS-GAAP reconciliation.<sup>11</sup>

A recognition of the validity of IFRS in regards to the fulfillment of financial disclosure requirements under U.S. securities laws marks

Company Act Release No. 27,924, 72 Fed. Reg. 45,600, 45,601 (Aug. 14, 2007) [hereinafter 2007 Concept Release] (“[T]he Commission historically has looked to private-sector bodies to provide standards for financial reporting by issuers in the U.S. public capital market.”).

7. See *id.* (soliciting public comments on the SEC’s proposal to give “U.S. issuers . . . the option to file . . . financial statements prepared in accordance with IFRS as published by the IASB”).

8. Press Release, U.S. Sec. & Exch. Comm’n, Accounting Standards: SEC Chairman Cox and EU Commissioner McCreevy Affirm Commitment to Elimination of the Need for Reconciliation Requirements (Feb. 8, 2006), <http://www.sec.gov/news/press/2006-17.htm> [hereinafter Cox-McCreevy Statement].

9. *Id.*

10. Acceptance from Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards Without Reconciliation to U.S. GAAP, Securities Act Release No. 8879, Exchange Act Release No. 57,026, 73 Fed. Reg. 986 (Jan. 4, 2008). The pertinent language provides that “financial statements [of foreign private issuers] may be prepared according to U.S. Generally Accepted Accounting Principles or International Financial Reporting Standards as issued by the International Accounting Standards Board.” 17 C.F.R. § 210.4-01(a)(2) (2008).

11. See, e.g., *International Accounting Standards: Opportunities, Challenges, and Global Convergence Issues: Hearing Before the Subcomm. on Securities, Insurance, and Investment of the S. Comm. on Banking, Housing, and Urban Affairs*, 110th Cong. 2 (2007) (statement of Teri Lombardi Yohn, Associate Professor, Kelley School of Business, Indiana University), available at [http://banking.senate.gov/\\_files/yohn.pdf](http://banking.senate.gov/_files/yohn.pdf) [hereinafter Yohn Statement] (arguing that “the elimination of the required IFRS-U.S. GAAP reconciliation is premature . . . and will cause U.S. investors to possess a significantly diminished set of relevant information for investment-related decision making”).

the first occasion upon which the SEC has given such recognition to international standards. This Note argues that the SEC's recognition of an international accounting standard-setter essentially acts as a further delegation, or subdelegation, of the rulemaking authority Congress originally vested in the SEC.<sup>12</sup> Recently, the U.S. Court of Appeals for the District of Columbia Circuit expressed concern about the validity of delegations of government power to foreign organizations,<sup>13</sup> and legal scholars have noted the complex issues and divergent interests inherent in such delegations.<sup>14</sup>

An assessment of the recognition of IFRS in the U.S. must necessarily extend beyond a purely economic analysis<sup>15</sup> and must also critically analyze the constitutional and political validity of recognition by a federal administrative agency of international standards in an area of law that previously had been strictly the domain of U.S.-based organizations.<sup>16</sup> This assessment can be broken down into two steps: (1) an analysis of the SEC's ability to subdelegate its authority to create accounting principles that are controlling under the federal securities laws; and (2) an analysis of the legality of and the policy considerations involved in delegating federal power to an international organization, either by one of the three main branches of the federal government or by an administrative agency in the form of a subdelegation. This Note concludes that though there are no specific constitutional limitations on the ability of the federal government to delegate authority to international organizations, there are two reasons why the SEC does not currently possess the authority necessary to recognize IFRS in

---

12. See 16A AM. JUR. 2D *Constitutional Law* § 299 (2008) (“[A] permissible delegation of legislative power sometimes may be subdelegated or redelegated.”). This proposition is discussed more thoroughly *infra* Part III.

13. See *Natural Res. Def. Council v. EPA*, 464 F.3d 1, 9 (D.C. Cir. 2006) (“There is significant debate over the constitutionality of assigning lawmaking functions to international bodies.”).

14. Compare Edward T. Swaine, *The Constitutionality of International Delegations*, 104 COLUM. L. REV. 1492, 1501 (2004) (arguing that “delegating national power to international institutions . . . provides a bulwark against the concentration of political power in the national government that is consistent with the ambitions of federalism”), with Julian G. Ku, *The Delegation of Federal Power to International Organizations: New Problems with Old Solutions*, 85 MINN. L. REV. 71, 74 (2000) (arguing that a stricter, more formalistic constitutional approach “is precisely what is needed in the case of international delegations because such delegations are meaningfully different from delegations to states and private parties”). These views are discussed further *infra* Part IV.A.

15. Although this Note will address some of the economic factors which would influence a potential SEC recognition of IFRS, it will focus primarily on the legal implications of such recognition. A summary of many of the economic arguments in favor of the adoption of IFRS in the U.S. can be found in Mark J. Hanson, *Becoming One: The SEC Should Join the World in Adopting the International Financial Reporting Standards*, 28 LOY. L.A. INT'L & COMP. L. REV. 521, 532–42 (2006).

16. Kirkendall, *supra* note 3, at 2307–08.

the U.S.: (1) because the recognition of IASB as an authorized accounting standard-setter constitutes a subdelegation to a private party, and the SEC lacks the express statutory authorization required to make such a subdelegation; and (2) because Congress, and not an administrative agency, is the proper body to make delegations of authority to international organizations.<sup>17</sup> Therefore, this Note also asserts that in order to validly recognize IASB as an official accounting standard-setter in the U.S., Congress must grant the SEC explicit authorization to make that recognition. If Congress does not give such specific authorization, the SEC's recognition of IFRS is likely reviewable in federal court.

Part II of this Note provides a brief overview of the history of the SEC, its delegations of the accounting rulemaking power to various organizations (including FASB, the current U.S.-based standard-setter), and the history of FASB and IASB, including the procedures used by both organizations in promulgating new accounting standards. Part III places the SEC's outsourcing of accounting rulemaking in the context of subdelegation and discusses both explicit and inherent limitations on the SEC's ability to make such subdelegations. Part IV discusses constitutional and policy-related limitations on the federal government's ability to delegate its powers to international or foreign-based organizations, with a particular focus on the SEC and IASB. Part V applies the subdelegation and the international delegation frameworks to the current SEC-IASB relationship and makes specific recommendations, and Part VI concludes with a few general observations.

## II. THE HISTORY OF ACCOUNTING RULEMAKING UNDER U.S. SECURITIES LAWS

### A. *The History of the SEC and Its Role as Accounting Standard-Setter*

The Securities Exchange Act of 1934 (the '34 Act)<sup>18</sup> established the SEC after the stock market crash of October 1929, which "dramatized the need for federal intervention in establishing and maintaining higher standards of business conduct in the capital markets."<sup>19</sup> Indeed, one major cause of the crash was that government "proposals . . . to require financial disclosure . . . were

---

17. See discussion *infra* Parts III, IV.A.

18. Securities Exchange Act of 1934 § 4(a), 15 U.S.C. § 78d(a) (2008).

19. U.S. SEC. & EXCH. COMM'N, ". . . GOOD PEOPLE, IMPORTANT PROBLEMS AND WORKABLE LAWS": 50 YEARS OF THE U.S. SECURITIES AND EXCHANGE COMMISSION 7 (1984) [hereinafter 50 YEARS].

never seriously pursued.”<sup>20</sup> The first set of federal securities laws was passed as the Securities Act of 1933 (the ’33 Act) and was for a short time administered by the Federal Trade Commission (FTC),<sup>21</sup> with the SEC taking over the FTC’s securities-related duties upon the passage of the ’34 Act (although not without some public backlash).<sup>22</sup> Among the powers conferred upon the SEC by the ’33 and ’34 Acts (as amended) are the powers to make “rules and regulations governing registration statements and prospectuses for various classes of securities and issuers,”<sup>23</sup> to exempt certain classes of securities from federal reporting requirements,<sup>24</sup> and to make rules requiring disclosure of specific information from companies who wish to have their securities listed on a national securities exchange.<sup>25</sup>

The SEC also has the authority “to prescribe . . . the methods to be followed in the preparation of accounts,”<sup>26</sup> or, in other words, to create what is known today as GAAP. The Sarbanes-Oxley Act of 2002 amended Section 19 of the ’33 Act to allow the SEC to subdelegate this rulemaking authority by “recogniz[ing], as ‘generally accepted’ for purposes of the securities laws, any accounting principles established by a standard setting body” that meets certain criteria.<sup>27</sup> These criteria are: (1) that the body is “organized as a private entity”; (2) that the body has “a board of trustees . . . serving in the public interest,” with limitations placed on the trustees’ connections to registered public accounting firms; (3) that the body is funded under the guidelines set out in Section 109 of the Sarbanes-Oxley Act;<sup>28</sup> (4) that the body “has adopted procedures to ensure

---

20. *Id.*

21. *Id.* at 9. The grants of power made to “the Commission” in the ’33 Act were thus originally made to the Federal Trade Commission and were transferred upon the creation of the SEC. *Id.* at 10. Interestingly, § 2 of the ’33 Act was not amended to read “[t]he term ‘Commission’ means the Securities and Exchange Commission,” as opposed to “Federal Trade Commission,” until 1987. Securities Act of 1933 § 2(a)(5), 15 U.S.C. § 77b(a)(5) (2008); Securities Act of 1933, Pub. L. No. 100-181, sec. 201, § 2(5), 101 Stat. 1240 (codified as amended at 15 U.S.C. § 77(b)(5) (2008)).

22. Publications such as *The New York Times* and *The Wall Street Journal* referred to the ’34 Act as “autocratic meddling” and “social control,” respectively. 50 YEARS, *supra* note 19, at 9.

23. Securities Act of 1933 § 19(a), 15 U.S.C. § 77s(a) (2008).

24. *Id.* § 3(b)–(c).

25. Securities Exchange Act of 1934 § 12(b)(1), 15 U.S.C. § 78l(b)(1) (2008).

26. Securities Act of 1933 § 19(a), 15 U.S.C. § 77s(a) (2008).

27. Sarbanes-Oxley Act of 2002 § 108, 15 U.S.C. § 7218 (2008). The language added by § 108 became the current § 19(b) of the ’33 Act (15 U.S.C. § 77s(b)). Although the language in the Sarbanes-Oxley Act states that the SEC grants recognition to accounting principles established by a standard-setting organization and not to the organization itself, this Note treats recognition of accounting standards and recognition of the standard-setting organization as identical and therefore interchangeable.

28. The funding guidelines established by § 109 are minimal, essentially requiring only that a fiscal year budget be approved at least one month before the start of the fiscal year, and that the organization be funded by an “accounting support fee”



prompt consideration . . . of changes to accounting principles necessary to reflect emerging accounting issues”; (5) that the body considers both “the need to keep standards current in order to reflect changes in the business environment” and “the extent to which international convergence on high quality accounting standards is necessary or appropriate in the public interest and for the protection of investors”; and (6) that the SEC determines that the body “is capable of improving the accuracy and effectiveness of financial reporting and the protection of investors under the securities laws.”<sup>29</sup>

Interestingly, Congress first granted explicit statutory authorization of the SEC’s subdelegation of accounting rulemaking authority in 2002, despite the fact that the SEC had subdelegated this authority since 1938.<sup>30</sup> At that time, the SEC recognized the American Institute of Accountants (currently known as the American Institute of Certified Public Accountants, or AICPA) as the first surrogate accounting standard-setter. The American Institute of Accountants in turn created the Committee on Accounting Procedure specifically to serve as the standard-setting body.<sup>31</sup> In 1959, due to demands for “more uniformity and specificity” in accounting practices, the AICPA replaced the Committee on Accounting Procedure with the Accounting Principles Board (APB).<sup>32</sup> In time, however, “the flow of new accounting issues outstripped the APB’s capacity,” and the APB lost stature among accounting practitioners.<sup>33</sup>

collected from securities issuers, as opposed to donations or other private contributions. Sarbanes-Oxley Act of 2002 § 109(b), (e), 15 U.S.C. § 7219(b), (e) (2008).

29. These six criteria are found in Securities Act of 1933 § 19(b)(1)(A)(i)–(v), (b)(1)(B), 15 U.S.C. § 77s(b)(1)(A)(i)–(v), (b)(1)(B) (2008).

30. See Donna M. Nagy, *Playing Peekaboo with Constitutional Law: The PCAOB and Its Public/Private Status*, 80 NOTRE DAME L. REV. 975, 987 (2005) (pointing to a 1938 SEC release as the first occasion on which the Commission “articulated its policy of private-sector delegation”). Courts have held that “subdelegations to outside [nongovernmental] parties are assumed to be improper absent an affirmative showing of congressional authorization,” a limitation which this Note discusses more thoroughly in Part III. *U.S. Telecom Ass’n v. FCC*, 359 F.3d 554, 565 (D.C. Cir. 2004). However, previous challenges to the “constitutionality of [the SEC’s] delegation” of accounting rulemaking authority have been “without success.” Nagy, *supra*, at 987. For one example of such an unsuccessful challenge, see *Arthur Andersen & Co. v. SEC*, No. 76C-2832, 1978 WL 1073, at \*5 (N.D. Ill. Mar. 1978), where the court ruled that plaintiff accounting firm lacked standing to challenge the subdelegation because the firm failed to “allege harm from compliance [with an accounting principle promulgated by FASB] as well as the threat of legal sanctions from noncompliance.” This Note does not address the question of whether the SEC’s original delegation of authority to FASB was legally valid, given that Congress has finally given explicit statutory authorization for this delegation (despite the troubling sixty-four-year gap noted above). This Note addresses only the question of whether such a delegation to IASB would be valid.

31. William W. Bratton, *Private Standards, Public Governance: A New Look at the Financial Accounting Standards Board*, 48 B.C. L. REV. 5, 11–12 (2007).

32. *Id.* at 12.

33. *Id.*

The failure of the APB led the AICPA to conclude that “independence” and “better constituent representation” were required in a new standard-setter, and private negotiations led to the formation of FASB in 1973.<sup>34</sup> The SEC wasted little time in recognizing FASB as the new authorized accounting standard-setter.<sup>35</sup> Although the SEC retains the power to engage in accounting rulemaking itself, it seldom overrules or refuses to recognize FASB pronouncements or makes any substantive accounting pronouncements of its own.<sup>36</sup>

### B. *The History and Standard-Setting Procedures of FASB*

In 1973, FASB was organized under the direction of the Financial Accounting Foundation (FAF).<sup>37</sup> FAF was originally designated as the standard-setter successor to the APB, and FAF in turn delegated the standard-setting authority to a full-time, seven member board known as FASB.<sup>38</sup> This structure allowed FASB to “act more quickly” than the twenty-one member, part-time APB.<sup>39</sup> In delegating its standard-setting power to FASB, FAF gave FASB “no substantive mandate on which to draw in drafting standards,” but “left this constitutional task to the agency itself.”<sup>40</sup> As a result, “[t]he

---

34. *Id.* at 13.

35. *Id.* The SEC recognized FASB as the authorized standard-setter by stating that “principles, standards and practices promulgated by the FASB . . . will be considered by the Commission as having substantial authoritative support, and those contrary to such FASB promulgations will be considered to have no such support.” Statement of Policy on the Establishment and Improvement of Accounting Principles and Standards, Accounting Series Release No. 150, 1973 WL 149263, at \*2 (Dec. 20, 1973) [hereinafter Statement of Policy]. The phrase “substantial authoritative support” refers to Administrative Policy on Financial Statements, Accounting Series Release No. 4, [1937–1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 72,005, at 72,005 (Apr. 25, 1938), wherein the SEC stated that “[i]n cases where financial statements . . . are prepared in accordance with accounting principles for which there is no *substantial authoritative support*, such financial statements will be presumed to be misleading or inaccurate.” (emphasis added).

36. See Matthew J. Barrett, *The SEC and Accounting, in Part Through the Eyes of Pacioli*, 80 NOTRE DAME L. REV. 837, 868 & n.120 (2005) (providing an example of the SEC overruling FASB in its “approach to income recognition in the oil and gas industry,” but noting that after its recognition of FASB, the SEC “rarely exercised its powers to establish accounting principles directly”). The SEC does issue Staff Accounting Bulletins (SABs); however, “[s]tatements in SABs are not rules or interpretations of the Commission, nor are they published as bearing the Commission’s official approval,” but merely “provide[] the staff’s views” on various accounting principles. Press Release, U.S. Sec. & Exch. Comm’n, SEC Staff Releases Accounting Bulletin for Written Loan Commitments Recorded at Fair Value Under GAAP (Nov. 5, 2007), available at <http://www.sec.gov/news/press/2007/2007-225.htm>.

37. Fin. Accounting Found., Financial Accounting Foundation Overview, [http://www.fasb.org/faf/faf\\_info.shtml](http://www.fasb.org/faf/faf_info.shtml) (last visited Feb. 17, 2009).

38. Bratton, *supra* note 31, at 14.

39. *Id.*

40. *Id.* at 15.

early FASB responded with the Conceptual Framework, a series of [six] statements intended to provide a unified theoretical basis from which to articulate standards," a process which took twelve years to complete.<sup>41</sup>

FASB also adopted Rules of Procedure (often referred to as FASB's "due process") as a framework for its standard-setting process.<sup>42</sup> FASB claims that "[t]his process was modeled on the Federal Administrative Procedure Act and, in several respects, is more demanding."<sup>43</sup> Indeed, some scholars have agreed that in recent years "changes in FASB's procedures have further enshrined many of the norms and practices of administrative law within this body of private governance."<sup>44</sup> The process can be broken down into eight main steps, although "[n]ot all of the steps may be necessary" for every project, and "[m]any other steps are followed during the course of the project that are not specifically required by the Board's Rules of Procedure."<sup>45</sup> These steps include holding public board meetings, issuing "Exposure Drafts," soliciting public comments on these drafts, and voting by simple majority to issue new "Standards" or "Interpretations."<sup>46</sup>

In recent years, FASB has become increasingly concerned with the development of international accounting standards and its effect on U.S. capital markets and accounting practices, and FASB has consistently favored the development of one internationally recognized set of accounting standards.<sup>47</sup> In October 2002, FASB and IASB jointly released a memorandum of understanding known as the "Norwalk Agreement," which "mark[ed] a significant step toward formalizing their commitment to the convergence of U.S. and international accounting standards."<sup>48</sup> In this document, both organizations committed to developing "high-quality, compatible accounting standards that could be used for both domestic and cross-

41. *Id.* at 15 & n.103.

42. Fin. Accounting Standards Bd., FASB Due Process Steps Required by the Rules of Procedure, [http://www.fasb.org/facts/due\\_process.shtml](http://www.fasb.org/facts/due_process.shtml) (last visited Feb. 17, 2009) [hereinafter FASB Due Process].

43. FIN. ACCOUNTING STANDARDS BD., FACTS ABOUT FASB—THE MISSION OF THE FINANCIAL STANDARDS ACCOUNTING BOARD (2007), [http://www.fasb.org/facts/facts\\_about\\_fasb.pdf](http://www.fasb.org/facts/facts_about_fasb.pdf).

44. Walter Matzli & Tim Büthe, *Global Private Governance: Lessons from a National Model of Setting Standards in Accounting*, 68 LAW & CONTEMP. PROBS. 225, 239 (2005).

45. FASB Due Process, *supra* note 42.

46. *Id.*

47. See Robert H. Herz & Kimberley R. Petrone, *International Convergence of Accounting Standards: Perspectives from the FASB on Challenges and Opportunities*, 25 NW. J. INT'L L. & BUS. 631, 631–32 (2005) ("FASB has pursued international 'convergence' for almost half of its more than thirty year existence.").

48. Fin. Accounting Standards Bd., Convergence with the International Accounting Standards Board (IASB), [http://www.fasb.org/intl/convergence\\_iasb.shtml](http://www.fasb.org/intl/convergence_iasb.shtml) (last visited Feb. 17, 2009).

border financial reporting” and “mak[ing] their existing financial reporting standards fully compatible as soon as is practicable.”<sup>49</sup> In 2007, FASB Chairman Robert Herz told a Senate subcommittee that FASB agrees with the SEC that “a widely used single set of high quality international accounting standards for listed companies would benefit the global capital markets and investors,”<sup>50</sup> and FASB responded to an SEC request for public comment<sup>51</sup> by stating that “[i]nvestors would be better served if all U.S. public companies used accounting standards promulgated by a single global standard setter as the basis for preparing their financial reports,” but still preferring not to give companies a choice between U.S. GAAP and IFRS.<sup>52</sup>

### C. *The History and Standard-Setting Procedures of IASB*

Although IASB was created in 2001,<sup>53</sup> its history extends back to 1973 when its overseer, the International Accounting Standards Committee (IASC), was founded in London.<sup>54</sup> IASC was founded by the national accounting organizations of nine countries (including the U.S.<sup>55</sup>) as “a vehicle for harmonizing accounting practices throughout the world.”<sup>56</sup> “In the 1990s, the IASC shifted its focus from . . . harmonizing accounting standards throughout the world to . . . being the primary international accounting standard setter.”<sup>57</sup> However, in shifting its focus, the IASC, which had previously been comprised of members of the national accounting bodies of its member states,<sup>58</sup> had to choose between adopting “an independence model based on accounting standards set by highly qualified full-time individuals who

49. FIN. ACCOUNTING STANDARDS BD. & INT’L ACCOUNTING STANDARDS BD., MEMORANDUM OF UNDERSTANDING: “THE NORWALK AGREEMENT” 1 (2002), available at <http://www.fasb.org/news/memorandum.pdf>.

50. *International Accounting Standards: Opportunities, Challenges, and Global Convergence Issues: Hearing Before the Subcomm. on Securities, Insurance, and Investment of the S. Comm. on Banking, Housing, and Urban Affairs*, 110th Cong. 3 (2007) (statement of Robert H. Herz, Chairman, Financial Accounting Standards Board), available at [http://www.fasb.org/testimony/10-24-07\\_prepared\\_statement.pdf](http://www.fasb.org/testimony/10-24-07_prepared_statement.pdf).

51. 2007 Concept Release, *supra* note 6, at 45,601.

52. Letter from Robert E. Denham, Chairman, Fin. Accounting Found. & Robert H. Herz, Chairman, Fin. Accounting Standards Bd., to Nancy M. Morris, U.S. Sec. & Exch. Comm’n 2 (Nov. 7, 2007), [http://www.fasb.org/FASB\\_FAF\\_Response\\_SEC\\_Releases\\_msw.pdf](http://www.fasb.org/FASB_FAF_Response_SEC_Releases_msw.pdf).

53. INT’L ACCOUNTING STANDARDS BD., IASB AND THE ISAC FOUNDATION: WHO WE ARE AND WHAT WE DO, available at [http://www.iasb.org/NR/rdonlyres/OA5A767C-E7DE-49E5-8B12-499F62F8870C/0/WhoWeAre\\_Final12508.pdf](http://www.iasb.org/NR/rdonlyres/OA5A767C-E7DE-49E5-8B12-499F62F8870C/0/WhoWeAre_Final12508.pdf) [hereinafter IASB AND THE IASC FOUNDATION].

54. David S. Ruder et al., *Creation of World Wide Accounting Standards: Convergence and Independence*, 25 NW. J. INT’L L. & BUS. 513, 519 (2005).

55. IASB AND THE IASC FOUNDATION, *supra* note 53.

56. Ruder et al., *supra* note 54, at 519.

57. *Id.* at 528.

58. *Id.* at 526.

serve the public interest” and “a representativeness model based on an international organization composed of country representatives.”<sup>59</sup> The IASC chose a hybrid of both models, wherein the IASB would function as an independent body under the oversight of the IASC, which was to be geographically representative.<sup>60</sup> The organization of the IASB as the new international standard-setter was completed on April 1, 2001.<sup>61</sup> The IASB consists of twelve full-time and two part-time members whom the IASC chooses by virtue of “professional competence and practical experience” and who are required to “meet appropriate guidelines of independence.”<sup>62</sup> Unlike FASB, which is funded through the collection of fees from securities issuers, IASB is a privately funded organization.<sup>63</sup> Since its inception, IASB’s promulgation of IFRS has been well-received, as “[n]early 100 countries now require or permit the use of IFRSs or are converging with the International Accounting Standards Board’s (IASB) standards.”<sup>64</sup>

Although not identical to the “due process” system of FASB’s, the IASB’s process is quite similar. The procedure for introducing a new IFRS is broken down into six steps: (1) “Setting the agenda,” or determining which projects IASB will take on; (2) “Project planning,” including working jointly with other standard-setting organizations; (3) “Development and publication of a discussion paper” as “a vehicle to explain the issue and solicit early comments from constituents”; (4) “Development and publication of an exposure draft,” “IASB’s main vehicle for consulting the public”; (5) “Development and publication of an IFRS,” containing revisions after public comments have been received; and (6) “Procedures after an IFRS is issued,” including

---

59. *Id.* at 519.

60. *Id.* at 520.

61. IASB AND THE IASC FOUNDATION, *supra* note 53.

62. International Accounting Standards Committee Foundation Constitution ¶¶ 18–19, June 21, 2005, available at <http://www.iasb.org/NR/rdonlyres/1904AEEE-3554-49C6-BD96-A4611A6964BE/0/IASCFoundationConstitution2.pdf>.

63. Int’l Accounting Standards Bd., Funding, <http://www.iasb.org/About+Us/About+the+IASC+Foundation/Funding.htm> (last visited Feb. 17, 2009); see also 2007 Concept Release, *supra* note 6, at 45,604 (acknowledging IASB’s “privately funded” status).

64. Int’l Accounting Standards Bd., IFRSs Around the World, <http://www.iasb.org/About+Us/About+the+IASB/IFRSs+around+the+world.htm> (last visited Feb. 17, 2009). Among the countries currently utilizing IFRS are all member states of the European Union. See 2007 Concept Release, *supra* note 6, at 45,602 (“The European Union . . . has, under a regulation adopted in 2002, required companies incorporated in its Member States and whose securities are listed on an EU-regulated market to report their consolidated financial statements using endorsed IFRS beginning in 2005.”).

review of its application.<sup>65</sup> Not all of these steps are mandatory in every IASB project.<sup>66</sup>

IASB has made a relationship with FASB and the convergence of U.S. and international accounting standards one of its top priorities.<sup>67</sup> The current IASB agenda is structured around the agency's commitment to convergence with U.S. GAAP,<sup>68</sup> and IASB has decided not to require companies to apply new IFRS, or amendments to existing IFRS, until 2009<sup>69</sup> (SEC Chairman Cox's previously stated target year for eliminating the reconciliation requirement from IFRS to U.S. GAAP).<sup>70</sup>

The validity of any recognition by the SEC of accounting standards promulgated by IASB as binding under federal securities law is subject to two potential limitations: the limitations on an administrative agency's ability to subdelegate its own authority, and the U.S. government's ability to delegate its authority to an international organization.<sup>71</sup>

---

65. INT'L ACCOUNTING STANDARDS COMM. FOUND., *DUE PROCESS HANDBOOK FOR THE IASB 7-13* (2006), available at <http://www.iasb.org/NR/rdonlyres/7D97095E-96FD-4F1F-B7F2-366527CB4FA70/DueProcessHandbook.pdf>.

66. Compare *id.* at 10 (“[A] discussion paper is not a mandatory step in . . . due process.”), with *id.* at 11 (“Publication of an exposure draft is a mandatory step in due process.”).

67. See Int'l Accounting Standards Bd., Memorandum of Understanding with the FASB, <http://www.iasb.org/Current+Projects/Memorandum+of+Understanding+with+the+FASB.htm> (last visited Feb. 17, 2009) (“A common set of high quality global standards remains the long-term strategic priority of both the FASB and the IASB.”).

68. See Int'l Accounting Standards Bd., IASB Work Plan, <http://www.iasb.org/Current+Projects/IASB+Projects/IASB+Work+Plan.htm> (last visited Feb. 17, 2009) (“The Work Plan . . . reflects the objectives of the Memorandum of Understanding with the FASB . . .”).

69. Press Release, Int'l Accounting Standards Bd., IASB Takes Steps to Assist Adoption of IFRSs and Reinforce Consultation—No New IFRSs Effective Until 2009 (July 24, 2006), available at <http://www.iasb.org/News/Press+Releases/IASB+takes+steps+to+assist+adoption+of+IFRSs+and+reinforce+consultation+No+new+IFRSs+effective+until.htm>.

70. Cox-McCreavy Statement, *supra* note 8.

71. See U.S. Telecom Ass'n v. FCC, 359 F.3d 554, 566 (D.C. Cir. 2004) (noting that “general delegation of decision-making authority to a federal administrative agency does *not*, in the ordinary course of things, include the power to subdelegate that authority beyond federal subordinates”); *infra* Part IV.A.

### III. SUBDELEGATION

#### A. General Limitations on the Ability of Government Branches and Agencies to Subdelegate Their Authority to Private Parties

##### 1. Delegation and Subdelegation in Administrative Law

Courts have long recognized that Congress cannot abdicate or delegate to another governmental branch or entity its “essential legislative functions,”<sup>72</sup> a prohibition known as the “nondelegation doctrine.”<sup>73</sup> That prohibition, however, does not prevent Congress from “obtaining the assistance of its coordinate Branches.”<sup>74</sup> Indeed, to date, the U.S. Supreme Court has found a delegation of congressional power excessive and in violation of the nondelegation doctrine in only two cases, both in 1935.<sup>75</sup> “[I]n our increasingly complex society, replete with ever changing and more technical problems, Congress simply cannot do its job absent an ability to delegate power under broad general directives.”<sup>76</sup> Therefore, Congress may delegate authority short of purely legislative authority, usually either to Cabinet-level Executive departments or to administrative agencies, by “lay[ing] down . . . an intelligible principle” which guides an agency in its exercise of the delegated authority.<sup>77</sup> Generally, all agency activities are classified as either rulemaking or adjudicatory in nature.<sup>78</sup> An agency’s exercise of its rulemaking and adjudicatory authority is governed primarily by the Administrative Procedures Act (APA).<sup>79</sup>

Once Congress has made a valid delegation of authority, the empowered department or agency can often further delegate that authority, an action known as “subdelegation.” Perhaps the most common form of subdelegation occurs when an agency that has been given specific authority by Congress allows an individual employee or division of the agency to exercise that authority on the entire agency’s behalf.<sup>80</sup> That an agency may make such a subdelegation seems only

72. *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495, 529 (1935).

73. *Touby v. United States*, 500 U.S. 160, 165 (1991).

74. *Mistretta v. United States*, 488 U.S. 361, 372 (1989).

75. *Whitman v. Am. Trucking Ass’n*, 531 U.S. 457, 474 (2001). Those two cases were *A.L.A. Schechter Poultry Corp.*, 295 U.S. at 541–42, and *Panama Refining Co. v. Ryan*, 293 U.S. 388, 430–33 (1935).

76. *Mistretta*, 488 U.S. at 372.

77. *Am. Trucking Ass’n*, 531 U.S. at 472.

78. William D. Araiza, *Agency Adjudication, the Importance of Facts, and the Limitations of Labels*, 57 WASH. & LEE L. REV. 351, 357 (2000).

79. Rulemaking activities are governed by 5 U.S.C. § 553 (2007), and adjudicatory activities are governed by 5 U.S.C. § 554 (2007).

80. See Securities Exchange Act of 1934 § 4A(a), 15 U.S.C. § 78d–1(a) (2008) (allowing the SEC to “delegate . . . any of its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee

logical because part of Congress's intent in delegating some of its power to an agency is to promote governmental efficiency.<sup>81</sup> Achieving such efficiency would be impossible if the entirety of the agency were required to make every decision and take every action. Indeed, "[w]hen a statute delegates authority to a federal officer or agency, subdelegation to a subordinate federal officer or agency is presumptively permissible absent affirmative evidence of a contrary congressional intent," even without a statutory provision explicitly authorizing the subdelegation.<sup>82</sup>

Different questions arise, however, when an agency subdelegates its power not to a subordinate, but to a nongovernmental actor. These questions might involve: (1) the fairness and impartiality of the actor exercising the subdelegated authority; (2) the reasons that the agency gave in justifying its subdelegation; (3) the factors that the agency considered in choosing a private actor to whom to subdelegate its authority; and (4) the efficiency with which the agency and the private actor work, both in establishing the original subdelegation and in the exercise of the authority once the original subdelegation is complete. Although many of these concerns might be considered purely practical, scholars have questioned whether these kinds of relationships might also pose constitutional problems.<sup>83</sup>

## 2. *U.S. Telecom Ass'n v. FCC*: Legal Limitations on Subdelegation

The D.C. Circuit's 2004 decision in *U.S. Telecom Association v. Federal Communications Commission* is perhaps the most important recent decision regarding the limitations on the ability of a government agency to subdelegate its authority to nongovernmental actors. *U.S. Telecom* involved efforts by the Federal Communications Commission (FCC) to increase competition in telecommunication markets by requiring "incumbent" local telephone companies to make their "network elements" available to companies who wished to

---

board"); *Touby v. United States*, 500 U.S. 160, 169 (1991) (upholding a delegation by the Attorney General to the Drug Enforcement Agency, an agency within the Department of Justice, of the Attorney General's power to define specific drugs as "controlled substances" for purposes of federal criminal law).

81. See Evan J. Criddle, *Fiduciary Foundations of Administrative Law*, 54 UCLA L. REV. 117, 121 (2006) ("[A]gency discretion may enhance the efficiency and responsiveness of public governance . . .").

82. *U.S. Telecom Ass'n v. FCC*, 359 F.3d 554, 565 (D.C. Cir. 2004).

83. See Jody Freeman, *Collaborative Governance in the Administrative State*, 45 UCLA L. REV. 1, 83–84 (1997) ("Institutional arrangements that empower private groups to make public policy might be unconstitutional at worst, and corrode legitimacy at best."); Jim Rossi, *Antitrust Process and Vertical Deference: Judicial Review of State Regulatory Inaction*, 93 IOWA L. REV. 185, 223 (2007) ("Administrative law has long recognized . . . that delegations of authority to private entities also present a unique set of problems—bordering, at some level, on the unconstitutional.").



compete with the incumbents, a process known as “unbundling.”<sup>84</sup> In deciding which network elements were to be made available to potential competitors in the unbundling process, a federal statute directed the FCC to “consider, at a minimum, whether . . . the failure to provide access to such network elements would *impair* the ability” of the potential competitor to provide the services it sought to provide.<sup>85</sup> However, because the question of impairment was necessarily linked to the unique characteristics of individual markets,<sup>86</sup> the FCC adopted a rule allowing state regulatory commissions, under certain circumstances, to make determinations regarding which network elements new competitors should have access to “under a purported delegation of the [FCC’s] own authority.”<sup>87</sup> Several incumbent local telephone companies appealed the FCC’s order as contrary to previous directives the D.C. Circuit had given to the FCC.<sup>88</sup>

On review, the D.C. Circuit held that “the [FCC’s] subdelegation of authority to the state commissions” was unlawful.<sup>89</sup> The court held that whereas subdelegations of administrative authority to federal subordinates carry a presumption of validity, no such presumption exists where the subdelegation is made to an actor outside of the federal government; in such a case, the validity of the subdelegation requires “an affirmative showing of congressional authorization.”<sup>90</sup> The court described this distinction as “entirely sensible”:

When an agency delegates authority to its subordinate, responsibility—and thus accountability—clearly remain with the federal agency. But when an agency delegates power to outside parties, lines of accountability may blur, undermining an important democratic check on government decision-making. . . . Also, delegation to outside entities increases the risk that these parties will not share the agency’s “national vision and perspective,” . . . and thus may pursue goals inconsistent with those of the agency and the underlying statutory scheme.<sup>91</sup>

The court also rejected the FCC’s argument that its decision to subdelegate to the state regulatory commissions deserved *Chevron* deference because “[a] general delegation of decision-making authority to a federal administrative agency does *not*, in the ordinary

---

84. *U.S. Telecom Ass’n*, 359 F.3d at 561.

85. *Id.* (citing 47 U.S.C. § 251(d)(2) (2004)).

86. *Id.* at 562.

87. *Id.* at 563.

88. *Id.* at 564.

89. *Id.* at 564–65.

90. *Id.* at 565.

91. *Id.* at 565–66.

course of things, include the power to subdelegate that authority beyond federal subordinates.”<sup>92</sup>

The D.C. Circuit’s decision in *U.S. Telecom* emphasized the importance of maintaining some semblance of democracy and “representativeness” in the actions taken by administrative agencies—bodies which have long been criticized as inherently undemocratic.<sup>93</sup> Placing limits on an agency’s ability to subdelegate its authority works to minimize “conflicts of interest” and simultaneously ensures that “oversight and review” of the establishment of binding agency policy remain within the agency<sup>94</sup> and with individuals within the agency who are politically accountable (or at least more so than members of a private body to whom authority would be subdelegated).

### B. *Recognition of Industry Standards Established by a Nongovernmental Entity as a Form of Subdelegation*

Given the limitations on private actor subdelegation articulated in *U.S. Telecom*, defining “subdelegation” becomes a vital task. In the context of the SEC, FASB, and accounting rulemaking authority, the question could be phrased as such: Does the recognition of industry standards by an administrative agency constitute a subdelegation of that agency’s authority? There are at least three good reasons to answer that question in the affirmative, at least with regards to the SEC’s recognition of accounting standards promulgated by FASB, and, by extension, any subsequent recognition of IFRS promulgated by IASB.

---

92. *Id.* at 566. The term “Chevron deference” is derived from *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844 (1984), where the Court stated that “a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency,” thus showing deference to the agency’s interpretations of the statutes which guide and empower it.

93. *See, e.g.*, Edward L. Rubin, *Getting Past Democracy*, 149 U. PA. L. REV. 711, 711–12 (2001) (“In contemporary constitutional and administrative law scholarship, the bureaucracy has been viewed as . . . an abandonment of our democratically based commitments to popular sovereignty and public accountability.”).

94. Brenda Lindlief Hall, *Subdelegation of Authority Under the Endangered Species Act: Secretarial Authority to Subdelegate His Duties to a Citizen Management Committee as Proposed for the Selway-Bitterroot Wilderness Grizzly Bear Reintroduction*, 20 PUB. LAND & RESOURCES L. REV. 81, 92 (1999).

1. Recognition of Externally Created Accounting Standards as a Subdelegation of the SEC's Authority
  - a. "Passing of Power"

The first ground for defining the SEC's recognition of the validity of FASB's accounting standards as a subdelegation is that the relationship constitutes the kind of "passing of power" inherent in any agency delegation or subdelegation.<sup>95</sup> To understand the concept of delegation as a "passing of power," it is necessary first to understand that, at least with regards to the exercise of rulemaking authority,<sup>96</sup> an agency only possesses and can only exercise as much power as is originally delegated to it by Congress.<sup>97</sup> This initial "passing of power" from Congress to the administrative agency is then analogous to any subsequent transfer of authority by the agency to a third party. Just as the agency's exercise of authority is bounded by Congress's original grant, a third party's exercise of that same authority is bounded by the agency's subsequent grant.

If an agency delegation or subdelegation is primarily characterized by a "passing of power," then a recognition by the SEC that accounting standards promulgated by either FASB or IASB are binding under U.S. securities law certainly qualifies. The SEC was originally granted authority by Congress to create substantive accounting rules in the '33 Act.<sup>98</sup> Therefore, any authority on the part of FASB or IASB to promulgate such binding accounting rules would necessarily be derived from a "passing of power" by the SEC.<sup>99</sup>

---

95. I am indebted to Professor Lisa Bressman of Vanderbilt University Law School for this formulation of the principle behind agency delegation. It is important to note here that the words "delegation" and "subdelegation" may be used interchangeably to describe the assignment of authority from the agency to the third party, given that many other scholars and authors have used the terms interchangeably.

96. The Administrative Procedure Act defines rulemaking as "agency process for formulating, amending, or repealing a rule." 5 U.S.C. § 551(5) (2007). A rule is defined as "the whole or a part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy." *Id.* § 551(4). Thus, rulemaking has been described as a "quasi-legislative activity." *Morrison v. Olson*, 487 U.S. 654, 725 (1988) (Scalia, J., dissenting). Accounting standards promulgated by FASB and recognized as authoritative by the SEC certainly seem to fit the APA definition of a rule, as they are of "general . . . applicability" as to issuers of securities and are designed to "implement, interpret, or prescribe" federal securities law. 5 U.S.C. § 551(4).

97. *Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 208 (1988).

98. See *supra* notes 1, 25 and accompanying text.

99. Interestingly, nowhere in the SEC's original recognition of FASB as the authorized accounting standard-setter for purposes of federal securities law does the SEC actually use the terms "delegate" or "delegation." Statement of Policy, *supra* note 35. In fact, in a later release, the SEC explicitly stated that "[t]he Commission's policy recognizes that the FASB operates to establish accounting standards, but it does not involve a delegation of the Commission's substantive rulemaking authority to the

The fact that accounting standards promulgated by FASB currently have the force of law, at least as to companies required to make periodic filings under federal securities law,<sup>100</sup> is evidenced by the fact that “[t]he SEC has enforced [the federal securities laws] in thousands of administrative proceedings and hundreds of federal court cases asserting violations of GAAP.”<sup>101</sup>

#### b. Previous Scholarly Work

The second reason, perhaps not controlling but still worth considering, for defining the SEC-FASB relationship (as well as the newly created SEC recognition of IFRS as created by IASB) as a subdelegation is the fact that many legal scholars over the years have characterized the recognition of FASB accounting standards as a delegation by the SEC.<sup>102</sup> In fact, some scholars have gone so far as to imply that such a delegation constitutes a dereliction of the SEC’s duty to effectively regulate U.S. capital markets.<sup>103</sup> Although making such a judgment falls beyond the scope of this Note, there seems to be some consensus among scholars familiar with these issues that the SEC has delegated at least some portion of its authority to FASB.

#### c. Comparisons to Other Delegations

The third reason for finding that the SEC-FASB, and the new SEC-IASB, recognition constitutes a delegation of the SEC’s rulemaking authority is that the relationship between the two parties is at least somewhat analogous to similar relationships in other areas

---

FASB.” Accounting Practices—Oil and Gas Producers, Solicitation of Comments, Securities Act Release No. 5892, Exchange Act Release No. 20,337, Investment Act Release No. 14,305 (Dec. 22, 1977).

100. See Securities Exchange Act of 1934 § 13(a), 15 U.S.C. § 78m(a) (2008) (requiring issuers of securities registered with the SEC to provide annual and quarterly reports “as the Commission may prescribe”).

101. Lawrence A. Cunningham, *Private Standards in Public Law: Copyright, Lawmaking and the Case of Accounting*, 104 MICH. L. REV. 291, 292 (2005). Some argue that the accounting principles which comprise GAAP are not laws but merely “business practices.” Alan Rappeport, *Marketing GAAP: Unlike FASB’s Avatars, International Financial Reporting Standards May Be Catching on Because Their Creators Are Super Sellers*, CFO, Jan. 11, 2008, <http://www.cfo.com/article.cfm/10519396?f=search>. However, given the SEC’s propensity for instituting litigation or administrative action as a result of GAAP violations by public companies, as noted in Cunningham *supra*, it is clear that no matter how GAAP is defined, the SEC imposes serious legal consequences on public companies who diverge from GAAP’s prescribed standards.

102. See, e.g., Bratton, *supra* note 31, at 27; Nagy, *supra* note 30, at 985 (using the term “delegate” to describe the SEC’s recognition of FASB and previous accounting standard-setters).

103. See George Mundstock, *The Trouble with FASB*, 28 N.C. J. INT’L L. & COM. REG. 813, 825 (2003) (referring to the SEC’s decision to recognize industry-established accounting standards as “[throwing] in the towel”).

of administrative law that have been characterized as delegations. Most notably, the relationship bears a striking resemblance to the delegation of authority the Supreme Court found excessive and thus unconstitutional in *A.L.A. Schechter Poultry Corp.*<sup>104</sup> In *Schechter*, Congress had called for the creation of “codes of fair competition” to be created by the President under the National Industrial Recovery Act.<sup>105</sup> The President’s code for the poultry industry provided for the establishment of an “‘industry advisory committee,’ to be selected by trade associations and members of the industry” in order to assist in the administration of the code.<sup>106</sup> In declaring the delegation of congressional authority excessive, the Court queried, “[W]ould it be seriously contended that Congress could *delegate* its legislative authority to trade or industrial associations or groups so as to empower them to enact the laws they deem to be wise and beneficent for . . . their trade or industries?”<sup>107</sup>

This Note does not argue that *Schechter* dictates that the promulgation of binding accounting rules by FASB should be held unconstitutional or an excessive delegation of legislative authority. The problem in *Schechter* was not that a delegation was made to an industrial committee, but that the delegation was overbroad and constituted a transfer of purely legislative authority which only Congress can exercise.<sup>108</sup> The critical point that *Schechter* makes for the purpose of this Note is that the President’s (and, by extension, Congress’) recognition of standards created by a trade or industry group was in fact a delegation.<sup>109</sup>

## 2. Delegation vs. Incorporation

However, not all agency recognition of industry standards could properly be referred to as a “delegation” or “subdelegation”; in many cases, such recognition would more correctly be labeled as “incorporation.”<sup>110</sup> One case that involved such an incorporation by a government agency, and that can be distinguished in several ways from the relationship between SEC and FASB, is *Noblecraft Industries, Inc. v. Secretary of Labor*.<sup>111</sup> In *Noblecraft*, lumber processors appealed citations by the Occupational Safety and Health

104. See *supra* text accompanying notes 72–73, 76.

105. *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495, 521–22 (1935).

106. *Id.* at 524.

107. *Id.* at 537 (emphasis added).

108. See *supra* notes 72, 75 and accompanying text.

109. *Schechter*, 295 U.S. at 537.

110. See *Hurt v. Coyne Cylinder Co.*, 956 F.2d 1319, 1324 (6th Cir. 1992) (referring to adoption by U.S. Department of Transportation of industry standards published by the Compressed Gas Association as “incorporation”).

111. *Noblecraft Indus., Inc. v. Sec’y of Labor*, 614 F.2d 199 (9th Cir. 1980).

Administration (OSHA) for violations of various safety standards.<sup>112</sup> The standards, promulgated by the American National Standards Institute (ANSI), were adopted by the Secretary as “national consensus standard[s]” as authorized by applicable federal law.<sup>113</sup> On review, the Ninth Circuit upheld the standards against a challenge to their validity, stating that OSHA’s recognition of the standards did not constitute an “undue delegation of power.”<sup>114</sup>

There are two important factors which distinguish OSHA’s acceptance of the ANSI standard in *Noblecraft*, which could correctly be considered one of “incorporation,”<sup>115</sup> from the SEC’s acceptance of accounting standards promulgated by FASB (or, given recent developments, IASB). First, the court in *Noblecraft* explicitly stated that OSHA “selected among the ANSI standards with apparent discrimination.”<sup>116</sup> In contrast, not only has the SEC officially recognized as authoritative essentially all of the accounting standards promulgated by FASB since its inception in 1973,<sup>117</sup> but the SEC’s recognition of FASB as an authorized standard-setter essentially grants authoritative status to FASB pronouncements prospectively.<sup>118</sup> Second, the *Noblecraft* court noted that in accepting the ANSI standard, the Secretary of Labor “did not comply with the notice and hearing provisions of the Administrative Procedure Act” only because the statute directing the Secretary to adopt “national consensus standard[s]” authorized him to do so without following

---

112. *Id.* at 201.

113. *Id.* at 202.

114. *Id.* at 203.

115. There seems to be no widely recognized legal definition for “incorporation” in the context of a government agency adopting an industry standard for official use. Although *Hurt*, 956 F.2d 1319, is short on details, the “incorporation” discussed in *Hurt* seems to have involved (1) an industry standard promulgated primarily for industry as opposed to governmental use that was (2) adopted for governmental use through statutorily prescribed rulemaking procedures. For an example of the Department of Transportation’s process of incorporating industry standards, as in *Hurt*, see Rules and Regulations, Department of Transportation, Pipeline and Hazardous Materials Safety Administration, 73 Fed. Reg. 4699, 4700 (Jan. 28, 2008) (containing a final rule “[u]pdating provisions incorporating consensus standards issued by the . . . Compressed Gas Association,” the standard-setting body in *Hurt*, in response to a “notice of proposed rulemaking” issued by the Department). *Noblecraft* also involved the two elements noted above.

116. *Noblecraft*, 614 F.2d at 203.

117. See *supra* note 35 and accompanying text. Here it should be noted that FASB does not promulgate GAAP in its entirety, as there are other bodies (including the SEC and the accounting standard-setters which predated FASB) that are or were involved in the development of the body of accounting standards properly known as GAAP. *Bolt v. Merrimack Pharm., Inc.*, 503 F.3d 913, 917 n.6 (9th Cir. 2007). However, FASB pronouncements in some form or another are found in all of the “five categories in the GAAP hierarchy” established by the American Institute of Certified Public Accountants. *Id.*

118. Statement of Policy, *supra* note 35, at 1.

normal APA requirements.<sup>119</sup> The court's statement suggests that without statutory authorization to circumvent regular notice-and-comment requirements, any "incorporation" of industry standards by an agency must be done in accordance with these requirements. However, the SEC does not utilize APA-required notice-and-comment procedures when it accepts a new FASB accounting standard as authoritative.<sup>120</sup> And despite the fact that FASB follows its own relatively stringent set of due process standards in developing new accounting rules,<sup>121</sup> there is no indication that the SEC can assign or outsource to FASB the undertaking of any rulemaking procedures the APA would impose upon the SEC.<sup>122</sup> This seems to indicate that the SEC has simply delegated its rulemaking authority to FASB, as opposed to viewing FASB promulgations as recommendations or submissions and then "incorporating" them through regular notice-and-comment procedures.

---

119. *Noblecraft*, 614 F.2d at 202. Under most circumstances, the APA dictates that when agencies engage in rulemaking activities, they must observe such procedural requirements as publishing notice of proposed rulemaking in the Federal Register and "giv[ing] interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments." 5 U.S.C. § 553(b)–(c) (2008). This process is known as "notice-and-comment rulemaking." *United States v. Mead Corp.*, 533 U.S. 218, 230 (2001).

120. See General Revision of Regulation S-X, Securities Act Release No. 6233, Exchange Act Release No. 17,116, Investment Company Act Release No. 11,325, 20 SEC Docket 1356 (Sept. 2, 1980) (contrasting the possibility of an SEC "decision to require a particular method of accounting through rulemaking" with "the basic policy of relying on the FASB for leadership in establishing financial accounting and reporting standards").

121. See *supra* notes 42–46 and accompanying text.

122. There seems to be no statutory language, either in the '33 Act (giving the SEC authority to promulgate substantive accounting rules) or in the Sarbanes-Oxley Act (allowing the SEC to recognize an outside standard-setter), which would allow the SEC either to disregard or to outsource its APA-dictated rulemaking requirements. The best argument for such a stance would be that Sarbanes-Oxley allows the SEC to "recognize" accounting standards issued by an authorized standard-setter as "generally accepted" and makes no mention of regular notice-and-comment or other rulemaking procedures, but this argument is hardly convincing. Securities Act of 1933 § 19(b), 15 U.S.C. § 77s(b) (2009). Generally, cases such as *A.L.A. Schechter Poultry Corp.* and *U.S. Telecom Ass'n* seem to suggest the opposite view—that the ability to delegate powers and responsibilities normally possessed by the federal government to private parties would result in a dearth of public accountability. See Jody Freeman, *Extending Public Law Norms Through Privatization*, 116 HARV. L. REV. 1285, 1304 (2003) ("Public law scholars worry that privatization may enable government to avoid its traditional legal obligations, leading to an erosion of public law norms and a systematic failure of public accountability."). Again, it is important to note that questions regarding the validity of the SEC's current delegation to FASB are beyond the scope of this Note, except to the extent that a delegation to IASB poses similar questions.

C. *Specific Limitations on the SEC's Ability to Subdelegate Accounting Rulemaking Authority*

If the SEC's recognition of accounting standards established by outside bodies is a subdelegation of its authority to create substantive accounting rules under the '33 Act, then the SEC's ability to make such subdelegations must be subject to certain limitations. The most important limitation is emphasized in *U.S. Telecom*: the SEC cannot subdelegate its authority to a private party absent express Congressional authorization.<sup>123</sup>

In the Sarbanes-Oxley Act of 2002, Congress set forth six criteria that an organization must meet before the SEC can deem accounting standards promulgated by that organization authoritative.<sup>124</sup> Soon after the Sarbanes-Oxley Act was signed into law, and after FASB made changes to its own funding mechanism,<sup>125</sup> the SEC found that FASB met these six criteria and reaffirmed FASB's status as the preeminent accounting standard-setter.<sup>126</sup> Looking forward, a vital question should now be asked: Does the IASB meet all six necessary criteria? Currently, the answer appears to be no.

IASB definitely falls short of at least one of the standards set by Congress in the Sarbanes-Oxley Act: that an organization promulgating accounting standards must be publicly funded. The SEC acknowledges that IASB has been funded "largely through voluntary contributions from companies, accounting firms, international organizations and central banks."<sup>127</sup> In the context of promulgating rules which can be binding on a wide swath of private actors in all parts of the world, the problem with such a financing scheme is that "[p]rivate funding can create real or apparent conflicts, if donors contribute believing the board will return the favor by passing accounting standards that they prefer. [Sarbanes-Oxley's] funding provision eliminated that problem for FASB. Recognizing IASB despite that problem reintroduces a concern that Congress sought to eliminate."<sup>128</sup> The requirement for public funding is particularly noteworthy because at the time the Sarbanes-Oxley Act

---

123. See *supra* text accompanying notes 89–92.

124. See *supra* text accompanying notes 26–29.

125. Previously, FAF was responsible for funding FASB, and the change to public funding was made pursuant to Sarbanes-Oxley. Commission Statement of Policy Reaffirming the Status of the FASB as a Designated Private-Sector Standard Setter, Securities Act Release No. 8221, Exchange Act Release No. 47,743, Investment Company Act Release No. 26,028, 68 Fed. Reg. 23,333, 23,335 (May 1, 2003) [hereinafter FASB Status Statement].

126. *Id.* at 23,334.

127. 2007 Concept Release, *supra* note 6, at 45,605.

128. Letter from Lawrence A. Cunningham, Professor of Law, George Washington Univ., to Sec. & Exch. Comm'n 4 (Aug. 10, 2007), <http://www.sec.gov/comments/s7-20-07/s72007-1.pdf> [hereinafter Cunningham Letter].



was passed, this was the only requirement that FASB did not already meet under its pre-existing structure.<sup>129</sup> Thus, it would seem that the potential for such conflicts of interest would cripple the hopes of any organization that wished to be recognized as an authoritative standard-setter under Sarbanes-Oxley.<sup>130</sup>

Another of the six Sarbanes-Oxley criteria which IASB may or may not meet is that a standard-setting body must be “capable of improving the accuracy and effectiveness of financial reporting and the protection of investors under the securities laws.”<sup>131</sup> This seems to be a factual determination which the SEC itself must make on a case-by-case basis.<sup>132</sup> It does, however, seem potentially troubling that the SEC itself, as opposed to Congress, has the final say as to whether a standard-setting body can assist the SEC in its “mission . . . to protect investors.”<sup>133</sup> This is particularly true where the SEC itself recognizes that its “relationship with the IASB . . . is different *and less direct than* [its] oversight role with the FASB.”<sup>134</sup> Yet another criterion which IASB might not currently meet, but which seems less consequential, is that changes to accounting principles are adopted by a “majority vote of [the body’s] members.”<sup>135</sup> While this seems to imply a simple majority, IASB currently approves new accounting standards only by a 9/14 supermajority.<sup>136</sup>

The fact that IASB currently fails to meet one or more of the six criteria set out in the Sarbanes-Oxley Act would seem unavoidably fatal to its efforts to secure authorized status as a standard-setter from the SEC. However, given that these six criteria were “nearly tailor made for FASB”<sup>137</sup> (with the one exception of the public funding requirement), yet another question seems to arise: Did Congress actually intend that any organization meeting these six criteria be

129. Lawrence A. Cunningham, *The SEC’s Global Accounting Vision: A Realistic Appraisal of a Quixotic Quest*, 87 N.C. L. REV. 1, 28–29 (2008) [hereinafter Cunningham, *SEC’s Global Accounting Vision*].

130. See *Sierra Club v. Sigler*, 695 F.2d 957, 962 n.3 (5th Cir. 1983) (“[A]n agency may not delegate its public duties to private entities, . . . particularly private entities whose objectivity may be questioned on grounds of conflict of interest.”).

131. Securities Act of 1933 § 19(b)(1)(B), 15 U.S.C. § 77s(b)(1)(B) (2008).

132. Cunningham Letter, *supra* note 128, at 4. The statutory provision explicitly states that the SEC is to make the determination whether a standard-setting body meets this criterion. 15 U.S.C. § 77s(b)(1)(B) (2008).

133. U.S. Securities and Exchange Commission, *The Investor’s Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, <http://www.sec.gov/about/whatwedo.shtml> (last visited Feb. 17, 2009).

134. 2007 Concept Release, *supra* note 6, at 45,605 (emphasis added).

135. 15 U.S.C. § 77s(b)(1)(A)(iv) (2008).

136. Cunningham Letter, *supra* note 128, at 3 n.4. There is a good argument that the supermajority voting rule is not so trivial, because “[t]he voting rule influences the standard setting process and the probability that the body will have the capacity to respond quickly and independently to emerging accounting issues.” Cunningham, *SEC’s Global Accounting Vision*, *supra* note 129, at 22.

137. Cunningham, *SEC’s Global Accounting Vision*, *supra* note 129, at 21.

recognizable by the SEC, or did Congress specifically have FASB in mind when it set out these criteria? Given some of the legislative history behind the Sarbanes-Oxley Act, it seems that Congress intended that FASB was to be the standard-setter the SEC officially recognized:

Since 1973, the SEC has generally required public companies operating in the United States to prepare their financial statements in accordance with 'principles, standards, and practices' promulgated by the Financial Accounting Standards Board . . . . [The Sarbanes-Oxley Act] seeks to formalize the SEC's reliance on the FASB . . . .<sup>138</sup>

Thus, even in the event that IASB did meet all six of the criteria laid down in the Sarbanes-Oxley Act, it is unclear that Congress actually intended to authorize the SEC to recognize any standard-setting body other than FASB.

Given IASB's failure to meet all of the conditions necessary to be recognized as an authoritative accounting standard-setter in the U.S., and given Congress's apparent intent that FASB was to be the sole standard-setter recognized by the SEC,<sup>139</sup> it appears that the SEC does not currently possess the necessary statutory authorization under *U.S. Telecom* to delegate accounting rulemaking authority to IASB by recognizing IFRS as authoritative under the federal securities laws. The cure for this problem is simple: if Congress agrees with the SEC's position that "having a widely used single set of high quality globally accepted accounting standards . . . could benefit . . . investors,"<sup>140</sup> Congress can by statute expressly authorize the SEC to recognize IASB as an authoritative standard-setter, either on the condition that they meet the six criteria set out in the Sarbanes-Oxley Act or by scrapping or adjusting one or more of these six criteria. However, even if Congress should give such express authorization, one potential problem remains: Congress still would be delegating some of its own authority to an internationally-based organization to oversee U.S. capital markets and to protect investors in those markets.

---

138. S. REP. NO. 107-205, at 12–13 (2002).

139. *Id.* But see FASB Status Statement, *supra* note 125, at 23,333 n.5 (expressing the SEC's position that the Sarbanes-Oxley Act "does not limit the number of private-sector bodies the Commission may recognize").

140. 2007 Concept Release, *supra* note 6, at 45,604.

## IV. INTERNATIONAL DELEGATION

A. *Constitutional Limitations on Delegations of Power to International Organizations*

Although not an entirely new phenomenon, the concept of nations delegating a portion of their authority or sovereignty to an international organization seems recently to have gained increasing momentum.<sup>141</sup> Considering the trend in this direction, it may as yet be impossible to ascertain or predict all of the complexities which are or may be associated with such delegations. However, it is essential to explore the positives and negatives associated with international delegations if the full effect of the potential acceptance of IFRS in the U.S. is to be determined.

At this point, it may be helpful to define the term "international delegation." Bradley and Kelley define an "international delegation" as "a grant of authority by two or more states to an international body to make decisions or take actions,"<sup>142</sup> and Swaine defines "delegat[ions] to international institutions" as "vesting them with the authority to develop binding rules."<sup>143</sup> These definitions comport with the "passing of power" definition of delegation used in Part III.<sup>144</sup> Recognition by the SEC of IASB as an authorized accounting standard-setter would surely meet these definitions. "Almost 100 countries now either require or allow the use of IFRS for the preparation of financial statements by listed companies,"<sup>145</sup> (meeting the first portion of the Bradley/Kelley definition), and given that the SEC extend official recognition to IASB as it has to FASB, IFRS as promulgated by IASB would presumably constitute the kind of "substantial authoritative support"<sup>146</sup> the SEC requires in financial statements filed by registered securities issuers (and the promulgation of IFRS would thus constitute "mak[ing] decisions or tak[ing] actions," meeting the second portion of the Bradley/Kelley definition).

Assuming that the SEC's potential recognition of IASB does constitute an "international delegation," the first important question to ask is whether there are any substantive constitutional limitations

141. See Curtis A. Bradley and Judith G. Kelley, *The Concept of International Delegation*, 71 LAW & CONTEMP. PROBS. 1, 1 (2008) ("[S]tates increasingly find international delegation useful in addressing the challenges associated with their growing interdependence.").

142. *Id.* at 2.

143. Swaine, *supra* note 14, at 1494.

144. See *supra* notes 95–97 and accompanying text.

145. 2007 Concept Release, *supra* note 6, at 45,602.

146. See *supra* note 35; see also 2007 Concept Release, *supra* note 6, at 45,603 (soliciting public comments on whether the SEC "should accept financial statements prepared in accordance with IFRS as published by the IASB from U.S. issuers").

on the government's ability to make such a delegation. Appealing directly to the text of the U.S. Constitution for an answer to this question provides little help. The most direct mention of international law is found in Article I, where Congress is given the authority to "define and punish . . . Offences against the Law of Nations."<sup>147</sup> However, it is Congress, and not any international body, that has the power to "define and punish" such offenses.<sup>148</sup> To further complicate matters, "[t]he world of the Framers is not our world. The modern administrative state in which we live is much more complicated than the republic envisioned by the Framers. This complexity has engendered an amount of lawmaking and legal regulation inconceivable to the Framers."<sup>149</sup> And while the Constitution assigns "[a]ll legislative [p]owers" to Congress,<sup>150</sup> that exclusive grant of power has not stopped Congress from assigning much of that power away.<sup>151</sup> Should the fact that the assignee is based in London or Geneva make any difference?

The difficulty in resolving the constitutional questions posed by international delegation has led legal scholars to reach very different conclusions. Some scholars believe that international delegations are not only constitutional but beneficial and even necessary for the efficient operation of a national government in today's globalized society.<sup>152</sup> Swaine argues that although "[i]nternational delegations are demonstrably different from domestic delegations of legislative authority," this does not necessarily mean that "international delegations are an affront to the Constitution."<sup>153</sup> Actually, Swaine asserts, international delegations "promote[] a . . . specific constitutional value: the diffusion of political authority prized by federalism."<sup>154</sup> To Swaine, this does not mean that "international delegations should always withstand constitutional scrutiny," as they will still be subject to "the nondelegation and federalism doctrines," but simply that there should not exist a "preemptive, undifferentiated constitutional objection to such activities."<sup>155</sup>

---

147. U.S. CONST. art. I, § 8, cl. 10.

148. Although "[i]nternational law is part of our law," the "customs and usages of civilized nations" are only controlling "where there is no treaty and no controlling executive or legislative act or judicial decision." *The Paquete Habana*, 175 U.S. 677, 700 (1900).

149. William N. Eskridge, Jr. & John Ferejohn, *The Article I, Section 7 Game*, 80 GEO. L.J. 523, 533 (1992).

150. U.S. CONST. art. I, § 1.

151. See *supra* notes 71–77 and accompanying text.

152. Neil S. Siegel, *International Delegations and the Values of Federalism*, 71 LAW & CONTEMP. PROBS. 93, 113 (2008).

153. Swaine, *supra* note 14, at 1501.

154. *Id.*

155. *Id.*

On the other hand, critics have come to doubt the constitutionality of international delegations, or at least have concluded that such delegations should be subject to a higher level of scrutiny than other delegations. Ku argues that strict constitutional formalism should apply to international delegations because they “place an unusually heavy strain on the ideal of political accountability that animates much of the Constitution’s structural design” and because “international organizations lack an independent source of political legitimacy.”<sup>156</sup> Ku proceeds to argue that “[c]ourts can and should play a role in policing the delegations of powers from the federal government to international organizations” due to their preexisting role as overseers of the process of delegating power within the federal government.<sup>157</sup>

Further complicating the question of the constitutionality of international delegations is the existence of many different types of such delegations. Bradley and Kelley point out eight categories of international delegations: “legislative, adjudicative, regulatory, monitoring and enforcement, agenda-setting, research and advice, policy implementation, and redelegation.”<sup>158</sup> Given the fact that international delegations can take so many different forms, it does not seem prudent or even feasible to analyze all of these types of delegation under the same constitutional framework. On the contrary, it seems that these types of delegation should be individually analyzed under a framework similar to their domestic analogues. For example, while a delegation by Congress of purely legislative authority would be barred in both the domestic and the international contexts by the nondelegation doctrine,<sup>159</sup> the delegation of administrative authority (or “regulatory” authority, as Bradley and Kelley refer to it)<sup>160</sup> to an international organization should be analyzed in much the same way as a domestic delegation of administrative authority, but with an added, international element.<sup>161</sup>

---

156. Ku, *supra* note 14, at 77.

157. *Id.* at 77–78. It is important to point out, however, that federal courts’ willingness to nullify federal delegations of power under the nondelegation doctrine is almost nonexistent, and so Ku may be overstating the point. See Swaine, *supra* note 14, at 1544 (stating that the nondelegation doctrine “plainly lacks vitality” and describing it as an “[u]nderenforced [n]orm”); *supra* note 75 and accompanying text.

158. Bradley & Kelley, *supra* note 141, at 10.

159. See *supra* text accompanying notes 72–73.

160. Bradley & Kelley, *supra* note 141, at 14.

161. *Cf. id.* (“Regulatory delegations also may raise questions for legal scholars about the extent to which domestic administrative-law concepts should be applied to the international arena.”). Bradley and Kelley point out that “[a]s can be the case in domestic law, there may be uncertainties associated with the distinction between legislative and regulatory delegations.” *Id.* However, as noted below, see *infra* text accompanying note 171, a delegation of accounting authority, such as Congress’ delegation to the SEC in the ’33 Act, seems on its face to be a delegation of “authority

The dearth of explicit constitutional guidance on the subject of international delegations means that any constitutional limitations on such delegations must be inferred from the governmental structure established by the Constitution and from a critical analysis of the effects of international delegations on that structure. Because the Constitution was written at least in part to establish a sovereign nation with the capability to act independently in the international sphere,<sup>162</sup> this Note takes the position that any constitutional bar to international delegations must be derived from such delegations' effects on the kind of independent national sovereignty the U.S. Constitution, or, for that matter, any constitution, establishes or reaffirms.<sup>163</sup> Thoroughly defining national sovereignty is neither possible nor necessary within the framework of this Note; for the purposes of this Note, it is enough to say that the United States, by virtue of its Constitution, possesses the kind of sovereignty, particularly in relation to international bodies, possessed by other independent nations.<sup>164</sup>

While some scholars argue that an international delegation is equivalent to a derogation of national sovereignty,<sup>165</sup> others assert that such a delegation is actually an exercise of that sovereignty.<sup>166</sup> Hathaway argues that "[i]f international delegations exist only when domestic lawmaking authorities say they do, then international

to create administrative rules to implement, fill gaps in, or interpret" laws passed through normal legislative channels. Bradley & Kelley, *supra* note 141, at 14.

162. Cf. *United States v. Curtiss-Wright Exp. Corp.*, 299 U.S. 304, 318 (1936) ("As a member of the family of nations, the right and power of the United States in [the field of foreign affairs] are equal to the right and power of the other members of the international family. Otherwise, the United States is not completely sovereign."); *Osborn v. President of Bank of U.S.*, 22 U.S. (9 Wheat.) 738, 808 (1824) ("Those who framed the constitution, intended to establish a government complete for its own purposes, supreme within its sphere, and capable of acting by its own proper powers."); *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 358 (1819) ("[T]he United States are sovereign, as to all the powers specifically given to their government, and as to all others necessary and proper to carry into effect those specified.")

163. Cf. Nathan J. Brown, *Constitutionalism, Authoritarianism, and Imperialism in Iraq*, 53 *DRAKE L. REV.* 923, 924 (2005) (noting that one purpose of constitution drafting is to affirm and support national sovereignty).

164. See *Curtiss-Wright Exp. Corp.*, 299 U.S. at 318.

165. See, e.g., JEREMY RABKIN, *WHY SOVEREIGNTY MATTERS* 34 (1998).

[T]he threat . . . that international commitments will distort or derange the normal workings of our own system, leaving it less able to resolve policy disputes in ways acceptable to the American people. Global governance, then, does not threaten to replace the American government, but it does threaten to distract and confuse and, ultimately, to weaken it.

*Id.*

166. See T. Alexander Aleinikoff, *Thinking Outside the Sovereignty Box: Transnational Law and the U.S. Constitution*, 82 *TEX. L. REV.* 1989, 1994 (2004) (viewing various international conventions as "the results of an exercise of sovereignty, not as evidence of a lapse of sovereignty").

delegations are not best understood as contrary to legitimate domestic authority; they are instead better understood as another site through which that authority is expressed."<sup>167</sup> Likewise, Gelber argues that "[s]overeignty and state power have never in practice been absolute, even in the domestic realm" because "in the case of major powers many, and certainly most, of the important limitations upon sovereignty have been by choice."<sup>168</sup>

In this sense, an international delegation of authority by Congress is no different from a delegation of authority to a federal administrative agency, in that Congress chooses to exercise its own power by giving away a portion of it. The comparison is particularly apt where Congress chooses to make a delegation of authority, either to an international body or to a federal administrative agency, in order to take advantage of that particular body's expertise in a specialized or highly technical field.<sup>169</sup> In the context of taking advantage of an organization's expertise, a delegation by Congress to an accounting standard-setting body makes perfect sense. Furthermore, because Congress' original delegation of accounting rulemaking authority to the SEC merely allows the SEC to fill gaps in the original statutes, as opposed to making new law,<sup>170</sup> it seems that the delegation of such authority would not violate the nondelegation doctrine as a delegation of pure legislative authority. Hence, analyzing an international delegation of accounting rulemaking authority under the same framework as a domestic delegation of that same authority would at least lead to the conclusion that such a delegation would not be presumptively invalid under current constitutional limitations on Congress' ability to delegate. It is important to note, though, that to the extent such a delegation is both an exercise and a ceding of some portion of national sovereignty, it is necessary that a representative lawmaking body takes responsibility for and actually makes the delegation in question.<sup>171</sup>

167. Oona A. Hathaway, *International Delegation and State Sovereignty*, 71 LAW & CONTEMP. PROBS. 115, 122 (2008).

168. HARRY G. GELBER, SOVEREIGNTY THROUGH INTERDEPENDENCE 75 (1997).

169. Cf. Susannah T. French, Comment, *Judicial Review of the Administrative Record in NEPA Litigation*, 81 CAL L. REV. 929, 930 (1993) ("[A]dministrative agencies are presumed to have special knowledge in the fields that they regulate. Thus, Congress generally has given agencies significant authority and discretion to use their expertise to serve the broader public good.").

170. See *Morton v. Ruiz*, 415 U.S. 199, 231 (1974) ("The power of an administrative agency to administer a congressionally created . . . program necessarily requires . . . the making of rules to fill any gap left, implicitly or explicitly, by Congress.").

171. See *supra* text accompanying note 167 (asserting that a delegation of sovereignty as an exercise of sovereignty when performed by "domestic lawmaking authorities"). A delegation of authority to an international body would, of course, likely also involve some interaction between Congress and the Executive branch; the main

A similar assertion is that international delegations should be judged through a cost-benefit analysis, weighing the costs incurred when a nation elects to transfer some of its own authority to an international organization versus the benefits that accrue to that nation.<sup>172</sup> For example, Gelber asserts that, given the “progressive internationalisation and globalisation of economic and technical forces,” such international arrangements are critical because questions had arisen as to whether “the nation-state [was] any longer adequate for the management of its citizens’ interests.”<sup>173</sup> Judging international delegations from a cost-benefit perspective will necessarily entail case-by-case consideration, but such consideration is precisely the kind of task a deliberative body such as Congress is designed to undertake.

The sum total of all that has thus far been said on the constitutionality of international delegations leads to but one clear conclusion: if there exists any constitutional limitation or bar on such delegations, it is implied and not express. This Note does not seek to answer the question of the constitutionality of any and all international delegations (particularly as it is likely that no concrete answer to the question will be had until the issue is brought before the Supreme Court, and possibly not even then), but merely to address the question as it specifically relates to the recognition of IFRS, as promulgated by IASB, in the U.S. Because the debate concerning the constitutionality of international delegations is currently unsettled, and because there is at least no express, textual constitutional bar to such delegations, this Note takes the position that a recognition of IASB as an authoritative accounting standard-setter is constitutionally permissible, but only if Congress, and not the SEC, makes such an international delegation of authority. In addition to the arguments made above related to international delegations as an exercise of sovereignty and to the validity of international delegations as a function of specific costs and benefits, there are at least two reasons, taken together, that recognition of IASB by Congress would not be constitutionally offensive. First, any such recognition would presumably be revocable at the will of Congress because no treaty or other binding agreement would be required for such recognition.<sup>174</sup> Second, given the ability of Congress

---

thrust of Hathaway’s statement cited in *supra* note 167 seems to be that an international delegation of sovereignty must be performed by some elected, politically accountable body.

172. See Hathaway, *supra* note 167, at 116 (“[R]ecent scholarship portrays the costs of delegation as larger than they in fact are. Moreover, recent work has lost sight of some of the substantial *benefits* of cooperation.”).

173. GELBER, *supra* note 168, at 33.

174. Cf. Cunningham, *SEC’s Global Accounting Vision*, *supra* note 129, at 41 (“Indeed, the SEC has plenary power over establishing accounting standards in the US. Its delegation to FASB, or to any other body, is revocable at will.”). This assumes that



to revoke IASB's authoritative status, Congress would still be politically accountable should IASB fail to prove "capable of improving the accuracy and effectiveness of financial reporting and the protection of investors under the securities laws,"<sup>175</sup> thus negating one of Ku's main concerns.<sup>176</sup>

At this stage, it is important to note that though there may not be a constitutional bar on Congress's ability to make such a delegation, this does not necessarily mean that Congress should take such action—or, in other words, that such action would constitute good policy.

### B. Policy Considerations Regarding International Delegations

Although some policy considerations may be universal to all different types of international delegations, this section will focus on those considerations specifically related to the U.S. recognition of IASB, centering on one overarching question: Would the U.S. use of international accounting standards work to further the SEC's mission? Perhaps the most perplexing difficulty in answering this question is that the SEC's mission is not only to protect investors.<sup>177</sup> In its rulemaking activities, the SEC is also statutorily commanded to consider "whether the action will promote efficiency, competition, and capital formation."<sup>178</sup> The IASB's potential for furthering both of these two potentially competing priorities<sup>179</sup> must be analyzed in order to judge the wisdom of the recognition of IASB and IFRS in the U.S.

#### 1. Accounting as an Expression of National and Financial Forces

One of the primary difficulties involved in assessing the potential efficacy of U.S. use of IFRS is that U.S. investors have long been

---

such a recognition of IASB would carry the same degree of formality and revocability as the SEC's current recognition of FASB.

175. See *supra* note 131 and accompanying text.

176. See *supra* note 156 and accompanying text.

177. See *supra* note 135 and accompanying text.

178. Securities Act § 2(b), 15 U.S.C. § 77b(b) (2008).

179. The argument that these two priorities are in some sense competitive is as follows: A financial disclosure scheme which requires essentially no detailed financial information from a company seeking to access public capital would allow essentially any company to procure funds from investors, but would expose such investors to a high risk that the companies in which they invest are not financially viable, if not in some cases an outright sham. On the other hand, an incredibly restrictive financial disclosure scheme which requires companies to produce a high volume of financial data, potentially at a prohibitive cost, gives investors greater assurance that any company in which they choose to invest has a high likelihood of financial viability, but limits the number of companies which will be able to access public capital given such limitations.

accustomed to accounting standards issued by an organization, FASB, which specifically addresses U.S. accounting issues.<sup>180</sup> “[A]s an international organization with international members and constituencies, it could be difficult for IASB to commit to protecting investors under US law. Certainly it is harder for IASB to look out for US investors than it is for FASB to do so.”<sup>181</sup> This conclusion naturally flows from the fact that accounting systems developed in individual countries (before the proliferation of international accounting standards) reflect two major driving forces, or two major categories of driving forces—this Note refers to them as “national” and “financial”—that are not identical in any two countries.<sup>182</sup>

a. National Forces

The “national” forces which shape the development of accounting regimes in individual countries are those forces related to and derived from the country’s unique governmental and cultural identity.<sup>183</sup> These forces can be grouped into at least five categories: “cultural,” “linguistic,” “political and civil,” “economic and demographic,” and “legal and tax.”<sup>184</sup> The principle is simple: “accounting objectives, standards, policies, and techniques result from environmental factors in each country; if these environmental factors differ significantly between countries, it would be expected that the major accounting concepts and practices in use . . . would also differ.”<sup>185</sup> National factors run the gamut from the concrete (i.e., a country’s statutory method of tax collection)<sup>186</sup> to the abstract (i.e., “attitudes, norms, [and] values”).<sup>187</sup> An accounting system which attempts either to ignore or transcend the fundamental differences between nations in these fields might well prove confusing to businesses, investors, and accounting practitioners, all of whom are accustomed to dealing with accounting principles which more closely align with the nationalistic factors with which they are personally and institutionally familiar. And while it is possible to draw similarities between various nations’

---

180. See *supra* text accompanying notes 3–4.

181. Cunningham Letter, *supra* note 128, at 4.

182. These two broad categories necessarily overlap. For example, the extent to which a nation’s economy is considered a capitalist economy would alter both the national and the financial dynamic. Nevertheless, there are enough unique components to each category that it is useful to view the two separately.

183. AHMED BELKAOUI, INTERNATIONAL ACCOUNTING: ISSUES AND SOLUTIONS 28 (1985).

184. *Id.* at 29.

185. *Id.* at 28.

186. *Id.* at 49.

187. *Id.* at 29 (quoting H. TRIANDIS, THE ANALYSIS OF SUBJECTIVE CULTURE 3 (1972)).

accounting systems based on their national similarities,<sup>188</sup> it is equally impossible to craft one set of accounting principals which could apply with equal force and accuracy to all nations regardless of their national differences.<sup>189</sup>

#### b. Financial Forces

The “financial” forces which shape the development of various accounting systems deal with the structure of the particular nation’s capital markets and monetary and investment frameworks.<sup>190</sup> These forces include the sources of capital and their relationships to business enterprises,<sup>191</sup> the nation’s level of inflation,<sup>192</sup> the relative “[s]ize and [c]omplexity” of the nation’s business entities,<sup>193</sup> and the “[s]ophistication” of the nation’s “[f]inancial [c]ommunity.”<sup>194</sup> So, for example, a country whose businesses primarily derive their capital from public securities markets (such as the U.S. or UK) would necessarily differ in its accounting principles from a country whose businesses primarily derive capital from large, private banks (such as Japan or Germany).<sup>195</sup> Just as no two countries’ nationalistic factors are identical, as noted above, neither are any two countries’ financial forces identical.

With regard to investors in a securities market, these financially driven differences in accounting systems across countries are

188. One accounting text defines “four major accounting models” into which most nations can be grouped: “British-American,” “Continental,” “South American,” and “Mixed Economy.” GERHARD G. MUELLER ET AL., ACCOUNTING: AN INTERNATIONAL PERSPECTIVE 8–12 (1994). An even broader classification places accounting systems into one of two groups—“rules-based” and “principles-based”—with U.S. GAAP being considered a “rules-based” system and IFRS a “principles-based” system. Cunningham, *SEC’s Global Accounting Vision*, *supra* note 129, at 13. The line dividing the two systems was considered clear enough that as part of the Sarbanes-Oxley Act, Congress directed the SEC to “conduct a study on the adoption by the United States financial reporting system of a principles-based accounting system.” Sarbanes-Oxley Act § 108(d)(1)(A), 15 U.S.C. § 7218(d)(1)(A) (2008). However, some commentators argue that a rules-based vs. principles-based distinction is overbroad and inaccurate. *See, e.g.*, Lawrence A. Cunningham, *A Prescription to Retire the Rhetoric of “Principles-Based Systems” in Corporate Law, Securities Regulation, and Accounting*, 60 VAND. L. REV. 1411, 1413 (2007) (“These classifications are too crude to describe or guide the design of . . . accounting systems.”).

189. *See* MUELLER ET AL., *supra* note 188, at 8 (“No two countries have *identical* financial accounting practices. Each country is a unique mixture of environmental variables that together have influenced the pattern of accounting development in that country.”).

190. *See id.* at 3–8 (outlining variables that shape accounting development).

191. *Id.* at 3.

192. *Id.* at 6.

193. *Id.* at 7.

194. *Id.*

195. *See id.* at 3–4 (contrasting the securities-based and banking-based systems).

significant because, in some respect, accounting data can serve as an indicator of a company's risk (and, therefore, the risk passed on to any investor who might consider purchasing the company's securities).<sup>196</sup> To the extent that two different accounting systems would produce two different sets of data regarding a company's current financial status, these two data sets would provide different assessments of the risk inherent in investing in the company.

An illustration of this phenomenon proves helpful. "It is widely believed that larger firms are less risky than smaller firms" when the firm's size is defined as the sum total of its assets.<sup>197</sup> Assume, then, that a fictional company, XYZ Co., owns a certain mix of assets at some given point in time. Assume also that at least some of these assets do not have a concrete and definite value at any given point in time.<sup>198</sup> To the extent that two different accounting systems would dictate that these assets be assigned a different value at any given point in time, the two accounting systems would produce a different financial "snapshot" of XYZ Co. The use of one asset valuation scheme—a system which assigned the assets the lower aggregate value—might dissuade some potential investors from purchasing XYZ stock, while the use of the system assigning the assets the higher aggregate value might encourage some investors to purchase XYZ stock. This occurs even though the objective quality, nature, and character of XYZ's assets are exactly the same no matter which accounting regime is utilized. In short, because investors (at least many of them) base their investment decisions on financial accounting data, changing the accounting system which produces the data will in many cases change the behavior of investors.

---

196. See William Beaver et al., *The Association Between Market Determined and Accounting Determined Risk Measures*, 45 ACCT. REV. 654, 654 (1970) ("The accounting system generates information on several relationships that are considered by many to be measures of risk.") As an interesting side note, one of this article's co-authors, Myron Scholes, shared the 1997 Nobel Prize in economics. All Laureates in Economics, [http://nobelprize.org/nobel\\_prizes/economics/laureates/](http://nobelprize.org/nobel_prizes/economics/laureates/) (last visited Feb. 17, 2009).

197. Beaver et al., *supra* note 196, at 662.

198. The most obvious example of an asset with a concrete and definite value is cash. An example of an asset without such a concrete value, thereby necessitating the use of one particular valuation method as opposed to another, would be a machine used in a manufacturing business. Perhaps the two most sensible and common methods of valuation for such an asset are (1) to determine the fair market value of the machine at a given point in time (assuming that such a value could be reasonably ascertained), or (2) to determine the value as a function of the original purchase price of the machine less the value of the "wear and tear" incurred in the machine's use to date. Although these two valuation methods should generally approximate one another, they are by no means identical. For illustrations of the use of these two methods of asset valuation, known respectively as "[n]et realizable value accounting" and "[h]istorical cost accounting," see BELKAOUI, *supra* note 183, at 133, 130.

Currently, U.S. GAAP and the IFRS system promulgated by IASB differ in many ways in how they value particular assets.<sup>199</sup> Therefore, viewing a certain company through the lens of IFRS as opposed to GAAP (or vice versa) might well give investors the impression that the company is either a more or a less risky investment than would viewing the company through the lens of the other accounting system, potentially leading investors to change their investment decision, which could, quite possibly, change the company's ability to raise capital. Overall, the current differences in GAAP-based and IFRS-based accounting methodologies are significant enough to affect how investors would view a company that produced financial statements under both accounting systems.<sup>200</sup> Because a country's accounting system is so fundamentally grounded in that particular country's unique nationalistic and financial characteristics, a switch to an alternate accounting system—one based on different nationalistic and financial characteristics, and possibly on the conglomerate of many countries' nationalistic and financial characteristics—might well result in that country's investors being confused by the new system and thereafter making less efficient investment decisions.

## 2. The Effect of Accounting System Choice on Capital Formation

If a switch from GAAP to IFRS in the U.S. capital markets would result in confusion and potentially inefficient investment decisions by U.S. investors, thereby seemingly undermining the SEC's performance of its mission to protect investors, the adoption of an IFRS-based accounting system would undoubtedly assist the SEC in performing the other part of its mission: fostering competition and

199. See PRICEWATERHOUSECOOPERS, SIMILARITIES AND DIFFERENCES: A COMPARISON OF IFRS AND U.S. GAAP 39–49 (2007), available at [http://www.pwc.com/gx/eng/about/svcs/corporatereporting/SandD\\_07.pdf](http://www.pwc.com/gx/eng/about/svcs/corporatereporting/SandD_07.pdf) (outlining differences between IFRS-based and GAAP-based asset valuation schemes).

200. A recent study found that out of 130 companies that produced IFRS-based financial statements containing a reconciliation to GAAP, only two companies reported the same earnings under both regimes. Of the eighty-four companies which reported higher earnings under IFRS, “the median earnings increase was 12.9%” over GAAP; of the forty-four companies which reported higher earnings under GAAP, “the difference was 9.1%.” *International Accounting Standards: Opportunities, Challenges, and Global Convergence Issues: Hearing Before the Subcomm. on Securities, Insurance, and Investment of the S. Comm. on Banking, Housing, and Urban Affairs*, 110th Cong. 5–6 (2007) (statement of Jack T. Ciesielski, President, R.G. Associates, Inc.), available at [http://banking.senate.gov/\\_files/ciesielski.pdf](http://banking.senate.gov/_files/ciesielski.pdf). The study noted that differences of these magnitudes were large enough that the SEC would consider them “material,” meaning that “it is probable that the judgment of a reasonable person relying upon the report would have been changed or influenced.” *Id.* at 6 (quoting SEC Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45, 150 (1999)).

capital formation.<sup>201</sup> In recent years, the U.S. has begun to lose its grip on its status as the world leader in raising capital through public securities markets.<sup>202</sup> Indeed, the percentage of worldwide initial public offerings occurring in the U.S. dropped from 50% in 2000 to a mere 5% in 2006.<sup>203</sup> While some of that decrease can undoubtedly be blamed on the more stringent internal control requirements dictated by the Sarbanes-Oxley Act<sup>204</sup> (for better or for worse), a switch to an IFRS-based financial disclosure system in the U.S. would certainly encourage some foreign companies, for whom preparing financial statements according to U.S. GAAP (or even providing a reconciliation to U.S. GAAP) would prove prohibitively costly or inefficient, to list their securities on a U.S.-based exchange and gain access to U.S. public capital markets.<sup>205</sup> The SEC has even publicly acknowledged that recognition of IFRS in the U.S. would promote capital formation in the U.S. by foreign securities issuers.<sup>206</sup>

---

201. See *supra* note 178 and accompanying text. Professor Lawrence Cunningham notes that it is overly simplistic to conclude that a U.S. switch to IFRS would facilitate capital formation, because “[i]f investors are confused, capital formation likely will be impaired.” E-mail from Lawrence A. Cunningham, Professor of Law, George Washington University Law School, to Jacob L. Barney (Feb. 26, 2008) (on file with author). However, given the statistics found in note 202 and the text accompanying note 203, *infra*, it seems that the use of IFRS might well provide a shot in the arm to a U.S. IPO market that has seemingly floundered over the past several years.

202. See Jenny Anderson, *About Those Fears of Wall Street's Decline*, N.Y. TIMES, Jan. 26, 2007, at C6 (explaining that “[i]n 2006, the New York exchanges raised \$46.6 billion; Hong Kong raised \$47.1 billion; and London, \$55.2 billion” and that while “New York raised 54 percent less than it did in 2000,” “London raised 303 percent more and Hong Kong, 225 percent more”).

203. William A. Niskanen, Op-Ed., *Enron's Last Victim: American Markets*, N.Y. TIMES, Jan. 3, 2007, at A21.

204. See Anderson, *supra* note 202 (“[W]hen the Industrial and Commercial Bank of China went public in 2006, raising \$22 billion, it opted against a United States listing because of Sarbanes-Oxley, according to people involved in the I.P.O. discussions.”).

205. See Jeremy Grant & Jennifer Hughes, *SEC Launches Effort to Streamline Reporting for Non-US Companies*, FIN. TIMES (London), June 20, 2007, at 27 (quoting an accounting firm partner as stating that “[f]or those who aren't yet listed in the US and have been concerned about the costs of obtaining a listing,” the ability to file IFRS-based financial statements “no doubt . . . removes one of the obstacles”).

206. See *Acceptance From Foreign Private Issuers of Financial Statements Prepared in Accordance With International Financial Reporting Standards Without Reconciliation to U.S. GAAP*, 72 Fed. Reg. 37,962, 37,966–67 (proposed July 11, 2007) (to be codified at 17 C.F.R. pts. 210, 230, 239 & 249) (acknowledging that when the SEC first “sought to facilitate the transition to IFRS,” it “recognized that this accommodation would reduce costs to foreign issuers and encourage their continued participation in the U.S. public capital market, which would benefit investors by increasing investment possibilities and furthering the efficient allocation of capital”). It is important to note here that, as the SEC recognized in the quote above, there is value given to investors by allowing them a broader range of investment choices in U.S. capital markets. Although giving securities issuers a choice as to which accounting system (IFRS or U.S. GAAP) controls the creation of their financial statements and

In the end, the question of whether a U.S. adoption of international financial reporting standards would constitute sound policy must be answered by balancing the need to protect investors with the need to promote healthy, vibrant, and robust capital markets in the U.S. The answer to this question is primarily a policy judgment, and attempting to determine the correct answer is beyond the scope of this Note. Given the actions that the SEC has already taken,<sup>207</sup> it seems impossible to doubt that the current trajectory makes universal acceptance of IFRS in the U.S.—for both foreign and domestic securities issuers—almost certain. It is certainly reasonable to conclude that such a course is the right one for the U.S. and its capital markets. However, it is also reasonable to expect that such a dramatic shift in U.S. financial policy should come as a result of careful consideration and extensive deliberation by a representative body—Congress.

## V. RECOMMENDATIONS AND PROPOSALS FOR FUTURE ACTION

This Note concludes that, at this time, the SEC has no statutory authority to subdelegate its accounting rulemaking authority to the IASB, given the limitations set out in *U.S. Telecom*. Under *U.S. Telecom*, express congressional authorization is required before such a delegation can be made.<sup>208</sup> Likewise, this Note concludes that it is essential that any delegation of federal power to an international organization be made by a representative and politically accountable body—in this case, Congress. Therefore, Congress must step in and take a more active role in the discussion of whether a U.S. recognition of IFRS would promote both the SEC's obligation to protect investors and its obligation to promote market efficiency and the free flow of capital.

### A. *A Path Forward for Congress*

Congress has already held one set of hearings on the issues posed by the adoption of international accounting standards in the United States.<sup>209</sup> However, given that four of the eight panel members at the hearing represented either the SEC, FASB, or

---

other disclosures might not truly be an activity meant to “protect” investors, this is not to say that investors do not in the end reap some benefit from the representation of a wider variety of securities issuers, and thereby a wider variety of investment opportunities, in U.S. markets.

207. See *supra* note 7–10 and accompanying text.

208. See *supra* note 90 and accompanying text.

209. 110 CONG. REC. S13, 273–390 (daily ed. Oct. 24, 2007).

IASB,<sup>210</sup> more independent dialogue is needed to establish the full ramifications of a recognition of international accounting standards—both for investors and for public companies. Further hearings should devote adequate time and attention to issues of investor protection, capital formation, and legal and oversight-related issues inherent in an SEC subdelegation to and relationship with a foreign-based standard-setting body. A study of the effects, both as to the protection of investors and as to capital formation and market efficiency, that the adoption of IFRS has had on another country—for example, the UK, whose national accounting system is in many ways similar to U.S. GAAP<sup>211</sup>—would also be illustrative of the potential costs and benefits of IFRS adoption in the U.S., and Congress would serve the public interest well by conducting such a study.

Ultimately, given the SEC's lack of authority to delegate accounting rulemaking authority to a private organization without express congressional authorization under *U.S. Telecom*, Congress must provide the SEC with explicit statutory authorization to recognize IASB as an organization with the power to create accounting standards which are controlling under U.S. securities laws. This is especially true if Congress finds that an adoption of international accounting standards would help the SEC to fulfill its twofold mission of protecting investors and promoting capital formation and market efficiency. Given that such accounting standards constitute "rules" under the APA,<sup>212</sup> the SEC would be required to follow APA-prescribed rulemaking procedures<sup>213</sup> in approving new accounting standards. As an alternative to this process, and to allow new accounting standards to be introduced efficiently and expeditiously, Congress could give the SEC statutory

---

210. *Id.*

211. *See supra* note 188.

212. *See supra* note 96.

213. *See supra* note 119 for discussion of "notice-and-comment rulemaking." It is important to note that the SEC did engage in typical notice-and-comment rulemaking procedures when it recently promulgated a final rule allowing foreign private issuers to file with the SEC financial statements prepared in accordance with IFRS and without a reconciliation to U.S. GAAP. *See supra* notes 7–8 and accompanying text. However, given that such a rule incorporates dozens of preexisting accounting standards which themselves seem to meet the definition of a "rule," as well as giving IASB the authority to promulgate binding accounting standards in the future without utilizing further notice-and-comment procedures to ratify those future standards for official use, the author is of the opinion that passing one rule to encompass and grant official recognition to all past and future IFRS is simply insufficient. *Cf.* IFRS and IAS Summaries: English, <http://www.iasb.org/IFRS+Summaries/IFRS+and+IAS+Summaries+English+2008/IFRS+and+IAS+Summaries+English.htm> (last visited Feb. 17, 2009) (noting the existence of eight International Financial Reporting Standards and forty-one International Accounting Standards as of January 1, 2008).



authorization to bypass normal notice-and-comment rulemaking requirements, as it did for OSHA in *Noblecraft*.<sup>214</sup>

### B. *Judicial Review of the SEC's Recognition of IFRS*

If Congress does not give the SEC explicit statutory authorization to subdelegate rulemaking authority to IASB, as required under *U.S. Telecom*, the SEC's recognition of IFRS as controlling under the federal securities laws is likely reviewable in federal court.<sup>215</sup> The APA gives "[a] person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action" the right to judicial review of such action.<sup>216</sup> The APA precludes access to judicial review when the underlying agency statute "preclude[s] judicial review" or when "agency action is committed to agency discretion by law,"<sup>217</sup> but it appears that nothing in either the '33 Act or the Sarbanes-Oxley Act, which grant the SEC authority to promulgate substantive accounting rules, precludes judicial review of actions taken thereunder, and the presence of specific requirements which an accounting "standard setting body" must meet in order to gain official recognition from the SEC under the Sarbanes-Oxley Act<sup>218</sup> make it clear that granting such recognition is not "committed to [the SEC's] discretion by law." Furthermore, the U.S. Supreme Court has held that the APA provision for judicial review should be interpreted liberally:

The legislative material elucidating [the APA] manifests a congressional intention that it cover a broad spectrum of administrative actions, and this Court has echoed that theme by noting that the Administrative Procedure Act's "generous review provisions" must be given a "hospitable" interpretation. . . . [O]nly upon a showing of "clear and convincing evidence" of a contrary legislative intent should the courts restrict access to judicial review.<sup>219</sup>

Of course, a judicial challenge to the SEC's subdelegation must come from a party actually "adversely affected or aggrieved" by the recognition of IFRS.<sup>220</sup> The U.S. Supreme Court has held that standing to challenge an administrative agency's action requires that "the complainant is arguably within the zone of interests to be protected or regulated by the statute . . . in question."<sup>221</sup> Such a complainant might be a U.S. investor who owns shares in a foreign

214. See *supra* text accompanying notes 119–20.

215. 5 U.S.C. § 702 (2008).

216. *Id.*

217. *Id.* § 701(a)(1)–(2).

218. See *supra* notes 26–29 and accompanying text.

219. Heckler v. Chaney, 470 U.S. 821, 843 (1985) (alterations in original) (quoting *Abbott Laboratories v. Gardner*, 387 U.S. 136, 140–41 (1967)).

220. 5 U.S.C. § 702.

221. Ass'n of Data Processing Serv. Orgs. v. Camp, 397 U.S. 150, 153 (1970).

securities issuer that is no longer required to file financial statements prepared in accordance with U.S. GAAP (either directly or via reconciliation from IFRS). This would particularly be the case where the company's previous filings showed a wide discrepancy between, for example, IFRS-based and GAAP-based earnings,<sup>222</sup> thus raising in the mind of such an investor questions as to the reliability of such financial statements,<sup>223</sup> at least with respect to the comparability of current financial statements with previous financial statements issued by the company. Such an investor would definitely fall within the "zone of interest" of the '33 Act, which gave the SEC authority to promulgate substantive accounting rules,<sup>224</sup> as the Act was passed largely to protect investors by providing them with the information necessary to make sound investment decisions.<sup>225</sup> The investor would be "adversely affected or aggrieved" because the SEC's allowance of foreign issuers to file financial statements prepared under IFRS (the "agency action" required by the APA) would result in the investor receiving a financial data set that is either incomplete or misleading, at least when compared to the company's previous GAAP-based financial statements (meeting the "adversely affected or aggrieved" requirement). An investor's challenge in court of the SEC's actions would not, however, be based on substantive differences in the financial statements of a company in which he owns stock; it would be based on the SEC's lack of legal authority to grant recognition to IFRS, recognition that would lead directly to the substantive differences in the financial statements. The APA provides multiple grounds for a judicial remedy to an agency action not supported by sufficient legal authority.<sup>226</sup> In such a case, a reviewing court should

---

222. See *supra* note 200 and accompanying text.

223. See Yohn Statement, *supra* note 11 (arguing that IFRS-based financial statements do not currently provide U.S. investors with sufficient information on which to base their investment decisions).

224. See Securities Act of 1933 § 19(a), 15 U.S.C. § 77s(a) (2008).

225. See *SEC v. R.G. Reynolds Enters., Inc.*, 952 F.2d 1125, 1133 (9th Cir. 1991) (noting that the court "construe[s] the Securities Acts broadly to effectuate Congress' purpose to protect investors"); *SEC v. Gorsek*, 222 F. Supp. 2d 1099, 1104 (C.D. Ill. 2001) ("The Securities Act of 1933 was intended to provide investors with full disclosure of material information concerning public offerings of securities in commerce . . ."). In addition, such an investor would fall within the "zone of interest" of the Sarbanes-Oxley Act, which allows the SEC to recognize as authoritative accounting standards promulgated by a body which meets certain standards. See Sarbanes-Oxley Act of 2002 § 108(b)(1), 15 U.S.C. § 77s (2008); S. REP. NO. 107-205, at 2 (2002) (noting that consideration of the bill came largely as a result of the "investor protection issues raised by the financial revelations involving Enron and other public companies").

226. See 5 U.S.C. § 706(2) (2008) (directing a "reviewing court" to "hold unlawful and set aside any agency action . . . found to be" either "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law"; "in excess of statutory jurisdiction, authority, or limitations, or short of statutory right"; or "without observance of procedure required by law").

conclude that the SEC did not have the required statutory authority under *U.S. Telecom* to recognize IASB as an authorized standard-setter.

## VI. CONCLUSION

Although delegations of the federal government's authority to international organizations involve many complex legal and policy-related issues, international subdelegations by administrative agencies involve a unique intersection of international and administrative law which does not lend itself to easy or even universally applicable solutions. And though such subdelegations are bound to become more and more commonplace given the proliferation of substantive international law in recent years, it does not necessarily follow that they will become any less controversial or easier to analyze. The U.S. recognition of IFRS and its inherent difficulties serve to underscore this point.

Considering the near-seismic shift in U.S. securities law and financial reporting that will likely result from a recognition of international accounting standards in the U.S., it seems only reasonable to expect that Congress, the most representative and most politically accountable of all branches of the federal government, would take the lead in deliberating and coming to a conclusion as to whether such recognition should be extended. While the SEC's expertise in administering the nation's securities laws should go a long way in informing the congressional dialogue, ultimate approval of the transition to IFRS must come from Congress.

*Jacob L. Barney\**

---

\* J.D. Candidate, Vanderbilt University, May 2009. This Note is dedicated to my wife Nicole and my son Nathan. Special thanks go to Professors Lisa Bressman, Chris Brummer, and Kevin Stack of Vanderbilt University Law School, and to Professor Lawrence Cunningham of the George Washington University Law School, for their encouragement, feedback, and assistance. I would also like to recognize the effort and dedication of the editors and staff of the VANDERBILT JOURNAL OF TRANSNATIONAL LAW, without whom I would not have had this wonderful opportunity.