

CAUSE NO. D-1-GN-09-001193

**JOHN W. BEAKLEY and  
BEAKLEY & ASSOCIATES, P.C.,  
Plaintiffs,**

**v.**

**TEXAS STATE BOARD OF PUBLIC  
ACCOUNTANCY, GREGORY L.  
BAILES, CPA, A. CARLOS BARRERA,  
CPA, JOHN W. (JAY) DUNBAR, CPA,  
EVERETT R. FERGUSON, CPA,  
JAMES C. FLAGG, PH.D, CPA,  
DOROTHY M. FOWLER, CPA, JON R.  
KEENEY, DAVID L. KING, CPA.,  
EVELYN M. MARTINEZ, ESQ.,  
MERIBESS L. MILLER, CPA, STEVE  
D. PENS, CPA, JAMES W. POLLARD,  
THOMAS G. PROTHRO, CPA,  
CATHERINE J. ROSEWALD, JOHN  
W. STEINBERG, CFE, and WILLIAM  
TREACY,  
Defendants.**

**IN THE DISTRICT COURT**

**OF TRAVIS COUNTY, TEXAS**

**345TH JUDICIAL DISTRICT**

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**NATIONAL ASSOCIATION OF STATE BOARDS OF ACCOUNTANCY'S  
AMICUS BRIEF IN SUPPORT OF DEFENDANTS' RESPONSE TO  
PLAINTIFFS' MOTION FOR FINAL SUMMARY JUDGMENT**

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NATIONAL ASSOCIATION OF  
STATE BOARDS OF ACCOUNTANCY**

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The National Association of State Boards of Accountancy (hereinafter "NASBA"), as amicus curiae, submits this brief in response to the Motion for Final Summary Judgment filed by John W. Beakley and Beakley & Associates, P.C. (hereinafter "Plaintiffs") and in support of the Texas State Board of Public Accountancy, its board members, and its executive director (hereinafter collectively "Board").

## INTRODUCTION

NASBA is a non-profit corporation with its headquarters in Nashville, Tennessee. Its members are all of the state boards of accountancy of the fifty states, as well as the District of Columbia and the territories of Puerto Rico, Guam, the Northern Mariana Islands, and the Virgin Islands. For over a hundred years NASBA's primary mission has been to enhance the effectiveness of these state boards of accountancy. NASBA is also concerned with effective public protection through state regulation of public accounting. Some of the goals of NASBA are to preserve the public trust and confidence in the Certified Public Accountant (hereinafter "CPA") title, fostering compliance with ethical and all professional standards, and promoting the rights of boards of public accountancy to regulate licensees in all their professional activities. NASBA develops the Uniform Accountancy Act's Model Rules. NASBA, along with the American Institute of Certified Public Accountants (hereinafter "AICPA"), jointly prepares and promotes the Uniform Accountancy Act. NASBA also supports its member boards with briefs in state and federal courts. Other states have comparable accountancy laws to those of Texas, and which have been upheld under similar challenges. However, because of the increased mobility of CPAs and the fact that the applicable professional standards are common among the majority of states, effective public protection could be severely

undermined by an inconsistent, adverse ruling against the Texas State Board of Public Accountancy. Indeed, such a ruling would likely make Texas the only state in which CPAs could not be disciplined for violations of the Generally Accepted Accounting Principles (hereinafter "GAAP") and Generally Accepted Auditing Standards (hereinafter "GAAS").

### **ARGUMENT AND AUTHORITIES**

**A. The Board has the authority under Tex. Occ. Code Ann. § 901.502 to discipline a CPA for violations of GAAS and/or GAAP where the alleged violations do not rise to the level of gross negligence.**

**1. The Board may simultaneously discipline a licensee for violation of the rules of professional conduct and for conduct constituting fraud, dishonesty, or gross negligence.**

Plaintiffs contend that the Board's authority to discipline a CPA for a violation of professional standards is limited to conduct constituting "fraud, dishonesty, or gross negligence." This contention is totally at odds with the plain meaning of the statute. Texas Occupations Code § 901.502(2) does provide that the "Board may discipline a person under Section 901.501 for ... fraud, dishonesty, or gross negligence in the performance of services as a license holder." However, it also provides that a CPA may be disciplined for "a violation of a rule of professional conduct adopted by the Board," Tex. Occ. Code Ann. § 901.502(6), or "a violation ... of ... professional standards adopted by the board." Tex. Occ. Code Ann. § 901.502(12)(B). The statute contains twelve independent grounds for discipline, of which "gross negligence in the performance of services as a license holder" is just one. A violation of professional standards is an independent basis for discipline separate and apart from "gross negligence," and nowhere does the statute say the violation must rise to the level of gross negligence to constitute a

legally sufficient basis for discipline. In short, Plaintiffs are trying to read a requirement into the statute that simply isn't there.

Courts interpreting similar statutes from other jurisdictions have reached the same conclusion. For instance, in the case of *Zwygart v. State Bd. of Pub. Accountancy*, 273 Neb. 406, 730 N.W.2d 103 (2007), the Nebraska Supreme Court held that the Nebraska State Board of Public Accountancy could discipline a CPA for any one or any combination of nine enumerated causes set forth in Neb. Rev. Stat. § 1-137, a statute similar to Tex. Occ. Code Ann. § 901.502. *Id.* at 414, 730 N.W.2d at 111. According to the Nebraska Supreme Court, "[d]ishonesty, fraud, or gross negligence in the practice of public accountancy," and "[v]iolation of a rule of professional conduct adopted and promulgated by the board under the authority granted by the act" were independent grounds for discipline under this statute. *Id.* Other courts addressing this issue have followed a similar line of reasoning. *See, for example, Waldrop v. Alabama State Bd. of Pub. Accountancy*, 473 So. 2d 1064, 1067 (Ala. Civ. App. 1985) (Alabama board found that CPA's acts constituted dishonesty, fraud, and/or gross negligence in the practice of public accounting and violated several rules of professional conduct promulgated by the Board).

**2. The Board is statutorily authorized to enforce national accounting and auditing standards referenced in its rules of professional conduct.**

Indeed, the Fifth Circuit Court of Appeals has recognized the Board's authority to enforce its rules of professional conduct. In *Newby v. Enron Corp.*, 443 F.3d 416 (5th Cir. 2006), the Fifth Circuit specifically identified sections (6) and (12) of Tex. Occ. Code Ann. § 519.502 among those sections of the statute under which the Board may

bring disciplinary proceedings. Sections (6) and (12) are the very sections of the statute that Plaintiffs are charged by the Board with violating. The Court stated that:

[t]he Board is a state regulatory authority charged under the Texas Public Accountancy Act ("Act") with the duty of licensing and disciplining Texas CPAs as well as promulgating accounting rules. ... The Board may initiate disciplinary proceedings against a Texas licensed CPA for violations of rules of professional conduct adopted by the Board as well as for conduct indicating lack of fitness to serve the public as a professional accountant. Tex. Occ. Code § 901.502(6), (11) and (12). Furthermore, the Board is authorized to open investigations if it determines that there is a potential violation of its rules, regulations, or orders.

*Newby*, 443 F.3d at 418-19 (emphasis added).

In *Christensen v. Wyoming Bd. of Certified Pub. Accountants*, 838 P.2d 723, 727 (Wyo. 1992), the Wyoming board reprimanded a CPA regarding a review of an audited statement that he prepared for a small public water and sewer district. The matter was appealed to the state supreme court, which held that the board had the authority to require CPAs to conform to existing national standards of accounting practice. The court said,

[t]here is no impermissible delegation of authority by the state regulatory agency in requiring certified public audits to conform to existent national standards of accounting practice. The certification in the report attests to compliance. The constitutional and statutory right of the State Board to regulate the performance of a certified public accountant is not at issue.

*Id.* at 727. As the court recognized in *Christensen*, the certification contained in Christensen's audit report – as is the case with the certification in Plaintiffs' audit report – attests to the compliance of the report with the standards set out in the GAAS.

**3. The Board's rules of professional conduct are not inconsistent with the enabling statute.**

On page two of their Reply in Support of Motion for Final Summary Judgment, Plaintiffs argue that "the Board does not have unlimited power to enact a rule of professional conduct that is inconsistent with the statute." Their perceived inconsistency



is an alleged “strict liability disciplinary standard” for conduct measured against the professional standards articulated in the GAAS, GAAP, and other nationally-recognized accounting standards. “In deciding whether an administrative agency has exceeded its rulemaking powers, the determinative factor is whether the rule's provisions are ‘in harmony’ with the general objectives of the statute.” *Williams v. Texas State Bd. of Orthotics & Prosthetics*, 150 S.W.3d 563, 568 (Texas App. -- Austin 2004, no pet.), citing *Edgewood Indep. Sch. Dist. v. Meno*, 917 S.W.2d 717, 750 (Tex. 1995); *Patient Advocates of Tex. v. Texas Workers Comp. Comm'n*, 80 S.W.3d 66, 75 (Tex. App.-- Austin 2002), *aff'd in part*, 136 S.W.3d 643 (Tex. 2004). In order to determine whether a rule is in harmony with an act's general objectives, “courts must look to all applicable provisions of that act, rather than only one particular section.” *Williams*, 150 S.W.3d at 568 (emphasis added). Plaintiffs, however, urge the court to simply consider out of context one small section of the accountancy act, Tex. Occ. Code Ann. § 901.502(6), rather than the entirety of Section 901.502 or the role that Section 901.502 plays in the Board's statutory mission of protecting the public.

In *Chalifoux v. Texas State Bd. of Med. Examiners*, No. 03-05-00320-CV, 2006 Tex. App. LEXIS 9598 (Tex. App.-- Austin Nov. 1, 2006, pet. denied) (mem. opinion), the construction of several rules promulgated by the Texas State Board of Medical Examiners was at issue. The court recognized that the board's rules on medical standards of care were reflections of the board's interpretation of the statutory sections regarding the same. *Id.*, 2006 Tex. App. LEXIS 9598 at \*44 n.6. “Generally, if the construction given to a statute by the agency charged with its enforcement is reasonable and does not contradict the plain language of the statute, then it is entitled to serious consideration.”

*Id.*, citing *Continental Cas. Co. v. Downs*, 81 S.W.3d 803, 807 (Tex. 2002). Moreover, although not binding on the court, the board's interpretations and legal determinations that it employed in creating the rules at issue were relied upon by the court as "persuasive authority" with regard to the scope of statutes regarding medical standards of care. *Id.*

**4. The Board may bring disciplinary proceedings against a licensee for violations that do not rise to the level of gross negligence.**

Plaintiffs contend that the Board may not bring disciplinary proceedings against a licensee absent "gross negligence" on the licensee's part in the performance of his or her professional duties. This same issue was considered by the Court of Appeals of Texas in *Chalifoux, supra*. Dr. Chalifoux claimed that the medical board's conclusion of law that he "violated an accepted medical standard of care" did not support the board's subsequent conclusion that he failed to practice medicine in an acceptable professional manner and committed unprofessional or dishonorable conduct that was likely to deceive or defraud the public. Chalifoux maintained that the medical board misinterpreted Tex. Occ. Code Ann. §§ 164.051(a)(6) and 164.052(a)(5) because the legislature intended for the sections to address grossly immoral, dishonorable, or disreputable acts in connection with the practice of medicine. Similar to the Plaintiffs, he averred that a violation of the sections at issue required "more than the mere deviation or violation of an accepted medical standard" and that the sections were designed to address a complete "disregard of the public health and welfare" or grossly negligent conduct.

The Court of Appeals disagreed, explaining that,

[t]he legislature could have required a finding of actual injury or grossly negligent conduct before permitting the Board to discipline a physician under sections 164.051(a)(6) and 164.052(a)(5) of the Act. Or it could have delineated a tort standard for determining when discipline is appropriate. It did neither. Instead, the legislature expressly provided the

Board with the authority to take disciplinary action against a physician who either commits unprofessional or dishonorable conduct that is likely to deceive or defraud the public or fails to practice medicine in an acceptable professional manner consistent with public health and welfare.

*Chalifoux*, 2006 Tex. App. LEXIS 9598 at \*46-47. The court concluded that “construing these sections to require egregious or grossly negligent conduct would unnecessarily limit the scope of the statutes.” *Id.*, 2006 Tex. App. LEXIS 9598 at \*47. The same can be said for Plaintiffs’ attempts to rein in the Board’s disciplinary powers as contemplated by the Texas legislature.

**B. The GAAS and GAAP are not unconstitutionally vague as disciplinary standards without a scienter element.**

**1. The Texas legislature did not intend for scienter to be an element.**

Plaintiffs contend that the GAAP and GAAS are unconstitutionally vague as disciplinary standards without a scienter element. Once again, Plaintiffs seek to engraft some meaning or create an interpretation of Tex. Occ. Code Ann. §§ 901.502 (6) and 12(B) that is simply not there. If the Texas legislature had intended that a practitioner must willfully or knowingly violate the rules of professional conduct adopted by the Board in order for the conduct to be a violation subject to disciplinary action, it would have inserted that language in the statute. *Chalifoux*, 2006 Tex. App. LEXIS 9598 at \*46 (Texas legislature could have required a finding of grossly negligent conduct or delineated a tort standard before a physician could be disciplined for unprofessional conduct, but it did neither). An example of such a limitation may be found in the accountancy act of Kansas, which provides that a licensee may be subject to discipline for a “willful violation of a rule of professional conduct.” Kan. Stat. Ann. § 1-312(a)(6).

**2. Plaintiffs do not specify how the GAAS and GAAP are unconstitutionally vague.**

Further, Plaintiffs do not explain how the provisions of the GAAS and GAAP they are accused of violating are unconstitutionally vague; Plaintiffs simply contend in a rather conclusory fashion that the nationally-recognized standards set out in the GAAS and GAAP are unconstitutionally vague in their entirety. In *Shapiro v. State Bd. of Accountancy*, 856 A.2d 864 (Pa. Commw. Ct. 2004), *cert. denied*, 546 U.S. 871 (2005), the petitioners maintained that the terms “professional” and “standard” as used in the Pennsylvania accountancy act were unconstitutionally vague because the terms did not provide “a reasonable, ascertainable standard by which the Petitioners were supposed to act” and were “subject to many different meanings.” The statute at issue defined unprofessional conduct as the “failure to comply with any standard promulgated by any recognized public or private standard-setting body that is applicable to the professional service being performed.” *Id.* at 880. These terms were not unconstitutionally vague, in the court’s opinion, and were sufficiently specific to prevent arbitrary and discriminatory application. *Id.* Although the petitioners complained that the terms were “subject to many different meanings,” they did not identify those possible meanings and also failed to explain how the terms were so indefinite as to prevent a court from determining legislative intent to any reasonable degree of certainty. *Id.*

**3. The need to exercise professional judgment in the application of the GAAS and GAAP does not make these nationally-recognized standards unconstitutionally vague.**

The crux of the Plaintiffs’ unconstitutionally vague argument is found at the bottom of page six of Plaintiffs’ Reply in Support of Motion for Final Summary Judgment. There, Plaintiffs state that “[t]he constitutional infirmity of reinforcing GAAS

and GAAP as strict liability disciplinary rules stems from the fact that an interpretation of these complex rules requires the exercise of professional judgment.”<sup>1</sup> Two of the cases cited by Plaintiffs in support of this statement are not cases regarding a disciplinary proceeding in an office of administrative hearings (or before a board of accountancy as is the procedure in other states) – rather, they are civil actions involving accountants who were alleged to have been negligent or committed professional malpractice. Plaintiffs cite *Ling v. BDA&K Bus. Servs., Inc.*, 261 S.W.3d 341, 348 (Tex. App. -- Dallas 2008, no pet.) and *Greenstein, Logan & Co. v. Burgess Mktg., Inc.*, 744 S.W.2d 170, 185 (Tex. App. -- Waco 1987, writ denied) for the proposition that expert testimony is required for showing how CPAs breached a standard of care or failed to comply with the GAAS. However, in both of these cases, the accountants charged with the violations recognized the applicability of standards such as the GAAS to CPAs, as well as the necessity for CPAs to make judgment calls when performing their professional duties. See *Ling*, 261 S.W.3d at 348 (“The Accountants do not dispute the AICPA standards govern accountants’ conduct or that an accountant is required to form a good faith belief concerning the positions taken in a tax return.”) Indeed, the Court in *Greenstein* spoke of “recognized industry standards, such as the ‘Generally Accepted Auditing Standards,’” the violation of which was not contested by the defendant accounting firm. *Greenstein*, 744 S.W.2d at 185 (emphasis added). The experts in *Greenstein* were instead used to establish whether the firm’s failure to comply with the GAAS was negligence and proximately caused the client’s damages. *Id.* The need for expert testimony, whether in

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<sup>1</sup> It is not entirely clear whether Plaintiffs are referring to an exercise of judgment by the individual CPA charged with violating a board’s statutes or professional conduct rules or by the Board in its disciplinary proceedings. For purposes of this argument, NASBA will assume that Plaintiffs are referring to an exercise of judgment by both the Board and the individual CPA.

an administrative hearing or a court trial, is not justification for an alleged failure to comply with professional standards.

Plaintiffs' reliance on *Checkosky v. SEC (In re Checkosky)*, 23 F.3d 452 (D.C. Cir. 1994) is equally misplaced. The rule that Checkosky was charged with violating, 17 C.F.R. § 201.102(e)(1)(ii), did not internally reference any nationally recognized standards such as GAAS or GAAP (although the Commission did employ those standards as a gauge by which to determine whether the accountant was in violation). It simply stated that "[t]he Commission may censure a person or deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found by the Commission after notice and opportunity for hearing in the matter: ... (ii) To be lacking in character or integrity or to have engaged in unethical or improper professional conduct." 17 C.F.R. § 201.102 was amended by the SEC in 1998 as the result of the adverse finding in *Checkosky* case cited by the Plaintiffs and a subsequent decision after remand in the same case, *Checkosky v. SEC*, 139 F.3d 221, 227 (D.C. Cir. 1998), where the court ordered that the charges against the CPA be dismissed due to the SEC's inability to adequately explain its interpretation of its rule regarding improper professional conduct. As amended, the Rule 201.102 sets out standards for "improper professional conduct" by an accountant, defining it as "intentional or knowing conduct, including reckless conduct that results in a violation of applicable standards." 17 C.F.R. § 201.102(e)(1)(iv)(A). This is far below the scienter requirement advocated by Plaintiffs. Indeed, in *Marrie v. SEC*, 374 F.3d 1196, 1204-05 (D.C. Cir. 2004), a case decided after Rule 201.102 was amended, the court held that two accountants could be

found in violation of the rule despite the SEC's failure to find that they had acted consciously or deliberately violated applicable standards.

Finally, Plaintiffs cite *Colautti v. Franklin*, 439 U.S. 379 (1979), for the proposition that "strict liability, quasi-criminal sanctions" cannot be imposed by the Board for violations of professional standards that might require a CPA to make a judgment call as to the application of those standards to a particular accounting engagement. *Colautti*, which involved the standard of care to be used by a physician performing an abortion, is inapposite. In *Colautti*, the statute was held invalid because the fetus viability determination requirement failed to provide physicians with fair notice of what was required. For the reasons previously stated, no such fair notice problem exists here. In addition, *Colautti* has since been limited and explained by a subsequent Supreme Court case, *Webster v. Reproductive Health Servs.*, 492 U.S. 490, 517 (1989), which observed that constitutional law in the area of abortion regulation is "a virtual Procrustean bed." State statutes regulating judgment calls by CPAs are not burdened with the flaws contained in these statutes regulating physicians who perform abortions.

Similar to the judgments that physicians must make, CPAs must make judgments, based upon the applicable auditing standards and interpretations of those standards, about the manner in which to interpret financial data. Rule 501.60 of the Texas Administrative Code specifically sets out authorities that a CPA may consult in determining whether an audit complies with generally accepted auditing standards. These include "statements on auditing standards issued by the American Institute of Certified Public Accountants, auditing standards included in Standards for Audit of Government Organizations, Programs, Activities and Functions issued by the United States General Accounting

Office, Public Company Accounting Oversight Board, and ... other pronouncements having similar generally recognized authority, [which] are considered to be interpretations of generally accepted auditing standards.” 22 Tex. Admin. Code § 501.60.

In a recent case rejecting a vagueness challenge to provisions of the Kansas Rules of Professional Conduct for attorneys, the Kansas Supreme Court observed that “[t]his case involves an administrative action, *i.e.*, a disciplinary action, not a criminal offense. In evaluating constitutional challenges for vagueness, courts afford greater leeway to provisions regulating business than to those proscribing criminal conduct.” *In re Comfort*, 284 Kan. 183, 199, 159 P.3d 1011, 1024 (2007), citing *Papchristou v. City of Jacksonville*, 405 U.S. 156, 162 (1972). *Papchristou* is also cited by *Colautti*, a case heavily relied upon by Plaintiffs. The instant case is also related to a disciplinary action, and the challenged rules of professional conduct here are provisions regulating the business of accountancy.

Plaintiffs have unwittingly made a telling statement about the nature of occupational licensing boards in their assertion that reliance upon the standards embodied in the GAAS and GAAP in disciplinary actions against CPAs is unconstitutional because “interpretation of these complex rules requires the exercise of professional judgment.” State occupational licensing boards are particularly suited to making informed decisions about the professional standards applicable to the members of a profession. The majority (all in some states) of occupational licensing board members are themselves licensees with substantial experience in their field. They draw upon their professional experience and knowledge during their tenure on the board, including the decision-making process



that is involved in instituting or ruling upon disciplinary proceedings. They are supposed to use their professional judgment when weighing disciplinary matters related to the protection of the public. That is why they were appointed or elected to the board in the first place!

Because of the expertise of occupational licensing board members, courts will defer to their discretion in matters of professional practices. Indeed, pursuant to Tex. Gov't Code § 2001.174, a reviewing court "may not substitute its judgment for the judgment of the state agency on the weight of the evidence on questions committed to agency discretion." In *Christensen*, the Wyoming Supreme Court declined to make a factual analysis of the case, saying that "[t]he authority to make discretionary decisions about standards of CPA auditing practices is invested exclusively in the State Board." 838 P.2d at 727. Further, the delegation of authority by the state regulatory agency in requiring certified public audits to conform to national standards of accounting was not improper. *Id.* The Louisiana Court of Appeals in *Rabb v. State Bd. of Certified Pub. Accountants of La.*, 893 So. 2d 904 (La. Ct. App. 4th Cir. 2004), *cert. denied*, 896 So. 2d 1045 (La. 2005), held that the Louisiana's board's revocation of a CPA's license for failure to comply with professional standards was not an abuse of discretion. *Id.* at 908. Indeed, the Board should be permitted to exercise its professional judgment and discretion regarding the Plaintiffs' conduct in this matter.

### CONCLUSION

For the foregoing reasons, Amicus Curiae NASBA supports Defendant's Opposition to Plaintiffs' Motion for Final Summary Judgment.

This the 2nd day of October, 2009.

Respectfully submitted,

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STATE BOARDS OF ACCOUNTANCY**

## **CERTIFICATE OF SERVICE**

I hereby certify that on the 2nd day of October, 2009, I electronically filed the foregoing with the Clerk of Court using the TexasOnline E-File system and certify that a true and correct copy of the foregoing has been forwarded to the following counsel of record:

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This the 2nd day of October, 2009.

/s/ Mary A. Keeney  
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