UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-20794

In the Matter of	:
	:
Halpern & Associates, LLC	:
and Barbara Halpern, CPA	:
	:
Respondents.	:
	:

DIVISION OF ENFORCEMENT'S OPPOSITION TO RESPONDENTS' MOTION FOR JUDGMENT ON THE PLEADINGS

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The Division of Enforcement ("Division") of the Securities and Exchange Commission ("Commission") respectfully submits this opposition to Halpern & Associates, LLC ("H&A") and Barbara Halpern's ("Halpern" and collectively "Respondents") May 13, 2022 Motion for a Ruling on the Pleadings (the "Motion").[1] The Order Instituting Proceedings ("OIP") in this matter alleges that Respondents (an accounting firm and its managing member) failed to live up to their obligations, both procedurally and substantively, in conducting the 2015 and 2016 audits of ACP X, LLP ("ACP X"), a private equity fund. Respondents' audit failures are twofold. First, Respondents accepted financial valuations from ACP X regarding a major investment of the fund, despite the fact that ACP X had a history of providing inaccurate projections regarding that investment. Second, Respondents accepted the valuations from ACP X, despite knowing the valuations did not reflect actual revenues from the investment, market conditions, or H&A's own analysis.

I. The Legal Standard for a Ruling on the Pleadings.

The Motion seeks a ruling on the pleadings on the OIP in this matter under Rule 250(a), which provides for a ruling on the pleadings. As the Commission has explained:

> Rule 250(a) . . . permits any party, no later than 14 days after a respondent's answer has been filed, to move for a ruling on the pleadings on one or more claims or defenses. Rule 250(a) thus permits a respondent to seek a ruling as a matter of law based on the factual allegations in the OIP and permits either party to seek a ruling as a matter of law after the filing of an answer. We have recognized that the procedure provided under Rule 250(a) is analogous to that applicable in federal district court to motions to dismiss and for judgment on the pleadings under Rules 12(b)(6) and 12(c) of the Federal Rules of Civil Procedure. We have also considered precedent construing the Federal Rules of Civil Procedure when construing our Rules of Practice (although that precedent does not bind us when doing so). As with a motion under Federal Rules of Civil Procedure 12(b)(6) and 12(c), to succeed on a motion under Rule 250(a), ***a movant must establish that even accepting all of the nonmovant's factual***

[1] The Order Instituting Proceedings is hereinafter referred to as "OIP."

allegations as true and drawing all reasonable inferences in the non-movant's favor, the movant is entitled to a ruling as a matter of law.

ERHC Energy, Inc. et al., Exchange Act Release No. 90517, 2020WL 6891409, at *4 (November 24, 2020) (emphasis added).

The Commission has explained that motions under Commission Rule 250(a) "generally correspond to certain dispositive motions that may be filed in federal court under the Federal Rules of Civil Procedure," and that Rule 250(a) is analogous to Rules 12(b)(6) and 12(c). *See Amendments to the Commission's Rules of Practice*, File No. S7-I 8-15, 2016 WL 3853756, n. 100 (July 13, 2016). A motion for judgment on the pleadings under Fed. R. Civ. P. 12(c) "is decided under the same standard applicable to motion to dismiss under Fed. R. Civ. P. 12(b)(6)." *Cobalt Multifamily Investors I, LLC v. Arden*, 46 F. Supp. 3d 357, 359 (S.D.N.Y. 2014) *citing Johnson v. Rowley*, 569 F.3d 40, 43 (2d Cir. 2009).

II. Background.

Halpern & Associates, LLC is an accounting firm based in Connecticut. (OIP ¶ 2.) Halpern is its managing member and 90% owner. (OIP ¶ 3.) The OIP alleges that Respondents engaged in improper professional conduct in their 2015 and 2016 audits of private equity fund ACP X, LLP ("ACP X"). (OIP ¶ 1.) In 2019 the Office of the New York Attorney General ("NYAG") charged Laurence Allen, who controlled ACP X, with defrauding investors. (*Id*. fn. 3) Allen had invested at least 20% of ACP X's funds in securities issued by NYPPEX Holdings, LLC ("Holdings"), the owner of a registered broker-dealer that Allen also controlled. (*Id*.) H&A was ACP X's auditor. (OIP ¶ 8.) Halpern was the engagement partner for the audits of ACP X. (OIP ¶¶ 1 & 8.) As early as 2011, Halpern and other accountants at H&A expressed concern to Allen regarding the grossly inflated estimated revenue projections Allen was using to arrive at his valuation of Holdings. (OIP ¶ 10.) For each audit year, Allen provided Respondents

with a one page document called "Fair Valuation Analysis" ("FVA") referencing Holding's past revenues, expenses, and earnings as well as projected future revenues and profits. (*Id*.) However, the OIP specifically alleges that the FVAs "lacked an objective basis, ignored material information (including two decades of Holdings' operating history), and was based on unachievable future revenue and corporate growth." (*Id*.) In connection with ACP X's 2011 audit, although Holding's revenue for the first three quarters of 2011 was $2.3 million, Allen's projected revenue for 2011 in the FVA was $26 million. (OIP ¶ 11.) Allen successfully resisted H&A's efforts to obtain additional audit information to support the revenue projections, suggesting that the request could lead to a termination of the relationship. (OIP ¶ 11.) For example, for the 2014 Audit, although Holding's revenue through September of 2015 were less than $1 million, Allen's projected revenue in the FVA for 2015 was $10.5 million. (OIP ¶ 12.) That year, with the $10.5 million dollar 2015 revenue projection, the FVA valued Holding's shares at $.76 per share. (*Id*.) Allen agreed to adjust 2015 projected revenue, however, he then added an additional two years of revenue, adjusting the metrics to arrive at the same valuation of $.76 per share. (*Id*.) With respect to the 2015 and 2016 audits of ACP X, Allen declined Respondents' request to obtain an independent evaluation of the value of Holdings. (OIP ¶ 13.) Dating back to 2011 audits of ACP X (which were conducted by Respondents), Allen had repeatedly made changes to the valuation formula he utilized in the FVAs, using different holding periods, price/revenue multipliers, and implied investor discounts. (OIP ¶¶ 14 – 16.) These inconsistencies continued during the 2015 and 2016 audits. (*Id*.) With respect to the 2015 and 2016 ACP X audit, Allen proffered (and Respondents accepted) FVAs that were "not in line with the actual revenues of the company, other trends in the market, or H&A's own analysis." (OIP ¶ 19.) H&A and Halpern failed to perform additional audit procedures necessary to resolve

their doubts about the reliability of the ACP X valuation analysis, including the accuracy of the revenue projections and the calculations used. (OIP ¶ 18.)

Finally, Respondents' motion is devoid of any mention that the OIP specifically alleges that there has already been a finding in New York State Court that Allen: (i) defrauded ACP X's investors of at approximately $6 million by investing ACP X's funds into Holdings, which was contrary to ACP X's prospectus; and (ii) misappropriated $3.4 million from ACP X, characterized as carried interest. (OIP fn. 3.)

III. The Institution of this Proceeding Pursuant to 102(e)(1)(ii) of the Commission's Rules of Practice.

Under Rule 102(e)(1)(ii) of the Commission's Rules of Practice, which has been codified into Section 4C of the Exchange Act, the Commission may censure or deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person found to have engaged in, among other things, improper professional conduct. Regarding accountants, Rule 102(e)(1)(iv)(B) and Section 4C(b) provide that the following two types of conduct constitute "improper professional conduct":

(1) A single instance of highly unreasonable conduct that results in a violation of applicable professional standards in circumstances in which an accountant knows, or should know, that heightened scrutiny is warranted, or

(2) Repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards that indicate a lack of competence to practice before the Commission.

"Applicable professional standards" for auditors primarily refers to Generally Accepted Accounting Principles, Generally Accepted Accounting Standards ("GAAS"), the American Institute of Certified Public Accountants Code of Professional Conduct, and Commission regulations. *See Amendment to Rule 102(e) of the Commission's Rules of Practice,* Securities Act Release No. 7593 (Oct. 19, 1998)

("*Rule 102(e) Release*"). With respect to audits of private equity fund financial statements (which is the underlying subject of, the GAAS in effect during the relevant period is embodied in various Statements on Auditing Standards ("SAS"), as well as Codification of Statements on Auditing Standards ("AU-C"), both issued by the Auditing Standards Board of the AICPA.

"Highly unreasonable" conduct under subsection (B)(1) is an intermediate level of misconduct, between recklessness and ordinary negligence:

> The "highly unreasonable" standard in subparagraph (B)(1). . . is an intermediate standard, higher than ordinary negligence but lower than the traditional definition of recklessness used in cases brought under Section 10(b) and Rule 10b-5 of the Exchange Act. The "highly unreasonable" standard is an objective standard. The conduct at issue is measured by the degree of the departure from professional standards and not the intent of the accountant.
>
> . . . .
>
> "Heightened scrutiny" would be warranted when matters are important or material, or when warning signals or other factors should alert an accountant of a heightened risk, or as set forth in applicable professional standards.

Rule 102(e) Release.

"Unreasonable" conduct under subsection (B)(2) is a level of misconduct requiring a showing of ordinary or simple negligence:

> "The term "unreasonable," as distinguished from the term 'highly unreasonable' used in subparagraph (B)(1), connotes an ordinary or simple negligence standard. The lower standard of culpability is justified in this instance because the repetition of the unreasonable conduct may show the accountant's lack of competence to practice before the Commission. If an accountant fails to exercise reasonable care on more than one occasion, the Commission's processes may be threatened. More than one violation of applicable professional standards ordinarily will indicate a lack of competence."

Rule 102(e) Release.

"The highly unreasonable standard is an intermediate one, higher than ordinary negligence but lower than recklessness." *In the Matter of Halpern & Associates, LLC*, Rel. No. 939, 2016 WL 64862, *21 (Jan. 5, 2016).[2] Negligent deviations from GAAS are deemed unreasonable. *Id*.

[2] Respondents have been previously found to have been highly unreasonable in committing violations of GAAS. H&A was censured, and Halpern received a one year suspension from practicing before the Commission. *Id*. at *23, 34-35. The prior matter dealt with whether, in

IV. Respondents Are Not Entitled to a Ruling on the Pleadings.

Respondents assert that they are entitled to a ruling on the pleadings because "despite alleging that the OIP concerns the 2015 and 2016 audits, the OIP alleges no specific facts tending to show that the Respondents engaged in improper professional conduct with respect to those audits." (Motion at 3.) This is incorrect.

The OIP alleges that the 2015 and 2016 audits were procedurally deficient, insofar as the Allen repeatedly changed the valuation methodology underlying ACP X's ownership interest in Holdings, and refused to obtain an outside valuation despite Respondents' requests that he do so. (OIP ¶¶ 13-16.) In addition to the procedural deficiencies, the OIP alleges that the valuations proffered by Allen, which were accepted by Respondents in the 2015 and 2016 audits, were "not in line with the actual revenues of [Holdings]" – and that Respondents knew it. (OIP ¶ 19.) In so doing, Respondents violated four provisions of GAAS as described below in sub-section A.

A. The Provisions of GAAS to which Respondents Failed to Adhere.

GAAS requires that an auditor comply with all relevant ethical requirements relating to financial statement audits, which includes due care (Codification of Statements on Auditing Standards ("AU-C") 200.16). (OIP ¶ 18.) The auditor must also exercise professional judgment in planning and performing an audit (AU-C 200.18), by obtaining sufficient appropriate audit evidence, (AU-C 500A.06), and by maintaining an attitude of professional skepticism, which

conducting a faulty audit, Respondents caused a registered entity to violate its net capital requirements.

includes a questioning mind and a critical assessment of audit evidence. (AU-C 200.14 and 17.) (*Id*.) The OIP alleges that Respondents violated all four of these requirements. (OIP ¶¶ 18-19.)

B. The Specific Alleged Violations of GAAS in the Conduct of the 2015 and 2016 Audits of ACP X.

i. Respondents Failed to Obtain Sufficient Evidence of Asset Valuation.

Since at least 2011, Respondents were aware that Allen was making unrealistic projects about Holding's revenues, which were repeatedly not met. (OIP ¶¶ 11-12.) Nonetheless, Respondents continued to accept Allen's FVAs for the 2015 and 2016 audits, even though they presented projections that were "not in line with actual revenues, markets trends, or H&A's own analysis." (OIP ¶ 19.) Such procedural failures constitute unreasonable or highly unreasonable conduct for an auditor. *See, In the Matter of Barry C. Scutillo*, Rel. No. 1822, 2003 WL 21738818, at *6 (July 28, 2003) ("GAAS provides that representations from management are not a substitute for the application of auditing procedures necessary to afford a reasonable basis for an auditor's opinion"); *In the Matter of Oprins*, *CPA, et al*. Rel. No. 411, 2010 WL 5376531, at *25 (Dec. 28, 2010) ("GAAS expressly states that representations of management 'are not a substitute for the application of those auditing procedures necessary to afford a reasonable basis for an opinion regarding the financial statements under audit.' [Citation Omitted].") Given Allen's history of inaccurate predictions of future revenue streams dating back to 2011, accepting his future predictions constituted unreasonable or highly unreasonable conduct. *See Scutillo*, 2003 WL 21738818 at *6 ("If an auditor is in substantial doubt about any assertion of material significance, he or she must not form an opinion until sufficient competent evidential matter has been obtained to remove that doubt.") In short, the OIP alleges Respondents failed to exercise the due care, professional judgment and skepticism required of auditors, or perform a critical assessment of audit evidence. *See e.g. Halpern & Associates, LLC*, 2016 WL 64862,

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*30. ("'Due professional care [also] requires the auditor to exercise *professional skepticism* … [which] is an attitude that includes a questioning mind and a critical assessment of audit evidence.' AU § 230.07.") Additionally, the OIP alleges that Respondents failed to take steps necessary to resolve their doubts about the accuracy of the FVAs. *See e.g. id*., *31 (Where an auditor allows itself to be satisfied by documents it has doubts about, it violates the standard of professional skepticism.)

Respondents attempt to argue that the allegations in the OIP constitute a "normal back-and-forth" between auditor and client. (Motion at 7.) This is a factual conclusion the Division disputes, and that cannot be drawn at this state of litigation. However, the OIP specifically alleges that the FVAs proffered to Respondents were "not in line with actual revenues, market trends, or H&A's own analysis." Respondents offer no citation to GAAS or case law to support the idea that if an auditor receives financial projections from its client that it knows or suspects to be inaccurate, that the auditor may freely rely upon it. In fact, the opposite is true. *See Scutillo*, 2010 WL 5376531, *6 ("If an auditor is in substantial doubt about any assertion of material significance, he or she must not form an opinion until sufficient competent evidential matter has been obtained to remove that doubt.") Respondents' reliance on the Supreme Court's decision in *Ashcroft v. Iqbal*, 566 U.S. 662, 678, 129 S. Ct. 1937 (2009) and *Hayden v. Paterson*, 594 F.3d 150, 161 (2d Cir. 2010) (quoting *Ashcroft)* is likewise misplaced. (Motion at 5.) *Ashcroft* and *Hayden* hold that a plaintiff may not merely rely on conclusory allegations in a complaint. In the present case, the OIP: (i) identifies that Respondents knew that Allen was an unreliable creator of financial projections (based upon his history); (ii) identifies the documents (the FVAs) created by Allen during the 2015 and 2016 audits that underlie this action and which were relied upon by Respondents; (iii) alleges that Respondents knew that the FVAs created by Allen were

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inconsistent from year-to-year; (iv) alleges that Respondents knew the FVAs were not in line with Holdings' actual revenues, market conditions, or H&As own analysis; and (v) alleges that Respondents requested that Allen/ACP X obtain a third-party valuation of the assets, but gave up in lights of their client's refusal and signed off on ACP X's audits despite their own concerns about Allen's valuation of Holdings. (OIP ¶¶ 1, 10-16, 19.)

ii. Violations of GAAS in the Issuance of Audit Reports Containing Inaccurate Valuations of Holdings.

Not only did Respondents fail to follow proper procedures with respect to the 2015 and 2016 ACP X audits, but they signed off on audits based upon FVAs provided by Allen that Respondents knew or suspected were inaccurate. The OIP specifically alleges that Respondents approved the issuance of 2015 and 2016 audit reports for ACP X despite having strong indications that Allen's valuations of Holdings' securities were "not in line with actual revenues of the company, other trends in the market, or H&A's own analysis." (OIP ¶¶ 1 & 19.) In conducting the 2015 and 2016 audits, Respondents relied upon FVAs created by Allen, even though projections in prior year's FVAs "had not come close to being met." (OIP ¶ 13.)

As noted above, Allen both had a history of providing FVAs to Respondents that contained inaccurate projections. If an auditor knows that an unreliable individual is giving the auditor documents that the auditor does "not fully understand or can verify," to rely upon such documents (as Respondents did with respect to Allen's FVAs) constitutes highly unreasonable conduct under GAAS. *See In the Matter of Halpern & Associates, LLC*, 2016 WL 64862, *32 (Relying upon screenshots of brokerage account statements instead of actual account statements deemed highly unreasonable.)

Respondents' motion argues that the OIP does not allege that investors in ACP X were harmed by the faulty audits. (Motion at 8.) This is irrelevant. Respondents are not charged with

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causing the fraud perpetrated by Allen. The relevant question is whether Respondents acted highly unreasonably or unreasonably in conducting the audits of ACP X. The fact that Allen was defrauding investors in ACP X is relevant, but it is not necessary to prove that Respondents failed to conduct the 2015 and 2016 audits of ACP X in accordance with their professional obligations.

C. Respondents Engaged in Improper or Unethical Conduct Under Rule 102(e).

Respondents argue that as a predicate, the Division must allege in the OIP that Respondents lack competence to perform their duties as auditor under Rule 102(e)(1)(iv)(B). (Motion at 8.) This argument inverts Rule 102(e). Invoking the word "competence" is not required under the Rule. Rather, the OIP must allege that Respondents committed either a single act that it highly unreasonable under circumstances where they knew heightened scrutiny was warranted, or multiple acts that are unreasonable and indicate a lack of competence on the part of the auditor. Moreover, paragraph 17 of the OIP identifies the relevant text of Rule 103, including the term "competence" and paragraph 21 alleges that Respondents' violated the Rule. (OIP ¶¶ 17 & 21.)

CONCLUSION

Accordingly, the Division respectfully requests that the Commission deny Respondents Motion for a Ruling on the Pleadings.

Dated: June 3, 2022

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I caused true copies of the Division of Enforcement's Opposition to Respondent's Motion to Dismiss the Order Instituting Proceedings to be served on the following on June 3, 2022, via electronic mail:

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