UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
November 29, 2004

Administrative Proceeding
File No. 3-11748

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| In the Matter of<br><br>KENNETH L. RUBIN, CPA and<br>MICHAEL W. LEWIS, CPA<br><br>Respondents. | ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE |

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be instituted against Respondents Kenneth L. Rubin ("Rubin") and Michael W. Lewis ("Lewis") ("Respondents") pursuant to Rule 102(e) of the Commission's Rules of Practice.[1]

II.

After an investigation, the Division of Enforcement and the Office of the Chief Accountant allege that:

[1] Rule 102(e)(1)(ii) of the Commission's Rules of Practice provides, in relevant part, 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 … to have engaged in … improper professional conduct…." Rule 102(e)(1)(iv) provides in relevant part that: "[w]ith respect to persons licensed to practice as accountants, 'improper professional conduct' under Rule 102(e)(1)(ii) means: (A) intentional or knowing conduct, including reckless conduct, that results in a violation of applicable professional standards; or (B) either of the following two types of negligent 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…"

## RESPONDENTS

1. Rubin, age 47, resides in St. Louis, Missouri and is licensed as a certified public accountant ("CPA") in Missouri. Rubin has been associated with the accounting firm of Rubin, Brown, Gornstein & Co., LLP ("RBG") since 1979, and has been a partner since 1986.

2. Lewis, age 35, resides in St. Louis, Missouri and is licensed as a CPA in Missouri. Lewis has been associated with RBG since 1992 and has been a manager since 1998.

## RELATED ENTITIES

3. Eisner Securities, Inc. ("ESI") was registered with the Commission as a broker-dealer pursuant to Section 15(b) of the Securities Exchange Act of 1934 effective May 15, 1996. On September 26, 2001, ESI notified the Commission and the National Association of Securities Dealers ("NASD") that it was not in compliance with its $50,000 minimum net capital requirement and was ceasing operations immediately. On October 2, 2001, ESI voluntarily withdrew its registration with the Commission as a broker-dealer, which became effective on December 2, 2001. On October 30, 2001, ESI was placed in SIPC liquidation.

4. RBG is an accounting firm located in St. Louis, Missouri. RBG was ESI's audit firm throughout its existence. Rubin was the engagement partner and Lewis was the engagement manager on RBG's audit of ESI's financial statements for its fiscal year ended December 31, 2000.

## ESI'S NET CAPITAL VIOLATIONS AND FAILURE TO COMPLY WITH GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

5. From 1997 through 2000, Joseph E. Erwin ("Erwin") was employed by ESI as the branch manager of its Columbus, Ohio, office. During that time, Erwin misappropriated approximately $2 million from at least 11 ESI customer accounts.

6. ESI terminated Erwin in September 2000 and conducted an internal investigation of his illegal activities. In October 2000, ESI created a spreadsheet of the exact amount misappropriated from each customer account, totaling approximately $2 million. Erwin's misappropriations represented more than 100% of ESI's total assets.

7. By at least November 2000, ESI initiated contact with the customers affected by Erwin's misappropriations to resolve their claims. In November 2000, ESI sent letters to most, if not all, of the customers affected by Erwin's misappropriations promising to handle their claims directly if the carrier of ESI's errors and omissions policy had not paid the claims by March 31, 2001. In December 2000, ESI, through counsel, sent letters to most, if not all, of the customers affected by Erwin's misappropriations identifying the exact amount of each customer's loss and saying that "[ESI] intends to restore your loss as promptly as possible." The December 2000 letters

went on to offer to restore to the customer 50% of the amount misappropriated from their accounts, in cash, immediately, with the remaining 50% paid out over 18 months, with interest. At the time ESI made these offers to repay its customers, ESI did not have sufficient reserves to pay the up-front 50% cash reimbursements.

8. On January 23, 2001, in the case of United States of America v. Joseph E. Erwin, Case No. CR2-01-012, in the United States District Court for the Southern District of Ohio, Eastern Division, Erwin pled guilty to one count of mail fraud (18 U.S.C. §1341) and one count of wire fraud (18 U.S.C. §1343), and was subsequently sentenced to ten years incarceration and ordered to make restitution of $2,013,404.15.

9. From at least October 2000 through September 2001, ESI did not include the liability owed to customers resulting from Erwin's misappropriations in ESI's net capital computations, and books and records. ESI also did not include the liability owed to customers resulting from Erwin's misappropriations in ESI's FOCUS reports filed with the NASD for the quarters ended December 31, 2000, March 31, 2001, and June 30, 2001. ESI also failed to include the liability incurred as a result of Erwin's misappropriations in its audited financial statements for its fiscal year ended December 31, 2000. Had ESI accrued the amount of Erwin's misappropriations as a liability between October 2000 and September 2001, then its net capital computations, books and records, and FOCUS reports would have reflected a net capital deficit ranging between $1.7 million and $2 million.

10. ESI's audited financial statements for its fiscal year ended December 31, 2000 were not prepared in accordance with Generally Accepted Accounting Principles ("GAAP"). The controlling accounting principle for determination of whether to accrue a loss contingency is Statement of Financial Accounting Standards No. 5 ("FAS 5"). Paragraph 8 of FAS 5 required ESI to accrue the amount misappropriated as a liability if it was probable that a liability had been incurred as a result of Erwin's misappropriations and if the amount of loss could be reasonably estimated. Under this analysis, it was probable that a liability had been incurred by ESI because Erwin was an ESI branch manager and he stole ESI's customers' funds using the special access that ESI granted him to the clearing firm's computer system, which ESI failed to monitor. Further, ESI never disputed its liability with the customers affected by Erwin's misappropriations and it initiated contact with Erwin's customers to resolve their claims out-of-court by fully restoring their losses. The amount of loss for Erwin's misappropriations also was estimated by at least October 2000 when ESI created a spreadsheet of the exact amount misappropriated from each customer account.

11. From at least October 2000 through September 2001, ESI violated Section 15(c)(3) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 15c3-1. During this period, by use of the mails, or means or instrumentalities of interstate commerce, ESI effected transactions in, or induced or attempted to induce the purchase or sale of, securities (other than an exempted security (except a government security) or commercial paper, bankers' acceptances or commercial bills) in contravention of the rules and regulations prescribed by the Commission as necessary or appropriate in the public interest or for the protection of investors to provide safeguards with respect to the

financial responsibility and related practices of brokers and dealers. Rule 15c3-1, known as the "net capital rule," requires a broker-dealer to maintain a certain minimum ratio of net capital to aggregate indebtedness so that the broker-dealer's assets will be sufficiently liquid to enable it to meet all of its current obligations. From at least October 2000 through September 2001, ESI had a net capital deficit ranging between $1.7 and $2 million as a result of the liability created by Erwin's misappropriations.

12. Section 17(a) of the Exchange Act and Rule 17a-3 thereunder require that every registered broker-dealer make and keep current books and records reflecting, among other things, all liabilities and the firm's net capital computations. Rule 17a-5 also requires that registered broker-dealers such as ESI file quarterly FOCUS reports with the NASD and annual audited financial statements with the Commission. Implicit in these provisions is the requirement that information contained in a required book or record be accurate.

13. From at least October 2000 through September 2001, ESI did not include the liability owed to customers resulting from Erwin's misappropriations in ESI's net capital computations, and books and records. ESI also did not include the liability owed to customers resulting from Erwin's misappropriations in ESI's FOCUS reports filed with the NASD for the quarters ended December 31, 2000, March 31, 2001, and June 30, 2001. ESI also filed with the Commission its audited financial statements for its fiscal year ended December 31, 2000, which failed to include a liability for Erwin's misappropriations. Had ESI accrued the amount of Erwin's misappropriations as a liability between October 2000 and September 2001, then its net capital computations, books and records, and FOCUS reports would have reflected a net capital deficit ranging between $1.7 million and $2 million. Accordingly, ESI violated Section 17(a) of the Exchange Act and Rules 17a-3 and 17a-5 thereunder.

14. Section 17(a) of the Exchange Act and Rule 17a-11(b)(1) requires broker-dealers, like ESI, whose net capital declines below the minimum required pursuant to Rule 15c3-1 to give notice to the Commission of this fact, the same day. Rule 17a-11(d) also requires broker-dealers who fail to make or keep current books and records required by Rules 17a-3 to give notice to the Commission of this fact, the same day, specifying the books and records which have not been made or which are not current.

15. ESI failed to provide any notice or report to the Commission that it was out of compliance with its minimum net capital requirement and that it failed to keep current books and records from at least October 2000 through September 2001. Therefore, ESI violated Section 17(a) of the Exchange Act and Rule 17a-11 thereunder.

## RESPONDENTS' IMPROPER PROFESSIONAL CONDUCT

16. RBG's retainer letter to audit ESI's financial statements for its fiscal year ended December 31, 2000 was dated October 16, 2000. As engagement partner and engagement manager, Rubin and Lewis were responsible for ensuring that RBG's audit was conducted in accordance with Generally Accepted Auditing Standards ("GAAS"). Rubin and Lewis violated GAAS by failing to obtain sufficient competent evidential

matter to adequately evaluate the effect of Erwin's misappropriations on ESI's financial statements, failing to exercise due professional care in connection with the audit, and failing to render an accurate auditors' report.

17. Rubin and Lewis knew about Erwin's misappropriation of approximately $2 million from customer accounts before the audit began. The ESI audit plan discusses Erwin's alleged embezzlement of approximately $2 million of customers' money in two places: first, under the heading "key client issues and recent developments" and second, under the heading "inquiry of management" relating to the risk of fraud. Both discussions contain notations to review the attorney letters for further investigation. Based on Erwin's misappropriations, Rubin and Lewis also raised the audit risk of ESI's 2000 financial statements from a "low-to-moderate risk" engagement to a "moderate risk" engagement.

18. RBG conducted field work for the ESI audit from approximately January 30, 2001 until February 2, 2001. Rubin's and Lewis's sole audit procedure to obtain information to evaluate the effect of Erwin's misappropriations on ESI's financial statements aside from obtaining management's representations was to request that ESI send letters of audit inquiry to ESI's counsel relating to pending or threatened litigation, claims and assessments and unasserted claims and assessments that may call for financial statement disclosure. This procedure was RBG's standard audit procedure relating to pending and possible litigation that it employed with regard to all of its clients.

19. ESI sent a letter of audit inquiry dated January 22, 2001 to counsel handling the Erwin matters. ESI's letter advised counsel that ESI had represented to RBG that there were no unasserted claims that counsel had advised were probable of assertion and must be disclosed in accordance with FAS 5. ESI's letter requested that counsel furnish RBG with any explanation that counsel considered necessary to supplement ESI's representations, including an explanation of those matters as to which counsel's views may differ from ESI's representations. RBG received a copy of ESI's January 22, 2001 correspondence to counsel.

20. ESI also sent RBG a management representation letter dated February 2, 2001, which stated, in relevant part that: (1) "we are not aware of any . . . instances of errors or fraud involving management or employees that could have a material effect on the financial statements," and (2) "there are no unasserted claims or assessments that our lawyer has advised us are probable of assertion and must be disclosed in accordance with [FAS 5]."

21. By correspondence dated February 23, 2001, ESI's counsel provided RBG with an attorney letter that contradicted, rather than confirmed, ESI's representation that there were no unasserted claims against ESI that were probable of assertion and must be disclosed in accordance with FAS 5. In the attorney letter, counsel acknowledged that Erwin "misappropriated assets from some of the customers whom he serviced." The attorney letter identified and discussed in some detail two pending NASD arbitration proceedings relating to Erwin's misappropriations in which ESI was denying liability and had not yet made offers of settlement because, among other things, the claimants'

possible participation in or aiding the concealment of Erwin's misconduct and the lack of evidence that certain funds had been misappropriated by Erwin. However, the attorney letter also contained a section identifying and discussing "Unasserted Claims and Assessments," which stated:

> **<u>Unasserted Claims and Assessments</u>**
> Approximately ten other customers of Joseph E. Erwin were affected by his misconduct. [Counsel] has contacted each customer on behalf of ESI and initiated discussions in order to resolve any matters pertaining to Mr. Erwin's acts.

22. After receiving this letter, Rubin and Lewis failed to conduct any follow-up procedures to obtain additional information to evaluate the effect of the unasserted claims of the ten other Erwin customers on ESI's financial statements. Rubin and Lewis did not contact ESI's counsel or ESI regarding these unasserted claims. Rubin and Lewis did not request copies of documents relating to the unasserted claims. Rather, a handwritten note on the attorney letter by Lewis reflects that Lewis simply concluded that "appropriate disclosures made on f/s re: arbitration proceedings – based on response below – no accrual for potential claims appears necessary."

23. On February 26, 2001, RBG issued an audit report dated February 2, 2001 containing an unqualified opinion on ESI's financial statements for its fiscal year ended December 31, 2000. The auditors did not disclose in their report, or require accrual in the financial statements, a liability for the unasserted claims identified in the attorney letter. RBG's unqualified opinion stated that ESI's financial statements for the year ended December 31, 2000 were presented in conformity with GAAP and that RBG conducted its audit in accordance with GAAS.

24. ESI filed its audited financial statements in its annual FOCUS report for the year ended December 31, 2000 with the Commission on February 28, 2001.

25. Rubin and Lewis failed to obtain sufficient competent evidential matter to evaluate the effect of Erwin's $2 million misappropriation on ESI's financial statements. Rubin and Lewis knew that Erwin's misappropriations represented more than 100% of ESI's total assets. Rubin and Lewis identified Erwin's misappropriations as the key client issue in planning the ESI audit, and elevated the engagement risk on that basis. Yet, the only audit procedure they applied to Erwin's misappropriations aside from obtaining management's representations was RBG's standard practice of requesting attorney letters related to pending or possible litigation. Upon obtaining an attorney letter which, contrary to ESI management's representations, notified them of the existence of the unasserted claims of ten customers affected by Erwin's misconduct and that counsel had initiated contact with these customers to resolve any matters pertaining to Erwin's acts, Rubin and Lewis did nothing to obtain further information regarding the unasserted claims or the conflict between the representations of ESI management and counsel. Rubin and Lewis were in possession of conflicting information regarding the effect of Erwin's misappropriation on ESI's financial statements and took no steps to resolve the conflict.

26. Rubin and Lewis failed to exercise due professional care in performing the ESI audit. As discussed above, Rubin and Lewis also failed to obtain sufficient competent evidential matter to evaluate the effect of Erwin's $2 million misappropriation on ESI's financial statements. In addition, Rubin and Lewis failed to exercise professional skepticism in relying on ESI management's representations, which were in conflict other information in Rubin and Lewis' possession. ESI's management represented that it was not aware of any instances of errors or fraud involving management or employees that could have a material effect on the financial statements and that there were no unasserted claims or assessments that ESI's counsel had advised were probable of assertion and must be disclosed in accordance with FAS 5. However, Rubin and Lewis received the attorney letter notifying them that ten customers were affected by Erwin's misconduct and that counsel, on behalf of ESI, had initiated contact with these customers to resolve the Erwin claims.

27. Rubin and Lewis failed to render an accurate audit report. RBG's report inaccurately represented that ESI's financial statements for the year ended December 31, 2000 were prepared in conformity with GAAP and that RBG's audit was performed in accordance with GAAS. ESI's financial statements were not in conformity with GAAP because no accrual was made for Erwin's misappropriations. Moreover, RBG's audit was not performed in accordance with GAAS because Rubin and Lewis failed to obtain sufficient competent evidential matter to evaluate the effect of Erwin's misappropriations on ESI's financial statements under FAS 5.

28. By engaging in the conduct alleged above, Rubin and Lewis engaged in improper professional conduct within the meaning of Rule 102(e) of the Commission's Rules of Practice in that their conduct (i) constituted intentional or knowing conduct, including reckless conduct, that resulted in violation of applicable professional standards, or in the alternative, (ii) constituted negligent conduct, consisting of a single instance of highly unreasonable conduct that resulted in a violation of applicable professional standards in circumstances in which Rubin and Lewis knew, or should have known, that heightened scrutiny was warranted.

## III.

In view of the allegations made by the Division of Enforcement and the Office of the Chief Accountant, the Commission deems it necessary and appropriate that public administrative proceedings be instituted to determine:

1. Whether the allegations set forth in Section II above are true and, in connection therewith, to provide Respondents an opportunity to establish any defenses to such allegations; and

2. What, if any, remedial action is necessary and appropriate pursuant to Rule 102(e) of the Commission's Rules of Practice.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that each Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If any Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f) and 201.310.

This Order shall be served forthwith upon each Respondent personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice, 17 C.F.R. § 201.360(a)(2).

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Jonathan G. Katz
Secretary