UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 68605 / January 9, 2013

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3436 / January 9, 2013

ADMINISTRATIVE PROCEEDING
File No. 3-15168

In the Matter of	:	**ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 4C OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE**
JOHN J. AESOPH, CPA, and DARREN M. BENNETT, CPA	:	
Respondents.	:	

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against John J. Aesoph, CPA ("Aesoph") and Darren M. Bennett, CPA ("Bennett") pursuant to Section 4C of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 102(e)(1)(ii) of the Commission's Rules of Practice to determine whether Aesoph and Bennett engaged in improper professional conduct.

II.

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

A. Summary

1. Aesoph and Bennett (collectively, "the auditors") repeatedly engaged in improper professional conduct during their year-end 2008 audit of TierOne Corporation, a holding company for TierOne Bank (collectively "TierOne"). They did so by failing to subject TierOne's loan loss estimates – one of the highest risk areas of the audit – to appropriate scrutiny. Aesoph served as the audit partner and Bennett served as the senior manager on the engagement; they each had significant responsibility for the audit decisions, the inadequately designed and

implemented audit programs, the review of audit work papers, and the failures to follow audit standards that are the subject of this proceeding.

2. TierOne's loan losses were a critical audit area that warranted heightened scrutiny. Up to and during 2008, as a result of the financial crisis and related real estate market crash, TierOne had been experiencing a dramatic increase in the number of its troubled real estate loans. TierOne estimated its loan losses for a key component of its troubled loan portfolio – large, unique loans accounted for under Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 114 ("FAS 114") – by using the value of the collateral underlying these loans. Rather than get updated appraisals to value the collateral of the loans that TierOne evaluated for impairment under FAS 114 (called here "the bank's FAS 114 loans" [1]), TierOne frequently relied on stale, dated appraisals to which the bank's management sometimes applied a discount. TierOne's determination of the discount amounts, and its decisions not to apply a discount, were not documented, nor were they supported by reliable facts or evidence.

3. Aesoph and Bennett violated numerous Public Company Accounting Oversight Board ("PCAOB") audit standards in both their audit of internal control over financial reporting and their audit of the financial statements. The auditors correctly identified TierOne's loan losses as presenting a fraud risk and a significant risk of material misstatement. The actual audit test work in this area, however, was inadequate considering the associated audit risk and materiality. For example, the internal controls identified and tested by the audit engagement team relating to the allowance for loan and lease losses ("ALLL") did not effectively address one of the most important and riskiest components of the bank's loan loss calculations: management's use of stale and inadequate appraisals to value the collateral underlying the bank's FAS 114 loans. Based on this test work, Aesoph and Bennett had no reasonable basis to conclude that TierOne maintained, in all material respects, effective internal control over financial reporting. Moreover, the auditors failed to adequately identify and evaluate defects in the design and operating effectiveness of controls over collateral valuation that would have been important to the auditors' conclusion about whether TierOne's controls sufficiently addressed the assessed risk of misstatement. The auditors violated PCAOB standards, including specifically Auditing Standard No. 5 ("AS No. 5"), in their audit of internal control over financial reporting.

4. Compounding these flaws in the audit of internal control over financial reporting were Aesoph and Bennett's failures to comply with PCAOB standards in their substantive audit procedures over the bank's FAS 114 loans. The relevant audit work on these loans consisted of checking management's basic math, confirming that appraisals (no matter how stale) existed, reviewing a sample of appraisals, and relying on management's uncorroborated representations concerning property-specific issues, including whether stale appraisals required adjustment. These procedures fell short of the requirements of a number of PCAOB standards, including specifically AU Sections 328 and 342, which address auditing fair value and accounting estimates, respectively. In short, the auditors failed to subject management's estimates to appropriate scrutiny.

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[1] The specific loans at issue in this proceeding are listed on 2008 audit work papers L-22.2F, L-22.2H, L-32.1, L-32.2, and L-32.3.

5. Aesoph and Bennett failed to obtain sufficient, competent evidential matter to provide assurances that management's estimates were reasonable. They further failed to act with due professional care or appropriate professional skepticism.

6. These failures, along with others detailed below, demonstrate a single instance of highly unreasonable conduct that resulted in a violation of applicable professional standards in which Aesoph and Bennett knew, or should have known, heightened scrutiny was warranted; and 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.

B. Respondents

7. **John J. Aesoph**, CPA, age 40, is a resident of Omaha, Nebraska. Aesoph has been an auditor at KPMG, LLP ("KPMG") since 2001 and a partner at the firm since 2005. He was on the TierOne audit engagement from 2002 through KPMG's resignation in 2010, and was the engagement partner for the 2008 audit. Aesoph is currently licensed as a CPA in Nebraska and North Dakota. He has previously been licensed as a CPA in Idaho, Indiana, Iowa, Kansas, and South Dakota.

8. **Darren M. Bennett**, CPA, age 35, is a resident of Elkhorn, Nebraska. Bennett has been an auditor at KPMG since 2001. He worked on the TierOne audit each year from 2003 through KPMG's resignation in 2010, with the exception of one year. Bennett was the senior manager for the 2008 TierOne audit. Bennett was also a member of KPMG's financial services practice and served as manager or senior manager on at least four financial services audits in addition to TierOne. Bennett is licensed as a CPA in Nebraska, North Dakota, and South Dakota.

C. Other Relevant Parties

9. **TierOne Corporation**, a Wisconsin corporation, was, during the relevant time period, a holding company for TierOne Bank, a federally-chartered savings bank headquartered in Lincoln, Nebraska. TierOne's common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act; that registration was revoked by consent on June 4, 2012. Prior to May 7, 2010, TierOne's shares were listed on the NasdaqGS exchange under the stock symbol "TONE." TierOne's common stock was thereafter quoted on OTC Pink, which is operated by OTC Markets Group Inc. On June 4, 2010, TierOne Bank was closed by its primary regulator, the United States Office of Thrift Supervision ("OTS"). The Federal Deposit Insurance Corporation ("FDIC") was named receiver and another bank took over TierOne's assets and deposit accounts. TierOne subsequently filed for Chapter 7 bankruptcy protection on June 24, 2010.

10. **KPMG LLP** is a limited liability partnership headquartered in New York, New York, engaged in the business of providing accounting and auditing services. KPMG audited TierOne's 2008 financial statements and internal control over financial reporting as of December 31, 2008 and issued unqualified opinions. KPMG also performed quarterly reviews for TierOne during the relevant time period.

D. TierOne's Risky Problem Loan Portfolio

11. TierOne was a century-old thrift bank that had historically focused on residential and agricultural loans in the Nebraska/Iowa/Kansas region. Beginning in about 2004, however, TierOne expanded into high-risk types of lending in regions such as Las Vegas, Florida, and Arizona, which were experiencing unusual, rapid escalation in market values. This strategy made the bank particularly vulnerable to the fallout from the financial crisis, as these areas were hardest hit by the precipitous fall in real estate prices, which began in late 2006 and early 2007.

12. Throughout 2008, TierOne was experiencing a dramatic rise in high-risk problem loans including land and land development and residential construction. Certain of these problem loans – typically larger and non-homogenous (*i.e.*, not car or residential mortgage loans) – were deemed "impaired" pursuant to FAS 114, meaning it was probable the bank would not recover all amounts as contractually due. TierOne's reported FAS 114 impaired loan balance had increased from less than $4 million as of December 31, 2006 to nearly $186 million as of December 31, 2008.

13. In June 2008, the OTS conducted a "risk-focused examination" of the bank that focused on asset quality, credit administration, management, earnings, and the adequacy of ALLL. As a result of that examination, the OTS downgraded the bank's composite CAMELS rating from a one (indicating a financial institution that was "sound in every respect") to a four (indicating a financial institution with "serious financial or managerial deficiencies" that require close supervisory attention). The OTS provided the bank with a report that deemed the institution to be in troubled condition and board and management performance to be exceptionally poor. OTS concluded that TierOne had experienced a significant deterioration in asset quality due to eroding real estate values in Nevada and Florida, and that poor board and management oversight had exacerbated the problem. The OTS cited data demonstrating that real estate values were declining at unprecedented rates in states and markets where the bank had a concentration of loans. The OTS also directed TierOne to maintain higher minimum capital ratios. Failure to correct the problems identified by the OTS or to meet the heightened capital requirements would result in additional OTS enforcement action.

14. The bank's FAS 114 loans had a negative effect on TierOne's ability to meet the heightened capital requirements mandated by the OTS. Under Generally Accepted Accounting Principles ("GAAP"), TierOne was required to assess probable losses associated with its impaired loans and record those losses in its ALLL. GAAP permits the impairment to be measured using the fair value of the underlying collateral if the loan is collateral dependent, which is the method that was typically utilized by TierOne on its FAS 114 loans. As loan losses increased, the bank's capital was further eroded, directly impacting the OTS capital requirements.

15. In order to assess loan losses for the bank's FAS 114 loans, TierOne prepared loan-by-loan spreadsheets that contained estimates of collateral values and loan impairment determinations. TierOne generally based the valuation on the most recent appraisal in its loan files. If the appraisal was aged, as it typically was, TierOne would sometimes apply a discount to the appraised value. These discounts were determined by an informal committee at the bank. The

rationale for applying any particular discount – or for not discounting an appraisal at all – was not documented.

16. In the summer of 2009, when the OTS began its annual exam, the bank was forced to get a significant number of updated appraisals and to use those appraisals in its loan loss calculations. In the fall of 2009, TierOne disclosed over $130 million in additional loan loss provisions. TierOne was shut down by bank regulators on June 4, 2010 and filed for bankruptcy later that month.

17. In April 2010, KPMG resigned as TierOne's auditor. KPMG withdrew its audit opinion relating to TierOne's 2008 financial statements on the basis that they were materially misstated with respect to certain out-of-period adjustments for loan loss reserves. KPMG also withdrew its opinion relating to TierOne's internal control over financial reporting as of the year-end 2008 due to a material weakness in internal control over financial reporting related to the material misstatements.

E. The Auditors Recognized the Risks in TierOne's Problem Loan Portfolio

18. Prior to and during their 2008 audit of TierOne, Aesoph and Bennett were aware of the risk and significance of the bank's loan loss provisions, and of the loan loss component related to the bank's FAS 114 loans specifically.

1. The Auditors Identified ALLL Risks

19. The bank's ALLL had two primary components: an allowance for loans impaired under FAS 114 and an allowance for loans impaired under Statement of Financial Accounting Standards No. 5 ("FAS 5"). The portion of the ALLL allocable to loans that TierOne evaluated for impairment under FAS 114 was individually material to the financial statements and presented a significant risk of material misstatement.

20. The audit planning document – reviewed and approved by both Aesoph and Bennett – identified the ALLL as a risk that could result in a material misstatement of TierOne's financial statements. Specifically, the audit plan noted that the ALLL presented a significant risk of material misstatement, both with respect to inherent risk and control risk, including the risk of fraud.

2. Numerous Red Flags Further Underscored the Risks

21. Compounding the identified risks were numerous red flags and other irregularities that should have triggered Aesoph and Bennett's professional skepticism and led them to investigate further.

a. OTS Identified a Significant Understatement of the ALLL

22. In connection with its June 2008 examination, the OTS identified a deficiency in TierOne's ALLL as of March 31, 2008 of between $17 million and $22 million, representing an approximate 25% increase over the previously reported ALLL. Aesoph and Bennett were aware of this deficiency: Bennett directly identified it in a memo he authored – and Aesoph reviewed –

that discussed the OTS report. Further, the June 2008 OTS report, discussed above in paragraph 13, was provided to KPMG and included in the auditors' work papers.

b. Third-Party Market Data Showed Significant Declines in Real Estate Values That Were Not Reflected in TierOne's Valuations of its FAS 114 Loans

23. As another red flag, TierOne's valuation adjustments on the collateral underlying the bank's FAS 114 loans were inconsistent with independent market data. Third-party market data indicated that real estate values were declining precipitously in many of the markets where the bank's FAS 114 collateral was located, including Las Vegas, Nevada and Phoenix, Arizona. At year-end 2008, TierOne had prepared spreadsheets analyzing more than fifty borrower relationships, totaling approximately $255 million in loans, for evaluation for impairment under FAS 114. Approximately $186 million of these loans were actually deemed impaired by the bank. The majority of the loans that the bank evaluated for impairment under FAS 114 were collateralized by property with appraisals more than a year old; over half of those stale appraisals were not discounted. Critically, when management did discount appraisals, those discounts were typically inconsistent with – and more favorable to the bank than – the declines indicated by the independent market data.

c. Management Typically Did Not Get Updated Appraisals

24. Further, despite the market declines, TierOne management often did not get updated appraisals on the collateral underlying the bank's FAS 114 loans. This failure came despite the fact that the OTS and members of the audit engagement team noted stale appraisals and recommended that appraisals be updated.

d. New Appraisals Obtained Throughout 2008 Indicated Management Overestimated Collateral Values and Understated Loss Provisions

25. In the limited instances where TierOne did get updated appraisals or valuations on the bank's FAS 114 loans during 2008, the collateral value typically showed a significant decline from the amount used by management in the immediately preceding quarter. Appraisals received throughout 2008 showed that management's estimates were inflated by twenty to almost fifty percent in the prior quarter. The magnitude of the quarter-to-quarter declines could not be explained by market conditions alone.[2] In addition to the updated appraisals showing differences in value from the immediately-preceding quarter, some of those appraisals revealed tremendous drops in the value TierOne had used at year end 2007.[3]

[2] New appraisals or valuations were received on several of the bank's FAS 114 loans, including: Storybook Homes; Rising Sun; Grand Teton; Quarter 10; Stetson Ridge; La Madre 48; Rome 24; Clearwater Estates; Equestrian Meadow; HD Tbella; and HDB, LLC.

[3] TierOne received new appraisals on several loans that had been booked as FAS 114 loans at year-end 2007, including: Storybook Homes, Clearwater Estates, Grand Teton, and Rising Sun.

26. When considered in conjunction with management's reluctance to obtain new appraisals, these sharp declines in collateral values should have raised significant questions about management's motivations.

e. Stale Appraisals Were Not Discounted Despite TierOne's Internal Policy

27. During the 2008 audit, the auditors reviewed a memorandum that was prepared by TierOne and annotated by the audit engagement team that assessed the adequacy of the fourth quarter 2008 ALLL balance. That memorandum stated that, for Nevada land and residential construction loans, TierOne "tries to estimate collateral value declines in real estate by discounting appraised values, which are older than six months." Despite this stated policy, TierOne often failed to discount Nevada appraisals that were more than six months old.

f. TierOne's Unallocated Loan Loss Reserve Decreased at Year End

28. TierOne designated a portion of its ALLL as an "unallocated" reserve which was intended to cover loan losses inherent in TierOne's loan portfolio, including particularly loans in Nevada. However, despite the fact that market conditions continued to deteriorate throughout 2008, TierOne's unallocated reserve decreased significantly at year end. The unallocated reserve dropped from approximately $7 million in the second and third quarters to approximately $4 million at year end. This decrease was particularly troubling given that during its year end audit, the audit engagement team relied on the unallocated reserve to absorb potential errors in TierOne's calculation of its ALLL or to justify not performing additional audit work. These conclusions by the audit engagement team were reviewed by Aesoph and Bennett.

g. Management Failed to Document Their Discounting Decisions

29. As a final red flag to the auditors, TierOne did not document the rationale and basis for management's assumptions regarding valuation of the collateral underlying the bank's FAS 114 loans, despite the guidance in Financial Reporting Release ("FRR") No. 28. *See also* Staff Accounting Bulletin No. 102 ("SAB 102").

3. TierOne's FAS 114 Loans Were Material

30. In addition to these red flags, the portion of the ALLL related to the bank's FAS 114 loans was material. PCAOB auditing standards recognize that financial statements are materially misstated when they contain misstatements whose effect, individually or in the aggregate, is important enough to cause the financial statements not to be presented fairly, in all material respects, in conformity with generally accepted accounting principles. AU § 312, ¶ 4.

31. The portion of the ALLL related to the bank's FAS 114 loans was material to the financial statements taken as a whole. It far exceeded the $1.9 million materiality threshold established for the 2008 audit. It was reasonably possible that even a relatively small change in the value of the bank's FAS 114 loans would cause a material error in the financial statements.

32. The portion of the ALLL related to the bank's FAS 114 loans was material for additional reasons. For example:

a. Any additional loan losses discovered by the audit engagement team would have pushed the bank closer to falling below the OTS-mandated 8.5% core capital ratio and 11% risk-based capital ratio. TierOne's core and risk-based capital ratios at December 31, 2008 were 8.9% and 11.6%, respectively.

b. The bank's loan losses factored significantly into TierOne's overall operating results and profitability. The bank's net interest income after provision for loan losses was only $2.9 million at year end 2008, meaning a small increase in loan losses would change a reported net income to a reported net loss. Further, the trend in this net interest income figure was in precipitous decline, decreasing from $119.8 million at year end 2006 to $48 million at year end 2007 to $2.9 million at year end 2008.

c. TierOne itself acknowledged the importance of its ALLL, including its FAS 114 loans, devoting several pages in its 2008 Form 10-K to a discussion of problem loans and the ALLL. Indeed, the 10-K expressly stated that "[a]n inadequate allowance for loan losses could adversely affect our results of operations."

33. Given the risk and materiality of the ALLL related to the bank's FAS 114 loans, and the many red flags, Aesoph and Bennett had heightened responsibilities in auditing this area, and were required to apply professional skepticism in obtaining sufficient competent evidential matter to support their opinions. They failed in these responsibilities.

F. Aesoph and Bennett's Improper Professional Conduct

34. The Commission's Rules allow the Commission to censure or deny, temporarily or permanently, the privilege of appearing or practicing before it in any way certain professionals who violate "applicable professional standards." 17 C.F.R. § 201.102(e). For auditors of issuers such as TierOne, the applicable professional standards include standards issued by the PCAOB.

1. General Standards

35. The PCAOB's three general standards of auditing require that an auditor (1) have adequate technical training and proficiency, (2) maintain an independent mental attitude, and (3) act with due professional care in the performance of the audit. AU § 150, ¶ 2. The three basic standards of field work require the auditor to (1) adequately plan and properly supervise the audit, (2) obtain a sufficient understanding of internal control to plan the audit, and (3) obtain sufficient competent evidential matter to afford a reasonable basis for an opinion. AU § 150, ¶ 2.

36. "Due professional care imposes a responsibility upon each professional within an independent auditor's organization to observe the standards of field work and reporting." AU § 230, ¶ 2. The concept of due professional care includes acting with reasonable diligence. AU § 230, ¶ 3. It also includes exercising professional skepticism. AU § 230, ¶ 7. "Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence." AU § 230, ¶ 7. "The auditor neither assumes that management is dishonest nor assumes unquestioned honesty. In exercising professional skepticism, the auditor should not be satisfied with less than persuasive evidence because of a belief that management is honest." AU § 230, ¶ 9.

37. Auditors are required to obtain "sufficient competent evidential matter" to afford a reasonable basis for the auditor's opinions. AU § 326, ¶ 1; *see also* AU § 230, ¶ 11 ("The independent auditor's objective is to obtain sufficient competent evidential matter to provide him or her with a reasonable basis for forming an opinion."). "Gathering and objectively evaluating audit evidence requires the auditor to consider the competency and sufficiency of the evidence." AU § 230, ¶ 8. PCAOB standards attach greater validity to evidential matter obtained directly by the auditors, and to evidential matter obtained from independent sources outside an entity. AU § 326, ¶ 21. Representations from management, while part of the evidential matter the auditor obtains, "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." AU § 333, ¶ 2.

38. Further, audit procedures, and the amount and persuasiveness of evidence auditors are required to obtain, are driven by risk. "Audit risk and materiality, among other matters, need to be considered together in determining the nature, timing, and extent of auditing procedures and in evaluating the results of those procedures." AU § 312, ¶ 1; *see also* AU § 312, ¶ 12 ("The auditor should consider audit risk and materiality both in (a) planning the audit and designing auditing procedures and (b) evaluating whether the financial statements taken as a whole are presented fairly, in all material respects, in conformity with generally accepted accounting principles. The auditor should consider audit risk and materiality in the first circumstance to obtain sufficient competent evidential matter on which to properly evaluate the financial statements in the second circumstance."). When auditors identify a significant risk of material misstatement, as they did here, that fact is relevant to the nature and extent of the audit procedures to be applied. AU § 312, ¶ 17. "Higher risk may cause the auditor to expand the extent of procedures applied, apply procedures closer to or as of year-end, particularly in critical audit areas, or modify the nature of procedures to obtain more persuasive evidence." AU § 312, ¶ 17.

39. Aesoph, as the engagement partner, was responsible for the audit engagement and its performance, for proper supervision of the work of the engagement team members, and for compliance with PCAOB standards. Aesoph sought and received the assistance of Bennett, who was the senior manager on the 2008 TierOne audit, in fulfilling his responsibilities as engagement partner.

40. Bennett contributed significantly to the planning of the audit, the design of tests of controls, and the design and implementation of substantive procedures. Additionally, Bennett was responsible for executing the audit, including directing the audit engagement team on how to conduct the audit. Bennett reviewed the audit work papers and was responsible for on-site supervision of the audit engagement team. Bennett also played a significant role in gathering and evaluating evidential matter to support the audit of ALLL, and specifically the valuation of collateral underlying the bank's FAS 114 loans. Bennett, like Aesoph, was responsible for compliance with PCAOB standards with respect to the supervisory responsibilities that were assigned to him.[4]

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[4] *See, e.g., In the Matter of Robert M. Harbrecht, CPA and Brian R. Spires, CPA*, Rel. No. 34-56469, AAE Rel. No. 2720 (Sept. 19, 2007) (experienced senior manager who was responsible,

41. At the completion of the audit, both Aesoph and Bennett signed off that "all necessary auditing procedures were completed," that "support for conclusions was obtained," and that "sufficient appropriate audit evidence was obtained." Further, Aesoph specifically signed off on the audit checklist's requirement that the audit engagement team had "performed and documented its work in compliance with . . . applicable auditing standards . . . , and the working papers demonstrate this compliance."

42. As detailed below, Aesoph and Bennett's conduct in planning, supervising, and implementing KPMG's audit of TierOne's 2008 financial statements – and specifically the portions of the audit relating to the bank's FAS 114 loans – violated numerous PCAOB standards. Most prominently, the auditors violated the requirements of AS No. 5 regarding audits of internal control over financial reporting, and AU Sections 328 (auditing fair value measurements) and 342 (auditing accounting estimates) related to the substantive audit procedures. Aesoph and Bennett also violated: the third general audit standard (due professional care), *see* AU § 150, ¶ 2; and the third standard of field work (obtaining sufficient competent evidential matter), *see* AU § 150, ¶ 2; AS No. 3; and AU §§ 230, 312, 316, 319, 326, 333, and 561.

2. The Audit of TierOne's Internal Controls Violated Professional Standards

43. KPMG performed an integrated audit of TierOne, meaning that the audit of TierOne's internal control over financial reporting was integrated with the audit of TierOne's financial statements. When an auditor assesses control risk below the maximum level, as the auditors did here, he or she should obtain sufficient evidential matter to support that assessed level. AU § 319, ¶¶ 80, 90. Moreover, if one or more material weaknesses exist, the company's internal control over financial reporting cannot be considered effective. AS No. 5, ¶ 2. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. AS No. 5, Appendix A, ¶ A7.

44. AS No. 5 provides specific requirements for auditing internal control over financial reporting in an integrated audit, including that the auditors should understand likely sources of potential misstatements and focus more of their attention on the areas of highest risk. But the key ALLL control that the audit engagement team identified (the bank's Asset Classification Committee) did not effectively address the riskiest component of the ALLL: the bank's valuation of collateral for the bank's FAS 114 loans with stale appraisals. In addition, the audit engagement team failed to identify or test any effective internal controls to determine whether TierOne was complying with its own policies for updating appraisals. The auditors therefore violated AS No. 5, and further lacked a reasonable basis for KPMG's conclusion that there were no material weaknesses in TierOne's internal control over financial reporting.

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along with partner, for planning and executing audit sanctioned pursuant to Rule 102(e) for violations of PCAOB standards).

a. Relevant PCAOB Standards

45. In an integrated audit, an auditor should design tests of controls to obtain sufficient evidence both to support his or her opinion on internal control over financial reporting and to support his or her control risk assessments for the purpose of the audit of the financial statements. AS No. 5, ¶ 7.

46. Auditors also should determine and understand the likely sources of potential misstatements. One of the ways to do so is "by asking himself or herself 'what could go wrong?' within a given significant account or disclosure." AS No. 5, ¶¶ 28-31.

47. To further understand the likely sources of potential misstatements, and as part of selecting the controls to test, the auditor should understand the flow of transactions related to the relevant assertions, identify points within the company's processes at which a misstatement could arise that would be material, and identify the controls that management has implemented to address these potential misstatements. AS No. 5, ¶ 34.

48. Performing a "walkthrough" is often the most effective way to understand likely sources of potential misstatements and identify the appropriate controls to test. AS No. 5, ¶ 37. Walkthroughs require the auditor to "follow[ ] a transaction from origination through the company's processes . . . until it is reflected in the company's financial records, using the same documents and information technology that company personnel use." AS No. 5, ¶ 37.

49. The selection of the controls to test, and the evidence needed to evaluate a given control, are driven by the auditors' risk assessment. AS No. 5, ¶ 10. "The auditor should focus more of his or her attention on the areas of highest risk," taking into consideration the risks such as the risk of fraud with respect to significant management estimates. AS No. 5, ¶¶ 11, 14. Further, the level of evidence needed increases as the risk associated with the control increases. AS No. 5, ¶¶ 46-47.

50. Some types of tests, by their nature, produce greater evidence of the effectiveness of controls than other tests. AS No. 5, ¶ 50. PCAOB standards include a hierarchy of tests. Inquiry, which ordinarily produces the lowest level of evidence, is never alone sufficient to support a conclusion about the effectiveness of a control. AS No. 5, ¶¶ 45, 50.

51. If there are deficiencies in a company's internal control over financial reporting that, individually or in combination, result in one or more material weaknesses, the auditor "must express an adverse opinion on the company's internal control over financial reporting, unless there is a restriction on the scope of the engagement." AS No. 5, ¶ 90.

52. Aesoph and Bennett's internal control test work did not comply with the foregoing PCAOB standards.

b. Failure to Identify Effective Controls over the Valuation of the Collateral for the Bank's FAS 114 Loans

53. Aesoph and Bennett both reviewed and approved key audit work papers involving the evaluation and testing of TierOne's internal controls over the ALLL. These work papers

identified seventeen key controls over TierOne's loan process. The audit engagement team used the work of TierOne's internal audit department to provide evidence on many of these controls, but determined to independently test five key controls "due to the fraud risk and/or the high risk of failure associated with the controls." Each of these five controls purported to address some aspect of TierOne's problem loans. None, however, effectively addressed TierOne's valuation of the collateral underlying the bank's FAS 114 loans.

54. The key control identified for prevention of a material misstatement of the ALLL was TierOne's Asset Classification Committee review. However, while the audit work papers do identify that the Asset Classification Committee had general responsibility for the ALLL, there is no reference to whether or how the Committee assessed the value of the collateral underlying individual loans evaluated under FAS 114, including any necessary adjustments to appraised values. The Asset Classification Committee meeting minutes included in the work papers contain no discussion about discounting stale appraisals or otherwise estimating the value of collateral.

55. The Asset Classification Committee was not an effective control over valuation of the collateral underlying the bank's FAS 114 loans. The Committee did not generate or review written documentation to support TierOne's calculations, including, specifically, documentation of the rationale and basis for management's assumptions regarding valuation of collateral. Without such documentation, there was insufficient evidence upon which to conclude that the bank's internal controls related to valuation of collateral were effective. *See* FRR No. 28; *see also* SAB 102.

56. The other controls independently tested during the audit also failed to address TierOne's valuation of collateral underlying the bank's FAS 114 loans. Further, the "walkthrough" described in the audit work papers, which was specifically reviewed by Bennett, was insufficient to provide a sufficient understanding of the valuation process or to identify important points at which a necessary control in the process was missing or was not designed effectively. *See* AS No. 5, ¶¶ 37, 38.

c. Failure to Identify or Test Controls Relating to Compliance with TierOne's Appraisal Policies

57. TierOne's written lending policy required all loans to be supported by "current appraisals or evaluations." The policy noted that "[i]n a rapidly escalating or deteriorating market, a value may be valid for only a few months." The policy also stated that new appraisals should be obtained when a loan was renewed, extended, or refinanced if market deterioration indicated that the collateral may no longer fully protect the loan.

58. While TierOne's lending policy may have been sound, it was not in and of itself a control. The auditors failed to identify any control to ensure compliance with this policy. In fact, TierOne frequently ignored or violated this policy, continuing to rely on stale appraisals in significantly deteriorated markets. TierOne also failed to obtain new appraisals on loans that had been modified.

d. The Absence of These Controls Was a Material Weakness

59. PCAOB audit standards define a material weakness as a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. AS No. 5, Appx. A, ¶ 7. Whether a deficiency or combination of deficiencies rises to the level of a material weakness depends on the severity of the deficiencies. AS No. 5, ¶¶ 62-63. The absence of effective controls over the valuation of collateral underlying the bank's FAS 114 loans and over compliance with TierOne's appraisal renewal policy, individually or in combination, represented a material weakness in TierOne's internal control over financial reporting as of December 31, 2008. Because of the material weakness in internal control, KPMG should have issued an adverse opinion on the bank's internal control over financial reporting. Further, the auditors' inappropriate conclusion that controls were effective led to an unsupported – and incorrect – conclusion that, for purposes of the financial statement audit, the risk of significant misstatement with respect to the ALLL was only moderate.

3. Substantive Testing of the Bank's FAS 114 Loans Violated Professional Standards

60. Adding to the failures in connection with auditing TierOne's internal control over ALLL were Aesoph and Bennett's deficient substantive audit procedures. Specifically, the audit engagement team failed to follow PCAOB standards in reviewing the reasonableness of management's estimates of the value of the collateral underlying the bank's FAS 114 loans – one of the riskiest and most critical elements of the bank's FAS 114 loss estimate calculation. The audit engagement team relied principally on the most recent (and often stale) appraisals given them and on management's uncorroborated representations of current value. The audit engagement team relied on these representations despite evidence that management's estimates were biased and inconsistent with independent market data. Bennett was directly involved in the audit engagement team's FAS 114 test work. Specifically: Bennett initially reviewed the individual spreadsheets prepared by TierOne that purported to justify the valuation of the underlying collateral of the bank's FAS 114 loans; Bennett supervised the audit test work and collection of evidential matter, including meeting directly with management to discuss management's estimates of the value of collateral; and Bennett approved the audit engagement team's FAS 114 test work prior to passing it to Aesoph. Aesoph reviewed the FAS 114 test work prior to signing the audit opinion. By failing to subject management's estimates to appropriate scrutiny, the auditors violated PCAOB standards, including particularly AU Sections 328 and 342, which address auditing fair value and accounting estimates, respectively. The auditors failed to obtain sufficient, competent evidential matter to provide assurances that management's estimates were reasonable. They further failed to act with due professional care or appropriate professional skepticism.

a. Relevant PCAOB Standards

61. TierOne's calculation of the appropriate loss reserve on the bank's FAS 114 loans, which was based largely on an assessment of the value of the underlying collateral, was an estimate. As such, the auditors' responsibility was to obtain sufficient competent evidence to

provide reasonable assurance that the estimates were reasonable and presented in conformity with the relevant accounting principles. AU §§ 328, ¶ 3; 342, ¶ 7.

62. In evaluating reasonableness, the auditor should obtain an understanding of how management developed the estimate. Based on that understanding, the auditor should use one or a combination of the following approaches: (1) review and test the process used by management to develop the estimate; (2) develop an independent expectation of the estimate to corroborate the reasonableness of management's estimate; or (3) review subsequent events or transactions occurring prior to the date of the auditor's report. AU § 342, ¶ 10; *see also* AU 328, ¶ 23.

63. Where management's estimate is based on a valuation, such as an appraisal, that was made prior to the financial reporting date, the following is an example of a consideration in the development of audit procedures: "obtain[ing] evidence that management has taken into account the effect of events, transactions, and changes in circumstances occurring between the date of the fair value measurement and the reporting date." AU § 328, ¶ 25; *see also* AU § 313, ¶ 3 ("Applying principal substantive tests to the details of an asset or liability account as of an interim date rather than as of the balance-sheet date potentially increases the risk that misstatements that may exist at the balance-sheet date will not be detected by the auditor."), ¶ 6 ("The auditor should consider whether there are rapidly changing business conditions or circumstances that might predispose management to misstate financial statements in the remaining period. If such conditions or circumstances are present, the auditor might conclude that the substantive tests to cover the remaining period would not be effective in controlling the incremental audit risk associated with them. In those situations, the asset and liability accounts affected should ordinarily be examined as of the balance-sheet date.").

64. Importantly, because estimates were involved, the auditors were required to be particularly attuned to management bias – intentional or not. Among other things, auditors normally should consider "the historical experience of the entity in making past estimates." AU § 342, ¶ 9. "Even when management's estimation process involves competent personnel using relevant and reliable data, there is potential for bias in the subjective factors. Accordingly, when planning and performing procedures to evaluate accounting estimates, the auditor should consider, with an attitude of professional skepticism, both the subjective and objective factors" management used in making the estimates. AU § 342, ¶ 4.

65. Further, as the auditors had correctly identified TierOne's ALLL as presenting a risk of fraud and a high risk of error, the auditors had a heightened responsibility over this area. AU § 312, ¶ 17 ("Higher risk may cause the auditor to expand the extent of procedures applied, apply procedures closer to or as of year end, particularly in critical audit areas, or modify the nature of procedures to obtain more persuasive evidence."); AU § 316, ¶ 2 ("[T]he auditor's response to the risks of material misstatement due to fraud involves the application of professional skepticism when gathering and evaluating audit evidence.").

> Because of the characteristics of fraud, the auditor's exercise of professional skepticism is important when considering the risk of material misstatement due to fraud. Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence. The auditor should conduct the engagement with a mindset that recognizes the possibility that a material misstatement due to fraud could be present, regardless of any past experience with the entity and regardless of the auditor's belief about management's honesty and integrity. Furthermore, professional skepticism requires an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred. In exercising professional skepticism in gathering and evaluating evidence, the auditor should not be satisfied with less-than-persuasive evidence because of a belief that management is honest.

AU § 316, ¶ 13.

66. The risk of material misstatement generally increases where, as here, the relevant account is an estimate. AU § 312, ¶ 36. While estimates may differ, an unreasonable estimate should be considered a likely misstatement. AU § 312, ¶ 36. The auditor should also consider whether differences in management's estimates and estimates best supported by the audit evidence suggest possible management bias. AU § 312, ¶ 36.

67. While representations from management are a part of the audit evidence, "they 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." AU § 333, ¶ 2. This is particularly true in an area, like the ALLL, involving estimates. AU § 316, ¶ 54 ("In addressing an identified risk of material misstatement due to fraud involving accounting estimates, the auditor may want to supplement the audit evidence otherwise obtained …."). It is even more critical where the audit area involves a risk of fraud. AU § 316, ¶ 46 ("Examples of the application of professional skepticism in response to the risks of material misstatement due to fraud are … obtaining additional corroboration of management's explanations or representations concerning material matters, such as through third-party confirmation, the use of a specialist, analytical procedures, examination of documentation from independent sources, or inquiries of others within or outside the entity."); AU 316 ¶ 53 (example of modification of procedures in response to identified risks of material misstatement due to fraud include "[i]nterviewing personnel involved in activities in areas where a risk of material misstatement due to fraud has been identified to obtain their insights about the risk and how controls address the risk"); AU § 326, ¶ 21 ("When evidential matter can be obtained from independent sources outside an entity, it provides greater assurance of reliability for the purposes of an independent audit than that secured solely within the entity …. The independent auditor's direct personal knowledge, obtained through physical examination, observation, computation, and inspection, is more persuasive than information obtained indirectly.").

68. The auditor should be thorough in his or her search for evidential matter and unbiased in its evaluation. AU § 326, ¶ 25; *see also id.* ("In developing his or her opinion, the auditor should consider relevant evidential matter regardless of whether it appears to corroborate or to contradict the assertions in the financial statements."). The inability to obtain sufficient

competent evidential matter may require the auditor to qualify his or her opinion or to disclaim an opinion. *See* AU § 508, ¶ 22.

69. Finally, auditors are required to clearly document the work they perform. *See* AS No. 3. "Audit documentation should be prepared in sufficient detail to provide a clear understanding of its purpose, source, and the conclusions reached." AS No. 3, ¶ 4. "The auditor must document the procedures performed, evidence obtained, and conclusions reached with respect to relevant financial statement assertions." AS No. 3, ¶ 6. "Audit documentation must clearly demonstrate that the work was in fact performed." AS No. 3, ¶ 6. "Because audit documentation is the written record that provides the support for the representations in the auditor's report, it should," among other things, "[d]emonstrate that the engagement complied with the standards of the PCAOB." AS No. 3, ¶ 5.

70. Aesoph and Bennett's substantive audit procedures fell short of these standards.

b. Improper Professional Conduct

71. TierOne estimated the value of the collateral underlying the bank's FAS 114 loans on a loan-by-loan basis because the bank's FAS 114 portfolio was made up of large, non-homogenous loans. Therefore, the audit engagement team performed a loan-by-loan review of the bank's FAS 114 loan portfolio to test whether management's estimates of value were reasonable. However, the substantive audit procedures and the evidence obtained from those procedures were insufficient to meet PCAOB standards.

i. Failure to Test Management's Estimates of Collateral Value

72. The audit engagement team obtained and reviewed each of the more than fifty FAS 114 spreadsheets prepared by the bank. Most of the audit work was simply "ticking and tying": recalculating figures, agreeing charge off amounts, and tying reported appraisal values to the actual appraisals.

73. The audit engagement team did, however, obtain a sample of original appraisals from management for additional testing. Specifically, the audit engagement team assumed that appraisals less than a year old were "current" (regardless of the market). For appraisals older than a year, they inquired whether a discount was applied to the appraised value, and if not, they inquired why TierOne didn't think it was necessary or appropriate. In addition, Bennett and members of the audit engagement team discussed with management a sample of FAS 114 calculations and recent trends, and "leveraged" information from certain loan reviews.[5] Following this test work, Bennett also reviewed and discussed the bank's FAS 114 spreadsheets with Aesoph to ensure that Aesoph was satisfied with the audit engagement team's conclusions. Based on the entirety of these procedures, the auditors concluded that "the FAS 114 calculations

[5] Although the auditors may have "leveraged" the aspects of the loan reviews that arguably supported their conclusions as to the reasonableness of management's valuations of certain of the bank's FAS 114 loans, they ignored information in those same loan reviews that contradicted management's valuation assessment.

appear to be properly prepared and adequately supported at 12/31/08." Aesoph and Bennett lacked a reasonable basis for this conclusion.

74. Aesoph and Bennett relied on an unsupported – and unsupportable – assumption that appraisals less than a year old were "current," without regard to the property's location or stage of development, and that market conditions had not materially deteriorated throughout the year. Many of the markets in which TierOne's collateral was located were seeing significant continuing quarterly declines in the value of real estate. In addition, many of the properties that served as collateral were under development and in varying stages of completion. TierOne's lending policy cautioned against relying on aged appraisals in these markets. According to the policy, "[i]n a rapidly escalating or deteriorating market, a[n appraisal] value may be valid for only a few months." Despite this policy, Aesoph and Bennett arbitrarily assumed that only appraisals older than a year potentially needed adjusting.

75. This assumption that appraisals up to a year old were current was unsupported by any evidence and particularly troubling in the Nevada market. As noted above, TierOne's memorandum prepared to support its ALLL balance – a memo annotated by the audit engagement team, included in the audit work papers, and reviewed by Aesoph and Bennett – noted that the bank would estimate collateral for Nevada real estate by discounting appraisals older than six months, acknowledging that six month old appraisals in that market were not reflective of current market conditions. Even so, the bank failed to discount many Nevada appraisals that were more than six months old and Aesoph and Bennett failed to reconcile the inconsistency between the bank's stated practice and its actual practice.

76. In addition, the test work over management's valuation estimates was insufficient. Again, according to its audit program, the audit engagement team would "inquire" of management whether discounts had been applied to older appraisals, and if not, why not. But uncorroborated management representations are not sufficient evidence in a high risk audit area.

77. Further calling into question the auditors' work, the auditors relied on management's uncorroborated representations even though independent evidence indicated that management's estimating and discounting decisions were biased. As noted above, earlier in 2008, the OTS had determined that TierOne had underreported its ALLL by nearly 25%. And the few times TierOne obtained a new appraisal on an impaired loan throughout 2008, that new appraisal typically showed that TierOne's valuation in the immediately preceding quarter was seriously deficient. In addition, TierOne's discount decisions and amounts were often significantly different on properties in the same market, and were typically inconsistent with third-party market information. Further, the rationale for TierOne's discounting decisions was not documented. Despite these red flags, the auditors continued to rely on management's representations regarding management's appraisal discounting decisions, without performing any additional test work or obtaining independent corroboration of management's representations.

78. Auditors are required to document their work, including the procedures performed and the evidence obtained. Based upon the documentation in the audit work papers, including the audit programs, memoranda, and individual FAS 114 loan analyses, the audit engagement team obtained little if any reliable or persuasive evidence with respect to management's adjustments (or lack thereof) to stale appraised values. The little that is documented shows that

Bennett and the audit engagement team made various inquiries of management and accepted management's representations. There is little to no documentation of management's representations with respect to specific properties, or of the auditors performing any rigorous testing or independent corroboration of management's discounting decisions. The audit documentation does not demonstrate that the engagement complied with the standards of the PCAOB.

ii. Failure to Corroborate Additional Information

79. In addition to appraisal information, TierOne's FAS 114 worksheets sporadically contained references to other information in support of management's estimates of the fair value of the collateral. This information included, for example, asking prices, borrower development plans and status, estimated costs to complete, offers to purchase, and other information. The auditors failed to obtain independent corroboration of any of this information.

4. The Auditors' Failure to Recognize Bias in Management's Estimates Violated Professional Standards

80. Exacerbating Aesoph and Bennett's failures surrounding the reasonableness of management's loan loss estimates on its FAS 114 loans was their failure to recognize bias in those same estimates.

a. Relevant PCAOB Standards

81. As noted above, auditors normally should consider "the historical experience of the entity in making past estimates." AU § 342, ¶ 9. Relatedly, "[t]he auditor also should perform a retrospective review of significant accounting estimates reflected in the financial statements of the prior year to determine whether management judgments and assumptions relating to the estimates indicate a possible bias on the part of management." AU § 316, ¶ 64. "With the benefit of hindsight, a retrospective review should provide the auditor with additional information about whether there may be a possible bias on the part of management in making the current-year estimates." AU § 316, ¶ 64.

b. Improper Professional Conduct

82. Consistent with PCAOB standards, KPMG's audit program required the auditors to assess management bias. The auditors claimed to do so, noting in the audit completion document that

> [t]he Company's historical ability to reliably develop significant estimates has been adequate. We have considered current events as they relate to prior quarters and years during our audit procedures and noted there was no indication of bias on management's part in developing their estimates.

83. This conclusion was inconsistent with the OTS' findings in June 2008 about management's numerous failures to develop reliable estimates. It was also inconsistent with evidence of management bias that surfaced throughout 2008. As discussed above, Aesoph and Bennett knew that the OTS identified a deficiency in TierOne's ALLL that represented

approximately 25% of the ALLL balance at the time. Further, as discussed above, Aesoph and Bennett knew, or should have known, that the limited instances in which the bank actually obtained new appraisals on impaired loans resulted in significant declines in the value of the collateral both compared to the previous quarter and, in some cases, compared to the values used in the prior year. In many cases, these new appraisals resulted in significant increases in the loan loss provisions associated with these loans. Despite this evidence, the auditors improperly concluded that the bank's estimation process was "adequate" and that there was "no indication of bias on management's part."

5. The Failure to Investigate Subsequent Discovery of Facts Violated Professional Standards

84. Finally, the auditors failed to investigate facts discovered after the date of their report on the 2008 financial statements that may have affected the 2008 financial statements.

a. Relevant PCAOB Standards

85. PCAOB audit standards set out a number of steps that should be taken by an auditor who, "subsequent to the date of the report upon audited financial statements, becomes aware that facts may have existed at that date which might have affected the report had he or she then been aware of such facts." AU § 561, ¶ 1. As an initial matter, "[w]hen the auditor becomes aware of information which relates to financial statements previously reported on by him, but which was not known to him at the date of his report, and which is of such a nature and from such a source that he would have investigated it had it come to his attention during the course of his audit, he should, as soon as practicable, undertake to determine whether the information is reliable and whether the facts existed at the date of his report." AU § 561, ¶ 4. If in fact the information is reliable and existed at the date of the report, other steps may be required. AU § 561, ¶¶ 5-8. "Subsequent events affecting the realization of assets . . . ordinarily will require adjustment of the financial statements . . . ." AU § 560, ¶ 7.

b. Improper Professional Conduct

86. During KPMG's 2009 quarterly reviews, the engagement team learned of several borrower relationships that had new appraisals or valuations that likely existed at the date of KPMG's 2008 audit report, issued on March 12, 2009. In each case, that new valuation showed a significant decline from management's estimate at year end.[6]

87. Despite learning that there were new appraisals and valuation assessments which were dated prior to the issuance of the 2008 audit report, Aesoph and Bennett failed to perform the procedures required by AU § 561. Rather, Aesoph and Bennett assumed they had no reason to investigate because, they claim, they received representations from management shortly before issuing their audit opinion that no new appraisals had been received that impacted the 2008 financial statements. This is, however, precisely what should have triggered AU § 561: new

[6] The specific loans included: Celebrate 50, MME, Ashley Turner, Stratton Group, Blake Home Builders, and Den Mark Construction.

information came to light after the audit report was issued that was inconsistent with previous information and, for that matter, management's purported representations that all new appraisals had been given to KPMG. Aesoph and Bennett had an obligation to investigate, but failed to do so.

G. Violations

88. As described in detail above, Aesoph and Bennett violated numerous PCAOB audit standards, failed to obtain sufficient competent evidential matter to support their audit conclusions, and failed to exercise due professional care and appropriate professional skepticism.

89. Specifically, Aesoph and Bennett violated: the third general audit standard (due professional care), *see* AU § 150, ¶ 2; the third standard of field work (competent evidential matter), *see* AU § 150, ¶ 2; AS Nos. 3 and 5; and AU §§ 230, 312, 316, 319, 326, 328, 333, 342, and 561.

90. Aesoph and Bennett engaged in improper professional conduct, as defined in Section 4C of the Exchange Act and Rule 102(e)(1)(ii), in that their conduct constituted negligent conduct consisting of (1) a single instance of highly unreasonable conduct that resulted in a violation of applicable professional standards in which Aesoph and Bennett knew, or should have known, that heightened scrutiny was 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.

III.

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

A. Whether the allegations set forth in Section II hereof are true and to afford Respondents Aesoph and Bennett an opportunity to establish any defenses to such allegations; and

B. What, if any, remedial action is appropriate against Respondents Aesoph and Bennett pursuant to Section 4C of the Exchange Act and Rule 102(e) of the Commission's Rules of Practice, including, but not limited to, censure or denying, temporarily or permanently, the privilege of appearing or practicing before the Commission.

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 Respondents Aesoph and Bennett shall file their answers 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 Respondents Aesoph or Bennett fail to file the directed answer, or fail to appear at a hearing after being duly notified, the Respondents may be deemed in default and the proceedings may be determined against the Respondents upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310.

This Order shall be served upon the Respondents 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 a witness or counsel in proceedings held pursuant to notice. Since this proceeding is not a "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.

Elizabeth M. Murphy
Secretary