

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 76401 / November 9, 2015

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3717 / November 9, 2015

ADMINISTRATIVE PROCEEDING
File No. 3-16952

In the Matter of

Larry D. Liberfarb, P.C.,

Respondent.

**ORDER INSTITUTING PUBLIC
ADMINISTRATIVE AND CEASE-
AND-DESIST PROCEEDINGS
PURSUANT TO SECTIONS 4C AND 21C
OF THE SECURITIES EXCHANGE ACT
OF 1934 AND RULE 102(e) OF THE
COMMISSION'S RULES OF PRACTICE,
MAKING FINDINGS, AND IMPOSING
REMEDIAL SANCTIONS AND A
CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Larry D. Liberfarb, P.C. ("Liberfarb" or "Respondent") pursuant to Sections 4C¹ and 21C of the Securities

¹ Section 4C provides, in relevant part, that:

The Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found . . . (1) not to possess the requisite qualifications to represent others . . . (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations thereunder.

Exchange Act of 1934 (“Exchange Act”) and Rule 102(e)(1)(ii) of the Commission’s Rules of Practice.²

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this the Order Instituting Public Administrative and Cease-and-Desist Proceedings Pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 and Rule 102(e) of the Commission’s Rules of Practice, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent’s Offer, the Commission finds³ that:

A. SUMMARY

This matter concerns violations of the Commission’s auditor independence rules by Liberfarb. Liberfarb audited the annual financial statements that were filed with the Commission for 20 broker-dealer audit clients for the fiscal years ending January 1, 2010 through September 30, 2011. For at least one audit of each of these broker-dealer audit clients, Liberfarb was not independent under auditor independence criteria established by the Commission and made applicable by Exchange Act Rule 17a-5(f)(3) to audits of brokers and dealers.⁴ As a result of this

² Rule 102(e)(1)(ii) provides, in relevant part, that:

The Commission may censure a person or deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found . . . to have engaged in unethical or improper professional conduct.

³ The findings herein are made pursuant to Respondent’s Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

⁴ The provisions of Exchange Act Rule 17a-5 referred to herein are those in effect during, and applicable to, the relevant conduct. On July 30, 2013, the Commission adopted certain amendments to Rule 17a-5. *See* Broker-Dealer Reports, SEC Exchange Act Release No. 34-70073 (July 30, 2013), 78 Fed. Reg. 51910 (Aug. 21, 2013). Among other things, the amendments to Rule 17a-5 require that audits of brokers and dealers be performed in accordance with Public Company Accounting Oversight Board standards, effective for audits of fiscal years ending on or after June 1, 2014. The auditor independence requirement of Rule 2-01 of Regulation S-X applied to broker-dealer audits both before and after the July 30, 2013 amendments. At the

conduct, Liberfarb engaged in improper professional conduct, violated the auditor independence rules, and caused each of the broker-dealers' failure to file an annual report audited by an independent accountant.

B. RESPONDENT

Respondent Liberfarb, a professional corporation, is an accounting and auditing firm registered with the Public Company Accounting Oversight Board ("PCAOB"). Liberfarb has one shareholder, Larry D. Liberfarb, and is located in Norwood, Massachusetts. During the Relevant Period, Liberfarb also employed, on a part-time basis, a Certified Public Accountant who assisted the firm with audit engagements.

C. FACTS

1. Lack of Independence

a. During fiscal years ending January 1, 2010 through September 30, 2011 (the "Relevant Period"), Liberfarb served as the independent public accountant for 20 broker-dealer audit clients. In connection with at least one audit performed for each of these broker-dealer audit clients during the Relevant Period, Liberfarb prepared the financial statements and/or notes to the financial statements that were filed with the Commission on Form X-17A-5.

b. For example, Liberfarb audited the annual financial statements for Broker-Dealer A for the fiscal year ending September 30, 2011. During the audit, Liberfarb was provided with financial documents generated by Broker-Dealer A, including a balance sheet and a profit and loss statement. Liberfarb reviewed and tested these documents, and the financial data contained therein, as part of the audit.

c. Liberfarb then utilized the information contained in these documents to create and revise a set of financial statements to be filed with the Commission. In particular, using the prior year's financial statements as a template, Liberfarb personnel working on Liberfarb computers typed and updated the new set of financial statements, including the notes to the financial statements. Liberfarb then provided the set of financial statements it had prepared to Broker-Dealer A's management for approval.

d. In November 2011, Broker-Dealer A filed with the Commission a Form X-17A-5 Part III for the fiscal year ended September 30, 2011. Included in that filing is an audit report signed by Liberfarb and stating, among other things, that Liberfarb's audit of Broker-Dealer A was conducted "in accordance with auditing standards generally accepted in the United States of America."

time of the relevant conduct, prior to the amendments, that requirement was set out in Rule 17a-5(f)(3). It is now set out in Rule 17a-5(f)(1).

e. Liberfarb engaged in substantially similar conduct in connection with at least one audit for 19 additional broker-dealer clients during the Relevant Period.

2. Violations

a. Section 17(e)(1)(A) of the Exchange Act requires that every registered broker or dealer “annually file with the Commission a balance sheet and income statement certified by an independent public accounting firm, or by a registered public accounting firm if the firm is required to be registered under the Sarbanes-Oxley Act of 2002, prepared on a calendar or fiscal year basis, and such other financial statements (which shall, as the Commission specifies, be certified) and information concerning its financial condition as the Commission, by rule may prescribe as necessary or appropriate in the public interest or for the protection of investors.”

b. Exchange Act Rule 17a-5(e)(1)(i) states: “An audit shall be conducted by a public accountant who shall be in fact independent as defined in paragraph (f)(3) of this section herein, and he shall give an opinion covering the statements filed pursuant to paragraph (d)” Exchange Act Rule 17a-5(f)(3) further states that, for such audits, “[a]n accountant shall be independent in accordance with the provisions of Rule 2-01(b) and (c) of Regulation S-X.”

c. Exchange Act Rule 17a-5(g) requires that “[t]he audit shall be made in accordance with generally accepted auditing standards” and Exchange Act Rule 17a-5(i) requires that “[t]he accountant’s report shall . . . [s]tate whether the audit was made in accordance with generally accepted auditing standards.” Generally accepted auditing standards (“GAAS”) require auditors to maintain strict independence from their audit clients; an auditor “must be free from any obligation to or interest in the client, its management or its owners.” *See* Statement on Auditing Standards No. 1, Section 220.03. Accordingly, if an auditor’s report states that its audit was performed in accordance with GAAS when the auditor was not independent, then it has violated Exchange Act Rule 17a-5(i). *See In the Matter of Rosenberg Rich Baker Berman & Company and Brian Zucker, CPA*, Exchange Act Release No. 69765 at p. 5 (June 14, 2013).

d. Rule 2-01(c)(4) of Regulation S-X provides that an accountant is not independent if, at any point during the audit and professional engagement period, the accountant provides prohibited non-audit services to an audit client. Rule 2-01(c)(4)(i) of Regulation S-X provides that prohibited non-audit services include bookkeeping or other services related to the accounting records or financial statements of the audit client, and defines such services as:

Any service, unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the audit client’s financial statements, including:

(A) Maintaining or preparing the audit client’s accounting records;

(B) Preparing the audit client’s financial statements that are filed with the Commission or that form the basis of financial statements filed with the Commission; or

(C) Preparing or originating source data underlying the audit client's financial statements.

e. Rule 2-01(c)(4)(i) of Regulation S-X specifically prohibits an audit firm from preparing an audit client's financial statements that are filed with the Commission. In this context, preparing financial statements includes but is not limited to: aggregating line items from internal books and records to the financial statements; changing line item descriptions; drafting or editing notes to the financial statements; and converting FOCUS reports or bookkeeping software program reports into financial statements. With respect to the audit of Broker-Dealer A, and the additional audits in which Liberfarb engaged in substantially similar conduct, Liberfarb engaged in one or more of the above prohibited actions.

f. As a result of Liberfarb's conduct in preparing the financial statements, including the notes thereto, Liberfarb was not independent of its broker-dealer audit clients under the independence criteria established by Rule 2-01(c)(4) of Regulation S-X, which Exchange Act Rule 17a-5 made applicable to the audits of broker-dealer financial statements. As the Commission explained in adopting Rule 2-01(c)(4), providing such services for an audit client "impairs the auditor's independence because the auditor will be placed in the position of auditing the firm's work when auditing the client's financial statements. . . . In addition, keeping the books is a management function, the performance of which leads to an inappropriate mutuality of interests between the auditor and the audit client." *Revision of the Commission's Auditor Independence Requirements*, Exchange Act Release No. 43602, at IV.D.4.b(i) (November 21, 2000). *See also Strengthening the Commission's Requirements Regarding Auditor Independence*, Exchange Act Release No. 47265 ("keeping the books is a management function, which also is prohibited")(January 28, 2003).

g. Liberfarb violated Exchange Act Rule 17a-5(i) by representing in its audit reports that it had performed the audits of the broker-dealers' financial statements in accordance with GAAS when in fact, because of the independence impairment described above, the audits had not been performed in accordance with GAAS.

h. Exchange Act Section 17(a) and Rule 17a-5 require broker-dealers to file annual reports containing financial statements audited by independent public accountants. No showing of scienter is necessary to establish a violation of Exchange Act Section 17(a)(1). *See In the Matter of Orlando Joseph Jett*, Exchange Act Release No. 49366 at n.45 (March 5, 2004) (citing *SEC v. Drexel Burham Lambert Inc.*, 837 F. Supp. 587, 610 (S.D.N.Y. 1993); *Stead v. SEC*, 444 F.2d 713, 716-17 (10th Cir. 1971), *cert denied*, 404 U.S. 1059 (1972)).

i. Under Section 21C of the Exchange Act, a person is a "cause" of another's primary violation if the person knew or should have known that his act or omission would contribute to the primary violation. Negligence is sufficient to establish "causing" liability under Section 21C when a person is alleged to have caused a primary violation that does not require scienter. *In re KPMG*

Peat Marwick, Exchange Act. Rel. No. 43862 (Jan. 19, 2001), *aff'd*, *KPMG v. SEC*, 289 F.3d 109 (D.C. Cir. 2002).

j. Liberfarb caused its broker-dealer audit clients to violate Exchange Act Section 17(a) and Rule 17a-5. Liberfarb, an audit firm registered with the PCAOB and operated by a Certified Public Accountant, knew or should have known that its conduct contributed to its audit clients' violations of Exchange Act Section 17(a) and Rule 17a-5.

k. Rule 102(e) of the Commission's Rules of Practice allows the Commission to censure a person if it finds that such person has engaged in "improper professional conduct." Exchange Act § 4C(a)(2); Rule 102(e)(1)(ii). Rule 102(e) defines improper professional conduct, in part, as: "[a] single instance of highly unreasonable conduct that results in a violation of applicable professional standards in circumstances in which the registered public accounting firm or associated person knows, or should know, that heightened scrutiny is warranted." Exchange Act § 4C(b)(2); Rule 102(e)(1)(iv)(B).

l. Questions regarding an auditor's independence always warrant heightened scrutiny. *See* Amendment to Rule 102(e) of the Commission's Rules of Practice, 63 Fed. Reg. 57164, 57168 (Oct. 26, 1998) (codified at 17 C.F.R. Part 201). The Commission has defined the "highly unreasonable" standard as:

an intermediate standard, higher than ordinary negligence but lower than the traditional definition of recklessness used in cases brought under Section 10(b) of the Exchange Act 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.

Id. at 57,167; *see also In the Matter of Ernst & Young LLP*, Admin. Proc. File No. 3-10933, SEC Initial Decision Release No. 249, at 60 (Apr. 16, 2004).

m. Based on the conduct set forth above, Liberfarb engaged in highly unreasonable conduct that resulted in violations of applicable professional standards when it knew or should have known that heightened scrutiny was required.

3. Findings

a. Based on the foregoing, the Commission finds that Liberfarb engaged in improper professional conduct pursuant to Exchange Act Section 4C(a)(2) and Rule 102(e)(1)(ii) of the Commission's Rules of Practice.

b. Based on the foregoing, the Commission finds that Liberfarb committed violations of Exchange Act Rule 17a-5(i) and caused 20 broker-dealers' violations of Section 17(a) and Rule 17a-5 promulgated thereunder.

4. Respondent's Remedial Efforts

In determining to accept the Offer, the Commission considered remedial acts promptly undertaken by Respondent.

5. Undertakings

Liberfarb undertakes:

a. within ninety (90) days from the date of the Order, to establish written policies and procedures, or to revise and/or supplement existing written policies and procedures, for the purpose of providing Liberfarb with reasonable assurance of compliance with applicable independence requirements, including those requirements of Rule 2-01 of Regulation S-X applicable to an SEC Registered Broker-Dealer Engagement (defined to mean an engagement to provide a report – whether an audit report, an examination report, or a review report – required under Exchange Act Rule 17a-5(d)(1)(i)(C), as amended);

b. within ninety (90) days from the date of the Order, to establish a policy of ensuring training, whether internal or external, on an annual or more frequent regular basis, concerning applicable independence requirements, including those requirements of Rule 2-01 of Regulation S-X applicable to an SEC Registered Broker-Dealer Engagement, of any Firm audit personnel who participate in any way in the planning or performing of any SEC Registered Broker-Dealer Engagement;

c. within ninety (90) days from the date of the Order and before Liberfarb's commencement of any SEC Registered Broker-Dealer Engagement (or, where Liberfarb by the date of this Order has already commenced but not completed such an engagement, before Liberfarb's release of its report), to ensure training pursuant to the policy described in paragraph (5)(b) above has been provided on at least one occasion;

d. to provide a copy of the Order –

(i) within thirty (30) days from the date of the Order, to all audit personnel employed by, or associated with (as defined in PCAOB Rule 1001(p)(i)), Liberfarb as of the date of the Order; and

(ii) within thirty (30) days from the date of the Order, to any client of Liberfarb as of the date of the Order for which Liberfarb has performed or has been engaged to perform an SEC Registered Broker-Dealer Engagement;

e. to certify, in writing, compliance with the undertakings set forth above in paragraphs 5(a) through 5(d)(ii). The certification shall identify the undertakings, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission staff may make reasonable requests for further

evidence of compliance, and Respondent agrees to provide such evidence. The certification and supporting material shall be submitted to Stephen L. Cohen, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549-5553, with a copy to the Office of Chief Counsel of the Enforcement Division, no later than one hundred twenty (120) days from the date of the Order.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Liberfarb's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

- A. Liberfarb is hereby censured.
- B. Liberfarb shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Exchange Act and Rule 17a-5 promulgated thereunder.
- C. Liberfarb shall comply with the undertakings enumerated in Section (III)(C)(5) above.
- D. Liberfarb shall pay a civil money penalty in the amount of \$30,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). Payment shall be made in the following installments: \$7,500 within ten days of the entry of this Order; \$7,500 within 120 days of the entry of this Order; \$7,500 within 240 days of the entry of this Order; and \$7,500 within 360 days of the entry of this Order. If any payment is not made by the date the payment is required by this Order, the entire outstanding balance of civil penalties, plus any additional interest pursuant to 31 U.S.C. § 3717, shall be due and payable immediately, without further application. Payment must be made in one of the following ways:
 - (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
 - (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
 - (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Larry D. Liberfarb, P.C. as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Stephen L. Cohen, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, DC 20549-5553.

E. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Brent J. Fields
Secretary