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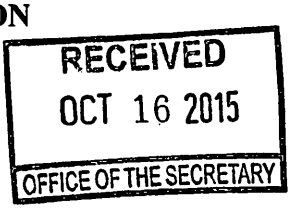
UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION



ADMINISTRATIVE PROCEEDING
File No. 3-16386

In the Matter of

TRACI J. ANDERSON, CPA
TIMOTHY W. CARNAHAN
AND CYIOS CORPORATION,

Respondents.

DIVISION OF ENFORCEMENT'S
POST-HEARING REPLY BRIEF

Dated: October 15, 2015.

Respectfully submitted,

Chris Davis, Texas Bar No. 24050483
Timothy McCole, Mississippi Bar No. 10628
Securities and Exchange Commission
Burnett Plaza, Suite 1900
801 Cherry Street, Unit #18
Fort Worth, Texas 76102-6882
E-mail: davisca@sec.gov
Telephone: (817) 900-2638 (Davis)
Telephone: (817) 978-6453 (McCole)
Facsimile: (817) 978-4927

COUNSEL FOR DIVISION OF ENFORCEMENT

I. Summary

In their post-hearing briefs,[1] Timothy Carnahan ("Carnahan") and CYIOS Corporation ("CYIOS"), and Traci Anderson ("Anderson") (collectively, "Respondents"), do not offer evidence on the limited issues remaining in this matter.[2] Rather, they improperly attempt to re-litigate issues already decided by the Court and to attack the Division for its purportedly "capricious" and "inequitable" case brought as part of its "prejudiced and excessive" enforcement of the federal securities laws. Because the Respondents fail to cite evidence supporting their positions, the Court should find in the Division's favor on all claims. And the Court should consider the Respondents' complete failure to admit the wrongful nature of their conduct along with the strong likelihood that they will commit future violations when deciding the appropriate sanctions against them.

II. Evidence and Argument

a. The Respondents cite to no evidence supporting their positions.

i. Securities Act Section 17(a) claims

The Division's evidence supporting its Securities Act Section 17(a) claims remains unrebutted.[3] Carnahan and CYIOS offer nothing more than conclusory statements to support their positions—with no citation to supporting evidence (because none exists). *See* Carnahan Br.

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[1] In this brief, the Respondents' post-hearing briefs are cited as "Anderson Br. at XX" and "Carnahan Br. at XX." The Division's post-hearing brief is cited as "Division Br. at XX."

[2] As noted in the Division's opening post-hearing brief, these issues are: (1) with respect to the Division's Securities Act Section 17(a) claims, whether CYIOS' untrue statements in periodic Commission filings were material, in the offer or sale of securities, and whether CYIOS obtained money or property as a result of those misstatements; (2) the proper measure of disgorgement for any Section 17(a) violations; (3) whether Carnahan knew or should have known of the PCAOB Order, and therefore whether CYIOS violated, and Carnahan caused CYIOS' violation of, Sarbanes Oxley ("SOX") Section 105(c)(7)(B); (4) and for purposes of determining the appropriate remedy for her violation, Anderson's state of mind (specifically, whether she deliberately or recklessly disregarded a regulatory requirement, subjecting her to enhanced civil penalties).

[3] See the Division's opening post-hearing brief at 2-7, detailing all of the evidence supporting the Section 17(a) claims.

at 5-8. Instead, they improperly attempt to re-litigate issues that have already been decided by the Court in its Order June 9, 2015 Order on Motions for Summary Disposition (the "Summary Disposition Order"). For instance, Carnahan and CYIOS argue that there has "been no 'misstatement' [or] 'misrepresentation'" and that "CYIOS did in fact evaluate ICFR." Carnahan Br. at 6. But the Court has already found that CYIOS' filings had misstatements and that it did not evaluate ICFR in accordance with COSO, as represented to investors. Summary Disposition Order at 6-8. Carnahan and CYIOS offer no evidence rebutting these filings.

Perhaps most importantly, Carnahan and CYIOS offer no evidence rebutting their admission that the misrepresentations were particularly important here, since CYIOS is a government contractor. *See, e.g.*, Ex. 12 at 7-8; Ex. 13 at 27. And as Carnahan testified during the hearing, the violations here have in fact had a material effect on CYIOS shareholders. Tr. at 198:9-14.

Finally, Carnahan and CYIOS do not dispute—even in conclusory fashion—that the misstatements: (1) were in the offer or sale of securities; (2) that CYIOS obtained money or property as a result; and (3) the amount CYIOS received by means of them was $37,500. Thus, as discussed at length in the Division's post-hearing brief, the evidence shows that the Commission should prevail on each of these elements. *See* Division Br. at 4-8.

ii. SOX Section 105(c)(7)(B) claims

It undisputed that Carnahan knew about the PCAOB Order—the sole remaining issue on the SOX Section 105(c)(7)(B) claims against CYIOS and Carnahan. None of the Respondents disputed this at the hearing and none disputes it now.

Instead, the Respondents continue to argue that Anderson was not barred from working for CYIOS—in spite of the plain language of the statue.[4] The Court has already rejected this argument twice and should again. As the Court stated in its Summary Disposition Order, the first time it ruled on this issue:

> [The Respondents'] reading of Section 105(c)(7)(B) is plainly incorrect because it reads the issuer associational bar, as distinct from the registered public accounting firm associational bar, entirely out of the statute. Thus, the undisputed fact that Anderson 'performs 'ZERO' percent in conjunction with the preparation or furnishing of an audit report' is beside the point.

The Court reiterated this holding in its June 17, 2015 Order Denying Certification of Ruling for Interlocutory Review, stating "The issuer associational bar is not limited to audit work or public accounting firms, but prohibits association with an issuer 'in an accountancy or a financial management capacity.'" *See* p. 3 (citing SOX § 105(c)(7)(B)).

The Court was correct both times, and the meaning of the statute is obvious. Ms. Anderson admitted as much during the hearing [Tr. at 139:12-140:1]:

> Q: So in other words, you are a person that has been suspended or barred from being associated with a registered public accounting firm; isn't that correct?
> A: Okay.
> Q: Is that correct?
> A: Yes.
> Q: If you look at the third line of that paragraph, it indicates "accountancy." Do you see the word "accountancy" there?
> A: Yes.
> Q: You understand that term "accountancy" to include more than just audit work, correct?
> A: Well, to me, accountancy is not audit work. Accountancy is accounting work.

And she acknowledged that she performed accountancy for CYIOS [Tr. at 142: 2-16]:

[4] Anderson notes in her brief that SOX § 105(c)(7)(B) was amended on July 22, 2010, during her settlement discussions with the PCAOB. Anderson Br. at 2. There is no dispute, however, that this change was effective before Anderson's settlement was entered on August 12, 2010. Further, Anderson testified during the hearing that the amendment had no bearing on her interpretation: "I had read it more before it had changed in July. Not that it, in all honesty, had any bearing on how I interpreted it." Tr. at 98:1-3.

Q: Let me rephrase. The list of duties that you indicate you will perform, is it your testimony that that laundry list of functions is not descriptive of accountancy?
A: It is -- I don't -- I'll just make the statement because I'm still not sure what you're -- to me that's accounting. It's accountancy. It's accounting work.
Q: So you understand that list to be accountancy, correct?
A: Yes.
Q: Throughout the time you were performing those functions for CYIOS, Mr. Carnahan knew you were performing those functions for CYIOS, correct?
A: Correct.

Thus, Ms. Anderson is perfectly capable of understanding the plain meaning of the statute—and that it prohibited her from working for CYIOS. The interpretation posited by the Respondents in their briefs—which they stand by today even in the face of Anderson's sworn testimony to the contrary— ignores the statute's unambiguous issuer associational bar and is thus an extreme departure from any reasonable interpretation of the statute. The Court was right to reject it twice before and should reject it once again.[5]

b. The Respondents' actions make them subject to second-tier or third-tier civil penalties.[6]

Securities Act § 8A(g) and Exchange Act § 21B(b) provide for three penalty tiers: (i) First Tier – for any violations; (ii) Second Tier – for violations involving "fraud deceit, manipulation or deliberate or reckless disregard of a regulatory requirement"; and (iii) Third Tier – for Second Tier violations that also directly or indirectly created a significant risk of substantial losses to others or resulted in substantial pecuniary gain to the party that committed the violation. Since the violations continued into mid-2014, the penalty amounts that went into effect on March

[5] In her brief Anderson claims that she understood that she could work for CYIOS based on "discussions [. . .] with legal counsel and the PCAOB." The Court has already said it will not consider an advice of counsel defense. Tr. at 96:17-20. And Anderson has offered no evidence that anyone at the PCAOB told her that she could continue to work for CYIOS. In fact, during her investigative testimony she admitted that she never sought consent from the PCAOB to remain as CYIOS' consultant CFO. Ex. 1 at 96:22-24.

[6] The Respondents are also subject to the injunctive relief sought by the division—including cease and desist orders against all respondents and a 102(e) bar against Anderson. *See* Division's April 30, 2015 Motion for Summary Disposition at 14-15.

5, 2013 are applicable. *See* Comm. Rule of Practice 1005. For Anderson and Carnahan, natural persons, those amounts are: (i) First Tier – up to $7,500; (ii) Second Tier – up to $75,000; and (iii) Third Tier – up to $150,000. *Id.* For CYIOS those amounts are: (i) First Tier - up to $75,000; (ii) Second Tier - up to $375,000; and (iii) Third Tier - up to $725,000. *Id.*

In assessing the appropriate remedial sanction, the Court is to consider: (1) the egregiousness of the respondent's actions; (2) the isolated or recurrent nature of the infraction; (3) the degree of scienter involved; (3) the sincerity of the respondent's assurances against future violations; (4) the respondent's recognition of the wrongful nature of her conduct; and (5) the likelihood that the respondent's occupation will present opportunities for future violations. *See, e.g., In the Matter of Wolf*, 2015 WL 4639230 at *19, S.E.C. Rel. No. 851 (Aug. 5, 2015) (citing cases). In determining whether a civil penalty is in the public interest, the Court may consider: (1) whether the violation involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; (2) the resulting harm to other persons; (3) any unjust enrichment and prior restitution; (4) the respondent's prior regulatory record; (5) the need to deter the respondent and other persons; and (6) such other matters as justice may require. *Id.* at *20 (citing 15 U.S.C. §§ 78u-2(c), 80b-3(i)(3)).

The Respondents' actions here show that second-tier or third-tier civil penalties are appropriate. As the Court has already found, both Carnahan and CYIOS (acting through him) acted in deliberate disregard of a regulatory requirement. *See* Summary Disposition Order at 6. And as discussed at length in the Division's opening post-hearing brief, Anderson acted in reckless disregard of a regulatory requirement. Division Br. at 9-10. Neither Carnahan nor Anderson has recognized that they violated the law—much less given any assurance against future violations. To the contrary, even in the face of the Court's prior findings that they did so,

both continue to deny any wrongdoing and to characterize these proceedings as "inequitable," "unmerited," and/or "capricious." *See, e.g.,* Anderson Br. at 3; Carnahan Br. at 6.

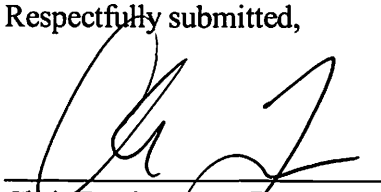
The conduct—which spanned many years and many public filings—was not isolated and the Respondents were significantly enriched by it, as detailed in the Division's prior filings. *See, e.g.*, Division's April 30, 2015 Motion for Summary Disposition at 14-15. The conduct—in particular, that of Carnahan and CYIOS—was egregious. As the Court has already noted, "[T]he contrast between Carnahan's complete failure to assess ICFR and the statements to which he attested in CYIOS' periodic filings was extreme, so much so that his statements were knowingly false." Summary Disposition Order at 6. And the conduct resulted in significant harm to others. As Carnahan testified, the violations in this case caused CYIOS to "los[e] a ton of business," which harmed CYIOS' shareholders. Tr. at 198:9-14.

The remaining factors also weigh in favor of enhanced penalties. As detailed at the hearing and in the Division's opening post-hearing brief, Anderson has a long history of regulatory violations. Division Br. at 9-10. And there is a strong need to deter the respondents—whose occupations present opportunities for future violations. Anderson continues to practice accounting and remains a CPA licensed in Florida. Carnahan remains CYIOS' CEO and stated that he would "definitely [. . .] without a question" work for a publicly-traded company again if given the opportunity. Tr. at 192:6-19.

Thus, taken collectively, these factors show that the Respondents are subject to second-tier or third-tier civil penalties, which the Court should award in its discretion.

Dated: October 15, 2015.

Respectfully submitted,



Chris Davis, Texas Bar No. 24050483
Timothy McCole, Mississippi Bar No. 10628
Securities and Exchange Commission
Burnett Plaza, Suite 1900
801 Cherry Street, Unit #18
Fort Worth, Texas 76102-6882
E-mail: davisca@sec.gov
Telephone: (817) 900-2638 (Davis)
Telephone: (817) 978-6453 (McCole)
Facsimile: (817) 978-4927

COUNSEL FOR DIVISION OF ENFORCEMENT

SERVICE LIST

Pursuant to Rule 150 of the Commission's Rules of Practice, I hereby certify that a true and correct copy of the ***Division of Enforcement's Post-Hearing Reply Brief*** was served on the following on October 15, 2015 via electronic mail and/or United Parcel Service, Overnight Mail:

Honorable Brenda P. Murray
Chief Administrative Law Judge
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-2557

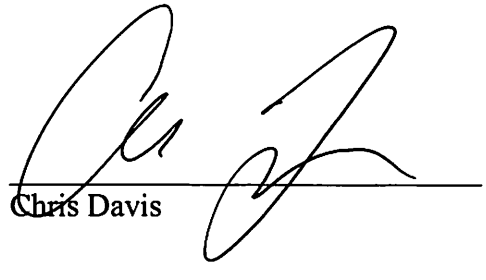
Honorable Cameron Elliot
Administrative Law Judge
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-2557

Chris Davis, Esq.
Fort Worth Regional Office
Securities and Exchange Commission
801 Cherry Street, Suite 1900
Fort Worth, TX 76102

Traci J. Anderson, CPA
[redacted]
Charlotte, NC [redacted]

Timothy W. Carnahan
President and CEO and Chairman
CYIOS Corporation
1300 Pennsylvania Ave., 700
Washington DC 20004

CYIOS Corporation
c/o Timothy W. Carnahan, President, CEO and Chairman
Ronald Regan Building
1300 Pennsylvania Ave., 700
Washington, DC 20004



Chris Davis