UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-16729

In the Matter of

MILLER ENERGY RESOURCES, INC., PAUL W. BOYD, CPA DAVID M. HALL, and CARLTON W. VOGT, III, CPA,

Respondents.

DIVISION OF ENFORCEMENT'S INITIAL PRE-HEARING BRIEF

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I. INTRODUCTION

The Division of Enforcement ("the Division") hereby submits its prehearing brief. In this action, the Division seeks cease and desist orders against Miller Energy Resources, Inc. ("Miller Energy" or the "Company"), Paul W. Boyd ("Boyd") and David Hall ("Hall"). The Division contends that the evidence at the hearing will establish violations of: 1) Section 17(a) of the Securities Act of 1933 ("Securities Act"), Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Securities Exchange Act of 1934 ("Exchange Act"), and Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13 thereunder, by Miller Energy; 2) Section 17(a) of the Securities Act, Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5, 13a-14, and 13b2-1 thereunder, and for causing Miller Energy's violations of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13 thereunder by Boyd; and 3) Section 17(a) of the Securities Act, Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5 and 13b2-1 thereunder, and for causing Miller Energy's violations of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13 thereunder by Hall. For these violations of the federal securities laws in addition to the cease and desist orders, the Division seeks disgorgement and prejudgment interest against Miller Energy, Boyd and Hall. The Division further seeks officer and director bars against Boyd and Hall. Pursuant to Section 4C of the Exchange Act and Rule 102(e)(1)(ii) of the Commission's Rules of Practice, the evidence will further establish that Carlton W. Vogt, III ("Vogt") engaged in "improper professional conduct" in the audit work conducted for Miller Energy for the year end audits in 2009 and 2010, and it is appropriate under those sections to deny Vogt the privilege of appearing or practicing before the Commission. Also pursuant to Section 4C of the Exchange

Act and Rule 102(e)(1)(iii) of the Commission's Rules of Practice, the evidence will further establish that Boyd willfully violated, and/or willfully aided and abetted, violations of the Federal securities laws or the rules and regulations thereunder and under those sections referenced above, the accountant Boyd should be denied the privilege of appearing or practicing before the Commission. Vogt's and Boyd's negligent conduct was either 1) a single instance of "highly unreasonable conduct" that resulted in a violation of applicable professional standards in which an accountant knows, or should know, "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." See Rule 102(e)(1)(iv)(B)(1) and (2) of Commission's Rules of Practice.

This case involves financial accounting and reporting fraud, as well as public accounting audit failures, related to the valuation of certain oil and gas assets acquired by Miller Energy, an oil and gas company headquartered in Knoxville, Tennessee. Miller Energy purchased these assets, which are located in Alaska, for $2.25 million in cash – along with the assumption of certain liabilities it valued at approximately $2 million – during a competitive bid in a bankruptcy proceeding in December 2009. The Company subsequently reported those assets at an overstated value of $480 million, and recognized a one-time "bargain purchase" gain of $277 million for its fiscal third quarter ended January 2010 and fiscal year ended April 2010. Based on an estimate prepared by an oil and gas valuation specialist hired by the Division, Miller Energy's valuation was overstated by more than $400 million.

The Alaska acquisition was the single most important event in Miller Energy's nearly forty year history, transforming it from a company long mired in the penny-stock arena to one traded on a national exchange. For the week preceding the acquisition, Miller Energy's stock

closed at an average price of $0.66 per share. Since the acquisition, Miller Energy has raised tens of millions of dollars in debt and equity, listed its stock on the New York Stock Exchange (the "NYSE"), had its stock traded at nearly $9 per share, and achieved in 2013 a market capitalization of $393 million.

Miller Energy's CFO at the time, Boyd, failed to account for the acquisition in accordance with generally accepted accounting principles ("GAAP"). Accounting Standards Codification ("ASC") 805, *Business Combinations*, required Miller Energy to record the value of its acquired Alaska assets at "fair value." However, contrary to authoritative accounting guidance, Boyd used as fair value a reserve report that was prepared by a petroleum engineer firm using the rules for supplemental oil and gas disclosures. As set forth in GAAP, the numbers used in these supplemental disclosures do not reflect fair value, and the reserve report used by Boyd expressly disclaimed that the numbers therein represented the engineer firm's opinion of fair value. The reserve report Boyd used also contained expense numbers that were knowingly understated by Hall, the CEO of Miller Energy's Alaska operations. In addition, Boyd double counted $110 million of certain fixed assets that were already included in the reserve report.

Miller Energy's financial statements for fiscal 2010, the first annual period in which the Company reported the fair value of the acquired assets, was audited by Sherb & Co. LLP ("Sherb & Co."), a now defunct CPA firm that was suspended by the Commission in 2013 for improper professional conduct unrelated to this matter. The lead engagement partner on the Miller Energy audit, Vogt, failed to comply with the Public Company Accounting Oversight Board (the "PCAOB") rules and standards in auditing Miller Energy's financial statements that included its accounting for its Alaska acquisition. Vogt failed to exercise due professional care and skepticism by not adequately assessing whether the Company's accounting treatment for the

acquisition complied with GAAP. Vogt also failed to obtain sufficient competent evidential matter for management's assertions regarding the fair value of the Alaska assets.

II. RESPONDENTS

A. Respondent Miller Energy is a Tennessee corporation with its principal place of business in Knoxville, Tennessee. It operates and develops oil and gas wells in north and south central Alaska. The Company operated oil and gas assets in the Appalachian region of east Tennessee until selling them in November 2014 for $3.3 million in cash. It changed its name from Miller Petroleum to Miller Energy Resources in April 2011. Miller Energy's common stock is currently registered pursuant to Exchange Act Section 12(b) and is listed on the NYSE under the ticker symbol "MILL."[1] It previously traded on the NASDAQ Global Market from May 6, 2010 to April 11, 2011, and before then was quoted on the OTC Bulletin Board and traded on the Pink Sheets. As of February 26, 2015, there were 46,664,223 shares of common stock outstanding. For fiscal years 2010 through 2014, Miller Energy reported annual operating losses every year totaling $79.2 million. Between March 2010 and August 2014, Miller Energy issued shares of common and preferred stock for proceeds of tens of millions of dollars.

B. Respondent Boyd, CPA, age 57, resides in Knoxville, Tennessee. From 2008 until 2011, Boyd was the CFO and Treasurer at Miller Energy. He was the director of risk management from 2011 until 2014. He is no longer employed by Miller Energy. He has been a licensed CPA in Tennessee since 1993.

C. Respondent Hall, age 45, resides in Anchorage, Alaska. Hall has degrees in Industrial and Electrical Engineering from Rochville University, an online institution described by a national newspaper as "a diploma mill that issues bogus degrees through the mail for a few

[1] In April 2015, Miller Energy received the first of two notices stating that it was in noncompliance with the NYSE's listing requirements and may be subject to suspension and delisting proceedings in the near future.

hundred dollars." He has served as a director of the Company and CEO of Miller Energy's Alaska subsidiary since December 2009, and as Miller Energy's Chief Operating Officer since July 2013. He has worked with the acquired Alaska assets since at least the mid-1990s, when Miller Energy's predecessors began compiling the assets. Prior to joining Miller Energy, Hall served from January 2008 to December 2009 as Vice President and General Manager of Alaska Operations for the immediate past owner of the acquired assets. In this capacity, Hall was the most senior employee in Alaska responsible for the day-to-day operations of the oil and gas properties.

D. Respondent Vogt, CPA, age 53, resides in Warwick, New York. He is currently a partner at Liggett, Vogt & Webb, P.A., and from January 2005 to October 2012 was a partner at Sherb & Co., LLP, an accounting firm based out of New York. He has been a licensed CPA in the state of New York since 1998.

III. FACTS

A. Background

Miller Energy was founded in 1967 as an oil and gas exploration and production company, and went public via a reverse merger in 1996. Between early 2002 and December 2009, Miller Energy's stock price regularly traded below one dollar per share, falling to a low of $0.04 per share in December 2007. During that same period, Miller Energy reported net losses in all but one year, 2004. For fiscal 2008 and 2009, for example, Miller Energy had cumulative operating losses in excess of $5 million on just over $2 million of revenue. In August 2008, Miller Energy named its founder's son-in-law, a former real estate agent turned penny-stock company financier, as CEO. Soon thereafter, the Company began acquiring additional oil and gas properties.

B. Miller Energy Acquires and Overvalues the Alaska Assets

In the fall of 2009, Miller Energy became aware of certain oil and gas properties in Alaska that were in the process of being "abandoned" as part of the bankruptcy proceedings of a California-based energy company. Unable to service its heavy debt and pay the significant monthly costs required to operate the properties, the bankrupt entity unsuccessfully sought for almost a year to sell its Alaska assets. When the sales process failed, the debtor shuttered its operations and abandoned the properties. Due to Miller Energy's expression of interest in the assets following their abandonment, the bankruptcy court permitted the debtor to reacquire the Alaska assets and sell them to Miller Energy in a competitive auction for $2.25 million in cash and the assumption of certain limited liabilities. The transaction closed on December 10, 2009.

On March 22, 2010, Miller Energy filed its quarterly report on Form 10-Q for its fiscal third quarter ended January 31, 2010 and reported a value of $480 million for the Alaska acquisition, which amount was comprised of $368 million for oil and gas properties and $110 million for fixed assets. Miller Energy also reported an after-tax $277 million "bargain purchase gain," which boosted net income for the quarter to $272 million – an enormous increase over the $556,097 loss reported for the same period the year before. As detailed below, these inflated balance sheet and income statement numbers were repeated in numerous documents subsequently filed with the Commission. The newly-booked value of the Alaska acquisition, which resulted in a nearly 5,000% increase in Miller Energy's total assets, also had a significant impact on Miller Energy's stock price. On December 10, 2009, the date of the transaction, Miller Energy's stock closed at $0.61 per share. By March 31, 2010, Miller Energy's stock closed 982% higher at $6.60 per share. Weeks later, its stock began trading on NASDAQ and,

after moving to the NYSE a year later, reached an all-time high price on December 9, 2013 of $8.83 per share.

Since October 2014, Miller Energy has recognized over a period of two quarters non-cash impairment charges of $414 million relating to the Alaska properties. Miller announced late on April 29, 2015 that, among other things, it had been informed by the NYSE that it was in non-compliance with listing requirements. The next day, its stock price dropped 21% to close at $0.73 per share, at which time it also had lost approximately $360 million in market capitalization from its 2013 high of $393 million.

1. Under GAAP, Miller Energy Was Required to Record the Alaska Acquisition at Fair Value

ASC 805 – formerly Statement of Financial Accounting Standards ("SFAS") 141(R) – became effective in December 2008.[2] Among its principal revisions, ASC 805 requires acquisitions that result in a "bargain purchase," *i.e.*, entities purchased at fire sales prices in non-orderly transactions, to be measured at fair value, with any resulting gain recorded on the income statement. ASC 820, *Fair Value Measurements* (formerly SFAS 157), provides the framework for measuring fair value. "Fair value" is defined in ASC 820 as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." A reporting entity must determine an appropriate fair value using one or more of the valuation techniques described in accounting literature.[3] ASC

[2] The Division agrees that ASC 805 is applicable to Miller Energy's Alaska acquisition. In consultation with the Division of Corporation Finance ("Corp Fin"), Miller Energy's acquisition had sufficient "inputs," "processes," and "outputs" to meet the definition of a business and trigger the fair value requirements of ASC 805.

[3] ASC 820 outlines three broad approaches to measure fair value: the market approach, income approach, and cost approach. Under the market approach, prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities are used to measure fair value. The income approach utilizes valuation techniques to convert future amounts to a single discounted present value amount. Finally, the cost approach is based on the amount that currently would be required to replace the assets in service, *i.e.*, current replacement cost.

820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and should be determined based on the assumptions market participants would use in pricing the asset or liability. As described below, Miller Energy purported to value its Alaska acquisition using the income approach for the oil and gas reserves and the cost approach for certain fixed assets.

2. The Valuation of the Acquired Oil and Gas Properties Was Based Upon a Reserve Report, Which Does Not Represent Fair Value

To record the value of the acquired oil and gas properties, Miller Energy and Boyd requested and improperly used a reserve report prepared by an independent petroleum engineer firm. Reserve reports are commonly used in the oil and gas industry to estimate quantities of oil and gas (the reserves) expected to be recovered from existing properties. Generally, these reports list reserves in categories based on a minimum estimated percentage probability of eventual recovery and production, *i.e.*, proved, probable, and possible. Information in reserve reports that are prepared in accordance with Commission rules and regulations is frequently used, for among other purposes, to satisfy supplemental accounting disclosure requirements

concerning estimates of future oil and gas production.[4] However, the numbers used in reserve reports for this purpose are expressly not considered "an estimate of fair market value."[5]

Shortly after the acquisition, Boyd asked Hall – a non-accountant with no formal accounting training – to obtain a reserve report for the Alaska properties in order to determine the fair value of the acquired assets to be reported on Miller Energy's Form 10-Q for the quarter ended January 31, 2010. On January 5, 2010, Hall hired a petroleum engineer firm to prepare a reserve report using PV-10 (*see* Note 8), which, while appropriate with further adjustments for SEC supplemental disclosures, was not indicative of fair value. Indeed, the two page engagement letter with the engineer firm includes no language about "fair value," "fair market value" or authoritative accounting literature. The individual engineer who authored the reserve report that Miller Energy used as fair value testified that his firm was not hired to opine as to fair market value and that he understood the purpose of the report was for use as supplemental data in the company's SEC disclosures. The reserve report was finalized in February 2010 and reflected a PV-10 of $368 million.

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[4] Oil and gas reporting companies are subject to two principal authoritative pronouncements governing financial accounting and reporting for oil and gas activities: Rule 4-10 of Regulation S-X (17 C.F.R. 210.4-10), *Financial Accounting and Reporting for Oil and Gas Producing Activities Pursuant to the Federal Securities Laws and the Energy Policy and Conservation Act of 1975* ("Rule 4-10"); and ASC 932-235-50-29 through 33 (formerly SFAS 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies* and SFAS 69, *Disclosures About Oil and Gas Producing Activities*). ASC 932 establishes disclosure requirements for significant oil and gas activities, including disclosure of the "standardized measure," which is the future after-tax net cash flows discounted at 10%. A non-GAAP measure known as "PV-10" is similar to the standardized measure but is typically presented on a pretax basis. The FASB has noted that the standardized measure supplies investors with useful information, however, they also noted their concern "that users of financial statements understand that it is neither fair market value nor the present value of future cash flows. It is a rough surrogate for such measures, a tool to allow for a reasonable comparison of mineral reserves and changes through the use of a standardized method that recognizes qualitative, quantitative, geographic, and temporal characteristics." Paragraph 83 of the Basis for Conclusions of SFAS 69.

[5] *See* Paragraph 77 of the Basis for Conclusions of SFAS 69 ("Although it cannot be considered an estimate of fair market value, the standardized measure of discounted net cash flows should be responsive to some of the key variables that affect fair market value, namely, changes in reserve quantities, selling prices, production costs, and tax rates.").

Upon receiving the reserve report, Boyd, without undertaking any additional analysis, merely recorded as the fair value of the acquired oil and gas properties the sum of the PV-10 estimates for 100% of the proved, probable, and possible reserves, which increased the book value of Miller Energy's oil and gas properties on its balance sheet by $368 million. The recklessness of Boyd's recording is further demonstrated by the fact that the reserve report itself clearly stated that the numbers therein were not an estimate of fair market value. Specifically, on page 3 of the report, it states that "*[t]he discounted values shown are for your information and should not be construed as our estimate of fair market value.*" Additionally, Boyd never reviewed or questioned any of the reserve report's assumptions or calculations, nor did he communicate with the engineer firm about the reserve report.[6]

The use of the PV-10 numbers as fair value conflicted with contemporaneous representations Miller Energy made to investors. Specifically, in its fiscal 2010 Form 10-K, which was the first annual report that included the inflated values, Miller Energy expressly told investors that "[o]ur PV-10 measure and the standardized measure of discounted future net cash flows do *not purport to present the fair value* of our natural gas and oil reserves." Despite this disclosure, Miller Energy had used its PV-10 measure in that very same report as the fair value of its acquired properties.

According to the preliminary fair value assessment conducted by the Division's valuation expert David B. Lerman, who is an oil and gas valuation specialist at FTI Consulting, Inc. ("FTI") with over 20 years of experience, Miller Energy materially overstated the value of its

[6] Testimonial and other evidence support the conclusion that Boyd, despite his CPA credentials, was largely inexpert regarding the requirements of oil and gas accounting and valuations. Boyd testified that he was unfamiliar with fair value accounting, and that he had no recollection of researching any accounting literature on the subject prior to recording the fair value of the Alaska acquisition in Miller Energy's public filings. He further testified that he did not know how other oil and gas reporting companies valued their properties because he did not research other companies' accounting and "just didn't have time to do that kind of thing." In testimony, Boyd was also generally unknowledgeable about reserve adjustment factors and the assumptions used to derive an appropriate discount rate.

Alaska assets by more than four hundred million dollars. A discounted cash flow analysis conducted by valuation expert Lerman was among the factors he relied on to confirm this conclusion. In oil and gas valuations, the forecasts used in discounted cash flow models are often based on engineering and accounting data readily available for the company or asset being acquired. Using basic production volume data from a reserve report, a typical oil and gas cash flow forecast is developed using assumptions for realized oil and gas prices, production, operating and development costs, production taxes, and capital expenditures necessary to produce the oil and gas reserves in the ground. In other words, a reserve report is used as a starting point in a valuation. A comparison of Miller Energy's recorded value and FTI's initial, *preliminary* valuation model is set forth in Table 1 in *Appendix A* to this brief.

As illustrated in Table 1, Miller Energy failed to use assumptions market participants would use, as is required under GAAP. First, Miller Energy used a single, flat price for every year of production in the reserve report. Market participants frequently use escalated prices to account for future inflation in the price of oil and gas. To account for that inflation, the Division's expert Lerman applied an annual growth rate to the realized prices in Miller Energy's reserve report based on information from the Department of Energy. This significantly increased the overall undiscounted cash flows obtained from the reserve report. However, when more appropriate, market participant assumptions were applied to other areas of the discounted cash flow model, the net present value of the reserves fell far short of Miller Energy's $368 value. Second, Miller Energy failed to consider market participants' views concerning the impact of income taxes. Valuation expert Lerman, calculated that the use of an appropriate tax rate reduced the value of the reserves by approximately $90 million.

Third, Miller Energy never considered whether the use of a 10% discount rate was appropriate under GAAP.[7] In a discounted cash flow model, a discount rate is used to account for the uncertainties associated with risk and the time value of money. A discount rate is the required rate of return that an investor would demand – based on the risks associated with the benefit stream under consideration – to induce the investor to make an investment. Valuation expert Lerman concluded, using a weighted average cost of capital, that market participants would have used a discount rate that would have further reduced the value of the reserves by approximately $179 million. Fourth, the valuation overstated cash flows from certain categories of reserve estimates (*e.g.*, "probable" and "possible" reserves) by failing to apply any risk weight to such reserves and the resulting cash flows. Given the high degree of uncertainty associated with cash flows from these reserve estimate categories, it is necessary to risk weight the estimated reserve quantities. By failing to include any risk weight to the reserves, Miller Energy overstated the value of its oil and gas properties. Valuation expert Lerman estimated that appropriate risk adjustments reduced the value of the reserves by in excess of $100 million. Fifth, Miller Energy failed to include certain asset retirement obligations ("ARO") that it would incur to plug and abandon the properties at the end of their useful lives. A third-party report prepared by a leading energy company serving the global oil and gas industry, dated August 2009, estimated the present value of the ARO for the properties at $41 million.

Finally, valuation expert Lerman has estimated that understated expense numbers used by Miller Energy overvalued the oil and gas properties by more than $60 million. The $237 million of projected operating and capital expenses – applied over a period of more than fourteen years –

[7] ASC 820 provides general guidance on the use of various valuation techniques under the income approach, including that "after-tax cash flows should be discounted using an after-tax discount rate" and "[p]retax cash flows should be discounted at a rate consistent with those cash flows." ASC 820-10-55-6. Without giving any consideration to authoritative accounting literature, Miller Energy and Boyd chose the 10% discount rate simply because it was the discount rate used to compute the standardized measure disclosures discussed above in Note 8.

in the reserve report, which were provided by Miller Energy and Hall, were intentionally understated, resulting in an overstated valuation. In fact, one petroleum engineer firm contacted but not used by Miller Energy thought that the expected level of expenses made a significant portion of the acquisition unprofitable. Initially, Hall contacted the petroleum engineer firm who had previously provided the past two owners of the properties with reserve reports, and thus had unfettered access to past operating data, and requested a quote for "updating" a prior reserve report. That firm told Hall that it would not assign any value to one of the largest fields acquired, the Redoubt Shoal field, because it was uneconomical – *i.e.*, expected future expenses exceeded expected future cash flows – and explained that it would not put its "name on a report that implies value exists where it likely does not."[8] Internal emails reveal that Miller Energy chose the new firm for the singular reason that the old one would not assign any value to the Redoubt Shoal field, and they show that Boyd was apprised of the issue. As described below, it appears that the Redoubt Shoal field – which represented $291 million of the $368 million in fair value recorded by Miller Energy – showed positive future cash flows in the reserve report primarily because Hall gave the new engineer firm understated and unsubstantiated expense numbers. Given the circumstances, including the enormous value assigned to it, the value attributed to the Redoubt Shoal field should have been a red flag to Boyd, particularly since Vogt had already told him that the lack of any controls over Hall's expense estimates was a "concerning void."

While market participants typically base their forecasts on data derived from a property's past performance, Miller Energy and Hall provided expense projections that, in many cases, were

[8] Unique among the oil and gas properties purchased by Miller Energy, Redoubt Shoal is an offshore field in Cook Inlet, Alaska, which requires the use of an offshore platform that sits in seventy feet of water, is accessible only by boat or helicopter, and drills to depths in excess of 12,000 feet. Offshore drilling presents risks and costs not associated with onshore operations.

significantly lower than past actual experience. For example, internal documents maintained by Hall indicate that the cost to drill a new well in the Redoubt field was roughly $13 million. However, Hall told the engineer firm to use a cost of $4.6 million per new well in its reserve report. And instead of using recent expense data, as is customary in the industry, Hall gave the engineer firm nearly three year old operating expense data, which he revised down purportedly because he believed Miller Energy could run a leaner operation than former operators of the properties. By way of example, Hall told the engineer firm that the offshore Redoubt Shoal field would cost $399,000 per month to operate when it actually cost the seller more than $600,000 per month, and when internal estimates show that Miller Energy and Hall expected the field to cost more than $800,000 per month once fully operational.

Additionally, in some years, the report included zero expenses for operating the facilities in Redoubt and another field. Overall, the reserve report implied operating expenses of $4 per barrel of oil equivalent ("boe") for all categories of reserves. That level of operating expenses was unreasonable in light of its predecessor's actual operating expenses of $32.50/boe in 2008 and $55.42/boe in the first half of 2009 before the wells were shut-in. Moreover, Miller Energy's actual costs since the acquisition only confirm the unreasonableness of its initial, 14 year cost estimate of $237 million. While the Alaska properties helped increase its overall oil and gas revenues from $4.4 million in 2010 to $69.4 million in 2014 (for cumulative revenues during that four year period of $157 million), Miller Energy had reported capital, operating, and general administrative costs in excess of $400 million for those years, during which time it recovered only 7% of the production projected in the reserve report.[9]

[9] The cumulative revenues of $157 million and costs of $400 million include Miller Energy's Appalachian properties; however, those properties were insignificant. For example, in fiscal 2014, the Appalachian properties accounted for 4% of the Company's revenues and 5% of its production.

3. Miller Energy and Boyd Relied on an Insurance Study That Did Not Reflect the Fair Value of the Fixed Assets

In addition to the $368 million value recorded for the oil and gas properties, Miller Energy also erroneously recorded a separate value of $110 million for acquired fixed assets, such as facilities and pipelines ancillary to the oil and gas reserves. In a February 8, 2010 email, Boyd informed Hall that he needed an amount to use as fair value for the fixed assets obtained as part of the Alaska acquisition. He noted that, ideally, the value should be what a willing buyer would pay for the assets, but "[i]n the absence of that, replacement values or something similar would probably work." Two days later, Boyd was sent an "asset replacement cost study" purportedly provided by an independent insurance broker, which appeared to list the replacement cost for the assets as $110 million.[10] The "study" was dated September 5, 2008, but "revised" on February 9, 2010. Without any additional analysis, Boyd recorded the amount in the revised insurance study on Miller Energy's balance sheet. The recording of assets at that value was improper for several reasons.

First, Miller Energy's use of the values in the insurance study resulted in counting the value of the fixed assets twice, thereby overstating the value of such assets. The reserve report Miller Energy relied on to value the acquired oil and gas properties used a discounted cash flow model. Valuation specialists use such models to estimate the value of an enterprise's "operating assets" – *i.e.*, the assets employed to generate future cash flows – by converting future benefit streams into a net present value. In Miller Energy's case, the fixed assets in the insurance study were the very same operating assets that were expected to generate the future cash flows in the reserve report. Accordingly, they should not have been separately valued. For example, prior to

[10] Miller Energy never separately engaged or paid the insurance broker for any report, replacement cost or otherwise.

the acquisition, all of the production from the offshore Redoubt Shoal field ran through the Osprey platform, which had no processing facilities or power generating capability of its own. Power was sent from generators housed within the Kustatan Production Facility to the platform via a subsea line, which was connected to an underground power grid that ran throughout all of the acquired properties. Moreover, production from the offshore platform was sent onshore for processing through pipes to the Kustatan Production Facility. In other words, absent the platform, there would have been no way to obtain oil and gas from Redoubt Shoal without incurring upfront capital expenditures to replace the platform and its related infrastructure. Similarly, without the other production facilities, the platform would have lacked power and somewhere to process its oil and gas. The reserve report Miller Energy used for the valuation recognized the interconnectedness of the properties, as it expressly listed the facilities and the offshore platform as assets used to generate the future cash flows. In short, because the fixed assets were integral to the operations of the acquired properties, their values were captured in the reserve report's cash flows. Consequently, by separately valuing the same operating assets, Miller Energy overstated the value of the Alaska assets by as much as $110 million.

Second, even if the fixed assets had a separate value, the insurance study did not reflect fair value for two other reasons. The version of the insurance study used by Boyd purported to show "asset replacement cost"; however, absent further adjustments, replacement cost new does not qualify as fair value under GAAP. In addition, evidence shows that Miller Energy, at the direction of Boyd and Hall, refashioned a preexisting insurance study to make it appear that its own value of $110 million derived from a third party. The numbers in the fixed asset study were given to the insurance broker, and its predecessor, by its clients (*i.e.*, Miller Energy and the previous owners of the fixed assets) as far back as 2007, and were used as starting points for

other types of estimates, such as estimates for possible losses resulting from fire or natural disasters. The two employees at the insurance broker who were most familiar with the original "Loss Estimates Study," including the engineer who authored it, confirmed that no one at the broker ever tested or in any way double-checked the values given to them.

Boyd and Hall knew or knowingly disregarded the fact that the insurance study did not reflect fair value or any analysis by the insurance broker. On February 8, 2010, Hall directed Alaska personnel to contact the insurance broker and another oil and gas consulting company to ask them for a report reflecting fair value or replacement cost. The insurance broker responded on February 9, and told Miller Energy in an email copied to Hall that it could not provide a report showing replacement costs. As Hall requested, Miller Energy also contacted a separate consulting firm and sent it the insurance broker's original 2008 insurance report. Late on February 8, the consulting firm informed Miller Energy that the insurance study it sent was a "good reference" but the report did not state "value or replacement cost." The firm offered to conduct its own analysis, but advised that the estimate would take "approximately 2-3 weeks to complete" and "cost around $15,000-$18,000." Upon hearing the news that a new report might take two to three weeks, Alaska personnel, including Hall, called Boyd. According to one participant on this call, Boyd said he could not wait weeks for a new report. He "needed it quickly and he needed to base it on something . . . a professional had to sign off on it, not us, some third party. . . ." During the call, Boyd and Hall decided to rely on numbers in the insurance report as replacement costs, despite Hall having been told by the broker that it could not provide Miller Energy with replacement costs. With the aim of making the report appear as though it reflected replacement costs, Hall provided a subordinate with edits to the 2008 insurance report that significantly altered its appearance, including changing its name from "Loss

Estimates Study" to "Asset Replacement Cost Study." The revised report, which Miller Energy gave to Sherb & Co., omitted entirely the insurance broker's methodology and analysis.[11] As a result, the only numbers reflected in the revised report were the ones provided to the broker by Miller Energy and its predecessors.

4. Other Red Flags

ASC 820 emphasizes that "valuation techniques used to measure fair value shall maximize the use of relevant observable inputs and minimize the use of unobservable inputs" and entities may not ignore assumptions market participants would use.[12] Miller Energy and Boyd admittedly never applied this guidance when computing their estimate of fair value, despite the existence of numerous, readily apparent data points strongly indicating that the assets were worth substantially less than the $480 million value Miller Energy recorded. Since the late 1960s, several oil companies have owned and operated the properties, including one that sold the assets to reduce its indebtedness and two others that filed for bankruptcy protection. The immediate past owner of the properties purchased them in a package with other properties in August 2007 for $400 million in cash, the issuance of 10 million shares, and a $29.3 million note. At closing, the buyer recorded $443 million for its newly acquired oil and gas properties. The portion of the assets later purchased by Miller Energy represented roughly 29% of that amount. Prior to Miller Energy purchasing them, the group of assets it acquired had a book

[11] Some insignificant revisions were sent via email to the insurance broker; however, based on testimony and other evidence, it does not appear that the most material changes, including the omission of the two-page insurance loss analysis at the end of the study, were ever sent to the insurance broker.

[12] ASC 820 defines "unobservable inputs" as "inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances" and "observable inputs" as "inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity."

value of $114 million. Table 2, attached hereto in *Appendix A*, compares Miller Energy's recorded value to the seller's net book value as of August 2009.

Beginning in December 2008, months before it filed for bankruptcy, the former owner of the assets, with the help of one of the world's leading financial advisory and asset management firms, marketed the same group of assets that Miller Energy ultimately bought to 40 potential buyers. This process failed to attract any bidders, and the assets were auctioned by the bankruptcy court in July 2009, with the winning bidder agreeing to a total purchase price of $8 million for the assets. A second entity, who bid $7 million, was designated as the back-up purchaser. Neither bidder closed. As a result, the former owner of the assets sought in August 2009, and was granted in September, an order from the bankruptcy court allowing it to abandon the assets due to a lack of interest. Following the abandonment, as a result of Miller Energy's expression of interest in the assets, the bankruptcy court vacated its abandonment order, which set off a second round of auctions. Miller Energy won the final auction for $2.25 million cash and the assumption of certain liabilities. Among the parties Miller Energy outbid was Nabors Industries, Ltd., an oil and gas drilling company with revenue of $3.5 billion and assets of $21 billion in 2009. These facts, including that the assets had been abandoned after a year-long sales process, should have been a strong indication to Miller Energy and Boyd that the assets were worth significantly less than the $480 million recorded value.

Furthermore, Miller Energy knew that no market participant would have paid anywhere near $480 million for the Alaska assets. For example, Hall, a former employee of prior owners of the assets who became the head of Miller Energy's Alaska operations, testified that no potential buyer in December 2009 would have paid the amount Miller Energy recorded for its unproved reserves ($153 million) because, in his experience, prices are typically based only on

proved reserves and "because the market was very depressed" at the time. Presentations created by Hall's company during his pre-Miller Energy attempts to buy the assets estimated a total purchase price for the assets of approximately $3 to $17 million. Despite months of effort, Hall was unable, prior to being introduced to Miller Energy, to find a financial partner willing to assist in purchasing and developing the assets.

As a result of the fraudulent valuation, Miller Energy filed with the Commission financial reports that materially misstated the value of its assets, as follows: Forms 10-Q for the third quarter of fiscal year 2010 and all three quarters of fiscal years 2011 through 2015; Forms 10-K for fiscal years ended 2010 through 2014; the Form S-1 filed on August 8, 2010; the Forms S-3 filed on September 6, 2012 and October 5, 2012; and prospectuses filed between August 25, 2010 through August 21, 2014 pursuant to Rule 424. The fraudulent valuation also resulted in Miller Energy filing with the Commission financial reports that materially misstated its net income, as follows: Forms 10-Q for the third quarter of fiscal year 2010, all three quarters of fiscal 2011, and the first two quarter of 2012; Forms 10-K for fiscal years ended 2010 through 2012; the Form S-1 filed on August 8, 2010; the Forms S-3 filed on September 6, 2012 and October 5, 2012; and prospectus supplements filed between August 25, 2010 through August 21, 2014 pursuant to Rule 424. In addition, the fraudulent valuation rendered no fewer than 15 Forms 8-K filed between March 2010 through at least December 2014 materially false and misleading.

C. Vogt's Fiscal Year 2010 Audit of Miller Energy

In August 2008, approximately two weeks after hiring the founder's son-in-law as its new CEO and Chairman of the Board of Directors, Miller Energy hired Sherb & Co. to become the company's auditor. Vogt led an audit team that audited Miller Energy's financial statements for

fiscal years ended 2009 and 2010, billing a total of $66,500 and $128,500 respectively for audit, review and other services provided for such fiscal years.

As the engagement partner for the fiscal year 2010 Miller Energy audit, Vogt failed to perform the 2010 Miller Energy audit in accordance with PCAOB Auditing Standards.[13] These deficiencies included, among other items, failing properly to audit the fair value measurements, use the work of a specialist, plan, staff and supervise the audit, obtain sufficient competent audit evidence, exercise due care and professional skepticism, and to perform required audit testing. Vogt's failures all related to the accounting and reporting of the Alaska asset acquisition. Despite the materiality of the transaction on Miller Energy's financial statements, Vogt failed to adequately test the valuation of the assets and the related calculation of the gain on acquisition. Instead, Vogt relied almost exclusively, with very limited and wholly inadequate testing, on the aforementioned $368 million reserve report and the so-called "asset replacement cost study" to justify Miller Energy's $480 million valuation of the Alaska assets and a bargain purchase gain of $277 million.

Workpapers prepared by a non-CPA staff accountant, purportedly pursuant to AU § 336, "Using the Work of a Specialist," show that Vogt performed only a limited evaluation of the petroleum engineer firm's work and its qualifications as a specialist (as a petroleum engineer, not as a fair value appraiser). A simple review of the reserve report and engagement letter would have alerted Vogt that the engineer firm was not engaged to – and did not in fact – perform a fair value estimate for the Alaska assets. Among other significant flaws, Vogt never obtained an understanding of the objectives and scope of the specialist's work or the appropriateness of using the specialist's work for the purpose of fair valuing the assets. *See* AU § 336.09. Nor did Vogt

[13] All references herein to PCAOB standards are to the PCAOB standards in effect at the time of the conduct.

make the appropriate tests of data provided to the specialist, including operating and capital expenses estimated and provided by Hall. *See* AU § 336.12.

The audit of the recorded fixed assets of $110 million was similarly flawed. A member of Vogt's audit team merely obtained the asset replacement cost study and placed a copy of it in the workpapers, but Vogt failed to consider the nature of the fixed assets and whether they would be utilized to generate the cash flow from the oil and gas properties, and, if so, what remainder value, if any, would exist. Nor did Vogt or his audit team perform any meaningful work to consider the expertise and experience of those persons determining the fair value measurement, the significant management assumptions used in determining the fair value, and the documentation supporting management's assumptions. *See* AU § 328.12.

Vogt knew at the time of the accounting for the acquisition that Miller Energy had insufficient accounting staff and that any accounting was suspect. In a December 22, 2009 email to Miller Energy's senior management, Vogt indicated that he believed the Company's accounting staff was deficient, and that Boyd cut too many corners on the accounting documentation. Furthermore, Vogt stated that Hall's modeling of cash flows and expenses (for use in the reserve report) was "concerning" because there was no one taking a detailed look at his estimates. In an email dated March 17, 2011, Vogt also knew that the reserve report used suspect data and was completed on what he described as a "rushed basis," as Miller Energy "had very little time if none for any true due diligence of much depth into what [it] purchased."

As a result, Vogt, on behalf of Sherb & Co., issued an audit report containing an unqualified opinion for use in Miller Energy's 2010 Form 10-K that stated falsely that the audit had been conducted in accordance with the PCAOB's standards and that Miller Energy's

financial statements were presented fairly, in all material respects, in conformity with GAAP. The specific failures are detailed below.

1. Failure Auditing Fair Value Measurements and Disclosures (AU § 328)

AU § 328 requires auditors to obtain sufficient competent audit evidence to provide reasonable assurance that fair value measurements and disclosures are in conformity with GAAP. AU § 328.03. The standard provides that "[t]he auditor should test the data used to develop the fair value measurements and disclosures and evaluate whether the fair value measurements have been properly determined" including "whether the data on which the fair value measurements are based, including the data used in the work of a specialist, is accurate, complete and relevant . . . ." AU § 328.39. In addition, "[t]he auditor should evaluate the sufficiency and competence of the audit evidence obtained from auditing fair value measurements and disclosures as well as the consistency of that evidence with other audit evidence obtained and evaluated during the audit." AU § 328.47. If a valuation model is utilized, the auditor reviews the model and evaluates whether the assumptions used are reasonable. AU § 328.38.

Vogt failed to comply with these requirements in connection with the 2010 audit of Miller Energy. While Vogt performed some testing on the data used to create the reserve report, he failed to test key elements such as the discount rate utilized, the risk weighting of the probable and possible reserves, estimated oil prices, and operating and capital expenses. Vogt also never properly considered the relevancy of the reserve report, improperly relying exclusively on the report since the specialist, a petroleum engineer, was not engaged to estimate a fair valuation, as expressly indicated in the report. Nor did he consider the consistency of the evidence in light of the other evidence, such as Miller Energy's actual purchase price of the assets (reported at less

than $5 million), and the fact that the assets had previously been abandoned during a bankruptcy proceeding. While Vogt and his staff reviewed some aspects of the specialist's valuation model, they failed to sufficiently review and evaluate the reasonableness of assumptions such as discount rate, risk weight of certain reserves, future oil prices, and operating and capital expenses.

Vogt also failed to obtain sufficient audit evidence to support the fair value of the fixed assets. Vogt performed limited, if any, testing of the asset replacement cost study purportedly supporting the fixed asset valuation. He did not assess the competency or sufficiency of the asset replacement cost study, or understand who created the Study, their qualifications, and the data underlying their valuation. Finally, Vogt failed to consider whether some or all of the fixed assets were being utilized in the estimated values captured in the reserve report.

2. Failure in Using the Work of a Specialist (AU § 336)

AU § 336 provides guidance to auditors when the work of a specialist is used in performing an audit of financial statements prepared in accordance with GAAP. Among other items, the standard requires the auditor to evaluate the specialist to ensure that he/she possesses the necessary skill or knowledge in the type of work under consideration and the appropriateness of using the specialist's work for the intended purpose. Specifically, AU § 336.08 states that "The auditor should consider the following to evaluate the professional qualifications of the specialist in determining that the specialist possesses the necessary skill or knowledge in the particular field: (a) the professional certification, license, or other recognition of the competence of the specialist in his or her field, as appropriate; (b) the reputation and standing of the specialist in the views of peers and others familiar with the specialist's capability or performance; and (c) the specialist's experience in the type of work under consideration."

Furthermore, AU § 336.09 states that the auditor should obtain an understanding of the nature of the work performed or to be performed by the specialist. This understanding should cover the following: (a) the objectives and scope of the specialist's work; (b) the specialist's relationship to the client; (c) the methods or assumptions used; (d) a comparison of the methods or assumptions used with those used in the preceding period; (e) the appropriateness of using the specialist's work for the intended purpose; (f) the form and content of the specialist's findings that will enable the auditor to make the evaluation described in paragraph [336].12."[14]

Although the Standard allows an auditor to use the work of a specialist as evidential matter in performing substantive tests to evaluate material financial statement assertions (*see* AU § 336.03), Vogt failed in several respects in his use of a specialist regarding the valuation of Miller Energy's Alaska acquisition.

Vogt did not properly consider the petroleum engineer's experience in fair valuation of assets, which was nonexistent. *See* AU § 336.08. Vogt also failed to obtain an understanding of the objectives and scope and intended purpose of the petroleum engineer's engagement for Miller Energy, which was to produce a reserve report for reserve disclosure purposes, not a fair valuation of acquired assets. *See* AU § 336.09. Indeed, the single page of the reserve report included in Vogt's workpapers, to support his evaluation of Miller Energy's $368 million valuation, clearly states that the "values shown . . . should not be construed as our estimate of fair market value."

[14] AU § 336.12 states that an auditor should evaluate the appropriateness and reasonableness of methods and assumptions used, during which the auditor should: "(a) obtain an understanding of the methods and assumptions used by the specialist, (b) make appropriate tests of data provided to the specialist, taking into account the auditor's assessment of control risk, and (c) evaluate whether the specialist's findings support the related assertions in the financial statements."

Furthermore, Vogt failed to adequately obtain an understanding of the methods and assumptions used by the specialist, or appropriately test data provided to the specialist. *See* AU § 336.12. There is no evidence that Vogt considered the appropriateness of certain key assumptions used by the petroleum engineer, such as the discount rate, estimated price of oil and gas, and the lack of risk weighting of probable and possible reserves. Finally, Vogt, despite alerting Boyd and Miller Energy's then CEO of the lack of sufficient review and inquiry, failed to adequately test the operating and capital expense estimates provided to the specialist by Miller Energy, and took few audit steps, other than inquiry, to assess the reasonableness of the expense estimates.

Vogt performed no steps to evaluate the qualifications of the authors of the asset replacement cost study, or understand the methods or assumptions they used or the appropriateness of using the Asset Replacement Study to support the valuation of the fixed assets at $110 million.

3. Failure to Exercise Due Professional Care in the Performance of Work (AU § 230)

PCAOB Standards require auditors to exercise due professional care in the planning and performance of the audit. *See* AU § 230.01. Due professional care requires the auditor to exercise professional skepticism: an attitude that includes a questioning mind and a critical assessment of audit evidence. *See* AU § 230.07. Moreover, gathering and objectively evaluating audit evidence requires the auditor to consider the competency and sufficiency of the evidence. *See* AU § 230.08.

Vogt failed to exercise due professional care regarding the audit of the Alaska acquisition valuation during the 2010 Miller Energy audit. Miller Energy had valued the assets purchased for a few million dollars at $480 million and had recorded a corresponding $277 million bargain

purchase gain. Given the size of the transaction, Vogt should have focused more closely on the diligence required to gather and objectively evaluate the evidence supporting the fair value of the oil & gas properties acquired to comply with ASC 805 and common industry practice. He failed to adequately consider the competency and sufficiency of the reserve report as evidence of the fair value of the acquired oil and gas properties. Vogt also performed limited procedures and failed to sufficiently evaluate the evidentiary value of the Asset Replacement Study, including failing to understand the source of the fixed asset values therein and the competency of the report authors.

4. Failure to Plan and Supervise (AU § 311)

AU § 311 requires an auditor to adequately plan the work and properly supervise assistants. AU § 311.01. In planning the audit, the auditor should consider, among other matters, the entity's business, the entity's accounting policies and procedures, and planned assessed level of control risk. AU § 311.03. A written audit program is required. AU § 311.05. Supervision involves directing the efforts of assistants who are involved in accomplishing the objectives of the audit and determining whether those objectives were accomplished. The extent of supervision appropriate in a given instance depends on many factors, including the complexity of the subject matter and the qualifications of persons performing the work. AU § 311.11.

Vogt's work did not meet this standard. Vogt's audit program to test Miller Energy's fair value assessment of the Alaska acquisition was insufficient. The planned procedures largely consisted of verifying the credentials of a specialist. Vogt's audit program failed to set forth procedures necessary to ensure the appropriateness of using the specialist's work for the purpose of a fair valuation. Nor did his audit program provide additional and alternate procedures for the insufficient evidence provided by the work of the specialist. As to the fixed assets, Vogt's

program was insufficient in that it merely required agreeing the asset balance to the Asset Replacement Study provided by Miller Energy.

Vogt's supervision of his staff was also deficient . Vogt spent little time on-site while the field work was conducted, and he knew the staff auditors had insufficient oil and gas industry experience. It was evident during their respective testimonies that the two staff members assigned by Vogt to the Miller Energy audit, whose experience consisted almost entirely of auditing microcap companies, were ill-prepared to test a transaction purportedly valued in excess of $400 million. The most junior staff member was not a Certified Public Accountant, did not appear to comprehend basic accounting principles, including elementary aspects of fair value accounting, yet was charged with the testing of the oil and gas properties fair valuation.

5. Failure to Properly Assess Audit Risk and Materiality in Conducting an Audit (AU § 312)

AU § 312 states that, when an auditor has concluded that there is a significant risk of material misstatement of the financial statements, the auditor should consider this conclusion in determining the nature, timing, or extent of procedures; assigning staff; or requiring appropriate levels of supervision. Ordinarily, higher risk requires more experienced personnel or more extensive supervision by the auditor with final responsibility for the engagement during both the planning and the conduct of the engagement. 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

Vogt's knowledge of the magnitude of the Alaska acquisition, and his knowledge of the inadequacy of Miller Energy's accounting personnel, including Boyd , should have resulted in increased scrutiny of Miller Energy's valuation of the Alaska assets. Yet Vogt assigned crucial

audit procedures to staff that lacked appropriate industry and auditing experience, and did not sufficiently supervise their work.

6. Failure to Obtain Sufficient Competent Evidential Matter (AU § 326)

Under the third standard of field work, sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit. AU § 326.01. Since he over relied on a reserve report and the Asset Replacement Study, and took limited to no additional audit steps to test that audit evidence, Vogt failed to obtain sufficient evidence of the fair value of the Alaska acquisition.

7. Failure to Issue an Accurate Audit Report (AU § 508)

Under AU § 508, an auditor may only express an unqualified opinion on historical financial statements when the auditor has formed such an opinion on the basis of an audit performed in accordance with PCAOB standards. AU § 508.07. Based upon the audit failures discussed above, Vogt should not have issued an audit report containing an unqualified opinion on Miller Energy's fiscal year 2010 financial statements.

IV. LEGAL DISCUSSION

A. Violations of the Antifraud Provisions of the Federal Securities Laws

Section 17(a) of the Securities Act prohibits fraud in the offer or sale of a security, and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit fraud in connection with the purchase or sale of securities. Specifically, these antifraud provisions prohibit: (1) any device, scheme or artifice to defraud; (2) any material misrepresentation or omission;[15] or (3) any act, practice, or course of business that operates as a fraud or deceit. To establish a violation of

[15] Section 17(a)(2) of the Securities Act further requires that the defendant "obtain[] money or property by means of" the material misrepresentation or omission.

Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5, the Commission must prove that the defendant acted with scienter. *Aaron v. SEC*, 446 U.S. 680, 701-02 (1980). Scienter is defined as "a mental state embracing intent to deceive, manipulate or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). Scienter "may be established through a heightened showing of recklessness." *In the Matter of John P. Flannery*, Exch. Act Rel. No. 73840, 2014 WL 7145625, *10 n. 24 (Dec. 15, 2014) (opinion of the Commission) (citations omitted); *see also Dolphin and Bradbury, Inc. v. SEC*, 512 F.3d 634, 639 (D.C. Cir. 2008). Recklessness is defined as "highly unreasonable conduct which is an extreme departure from the standards of ordinary care. While the danger need not be known, it must at least be so obvious that any reasonable man would have known it." *Ernst & Young*, 622 F.3d at 479. The scienter of a control person can be imputed to a corporation. *See SEC v. Manor Nursing Ctrs., Inc.*, 458 F.2d 1082, 1089 n.3 and1096 n.16 (2d Cir. 1972) (holding that an individual's "knowledge is imputed to the corporations which he controlled"). Scienter is not a necessary element of a violation of Sections 17(a)(2) and 17(a)(3) of the Securities Act, *Aaron*, 446 U.S. at 702; a showing of negligence is sufficient.

1. Sections 17(a)(2) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder

On March 22, 2010, Miller Energy filed with the Commission a Form 10-Q for its fiscal third quarter, which Boyd signed, that contained material misstatements concerning the Alaska acquisition. As described above, Miller Energy's valuation of the Alaska assets, which Boyd was responsible for developing, overstated the value of the oil and gas properties and fixed assets on its balance sheet, as well as the bargain purchase gain reflected in its income statement and statement of cash flows, in violation of GAAP. These misstatements were included in Miller Energy's subsequent Exchange Act and Securities Act filings. In addition, on March 29, 2010,

Miller Energy filed a Form 8-K, which Boyd signed, that not only reiterated the above misstatements concerning the valuation, but also stated falsely that the values were supported by independent appraisals. These misstatements were material and in connection with the purchase and sale of securities.[16] The fraudulent valuation resulted in Miller Energy recognizing a nearly 5,000% increase in its reported assets and net income of $272 million from a $556,000 net loss on a year-over-year basis for fiscal 3Q2010. Immediately following the Company's March 2010 announcement, there was substantial investor trading in Miller Energy shares.

Under *Janus Capital Group, Inc. v. First Derivative Traders*, 131 S. Ct. 2296 (2011), it is sufficient to charge officers for primary violations as "makers" when they sign a Commission filing that contains materially false and misleading statements or when statements are attributed to the individual. *See, e.g., City of Roseville Employees' Ret. Sys. v. EnergySolutions, Inc.*, 814 F. Supp. 2d 395, 417 (S.D.N.Y. 2011) (finding complaint adequately alleged that defendants were makers of statements in registration statements that they signed).[17] Boyd made material misstatements in violation of Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder by signing Miller Energy's periodic filings that reported $480 million in assets, as well as the resulting bargain purchase gain, when he knew, or was reckless in not knowing, that the valuations he relied upon had no reasonable basis. For example, as discussed above, Boyd knew he had to record the Alaska acquisition at "fair value," but he did nothing – other than confer in generalities with his auditor, who he knew had no prior oil and gas experience – to apprise himself of authoritative accounting literature applicable to Miller Energy's fair value assessment,

[16] The Supreme Court recently held that a fraudulent misrepresentation or omission within the meaning of Section 10(b) is not made "in connection with" the purchase or sale of a security "unless it is material to a decision by one or more individuals (other than the fraudster) to buy or sell" such security. *Chadbourne & Parke LLP v. Troice*, 134 S. Ct. 1058, 1066 (2014).

[17] The Commission has concluded that Section 17(a)(2) of the Securities Act is unaffected by *Janus*. *See, e.g., John P. Flannery*, 2014 WL 7145625, at *11.

and he admitted in testimony that he did not know how other oil and gas companies valued their properties. Boyd also ignored the disclaimer in the reserve report which stated unambiguously that the numbers therein were *not* fair value. Furthermore, as to the fixed assets, when told that a new fixed asset valuation would take weeks, Boyd decided to use as fair value the numbers in a preexisting report that was created for insurance purposes and included "replacement or repair" numbers supplied by Miller Energy. Documents dated after the initial valuation show that Boyd knew the insurance values were not fair value.[18] Boyd blindly accepted the purported values shown in the reserve report and in the insurance study, without questioning or double-checking in any way the assumptions used in either report. In short, Boyd, at a minimum, ignored red flags that were known or apparent to him.

Likewise, Hall "made" a statement within the meaning of *Janus* when he signed several of Miller Energy's filings with the Commission, including Forms 10-K for fiscal years 2010 through 2012 and the Form S-1 filed on August 13, 2010, which became effective on August 25, 2010, that contained material misstatements concerning the value of Miller Energy's assets and its net income.[19] As described above, Hall made these misstatements with scienter, having known that the reserve report's expenses were understated. Indeed, he provided the petroleum engineer with unsubstantiated cost information that contradicted not only historical data, but also

[18] On June 21, 2011, Boyd sent KPMG a draft letter with proposed responses to comments from Corp Fin about the insurance study used to value the fixed assets. In that letter, Boyd proposed to say that the broker's "report was prepared to determine asset replacement cost, not fair market value." It appears that KPMG revised the language to say that the broker "utilized the cost approach to value the subject personal property, specifically, the direct cost method," which is the final language used in the letter sent to Corp Fin. On June 22, 2011, several days prior to sending the aforementioned letter to Corp Fin, the insurance broker expressly told Boyd that its insurance study was not "intended to be used as a 3rd party appraisal" and it evaluated the properties using methodologies for insurance purposes, such as maximum foreseeable loss for fire – as previously noted, Miller Energy excised these methodologies and the resulting values from the study it sent to Vogt and Sherb & Co. Neither the insurance study nor the correspondence with the insurance company mentions the "cost approach" or the "direct cost method."

[19] These material misstatements were made in the offer and sale of securities, as Miller Energy has registered and sold tens of millions of dollars of common and preferred stock between 2010 and 2014. For example, in September 2012, Miller issued newly designated Series C Cumulative Redeemable Preferred Stock for net proceeds of $14.4 million, and, in February 2013, the Company sold additional Series C stock for proceeds of $13.3 million.

the expense projections he used in his own internal models and budgets. He also knew, or was reckless in not knowing, that the insurance study did not accurately reflect a third-party's estimate of replacement cost. As detailed above, after being told via email that the insurance broker could not supply Miller Energy with a report showing replacement values, Hall directed the revisions to the insurance report Miller Energy used to support the fair value of its fixed assets.

Miller Energy violated Section 10(b) and Rule 10b-5(b) because it made material misstatements in documents that it was obligated to file with the Commission and because the scienter of Boyd and Hall is imputed to it.

In addition, Miller Energy violated Section 17(a)(2) of the Securities Act by obtaining money or property by means of the false statements. This element of Section 17(a)(2) is satisfied because Miller Energy filed registration statements and prospectus supplements that made – or, in some cases, incorporated by reference – the same false and misleading set forth in the Company's periodic filings, and then conducted offerings in which it obtained millions of dollars of proceeds. Although there is no evidence that Boyd or Hall obtained proceeds directly from any of the offerings in question, Boyd oversaw the Company's fair value determination, with Hall supplying the underlying reports, and the Division will rely on the money received by Miller Energy in proving this case against them. *See John P. Flannery*, 2014 WL 7145625, at *25 ("a misrepresentation must be at least relevant to, if not the cause of, the transfer of money or property from an investor to the defendant (or perhaps his employer).").

2. Sections 17(a)(1) and 17(a)(3) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5(a) and 10b-5(c) thereunder

In addition to liability for fraudulent misrepresentations and omissions, the Securities Act and Exchange Act – specifically, Sections 17(a)(1) and (3) and Rules 10b-5(a) and (c) – impose

what is commonly referred to as "scheme liability." Section 10(b) makes it "unlawful for any person directly or indirectly . . . to use or employ, in connection with the purchase or sale of any security . . .any manipulative or deceptive device or contrivance in contravention of" Commission rules. It does so through three subsections that are "mutually supporting rather than mutually exclusive." *John P. Flannery*, 2014 WL 7145625, at *10. In addition to Rule 10b-5(b), discussed above, Rule 10b-5(a) and (c) prohibit "directly or indirectly . . . employ[ing] any device, scheme, or artifice to defraud" and "directly or indirectly . . . engag[ing] in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." Essentially the same elements are required under Section 17(a)(1) and (3) in connection with the offer or sale of a security, though no showing of scienter is required for the SEC to obtain an injunction under subsection (a)(3). *See SEC v. Monarch Funding Corp.*, 192 F.3d 295, 308 (2d Cir. 1999).

"[I]t is possible for liability to arise under both subsection (b) and subsections (a) and (c) of Rule 10b-5 out of the same set of facts, where the plaintiffs allege both that the defendants made misrepresentations in violations of Rule 10b-5(b), as well as that the defendants undertook a deceptive scheme or course of conduct that went beyond the misrepresentations." *SEC v. Patel*, No. 07-cv-39, 2009 WL 3151143, at *7 (D.N.H. Sept. 30, 2009) (quotation omitted); *John P. Flannery*, 2014 WL 7145625, at *12 ("primary liability under Rule 10b-5(a) and (c) also encompasses the "making" of a fraudulent misstatement to investors, as well as the drafting or devising of such a misstatement") (emphasis in original). Moreover, "[a] scheme to defraud may well include later efforts to avoid detection of the fraud." *SEC v. Holschuh*, 694 F.2d 130, 144 n.24 (7th Cir. 1982) ("Avoidance of detection and prevention of recovery of the money lost

by the victims are within, and often a material part of, the illegal scheme." (quoting *United States v. Riedel*, 126 F.2d 81, 83 (7th Cir. 1942))).

By way of the conduct described above, Miller Energy, Boyd, and Hall are primarily liable under Sections 17(a)(1) and (3) of the Securities Act, as well as subsections (a) and (c) of Rule 10b-5. Scheme liability is appropriate because Boyd and Hall orchestrated a scheme to defraud Miller Energy's shareholders by materially overstating the value of the acquired Alaska assets, which included, among other things, the use of a false fixed asset report. The Division therefore alleged scheme liability claims as well.

3. Boyd and Hall Caused Miller Energy's Violations of the Antifraud Provisions

To establish that a respondent was a cause of another entity's violations requires a showing that (1) there was a primary violation by the other entity, (2) an act or omission by the respondent caused the violation, and (3) the respondent knew or should have known that her act or omission would contribute to the violation. *In the Matter of Phlo Corp.* (Exchange Act Rel. No. 55562, March 30, 2007). Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. *See In the Matter of KPMG Peat Marwick LLP*, 54 S.E.C. 1135, 1175 (2001).

Through the conduct described above, Boyd and Hall caused Miller Energy's violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

B. Violations of the Reporting Provisions

Section 13(a) of the Exchange Act and Exchange Act Rules 13a-1, 13a-11, and 13a-13 thereunder require issuers of registered securities to file with the Commission factually accurate annual, current, and quarterly reports. *See generally Ponce v. SEC*, 345 F.3d 722, 734-38 (9th

Cir. 2003). Exchange Act Rule 12b-20 also requires that, in addition to the information expressly required to be included in such reports, there shall be added such further material information as may be necessary to ensure that the required information not materially misleading. No showing of scienter is necessary to establish a violation of these provisions. *SEC v. McNulty*, 137 F.3d 732, 740-41 (2d Cir. 1998). Financial statements incorporated in Commission filings must comply with Regulation S-X, which states that "[f]inancial statements filed with the Commission which are not prepared in accordance with GAAP will be presumed to be misleading or inaccurate."

Moreover, Exchange Act Rule 13a-14 requires an issuer's principal executive officer and principal financial officer to sign certifications, which are included as exhibits to the annual and quarterly reports. These certifications state that the signing officer has reviewed the report and, among other things, that based on his knowledge the periodic filing includes no material misstatements or omissions. *See generally In re Enron Corp. Sec., Derivative & ERISA Litig.*, 258 F. Supp. 2d 576, 588 n.7 (S.D. Tex. 2003).

1. Miller Energy Violated Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11 and 13a-13 Thereunder

Miller Energy violated these reporting provisions by filing with the Commission annual reports for fiscal years 2010 through at least 2014, and quarterly reports for the third quarter of fiscal 2010, for the first three quarters in the fiscal years 2011 through at least 2014, and for the first three quarters of fiscal 2015 that materially misstated its financial position. Miller Energy also filed current reports reiterating the material misstatements in its periodic reports. Through the conduct described above, Boyd and Hall caused Miller Energy's violations of Section 13(a) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, 13a-11, and 13a-13.

2. Boyd Violated Rule 13a-14

In addition, Boyd violated Rule 13a-14 by falsely certifying that, based on his knowledge, Miller Energy's Forms 10-K for fiscal years 2010 and 2011, and its Forms 10-Q for the third quarter of fiscal 2010 through the first quarter of fiscal 2012, contained no material misstatements or omissions.[20] Boyd knowingly signed false certifications: each falsely reported the value of the oil and gas properties attributed to the Alaska acquisition. As such, Boyd violated Exchange Act Rule 13a-14.

C. Violations of the Internal Controls and Books and Records Provisions

1. Exchange Act Sections 13(b)(2)(A) and (B)

Section 13(b)(2) of the Exchange Act requires an issuer: (A) to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of its assets, and (B) to devise and maintain a system of internal accounting controls which provide reasonable assurances that, among other things, transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP.

Miller Energy violated Section 13(b)(2)(A) of the Exchange Act by maintaining false and misleading books, records and accounts, including false records concerning the value of its oil and gas properties. In addition, Miller Energy violated the internal controls provisions of Section 13(b)(2)(B) of the Exchange Act, by, *inter alia*, failing to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurance that Miller Energy's assets were recorded appropriately. Through the conduct described above, Boyd and Hall caused Miller Energy's violations of Section 13(b)(2)(A) and (B).

2. Exchange Act Section 13(b)(5) and Rule 13b2-1

[20] While Hall signed various filings with the Commission in his capacity as a member of the Board of Directors, the Division did not charge Hall with violation of Rule 13a-14, because, as the CEO of Miller Energy's wholly-owned subsidiary, he did not certify the Company's financials.

Section 13(b)(5) of the Exchange Act provides that no person shall knowingly circumvent or knowingly fail to implement a system of internal accounting controls, or knowingly falsify any accounting book, record or account. Through the conduct described above, Boyd and Hall violated Section 13(b)(5) of the Exchange Act. First, as described above, Hall knowingly directly or indirectly falsified or caused to be falsified Miller Energy's books and records concerning the value of its oil and gas properties. Second, Boyd knowingly failed adequately to implement a system of internal accounting controls. Miller Energy's controls over financial reporting were a known problem that went uncorrected through at least fiscal 2011. For the period ended April 30, 2008, Miller Energy announced that it had identified a material weakness relating to its accounting resources not being "adequate to allow sufficient time for the accounting department to (i) perform a review of the consolidation and supporting financial statement disclosure schedules independent of the preparer (ii) adequately prepare for our quarterly reviews and annual audit and (iii) research all applicable accounting pronouncements as they relate to [its] financial statements and underlying disclosures." Based on the Division's investigation, it appears that Miller Energy's controls over financial reporting, as they related to accounting estimates, including management's fair value determinations, were grossly inadequate. Further, while he was informed in December 2009 that there were insufficient controls over the expense estimates prepared by Hall, there is no evidence that Boyd made any effort to ensure that Hall's estimates were reasonable and reliable.

Exchange Act Rule 13b2-1 provides that no person shall, directly or indirectly, falsify or cause to be falsified any book, record, or account subject to Section 13(b)(2). Evidence of negligence is sufficient to establish that a person caused a violation of Rule 13b2-1. *In the Matter of Joseph E. Williams*, Exch. Act Rel. No. 42412, 2000 WL 143999, *4 (Feb. 10, 2000)

(opinion of the Commission). Boyd and Hall caused Miller Energy's record-keeping violations, and they were at the very least negligent in not knowing, based on the information they received and/or could have determined through additional inquiry, that Miller Energy's recorded assets and income were overstated.

D. Rule 102(e)

Rule 102(e)(1)(ii) of the Commission's Rules of Practice provides that the Commission may deny to any person the privilege of practicing before it as an accountant, if that person is found to have engaged in improper professional conduct. Section 4C(a)(2) of the Exchange Act provides for the same authority. Improper professional conduct under Rule 102(e)(1)(ii) may be intentional or reckless. It can also be one of two types of negligent conduct: a single instance of highly unreasonable conduct that results in a violation of applicable professional standards in circumstances for which heightened scrutiny is warranted; or repeated instances of unreasonable conduct, each resulting in violations of applicable professional standards that indicate a lack of competence.[21] Rule 102(e)(1)(iii) provides the same relief against anyone found to have willfully violated, or willfully aided and abetted the violation of any provision of the Federal securities laws or the rules and regulations thereunder. A willful violation of the securities laws means merely "'that the person charged with the duty knows what he is doing.'" *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000) (citation omitted). There is no requirement that the actor "'also be aware that he is violating one of the Rules or Acts.'" *Id.* (citation omitted).

1. Vogt

[21] The term "applicable professional standards" refers broadly to promulgated accounting and auditing standards. References in Commission rules and staff guidance and in the federal securities laws to GAAS or to specific standards under GAAS, as they relate to issuers, should be understood to mean the PCAOB Standards plus any applicable rules of the Commission.

As discussed above, Vogt, as the engagement partner on Sherb & Co.'s audit of Miller Energy's financial statements for fiscal 2010, failed to comply with the relevant audit standards. For example, he failed adequately to examine the qualifications of the purported third-party appraisers relied on by Miller Energy and the appropriateness of the assumptions they used (AU §§ 328 and 336). He also failed to exercise due care and professional skepticism when reviewing and approving Miller Energy's fair value assessment (AU § 230) and failed to realize that the reserve report, the asset replacement cost study, and his staff auditor's workpapers on using the work of a specialist did not provide sufficient competent evidence to substantiate Miller Energy's fair value assessment (AU §§ 230, 326, 328, and 336). He also approved the audit planning without an adequate understanding of Miller Energy's business and its Alaska acquisition (AU §§ 311 and 312). In addition, he failed to implement adequate procedures to test Miller Energy's valuation of its Alaska assets to ensure they were not overvalued (AU §§ 312, 326, and 328). Vogt's failure to take these steps is proof that he acted recklessly in conducting the audit by knowingly turning a blind eye to specific accounting issues that presented a high risk of fraudulent financial reporting. Vogt's conduct represents a single instance of highly unreasonable conduct related to the valuation of Miller Energy's Alaska acquisition, a material transaction that should have been viewed with heightened risk.

2. Boyd

In addition, through the conduct described above, Boyd willfully violated Section 17(a) of the Securities Act, Sections 10(b) and 13(b)(5) of the Exchange Act, and Rules 10b-5, 13a-14, and 13b2-1 thereunder, and willfully aided and abetted and caused Miller Energy's violations of Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-11, and 13a-13. Given his prior education,

experience, and previous position as a Chief Financial Officer at a public company, it reasonably can be expected that he will seek to obtain future employment with a public company and thereafter appear and practice before the Commission as an accountant.

V. RELIEF REQUESTED

A. Administrative and Cease-and-Desist Orders

Section 8A of the Securities Act and Section 21C of the Exchange Act authorize the Commission to enter a cease-and-desist order when it finds that a person or entity is violating, has violated, or is about to violate any provision of either Act. Miller Energy, Boyd, and Hall engaged in conduct that resulted in multiple, systematic and egregious violations of the federal securities laws. Further, Boyd and Hall acted with a high degree of scienter. Boyd was responsible for drafting, reviewing, signing, and/or certifying Miller Energy's Commission filings through at least July 2011, and Hall participated in and was responsible for obtaining the valuation reports that formed the basis of Miller Energy's fraudulent valuation. All of these respondents are in a position to commit future securities fraud. Boyd and Hall, who are relatively young, may work with public companies in the future. Indeed, Hall remains a member of Miller Energy's senior management, as its chief operating officer.

B. Disgorgement and Prejudgment Interest

The Division seeks disgorgement and prejudgment interest from Miller Energy, Boyd, and Hall, disgorging them of any unjust enrichment that is causally connected to their securities law violation. Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act provide that the Commission may enter an order for disgorgement and prejudgment interest. During the course of the fraud, Miller Energy conducted offerings in which it raised approximately $143 million from investors. In addition, Boyd and Hall received bonuses and

stock awards that were at least partially tied to their work on Miller Energy's acquisition of the Alaska assets and its financial performance.

C. Civil Penalties

The Division also seeks the imposition of civil penalties against Miller Energy, Boyd, and Hall. Section 8A(g) of the Securities Act and Section 21B(a)(2) of the Exchange Act authorize the Commission to seek civil penalties in cease-and-desist proceedings against any person who has violated the Securities Act or Exchange Act. As discussed above, Miller Energy, Boyd, and Hall engaged in a course of conduct that involved fraud, deceit, manipulation, and deliberate or reckless disregard of regulatory requirements. Miller Energy also received a direct and material benefit from the fraud in that it raised significant funds from investors in the offering that occurred while the fraud was ongoing. Hall obtained the reports forming the basis of Miller Energy's fraud, and knowingly understated the expenses in the reserve report used to value the companies. Moreover, civil penalties will serve as a strong deterrent to others similarly situated. Under these circumstances, consideration of civil penalties against Miller Energy, Boyd, and Hall is appropriate.

D. Officer and Director Bar

Section 8A(f) of the Securities Act and Section 21C(f) of the Exchange Act expressly provide that the Commission may issue an order to prohibit any person from serving as an officer and director of a public company if the person violated the antifraud provisions of the Securities Act or the Exchange Act and the person's conduct demonstrates unfitness to serve as an officer or director of a public company. The Commission has previously sought and obtained officer and director bars where, as here, senior officers directed and coordinated an issuer's efforts to defraud the investing public. Although Boyd and Hall did not personally profit from this scheme, other than through increased compensation, or have a prior record of securities law

violations, their conduct was egregious, evidenced a high degree of scienter, and occurred while they were acting as officers of Miller Energy. Hall is currently Miller Energy's chief operating officer, and absent an officer-and-director bar, there is no barrier to either Boyd or Hall being employed as an officer or director of a public company in the future.

E. Rule 102(e) Suspensions

Rules 102(e)(1)(ii) and (iii) of the Commission's Rules of Practice and Sections 4C(a)(2) and (3) of the Exchange Act authorize the Commission to enter an order censuring a person, or denying, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who the Commission finds has engaged in improper professional conduct or willfully violated the federal securities laws. Here, the Division seeks this appropriate relief against Boyd and Vogt.

VI. DIVISION'S RESPONSE TO WELLS SUBMISSIONS

A. Miller Respondents

In their joint Wells submission, Miller Energy, Boyd, and Hall (the "Miller Respondents") principally advance three arguments, none of which is persuasive. ***First***, the Miller Respondents obfuscate the facts and contend that Miller Energy's valuation was reasonable and made in good faith. However, Miller Energy's $480 million valuation was not simply the result of permissible accounting judgments, about which reasonable minds could differ. As noted above, Miller Energy plucked the number it used to value reserves directly from a PV-10 reserve report that – as the respondents concede – was not representative of fair value, and there is no evidence that Miller Energy conducted any independent analysis to determine whether the use of the reserve report number was appropriate, and the respondents do not argue otherwise. Instead, the Miller Respondents ignore the fact that management conducted no analysis of the 10% discount rate used and argue that management believed at the time of the

valuation that future taxable income would be offset by development expenses. In other words, they believed future costs would outpace future net profits, resulting in no income taxes being owed. This argument is nonsensical and conflicts with their other arguments. For instance, they argue that the expenses in the reserve report were reasonable. But they cannot have it both ways. The reserve report projected *net profits* in every year but 2010, cumulating in total future undiscounted pretax profits of $630 million. If the expenses were reasonable, then the net profits were taxable.[22] Conversely, if the future cash flows were offset by future expenses, those expenses should have been – but were not – reflected in the reserve report and should have resulted in a significantly reduced present value.[23]

In any event, as noted above, the expense numbers used in the reserve report were not reasonable. As discussed above, the value of the Alaska assets was materially inflated due to the use of understated and unsubstantiated expense numbers – and, for several years, the omission of operating expenses altogether. By way of example, historical documents show that it cost between $13 million and $15 million in the early 2000s to drill a new well in the Redoubt Shoal field. However, Hall told the engineer firm to use a cost of $4.6 million per well in its reserve report, resulting in the undiscounted capital costs for Redoubt to be understated by roughly $65 million. Nevertheless, the Miller Respondents argue that subsequent events show that its largest field, Redoubt, to which the company attributed $291 million of value, was valuable because it has produced $75.6 million in revenue. But their argument overlooks the substantial expenses

[22] To formulate its discount rate, KPMG did use guideline companies that, with one exception, had a five year effective tax rate of zero. But that was because KPMG chose mostly unprofitable microcap companies. By contrast, the reserve report showed the Alaska assets generating hundreds of millions in net profit. Miller Energy has not paid taxes because, contrary to its projections, its expenses have far exceeded its gross revenue since the acquisition. In any event, under ASC 820, valuations must be conducted based on assumptions that a market participant would use and not on company-specific assumptions, such as whether Miller Energy believed it would pay taxes on the assets.

[23] The Miller Respondents' reliance on SFAS 109 is misplaced. That standard provides guidance for how companies recognize income taxes in their financial statements and does not in any way alter or limit the use of taxes in the context of valuations conducted under ASC 820.

for the Alaska assets – and for Redoubt, in particular – incurred by Miller Energy since the acquisition. For example, between 2012 and 2014, Miller Energy's actual operating costs per barrel of oil equivalent ("boe") for Redoubt averaged $89.54, whereas the reserve report implied operating expenses for Redoubt of $3.73/boe. In addition, as detailed above, through 2014, the Alaska properties overall have cost nearly $250 million more to operate and explore than they have generated in revenue. Finally, the respondents' argument about Redoubt's value rings hollow in light of the company's recent $346.8 million in impairment charges for that field.

Although acknowledging that the report used to value the reserves did not contain any adjustments for the uncertainty associated with the cash flows for probable and possible reserves, the Miller Respondents nevertheless argue that the absence of those adjustments is irrelevant because the reserve report "included likely overly conservative price assumptions." According to them, if the engineer firm who authored the reserve report used the alternative price and discount rate assumptions adopted as reasonable by KPMG one year later, it "would either yield the same discounted cash flow estimates as those disclosed at the time or greater estimated fair values." For the reasons set forth above in Section VII, Litigation Risks, the Miller Respondents' reliance on KPMG's analysis is misplaced. In addition, as detailed above and as illustrated in Table 1, when combined with other reasonable assumptions, the use of higher price assumptions does not result in a value remotely approaching Miller Energy's $368 million valuation of the reserves.

The Miller Respondents also argue that even if the company's fair value conclusion was wrong, it was arrived at in good faith and is not actionable as a statement of opinion under *Fait v. Regions Fin. Corp.*, 655 F.3d 105 (2d Cir. 2011) and *Omnicare, Inc. v. Laborers. Dist. Council Const. Indus. Pension Fund*, 135 S.Ct. 1318 (2015). Although a fair value conclusion is

arguably an opinion, the Division contends that it can show that the Miller Respondents did not have a reasonable basis for its fair value disclosures. Moreover, Miller Energy's fair value disclosures in its filings with the Commission omitted material facts about the scope of Miller's inquiry in producing the valuation, and the resulting disclosures, that conflicted with what a reasonable investor would have expected. Investors reasonably expect management when making a fair valuation to have conducted a process that considered the relevant facts in its possession and that was reasonably calculated to ensure that its publicly reported fair value complied with GAAP. *Id.* at 1329 (stating an investor "expects not just that the issuer believes the opinion (however irrationally), but that it fairly aligns with the information in the issuer's possession at the time"); *Id.* at 1328 ("an investor, though recognizing that . . . opinions can prove wrong in the end, still likely expects such an assertion to rest on some meaningful inquiry"). As discussed above, Miller Energy and Boyd never conducted a reasonable inquiry into the numbers and assumptions used in the valuation, and they had access to a multitude of facts that contradicted their fair value conclusion. Additionally, in Miller Energy's 10-K, the company falsely told investors that its "PV-10 measure and the standardized measure of discounted cash flows do not purport to present the fair value of our natural gas and oil reserves" when Miller Energy and Boyd used those exact measures to arrive at the company's fair value for its Alaska assets.

Second, the Miller Respondents contend that the $110 million in "fixed assets" was properly recorded because the assets were not double-counted and because the valuation report, which two auditors reviewed, was prepared by a company "intimately familiar" with the assets. With respect to double-counting, they offer an illustration and argue generally that "owned wells" included in a discounted cash flow analysis have "inherent, independent value regardless

of the value of the oil and gas properties." This argument misapprehends fair value requirements and the purpose and use of discounted cash flow models. As discussed above, such models value every aspect of a property, including oil and gas wells. The other arguments are similarly unavailing. As noted above, the broker who purportedly prepared the insurance study conducted no evaluation of the fixed asset values Miller Energy used, Sherb & Co. conducted no audit procedures as to the insurance study, and KPMG's review was significantly flawed.

Third, the Miller Respondents argue that reasonable investors would not have been misled and refer to the "bespeaks caution" doctrine, which protects "forward-looking statements" that are accompanied by meaningful cautionary language. Respondents' reliance on the doctrine is misplaced for at least two reasons. First, the bespeaks caution doctrine does not protect statements of present or historic fact, such as Miller Energy's fair value disclosures. Those disclosures, beginning in March 2010, represented that the supposed fair value of the Alaska assets was "as of" December 10, 2009. Second, the identified risk disclosures were not meaningful because they related to Miller Energy's supplemental disclosures of its standardized measure of oil and gas (*see* Note 8, *supra*), not its fair value assessment. Miller Energy, moreover, never disclosed that its value of the reserves was based on a PV-10 reserve report, so investors had no reason to assume that the statements, such as "[e]stimates of oil and natural gas reserves are inherently imprecise," related to management's fair value conclusion. In fact, in its 2010 10-K, Miller Energy expressly told investors that "[o]ur PV-10 measure and the standardized measure of discounted future net cash flows do *not purport to present the fair value* of our natural gas and oil reserves." In light of this assertion, investors reasonably would have assumed that the undisclosed "appraisal[s]," which Miller Energy purportedly relied on for its fair value conclusion, involved something more substantial than a PV-10 reserve report.

B. Boyd and Hall

In addition to the joint submission, Boyd and Hall submitted a short memo of their own. In it, Boyd argues unpersuasively that he should not be suspended from practicing before the Commission because he did not engage in improper professional conduct. This argument is moot, as the basis for the Rule 102(e) recommendation against Boyd is his willful conduct, and not improper professional conduct.

In his Wells submissions, Hall argues that a showing of recklessness is insufficient for aiding and abetting claims and that the Commission must – but cannot – demonstrate his "actual knowledge," and that Hall did not knowingly falsify any books and records. As discussed above, the understated expense numbers provided by Hall to the engineer firm, as well as his falsification of the insurance report, provide sufficient evidence of his knowledge.

C. Vogt

Vogt argues that he conducted an audit in good faith and exercised due care because he took "multiple steps." However, none of those steps demonstrate either good faith or due care.[24] First, Vogt argues that he reviewed the seller's registration statement, which showed that in 2007 the seller purchased assets in Alaska for approximately $463 million. Apparently he believed wrongly that this purchase price supported Miller Energy's $480 million valuation. In fact, the two properties Miller Energy did not buy represented the lion's share of the 2007 purchase price. Records produced to the Division by Miller Energy and provided to Vogt in December 2009 show that the properties purchased by Miller Energy represented roughly 29% of the seller's oil

[24] The Division retained a GAAP and audit expert (R. Larry Johnson) who has extensively analyzed the professional improprieties, inadequacies and PCAOB audit standard failures of Vogt's audit of Miller Energy, as well as of the GAAP violations of the other Respondents. This expert has prepared an extensive report which has been included as DOE Exhibit 244 on the Division's exhibits list and will be an expert witness at trial in this matter.

and gas properties.[25] Second, Vogt argues that he conducted research about how other companies accounted for bargain purchase gains; however, his workpapers reveal that his review consisted of reading public filings mainly to see how companies worded their bargain purchase gain and related deferred tax disclosures. There is no evidence that Vogt spent any time reviewing how companies calculated their fair values or what valuation techniques or assumptions they used, and Vogt's Wells submission does not argue to the contrary. Third, Vogt argues that he relied on his staff accountant's memo about the work and qualifications of the petroleum engineer firm. As discussed above, this memo was patently deficient under applicable audit standards. Finally, Vogt argues that he considered a second reserve report that used NYMEX prices and resulted in a higher value. But, as discussed above, the audit standards for fair value contemplate more than a binary exercise involving a change to a single assumption and finding reasonable the lower of the two outcomes.

Vogt also makes other arguments, such as purported disclosures made by Miller Energy, the use of PV-10 as a "metric," and KPMG's subsequent audit of the value, that are substantially

[25] Vogt contends that he requested but did not receive documents "that broke down detail about the assets." That is untrue. In December 2009, Boyd sent Vogt a spreadsheet detailing the assets and the seller's book value for them. That document showed that, as of August 2009, the assets Miller purchased had a book value of approximately $114 million.

the same as the arguments advanced in Miller Energy's Wells submission.[26] For the reasons already discussed, none of those arguments are persuasive.[27]

VII. CONCLUSION

Based on the foregoing, the Division seeks cease and desist orders against Miller Energy, Boyd and Hall for violations of the securities laws, along with disgorgement, prejudgment interest and civil penalties. Further, Vogt engaged in improper professional conduct pursuant to Section 4C(a)(2) of the Exchange Act and Rule 102(e)(1)(ii) of the Commission's Rules of Practice, and should be denied the privilege of appearing or practicing before the Commission. Also pursuant to Section 4C of the Exchange Act and Rule 102(e)(1)(iii) of the Commission's Rules of Practice, Boyd willfully violated, and/or willfully aided and abetted, violations of the Federal securities laws or the rules and regulations thereunder and under those sections, and as an accountant Boyd should be denied the privilege of appearing or practicing before the Commission.

Respectfully submitted, this 8th day of January, 2016.

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[26] Vogt contends misleadingly that Corp Fin addressed six different comment letters to the reserve report. Virtually all of those comment letters dealt primarily with different reserve reports and issues other than the Company's valuation of the Alaska assets. Moreover, Miller Energy appears not to have provided Corp Fin with a fulsome response concerning the value of the acquisition, as it never provided Corp Fin with the actual reports it used to value the properties. Instead, to support the value of the reserves, Miller Energy supplied Corp Fin with a reserve report that was prepared later than the one used for its valuation and that showed higher values largely because it used higher oil prices. In referring to the subsequently prepared report, which showed a PV-10 of $543 million, Miller Energy falsely suggested that it had adjusted down the numbers in the report to arrive at its $368 million value. Miller Energy also falsely represented that the insurance report was prepared by a "third party valuation specialist" using the "cost approach."

[27] On June 4, 2015, Vogt filed a supplemental Wells submission arguing incorrectly that the $110 million of fixed assets had value separate and apart from the reserve report because some of the facilities were capable of supporting production greater than what was anticipated in the reserve report. That an asset may be underutilized does not, by itself, increase the value of the asset. For example, a bus does not have value separate from the net present value of the cash flows from its bus route because it is expected to have empty seats. In fact, not only would an oversized bus not have a separate value, but, assuming the same future cash flows, it would have a smaller net present value than a more appropriately sized bus because it likely would be more expensive to operate, thus reducing future profits.

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Certificate of Service

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Appendix A

In the Matter of Miller Petroleum, Inc. (A-03310)
Tables 1 & 2

Table 1 (in millions)

	Oil and Gas Properties	Fixed Assets	Total
Miller Valuation Recorded 2010	$368	$110	**$478**[1]
Adjustments			
Forecast Prices	$228		**$228**
Omission of Taxes	($90)		**($90)**
Improper Discount Rate	($179)		**($179)**
Risk Adjustment Factors	($180)		**($180)**
Expense Underestimate	($66)		**($66)**
Asset Retirement Obligations	($41)		**($41)**
Double counting		($110)	**($110)**
Estimated Actual Fair Value	$40	$0	**$40**

[1] Table 1 reflects $478 million instead of the total recorded value of $480 million because the staff is not challenging the value of the $2 million worth of inventory and restricted cash acquired by Miller Energy.

Table 2 (in millions)

Asset/Field	Miller Energy	Seller Book Value[2]
Redoubt Shoal	$290.7	$83.2
West McArthur River	$45.4	$31.1
Sabre	$32.3	$0.01
Cosmopolitan	$0.2	$0.08
West Foreland	$2.7	$0
Kustatan	-$14.6[3]	$0
Three Mile Creek	$1.7	$0
Sword	$8.4	-
Raptor	$1.4	-
Platform, Facilities, and Pipelines	$110	-
Total	$478.2	$114.4

[2] Values as of August 2009. Sword, Raptor, and the "fixed assets" were not itemized among the seller's book values.

[3] The negative $14.6 million number relates to fixed expenses for the Kustatan Production Facility that was not specifically applied to any particular field.