UNITED STATED OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 71833 / March 31, 2014

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3547 / March 31, 2014

Admin. Proc. File No. 3-15012

In the Matter of

S.W. HATFIELD, CPA and
SCOTT W. HATFIELD, CPA
9002 Green Oaks Circle, 2nd Floor
Dallas, Texas 75243-7212

ORDER DIRECTING
THE FILING
OF ADDITIONAL BRIEFS

The Division of Enforcement appeals from the decision of an administrative law judge in a proceeding brought pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 and Rule 102(e)(1)(i) and (iii) of the Commission's Rules of Practice.[1] The law judge found, among other things, that S.W. Hatfield, CPA ("the Firm"), a Texas accounting firm, and Scott W. Hatfield, the Firm's sole proprietor (together, "Respondents"), did not violate Exchange Act Section 10(b) with respect to certain audit reports that Respondents allegedly issued while the Firm's state license was expired.[2] This order requests that the parties address (1) the legal theories and facts regarding the "in connection with" requirement under Exchange Act Section 10(b); (2) the implication on the Division's request for sanctions under Exchange Act Section 4C and Rule 102(e) of the disciplinary sanctions imposed on Respondents in a separate disciplinary proceeding after the conclusion of briefing in this matter before the law judge; and (3) the applicability of Rule of Practice 102(e)(1)(i) to Respondents where the Firm's state license had been renewed and was current as of the date of the institution of this proceeding.

I. The "in connection with" requirement under Exchange Act Section 10(b)

A September 6, 2012 Corrected Order Instituting Proceedings ("OIP") alleges that Respondents "issued thirty-eight audit reports that twenty-one issuers included in periodic reports and registration statements filed with the Commission." An appendix attached to the OIP

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1 15 U.S.C. §§ 78d-3, 78u-3; 17 C.F.R. § 201.102(e)(1)(i) and (iii).

2 15 U.S.C. § 78j(b).

identifies, among other things, the dates of each of the thirty-eight reports, and the date on which each report was included as part of a filing with the Commission.

The OIP further alleges that Respondents issued those audit reports between January 31, 2010 and May 19, 2011, a period during which the Firm's state license was expired ("Expired License Period"). The OIP alleges that the following activity occurred during the Expired License Period with respect to the securities of some of the twenty-one issuers:

- Five of the issuers (888 Acquisition Corp., Eight Dragons Co., HPC Acquisitions, Inc., Truewest Corp., and X-Change Corp.) were quoted on the Over-The-Counter Bulletin Board ("OTCBB"), and trading occurred during the Expired License Period for a specified number of days in each issuer's securities; the dates on which the trades occurred are not identified.[3]

- SMSA Kerrville Acquisition Corp. issued restricted, unregistered common stock on December 15, 2010.[4]

- Asia Green Agriculture Corp., f/k/a SMSA Palestine Acquisition Corp. ("SMSA Palestine"), issued shares for 100% of the outstanding common stock of Sino Oriental Agriculture Group Limited "in August 2010," and filed a Form S-1 on September 20, 2010 and subsequent amendments before going effective on July 15, 2011.[5]

- Three of the issuers (Signet International Holdings, Inc., SMSA Crane Acquisition Corp., and SMSA Gainesville Acquisition Corp.) "disclosed issuances" of unregistered, restricted common stock for acquisitions and for services during the Expired License Period.[6]

- X-Change Corp. issued securities to convert or retire outstanding debt and to obtain certain intellectual property rights during the Expired License Period.[7]

In the factual discussion of its motion for summary disposition, the Division reiterates the activity of the five issuers who were quoted on the OTCBB; SMSA Kerrville Acquisition Corp.; the three issuers who "disclosed issuances" of unregistered, restricted common stock; and X-Change Corp.'s issuance of securities. But the Division does not refer to SMSA Palestine. In the argument section of its motion, the Division states that "Respondents' actions were made in connection with the purchase and sale of securities of the 21 issuers for whom they issued audit reports." But, in support of this argument, the Division references only the five issuers whose securities traded on the OTCBB and a sixth issuer, SMSA Kerrville Acquisition Corp. The Division provides no analysis or citation to any authority other than *SEC v. Zandford*,[8] for the

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3 OIP ¶ A.8.

4 OIP ¶ A.9.

5 OIP ¶ A.9.

6 OIP ¶ A.10.

7 *Id*.

8 535 U.S. 813, 819-20 (2002).

proposition that the "in connection with" requirement under Exchange Act Section 10(b) should be read broadly, and *Ames Dep't Stores Inc. Stock Litig.*,[9] for the proposition that the "in connection with" requirement is satisfied if the misrepresentation occurs in periodic reports filed with the Commission.

The Division's reply brief in support of its motion for summary disposition alleges that a "[m]ore-[t]han [s]ufficient" number of misstatements were made in connection with the purchase and sale of securities, citing in support the same six issuers as discussed in the argument section of its motion for summary disposition, and arguing that the "in connection with" requirement was met because "Respondents' fraud 'somehow touche[d] upon' and had 'some nexus' with '*any* securities transaction.' *SEC v. Clark*, 915 F.2d 439, 449 (9th Cir. 1990) (emphasis added)." But the reply brief also argues that the fees earned for all thirty-eight reports issued for the twenty-one issuers are "directly traceable to Respondents' fraud" and should be disgorged. The Division's brief on appeal provides no further clarification of its theory of the "in connection with" element of its fraud charge.

After the Division filed its brief on appeal, the Supreme Court issued its decision in *Chadbourne & Park, LLP v. Troice*,[10] which addresses the scope of the "in connection with" element of Exchange Act Section 10(b) and Rule 10b-5 thereunder in the context of an implied private right of action. For purposes of determining whether the Securities Litigation Uniform Standards Act of 1988 ("SLUSA") forbade the bringing of a state securities class action, the Court determined that, under SLUSA, "[a] fraudulent misrepresentation or omission is not made 'in connection with' such a 'purchase or sale of a covered security' unless it is material to a decision by one or more individuals (other than the fraudster) to buy or to sell a 'covered security.'"[11] The Court clarified that its holding "does *not* limit the Federal Government's authority to prosecute 'frauds like the one here.'"[12] Rather, the Court pointed out that, "despite the Government's and the dissent's hand wringing, neither has been able to point to an example of any prior SEC enforcement action brought during the past 80 years that our holding today would have prevented the SEC from bringing."[13] The parties have not had the opportunity to

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9 991 F.2d 953, 962 (2d Cir. 1993).

10 134 S. Ct. 1058 (Feb. 26, 2014).

11 *Id*. at 1066. SLUSA forbids the bringing of large securities class actions "based upon the statutory or common law of any State" in which the plaintiffs allege "a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security." 15 U.S.C. § 78bb(f)(1). A covered security is one that trades on a national exchange. *Id*. at § 78bb(f)(1)(5)(E). In the underlying case, the plaintiffs alleged that the defendants helped Allen Stanford and his companies implement a Ponzi scheme by misrepresenting that the uncovered securities (certificates of deposit in Stanford International Bank) plaintiffs purchased were backed by highly-marketable and stable covered securities. The district court dismissed the case, concluding that the alleged misrepresentations provided the requisite "connection" to transactions in covered securities.

12 *Chadbourne & Park, LLP*, 134 S. Ct. at 1062 (emphasis in original).

13 *Id*. at 1070.

address any implications of that case on the analysis of the "in connection with" issue in this matter.

For the foregoing reasons, we direct the Division to submit supplemental briefing to:

- Identify specifically the issuers for which the Division argues that Respondents made misstatements "in connection with" the purchase or sale of the issuer's securities.

- For each issuer identified in response to the above, identify specifically: the purchases or sales of securities in connection with which alleged misstatements were made; Respondents' reports in which those alleged misstatements were made and the filing or filings with the Commission in which those alleged misstatements appeared; and when the purchases or sales of securities occurred in relation to when each of the filings were made.

- For each issuer identified in response to the above, explain in what way Respondents' alleged misstatements touch upon and have some nexus with any securities transaction.

- If, in responding to the above, the Division identifies alleged misstatements in fewer than all thirty-eight reports for the twenty-one issuers listed in the appendix to the OIP, explain the basis for the assertion that fees earned for all thirty-eight reports issued for the twenty-one issuers, are "directly traceable to Respondents' fraud" for purposes of assessing disgorgement.

- Address the significance, if any, of the decision in *Chadbourne & Park, LLP v. Troice* on any of the Division's arguments in this case.

II. Exchange Act Section 4C and Commission Rule 102(e)

A. Sanctions under Exchange Act Section 4C and Commission Rule 102(e)

The OIP instituted public administrative and cease-and-desist proceedings to determine whether, among other things, Respondents should be censured or denied, temporarily or permanently, the privilege of appearing or practicing before the Commission as accountants pursuant to Exchange Act Section 4C and Rule 102(e). In the Division's brief in support of its motion for summary disposition, and in a similar statement in its reply brief, the Division states that "Respondents are currently licensed as CPAs who continue to provide attest services to public—and possibly non-public—companies. They therefore pose a continuing threat to the Commission's processes and to the investing public." (citations omitted) Thus, the Division argues, "Respondents should be permanently barred from appearing before the Commission in accordance with Rule 102(e)(1)(i) and (iii)."

The parties completed their briefing before the law judge in March 2013. On July 3, 2013, the Commission issued an adjudicatory opinion regarding an appeal filed by Respondents that challenged disciplinary action taken by the Public Company Accounting Oversight Board

("PCAOB") against Respondents for conduct not at issue in this proceeding.[14] The Commission found that Respondents violated certain PCAOB rules by repeatedly failing to adhere to the PCAOB's interim auditing standards during the audits of two unrelated public companies. The Commission sustained the PCAOB's decision to permanently revoke the firm's registration and permanently bar Hatfield from association with a registered public accounting firm.[15] The Commission concluded that the PCAOB's sanctions were necessary "to protect the integrity of the Commission's processes and encourage more rigorous compliance with auditing standards both by [Respondents] and by other independent auditors."[16] Respondents did not appeal the Commission's decision.

We have stated that "[t]he Commission disciplines professionals pursuant to Rule 102(e) in order to 'protect the integrity of its processes.'"[17] There is a similarity between the purpose and scope of the PCAOB sanctions discussed above and the bar sought by the Division under Exchange Act Section 4C and Rule 102(e). The parties did not have the opportunity to address before the law judge, and have not addressed before the Commission, any implications that the July 3, 2013 Commission decision may have on the analysis of sanctions under Exchange Act Section 4C and Rule 102(e) in this matter. We direct the Division to submit supplemental briefing to explain the extent to which there is overlap, if any, between the PCAOB sanctions and sanctions under Exchange Act Section 4C and Rule 102(e), and whether such additional sanctions are necessary in the public interest in light of the PCAOB sanctions.

B. Applicability of Exchange Act Section 4C(a)(1) and Rule 102(e)(1)(i)

Exchange Act Section 4C(a)(1) and Rule 102(e)(1)(i) provide that the Commission may impose sanctions on any person who is found "not to possess the requisite qualifications to represent others."[18] The OIP alleges that "Respondents do not possess the requisite qualifications to represent others, pursuant to Section 4C(a)(1) and Rule 102(e)(1)(i) of the Commission's Rules of Practice."[19] Similarly, the Division states in its Motion for Summary Disposition that "Respondents do not possess the requisite qualifications to represent others," and, in its brief on appeal, that "Respondents lack the requisite qualifications to represent others." In support of these allegations, the Division points to the lapse in the Firm's state license

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14 *S.W. Hatfield, C.P.A. and Scott W. Hatfield, C.P.A.*, Exchange Act Release No. 69930, 2013 WL 3339647 (July 3, 2013). In the September 10, 2013 initial decision in this matter, the law judge mentioned the fact of the Commission's July 3, 2013 decision.

15 *Id*. at *21.

16 *Id*. at *26.

17 *Michael C. Pattison, CPA*, Exchange Act Release No. 67900, 2012 WL 4320146, at *12 & n.70 (Sept. 20, 2012) (citing *Robert W. Armstrong, III*, Exchange Act Release No. 51920, 2005 WL 1498425, at *11 & n.62 (June 24, 2005) (citation omitted)).

18 15 U.S.C. § 78d-3(a)(1); 17 C.F.R. § 201.102(e)(1)(i).

19 OIP ¶ C.2.

commencing on January 31, 2010. But the Firm's state license was renewed on May 19, 2011 and remained current at the time the Commission issued the OIP.

Moreover, the precedent cited by the Division in its brief on appeal regarding matters brought under Exchange Act Section 4C(a)(1) and Rule 102(e)(1)(i) involved parties who were *not* licensed at the time the Commission issued orders instituting proceedings and imposing remedial sanctions, *i.e.*, settlement orders.[20] Supplemental briefing should address the relevance, for purposes of Exchange Act Section 4C(a)(1) and Rule 102(e)(1)(i), of the fact that a respondent's state license is current when an order instituting proceedings issues.

Accordingly, it is ORDERED that the Division file a supplemental brief addressing all of the above, together with all appropriate citations to relevant facts and authority within fourteen calendar days from the date of service of this order and not exceeding 7,000 words. Respondents may file a reply brief responding to the Division's supplemental brief within fourteen days from the date of service of the Division's supplemental brief and not exceeding 5,000 words.

For the Commission by the Office of the General Counsel, pursuant to delegated authority.

Lynn M. Powalski
Deputy Secretary

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[20] *Alan S. Goldstein*, Exchange Act Release No. 34641, 1994 WL 499304, at *2-3 (Sept. 6, 1994); *Elliot Stumacher*, Exchange Act Release No. 39124, 1997 WL 587063, at *1, *3 (Sept. 24, 1997).