

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934

Release No. 72639 / July 17, 2014

ACCOUNTING AND AUDITING ENFORCEMENT

Release No. 3568 / July 17, 2014

Admin. Proc. File No. 3-14171

In the Matter of

JAMES M. SCHNEIDER, CPA
c/o W. Neil Eggleston
Kirkland & Ellis LLP
655 Fifteenth Street, N.W.
Washington, D.C. 20005

ORDER DENYING MOTION OR,
IN THE ALTERNATIVE,
APPLICATION FOR
MODIFICATION OF
COMMISSION ORDER IMPOSING
REMEDIAL SANCTIONS

James M. Schneider is a certified public accountant and the former chief financial officer of Dell, Inc. Schneider is currently suspended from appearing or practicing before the Commission as an accountant, with the right to apply for reinstatement after five years, pursuant to an order imposing remedial sanctions that we issued on December 22, 2010 under our Rule of Practice 102(e)(3)(i).¹ Schneider now asks the Commission to "clarify" that the order "does not prevent him from serving on the Audit Committee of General Communications, Inc. (GCI), a Commission registrant."

This is Schneider's second request to clarify our Rule 102(e) suspension order. In his first request, Schneider asked us to state that the order did not prohibit him "from accepting non-accountant positions, such as positions on an audit committee or as a non-accountant CFO [chief financial officer]." We denied that request on July 2, 2013. We explained that to grant such relief

¹ *James M. Schneider, CPA*, Securities Exchange Act Rel. No. 63600, 2010 WL 5183935, at *2 (Dec. 22, 2010) (instituting follow-on proceedings pursuant to our Rule of Practice 102(e) based on Schneider's consent to a permanent injunction, disgorgement, and civil penalties in a U.S. district court proceeding); 17 C.F.R. § 201.102(e)(3)(i) (providing that the Commission may suspend from practicing before it any accountant who has been "permanently enjoined by any court of competent jurisdiction" from violating any provision of the Federal securities laws in an action brought by the Commission).

would "exempt entire job titles from our order, regardless of what tasks or responsibilities those positions entailed."² In this second request, Schneider narrows the universe of potential jobs to a specific position (that of GCI audit committee member). But, as explained below, his request suffers from the same flaw as his first: asking for a declaration that his service on an audit committee will not constitute "appearing or practicing before the Commission as an accountant" based on only the title and other broad generalities about the position, rather than the actual conduct that Schneider might perform when serving in that role.³

BACKGROUND

The Commission filed a civil law enforcement action on July 22, 2010 against Dell, Schneider, and certain other Dell executives in the United States District Court for the District of Columbia, charging them with fraud and various reporting and recordkeeping violations. Among other things, the Commission alleged that Schneider, while serving as Dell's CFO, had used a fraudulent accounting scheme to create the false appearance that Dell was consistently meeting Wall Street earnings targets and reducing its operating expenses.⁴ Without admitting or denying the allegations, Schneider consented to a permanent injunction, disgorgement, and civil penalties.⁵ Schneider also consented to our instituting administrative follow-on proceedings against him, pursuant to which Schneider agreed to being "suspended from appearing or practicing before the Commission as an accountant," with a right to reapply after five years, under Rule 102(e).⁶

When the Commission filed its enforcement action in U.S. district court, Schneider was serving as a director and audit committee member at three publicly held companies. Schneider subsequently resigned from two of those companies, but he continued to serve as an audit committee member at GCI. On August 5, 2011, Commission staff notified GCI and Schneider's counsel that, by serving on GCI's audit committee, Schneider was violating the terms of the Commission's Rule 102(e) suspension order. Schneider subsequently resigned from GCI's audit committee.

² *James M. Schneider, CPA*, Exchange Act Rel. No. 69922, 2013 WL 3327751, at *4 (July 2, 2013).

³ On July 11, 2014, Schneider filed a motion for expedited consideration of his latest motion for clarification. Because we are hereby denying Schneider's motion for clarification, Schneider's motion for expedited consideration is moot.

⁴ Schneider was Dell's chief accounting officer from September 1996 to November 2002 and was Dell's CFO from March 2000 to January 2007. The alleged misconduct occurred between 2001 and 2006.

⁵ *SEC v. Dell*, No. Civ. 1:10-cv-01245 (D.D.C. Oct. 13, 2010) (imposing final judgment as to Schneider).

⁶ *Schneider*, 2010 WL 5183935, at *2.

A year after Schneider consented to the suspension order, Schneider filed his first request for clarification, arguing that our order did not preclude him from accepting a position on an audit committee or as a non-accountant CFO. Approximately three months after we denied that request, GCI extended an invitation for Schneider to rejoin its audit committee on the condition that Schneider first obtain an interpretation from the Commission, or a ruling by a court of competent jurisdiction, that the Rule 102(e) suspension order does not prohibit him from serving on the company's audit committee.

On October 25, 2013, Schneider informed Commission staff of GCI's offer to serve on its audit committee and asked Commission staff to approve his acceptance of that position. On January 29, 2014, the Office of the Chief Accountant ("OCA") wrote to Schneider that OCA lacked the authority to approve Schneider's acceptance of a particular position. OCA nevertheless explained that, while it was not in a position to offer legal advice, it remained "willing to provide guidance with respect to any potential positions" that Schneider may be offered. To that end, OCA wrote that it had analyzed the functions Schneider said he would be performing on GCI's audit committee, but concluded that "it is difficult to envision how performance of many of these activities would be consistent with Mr. Schneider's suspension." Schneider subsequently filed the present motion for clarification, asking us to state that the Rule 102(e) suspension order does not prevent him from serving on GCI's audit committee.⁷

ANALYSIS

We suspended Schneider from appearing or practicing before us as an accountant pursuant to our authority under Rule 102. As we explained when denying Schneider's first clarification request, Rule 102 defines "practicing before the Commission" as including but not limited to "[t]he preparation of any statement, opinion or other paper by any . . . accountant . . . filed with the Commission in any registration statement, notification, application, report or other document with the consent of such . . . accountant."⁸ This definition encompasses persons who "participate[d] in the preparation of" financial statements filed with the Commission by, for

⁷ As he did in his first motion, Schneider titles his present motion as a request for "modification" of our order. In his first motion, Schneider expressly represented that, despite the title of that motion, he was not seeking a modification of our order, only a clarification. *See Schneider*, 2013 WL 3327751, at *6 n.50. Schneider does not make a similarly explicit representation here, but the substance of his motion again does not contain a request for modification of our order, only a request for clarification. We therefore do not treat his present motion as a request to modify and thus have not applied our traditional analysis applicable to such modification requests. *See, e.g., Mark S. Parnass*, Exchange Act Rel. No. 65261, 2011 WL 4101087, at *2 (Sept. 2, 2011) (setting forth the standard for reviewing requests to lift or modify administrative bar orders).

⁸ *Schneider*, 2013 WL 3327751, at *4 (quoting 17 C.F.R. § 201.102(f)).

example, 'creat[ing],' 'compil[ing]' or 'edit[ing]' information or data incorporated into those documents and consenting to their incorporation."⁹ We explained:

Nothing in this definition discusses, let alone exempts, specific job titles, such as CFO or audit committee member. This is by design. As we recognized in our release adopting the 1998 amendments to Rule 102(e), the Commission's limited resources mean that the Commission and the investing public must "rely heavily on accountants to assure corporate compliance with federal securities law and disclosure of accurate and reliable financial information." Accountants play "a particularly important role . . . in preparing and certifying the accuracy of financial statements of public companies that are so heavily relied upon by the public in making investment decisions." This process is impaired if incompetent or unethical accountants are permitted to participate in the preparation of financial statements certified and filed with the Commission. . . . These remedial purposes would be undermined if we were to hold that Schneider could avoid the prohibition in our Rule 102(e) order by accepting a position based only on that position's title or on whether non-accountants could accept such a position.¹⁰

Instead, determining whether serving in a particular role violates our order depends on "a 'fact-specific inquiry' into the conduct involved when serving in such a position."¹¹

Because some positions will necessarily "involve duties that increase the likelihood that Schneider could engage in prohibited conduct, including . . . audit committee member," we warned Schneider that, "the more a prospective position is associated with the preparation of a company's financial statements, the more Schneider's acceptance of such a position without prior approval from the Commission would be done 'at his peril.'"¹² To that end, the Division and OCA have represented their willingness to provide Schneider with guidance regarding potential positions, and the Division has further suggested that Schneider might be able to limit his role on GCI's audit committee in such a way that does not conflict with our Rule 102(e) order. Yet Schneider has rejected any such limitation as "fanciful." Schneider contends that "[t]he board, shareholders, and Mr. Schneider's fiduciary duties would not tolerate such a position" and that he is "frankly shocked that the Staff would suggest it."¹³ Instead, Schneider argues that his service

⁹ *Id.* (quoting *SEC v. Brown*, 878 F. Supp. 2d 109, 127 (D.D.C. 2012)).

¹⁰ *Id.* (citations and footnotes omitted) (citing *Robert W. Armstrong, III*, Exchange Act Rel. No. 51920, 2005 WL 1498425, at *11–12 (June 24, 2005) (finding that a controller, who was no longer a certified public accountant at the time of the alleged misconduct, was appearing or practicing before the Commission)).

¹¹ *Id.* (quoting *Brown*, 878 F. Supp. 2d at 127).

¹² *Id.* at *6 (quoting *DiCola v. FDA*, 77 F.3d 504, 509 (D.C. Cir. 1996)).

¹³ Schneider nevertheless proposes some limits to his service on GCI's audit committee by, for instance, promising that he will not "make specific recommendations as to how certain items

on GCI's audit committee is *per se* allowable under the Rule 102(e) suspension order. But, as explained below, such open-ended service on GCI's audit committee could easily lead to appearing or practicing before us as an accountant and is why we cannot grant Schneider the declaratory relief that he seeks.

A. Schneider's proposed oversight of GCI's financial reporting could encompass conduct that violates our Rule 102(e) suspension order.

Schneider argues that his service on GCI's audit committee will fall outside the scope of our Rule 102(e) suspension order because, he claims, his service will involve "mere oversight of," rather than actual "participation in," the preparation of GCI's financial statements. But labeling his proposed service on the committee as "mere oversight" does not mean that his actual service could not involve appearing or practicing before the Commission as an accountant. In fact, a court rejected the use of just such a simplistic dichotomy between accounting and non-accounting functions in *SEC v. Prince*.¹⁴

In *Prince*, the Commission filed a district court action alleging that a barred accountant, Prince, violated a Rule 102(e) bar order by participating in the preparation of a registrant's filings while serving as a company's "Director of Mergers and Acquisitions."¹⁵ In hiring Prince, the company had created safeguards designed to "ensur[e] that Prince would not be involved with the accounting department and the accounting data," including the mandate that Prince "was not allowed to participate in accounting staff meetings and was not allowed to work on preparation of [the company's] financial statements."¹⁶ The court found that, despite these safeguards, Prince had drafted portions of the company's public filings, prepared financial data that was filed with the Commission, and made accounting judgments that affected the numbers that went into the financial statements—conduct the court found fell "well within" the definition of practicing as an accountant.¹⁷

In holding that Prince had violated our Rule 102(e) bar order, the court rejected Prince's argument that "practicing accounting" encompassed only accounting department personnel and executives who have final authority for financial disclosures. The court found that such a

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should be recorded" on the company's financial statements. But this promise appears to conflict with GCI's requirement that its audit committee members evaluate and choose between alternative accounting treatments and is too vague for us to determine with any certainty that Schneider's service on GCI's audit committee will not violate our Rule 102(e) suspension order. *See infra* notes 29–30 and accompanying text (discussing GCI's audit committee charter).

¹⁴ 942 F. Supp. 2d 108 (D.D.C. 2013).

¹⁵ *Id.* at 115.

¹⁶ *Id.* at 114–15.

¹⁷ *Id.* at 150.

"cramped" definition would impermissibly exclude from liability "people who review and decide on accounting treatments, even if those actions affected the data included in the financial statement, unless those people have final authority to implement their suggestions."¹⁸ The court explained that "accounting is not a mechanistic, quantitative endeavor, but instead requires many non-quantitative decisions on which people can reasonably disagree."¹⁹ "Because these non-quantitative decisions may greatly affect what final numbers are included in the financial statements," the court further reasoned, "those who participate in making those decisions are 'creating' and 'compiling' the relevant information, even if they do not have final authority over the exact numbers that are included."²⁰

Schneider attempts to limit *Prince's* holding by pointing to a footnote from that decision, which Schneider claims stands for the proposition that a Rule 102(e) suspension "would likely not apply to 'non-accountant executive officers and directors,' who simply oversee a company's financial reporting."²¹ But the footnote to which Schneider cites addressed only an assertion by Commission staff that "any editorial review" of the financial statements amounted to "practicing accounting."²² The court observed that this definition of practicing accounting "could arguably include non-accountant executive officers and directors, who identified typographical errors or engaged in editorial review of public filings," but concluded that it "need not delve into this challenging question," because there was substantial evidence in the record to find that the defendant had practiced accounting under a narrower definition.²³ And here, Schneider's proposed role on GCI's audit committee, as discussed below, potentially involves far more than the identification of typographical errors in financial statements about which the *Prince* court speculated.²⁴

¹⁸ *Id.* at 147 (citing *Armstrong*, 2005 WL 1498425, at *11–12 (finding that an accountant practiced before the Commission as an accountant by computing figures and providing information incorporated into public filings despite not having final authority over whether that information was included in the company's filings)).

¹⁹ *Id.* at 148.

²⁰ *Id.*

²¹ Quoting *id.* at 148 n.25.

²² *Id.* (emphasis added).

²³ *Id.*

²⁴ Schneider similarly misdescribes a footnote in *SEC v. Brown*, a related decision written by the same judge as part of the same case against *Prince*. (The *Brown* decision considered *Prince's* and another defendant's motions for summary judgment, while the *Prince* decision reflected the judge's ultimate findings of facts and conclusions of law following a bench trial.) According to Schneider, a footnote in *Brown* states that Rule 102(e)-barred accountants are permitted to oversee "financial statements and related disclosures," so long as they do so "as a corporate manager, not as an accountant." Quoting *Brown*, 878 F. Supp. 2d at 126. But, as in *Prince*, the

B. Schneider's claim that he will perform only those functions required by our rules does not foreclose the possibility that his service on GCI's audit committee could still involve conduct that violates our Rule 102(e) suspension order.

Schneider contends that, because our suspension order does not contain a blanket prohibition against his serving on an audit committee, he should be able to serve on an audit committee so long as he performs "only those functions that all public company audit committees are required to perform by applicable SEC regulations."²⁵ This argument mischaracterizes both the nature of our rules governing audit committees and how audit committees actually function. We promulgated our audit committee rules to provide uniform standards for issuers that would help ensure accurate and reliable financial reporting.²⁶ But we did so recognizing that "decisions regarding the execution of the audit committee's oversight responsibilities, as well as decisions regarding the extent of desired involvement by the audit committee, are best *left to the discretion* of the audit committee of the individual issuer in assessing *the issuer's individual circumstances*."²⁷ Therefore, while our rules "remove a certain

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court's footnote in *Brown* stated only that the court need not address an argument made by Commission staff that "those who merely 'review' a financial statement or related disclosure" are appearing or practicing before the Commission as an accountant because the record was "replete with genuine issues of material fact . . . as to whether [the defendant] practiced before the Commission as an accountant." *Id.*

²⁵ Schneider also notes that NASDAQ rules prohibit audit committee members of its listed companies, of which GCI is one, from having "participated in the preparation of the financial statements of the Company or any current subsidiary of the Company." NASDAQ Corporate Governance Rule 5605(c)(2)(A). But NASDAQ's rules involve their own, distinct regulatory regime and therefore do not preclude us from concluding that an audit committee member could be involved in "the preparation of financial statements" for purposes of our Rule 102(e).

²⁶ *Standards Relating to Listed Company Audit Committees*, Exchange Act Rel. No. 47654, 2003 WL 1833875, at *3 (Apr. 9, 2003) (emphasizing that audit committees "play[] a critical role in providing oversight over and serving as a check and balance on a company's financial reporting system").

²⁷ *Id.* at *15 (emphasis added); *see also Strengthening the Commission's Requirements Regarding Auditor Independence*, Exchange Act Rel. No. 47265, 2003 WL 183801, at *42 (Jan. 28, 2003) (stating that, in adopting Rule 2-07 of Regulation S-X, the Commission was "not requiring that [certain discussions involving the audit committee concerning accounting policies] follow a specific form or manner, but we expect, at a minimum, that the discussion of critical accounting estimates and the selection of initial accounting policies will include the reasons why estimates or policies meeting the criteria in the Guidance are or are not considered critical and how current and anticipated future events impact those determinations").

amount of individual control over the corporate governance process," they also "provid[e] great flexibility for implementation."²⁸

For example, GCI's audit committee charter provides some specifics about how the company has chosen to implement our rules, but still leaves significant room for interpretation. Among other things, GCI's charter states that its audit committee "shall review [disagreements between the company and its auditor] in a timely fashion and provide a written determination with supporting argument for it, and the determination of the Audit Committee regarding the Auditor Disagreement shall be final."²⁹ GCI's charter also requires its audit committee to, among other things, "review and assess" the company's financial reporting and controls and the auditor's recommendations. What this language means in practice will depend heavily on the types of issues and disagreements that arise and how the audit committee decides to handle them. But at the very least, it suggests that, by evaluating and choosing between alternative accounting treatments and drafting a final determination "with supporting argument" as to that appropriate accounting treatment, Schneider *could* engage in the type of non-quantitative decisions that would violate our Rule 102(e) suspension order.³⁰

We also note that, as a practical matter, the more difficult or significant the auditing issue, the more the audit committee is likely to rely on members who have accounting expertise—such as Schneider, who is a CPA and the former chief accounting officer of Dell. This is not to predict that Schneider *would* engage in prohibited conduct while serving on GCI's audit committee (which is why we have not specifically precluded him from serving in such a role). But it is why we cannot state with certainty that Schneider *would not* engage in prohibited conduct.³¹ And although this places some of the onus on Schneider to determine whether he can safely serve in a particular role, we noted in our July 2013 order that "'it is not unfair to require that one who deliberately goes perilously close to an area of proscribed conduct shall take the risk that he may cross the line.'"³²

²⁸ *Standards Relating to Listed Company Audit Committees*, 2003 WL 1833875, at *48; *see also id.* at *18 ("Given the variety of listed issuers in the U.S. capital markets, we believe audit committees should be provided with flexibility to develop and utilize procedures appropriate for their circumstances.").

²⁹ GCI's charter defines "Auditor Disagreements" as disagreements regarding financial reporting between the company and its independent certified public accountants.

³⁰ *Cf. Prince*, 942 F. Supp. 2d at 148 (finding that Prince violated a Rule 102(e) bar order and noting that "non-quantitative decisions may greatly affect what final numbers are included in the financial statements").

³¹ *Schneider*, 2013 WL 3327751, at *6.

³² *Id.* (quoting *DiCola*, 77 F.3d at 508). As further support for his claim that he must be allowed to serve on an audit committee, Schneider points to what he describes as a lack of judicial or administrative precedent expressly prohibiting a Rule 102(e)-barred accountant from

C. That non-accountants can serve on GCI's audit committee does not foreclose the possibility that Schneider's service on the committee could involve conduct that violates our Rule 102(e) suspension order.

As he did in his first motion for clarification, Schneider insists that he cannot violate our Rule 102(e) suspension order so long as he serves in a position in which non-accountants can also serve (which is the case with GCI's audit committee). We rejected this argument in our July 2013 order by explaining that persons without an accounting license "often serve as corporate officers, and the integrity of the Commission's processes is threatened when they execute fraudulent schemes by providing falsified financial information just as when licensed accountants engage in this conduct."³³ In fact, our Rule 102(e) suspension order against Schneider stems from the complaint filed in U.S. district court alleging that he engaged in just such a fraudulent accounting scheme while serving in a position, CFO, that he himself recognizes does not require an accounting license.

Schneider now makes the additional argument that, because our suspension order requires him to be current on his CPA license before we will consider his application to resume practicing as an accountant, it "make[s] no sense" that he could violate our Rule 102(e) suspension order by serving in a position in which non-accountants can also serve. We disagree. We promulgated Rule 102(e) to ensure that accountants, on whom we rely so heavily, "perform their tasks diligently and with a reasonable degree of competence."³⁴ One way we can ensure that Schneider maintains such diligence and competence is to require him to be current with his CPA license (one of several remedial requirements in our Rule 102(e) suspension order).³⁵ This requirement is

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serving on such a committee. But, as we have explained, our Rule 102(e) suspension order does not prevent Schneider from serving on an audit committee *per se*. Rather, our order prohibits Schneider from engaging in certain activities while serving in such a role. Moreover, any lack of precedent on this narrow issue likely reflects only that few, if any, individuals have sought to serve in such a role while suspended. A possible reason for this, the Division observes, is that "it is likely obvious to public companies and most individuals who have been suspended that many of the activities required of most audit committees are likely prohibited."

³³ *Id.* at *5 (quoting *Armstrong*, 2005 WL 1498425, at *12); *see also supra* notes 10–11 and accompanying text (discussing how the remedial purposes of Rule 102(e) would be undermined if Schneider could avoid the prohibition in our order by accepting a position based on only the title or on whether non-accountants could accept such a position).

³⁴ *Marrie v. SEC*, 374 F.3d 1196, 1200 (D.C. Cir. 2004) (quoting *Touche Ross & Co. v. SEC*, 609 F.2d 570, 582 (2d Cir. 1979)); *see also Amendment to Rule 102(e) of the Commission's Rules of Practice*, 63 Fed. Reg. 57,164, 57,165 (Oct. 26, 1998) (stating that, because of the Commission's limited resources, it "must rely on the competence and independence of . . . the accountants who prepare . . . financial statements").

³⁵ *See Schneider*, 2010 WL 5183935, at *2–3 (requiring, among other things, that Schneider resolve all other disciplinary issues with the applicable state boards of accountancy and that his

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not intended to define what it means to practice before us as an accountant. Nor, as Schneider claims, is it meant to serve as "an additional weapon in [our] enforcement arsenal."³⁶ Rather, it serves only to further the remedial purpose of Rule 102(e) by ensuring that Schneider "is fit to appear and practice before the Commission."³⁷

D. Our decision not to grant Schneider's requested relief does not violate his due process rights.

Schneider also repeats the due process arguments from his previous motion, claiming that he lacked notice that his service on GCI's audit committee could violate our order and that to interpret our order as barring such service would represent an "abrupt" regulatory change from existing precedent. As we explained when first denying these assertions, our Rule 102(e) suspension order is consistent with well-established precedent and "provides a sufficient standard by which Schneider can judge his ability to accept a particular position."³⁸ Schneider offers no new argument in support of his due process claims other than the assertion, which we rejected above, that not declaring his service on GCI's audit committee to be *per se* permissible under our Rule 102(e) suspension order would amount to a categorical bar on all audit committee service.³⁹

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application for reinstatement "must satisfy the Commission that [Schneider's] work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner").

³⁶ Quoting *Touche Ross*, 609 F.2d at 579.

³⁷ *Id.* (discussing the Commission's intent behind promulgating Rule 2(e), the predecessor to Rule of Practice 102(e)).

³⁸ *Schneider*, 2013 WL 3327751, at *6 (citing *DiCola*, 77 F.3d at 509 (concluding that it was "fanciful for [a debarred person] to say that he can only 'guess' at the meaning of the debarment order; he will usually have a pretty good idea whether a position at a firm that is not itself a drug manufacturer runs afoul of the remedial purpose for which he has been debarred from providing services to a drug house")).

³⁹ *See, e.g., supra* notes 31–32 and accompanying text (noting we are not prohibiting Schneider from serving on GCI's audit committee *per se*).

* * *

Accordingly, IT IS ORDERED that James M. Schneider's motion or, in the alternative, application for modification of the Commission's order imposing remedial sanctions is DENIED.

By the Commission.

Jill M. Peterson
Assistant Secretary