



UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-17950

In the Matter of

David Pruitt, CPA,

Respondent.

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**DIVISION OF ENFORCEMENT'S OPPOSITION TO
RESPONDENT'S MOTION FOR A MORE DEFINITE STATEMENT**

The Division of Enforcement ("Division") respectfully submits this Memorandum of Law in Opposition to Respondent David Pruitt, CPA's ("Pruitt" or "Respondent") Motion for a More Definite Statement ("Motion"), pursuant to the Commission's Rule of Practice 220(d), 17 C.F.R. § 201.220(d). The Division respectfully submits that Respondent's Motion should be denied.

Preliminary Statement

On April 28, 2017, the Commission issued an Order Instituting Proceedings against Pruitt ("OIP"), alleging that he caused L3 Technologies, Inc. (f/k/a L-3 Communications Holdings, Inc.) ("L3") to improperly recognize \$17.9 million in revenue at a subsidiary, the Army Sustainment Division ("ASD"). Pruitt, a highly experienced accountant,¹ served as the Vice President of Finance at ASD (essentially the principal financial officer of ASD). As alleged in detail in the OIP, Pruitt instructed his subordinates to create 69 invoices on unresolved claims with ASD's customer, the U.S. Army, but withhold delivery of those invoices from the Army,

¹ Pruitt is a certified public accountant, certified management accountant, certified government financial manager and certified defense financial manager. (OIP ¶ 4.)

thereby circumventing L3's internal accounting controls concerning recognition of revenue and delivery of invoices to the customer. As further detailed in the OIP, Pruitt took numerous deceitful acts to obfuscate the fact that when he asked that the sham invoices be generated in L3's internal accounting software (in order to trigger the recognition of revenue), he knew the amounts on the invoices had not been agreed to by the Army and that the Army would reject the invoices if they were delivered. As a result of Pruitt's conduct, L3 improperly reported an additional \$17.9 million in revenue in its Form 10-K filed with the Commission as of December 31, 2013, and in its Form 10-Q filed with the Commission as of March 31, 2014. By improperly recognizing an additional \$17.9 million in revenue in fiscal year 2013 and Q1 2014, L3 violated Generally Accepted Accounting Principles ("GAAP").

When the facts came to light after an internal investigation, L3 amended its 2013 Form 10-K and first quarter 2014 Form 10-Q, revising its financials to—among other things—remove the \$17.9 million in overstated revenue associated with the improper invoices. L3 terminated Pruitt in July 2014.

The OIP alleges that Pruitt caused L3's violations of Section 13(b)(2)(A) of the Securities Exchange Act of 1934 ("Exchange Act"), and primarily violated Rule 13b2-1 of the Exchange Act, by causing L3 to maintain inaccurate books, records and accounts that in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company.² The OIP also alleges that Pruitt violated Section 13(b)(5) of the Exchange Act, by knowingly

² On January 11, 2017, the Commission issued a settled order as to L3. *Matter of L3 Technologies, Inc.*, Rel. No. 34-79772 (S.E.C. Jan. 11, 2017). The settled order found that L3 violated Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act by failing to maintain adequate books and records and failing to maintain sufficient internal controls, based in part on Pruitt's misconduct. On April 28, 2017, the Commission issued a settled order as to Mark Wentlent, Pruitt's former immediate supervisor and president of ASD, for causing L3's violation of Section 13(b)(2)(A) of the Exchange Act and violating Rule 13b2-1, based on, among other things, Wentlent's failure to follow up on red flags that should have alerted him that Pruitt was improperly recognizing revenue. *Matter of Mark Wentlent*, Rel. No. 80547, (S.E.C. Apr. 28, 2017).

circumventing a system of internal accounting controls or knowingly falsifying the books, records or accounts of the company.

Respondent's Motion seeks a more definite statement as to:

1. the specific internal controls of [L3] that the Division alleged were violated,³ and
2. the specific books, records, and accounts that were made inaccurate or falsified as a result of Mr. Pruitt's misconduct and the factual and legal basis for concluding they were not maintained with "reasonable detail."

(Motion at 1.) For the reasons set forth herein, Respondent's Motion should be denied in its entirety.

I. LEGAL STANDARD FOR RULE 220(d) MOTIONS

Rule 200(b), which sets forth the pleading requirements for an OIP, requires "a short and plain statement of the matters of fact and law to be determined." Although Rule 220(d) allows for the filing of a motion for a more definite statement when an OIP is alleged to fall short of Rule 200(b), the standard applicable to a motion for a more definite statement is clear: a pleading must only "sufficiently inform[] [a respondent] of the nature of the charges so that he or she may adequately prepare a defense; however, a respondent is not entitled to a disclosure of evidence in advance of the hearing." *Matter of Wolfson*, 103 S.E.C. Docket 1153, 2012 WL 8702983, at *1 (Mar. 28, 2012) (citation omitted); *see also Matter of optionsXpress, Inc.*, Rel. No. 710, S.E.C. Docket 419, 2012 WL 8704501, at *2 (July 11, 2012) (denying motion because the Division met the burden to inform "respondents of the charges against them so they can prepare a defense;" refusing to require Division to disclose evidence or theory of the case). "[O]nce the factual basis of the allegation is sufficiently known by a respondent, any additional information is considered

³ Respondent incorrectly asserts that the Division has charged him with circumventing only one of L3's internal accounting controls. (*Compare* Motion at 1, 2 with OIP at ¶ 44 ("As a result of the conduct described above, Pruitt willfully violated Section 13(b)(5) of the Exchange Act, which prohibits any person from knowingly circumventing or knowingly failing to implement a system of internal accounting controls.") (emphasis added).)

evidence to which a respondent is not entitled prior to hearing.” *Matter of Western Pacific Capital*, 102 S.E.C. Docket 3633, 2012 WL 8700141, *2 (Feb. 7, 2012).

II. RESPONDENT HAS SUFFICIENT INFORMATION ABOUT THE BOOKS AND RECORDS CLAIMS TO PREPARE HIS DEFENSE

The OIP alleges that Respondent caused L3 to violate Section 13(b)(2)(A) of the Exchange Act, which requires certain reporting issuers, including L3, to “make and keep books, records and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer.” 15 U.S.C. § 78m(b)(2)(A). The OIP also alleges that Respondent primarily violated Rule 13b2-1 of the Exchange Act, which states that “[n]o person shall, directly or indirectly, falsify or cause to be falsified, any book, record or account subject to section 13(b)(2)(A) of the Securities Exchange Act.” 17 C.F.R. § 240.13b2-1. The OIP further alleges that Pruitt willfully violated Section 13(b)(5) of the Exchange Act, which, among other things, prohibits a person from “knowingly falsify[ing] any book, record, or account described in [Section 13(b)(2) of the Exchange Act.]” 15 U.S.C. § 78m(b)(5). The phrase “books, records and accounts” has been broadly construed as “any tangible embodiment of information made or kept by an issuer.” *See SEC v. World-Wide Coin Inv.*, 567 F. Supp. 724, 749 (N.D. Ga. 1983) (“Congress’ use of the term ‘records’ suggests that virtually any tangible embodiment of information made or kept by an issuer is within the scope of Section 13(b)(2)(A) ..., such as tape recordings, computer print-outs, and similar representations ... [T]he purpose of this provision is to strengthen the accuracy of records and reliability of audits.”)

The OIP is replete with allegations that identify books, records and accounts that Respondent falsified or caused to be falsified, including: (1) the fictitious invoices generated at Respondent’s direction, (2) emails to L3’s Corporate office and external auditor suggesting, contrary to the truth, that ASD had authority to invoice the Army on unresolved claims, and (3)

improper entries in L3's financial statements. Specifically, the OIP alleges that in December 2013, Respondent instructed a subordinate to recognize revenue on unresolved claims under the contract with the Army (the "C-12 Contract") by creating 69 invoices in L3's internal accounting system ("SAP"), but withhold those invoices from delivery from the Army.⁴ (OIP ¶¶ 2, 20-26.) Pruitt later helped procure a misleading e-mail, suggesting that ASD had authorization to submit invoices to the Army on the unresolved C-12 claims (which was not the case), which was subsequently communicated to L3's corporate headquarters and L3's auditor. (OIP ¶¶ 28-30, 33-36.) Pruitt also drafted two misleading statements to L3's auditor, failing to disclose that ASD had recognized revenue on certain unresolved claims, for which the associated invoices had not been sent to the customer. (OIP ¶¶ 31-32, 37-38.) The 69 invoices that were created at Pruitt's direction were discovered in a billing supervisor's office about six months after they had been created, and were not delivered to the Army. (OIP ¶ 39.)

L3 revised the financial statements disclosed in its Form 10-K for fiscal year 2013, and its Form 10-Q for Q1 2014, based in part on the improper C-12 revenue recognition, essentially admitting that the prior financial statements did not accurately and fairly reflect the transactions or disposition of assets of the company. (OIP ¶¶ 39-42.) These allegations are more than sufficient for Respondent to prepare a defense of the books and records claims.

To the extent the Respondent is asking that the Division identify *each* book, record or account that was allegedly falsified, the Division submits that such a request is beyond the scope of what is required by Rule 200(b). As Respondent acknowledges, L3 is a large issuer, having realized over \$12 billion in net revenue in 2013. (Motion at 1.) In light of the broad definition of "books, records and accounts," and given the myriad computer entries, ledgers and financial

⁴ The generation of an invoice in SAP automatically results in revenue being recognized on ASD's books, which Pruitt knew would be consolidated into L3's financial statements. (OIP ¶ 20.)

statements that a company the size of L3 would have maintained, it is not necessary for the Division to identify each book, record, or account that was falsified as a result of the Respondent's actions. Respondent's Motion for a more definite statement concerning the specific books, records and accounts that were falsified should be denied.

III. RESPONDENT HAS SUFFICIENT INFORMATION ABOUT THE INTERNAL CONTROLS CLAIMS TO PREPARE HIS DEFENSE

The Division's OIP alleges that "[t]he invoices had not been delivered to the U.S. Army, in violation of a specific internal control of L3 that required delivery of invoices." (OIP ¶ 39.) While the Division submits that the OIP is sufficient to apprise Respondent of the basis for the claims, the Division further notes that Pruitt intentionally circumvented the following of L3's Internal Controls Over Financial Reporting (among others): IR4, IR5, and FR4A.⁵

Pruitt has more than sufficient notice of the bases for the internal controls allegations against him. His request for more detail should be denied.

IV. RESPONDENT'S REMAINING ARGUMENTS ARE IRRELAVENT TO THE MOTION FOR A MORE DEFINITE STATEMENT

Respondent argues that in light of the size of the investigative file that has been produced, "the burden should not be on Mr. Pruitt to look for the proverbial needle in the haystack particularly where the additional detail sought is critical to the charges herein and can easily be set forth by the Division." (Motion at 6.) Implicit in that argument is that Respondent is only now—for the first time—being provided an opportunity to review the evidence supporting the allegations in the OIP, without any assistance to identify the key documents upon which the allegations are based. Respondent's argument is irrelevant and misleading.

⁵ Indeed, Pruitt was aware of these controls, as evidenced by the fact that he distributed these controls and associated process narratives (which provide guidance regarding the requirements of certain controls) to a group of L3 employees in an e-mail dated March 30, 2013, with the subject "ASD Leadership Conference."

Respondent was represented by separate counsel during the course of the investigation, but in the fall of 2016, retained Baker & Hostetler LLP upon learning that the Division was preparing to recommend charges against him.⁶ At the request of Respondent's then-new counsel, the Division identified one of the accounting controls—IR 4—that requires that revenue be recognized when invoices are generated and delivered to the customer, provided Respondent's counsel with a complete set of L3's internal controls over financial reporting, and afforded them an unlimited amount of time to review the document. In addition, the Division provided Respondent's counsel access to: (1) transcripts of investigative testimony, (2) the exhibits used during testimony, and (3) other documents that the Division believes implicate Respondent in the conduct set forth in the OIP. The Division even provided a reverse proffer to Respondent, highlighting the allegations and documents that are now summarized in the OIP. Contrary to Respondent's claim that the Division "provides detail only when it perceives a strategic advantage in doing so," (Motion at 5), Respondent has been afforded with virtually unfettered access to many documents in the Division's investigative file even prior to the commencement of this case.

Finally, Respondent argues that in light of the potential sanctions to be imposed on him, he should be afforded additional information upon which to prepare his defense. (Motion at 7.) As with all enforcement actions, this action may pose significant consequences for Respondent. But that argument has no bearing on a motion for a more definite statement. The only question before the Court is whether Respondent has sufficient information upon which to prepare his

⁶ Respondent characterizes this matter as an "almost three-year investigation." (Motion at 3.) The investigation commenced in August 2014, and the Division provided Respondent with a Wells notice in September 2016. Under the statute, the Division has a minimum of six months from the date of Wells notices to institute proceedings. Because Respondent subsequently retained new counsel, the date the proceedings were instituted was slightly delayed.

defense. The Division submits that Respondent has more than sufficient information upon which to prepare his defense. His motion should therefore be denied.

Conclusion

Based on the foregoing, the Division respectfully requests that the Court deny Respondent's motion for a more definite statement.

Dated: June 13, 2017
New York, New York

DIVISION OF ENFORCEMENT

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CERTIFICATE OF SERVICE

I hereby certify that I served the foregoing Notice of Appearance of Counsel by mailing a copy of the same via UPS, and via e-mail, on this 13th day of June, 2017, to Respondent:

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