

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 79368 / November 21, 2016

INVESTMENT ADVISERS ACT OF 1940
Release No. 4572 / November 21, 2016

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3826 / November 21, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17694

In the Matter of

GRASSI & CO., CPAs, P.C.,

Respondent.

**ORDER INSTITUTING PUBLIC
ADMINISTRATIVE AND CEASE-AND-
DESIST PROCEEDINGS PURSUANT TO
SECTION 4C OF THE SECURITIES
EXCHANGE ACT OF 1934, SECTION
203(k) OF THE INVESTMENT
ADVISERS ACT OF 1940 AND RULE
102(e) OF THE COMMISSION’S RULES
OF PRACTICE, MAKING FINDINGS,
AND IMPOSING REMEDIAL
SANCTIONS AND A CEASE-AND-
DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Grassi & Co., CPAs, P.C., (“Grassi” or “Respondent”) pursuant to Section 4C¹ of the Securities Exchange Act of 1934 (“Exchange Act”), Section 203(k) of the Investment Advisers Act of 1940 (“Advisers Act”) and Rule 102(e)(1)(ii) of the Commission’s Rules of Practice.²

¹ Section 4C provides, in relevant part, that:

The Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found . . . (1) not to possess the requisite qualifications to represent others . . . (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations thereunder.

² Rule 102(e)(1)(ii) provides, in pertinent part, that:

The Commission may . . . deny, temporarily or permanently, the privilege of appearing or

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Section 4C of the Securities Exchange Act of 1934, Section 203(k) of the Investment Advisers Act of 1940 and Rule 102(e) of the Commission’s Rules of Practice, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent’s Offer, the Commission finds³ that:

A. SUMMARY

1. Grassi served as independent auditor for several private funds advised by ClearPath Wealth Management, LLC (“ClearPath”) and ClearPath’s principal, Patrick Churchville (“Churchville”) between January 2012 and January 2013. During that time, Grassi issued nine audit reports containing unqualified opinions on the financial statements for four different funds, for years ended 2009 through 2011. From 2010 forward, however, ClearPath and Churchville were defrauding the funds they advised, and the investors in those funds, by misappropriating fund assets and by making repeated misstatements to investors about the value and existence of fund investments. For its part, Grassi repeatedly violated professional standards while failing to heed indications of ClearPath’s and Churchville’s fraud. As a result of its negligence, five of Grassi’s nine audit reports were materially false. This enabled ClearPath and Churchville to continue to report to limited partners materially inflated values of their investments without contradiction, to conceal use of limited partners’ investments for their own benefit, and continue their scheme to defraud the funds and their investors unimpeded. Grassi thereby engaged in improper professional conduct within the meaning of Section 4C(a)(2) of the Exchange Act and Rule 102(e)(1)(ii) of the Commission’s Rules of Practice, and was a cause of ClearPath’s and Churchville’s violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder.

practicing before it . . . to any person who is found . . . to have engaged in unethical or improper professional conduct.

³ The findings herein are made pursuant to Respondent’s Offer and are not binding on any other person or entity in this or any other proceeding.

B. RESPONDENT

2. **Grassi** is a New York domestic professional corporation and is registered with the Public Company Accounting Oversight Board as a public accounting firm with its headquarters in Jericho, New York. Grassi acquired the public accounting firm Pustorino, Puglisi & Co., LLP (“Pustorino”) effective January 1, 2012.

C. OTHER RELEVANT ENTITIES AND INDIVIDUAL

3. **ClearPath** is a Delaware limited liability company (“LLC”) and an investment adviser that was licensed by the State of Rhode Island with its principal place of business in Barrington, Rhode Island. ClearPath was registered with the Commission as an investment adviser beginning January 3, 2008 through November 16, 2012 (SEC File No. 801-68715). ClearPath is the manager of several LLCs that were the general partners of five private funds. ClearPath was also the adviser to these private funds pursuant to management agreements between ClearPath and each of the funds. On May 7, 2015, the Commission filed a civil complaint alleging fraud charges against ClearPath and its owner, Patrick Evans Churchville, in the United States District Court for the District of Rhode Island. *Securities and Exchange Commission v. ClearPath Wealth Management, LLC, Patrick Evans Churchville, as Defendants, and ClearPath Multi-Strategy Fund I, L.P., ClearPath Multi-Strategy Fund II, L.P., ClearPath Multi-Strategy Fund III, L.P., and HCR Value Fund, L.P., as Relief Defendants*, Civil Action No. 15-cv-00191 (D.R.I. May 7, 2015). ClearPath is now run by a court-appointed receiver.

4. **Churchville**, age 47, lives in Barrington, Rhode Island. He is the sole owner and President of ClearPath. On August 4, 2016, Churchville pled guilty to five counts of wire fraud and one count of tax evasion, in criminal charges alleging misconduct also alleged in the Commission’s complaint. *United States of America v. Patrick Churchville*, (CR 16 00068, D. R.I. July 5, 2016).

5. The four private funds managed by ClearPath and Churchville for which Grassi provided audit and tax services were (collectively, the “**Funds**”):

- a. **ClearPath Multi-Strategy Fund I, L.P.** (“MSF I”), formerly known as ClearPath Private Equity Fund, L.P., is a Delaware limited partnership formed in 2008.
- b. **ClearPath Multi-Strategy Fund II, L.P.** (“MSF II”) is a Delaware limited partnership formed in 2011.
- c. **ClearPath Multi-Strategy Fund III, L.P.** (“MSF III”), formerly known as the ClearPath Healthcare Receivables Investments Fund L.P., is a Delaware limited partnership formed in 2009.
- d. **ClearPath Alternative Investments Fund, L.P.** (“CPAI”) was a Delaware limited partnership formed in 2009. As of January 1, 2012, this Fund was merged into MSF I.

D. FACTS

Grassi's Relationship with ClearPath and the Funds

6. ClearPath retained Pustorino on behalf of three of the four Funds as their independent auditor in November 2011 (for MSF I, MSF III and CPAI). When Pustorino merged with Grassi in January 2012, the audit work was transitioned to Grassi. In May 2012, ClearPath retained Grassi for the audit of MSF II. Grassi was engaged to audit the Funds in accordance with U.S. generally accepted auditing standards (“GAAS”) and express an opinion about whether the Funds’ financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles (“GAAP”).⁴ Grassi was also engaged to prepare all required tax returns, including Forms K-1, for the Funds’ partners for the 2011 calendar year.

7. Grassi issued nine audit reports expressing an unqualified opinion on the fair presentation of the financial statements between April 2012 and January 2013 for the Funds. The table below identifies each audit report issued by Grassi including the audit report date.

	MSF I	MSF II	MSF III	CPAI
2009	6/12/2012	Not Audited	4/19/2012	Not Audited
2010	7/2/2012	Not Audited	6/11/2012	4/19/2012
2011	1/29/2013	1/22/2013	1/29/2013	1/26/2013

8. ClearPath sent Grassi’s audit reports to the custodian for the vast majority of the Funds’ limited partner investors.

Grassi's Audit Planning and Fund Structure

9. The Funds’ predecessor auditor sent ClearPath a resignation letter in October 2011 stating it could not complete the audits for MSF I and MSF III for the year ended December 31, 2009 because it had “...not received satisfactory documentation to support significant audit objectives related to certain investment and partner withdrawal transactions.” This letter, which originally was sent to Pustorino, was included in Grassi’s audit workpapers. Citing the reasons for the prior auditor’s resignation, Grassi assessed the audit risk related to the Investments and Equity sections as “significant.” Grassi’s risk assessment prescribed “extended” audit procedures for the Investments area and in the 2011 workpapers required 100% confirmation of partners’ contribution and withdrawal activity in the Equity area.

⁴ References to auditing standards in this Order are to generally accepted auditing standards in effect at the time the audit work was performed. Grassi was engaged to audit the ClearPath Funds in accordance with GAAS promulgated by the Auditing Standards Board (“ASB”) of the American Institute of Certified Public Accountants. The references are to standards as they existed before the ASB’s clarification project, which was effective for audits of financial statements for the years ending on or after December 15, 2012.

10. Grassi’s audit planning documents did not address the risk presented by the Funds’ series structure. The ClearPath Funds were organized as series funds. Each series within each Fund generally invested in one investment (e.g., limited partnership interests, secured debt instruments, or private equity). Limited partners, through their subscription agreements, designated in which specific series they wanted to invest. The Limited Partnership Agreements for each Fund established the series structure and how each series was intended to stand alone:

“The Partnership’s assets shall be divided into separate series...and each Series shall generally be accounted for as a ‘sub-partnership’ for purposes of this Agreement...the interests in any Series shall be considered a separate Series from interests in any other Series...the debts, liabilities and obligations incurred, contracted for or otherwise existing with respect to any one Series shall be enforceable against the assets of such Series only and not against the assets of the Partnership generally or of any other Series.”

11. Despite the fact that the Funds’ governing documents specified that each series must be accounted for as a sub-partnership and that the assets and liabilities of each series could not be commingled with any other series, Grassi did not identify inter-series commingling as an audit risk.⁵

Oppenheimer & Co. Investment (MSF I)

12. One of the series in MSF I was called the Oppenheimer Public Markets series. ClearPath raised approximately \$4.9 million from various limited partners in August 2011 and established a brokerage account at Oppenheimer & Co. (“OPCO”) where the cash was deposited. ClearPath used the cash to purchase short-term U.S. government and agency bonds. As of December 31, 2011, the OPCO account had a balance of \$4.8 million, which represented 23% of total partners’ capital in MSF I.

13. In connection with the MSF I audit for the year ended December 31, 2011, Grassi sent an audit confirmation to OPCO in May 2012 to confirm investment balances as of December 31, 2011 and the transactions for the year then ended. OPCO sent its confirmation response directly to Grassi. In addition to the account in the name of the Fund, which held the bonds, OPCO’s response disclosed that ClearPath and Churchville had also opened a margin account in the same name as the Fund, and an account in the name of MSF I’s general partner. As part of the confirmation response, OPCO also provided monthly account statements for all three accounts for all of 2011. Together, the monthly account statements for the three accounts showed that immediately after depositing investors’ cash with OPCO, ClearPath and Churchville had borrowed against the \$4.9 million investment and withdrawn \$4.1 million of the loan proceeds in wire transfers to ClearPath’s bank account. As alleged in the Commission’s complaint against ClearPath and Churchville, Churchville used \$2.5 million of the margin loan

⁵ ClearPath maintained only one bank account for each Fund, which further elevated the risk of prohibited inter-series commingling.

proceeds to purchase Churchville's personal residence overlooking Narragansett Bay in Barrington, Rhode Island and \$1.6 million of the proceeds to cover-up losses from misappropriation in MSF III as outlined in the following sections.

14. The Grassi junior auditor who obtained the OPCO statements sent an email to the Funds' administrator on July 2, 2012, inquiring about the margin account:

"We received the December 2011 bank statements from Oppenheimer – see attached – there are two accounts, do you know why one has a negative balance of \$4.1 million?"

15. On July 9, 2012, the administrator responded to the Grassi junior auditor that the administrator would have to discuss the issue with ClearPath because:

"I have never seen the statements or the other account with the negative balance. I have to find out what this account is and then I will get back to you about this. **This might change everything for the [OPCO] class.**" (emphasis added)

16. There is no evidence that Grassi completed its discussion with the Funds' administrator, discussed the accounts with its client, or applied any further audit procedures to the previously undisclosed accounts. Grassi's workpapers did not mention the margin account or the material cash withdrawals from the account in favor of ClearPath. Workpapers also did not include the email exchange above or otherwise document Grassi's decision not to include information regarding the margin account in the workpapers.

17. In April 2012, when the sole investment in the account, the U.S. Treasury bonds, matured, OPCO did not allow Churchville to roll over the proceeds to a new investment. Instead, OPCO applied the cash generated from the maturity of the bonds to the outstanding margin account, paying down the loan balance with the redemption proceeds, reducing the value of the OPCO Series to just under \$600,000. In October 2012, ClearPath transferred the remaining cash in the OPCO account to a bank account it did not disclose to Grassi or to the ClearPath Fund administrator in the name of MSF I. All of these transactions occurred after MSF I's December 31, 2011 balance sheet date, but months before Grassi issued its audit report. Grassi auditors did not request or review any OPCO account statements after the balance sheet date.

18. On January 29, 2013, Grassi issued its audit report containing an unqualified audit opinion for MSF I for the year ended December 31, 2011. The audited financial statements reflected a \$4.8 million value for the OPCO investment when the true value, as determined from the information in OPCO's confirmation response to Grassi, was less than \$650,000 at year-end 2011. The footnotes to the audited financial statements made no reference to the existence of the margin account, or the material related party transactions with ClearPath. The audited financial statements were materially misstated as a result. Limited partners in the ClearPath Funds lost \$4.1 million in connection with ClearPath and Churchville's theft of OPCO assets.

Feingold O’Keeffe (MSF I and CPAI)

19. The largest portfolio holding in MSF I (approximately 51% of total partners’ capital), and the only holding in CPAI, as of December 31, 2011, were limited partner interests in the Feingold O’Keeffe Distressed Loan Fund, L.P. (“Feingold O’Keeffe”).

20. In connection with the Funds’ audits for the year ended December 31, 2011, Grassi sent audit confirmations to Feingold O’Keeffe in May 2012 to confirm the capital balances as of December 31, 2011 and the transactions for the year then ended. Feingold O’Keeffe completed the audit confirmations and attached the December 31, 2011 statements of partner’s capital for MSF I and CPAI, the Forms K-1, as well as the audited financial statements for the Feingold O’Keeffe limited partnership.

21. Each of the first three pages of the confirmation response filed in both MSF I and CPAI workpapers included references indicating that the investments were “pledged.” The face of the confirmation form bears a handwritten note stating, “*note > Account is subject to a pledge agreement dated 2011.*” In December 2011, Churchville and ClearPath had secured a \$7 million line of credit from a Massachusetts-based bank by pledging the Feingold O’Keeffe assets held by MSF I and CPAI as collateral. The line of credit agreement also included a personal guarantee of Churchville, and corporate guarantees of ClearPath and the MSF I general partner. By January 9, 2012, ClearPath had borrowed \$3.75 million against the line of credit and used the proceeds to pay for investments, which were not recorded in the books and records of any ClearPath Fund.

22. At the end of 2012, ClearPath and Churchville instructed Feingold O’Keeffe to redeem the MSF I and CPAI investments, and Feingold O’Keeffe’s December 31, 2012 capital account statements reflected the complete redemption. ClearPath used the Feingold O’Keeffe redemption proceeds to pay down the credit line balance in January 2013.

23. Grassi auditors did not inquire of ClearPath, its administrator or Feingold O’Keeffe about the meaning of the “pledged” notification and its effect on the MSF I and CPAI financial statements subject to Grassi’s audit. The financial statements did not reflect that ClearPath had entered into the line of credit as of the end of 2011, and Grassi did not propose an audit disclosure that the audited financial statements disclose that after year end ClearPath had liquidated the Feingold O’Keeffe investment and used the proceeds to pay down the credit line balance. Grassi also did not request or review Feingold O’Keeffe statements after the December 31, 2011 balance sheet date. The audited financial statements did not disclose that ClearPath and Churchville used proceeds due to Feingold O’Keeffe series limited partners for their own purposes, and were therefore materially misstated. Limited partners in the Feingold O’Keeffe series lost \$3.75 million of their investment due to unauthorized borrowing under the undisclosed credit line outlined above.

Managed Futures (MSF III)

24. In December 2010, ClearPath redeemed the MSF III’s largest portfolio holding, referred to as the Managed Futures series. This redemption resulted in a \$6.6 million cash

deposit into the MSF III bank account on December 22, 2010. This transaction initiated a string of conspicuous transfers between MSF III series and between Funds in clear violation of the Funds' offering documents. ClearPath and Churchville attempted to cover up the misconduct by posting unsupported accounting entries. The 2010 audited financial statements for MSF III show that the limited partners' capital accounts were reduced to zero as of December 31, 2010 and the MSF III balance sheet included a Distributions Payable liability balance of approximately \$6.5 million.

25. Instead of distributing all of the Managed Futures proceeds to the applicable limited partners in the series, Churchville transferred approximately \$400,000 of the Managed Futures proceeds to ClearPath to cover administrative expenses. The MSF III limited partnership agreement obligated ClearPath to pay for the Fund's administrative expenses using the management and organization fees that it earned from the Funds, rather than investment proceeds. This transaction was reflected in the 2010 audited financial statements as a receivable Due from Investment Manager.

26. On December 30, 2010, in the last transaction of the year, ClearPath and Churchville used approximately \$1.0 million of the Managed Futures proceeds to make an investment in Drug Discovery Fund I, LLC ("DD1"), but ClearPath did not allocate any equity to limited partners in connection with the DD1 investment. As a result, the 2010 MSF III audited financial statements reflected an error (a \$1 million difference between partners' contributions and the portfolio investments balance for the DD1 series) on their face.

27. In January 2011, ClearPath distributed approximately \$4.9 million of the Managed Futures proceeds to limited partners, reducing the cash balance in MSF III to less than \$400,000. MSF III had a continuing obligation to pay the remaining \$1.6 million of distributions owed to the limited partners in the Managed Futures series. Grassi received and included in its audit workpapers cash activity schedules from ClearPath and its administrator that reflected that the Managed Futures series no longer had assets sufficient to satisfy this debt. These transactions were red flags of ClearPath's and Churchville's improper conduct. Yet Grassi's workpapers did not include evidence regarding how MSF III would be able to fund the remaining \$1.6 million of distributions payable to Managed Futures investors with less than \$400,000 cash and no other assets attributable to the series.

28. In July 2011, ClearPath and Churchville raised approximately \$2.1 million from limited partners to establish a new series in MSF III for a loan to Receivable Partners, LLC ("Receivable Partners"), purportedly to purchase a portfolio of healthcare receivables. However, instead of remitting the capital to Receivable Partners for the new investment ("RP5"), ClearPath and Churchville diverted \$1.6 million of new investors' money to pay off the remaining obligations to the Managed Futures investors.

29. On September 2, 2011, ClearPath and Churchville deposited approximately \$1.6 million into the MSF III bank account in a series of 14 intra-bank transfers all sourced from ClearPath's bank account. ClearPath and Churchville used these deposits, with existing money in the MSF III account, to pay Receivable Partners the \$2.1 million for the RP5 investment from which ClearPath and Churchville misappropriated investor proceeds in July.

30. Had Grassi traced the source of the \$1.6 million deposits into MSF III's account back through the cash activity schedules and confirmation responses already in its possession, Grassi could have discovered that the \$1.6 million was deposited only two days after ClearPath and Churchville transferred \$1.6 million from the OPCO margin account to the same ClearPath bank account. The \$1.6 million was misappropriated from investors in MSF I to cover up losses from ClearPath's and Churchville's misappropriation in MSF III, which was evident from Grassi's workpapers.

31. ClearPath and Churchville posted several unsupported journal entries that masked the misappropriation scheme. Had Grassi followed its own audit program, it could have discovered that the journal entries contained red flags. ClearPath and Churchville had caused four unsupported journal entries to be posted to the MSF III general ledger with effective dates of March, April, May and August 2011 to credit ClearPath with equity ownership in the DD1 series. These entries increased ClearPath's ownership in the series by approximately \$1.2 million but were not tied to contemporaneous cash investments in the series by ClearPath and were not accompanied by any subscription documents evidencing the investment. Since there was no cash received by the Fund for each of these ClearPath "investments," the entries increased the "Due from Investment Manager" receivable balance. By August 2011, the "Due from Investment Manager" account had ballooned to \$1.6 million. ClearPath and Churchville caused the balance of the "Due from Investment Manager" account to be improperly recorded as repaid when ClearPath transferred the \$1.6 million of OPCO money it misappropriated from MSF I to cover the hole ClearPath created in MSF III in September 2011.

32. Grassi's workpapers related to the 2011 audit of MSF III included a detailed schedule of "partner allocations" which showed all contributions, withdrawals and allocations of profit, loss and expenses for each partner's capital account in each series. Grassi's audit plan, developed in part in response to the risks raised by the prior auditor, required Grassi to confirm 100% of partner contribution and withdrawal activity with the partners in the Fund. The Grassi workpapers for the DD1 series showed Grassi traced all capital transactions in the series to confirmations, subscription documents or withdrawal notices *except for* the \$1.2 million in capital contributions ascribed to ClearPath. There were no contemporaneous cash receipts and no corresponding subscription agreements accompanying ClearPath's reported capital contributions to the DD1 series. Related party transactions should receive appropriate scrutiny under GAAS pursuant to AU § 334, but Grassi did not perform sufficient audit procedures on these related party transactions.

33. When ClearPath and Churchville transferred the \$1.6 million of OPCO loan proceeds from MSF I into MSF III on September 2, 2011, the "Due from Investment Manager" receivable account was reduced accordingly. ClearPath never repaid its \$400,000 loan to MSF III and ClearPath was allocated a material investment in the DD1 series without contributing any of its own cash.

34. The 2011 MSF III audited financial statements were materially misstated due to the transactions above because they (a) allocated unsupported equity to ClearPath in the DD1 series, (b) did not reflect a payable due from MSF III to MSF I for the \$1.6 million transferred

from the OPCO series, and (c) did not disclose the existence and nature of a series of unusual and material related party transactions.

Fair Value of Receivable Partners Loans (MSF III and MSF II)

35. In the fair value hierarchy under GAAP, the best evidence of fair value are quoted prices in active markets (Level 1), followed by evidence other than quoted prices that is observable for the asset (Level 2). The least reliable valuations are those based on unobservable inputs reflecting the reporting entity's own assumptions (Level 3). (FASB ASC 820-10-35).⁶

36. A significant portion of the Funds' assets reflected in the financial statements for the year ended December 31, 2011 were valued using methodologies relying on Level 3 inputs. According to the 2011 audited financial statements for MSF III and MSF II, approximately 85% and 49% of the Funds' portfolio investments relied on Level 3 inputs, respectively. The majority of these assets in both Funds were secured loans made to Receivable Partners during 2011, accounting for approximately 62% and 26% of total partners' capital in MSF III and MSF II, respectively.⁷

37. Despite its recognition of the audit risks associated with those assets, Grassi inaccurately documented its planned audit procedures for assets relying on Level 3 inputs, and failed to conduct adequate audit procedures to obtain evidence regarding the value of the largest investments in the MSF II and MSF III Funds.⁸

38. Grassi failed to document its planned audit procedures for the assets relying on Level 3 inputs in MSF III, and as a result, the audit program for the largest ClearPath Fund was devoid of procedures to sufficiently test management's assertion of their fair value as required by GAAS.

39. In workpapers related to the 2011 audit procedures for the fair values of MSF II and MSF III investments based on Level 3 inputs, Grassi's procedures were deficient because Grassi accepted as sufficient appropriate audit evidence the ClearPath-prepared valuation reports without performing substantive procedures on the information contained in the reports. Grassi also failed to recognize errors in those valuation reports that directly affected the reported fair values.⁹ For example, each report included a discounted cash flow model to support the

⁶ Financial Accounting Standards Board (FASB), Accounting Standards Codification (ASC) 820, *Fair Value Measurement*.

⁷ Receivable Partners, LLC had no operational history. It was formed at the same time as MSF III's initial investment in early 2011.

⁸ Grassi's workpapers highlighted the fair value of investments as one of the most significant risks in its audit planning documentation for the 2011 audits of the Funds and reflected the engagement partner's view that the prior auditor had resigned because it was "uncomfortable auditing Level 3 investments."

⁹ ClearPath had retained a valuation consultant to assist it in preparing the valuation reports, but the consultant informed Grassi that it did not perform sufficient work to sign off as the preparer on the reports. ClearPath, not the consultant, prepared the valuation reports for those assets, and the valuation reports do not refer to any involvement by a specialist. Nevertheless, in both the MSF II and MSF III audit workpapers, Grassi prepared a "SAS 73 Memo,"

assertion of fair value. ClearPath's assumptions in each model included estimated future cash flows and discount rates used to determine the present value of the loan. ClearPath's discounted cash flow models included errors in the data and assumptions, but Grassi accepted them without performing appropriate procedures regarding their reasonableness. For example, the discounted cash flow model for the first and largest of the seven Receivable Partners loans in MSF III attributed \$945,000 in fair value to certain interest payments in 2012 that were never made by the time of the audit report issuance in January 2013. The last quarterly interest payment made on the underlying loan occurred 355 days before the date of Grassi's audit report.

40. Grassi was aware that ClearPath had not received the 2012 interest payments for that same loan, but did not propose an adjustment to management's asserted fair value. A November 2012 workpaper titled, "Subsequent Interest Receipts on Loans – 2012," reflected that two payments due in May and August 2012 were not received, yet Grassi concluded that "...the loans are performing as expected." The conclusion that "the loans are performing as expected" applied to six of the seven Receivable Partners loans in MSF III (the seventh loan was not subject to this audit test), but in fact, only the two most recent loans were current when Grassi conducted its testing in August 2012. Each of the other four loans subject to Grassi's testing was behind in its interest payments. Grassi also did not consider the impact of this information on its assessment of the collectability of the subsequent capital and interest payments on the loans.

41. Grassi also performed insufficient procedures to test the existence, valuation, rights, and access to or transferability of the collateral underlying the secured debt investments in the Receivable Partners loans. While ClearPath provided Grassi with UCC filings which were filed months after each loan's origination, these forms only provided the "aggregate face value" of receivables reportedly purchased by Receivable Partners. Grassi's workpapers did not reflect any testing to evaluate the underlying portfolio of the acquired receivables or to verify whether MSF II and MSF III had effective rights to transfer the collateral in the event of Receivable Partners' default.

Subsequent Write-Down of Receivable Partners Loans (MSF III and MSF II)

42. In November 2012, Grassi followed up with ClearPath about the issue of the missed interest payments by Receivable Partners discussed above. Churchville emailed the Grassi engagement partner in December 2012 and explained that ClearPath wrote down the value of the loans upon technical default in September 2012.

43. On January 7, 2013, Churchville emailed three auditors on the engagement team and attached two reports prepared by a third-party consultant ("Consultant") that contained purported collateral files that ClearPath was negotiating to have assigned to it in lieu of payment

pursuant to Statement on Auditing Standards No. 73 ("SAS 73") (subsequently codified as AU § 336 – *Using the Work of a Specialist*) which is intended to document an auditor's use of a specialist's work as audit evidence. While the SAS 73 memo in part asserted that the "specialist's report" could be used for purposes of the audit of the financial statements of MSF II and MSF III and that Grassi intended to rely on the valuation consultant "as specialists," Grassi concluded that it "...did not rely on [the valuation consultant], but merely utilized their assistance in gaining comfort on the loan valuations."

by Receivable Partners. Grassi included the email and attached reports in its workpapers. The reports, totaling more than 1,300 pages, provided data on two pools of healthcare receivables acquired from a hospital group, but they did not identify the date of acquisition nor the acquirer. The reports were last updated in February and March 2011, nearly two years before the Grassi audit report and did not describe any connection between the Consultant and the healthcare receivable portfolios to Receivable Partners. ClearPath provided no evidence, and there is no documentation in Grassi's audit workpapers reflecting that Grassi attempted to verify that the reported collateral related in any way to the ClearPath Funds' investments.¹⁰

44. Grassi's sole inquiry about the collateral report was made to Churchville directly. On January 8, 2013, after a meeting with Grassi's engagement partner and "QC department," the senior manager on the Grassi engagement team emailed Churchville reminding him that Grassi had asked to speak with Receivable Partners in an earlier telephone call, and asking again whether there was "...anyone at [Receivable Partners] who can discuss their analysis of the underlying pool at 12/31/11 and going forward through today?" Churchville, citing "legal negotiations," claimed there was no one at Receivable Partners who would be "forthcoming with any more information until we reach an agreement or they resume payments and make us whole (which they are still claiming they will do ASAP)."

45. A Grassi subsequent events memo dated less than a week later documented Grassi's conclusion that the 2012 write down of the Receivable Partners loan values did not require an adjustment to the numbers included in the 2011 financial statements because there was "no reason to believe the loans were impaired at 12/31/11." The memo did not address the fact that Grassi asked two times to contact Receivable Partners to discuss the status of the healthcare receivables pools, but that Churchville denied this request. The fact that Churchville rebuffed auditors' requests to independently verify the collateral for the largest investments in MSF III should have caused Grassi to undertake more audit procedures. Instead, Grassi accepted all of Churchville's representations and performed no substantive testing procedures to verify the existence, valuation and transferability of the loan collateral or the status of negotiations and likelihood of successful resolution.

46. The audited financial statements disclosed that ClearPath wrote down the fair value of the Receivable Partners loans significantly in 2012. The write downs were \$10.4 million in MSF III and \$18,000 in MSF II and represented 52% and 18%, respectively, of the December 31, 2011 values of the loans reported in the Funds' audited financial statements. Grassi included an explanatory paragraph in its 2011 audit reports issued in January 2013 for both Funds referencing the write down, which Grassi referred to as a significant "impairment." The audited financial statements also included a subsequent events note discussing the issue (excerpt from MSF III's financial statements):

¹⁰ The total face value of the alleged collateral in the Consultant's report was over \$900 million which was more than three times the minimum aggregate face value of the receivables securing the MSF III and MSF II loans according to the UCC filings included in Grassi's workpapers. There is no documentation in Grassi's workpapers that attempts to explain this inconsistency.

“In August of 2012, it was determined by management that the loans made to Receivable Partners, LLC (the ‘Borrower’) became impaired due to the lack of the receipt of scheduled interest payments specified in the loan agreements. Management issued demand letters for those amounts to be paid and is currently in settlement discussion [sic] with the Borrower. For the third quarter of 2012, management has reduced the valuation of these loans significantly. The reduction is approximately 52% or \$10,400,000.”

47. Receivable Partners was a sham organization, founded in early 2011 through the collusive efforts of Churchville and Jonathan E. Rosenberg. The ClearPath Funds had prior investments in healthcare receivables instruments with another Rosenberg entity, JER Receivables, LLC (“JER Receivables”) dating back to 2008. These investments began to deteriorate in 2010 and 2011. In order to mask the collapse of the JER Receivables investments, Churchville and Rosenberg established Receivable Partners in January 2011 for the purpose of “refinancing” the JER Receivables investments. Churchville and ClearPath raised more than \$20 million from new limited partners in MSF III and MSF II for Receivable Partners loans purportedly to finance the purchase of new healthcare receivables portfolios. Instead, with Churchville’s knowledge and direction, Rosenberg transferred the cash from Receivable Partners over to JER Receivables and sent it back to the Funds to close out the prior investments in JER Receivables in MSF I and MSF III. After the JER Receivables investments were closed out, the last several rounds of capital raised for Receivable Partners loans were used to pay “interest” on the earlier Receivable Partners loans. Receivable Partners never used any of the cash raised from MSF III or MSF II investors to purchase any healthcare receivables portfolios. There was never any collateral underlying these investments which were reported with a fair value in excess of \$20 million on the 2011 audited financial statements for MSF III and MSF II.¹¹ Limited partners in the Receivable Partners series in MSF III and MSF II incurred losses in excess of \$16 million.

Supervision Review and Approval Issues

48. Grassi permitted its engagement partner to approve release of the audit reports despite evidence that he had not conducted adequate review as part of his engagement partner responsibilities, and did not comply with firm policy with regard to quality control procedures in other audits. Grassi had a single engagement partner for all nine ClearPath Fund audits, who authorized the release of each of Grassi’s audit reports. Under GAAS, the engagement partner was “the auditor charged with final responsibility for the engagement[s].” With respect to the two audits with the most significant errors, the 2011 audits of MSF I and MSF III, Grassi’s workpapers showed that the engagement partner signed off on only six of the 94 workpapers in the Grassi electronic workpaper binder for the 2011 audit of MSF I and only two of the 134 workpapers in the 2011 MSF III audit.

¹¹ Rosenberg pleaded guilty to conspiracy to commit wire fraud in connection with a complex scheme to defraud investors and lenders by selling fraudulent investment portfolios of debts purportedly owed by hospital patients. *United States v. Shusterman*, *Crim. No. WDQ-13-0460 (U.S. Dist. Ct. D. Md.)*; see also <https://www.justice.gov/usao-md/pr/new-jersey-man-guilty-148-million-investment-fraud-scheme>

49. The engagement partner was on medical leave for significant portions of 2012 while the ClearPath audits were underway, and worked a sharply reduced work schedule from June through October 2012. While the engagement partner was on medical leave and on a reduced work schedule, another Grassi partner took on the work that the engagement partner would typically have done, effectively replacing the engagement partner. The replacement Grassi partner left Grassi effective December 31, 2012.

50. The engagement partner then resumed that role on the ClearPath audits, but did not substantively review workpapers upon the return to the engagement as part of his engagement partner responsibilities before authorizing the release of the audit reports at the end of January 2013.

51. Grassi permitted the engagement partner to continue to work on the ClearPath engagements and to sign audit reports, despite evidence that he did not comply with Grassi's quality control procedures. Grassi's quality control procedures required Grassi to perform an engagement quality control review ("EQCR") on all audit engagements. In January 2013, Grassi senior executives discovered that the engagement partner had permitted the issuance of two non-ClearPath audit reports under the Grassi name without subjecting the audits to EQCR. After learning the engagement partner had circumvented firm policy, Grassi permitted the engagement partner to continue his contact with audit clients, including to solicit payment from ClearPath, and to approve Grassi's release of the 2011 audit reports. On January 24, 2013, the engagement partner reported in an email to Grassi's Chief Administrative Officer that ClearPath had made a "substantial payment" and asked, "...can we take them off credit hold so we can start issuing statements and get paid for the remainder?" On January 29, 2013, Grassi permitted the engagement partner to authorize the issuance of the 2011 reports for MSF I and MSF III. Shortly thereafter, Grassi agreed to the engagement partner's withdrawal from the firm.

52. Grassi also permitted release of two ClearPath Fund audit reports despite failing to obtain certification from the engagement partner that audits were performed in accordance with GAAS. Grassi used an off-the-shelf audit form called the Supervision, Review, and Approval Form ("SRA Form") to document the completion of the detailed review, partner review and EQCR. The SRA Form instructs that "[s]ufficient audit evidence includes evidence that the audit documentation has been reviewed." The SRA Form served as Grassi's prescribed workpaper "to assist in performing and documenting the review" and to record that the audit work "...was conducted in accordance with generally accepted auditing standards and applicable regulatory and legal requirements." According to the engagement partner, the SRA Form was "the final evidence of signing off...on the financial statements."

53. The SRA Forms for the 2011 audits of MSF I and MSF III financial statements did not accurately reflect which partner had completed the review to comply with GAAS at the time that the audit report was issued. The electronic audit trail for the SRA Form for MSF I and MSF III also does not reflect that the engagement partner signed off on the release of the two audit reports.

54. Grassi had a practice of obtaining email authorization from the members of the engagement team before releasing the audit reports, referred to as the "good to go" or "GTG"

email. Grassi permitted the engagement partner to approve the MSF III audit report merely by responding to the “GTG” email inquiry.

55. The SRA Forms for those audits were inaccurate and incomplete at the time Grassi permitted the release of the 2011 MSF I and MSF III audit reports and as a result the workpapers did not properly document the reviewers’ certifications that the audits were performed in accordance with GAAS.

**Grassi’s Improper Professional Conduct –
Violations of General, Planning and Supervision Standards**

56. Grassi’s audit for the 2010 financial statements of MSF III and its audits for the 2011 financial statements for MSF I, MSF II, MSF III and CPAI were deficient and not performed in accordance with GAAS. Section 4C(b) and Rule 102(e)(1)(iv) define improper professional conduct with respect to persons licensed to practice as accountants. “Improper professional conduct” includes two types of negligent conduct: (1) a single instance of highly unreasonable conduct that results in a violation of professional standards in circumstances in which an accountant knows, or should know, that heightened scrutiny is warranted; or (2) repeated instances of unreasonable conduct, each resulting in violations of professional standards, that indicate a lack of competence.

57. As set forth above, Grassi should have known that the five sets of financial statements accompanying the audit reports were materially misstated, yet Grassi issued audit reports containing an unqualified opinion on each. Grassi reported that the audits were conducted in accordance with GAAS when they were not. Grassi also reported that the financial statements were fairly presented in all material respects in accordance with GAAP when they were not. The five false audit reports and the associated accounting and disclosure errors included, but were not limited to:

Fund	Audit Year	Material Errors and Omissions in Financial Statements
MSF III	2010	<ul style="list-style-type: none"> • Material discrepancy between the investment and capital balances in the DD1 series • Lack of disclosure regarding the misappropriation of Managed Futures series’ redemption proceeds • Lack of disclosure regarding the source of funding for the Managed Futures distributions paid in 2011 including prohibited inter-fund transfers
MSF I CPAI	2011	<ul style="list-style-type: none"> • MSF I financial statements materially overstate the fair value of the OPCO investment by \$4.1 million • MSF I and CPAI financials lack disclosure relating to the pledge agreement encumbering the largest asset in both Funds, Feingold O’Keeffe • MSF I and CPAI financial statements lack disclosures regarding material subsequent events, including the complete

Fund	Audit Year	Material Errors and Omissions in Financial Statements
		redemptions of the OPCO and Feingold O’Keeffe series <ul style="list-style-type: none"> • MSF I and CPAI financials lack disclosures related to material related party transactions with ClearPath including the transfers of OPCO proceeds, and the Churchville and ClearPath personal and corporate guarantees
MSF III MSF II	2011	<ul style="list-style-type: none"> • MSF III financials fail to disclose inter-series and inter-fund commingling and material related party transactions involving the Managed Futures / DD1 / RP5 series • MSF II and MSF III financials materially overstate the value of investments in Receivable Partners loans by more than \$20 million

Failure to Exercise Due Professional Care and Professional Skepticism (AU §§ 230, 316)

58. GAAS requires auditors to exercise due professional care in the performance of the audit. (AU § 230.01). Auditors must maintain an attitude of professional skepticism, which includes a questioning mind and a critical assessment of audit evidence. (AU § 230.07). Auditors should consider the competency and sufficiency of the evidence and exercise professional skepticism throughout the audit process. (AU § 230.08). An auditor should not be satisfied with less than persuasive evidence because of a belief that management is honest (AU §§ 230.09 and 316.13), and should: (1) perform an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred; and (2) conduct the engagement with a mindset that recognizes that a material misstatement due to fraud could be present, regardless of past experience with the entity and the auditors’ belief about management’s honesty and integrity. (AU § 316.13).

59. As a result of Grassi’s conduct described throughout, Grassi failed to exercise due professional care and professional skepticism in its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II, MSF III and CPAI.

Failure to Properly Plan the Audit (AU § 311)

60. GAAS requires the auditor to adequately plan the work and properly supervise any assistants. (AU § 311.01). Audit planning involves developing an overall audit strategy for the expected conduct, organization and staffing of the audit. (AU § 311.02). The overall audit strategy should consider areas of higher risks of material misstatement and determine which resources should be assigned to the audit and how the resources are to be managed, directed and supervised. (AU § 311.14-15). Once the audit strategy has been established, the auditor should develop a more detailed audit plan to achieve the audit objectives. (AU § 311.17). The audit plan should include a description of the nature, timing and extent of planned risk assessment procedures sufficient to assess the risks of material misstatement and further procedures at the relevant assertion level for each material class of transactions, account balance and disclosure

and any other audit procedures in order to comply with GAAS. (AU § 311.21). Planning is not a discrete phase of the audit, but rather an iterative process. If, as a result of performing planned audit procedures, the auditor obtains disconfirming evidence, the auditor may need to revise the overall audit strategy. (AU § 311.03).

61. Grassi failed to include audit procedures whose nature, timing and extent were appropriately responsive to the risk presented by the Funds' series structure, and thereby failed to note ClearPath and Churchville's many inter-series and inter-fund transactions undertaken in violation of fund governing documents. Grassi also failed to plan appropriate procedures to audit the valuation of Level 3 investments for MSF III. Grassi also failed to amend its audit plan and execution in light of the audit evidence that was either insufficient or contradicted management's assertions in the Funds' financial statements. As a result, Grassi failed to properly plan its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II and MSF III.

Failure to Properly Supervise the Engagement Team (AU § 311)

62. GAAS requires the auditor with final responsibility for the audit to properly supervise the audit assistants, including firm personnel other the engagement partner. (AU § 311.01). Supervision involves directing the efforts of assistants who are involved in accomplishing the objectives of the audit and determining whether those objectives were accomplished. (AU § 311.28). The auditor with final responsibility for the audit should communicate with members of the audit team regarding the susceptibility of the entity's financial statements to material misstatement due to error or fraud, with special emphasis on fraud. (AU § 311.29). The auditor with final responsibility for the audit should direct assistants to bring to his or her attention accounting and auditing issues raised during the audit that the assistant believes are of significance to the financial statements or auditor's report so the auditor with final responsibility may assess their significance. (AU § 311.30). The work performed by each assistant, including the audit documentation, should be reviewed to determine whether it was adequately performed and documented and to evaluate the results, relative to the conclusions to be presented in the auditor's report. (AU § 311.31).

63. As a result of Grassi's conduct described above, including among other things the fact that Grassi permitted audit reports to be issued even though the engagement partner had not, as part of his engagement partner responsibilities, adequately reviewed the audit team's work to determine whether it had been sufficiently performed and documented, Grassi failed to properly supervise the engagement team in its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II, MSF III and CPAI.

Failure to Obtain Sufficient Appropriate Audit Evidence (AU § 326)

64. GAAS requires auditors to obtain sufficient appropriate audit evidence to provide a reasonable basis for an opinion with respect to the financial statements under audit. (AU §§ 326.01, 326.06). To obtain reasonable assurance, the auditor must not be satisfied with audit evidence that is less than persuasive. (AU § 326.13). In general, audit evidence is more reliable when it is obtained from knowledgeable independent sources outside the entity, when it is obtained directly by the auditor, or when it exists in documentary form. (AU § 326.08). When audit evidence obtained from one source is inconsistent with that obtained from another, the

auditor should determine what additional audit procedures are necessary to resolve the inconsistency. (AU § 326.11).

65. Among other things, Grassi failed to obtain sufficient appropriate audit evidence of purported investments by ClearPath, and of the value of the Receivable Partners loans, and failed to consider discrepancies between the audit evidence obtained and ClearPath's records of value concerning the OPCO and other investments. As a result, Grassi failed to obtain sufficient appropriate audit evidence for its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II, MSF III and CPAI.

Failure to Properly Document the Audit (AU § 339)

66. GAAS requires auditors to prepare audit documentation in connection with each engagement in sufficient detail to provide a clear understanding of the work performed (including the nature, timing, extent, and results of audit procedures performed), the audit evidence obtained and its source, and the conclusions reached. (AU § 339.03). The auditor should prepare audit documentation that enables an experienced auditor, having no previous connection to the audit, to understand, among others, the results of the audit procedures performed and the audit evidence obtained, and the conclusions reached on significant matters. (AU § 339.10). The auditor should document significant findings or issues, actions taken to address them (including any additional evidence obtained), and the basis for the final conclusions reached. Judging the significance of a finding or issue requires an objective analysis of the facts and circumstances. Significant findings or issues include, but are not limited to, circumstances that cause the auditor significant difficulty in applying auditing procedures the auditor considered necessary, for example, the lack of responsiveness to confirmation or information requests, or the lack of original documents. (AU § 339.14). The auditor should document discussions of significant findings or issues with management and others on a timely basis, including responses. The audit documentation should include documentation of the significant findings or issues discussed, and when and with whom the discussions took place. (AU § 339.15). If the auditor has identified information that contradicts or is inconsistent with the auditor's final conclusions regarding a significant finding or issue, the auditor should document how the auditor addressed the contradiction or inconsistency in forming the conclusion. (AU § 339.16). In documenting the nature, timing, and extent of audit procedures performed, the auditor should record who performed the audit work and the date such work was completed, and who reviewed specific audit documentation and the date of such review. (AU § 339.18).

67. Among other things, Grassi failed to adequately document the audit procedures performed and evidence obtained to audit the valuation and existence of certain investments as of the date the audit reports were issued. Grassi did not document such audit procedures for the OPCO, Feingold O'Keeffe and Receivable Partners investments. Grassi also failed to adequately document discussions of certain significant findings or issues, including subsequent events, with management and its conclusions on the issues in accordance with the auditing standards referenced above. As a result of Grassi's conduct described above, Grassi failed to prepare sufficient audit documentation in support of its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II, MSF III and CPAI.

**Grassi's Improper Professional Conduct –
Specific Violations of Fieldwork and Reporting Standards**

Subsequent Events (AU § 560)

68. Subsequent events are events or transactions that occur after the balance-sheet date, but before the issuance of the financial statements that have a material effect on the financial statements and therefore require adjustment or disclosure in the statements. (AU § 560.01). Type 2¹² subsequent events provide evidence with respect to conditions that did not exist at the date of the balance sheet being reported on but arose after that date. These events should not result in adjustment of the financial statements. Some of these events, however, may be of such a nature that disclosure of them is required to keep the financial statements from being misleading. (AU §560.05). Occasionally, a Type 2 subsequent event has such a material impact on the entity that the auditor may wish to include in his report an explanatory paragraph directing the reader's attention to the event and its effects. (AU § 560.09).

69. GAAS requires auditors to perform procedures with respect to the period after the balance-sheet date for the purpose of ascertaining the occurrence of subsequent events that may require adjustment or disclosure essential to a fair presentation of the financial statements in conformity with generally accepted accounting principles. These procedures should be performed at or near the date of the auditor's report. (AU § 560.12).

70. Grassi's audit program to address the GAAS requirements for subsequent events included the following procedures:

- a. Read the accounting records subsequent to year end to the date of the auditor's report for evidence of significant transactions related to the financial statements under audit.
- b. Read any financial statements or significant financial reports that have been prepared since the balance-sheet date.
- c. Inquire of management about the existence of material subsequent events. Inquire about the status of items unresolved at the balance-sheet date.

71. The 2010 audit report for MSF III was issued in June 2012 – 18 months after the balance sheet date. The 2011 audit reports for MSF I, MSF II, MSF III and CPAI were issued in January 2013 – 13 months after the balance sheet dates. Grassi had the obligation under GAAS to review subsequent events through a period “at or near the date of the auditor’s report.” Grassi auditors testified generally that auditors should have looked at the periodic statements for the portfolio investments up to the date of the audit report as part of the subsequent events review. Instead, in the ClearPath audits and in general practice, Grassi simply relied upon management’s representations about subsequent events and did not request or review accounting records through the date of the audit report.

¹²Type 1 subsequent events are events that provide additional evidence with respect to conditions that existed at the date of the balance sheet and affect the estimates inherent in the process of preparing financial statements. The financial statements should be adjusted for any changes in estimates resulting from the use of such evidence. (AU § 560.03).

72. Several of the material accounting errors outlined in the preceding sections could have been further highlighted through a GAAS-compliant subsequent events review, but Grassi failed to execute its own audit plan. For example:

OPCO (MSF I, 2011)	Grassi did not request or review any OPCO brokerage statements after December 31, 2011. If Grassi had reviewed OPCO statements as early as April 2012, Grassi would have seen the effect of OPCO’s margin call. Statements on or after October 2012 showed that the remaining balance in the series was completely liquidated.
Feingold O’Keeffe (MSF I and CPAI, 2011)	Grassi did not request or review Feingold O’Keeffe statements of partner’s capital accounts after December 31, 2011. Feingold O’Keeffe’s December 31, 2012 statements reflected the full redemption of the MSF I and CPAI series in excess of \$10 million. Further, upon reasonable inquiry, if Grassi followed up on the “pledge agreement” referred to on the Feingold O’Keeffe confirmation, Grassi could have discovered ClearPath’s borrowing against the credit line within nine days of the 2011 balance sheet date and the existence of a previously undisclosed bank account.
Receivable Partners (MSF II and MSF III, 2011)	Grassi failed to properly consider whether Receivable Partners’ default on interest payments in 2012 should have resulted in an adjustment to the fair value of the assets at December 31, 2011.
Managed Futures (MSF III, 2010)	Grassi did not properly evaluate how the largest liability on the 2010 financial statements, the Distributions Payable balance of \$6.5 million related to the Managed Futures series, was settled during 2011 after the assets in the series were fraudulently dissipated.

73. As a result of Grassi’s conduct described above, Grassi failed to comply with GAAS requirements for subsequent events testing in its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II, MSF III and CPAI.

The Confirmation Process (AU § 330)

74. Confirmation is undertaken to obtain evidence from third parties about financial statement assertions made by management. AU § 326 – *Audit Evidence*, states that, in general, it is presumed that “audit evidence is more reliable when it is obtained from knowledgeable independent sources outside the entity.” (AU § 330.06). The auditor should evaluate the combined audit evidence provided by the confirmations and the alternative procedures to determine whether sufficient audit evidence has been obtained about all the applicable financial

statement assertions. In performing that evaluation, the auditor should consider (a) the reliability of the confirmations and alternative procedures; (b) the nature of any exceptions, including the implications, both quantitative and qualitative, of those exceptions; (c) the audit evidence provided by other procedures; and (d) whether additional audit evidence is needed. If the combined audit evidence provided by the confirmations, alternative procedures, and other procedures is not sufficient, the auditor should request additional confirmations or extend other tests, such as tests of details or analytical procedures. (AU § 330.33).

75. As described above, among other things, Grassi failed to obtain confirmation or other audit evidence of the purported investments by ClearPath, and also, failed to adequately evaluate the OPCO confirmation and obtain additional audit evidence based on that confirmation. As a result, Grassi failed to comply with GAAS requirements for the confirmation process in its 2011 audits of MSF I and CPAI.

*Auditing Fair Value Measurements and Disclosures and
Using the Work of a Specialist (AU §§ 328, 336)*

76. GAAS requires auditors to obtain sufficient appropriate audit evidence to provide reasonable assurance that fair value measurements and disclosures are in conformity with GAAP. (AU § 328.03). Fair value measurements for which observable market prices are not available are inherently imprecise. That is because, among other things, those fair value measurements may be based on assumptions about future conditions, transactions, or events whose outcome is uncertain and will therefore be subject to change over time. The auditor's consideration of such assumptions is based on information available to the auditor at the time of the audit. (AU § 328.05).

77. When there are no observable market prices and the entity estimates fair value using a valuation method, the auditor should evaluate whether the entity's method of measurement is appropriate in the circumstances. That evaluation requires the use of professional judgment. It also involves obtaining an understanding of management's rationale for selecting a particular method by discussing with management its reasons for selecting the valuation method. The auditor considers whether:

- a. Management has sufficiently evaluated and appropriately applied the criteria, if any, provided by GAAP to support the selected method.
- b. The valuation method is appropriate in the circumstances given the nature of the item being valued.
- c. The valuation method is appropriate in relation to the business, industry, and environment in which the entity operates. (AU § 328.18).

78. Based on the auditor's assessment of the risk of material misstatement, the auditor should test the entity's fair value measurements and disclosures by performing audit procedures that may involve (a) testing management's significant assumptions, the valuation model, and the underlying data, (b) developing independent fair value estimates for corroborative purposes, or (c) reviewing subsequent events and transactions. (AU § 328.23).

79. Collateral often is assigned for certain types of investments in debt instruments that either are required to be measured at fair value or are evaluated for possible impairment. If

the collateral is an important factor in measuring the fair value of the investment or evaluating its carrying amount, the auditor obtains sufficient appropriate audit evidence regarding the existence, value, rights, and access to or transferability of such collateral, including consideration of whether all appropriate liens have been filed, and considers whether appropriate disclosures about the collateral have been made. (AU § 328.25).

80. The auditor's understanding of the reliability of the process used by management to determine fair value is an important element in support of the resulting amounts and therefore affects the nature, timing, and extent of audit procedures. When testing the entity's fair value measurements and disclosures, the auditor evaluates whether:

- a. Management's assumptions are reasonable and reflect, or are not inconsistent with, market information,
- b. The fair value measurement was determined using an appropriate model, if applicable.
- c. Management used relevant information that was reasonably available at the time. (AU § 328.26).

81. During the audit ... an auditor may encounter complex or subjective matters potentially material to the financial statements. Such matters may require special skill or knowledge and in the auditor's judgment require using the work of a specialist to obtain appropriate audit evidence. (AU § 336.06). 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, among others:

- 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. (AU § 336.09).

82. If the auditor determines that the specialist's findings support the related assertions in the financial statements, he or she reasonably may conclude that sufficient appropriate audit evidence has been obtained. (AU § 336.13).

83. As outlined in the section above regarding the fair value of the Receivable Partners loans in MSF II and MSF III, ClearPath engaged a valuation firm to assist management in the year-end valuation of the loans made to Receivable Partners which were all assets valued using Level 3 inputs. There was no documentation provided by the valuation firm that would allow Grassi to obtain an understanding of the nature of the work performed by the valuation firm and its effect on the further audit procedures, as required by AU § 336.09. Furthermore, Grassi audit documentation noted that the valuation firm did not perform sufficient work that would allow Grassi to use the valuation firm's findings as audit evidence. Instead, Grassi accepted the ClearPath-prepared valuation reports without evaluating the appropriateness of management's valuation method and model, evaluating the reasonableness of management's

assumptions in the model, or testing the reliability of the information used in the preparation of the model.

84. Further, AU § 328 provides guidance for evaluating fair value assertions of secured debt instruments similar to the Receivable Partners loans. Grassi failed to design or execute audit procedures to properly test the existence, valuation and transferability of the underlying collateral.

85. As a result of Grassi's conduct described above, Grassi failed to comply with GAAS requirements in connection with testing management's fair value assertions in its 2011 audits of MSF II and MSF III.

Consideration of Fraud in a Financial Statement Audit (AU § 316)

86. GAAS requires auditors to design procedures to test the appropriateness of journal entries recorded in the general ledger and other adjustments (for example, entries posted directly to financial statement drafts) made in the preparation of the financial statements. More specifically, the auditor should:

- a. Obtain an understanding of the entity's financial reporting process and the controls over journal entries and other adjustments.
- b. Identify and select journal entries and other adjustments for testing.
- c. Determine the timing of the testing.
- d. Inquire of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments. (AU § 316.58).

87. As noted in the Managed Futures section above, ClearPath and Churchville caused a series of journal entries to be posted to the MSF III general ledger during 2011 which created and subsequently increased ClearPath's equity position in the DD1 series with no contemporaneous cash contribution by ClearPath to MSF III. These journal entries were manual, non-standard, round dollar and material entries representing unusual transactions that affected a related party account – exactly the types of journal entries that should have been flagged for review in AU § 316 journal entry testing.

88. The audit workpapers for each of the Grassi audits included an identical memo co-authored by the Grassi manager and junior auditor purportedly documenting Grassi's procedures related to journal entry testing performed in satisfaction of GAAS requirements under AU § 316. Other than the title of each three-page memo which was changed to reflect the specific Fund and the applicable year, the memo does not include references specific to ClearPath or its personnel, the fund administrator or its personnel, the accounting system used, the general ledger or journal entry reports requested or reviewed, the entries selected for testing, or the results of Grassi's testing. In fact, there is no evidence in Grassi's workpapers or otherwise that Grassi ever requested or reviewed the Funds' general ledgers or specific journal entries. The memo claimed that Grassi reviewed the journal entries and focused on entries that were "nonstandard," "large and unusual," "processed outside the normal course of business," and "[contained] round numbers or a consistent ending number," but there is no evidence that Grassi conducted that review. At the same time, all of the journal entries resulting in ClearPath's

unsupported allocation of equity in the DD1 series fit the testing criteria outlined in Grassi's memo, but those entries evidently were not subjected to testing.

89. The Grassi journal entry testing memo includes the following unsupported statements:

- a. There were no instances of non-standard journal entries other than topside or adjusting journal entries,
- b. Grassi scanned the general ledger and noted no activity other than normal purchases and sales of investments and or expenses paid,
- c. Entries appear to be for transactions in connection to the ordinary course of business, i.e.: investment purchases, income/expense accruals.
- d. There were no material unusual journal entries found, and
- e. Based upon procedures performed above, Grassi auditor was satisfied that all material journal entries described above were recorded properly.

90. During the course of the audit, the auditor may become aware of significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment. The auditor should gain an understanding of the business rationale for such transactions and whether that rationale (or the lack thereof) suggests that the transactions may have been entered into to engage in fraudulent financial reporting or conceal misappropriation of assets. (AU § 316.66).

91. In understanding the business rationale for the transactions, the auditor should consider, among others:

- Whether the form of such transactions is overly complex (for example, involves multiple entities within a consolidated group or unrelated third parties).
- Whether management is placing more emphasis on the need for a particular accounting treatment than on the underlying economics of the transaction. (AU § 316.67).

92. In addition to the required journal entry testing, GAAS requires auditors to consider conditions identified during fieldwork that change or support a judgment regarding the assessment of the risks of material misstatement due to fraud, including, among others:

- a. Discrepancies in the accounting records, including unsupported or unauthorized balances or transactions
- b. Conflicting or missing audit evidence, including missing documents, significant unexplained items on reconciliations, or unusual discrepancies between the entity's records and confirmation replies
- c. Problematic or unusual relationships between the auditor and management, including denial of access to records, facilities, certain employees, customers, vendors, or others from whom audit evidence might be sought. (AU § 316.68).

93. Grassi failed to update its risk assessment and audit plans to address fraud indicators including, but not limited to: (a) undisclosed accounts, (b) prohibited and undisclosed borrowing against Fund assets, (c) unusual discrepancies in confirmation responses, (d)

unsupported and unusual journal entries, and (e) the scope limitation related to Grassi's request to contact Receivable Partners.

94. As a result of Grassi's conduct described above, Grassi failed to properly consider fraud risk factors in violation of GAAS in its 2010 audit of MSF III and its 2011 audits of MSF I, MSF II, MSF III and CPAI.

Related Parties (AU § 334)

95. GAAS specifies that auditors should be aware of the possible existence of material related party transactions that could affect the financial statements and of common ownership or management control relationships for which FASB ASC 850-10-50 requires disclosure.¹³ (AU § 334.04). The auditor should place emphasis on testing material transactions with parties the auditor knows are related to the reporting entity. (AU § 334.07).

96. After identifying related party transactions, the auditor should apply the procedures the auditor considers necessary to obtain satisfaction concerning the purpose, nature, and extent of these transactions and their effect on the financial statements. The procedures should be directed toward obtaining and evaluating sufficient appropriate audit evidence and should extend beyond inquiry of management. Procedures that should be considered include the following, among others:

- a. Obtain an understanding of the business purpose of the transaction.
- b. Examine pertinent documents.
- c. Test for reasonableness the compilation of amounts to be disclosed, or considered for disclosure, in the financial statements.
- d. Inspect or confirm and obtain satisfaction concerning the transferability and value of collateral. (AU § 334.09).

97. When necessary to fully understand a particular transaction, the following procedures, which might not otherwise be deemed necessary to comply with generally accepted auditing standards, should be considered, among others:

- a. Confirm transaction amount and terms, including guarantees and other significant data, with the other party or parties to the transaction.
- b. Inspect evidence in possession of the other party or parties to the transaction.
- c. Confirm or discuss significant information with intermediaries, such as banks, guarantors, agents, or attorneys, to obtain a better understanding of the transaction. (AU § 334.10).

98. For each material related party transaction (or aggregation of similar transactions) or common ownership or management control relationship for which FASB ASC 850-10-50 requires disclosure,¹⁴ the auditor should consider whether he has obtained sufficient appropriate

¹³ FASB ASC 850, *Related Party Disclosures*.

¹⁴ FASB ASC 850-10-50 requires disclosure "of material related party transactions, other than compensation arrangements, expense allowances, and other similar items in the ordinary course of business."

audit evidence to understand the relationship of the parties and, for related party transactions, the effects of the transaction on the financial statements. He should then evaluate all the information available to him concerning the related party transaction or control relationship and satisfy himself on the basis of his professional judgment that it is adequately disclosed in the financial statements. (AU § 334.11).

99. Grassi failed to examine, document and satisfy itself as to the adequate disclosure of material related party transactions that it knew, or should have known about, including:

OPCO (MSF I, 2011)	Even though Grassi learned of OPCO brokerage accounts that management did not disclose to auditors through third-party confirmation provided directly to the audit team, Grassi’s workpapers made no reference to the undisclosed OPCO brokerage accounts. Further, Grassi’s workpapers did not address the fact that \$4.1 million of cash was transferred from the OPCO accounts to ClearPath. There are no disclosures in the audited financial statements related to these transactions.
Feingold O’Keeffe (MSF I and CPAI, 2011)	Despite the “pledged” notification on a confirmation statement received from Feingold O’Keeffe, Grassi auditors did not evaluate the meaning of the “pledged” notification; as a result, Grassi’s workpapers did not reveal that the “pledge” related to a credit line that Churchville and ClearPath secured with the Feingold O’Keeffe assets as collateral, with personal and corporate guarantees, none of which were reflected in the Funds’ audited financial statements.
DD1 (MSF III, 2011)	Grassi workpapers did not include any evidence of the auditor’s evaluation of the allocation of more than \$1 million of equity in the DD1 series to ClearPath outside the ordinary course of business. Furthermore, no disclosure of the transaction was included in the audited financial statements.

100. As a result of Grassi’s conduct described above, Grassi failed to comply with GAAS requirements for the testing and disclosure of related party transactions in its 2011 audits of MSF I, MSF III and CPAI.

Adequacy of Disclosure in Financial Statements (AU § 431)

101. The presentation of financial statements in conformity with generally accepted accounting principles includes adequate disclosure of material matters. These matters relate to the form, arrangement, and content of the financial statements and their appended notes, including, for example, the terminology used, the amount of detail given, the classification of items in the statements, and the bases of amounts set forth. An independent auditor considers

whether a particular matter should be disclosed in light of the circumstances and facts of which he is aware at the time. (AU § 431.02).

102. Grassi’s audit plan included the use of a disclosure checklist specifically designed for investment companies. The disclosure checklist section for Notes Payable and Other Debt included the question, “Is information related to unused lines of credit, conditions of credit agreements, and long-term debt maturities disclosed in the notes to the financial statements?” The checklist indicated that this question was “not applicable” despite the fact Feingold O’Keeffe reported directly to Grassi as part of its audit confirmation response that the largest assets in the MSF I and CPAI Funds were pledged. The checklist was prepared by the Grassi audit manager and reviewed by the engagement partner and the EQCR Reviewer. The 2011 audited financial statements for these Funds do not include a disclosure of the line of credit.

103. As a result of Grassi’s conduct described above, Grassi failed to comply with GAAS requirements regarding the adequacy of disclosures in the 2011 audits of MSF I and CPAI.

Grassi’s Improper Professional Conduct – Violation of Quality Control Standards

Quality Control Standards (AU § 161, QC § 10)

104. GAAS requires accounting firms to adopt a system of quality control in conducting an audit practice. (AU § 161.02). The elements of quality control are identified in QC section 10 – *A Firm’s System of Quality Control*.¹⁵ A system of quality control consists of policies designed to provide the firm with reasonable assurance that the firm and its personnel comply with professional standards and applicable legal and regulatory requirements and that reports issued by the firm are appropriate in the circumstances, and the procedures necessary to implement and monitor compliance with those policies. (AU § 161.01 [f/n 1]).

105. Grassi maintained a “Quality Control Document” which set forth the policies and procedures to be followed by the firm’s partners and employees in order to comply with the GAAS requirement to adopt a system of quality control.

106. The GAAS quality control standards require firms to, among other things, establish policies and procedures designed to provide it with reasonable assurance that it has sufficient personnel with the competence, capabilities, and commitment to ethical principles necessary to perform engagements in accordance with professional standards and applicable legal and regulatory requirements and enable the firm to issue reports that are appropriate in the circumstances. Further, the firm’s policies and procedures should provide that personnel selected for advancement have the qualifications necessary for fulfillment of the responsibilities that they will be called on to assume. (QC §§ 10.31-32)

¹⁵ References herein are to QC Section 10 as applicable to a CPA firm’s system of quality control for its accounting and auditing practice as of January 1, 2012.

107. When assigning partners and staff to audit engagements, the quality control standards require the firm to establish policies and procedures requiring, among others, that the engagement partner has the appropriate competence, capabilities, and authority to perform the role. Further, these policies and procedures should provide the firm with reasonable assurance that appropriate personnel are assigned to the engagement with the necessary competence and capabilities to perform engagements in accordance with professional standards and applicable legal and regulatory requirements and enable the firm to issue reports that are appropriate in the circumstances. (QC §§ 10.33-34)

108. Quality control standards require audit firms to monitor compliance with their quality control policies and procedures and evaluate, communicate and remedy identified deficiencies in systems of quality control. These monitoring standards require firms, among other things, to identify systemic, repetitive, or other significant deficiencies that require prompt corrective action. Remedial actions may include disciplinary action against individuals that failed to comply with the policies and procedures of the firm. Based on these monitoring controls, a firm may find that a report may be inappropriate or that procedures were omitted during the performance of the engagement. Such policies and procedures should require the firm to determine what further action is appropriate to comply with relevant professional standards and legal and regulatory requirements, and consider whether to obtain legal advice. (QC §§ 10.52-57).

109. Grassi permitted the ClearPath engagement partner to sign for release of the 2011 audit reports, even though the engagement partner had not properly reviewed the audit workpapers, and despite the fact that Grassi had learned that the engagement partner had previously circumvented firm policy for engagements other than ClearPath. Grassi also failed to appropriately document that the audits were performed in accordance with GAAS, and instead permitted issuance of the reports by sending an email. As a result, Grassi failed to comply with GAAS requirements regarding quality control standards in the 2011 audits of MSF I, MSF II, MSF III and CPAI.

FINDING

110. Based on the foregoing, the Commission finds that Grassi engaged in improper professional conduct within the meaning of Section 4C(a)(2) of the Exchange Act and Rule 102(e)(1)(ii) of the Commission's Rules of Practice. Grassi's conduct in the 2010 audit of MSF III and the 2011 audits of MSF I, MSF II, MSF III and CPAI involved repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards and indicating a lack of competence to practice before the Commission, and also satisfies the standard of highly unreasonable conduct that resulted in a violation of applicable professional standards in circumstances in which heightened scrutiny was warranted.

GRASSI WAS A CAUSE OF VIOLATIONS OF SECTIONS 206(2) and 206(4) of the ADVISERS ACT and RULE 206(4)-8 THEREUNDER.

111. Section 206(2) of the Advisers Act prohibits any investment adviser from engaging in any transaction, practice, or course of business which operates as a fraud or deceit

upon any client or prospective client. A violation of Section 206(2) may rest on a finding of negligence. *SEC v. Steadman*, 967 F.2d 363, 643 n.5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963)). Proof of scienter is not required to establish a violation of Section 206(2). *Id.*

112. Section 206(4) of the Advisers Act and Rule 206(4)-8 thereunder make it unlawful for any investment adviser to a pooled vehicle to make any untrue statement of a material fact or to omit to state a material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle, or to otherwise engage in any act, practice, or course of business that is fraudulent, deceptive or manipulative with respect to any investor or prospective investors in the pooled investment vehicle. A violation of Section 206(4) of the Advisers Act and the rules thereunder does not require scienter. *Steadman*, 967 F.2d at 647.

113. As a result of the conduct described above, Grassi was a cause of ClearPath's and Churchville's violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder.

E. UNDERTAKINGS

114. Independent Consultant. Grassi has undertaken to retain, within 30 days of the date of the issuance of this Order, the services of an Independent Consultant ("Consultant") not unacceptable to the staff of the Commission. Grassi shall provide to the Commission staff a copy of the engagement letter detailing the scope of the Consultant's responsibilities. The Consultant's compensation and expenses shall be borne exclusively by Grassi.

115. Grassi shall require the Consultant to conduct a review (the "Consultant Review") of the following:

- a. Grassi's quality controls, including policies and procedures for audits and reviews regarding the following (hereinafter referred to as "Grassi's Policies") to determine whether Grassi's Policies are adequate and sufficient to provide reasonable assurance of compliance with all relevant Commission regulations and auditing standards and rules:
 - i. Professional conduct for general, planning and supervision standards, including:
 1. The exercise of due professional care and professional skepticism;
 2. Properly planning an audit;
 3. Supervising the engagement team;

4. Obtaining sufficient appropriate audit evidence, including from independent sources, directly by the auditor, and in documentary form;
 5. Properly documenting an audit in sufficient detail to provide a clear understanding of the work performed, including in situations involving lack of responsiveness or original documents from the client, documentation of findings or issues with management, information that contradicts or is inconsistent with final conclusions, and documentation of when and with whom significant discussions occurred; and
 6. Properly training the engagement team, in particular, in audits of pooled investment vehicles as that term is defined by Rule 206(4)-8(b) promulgated under the Advisers Act (a “PIV”), and in technical training related to such audit work;
- ii. Professional conduct for fieldwork and reporting, including;
1. Subsequent events testing, including obtaining financial reports, accounting records or other independent evidence related to material subsequent events, aside from inquiry of management;
 2. The confirmation process, including obtaining evidence from third parties, evaluating that evidence and determining whether further testing is required;
 3. Fair value measurements and disclosures, including use of and/or reliance on the work of a specialist, and designing and executing audit procedures to test existence, valuation and transferability of collateral;
 4. Consideration of fraud in a financial statement audit, including review and testing of journal entries;
 5. Identification, examination and evaluation of appropriate disclosure of related party transactions; and
 6. Adequacy of disclosure in financial statements, including lines of credit or other agreements that might affect the value of investments;
- iii. Appropriate design and monitoring of compliance with quality control standards, including accurate review and sign-off on key workpapers, and objective review;

- b. A sample, to be selected by the Consultant on a reasonable and defined basis not unacceptable to the SEC, of Grassi's audits of financial statements of a PIV for periods ended on or after December 31, 2013.

116. Grassi shall cooperate fully with the Consultant and shall provide reasonable access to firm personnel, information and records as the Consultant may reasonably request for the Consultant Review (including training materials), subject to Grassi's right to withhold from disclosure any information or records protected by any applicable protection or privilege such as the attorney-client privilege or the attorney work product doctrine.

- a. At the end of the review, which in no event shall be more than six months after the date of the issuance of this Order, Grassi shall require the Consultant to issue a detailed written report (the "Consultant Report") to Grassi, (a) summarizing the Consultant Review, (b) making recommendations, where appropriate, reasonably designed to ensure that Grassi's Policies are adequate and sufficient to provide reasonable assurance of compliance with all relevant Commission regulations and auditing standards and rules, and (c) identifying any violations of auditing standards found in the review of Grassi's audits of financial statements of private or registered fund clients required in Paragraph 115.b. Grassi shall require the Consultant to provide a copy of the Consultant Report to the Commission staff when issued.
- b. Grassi shall adopt, as soon as practicable, all recommendations of the Consultant in the Consultant Report; provided, however, that within thirty days of issuance of the Consultant Report, Grassi may advise the Consultant in writing of any recommendation that it considers to be unnecessary, outside the scope of this Order, unduly burdensome, or impracticable. Grassi need not adopt any such recommendation at that time, but instead may propose in writing to the Consultant and the Commission staff an alternative policy or procedure designed to achieve the same objective or purpose. Grassi and the Consultant shall engage in good-faith negotiations in an effort to reach agreement on any recommendations objected to by Grassi. In the event that the Consultant and Grassi are unable to agree on an alternative proposal within 30 days, Grassi shall abide by the determinations of the Consultant. Grassi may also advise if it disagrees with the Consultant's identification of violations of audit standards found in the review of Grassi's audits of financial statements of private or registered PIV clients required in Paragraph 115.b.
- c. Within nine months after the date of issuance of this Order, Grassi shall require the Consultant to complete its review and submit a written final report ("Final Report") to Commission staff. The Final Report shall describe the review made of Grassi's policies and procedures; set forth the conclusions reached and the recommendations made by the Consultant, as well as any proposals made by Grassi; describe how Grassi is implementing the Independent Consultant's final recommendations; certify that the Consultant agrees with Grassi's adoption and

implementation of the recommendations; and identify the violations of auditing standards identified by the Consultant in its review of Grassi's audits of financial statements of private or registered PIV clients required in Paragraph 115.b.

- d. Grassi shall take all necessary and appropriate steps to adopt and implement all recommendations contained in the Final Report. The date of completion of the undertakings shall, in no event, be later than one year from the date of issuance of this Order;
- e. Grassi shall require the Consultant to enter into an agreement providing that for the period of the engagement and for a period of two years from completion of the engagement, the Consultant shall not enter into any employment, consultant, attorney-client, auditing or other professional relationship with Grassi, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such. The agreement will also provide that the Consultant will require that any firm with which he/she is affiliated or of which he/she is a member, and any person engaged to assist the Consultant in the performance of his or her duties under this Order shall not, without prior written consent of the Commission staff, enter into any employment, consultant, attorney-client, auditing or other professional relationship with Grassi, or any of its present or former affiliates, directors, officers, employees, or agents acting in their capacity as such for the period of the engagement and for a period of two years after the engagement.

117. Grassi shall inform its audit professionals involved in financial services audits of the non-financial terms of this Order and undertakings, within 10 business days after entry of the Order.

118. Training. Within 15 months of the issuance of this order, Grassi shall require each audit professional serving audits of a PIV to complete successfully a minimum of 8 hours of audit-related training. The audit-related training shall address any recommendations made by the Consultant regarding changes in Grassi's Policies related to the auditing standards set forth above (the "Audit Training").

119. Within 16 months of the issuance of this order, Grassi shall certify, in writing, compliance with the undertakings set forth above. The certification shall identify the undertakings, provide written evidence of compliance in the form of a narrative, and be supported by exhibits sufficient to demonstrate compliance. The Commission's staff may make reasonable requests for further evidence of compliance, and Grassi agrees to provide such evidence. The certification and supporting material shall be submitted to Robert B. Baker, Assistant Director, Asset Management Unit, Boston Regional Office, Securities and Exchange Commission, 33 Arch Street, 24th Floor, Boston, MA 02110, with a copy to the Office of the Chief Counsel of the Enforcement Division.

120. For good cause shown, the Commission staff may extend any of the procedural dates related to the undertakings. Deadlines for procedural dates shall be counted in calendar

days, except that if the last day falls on a weekend or federal holiday, the next business day shall be considered to be the last day.

121. In determining whether to accept Grassi's Offer, the Commission has considered these undertakings. Grassi agrees that if the Division of Enforcement believes that Grassi has not satisfied these undertakings, it may petition the Commission to reopen this matter to determine whether additional sanctions are appropriate.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED that:

A. Grassi shall cease and desist from committing or causing any violations and any future violations of Sections 206(2) and 206(4) of the Advisers Act and Rule 206(4)-8 thereunder.

B. Grassi is censured.

C. Grassi shall comply with the undertakings enumerated in Section III.E. above.

D. Grassi shall pay disgorgement of \$130,000 and prejudgment interest of \$11,510.41, for a total payment of \$141,510.41, to Stephen F. Del Sesto, Esq., the court-appointed receiver for ClearPath pursuant to Rule 1102 of the Commission Rules of Fair Fund and Disgorgement Plans [17 C.F.R. § 201.1102]. Payment shall be made in the following installments: \$28,302.09 within 10 days of the issuance of the Order; \$28,302.08 within 90 days of the issuance of the Order; \$28,302.08 within 180 days of the issuance of the Order; \$28,302.08 within 270 days of the issuance of the Order; and \$28,302.08 within 360 days of the issuance of the Order. If timely payment is not made, additional interest shall accrue pursuant to Commission Rule 600. Payment must be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to Stephen F. Del Sesto, Esq.; (C) hand-delivered or mailed to Stephen F. Del Sesto, Esq., Donoghue Barrett & Singal, P.C., One Cedar Street, Suite 300, Providence, RI 02903; and (D) submitted under cover letter that identifies Grassi as a Respondent in these proceedings, the file number of these proceedings, and *Securities and Exchange Commission v. ClearPath Wealth Management, LLC, Patrick Evans Churchville, as Defendants, and ClearPath Multi-Strategy Fund I, L.P., ClearPath Multi-Strategy Fund II, L.P., ClearPath Multi-Strategy Fund III, L.P., and HCR Value Fund, L.P., as Relief Defendants*, Civil Action No. 15-cv-00191, a copy of which cover letter and money order or check must be sent to Robert B. Baker, Assistant Director, Asset Management Unit, Securities and Exchange Commission, 33 Arch Street, 24th Floor, Boston, MA 02110.

E. Grassi shall pay a civil money penalty of \$260,000 to Stephen F. Del Sesto, Esq., the court-appointed receiver for ClearPath pursuant to Rule 1102 of the Commission Rules of Fair Fund and Disgorgement Plans [17 C.F.R. § 201.1102]. Payment shall be made in the

following installments: \$52,000 within 10 days of the issuance of the Order; \$52,000 within 90 days of the issuance of the Order; \$52,000 within 180 days of the issuance of the Order; \$52,000 within 270 days of the issuance of the Order; and \$52,000 within 360 days of the issuance of the Order. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. § 3717. Payment must be: (A) made by United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to Stephen F. Del Sesto, Esq.; (C) hand-delivered or mailed to Stephen F. Del Sesto, Esq., Donoghue Barrett & Singal, P.C., One Cedar Street, Suite 300, Providence, RI 02903; and (D) submitted under cover letter that identifies Grassi as a Respondent in these proceedings, the file number of these proceedings, and *Securities and Exchange Commission v. ClearPath Wealth Management, LLC, Patrick Evans Churchville, as Defendants, and ClearPath Multi-Strategy Fund I, L.P., ClearPath Multi-Strategy Fund II, L.P., ClearPath Multi-Strategy Fund III, L.P., and HCR Value Fund, L.P., as Relief Defendants*, Civil Action No. 15-cv-00191, a copy of which cover letter and money order or check must be sent to Robert B. Baker, Assistant Director, Asset Management Unit, Securities and Exchange Commission, 33 Arch Street, 24th Floor, Boston, MA 02110.

F. Pursuant to Section 308(a) of the Sarbanes-Oxley Act of 2002, as amended, a Fair Fund is created for disgorgement, prejudgment interest and penalties referenced in paragraphs D. and E. above. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Brent J. Fields
Secretary