

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 53953 / June 7, 2006**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 2441 / June 7, 2006**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-12326**

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**In the Matter of**

**NEVANNA SACKS, CPA,**

**Respondent.**

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**:**  
**:** **ORDER INSTITUTING PUBLIC**  
**:** **ADMINISTRATIVE PROCEEDINGS**  
**:** **PURSUANT TO RULE 102(e) OF THE**  
**:** **COMMISSION’S RULES OF PRACTICE,**  
**:** **MAKING FINDINGS, AND IMPOSING**  
**:** **REMEDIAL SANCTIONS**  
**:**  
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**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate that public administrative proceedings be, and hereby are, instituted against Nevanna Sacks, CPA (“Respondent” or “Sacks”) pursuant to Rule 102(e)(1)(ii) of the Commission’s Rules of Practice.<sup>1</sup>

**II.**

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (“Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceeding brought by or on behalf of

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<sup>1</sup> Rule 102(e)(1)(ii) provides, in pertinent part, that:

The Commission may ... deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found ... to have engaged in ... improper professional conduct.

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 her and the subject matter of these proceedings, Respondent consents to the entry of this Order Instituting Public Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

### III.

On the basis of this Order and Respondent's Offer, the Commission finds<sup>2</sup> that:

#### A. RESPONDENT

Nevanna Sacks is a certified public accountant licensed in California and Florida. Sacks was an audit manager on Arthur Andersen LLP's ("Arthur Andersen") audit of the fiscal year 2001 financial statements of Peregrine Systems, Inc. ("Peregrine") and on Arthur Andersen's reviews of Peregrine's quarterly financial statements for the company's third quarter of 2001 and first, second and third quarters of 2002.<sup>3</sup> Sacks previously was an audit senior on Arthur Andersen's audit of Peregrine's fiscal year 2000 financial statements and review of the company's quarterly financial statements for the third quarter of 2000 and the first and second quarters of 2001. Sacks left Arthur Andersen in May 2002. She is currently the CFO of a privately-held company.

#### B. OTHER RELEVANT ENTITY

Peregrine Systems, Inc. was a Delaware corporation headquartered in San Diego, California. Peregrine developed and marketed infrastructure management software products. Peregrine's common stock was registered with the Commission pursuant to Section 12(g) of the Securities Exchange Act of 1934, from its initial public offering in April 1997 until its acquisition by Hewlett-Packard Company in December 2005. Peregrine filed a Form 15 on December 19, 2005.

In February 2003, Peregrine restated its financial results for its fiscal years 2000 and 2001 and for the first three quarters of its fiscal year 2002. In its restatement for fiscal year 2001 – the year-end audit for which Sacks served as an audit manager – Peregrine reduced previously reported software license revenues by approximately \$259.7 million, from \$354.6 million down to approximately \$94.9 million.<sup>4</sup>

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<sup>2</sup> The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceedings.

<sup>3</sup> Peregrine's fiscal year ended on March 31. Therefore, Peregrine's fiscal year 2001 involves the period from April 1, 2000, to March 31, 2001. Peregrine filed a materially false and misleading Form 10-K with the Commission for its fiscal year 2001 on June 29, 2001.

<sup>4</sup> In June 2003, the Commission filed a civil injunctive action against Peregrine, and the U.S. District Court in San Diego entered a Final Judgment by consent against the company, which, among other

## C. FACTS

### 1. Sacks' Conduct

#### Peregrine's Reseller Revenue Scheme

a. Sacks' improper professional conduct as an auditor occurred in the context of a revenue recognition fraud being conducted by Peregrine personnel and others. Peregrine sometimes used "resellers" to help in the marketing of its software. Resellers – also called "channel partners" – are companies that purchase software for resale to end users. Peregrine frequently entered into undisclosed oral or written agreements with channel partners that made its "sales" to them conditional. These agreements freed the channel partners from any enforceable obligation to Peregrine if they failed to resell the software. Despite these side agreements, Peregrine generally recognized the revenue from these reseller agreements and used reseller revenue to meet or exceed revenue predictions. However, Peregrine's channel partners frequently failed to resell the software, and therefore failed to pay Peregrine on the deals. As a result, Peregrine did not have a history of collecting payment on its agreements with channel partners.

b. Peregrine's recognition of reseller revenue did not comply with generally accepted accounting principles ("GAAP"). The recognition of revenue from the sale of software products is controlled by the American Institute of Certified Public Accountants' Statement of Position (SOP) 97-2, "Software Revenue Recognition." SOP 97-2 prohibited Peregrine from recognizing revenue on software sales unless each of four criteria was met: (a) persuasive evidence of an arrangement exists; (b) delivery has occurred; (c) the fee is fixed or determinable; and (d) collectibility is probable. Peregrine's undisclosed side agreements with resellers made revenue recognition improper. As a separate matter, much of Peregrine's reseller revenue was not properly recognized under GAAP because collectibility was less than probable. Historically, Peregrine often failed to collect payment on agreements with resellers.

c. In addition, Peregrine's reseller agreements sometimes included extended payment terms, giving resellers as long as three years to pay Peregrine. If payment terms exceed one year, SOP 97-2 presumes the fee is not fixed or determinable and therefore revenue can not be recognized. Peregrine could overcome this presumption only by demonstrating a history of successfully collecting all payments as due under comparable arrangements. Peregrine did not have such a history.

#### Sacks Failed to Exercise Due Professional Care While Conducting the Peregrine Audit

d. During her work as audit senior on the Peregrine engagement, Sacks learned that other Arthur Andersen auditors had concerns regarding Peregrine's

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things, enjoined it from further violations of the anti-fraud, reporting, and books and records provisions of the federal securities laws.

reseller arrangements. In January 2000, shortly after she began work on the Peregrine engagement, Sacks learned that the Arthur Andersen partner then assigned to the Peregrine audit was concerned that Peregrine channel partners appeared to be reselling Peregrine software more slowly than the Arthur Andersen partner had anticipated. Sacks understood that as a result of his concerns, the audit partner had advised Peregrine not to recognize revenue on reseller agreements with extended payment terms. Sacks knew that Peregrine – already identified by Arthur Andersen as a high-risk audit client due to revenue recognition issues – had agreed to stop recognizing revenue on these agreements due to the audit partner’s concerns. Additionally, in April 2000 a German affiliate of Arthur Andersen (“Arthur Andersen Germany”), after reviewing Peregrine’s German subsidiary (“Peregrine Germany”), suspected that Peregrine Germany had been improperly recording reseller revenue. In an email memorandum dated April 14, 2000, an Arthur Andersen Germany auditor informed Sacks that, in Arthur Andersen Germany’s opinion, Peregrine Germany was recording “bad revenue.”

e. Sacks became an audit manager on the Peregrine engagement in September 2000 (Peregrine’s second quarter of fiscal year 2001), reporting to a new partner on the engagement. Peregrine was Sacks’ first assignment as an audit manager. Almost immediately after becoming a manager, Sacks received additional reports and information putting her on notice of risks regarding Peregrine’s revenue recognition. For example, in October 2000, Sacks and others on the Arthur Andersen U.S. audit team received a report from an auditor with Arthur Andersen Germany identifying what the auditor characterized as “major revenue recognition issues.” Later that month, Sacks was provided with a significant Peregrine contract with a reseller that provided the reseller with the right to cancel the contract. Despite the conditional nature of the agreement with the reseller, Sacks and the Arthur Andersen U.S. audit team failed to question Peregrine’s recognition of revenue on it.

f. The next quarter – Peregrine’s third quarter of fiscal year 2001, ended December 31, 2000 – Sacks received a report stating that a Peregrine subsidiary in the United Kingdom was experiencing collection problems on deals with resellers. Sacks also knew that the amount of channel inventory Peregrine reported to the Arthur Andersen U.S. audit team had increased by more than 25% since she had become an audit manager. Sacks also learned that Peregrine had resumed recording material amounts of software license revenue on contracts with extended payment terms. This was contrary to Peregrine’s prior policy – adopted on the advice of Andersen – not to recognize revenue on agreements with extended payment terms. Sacks and the Arthur Andersen U.S. audit team did not obtain sufficient competent evidence establishing that Peregrine had the history of collections required under GAAP to recognize this revenue.

g. Sacks also served as audit manager on Arthur Andersen’s audit of Peregrine’s financial statements to be included in Peregrine’s Form 10-K for the company’s fiscal year 2001, ended March 31, 2001. Peregrine filed that Form 10-K with the Commission on June 29, 2001. During the audit, Sacks learned that auditors with Arthur Andersen Germany had refused to issue a report on the financial statements of Peregrine Germany due to revenue recognition issues, control issues, and what they

described as “questionable system integrity.” The Andersen Germany auditors therefore concluded that the financial statements for Peregrine Germany – identified by the Arthur Andersen U.S. audit team as a material subsidiary – were not auditable. Sacks also knew that the Arthur Andersen Germany auditors had identified three reseller contracts that Peregrine Germany had entered into in the fourth quarter of 2001 that granted extended payment terms. Sacks learned that the Arthur Andersen Germany auditors concluded that it was inappropriate to recognize revenue on these extended payment term contracts.

h. Sacks knew that the Arthur Andersen Germany auditors refused to provide an audit report regarding Peregrine’s material German subsidiary. Despite the Arthur Andersen Germany auditors’ refusal to provide an audit report, Sacks and the Arthur Andersen U.S. audit team did not obtain sufficient competent evidence to provide a reasonable basis for Arthur Andersen to form an opinion on Peregrine’s consolidated financial statements, which included the revenue from the Peregrine Germany contracts with extended payment terms.

i. As audit manager, Sacks failed to appropriately plan and perform the audit of Peregrine’s accounts receivable to obtain sufficient competent evidence to conclude that Peregrine’s recognition of revenue on extended payment term deals was appropriate. In particular, Sacks did not obtain sufficient competent evidence establishing that Peregrine had the history of collections required by SOP 97-2 to overcome the presumption that revenue should not be recognized on extended payment term contracts. Peregrine had no such history of collections. The company rarely collected its reseller receivables, and Sacks knew that Peregrine had millions of dollars in unpaid inventory with resellers. Peregrine inappropriately recognized material amounts of revenue on reseller agreements in violation of GAAP, and the company materially overstated its software license revenue in its fiscal year 2001 financial statements.

j. Additionally, Sacks assisted in preparing Peregrine’s response to a Comment Letter issued by the Commission’s Division of Corporation Finance on March 28, 2001 (“Comment Letter”). The Comment Letter questioned certain aspects of Peregrine’s reporting in its Form 10-K for fiscal year 2000 and Forms 10-Q for fiscal year 2001, including how it accounted for concession risks in extended payment term and other contracts. Peregrine’s response to the Comment Letter, dated April 12, 2001, included false statements regarding, among other things, the company’s history of collections. In particular, the company’s response to the Comment Letter falsely stated that Peregrine had successfully collected on all extended payment term contracts. Sacks helped to prepare an initial draft of Peregrine’s response to the Comment Letter, and also reviewed the final version of the response with Peregrine executives and the Arthur Andersen audit partner then assigned to the engagement before the false and misleading response was submitted to the Commission staff.

k. The conduct described above represents repeated instances of unreasonable conduct that resulted in violations of professional standards in the performance of Sacks’ reviews and audit of Peregrine’s financial statements.

## **2. Violations**

a. Rule 102(e)(1)(ii) of the Commission's Rules of Practice provides that the Commission may deny the privilege of appearing or practicing before it to any person who is found to have engaged in improper professional conduct. With respect to persons licensed to practice as accountants, "improper professional conduct" may include negligent conduct evidenced by "repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission." Rule 102(e)(1)(ii).

b. Sacks engaged in improper professional conduct by repeatedly engaging in unreasonable conduct, resulting in a violation of applicable professional standards that indicate a lack of competence to practice before the Commission. As discussed above, Sacks (i) failed to adequately audit Peregrine's accounts receivable; (ii) did not obtain sufficient competent evidential matter to conclude that Peregrine had a history of collecting on reseller agreements; (iii) failed to make adequate inquiries into Peregrine's agreements with resellers; (iv) failed to obtain sufficient competent evidential matter to afford a reasonable basis for Andersen to issue a report on the financial statements of Peregrine, which consolidated the financial statements of Peregrine Germany, a material subsidiary, after Arthur Andersen Germany refused to provide an audit report on the financial statements of Peregrine Germany; (v) failed to exercise due professional care in connection with Peregrine's false and misleading response to a Commission Comment Letter; and (vi) failed to exercise due professional care in connection with the audit and reviews.

## **3. Findings**

a. Based on the foregoing, the Commission finds that Sacks engaged in improper professional conduct pursuant to Rule 102(e)(1)(ii) of the Commission's Rules of Practice.

## **IV.**

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

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Sacks is denied the privilege of appearing or practicing before the Commission as an accountant.

B. After two (2) years from the date of this order, Sacks may request that the Commission consider her reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in her practice before the Commission will be reviewed either by the independent audit committee of the public company for which she works or in some other acceptable manner, as long as she practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which she is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which she is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the Respondent's or the firm's quality control system that would indicate that the Respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges her responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that her state CPA license is current and she has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Nancy M. Morris  
Secretary