Securities Regulation Daily Wrap Up, TOP STORY—SEC charges former PCAOB and KPMG officials for misappropriating confidential information, (Jan. 22, 2018)

Securities Regulation Daily Wrap Up

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By Jacquelyn Lumb

The SEC has announced charges against three former accountants who worked at the PCAOB and three former KPMG senior officials for their participation in a scheme to use confidential information about the Board's inspection plans for the firm. Steven Peikin, the co-director of the SEC's Enforcement Division, characterized their misconduct as shocking and serious, and said it amounted to "stealing the exam." In a parallel action, the U.S. Attorney's Office for the Southern District of New York announced criminal charges against the six accountants. Peikin would not comment on potential additional charges but advised that the SEC's investigation is ongoing (*In the Matter of Cynthia Holder, CPA, Jeffrey Wada, CPA, David Middendorf, CPA, Thomas Whittle, CPA, and David Britt, CPA*, Release No. 34-82556, January 22, 2018).

Inspection results. Peikin explained during a press briefing that KPMG had a high and increasing rate of deficiencies that were discovered during PCAOB inspections, having received nearly twice as many comments in 2014 as its competitors. The firm was intent upon improving its inspection results and the SEC alleges that its effort to "get a better grade" was accomplished through illegal conduct by KPMG and PCAOB personnel—the misappropriation of confidential information about the audit engagements the Board planned to inspect, the criteria used to select the engagements for inspection, and the focus areas of the inspection.

PCAOB employees' actions. According to the SEC's charges, Brian Sweet took confidential PCAOB information on his last day of employment before joining KPMG. Cynthia Holder, another PCAOB employee, provided Sweet with additional confidential materials while she was seeking employment at KPMG. After she joined KPMG, a third PCAOB employee, Jeffrey Wada, provided confidential information about planned inspections to Holder and also began seeking employment with the firm.

The SEC's administrative proceeding states that Sweet told his supervisors in KPMG's national office that he had taken confidential information from the PCAOB and that he had access to additional information from PCAOB employees. KPMG partners David Middendorf and Thomas Whittle encouraged Sweet to share the information and, in reliance on that information, analyzed and reviewed audit work papers in order to suggest revisions to help avoid findings of deficiencies by the PCAOB.

KPMG discovers misconduct. After Sweet warned a number of engagement partners about impending inspections, one of them suspected that he had received confidential PCAOB information, which led to an internal investigation by KPMG's office of general counsel. The general counsel's office reported the matter to the SEC and the PCAOB.

Alleged violations. The SEC alleges that the former PCAOB employees violated the Board's ethics code and that the KPMG officials aided and abetted their violations. All of the respondents lacked integrity and/or engaged in improper professional conduct in violation of Exchange Act Section 4C(a)(2) and Rule 102(e)(1)(ii) of the Commission's rules of practice. The administrative and cease-and-desist proceedings were instituted to determine whether the allegations are true, whether to order the payment of disgorgement and civil penalties, and whether the respondents should be barred from appearing before the Commission as accountants. Sweet was named in a separate administrative and cease-and-desist proceeding from the other respondents (*In the Matter of Brian Sweet, CPA*, Release No. 34-82557, January 22, 2018).

Chairman's statement. SEC Chairman Jay Clayton issued a statement in support of the enforcement action and advised that based on discussions with the staff, he did not believe the actions affected the ability of affected SEC registrants to continue to use the audit reports issued by KPMG in their filings or for investors to rely on those reports. The SEC will continue to monitor this matter closely and Clayton has asked PCAOB Chairman Duhnke to review the Board's assessment of its internal information technology and security controls following the discovery of the alleged breaches to determine whether any further actions were necessary.

The releases are No. 34-82557 and No. 34-82556.

Companies: KPMG LLP

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