

[Securities Regulation Daily Wrap Up, TOP STORY—KPMG hit with \\$50M penalty for stealing PCAOB inspection documents, cheating on exams, \(Jun. 17, 2019\)](#)

Securities Regulation Daily Wrap Up

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Enforcement Co-Director Steve Peiken said that in two separate courses of conduct, KPMG personnel attempted to compromise efforts to test their performance through the theft of confidential PCAOB inspection documents and cheating on internal training examinations.

The SEC announced that KPMG will pay a \$50 million penalty for the illicit use of confidential PCAOB data and cheating on internal training exams. The SEC alleged that former PCAOB employees, two of whom were hired by KPMG, gave PCAOB inspections documents relating to KPMG's inspections to senior KPMG personnel ahead of the Board's inspection of the firm. The SEC also alleged that audit professionals shared answers and manipulated results in KPMG's internal training examinations. In addition to the penalty, KPMG admitted to wrongdoing and agreed to a series of undertakings, including the retention of an independent consultant to review the firm's policies and procedures (*In the Matter of KPMG LLP*, [Release No. 34-86118](#), June 17, 2019).

From the PCAOB to KPMG. The PCAOB's report on its 2013 inspections of KPMG's audits, issued in September 2014, found that 23 of the 50 audits inspected had deficiencies. Following the negative report, KPMG sought to improve its inspection results and hired Brian Sweet, who was an associate director at the PCAOB who had worked on the inspection team of KPMG audits. According to the SEC, before Sweet left the PCAOB, he copied confidential inspection-related materials and transferred them to a personal hard drive, which he then transferred to his computer at KPMG after joining the firm in May 2015.

The SEC alleged that KPMG national managing partner David Middendorf and national partner-in-charge for quality measurement Thomas Whittle directed that the information obtained by Sweet be used to prepare for KPMG's upcoming inspection. This included the confidential list of the PCAOB's planned inspections for 2015 and the PCAOB's confidential criteria used for selecting audits to inspect. Sweet had also provided confidential PCAOB comment forms related to the audit of a Spanish bank while KPMG was preparing an audit pitch for a different Spanish bank's audit business.

The SEC also alleged that Sweet was going to push for KPMG to hire PCAOB inspections leader Cynthia Holder and that shortly after he started working at the firm, he asked Holder to send him a confidential PCAOB document of his comments he had written about KPMG's audits during his time at the PCAOB, which she did. KPMG sent Holder an employment offer in July 2015 and she joined the firm a month later.

In addition, KPMG received confidential information from a PCAOB inspections leader, Jeffrey Wada, who, according to the SEC, reacted "angrily" when he was passed over for a promotion. The information KPMG allegedly obtained from Wada included a list of the PCAOB's planned inspections for 2016 and 2017. According to the SEC, Middendorf and Whittle had instructed at a briefing that no one should disclose that they had obtained confidential PCAOB information. When Sweet questioned what to do with the confidential information, Middendorf allegedly said that the information was "too good not to use."

In contrast to prior years, KPMG's 2016 inspection results did not include comments related to the general Allowance for Loan and Lease Losses. One KPMG engagement partner suspected that the firm had received confidential PCAOB information and reported her concerns to the firm's management, who reported the matter to the PCAOB and commenced an investigation.

Cheating on training exams. The SEC also alleged that KPMG audit officials improperly shared training exam answers. KPMG administers its own set of online training programs to qualify for continuing professional education (CPE) credit. According to the SEC, several KPMG employees who had passed the exams, including lead audit engagement partners, sent their answers to their colleagues to help them pass the exams.

The SEC also alleged that some audit professionals at KPMG manipulated the scoring of the training exams to lower the scores required to pass. According to the SEC, 28 auditors did so on four or more occasions, and some lowered the required score to allow a passing grade when answering only 25 percent of the questions correctly.

Sanctions. The SEC charged KPMG with violating PCAOB Rule 3500T, which requires firms and personnel to maintain integrity. In addition to admitting wrongdoing, KPMG [agreed](#) to pay a \$50 million civil penalty to settle the SEC's charges. KPMG also committed to a number of undertakings, including the retention of an independent consultant to review and assess KPMG's quality controls and the adoption of the consultant's recommendations. All KPMG audit professionals will be required to complete a minimum of 12 hours of ethics and integrity training each year. In addition, KPMG's CEO must certify the sufficiency of KPMG's policies and procedures related to the enumerated undertakings in 2020 and 2021.

On a press call with reporters, SEC Enforcement Co-Director Steve Peiken said that while KPMG's violations involved two separate courses of misconduct, they had the common theme of violating the fundamental concept that auditors act with integrity. In each case, the conduct involved senior personnel at the firm, Peiken observed, and the misconduct went on for several years before coming to light. It was "an extraordinary situation that merits an extraordinary response," Peiken said.

Criminal charges and continuing litigation. Middendorf and Wada were [convicted](#) in March of wire fraud for their roles in the scheme to steal PCAOB documents. In October, Holder [pleaded](#) guilty to conspiracy against the United States, wire fraud, and conspiracy to commit wire fraud. The SEC [charged](#) the individuals involved in the scheme in January 2018. The SEC's enforcement action was stayed pending final resolution of the criminal charges.

The release is [No. 34-86118](#).

Companies: KPMG LLP

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