Press Release

SEC Charges KPMG With Violating Auditor Independence Rules

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Washington D.C., Jan. 24, 2014

The Securities and Exchange Commission today charged public accounting firm KPMG with violating rules that require auditors to remain independent from the public companies they're auditing to ensure they maintain their objectivity and impartiality.

The SEC issued a separate report about the scope of the independence rules, cautioning audit firms that they're not permitted to loan their staff to audit clients in a manner that results in the staff acting as employees of those companies.

An SEC investigation found that KPMG broke auditor independence rules by providing prohibited non-audit services such as bookkeeping and expert services to affiliates of companies whose books they were auditing. Some KPMG personnel also owned stock in companies or affiliates of companies that were KPMG audit clients, further violating auditor independence rules.

KPMG agreed to pay $8.2 million to settle the SEC's charges.

"Auditors are vital to the integrity of financial reporting, and the mere appearance that they may be conflicted in exercising independent judgment can undermine public confidence in our markets," said John T. Dugan, associate director for enforcement in the SEC's Boston Regional Office. "KPMG compromised its role as an independent audit firm by providing prohibited non-audit services to companies that it was supposed to be auditing without any potential conflicts."

According to the SEC's order instituting settled administrative proceedings, KPMG repeatedly represented in audit reports that it was "independent" despite providing services to three audit clients that impaired KPMG's independence. The violations occurred at various times from 2007 to 2011.

According to the SEC's order, KPMG provided various non-audit services – including restructuring, corporate finance, and expert services – to an affiliate of one company that was an audit client. KPMG provided such prohibited non-audit services as bookkeeping and payroll to affiliates of another audit client. In a separate instance, KPMG hired an individual who had recently retired from a senior position at an affiliate of an audit client. KPMG then loaned him back to that affiliate to do the same work he had done as an employee of that affiliate, which resulted in the professional acting as a manager, employee, and advocate for

the audit client. These services were prohibited by Rule 2-01 of Regulation S-X of the Securities Exchange Act of 1934.

The SEC's order finds that KPMG's actions violated Rule 2-02(b) of Regulation S-X and Rule 10A-2 of the Exchange Act, and caused violations of Section 13(a) of the Exchange Act and Rule 13a-1. The order further finds that KPMG engaged in improper professional conduct as defined by Section 4C of the Exchange Act and Rule 102(e) of the Commission's Rules of Practice. Without admitting or denying the findings, KPMG agreed to pay $5,266,347 in disgorgement of fees received from the three clients plus prejudgment interest of $1,185,002. KPMG additionally agreed to pay a penalty of $1,775,000 and implement internal changes to educate firm personnel and monitor the firm's compliance with auditor independence requirements for non-audit services. KPMG will engage an independent consultant to evaluate such changes.

The SEC's investigation separately considered whether KPMG's independence was impaired by the firm's practice of loaning non-manager tax professionals to assist audit clients on-site with tax compliance work performed under the direction and supervision of the clients' management. While the SEC did not bring an enforcement action against KPMG on this basis, it has issued a report of investigation noting that by their very nature, so-called "loaned staff arrangements" between auditors and audit clients appear inconsistent with Rule 2-01 of Regulation S-X, which prohibits auditors from acting as employees of their audit clients.

The report also emphasized:

- An auditor may not provide otherwise permissible non-audit services (such as permissible tax services) to an audit client in a manner that is inconsistent with other provisions of the independence rules.
- An arrangement that results in an auditor acting as an employee of the audit client implicates Rule 2-01 regardless of whether the accountant also acts as an officer or director, or performs any decision-making, supervisory, or ongoing monitoring functions, for the audit client.
- Audit firms and audit committees must carefully consider whether any proposed service may cause the auditors to resemble employees of the audit client in function or appearance even on a temporary basis.

The SEC's Office of the Chief Accountant has a Professional Practice Group that is devoted to addressing questions about auditor independence among other matters. Auditors and audit committees are encouraged to consult the SEC staff with questions about the application of the auditor independence rules, including the permissibility of a contemplated service.

"The accounting profession must carefully consider whether engagements are consistent with the requirements to be independent of audit clients," said Paul A. Beswick, the SEC's chief accountant. "Resolving questions about permissibility of non-audit services is always best done before commencing the services."

The SEC's investigation was conducted by Britt K. Collins, Dawn A. Edick, Michael Foster, Heidi M. Mitza, and Kathleen Shields. The SEC appreciates the assistance of the Public Company Accounting Oversight Board.

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