KPMG

Ethics and Compliance Report 2009

KPMG'S ETHICAL CULTURE

A Continuing Conversation on Ethics and Integrity

AUDIT ▪ TAX ▪ ADVISORY

Our Core Values

The KPMG Way is our definition of who we are, what we do, and how we do it. Our core values lie at the heart of The KPMG Way. They define our culture and our commitment to the highest principles of personal and professional conduct. They also represent how our people relate to each other, what we expect of our clients and vendors, and what our clients, vendors, and the marketplace should expect of us.

WE LEAD BY EXAMPLE at all levels, acting in a way that exemplifies what we expect of each other and our member firms' clients.

WE WORK TOGETHER bringing out the best in each other and creating strong and successful working relationships.

WE RESPECT THE INDIVIDUAL respecting people for who they are and for their knowledge, skills, and experience as individuals and team members.

WE SEEK THE FACTS AND PROVIDE INSIGHT challenging assumptions, pursuing facts, and strengthening our reputation as trusted and objective business advisers.

WE ARE OPEN AND HONEST IN OUR COMMUNICATION sharing information, insight, and advice frequently and constructively, and managing tough situations with courage and candor.

WE ARE COMMITTED TO OUR COMMUNITIES acting as responsible corporate citizens, and broadening our skills, experience, and perspectives through work in our communities.

ABOVE ALL, WE ACT WITH INTEGRITY complying with all applicable laws and regulations, upholding the highest professional standards, providing sound advice, and rigorously maintaining our independence.

INTEGRITY underlies all of these principles.

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ON THE COVER: Roundtable on ethical culture participants (from left) Sven Erik Holmes, Donna Boehme, Keith Darcy, Steve Priest, Candy Duncan, and Rich Girgenti. *Photo by Roger Tully*

Foreword

TIM FLYNN, CHAIRMAN
JOHN VEIHMEYER, CEO AND DEPUTY CHAIRMAN

AT KPMG, NOTHING IS MORE IMPORTANT THAN ETHICS AND INTEGRITY. THAT IS WHY, SEVERAL YEARS AGO, WE COMMITTED TO BUILDING AN ETHICS AND COMPLIANCE PROGRAM AND CULTURE THAT SERVES AS A MODEL FOR THE PROFESSION AND OTHER INDUSTRIES.

The success of an ethics and compliance program can be measured, in large part, by the ethical culture of the organization. At KPMG, we have worked to create a culture in which every individual feels a sense of personal responsibility for the ethical environment of the firm. In these challenging economic times, it is especially important that we uphold this responsibility and do the right thing, in the right way, no matter what pressures we face.

Over the long term, our ethical culture will help KPMG thrive because it will allow us to attract and retain the best people and to achieve our Quality Growth objectives in the marketplace.

Ethics and integrity also are critical to the broad economic recovery. We often share our vision of an ethics-driven business with audiences outside the firm, and the message has been well received. Business leaders recognize that ethics and integrity are fundamental and essential to maintaining trust in the capital markets.

Having an ethical culture means that we are open and honest in our communication, and that we share information, insight, and advice frequently and constructively. This report is an important part of that communication. This year, the report begins with a roundtable on business ethics. Led by Sven Erik Holmes, KPMG's Executive Vice Chair, Legal and Compliance, the roundtable brings together outside specialists and KPMG partners to discuss major issues in business ethics: How does an organization build and sustain an ethical culture? What makes an ethical leader? What are some emerging trends in business ethics?

Much of the report is devoted to examining some of the leading practices in KPMG's ethics and compliance program, showing how they are integrated with the day-to-day operations of the firm. For instance, a discussion with Partners Lynne Doughtie, Scott Frew, and Rick Smith describes how our Management Review Panel ensures consistency of discipline across the firm.

"Partnering with Human Resources" shows the close collaboration between our Ethics and Compliance Group and Human Resources in the critical area of career management. As you will see, a good record in ethics and compliance is good for one's career.

Similarly, "Ethics and Compliance Training" shows how ethics and compliance is an integral part of the training curriculum at the firm. A close look at the Quarterly Training Summit explains how ethics and compliance messages are woven into all aspects of the training received by every professional in Audit, Tax, and Advisory as well as our client service support people.

We also are mindful of the latest thinking on business ethics. We know that the definition of ethical culture itself is broadening to include corporate social responsibility and accountability, and we are thinking about how to shift and accommodate our program accordingly.

This report is part of an ongoing dialogue about the critical importance of ethics and integrity that is taking place throughout KPMG. We encourage you to continue the dialogue and talk with each other about ethics and integrity, especially when you need support in doing the right thing, in the right way. And we thank you for taking personal responsibility for ethics and compliance at KPMG. Because of you, KPMG is a model of ethics and integrity.

"Over the long term, our ethical culture will help KPMG thrive because it will allow us to attract and retain the best people and to achieve our Quality Growth objectives in the marketplace." — TIM FLYNN

A ROUNDTABLE: Building an Enduring Ethical Culture

HOW DOES AN ORGANIZATION BUILD AN ETHICAL CULTURE THAT STANDS THE TEST OF TIME? WHAT MAKES AN ETHICAL LEADER? WHAT CHANGES AND CHALLENGES ARE ON THE HORIZON IN THE WORLD OF BUSINESS ETHICS? AS A PART OF KPMG'S COMMITMENT TO MAINTAINING ITS MODEL ETHICS AND COMPLIANCE PROGRAM, THE FIRM HELD A ROUNDTABLE DISCUSSION TO EXPLORE THESE AND MANY OTHER CRITICAL QUESTIONS.

The roundtable was moderated by Sven Erik Holmes, KPMG's Executive Vice Chair, Legal and Compliance, and the leader of the firm's ethics and compliance program.

Donna Boehme is Principal, Compliance Strategists, LLC; Special Advisor to Compliance Systems Legal Group; and former Group Compliance and Ethics Officer of BP plc. She advises a wide spectrum of private, public, governmental, academic, and non-profit entities on ethics and compliance issues.

Keith Darcy is the Executive Director of the Ethics & Compliance Officer Association (ECOA). ECOA is the largest association of ethics and compliance professionals worldwide, with more than 1,400 members across six continents.

Steve Priest founded the Ethical Leadership Group, now a Global Compliance company, and has consulted on ethics in more than 40 countries for organizations in most major industries.

Candy Duncan recently was named KPMG's Office Managing Partner for the Washington Metropolitan area and a member of the KPMG board of directors. She served as the Area Managing Partner for KPMG's Midatlantic Area since 2005 and has more than 30 years of experience as an Audit professional with KPMG.

Rich Girgenti is the National and Americas leader for KPMG's Forensic Advisory Services practice. A former member of the KPMG board, he has more than 30 years of experience conducting investigations and providing fraud risk management advisory services to corporations and non-profit organizations.

SVEN: Why should an organization have an ethical culture? What is the value beyond helping to ensure compliance with applicable laws?

KEITH: One must have an ethical culture because the alternative is unthinkable — a breakdown of trust among your stakeholders, a badly damaged brand. There is a large body of evidence showing that truly great companies have very strong cultures supporting them.

SVEN: What constitutes a strong ethical culture?

STEVE: Organizations with strong ethical cultures look very similar. They are the kinds of companies we want to buy from, the kind we trust with our investment dollars. But it's interesting to examine the obstacles to creating an ethical culture, and our research shows there are several. One obstacle is when employees don't understand their organization's rules or values, or don't believe those rules apply to them. Another is when employees believe that management doesn't follow the rules.

To have a strong ethical culture, you need accountability. There are too many companies out there where great performers get a pass. If they don't live up to the company's values, it doesn't matter because they're making the numbers. So a company that has the right approach in this area is probably going to have an ethical culture where people do the right things every day automatically.

RICH: I look for tone at the top. First, is leadership sending the right messages throughout the organization? Second, are line supervisors really behaving like role models for the rest of the organization? Third, do employees feel ownership for the brand and the culture?

DONNA: I would add that we should look at small moments in day-to-day operations. What happens when somebody in a meeting raises their hand and says something a little controversial? What's the immediate reaction? What happens if a business unit leader finds out that there is a hotline investigation in his unit? What's his immediate reaction? All of these things tell you about the DNA of a company.

CANDY: Sometimes, what seems to be an insignificant moment or decision is really what's building the culture and legacy of the organization. That's what it's really all about — the decisions that we make every day and how they add up over time.

SVEN: What leading-edge initiatives are companies using to build that kind of a culture?

DONNA: The most encouraging thing I'm seeing is companies are implementing programs that drive the kind of conduct we want to see. They're building ethics into the compensation and promotion processes, incorporating ethical leadership into performance reviews. These are practices we didn't see five years ago. I'm also seeing better information flowing up to the board of directors. Thanks to ethics and compliance people, the board is getting a holistic picture, beyond just hotline statistics, which allows the organization to address issues as they come up.

SVEN: What else are you seeing?

STEVE: As we talk today, our economy is still struggling, and some companies have cut back on their ethics and compliance efforts. This is a big mistake. You have to stick with your program through good times and bad. This isn't exactly a cutting-edge practice, but it is a sign of leadership and good business.

KEITH: Jim Collins wrote a book some years back called *Built to Last*, about great companies that endure. All the companies he wrote about had very strong cultures, and


SVEN ERIK HOLMES

"The most encouraging thing I'm seeing is companies are implementing programs that drive the kind of conduct we want to see…These are practices we didn't see five years ago." — DONNA BOEHME

it was the culture that allowed them to ride out the peaks and troughs of business cycles. A few years later he wrote a magazine article called "Built to Flip," in which he said we have become a nation of "flippers." We want to exploit an opportunity, make as much money as we can as quickly as we can. He said the soul of our economy is at stake now. I'll never forget the compelling words at the end of that article, when he said that growth at any cost is not a strategy that can endure. A culture needs to aim for managed growth that meets the needs of all its stakeholders.

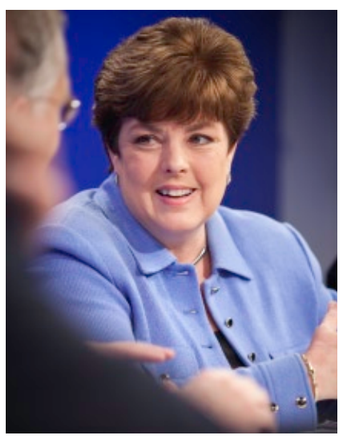
CANDY: And you accomplish that by doing the right things in the right way consistently across the entire organization, and from the most junior people all the way to the top of the firm. That consistency is really what builds a culture that can endure and thrive no matter what the times are like.

SVEN: Speaking of consistency, what's the best way to make sure you are dealing effectively with potential violations and ensuring that the discipline is appropriate and handled consistently?

RICH: It starts with the ability to identify problems within the organization. When you receive allegations of misconduct, you must be able to conduct investigations that are thorough, timely, and fair. You must also work to ensure that the information about what went wrong gets fed back to the business units. You need a feedback loop so your people can learn from issues in the organization. And as you said, the discipline itself needs to be consistent. People need to know that the same standards apply to everyone. And line management has to be included in the actions taken for particular problems.

It's also very important that the people who raise an issue know that something is being done about it. Otherwise, the system will lose credibility.

"At KPMG, we emphasize personal responsibility and accountability. And we help people understand that they are really setting the tone at our firm." — CANDY DUNCAN



STEVE: But how do you deal with the person who is a discipline problem but also a top performer? Maybe he hasn't done anything terribly wrong, but he's certainly not a paragon of the firm's values. How do you work through that issue?

RICH: You deal with it through mentoring, coaching, and performance review. And you deal with it through compensation. People have to understand that they're not just paid for performance. The manner in which you perform matters a great deal.

SVEN: Let's talk about the problem of retaliation against people who raise their hand. Here at KPMG, we encourage everyone to speak up if they have a concern, and we make it clear that we will not tolerate retaliation against anyone who raises their hand in good faith. Still, we all know it's not easy to raise your hand, and we know that some people do fear retaliation. What are the best ways to alleviate that fear and to guard against retaliation?

STEVE: In our work we find that the majority of people who see problems in their organizations don't report them. And the number one reason for not reporting isn't fear of retaliation. Employees do not believe that management is going to take the proper action anyway, so why take the risk of reporting? The second reason they choose not to report is fear of retaliation. So, on this issue, leadership has two big challenges to manage.

How do you address the fear of retaliation? It takes solid policies. KPMG actively looks for signs of retaliation and has a terrific practice. But this is a challenging issue that takes time. It takes informal stories that travel through the grapevine — people telling each other, "You know, this is a company where you get rewarded for doing the right thing."

DONNA: Retaliation is a difficult subject because it can be subtle and difficult to recognize. I've found it's helpful to educate leaders about the many forms that it can take. I've seen organizations that couldn't find instances of retaliation because they were looking for the wrong things. It's important for people to be able to really recognize the subtleties.

SVEN: Let's talk about some of the root causes of misconduct. Rich, you've done a lot of work on this with KPMG's board and with clients. What is your view?

RICH: You start with the fact that none of us is perfect, and people can be tempted to do the wrong thing. Sometimes the action is unintentional — a person doesn't know what he is doing violates a standard or requirement. Very often, the misconduct starts out small — someone crosses a line thinking, "I'll do it just this once."

When we investigate, very often we find the people who are engaged in misconduct have engaged in other forms of misconduct or non-compliance, but for some reason the organization didn't pick up on it.

We also look for evidence of employee dissatisfaction. When employees feel they're not being treated properly, the organization is often more vulnerable to misconduct. Companies need to pay attention to this and seek to create an Employer of Choice atmosphere.

DONNA: Misconduct usually occurs because of two things: an individual who makes a bad decision and a culture that allows it to happen. Even a rogue like Bernie Madoff can be stopped by a strong culture, where people see what's going on and want to raise their hand and stop it.

SVEN: We talked earlier about the economy and the special kinds of pressures that it puts on an organization. How would you recommend we respond?

KEITH: I think we've really got to pay attention to culture. Trust is the biggest issue in the world today. There has been a profound loss of trust in our markets, in our organizations, in our government, in our leaders. Every organization — even ones with great brands, like KPMG — has to pay attention to this.

At the end of the day, it's all about people. Yes, processes and programs are important, but there's no substitute for talking with people, understanding what they feel, think, and believe, and seeing how those things are reflected in organizational life.

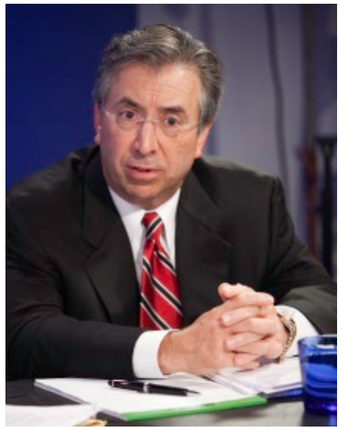
SVEN: How do you empower your employees to resist the pressures, do the right thing, and make the right judgments?

CANDY: At KPMG, we emphasize personal responsibility and accountability. And we help people understand that they are really setting the tone at our firm. You might not be the business unit leader, but by your actions you can be very influential and make a real impact on our culture.

Ethical Leadership

SVEN: Turning now to ethical leadership, what makes a strong ethical leader?

CANDY: I think it's someone who leads by example, who respects people's individuality, and who is not afraid to take on issues or problems. If there is something that needs to be addressed, the ethical leader is going to address it head-on. I have learned that problems don't go away, they just get bigger until they explode. A good leader will get on top of the problem and deal with it in a timely, consistent way.



"People have to understand that they're not just paid for performance. The manner in which you perform matters a great deal." — RICH GIRGENTI

SVEN: Steve, you've worked with many people in leadership roles. What do you see as the key characteristics of an ethical leader?

STEVE: The ethical leader has compassion, courage, and competence. Employees want to be treated with respect and recognized as the individuals they are. They expect an ethical leader to be compassionate.

Courage is not a fashionable word these days, but it's very relevant to this discussion. Courage for a businessperson is often found in smaller things, like disciplining employees or telling them where they need to improve. Most of us are uncomfortable doing that, but one of the primary jobs of a leader is to offer that coaching so the person has a chance to change before we have an explosive issue on our hands, as Candy said.

Third is competence. You can't be an ethical leader if you're not a good business leader. A leader has to set an example, and that includes doing your job correctly. You can be decent and courageous, but you won't be an effective leader if you're not also a solid performer.

KEITH: Warren Bennis, who's written prolifically on leadership, wrote about the myths of leadership some years ago, and I'm reminded of one of them — leaders are born, not made. This is not true. We can develop leadership skills, in part by tapping into our experiences and learning from the good leaders who have influenced us. Leaders are not necessarily charismatic either. Quite often a leader is humble and unassuming.

Everybody in an organization has the capacity to lead, even if it's just moments of leadership. One of our jobs as leaders is to nurture that ability in others.

SVEN: Following up on that, how do you bring out the best in employees? How do you recognize and reward them?

DONNA: If you want ethical leaders, you need to reward and recognize ethical leadership. You should offer incentives through the performance review process and through your compensation programs. But you should also utilize soft incentives. People want to be recognized, and you can do that in many sincere ways.

CANDY: One of the things that has meant the most to me has been a handwritten note from a supervisor or colleague. And so, I send handwritten notes to people who have gone above and beyond. And it's interesting — as I travel from office to office, I'll occasionally see one of those notes on someone's pegboard or wall, and you know it meant something to them.

SVEN: What advice would you give someone who is taking on a leadership role for the first time and wants to be an ethical leader?

STEVE: The first thing I would tell them is they don't get a pass. A leader has to be a person of integrity, first and foremost. I would also tell them to practice true, mindful empathy. Put yourself in someone else's shoes; you'll make better business and ethical decisions.

You also need to find a way to hold yourself accountable, and this is hard to do on your own. When we look in the mirror we usually see a younger, more handsome version of our true selves. We don't see ourselves objectively. And the higher up you go in an organization, the harder it is to find people who will tell you when you've done something wrong. At every phase of a career, you need to find someone who will point out your imperfections and hold you accountable.

"The ethical leader has compassion, courage, and competence." — STEVE PRIEST

Looking Ahead

SVEN: Now let's talk about emerging issues on the business ethics horizon. What's next?

DONNA: The risks and opportunities associated with technology will be important. Social networking sites like Facebook and Twitter can be constructive and support a culture, but they also add legal risks and concerns.

A second emerging issue is globalization and its impact on ethics and compliance issues. There is a kind of harmonization taking place — common global approaches to such issues as privacy and anti-bribery. We will see more common standards and approaches to enforcement.

KEITH: I would add something that's indicative of the times we're in now. Business ethics is evolving to include the notion of corporate accountability. We need to understand how our decisions as businesspeople are being received and impacted by all of our stakeholders. It's about stewardship, not just for our own organization but for our communities and our environment.

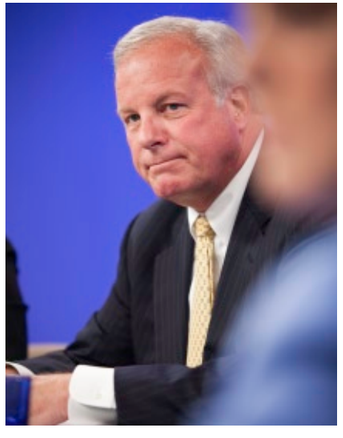
I'll go one step further and say that we need to recognize that we are living in a defining moment. I hear some saying we need to restore the status quo and go back to business as usual. We cannot and we must not. With everything that has happened in this financial crisis, I think we need to be having a new conversation about culture, leadership, and integrity. This is an opportunity to make a new commitment to values and begin to restore trust.

STEVE: Keith is right, the American public doesn't trust us at all. A recent Gallup survey said 12 percent of Americans believe that business executives are honest. That's a crisis.

So regardless of how some people feel about returning to the status quo, that's not going to happen. Businesses are going to have to respond to a much stricter and more extensive set of regulations driven by public opinion. And public accounting firms will be expected to help enforce these new regulations. I can't think of an organization in America that is going to be held to a higher standard than public accounting firms.

SVEN: Rich, you served on the board for five years and have made important contributions to our ethics and compliance program. What are the keys to keeping it going and continuously improving?

RICH: We have to remember the stakeholders to whom we owe an obligation. We certainly have an obligation to each other, and that means doing the right things in the right way. We have an obligation to the owners of the firm to make sure that this is a profitable business. We have an obligation to the capital markets and to the clients we serve. We have an obligation to the regulatory bodies that oversee this organization. At the end of the day, this is a service business, and that means we must be of service and uphold our obligations. ■



"With everything that has happened in this financial crisis, I think we need to be having a new conversation about culture, leadership, and integrity. This is an opportunity to make a new commitment to values and begin to restore trust."

— KEITH DARCY

Leading an Ethical Culture

Leadership Perspectives

A STRONG MORAL COMPASS

Jack Taylor, Executive Vice Chair, Operations

THE TWO MOST IMPORTANT ASSETS FOR A PROFESSIONAL SERVICES FIRM — OR ANY BUSINESS — ARE ITS PEOPLE AND ITS REPUTATION.

We know that our clients count on us to have professionals who not only have excellent skills and deep knowledge and experience, but who approach everything they do with the highest ethical standards.

So, from an operations perspective, we continue to put doing the right thing, in the right way, at the center of every decision. Our go-to-market strategy is premised on our commitment to Quality Growth, which means finding the right clients and providing them with the right services. We do this by building strong relationships in our communities, by making thought leadership around emergent professional and industry issues a priority, and by competing aggressively and fairly.

Additionally, we understand that how we spend our money speaks volumes about what we value as a firm. We ask our partners and employees to uphold their personal and professional responsibility to charge their time and expenses accurately, and we have been increasingly vigilant about monitoring compliance with firm policies in this area. We take great care with the vendor selection process to avoid real and perceived conflicts of interest. And as a firm, our Living Green initiative has reduced our carbon footprint while also saving us money, making it a huge win on many levels.

There are some who would say that it is easier to operate a business with integrity when economic times are good; that it is only when economic times become difficult or competition becomes too intense that ethical standards erode. At KPMG, we believe that when a business creates and fosters a culture that values and rewards ethical behavior at every level, that culture will endure even in the toughest of times. That's the model we've adopted and the one we actively and openly share with our clients, the profession, our suppliers, and the communities where we work and live.

THE HIGHEST ETHICAL AND PROFESSIONAL STANDARDS

Larry Leva, Vice Chair, Risk Management

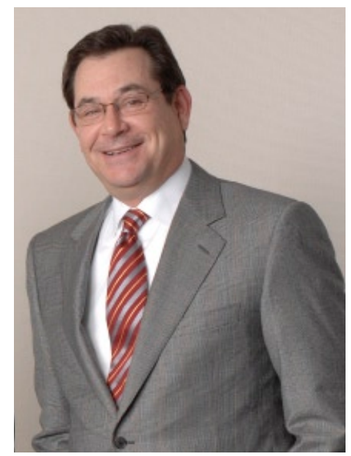
AT KPMG, RISK MANAGEMENT HELPS THE FIRM ACHIEVE ALL ITS STRATEGIC PRIORITIES, INCLUDING PROFESSIONALISM AND INTEGRITY, AND QUALITY GROWTH.

Risk Management oversees a system of quality control that helps us meet the highest ethical and professional standards and covers a number of key areas relating to our professional services, including: reviews of new service offerings; client acceptance and continuance; compliance with engagement and personal independence rules and other regulatory requirements; and engagement performance through our Quality Performance Reviews and "in-flight" engagement quality reviews, which take place while an engagement is in progress.

Through our reviews of new service offerings and oversight of the client acceptance and continuance process, Risk Management helps to ensure a key tenet of Quality Growth: Provide the right services to the right clients. We welcome new engagement opportunities, of course, but we think carefully before accepting them. Do we have the right people with the right skills and experience to provide a quality service on this engagement? Are we comfortable doing business with the client's senior management? Can we mitigate the engagement risk to an acceptable level?

With the deployment of our new Client Engagement and Acceptance System (CLEAS), we are able to evaluate new client and engagement opportunities more efficiently, while ensuring that the firm meets its professional obligations, including compliance with independence and regulatory requirements. CLEAS will make our professionals more productive and allow us to be even more responsive to the needs of our clients.

Our goal is to do business with companies that share our values. In the long run, this will help us grow our business profitably, enhance our brand, and attract the most talented, professional, and ethical people to our firm.



MEETING OUR PEOPLE'S EXPECTATIONS

Bruce Pfau, Vice Chair, Human Resources

AS A PUBLIC ACCOUNTING FIRM, KPMG'S SUCCESS HINGES ON THE TALENT, DEDICATION, AND PROFESSIONALISM OUR PEOPLE BRING TO THEIR WORK EVERY DAY.

Having a model ethics and compliance program is critical to this effort as it instills within our people a sense of pride that comes from knowing we strive to meet the highest ethical standards and that we always seek to do the right thing, in the right way.

KPMG's Human Resources (HR) organization works closely with leaders in the firm's Legal and Compliance structure to help develop policies, communicate the importance of ethics and compliance, and investigate instances when unethical behavior has been alleged. What's more, HR supports an ethical culture by developing initiatives that create a work environment where our people trust those around them and trust that the firm is working in a way that's consistent with their own high ethical standards.

We invest significant time, energy, and resources to make KPMG an Employer of Choice, and this includes many leading practices to instill and strengthen an ethical culture. For example, we conduct extensive screening to help ensure we hire people of character, and our performance management system includes specific professionalism and integrity goals against which our people are measured when it comes to decisions on salary adjustments and promotions. And we also ensure that ethics is a critical and required part of our training programs.

Simply put, KPMG sets high ethical standards, asks our people to live up to them, provides the tools and guidance to do so, and measures whether our people are meeting expectations in this area. Our people demand this from us. They want to — and do — feel a sense of pride in working for KPMG, and that pride is rooted in the strong ethical culture we have established.

Combined with our programs to drive career development, employee engagement, diversity and inclusion, and work/life balance, this focus on ethics and integrity makes KPMG a great place to work and a great place to build a career in the eyes of our people. ■

Leading an Ethical Culture

LEFT TO RIGHT: Scott Frew, Lynne Doughtie, Rick Smith

Management Review Panel

THE MANAGEMENT REVIEW PANEL (MRP) IS A CENTRAL COMPONENT OF THE FIRM'S ETHICS AND COMPLIANCE PROGRAM.

The primary functions of the MRP are to help ensure that appropriate remedial measures are implemented in response to substantiated instances of misconduct and to implement a system of fair and consistent treatment of individuals by the ethics and compliance program. To achieve these goals, leaders from several different operational functions in the firm, including Audit, Tax, and Advisory, meet regularly to review, among other things, investigations and remedial actions taken.

Here, three MRP members discuss the value of the panel to the firm's ethics and compliance program. Lynne Doughtie is National Managing Partner, Advisory; Scott Frew is National Partner in Charge — Inspections for Audit; Rick Smith is National Managing Partner, Tax.

How does the MRP help to ensure fairness in investigations and their resolution?

RICK: Firm leadership recognizes that, to have a model ethics and compliance program, we need to have an effective, consistent process for reviewing investigations and remediating confirmed instances of misconduct. The MRP does this by reviewing, on a firmwide basis, the types of misconduct that are investigated and the remedial actions taken when the reports are substantiated. This review provides each of the members of the MRP, including myself, Lynne, and Scott, with a foundation upon which to evaluate investigations that affect the people in our own functions and to guide others in the field in making judgments about appropriate remedial measures.

It also gives the MRP the ability to recognize areas that may require additional training or guidance. If we see this, the MRP makes recommendations to the Quarterly Training Summit or the Legal and Compliance Committee to develop policies or training that may help our partners and employees better understand the expectations of the firm.

What makes the MRP a leading practice?

SCOTT: In an organization with more than 20,000 people, it's a challenge to ensure consistency without slowing down the process. Obviously, we can't wait for a formal meeting of the MRP to determine the appropriate remedial action for every case. And having a formal committee actually imposing discipline would not be consistent with KPMG's goal of having every individual take personal responsibility for the ethical culture of the firm. Instead, local leadership and performance managers need to drive that process in most cases.

So, I think that KPMG balances the need for consistency and personal responsibility in a very unique way by having the individuals who are most knowledgeable about the ethics and compliance matters across the firm use that knowledge to inform the decisions of local leadership and performance managers throughout the firm.

LYNNE: I think our ability to handle matters in real time in this way is very important. Members of the MRP are kept aware of all of the pending cases in our functions in a number of ways. When reports of significant matters are substantiated, we work with the individuals in the field and other members of the MRP to ensure that the action taken in response to the investigation is consistent with the action taken in similar cases elsewhere in the firm.

SCOTT: And in that regard, we're always seeking continuous improvement; we try to gather feedback that will help us make improvements to our investigative processes. Ensuring the most fair and expedient outcomes is our priority.

Why is it important that partners in operational management participate on the panel?

LYNNE: That's essential, because we're the ones who ultimately are responsible for resolving the ethics and compliance matters that affect the people in our respective functions.

SCOTT: Having been in operations for a long time, you're able to bring empathy to the deliberations and the decisions that are being made. You've been in the field, you understand the challenges that your colleagues are facing.

How does the panel accommodate and resolve the range of matters that come up?

SCOTT: It's very helpful that we operate both formally and informally. The formal meetings keep us focused on all the matters over which we have responsibility and give us the information we need. But by working informally we can handle matters as they come up, which is critical. If someone is going through one of these matters, it's affecting his or her work life and personal life; it's very important that we address it as quickly as possible.

RICK: One of the most important things about the panel is that it allows us to collaborate closely with our colleagues in the Ethics and Compliance Group, the Office of General Counsel, Human Resources, and others. It makes resolving matters a coordinated effort. And when we need to seek insight, counsel, and advice, there's a real sense of collaboration among us. So when we're faced with a particularly difficult issue, we're able to pull together, come to a consensus, and try to arrive at an outcome that is measured, fair, and appropriate for the whole firm.

What is your biggest challenge in serving on this panel?

SCOTT: When a partner or employee is going through the process, what they want is swiftness and certainty. But it can be difficult to deliver that when you're also trying to be as thorough as possible.

LYNNE: This brings us back to Scott's comment about empathy. I think it's important for everybody to know that we invest a great deal of time and energy in carrying out our responsibilities in this area. Resolving ethics and compliance matters can involve very difficult decisions, and we don't make those decisions lightly. If we are somewhat deliberate in how we approach these matters, it's only because we are trying to ensure that the outcome is fair for the people involved, and for KPMG.

RICK: The challenge, very often, is balancing speed with getting to the best resolution.

What advice can you offer to people who wish to raise issues or concerns? What are some of the lessons you've learned from serving on the panel?

RICK: Everybody should feel empowered to raise issues that make them uncomfortable, and that means using the channels available to them, whether it's a local or national resource.

LYNNE: I've learned that we have a strong culture that encourages communication, discussion, and self-examination. We can and should be transparent about anything we feel is not in accordance with our core values or policies. ■

The Ethics and Compliance Program

Tom DiLeonardo *Chief Compliance Officer*

KPMG HAS WORKED HARD TO CREATE AN ETHICS AND COMPLIANCE PROGRAM THAT IS A MODEL FOR THE PROFESSION. BUT WHAT MAKES IT WORK EFFECTIVELY? TOM DILEONARDO, KPMG'S CHIEF COMPLIANCE OFFICER, GIVES US HIS VIEW ON THE PROGRAM'S LEADING PRACTICES.

KPMG emphasizes each individual's responsibility to raise his or her hand when they see something that isn't right. What does KPMG do to help individuals report potential misconduct?

The reporting of concerns is not only important, but it's also essential to any compliance program. To encourage a "raise your hand" culture, an organization must have multiple channels of communication, including an anonymous reporting mechanism like KPMG's Ethics and Compliance Hotline. Additionally, KPMG's Code of Conduct lays out, in plain English, the firm's expectations of its people — not only with regard to reporting (where we provide several potential channels of communication), but also with regard to how our people should conduct themselves generally. If people can clearly understand what is expected of them, they are more likely to recognize potential misconduct by others and feel comfortable reporting it.

Additionally, KPMG strives, through initiatives such as our retaliation monitoring program, to build trust with our partners and employees. If our people believe that the firm will support them when they report a concern in good faith, they are more likely to raise concerns through the hotline or one of our other channels.

When someone raises a concern through the hotline, he or she may choose to report confidentially or anonymously. What is the difference?

All reports are treated confidentially, to the extent allowed by law, so every reporter can feel comfortable that their name is being protected. But anonymous reporters don't provide their name or any identifying information, while confidential reporters do. Obviously we can contact confidential reporters directly, since we know who they are. We encourage anonymous reporters to call in or log on to the hotline regularly to check their reports, and we provide them with a confidential report key that allows them to do so while maintaining their anonymity. Investigators may have questions or need additional information. With anonymous reporters, we can even schedule anonymous webchats, if necessary, to ask questions in real time. If the anonymous reporter stays actively engaged in the case, we usually are able to undertake a thorough and complete investigation no different than if the reporter had provided his or her name — and that's the best outcome for everyone.

The firm has gone to great lengths to establish effective oversight of our incident reporting and investigation processes. Can you describe how this leading practice is achieved at the firm?

We have taken several important steps. Each and every report, investigation, outcome, and disciplinary measure is overseen by several oversight bodies and individual firm leaders. The Legal and Compliance Committee provides management oversight of all open and closed investigations, and reports made to the Professional Practice, Ethics and Compliance Committee (PPECC) of the board of directors provide the board with a line of sight into the same. We also meet regularly with the firm's Chairman, Chief Executive Officer, and the Chair of the PPECC to review investigations and outcomes.

How does the firm go about making sure that any discipline imposed for substantiated allegations is consistent across the firm, across functions, and across levels of seniority?

The individuals investigating reports, whether they are from the Ethics and Compliance Group (E&C Group), the Office of General Counsel, Firmwide Security, Human Resources, or the Office of the Ombudsman, do not determine discipline for those individuals found to have violated law or policy, or who have otherwise acted in a manner outside the firm's core values. Instead, the firm strives to instill personal responsibility for the resolution of ethics and compliance matters by making supervisors accountable for determining discipline. This also tends to allow the discipline imposed to have a more lasting impression on the individual. When you are held accountable by those who manage your career, it drives home, in a tangible way, that your future at KPMG depends on your integrity and choices.

In significant matters, KPMG strives to ensure that discipline is consistent by having supervisors consult with members of the firm's Management Review Panel (MRP), a group of individuals who are knowledgeable about all discipline imposed across the firm, to determine if the discipline that the supervisor is imposing is consistent with past practice. I am on the MRP, as are the National Managing Partners for Tax and Advisory, the National Partner-in-Charge — Inspections for Audit, and our Vice Chair of Human Resources.

Can you describe how ethics and compliance is linked to career advancement?

The E&C Group contributes to the firm's due diligence reviews to help ensure that those selected for key promotions are good role models and are living the firm's core values. This review includes assessing whether the candidate has fulfilled in a timely way his or her requirements regarding CPE credits, mandatory firm training, licensing, and independence, among other things.

But it's not just key promotions. Ethics and compliance has been integrated into other aspects of the performance management process, which speaks volumes about the firm's strong commitment to build and maintain a model ethics and compliance program. There are pre-populated ethics and compliance goals in our performance management system for every individual in the firm. In addition, PML training and tools include guidance on how to review and reinforce key ethics and compliance areas as part of the interim and year-end review processes. And, there are questions in the upward feedback surveys about acting with ethics and integrity, along with suggested resources so that those who manage others are aware of their own strengths and weaknesses and have the opportunity to improve. All of this results in us being able to draw a straight line between the firm's core values and how we reward our partners and employees, which in turn has a positive impact on our ethical culture. ■

Use the Ethics Checklist

When making decisions or following a directive, ask yourself:

- Does my action comply with the spirit and letter of the law?
- Is my behavior consistent with KPMG's core values, and ethical and professional standards?
- Does my decision reflect the right thing to do?
- Is my decision being driven by responsible professional judgment?
- Would I feel confident that I could explain my decision if it were made public?

The Ethics and Compliance Program

Vicki Sweeney *Principal-in-Charge, Ethics and Compliance*

KPMG HAS HAD AN ETHICS AND COMPLIANCE HOTLINE SINCE 2004, LOGGING SOME 900 REPORTS VIA THE PHONE AND THE WEB. WE TALKED WITH VICKI SWEENEY, PRINCIPAL-IN-CHARGE OF ETHICS AND COMPLIANCE, TO HELP US BETTER UNDERSTAND THE TRENDS THAT EMANATE FROM THESE REPORTS AND WHAT THAT DATA REVEALS ABOUT OUR FIRM'S CULTURE.

KPMG tracks a number of hotline metrics, based on the total number of hotline reports filed each year. What are the significant data points and why are they important?

One significant data point is the percentage of reports filed anonymously, which sits around the 50-percent mark and is in line with the average for organizations of our size. As we work to increase awareness and trust in our ethics and compliance program and increase transparency around the reporting process, our goal is to increase the percentage of reports filed confidentially.

With increased confidential reporting, reporters feel comfortable giving their name, and there's less of a chance that a significant issue will fall between the cracks. Every year, we have a handful of cases that cannot be fully investigated because they are filed anonymously and the reporter does not provide enough information to make the report actionable. If we know the identity of the reporter, we can contact him or her directly with questions to help ensure a thorough investigation.

We also evaluate the types of reports we receive, including Human Resources (HR) issues, professional practice issues, and firm policy issues, such as accuracy of firm records. Monitoring this key metric led us to make a few important revisions around how we categorize the most common report topics. We updated them to reflect the leading practice and now have the ability to compare our overall results against other organizations, both within and outside our profession. When we find significant differences, we can often highlight where we are doing something that's more effective.

With five years of hotline data to analyze, have you been able to identify trends or find hot spots that might indicate something bigger than just the issues raised in individual hotline reports?

At the moment, we are looking at the level of reporting across various locations, including cities, functions, and departments. It's also important that we interpret the data based on the number of employees in a location or function. With a baseline established, we can then add other data points, such as survey results and turnover data, to determine if there may be issues in a particular location.

If we believe that the data, such as a high report volume, indicates that there may be issues at a particular location, we look for reasons. The reasons are important, both for their immediate implications at that location and because we are able to draw wider conclusions that help inform training, communication, and firm policy.

On the other hand, a low report volume might also lead us to conclude that our channels of communication are not functioning as effectively in a given city or department. We'd then do more research to find out why. Perhaps there were recent changes in leadership and employees are still building relationships; perhaps the local HR professional is shared across several locations and is not always on site to help resolve issues.

We know from our internal surveys that a majority of people feel most comfortable raising issues to someone they know, and generally that person is their direct manager or partner. When they choose another route, there is usually a good reason why. By digging into the trends in hotline data, those reasons become more apparent. Then, when we look across all locations, we can present wider conclusions to management, the board, and our business leaders in an effort to continually improve our ethics and compliance program.

KPMG encourages people who feel they may have been subject to retaliation after raising a concern to report the potentially retaliatory behavior. What does the firm do to protect partners and employees who raise their hands?

Our policy is clear: KPMG prohibits retaliation for good-faith reporting, and we have implemented a proactive monitoring program for those individuals who raise issues confidentially through the hotline, Ombudsman, or the Ethics and Compliance Group, and that we know may be at risk for retaliation. Some people may not even realize that we are monitoring them on their behalf.

For example, someone who raises a concern about a supervisor has a greater risk of being subject to retaliation than someone who raises a concern about a person more junior because the supervisor's decisions can directly impact the individual's career. We monitor a variety of data points related to the individual's performance at the firm, following up when necessary to determine whether an individual may have been subject to retaliation. We also extend the monitoring to witnesses and others involved in an investigation if we believe they may also be at risk of retaliation.

If we find evidence of retaliation or if an individual files a report of retaliation, we conduct a comprehensive investigation. We terminate people for retaliation, and that sends a clear message that we have zero tolerance for that type of conduct.

We have a strong monitoring process, and we can feel very proud of our leadership role in this area. ■

Raise Your Hand: Personnel Compliance Program Statistics at a Glance

INCIDENT REPORTS

Between October 1, 2008, and September 30, 2009, the firm received 443 reports through its established channels of communication, including the Ethics and Compliance Hotline (both Web and phone options), the Ombudsman, the Ethics and Compliance Group, the Office of General Counsel, Human Resources, leadership, and others. These reports were investigated by various firm resources, under the supervision of the Chief Compliance Officer.

- 50 percent of the reports made through the firm's hotline or directly to the Ombudsman or Ethics and Compliance Group were made anonymously.
- 7 percent of the reports made through all channels could not be investigated because the reporter did not provide enough information in the report and did not respond to requests for additional information.

ISSUES RAISED

Between October 1, 2008, and September 30, 2009, the following were the top five issues raised in the reports received (note that reports can involve more than one issue):

1. Lack of Professionalism
2. Adverse Finding on a Background Investigation
3. Other Violation of HR Policy / Procedure
4. Improper Charging of Time
5. Unfair Performance Criticism

RESOLUTIONS

Between October 1, 2008, and September 30, 2009, 42 percent of the issues raised were substantiated. The following are the top resolutions for substantiated issues:

- 194 individuals received counseling, verbal reprimands, or written reprimands
- 41 individuals were separated from the firm (terminations and resignations)
- 22 individuals had new hire offers rescinded
- 12 individuals received training

Partnering with Human Resources

EVERYONE AT KPMG UNDERSTANDS THE IMPORTANCE OF ETHICS AND COMPLIANCE. WE KNOW WE MUST DO THE RIGHT THING, IN THE RIGHT WAY, FOR OUR PEOPLE, FOR OUR CLIENTS, AND FOR THE CAPITAL MARKETS WE SERVE. BUT HOW IS THIS MESSAGE CONVEYED AND INSTILLED AT THE FIRM? HOW IS ETHICS AND COMPLIANCE INTEGRATED INTO OUR DAY-TO-DAY WORK LIVES? AND HOW IS IT MADE "REAL" AND RELEVANT THROUGHOUT OUR CAREERS?

The answer is, ethics and compliance at KPMG is a highly collaborative effort, in which numerous departments and individuals share responsibility for program implementation and communications. The partnership between the Ethics and Compliance Group (E&C Group) and Human Resources (HR) is vital, because HR has an ongoing working relationship with everyone at the firm and has an opportunity to communicate and reinforce values of professionalism and integrity in every KPMG partner or employee throughout their careers with the organization.

"As our ethics and compliance program has evolved, our team has developed a close working relationship with the Ethics and Compliance Group," says Bruce Pfau, Vice Chair, Human Resources. "Research shows that a strong, ethical culture contributes to employee satisfaction and retention. We want to do everything we can to strengthen that culture, foster employee satisfaction and pride, and contribute to the overall success of the organization."

Setting the Tone

Members of HR help to communicate the ethics and compliance message even before a person joins KPMG. HR uses every interview, whether on campus or with experienced candidates, as a first opportunity to set the tone and convey what it means to be part of KPMG. HR also helps ensure that candidates for employment are evaluated on their commitment to ethics and professionalism.

The communications process continues immediately after a candidate agrees to join the firm. With every offer letter sent by HR, new partners and employees receive the Code of Conduct and are asked to review it and confirm that they will comply. On their first day of orientation, new hires receive training about our Code, the ethics and compliance resources available to them, and the behavior we expect, including the responsibility to "raise your hand" if one sees behavior not consistent with KPMG's values.

In the first month of employment, KPMG personnel are required to complete a number of Web-based training programs that guide them on how to do the right thing, in the right way. Thereafter, the firm reaches out at other key touchpoints by integrating ethics and compliance messages into milestone training events, for example. All of our leadership development programs include ethics and compliance components.

Career Management

But the HR-E&C partnership is not just about communications and touchpoints. HR helps to ensure that ethics and compliance is inextricably linked with career and performance management, ensuring that a good record in ethics and compliance is good for one's career.

KPMG's primary performance management system, Dialogue, contains ethics and compliance goals upon which everyone is evaluated. There is a core set of goals for all KPMG people; a broader set of goals for those who manage others; and a set of goals specifically for Office Managing Partners because of their "tone-at-the-top" responsibilities.

In addition, HR and the E&C Group created an online personnel file that contains key personnel data such as title, location, and performance ratings, as well as any documents related to ethics or disciplinary actions. This tool is used during ethics investigations and at key promotion times, providing HR and performance managers all the information they need to make personnel decisions in line with the firm's core values.

Doug Daniels

Director, Human Resources, Midwest Area

I STARTED MY CAREER 20 YEARS AGO as an auditor with another Big Four firm before moving into Human Resources (HR). My client service background provides some meaningful perspective on the environment in which our people work and the challenges they face every day in the field.

I view HR as a critical link between our people in the field and the Ethics and Compliance Group (E&C Group). When someone comes to me with a complaint or concern, I first ask myself: Has there been a potential violation of law, a departure from firm policy, or a threat to personal safety? If so, it's my responsibility to contact the E&C Group, the Office of General Counsel (OGC), or Firm Security immediately.

If the issue involves behavioral concerns or inappropriate conduct requiring further investigation, I gather the facts and create a case within the Issue and Event Management system, which tracks the investigation through its conclusion and essentially ensures that no investigation goes unresolved. This helps to build the credibility of the program with our people and, most importantly, ensures that anyone filing a report will have their voice heard. We should feel good about having a process in place that supports and reinforces our core values.

When I'm dealing with a particularly difficult issue, I don't hesitate to pick up the phone and call someone in the E&C Group or OGC. I'm a big believer in proactive consultation — in our business, we're all about asking questions and sharing experiences. The professionals in E&C and OGC have the deepest knowledge of law and firm policy, as well as a broader view of how investigations are being handled across the firm. I think the collaborative relationship between the E&C Group, HR, and OGC helps us collectively resolve ethics- and compliance-related issues in the most fair and consistent way — and with the best interests of our people at heart.

Compliance Monitoring

The Compliance Profile system is another tool supporting both ethics and compliance and career management objectives. The system monitors individual compliance with mandatory firm requirements and is linked to the online personnel file. HR and the E&C Group follow up with people who are at risk for missing deadlines, and this information is reported to performance managers and noted in Dialogue. This way, compliance is part of everyone's performance record and is a factor when someone is considered for advancement. ■

Ethics and Compliance Training

The Quarterly Training Summit

When key members of KPMG's training organization gathered for the first Training Summit in April 2007, they had one goal in mind: to make ethics and compliance an integral part of every training curriculum throughout the firm so that everyone would have a clear understanding of what's expected of them as they face challenges on the job. The Quarterly Training Summit (QTS) is a dynamic forum in which representatives from the firm's Audit, Tax, and Advisory practices, the Center for Learning and Development, and Human Resources regularly collaborate with firm leadership to continue making this goal a reality.

LEFT TO RIGHT: Carol McCoy, Tina Kelly, Eileen Walsh, and Phil Sollecito

"Ethics and Compliance is one of our critical stakeholders. That direct tie is essential to better understanding what our professionals need to know and when they need to know it."

— EILEEN WALSH

In addition to making sure consistent messages about ethical culture permeate the firm, QTS participants continuously track and monitor where and when such messages are being delivered in firm training. Together with the support of the Ethics and Compliance Group (E&C Group), QTS participants who are responsible for all of the training at KPMG have become the firm's ethics and compliance advocates.

"Ethics and Compliance is one of our critical stakeholders," says Partner Eileen Walsh, who heads Audit Learning and Development. "That direct tie is essential to better understanding what our professionals need to know and when they need to know it."

A Leading Practice

The Summit has become a leading practice in the accounting profession — a successful partnership between ethics and compliance and training that delivers consistent messaging and strengthens the firm's ethical culture. "It helps us keep our finger on the pulse of ethical issues at the firm and then turn them into teachable opportunities," says Phil Sollecito, Executive Director, Human Resources.

"We know that people see their supervisors as role models for ethical behavior," he says. "And we know an organization thrives when employees feel confident about the ethical behavior of their supervisors, their leaders, and their organization." In fact, surveys show that employees who have this level of confidence feel less pressure to compromise their own ethics.

Catalyst for New Training

Through the QTS, the firm has developed a number of ethics and compliance training programs. For example, after Sven Erik Holmes, Executive Vice Chair, Legal and Compliance, conducted a series of focus groups across the firm to understand who KPMG people turn to when they wish to raise a concern or issue, he learned that early-career professionals often consider the senior associate on their engagements to be their consult of choice. From there, role model training for all third- and fourth-year seniors was born.

Audit, Tax, and Advisory training teams brainstormed with the E&C Group to build training that would help to mold these young professionals into role models. In the Tax practice, the materials were embedded in the new senior associate training. Advisory placed it in staff risk management training. Audit integrated the training into its in-charge auditor and advanced-in-charge program.

"People have begun to look at ethics and compliance through the same lens as their technical learning experience," says Partner Carol McCoy, who leads the firm's Tax training efforts. "We're not just teaching technical rules but also what is right about those rules. QTS provides a window into leading practices throughout the firm and helps us synthesize our technical training with ethics and compliance."

Case in point: Most of the attendees at the firm's Tax Management Seminar are Washington National Tax professionals or service line leaders working in specific practice areas such as Mergers & Acquisitions, International Executive Services, and State and Local Tax. The Tax training team worked closely with the E&C Group

"There's undeniable value in leveraging what others are doing."

— CAROL McCOY

to develop an online training tool called "The Instructor Lounge," which provides instructors with materials to discuss ethical decision-making using scenarios that include technical knowledge and difficult client interactions.

"There's undeniable value in leveraging what others are doing," McCoy explains. "We've now built ethical scenarios into our Tax Skills Seminars. Those scenarios deal with an actual technical issue and showcase the ethical component of the issue."

New Connections, New Training

The QTS also has become an important networking and relationship-building opportunity for attendees. For example, when the firm wanted to provide additional training to Audit partners and managers on a section of the Securities and Exchange Act relating to possible illegal acts by clients, the Office of General Counsel developed the training content but worked, through the QTS, with the Audit training team to embed the content into the Audit Partner-Manager Training curriculum.

Ultimately, the great benefit of the QTS is learning firsthand about which ethical topics are "top-of-mind" at the firm, says Tina Kelly, Partner-in-Charge of Advisory Learning and Development. For example, the QTS made Advisory more aware of data protection, an emerging issue. "Because so much of what we do in Advisory deals with client information, we quickly built specific discussions around the importance of protecting Personally Identifiable Information directly into our training," she says. ■

Mutual Respect: KPMG and the Coast Guard

What do KPMG and the U.S. Coast Guard have in common when it comes to values and ethics? Quite a lot.

That is what Partner Tom Duffy quickly discovered when he presented a session on ethics at KPMG to a group of graduating cadets at the U.S. Coast Guard Academy in Groton, Connecticut.

"When I spoke of having an ethical compass when making difficult business decisions, the cadets proudly explained how their core values of honor, respect, and devotion to duty guide their daily actions," says Duffy. "It was striking to learn how these cadets draw upon the same values as our KPMG partners and employees when faced with tough choices, even though our respective worlds are very different."

Another cornerstone of KPMG's ethics and compliance program that strongly resonated with the young cadets was the firm's emphasis on individual responsibilities such as leading by example, standing firm, and raising your hand when something is wrong. Duffy says, "When I explained that KPMG is an organization with mechanisms to support its people and to ensure wrongdoing is effectively dealt with, they described the avenues available for them to get help and support within the Coast Guard."

The interchange was a powerful one: It illustrated how organizations with different goals can be built on similar values of settling for nothing less than excellence and integrity.

"The goal was to connect ethics with how we do business at KPMG," Tom says. "Going into the conversation, the cadets thought their military training created a stronger code than in the business world. This showed them that ethics is central to the success of every mission — military or otherwise."

Ethics Cases

CHARGING TIME

A report came into Human Resources alleging that a professional had been inflating the total number of hours billed to a client at the end of each billing cycle and did not reconcile the actual hours reported in the Work in Progress (WIP) Report.

An investigation by the Office of the Ombudsman found that the professional exhibited a pattern of disregard for certain billing procedures and firm policies and that this misconduct resulted in an over-billing to the client. Further, it was determined that the professional manipulated engagement charge codes on several engagements by, among other things, transferring time between engagements to avoid taking a loss or to minimize the loss on certain contracts.

The investigation determined that the professional violated firm policy, acted in a manner inconsistent with the Code of Conduct, and was not fully cooperative during the investigation. After reviewing this matter, firm and area functional leadership determined that the professional should be separated from the firm. The client was reimbursed for the amount that was improperly billed.

KPMG's Code of Conduct provides that KPMG partners and employees must charge all time and expenses incurred to the appropriate engagement or internal charge code, no more and no less, and the firm's core values include being open and honest and acting with integrity at all times. Managing budgets or contracts through inaccurate time or expense recording, whether or not the time is charged through to the client, and not being fully cooperative during an investigation violate the Code of Conduct and can lead to serious sanctions, up to and including separation.

CONTRACT MANAGEMENT

An individual contacted firm leadership raising concerns about a possible violation of the firm's client engagement and set-up policies.

The investigation by the Office of the Ombudsman revealed that a professional authorized the start of work on a new client engagement before getting formal engagement approval. The professional then instructed the engagement team to charge hours and expenses to a pre-existing project code for another client pending approval of the new engagement.

The findings of the investigation were communicated to firm and area functional leadership, who determined that the professional should receive a significant reduction in compensation, a written reprimand, and additional engagement review procedures.

Among other things, firm policy, as set forth in the *Risk Management Manual*, requires an evaluation of each prospective client prior to accepting an engagement or performing any work. This evaluation seeks to identify any potential conflicts of interest or independence concerns and to determine the legal, professional, regulatory, ethical, and financial risks that may result from providing services to the client. It is imperative that firm professionals follow all applicable client engagement and set-up procedures. Failure to do so not only puts the firm at risk but also can lead to disciplinary action.

EXPENSE REIMBURSEMENT

A report was filed with the Ethics and Compliance Group alleging a professional's improper personal use of a firm-issued credit card, submission of duplicate and inaccurate expenses, and late payment of credit card balances.

An investigation by the Ethics and Compliance Group revealed that the professional had used a firm-issued credit card to charge a significant number of personal items over a three-year period. The investigation also confirmed that the professional was carrying a substantial unpaid credit card balance as a result of the personal expenditures. In addition, it was determined that the professional had repeatedly submitted duplicate and inaccurate expense receipts for reimbursement by the firm in an effort to pay, at least in part, for the personal charges.

Although none of the firm's clients was billed for these expenses, the firm's Expense Reimbursement policy had been violated. The professional was separated from KPMG and was required to reimburse the firm.

KPMG policy, which can be found on the Policy Center Web site, provides that firm-issued credit cards must be used only for business-related expenses, and all expenses should be appropriate and reasonable based on the circumstances. Personal expenses should never be charged to firm-issued credit cards, submitted to the firm for reimbursement, or billed to clients. Failure to follow KPMG's expense policies will result in discipline up to and including separation from the firm.

(continuted on next page)

(Ethics Cases continued)

INAPPROPRIATE WORKPLACE BEHAVIOR

Issues regarding inappropriate behavior in the workplace are reported through the hotline, Human Resources, and other channels of communication. Here are some examples of those reported matters:

- A Human Resources investigation into a report received from the National Service Center (NSC) resulted in a professional receiving a written reprimand for using profanity and other unprofessional conduct while requesting computer-related assistance from an NSC representative.
- Human Resources received a report that a professional was acting inappropriately toward engagement team members by yelling and asking invasive questions. An investigation confirmed the allegations. As a result, firm and area functional leadership demoted the professional to a position with no performance management duties and reduced the professional's annual performance rating for the purposes of determining compensation.
- A hotline report was filed alleging business integrity issues, such as over-stating credentials to a client, about a professional. Additional concerns of unprofessional conduct, such as demeaning team members, were raised by other reporters shortly thereafter. An investigation by the Ethics and Compliance Group substantiated the allegations. Firm and area functional leadership demoted the professional, issued a written reprimand, appointed a coach, and reduced the professional's annual performance rating for the purposes of determining compensation.
- A young professional contacted her Office Managing Partner (OMP) to report that a contractor had acted inappropriately toward her. Specifically, the contractor, who was providing professional services to the firm, sent her suggestive e-mails from his personal e-mail account. The OMP contacted firm leadership, and the contractor was sanctioned and removed from the office. KPMG informed the contractor's supervisor of the inappropriate conduct, and the OMP made clear to the professional that she did the right thing in reporting the matter.

As set forth in the Code of Conduct, KPMG is committed to treating everyone with respect and dignity and to providing a workplace that is free of harassment. Inappropriate comments and unwanted sexual advances, whether made by firm personnel or outside vendors, will not be tolerated.

INDEPENDENCE

In fiscal year 2009, the firm conducted more than 500 independence audits of partners and employees of the firm. Most professionals are selected for audits on a random basis. Here are some examples:

- An independence audit by the Ethics and Compliance Group found that a professional had 17 investments not reported in the KPMG Independence Compliance System (KICS), eight of which were restricted entities.

  The audit found that the professional had not accessed KICS for a number of years and had violated firm policy by failing to report investments in a timely manner. The results of the audit were communicated to the professional, along with a request for a response as to how the current violations would be cured and future violations prevented.

  The Management Review Panel reviewed the findings and, although none of the firm's policy violations resulted in a violation of the Securities and Exchange Commission's (SEC) independence rules, the panel imposed a significant monetary penalty. A disciplinary letter was sent to the professional, with copies to his People Management Leader (PML), Office Managing Partner (OMP), and Area Managing Partner (AMP). The professional also was required to take a three-hour independence training course and is subject to a re-audit in the next audit cycle.
- An independence audit by the Ethics and Compliance Group found that a professional had 49 investments that were not reported in KICS, seven of which were restricted entities. The professional had also failed to dispose of a newly restricted entity within five business days, as required by firm policy.

  Some of the restricted entities were underlying investments in variable annuities, and the other investments were owned by the professional's spouse. The Management Review Panel reviewed the findings and determined that the professional had violated firm policy by, among other things, failing to check if investments were restricted prior to purchase and failing to report all investments in KICS in a timely manner. Although none of the firm policy violations resulted in a violation of the SEC's independence rules, the panel imposed a significant monetary penalty, and a disciplinary letter was sent to the professional, with copies to the PML, OMP, and AMP. The professional also was required to take a three-hour training course and is subject to a re-audit in the next audit cycle.

All firm personnel should be familiar with Chapter 12 of the *Risk Management Manual*, which sets forth the firm's policies related to independence. Firm policy, which is more restrictive than the SEC's independence rules, requires that potential investments be reviewed against the firm's list of restricted entities prior to making an investment. All new investments and sales must be reported in the firm's KICS within 14 days of purchase or sale date, including underlying investments in variable annuities and the investments of an individual's immediate family members. The firm's Management Review Panel reviews all violations of KPMG's independence policies to determine discipline and ensure that it is consistent across the firm.

COMPROMISING CLIENT DATA

The Chief Compliance Officer received a report about a professional working on a client engagement who may have compromised client data by taking an electronic media storage device (USB drive) from the client facility without authorization.

One USB drive was authorized for use on this engagement. However, it was fingerprint-encrypted, and it was to remain at all times in the secure engagement workroom located in the client facility.

At some point during the engagement, the USB drive could not be located by the engagement team members, and a search for the drive commenced. Shortly thereafter, a professional reported that the USB drive was in her possession and that she may have placed it in her purse when she was last at the client site several days earlier.

An investigation by the Office of General Counsel determined that the professional had, on several occasions, connected the USB drive to her firm-issued laptop during the timeframe in which the device had been missing. The investigation concluded that the professional violated firm policy by transporting the USB drive from the secure client facility and attempting to impede the investigation by providing a false statement. The findings of the investigation were communicated to firm and area leadership, who determined that the professional should be separated from the firm. The firm was able to determine that the USB drive did not contain classified data, and notified the client accordingly.

Firm policy, which can be found on the Policy Center Web site, generally precludes the use of removable electronic media devices, such as USB drives for the storage of client data (even where such devices are used to share client data between engagement team members). In all cases, whether e-mail or external media is used for the transfer of confidential information, and depending on the nature of information being transferred, the expectations of the client, and applicable legal requirements, the use of current firm-approved encryption methods should be considered. In the limited circumstances where such devices are authorized, the consequences for violating the policies regarding their use and security can be severe.

Additionally, the firm's core values include being open and honest and acting with integrity at all times. The firm expects that its partners and employees will be fully cooperative and candid during an investigation. Failure to do so will result in discipline. ■

Compliance Testing

COMPLYING FULLY WITH LAWS, REGULATIONS, AND FIRM POLICIES IS CRITICAL TO MAINTAINING A MODEL ETHICS AND COMPLIANCE PROGRAM. IN ORDER TO DEMONSTRATE AND DOCUMENT OUR COMMITMENT TO COMPLIANCE, WE PERFORM AUDIT TESTING THROUGHOUT THE YEAR. THE FOLLOWING FOUR PAGES FEATURE HIGHLIGHTS OF OUR COMPLIANCE TESTING AND INITIATIVES.

Independence Audit Testing and Compliance

The Ethics and Compliance Independence Audit team helps to ensure compliance with Securities and Exchange Commission independence rules and firm policy by conducting independence audits of the financial affairs of partners and employees who are subject to those requirements.

Currently, the firm performs a minimum of 500 independence audits per year. During the first three quarters of fiscal year 2009, 313 audits were completed.

The Management Review Panel meets quarterly to review the results of both the independence audits and self-reported independence violations. In the first three quarters of fiscal year 2009, the Management Review Panel imposed disciplinary measures on 131 partners and employees who were found to have violated the firm's independence policies.

The most common violations of firm policy include:

- Investments not entered into the KPMG Independence Compliance System (KICS) or not entered within 14 days;
- A loan with a restricted entity; and
- Purchasing stock in an entity without obtaining conclusive evidence that the entity is not restricted.

In addition, the most common covered-person violations include:

- Overdraft lines of credit;
- Savings/checking account balances exceeding the Federal Deposit Insurance Corporation limit; and
- Originating an insurance policy or making changes to an otherwise grandfathered policy.

The Ethics and Compliance Group (E&C Group) also performs monthly audit testing of approximately 35 randomly selected engagements across all practices and regions to confirm that all client and engagement acceptance policies and procedures are being followed and completed in a timely manner. Test results are shared with engagement teams and functional leadership.

Due Diligence Reviews

The E&C Group conducts due diligence reviews in advance of all leadership appointments and partner promotions and, upon request, for managing directors and People Management Leaders (PMLs), as well as other reviews, as necessary.

Melissa Howell

Manager, Human Resources, Midwest Area

BEYOND PARTICIPATING IN ETHICS AND COMPLIANCE INVESTIGATIONS, our Area Human Resources (HR) teams play an important role in educating our employees about KPMG's core values, our Code of Conduct, the Ethics and Compliance Hotline, and our other channels of communication. A large amount of Ethics and Compliance content is embedded in our HR initiatives, and when I lead a training course I always address the seven core values of the firm.

In the business unit I support, I facilitate our performance management training. Career development and ethics and compliance are tightly linked at KPMG, and we emphasize the importance of professionalism and integrity when evaluating an individual's performance and potential for advancement. By doing so, we're sending a message to our people that we expect acting with ethics and integrity to be just as important as achieving business results.

As an HR professional, I try at all times to lead by example and demonstrate to others the behavior we expect from our people. I've taken a personal interest in the ethics and integrity of KPMG, and my goal is to instill that in all the employees I work with.

As part of this process, the E&C Group reviews compliance in the following areas:

- CPE compliance
- Mandatory confirmation and training as recorded in the Compliance Profile
- CPA licensing compliance
- Independence compliance
- Data breach incidents (as applicable)
- Discipline resulting from an ethics investigation (as applicable)

Through the third quarter of fiscal year 2009 (ending June 30), 2,328 due diligence reviews were completed.

CPA Licensing and Continuing Professional Education

The E&C Group monitors partners' and employees' adherence to the firm's licensing policies, which require partners and employees to have a CPA license in the state of the office to which they are assigned ("home office") and in any other state where they are performing work that requires them to have an additional license.

The team monitored 9,094 CPA licenses for 6,370 partners and professionals during the first three quarters of fiscal year 2009. Our robust compliance efforts have resulted in increased compliance with licensing requirements.

The E&C Group also monitors compliance with CPE requirements established by the Public Company Accounting Oversight Board (PCAOB). Working closely with both the Center for Learning and Development and the Human Resources Services Center, this program also is intended to ensure that firm-sponsored courses are compliant with the requirements we must meet to be a National Association of State Boards of Accountancy CPE sponsor.

For calendar year 2008, the team monitored 12,429 partners and other professionals for compliance with firm and PCAOB CPE requirements. Two expatriate partners failed to become CPE-compliant for 2008 and were therefore referred to the Management Review Panel. By June 2009, both individuals had completed enough credits to make up their 2008 CPE deficiencies.

Compliance Profile

The Compliance Profile is a tool that helps partners and employees track compliance with mandatory firm training requirements that apply to them because of their level in the firm or practice area. Reminders are sent when a deadline is approaching, and non-compliance is escalated to performance managers and, when appropriate, to leadership of the firm.

In fiscal year 2009:

- A total of 39 requirements were tracked;
- Ten of these were new requirements launched during the fiscal year; and
- On average, 96 percent of all requirements were completed prior to the deadline.

Privacy Compliance

The firm's Privacy team, which now resides in Risk Management, along with the Office of General Counsel, the Ethics and Compliance Group, Firmwide Security, Information Technology Services, Operations, and Internal Audit, assists partners and employees in their efforts to help ensure that the confidentiality of firm and client information is not compromised.

Initiatives include:

- A Data Breach Response process that investigates potential data losses affecting partners and employees, clients, and others;
- Providing guidance related to all aspects of data privacy and the protection of confidential information;
- Privacy risk reviews for KPMG projects and initiatives;
- An annual firmwide privacy review to assess continued compliance with legal, regulatory, professional, contractual, and ethical privacy obligations, which is a required activity to support the firm's annual Safe Harbor re-certification; and
- Firmwide privacy training and awareness activities. ■

Doing Business with the Federal Government

A COMMITMENT TO COMPLIANCE IN THE FEDERAL MARKETS

IN WORKING WITH U.S. GOVERNMENT CLIENTS, KPMG MUST COMPLY WITH NUMEROUS POLICIES AND REGULATIONS THAT ARE SPECIFIC TO GOVERNMENT CONTRACTS AND OFTEN ARE MORE STRINGENT THAN THOSE RELATED TO DOING BUSINESS WITH COMMERCIAL CLIENTS.

Because a reputation for compliance is critical to success in the Federal markets, the Federal practice has developed a robust set of guidelines and processes to help ensure full compliance throughout each and every Federal engagement, as well as a unique organizational structure that makes compliance a top priority.

"There are a tremendous number of opportunities to do business with the Federal Government, particularly in the current economy," says Diane Dudley, Audit Sector Leader for the Federal practice. "The structure we've built at KPMG allows us to pursue those opportunities while demonstrating to our clients a commitment to compliance in this increasingly regulated environment."

Training and Guidance

To help the nearly 600 Audit and Advisory professionals in the Federal practice become familiar with the rules associated with doing business with Government entities and remain up-to-date on the latest laws and regulations, KPMG developed the *Federal Practice Guide*, an online resource that provides guidance on everything from client and engagement pursuit and acceptance, to contracting, to teaming relationships. In particular, the Guide focuses on the Federal Acquisition Regulation (FAR) System, the suite of regulations issued by Federal agencies to manage the process through which the Government purchases goods and services. Each year, all members of the

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— CHARLES WILKINS

practice — as well as others in the firm who work with Federal clients — must certify that they have read and understand the Guide, in order to remain active in the Federal space.

In addition, training courses are developed annually to raise awareness about any legal or regulatory issues that are particularly timely or significant. A new, eight-hour case study course, "Federal Government Contract Compliance — A Practical Guide," was launched this year, and other recent training events have focused on lobbying Federal officials, a new mandatory disclosure rule, organizational and personal conflicts of interest, and "Getting it Right" relative to winning and performing on Government contract engagements.

"Our goal is to ensure that all of our people understand the nuances of the FAR, which applies to all executive agencies of the Government, as well as its supplements, which are specific to the individual Government bodies," says Charles Wilkins, Executive Director, Government Contract Compliance. "The regulatory requirements involved with Federal procurement have very serious penalties associated with them, so we must be exceptionally careful to avoid any activity that might raise an issue or concern. As a practice and as a firm, we emphasize the importance of applying the highest ethical standards at all times, and going above and beyond to ensure that our reputation as an ethically responsible firm is never compromised."

Creating a Conversation

Communication and collaboration among Federal practice leaders are critical to ensuring compliance. The firm's Federal Deals Board — chaired by John Cherbini, Advisory Sector Leader for the Federal practice, and Diane Dudley — convenes once a week to discuss large pursuit opportunities and serves as a particularly effective compliance mechanism. Deals Board meetings also include Charles Wilkins, Professional Practice Partner Sean Hoffman, Government Contracts Director Bonnie Brandon, and certain other Federal practice partners from across Audit and Advisory.

Cherbini sees the Deals Board as a key component of the Federal practice's compliance program — one that serves not only to protect the firm from risk but also to set the tone for the Federal organization. "When a pursuit opportunity arises, we ask the lead partner or senior manager to present the opportunity to the Deals Board and account for any issues related to ethics and compliance," he explains. "Therefore, we approach each opportunity from a strategic perspective as well as a compliance perspective from the beginning, working to identify any potential conflicts of interest or independence issues. It's only after fully vetting a Government opportunity in the Deals Board that we make a decision as to whether or not to pursue the engagement."

For those opportunities that pass the board's review, the Federal practice includes a dedicated proposal team with a deep knowledge of relevant laws, regulations, and policies. "Developing a proposal for a Federal Government client requires a keen understanding of the enhanced regulatory environment in which we do business, in addition to the client's needs," Dudley notes. Therefore, the firm hires and retains professionals who are well trained on the complex rules and requirements by which both KPMG and our Federal clients must abide.

With the right people, resources, and structure in place, it's no surprise KPMG is considered a leader in the Federal marketplace. "Our culture of ethics and compliance is a definite factor in our ability to win business," says Cherbini. "We are regarded as one of the leading practices, recognized for the integrity with which we manage our business, and that contributes to our client relationships as well as our top-line growth." ■

"We approach each opportunity from a strategic perspective as well as a compliance perspective from the beginning, working to identify any potential conflicts of interest or independence issues."

— JOHN CHERBINI

Looking Ahead

AT KPMG, WE ARE PROUD TO SAY THAT WE HAVE ESTABLISHED A MODEL ETHICS AND COMPLIANCE PROGRAM, WHICH IS BUILT ON THE FOUNDATION OF A STRONG ETHICAL CULTURE. THE ELEMENTS OF THE PROGRAM ARE IN PLACE AND FUNCTIONING WELL, AND THE CULTURE IS CLEAR FROM VARIOUS INTERNAL SURVEYS AND MONITORING ACTIVITIES.

Still, we understand that we are engaged in an ongoing process that requires constant thought and renewed commitment. Looking ahead, we will be re-examining our efforts to reinforce what is right and eliminate what is wrong, and to instill in everyone at KPMG a sense of personal responsibility for doing the right thing, in the right way.

We also will stay at the forefront in the field of business ethics and compliance. For example, we recognize that as the business world becomes increasingly global, compliance standards are "harmonizing" across borders. As this harmonizing changes the standards applicable to the work of the U.S. firm, we will make the necessary adjustments in our program.

We also recognize that our ethical culture must extend to parties who do business with the firm. We expect our vendors and contractors to meet the same ethical standards that we impose on our own personnel, and we communicate those standards regularly and consistently to the external parties with whom we do business.

Recently, the definition of ethical culture has been expanding to include corporate social responsibility (CSR), which involves a company's consideration of the impact of its activities on the environment, consumers, employees, communities, and other stakeholders. We recognize that the two areas share common ground, and we are thinking about how to integrate additional CSR initiatives into the firm's day-to-day business. Ethics and integrity, as well as community service and stewardship, are embodied in KPMG's core values, which guide us in everything that we do. ■

Ethics and Compliance Leadership

Tim Flynn
Chairman

John Veihmeyer
CEO and Deputy Chairman

Sven Erik Holmes
Executive Vice Chair, Legal and Compliance

Tom DiLeonardo
Chief Compliance Officer

Vicki Sweeney
Partner-in-Charge, Ethics and Compliance

Mike Plansky
Ombudsman

Contact Information

Hotline Number:
877-576-4033

Hotline Web:
www.kpmgethics.com

Ombudsman Number:
212-872-4458

kpmg.com