UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES OF AMERICA	:	
- v. -	:	18 Cr. 36 (JPO)
DAVID MIDDENDORF,	:	
Defendant.	:	

SENTENCING MEMORANDUM OF THE UNITED STATES OF AMERICA

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The Government respectfully submits this memorandum in connection with the sentencing of defendant David Middendorf, which is scheduled for September 11, 2019 at 10:30 a.m. On March 11, 2019, Middendorf was convicted of one count of conspiracy to commit wire fraud and three counts of wire fraud following a four-week trial. On July 10, 2019, the United States Probation Office ("Probation") issued the Final Presentence Report ("PSR") in this case. In the PSR, Probation calculated a Guidelines range of 46 to 57 months' imprisonment, based on a 16-level offense level increase for loss amount. As reflected in the Government's July 26, 2019 letter on loss amount and restitution (Dkt. No. 378), the Government is seeking only a 14-level increase for loss amount, which would result in a Guidelines range of 37 to 46 months' imprisonment.

In his sentencing submission, Middendorf seeks a non-incarceratory sentence, arguing principally that his history and characteristics weigh against a custodial sentence. But his history and characteristics show exactly why a custodial sentence is appropriate. Unlike many defendants who pass through this courtroom, Middendorf has had every opportunity in life, and he has supportive friends and family. Despite all of this, Middendorf engaged in a criminal scheme to cheat on inspections by the Public Company Accounting Oversight Board ("PCAOB"), corrupting a process that should have been undertaken with truthfulness and integrity. Of all the defendants, Middendorf held the highest position at KPMG and could have simply directed his subordinates to stop their criminal conduct. But instead, he dove right in, knowing the misappropriated inspection lists could give KPMG a critical advantage in PCAOB inspections – which he had ultimate responsibility for improving. Given his status as head of KPMG's Department of Professional Practice ("DPP"), his approval of the scheme could have corrupted KPMG to its core. Accordingly, and for the reasons that follow, the Government respectfully submits that a sentence within the Guidelines range would be appropriate.

I. Offense Conduct

In 2015, KPMG recruited and hired Brian Sweet, an Associate Director at the PCAOB, to work as an audit partner in KPMG's Inspections Group. During Sweet's first week at KPMG, Middendorf repeatedly asked and implored Brian Sweet to share confidential PCAOB inspection information that Sweet already had and on a going forward basis, implying that Sweet's paycheck depended on it. (Tr. 761-65, 772-74, 1856-61).

For example, on Sweet's first day at KPMG in 2015, Middendorf asked Sweet whether Wells Fargo and Stonegate Mortgage were going to be selected for inspection in 2015, which was confidential PCAOB information Sweet was duty-bound not to share. (Tr. 761-65). After Sweet shared the confidential information, Middendorf got so animated he slapped the table. (Tr. 763).

On Sweet's second day at KPMG, Middendorf met with Sweet alone in a conference room on an executive floor at KPMG. Middendorf referred to the prior day's lunch during which Middendorf had asked Sweet to share confidential PCAOB information about Stonegate Mortgage, described it as a "gray area," told Sweet that he was to share insight and add value wherever he could, and implored Sweet to remember where his paycheck came from. (Tr. 772-74). Middendorf asked Sweet to stay in touch with his contacts at the PCAOB and, based on the context of the conversation, Sweet understood Middendorf to be directing him to "keep a listening ear to be close with those contacts and stay aware of anything that they might share." (Tr. 774).

On Sweet's fourth day at KPMG, Sweet told Whittle that Sweet had taken the PCAOB's confidential inspection list for 2015 from the PCAOB. (Tr. 777). Whittle relayed that to Middendorf, who said "get that list," which Whittle did. (Tr. 1856-61). At the time Whittle asked Sweet for the 2015 list, Whittle knew full well that what he was doing was wrong. (Tr. 1978-79). Whittle's email to Middendorf with the confidential list of 2015 inspection targets obtained from Sweet made plain its confidential nature: "The complete list. Obviously very sensitive. We will

not be broadcasting this." (GX 754). Based on Sweet's disclosure of the confidential 2015 inspection list, Middendorf took action to improve KPMG's inspection results without disclosing to the PCAOB that KPMG had the inspection list. (Tr. 810-11, 1859-65). For example, Middendorf asked Sweet to help the Wells Fargo engagement team prepare for its 2015 inspection before the inspection had been announced. (Tr. 810).

On March 28, 2016, Jeffrey Wada shared with Cynthia Holder the confidential list of PCAOB's inspection selections for KPMG's banking clients, which Holder promptly passed to Sweet for use by KPMG. (GX 953, 1362, 1443; Tr. 856). After Sweet obtained the confidential 2016 PCAOB list of banking inspection targets from Wada, Middendorf participated in a meeting with Whittle and Britt, and Sweet participated by phone. (Tr. 868-74). Whittle testified that Middendorf participated in all key aspects of the co-conspirators' agreement: to "us[e] the ALLL monitoring program to conduct secret reviews of the workpapers," how to "arrange for access to workpapers so re-reviews could be conducted," when Sweet told everyone "that he had obtained confidential PCAOB information about the 2016 inspections." (Tr. 2146-47). Whittle and Middendorf divided responsibility for gaining access to the work papers for audits on the 2016 list that were not in the ALLL monitoring program. (Tr. 1887). Indeed, Middendorf thought it was a good idea to assign additional people to do re-reviews of certain engagements in the ALLL monitoring program that were not on the 2016 inspection list to avoid a mismatch between the internal and external inspection results, which could lead to detection. (Tr. 1902-05).

The re-reviews worked, and comments in the ALLL area dropped significantly. (GX 1358). Middendorf expressed how pleased he was that the inspection results had been so improved from the prior year, particularly the banking inspections, including the ones that had been subject to the stealth re-reviews. (Tr. 947). Whittle, Middendorf, and Britt acted in a way that made clear

their request for the 2017 preliminary inspection list: "Based on the fact that we had [been] encouraging him to get information from the PCAOB, certainly we had been positive with him with respect to receiving the 2016 list and the 2015 list. I believe there was an implied request for any information, and that would include a preliminary list." (Tr. 1919). The encouragement worked: Sweet testified that based on his interactions and experiences with Middendorf and Whittle, he understood that "it was clearly an expectation that we would continue to get this, that Cindy and I would continue to get this information." (Tr. 1014).

On January 9, 2017, Wada obtained and disclosed to KPMG the confidential preliminary inspection list for 2017. (GX 655). That night, Wada sent his resume to Holder in search of a job at KPMG. (GX 1073). After Sweet shared the list with Whittle, he passed it to Middendorf, who took it down in his phone. (GX 655, 656-A, 1362). Once again, Middendorf acted on the confidential PCAOB information. Whittle and Middendorf decided to and did devote additional resources to engagements on the preliminary list in light of their presence on the list. (Tr. 1921-24).

On February 3, 2017, Wada shared with Holder the complete list of KPMG inspections for 2017. Once again, Wada passed the information to Sweet, who shared it with Middendorf, Whittle, and Britt. Middendorf took the entire list of approximately 47 audit clients down in the notes function of his phone. (GX 657). As Middendorf was considering how to best make use of the information, Sweet was giving a heads up to certain engagement partners, and Sweet's conversation with the engagement partner was ultimately reported to Middendorf. (Tr. 1061, 1072-73, 1580-85, 1932).

When confronted about his use of the confidential 2017 inspection list by another partner, Middendorf deflected and minimized. He said that there were really not a lot of surprises on the

list, most of them were in the monitoring program, and he couldn't "unknow" the information. (Tr. 1663-64). He was noncommittal about whether he intended to take any action. And after that, he stormed into Whittle's office, livid that Sweet hadn't been discrete about the information. (Tr. 1932-34). It was only *after* Dave Marino threatened to report the issue to the Vice Chair of Legal and Compliance at KPMG, Judge Sven Holmes, that Scott Marcello and Middendorf reported the information to Holmes on February 14. (Tr. 1626-32).

II. Applicable Law

The Guidelines are no longer mandatory, but they continue to play a critical role in trying to achieve the "basic aim" that Congress tried to meet in enacting the Sentencing Reform Act, namely, "ensuring similar sentences for those who have committed similar crimes in similar ways." *United States v. Booker*, 543 U.S. 220, 252 (2005); *see also United States v. Crosby*, 397 F.3d 103, 113 (2d Cir. 2005) ("[I]t is important to bear in mind that *Booker/Fanfan* and section 3553(a) do more than render the Guidelines a body of casual advice, to be consulted or overlooked at the whim of a sentencing judge."). "[A] district court should begin all sentencing proceedings by correctly calculating the applicable Guidelines range," which "should be the starting point and the initial benchmark." *Gall v. United States*, 552 U.S. 38, 49 (2007). The Guidelines range is thus "the lodestar" that "anchor[s]" the district court's discretion. *Molina-Martinez v. United States*, 136 S. Ct. 1338, 1345-46 (2016) (quoting *Peugh v. United States*, 569, U.S. 530, 549 (2013)) (internal quotation marks omitted).

After making the initial Guidelines calculation, a sentencing judge must consider the factors outlined in Title 18, United States Code, Section 3553(a), and "impose a sentence sufficient, but not greater than necessary, to comply with the purposes" of sentencing: "a) the need to reflect the seriousness of the offense, to promote respect for the law, and to provide just punishment for that offense; b) the need to afford adequate deterrence to criminal conduct; c) the

need to protect the public from further crimes by the defendant; and d) the need for rehabilitation." *United States v. Cavera*, 550 F.3d 180, 188 (2d Cir. 2008) (citing 18 U.S.C. § 3553(a)(2)). Section 3553(a) further directs the Court "in determining the particular sentence to impose" to consider: (1) the nature and circumstances of the offense and the history and characteristics of the defendant; (2) the statutory purposes noted above; (3) the kinds of sentences available; (4) the kinds of sentence and the sentencing range as set forth in the Sentencing Guidelines; (5) the Sentencing Guidelines policy statements; (6) the need to avoid unwarranted sentencing disparities; and (7) the need to provide restitution to any victims of the offense. *See* 18 U.S.C. § 3553(a).

In light of *Booker*, the Second Circuit has instructed that district courts should engage in a three-step sentencing procedure. *See Crosby*, 397 F.3d at 103. First, the Court must determine the applicable Sentencing Guidelines range, and in so doing, "the sentencing judge will be entitled to find all of the facts that the Guidelines make relevant to the determination of a Guidelines sentence and all of the facts relevant to the determination of a non-Guidelines sentence." *Id*. at 112; *see also United States v. Corsey*, 723 F.3d 366, 375 (2d Cir. 2013) ("Even in cases where courts depart or impose a non-Guidelines sentence, the Guidelines range sets an important benchmark against which to measure an appropriate sentence."). Second, the Court must consider whether a departure from that Guidelines range is appropriate. *See Crosby*, 397 F.3d at 112. Third, the Court must consider the Guidelines range, "along with all of the factors listed in section 3553(a)," and determine the sentence to impose. *Id.* at 113. In so doing, it is entirely proper for a judge to take into consideration his or her own sense of what is a fair and just sentence under all the circumstances. *United States v. Jones*, 460 F.3d 191, 195 (2d Cir. 2006).

III. Discussion

The Government respectfully submits that an incarceratory sentence within the Guidelines range is necessary to reflect the seriousness of Middendorf's offense conduct, provide just punishment, afford general deterrence, and promote respect for the law.

First, the nature and seriousness of the offense warrants a Guidelines sentence. While serving as one of the most senior executives at KPMG, Middendorf and his co-conspirators perpetrated a fraud that caused the PCAOB to suffer over $1 million in lost employee time. But more significantly, it undermined the PCAOB's role as a watchdog, tasked with the important job of overseeing auditors and ensuring that auditors could be counted on to accurately review the financial statements of public companies. As the Court knows, the PCAOB was created by Congress in the wake of the Enron and Arthur Andersen scandals, in an effort to improve oversight of auditors and restore investor confidence in the financial markets. The PCAOB engages in that oversight through its inspections process, which is an effort to measure audit quality at firms like KPMG. Here, Middendorf's actions interfered with the inspections process and thus the mission of the PCAOB in overseeing audits of public companies.

Moreover, Middendorf's role at KPMG enhances the gravity of his conduct. Throughout the fraudulent scheme, Middendorf was KPMG's head of DPP and the National Managing Partner for the Audit Quality and Professional Practice Group. He was at the height of his professional career. Given his role as head of DPP, Middendorf could have stopped the conduct immediately had he so chosen. He could have told Whittle and Sweet that acting on confidential PCAOB information was wrong. But he did just the opposite: he praised Sweet for repeatedly obtaining confidential information and he authorized acting on the information, knowing full well it was wrong to do so. In a profession where "tone at the top" is critical, Middendorf's actions corrupted

others at KPMG and caused pervasive wrongdoing. As such, his conduct was incredibly serious and warrants a sentence within the Guidelines range.

Second, a Guidelines sentence is necessary to promote general deterrence and respect for the law. As the trial made clear, there were systemic problems at KPMG regarding the use of confidential PCAOB information. It is important to send a message in this case that such behavior in the auditing profession—particularly among executives—will not be tolerated. A non-incarceratory sentence, as Middendorf suggests, simply will not accomplish that goal. Rather, it will feed into Middendorf's effort to minimize this multi-year fraudulent scheme as a "mistake in judgment." (Midd. Sent. Sub. at 20). As a jury found, Middendorf's conduct was not a lapse in judgment; it was criminal. A custodial sentence would serve as a powerful deterrent to other executives who are considering engaging in similar conduct. In contrast, a non-custodial sentence could suggest to other executives that the benefits of such a fraud outweigh the consequences.

In his submission, Middendorf argues that his history and characteristics warrant a non-custodial sentence. To the contrary, the Government submits that Middendorf's conduct is even more egregious in light of his history. As reflected in his submission, Middendorf had a strong support network of friends and family. He had achieved significant professional success at KPMG. And given his many years in the auditing profession, Middendorf is clearly someone who knows right from wrong. Despite these advantages, he chose to engage in a complex fraudulent scheme over the course of multiple years to help KPMG improve inspections results. Accordingly, Middendorf's history and characteristics do not warrant the extraordinary non-custodial sentence urged by the defense.

CONCLUSION

For the reasons set forth above, the Government respectfully submits that the Court should impose a sentence of incarceration within the Guidelines range on the defendant.

Dated: New York, New York
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Respectfully submitted,

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