

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 56074 / July 13, 2007

ACCOUNTING AND AUDIT ENFORCEMENT
Release No. 2635 / July 13, 2007

ADMINISTRATIVE PROCEEDING
File No. 3-12689

In the Matter of

Paul Kearney,

Respondent.

**ORDER INSTITUTING CEASE-AND-
DESIST PROCEEDINGS, MAKING
FINDINGS, AND IMPOSING A CEASE-
AND-DESIST ORDER PURSUANT TO
SECTION 21C OF THE SECURITIES
EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”), against Paul Kearney (“Kearney” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist Order Pursuant to Section 21C of the Securities Exchange Act of 1934 (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that:

Respondent

1. Paul Kearney, age 33, is an Irish citizen and a resident of Hollywood, Ireland. Kearney was the financial accountant of Zomax Limited's Operations Facility in Clondalkin, Ireland from April 2000 until January 2005, when he voluntarily resigned.

Relevant Entities

2. Zomax, Inc. ("Zomax") was a Minnesota corporation founded in February 1996 with its headquarters in Plymouth, Minnesota. Zomax was a manufacturer of CDs and DVDs, and provides software and related services to computer manufacturers and other producers of multimedia products. Zomax operated eleven facilities across the United States, Canada, Mexico, and Ireland. Zomax's common stock was registered with the Commission pursuant to Section 12(g) of the Exchange Act and was listed on the Nasdaq National Market. For the period ended December 31, 2004 the Company's revenue was \$199 million with operating losses of \$15.3 million and net losses of \$8.4 million.

3. Zomax Limited ("Zomax Ireland") was an Irish limited liability company and the Irish subsidiary of Zomax. Zomax Ireland was comprised of two distinct divisions: the Marketing Service Group located in Santry, Ireland and the Operations Facility located in Clondalkin, Ireland ("Operations Facility"). The Marketing Service Group was a customer contact center, and the Operations Facility was engaged in replication, print management, printing, packaging, warehousing, and distribution activities. For the period ended December 31, 2004, Zomax Ireland's revenue was approximately \$35 million, which represented approximately 17.5 percent of Zomax's total revenues. For the period ended December 31, 2004, Zomax Ireland's operating losses were \$3.4 million with net losses of \$3.3 million.

Background

4. From the end of 2003 through 2004, the former general manager of Zomax Ireland ("General Manager"), the former financial controller of the Operations Facility ("Controller"), and Kearney were the Zomax Ireland employees primarily responsible for reporting Zomax Ireland's financial results to Zomax. The General Manager was the top executive officer of Zomax Ireland and the Controller was the top financial officer of Zomax Ireland's Operations Facility. As the financial accountant for the Operations Facility, Kearney reported directly to the Controller and he also took direction from the General Manager. Kearney's duties included making journal entries for the operations facility and sending Zomax Ireland's monthly financial documents to Zomax.

¹ The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

5. Zomax Ireland's performance started to decline in late 2003, due to increased manufacturing costs, decreased demand, and a corresponding drop in prices to attempt to address the falling demand. These problems were caused by a substantial increase in the cost of raw materials, specifically petroleum based materials, which drastically increased Zomax Ireland's costs. Also, many of Zomax Ireland's customers started moving to competitors with production plants located in Eastern Europe and other parts of the world with lower labor costs. Finally, Zomax Ireland's machinery was aging, making it more difficult to produce CDs and DVDs in a cost effective manner. These problems led to significant declines in Zomax Ireland's operating performance beginning in late 2003 and continuing throughout 2004.

6. From the end of 2003 through 2004, the General Manager, the Controller, and Kearney engaged in a fraudulent scheme to inflate the financial results of Zomax Ireland by manipulating certain accounts to hide the declining performance of Zomax Ireland during 2004. Specifically, the General Manager and the Controller directed Kearney to conceal Zomax Ireland's losses by making false journal entries to overstate the sales accrual account, to capitalize spare machine parts that should have been expensed, to understate accruals for employee holiday pay, and then to conceal the fraudulent conduct by sending false Zomax Ireland financial information to Zomax.

7. The General Manager, the Controller, and Kearney's fraudulent scheme to manipulate the sales accrual account throughout 2004 resulted in this account being substantially overstated by \$367,424, \$573,804, and \$392,266 during the first three quarters of 2004. These sales accrual overstatements, in turn, resulted in revenue being overstated for the first three quarters of 2004. The General Manager, the Controller, and Kearney also inappropriately capitalized \$136,470 and \$79,129 of spare machine parts in the second and third quarters of 2004, respectively. The inappropriate capitalization of spare machine parts resulted in the corresponding understatement of Zomax Ireland's expenses and overstatement of its earnings in the second and third quarters of 2004. Lastly, their understatement of accruals for employee holiday pay during the third and fourth quarters of 2004 understated expenses by \$54,896 during these quarters.

8. Throughout 2004, the General Manager and the Controller hid this fraudulent scheme by continually misrepresenting Zomax Ireland's true financial status to Zomax. At the direction of the General Manager and the Controller, Kearney submitted fraudulent monthly financial packages to Zomax. Then the General Manager and the Controller reaffirmed the false financial information contained in the fraudulent monthly financial packages during telephone meetings with Zomax senior officers. In addition, the General Manager and the Controller each signed and submitted to Zomax false certifications for Zomax Ireland's quarterly financial statements. In turn, Zomax's senior officers relied on these false certifications in connection with their certifications to the Commission as required by Sections 302 and 906 of the Sarbanes-Oxley Act for Zomax's Forms 10-Q for the first three quarters of 2004.

9. Zomax unknowingly incorporated Zomax Ireland's false financial information in its Forms 10-Q for the first three quarters of 2004. The General Manager, the Controller, and Kearney's fraudulent scheme to inflate the financial results of Zomax Ireland had a material effect on Zomax's consolidated quarterly financial statements during 2004. On March 31, 2005, Zomax

filed its Form 10-K for 2004, which restated the financial statements for 2003 and the first three quarters of 2004. This restatement, caused primarily by the General Manager, the Controller, and Kearney's fraudulent scheme, negatively impacted the previously reported quarterly results for 2004. For the first quarter of 2004, Zomax previously reported a net loss of \$981,000; the restatement increased this net loss by \$565,000 to \$1,546,000, which represents a 58% increase in net loss. For the second quarter of 2004, Zomax previously reported net income of \$1,252,000; the restatement decreased net income for this period by \$718,000 to \$534,000, which represents a 57% decrease in net income. Finally, for the third quarter of 2004, Zomax previously reported a net loss of \$5,497,000; the restatement increased this net loss by \$540,000 to \$6,037,000, which represents a 10% increase in net loss.

10. The General Manager, the Controller, and Kearney, as part of their fraudulent scheme, knowingly circumvented a system of internal accounting controls, knowingly falsified books, records or accounts, and directly or indirectly falsified or caused to be falsified any book, record, or account.

11. The General Manager, the Controller, and Kearney's fraudulent scheme caused Zomax to fail to make and keep its books, records, and accounts in reasonable detail to accurately and fairly reflect its transactions and dispositions of assets.

12. The General Manager, the Controller, and Kearney's fraudulent scheme caused Zomax to file with the Commission Forms 10-Q for the first three quarters of 2004 that contained false statements of material fact and omitted to state material facts necessary to add such further material information as was necessary, in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

13. As a result of the conduct described above, Kearney violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in connection with the purchase or sale of securities.

14. Also, as a result of the conduct described above, Kearney violated Section 13(b)(5) of the Exchange Act and Rule 13b2-1 thereunder, which prohibit persons from knowingly circumventing a system of internal accounting controls, knowingly falsifying any book, record or account, and directly or indirectly falsifying or causing to be falsified any book, record, or account.

15. Also, as a result of the conduct described above, Kearney caused Zomax's violations of Section 13(b)(2)(A) of the Exchange Act, which requires reporting companies to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect their transactions and dispositions of their assets.

16. Lastly, as a result of the conduct described above, Kearney caused Zomax's violations of Sections 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.

17. In determining to accept the Offer, the Commission considered the cooperation that Respondent afforded the Commission staff.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Kearney's Offer.

Accordingly, it is hereby ORDERED that Paul Kearney cease and desist from committing or causing any violations and any future violations of Sections 10(b) and 13(b)(5) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder, and from causing any violations and any future violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder

By the Commission.

Nancy M. Morris
Secretary