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**Inspection of
KPMG Audit plc
(Headquartered in London, United Kingdom)**

**Issued by the
Public Company Accounting Oversight Board**

October 1, 2009

THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT

**PORTIONS OF THE COMPLETE REPORT ARE OMITTED
FROM THIS DOCUMENT IN ORDER TO COMPLY WITH
SECTIONS 104(g)(2) AND 105(b)(5)(A)
OF THE SARBANES-OXLEY ACT OF 2002**

PCAOB RELEASE NO. 104-2009-149



Notes Concerning this Report

1. Portions of this report may describe deficiencies or potential deficiencies in the systems, policies, procedures, practices, or conduct of the firm that is the subject of this report. The express inclusion of certain deficiencies and potential deficiencies, however, should not be construed to support any negative inference that any other aspect of the firm's systems, policies, procedures, practices, or conduct is approved or condoned by the Board or judged by the Board to comply with laws, rules, and professional standards.
2. Any references in this report to violations or potential violations of law, rules, or professional standards should be understood in the supervisory context in which this report was prepared. Any such references are not a result of an adversarial adjudicative process and do not constitute conclusive findings of fact or of violations for purposes of imposing legal liability. Similarly, any description herein of a firm's cooperation in addressing issues constructively should not be construed, and is not construed by the Board, as an admission, for purposes of potential legal liability, of any violation.
3. Board inspections encompass, among other things, whether the firm has failed to identify departures from U.S. Generally Accepted Accounting Principles ("GAAP") or Securities and Exchange Commission ("SEC" or "Commission") disclosure requirements in its audits of financial statements. This report's descriptions of any such auditing failures necessarily involve descriptions of the related GAAP or disclosure departures. The Board, however, has no authority to prescribe the form or content of an issuer's financial statements. That authority, and the authority to make binding determinations concerning an issuer's compliance with GAAP or Commission disclosure requirements, rests with the Commission. Any description, in this report, of perceived departures from GAAP or Commission disclosure requirements should not be understood as an indication that the Commission has considered or made any determination regarding these issues unless otherwise expressly stated.



INSPECTION OF KPMG AUDIT PLC

The Public Company Accounting Oversight Board ("PCAOB" or "the Board") has conducted an inspection of the registered public accounting firm KPMG Audit plc ("the Firm"). The Board is issuing this report of that inspection in accordance with the requirements of the Sarbanes-Oxley Act of 2002 ("the Act").

The Board is making portions of the report publicly available. Specifically, the Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report.^{1/}

The Board has elsewhere described in detail its approach to making inspection-related information publicly available consistent with legal restrictions.^{2/} A substantial portion of the Board's criticisms of a firm (specifically criticisms of the firm's quality control system), and the Board's dialogue with the firm about those criticisms, occurs out of public view, unless the firm fails to make progress to the Board's satisfaction in addressing those criticisms. In addition, the Board generally does not disclose otherwise nonpublic information, learned through inspections, about the firm or its clients. Accordingly, information in those categories generally does not appear in the publicly available portion of an inspection report.

^{1/} The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits from, or any inaccurate statement in the draft that the Board corrects in, the final report.

^{2/} See Statement Concerning the Issuance of Inspection Reports, PCAOB Release No. 104-2004-001 (August 26, 2004).

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's inspection staff ("the inspection team") conducted primary procedures for the inspection from October 2, 2006 to October 13, 2006 and from November 6, 2006 to November 17, 2006.^{3/} These procedures were tailored to the nature of the Firm, certain aspects of which the inspection team understood at the outset of the inspection to be as follows:

Number of offices	23 ^{4/}
Ownership structure	Public limited company
Number of partners	— ^{5/}
Number of professional staff	— ^{6/}

^{3/} The Board's inspection was conducted in cooperation with the Audit Inspection Unit of the Professional Oversight Board, a part of the Financial Reporting Council of the United Kingdom.

^{4/} The Firm's offices are located in Aberdeen, Birmingham, Bristol, Cambridge, Cardiff, Crawley, Edinburgh, Glasgow, Ipswich, Leeds, Leicester, Liverpool, London, Manchester, Milton Keynes, Newcastle upon Tyne, Nottingham, Plymouth, Preston, Reading, Southampton, St Albans, and Watford, United Kingdom.

^{5/} The Firm has three directors who are also partners in KPMG LLP, a United Kingdom limited liability partnership. The Firm is wholly-owned by KPMG LLP, which has 555 partners who, by arrangement with the Firm, may provide professional services on behalf of the Firm. KPMG LLP is separately registered with the Board.

^{6/} The Firm does not employ personnel who provide professional services, but, rather, uses 9,569 persons employed by another KPMG owned entity with which it is under common ownership, to provide professional services on behalf of the Firm. The number of partners and professional staff is provided here as an indication of the number of persons who provide professional services on behalf of the Firm, and does not necessarily represent the number of such persons who participate in audits of issuers or are "associated persons" (as defined in the Act) of the Firm.

Number of issuer audit clients^{7/} 11

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm conducts audits.^{8/} To achieve that goal, Board inspections include reviews of certain aspects of selected audits performed by the firm and reviews of other matters related to the firm's quality control system.

In the course of reviewing aspects of selected audits, an inspection may identify ways in which a particular audit is deficient, including failures by the firm to identify, or to address appropriately, respects in which an issuer's financial statements do not present fairly the financial position, results of operations, or cash flows of the issuer in conformity with GAAP.^{9/} It is not the purpose of an inspection, however, to review all of a firm's audits or to identify every respect in which a reviewed audit is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audits, or its issuer clients' financial statements, are free of any deficiencies not specifically described in an inspection report.

^{7/} The number of issuer audit clients shown here is based on the Firm's self-reporting and the inspection team's review of certain information for inspection planning purposes. It does not reflect any Board determination concerning which, or how many, of the Firm's audit clients are "issuers" as defined in the Act. In some circumstances, a Board inspection may include a review of a firm's audit of financial statements of an issuer that ceased to be an audit client before the inspection, and any such former clients are not included in the number shown here.

^{8/} This focus necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools.

^{9/} When it comes to the Board's attention that an issuer's financial statements appear not to present fairly, in a material respect, the financial position, results of operations, or cash flows of the issuer in conformity with GAAP, the Board's practice is to report that information to the SEC, which has jurisdiction to determine proper accounting in issuers' financial statements.

A. Review of Audit Engagements

The inspection procedures included a review of aspects of the Firm's auditing of financial statements of four issuers. The scope of this review was determined according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the scope.

The inspection team identified what it considered to be audit deficiencies.^{10/} The deficiencies identified in two of the audits reviewed included deficiencies of such significance that it appeared to the inspection team that the Firm did not obtain sufficient competent evidential matter to support its opinion on the issuer's financial statements.^{11/} Those deficiencies were –

- (1) the failure to perform sufficient procedures to evaluate the issuer's decision not to record a loss contingency; and

^{10/} PCAOB standards require a firm to take appropriate actions to assess the importance of audit deficiencies identified after the date of the audit report to the firm's present ability to support its previously expressed opinions. *See* AU 390, *Consideration of Omitted Procedures After the Report Date*, and AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report* (both included among the PCAOB's interim auditing standards, pursuant to PCAOB Rule 3200T). Failure to comply with these PCAOB standards could be a basis for Board disciplinary sanctions.

^{11/} In some cases, an inspection team's observation that a firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if a firm claims to have performed the procedure. PCAOB Auditing Standard No. 3, *Audit Documentation* ("AS No. 3"), provides that, in various circumstances including PCAOB inspections, a firm that has not adequately documented that it performed a procedure, obtained evidence, or reached an appropriate conclusion must demonstrate with persuasive other evidence that it did so, and that oral assertions and explanations alone do not constitute persuasive other evidence. *See* AS No. 3, paragraph 9; Appendix A to AS No. 3, paragraph A28. For purposes of the inspection, an observation that the Firm did not perform a procedure, obtain evidence, or reach an appropriate conclusion may be based on the absence of such documentation and the absence of persuasive other evidence.

(2) the failure to perform sufficient procedures to test certain accrued contingencies and reserves.

B. Review of Quality Control System

In addition to evaluating the quality of the audit work performed on specific audits, the inspection included review of certain of the Firm's practices, policies, and procedures related to audit quality. This review addressed practices, policies, and procedures concerning audit performance and the following eight functional areas (1) tone at the top; (2) practices for partner evaluation, compensation, admission, assignment of responsibilities, and disciplinary actions; (3) independence implications of non-audit services; business ventures, alliances, and arrangements; personal financial interests; and commissions and contingent fees; (4) practices for client acceptance and retention; (5) practices for consultations on accounting, auditing, and SEC matters; (6) the Firm's internal inspection program; (7) practices for establishment and communication of audit policies, procedures, and methodologies, including training; and (8) the supervision by the Firm's audit engagement teams of the work performed by non-United Kingdom affiliates on non-United Kingdom operations of the Firm's issuer audit clients. Any defects in, or criticisms of, the Firm's quality control system are discussed in the nonpublic portion of this report and will remain nonpublic unless the Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

END OF PART I

PARTS II AND III OF THIS REPORT ARE NONPUBLIC
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

PART IV

RESPONSE OF THE FIRM TO DRAFT INSPECTION REPORT

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Firm provided a written response to a draft of this report. Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report.^{12/}

^{12/} In any version of an inspection report that the Board makes publicly available, any portions of a firm's response that address nonpublic portions of the report are omitted. In some cases, the result may be that none of a firm's response is made publicly available.



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23 September 2008

Dear Sir

Draft Report of Inspection – Part I (Public)

We have read and comment below on the PCAOB's draft report, Part I, on its 2006 Inspection of KPMG Audit Plc dated 21 August, 2008 (the "draft report"). We appreciate the efforts made by the PCAOB to ensure continued improvements to the quality of audits and the time made available to discuss with us the draft report.

We are passionate about ensuring a high quality audit profession which continues to play an important part in global Capital Markets. We strive to improve quality on a continuous basis and continue to make improvements to our operating and risk management processes and controls, and put cultural and governance changes into effect that reflect the highest ethical standards.

Key to a high quality profession is the ability to attract and retain high quality people who are respected and motivated by the quality of what they do. It is unfortunate therefore, in our opinion, that the PCAOB's public reports only comment on perceived deficiencies and do not aim to provide a balanced view of the work they have reviewed. In this connection we note that during the closing meeting with us, the inspection team commented favourably regarding the quality of the audits they reviewed, particularly in respect of the teams' understanding of the clients' businesses and their resulting focus of audit effort and evidence on the right financial statement risks.

Just as auditors use their judgment to determine the auditing procedures to be performed, the PCAOB inspection staff members' observations are based upon their assessment of audit risk and financial statement materiality. We may have differing views as to the nature and extent of necessary auditing procedures, resulting conclusions, and/or required documentation in specific circumstances, but we recognise that judgments are involved in both the performance of an audit and the subsequent inspection process. This is particularly the case when considering accounting estimates which by their nature are highly judgemental and depend on an assessment of future events.



*KPMG Audit Plc
Draft Report of Inspection – Part I (Public)
23 September 2008*

In that regard we reached a different conclusion to that reached by the PCAOB. In particular:

- 1 We are of the opinion that we did perform sufficient procedures to evaluate Issuer A's accounting judgment; and
- 2 We consider that we had performed sufficient procedures to test certain accrued contingencies and reserves in the context of Issuer B's financial statements.

Having regard to our obligations under AU 390 and AU 561, neither of the matters identified by the PCAOB required us to perform additional audit work or the re-issuance of our previously issued reports.

Yours faithfully

KPMG Audit Plc

KPMG Audit Plc