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Report on

2008 Inspection of KPMG LLP
(Headquartered in New York, New York)

Issued by the

Public Company Accounting Oversight Board

June 16, 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

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Preface to Reports Concerning Annually Inspected Firms

The Sarbanes-Oxley Act of 2002 requires the Public Company Accounting Oversight Board ("PCAOB" or "the Board") to conduct an annual inspection of each registered public accounting firm that regularly provides audit reports for more than 100 issuers. The Board's report on any such inspection includes this preface to provide context for information in the public portion of the report.

A Board inspection includes, among other things, a review of selected audits of financial statements and of internal control over financial reporting. If the Board inspection team identifies deficiencies in those audits, it alerts the firm to the deficiencies during the inspection process. Deficiencies that exceed a certain significance threshold are also summarized in the public portion of the Board's inspection report. The Board encourages readers to bear in mind two points concerning those reported deficiencies.

First, inclusion in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. Under PCAOB standards, a firm must take appropriate action to assess the importance of the deficiency to the firm's present ability to support its previously expressed audit opinions. Depending upon the circumstances, compliance with these standards may require the firm to perform additional audit procedures, or to inform a client of the need for changes to its financial statements or reporting on internal control, or to take steps to prevent reliance on previously expressed audit opinions. A Board inspection does not typically include review of a firm's actions to address deficiencies identified in that inspection, but the Board expects that firms are attempting to take appropriate action, and firms frequently represent that they have taken, are taking, or will take, action. If, through subsequent inspections or other processes, the Board determines that the firm failed to take appropriate action, that failure may be grounds for a Board disciplinary sanction.

Second, the Board cautions against drawing conclusions about the comparative merits of the annually inspected firms based on the number of reported deficiencies in any given year. The total number of audits reviewed is a small portion of the total audits performed by these firms, and the frequency of deficiencies identified does not necessarily represent the frequency of deficiencies throughout the firm's practice. Moreover, if the Board discovers a potential weakness during an inspection, the Board may revise its inspection plan to target additional audits that may be affected by that weakness, and this may increase the number of deficiencies reported for that firm in that year. Such weaknesses may emerge in varying degrees at different firms in different years.

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.



2008 INSPECTION OF KPMG LLP

In 2008, the Board conducted an inspection of KPMG LLP ("KPMG" or "the Firm"). The Board is today 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, Appendix A, and portions of Appendix B. Appendix A provides an overview of the inspection process. Appendix B includes 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. 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") performed an inspection of the Firm from April 2008 through October 2008. The inspection team performed field work at the Firm's National Office and at 29 of its approximately 90 U.S. practice offices.

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm conducts audits.^{3/} 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. Appendix A to this report provides a description of the steps the inspection team took with respect to the review of audits and the review of certain firm-wide quality control processes.

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.^{4/} 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 or reporting on internal control, are free of any deficiencies not specifically described in an inspection report.

^{3/} This focus on weaknesses and deficiencies 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.

^{4/} When the Board becomes aware 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 scope of the inspection procedures performed included reviews of aspects of selected audits performed by the Firm. Those audits and aspects were selected according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the selection process.

In reviewing the audits, the inspection team identified matters that it considered to be audit deficiencies.^{5/} These deficiencies included a failure by the Firm to identify or appropriately address an error in the issuer's application of GAAP. In addition, the deficiencies included failures by the Firm to perform, or to perform sufficiently, certain necessary audit procedures.

In some cases, the conclusion that the Firm failed to perform a procedure may be based on the absence of documentation and the absence of persuasive other evidence, even if the 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.^{6/} 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.

When audit deficiencies are identified after the date of the audit report, PCAOB standards require a firm to take appropriate actions to assess the importance of the deficiencies to the firm's present ability to support its previously expressed opinions.^{7/}

^{5/} The discussion in this report of any deficiency observed in a particular audit reflects information reported to the Board by the inspection team and does not reflect any determination by the Board as to whether the Firm has engaged in any conduct for which it could be sanctioned through the Board's disciplinary process.

^{6/} See AS No. 3, paragraph 9; Appendix A to AS No. 3, paragraph A28.

^{7/} See AU 390, *Consideration of Omitted Procedures After the Report Date*, AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*

and failure to take such actions could be a basis for Board disciplinary sanctions. In response to the inspection team's identification of deficiencies, the Firm, in some cases, performed additional procedures or supplemented its work papers.^{8/}

In some cases, the deficiencies identified were of such significance that it appeared to the inspection team that the Firm, at the time it issued its audit report, had not obtained sufficient competent evidential matter to support its opinion on the issuer's financial statements. The deficiencies that reached this degree of significance are described below, on an audit-by-audit basis, with the exception of deficiencies that were observed in multiple audits and are therefore grouped together.

Deficiencies in testing pension plan assets (three audits)

In three audits, due to deficiencies in testing assets held by the issuers' pension plans, the Firm failed to obtain sufficient competent evidential matter to support its audit opinions. The deficiencies are as follows:

- In one audit, the Firm failed to test sufficiently the existence and valuation of the issuer's pension plan assets. Specifically, the Firm failed either to obtain a service auditor's report for the trustee of the plan assets or to identify and test controls over the existence and valuation of the pension plan assets held by the trustee. The Firm also failed to obtain a confirmation from the trustee of the individual assets that the trustee held and the fair value of the individual assets. In addition, the Firm relied on uncorroborated representations from the issuer's management that none of the plan assets related to subprime assets or alternative investments, such as hedge funds. Further, the Firm failed to obtain an understanding of the issuer's methods for determining fair value, and it failed to test the fair values of any of the plan assets. [Issuer A]

(both included among the PCAOB's interim auditing standards, pursuant to PCAOB Rule 3200T), and PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over Financial Reporting That Is Integrated with An Audit of Financial Statements* ("AS No. 5"), ¶ 98.

^{8/} The Board inspection process generally did not include review of such additional procedures or documentation, although future Board inspections of the Firm may, as appropriate, include further review of any of these matters.

- In another audit, the Firm failed to sufficiently test the valuation of the issuer's pension plan assets, the majority of which did not have quoted market prices in active markets. The Firm selected a sample of securities for testing. For the majority of the items selected, however, the Firm only compared the securities' recorded values to amounts determined by the issuer's investment manager or the issuer's plans' trustees. The Firm failed to obtain an understanding of the methodologies, and to evaluate the reasonableness of the assumptions, that the investment manager or the trustees had used to estimate the fair values of the securities. [Issuer B]
- In the third audit, the Firm failed to sufficiently test the existence and valuation of the issuer's pension plan assets, the majority of which did not have quoted market prices in active markets. The issuer obtained fair value estimates for securities held by the pension plan from the plan's trustee, and the Firm selected a sample of 25 securities to evaluate the fair value estimates. The Firm failed to obtain an understanding of how the trustee determined the fair values of any of the sample selections for which no quoted market prices existed, and to evaluate the reasonableness of the assumptions the trustee had used to determine fair value. Furthermore, the Firm failed to obtain a confirmation from the trustee of the individual assets held and the fair value of the individual assets. [Issuer C]

Issuer D

In this audit, the Firm failed in the following respects to obtain sufficient competent evidential matter to support its audit opinion –

- The issuer provides financing through multiple business units. The issuer used different methodologies and assumptions to estimate the allowance for loan losses (ALL) at its business units based on the characteristics of the loans at each business unit. The Firm tested the consolidated ALL by testing the issuer's estimate of the ALL at specific business units that the Firm had selected. Deficiencies in the Firm's audit procedures regarding the ALL at selected business units included:
 - The degree of reliance the Firm placed on controls at certain of the business units was inappropriate in light of the control testing

performed. For example, in one instance the Firm relied on a control that did not achieve the specified control objective. In another instance, the Firm's sample of one used to test certain manual controls was insufficient to support the reliance that the Firm placed on those controls.

- At certain of the business units selected for testing, the Firm failed to test certain of the issuer's assumptions, including those developed by the issuer's specialist, and/or data used in estimating the ALL, including loan loss rates, environmental factors, enterprise valuations, liquidation analyses, debt service coverage and loan-to-value ratios, weighting factors, and the homogeneity of loan pools.
- The Firm failed to expand testing as a result of exceptions that the issuer's internal audit department had identified in its tests of the data that the issuer had used to estimate the ALL at a business unit.
- To test the valuation of the issuer's securities, the Firm obtained valuations for the securities from outside pricing services. The Firm failed, however, to determine which of those valuations were based on financial models and failed to obtain an understanding of the assumptions and methods used in any such models. In addition, with respect to some of the issuer's securities, the Firm was unable to obtain values from outside pricing services and failed to perform procedures to test the issuer's valuation of those securities.
- The Firm failed to perform sufficient audit procedures with respect to certain financing receivables. The Firm did not send confirmation requests for two of the 14 sample items selected for confirmation, one of which represented the largest item in the sample. For this receivable, the Firm relied on documents supplied by the issuer but failed to perform procedures to obtain the necessary corroboration of those documents. In addition, the Firm selected the sample to confirm from a population that excluded certain financing receivables. Also, there was no evidence in the audit documentation, and no persuasive other evidence, that the Firm had reconciled the differences between the amounts on the individual confirmation requests and the recorded amounts of the receivables.

Issuer E

In this audit, the Firm failed in the following respects to obtain sufficient competent evidential matter to support its audit opinion –

- The Firm failed to perform sufficient audit procedures with respect to the valuation of certain hard-to-price financial instruments. First, the degree of reliance the Firm placed on the issuer's controls exceeded what was appropriate in light of the Firm's assessment of the overall risk of material misstatement as high, the existence of fraud risk factors related to the valuation of financial instruments, and deficiencies in the nature and extent of the tests of controls the Firm performed. For example, in one instance in an area of higher risk, the Firm limited its tests of a price verification control it relied on to inquiry and observation without obtaining corroboration, and in another instance, the Firm's sample of one used to test certain manual controls was insufficient. Second, the substantive procedures the Firm performed to test the valuation of the financial instruments did not provide the Firm with the necessary level of assurance. For example, the Firm selected sample sizes based on its preliminary view of the acceptable threshold for errors, which was nearly three times as large as its revised acceptable threshold for errors, and the Firm failed to obtain, from an independent source, information corroborating key data and assumptions underlying the fair values the issuer had used for approximately 30 percent of the financial instruments the Firm tested.

In addition, the Firm's tests of controls that it performed to evaluate the issuer's classification of financial instruments were not sufficient because the controls identified and tested were not relevant to the assertion being tested.

- With respect to the valuation of certain other hard-to-price financial instruments, the Firm failed to identify and test controls over the issuer's process for valuing these instruments, and the Firm failed to perform substantive procedures to test the values the issuer had assigned to these instruments.
- During the fourth quarter of the year, the Firm lowered its assessment of the acceptable threshold for errors in certain accounts by two-thirds due to the

market disruption that had occurred during the second half of the year. Other than inquiry of management, the Firm did not test certain significant information and assumptions the issuer had used in assessing whether the impairment in a portion of its portfolio of available-for-sale mortgage-backed securities was other than temporary, even though securities representing approximately 90 percent of this portion of the portfolio had been in an unrealized loss position for more than 12 months, and the unrealized losses were nearly twice the Firm's revised acceptable threshold for errors. In addition, the Firm did not evaluate whether the issuer's analysis considered the negative developments affecting the mortgage market and mortgage-backed securities. The Firm also failed to consider certain of the audit implications of the other-than-temporary impairment charges that the issuer had recorded for this portion of the portfolio in the first month after year end, such as whether it needed to determine whether the conditions that resulted in such charges were present in the issuer's securities included in its portfolio in the year under audit.

Issuer F

The issuer had experienced significant deterioration in its loan portfolio during the year under audit. For example, the issuer had an increase of over 80 percent in non-performing mortgage loans. The issuer's allowance for losses on mortgage loans ("ALL") included a "non-current component" related to loans more than 90 days past due. The issuer calculated the non-current component of its ALL by applying certain percentages to different aging categories of loans in that component.

As part of its procedures to audit the ALL, the engagement team used a Firm Credit Risk Specialist ("FCRS") to review the issuer's ALL methodology, and the FCRS observed that the issuer needed to develop additional quantitative support for its ALL methodology, including for loss experiences on delinquent mortgage loans, and to further analyze the validity of historical percentages in light of new economic circumstances. Despite these concerns, the Firm accepted the percentages the issuer had used to calculate the non-current component of the ALL without determining whether they were supportable and appropriate.

Issuer G

In this audit, the Firm failed in the following respects to obtain sufficient competent evidential matter to support its audit opinion –

- In the year under audit, the issuer changed its accounting for an agreement it had entered into in the prior year to outsource its information technology function. Under the revised accounting, the issuer deferred certain transition costs that had been, or would have been, expensed as incurred under the original accounting. The Firm failed to identify that the issuer's revised accounting was not in compliance with GAAP because certain of the deferred costs did not meet the definition of an asset, as the costs did not represent a probable future economic benefit for the issuer.
- The Firm noted that the revenue growth rates that management had used in its cash flow projections to evaluate whether a reporting unit's goodwill was impaired appeared aggressive. The Firm performed a sensitivity analysis using lower revenue growth rates, which resulted in an estimated fair value of the reporting unit that was lower than its carrying value. Also, the issuer had received an offer to purchase the reporting unit for less than its year-end carrying value. Despite these indicators of potential impairment, the Firm relied on management's representations that it would not sell the unit for less than its carrying value, and accordingly accepted management's assertion that goodwill for this reporting unit was not impaired.

Issuer H

The issuer determined that operating losses for an asset group, combined with delays in product release and increased competition, constituted a triggering event, which required that the asset group be evaluated for impairment. The issuer's memorandum assessing possible impairment that was included in the Firm's work papers stated that the issuer had determined that the group's primary assets had a longer life than had previously been estimated, so that an additional year of cash flows should be included in the impairment analysis. The memorandum concluded that the asset group's estimated future cash flows exceeded its carrying value, although the projected cash flow schedules attached to the memorandum in the Firm's work papers indicated the opposite.

The Firm failed to perform sufficient procedures to audit the issuer's impairment analysis. For example, the Firm compared the projected revenue growth to the most recent period and to other internal projections, but did not evaluate the appropriateness of the significant increase in the revenue projections from those used to value the assets when the issuer acquired them in the prior year, nor did it assess certain significant assumptions, such as the price and volume information, that drove the revenue increases. Also, the Firm failed to substantiate, beyond inquiry of issuer personnel, a substantial projected decrease in research and development costs in light of the issuer's position that it intended to continue to develop the group's products. The Firm concluded, based on these adjusted projections, that the projected cash flows exceeded the carrying value of the asset group, and that the asset group was not impaired. In addition, the Firm's analysis of possible impairment excluded from the group certain tangible assets that should have been included and that the issuer had included in its analysis. Had the Firm's analysis included the carrying value of these tangible assets in the asset group, the projected cash flows would have been less than the carrying value of the asset group.

Issuer I

In this audit, the Firm failed to sufficiently test the existence and accuracy of a substantial portion of the issuer's payroll costs, which formed the basis for the recognition of much of the issuer's revenue. Specifically, the Firm planned to select a single sample for two purposes: to test the issuer's controls over payroll and to substantively test the existence and accuracy of payroll costs. The Firm, however, failed to calculate the sample size it would need to achieve both purposes. As a result, the sample tested by the Firm was not sufficient for substantive testing of the existence and accuracy of the payroll costs.

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 processes related to audit quality. This review addressed practices, policies, and procedures concerning audit performance and the following five areas (1) management structure and processes, including the tone at the top; (2) practices for partner management, including allocation of partner resources and partner evaluation, compensation, admission, and disciplinary actions; (3) policies and procedures for considering and addressing the risks involved in accepting and retaining clients,

including the application of the Firm's risk-rating system; (4) processes related to the Firm's use of audit work that the Firm's foreign affiliates perform on the foreign operations of the Firm's U.S. issuer audit clients; and (5) the Firm's processes for monitoring audit performance, including processes for identifying and assessing indicators of deficiencies in audit performance and processes for responding to weaknesses in quality control. 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

APPENDIX A

THE INSPECTION PROCESS

The inspection process was designed and performed to provide a basis for assessing the degree of compliance by the Firm with applicable requirements related to auditing issuers. This process included reviews of components of selected issuer audits completed by the Firm. These reviews were intended both to identify deficiencies, if any, in those components of the audits and to determine whether the results of those reviews indicated deficiencies in the design or operation of the Firm's system of quality control over audits. In addition, the inspection included reviews of policies and procedures related to certain quality control processes of the Firm that could be expected to affect audit quality.

1. Review of Selected Audits

The inspection team reviewed aspects of selected audits, which it chose according to the Board's criteria. The Firm was not allowed an opportunity to limit or influence the engagement selection process or any other aspect of the review.

For each audit engagement selected, the inspection team reviewed the issuer's financial statements and certain SEC filings. The inspection team selected certain higher-risk areas for review and inspected the engagement team's work papers and interviewed engagement personnel regarding those areas. The areas subject to review included, but were not limited to, revenues, fair value, financial instruments, income taxes, reserves or estimated liabilities, inventories, consideration of fraud, related party transactions, supervision of work performed by foreign affiliates, and assessment of risk by the engagement team. The inspection team also analyzed potential adjustments to the issuer's financial statements that were identified during the audit but not corrected. For certain selected engagements, the inspection team reviewed written communications between the Firm and the issuer's audit committee. With respect to certain engagements, the inspection team also interviewed the chairperson of the issuer's audit committee.

When the inspection team identified a potential issue, it discussed the issue with members of the engagement team. If the inspection team was unable to resolve the issue through this discussion and any review of additional work papers or other documentation, the inspection team issued a comment form on the matter and the Firm provided a written response to the comment form.

2. Implementation of AS No. 5

Shortly after the approval of AS No. 5, members of the Board's Office of the Chief Auditor and of the Division of Registration and Inspections reviewed documentation of the Firm's initial approach to the implementation of AS No. 5 and provided feedback to the Firm's National Office. Field inspection procedures in this area began with discussions with members of the Firm's leadership to address specific areas of inspection emphasis and the appropriate use of auditor judgment, and to outline planned communications with the Firm. The reviews of certain audits included discussions with engagement teams and the review of documentation regarding the following aspects of the Firm's audit of internal control over financial reporting: (1) risk assessment; (2) risk of fraud; (3) entity-level controls; (4) the nature, timing, and extent of tests of controls; and (5) evaluating and reporting deficiencies. The inspection team discussed its observations about the effectiveness of the implementation of AS No. 5 with the engagement teams, with emphasis on areas where implementation could be improved in subsequent audits. Periodically the observations were summarized and discussed with the Firm's National Office.

3. Review of Firm Management and Monitoring Processes Related to Audit Quality Control

The inspection team's approach to its review of the Firm's system of quality control was intended to further its understanding of how the Firm manages audit quality, so as to enhance its basis for assessing, in this year and in future years, whether that system is appropriately designed and implemented to achieve the goal of conducting audits that are in compliance with applicable standards. The inspection team also continued its assessment of the Firm's processes and controls that relate to certain specific functional areas that relate to audit performance. The overall approach was designed to identify possible defects in the design or operation of the Firm's system of quality control, while also continuing and enhancing the evaluation of the Firm's ability to respond effectively to indications of possible defects in its system of quality control.

a. Review of Business Management

The objectives of the inspection procedures in this area were (a) to obtain an enhanced understanding of how the Firm's management is structured and operates the Firm's business, and the implications that the management structure and processes have on audit performance and (b) to continue assessing whether actions and

communications by the Firm's leadership – the Firm's "tone at the top" – demonstrate a commitment to audit quality. Toward that end, the inspection team interviewed members of the Firm's national, regional, and local leadership to obtain an understanding of the Firm's approach to, and processes for, its management, including the various management committees or other mechanisms, formal or informal, that relate to assessing and monitoring audit performance, or that otherwise affect audit performance. The inspection team also obtained and reviewed significant management reports and documents, as well as information regarding financial metrics and the budget and goal setting processes that the Firm uses to plan for, and evaluate the success of, its business.

b. Review of Partner Management

The objectives of the inspection procedures in this area were (a) to continue to assess whether the design and application of the Firm's processes related to partner evaluation, compensation, admission, termination, and disciplinary actions could be expected to encourage an appropriate emphasis on audit quality and technical competence, as compared to marketing or other activities of the Firm; (b) to assess the Firm's quality controls over the allocation of its partner resources; and (c) to identify and assess the accountability and responsibilities of the different levels of Firm management with respect to partner management. The inspection team interviewed members of the Firm's management, as well as audit partners in practice offices, regarding these topics. The inspection team's interviews of audit partners included their time and responsibilities and the interviews of practice office management included the performance of the partners being inspected, the evaluation and compensation process, any disciplinary actions, and any situations where client management requested a change in the lead audit partner. In addition, the inspection team reviewed a sample of partners' personnel files, including files of partners who resigned or took early retirement and partners who had significant negative inspection results from recent internal and PCAOB inspections.

c. Review of Client Acceptance and Retention, Including the Firm's Risk-Rating System

The objectives of the inspection procedures in this area were to continue to assess whether the Firm appropriately considers and addresses the risks involved in accepting and retaining clients in the particular circumstances and to assess the Firm's responses to the risks identified, including the extent to which an observable link exists

between those risks and the audit procedures performed. Toward those objectives, the inspection team obtained an understanding of any changes in the acceptance and retention processes and evaluated the Firm's policies and procedures relating to the Firm's risk-rating systems. The inspection team interviewed members of the Firm's management and selected a sample of issuer audits to (a) evaluate compliance with the Firm's policies and procedures for identifying and assessing the risks involved in accepting or continuing the client and (b) observe whether the audit procedures were responsive to the risks identified during the process.

d. Review of Policies Related to Foreign Affiliates

The objective of the inspection procedures in this area was to evaluate the processes the Firm uses to ensure that the audit work that its foreign affiliates perform on the foreign operations of U.S. issuers is effective and in accordance with applicable standards. To accomplish its objective, the inspection team reviewed the Firm's policies and procedures related to its supervision and control of work performed by foreign affiliates on the operations of U.S. issuer clients, reviewed available information relating to the most recent foreign affiliated firms' internal inspections, interviewed members of the Firm's leadership, and reviewed the U.S. engagement teams' supervision and control procedures concerning the audit work that the Firm's foreign affiliates performed on a sample of audits. The inspection team also reviewed, on a limited basis, certain of the audit work performed by the Firm's foreign affiliates on the foreign operations of U.S. issuer clients.

e. Review of Firm's Processes for Monitoring Audit Quality

(i) Review of Processes for Identifying and Assessing Indicators of Deficiencies in Audit Performance

The objective of the inspection procedures in this area was to identify and assess the monitoring processes that the Firm considers to be significant to its ability to monitor audit quality for individual engagements and for the Firm as a whole. Toward that objective, the inspection team interviewed members of the Firm's management to build on its understanding of how the Firm identifies, evaluates, and responds to possible indicators of deficiencies in audit performance, including internal inspection findings, PCAOB inspection observations, restatements, and litigation. In addition, the inspection team reviewed documents related to the design, operation, and findings of the Firm's

internal inspection program, and reviewed certain audits that the Firm had inspected and compared the results to those of the Firm.

(ii) Review of Response to Weaknesses in Quality Control

The objectives of the inspection procedures in this area were to assess the design and test the effectiveness of the Firm's processes for addressing possible deficiencies in the Firm's system of quality control, including any deficiencies in the Firm's system of quality control that were noted in prior PCAOB inspection reports. Toward those objectives, the inspection team reviewed steps the Firm has taken in the past several years to address possible quality control deficiencies. The inspection team then assessed the design and evaluated the effectiveness of the processes identified. In addition, the inspection team conducted focused inspections of audits of certain issuers whose audits had been reviewed during previous PCAOB inspections of the Firm to ascertain whether the audit procedures in areas with previous deficiencies had been improved.

(iii) Review of Certain Other Policies and Procedures Related to Monitoring Audit Quality

The procedures in this area included obtaining an update of the inspection team's understanding of policies, procedures, and guidance related to the Firm's independence requirements and its consultation processes and the Firm's compliance with them. In addition, the inspection team reviewed documents, including certain newly issued policies and procedures, and interviewed Firm management to update its understanding of the Firm's methods for developing audit policies, procedures, and methodologies, including internal guidance and training materials.

APPENDIX B

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.^{9/}

^{9/} 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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May 27, 2009

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Re: Response to Public Company Accounting Oversight Board (PCAOB) Draft Report on 2008 Inspection of
KPMG LLP

Mr. Diacont:

We appreciate the opportunity to read and comment upon the PCAOB's Draft Report on the 2008 Inspection of KPMG LLP dated April 24, 2009 ("Draft Report"). We share a common objective – serving our capital markets by performing high quality audits – and we value the input and information provided by the PCAOB in connection with its inspection process.

We acknowledge the professionalism and commitment of the PCAOB inspection staff and the important role the PCAOB plays in improving audit quality. We would also like to recognize the people of KPMG and the effort they expend to perform high quality audits in an increasingly challenging environment.

We recognize that professional judgments are involved in both the performance of an audit and the PCAOB's inspection process. In specific circumstances, we may have differing views on the assessment of audit risk, the materiality of particular issues in the context of the financial statements taken as a whole and the related nature and extent of necessary auditing procedures, resulting conclusions, and/or required documentation. We also understand that the comments made on individual Issuers cannot by their nature include a description and analysis of all procedures performed in a particular audit area.

As we previously communicated to the PCAOB, we conducted a thorough review of the matters identified in the Draft Report and addressed the engagement-specific findings in a manner consistent with PCAOB auditing standards and KPMG policies and procedures. Based on this review, in some cases, we performed additional audit procedures and/or supplemented our audit documentation; in other cases, we determined that no remediation was necessary.

None of the matters identified by the PCAOB required the reissuance of any of our previously issued reports.

In the past several years, we have further strengthened our commitment to quality. We remain dedicated to evaluating our systems of quality control, monitoring audit quality and implementing changes to our policies and practices in order to enhance audit quality. We have taken these actions mindful of our responsibility to the capital markets. We are committed to continually improving our firm and the profession and working constructively with the PCAOB to improve audit quality.

Very truly yours,

KPMG LLP