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Report on

2009 Inspection of KPMG LLP
(Headquartered in New York, New York)

Issued by the

Public Company Accounting Oversight Board

October 5, 2010

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. 104-2010-132



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.



2009 INSPECTION OF KPMG LLP

In 2009, the Board conducted an inspection of the registered public accounting firm KPMG LLP ("KPMG" or "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, Appendix B, and portions of Appendix C. Appendix B provides an overview of the inspection process. Appendix C 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") conducted primary procedures for the inspection from October 2008 through September 2009. The inspection team performed field work at the Firm's National Office and at 26 of its approximately 87 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 B 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 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 reviews of aspects of 60 audits performed by the Firm. 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.

In reviewing the audits, the inspection team identified matters that it considered to be audit deficiencies.^{5/} Those deficiencies included failures by the Firm to identify or appropriately address errors in the issuer's application of GAAP, including, in some cases, errors that could be material to the issuer's financial statements. 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, and in at least one instance, follow-up between the Firm and the issuer led to a change in the issuer's accounting or disclosure practices.^{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.

Issuer A

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 test whether the components of the issuer's allowance for loan losses ("ALL") appropriately reflected each of the significant environmental factors, and whether any of the factors were duplicated. In addition, with respect to certain components of the ALL, the Firm failed to assess the reasonableness of certain significant assumptions, including the time period for inherent losses to be recognized, the probability-of-default rates, and the collateral-value adjustment factors, and to test the completeness and accuracy of loan data that the issuer used to calculate these components.

(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.

- The Firm failed to perform adequate audit procedures to test the issuer's estimates of fair values of financial instruments as described below:

For certain less liquid financial instruments, the Firm failed to obtain an understanding of how the issuer's outside pricing services, or the pricing services used by the Firm, developed their fair value measurements, including whether the fair value measurements were determined using quoted prices from active or inactive markets, prices for similar assets, or were based on a model. For certain other less liquid financial instruments, the Firm failed to (1) determine whether the securities used as pricing references were comparable to the issuer's specific securities, (2) determine the sensitivity of the fair value estimates to the related discount margins in light of the significant spreads in the margins, and (3) test any of the other assumptions underlying the fair value measurements.

The Firm's samples selected at year end for fair value testing failed to include certain types of securities and certain portfolios of loans held for sale, notwithstanding their significance and the risks associated with estimating their fair value.

In addition, for certain mortgage-backed securities resulting from loans the issuer had securitized the Firm failed to test management's assertion that the recorded value, which equaled the book value of these securitized loans, represented fair value.

- Regarding the issuer's off-balance sheet structures, the Firm failed to perform adequate tests of controls over, or perform other procedures (beyond inquiry of management) to test, the issuer's process for identifying events affecting continued off-balance sheet accounting treatment and the completeness of the issuer's inventory of off-balance sheet structures. Specifically, the controls tested were entity-level controls that were not precise enough to identify all such events or structures. In addition, the Firm failed to test the issuer's on-going compliance with certain of the qualifications for the off-balance sheet accounting used for Qualifying Special Purpose Entities, including servicing activities, clean-up calls, limits on asset sales, amendments, and events of default. In addition, the Firm failed to sufficiently test the issuer's assertion that it was not the primary beneficiary of a variable interest entity because the Firm did not test the reasonableness of the entity's expected losses as estimated by the issuer,

despite indicators of an increase in the risk that the variable interest entity would be required to be consolidated.

- The issuer securitized and sold financial instruments using off-balance sheet entities. The Firm failed to obtain written corroboration from legal counsel that the financial instruments involved in certain of these complex transactions were isolated from the issuer even in bankruptcy or other receivership.
- Regarding the test of goodwill for impairment:

The Firm failed to identify and appropriately address that the issuer's methodology for testing goodwill for impairment did not comply with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ("SFAS No. 142"). The issuer's methodology to determine the carrying value of its reporting units did not take into consideration the different risk profiles of the reporting units and did not reflect a market participant's view of the differing risks associated with operating the various businesses. In addition, the method for determining the carrying value of the reporting units was inconsistent with the method used for determining the fair value of the reporting units.

In the first quarter of the subsequent fiscal year, the issuer revised certain assumptions underlying its fair value estimates of some of these same reporting units, which increased their estimated fair value from year end. The Firm failed to test certain assumptions underlying the fair value estimates used in the year-end goodwill impairment tests and to evaluate the appropriateness of the changes in certain of those assumptions from the year-end impairment test to the first-quarter impairment test in light of the continued deteriorating performance of the issuer.

Issuer B

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 sufficiently test the issuer's year-end goodwill impairment analysis. A significant portion of the increase in the issuer's capital during the year was allocated to a reporting unit that had experienced recent significant

losses and whose assets had significant inherent risk and volatility. Despite these factors, the issuer's valuation of this reporting unit assumed that it had significant excess capital that could be distributed to a market participant within a year. The Firm, however, failed to take into account that this assumption was inconsistent with the issuer's own projections of capital needs. Also, the Firm failed to evaluate whether this assumption, together with other significant assumptions used by management in measuring the fair value of this reporting unit, provided a reasonable basis for the fair value measurement.

- The Firm failed to sufficiently test the issuer's valuation of deferred income tax assets. The issuer concluded that realization of the recognized net deferred tax asset was more likely than not based on projections of future taxable income and available tax planning strategies. Despite recent losses, the Firm failed to test, beyond inquiry of management, certain significant assumptions underlying the projections of future taxable income. With respect to the tax planning strategy to realize gains from the sale of business units, the Firm failed to perform procedures, beyond inquiry of management, to evaluate the reasonableness of the issuer's strategy. Further, the estimated fair values of the business units used to determine the gains were based on the same valuations used in the goodwill impairment analyses; deficiencies in the Firm's testing of one of these valuations are discussed above.
- The Firm failed to perform sufficient procedures to test the issuer's valuation of financial instruments. The degree of reliance the engagement team placed on the issuer's price verification and model validation controls over financial instruments valued using unobservable inputs ("Level 3 financial instruments") was inappropriate because the Firm failed to test certain important aspects of the price verification controls and failed to complete its testing of the model validation controls. In addition, many of the samples the Firm used in its substantive tests of the valuation of various types of the Level 3 financial instruments were insufficient (sometimes a sample of only one item) in light of the significance and complexity of the instruments and the heightened risk the Firm identified with respect to their valuation.

Issuer C

In this audit, the Firm failed to sufficiently test the fair value measurements of the issuer's significant investments in debt and equity securities of private companies.

Specifically, the Firm failed to test significant data on which certain of the fair value measurements were based. For some investments, the investees' unaudited financial results were a significant factor in determining the fair value measurements, but the Firm failed to apply, or request that the issuer arrange with the investee to have another auditor apply, auditing procedures to such financial results. Another significant assumption in the fair value measurements of certain investments was a valuation multiple derived by the issuer; however, in some instances the Firm failed to test the data used to derive the multiple. For another investment, the Firm failed to test the projected cash flows and underlying assumptions used in estimating the fair value. In another instance, the Firm failed to evaluate whether the issuer's approach of averaging the prior year's financial data with the current year's projected data was appropriate when estimating the fair value of an investment given that the projections indicated a decline in the investee's earnings.

In addition, in testing the reasonableness of the discount rates the issuer used to estimate the fair value of certain collateralized loan obligations, the Firm noted that market information suggested that a higher discount rate may be more appropriate, but it deemed the discount rate used by the issuer to be reasonable based on general, unquantified information.

Issuer D

In response to concerns raised by a member of the issuer's Board of Directors and the Firm, the issuer revised the discount rates that the issuer used in its discounted cash flow models to estimate the fair values of its residual and other interests in asset-backed loan securitizations (the "retained interests"). (The effect of this revision was to reduce the estimated fair values of the retained interests.) The Firm failed to sufficiently evaluate the reasonableness of these revised discount rates. Specifically, the issuer and the Firm evaluated the discount rates, in part, by comparing them to the discount rates used by the issuer's competitors, noting that they were consistent. The Firm, however, failed to evaluate whether this consistency was appropriate, in light of indicators that the issuer's retained interests were of higher risk than those of its competitors, including the presence of significantly greater downgrades by rating agencies of the issuer's securities and the poor financial condition of the guarantor of the issuer's securities.

In addition, the Firm's valuation specialist raised concerns about the significant difference between the discount rates the issuer used to estimate the fair value of its

two different types of retained interests. The Firm accepted the different discount rates used by the issuer without obtaining evidence that justified the amount of the difference between the rates.

Deficiencies in testing pension plan assets (two audits)

In two audits, due to deficiencies in testing the fair value of 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 assessed control risk below the maximum, but it failed to obtain a service auditor's report for the trustee of the plan assets or, alternatively, to identify and test controls over the valuation of the pension plan assets held by the trustee. The Firm also failed to test the valuation of two individually significant assets, which constituted approximately half of the plan assets. [Issuer E]
- In another audit, the Firm assessed control risk below the maximum, but it failed to obtain a service auditor's report for the trustee of the plan assets or, alternatively, to identify and test controls over the valuation of the pension plan assets held by the trustee. The Firm also failed to obtain an understanding of the issuer's process for valuing pension plan assets that did not have quoted market prices in active markets. Finally, the Firm's substantive tests were insufficient because it did not test the valuation of hard-to-value investments. [Issuer F]

Issuer G

In this audit, the Firm failed to identify that the issuer performed its annual goodwill impairment analysis inappropriately in that the issuer's allocation of goodwill to its reporting units was not in conformity with SFAS No.142.

Issuer H

In this audit, the Firm failed to sufficiently test the existence of the issuer's cash, cash equivalents, and marketable securities, which constituted approximately half of the issuer's total assets. Specifically, while the Firm obtained a confirmation from the issuer's investment adviser, it failed to confirm these assets with the custodian of the assets or to perform other procedures to test the existence of these assets.

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 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, independence policies and procedures, 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

PART II, PART III, AND APPENDIX A OF THIS REPORT ARE NONPUBLIC
AND ARE OMITTED FROM THIS PUBLIC DOCUMENT

APPENDIX B

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 of financial statements and of internal control over financial reporting, 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, revenue, fair value measurements, 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. 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 Management Structure and Processes, Including the Tone at the Top

The objectives of the inspection procedures in this area were (a) to update the inspection team's 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 those ends, the inspection team interviewed members of the Firm's national leadership to obtain an understanding of any significant changes in 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.

b. Review of Practices for Partner Management, Including Allocation of Partner Resources and Partner Evaluation, Compensation, Admission, and Disciplinary Actions

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 and reviewed and also evaluated documentation regarding certain of these topics.

In addition, the inspection team reviewed a sample of partners' personnel files, including files of partners who resigned and partners who had significant negative inspection results from recent internal and PCAOB inspections.

- c. Review of 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

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 the identified risks of material misstatement and the audit procedures performed. Toward those objectives, the inspection team obtained an understanding of any changes in the acceptance and retention processes, evaluated the Firm's policies and procedures relating to the Firm's risk-rating systems, and interviewed members of the Firm's management.

- d. Review of 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

The inspection team performed procedures in this area with respect to 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. For its procedures in this area, 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 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.

- e. Review of the Firm's Processes for Monitoring Audit Performance, Including Processes for Identifying and Assessing Indicators of Deficiencies in Audit Performance, Independence Policies and Procedures, and Processes for Responding to Weaknesses in Quality Control
 - (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 continue 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 and reviewed certain documents 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 evaluation of findings of the Firm's internal inspection program. The inspection team also 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 interviewed members of the Firm's national and regional leadership and conducted focused inspections of audits to assess the design and 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

In this area, the procedures included obtaining an update of the inspection team's understanding of policies, procedures, and guidance related to aspects of 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 audit 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 C

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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September 22, 2010

Mr. George H. Diacont
Director
Division of Registration and Inspections
Public Company Accounting Oversight Board
1666 K Street, N.W.
Washington, DC 20006

Re: Response to Part I of Public Company Accounting Oversight Board (PCAOB) Draft Report on 2009 Inspection of KPMG LLP

Dear Mr. Diacont:

We appreciate the opportunity to read and comment on Part I of the PCAOB's Draft Report on the 2009 Inspection of KPMG LLP dated August 23, 2010 ("Draft Report"). We share a common objective – serving our capital markets by performing high quality audits – and the PCAOB's inspection process serves to assist us in identifying areas where we can continue to improve our performance and strengthen our system of quality control. We would also like to acknowledge the professionalism and commitment of the PCAOB inspection staff and the important role the PCAOB plays in improving audit quality.

We recognize that professional judgments are involved in both the performance of an audit and the PCAOB's inspection process, and that professionals may reach different conclusions regarding the sufficiency of audit evidence obtained or other assessments made in an audit. 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 evaluation 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.

We remain dedicated to evaluating our system of quality control, monitoring audit quality and implementing changes to our policies and practices in order to enhance audit quality. We are mindful of our responsibility to the capital markets and 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

cc: Mr. Daniel L. Goelzer
Mr. Bill Gradison
Mr. Steven B. Harris
Mr. Charles D. Niemeier