



ASIC

Australian Securities & Investments Commission

KPMG Australia

Audit inspection report for 2018-19

December 2019

About this report

This report summarises findings from our reviews of key areas in audits at KPMG Australia (KPMG) in the 12 months to 30 June 2019.

This report also lists any findings from our reviews of financial reports audited by the firm in the 12 months to 30 June 2019.

Although this report may describe deficiencies identified, this should not be taken to provide assurance that the firm's audits and systems, or audited financial reports, are free of other deficiencies.

This report is intended to communicate our findings in a clear and concise manner to leadership of the firm who are informed auditing and accounting professionals. While there are no restrictions on the firm providing this report to third parties or releasing the report to the public, other readers of this report may not have the full context of this report and the findings summarised herein.

ASIC Information Sheet 224 *ASIC Audit Inspections* and ASIC Report 648 *Audit inspection report for 2018-19* provide further information on our audit firm inspection process.

Background

- 1 ASIC’s audit inspections involve the review of key areas in the audits of listed entities and other public interest entities.
- 2 This report summarises our findings from audit reviews substantially completed in the 12 months to 30 June 2019, and financial reporting surveillances relating to entities audited by KPMG completed in the 12 months to 30 June 2019. If it has not already done so, the firm should identify underlying root causes for the matters reported, and for findings from internal reviews, and implement new and improved actions to achieve sustainable improvements in audit quality.
- 3 For more information refer to the detailed comment forms provided separately to the firm (matters in Tables 1 and 2). The comment forms include the firm’s response to our findings.
- 4 This report does not include details of enforcement actions (if any) involving members of the firm that may have been underway or finalised in the 12 month period.

Audit file review findings

- 5 In our view, the auditor did not obtain reasonable assurance that the financial report was free of material misstatement in 12 of the 36 key areas reviewed in total across 10 audits reviewed at the firm (33% of the key areas reviewed). A limited number of audits and audit areas were selected for review on a risk basis, and so caution is needed in generalising from the results to all audits conducted by the firm and all areas of those audits.
- 6 Table 1 summarises the findings. The firm did not necessarily agree with all of our findings. The findings should not be taken to infer that the financial report was materially misstated, but rather that the auditor did not obtain sufficient evidence to support their opinion.

Table 1: Audit file review findings – risk of material misstatement

Entity	Areas with findings	Findings
Entity A	1 of the 4 key areas reviewed	<ul style="list-style-type: none"> • <i>Inventories work in progress</i> - the auditor did not obtain sufficient evidence on existence and valuation of work in progress inventory and incorrectly applied an expected loss percentage to the closing quantity of raw materials rather than to raw material used.

Entity	Areas with findings	Findings
Entity B	2 of the 3 key areas reviewed	<ul style="list-style-type: none"> • <i>Construction revenue</i> – the auditor did not perform adequate substantive tests on the completeness, accuracy and existence of costs incurred and estimated forecast costs to complete, which are key to the calculation of percentage of completion contracts and revenue recognised. • <i>Goodwill impairment</i> – the auditor did not obtain sufficient evidence over goodwill arising from a business combination. The auditor relied on the proximity of a recent acquisition to the reporting date as evidence of the fair value of the business acquired, a planned earnout rate being exceeded (but with inadequate testing of revenue), and a due diligence report by another accounting firm on future maintainable earnings, without further challenge.
Entity C	1 of the 4 key areas reviewed	<ul style="list-style-type: none"> • <i>Financial instruments valuation</i> – the auditor did not obtain sufficient evidence to support the assessment of low control risk over the valuation of derivative financial instruments, use an adequate sample size for the substantive testing, ensure rates or inputs tested were those used in the entity's valuation system, test an appropriate sample to provide sufficient evidence on the rates accuracy and valuation of the remaining population, or verify or test the inputs and calculation of two key components of the cash flow hedge reserve.
Entity D	2 of the 5 key areas reviewed	<ul style="list-style-type: none"> • <i>Valuation of biological assets</i> – the auditor did not obtain sufficient evidence over the quantity of biological assets. • <i>Impairment of non-financial assets</i> – the auditor did not adequately assess the impact of a decision by management after balance date to suspend processing operations.
Entity E	1 of the 2 key areas reviewed	<ul style="list-style-type: none"> • <i>Share based payments</i> – the auditor did not adequately assess indicators of a possible implicit service condition existing in an option arrangement which would have resulted in the recognition of an expense.
Entity F	2 of the 2 key areas reviewed	<ul style="list-style-type: none"> • <i>Impairment of assets</i> – the auditor did not undertake appropriate testing of management's estimate to conclude on the reliability of values which were a significant input in the fair value estimate, cross check values against other sources, and adequately consider the methodology adopted by an external information source in establishing these values. • <i>Revenue</i> – the auditor did not set expectations that were sufficiently precise in a substantive analytical procedure (SAP), demonstrate that prior year average revenue per customer was a sufficiently plausible relationship to predict current year revenue, adopt a consistent approach in setting thresholds for identifying variances to be investigated, or evaluate the reliability of external data used to support changes in prices. The auditor did not adequately assess the appropriateness of recognising specific types of revenue in advance or adequately test management's calculations.

Entity	Areas with findings	Findings
Entity H	1 of the 3 key areas reviewed	<ul style="list-style-type: none"> <i>Revenue</i> – the auditor did not set expectations that were sufficiently precise in a SAP, demonstrate that prior year average revenue per unit was a sufficiently plausible relationship to predict current year revenue, evaluate the reliability of external price information used to explain changes in revenue, evidence their consideration of the suitability of using cash receipts to predict revenue or adequately review another auditor’s work on material overseas revenue.
Entity I	1 of the 4 key areas reviewed	<ul style="list-style-type: none"> <i>Purchase price allocation</i> – the auditor did not adequately assess the judgements and key assumptions for values attributed to the individual assets in a business combination, perform sufficient procedures when a cross check did not support key assumptions or assess the competence, capabilities and objectivity of an investment bank whose model was used as audit evidence.
Entity J	1 of the 5 key areas reviewed	<ul style="list-style-type: none"> <i>Carrying value of non-current assets</i> – there is no evidence that the group auditor reviewed the work of an overseas auditor on asset values, the entity’s impairment model or experts’ reports supporting that model.

- 7 Our audit file review findings which did not involve risk of material misstatements are summarised in Table 2. These findings include matters that could be relevant to obtaining reasonable assurance for the audited entity in future or another audited entity.

Table 2: Audit file review findings – other

Entity	Findings
Entity G	<ul style="list-style-type: none"> <i>Bill and hold revenue</i> – the auditor did not sufficiently understand bill and hold arrangements, adequately test bill and hold records, sufficiently document whether payment had been received, stock delivered and transactions included in the bill and hold records, or adequately document attendance at stock counts.

Financial report findings

- 8 We completed risk-based reviews of aspects of 36 financial reports of listed and other public interest entities audited by the firm in the 12 months to 30 June 2019. There were no material changes to net assets or profit as a result of our inquiries.