



# Audit quality

**Our hands-on process**  
of maintaining integrity,  
independence, ethics,  
objectivity, skepticism  
and quality performance





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# The many aspects of audit quality

**At KPMG, building and maintaining a culture of quality is central to what we do.**



In their 2014 inspection of Big Four engagement files, CPAB found an overall improvement in audit quality, including a 36% decline over the previous year in files with significant audit deficiencies and an overall decline of more than two-thirds since issuing its 2011 mandate to improve audit quality.<sup>1</sup>

That's why we're pleased that you've taken an interest in our **Audit Quality** report. Through this report, you can learn about our firm's ongoing commitment to continuous audit quality improvement – a commitment that is regularly honed and upheld by our 2,500+ audit professionals across the country. Together and as individuals, we believe we make a difference through the work we do. Our professionals consistently work to meet the highest quality standards and their efforts enable us to improve audit quality each year.

To be sure, some of these quality improvements are due to the ongoing focus on auditor performance. The Canadian Public Accountability Board (CPAB), in particular, regularly inspects the quality of audits conducted by public accounting firms and has played a large role in helping firms like ours improve audit quality and maintain the public's trust in the capital markets.

Other initiatives, such as Data and Analytics (D&A) have also played a role. KPMG has provided D&A-enabled training to all audit partners and managers across the country and we continue to embed it into our audit process. With the capability of the D&A audit to provide insight into 100% of the available data population rather than selected samples, it is now largely accepted as a critical tool for enhancing audit quality.

KPMG also continues to challenge our practitioners and provide innovative opportunities for learning, training and coaching, including e-learning and other methods tailored to individual needs. And as our KPMG professionals get better, so do the tools we provide them with. For example, eAudit leverages our teams' wisdom, industry knowledge and technical skills, embedding standards directly into customizable electronic audit workflows, ensuring the right questions are asked and all critical information is included.

We are also committed to staying at the forefront of audit developments on every stage, from regulatory change and client impacts to audit improvement initiatives. For example, audit committees are serious about realizing the recommendations of the Audit Committee Working Group – arising from the CICA/CPAB initiative to enhance audit quality – in areas such as conducting more rigorous assessments and improving audit transparency. We fully support these efforts and continue to learn from the process.

Yet, despite the improvements achieved to date, we firmly believe that audit quality must continue to evolve to meet the increasingly complex issues our clients face and the rising expectations of investors, audit committees and management teams. It is in response to our teams, our clients and our regulators that we continue to refine our approach to audit quality, not only by expanding the use of D&A in our audits, but by enhancing the reports and other deliverables we produce and taking proactive steps to attract and retain the most qualified professionals in the industry.

The audit profession has rarely faced a landscape of so many converging challenges, but KPMG firmly believes that our innovative approach, clear purpose and dynamic vision will enhance audit quality and make a real, lasting difference as businesses and markets continue to evolve. In this way, we hope not only to foster enhanced independence, objectivity and ethical behaviour, but also to contribute to the maintenance of public and stakeholder confidence in our capital markets.

CPAB noted in its 2014 public report, “With greater focus being placed on audit quality, the expectations of participants have changed as well, causing closer examination of the roles and responsibilities of all those involved in financial reporting.”<sup>2</sup>

Yours truly,



Kristen Carscallen  
Canadian Managing Partner, Audit



Because our professionals are the most important element of the quality service we provide, our system of audit quality control is designed to help them succeed.

# A commitment to quality

**Our operating and leadership structure is designed to enable our professionals to provide outstanding client service while responding to the evolving economic and regulatory environment in which we compete.**

In addition to supporting our one-firm approach, this structure allows us to maintain the safeguards we need to monitor our business practices so we can meet the needs of the marketplace, reinforce our sense of partnership and deliver on our commitment to quality – to each other, our clients and the capital markets we serve. Our operating structure separates risk management and compliance from operations at the highest levels of the firm to help ensure appropriate checks and balances in our governance. We have assigned roles and responsibilities to specific groups within this structure to help ensure that we fulfil our professional obligations.

Because our professionals are the most important element of the quality service we provide, our system of audit quality control is designed to help them succeed. It incorporates components implemented and operated by our audit practice as well as components administered by our other firm functions, including our Quality and Risk Management Group.

## **Inside our audit practice**

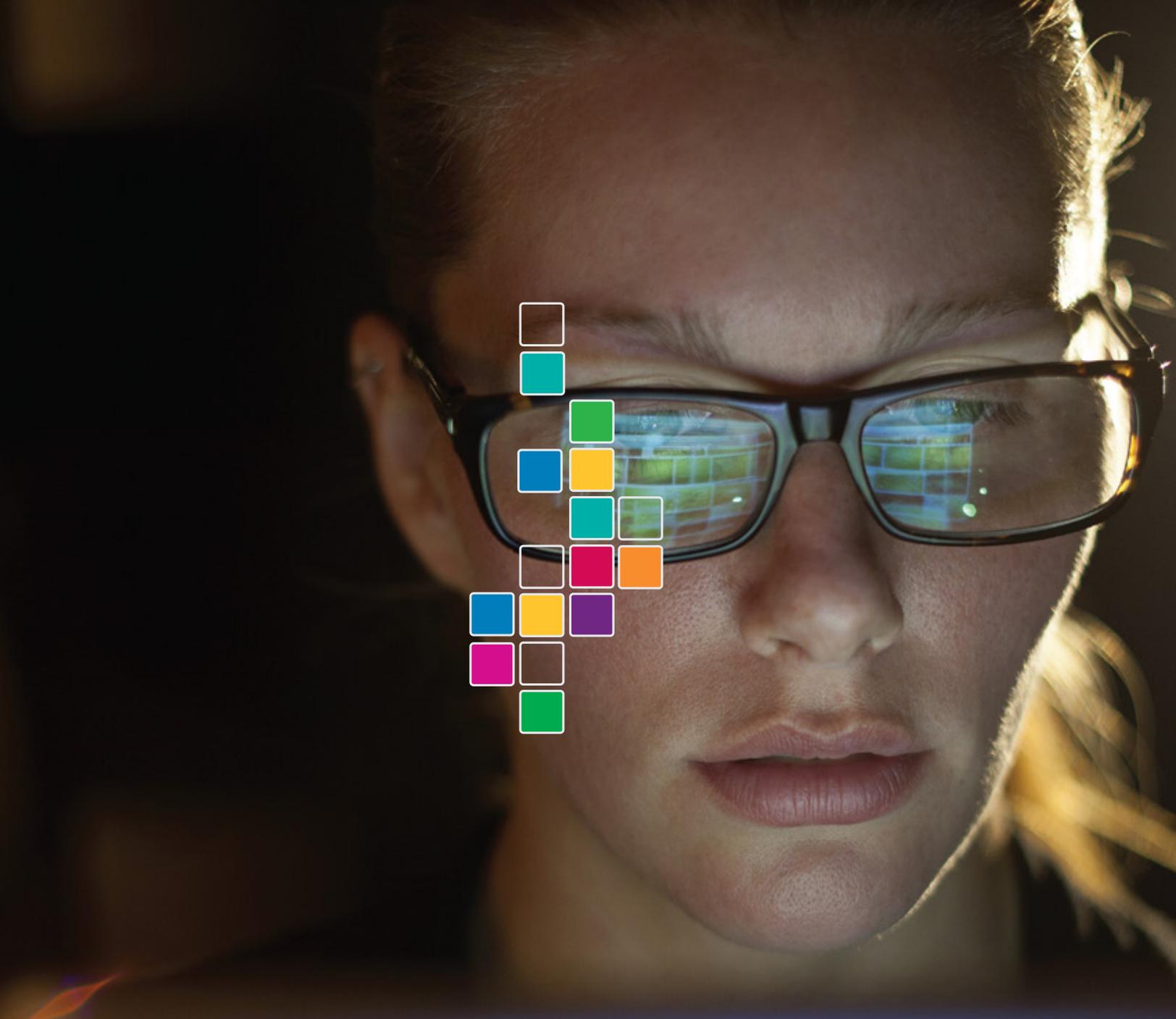
The key components of KPMG's system of audit quality control embedded within KPMG in Canada's audit practice are:

- **KPMG International's Global Services Centre**, which develops the methodologies and supporting technology tools used in our audit service processes
- **Global Audit Quality Framework**
- **Our Audit Quality and Professional Practice Network**
- **Department of Professional Practice (DPP)**
- **Professional Practice Partners**
- **Audit Quality Council**
- **Local Audit Quality Groups** and our Accounting and Audit Technical Topic Team members in the various geographies.

## **Outside our audit practice**

The key components of our system of audit quality control administered by functions outside the audit practice are:

- **KPMG's Code of Conduct**, which defines the values and standards by which KPMG fulfils its professional obligations and outlines the resources available to help partners and employees comply with them
- **Independence Policies**, supported by systems to facilitate firm and personnel compliance with applicable independence requirements
- **Our Quality and Risk Management Group-Audit**, which is responsible for oversight and monitoring of our audit practice as well as certain firm-wide processes to manage risk.



The audit practice is supported by a network of senior partners who provide professional practice and audit quality leadership.

# Audit quality control

**To ensure every partner and employee concentrates on the skills and behaviours needed to deliver an appropriate, robust and independent opinion, KPMG has developed a global Audit Quality Framework.**

## Audit Quality Framework

The seven drivers in this framework give KPMG member firms a common language to describe what we believe drives audit quality and, importantly, to highlight how every one of us at KPMG contributes to the delivery of audit quality.

KPMG's system of audit quality control not only reflects our drive and determination to deliver independent, unbiased assurance and opinions, but also meets the requirements of regulations and professional standards.

Audit quality is integral to our business and is the responsibility of every one of us. Our training, processes, systems and controls are all designed to provide objective, independent advice and opinions on which stakeholders can rely.



KPMG's System of Audit Quality Control provides the Canadian firm with reasonable assurance of complying with regulations, professional standards and firm policies by encompassing:

- **Leadership Responsibilities** or quality within the firm (the "tone at the top")
- **Engagement Performance**
- **Relevant Ethical Requirements**
- **Human Resources**
- **Acceptance and Continuance** of client relationships and specific engagements
- **Monitoring**

**Our Canadian Managing Partner (CMP) of Audit**, who reports to the CEO of the firm, has ultimate responsibility for our Audit practice, which includes our system of audit quality control.

**Our National Managing Partner in Charge of Professional Practice**, who reports to the CMP of Risk Management, is responsible for accounting and auditing standards and their interpretation, as well as for promoting technical excellence and quality service delivery through training and accreditation, investment in technical support, development of Risk Management, accounting and auditing specialist networks and effective consultation processes.

**Our CMP of Risk Management** works closely with the CMP of Audit to initiate, shape and lead our initiatives to enhance the quality and effectiveness of our audit practice and to provide ongoing support to our audit activities across the country.



We exercise professional skepticism throughout the audit in gathering and objectively evaluating the competency and sufficiency of audit evidence obtained.

### **Audit Quality and Professional Practice Network**

The audit quality and professional practice network consists of more than 130 partners, directors, senior managers and other professionals who support the firm's audit professionals in meeting their responsibilities in the areas of auditing and attestation, accounting and financial reporting, securities including Canadian and SEC reporting matters, continuous improvement in audit quality and internal and external inspection processes.

### **Department of Professional Practice (DPP)**

DPP develops firm standards and guidance relating to accounting, auditing, securities and quality matters; provides technical guidance to engagement teams on engagement-specific issues; develops and disseminates topic-specific guidance on emerging technical, professional and quality issues; and assists with firm and individual issues pertaining to compliance with regulatory and professional standards. Through liaisons with the KPMG global network, as well as active participation in Canada's standards-setting processes, DPP professionals develop and represent KPMG's positions on current topics being addressed by regulatory and other standard-setting bodies. In addition, DPP professionals actively liaise with the KPMG International Standards Group, located in London, on international accounting

and auditing standards matters, and with professionals in the Department of Professional Practice, located in New York, on accounting and auditing standards matters related to the Financial Accounting Standards Board (FASB), the Public Company Accounting Oversight Board (PCAOB), the Emerging Issues Task Force (EITF) and the Auditing Standards Board of the AICPA.

### **Professional Practice Partners**

The audit practice is supported by a network of senior Professional Practice Partners who provide professional practice and audit quality leadership and direct adherence to firm policies and professional standards within their respective offices and regions.

The roles of our Professional Practice Partners are to (1) support and advise the partners on client-related matters, (2) assimilate information pertaining to the professional risks of the firm, (3) provide reasonable assurance that firm policies and professional standards are followed and (4) continuously review and seek to improve firm policies and processes. Local Audit Quality Groups and our Accounting and Audit Technical Topic Team members in the various geographies support the activities of our Professional Practice Partners by assisting teams, in conjunction with DPP, to resolve accounting and auditing matters and enhance audit quality.

### **Audit Quality Council**

The Audit Quality Council, chaired by the CMP of Audit, provides input to and oversight of issue identification, analysis and remediation relating to the most significant matters relative to audit quality and our system of audit quality control.

The Audit Quality Council oversees the:

- Accumulation and analysis of information relative to audit quality matters on a timely and consistent basis (e.g., from internal and external inspections, DPP consultations, litigation and regulatory matters)
- Analysis of such information and identification of common themes and related root causes
- Development of appropriately-focused remedial actions in response to those root causes
- Timely implementation, execution and effectiveness of the remedial action plans.

In addition, the Audit Quality Council, with the support of the local business unit Professional Practice Partners, helps identify particular characteristics of our audit engagement portfolio for which proactive risk assessment plans are developed (e.g., entities or industry sectors exhibiting higher risk characteristics).

# Quality control elements

**Every KPMG partner and employee is responsible for professional practice, risk management, and quality control and is expected to understand, apply and adhere to KPMG's policies and associated procedures at all times.**

Our policies reflect individual quality control elements to help KPMG partners and employees act with integrity, skepticism, and objectivity, perform their work with diligence, and comply with applicable laws, regulations and professional standards.

**This section summarizes those policies and procedures specific to our system of audit quality control.**

## **Engagement performance**

Fundamental to our audit quality is our system of audit quality control, which is embedded throughout the firm's audit engagement process.

Engagement performance encompasses all aspects of the design and execution of an audit engagement, including the firm's audit methodology and the review, supervision, consultation, documentation and communication of audit results.

## **The KPMG Audit**

KPMG International's Global Services Centre is comprised of professionals who develop and regularly update our global audit process methodologies in cooperation with KPMG International's Global Quality and Risk Management, the International Standards Group and Canada's DPP.

The KPMG Audit serves as the foundation for both KPMG in Canada's financial statement and integrated audit model.

Where applicable for SEC registrants, the KPMG Audit is an integrated audit model, which incorporates both the audit of an issuer's financial statements and the audit of internal control over financial reporting. Our integrated audit is enhanced through timely communications with the audit committee and management throughout the audit process.

In an integrated audit, we use our knowledge and experience to identify a number of different risks (e.g., inherent risk, control risk, fraud risk, and risk of failure of a control).

We assess each of these risks within a continuous range from lower to higher. The higher the risk, the more persuasive the audit evidence needs to be to mitigate that risk. We exercise professional skepticism throughout the audit in gathering and objectively evaluating the competency and sufficiency of audit evidence obtained, which includes both confirming and contradictory evidence.

The following discussion is a highly summarized depiction of our audit methodology workflow for both financial statement and integrated audits:

## **Risk Assessment**

- Obtain an understanding of the entity and its environment, including internal control
- Perform risk assessment procedures and related activities
- Identify and assess risks of material misstatement
- Design audit responses to address the assessed risks of material misstatement

## **Testing**

- Test operating effectiveness of selected controls
- Plan and perform substantive procedures

## **Completion**

- Perform completion procedures, including overall review of financial statements
- Document significant findings and issues
- Consider if audit evidence obtained is sufficient and appropriate
- Form an audit opinion
- Communicate to the audit committee or those charged with governance our responsibilities under applicable auditing standards, an overview of the planned scope and timing of the audit and significant findings from the audit

**The KPMG Audit addresses both manual and automated controls and integrates the firm’s information technology professionals and other specialists into the core audit engagement team when appropriate. Our audit includes procedures aimed at detecting and responding to fraud risks.**

The KPMG Audit also guides the conduct of audits of financial statements comprised of two or more components (group audits) and clearly delineates responsibilities relative to managing group audits and the involvement of the group audit engagement team in the work performed by the component auditor.

Our audit methodology includes policies and guidance related to those matters that merit special consideration in performing group audits, including identifying significant components, evaluating group-wide controls, evaluating aggregation risk, establishing group and component materiality and communicating with the component auditor.

**Supervision, review and support for the engagement team**

Supervision entails directing the efforts of professionals involved in meeting the objectives of the audit and determining whether those objectives are accomplished. Elements of supervision include instructing and guiding professionals, keeping informed of significant issues, reviewing the work performed, reconciling issues and agreeing on appropriate conclusions.

KPMG’s supervision and review guidelines for audit work include:

- Tracking the progress of an engagement
- Considering the capabilities and competencies of individual members of an engagement team
- Identifying matters for consultation or consideration by more experienced engagement team members
- Reviewing and approving engagement planning and risk assessment prior to the start of significant fieldwork
- Reviewing all audit documentation by a KPMG professional other than the preparer. The engagement partner’s responsibilities include reviewing audit documentation related to critical areas of judgement, significant findings and issues, and significant risks at the financial statement level and the relevant assertion level with respect to significant accounts and disclosures, including work performed by KPMG specialists relative to these significant risks
- Involving an engagement quality control review partner on financial statement and integrated audit engagements
- Preparing planning and completion documentation that summarizes significant issues, which are approved by various parties, including the engagement partner and engagement quality control review partner
- Performing in-depth technical reviews in certain situations, led by the engagement quality control review partner.



EQCR professionals are the Canadian firm's leading technical partners knowledgeable and experienced in accounting and reporting matters and auditing standards.

### **Engagement quality control review (EQCR)**

The EQCR partner has no responsibilities on the engagement other than those relating to performing an objective review of the financial statements, auditors' reports and certain audit documentation.

All partners who perform EQCR of reporting issuer audits have received training to serve in this capacity; these individuals are the Canadian firm's leading technical partners and are knowledgeable and experienced in accounting and reporting matters and auditing standards.

EQCR partners review certain audit documentation, the appropriateness of the financial statements and related disclosures, the key conclusions of the engagement team with respect to the audit, and the auditors' reports to be issued. Completion of an EQCR is documented when the EQCR partner believes that all significant questions raised have been satisfactorily resolved.

### **Consultation and differences of opinion**

Internal consultation with others is encouraged and in certain circumstances required. Technical support for each engagement team comes from a network that includes DPP as well as the Professional Practice Partners and Accounting and Auditing Technical Topic Teams.

The firm has established protocols for consultation regarding difficult or contentious accounting and auditing matters, including procedures to resolve differences of opinion on engagement issues. Consultation with a team member at a higher level of responsibility than either of the differing parties usually resolves such differences.

In circumstances where partners involved in the audit are unable to resolve an issue, the matter may be escalated for resolution to DPP.

### **Confidentiality, safe custody, integrity, accessibility and retrievability of engagement documentation**

KPMG's policies and Code of Conduct require its personnel to maintain the confidentiality of client or former client information, including privacy of personally identifiable information, in accordance with professional standards and applicable laws and regulations. The firm also requires its professionals to affirm that they understand and will comply with the firm's policies related to privacy and confidentiality at commencement of employment and as part of the annual compliance confirmation process.

Furthermore, the firm has implemented administrative, technical, and physical safeguards designed to protect the confidentiality and integrity of client and firm information.

In addition, our audit professionals are required to apply appropriate and reasonable controls to:

- Clearly determine when and by whom audit documentation was created, changed or reviewed
- Protect the integrity and confidentiality of information throughout the audit, especially when the information is shared within the engagement team or electronically transmitted to other parties
- Prevent unauthorized changes to audit documentation
- Allow access to documentation by an engagement team and other authorized parties as necessary to properly discharge their responsibilities.

### **Retention of engagement documentation**

The firm's formal document retention policy governs matters such as the retention period for audit documentation and other records relevant to an engagement in accordance with the relevant rules, standards and regulations.

# Independence

**KPMG's independence policies require that the Canadian firm, its partners and management group, and the personnel assigned to each audit engagement must be free from financial interests in and prohibited relationships with the client, its management, its directors and its significant owners.**

The firm requires adherence to applicable independence requirements and ethical standards, which meet or exceed the standards set by applicable regulatory bodies. These policies and procedures, which cover areas such as personal independence, post-employment relationships, partner rotation, and approval of audit and non-audit services, are monitored continuously to keep pace with current developments.

## Personal independence

-  Each professional is responsible for maintaining his/her personal independence
-  Partners, managers, and those providing professional services to an audit client may not have direct or material indirect investments in an audit client or its affiliates (e.g., restricted entities)
-  Certain other financial relationships with audit clients or affiliates of audit clients (e.g., loans, credit cards, insurance products and brokerage accounts) are either prohibited or subject to limitations
-  Close family members of certain KPMG partners and employees may not hold certain accounting or financial reporting roles with audit clients or their affiliates

## Post-employment relationship

-  KPMG professionals are required to report promptly to the firm any discussions or contacts between them and an audit client regarding possible employment
-  KPMG professionals engaged in discussions or negotiations regarding possible employment with an audit client are immediately removed from the audit engagement
-  If a professional accepts employment with a client, the ongoing engagement team gives active consideration to the appropriateness or necessity of modifying the audit procedures to adjust for risk of circumvention by the former professional of the firm
-  For certain reporting issuer audit clients, a former member of the audit engagement team may not accept employment in a financial reporting oversight role until the required "cooling-off" period has expired

### **Partner rotation**

Under the Canadian Rules of Professional Conduct, the *Sarbanes-Oxley Act* of 2002, and the SEC's independence rules, the firm's audit partners are subject to specific rotation requirements that limit the number of consecutive years an individual partner may provide services to a reporting issuer audit client.

To monitor compliance with these requirements, the firm uses its Partner Rotation System, which helps monitor partner assignments and signals partner changes on our reporting issuer audit clients.

Our monitoring system also aids in the development of timely transition plans that help the firm deliver consistent quality service to our clients. The process of monitoring and tracking service time and partner rotation is subject to compliance testing as part of various monitoring functions.

### **Approval of audit and non-audit services**

The lead audit engagement partner evaluates all services provided to reporting issuer audit clients and their affiliates and also obtains pre-approval of permitted services from the audit committee. KPMG's system, Sentinel™, facilitates compliance with these policies and is used to identify and manage potential conflicts of interest within and across member firms in the KPMG network. Along with our policies, Sentinel™ helps KPMG member firms resolve potential conflicts of interest, prevent the provision of prohibited services to reporting issuers and certain non-public audit clients, and determine that permitted services are properly pre-approved.

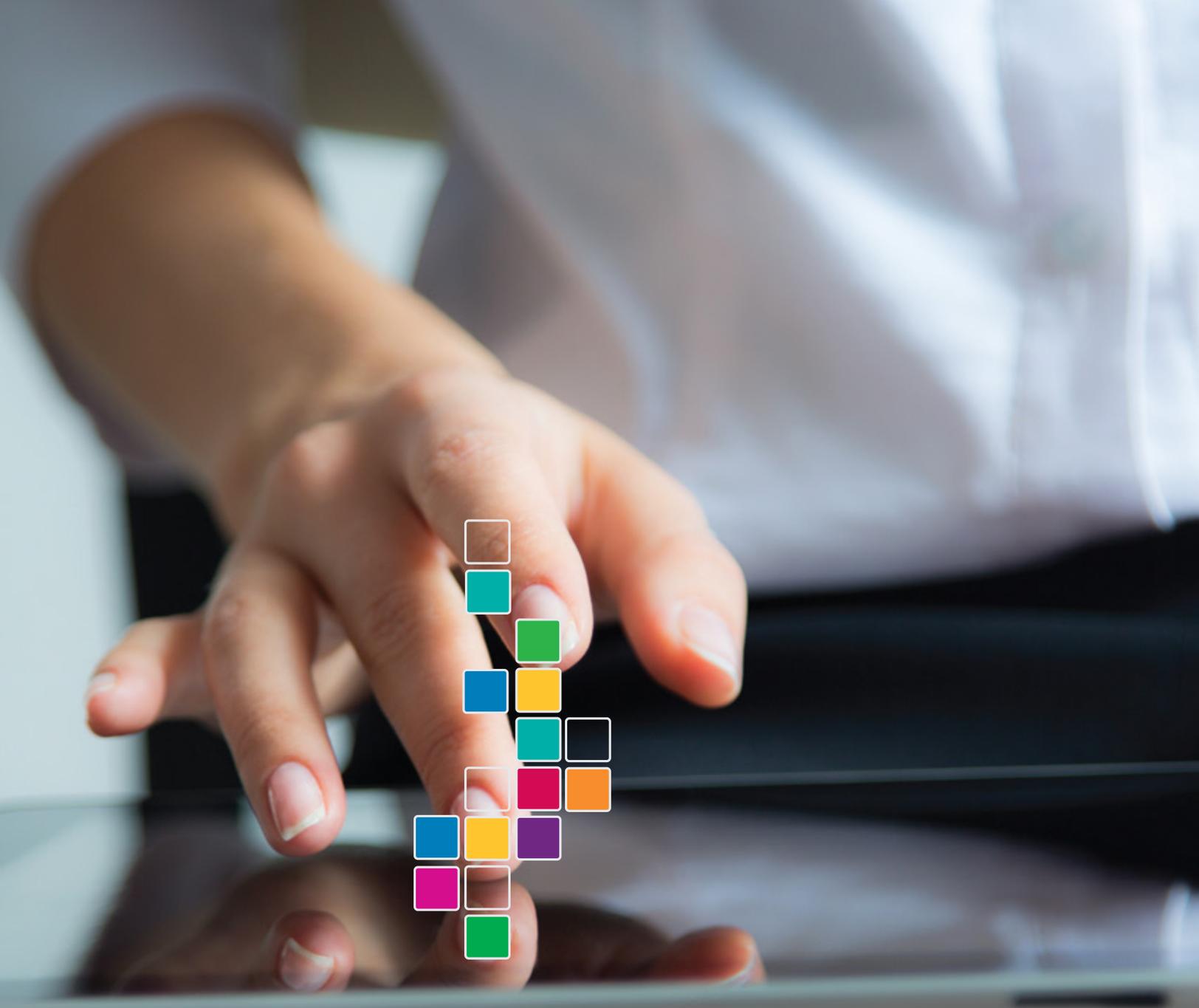
KPMG has established processes to communicate independence policies and procedures to our personnel.

Among other things, the Canadian firm requires all professionals to complete independence training every year and affirm their independence using an electronic confirmation system. This confirmation is completed upon commencement of employment at the firm and every year thereafter.

KPMG monitors compliance with its independence policies for financial interests through an independence compliance system (KICS), as well as through a compliance audit process.

KICS contains an inventory of reporting issuers and the securities they have issued. KPMG's reporting issuers audit clients are marked "restricted" in KICS. Before purchasing a security, securing a loan or initiating another financial relationship, partners and managers are required to use KICS to determine if the entity is restricted. Additionally, investments are required to be reported in KICS, which automatically notifies professionals if their investments become "restricted".

To confirm our professionals' and the Canadian firm's independence, in FY 2015, the firm's Ethics and Compliance group audited the financial relationships of more than 185 professionals subject to the independence requirements. This group also performs annual audits of the firm's financial interests. Any failure to comply with the firm's independence policies is referred to a Discipline Committee for review and remediation, helping to ensure consistent resolution.



Technical support for each engagement team comes from a network that includes DPP as well as the Professional Practice Partners and Accounting and Auditing Technical Topic Teams.

# Ethics and integrity

**KPMG is committed to doing the right thing, in the right way, for our people, our clients and the capital markets we serve.**

It is this commitment that underlies our values-based compliance culture, in which individuals are encouraged to raise their hands to voice concerns when they see behaviours or actions that are inconsistent with our values or professional responsibilities. In this culture, they know the concern will be constructively reviewed and considered, and that consistent and appropriate action will be taken. Individuals who raise their concerns at KPMG are recognized for delivering on our promise of professionalism and their commitment to ethics and integrity.

KPMG in Canada's Code of Conduct is the central tool that articulates the values and principles embodied in our ethics and integrity policies. Each year, all personnel acknowledge that they understand and agree to comply with the firm's Code of Conduct. Additionally, the firm seeks to embed ethics and compliance training in its technical and leadership training to reinforce relevant standards of behaviour.

## **Complaints and allegations**

To extend our commitment to integrity and ethical culture, KPMG maintains an Ethics and Compliance Hotline that allows phone reports to be made through an independent third-party provider. The firm encourages use of the hotline when KPMG partners and employees feel uncomfortable reporting concerns about possible illegal, unethical, or improper conduct through normal channels or when the normal channels of communication are impractical or perceived as ineffective.

The hotline is available to external parties as well, and any person, including clients, vendors, and professionals from other KPMG member firms working on any KPMG engagements, may file reports by calling the toll-free number, 1-866-683-5434.

Reports filed through the hotline are directed to the Canadian firm's Ethics and Independence officer for review and, if necessary, for assignment of appropriate firm resources for investigation and resolution. The firm's Ethics and Independence officer manages, on a day-to-day basis, all personnel matters under investigation.

Reports are handled confidentially (to the extent allowable by law and consistent with the needs of a thorough investigation) and anonymously, if requested, and retaliation or retribution of any kind for good-faith reporting is prohibited.

A KPMG International Hotline is also available for KPMG personnel; partners, employees, and clients of KPMG International member firms and other parties to confidentially report possible illegal, unethical or improper conduct in violation of KPMG International's Code of Conduct.

## **Compliance testing**

The Ethics and Compliance Group is also responsible for testing and monitoring compliance with certain KPMG in Canada policies such as those related to independence, continuing professional education and licensing.

# Objectivity

**Integrity, independence, ethics and objectivity are the pillars of our firm.  
That's why we work diligently to avoid even the appearance of a conflict of interest.**

KPMG personnel work to recognize actual and potential conflicts of interest, identifying them at the earliest opportunity to resolve, manage or avoid the conflict. Conflicts of interest may preclude KPMG from accepting a client or an engagement.

## **Human resources**

The firm's personnel management system encompasses the areas of:

- Recruitment and hiring
- Determining capabilities and competencies
- Assignment of engagement teams
- Professional development
- Performance evaluation, advancement and compensation.

## **Recruitment and hiring**

Prior to receiving an offer of employment, candidates are interviewed and all experienced-hire candidates are subject to background checks through independent sources. Before their start date, all candidates for professional positions get access to the firm's independence guidelines to ascertain and confirm their independence. Situations involving independence or conflicts of interest must be resolved before the individual can begin employment with KPMG. Upon joining the firm, personnel must also confirm their agreement to comply with KPMG's Code of Conduct and to complete training programs on independence, ethics, respect and dignity, and security, in addition to any practice-related modules.

## **Determining capabilities and competencies**

The appropriate capabilities and competencies of an audit engagement team include the following:

- An understanding of, and practical experience with, audit engagements of a similar nature and complexity through appropriate training and participation
- An understanding of professional standards and legal and regulatory requirements
- Technical skills, including knowledge of relevant information technology and other specialized areas of accounting or auditing
- Knowledge of relevant industries in which the client operates
- Ability to apply professional judgement
- An understanding of KPMG's audit quality control policies and procedures.

Our process for admission to the partnership is rigorous and thorough, involving the appropriate members of KPMG leadership. Each candidate for the partnership, whether via direct-entry hire or internal nomination, undergoes a background check and is interviewed by several members of firm leadership. Furthermore, an extensive review for each internal partner candidate is completed by several departments, including the Ethics and Compliance Group.

## **Assignment of engagement teams**

Individuals are assigned to specific engagements based on their skill sets, relevant professional and industry experience, and the nature of the assignment or engagement. Engagement partner and EQCR partner assignments are approved by business unit leadership and may also be approved by regional and national leadership based on the individual characteristics of the audit client.

### **Professional development**

Our policies require our professionals to maintain their technical competence and comply with applicable regulatory and professional requirements. The firm provides continuous learning opportunities to help our professionals meet their CPE requirements as well as their own professional development goals. Training and development programs include varied delivery methods including self-study courses; classroom courses at the national, business unit, and local levels; and real-time web-based seminars. KPMG also maintains a system that helps professionals monitor compliance with their CPE requirements.

Audit quality and professional skepticism is continually emphasized to KPMG professionals through timely training and communication of accounting, auditing and reporting matters. The firm's training includes programs designed to enhance professionals' ability to make judgements by employing a standardized framework that addresses how biases impact decision making and how to recognize and overcome biases in making judgements and applying appropriate professional skepticism. In addition, the Canadian firm requires all professionals to complete KPMG's annual training on independence standards. The firm also encourages professionals to stay abreast of technical updates by attending industry-specific training programs and conferences as well as reviewing pertinent bulletins and periodicals.

The firm's My Development program also helps partners and employees understand their career opportunities through expansion of their skills, experiences and networks within KPMG.

### **Performance evaluation, advancement and compensation**

All professionals, including partners, undergo annual goal setting and performance evaluations on their attainment of agreed-upon goals, demonstration of skills/behaviours, and adherence to KPMG values. The skills and behaviours evaluated include quality focus and professionalism, technical knowledge, accountability, business and strategic focus, leading and developing people, continuous learning and relationship building.

The firm's performance evaluation model was developed to provide a consistent framework by which leadership and performance management leaders may discuss performance relative to goals and objectives and career development aspirations. The results of the annual performance evaluation directly affect compensation of KPMG personnel, including partners, and in some cases, their continued association with the firm.

Audit partner compensation is determined annually by audit leadership and approved by the Management Committee and Board of Directors. The Professional Practice Partners are involved in evaluating audit partner performance and compensation. Partner compensation is based on a targeted allocation, which considers a partner's responsibilities as well as their audit quality performance. Our policies for setting compensation amounts prohibit audit partners from being compensated for the sale of non-audit services to their audit clients.



All professionals, including partners, undergo annual goal setting and performance evaluations on their attainment of agreed-upon goals, demonstration of skills/behaviours and adherence to KPMG values.



# Client acceptance and continuance

**Rigorous client and engagement acceptance and continuance policies are vitally important to the firm's ability to provide high-quality professional services. We have established policies and procedures for deciding whether to accept or continue a client relationship and whether to perform specific services for a particular client.**

## **Prospective client/engagement evaluation processes**

Prior to accepting a new audit engagement, a partner performs an evaluation of the entity and its principals, its business, and engagement-related matters, as appropriate. This evaluation typically includes a background investigation of the entity and selected senior management personnel.

Factors considered during the acceptance process include, but are not limited to:

- **Client-related matters**  
(e.g., financial strength, reputation, accounting policies and practices and character and competency of management personnel)
- **Business-related matters**  
(e.g., industry, products and competitors)
- **Service-related matters**  
(e.g., firm and engagement team competency and technical risk associated with services requested)
- **Independence related matters**  
(e.g., employment related matters, financial relationships, investments, loans, and non-audit services).

The firm also evaluates potential independence issues and conflicts of interest. Engagement teams proposing to perform a new audit engagement are required to perform a series of procedures including a review of non-audit services provided to the potential audit client. Any potential independence issues and conflicts identified are resolved in consultation with other parties and fully documented. Generally, before agreeing to pursue the engagement, the parties involved in the professional service are notified of the potential conflict of interest.

Resolution of potential conflicts requires approval from a second party, which could include the Professional Practice Partner, Sentinel™ conflicts resolver, or the functional risk management group.

If the initial audit engagement is accepted, it may be necessary to establish "ethical dividers" with respect to the professionals assigned and to communicate with appropriate parties. If a potential independence issue or conflict cannot be resolved satisfactorily, in accordance with professional and firm standards, the prospective client or engagement is declined.

Prospective audit engagement evaluations require approval of the Professional Practice Partner and the business unit partner in charge. New SEC audit engagements require additional approvals by the Ethics and Independence partner.

## **Continuance process**

Engagement partners are required to review and evaluate their existing audit and attestation clients with their Professional Practice Partner at least annually. A client continuance evaluation is a process of formal approvals by various parties. The objective is to identify those clients where the firm should consider implementing additional safeguards to address audit risk and those instances where we should discontinue our professional association with the client.

In addition, certain factors that require additional evaluation procedures include, but are not limited to:

- New legal, regulatory, or professional requirements that alter our reporting responsibilities and professional risks
- A significant change in the nature, size, or structure of a client's business

- A significant change in ownership
- A significant change in client management, directors, principal owners, or other key personnel
- A significant, adverse change in the perceived integrity of current management or principal owners
- A significant, adverse change in the financial performance of the client
- Particular audit findings (e.g., material weaknesses in internal control not being addressed by management or material proposed adjustments to financial statements)
- An existing non-public audit client plans to become a reporting issuer
- A restatement of financial statements
- Investigation of the client by a regulatory body or its audit committee that involves a current member of management.

### Monitoring

Monitoring procedures involve ongoing consideration and evaluation, by the firm, of the following matters:

- Relevance and adequacy of the firm's policies and procedures
- Appropriateness of the firm's guidance materials and practice aids
- Effectiveness of professional development activities
- Compliance with professional and firm standards, policies and procedures
- Effectiveness of action plans developed to address findings related to engagement reviews by the firm or by audit regulators.

### Internal inspection processes

Along with the monitoring activities previously described, KPMG meets the profession's monitoring requirement through the implementation of our internal inspection processes, including the Quality Practice Review (QPR) and the Risk Compliance Program.

Components of the internal inspection processes include:

- Regular reviews of audit engagements of individual partners following a three-year rotating schedule
- Reviews of other audit engagements using risk-based selection criteria
- Reviews of general and functional controls, including independence, client acceptance and continuance, personnel evaluations, CPE compliance and document retention
- Frequent, timely reporting of firm-wide inspection results
- Training and guidance that communicates to audit professional's common inspection findings, those areas where audit quality can be improved, and, where appropriate, the tools needed to improve audit quality.

### Regulatory external reviews

KPMG is subject to annual inspection by CPAB. Its mission is: "To contribute to public confidence in the integrity of financial reporting of reporting issuers in Canada by effective regulation and promoting quality, independent auditing." We receive annual comments from CPAB and consider them in our efforts to continuously improve audit quality.

For its part, the PCAOB oversees the auditors of reporting issuers to protect the interests of investors and further the public interest in the preparation of informative, fair, and independent audit reports. As part of its mission, the PCAOB conducts periodic inspections of registered firms. KPMG has been subject to annual inspection by the PCAOB. Because the PCAOB plays an important role in improving audit quality, the PCAOB's inspection helps us identify opportunities to improve our performance and strengthen our system of audit quality control.

The 2012 and 2013 PCAOB inspection reports on KPMG are the firm's most recent inspection reports and are accessible through the PCAOB's Web site at:

[http://pcaobus.org/Inspections/Reports/Documents/KPMG\\_LL.pdf](http://pcaobus.org/Inspections/Reports/Documents/KPMG_LL.pdf).



# Risk management

**To enhance our system of quality control, KPMG separates the responsibility for risk management and oversight of quality control monitoring from the responsibility for managing the firm's business and professional practice activities.**

## **Quality and Risk Management**

Reporting directly to the firm's CEO, the Canadian Managing Partner (CMP) – Risk Management oversees all aspects of the firm's regulatory, compliance, and related risk management activities, including the firm's quality control monitoring processes and its ethics and compliance program.

## **Risk Management Groups**

### **The Risk Management Groups**

(Audit, Tax, and Advisory) consist of partners and other professionals who oversee quality control and monitor risk for the Audit, Tax, and Advisory practices. In addition, these groups are responsible for a firm-wide privacy policy, which is an important part of KPMG in Canada's overall efforts to protect personally identifiable information and comply with the applicable laws, regulations, professional standards, firm policies and agreements in the area of privacy.

**Risk Management-Audit** oversees, monitors, and/or participates in the audit practice, oversees our audit QPR and develops certain firm-wide processes and policies to manage risk, including those relating to client and engagement acceptance and continuance.

KPMG's risk management systems, including Client/Engagement Acceptance and Continuance (CEAC) and the Partner Rotation System, also fall under this group's responsibilities.

**Risk Management-Tax** oversees compliance with the firm's professional standards and requirements. This group develops risk management policies specific to our Tax practice and seeks to mitigate risk with frequent guidance and training; approval of certain new Tax engagements at inception; and close monitoring of compliance, including administration of our Tax QPR.

**Risk Management-Advisory** develops risk management policies specific to our Advisory practice. This group monitors compliance with our Advisory risk management policies and procedures, including the Advisory QPR, and also reviews new advisory service offerings.

Risk Management-Advisory is supported by a network of service line risk management partners.

## **Ethics and Independence Group**

The Ethics and Independence Group is responsible for KPMG in Canada's policies, practices, and controls with respect to independence matters, including those relating to Sentinel™ and KICS and is assisted by the business unit Professional Practice Partners.

## **Conclusion**

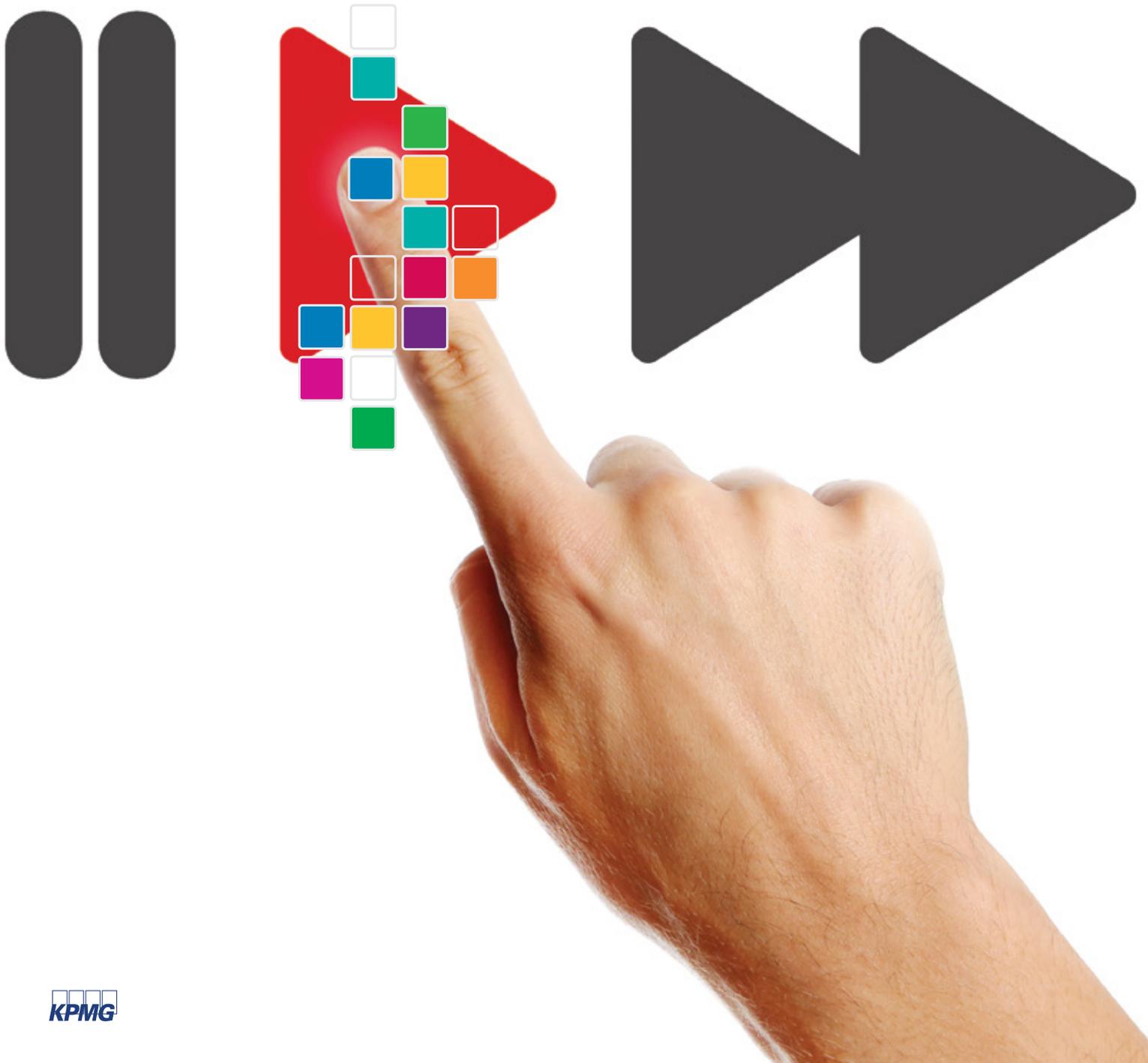
We are confident that our firm's tone at the top, structure, policies, and procedures support our professionals and enable them to provide a high level of audit quality in an independent, objective, and ethical manner, maintaining public and stakeholder confidence.

As businesses and markets evolve, we pledge to keep pace by continuing our substantial investment in the research and development needed to maintain audit quality and by staying abreast of changing public and regulatory expectations in the audit environment.

KPMG intends to continue providing our professionals with training, technology-based tools, and audit methodologies that contribute to high-quality audits.

We encourage you to contact KPMG with any comments or questions you may have.

KPMG fully intends to implement the recommendations for improvements that CPAB has made related to our audit methodology.



# Addendum

## Quality control

KPMG's system of audit quality control is designed to meet or exceed the requirements of applicable professional standards.

Our **Audit Quality** report describes our system of serving the public interest through independence, integrity, ethics, objectivity, skepticism and quality performance.

Topics covered in the report include:

- Leadership responsibilities for quality within KPMG (the "tone at the top")
- Engagement performance
- Relevant ethical requirements
- Human resources
- Acceptance and continuance of client relationships and specific engagements
- Monitoring.

KPMG continuously reviews its policies and practices to respond to changes in regulatory and professional requirements.

## External regulatory reviews

In November 2014, CPAB released its first annual inspections report focused on Canada's four largest firms.

That report, entitled Changing Expectations, covers the 2014 inspections of the Big Four, including KPMG in Canada.

CPAB released its all-firm inspection findings report on its 2014 inspections in March 2015.

KPMG in Canada and CPAB share the common goals of improving audit quality and maintaining the public's trust in the capital markets. The inspection of public accounting firms represents an important element of this initiative and we fully support CPAB's responsibility.

A copy of this report is available on CPAB's website at <http://www.cpab-ccrc.ca/>.

## CPAB inspections of KPMG in Canada

CPAB has issued a confidential report to KPMG in Canada on the results of its inspections for each of the past eleven years. Under CPAB's rules, the recommendations or other comments contained in these reports may not be made public by either CPAB or the inspected firms. KPMG in Canada fully intends to implement the recommendations for improvements that CPAB has made related to our audit methodology, quality control processes and engagement execution.

## The PCAOB inspections of KPMG in Canada

KPMG in Canada issues audit opinions on the financial statements of registrants with the U.S. Securities & Exchange Commission (SEC) and is registered with the PCAOB. KPMG in Canada has been subject to an annual PCAOB inspection since 2005.

For its 2015 inspection, as in prior inspections of KPMG in Canada, the PCAOB selected a cross-section of audit engagements to review. In addition, the PCAOB performed certain procedures relating to KPMG in Canada's executive and national offices. KPMG in Canada has not yet received the PCAOB's report on its 2014 or 2015 inspections.

In October 2014, the PCAOB released its Reports on the 2012 and 2013 inspections of KPMG in Canada. The PCAOB's Reports are presented in two parts. Part I is a public document containing observations relating to specific engagements reviewed by the PCAOB. Part II is a private document containing the PCAOB's observations regarding KPMG in Canada's quality control systems related to audit performance and firm-wide functions.

This part of the Report will be made public only to the extent that any of the PCAOB's comments and observations have not been adequately addressed within 12 months of the date of the Report.

KPMG in Canada is committed to responding to all reports on a timely basis. The following documents are available on PCAOB's Website at <http://www.pcaobus.org/>:

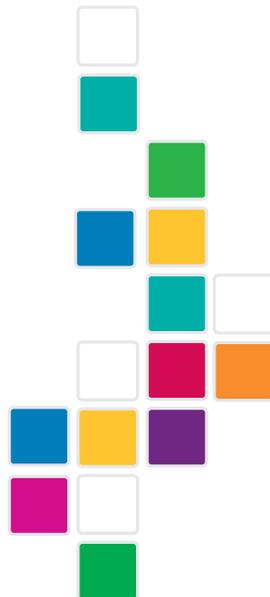
- **PCAOB Reports Part I for years 2005 to 2013** – The complete, publicly available inspection Reports Part I
- **KPMG in Canada's Responses to Part I for years 2005 to 2013** – KPMG in Canada's response, which provides context to the Reports Part I, as submitted to PCAOB.

## Internal quality reviews

KPMG in Canada conducts an annual internal review of its audit practice through its QPR program. The QPR is designed to meet the quality control elements of monitoring as required by professional standards. For the five-year period ended September 30, 2015, our QPR that has not identified any issues considered to have a material effect on the conduct of the firm's audit practice. Like most companies with quality review programs, we identify areas for continuous improvement and address our findings through the enhancement of policies and guidance. We provide communications and training to our partners, managers and staff to address the areas identified for improvement.

## Governmental or other inquiries

Currently, KPMG in Canada is not aware of any inquiry or investigation by governmental or regulatory authorities against the firm or any of its partners that might adversely affect the firm's operations or its ability to fulfil its obligations as independent auditor to its clients.





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