Work and Pensions Committee
Business, Energy and Industrial Strategy Committee
[redacted]
Tel 020 7219 8976/5777 Email workpencom@parliament.uk / beiscom@parliament.uk

From the Chairs

25 January 2018

Bill Michael
Chairman and Senior Partner
KPMG UK

Dear Mr Michael

Carillion

Following the compulsory liquidation of Carillion Plc and its subsidiaries announced on 15 January 2018, the Work and Pensions and Business, Energy and Industrial Strategy Committees have launched a joint inquiry into the group.

As part of that inquiry, we are seeking to establish what services, if any, the Big Four accountancy firms have offered Carillion, its subsidiaries and their pension scheme. Conflicting tales as to who has provided professional services to Carillion over various issues means we are keen to establish a clear timetable setting out who was involved when with the company.

Could you therefore provide details to us, broken down on an annual basis dating back to 2008, on any terms of engagement that you had with Carillion Plc, any subsidiaries of Carillion Plc and the Carillion Pension Plan. We would request those details include overviews of what the contracted services related to and also the fees charged for those services.

One service we know that KPMG provided to Carillion is the financial audit of their consolidated financial accounts. KPMG have audited their accounts every year since the company's inception in 1999, receiving £29.4 million in fees in the process. The latest set of audited financial accounts were signed off by KPMG with an unmodified opinion in March 2017, only for the company to go bust 9 months later. In light of that dramatic turn of events, could you explain to the Committee:

1. In light of Carillion's collapse, have KPMG conducted a cold review of their 2016 audit? If so, do KPMG stand by their audit opinion that gave Carillion's consolidated accounts a clean bill of health?
2. Your 2016 audit opinion noted the risks relating to estimates around revenue recognition from contracts, but concluded that there was no material misstatement in the accounts. Yet three months later, a KPMG-led review of Carillion's contracts resulted in a £845 million provision relating to these contracts. KPMG's 2016 audit

opinion outlines in detail the audit work conducted on these contracts, but concluded no provision was required. What changed?

3. Accounting standards require that the total loss of a contract is recognised if it is deemed that the contract is loss-making. What proportion of Carillion's contracts were loss-making to financial year-end 2016? Were KPMG satisfied that all loss-making contracts were fully recognised at that point?
4. The 2017 interim financial statements concede that there likely would have been a further hit to the company's reserves of around £125-150 million when IFRS 15 (a new international financial reporting standard relating to revenue recognition) was expected to be retrospectively adopted on 1 January 2018. The financial statements in 2016 noted that this standard would be adopted on that date but said only it was "difficult to determine with any certainty the impact on revenue" this would have. This standard was introduced in part to guard against companies aggressively recognising contract revenue, so why were KPMG not more proactive in highlighting the risk this presented in the 2016 accounts?
5. The accounts show that the pension schemes suffered a £725 million actuarial loss due to changes in financial assumptions. This accounts for more than 90% of the total net pension liability. What work did KPMG to verify the validity of the actuarial assumptions?
6. Goodwill, at £1.57 billion, is the largest single item on the balance sheet, and represented over 70% of the groups non-current assets. Given the inherent uncertainty in valuing such an intangible asset, did KPMG form a view as to whether this reliance on goodwill was sustainable in the long-run?

Additionally, we will be looking at what advice and assurances the Government were receiving about the contracts they had entered into with Carillion. Could you therefore provide similar details about any advisory services that your firm may have entered into with the Government relating to contracts with Carillion and its subsidiaries. We would also like this information dating back to the start of 2008.

We would be grateful for a response by Friday 2 February.

Many thanks

Rt Hon Frank Field MP
Chair, Work and Pensions Committee

Rachel Reeves MP
Chair, Business, Energy and Industrial Strategy Committee