IN THE MATTER OF

THE EXECUTIVE COUNSEL TO THE FINANCIAL REPORTING COUNCIL

- and -

(1) KPMG AUDIT PLC

(2) ANDREW WALKER

SETTLEMENT AGREEMENT

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1. This Settlement Agreement ("**Agreement**") is made on 8 February 2019 between Claudia Mortimore as the Deputy Executive Counsel of the Financial Reporting Council ("**the Executive Counsel**"), KPMG Audit Plc ("**KPMG**") and Andrew Walker ("**Mr Walker**"). The Executive Counsel, KPMG and Mr Walker together are described as "**the Parties**". The Agreement is evidenced by the signatures of the Executive Counsel on her own behalf, by Mr Walker on his own behalf and by David Matthews on behalf of KPMG.

2. The Particulars of Fact and Acts of Misconduct concerning KPMG and Mr Walker ("**the Particulars**") were agreed by the parties in accordance with the FRC Accountancy Scheme ("**the Scheme**") and are annexed hereto. The Particulars relate to the conduct of each of KPMG and Mr Walker in relation to the audit of the financial statements of The Co-operative Bank plc ("**the Co-op Bank**") for the financial year ended 31 December 2009 ("**FY09**"). Mr Walker and KPMG admit the Acts of Misconduct set out in the Particulars.

3. The Parties recognise that the determination to be made in this case is a matter for the Tribunal member in accordance with paragraph 8(4)(ii) of the Scheme.

4. Terms used in this Agreement shall have the same meaning as set out in the Scheme and the Sanctions Guidance dated April 2018, effective from 1 June 2018 ("**the 2018 Sanctions Guidance**").

Sanction

5. The Parties have agreed the following terms of settlement:

   KPMG:

   (a) A fine of £5 million (reduced in accordance with paragraph 73 of the 2018 Sanctions Guidance relating to settlement adjustments by 20% to £4 million);

   (b) A Severe Reprimand;

   (c) A Condition that all KPMG's audit engagements with credit institutions (for audits with 2019, 2020 and 2021 year-ends) will be subjected to an additional review by a separate KPMG Audit Quality team. The review will focus, in particular, on:

i) whether appropriate consideration has been given to the assessment of the risks and the implications of possible management bias in management's determination of accounting estimates; and

ii) whether the audit work in relation to loan loss provisioning is compliant with audit standards, as well as KPMG's guidance issued through the Audit Quality Transformation Programme ("AQTP").

At the end of each of the three years, KPMG will provide a report to the FRC's Executive Counsel and the FRC's Executive Director of Audit, setting out the themes arising from the reviews; the planned actions; and the progress to address them.

The first report is to be provided to the FRC by 30 June 2020.

Mr Walker:

(a) A fine of £125,000 (reduced in accordance with paragraph 73 of the 2018 Sanctions Guidance relating to settlement adjustments by 20% to £100,000);

(b) A Severe Reprimand.

6. The fines shall be paid not later than 28 days after the date when this Agreement takes effect.

7. In determining the appropriate sanctions, the Executive Counsel adopted the approach set out in paragraph 18 of the 2018 Sanctions Guidance, as follows:

Nature and Seriousness of the Misconduct

8. The Executive Counsel considers that the factors relevant to assessing the nature and seriousness of the Misconduct are:

(a) The Misconduct related to the audit of the Co-op Bank, a retail and commercial bank. There was an obvious public interest in the proper auditing of this bank, particularly in 2009, when the financial crisis had taken hold and the Co-op had concluded an ambitious merger with Britannia;

(b) The Misconduct potentially adversely affected a significant number of people in the United Kingdom;

(c) The Misconduct involved failing to comply with important auditing standards and included failings in relation to the exercise of professional scepticism. In those circumstances the Misconduct could undermine confidence in financial reporting and/or corporate governance and/or the profession generally;

(d) As the engagement partner, Mr Walker was the senior member of the Audit team with overall responsibility for the conduct of the Audit and with supervisory responsibilities;

(e) The Misconduct did not involve a failure to act with integrity, nor was it dishonest or reckless;

(f) The Misconduct related to only one audit year;

(g) The Misconduct related to discrete areas of the audit and was not pervasive.

Identification of Sanction

9. Having assessed the seriousness of the Misconduct and considered the range of available sanctions, the Executive Counsel considers that the sanctions identified above are appropriate sanctions for each of KPMG and Mr Walker.

10. The Executive Counsel has taken into account aggravating and mitigating factors set out below, to the extent that they have not already been taken into account in considering the nature and seriousness of the Misconduct. The Executive Counsel has also considered whether any adjustment to the sanctions for deterrence is required in this case. The conclusion reached is that the sanctions set out in paragraph 5 above are appropriate, having regard to the purpose of the Scheme.

Aggravating Factors

11. KPMG has been sanctioned for Misconduct in relation to audit on three previous occasions during the past 12 months:

    (a) In May 2018, KPMG was sanctioned with a fine of £4.5m (reduced to £3,150,000 after settlement discount) and a Reprimand, having admitted Misconduct in relation to the audit of Quindell plc for the year ended 2013;

    (b) In July 2018, KPMG was sanctioned with a fine of £3m (reduced to £2.1m after settlement discount) and a Severe Reprimand, having admitted Misconduct in relation to compliance with Ethical Standards in connection with the provision of non-audit services to Ted Baker plc for the years ended 2013 and 2014;

    (c) In January 2019, KPMG was sanctioned with a fine of £6m and a Severe Reprimand in relation to the audit of Equity Red Star (Syndicate 218) for the years ended 2008 and 2009, following a full hearing before the Tribunal.

12. There are no aggravating factors applicable to Mr Walker.

Mitigating Factors

13. The following mitigating factors were identified:

    (a) KPMG and Mr Walker have expressed contrition for their Misconduct.

    (b) KPMG has taken remedial steps including enhancing training for auditors in the audit of loan loss provisions and the application of professional scepticism, and the introduction of an Audit Quality Transformation Programme across the whole audit practice, including Financial Services.

    (c) Mr Walker has a good disciplinary record.

Discount for Settlement

14. Having taken into account the admissions made by KPMG and Mr Walker and the stage at which those admissions were made in accordance with paragraph 73 of the 2018 Sanctions Guidance a reduction of 20% to the fines is appropriate for both KPMG and Mr Walker.

Amount of fine

15. The Executive Counsel considers that, having had regard to the circumstances of this case and the Parties, and previous relevant outcomes of cases under the Scheme, fines of £5 million and £125,000, pre-application of the discount, for KPMG and Mr Walker respectively are proportionate to the Misconduct and will act as an effective deterrent.

Costs

16. The Parties have agreed the following terms of settlement for costs:

    (a) That the FRC's costs of, and incidental to, the investigation of £500,000 be paid by KPMG.

    (b) The costs shall be paid no later than 28 days after the date when this Agreement takes effect.

17. If the decision is to approve the Agreement, including the sanctions set out above, then the Agreement shall take effect from the next working day after the date on which the notice of the decision is sent to KPMG and Mr Walker in accordance with paragraph 8(4)(iv) of the Scheme.

[redacted]

8 February 2019

Claudia Mortimore
Deputy Executive Counsel

Date

[redacted]

8 February 2019

David Matthews
On behalf of KPMG Audit Plc

Date

[redacted]

8 February 2019

Andrew Walker

Date