

## SUMMARY OF FINDINGS IN DECISION 2

**This summary of findings concerns the outcomes of investigations into the relevant Statutory Auditor(s). No part of this summary of findings should be treated as making any findings in respect of the conduct of any other persons or entities.**

### The transactions

In 2013 Carillion decided to change its provider of a range of outsourced services. In December of that year it concluded an agreement with the new provider, which provided for:

- An assignment of certain intellectual property rights by Carillion to the new provider. These related to an eco-friendly heating system, for which the new provider would pay £27 million.
- A £14 million contribution to an 'exit fee' payable by Carillion to the former provider of the services
- The services to be provided and charges to be paid. These included "Other Charges" totalling £40.8m over the life of the contract which did not appear to relate to any specific services
- A charge payable by Carillion to the new provider, in the event the agreement was terminated early, initially amounting to c.£40 million and reducing over the life of the agreement

The combined effect of these elements resulted in an increase of £41 million reported profit in the 2013 financial statements.

The most likely explanation for the transactions was that all the elements were linked in substance, that the new provider's agreement to the contribution to the exit fee and the IP assignment was a *quid pro quo* for the award of the outsourcing contract, and the £41 million paid for these was in substance either an advance discount on the charges for the outsourced services, or a loan that would be recovered by those charges being inflated. In either case the cash received would not represent income earned in 2013 and should not result in increased profit.

### The audit

The accounting treatment adopted by Carillion was only possible if the transactions were treated as separate and independent of each other, with the contractual values for each element being at fair value. KPMG did not treat the question of linkage between the various elements as a significant risk and failed to approach the transactions with an adequate degree of professional scepticism or consider and respond to the risk of fraud.

KPMG was aware of the significance of the profit being recognised and of evidence that the IP assignment was not at fair value but failed to perform audit procedures that would provide sufficient appropriate audit evidence to enable it to conclude on the appropriate accounting treatment of the transactions. KPMG also failed to identify that disclosures in the 2013 financial statements relating to the transactions might be misleading.