

Funding the Future

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My friend [Atul Shah](#) of [Suffolk Business School](#) asks questions of KPMG's latest annual report:

The growing size and influence of Big 4 global accounting firms, and their supermarket of business consulting and advisory services, is [generating alarm among scholars](#) concerned about ethics, independence, and truth. Our research at [Suffolk Business School](#) has raised a number of questions about their [ethics, conflicts of interest and culture](#). There is confusion as to whether they are a regulator of business, or help business escape regulatory control through skilled professional services — the primary driver seems to be maximising profit. We also found high level corporate and political networks and influence on government and regulatory processes.

Given that they are world 'experts' in accounting, one would expect that their own [Annual Report](#) is clear, legally compliant and transparent. I tell my MBA students to read annual reports very carefully — it's a bit like asking people to write their own evaluation, so objectivity will be compromised. The latest annual report by KPMG UK, sadly falls short of objectivity and transparency. Here are the specific concerns it continues to raise:

- * *It claims to have paid £786mn to HMRC from before tax profits of £383mn. This seems very generous, until one discovers that the tax paid includes £673m (e.g. PAYE and VAT) where KPMG are merely a tax intermediary;*
- * *The governance of the firm is still primarily closed — all executives and non-executives are partners of the firm, and there is no cultural/national diversity in spite of it being a global firm and stated aspirations about inclusiveness. Quoted companies have to have independent non-executive directors by law, and this is policed by Big 4 firms, but somehow such a rule does not apply to them.*
- * *The 'independent' Public Interest Committee (whose legal status is unclear, and appointments are made by KPMG) was previously Chaired by Sir Steve Robson. Our research raised a number of questions about the conflicts of interest from this appointment. He has now been replaced by a new Chair, Prof Laura Empson, who claims that 'public interest is notoriously difficult to define.' How about ensuring that audits are genuinely independent and clients challenged robustly for aggressive accounting?*
- * *There is an acknowledgement of the 'debate on tax' and the need for companies to*

change their ethics and practices, with KPMG trying to be at the forefront of this new era.

* The most critical audit area would be contingency provision for fines and losses relating to the major multi-billion pound business failures where KPMG were auditors and are being investigated — e.g. Co-op Bank and **HBOS**. There is virtually a total silence about these real threats, including from the Public Interest Report. The declarations here are very vague, citing insurance cover and commercial confidentiality, and there is a cop-out clause used by both KPMG and their auditors Grant Thornton — there is a ‘significant degree of inherent uncertainty in the assumptions and estimates’. Does this mean the audit is qualified because of this uncertainty? Word play is used not to give an audit opinion in risky areas — precisely where people need a good audit. Should we be surprised given the audit industry’s mastery in regulatory arbitrage?

* Our research raised a number of questions about their ethics policies and practices. In particular, we were concerned that there were no rules or explicit pro-active monitoring and enforcement processes e.g. there were no rules or limits on client entertainment, a direct conflict of interest. The latest report explains that policies are being developed in this area — so no rules in sight again then.

* One major expansion area for the firm has been in the provision of legal services, where they grew by 53% in one year, and more growth is expected. KPMG claim that clients really like their ‘multi-disciplinary services’. However, this can also further increase conflicts of interest — not only is the firm an auditor, but it is now also a lawyer, and a tax advisor, consultant....The risks generated by such conflicts for audit quality are growing.

* Our research raises major question marks about the systemic role of Big 4 firms in ‘regulatory arbitrage’ activities — using their knowledge of rules and regulations to help clients avoid them — something well known in the area of tax avoidance. The latest KPMG report sadly reinforces this view. Regulatory management is one of their core business activities.