

Should four become three? Should KPMG survive?

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The FT [reported this last night](#):

KPMG auditors misled regulators during inspections of their work on the audits of outsourcers Carillion and Regeneris, the accounting firm's UK boss said.

The Financial Reporting Council accused the Big Four firm and six of its former auditors of forging documents and misleading its inspectors as the UK accounting watchdog opened its case before an industry tribunal on Monday.

If true, and it would seem that KPMG is itself not challenging these claims although former employees are, then this is an admission of gross misconduct. Fabricating evidence after an event is hard to pass off as anything but fraudulent. No doubt the Tribunal hearing this issue will seek to determine whether this happened, but as noted KPMG is not defending the claim.

The real question this raises is what does this mean for a firm that was, for the sake of the record, forty years ago my employer? My suggestion is that the claim, so often made, that there were just 'bad apples' in this firm and occasional lapses of quality is ceasing to make any sense now. KPMG has a long list of failings, and is at present not taking government contracts because of doubts about its ethics.

That last point is key. An audit firm is only as good as its ethics. The quality of its opinion making is all that matters, and ethical objectivity is key to that. If KPMG cannot be believed, and I cannot be alone in no longer believing it can be, then there is nothing left for it to do.

That is, I think, the point that has been reached now by KPMG. This firm has failed. No objective regulator could, in my opinion, any longer think it a fit and proper organisation to undertake audits. In that case its licence should be revoked.

Why isn't that happening? Only, I suggest, because everyone knows that when four becomes three the audit market ceases to exist, even if it is the smallest that might be failing.

But if that market has failed - and I think that apparent - then to pretend otherwise is to undermine everything about the audit process, which either matters, in which case action is needed, or it does not, when the requirement to audit should be abandoned.

I know of no one suggesting that the audit requirement should end.

In that case we need stronger audit, and only fundamental, state driven reform can supply that. This month the government is meant to publish its plans for audit reform after a major consultation process on the issue. I suspect they will fall way short of what is required. The result will be that capitalism will be in crisis, because without proper audit it ceases to operate as a functioning market and simply becomes a short term exploitative free for all.

With KPMG no longer fit for purpose, as its ban from government contracting already proves, the government has to act, unless it does not believe in functioning markets, of course. And one has to wonder whether that is the case now.