

RESPONSES TO THE CONSULTATION PAPER ON THE REVIEW OF THE OECD ANTI-BRIBERY INSTRUMENTS

Comments from PricewaterhouseCoopers LLP

PricewaterhouseCoopers is pleased to participate in this consultation. Our comments principally address the role of the independent external audit in detecting and reporting acts of bribery. As signatories to World Economic Forum's "Partnering Against Corruption - Principles for Countering Bribery" initiative, we support strong efforts to counter bribery and corruption.

This response summarises the views of the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

The Respective Roles of Management, Boards of Directors and Auditors

The OECD's 1997 Revised Recommendation of the Council on Combating Bribery in International Business Transactions put forward a series of recommendations beyond the original OECD convention on bribery. The Revised Recommendation identified specific elements of the financial reporting and auditing process that can be used to combat bribery and corruption, and specifically identifies steps that can and should be taken by various participants. When discussing the role of the independent external auditor in detecting and reporting bribery, it is helpful to look at the broader process of financial reporting and the respective roles played by management, the board of directors (or similar governing body) and the independent external auditor.

Our comments are provided from the perspective of International Standards on Auditing (ISA), which are promulgated by the International Auditing and Assurance Standards Board (IAASB). Among other things, ISAs describe the roles of the various parties in the preparation and audit of financial statements. Paragraph 33 of ISA 200 states "[T]he responsibility for the preparation and presentation of the financial statements...is that of the management of the entity, with oversight from those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities." Paragraph 36 of ISA 200 goes on to say that "...[m]anagement is also responsible for...[d]esigning, implementing and maintaining internal control relevant to the preparation and presentation of financial statements that are free from material misstatement, whether due to fraud or error."

Thus, any responsibility assigned to the independent external auditor as an extension of its responsibility to report on the financial statements must be viewed in the context of the responsibilities of the various parties for those financial statements.

The Independent External Audit: Issues for Consultation

The subject Consultation raises three principal issues with respect to the independent external audit. They are:

- Companies subject to external audit;
- Reporting to competent authorities; and
- Standard for triggering a report.

We wish to address these issues but in a somewhat different order than they are discussed in the Consultation.

1. Standard for triggering a report

The Consultation raises a question about whether financial statement materiality is an appropriate threshold for triggering reporting of bribery in the context of an independent external audit. This question is posed on the basis that there is some ambiguity or inconsistency in the determination of materiality.

The objective of an audit is to provide reasonable assurance that the financial statements taken as a whole present fairly the financial position and results of operations of the enterprise in all material respects. As such the independent external auditor is concerned with risks of material misstatements to the financial statements. An audit designed to provide assurance against any bribery would be a different and more costly task than an audit of financial statements.

To be sure, an auditor's determination of what is material is to some extent a matter of professional judgement. ISA 320 states that information is material if "...its omission or misstatement could influence the economic decisions of users on the basis of the financial statements. Materiality depends on the size of the item or the error judged in the particular circumstances of its omission or misstatement." However, this does not mean that a materiality standard is vague or unworkable. Making judgements about materiality is fundamental to the auditor's role and is a key element of the auditor's training and experience.

This does not mean that an independent external audit cannot uncover acts of bribery. In fact, ISA 240 states that the auditor has a responsibility to consider the possibility of fraud when planning and conducting an audit.

2. Reporting to competent authorities

The Consultation expresses concern about the lack of requirements in many countries for independent external auditors to report actual or potential instances of bribery that are uncovered during the conduct of an audit, and that such requirements may not be followed in all instances. We believe there are adequate professional standards, and instances of national laws, that protect the public interest while addressing the issue in a manner consistent with the non-managerial role of an independent external auditor. We support the enactment of such laws where they do not exist.

ISA 250, titled "Consideration of Laws and Regulations in an Audit of Financial Statements" guides the independent external auditor on how to proceed when conduct is uncovered which might violate anti-bribery laws. The response is carefully measured because whether certain conduct is a likely violation of the law is typically outside the independent external auditor's professional competence. Also, as the conduct becomes further removed from the subject matter of the financial statements being audited, it is less likely that the independent external auditor will learn of it or recognize it as a possible violation of the law.

An independent external auditor that discovers potential violations of anti-bribery laws is required to bring them to the attention of the company's senior management or, if senior management is involved, to a governing body such as the audit committee or the supervisory board. The independent external auditor must then assess the remedial actions taken by the company, which could include the company having to notify outside authorities if the law so specifies. If the company's actions are considered inadequate, the independent external auditor may have to qualify the audit report, disclaim an opinion, or resign, depending on the circumstances and materiality. In some countries, local laws may require separate reporting to competent authorities as well.

ISA 250 recognizes that it is the company, its management and its audit committee or supervisory board which have, and must continue to have, the primary duty to disclose relevant information, including acts of actual or potential bribery. This standard was adopted and issued after a careful public consultation

process that includes advice and input from a select group of 12 National Audit Standard Setters, 10 of whom are from countries that are signatories to the OECD treaty. We believe it is an appropriate standard to govern the auditor's role detecting and reporting bribery.

3. Companies subject to external audit

The Consultation Paper expresses concern that in many countries, some very large unlisted companies are presently exempt from external audits and therefore not subject to the procedures described above.

We would observe that preventing bribery and other forms of fraud are among a large number of public policy objectives that governments face when regulating businesses. A statutory audit is one of a number of tools that government regulators use to protect investors and other stakeholders, especially with regard to their interests in limited liability entities. Countries vary widely as to the tools they employ to accomplish their public policy objectives. While independent external audits satisfy a number of public policy objectives, they are neither designed nor intended with the principal intent to ferret out fraud and corruption. Thus policymakers who are considering statutory audits should consider carefully the relative costs and benefits for unlisted entities of all sizes and to meet a wider variety of public policy objectives, not just preventing and detecting bribery.