

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

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We appreciate this opportunity to comment on the *Review of the OECD Instruments on Combating Bribery of Foreign Public Officials in International Business Transactions Ten Years after Adoption* (the “Consultation Paper”). We are strongly supportive of OECD’s efforts to combat bribery and believe its successes on this front are significant and commendable. The OECD and its Working Group on Bribery have provided significant resources to develop sound anti-bribery systems and perform reviews that provide an assessment of progress in implementing anti-bribery programs. We encourage the OECD to continue these efforts and to continue to work with the 37 parties (“Parties”) to the *OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions* (the “Convention”), as well as governments of all nations, to ensure the Convention is properly implemented and functioning.

As the Consultation Paper recognizes, however, further steps are needed to maintain or enhance the effectiveness of these measures, and we encourage OECD’s ongoing efforts in this regard. Additionally, we encourage the OECD to urge the Parties to enhance awareness and enforcement, both within governments and in companies, in furthering the requirements of the Convention. In order to help advance these efforts, this letter provides comments and suggestions on several of the key issues addressed in the Consultation Paper.

I. Preventive and Detective Measures

We share the concern highlighted in the Consultation Paper about the apparent inconsistent and low level of awareness of the illegality of bribery of foreign officials among law enforcement authorities and at the company level.¹ Awareness of the illegality of bribery of foreign officials is driven both through the efforts of governments and companies. We believe prevention is the first line of defense to combat any form of corruption and prevention begins with awareness. Awareness throughout all levels of government that requesting and/or accepting bribes is illegal must be promoted by the Parties to the Convention. Further, enforcement efforts by government, discussed in more detail later, should be adequately robust.

At the company level, a low level of awareness can be indicative of potential compliance deficiencies. It suggests, for example, that a foreign bribery compliance program may not be present, or if it is present, that it is not effective or not yet embedded in the company culture, because of inadequate and sparse training, the absence of a proper tone at the top, non-enforcement of related disciplinary policy, or other reasons. In light of these considerations, we endorse the best practices designed to raise awareness and improve compliance discussed in the Consultation Paper. We recommend that the Parties encourage all corporations that engage in substantial public or international transactions (including unlisted corporations) to put in place the following preventive and detective measures at a minimum:

First, companies should adopt an effective compliance program. That program starts with a clearly articulated corporate policy against foreign and domestic bribery of public officials that is incorporated in the company’s employee handbook or in a separate corporate compliance code. The corporate policy should include disciplinary sanctions to deter persons who may be tempted to violate it.

Because an anti-corruption policy existing only on paper is not likely to be effective in instilling anti-corruption vigilance in the company’s employees, officers, and directors, periodic training should be required to educate employees about the corporate policy and also to teach them how to identify suspicious transactions that raise red flags and what to do, including who to consult, in that event. For example,

¹ Consultation Paper, paragraphs 79-82

employees should be taught to perform due diligence on new parties to whom payments are made, and to scrutinize payments meant for companies that do not seem to be engaging in any actual business activity or whose beneficial owners are unduly hard to identify, because such corporations may be potential bribery intermediaries. When employees are trained to seek out unusual transactions and are encouraged to raise questions, improper payments may be prevented before they occur. This heightened awareness by all company personnel will help to ensure that the compliance program functions effectively in its role as the first line of defense to prevent bribery from occurring. Further, some corporations require all employees, officers, and directors to annually certify compliance with the anti-bribery policies in writing.

Second, companies should adopt a proper tone at the top stressing that bribery is not acceptable and that appropriate disciplinary actions will be taken when instances of bribery are detected. Senior corporate officers should have the responsibility and authority to report compliance matters directly to the company's audit committee and board of directors, or the organization's functional equivalent of those governing bodies.

Third, where preventive measures have failed and an improper payment has been made, an effective reporting mechanism (*e.g.*, whistle blowing policy) should be in place to allow for the reporting of detected bribery and to prevent future instances of bribery. Reporting instances of improper transactions should be clearly communicated to personnel as constituting an acceptable and encouraged action. Because reporting of wrongdoing has not been the cultural norm in many countries or business environments, confidentiality must be ensured in order for the reporting mechanism to be effective.² It is recognized that establishing effective reporting channels whereby personnel are afforded the appropriate protections in order not to fear reprisal for reporting instances of bribery is challenging; sharing of best practices learned by OECD during its review process would be beneficial in this regard.

Fourth, effective implementation and monitoring of internal controls is also important in the prevention and detection of improper transactions. Internal controls are "the process designed and effected by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations."³ Put differently, internal controls are the framework management uses to provide assurance that employees are properly processing transactions and acting in legal and ethical manners. Those charged with governance, such as the board of directors, similarly rely on the company's internal control system as a mechanism to support management's activities.

One type of internal control that can reduce the opportunities for a person to conceal errors or fraud, such as disguising bribery payments as legitimate payments, is segregation of duties. The premise of this internal control is that different responsibilities, such as authorizing transactions, recording transactions, and maintaining custody of assets, are assigned to different people. This prohibits one person from handling all parts of a transaction. In the bribery example, segregating duties so that one person maintains custody of the company's cash (assets), with a second person authorizing payments to vendors, and a third person recording the payments in the company's books and records, requires the involvement of three persons to complete one cash transaction. This procedure is much more effective at identifying bribes than a procedure in which one person makes a bribery payment, authorizes payment of funds to the foreign official, and records the payment on the company's books and records under a legitimate classification.

Certain Parties to the Convention have recently enhanced the focus on corporate internal control programs. Examples of these enhancements include: the Sarbanes-Oxley Act of 2002 in the United States,

² Consultation Paper, paragraphs 87, 90

³ International Standards on Auditing Glossary of Terms, definition of "Internal control"

the French Financial Security Law of 2003, and the Financial Instruments Exchange Law of 2006 in Japan. On a global basis, the OECD and the Parties to the Convention should encourage companies to adopt internal controls that are designed to prevent and detect improper transactions.⁴

We believe that unlisted corporations engaging in substantial public and international transactions, including small and medium sized enterprises (“SMEs”), should also be encouraged to implement the preventive and detective measures described above. As SMEs are a large component of international business, their adoption of these measures is essential to the success of OECD’s anti-bribery initiatives. Not only would adoption of these practices help prevent bribery by the SMEs themselves, but it would also ensure that corporations that have succeeded in cleansing themselves of corruption will not become “re-infected” by acquiring or doing business with an SME in which bribery exists.⁵

Although it is often commented that SMEs do not have the resources to implement compliance measures, limited resources are not necessarily an obstacle to the implementation of the measures described above. Such measures can be implemented cost effectively, by adapting them to the complexity and available resources of the company. While some SMEs may not be subject to external auditing requirements and may not have internal audit functions, the implementation of compliance policies, reporting mechanisms, internal controls, and tone at the top by management are instrumental in helping to prevent bribery. We believe the OECD plays an important role by sharing as examples the best practices of SMEs and of larger organizations that have effective systems in place.

II. Independent External Audit

The measures described in I. above represent certain preventive and detective actions which may be taken on the part of corporations and their employees, officers and directors to counteract bribery. Additionally, it is important to look at the role external auditors play in the detection and reporting of bribery at companies they audit.

The Consultation Paper notes that “relatively few” Parties instill legal requirements for external auditors to report possible illegal acts of bribery to competent authorities.⁶ It is important to note, however, that the absence of such legal requirements does not equate to an absence of the external auditor reporting of such instances to management and/or the audit committee of the company and, in some instances, to external authorities.

Professional auditing standards generally guide the duties and responsibilities of external auditors. In many countries, those standards are based on the International Standards on Auditing (“ISAs”), which are issued by the International Auditing and Assurance Standards Board (“IAASB”) of the International Federation of Accountants (“IFAC”). These standards are created with input from the member bodies of IFAC and the IAASB Consultative Advisory Group, who represent 123 countries, through a due diligence process that involves public comment, which is open to all interested parties. When performing an audit engagement, an auditor is to perform the engagement in accordance with the ISAs and all local or national standards.

The professional auditing standards address the reporting requirements of the auditor, as well as the auditor’s responsibilities for and limitations that arise in the detection of fraudulent activities, such as bribery. The discussion of fraud within auditing standards rests on the foundational premise that the

⁴ Consultation Paper, paragraphs 97-99

⁵ Consultation Paper, paragraphs 79, 100, and n. 34

⁶ Consultation Paper, paragraph 108

“primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and with management.”⁷ This is consistent with the Consultation Paper, which states that, “sound principles of corporate governance and management commitment to those principles form the foundation for the prevention of foreign bribery.”⁸

The auditor has detective responsibilities to design “procedures to detect material misstatements due to fraud.”⁹ However, due to inherent limitations of an audit, “an auditor cannot obtain absolute assurance that material misstatements in the financial statements will be detected.”¹⁰ What this means is that an auditor designs an audit to identify misstatements due to fraud that would impact a reasonably informed user of the financial statements’ ability to understand the financial presentation of the company. However, among other reasons, because an external auditor is not a member of the management of a company, does not review every transaction undertaken by the company, and does not participate in all activities undertaken by all employees of the company, an audit may not identify all fraudulent activities, or instances of bribery, included in the financial statements that the auditor opines on.

It is also important to note another potential limitation in the auditor’s ability to detect noncompliance with laws and regulations. Professional auditing standards state that “the auditor should recognize that noncompliance by the entity with laws and regulations may materially affect the financial statements,” but the “further removed noncompliance is from the events and transactions ordinarily reflected in financial statements, the less likely the auditor is to become aware of it or to recognize its possible noncompliance”.¹¹ In other words, an audit is not designed specifically to detect noncompliance with all laws to which the company is subject.

A. Reporting By Auditors

The professional auditing standards state that “the auditor should communicate [] matters as soon as practicable to the appropriate level of management” when an instance of fraud exists or may exist, “even if the matter might be considered inconsequential.”¹² Further, the auditor should bring instances of noncompliance with laws and regulations identified during the course of an audit to the attention of the company’s senior management or, if senior management is involved, to others such as the audit committee or the supervisory board.¹³

The Consultation Paper notes that there have been few instances of external reporting by auditors of foreign bribery.¹⁴ We suggest that this is not attributable to the absence of reporting requirements or their disregard by auditors, but is due to the complexities surrounding detection and reporting. As mentioned above, noncompliance with laws and regulations may not be detected by auditors to the extent that such laws and regulations do not relate to financial statement matters that are within the scope of an audit. When instances of potential bribery are identified by the company or the auditor, management or the audit

⁷ ISA 240, *The Auditor’s Responsibility to Consider Fraud in an Audit of Financial Statements* (“ISA 240”), paragraph 13

⁸ Consultation paper, paragraph 96

⁹ ISA 240, paragraph 22

¹⁰ ISA 240, paragraph 21

¹¹ ISA 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*

¹² ISA 240, paragraphs 93, 94

¹³ ISA 250, paragraphs 32-34

¹⁴ Consultation paper, paragraph 108

committee, with legal assistance, often is in a better position to investigate more fully the facts surrounding the suspected bribery. After an investigation, the company may self-report to the authorities, depending on local reporting requirements, if a violation is indeed found. Thus, if the company, not the auditor, reports the violation to the authorities, it does not indicate that the auditor has failed to perform its obligations under applicable professional standards.

As professional auditing standards and the Consultation Paper recognize, it is management's responsibility to prevent and detect noncompliance with laws and regulations. The primary duty for external reporting of violations therefore should rest with management and we support efforts to strengthen these company reporting obligations. We do not, however, support transferring that reporting duty to external auditors, given the limitations in the ability of an audit to detect noncompliance described above and given that the company and its legal counsel are in a better position to investigate more fully the facts surrounding instances of noncompliance. In the absence of such diligent reporting on the part of the company, the external auditor could be permitted to notify the appropriate authorities if the local laws requiring such reporting specifically override the applicable auditor's client-confidentiality obligations in the jurisdiction.

With regards to current external reporting made by the auditor, it is important to note that in some countries the duty of confidentiality is overridden by local laws or statutes, and the auditor is required to report any material violations not reported by the company to the relevant authorities.¹⁵ Further, noncompliance by a company may be evident through reporting, to the extent such information is made public, of instances in which an auditor has to qualify or disclaim an audit report or resign from an engagement.

External reporting of bribery can have serious negative consequences on a company or an individual, even in instances where an investigation ultimately finds no bribery occurred. And, given the legal expertise necessary to determine noncompliance, auditors are justifiably cautious when reporting suspected bribery to authorities. Companies or even individuals may decide to sue an auditor for making a report which, in the end, is not substantiated as an act of bribery. Therefore, we also recommend that the Working Group encourage Parties to afford external auditors a legal "safe harbor" regarding any reporting of potential bribery transactions that the auditor makes reasonably and in good faith.

B. The Materiality Standard For Triggering External Reporting

Fearing that the concept of materiality is "vague," the Consultation Paper also seeks comment on the level of materiality which would adequately trigger reporting of potential bribery "either internally or externally."¹⁶ It should be noted that for internal reporting, materiality is not required to trigger an auditor's reporting obligation. Rather, under professional auditing standards, an auditor should internally report potential instances of noncompliance with laws and regulations unless they are "clearly inconsequential or trivial."¹⁷ Moreover, auditors are required to report fraudulent acts "even if the matter might be considered inconsequential."¹⁸ Thus, as a general matter, auditors already internally report potentially immaterial violations.

With respect to the external reporting obligation, we believe that the existing materiality standard under the International Accounting Standard Board's ("IASB") *Framework for the Preparation and*

¹⁵ ISA 250, paragraph 38 and ISA 240, paragraph 102

¹⁶ Consultation paper, paragraphs 66, 106, 111

¹⁷ ISA 250, paragraph 32

¹⁸ ISA 240, paragraph 94

Presentation of Financial Statements is workable and not vague. Auditors make determinations of materiality on a regular basis when conducting an audit. Information is material to both a company and an auditor if its “omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatement.”¹⁹ The misstatement is evaluated based upon “both the amount (quantity) and nature (quality)” of the misstatement.²⁰

The Consultation Paper expresses concern that the definition of “materiality” is vague unless it “takes into account certain qualitative factors.”²¹ Based upon the accounting and auditing standards cited above, indeed both quantitative and qualitative factors are evaluated relative to all identified misstatements. Put in the context of an identified bribery transaction, the auditor, for example, would determine materiality only after evaluating all factors related to the misstatement; even if quantitatively immaterial, the auditor would evaluate qualitative factors, such as the involvement of senior management or potential contingent liabilities (*e.g.*, fines, confiscation, the cost of legal proceedings, loss of future government contracts, and damage to the company’s reputation). We recommend therefore that international standards on accounting and auditing drive the materiality considerations for triggering external reporting.

III. Enforcement

The Consultation Paper reports that law enforcement officials lack awareness that bribery of foreign officials is an offense, and that, in cases where foreign bribery is reported to the relevant authorities, it is often not prosecuted, or if prosecuted, then not adequately sanctioned.²² We agree that these deficiencies, if they exist, are a matter of concern because efforts to achieve deterrence will be unsuccessful if improper conduct is not punished by applying appropriate sanctions. Where necessary, government intervention to enforce anti-bribery punishments should be strengthened. The OECD should work with all Parties to the Convention to ensure that they are not only creating awareness of the illegality of bribery within their countries, but are also supporting its proper enforcement, including providing adequate resources and imposing effective and timely sanctions.

The reluctance of many prosecutors to indict companies for foreign bribery offenses reported in the Consultation Paper²³ may stem from the harsh consequences on innocent third parties flowing from criminal prosecution, and could be minimized by providing leniency incentives. In the United States, for example, deferred prosecution agreements achieve enforcement goals—such as punishment (through public disclosure of the illegal behavior and disgorgement) and ensuring that the company implements an effective compliance program—without the negative collateral consequences on innocent employees and shareholders that would flow from a criminal conviction of the corporation. Moreover, the availability of such deferred prosecution programs encourages many companies to voluntarily self-report improper behavior, or to cooperate fully with the government once an investigation has begun, which in turn reduces enforcement costs.

We note that the Consultation Paper states that “by the time of the Mid-Term Study, there were no examples” of “confiscation” sanctions being imposed.²⁴ The United States, as an example, has in fact

¹⁹ IASB *Framework for the Preparation and Presentation of Financial Statements*, paragraph 30, and ISA 320 *Audit Materiality* (“ISA 320”), paragraph 3

²⁰ ISA 320, paragraph 5

²¹ Consultation paper, paragraph 66

²² Consultation paper, paragraph 34, 49-54, 79

²³ Consultation paper, paragraph 49-54

²⁴ Consultation paper, paragraph 33

required disgorgement of the proceeds generated by the payment of a bribe—usually calculated by deducting costs (such as labor and equipment, but not the bribe) from the sales revenues occasioned by the bribe—in many criminal and civil prosecutions of bribery of foreign officials. And although the Consultation Paper fears²⁵ that the disgorgement calculation is difficult to perform because it may require forensic accounting experience, its widespread use in U.S. cases indicates that it is not always an extremely difficult operation.

With respect to the sanction of debarment (*i.e.*, disqualification from doing further business with the government) discussed in the Consultation Paper,²⁶ the Working Group may wish to clarify that it is not encouraging Parties to require debarment inflexibly. If the market for a certain product or service is not competitive, debarment of a government contractor can often leave the government unable to secure a needed product or service. In addition, debarment may often be too severe. For these reasons, the imposition of the sanction of debarment should be left to the discretion of the contracting government agency.

IV. Expanding Coverage

It is undisputable that significant anti-corruption advances have been made in recent years. The Convention, which entered into force a decade ago, now unites 37 governments in the anti-corruption initiative. While the efforts and progress made by the OECD and the Parties to the Convention have been significant, the absence of full global support is a lingering major obstacle to the anti-corruption efforts. With the growth of the capital markets, the significant increase in the amount of cross-border transactions, the heightened complexity of such transactions, and the emergence of new countries in the international markets, a level playing field for international business to ensure honest and reliable business activity is essential.

The OECD's effort to encourage accession to the Convention by non-Parties, including major emerging economic players, is crucial to this endeavor—and we fully endorse it. We recognize the OECD has commenced the OECD membership process with Chile, Estonia, Israel, Russia, and Slovenia, of which Chile, Estonia, and Slovenia are already Parties to the Convention as non-OECD members. Also, as part of the OECD's enhanced engagement process, Brazil and South Africa have become Parties to the Convention as non-OECD members. It is our hope the OECD will similarly make accession to the Convention a priority in its enhanced engagement process with China, India and Indonesia. Indeed we believe the OECD and other Parties to the Convention should make it a priority to instill in all governments the importance of accession to the Convention.

While we also encourage the work being done with non-Parties to the Convention to seek mutual legal assistance and other cooperation, such cooperation should be recognized as only an initial small step, so as not to hinder (through potential complacency) the progress towards the more important final goal: accession.

²⁵ Consultation paper, paragraph 34

²⁶ Consultation paper, paragraph 35