PricewaterhouseCoopers, Biggest Accountant, Faces IRS Audit

By Vineeta Anand

Aug. 25 (Bloomberg) -- PricewaterhouseCoopers LLP, the world's largest accounting firm, is being audited by the Internal Revenue Service for potential violations in reporting its own taxes, according to IRS and company documents.

The IRS is evaluating the timing of tax deductions, PricewaterhouseCoopers' pension plan, and how the firm moved profits between international units, said a person briefed on the audit. The review may be completed later this month and the IRS is expected to reach its conclusions by the end of the year, PricewaterhouseCoopers' tax partner Samuel Starr said in a June 15 letter to the New York-based firm's 2,000 U.S. partners, who could be liable for any back taxes.

Additional taxes or penalties could damage the reputations of the firm and the industry, which have been under increased scrutiny since the 2001 collapse of Houston-based energy trader Enron Corp. and the demise of its auditor, Arthur Andersen LLP.

The IRS review may cost partners at PricewaterhouseCoopers ``scores of millions'' of dollars, said Robert Willens, a tax and accounting analyst at Lehman Brothers Holdings Inc. in New York.

``If the pension plan were to be disqualified, the results would be potentially nuclear,'' said Richard Susko, a pension attorney and partner at the New York law firm of Cleary, Gottleib, Steen & Hamilton. PricewaterhouseCoopers could lose deductions it took on contributions to the pension plan, though the IRS probably will ``work out something less draconian,'' he said.

Partner's Letter

Officials at PricewaterhouseCoopers declined to discuss the audit. IRS spokesman Bruce Friedland also declined to comment, saying federal audits are confidential.

``PricewaterhouseCoopers is a large organization and like any large entity is under constant review by various taxing jurisdictions,'' said Steven Silber, a spokesman for the firm.

Edward Nusbaum, chief executive officer of Chicago-based Grant Thornton LLP, the sixth-largest accounting firm, said he was unaware of previous IRS audits of accounting firms. ``In general, accounting firms don't get audited,'' he said. ``I know we have not been audited.''

The IRS notified PricewaterhouseCoopers of the audit in a June 3, 2005, letter to Starr, a partner based in Washington and an adjunct professor of law at Georgetown University. Starr's letter to his fellow partners, sent June 15 of this year, said the audit covers the

firm's fiscal years ending September 2002 and September 2003. Copies of both letters were provided to Bloomberg News.

``To date, the IRS has not proposed any adjustments," Starr wrote in the letter. ``However, we are not finished yet, and I will keep you advised in the event of any significant developments."

`Squeaky Clean'

PricewaterhouseCoopers audits some of the world's biggest companies, including Irving, Texas-based Exxon Mobil Corp., the No. 1 oil producer; Dearborn, Michigan-based Ford Motor Co., the second-largest U.S. automaker; and New York's JPMorgan Chase & Co., the No. 3 U.S. bank by assets. It employs more than 130,000 people in 148 countries.

Accounting firms rarely get audited because they are experts in tax matters and would probably avoid taking deductions that could raise a red flag at the IRS, said Tom Ochsenschlager, vice president of taxation at the American Institute of Certified Public Accountants, the industry trade group in Washington.

``Between saving a few dollars and being squeaky clean, I'd think they'd want to be squeaky clean," he said of PricewaterhouseCoopers.

Arthur Andersen was convicted of obstructing justice for shredding documents of its Enron audits. A subsequent Supreme Court ruling overturned the conviction after the firm had already gone out of business, reducing the number of biggest accounting firms to four. Congress established the Public Company Accounting Oversight Board in 2002 to provide stricter oversight of the accounting profession.

Tax Shelters

KPMG LLP, the No. 4 U.S. accounting firm, agreed a year ago to pay the government $456 million to avoid criminal prosecution for selling illegal tax shelters, while eight of its partners were indicted for fraud. At the time, industry and government officials said the administration of President George Bush was trying to punish the firm's conduct without driving it out of business.

At PricewaterhouseCoopers, the IRS is examining so-called transfer pricing, where global companies sell goods and services between divisions, often to take advantage of lower tax jurisdictions, said the person briefed on the audit, who declined to be identified because the matter is confidential.

The IRS claims GlaxoSmithKline Plc, Europe's top pharmaceutical maker and a longtime PricewaterhouseCoopers client, owes more than $5 billion in taxes and interest. The tax agency alleged its U.S. subsidiary reduced taxable income by overpaying the British parent for drugs. Glaxo denies the claims and the case is set for a trial next February in U.S. Tax Court.

Pension Plan

PricewaterhouseCoopers set up a cash-balance pension plan for its U.S. employees in 1998 and designed similar programs for clients including Bank of America Corp., the nation's second- largest bank.

Bank of America, based in Charlotte, North Carolina, disclosed in March that the IRS found its cash-balance plan violated tax laws. By encouraging employees to move 401(k) retirement savings into the new pension, the bank took away benefits workers had already earned, the IRS determined.

Bank of America is ``in administrative proceedings with the IRS in an attempt to work out a resolution to the technical issues raised in the audit," spokesman Terry Francisco said.

Starr's June 15 letter to PricewaterhouseCoopers' partners said the IRS audit began in January of 2005.

Two months earlier, a former employee at the firm, Timothy Laurent, sued PricewaterhouseCoopers, alleging it misused the cash- balance plan as a tax shelter. He claimed the firm's practices enriched its partners while depriving rank-and-file employees of full pension benefits.

PricewaterhouseCoopers denied the claims and is seeking to have the suit dismissed.