Dear Reader

Historically the tax director was predominantly a technical expert within the finance function. With a focus on technical reporting, compliance and tax planning, there was little, if any, alignment with the rest of the business. Today, a tax director is more of a real-time commentator and advisor to management than a historical custodian. This means that in addition to their technical knowledge they need a range of other skills and tools: strong influencing and communication skills, people and team-building skills, the right technology tools and a tax risk management mindset.

In the same way that finance functions have evolved to become “business partners,” so tax directors are also stepping into the limelight. Tax directors no longer sit in a corner of the finance department, but are interacting with managers across almost every function in the business.

The economic and fiscal environment is a key driver of this change. With governments around the world seeking to manage their finances better and administrations sharing information to an unprecedented extent, tax policy and enforcement activities are more pervasive to business than at any time in recent memory. Companies that do not understand the implications of these trends will quickly find themselves facing greater scrutiny from tax administrations, as well as the potential for reputational risk. In this environment, it is crucial for companies to adopt a proactive approach to tax management that is closely aligned with their strategic choices.

The role of the tax director is now broader, higher-profile and more commercial than it was in the past. Tax directors have more opportunities than ever to step into other roles, and companies are now keen to create careers for tax professionals that give them exposure to different disciplines and geographical locations.

A higher profile for the tax director has also added significantly to the demands of the role. The tax function often faces conflicting expectations: On the one hand, it is expected to bring down the effective tax rate at least to the level of the company’s peers but, at the same time, it must carefully manage relationships with many different tax administrations around the world and ensure that the business is not exposing itself to reputational or financial risk. Along with this, tax directors are under pressure to increase the efficiency of their operations and often have fewer resources at their disposal to manage the company’s tax affairs.

In this ninth issue of T Magazine, we explore the changing role of tax directors and examine how they must interact with the rest of the business. This is an important topic not only for tax directors themselves, but also for the entire management team and the business at large. With tax likely to remain high on the political agenda for some years to come, the way in which companies manage tax and build links between the tax department and the rest of the business is increasingly critical.

We hope you find this publication valuable and stimulating.

Stephan Kuhn

Stephan Kuhn is Area Tax Leader for the Europe, Middle East, India and Africa (EMEIA) region at Ernst & Young.
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Cover

“We need a political union. That means we have to give up further competencies to Europe, step by step, in an ongoing process.”

German Chancellor Angela Merkel on Europe’s greater future integration (see page 16).
Global tax news
A roundup of recent developments from major governments and tax administrations

1 Spain
July 2012
Spain has published measures to achieve a balanced budget and promote competitiveness. This includes several steps aimed at increasing the tax burden of large companies, including restrictions on compensating losses, limited depreciation of intangible assets and increased advance payments for larger companies. With effect from 1 September 2012, the general VAT tax rate has increased from 18% to 21%, while the reduced 8% VAT tax rate increased to 10%. Several transactions previously subject to the reduced rate will be subject to the new general VAT rate.

2 European Union
July 2012
The European Commission set up an EU VAT Forum intended to improve the relationship between business and tax authorities. The Forum aims to create conditions for a smoother-functioning VAT system in the EU, while reducing the costs and administrative burden on both sides. The Forum shall comprise representatives from member states and from 15 organizations representing business or tax practitioners.

3 United Kingdom
July 2012
The UK Government has published its definition of environmental taxes which monitors the progress on the pledge to increase the proportion of tax revenue that comes from these taxes. Environmental taxes are those that are explicitly linked to the Government’s environmental objectives, encouraging environmentally friendly behavior. The following taxes qualify as environmental taxes: Climate Change Levy, Aggregates Levy, Landfill Tax, EU Emissions Trading System, CRC Energy Efficiency Scheme and Carbon Price Support. This definition excludes vehicle excise duty, fuel duty and air passenger duty, which were previously classified as environmental taxes.

4 India
July 2012
An expert committee in India has been finalizing guidelines for the application of a general anti-avoidance rule (GAAR), for implementation in September 2012. Its mandate has been expanded to look into the taxation of portfolio investment, focusing on recent amendments to Indian income tax law, relating to the taxation of non-resident transfer of assets.

5 United States
July 2012
The US Treasury Department and the US Internal Revenue Service (IRS) issued Notice 2012-45 with guidance on the treatment of income from certain government bonds for purposes of determining whether a foreign corporation is a passive foreign investment company (PFIC) under section 1297 of the US Internal Revenue Code (IRC). The IRS noted current economic conditions have resulted in foreign financial institutions holding government bonds in higher levels compared to historical norms, and that this has raised issues regarding the treatment of these institutions under PFIC rules.
The internationalization of tax policy and administration means tax directors must think more globally than ever before. Recent years have seen many new taxes, regulations and codes of conduct to comply with. The OECD, for example, has issued guidelines for areas including transfer pricing, tax havens and joint tax audits. Meanwhile, the EU has started to explore increased tax harmonization.

At the same time, tax directors must work with their local tax authorities who are increasing efforts to combat aggressive tax planning. The US, most prominently, is pushing ahead with the provisions of the Foreign Account Tax Compliance Act (FATCA), which targets tax evasion via foreign investments and accounts. Due to be implemented in 2013 and 2014, FATCA has global ramifications and will create a huge administrative burden for financial institutions.

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**“Aggressive” cross-border tax planning concerns for policy makers**

Comparison of cross-border situations highlighted in European Commission and OECD reports

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<td>Transfer pricing and unilateral advance pricing arrangements</td>
<td>Dual residence entities</td>
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<td>Debt financing of tax-exempt income</td>
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<td>Different treatment of passive and active income</td>
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Source: Ernst & Young

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**OECD’s watch list of tax standards compliance at 2 April 2009**

Increased transparency has seen a rush by jurisdictions to substantially comply with international tax standards, seeking to move off the OECD’s “black list”.

**OECD’s watch list of tax standards compliance at 18 May 2012**

Source: OECD

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**2002**

**The globalization of tax**

**April 2002**

The OECD Global Forum Working Group on Effective Exchange of Information released a legal instrument which now forms the basis for hundreds of bilateral Tax Information Exchange Agreements.

**November 2004**

The United Nations Economic and Social Council formalized a Committee of Experts on International Cooperation in Tax Matters, designed to enhance tax cooperation among national tax authorities.

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**2008**

**August 2008**

The African Tax Administration Forum (ATAF) was established to promote and facilitate mutual cooperation among African tax administrations to help improve the efficiency of their tax legislation and administration.

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**2009**

**April 2009**

Prompted by the G20, the OECD launched a black, gray and white listing for jurisdictions surveyed by the Global Forum in implementing internationally agreed tax standards.

**September 2009**

The OECD Global Forum called together 178 delegates from 70 jurisdictions and international organizations to respond to a global drive from governments to protect their tax bases from non-compliance.
The OECD strives to eliminate double taxation and other obstacles to cross-border trade and investment. We are also working hard to make sure there are no tax loopholes between tax systems that would allow some to gain an unfair competitive advantage.”

Pascal Saint-Amans, Director of the OECD Centre for Tax Policy and Administration

97% of tax administrators report that they will increase their focus on tax risk related to international structures and cross-border transactions in the coming three years.

75% of tax directors in large companies report heightened risk or uncertainty around tax legislation. This figure rises to 78% for BRIC-based companies and 83% for US-based companies. However, only 57% of CFOs report that they feel heightened risk or uncertainty around tax legislation.

$8b the amount in US$ expected to be recovered by FATCA over 10 years. The cost of FATCA compliance for some large firms is estimated at between US$70m and US$100m.

Germany
Discussion on the proposal for a CCCTB in the EU is shaping the national debate on tax policy in Germany. Given the strong involvement of the Federal Minister of Finance and Chancellor Merkel, it is expected that at least symbolic steps will be made toward harmonizing business taxes between Germany and France (despite substantial obstacles to implementation).

India
In a letter to the United Nations (UN), the Indian Government has condemned the OECD Transfer Pricing Guidelines on the grounds they are not well suited to developing countries. According to the Indian Government, “These guidelines on transfer pricing only reflect the agreements amongst governments of those countries that are members of the OECD (developed countries) and accordingly tend to take care only of the interests of developed countries.” UN involvement was sought to address these concerns.

March 2010
The US Hire Act passed including the FATCA, requiring US taxpayers to report foreign financial assets to the Internal Revenue Service (IRS), and foreign financial institutions to disclose accounts held by US taxpayers.

April 2010

September 2010
The OECD Forum on Tax Administration saw the release of the OECD’s Joint Audit Report and Joint Audit Participant’s Guide. These provide a framework for multijurisdictional tax audits of companies with cross-border activities.

March 2011
The European Commission proposed the CCCTB, a “one-stop shop” system for calculating the tax base of businesses operating in the EU.

January 2013
The original deadline for compliance with the FATCA, the US Government’s tool against offshore tax evasion. Firms must now comply with a phased-in schedule during 2013 and 2014.
The focus of the tax director is changing and becoming much more aligned with the business. This will help companies manage risk and achieve their objectives, but it has major implications for the entire finance function.

Shifting from custodian to advisor

Recent years have seen significant changes to the role and scope of the tax department. Until recently, their work was largely seen as separate from the rest of the business. While the rest of the company focused on the strategic requirements of the present and future, the role of the tax director was to oversee a function that was predominantly looking into the past. With a focus on technical reporting, compliance and tax planning, there was little, if any, alignment with the rest of the business.

The situation today is very different. The emphasis has shifted from historical reporting to a much closer engagement with the broader business. In a recent Ernst & Young survey of European and American tax executives and CFOs, 95% said that the ability for tax directors to design and execute business and tax strategy would be more important over the next three years compared with today. Only 52% said the same of the deep tax technical skills that so shaped the role in the past. “The role of tax director has shifted from being a custodian and reporter of the numbers to more of a real-time commentator who adds value and supports the business,” says Carmel Moore of Ernst & Young’s Tax Advisory Team in the UK.

This is not to say that an in-depth understanding of technical areas is no longer relevant. Among the survey respondents, 86% of tax directors felt that this technical knowledge would remain a prerequisite for positions of tax leadership. “There are certain things that simply remain necessary for a tax function,” says Martin Rabenort, Ernst & Young’s Tax Performance Advisory leader of Belgium and the Netherlands. “Above all, you need to comply with the law and regulation.”

The result is that tax directors must now demonstrate a broader palette of skills than at any time in the past. “The role of tax has become more inclusive,” says Erik Fredriks, Head of Group Taxation at NXP Semiconductors, the Netherlands-headquartered, global semiconductor company. “Although companies still need specialists in a variety of areas, such as indirect taxes, tax accounting, and corporate tax law in major jurisdictions, there have been more tasks added.”

Regulation drives change

So what is driving the increased demands of the tax director role? One clear catalyst of change has been increased regulation. Sarbanes-Oxley, now a decade old, and similar laws passed in other jurisdictions, ushered in a new era of greater oversight. In the meantime, the financial turmoil since 2008 has led officials in many countries to be more aggressive in seeking tax revenue. The result is that board audit committees, CEOs and CFOs can no longer simply trust tax functions to achieve the traditional goal of “no surprises.” Corporate leaders need to know the important tax risks that they face, whether arising from positions taken, corporate structuring or shifting political winds.

At the same time, globalization has brought added complications to the role of tax director. Companies now typically have complex structures spanning multiple jurisdictions, often including a presence in multiple rapid-growth markets, where legislation and enforcement may not always meet the norms of more developed countries. The challenge of sorting through the tax implications of such transnational arrangements is therefore quickly growing.
Erik Fredriks — The Head of Group Taxation at NXP Semiconductors, the Netherlands-based semiconductor giant, Fredriks says businesses still require tax professionals with specialist expertise, but need directors who have a more rounded set of talents.
A widening domain

The changing dynamics of tax and the tax function have opened up new opportunities for tax directors. More so than ever before, tax leaders can play a greater role in tasks that are much more forward-looking than in the past. Some of the most prominent at just one company, NXP Semiconductors, include:

Strategic planning: More up-to-date data allows tax functions to have a better grasp of upcoming liabilities. The precise needs will vary depending on external circumstances. For example, Erik Fredriks, the company’s Head of Group Taxation, notes that, during the economic downturn, cash tax forecasting became increasingly important because cash levels were crucial. On the other hand, he adds, lower profits during such a period can make other tax issues of less immediate strategic concern.

Major transactions: Mergers and acquisitions (M&A), disposals and large investments all have important tax implications that can have a substantial impact on return on investment. This is particularly true of cross-border, or complex, transactions, where bringing in the expertise of tax executives early in the process is increasingly seen as best practice. Fredriks notes that, even as tax’s strategic input into other areas has varied with economic conditions, it has remained at the forefront with M&A.

Supply chain: International supply chains raise a host of tax questions. Transfer pricing is a major issue, although by no means the only one, as questions of indirect and direct taxation arise in almost every shift or reorganization. At NXP, tax is represented with all the other relevant functions on a Goods Flow Control Board, which analyzes all potential supply chain changes from every perspective, including tax.

Reputational issues: The role of tax in risk management now goes beyond the possibility of unexpectedly large assessments. Increasingly, says Fredriks, government officials are more interested in substance over form. Thus, authorities may reject technically legal tax arrangements because they feel that they breach the spirit of legislation. This means that tax functions need to judge the potential reputational impact of positions as well as their legality.

For Albert Lee, an Ernst & Young EMEIA Tax Performance Advisory Partner, the role of tax director has never been so holistic. “It now encompasses things like people management, reputational risk, commercial skill, systems and processes,” he explains. “It is not just technical: It is operational and commercial as well.”

Identifying the risk areas
The widening responsibilities of the tax function, and the need for highly specialist skills across a large number of geographies and activities, mean that tax functions have typically become much larger in recent years. “The tax function is now often a significantly sized team,” says Lee. “Some are like mini-firms in themselves. Simply managing these large teams has added to the demands of the tax director role.”

Regulation and globalization inevitably mean that tax directors need to play a greater role in risk management. This involves enhanced interaction with other parts of the company. “Tax is now much more involved in the design and running of control processes because the function needs to have a thorough knowledge of how they work and what the data they produce mean,” explains Erik Fredriks. “You can only define your processes and controls after you have identified the risk areas with your peers. This means that tax directors need to reach out to other functions to agree upon the risks they see and upon handover points. Tax must not operate in isolation.”

Improved technology and Big Data also have major implications for tax functions and their directors. First, they mean that controls and processes that gather data – for risk management or any other reason – can now do so in real time. For tax executives, who previously concentrated solely on reporting the past, this permits a fundamental shift in focus toward the present. Second, the new role has taken tax directors out of their traditional silos, moving them toward being partners with other leaders in the business rather than rulers of their own, restricted domain.

A new CFO dynamic
Along with this evolution comes a clear change in the dynamic between the CFO and the tax director. “Gone are the days when all CFOs expected from their tax directors was ‘no surprises’”, says Moore. “These days tax risk issues can arise quickly and evolve in very different ways. As such, the CFO now expects insightful and articulate business-like interaction with his tax director, to keep him appraised of tax risk management issues, both globally and in real time.”

Such expectations are just a part of what CFOs are increasingly looking to their tax directors to deliver on, and what value they hope to get from their leadership.”

Director or coach?
“Tax directors have a duty to mentor and coach potential tax leaders within their organization.”

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<th>Percentage</th>
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<td>32%</td>
<td>Tax Directors</td>
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<td>40%</td>
<td>Assistant Tax Director</td>
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<td>41%</td>
<td>CFOs</td>
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Strongly agree
Agree

Source: Ernst & Young
Former US President George W. Bush signed into law the Sarbanes-Oxley Act of 2002 on 30 July 2002. President Bush described the act as “the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt.”

95% The number of CFOs who say the ability for tax directors to design and execute business and tax strategy will become more important over the next three years, according to an Ernst & Young survey.

52% The number of CFOs who believe that the sort of deep tax technical skill tax professionals have developed in the past will become more important in the next three years.

86% The number of tax directors who believe that technical knowledge will remain a prerequisite for positions of tax leadership despite the shift in focus to other skills and talents.
from them, notes Richard Baker of Ernst & Young in the UK. “CFOs are really looking for someone to help share the load, and they want to see more initiative and leadership coming from within the finance leadership team, including the tax director,” he says. “Along with this, they’d like to see a bit more decisiveness and a greater speed of decision-making from tax leaders, a sense of greater ambition and responsibility.”

As part of all of this, the contribution from tax directors that CFOs now expect breaks down into several key areas. One is clearly a strong technical understanding of tax matters, including a detailed understanding of the company’s prior tax history. Another aspect is about loyalty and commitment, and the reassurance that the tax team would not fail on any of the basics. A further aspect is about ensuring good relationships with the tax authorities, while still delivering within the best interests of the business. Finally, says Baker, it is about ensuring that tax makes a tangible contribution to the company’s overall earnings per share: “This is probably the thing that the CFO values more than most other parts,” he says.

**Deeper partnerships required**

To deliver on all of these objectives, tax directors have to acquire a deeper knowledge of the business than before, argues Lee. “You need to be ahead of the transaction before it happens and that requires knowledge of how the business operates,” he says. “You can’t do transfer pricing unless you understand the activities and risks of each business unit, and unless you have real-time connectivity with the managers who lead those units.”

In addition, tax directors must align themselves with the operational aspects of the business, working closely with a range of back office functions. “Tax directors need to work with IT to get their jobs done and they need to integrate with finance as tax relies on their data,” explains Lee. “They also need to work with HR because tax teams have grown and people are more mobile, while they must also work with treasury, because tax is a huge cash flow issue, and with legal, because tax is still about law form. There is a huge interdependency and tax directors need to embed themselves in those functions.”

Such a dramatic shift from the past has required tax directors to make important changes of their own. If tax functions bury themselves in compliance and securing the past, then they will not have enough time to understand how to be a good business partner. “Sometimes, you see companies where people look at tax as the guys who are not an integral part of finance but have their own show,” says Rabenort. “It is important for tax to cross the bridge.”

What, though, does crossing the bridge require? A crucial ingredient is strong leadership, and clarity of vision around the role of the tax function. In particular, tax directors need to ensure that tax is no longer a separate kingdom but aligned with broader business strategy. Presenting the tax function as an enabler is also important. “Tax is always cautious about risk and there may be the view that tax will hit the brakes but not tell you what to do instead,” says Rabenort. “Business is always looking for more business.”

Even with a vision that is more closely aligned with the company, tax directors believe that their function will still have to get better at explaining itself to the rest of the business. A recent survey by Ernst & Young found that stakeholder management, in particular, will be a much more important skill for tax directors in the next three years. Yet worryingly, respondents also think that those skills are in short supply. “Leading organizations are skilling themselves up to meet the new challenges facing tax but, by and large, they are still a minority,” says Albert Lee.

The people aspects and softer side of tax may be increasingly vital, but so too is the need for high-quality, accurate and complete data. “Tax people have to embrace technology a lot more, because they will always be asked to do more with less,” says Lee. “If you have no data, you can’t tax plan or do compliance efficiently. Even the two traditional jobs of tax are impeded by the lack of quality data.”

This returns us to the point of noting that while the role of the tax director has been evolving to include additional responsibilities, the nature of their existing ones has also changed. Regulators, faced with their own administrative resource constraints, are increasingly shifting to a risk-based approach. This means that companies must have the right data-gathering processes in place, and be able to demonstrate this as part of their compliance.

In the Netherlands, for example, Erik Fredriks reports that Dutch tax authorities increasingly want a relationship with taxpayers. If a complex situation arises, companies and the authorities discuss it upfront, before a return is filed, and then agree on how to address it. “This enhanced relationship is based around transparency and disclosure, where tax administrations trust that the taxpayers are doing their best to come up with a correct final return,” he says. “It is a new way of working.”

**Looking to the present and future**

Similarly, tax auditors may examine the processes and controls currently used to obtain the data rather than focusing on reported information from years earlier.

In many ways, this sums up the shift in the role of the tax director. Focusing on the past is no longer enough. To be an effective business partner, and to manage complex risks in a highly dynamic environment, tax directors must look to the present and future. This will align them with the broader business, and enable them to become more valued for both their traditional and their more recent set of responsibilities.
Interview

Fostering internal business relations

An interview with Dmitry Kornev, Director of Taxes at MTS, the leading telecommunications provider in Russia and the CIS.

T Magazine: How has the role of the tax function changed at MTS?
The function's role has changed dramatically. We realized that the tax department could play both a direct and an indirect role in our company – by providing back-office support to our business as well as adding more value to the company as a whole.

Our shareholders believe that free cash flow, along with capitalization, is a very important financial indicator. Tax management can have an influence on this indicator. As a result, we changed the performance goals of the tax function and its relationship with the other units within the company. Before that, the tax function had been a part of the accounting function that dealt with matters concerning tax payments and submission of declarations. But viewing the tax function as a proactive division within the company meant changes in the nature of interactions and related processes were required.

What has this meant to the relationship between the tax function and the business?
Repositioning the function as an active unit has meant that the tax department gets involved in certain business processes at their early stages when operating models are still either being developed or discussed. This has led to much closer interaction between the tax function and practically all the main subdivisions of the company, especially in financial subdivisions. This also means we need to have efficient tax due diligence at the earliest stages of any business processes that have an influence on taxes.

What was the main stimulus for the change?
It came about when we were looking for the instruments to improve internal efficiency. Our vision was twofold – to implement the existing business models and follow the path of proactive expansion into new markets, and to improve efficiency. When a function positions itself as an active one that is constantly on the look for ways to improve its efficiency, it quickly becomes perceived as essential for the business.

What are the challenges to smooth interaction between the tax function and the other parts of the business?
It depends on the role your company wishes to play. For example, if your company’s corporate culture encourages every business unit to seek ways to improve their efficiency, then the interaction will be straightforward because you all have the same goals. Moreover, the reverse is probably true, especially in a situation where this sort of philosophy is not shared by the various units of your company. Problems with interaction only arise if there are differences in attitude.

How do you best achieve good relationships with the business, particularly when people with whom you are dealing might have only limited knowledge about tax?
We tell them that we respect their competencies and give them freedom to set strategic objectives, whereas we are responsible for the efficient implementation of these objectives from the point of view of accounting, tax efficiency and legality. Our main task is to let the management know our competencies, and explain what we can do and the instruments we have at our disposal to achieve business objectives.

Adding value
Businesses are discovering that the tax function has a role in adding value as well as providing traditional support services.
Tax as a career

Exciting, vital, terrifying or dull, views on tax as a profession inevitably vary widely. But few people appreciate its diversity and depth, or its potential rewards for those who successfully climb up the ranks.

Although many think of tax as a single area of specialism, there are diverse routes that tax professionals can pursue. The following highlights nine common routes that can be followed.

**Many routes to follow**

- **International tax**
  - International tax professionals deal with cross-border compliance and planning issues

- **Expatriate tax**
  - These individuals handle tax affairs involving overseas assignments

- **Transfer pricing**
  - Much in demand currently, transfer pricing professionals handle taxes involving cross-border transactions

- **Employee tax**
  - These professionals deal with tax liabilities associated with employees, such as payroll and social security

- **Treasury**
  - Treasury tax professionals deal with tax issues associated with corporate financing

- **Personal tax**
  - These advisers deal with tax affairs of individuals

- **VAT & indirect tax**
  - These professionals handle sales taxes, customs and excise duties

- **Corporate tax**
  - The central tax function focused on tax compliance, planning and managing corporate tax liabilities

- **Trusts**
  - This category of tax professional looks after tax issues associated with inheritance and trusts

- **Expatriate tax**
  - These individuals handle tax affairs involving overseas assignments

- **Transfer pricing**
  - Much in demand currently, transfer pricing professionals handle taxes involving cross-border transactions

**A traditional career path**

- **School leaver entry**
  - 0-1 year

- **Graduate trainee**
  - 0-2 years

- **Newly qualified tax advisor**
  - 1-3 years

- **Tax advisor**
  - 2-4 years

Sources: CIOT, ACCA, Brewer Morris, Hays, HMRC / Graphic: Käthi Dübi
Top three things that tax professionals most enjoy about their career choice:

1. Build strong relationships with clients
2. Apply technical knowledge and skills
3. Advocacy – arguing a case to the tax authorities, for example

Top three things that tax professionals dislike about their careers:

1. Constant changing of the rules by tax authorities
2. The rise in litigation accusing accountants and tax professionals of negligence
3. The public perception that they facilitate tax evasion

95% The number of employers planning to increase their tax professionals' salaries during 2012.

70 The number of countries in which students are currently studying for the Advanced Diploma in International Taxation.

40% The number of employers planning to pay tax professionals a bonus during 2012.

Jobs taken by UK accounting graduates one year after achieving degree
Harmonizing taxation - reducing bureaucracy

From 2013, a uniform corporate tax rate is due to go into effect in Germany and France. This is part of wider plans by Chancellor Angela Merkel to create a more competitive private sector across Europe by harmonizing and streamlining taxes.
By James Watson, Elmar zur Bonsen

The lingering euro crisis has raised profound questions about the future direction of Europe's political and economic integration. Much of this pressure has been laid on Germany's Chancellor, Angela Merkel, regarding the fate of the Eurozone. An early August cover of the UK's Economist newspaper showed the Chancellor reading a (fictionitious) report on “How to break up the euro,” while the title asked whether she was tempted to do so.

Officially, though, Chancellor Merkel’s argument is that she wants more Europe, not less. In her bid to save the common currency, she is willing to go to the very limits of what is permissible under the German constitution. That was made clear by her support for the permanent euro rescue fund, the European Stability Mechanism, and also the Fiscal Compact, a deficit reduction treaty signed by all Member States barring the UK and Czech Republic. But Chancellor Merkel still wants more. “We need a political union,” as she recently argued in an interview on ARD, a German television channel. “That means we have to give up further competencies to Europe, step by step, in an ongoing process.”

Across the border in France, President François Hollande also remains enthusiastic about Europe’s greater integration. While both leaders have their differences on the economic question of stimulus versus austerity, they do agree on certain arguments, such as taxing certain financial transactions. Together, the two leaders are working to build a coalition of the willing to support the tax, even while conceding that some Member States, notably the UK, won’t be joining.

This builds on earlier efforts toward harmonizing Europe’s tax policy. Earlier this year, Chancellor Merkel and President Hollande’s predecessor, Nicolas Sarkozy, put forward common tax plans, including an agreement to harmonize corporate income tax rates in both countries by 2013. This move increases the prospect of an EU-wide corporate tax rate — something that Ireland, which offers an ultra-low business tax rate of 12.5%, and the UK, are heavily opposed to. Similar proposals have come from the European Commission, which has called for a single “aligned” business tax rate known as the Common Consolidated Corporate Tax Base for all of Europe (see Outlook on p.48 for more).

Streamlining tax

These headline moves follow on from other moves to simplify and harmonize Europe’s tax regimes. In a joint green paper, released at a summit in February 2012, the German and French authorities outlined a clear aim: “Our goal is to push on with the elimination of bureaucratic barriers in Germany and the rest of Europe in order to relieve the tax burden posed to small and medium-sized enterprises.” Chancellor Merkel has been at the forefront of such moves. Outlining the green paper at the summit in Paris in February, she made the case for more commonality in fiscal and economic policy. As she argues, such efforts could go a long way toward creating a more level playing field with regard to competition.

“Companies operating in several countries have to expend considerable resources in dealing with 27 different systems,” she noted. “This presents problems for small and medium-sized companies in particular.”

Indeed, tax harmonization, along with closer cooperation between national tax authorities, could relieve some of the cost burden of corporates and thus help to facilitate investment. In the Chancellor’s eyes, the German-French axis is intended to serve as the driver of further European regulation.

Removing obstacles

The German leader also seems determined to eliminate bureaucratic obstacles for companies, also acting in concert with France and other EU partners. At home, the German Government had already achieved “remarkable success in reducing bureaucracy and, in so doing, fortified Germany as a business location,” as she noted in a declaration of her party, the Christian Democratic Union (CDU). Already, more than 400 measures have been initiated between 2006 and the end of 2011, providing some €11b in relief to the business community each year.

For tax directors, all this adds up to a considerable amount of political attention being paid to their specialist area of expertise. While challenging in many respects, given the recent increase in activity and wide-ranging uncertainties as to how much of this will develop, it also provides new opportunities to advise others within the business – and to deliver clear bottom-line savings. Of course, this requires them to take a more outward-looking perspective from the tax function, to reach out proactively to other business unit leaders and executives to show them how they can help.

There is also scope to streamline and improve the tax function’s operating processes and efficiency, such as a shift to electronic reporting for tax. This underlines one of Chancellor Merkel’s fundamental aims, which is to try and revitalize the private sector. “Processes that are as simple and unbureaucratic as possible are a key location factor for small businesses in particular. Doing away with superfluous red tape will remain an ongoing task,” as she argues. Such steps have done much to bolster Germany’s economic competitiveness – and if Chancellor Merkel has her way, it will also help reposition her as the champion of Europe’s competitive reawakening. For tax directors looking to gain a more valued role in the business, they should be looking to grab the opportunity too.

Corporate tax rates

Companies operating in the EU currently have to deal with 27 different national tax systems. In 2012, the average corporate tax rate among the 27 Member States was 23.5%.

<table>
<thead>
<tr>
<th>Country</th>
<th>Standard corporate income tax rate</th>
<th>Nominal corporate tax burden</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>15%</td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>34.43%</td>
<td></td>
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</tbody>
</table>

Sources: Eurostat; Federal Ministry of Finance, Germany

2013

The year that a range of tax measures will come into effect in Germany. For example, under the 2013 annual tax act, statutory retention periods applicable to tax records have been reduced from 10 to 8 years, dropping further to 7 years in 2015. Additionally, electronic financial reporting (e-reporting) will be launched, with special consideration for the small and midsize business community.
Balancing the global and the local

Tax directors have a clear remit to optimize the overall tax position of the global business. But accomplishing this requires close local collaboration. Marc Linnenbaum of Axpo reveals his approach. Interview by Bill Millar

Marc Linnenbaum
Marc Linnenbaum is both the Managing Director of Axpo International AG, the Luxembourg-based holding company and Head of International Tax for the Axpo Group. The Group has approximately 30 subsidiaries in total, including a range of independent power producers, energy trading companies, gas-fired plants and wind farms.

How do you define the role of a tax director?
Marc Linnenbaum: Overall, my role is to optimize the tax position of the group and to make certain we are tax compliant. This requires an overview of all operations and an understanding of the associated tax risks. And, most importantly, it is my role to ensure that we are a good corporate citizen, which means respecting the tax code and not being overly aggressive in our tax planning.

What are the most difficult aspects of the job?
Compliance is not without challenges, though relatively speaking, it is the easiest. But all the planning and structuring, that is very difficult. I would say the greatest challenge we face is working through the view of the group overall and local businesses. What might make sense for the group will not necessarily have the greatest appeal for the operations in each country, and it requires a significant effort to gain cooperation on such changes.

Another issue that is becoming much more challenging is the budget gap in so many European countries, which is driving tax authorities to become much more questioning with regard to cross border group transactions. They are in need of revenue and they are not shy about picking up operating and tax approaches in order to find it.

In tackling these issues, whom do you view as your key constituent?
I clearly work for the group benefit. I may work with the local business managers to get the job done, but my clear objective is to optimize the tax portfolio of the group overall. And so the tax function reports to the group CFO. He is my key constituent in all this.

How do you enlist the cooperation of local businesses in optimizing the global tax position?
You have to earn their respect. I believe one of the problems is that too many tax directors get caught up in being the one who is always saying ‘no’. They don’t get involved until the last moment, and that means the only thing left to say is that you can’t do it this way or that way.

This is why, within our group, tax is involved at a very early stage. Tax has the opportunity to actively work as a kind of a “sparring partner” with the business units to find a solution for all the identified tax issues and therefore create additional value to the project.

By getting involved fairly early on in the process, it was easier to help people be more effective in their tax planning.

What would you say to non-tax executives about their relationship with a tax director?
I would say that it pays to have a dialogue, as this can help avoid problems and expand opportunities. In my own role, it is my job to speak regularly with the local CFOs in our various operations. But I also stay in touch with the local business people as a way to help minimize surprises.

Can you give an example of such a surprise that might emerge?
The local business managers are entrepreneurial. Their goal is to find market opportunities. Expanding internationally means that besides all business related questions also tax has to analyze the situation which might include compliance topics as well as tax risk related issues such as e.g. VAT, withholding tax etc. All this needs to be checked ex ante to be sure that no hidden tax issues pop up when turning into operations.
To what extent do you assist subsidiaries in obtaining tax relief or cash grants?
The choices we undertake are driven by the business first; we are never driven by tax issues. But it is true that there is growing competition between jurisdictions and there are many programs to consider.

Today, when one of our business units has an idea, they develop what we call a “working paper” very early on. For example, this might be to expand a resource in one place, or build a wind park somewhere. This working paper is then run through our various departments, one of which is tax.

At this point I then get involved, reviewing the potential issues and probably working with an external advisor to get an update on what the best approach might be in a given country - what incentives or grants might be available and how to earn them. It is a way we can add value to a project, but it would never drive the project.

Another of the key issues you mention is the growing aggression from tax authorities in pursuit of revenue. How do you address this?
Our opening position is that we want to be a good corporate citizen. We want to pay the taxes in those countries where the profit is created. But, as with all international companies, it is not always so clear as to how much profit belongs where. So while we do try to optimize our tax position overall, we are never actively pushing the limits, but instead stick to accepted practices.

Could you give an example of where the rules on tax are not clear?
The OECD has published guidelines on implementing a management services concept. The idea is that central management services activities can be charged to the subsidiaries on an indirect basis (via indirect allocation keys), for example, as a percentage of turnover or perhaps the number of full time equivalents (personnel assigned to the defined task). But local authorities often will not accept these indirect charges, which means that they are tax deductible unless it can be supported by a benefit test which has to be performed on a single service approach. This indirect charging method versus a evidence on a direct approach is the problem. So there are the rules and the guidelines, but making them work in specific instances can require a lot more work in planning and operation.

What do you see as your greatest challenges going forward?
With Axpo, I believe our greatest challenge will be responding to the increasing audit activity of tax authorities, particularly in transfer pricing. Many jurisdictions are challenging transfer pricing schemes instead of the old fashioned tax audit topics as in this area of tax there it is not just white or black but in many cases grey. Generally, they are concluding that transfer pricing is the most vulnerable.

This is becoming more contentious. Ten years ago, you did not see much activity in this area. But now, nearly every country is developing detailed transfer pricing rules. As a consequence you must think through your approach clearly, justify what you do and be able to provide clear documentation.

It will be interesting to see how this all plays out. Jurisdictions can increase their enforcement or increase their tax rates. But when they do so, they will also see companies reacting, perhaps by moving their operations to another country. It’s a globally integrated economy and they cannot make their local changes without expecting a wider response.

Energy trading
Axpo is actively engaged in the trading of electricity on the international energy markets. The Axpo Group is Switzerland’s leading energy utility. It combines strong local roots with an international outlook.
Anna Elphick, The Vice-President Tax, Head of Plc and M&A at Unilever, Elphick, says the role of departments such as hers has been transformed during her years in the profession, with the tax function now expected to operate as a partner to the business.
A changing tax landscape opens new career doors

A higher profile for tax in the corporate hierarchy means that tax professionals can enjoy a broader career and benefit from higher remuneration.

By David Prosser

The role of the tax professional is changing. Just a few years ago, tax departments were primarily comprised of technicians who liked nothing better than burying themselves in a textbook. They inhabited a distant corner of the finance department and had few, if any, links with the broader business. Today, however, tax professionals are expected to be business partners who can forge excellent relationships with internal and external stakeholders, while also showing strong commercial instincts.

The journey from Clark Kent to Superman is ongoing for many tax professionals, but there is no doubt about the direction of travel. There is also no question that these changes are broadening the career options in tax - and encouraging the profession to recruit different types of people. “When I started out, tax was very much a numbers-based role and we were focused on getting our point across within the tax function,” says Anna Elphick, Vice-President Tax, Head of Plc and M&A at Unilever. “Now, there is so much more integration with almost every other function in the business. We are a hub for a great deal of activity and we’ve gone from being quite an introverted department to one that is expected to be a true business partner.”

There are a number of crucial trends that are driving this transformation. One is a growing awareness of the effect that tax policy can have on the bottom line, particularly as tax systems, both domestic and international, become more complex. Another is the impact of tax issues on so many diverse areas of companies’ operations - from tax incentives for research and development, say, to the tax treatment of employees working across borders.

It is not just internally that tax professionals have seen their profiles raised. In this age of austerity, tax authorities around the world are taking a much more proactive approach to raising revenue. For the most part, it is tax professionals who shoulder the burden of coping with these demands. Globalization is also having a major impact. Jane Djaté, Executive Director for Human Capital at Ernst & Young in Switzerland, advises leading companies around the world on performance and reward in many different functions, including tax. In a global business environment, she says, the most senior tax staff can no longer primarily be technicians - and nor should they be. “No tax director can be expected to be familiar with the detail of tax regimes in 100 different countries,” says Djaté. “Instead, we’re seeing the emergence of tax directors who are focused on process and risk management.”

The latter is especially important, for it is not just tax authorities that are becoming more inquisitive about companies’ tax affairs. Companies also face scrutiny of their tax arrangements from the media and special interest groups, and any perceived shortcomings can quickly cause serious reputational damage.

Elphick says that the challenge for tax directors and their teams today is to embed tax across the business. This ensures that the tax function has a clear view of the activities of every business unit while also being seen as an enabler of operations rather than an obstacle to commercial success.

“Tax can help drive change but it has to have a place at the table right from the beginning,” she explains. “And while your technical skills have to be the basis of the value you add, you’ve also got to be an articulate and tactful communicator. You can’t just impose your views on other departments, you have to explain how you can help.”

New experience required

Mark Pryor, the lead partner of Brewer Morris, the first recruitment consultant to specialize in tax, says that these developments have had a noticeable effect on the skills for which recruiters of tax professionals - both corporate and in private practice - are now looking. “Whenever I’m asked by a CFO to find a new head of tax, technical skill is probably now eighth out of 10 in the list of requirements,” says Pryor. “Higher up the list is the need for candidates to display leadership, understand risk management and be a strong commercial interface with the business.”

Summary

The changing nature of the tax function’s role should be welcomed by those who hope for a more varied career path. The options for tax professionals are growing by the day and salaries are rising too.
Ernst & Young

Focus

Career choice

Pryor thinks that many tax departments have more work to do if they are to realize the sort of ambitions expressed by Elphick. "Tax is already much more visible to the rest of the company and its staff is now forging much better relationships internally and externally," he says. "But more could be done by heads of tax to change the perception of how their departments can add value; this starts with how they put together business case for recruitment in a time of cost constraint – the all-singing and all-dancing tax departments are still in the minority."

There may also need to be an acceptance on the part of in-house tax teams that working life is going to become more demanding. Cornelius Grossmann, Ernst & Young’s EMEIA law leader based in Germany, argues that the old perception that in-house tax professionals have it easier than those working in private practice is no longer accurate. "In the past, it could be said that you would have a better work-life balance working in-house but, these days, the same pressures apply," says Grossmann.

Still, those who need a reason to speed up their modernization should recognize that, while boosting the role of tax is in the corporate interest, it is also in the selfish interests of tax professionals. The increased visibility of staff from the tax function and the broadening of their roles have not only made the day-to-day work more varied and challenging, but also boosted their career potential.

Good news for tax professionals

In many companies, senior tax staff now stands a much better chance of competing against others in finance – and elsewhere – for the most senior roles in the company than they did even five years ago. "Given the broader nature of the role, its higher profile and status, there are certainly now more opportunities to move beyond it," says Elphick. "But even if you stay within the tax function, the role is so much wider and more varied that it’s certainly no longer a silo."

There is more good news for tax professionals. Not only have their career options been transformed by the emergence from isolation of the tax function, but so too has their earning potential. Remuneration levels in the tax department have already begun to exceed those in other areas of finance.

There are several reasons for this. The most basic explanation is the dynamics of demand and supply – there are simply not enough qualified tax professionals to go round, says Brewer Morris’s Mark Pryor, particularly when compared with the supply of staff in mainstream finance. "As a result, tax professionals at virtually all grades can expect to earn 10% to 15% more than their peers in the finance department," says Pryor. "And there really has been a noticeable movement upwards in base salaries over the past two to three years, with increases over and above inflation across the sector – especially at newly qualified and head of tax level."

One might expect that demand and supply mismatch to level out, given the premium tax professionals are currently demanding. But the perception that tax is a more ambiguous area of accounting and finance, however misguided, appears to be working in favor of its professionals, with trainees less likely to take their careers in this direction for fear of specializing too early.

The exception to the rule that tax professionals lead on earnings, says Pryor, is at the most senior level, where a company’s tax director would typically earn less than, say, the account director or the group treasurer. Unusually, however, in-house tax professionals can generally expect to earn more than their peers in private practice. "From the newly qualified level up to senior management, total earnings tend to be higher in-house," adds Pryor. "In companies, the base salary might be slightly
higher, but that's the crucial component of the package, whereas in-house staff generally enjoys a much wider range of benefits, including bonus, car allowance and better pensions.”

Another factor driving salaries is that, in much of Europe, tax professionals are qualified lawyers. In countries such as Spain and France, every tax adviser is a lawyer while, in many other countries, a significant portion of the industry holds legal qualifications. Ernst & Young’s Cornelius Grossmann says that the Big Four tax and audit firms are now having to work hard to compete for the best people. “The top firms offer tax specialists very attractive packages and, if the Big Four do not offer similar deals to candidates, they will lose out,” says Grossmann. “The same is true for companies competing for staff to come and work in-house.”

That said, Grossmann identifies advantages that the Big Four accounting practices have when recruiting. Unlike most of the law firms, he points out, the large accounting firms are truly global businesses with networks of offices in many different countries across the world. They may be able to offer new staff a much more varied career path, with greater scope for working internationally than the law firms. This is due to the multi-disciplinary teams that work together within the Big Four.

It’s not just a matter of the absolute amount, of course – the structure of remuneration is important too. Here, the changing nature of the tax professional’s role, from technician to business partner, is driving a debate about reward. On the other hand, there are dangers in remunerating tax professionals in similar ways to staff on the frontline of operations. “In my view, remuneration in tax should be weighted toward fixed rather than variable pay,” says Djaté. “You don’t want to be incentivizing anyone in a control function to take unreasonable level of risk.”

A balancing act
A balance is difficult to achieve. Some measures might seem obvious key performance indicators (KPIs) for senior tax professionals - the company’s effective tax rate, or the value of its savings from good tax planning, for example. But if these measures were to encourage tax directors to be too aggressive, the damage caused by challenges from tax authorities, or embarrassment in the media, might be counterproductive. Therefore other KPIs are worth considering, adds Djaté.

“One possibility is the number of audits the company is subjected to by the tax authorities and the length of time it takes to conclude these.”

Brewer Morris’s Pryor says that, among his clients, bonus levels are definitely on the increase after a few disappointing years. For newly qualified tax professionals, 10% to 15% of salary is now typical, he says, while the most senior directors might expect bonus potential of 50% to 100% of base salary - or even multiples of it. Pryor too is aware of the dangers of incentives.

“Currently, tax professionals’ bonuses are determined in the classic way – 50% on corporate performance and 50% on individual targets,” he says. “What many people would like to see is a link between their bonus and how much tax they’ve saved the company.”

In the end, says Ray Harraway, a Director at the Human Capital, Performance and Reward Group at Ernst & Young in South Africa, the challenge is to build remuneration packages that reward the sort of tax professionals employers want. “We need new KPIs for these people,” says Harraway. “We’ve seen the role of the tax director move from the supportive to requiring a broader understanding of risk management and how that is integrated into the risk management programe of the whole company. That does require new skills, particularly in the areas of relationship building and commercial awareness.”

Case study
Hans van Hout, Corporate Director Tax, FrieslandCampina

__Hans van Hout has been corporate director tax at FrieslandCampina since the formation of the company, one of the world’s largest dairy companies, following a merger of two smaller cooperatives in 2008. FrieslandCampina has operations across Europe and the Middle East, as well as growing business in Asia.

Van Hout says his role today is far broader than the equivalent job would have been, say, a decade ago. “Internal tax professionals used to be technical advisers on technical issues,” he says. “The only instruction from the Chief Financial Officer was that he didn’t want any surprises.”

The contrast with today could not be more marked, he says, with the increasing importance of the tax function having been driven by developments such as the IFRS accounting regulations, the introduction of corporate governance codes and, at certain companies, the Sarbanes-Oxley legislation in the US. “Internal stakeholders have become much more aware that tax is more than just a technical issue,” says van Hout. “What we see now is that tax structures are an integral part of the business, at the very foundation of how we operate.”

Getting to that stage has required persistence and determination. At FrieslandCampina, van Hout’s team, while remaining ultimately accountable for tax policy, has sought to devolve responsibilities to business units, working to instill sensible risk management practices in each area.

Sometimes there is a need to be resolute, van Hout adds. “I’m not primarily here to decide what we do as far as tax is concerned,” he says. But that doesn’t have to mean confrontation with the business units. “The skill is to be able to communicate effectively with people who do not have a background in tax,” he says. “What I stress to my team is that we must explain the consequences of a particular scenario and seek to provide an alternative, rather than prohibit the business from operating.”

Get it right and this approach makes for a much more fulfilling role professionally, van Hout says. “People who join my team from advisory backgrounds often say they have had their eyes opened,” he explains. “Our integration and alignment with the business is now so developed that they are really at the centre of our commercial activity. Business is now so developed that they are really at the center of our commercial activity.”
Companies are facing increased scrutiny in how they handle their tax affairs, as part of a wider push for greater tax transparency and fairness. Getting it wrong can put an otherwise excellent brand at risk and associate its management and products with tax evasion.

1929

In 1929, a famous quote from Lord James Avon Clyde, then the UK's Lord Justice General, stated that “no man in this country is under the least obligation... so as to arrange his legal relations to his business or to his property as to enable the Inland Revenue to put the largest possible shovel into his store.”
By Gerry Chanel

Whether it’s protests outside retail stores in the UK, Swedish television accusing seven large multinationals headquartered there of unacceptable practices, or prominent critical articles in international financial papers, multinational companies have been subject to a lot of criticism lately. But the issue for each of these companies was not child labor, unacceptable working conditions or poor environmental practices – the typical concerns that usually give rise to reputational risk. Rather, they were based on concerns about the tax affairs of these companies. Companies today face unprecedented disclosure requirements by tax authorities, while audits are more frequent and aggressive. All this is creating the ripest environment for tax controversy in years. More rigorous financial statement disclosures around tax are on the rise too. And now, from one country to another, there is increasing public debate about corporate tax avoidance and the boundaries of acceptable tax behavior. As these pressures continue to rise, so does the issue of tax reputational risk on the corporate agenda. The intense scrutiny, even when unwarranted or inaccurate, can hurt brand reputation and – potentially – shareholder value.

Tax activism on the rise

Even after the international push for tax-related transparency, triggered by the 2002 Sarbanes-Oxley Act, the public at large expressed relatively little interest in tax disclosures. However, the austere economic environment and sweeping public sector cuts in many countries have generated new interest in corporate tax information. This has been led by journalists, as well as activist groups, angered over reductions in government services, both of whom want companies to “pay their fair share.” Their approach is aided by technology, such as Twitter and other social media platforms, which gives anyone a platform for promoting a new cause. These parties are scrutinizing corporate reports and other information sources for news of tax controversies and are spotlighting low effective tax rates, or overly aggressive tax planning activities. Pierre Jansson, Vice President of Taxes at Sandvik AB, a global technology and engineering group headquartered in Sweden, says: “Our first quarter this year was our best quarter ever,” he says, “but the questions about the quarter were not about the business, they were about our tax planning.”

Media claims often reach inaccurate or misleading conclusions that ignore permissible, straightforward activities, such as deliberately enacted tax incentives or government approved transactions. “The facts cited in these stories are often incorrect,” explains Monique van Herksen, Ernst & Young’s EMEIA Tax Controversy leader. And the problem with handling the issue is often that the charge that challenges your reputation is merely a one-liner, but the explanation or correction takes far longer to express. It doesn’t meet the media’s ‘elevator test.’ It becomes necessary to have another set of one-liners back to whomever made the charge in order to survive the issue, and that can be difficult to do.”

In Vodafone’s case, a media report claimed that the company paid just £1.25b to settle a UK tax bill in 2010 that was allegedly as much as £8b, triggering nationwide protests by a watchdog group calling the company a “tax dodger.” The UK authorities called the £8b figure an “urban myth” and said the settlement of the

Companies face unprecedented disclosure requirements by tax authorities today

In Vodafone’s case, a media report claimed that the company paid just £1.25b to settle a UK tax bill in 2010 that was allegedly as much as £8b, triggering nationwide protests by a watchdog group calling the company a “tax dodger.” The UK authorities called the £8b figure an “urban myth” and said the settlement of the
Focus / Tax transparency /

to tax planning. They take the position that a company with operations in a particular country should pay “adequate” tax revenues in return for using the resources and infrastructure of that country, explains Albert Lee, leader of Ernst & Young’s EMEIA Tax Performance Advisory team.

Pressure remains

The idea of country-by-country tax payment reporting was considered by the OECD in 2010, though it later backed off the proposal, but the European Commission has now presented a package of disclosure measures that would apply to public and private companies active in the oil, gas, mining and logging sectors. But pressure remains. A recent survey from Transparency International reviewed the world’s 105 biggest listed firms and measured, among other things, whether they publish detailed financial information about their activities in every country where they operate, including how much they pay in taxes.

Such activist groups are not alone. Tax authorities around the world have also increased measures for tax transparency, even as they simultaneously increase enforcement. Some measures require disclosure of uncertain or aggressive positions on tax returns, but certain countries are going far beyond mere reporting requirements. “In the UK and Australia,” says van Herksen, “the heads of the revenue authorities are asking the leaders of large multinationals, one-on-one, to explain why they think they are paying their fair share of taxes.”

Based on these conversations, the tax authorities are developing risk ratings that affect the audit approaches of these companies.

Another risk of tax reputational damage arises from a lack of visibility over a company’s local subsidiaries, says Steve Schultz, Global Director for Global Compliance & Reporting Services at Ernst & Young. “As companies revisit their finance operating models, standardize these, and move to shared service centers and business process outsourcers, there tends to be less local tax competency. This comes at a time when local expertise and relationships with tax authorities have never been more important for managing tax risk.”

So how can companies respond to all this? Van Herksen argues that compliance is the first place to gain ground over reputational risk, “and then managing that compliance in such a way that you have effective processes and controls and an effective dashboard of information on where your potential exposures lie. In those places, it is important to know what potential dispute resolution mechanisms exist.”

Tax audit resolution should also take reputational risk into account. “Audit settlement discussions and resolutions used to be relatively private matters between the tax authorities and the taxpayer,” says Kealy. “Today, it is essential to consider the possible reputational impact if audit settlement details were to end up in the news media, and to keep in mind that there is interest in financial statement disclosures about years under audit and material issues.”

Such considerations go beyond the tax director alone. Indeed, managing tax reputational risk is a C-suite and board level concern, since it is here that the business’ policies for tax risk and tax controversies should be established. Tax planning should be lined up with those policies and with the corporate message to the community at large, all of which should be assessed in light of how the public and the revenue authorities may perceive it.

At Sandvik, says Jansson, high level tax strategy is decided by the board. The company also does tax planning in a very structured way. For example, he says, the company has a process for evaluating whether specific tax planning activities align with the company’s established strategy. “Reputation is an important area to evaluate, as well as commerciality, to be sure that tax planning has a business purpose. Planning activities also require advice from general counsel and from our financial controller, decision approval levels are very clear and specific sign-offs are needed. And the tax director needs to be a business partner, able to explain difficult issues in a non-technical way so that others who should be involved will understand what you are doing.”

Managing tax reputational risk is clearly a C-suite and board level concern

Reputation management in a real-time world

Overall, the tax director needs a clear grasp of the firm’s risk appetite, has to ensure transparent reporting on this internally, and must help establish clear processes and protocols for flagging and managing risks. “You never know when somebody is watching what you do in today’s environment,” says Kealy. “Whatever decisions a company makes should take into account the fact that somebody will have full knowledge of them, that you’ll be second-guessed on them, and that commentary – whether in the correct context or not – can be shared quickly.”

Tax reputation risk is yet another pressure and managing it involves more robust, regular interaction between tax executives, their boards and audit committees. But the upside is that this also helps make a more resilient company.
By Bill Millar

A transparently conservative approach

Trust matters
TD Bank believes its focus on transparency has strengthened its relationship with the authorities and enhanced its credibility.

Peter van Dijk
Senior Vice-President for Taxation at Toronto-based TD Bank Group

__ The idea of maximizing profit suggests that companies should seek to operate their businesses as tax-efficiently as possible. But when it comes to doing so, there is rarely a definitive answer as to what that means. It is for such reasons, says Peter van Dijk, Senior Vice-President for Taxation at Toronto-based TD Bank Group, that acceptable tax planning and the degree of tax risk a company is willing to accept are issues for the board and CEO. “Risk is relative,” says van Dijk. “What might be too risky for some will be acceptable for others.”

For its part, TD has a conservative risk appetite, choosing to compete on the quality of its customer service and its retail-based business model as opposed to potential financial returns generated through riskier, more opaque investment strategies. The firm pursues a similarly conservative approach to tax planning.

This includes a commitment to transparency, with the bank providing more information to the tax authorities than is strictly required by law, according to van Dijk. TD was in fact one of the first to sign on to the UK’s Code of Conduct for Taxation and is also entering into the Compliance Assurance Program (CAP) in the United States, both of which promote openness and transparency. In addition, the bank organizes business awareness sessions with the largest revenue agencies, such as the Canada Revenue Agency and the US Internal Revenue Service.

“These sessions help tax authorities get a clearer picture of TD’s businesses and what is driving our effective tax rate,” says van Dijk.

TD could, of course, be more aggressive in its tax planning. But in the tax director’s view, any potential rewards are outweighed by the risks. “If you lose trust with the tax authorities, then other regulators will begin to wonder where else the company is pushing itself to the limits,” says van Dijk. “And that is something we just won’t risk.”

This is not to say that van Dijk believes that today’s level of corporate taxation is ideal. “Taxes on businesses are passed on throughout the economy,” he says. “This translates into higher prices, less competitive businesses, lower investment returns and slower job growth.”

These are messages that van Dijk says his firm is comfortable sharing with legislators in not only Ottawa and Washington, D.C., but also London. In his view, there needs to be a healthy public debate about taxation systems and levels and their relative strengths and challenges.

“If today’s corporate tax rates were lowered, both economic activity and total tax revenue would increase,” he argues. “In the meantime, however, we as a bank will maintain high levels of transparency and avoid risks that could damage our reputation.”

Trust matters
TD Bank believes its focus on transparency has strengthened its relationship with the authorities and enhanced its credibility.
By Nigel Gibson

As globalization gathers pace, it is not just business managers who must become mobile as their firms embrace new markets. The professionals who manage a firm’s tax affairs should do so too. This does not mean spending a few months in a haven by the sea. Often, it involves tax professionals joining their colleagues on the front line as companies expand their businesses around the globe.

More complex global corporate structures have been an important driver of this trend. “At one time, tax professionals remained close to the Chief Financial Officer,” says Kevin Cornelius, Head of Human Capital Switzerland and global responsible for Ernst & Young’s HR advisory in Tax Effective Supply Chains. “Now, because of globalization and the risks associated with it, they need to be closer to the business itself.”

Procter & Gamble (P&G), the consumer products company, provides one illustration of this change. At the last count, the company had operations in no fewer than 80 countries, selling household brands to 4.4b customers worldwide. These days, says Tadd Fowler, one of P&G’s Vice-Presidents for Global Tax, the company’s tax professionals no longer spend their time pondering complex rules at head office. Instead, many now work alongside their colleagues managing businesses. “One of the more important developments in policy around the world is the concept of enhanced transparency between taxpayers and governments,” he says. “As a result, we need people who can articulate in an understandable way our business model and its associated tax issues.”

This more frontline role for tax professionals demands strong communication skills, along with the expected technical and business knowledge. “Tax professionals increasingly need to interact with a range of different stakeholders, and that means that we need to train our people accordingly,” says Fowler. “This is particularly important as our business continues to grow its global footprint and we become significant taxpayers in more and more countries.”

Managing new risks

Globalization is not the only force at work. In addition, companies must become accustomed
Tadd Fowler

A Vice-President for Global Tax at Procter & Gamble, Fowler says many of the company's tax professionals are to be found all over the world working alongside their colleagues managing businesses.
to an environment in which tax policy is evolving rapidly, and in which governments are demanding significant levels of transparency and disclosure on tax affairs. These changes have an impact on the skills that tax professionals require, and the structure of tax departments themselves.

In the past, many tax professionals were trained as broad-based, technical generalists: They knew a little about a lot of things. These days, the complexity of tax policy requires more specialization - whether in transfer pricing, indirect taxation, mergers and acquisitions or other areas. At the same time, demands for transparency and increased coordination between tax administrations mean that companies must also adopt a global approach to managing their tax profile.

Unsurprisingly, says Cornelius, the hazards to which firms are exposed increase as governments, during a period of austerity, become more assertive in their demands. Since governments now exchange more information about tax than ever before, companies must have a global picture; and the quality of the advice they receive must be international too.

Leading the way
This closer engagement with the business means that tax departments must adapt themselves to be aligned with the broader corporate goals of the organization. “As a company’s sales grow, so the support it receives from tax professionals and others must evolve too,” says Cornelius. “For example, a Brazilian company operating in Europe may have tax professionals in Switzerland.”

It is also important, says Fowler of P&G, that the business determines the structure of the tax department, not the other way round. This has an impact on the career of tax professionals, who must increasingly gain knowledge across a wide variety of different regions and functions in order to perform their role effectively. “It is in the interests of the individual as well as the company to give tax professionals as wide a range of technical, business and organizational experience as we can,” he says. “If, and when, they become a leader within the company, such individuals will have a range of experience to draw on in their leadership roles.”

Broader experience can come from a number of different dimensions. First, tax professionals can be given secondments in another geographical market. This exposes them to a different tax environment, and enables them to develop their communication skills and ability to assimilate different cultural and business practices. This broader knowledge can help them greatly as they make the transition to senior management roles.

There are barriers to mobility that need to be considered, however. Not all employees will be at an appropriate stage in their life to consider a move overseas. They may have young families or spouses with successful jobs, and companies must be sensitive to these personal circumstances when putting in place mobility plans. In addition, senior management may be reluctant to see key employees move to another location, particularly at a time when many companies have already reduced headcount. Overcoming this barrier requires strong leadership from the top, and the ability to persuade managers that mobility is good for the company as a whole in the long term.

Second, tax professionals can be moved to different specialties. And, in some cases, tax professionals may move outside of the tax department altogether, at least temporarily. “It is more than just geography,” says Tadd Fowler. “We consider the roles and skills of individuals,
both managerial and technical. So, if we move them from one country to another, they benefit from learning new technical skills as well as working in a different economy. We also have tax professionals who, for a time, are involved in helping to run parts of the business.”

As well as moving tax professionals to new markets or roles, companies need to consider how to build a better understanding of tax issues among the broader business. “It is not just tax professionals who need to pick up new skills,” says Fowler. “Employees involved in finance and accounting, or in the broader business, should also be trained to understand tax, so that they can apply this knowledge in their day-to-day roles.”

The biggest opportunities
Deploying tax professionals around the world is a complex exercise in resource allocation. In the past, much of the talent resided at head of the Second World War enabled P&G to hugely increase its output and speed up its growth.

Deploying tax professionals around the world is a complex exercise in resource allocation. In the past, much of the talent resided at head of the Second World War enabled P&G to hugely increase its output and speed up its growth.

Simon Burke, Group Tax Director of Legal & General, on the shifts within his company’s tax function

A change of focus

Compliance across all taxes is now far more important than analyzing potential opportunities to optimize tax. Accordingly, I have been recruiting more accountants and fewer tax specialists. The type of work they do, and the experience they gain, is now quite similar to the people in the financial reporting and financial control teams. This change is happening quickly and is coming as something of a surprise to people from a traditional tax background.

By far the biggest tax contributions to the UK Exchequer are income tax and National Insurance contributions, which together account for nearly half the UK’s total tax receipts. Financial services industry is a big employer and contributed over 12% of the UK’s total payments of Pay As You Earn income tax. In addition, financial services companies are responsible for significant amounts of income tax withheld from payments such as interest and annuities. Our tax teams have tended to focus on corporation tax, whether UK or overseas, but have often had little involvement with operational taxes. Due to initiatives such as the Senior Accounting Officer (SAO) regime, which requires an SAO to sign off on a company’s tax accounting arrangements, this is changing. HMRC, the Government’s revenue and customs office, asks more about the quality of the data used in operational taxes and we need to improve our understanding accordingly. So we have steadily downsized the central tax team, but increased the presence of tax professionals in business areas.

There is certainly additional cost associated with the extra emphasis placed on managing tax risk. However, in net terms, we see significant cost reductions. Professional fees are lower and staff costs are reducing as, gradually, tax technical people are replaced by those more orientated toward process. At Legal & General, I have been focused on retaining our best tax technical people within the Group: Two of my former direct reports are now in non-tax roles and doing very well. It is a great morale booster for the tax team to see that the skills and knowledge we develop as tax professionals are truly portable. There is a latent pool of talent across British industry in the form of tax people, more and more of whom, I believe, will migrate into other technical specialisms or wider managerial roles.

Simon Burke, Group Tax Director of Legal & General, on the shifts within his company’s tax function
What do you enjoy about your job?
The best thing is dealing with people - everything I do for my clients and for the firm is about people.

What will be a big challenge for tax directors in the future?
Tax authorities are fast becoming more sophisticated and so tax directors will find it challenging to anticipate changes and adapt their companies.

What is the most important character trait to have as a tax director?
I think it’s confidence, because the tax director needs to feel on an equal footing with all other executives.

Carolyn Libretti
Tax Partner
Rio de Janeiro, Brazil

YTPY 2011 jury member
The people in tax

The working lives of tax professionals at all levels have changed significantly in the past 20 years. As a result, a new set of character traits and attitudes has become as important to success as the technical skills that defined the roles in the past.

Tax talent
The annual Young Tax Professional of the Year (YTPY) award, hosted by Ernst & Young and judged by an expert panel from organizations, regulators and academic institutions across the globe, seeks to profile tax as a career in an increasingly competitive marketplace. This competition allows successful students from more than 20 countries to participate and demonstrate their tax technical and professional skills.

By Stephen Edwards

What does it take to be a top tax director today? Some 20 years ago, common answers may have included technical knowledge, attention to detail and a head for numbers. And while those attributes are still fundamental, contemporary responses are markedly different.

Claire Goudet, Tax Corporate Law and Customs Director at Yves Rocher, a global cosmetics firm, for example, explains that “it is difficult to become, and more difficult again to stay, a tax professional without passion.”

While Asmita Paranjpe, an intern in Tax and Regulatory Services at Ernst & Young in Pune, India, believes curiosity is key: “The thing about tax is that the more curious you are, and the more you decide to learn, the more you end up liking what you do, and the better you get at it.” And with tax directors now more involved in business strategy, Carolyn Libretti, Tax Partner at Ernst & Young in Rio de Janeiro, Brazil, says that confidence is now a vital characteristic for an effective tax director: “They must approach their colleagues as business peers. Even though they have a technical role, they need to have the confidence to put forward their ideas on an equal footing.”

Passion, curiosity, confidence – perhaps hardly the markers of tax directors of yesteryear, but these traits are now needed to deal with a fast-evolving mandate. Ms. Goudet, who has been with Yves Rocher for 16 years, has seen firsthand how the skill-set required to be a tax director has changed over the last two decades. “When I started, we just had to know – and perfectly know – the tax law,” she explains. “Now we have to have a global view; we must perfectly understand how the business runs, propose new ideas and be a true business partner.”

And, of course, it's not only the roles of tax professionals that are changing faster than ever, so are the rules. Recent years have seen a bewildering volume of amendments to national and international tax regulations. It’s fortunate then that a fast-changing landscape is actually attractive to some tax professionals. “The subject is moving,” says Viviane Boissard, a fifth-year tax law student at Dauphine University in Paris; “It’s never the same each year and I like that. It’s more challenging because you need to be updated each day.” Ms. Paranjpe shares this same attraction to the “unpredictable nature” of her job, as does Ms. Goudet, who enjoys the fact that “nothing is defined to be fixed, everything is moving each year.”

This constant flux is one thing that many – no doubt lacking in the right kind of passion for the job – would most dislike about a tax career, particularly in today’s environment. In fact, such demands also prepare tax professionals for a wider range of careers.

Meanwhile, what is often underreported, is that these same forces of change are having a dramatic impact on working life for people on the other side of the fence. Jean-Pierre Lieb, Inspector General of Finance at France’s Department of Taxation, says that companies are now more open with tax authorities about their impending transactions. “They know that the fiscal landscape or the tax landscape is more complex,” he explains. “It’s more difficult for them to choose the right path to reach their objective.” What this means for Mr. Lieb’s department is much more work. “People are coming to see us to ask for rulings before doing things, so in five years we increased the number of our rulings from around 3,000 to over 22,000 rulings each year. It’s very demanding on our resources, because on each transaction we will spend quite a lot of time and companies have a very short period of time. We have to be quick.”

To meet the challenge, Mr. Lieb shares the same enthusiasm for, and interest in, his work that both seasoned tax professionals and bright young students identify as a new hallmark of today’s best tax directors.
What do you enjoy about your studies?
I enjoy having a challenging problem to solve or when having a point of law to research.

What will be a big challenge for tax professionals in the future?
These days, there are more and more changes in tax law so, for students, the challenge is to enter a system that is always changing.

What is the most important character trait to have as a tax professional?
I guess to be interested and curious, and to not simply give general advice but advice that is best suited to every client situation.

Viviane Boissard
Tax Law Student
Paris, France

YTPY 2012 finalist
What do you enjoy about your job?
So many things: the intellectual challenge, the diversity of issues, the high level of professional involvement and working with my high-performing teams.

What will be a big challenge for tax professionals in the future?
It will be a challenge to implement innovative tax planning while improving trust and confidence with tax authorities.

What is the most important character trait to have as a tax professional?
To be able to see - and balance - both the big picture and the technical details.
What do you enjoy about your job?
The main thing is that nothing is defined, everything is moving each year, so we create things and learn every day - I enjoy that.

What will be a big challenge for tax directors in the future?
To keep our independence while working closely with the business, and also to learn to act in a more globalized environment.

What is the most important character trait to have as a tax director?
To have a love of discovery because you have to be aware about what’s happening in business; to be curious.
What do you enjoy about your job?
The unpredictability of the job - the permutations are so vast, it's so big, that you never know what you're going to do the next day.

What will be a big challenge for tax professionals in the future?
To continue to convince other parts of the business that tax is more than just a cost you have to bear, that it should be part of business strategy.

What is the most important character trait to have as a tax professional?
You need to be passionate about it and interested in knowing more.

Asmita Paranjpe
Tax Intern
Pune, India

YTPY 2011 winner
Performance management is a relatively new concept for many tax departments, and a broad range of quantitative and qualitative yardsticks is still being fully developed. So what should these indicators look like?

By Fergal Byrne

Until recently, managing the performance of the tax department was rarely a top priority for CFOs and other members of the management team. Tax was seen as a necessary cost of doing business, but not something that required close scrutiny. Over the past few years, however, all that has changed. Tax directors face ever-tighter regulations and accounting standards. Meanwhile, corporate tax affairs are under greater scrutiny and enforcement from tax authorities and other stakeholders. As a result, the pressure for tax departments to perform, while at the same time managing risks and remaining accountable, is greater than ever.

Historically, many companies used their effective tax rate as the key measure of performance for the tax function. The advantage of this approach is that the effective tax rate is tangible, easy to measure and can be a good reflection of the effectiveness of a company’s tax planning. But the effective tax rate also has its drawbacks as a metric. For one, the overall level of the effective tax rate can depend on other factors, such as the company’s business model, that are outside of the tax department’s control. Perhaps, more importantly, there is also a danger that a reliance on the effective tax rate can distort the risk profile of the tax function. “Focusing on the effective tax rate tends to be one-way thinking,” says Todd Tuckner, Chief Operating Officer for UBS’s global finance function, including the UBS tax department, which he functionally ran until his promotion earlier this year. “You can certainly reduce your effective tax rate in the short term but, very often, that leads to poorly priced long-term risks.”

A bigger issue is that tax planning is only one part of what the tax function does. Tax
Todd Tuckner
Chief Operating Officer for UBS’s global finance function, including the UBS tax department, Tuckner warns that a narrow focus on the effective tax rate of a business can create problems over the longer term.
UBS draws on its 150-year heritage to serve private, institutional and corporate clients worldwide, as well as retail clients in Switzerland. Headquartered in Zurich and Basel, UBS has offices in more than 50 countries and employs approximately 63,500 people.

Management / Measuring performance /

departments also need to be measured according to their performance in a host of other areas, including indirect taxes, transfer pricing, the efficiency of their processes and their interaction with the business. In some of these areas, there are fewer benchmarks in place for tax function performance.

Martin Rabenort, Ernst & Young’s Tax Performance Advisory leader of Belgium and the Netherlands, believes that there has been a gradual shift away from a reliance on effective tax rate within many companies. “Things are changing slowly,” he says. “Companies are gradually embracing a broader set of metrics that reflect the different roles of the tax function. These might encompass compliance, risk management, supporting the business, tax reporting and, in some cases, tax policy and tax lobbying.”

Despite this shift, Rabenort says that many companies still tend to rely on a generic set of key performance indicators (KPIs) that can be easily measured and achieved. This might include indicators such as the timely filing of tax returns. “These generic KPIs are all about the baseline level of performance for a tax function,” he says. “They do not challenge a tax function to be as good as it can be, so are not that useful when used for performance measurement and management purposes.”

Tuckner of UBS agrees that these more basic measures do little to motivate or incentivize top performance in a tax function. “I think there is only so much you can achieve with measures such as timely and accurate submission of returns and measures of fines and penalties,” he says. “For the biggest organizations in the world, those aren’t really concerns because you hire quality people and so the KPIs around those measures tend to be less instructive.”

Forward-looking indicators

Ambiguous metrics are another problem for many companies. “Vague KPIs, usually based on poorly defined objectives and weak leadership, are useless,” says Rabenort. He advises that companies should instead devise a set of metrics that enable historical performance to be measured alongside more proactive indicators. “Backward-looking metrics tend to be the most prevalent, but they don’t work so well for managing the tax function,” says Rabenort. “You need a ‘red flag’ at the moment where you can still change behavior. Using forward-looking indicators allows for a more fluid situation where you can adapt and respond accordingly.”

Perhaps the biggest danger of all is that companies rely upon simple measurable targets that do not tie in with the higher-level strategic role of the tax function. Tax departments therefore need to develop individual KPIs that are linked to strategic objectives, yet responsive to the different dimensions of the tax service provision. In other words, the metrics chosen should be based on the context of the business. “You would have a very different set of KPIs in a business where there are ambitious objectives but poor processes and limited resources, compared with a situation where you have the same objectives but smooth processes and a clear governance model,” says Rabenort. “The context needs to be taken into account so that you can reward the behavior you are seeking to create.”

The qualitative approach

Tuckner emphasizes the importance of a qualitative approach to performance management. This might include measures relating to the relationship between the company and the tax authorities. “You probably can’t measure it necessarily in each exchange with the administration but, over time, you can keep an eye on soft factors like the relationship with tax authorities, and how transparent the tax department is in its dealings with regulators, tax authorities and even the public,” says Tuckner. Developing the right qualitative measures requires a strong mutual understanding between the tax department and executive management. “It’s important that the tax managers can articulate the tax strategy and the way they look at things,” he says. “Otherwise, it is difficult for management to know how to measure the department. UBS has, for example, published a code of practice for tax and we’ve shared that within the organization. We also share that with tax authorities because that’s what we stand for.”

Exposure to senior management also helps. Tuckner, for example, regularly presents to the audit committee on a variety of different issues, which provides him with the opportunity to bring tax into the boardroom. “I think that has helped us enormously to review and manage the performance of the tax function,” he says. “The more you can communicate the strategy of tax and the issues that it is dealing with to senior management, the better.”

Looking forward, Tuckner believes that the qualitative approach will become more important as the tax department assumes a greater advisory- and relationship-oriented role. Greater use of shared service centers and outsourcing will accelerate this shift because the more basic activities, such as filing tax returns, will be handled outside the tax department. “As companies seek to locate all the processing-related activities they can in lower-cost jurisdictions, the more commoditized metrics around efficiency and timeliness will become less relevant for the core tax department,” he says. “At that point, it is the more qualitative, strategic metrics that will matter more.”

Indirect taxes and the shadow tax function

The so-called shadow tax function, which refers to functions outside the tax department that get involved in tax matters, presents a particular
ERP systems and indirect tax compliance

Value added tax (VAT) is a transactional tax with complex local country compliance requirements. Correct enterprise resource planning (ERP) system configuration is essential to ensure that large-scale errors are not present for the company in both the charging of VAT to customers, the production of VAT-relevant documentation and the reporting of VAT-relevant information.

The areas that companies will need to consider from a VAT perspective when implementing an ERP system are: tax-relevant master data, tax condition rules, tax codes, invoicing and documentation, reporting.

For the financial year 2011 UBS reported a net profit attributable to shareholders of CHF4.2b (about €5.04b).

more balanced and aligned with the tax function’s roles and responsibilities. It will focus on the areas that can be genuinely influenced by the tax function rather than taking the effective tax rate as a given. “I think the tax function will become more responsible for the overall global position of all taxes, including indirect taxes,” he explains.

Role for internal audit

Internal audit can play an important role in helping with performance management, in line with the “three lines of defense” approach to risk management. According to this model, the tax function is the first line of defense for the business, the second is the risk organization, and the third line is internal audit, which provides an independent perspective.

“Internal audit can be particularly helpful when it comes to doing reviews in remote locations, acting almost as an extension of the tax department,” says Rabenort. “Also, internal audit can help to identify situations that could be done better by other people than the tax department.”

At UBS, internal audit’s role is focused primarily on processes such as tax accounting and transfer pricing. “These are complex processes that are easier to measure and evaluate quantitatively than, say, providing a business with high-level consulting on a transaction,” says Tuckner. “In that situation, it’s less about process and more about the advisory.”

As the role of the tax department evolves, the management of its performance needs to change accordingly. By ensuring that it has the right metrics in place to guide behavior, companies will be able to accelerate this evolution and ensure that they have a tax department that is fit for the future, rather than focused on the past.

challenge when it comes to performance measurement. As the tax department has no real say over what the shadow tax function is doing, it is difficult to pinpoint the root of any underperformance. Moreover, it is often something that lies outside the control of the core tax team.

Consider indirect tax as an example. This is an increasingly attractive source of tax revenue for many governments and yet the handling of indirect tax may be carried out in many areas of the business, including finance or accounts payable. “Indirect taxes tend to be highly automated and embedded in the ERP system,” says Rabenort. “Tax returns are usually prepared by people in finance, or in an administrative function, who do not have a lot of know-how about the VAT laws and regulations.”

He advises that companies need to take more control of the shadow tax function. One effective approach is where the shadow tax function has a dotted-line (or indirect) reporting relationship into the head of tax, accompanied by an escalation model. “The escalation model allows the tax leadership to get the commitment and endorsement of the CFO to approach the local finance team to make sure that they are giving tax the right priority and doing what is necessary from a group perspective,” says Rabenort.

The tax function can help by providing coaching, training and guidance to the shadow tax function. It can also prepare manuals so that there is a framework for teams outside the tax department to operate effectively. This means that, when they see something strange, they can flag it and prevent risks rather than mechanically creating problems for the tax department to address later.

Rabenort believes that, over time, the metrics used to evaluate the tax function will become
Andreas Lindner

The Group CFO at Swiss manufacturer Ricola, Lindner argues that executives in his position have no choice but to take a much more active role in the tax function and that tax professionals will need to work out how to facilitate this.
My CFO has needs

The need for greater efficiency is altering the structure and operation of the typical finance function. These forces demand closer collaboration between the CFO and the tax director.

By Bill Millar

In the past, tax was almost an afterthought for many companies. They would typically devise strategies, execute them and then figure out the tax consequences afterwards. Today, however, tax is so much more visible and material that most companies involve the function at a much earlier stage in the process. And that means that CFOs and tax directors must work together more closely than ever.

Tax to the fore
Andreas Lindner, group CFO at the Swiss manufacturer of herbal cough drops and teas, Ricola, points to several key drivers to explain this shift in perspective. First, he says that governments all over the world are stepping up efforts to increase their tax revenues. “They are looking much more closely at business operations and they are very focused on identifying taxable activities and growing the tax base,” he says.

As tax administrations peer more deeply into corporate operations, there is greater potential for disputes to arise regarding which jurisdiction is entitled to the tax from particular activities. Consequently, cross-border transactions between related corporate entities – transfer pricing – is becoming an increased source of contention. “This is becoming a critical focus area and one that requires senior management attention as well as robust elaboration and documentation of policies,” says Lindner.

Globalization is also driving greater complexity in tax affairs, particularly for companies such as Ricola that are accelerating their international expansion to currently over 55 countries. “We now have more affiliates operating in more countries and offering a wider range of products than ever before,” says Andreas Lindner. “Tax is now much more important, more visible and more demanding - and it all means that the CFO has to be more proactive and more immersed in this area.”

For CFOs to become more proactive in tax, they will need the support of the tax department. Here, says Martin Holyoake of the Advisory practice at Ernst & Young in the UK, tax directors must rise to these new challenges. “The basic compliance role for tax functions will never go away,” he says. “But there also has to be a major shift toward a more transformational, entrepreneurial role for tax directors. They need to step up and provide the CFO with all the strategic insight and support necessary to optimize the tax footprint.”

This is easier said than done, particularly as, from the perspective of the tax director, the needs of the CFO can sometimes appear to be in conflict. On the other hand, finance leaders want a lower effective tax rate, or one that at least compares favorably with the company’s peers. CFOs also want to minimize the risks associated with tax. They want returns to be filed on time, transfer pricing documentation to be complete and up-to-date and, above all, to prevent the risk of controversy or adverse publicity for aggressive tax planning. “Companies don’t want to pay more tax than they need to, but they also want to appear to be a corporation that is doing its best for society,” says Holyoake.

A shared services model
Another CFO imperative, particularly in today’s broadly anemic global economy, is a requirement to accomplish more with less. Accordingly, the operating models of many companies are in a state of flux. Finance functions, which customarily include tax compliance and planning operations, are in many instances shifting to a shared services model. As such, tax directors need to become acutely involved in determining an optimum mix of local and centralized presence. The goal is to have the necessary

Summary
As tax has moved up the agenda for businesses, chief financial officers have focused more closely on the function. That represents a challenge for tax directors and their staff, who must have sufficient understanding of the business to anticipate exactly what their CFOs need.
Management / The CFO relationship /

expertise and resources to accomplish local compliance objectives, albeit within an optimized cost environment. Given the scale of the challenges that finance functions and tax departments face, it is no surprise that companies are considering carefully how these roles should interact. As the tax director role becomes more challenging and visible, CFOs need to know that tax risks are being managed and reputations protected. At the same time, an ongoing focus on cost management means that no company wants to pay any more tax than is required.

He would know
Who better to understand what the CFO needs from his tax director than an executive who concurrently wears both hats? Hong Kong-based Andrew Morgan is CFO for the Asia Pacific region at the global financial services giant, Credit Suisse. At the same time, he is the company’s most senior tax executive, responsible for compliance, strategy and planning on a global basis. The regional CFO role is a very demanding one. It involves dealing with all the issues a financial services company might encounter in a fast-growing and complex set of regional markets. From a tax perspective, says Morgan, the key is to support this growth and the operations of the company overall – and that means providing a great deal of support to the group CFO.

Credit Suisse, like many banks worldwide, faces an environment of more stringent regulation, which will place additional demands on its capital. At the same time, it must manage its tax footprint in the context of governments which are all seeking ways of capturing their share of taxes. For an international institution, there are transfer pricing considerations to bear in mind, which require clear policies and appropriate documentation. The bank must also strike a balance between paying a fair and appropriate amount of tax, while protecting the company’s image of good corporate citizenship.

The most public face
Tax is, therefore, a high-profile role, which requires visibility at the highest level of the company. “I’m counted on to be the most public face of the tax department,” says Morgan. “The information we provide is what populates our financial statements, quarterly and annually. That’s what the investment world and the analysts see, so it’s got to be accurate, and that’s a big part of what we do.”

It is no longer enough, however, just to provide the figures. Increasingly, the tax director must also provide the CFO with insight. “It’s my job to understand what’s driving the business, and then show the CFO what, in turn, is driving the tax,” says Morgan. Even more importantly, tax directors are increasingly being called upon to assist with strategic planning and forecasting. “The business needs to have an idea of what the tax charge is going to be – not just now but in one, two or three years’ time,” says Morgan. “This analysis is complex, but crucial, at a time when the list of regulatory changes surrounding financial services is growing.”

CFOs hate surprises, so a key part of the tax director role is to anticipate change and ensure that it is clearly communicated to the finance leadership of the company. For many companies, avoiding surprises is critical but, when tax policy is moving at a rapid rate, it is highly challenging. This is particularly true in financial services, which is an inherently fast-moving and constantly evolving sector. “No matter how much guidance and direction is available, you are going to have people undertaking activities in locations where you might not have had a presence before, and that can create issues and liabilities,” says Morgan. “In addition, rules change, and when they do, you have to go in, interpret and respond in ways to minimize the pain – or in some cases just recognize you’re going to have to grin and bear it.”

Shifting sensitivities
Beyond constant regulatory changes, Morgan says that groups such as Credit Suisse must also deal with shifting sensitivities. They must pay close attention to reputational risk, while at the same time paying the right amount of tax against a backdrop where the rules are not always clear. “No one goes into a major transaction or structures a business without confidence that the terms are in compliance,” he says. “Consequently, you need to understand where the tax risks lie – what is clear and what is gray. And, from there, we need to present those issues clearly to our CFO so that he and the board can make an informed set of decisions.”

Finally, the CFO wants the tax function to perform as efficiently and flexibly as possible. Companies such as Credit Suisse are engaged in a cycle of continuous improvement and are always looking for a better way to manage the tax function. Examples of this include the company’s efforts to introduce greater automation, alongside its shift toward centers of excellence. It is also shifting more commoditized work to a site in India, where a team produces tax reports and returns for operations in Australia, Singapore and other locations. “We’re working right now to eliminate the reliance on spreadsheets, and implementing a highly customized set of software tools that are designed to help with financial statements,” says Morgan. “This not only enhances compliance, which is the starting point for tax returns, but also reduces human error. We are also taking tax talent that’s been developed in India and then deploying that into global operations.”

What the CFO values most from a tax director can often change, according to circumstance. Consider the experience of Jill Kyne, Head of Tax and Treasury at music and publishing group EMI. When she first took the position, her role was to
Kyne also stresses the importance of being proactive. “There’s a tendency among tax people to focus too intently on compliance and not enough on the future of the business,” she argues. “In my experience, the earlier and more actively you get involved in business planning and operation, the greater the impact you can have as a tax executive.”

Embracing an expanded role
Even today, traditional tax functions too often operate with a backward-looking orientation. “In too many cases, we still see the tax department being brought in at the last minute – and that forces them into a role where they’re just a scorekeeper or a policeman saying ‘No, you can’t do it that way, you have to do it this way,’” says Ernst & Young’s Holyoake.

But, in today’s environment, tax directors must up their game to become fully fledged partners in the planning and execution of business strategy. “CFOs aren’t looking for an after-the-fact assessment,” says Holyoake. “They want a proactive, risk-focused, cost-focused, strategy-focused partnership. Given the challenges that many companies face, this is a time of unprecedented opportunity to create greater value through a closer relationship between the CFO and the tax director.”

work within the finance transformation program to scope out and develop the tax function. But soon afterwards, her role and focus swiftly changed. “It was my job to shepherd us through a huge transaction – selling half of the business initially, with the remainder, provided there’s no holdup by antitrust, about to change hands for what will be the third time in five years.”

Kyne offers a clear example of how radically the needs of the CFO can shift. Prior to the downturn, the focus of the tax department at EMI was much more long-term oriented. If the group had overpaid its taxes in any given jurisdiction, the likelihood was that the company would take it as a credit toward next year’s liability, according to Kyne. But, with the arrival of the economic downturn, the focus on cash became more important. “We very quickly started going around from country to country, taking a closer look at liabilities and, wherever we might have overpaid, asking for the overpayment to be returned.”

Asked what is of paramount importance to the CFO, Kyne responds that a tax director needs to understand core group strategies. “You need to be aware of what is important now and what will be important in the future,” she says. “It is only through a clear understanding of business imperatives that you can make the most optimized decisions from a tax perspective.”

Andrew Morgan
Hong Kong–based
Andrew Morgan is CFO for the Asia Pacific region at Credit Suisse.
The importance of alignment

The days when tax could operate in isolation from the business are long gone, argues Andrew Bonfield, Chief Financial Officer of National Grid and Chair of the tax committee of The Hundred Group of Finance Directors. Instead, tax directors need to think commercially and demonstrate that they can add value to key business decisions. Interview by Andrew Sawers
T Magazine: How do you see the role of the tax function developing?
Andrew Bonfield: Tax needs to work very closely with the business and be aligned with it. By engaging with the business in this way, the tax function can ensure that it is performing a commercial role and is fulfilling its responsibilities. Tax is a cost of doing business and so needs to be able to demonstrate that it is providing value, just like any other cost center.

What, in practical terms, does engagement with the business involve?
You need to ensure that you have the right structures, planning mechanisms and processes to enable strong dialog with the business. This is absolutely critical to be a successful tax department and a successful tax director. It’s no use just sitting in an ivory tower making up schemes which are purely tax planning ideas and have no business value. Those kinds of initiatives are doomed to failure because the business will find it very difficult to implement them.

How can the tax function ensure that it engages with the business throughout the decision-making process?
Tax needs to be a party to business decisions but should not be the sole driver of them. Tax directors need to make sure they have a place at the table, but they have to earn that place by demonstrating that they can add value.

I remember one case when we acquired a business and the tax structuring that we built into the transaction almost generated the full value of the synergies that were required to do the deal. After that, the business team wanted the tax director at the table when any big decisions were being made.

How should companies manage the performance of their tax function?
It is important to set targets and objectives but you need to be careful to create the right balance. Focusing on one metric alone is dangerous. For example, if you set your target as the effective tax rate, then you might encourage people to take risks that may not be consistent with long-term value creation.

It’s much more important to put in place a combination of financial and non-financial measures. This should include the level of engagement with the rest of the business to ensure that the tax function is generating real value.

How do you measure engagement with the business?
You can get feedback from different areas within the business, either through surveys, or informally. Your finance director will tell you very quickly if the tax department is adding value or is being helpful. You need to try to make sure that you’re looking at tax planning ideas that create positive net present value rather than just a short-term, one-year benefit to the effective tax rate.

With the various responsibilities that you have as CFO, how do you prioritize tax in your working week?
At National Grid, we are relatively simple because we only have businesses in the US and the UK. So tax is less important than it would be at a global pharmaceutical company, for example, where there are all sorts of complexities involving structures, manufacturing, intellectual property and transfer pricing. I sit with the director of tax on a regular basis but tax is a lower-level activity than it would be at some other companies. As a utility, financing is critical to the sustainability of the company. So tax plays more of a role in looking at the financing elements of the group rather than the operational side.

From what you see at The Hundred Group tax committee, is the compliance landscape getting more difficult to manage?
There are always a lot of compliance requirements everywhere and they never get any easier. It’s like financial reporting: We talk about simplifying the annual report and then add another 30 pages to it. It’s just a cost of doing business. Unfortunately, we are buried everywhere in regulation and red tape. In the US, for example, we operate in several states, so we have a state compliance burden on top of the federal tax burden. And in the UK, we have other matters that have increased our compliance burdens, such as the requirement to have sign-off by a senior accounting officer. Compliance is an ongoing battle, so you have to look at your options. Do you do everything in-house, or do you outsource? In reality, what most businesses outsource tends to be the form-filling part rather than the value-added side.

Tax planning comes with challenging corporate reputational issues these days. How does that affect tax strategy?
There are two tests that you should always look at with tax planning. First, would you be comfortable if this was on the front page of the newspaper? Could you justify or explain it? Often, that’s a challenge because tax is complicated. Second, would you want to be out there when the chancellor of the exchequer or finance minister gets up in Parliament and says that he is enacting a new piece of legislation because of your company’s tax activities? That’s why I said at the beginning that one of the most important things we can do is to make sure that the tax department is not working in isolation but working very closely with the business - because any tax planning idea has to have a commercial purpose.
Two steps to tax harmonization

Last March, the European Commission put forward a proposal that represents one of the most fundamental changes in corporate taxation ever attempted in Europe. The Common Consolidated Corporate Tax Base (CCCTB) proposes, in effect, a single set of rules that would allow companies active in different European countries to calculate one tax figure for all their activities across the EU. This “one-stop-shop” would allow companies to file a single tax return, rather than deal with up to 27 different sets of rules. The tax would be paid to a single authority and then passed on to different countries where the company is active.

This initiative promises to reduce tax distortions across the EU. It would enhance competitiveness, representing an important step towards European economic union. The CCCTB would also offer considerable benefits for companies. A harmonized tax base would cut compliance costs, while dealing with one principal tax office would simplify the tax audit process considerably. It would sharply reduce complexity, while lowering double taxation risk.

Significantly, this is an initiative that is primarily driven by the needs of taxpayers themselves. Many multinationals based in Europe have been calling for a harmonized common tax base for some time. As they expand their business into new emerging markets, they need greater confidence that their compliance in Europe will run smoothly and cost-effectively.

As currently envisaged under the CCCTB regime, there are three steps to calculate a company’s tax position. First, income will be determined according to a single set of tax accounting regulations. This will require the rules for calculating the tax base and the definition of taxable profit to be harmonized across the EU - in effect, the development of a common corporate tax base. This is long overdue. The economic cost of having 27 different sets of tax rules to calculate the taxable profit is significant.

Second, income will be consolidated for the whole of a company’s activity across the EU. And third, this consolidated tax base will then be allocated to different Member States where the company is active, according to a formula that is based on the group’s assets, labour force and sales.

Recent research by Ernst & Young, which was conducted in collaboration with the Center for European Economic Research (ZEW) and the University of Mannheim, has explored the impact of the first step on the tax burden. This compared and contrasted taxable income under the proposed CCCTB with corporate tax regulations in all 27 Member States, Switzerland and the US. The results suggest that the difference between current international tax practice and the proposed CCCTB is relatively minor. Although there would be winners and losers among member states, the effective tax burden remains largely unchanged.

Unfortunately, when it comes to the second and third steps – the consolidation and allocation of profits – the scheme is on much less certain ground. We know little about the likely impact of these changes. It is just too early to have a clear understanding of how consolidation could be achieved, or indeed the impact of the allocation formula. There are many unanswered questions.

Given these uncertainties, our research suggests a two-step approach to implementation. The first step, determining income according to a harmonized set of tax accounting regulations, could be undertaken initially. Once implemented, we would be in a better position to evaluate its effects. We can then assess how the regime would impact the tax burdens of corporations and tax revenues.

While it is clear some of the fundamental advantages of the CCCTB would not be realized by the first step alone, the two-step approach seems more likely to succeed through the political process in the EU and appears to be a promising starting point for corporate tax harmonization.

There may, of course, be some business leaders who are hesitant because the CCCTB may appear to be a very long-term proposition and one that seems somewhat theoretical. While much depends on the negotiations within the EU, our study suggests that it should be feasible to finalize step one in two to three years. There may be single Member States who do not support this initiative, because they may be looking at it from their own distinct, national and political agenda. But our research suggests that the differences are not particularly significant. As such, these considerations should not be enough to stall progress.

York Zöllkau, the Tax Leader for Germany, Switzerland and Austria at Ernst & Young
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