Taxation in the evolving post-COVID world

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Good morning and thank you for the opportunity to speak to you today. It’s great to be back for a second year at this very important conference.

When I reflected on the theme for this speech, “taxation in the evolving post-COVID world”, it got me thinking about how much the world has changed for CFOs and tax professionals in the space of twelve months, but perhaps more importantly how it will change in the years ahead.

My focus today will be on how the societal challenge of COVID might affect community attitudes towards taxation and the role of socially responsible companies concerned about their licence to operate, and what you, as CFOs, can do to ensure you meet the community’s changing standards and not put your companies at financial or reputational risk.

Before I start, note that I am a tax administrator, not a policy maker, and so cannot comment on the pros and cons of policy or what policy changes may be coming down the track.

I have split my presentation today into three themes:

- The impact of COVID-19 on community expectations,

- Some observations on the stimulus packages and expectations of those accessing them, and
- What you, as a concerned CFO, can do to steer your companies through these taxing times.

The impact of COVID-19 on community expectations

Large companies, on the whole (and particularly Australian owned companies) are largely tax compliant in relation to their Australian affairs. Our latest estimates, published last week are that they are at about 92.5% voluntary compliance at lodgment, moving up to 96.3% after ATO compliance activity. These estimates are for the 2017–18 year: the ATO's aspiration is to increase these levels to 96% voluntary compliance at lodgement and 98% after compliance activity in the short to medium term.

The 92.5% / 96.3% is a globally high level of compliance, and yet there is lingering concern in the Australian community that large companies are still getting away with tax avoidance. Much of this community concern is currently focused on large, mainly tech multinationals. The unease may be expressed in an unsophisticated way (for example by focusing on tax versus revenue), but the unease is real (and in some cases quite justified).

Pre-COVID, there was also an increasing push from social justice groups that the Australian community should not just be concerned with avoidance of Australian tax, but the offshore tax avoidance of Australian multinationals in a broader view of social responsibility.

I am often asked why the Australian community is much more concerned with the tax performance of large companies than citizens of other countries, when objectively the problem is less.

My personal perspectives are that it has something to do with the economic literacy and deficit aversion of the Australian community, as well as the fact that the average Australian is largely tax compliant and has little appetite or scope for tax avoidance (our latest estimates are that Australian individuals not in business pay about 94% of their tax voluntarily, which is a higher rate than large corporates).

Stimulus package observations

The business community has been entrusted with the weighty responsibility to recover the post COVID economy, supported by extraordinary amounts of Government funds, most notably JobKeeper phase one (about $70bn), JobKeeper phase two (currently estimated to be in the order of $30bn over the next six months), cash flow boost for smaller companies ($35bn) and the JobMaker hiring credit.

The quid pro quo in the community's mind is that large corporates, in particular but not limited to those who accessed these schemes, will pay their share and improve their approach to tax. Yes, follow the tax law, but also follow the spirit of the law.

I suspect the community will have even less sympathy for companies seen to be

exploiting loopholes. The line “we follow the tax laws in every country in which we operate” will play even less well when aggressive tax behaviour spills into the public domain, particularly in times of budget deficit.

By way of example, there was nothing explicit in the rules for the stimulus measures that required companies to stop paying executive bonuses or from increasing dividends to shareholders: but there was a quick backlash for those companies seen to be exploiting the spirit of the measures.

The Business Council’s Jennifer Westacott told ABC’s Insiders that companies should not be paying executive bonuses if they are receiving JobKeeper because it wasn’t designed for that, it was designed to keep people working.

And Ownership Matters is reported saying “The cultural signal of a board deciding to pay — and a management team electing to receive — bonuses in a year where a listed entity received significant government subsidies is an important one for investors to consider, especially for listed entities with significant exposure to government as a regulator or customer.”

I encourage you to consider the optics of making a statement in your annual report noting that the pandemic has not substantially impacted the operations of your business while at the same time collecting hundreds of millions of dollars in stimulus.

In the recent Budget, two more measures were introduced with the aim of encouraging business to invest: full expensing of plant and equipment, and the ability to carry back losses.

These measures should be embraced, but for the purpose for which they were introduced. Invest in new plant, upgrade your facilities, claim a tax offset and reinvest the money in your business and jobs! At a more granular level as CFOs, make sure your business analysts are including these tax cash flow advantages in your DCF models, in conjunction with your heads of tax making appropriate variations to your tax instalments to bring home that cash flow advantage.

But I would suggest thinking twice before entering into artificial mechanisms to take advantage of these measures, for example: structured transactions where the plant and equipment is not actually used in your business, intellectual property migration with no change in real activity; asset swaps with related parties. Do not artificially shift profits (and losses) around your group to access the loss carry back.

Similarly, accessing the loss carry back to support executive bonuses, increased dividends or to repatriate cash to offshore related parties is likely to be viewed poorly by the community.

Steering your company through taxing times

So the question arises, how do you as a CFO, ensure that your company meets (and is perceived to meet) community standards in an evolving post-COVID world?

I know that in practice it’s been hard for CFOs to truly understand where their

company sits in the tax behaviour spectrum. Tax can be hard, and it has been difficult to get an objective handle on whether your advisors (inside or outside the company) have a risk appetite consistent with the board – sometimes a “big 4” or “big law” signature has been the practical standard, but even then there is a broad spectrum of risk appetite within those firms.

There are some practical ways that, as a CFO, you can understand where your company stands and either protect that position if you’re happy with where you are, or improve it if you’re not.

Ensure your tax team’s KPIs are driving desirable behaviours

Like everyone else, tax teams will be focused on their KPIs. Make sure that their KPIs are not just rolled over from a decade ago but are up to date. Historically, “tax savings” or “low effective tax rates” were relatively common but are now rare: by contrast, “achieving/maintaining a high ATO assurance rating” is increasingly used as the KPI.

Make sure there is a strong, board-endorsed, tax governance framework, and that it is “lived” in practice

Our reviews show us that most organisations have a tax governance framework but the ability to demonstrate that these frameworks operate effectively in practice has been varied. Evidence for this is that governance and systems failures are the single greatest reason for significant GST audit collections in the large market. Accordingly this year we have also published a best practice governance guide testing and assessing your GST governance, systems and controls.

Embed processes that allow you to easily reconcile financial statements and tax

With global supply chains now commonplace it is important to understand where profit is booked around the world for tax purposes. Using a tool like the effective tax borne allows you to identify your economic group’s worldwide profit from Australian-linked business activities and the Australian and offshore tax paid on that profit. This is particularly relevant to obtain confidence that you are not engaged in transfer mis-pricing.

We have recently introduced a similar concept for GST. Our GST Analytic Tool (or GAT), allows you to reconcile financial statements to the BAS, identifying and testing appropriateness of variations or differences. Fleshing this out, in our experience, GST systems are often “bottom up” and prone to omissions or double counts when links break or underlying systems change. Companies without a “top down” sense check have little protection against this sort of error, often with very large impacts when identified years down the track.

Understand where you sit relative to your peers

By the end of this year, Australia’s largest 1,000 companies will have been reviewed under our Justified Trust program. Assurance ratings provided under this program provide an objective assessment for CFOs as to whether you are satisfying your tax

obligations.

Each year we also write out to the Top 100 largest groups in Australia to advise them how we perceive their tax risk profile relative to their peers. Elevating the message above tax groups provides an important sense check to CFOs and Boards about their tax performance and health of their relationship with the ATO.

We have also now published data that allows you to compare your performance against that of your peers, both top 100 and top 1,000.

Similarly, on many types of important industries and business models, we have published practical compliance guidance (a PCG) on the margins we view as low risk and high risk. Make sure you understand your risk "zone" if any of this guidance is relevant to your organisation.

Get a proper level of assurance on your tax "infrastructure"

In most groups, there are some tax consequences which are so material, they should be viewed as part of your corporate infrastructure. And, like any piece of key physical infrastructure, you should have appropriate assurance that the infrastructure will hold.

It still surprises me how many large companies rely on an advisor's "more likely than not", "reasonably arguable" or "should" opinion (whether a "weak should" or a "strong should"), on their tax infrastructure (which at most only provides penalty protection if it all goes wrong). I would strongly recommend obtaining assurance commensurate with importance, for example through a private binding ruling. (And if your advisor says that it is too dangerous to expose the issue through a private binding ruling process, this is probably even more of a warning sign – it is an unambiguously bad idea to rely on non-detection by the ATO.)

Understand your reportable disclosures

Large corporates are required to disclose to us how they stack up against expected norms for systemic corporate tax risks and also whether they are involved in arrangements of concern. Understanding these disclosures can affirm confidence in your tax outcomes, or conversely highlight areas that are high risk that may require more of your attention.

I have observed that organisations with high risk disclosures will often downplay the significance of these disclosures by assuming that everyone is just like them. Typically, this is the result of the personal experience of key tax personnel being narrower than they (or their organisation) appreciate.

We will shortly publish the Reportable Tax Position Insights Report which will allow you for the first time to understand your ratings relative to that of your peers. The report will show that it is not normal or ordinary practice for large corporates to have high risk arrangements, or to be involved in arrangements of concern.

Resolve disputes

Granted, no one wants to be under audit, but tax is complicated and at times there will be disputes. There are ways that this can be a more positive experience. Open communication, engagement and transparency creates space for the parties to work better together to resolve differences and even in circumstances where resolution is not achieved, refine and narrow the issues in dispute.

Tricky delay or obfuscation tactics by taxpayers and advisors will generally only lead to a more intense and uncomfortable experience. The consequence of which is unnecessary financial costs and resource diversions for taxpayers and the ATO alike.

In certain circumstances, information is not required to be disclosed to us, for example where it is subject to legal professional privilege (LPP). We are strong supporters of LPP but have seen too many instances where it appears to be being abused with privilege being claimed for obviously non-privileged documents. We are currently developing an LPP protocol to help you and the ATO be confident about your LPP claims. We would recommend following this protocol (and instructing your lawyers and advisers to do so also) as it will provide an objective benchmark for both you and the ATO as to how you are conducting your tax dispute.

Resolve legacy disputes and have a less complicated tax experience

I have observed that long-standing disputes are often the result of disputes being "captured" by the process and key personnel (internal or external to the organisation) being reputationally locked into positions. CFOs can provide a circuit breaker and bring these disputes to an end. Typically, to settle matters, we look to obtain certainty for both past and future years. Although, settlement terms themselves are confidential, we are transparent about our settlement parameters (through our PCGs), creating a level playing and confidence that no-one is getting a better "deal". In certain higher profile cases, we encourage taxpayers to publish the settlement: this provides confidence to the community that matters are being resolved fairly.

Opt for a wise adviser, not a 'clever' one

A wise advisor can advise you on the Australian environment and help you make fully informed decisions having regard to more than just technical or legal risk. Your alarm bells should ring loudest when the "clever" advisor tells you that your tax manager is too conservative or (particularly dangerous) they bring a tax driven transaction to you supported by a suite of potential commercial rationales for the transaction.

Be a transparency role model

We encourage corporates to participate in the corporate tax transparency code to improve tax transparency and community confidence. To date, around 180 corporate groups have published reports, typically large Australian corporate groups with strong tax results.

If not already signed up, I encourage to you to actively participate in order to unlock the benefits that improved transparency and community confidence can bring.

Similarly, for groups with complicated Australian operations (particularly where there is limited requirement to prepare general purpose financial statements (GPFS), and hence there is an obligation to lodge GPFS with the ATO), we encourage companies to prepare notional Australian stand alone GPFS and provide them to the ATO for on-provision and publication by ASIC.

And, for those companies which have achieved a "high assurance" rating from the ATO, don't be shy! Tell your investors and even (or especially!) your employees – they also want to know that they are working with a company that does the right thing.

I commend those of you that have already risen to the challenge and have demonstrated to the ATO and the community that you are a good corporate tax citizen by achieving a high assurance rating. You now also have an important role in influencing other companies to step up. This will be important if you are to achieve the collective improvement (in reality and perception) needed to gain community support for business-led policy proposals.

Whilst there is a general reluctance by companies to comment on affairs of others, there are ways that you can influence your peers, for example, through your participation in professional or industry associations. Importantly, do not disengage from industry associations because you have achieved high assurance and comfort around your tax positions – if companies like yours disengage, you leave the associations (and their platforms) to others who do not share your position.

Conclusion

In this climate of uncertainty and rapidly changing social norms and expectations, there really is a 'Team Australia' opportunity that all taxpayers can seize upon.

I challenge you, as the CFOs of Australia's largest taxpayers to consider the potential reputational impact of tax decisions made – or not made – in the evolving post-COVID world.

You have been entrusted by the Government with leading the economic recovery with a range of stimulus measures. With this comes increased expectations around corporate behaviour including tax. There is an opportunity to rise to these expectations and increase the community's trust in large organisations. Conversely, clinging to old perspectives on tax compliance may put your organisations out of line with emerging community expectations.

Ultimately a tax system is about underpinning a country's social contract, by collecting the revenue that funds its programs and services. Australia is fortunate to have a robust tax system and an effective tax administration that supports the social benefits we all enjoy.

Thank you for your attention and I'm happy to take any questions.

We are committed to providing you with accurate, consistent and clear information to help you understand your rights and entitlements and meet your obligations.

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