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Public tax transparency

Establishing trust in a digital (tax) world

2. Is it in your interests to be publicly tax transparent?

Overview of the public tax transparency series of papers

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1. Introduction

The general perception that large corporations enjoy an oversized slice of the globalisation pie has triggered close media and political scrutiny of the tax affairs of multinationals.[1] Tax administrations in the process of digitally transforming have started using technology to shed intense new light on tax matters. The result is that we've embarked on a journey to a significantly more scrutinised world of tax.[2]

The role of tax functions will inevitably change in the wake of this development. An increasingly important challenge is managing tax-related reputational risks. Public tax transparency could play a significant part in this. In an increasingly transparent tax environment, companies may want to communicate their positive financial impact on the societies they operate in. If you no longer want to simply watch the journey to transparency from the sidelines, the time for action is now.

We are dedicating a series of four brief papers to public tax transparency. This, the second in the series, explores in detail why we believe public tax transparency is so essential. We also share an insider's view in the form of an interview with the head of tax of a multinational organisation.

1 For more information, see the first paper in this series 'What is public tax transparency about?'.

2 For detailed information on this topic, see our paper regarding the digital transformation of tax administrations and tax functions, 'Tax disruption management', https://www.pwc.ch/en/insights/tax/taxdisruption-management.html [May 2019].

2. How important is public tax transparency?

Public tax transparency is more than just publicly disclosing how much and where taxes are paid. It's about presenting easily understandable information on the broader economic contributions a taxpayer makes by paying taxes in the environment in which they operate, and putting this information in the right context.[3]

This kind of public tax transparency can be very beneficial, and in more ways than you might think at first. We have identified five areas where it will most likely be in your company's direct interests, plus a sixth area where you might indirectly profit from the process of becoming publicly tax transparent.

1. Corporate sustainability: actively building public and stakeholder trust

2. Institutional investors: meeting their expectations

3. Media: regaining control of your reputation

4. Tax administrations: improving relationships

5. Lawmakers: actively participating in the design of new transparency standards

6. Business strategy: gaining new insights

1. Corporate sustainability: actively building public and stakeholder trust

In times of omnipresent news coverage and polarising debates, for some companies it may no longer be sufficient to be correct and compliant. Instead, they can choose to become active and demonstrate their compliant behaviour convincingly. This would be an opportunity to try to ensure that the debate also takes your point of view into account.

Communicating an organisation's contributions to the society in which it operates is one important way of building long-term trust with the public (people in the street, customers and media) and other stakeholders (employees, the board, suppliers and other business partners, NGOs, lawmakers and supranational bodies like the OECD).

Furthermore, public tax transparency is also a way of demonstrating that you actually do business in a sustainable and responsible way, as companies paying taxes are an integral part of the sustainability debate.[4] Being an important source of government revenue, taxes play a vital role in advancing the achievement of the UN's Sustainable Development Goals. A company's tax payments are therefore a way of compensating society for the institutions and services (legal system and legal certainty, education for the workforce, public infrastructure, conditions for ongoing economic growth, and so on) it has access to.[5]

Having recognised this, nowadays some multinational organisations have integrated tax affairs into their environmental, social and governance (ESG) framework. For the same reason, an element of public tax transparency has become a mandatory section in major sustainability indices, such as the Dow Jones Sustainability Index (DJSI) and the FTSE4Good Index Series.

The sustainability debate is no flash in the pan. It will stay: the challenges we face are too big. Highlighting your (tax) contributions to society and sustainable development is a reasonable way to build a sustainable reputation. Moreover, it's a more directly business-related and affordable measure for building public trust.

[3] Read more on this topic in the third of this series of brief papers, 'How to implement public tax transparency'.

[4] See, for example, The Principles for Responsible Investment (PRI), Engagement Guidance On Corporate Tax Responsibility, 2015, https://www.unpri.org/download?ac=5601; Exposure draft of GRI topic-specific Standard: Tax and Payments to Governments, Global Reporting Initiative, https://www.globalreporting.org/standards/media/2160/public-comment-form-exposure-draft-standard-for-tax-and-payments-to-governments.pdf [May 2019].

[5] In addition, taxes have many implications in terms of the sustainability of a company's own economic activity, for example direct effects such as potential long-term damage to brand value, and indirect effects such as triggering a downward spiral if general taxpayer trust in the system is damaged, diminishing the overall willingness to comply and weakening the institutions and services offered by society. Because trust and minimal transaction costs are so crucial for economic success, in the end all taxpayers will suffer.

2. Institutional investors: meeting their expectations

Institutional investors like Norges Bank Investment Management (responsible for managing the Government Pension Fund Global, with assets of about USD 1 trillion)[6] and Ethos Engagement Pool Switzerland (pooling 135 pension funds managing total assets of CHF 223 billion)[7] have started to explicitly set expectations in terms of the transparent tax behaviour of their investment targets.[8]

That's no surprise. In the last few years tax has turned out to be an increasingly important consideration for investors. This new scrutiny of companies' tax affairs may create serious investment risks that are currently hard to monitor, and may emerge at some uncertain point in the future. Opaque tax behaviour could disguise risks not reflected in the valuation, such as earnings risks (penalties, damages, cancellation of rulings, for example), rising workforce costs for tax disputes, potential exclusion from public contracts, and so on. Even more important is potential damage to reputation or brand value.

Institutional investors in particular are increasingly coming under pressure to show that their investments are responsible and sustainable, meaning they're forced to concentrate even more on the long term.

Investing in a company with a transparent approach to tax allows institutional investors to demonstrate sustainable behaviour and properly assess tax-related risks. This is beneficial for you, isn't it?

3. Media: regaining control of your reputation

Based on our observations, our impression is that, at present, the media coverage of tax issues is generally and constantly negative. Tax functions have started to work with their communications and investor relations (IR) teams to highlight the benefits of tax matters.

Your tax affairs are complex and nuanced, so they need to be explained carefully. Corporate tax isn't the same thing as all the taxes paid by a company. Profit isn't the same as revenue. Tax functions have to explain and clarify to avoid a situation where public expectations diverge from the way the tax system is actually built.

The news business is increasingly fast-moving, and journalists sometimes lack the time to research. Tax functions may want to step into the breach and provide guidelines for interpreting the numbers. This can help prevent misinterpretations and exaggerations appearing in the media.

Openly providing information may also reduce media interest and get your company out of the line of fire. It could be beneficial to avoid the impression that you have something to hide.

One way to go is to be more transparent but at the same time to control, to some extent, the information that you share externally.

4. Tax administrations: improving relationships

Tax authorities around the world have to deal with budget constraints alongside growing pressure to increase levels of compliance.

Being publicly transparent about tax issues promotes trust and credibility. Tax administrations should welcome this, as it may reduce the need for scrutiny. Strong and open relations with the authorities could also lead to other benefits, such as quicker decisions and more planning security for your organisation.

5. Lawmakers: actively participating in the design of new transparency standards

In addition to this, we're already noticing that regulators are increasingly displaying an appetite for mandatory public tax disclosures. For example, the UK requires the public disclosure of tax strategies, Australia has introduced its quasi-mandatory Tax Transparency Code (TTC), and the EU has put forward a proposal for mandatory public country-by-country tax disclosures. On 25 March 2019, the FASB re-issued an exposure draft on the income taxes disclosure framework to improve the effectiveness of the disclosures in the notes to financial statements by facilitating clear communication of the information required under the generally accepted accounting principles (GAAP) that is most important to users of each entity's financial statements.[9]

Increasing your public tax transparency and developing innovative disclosures containing relevant and understandable data can be beneficial in establishing standards. It may give you a credible voice in the debate on what mandatory public tax disclosures should cover and how they should be designed.

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6 https://www.nbim.no/en/the-fund/market-value/ [May 2019].

7 https://www.ethosfund.ch/en/members-ethos-engagement-pool [May 2019].

8 See Norges Bank Investment Management, Tax and Transparency, https://www.nbim.no/contentassets/48b3ea4218e44caab5f2a1f56992f67e/expectations-document---tax-and-transparency---norges-bank-investment-management.pdf [May 2019].

9 For more information, see https://www.pwc.com/us/en/services/tax/library/insights/fasb-issues-second-proposed-accounting-standards-update.html [May 2019].

6. Business strategy: gaining new insights

There's another dimension that's more of a by-product of the whole process but might nevertheless turn out to be quite advantageous. Collecting the necessary information and developing an easily understandable, contextual and geographic overview of your organisation's tax obligations could help you in various ways. It could provide you with additional arguments for conversations with governments, or it could deepen your understanding of the connection between the value creation, location, government payments and profits for your business. This could lead to new insights that enable you to improve your general business strategy and optimise and adapt your priorities.

3. Sharing an insider's view: interview with Carl Emanuel Schillig, Group Tax Director, Zurich Insurance Group[10]

We have spoken to different leaders currently dedicating a lot of time and energy to developing public tax transparency disclosures. We'd like to share here Carl Emanuel Schillig's insider view. Carl Emanuel joined Zurich Insurance Group in 2004 as Group Tax Director. We hope this interview helps improve your understanding of issues around implementing public tax transparency.

In March 2019, Zurich Insurance Group published a tax transparency report for the first time. How does it feel to become tax transparent?

Actually, it feels good. I'm thankful for the opportunity to disclose comprehensive tax-related information in the way we thought made most sense. It's also a good feeling to be leading a global trend that's here to stay.

Had Zurich Insurance Group received any negative media coverage of its tax affairs in recent years? Was this your motivation?

No, not at all. Negative media coverage wasn't what drove us. The drivers were completely different.

So can you tell us then what the main drivers of this decision were?

We believe it is important that Zurich, as a provider of insurance coverage, acts as a responsible corporate citizen. This means that Zurich is committed to being a responsible taxpayer and, as such, a supporter of economic and societal development in the communities where we operate. We see the increase in tax transparency as part of our sustainability effort.

Also, we identified a clear trend towards more transparency and took the decision to stay ahead of the curve. In the last few years we've observed many regulatory changes, all of which increase transparency. Initially it was mainly individuals that were targeted, with FATCA and CRS. This soon extended to multinational companies with country-by-country reporting (CbCR), the preparation of master and transfer pricing local files, and the publication of the tax strategy. Sooner or later, I expect that there will be further public reporting requirements.

We wanted to pre-empt this development and take advantage of the freedom we currently have to present the facts in a more holistic way that better reflects Zurich Insurance Group's approach to sustainability.

Why did you decide to go live now?

In addition to the idea that we wanted to do something, we realised that institutional investors were getting increasingly interested in this topic.

I guess that, in the end, the letter sent out by Ethos Foundation in November 2018 created the necessary momentum to tip the scales.

[10] As initially published in Tax Adviser Magazine, p. 27, https://www.taxadvisermagazine.com/edition/5326 [September 2019].

When and how did you first come across the idea of public tax transparency? What was your reaction at that point?

This was a couple of years ago. After the financial crisis of 2007-08, the whole debate about companies not paying their fair share of taxes started. I was sure that this debate wouldn't just disappear again and, instead, would trigger requests for additional public tax disclosure. After a while, the first multinationals started extending their annual reports and disclosing information in greater detail.

I knew I also wanted to contribute to the debate. Finally, I realised that the best way to counter accusations of not paying your 'fair share' is to point out what you are really paying in taxes in total.

What features of tax transparency are important for you? Is there an aspect you particularly want to emphasise?

Besides illustrating the dimensions of the Total Tax Contributions we make and how we support economic and societal development, for me it's particularly important to disclose the tax strategy we have here at Zurich Insurance Group. The tax strategy is supervised by our Board of Directors and executed by the Group Executive Committee. We want to show our commitment to being a responsible taxpayer and complying with regulations in the countries we operate in.

Saying that, I want to stress that I have doubts about CbCR being a meaningful document if externally published. It's very open to misinterpretation by people without a proper tax background, and it only tells part of the story.

What advantages do you expect? Is public tax transparency designed to address any stakeholders in particular?

For us, a particularly important group of stakeholders is institutional investors. I'm convinced that becoming publicly tax transparent will help us further strengthen their trust and confidence in our company.

We assume it was quite a ride, from the day you decided to become publicly tax transparent until the day of publication this March. Can you describe the process? What were the milestones?

The first challenge we faced was to collect the necessary information. We had to persuade the local teams to collect information that they usually didn't and which they were not obliged to report in such detail for the consolidated Group IFRS accounts. Another important step was to consolidate the information we received. Only then we could start to generate the report.

The final report contains a lot additional information beyond reporting tax figures, and it's not just a product of the tax department. It's the result of intense interdisciplinary collaboration with other teams like Investor Relations, Communications and Sustainability.

Have you established an automated process to support your disclosures?

Yes. Though we started with Excel sheets, we finally managed to feed the information into our finance consolidation tool. This automation resulted in an efficient and effective data collection process.

Do you think you're spearheading a general trend? Will all major multinationals soon become publicly tax transparent?

As I said at the beginning of this conversation, I'm convinced that we're leading a global trend. When I talk to my peers, I see this topic is hot, and more and more of them are interested in learning from our experience.

Was this step controversial within Zurich Insurance Group?

Not as such. The board had been familiar with the topic for several years. From the beginning, we all agreed on the direction of travel. The discussions we had were more about the type and granularity of the information we wanted to release, and how we could make sure that the information was disclosed in a meaningful way.

Finally, are there any steps you're planning next?

I'm convinced that tax transparency is here to stay, and that it will even evolve in the coming years. We at Zurich Insurance Group will be carefully monitoring these developments and will act as ambassadors, advocating to the broader public the benefits of tax transparency.

4. What should I do now?

The very first step should be to decide whether you want to meet the requirements of an increasingly transparent world of tax.[11] The second step should be to adopt a position and start to develop a strategic response. Finding an approach to public tax transparency may be part of it.

Before providing a benchmark study in the fourth and last paper in this series, in the penultimate paper we'll be presenting our view of what public tax transparency should look like to get the most out of it, and propose specific steps. Stay tuned!

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[11] See our white paper, 'Tax disruption management', https://www.pwc.ch/en/insights/tax/taxdisruption-management.html [May 2019].

Questions?

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