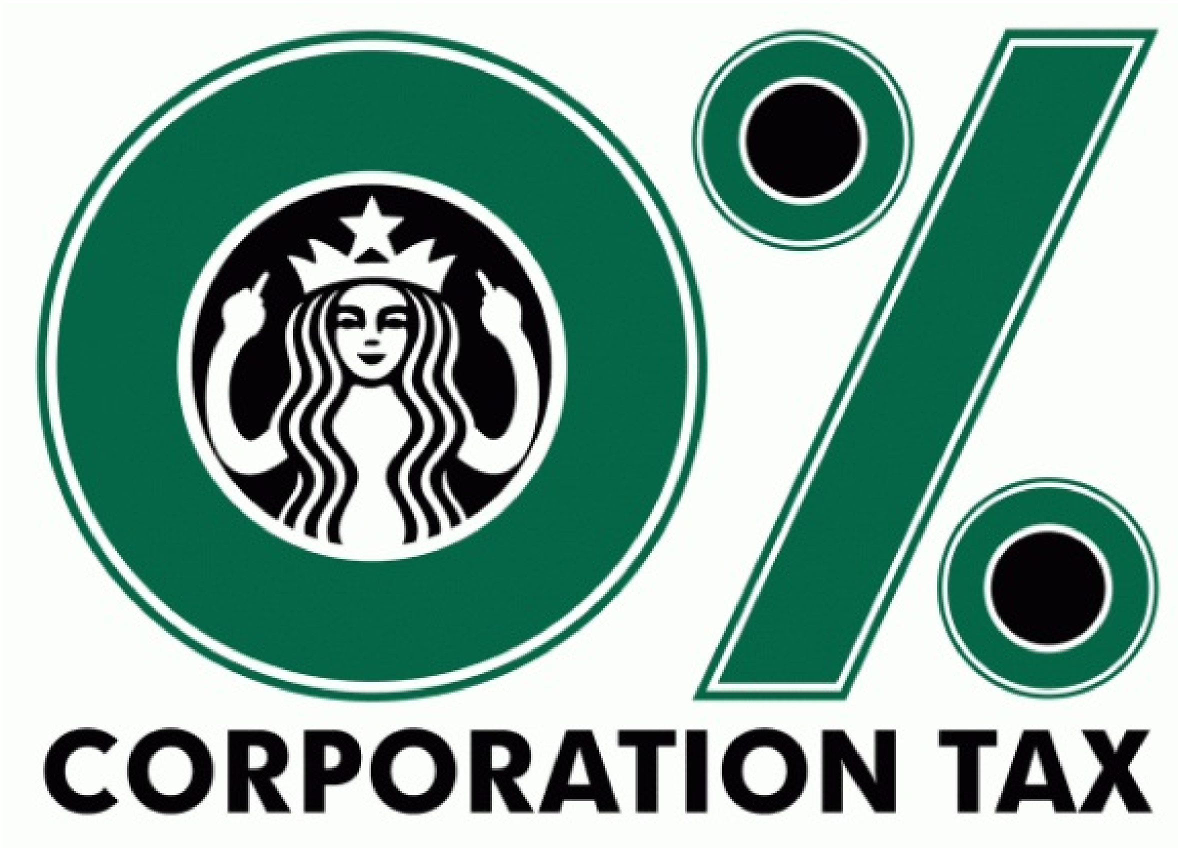
Tide Turns Against Company Tax Avoidance



The tax arrangements of companies including Starbucks and Google have sparked a global debate about corporate tax avoidance that could have big implications for the revenue and reputations of accountancy firms. [IAB reports]

Multinationals' have complicated tax structures and follow practices (such as profit shuffling, transfer pricing, and so on) that are legal but increasingly controversial.

Business and many accountants often argue that if governments think tax loopholes are being exploited, they should close them by changing the law.

Critics say corporate tax avoidance is morally wrong and unfair with protests and boycotts against companies such as Starbucks and Amazon becoming news of late. Politicians have also grilled partners at the Big Four accountancy firms about their role in helping companies dodge tax.

Governments are trying to counter tax avoidance and evasion by sharing information about taxpayers and requiring companies to reveal those countries in which they make profits and pay tax.

There is a consensus among politicians and accountants that the global tax system hasn't kept pace with digital services, and global companies that shift profits between countries to reduce their tax bills.

One of the emerging issues in the tax avoidance debate is over law interpretation.

"Who's to know what the spirit of the law is?" says Peter Simons, technical specialist, research and development, education department at the Chartered Institute of Management Accountants (CIMA). "The spirit of the law is not documented."

Simons gives some examples of possible tax conundrums facing tax advisers.

In example one, principals of very small owner-managed companies, including self-employed tradesmen and professionals, are alert to tax advantages in how their income might be treated if taken as dividends rather than salary. Often a SME might be owned 50:50 by a couple. If business income of up to £80,000 is split evenly as dividends rather than as an individual's salary, this can significantly affect the tax bill.

Will the taxman see this practice as an acceptable loss of tax receipts in order to encourage enterprise, or an abuse of the tax system?

Example two is the Netherlands' tax treatment of royalties. The reduced tax rate for corporate royalty payments came to the public's attention because Starbucks seems to have limited the level of profits reported in the UK by paying a royalty to a related company in the Netherlands.

The Dutch tax authority will usually allow such income to be transferred elsewhere, without applying any withholding tax, giving companies more certainty when planning their tax, Simons says.

But in light of the Starbucks tax row could similar tax arrangements be challenged even though the UK ministers signed a new tax treaty with the Netherlands only a short while ago?

Tax advisers could be forgiven for feeling confused, but what about in-house accountants?

Management accountants don't normally give tax advice, of course. However, they may need to explain to their board the risks of tax advice offered by an external adviser.

"My personal tip [is] if in doubt if rules are being bent, consider if one would be prepared to be transparent," Simons says. "Disclosure in accounts may not be necessary, but how would customers or other stakeholders react if an advanced tax structure were made public in a newspaper?"

Accountants also need to consider the risk of a customer backlash if a company's tax arrangements are considered unethical.

Even if it's legitimate, there may be a risk to a company's reputation and brand that might outweigh any potential tax saving.

Management accountants often have to say: "Hang on, what about the damage to our brand," Simons says.

Updating guidelines

The accountancy institutes are updating their ethical guidelines for their members, but how many members stick to them or find them useful?

Also, accountants often moan that journalists and politicians often don't understand or oversimplify tax. So why don't the accountancy institutes rebut what they believe are tax myths? Or if they believe the tax system is hopelessly outdated and unwieldy why don't they lobby governments more vocally?

Chas Roy-Chowdhury, head of taxation at the Association of Chartered Certified Accountants (ACCA) says accountants need to "be much more articulate about tax structures and not hide behind the parapet", explaining the reasons for companies' tax arrangements to politicians, the media and public.

But others in the profession are more cautious about accountants' role in the tax avoidance debate.

Ian Young, a specialist in international tax at the tax faculty of the Institute for Chartered Accountants in England and

Wales (ICAEW), says that the tax system is “not working as it should be” but says the ICAEW is not a lobby group.

Companies are under more pressure to publish more information about their tax arrangements and accountants like to talk about the importance of transparency in business. So shouldn’t accountants encourage clients to reveal where they make profits and pay their tax?

Young says he’s not in favour of the G8’s recent proposal for country-by-country reporting.

He says: “If you have lots of information it’ll be picked over by campaigning groups to further their agenda. [Companies] don’t need to have to expose absolutely everything …. it sounds attractive but I’m not sure it will get the results civil society wants.”

Young says that a director of General Electric told him that the industrial conglomerate probably has millions of different pieces of information in its accounts that it has to provide to the US Internal Revenue Service. “If it was produce [publish] all the information we would be none the wiser,” Young says.

But some accountants want the profession to be bolder in shaping the debate about tax avoidance.

CIMA’s Simons says the tax debate should be broadened to look at the value companies generate for society.

He says: “They exist to produce goods and services, to generate employment and wealth, not primarily as corporation tax cash cows.

The debate about tax avoidance has produced more rhetoric than action but it has begun to change the tax system. Governments are trying to making it harder for companies to avoid tax by sharing information and passing new laws.

All this means it’s an interesting time to be a tax accountant. Advising companies on tax avoidance scheme is increasingly risky; too likely to be challenged by tax authorities, plus the risk of damage to the reputation of the client and the accountancy firm.

But there are also new opportunities – such as advising clients on how to comply with new tax rules and explaining tax arrangements to sceptical politicians, media and the public. As Roy-Chowdhury says: “In the twenty-first century it’s not just enough to crunch the numbers and be technically proficient. [Accountants] have to go out and explain tax.”