



## SPECIAL REPORT

# Tax planning: new risk to corporate reputation?

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With the collaboration of:

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1. SOCIAL PRESSURE ON THE ENTREPRENEURIAL BEHAVIOR: ARE NOW THE CITIZENS EXPERTS IN BUSINESS TAXATION?
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## 1. SOCIAL PRESSURE ON THE ENTREPRENEURIAL BEHAVIOR: ARE NOW THE CITIZENS EXPERTS IN BUSINESS TAXATION?

In recent years, the economic, social and political sector, particularly in the countries most affected by the crisis, has changed the existing relation between companies and citizens. From a situation that we could consider of “necessary co-existence” between community and corporations, it has turned to a “**permanent scrutiny**” on companies’ action in their different dimensions: as jobs generators, as value-creating entities for their shareholders, as drivers of innovation and other, but particularly, as business taxpayers to the Treasury.

Austerity policies, together with the existing corruption cases in the political and business world, have turned public opinion into a stern judge of companies’ behavior in the long march towards the economic recovery. All the corporate decisions are evaluated according to whether they favor or harm the weakened public treasury. **At this point, taxes have therefore become evidence of such “commitment to the country” required to businessmen by the society, which is constantly questioned.**

This situation challenges the reputation of companies operating in **many countries with different tax legislation and policies that sometimes can even be contradictory.** Whilst certain governments still opt for protectionist policies, many others choose more liberal alternatives, with laxer regulations focusing on attracting foreign investment.

Moreover, such models are in constant evolution. According to what the **International Monetary Fund** explained in the Annual Report 2013: *“The last decade and a half has seen a concerted effort to develop a set of internationally accepted standards for tax transparency and to monitor and promote their implementation. This period has also witnessed a steady improvement in the comprehensiveness, quality, and timeliness of countries’ public financial reporting. [...] Nevertheless, understanding of governments’ underlying tax positions and the risks to those positions remains inadequate”.*

In light of the increasing complexity in the market and the uncertainty generated due its evolution, **the risk that a company’s reputation is challenged due to its tax contribution has substantially increased.** Facts to be considered are growing, as the potential risks that may affect a company. All of this, under the watchful eye of governments,

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controllers (both national and local) and, of course, the society.

Thus, economic factors are no longer the only aspect involved in the design of companies’ tax planning, companies are increasingly aware of the possibility of being the focus of social attention, like Caesar’s wife. This is, apart from complying with the tax legislation in force, it should become evident that they are helping the economy and not taking advantage of it.

As a result of such social sensitivity, companies’ tax planning is now submitted to a kind of “perfect storm”, **surveillance from three complementary fronts: Government, the media and social networks.**

- **Government surveillance**

In recent times, Governments have been compelled to ask citizens major efforts within their household economy. Such efforts are accepted (at different levels) in return for the rules of the game being the same for everybody, in particular for companies.

In the words of the Vice President of the European Commission, **Joaquín Almunia**, when announcing last February that is investigating certain tax regimes, he wondered: *“how can Governments ask ordinary citizens to accept adjustments and pay the corresponding tax rate if large companies do not do it?”*

In this line, for instance, the Spanish Agencia Tributaria has been quite clear regarding its objectives, with obvious examples of the type of companies that are in its prime focus, by creating the **Oficina Nacional de Taxidad Internacional (ONFI)** or the **Delegación Central de Grandes Contribuyentes**. It has also focused on the Internet, as proven in the statements made by this body when presenting the **Plan de Control Tributario y Aduanero 2014 –Tax and Customs Control Plan 2014–** on the *“control actions over natural persons or bodies’ holders of websites [...] and manufacturers or service suppliers that market their goods or services through the Net”*.

- **Media attention**

The described scenario implies that mass media focus on files created on tax matters to large companies, with which are particularly critical. This has been reinforced by the new paradigm of mass media, in which they **respond to the social request of raising the criticism to the lesser committed companies.**

The called “investigative journalism” has recovered its role, mainly due to the **necessity of appealing and differentiating contents**, which also contribute with an added value to payment information (in paper or

on-line). For instance, the American news agency Bloomberg wrote in February 2014 a critical article “revealing” that one of the main Spanish multinationals has taken advantage of loopholes in another EU country to pay fewer taxes.

Mass media conduct now more than ever **thorough analyses of the results reports and of any document that may contain information on tax schemes**. Reports and accounting documents are now sources of information in which any message may imply a risk to company’s reputation, although their bases perfectly comply with the legislation in force.

- **Discussion on social networks**

The new model of social communication is global and free, it has raised the importance of the “activism in social networks”. This field mixes opinion and mobilization in real time, is critical by default and **focuses especially on large companies whenever its**

**activities can be branded as “lacked of solidarity”**. In certain cases, the criticism had reached an important dimension, thus its eventual impact on corporate reputation has made imperative a reaction, which would has been unnecessary at other times.

The fact that the tax planning of a company comply perfectly with legislation does not eliminate the risk of criticism. Reputational risk continues to exist if the behavior appears to be “not acceptable for society” within the context explained above. The particular difficulty in this field is that many of the people who criticize do not have enough information on the reality of the company at a whole or technical knowledge on tax regulation.

## 2. THE REPUTATION ECONOMY: IS IT NOT ENOUGH TO MEET THE STANDARD?

The “surveillance scenario” described compels companies to take care of some aspects



El País, 18/01/2014

The seven Internet giants pay in Spain only a million in taxes.

El País - Economía  
The big deal of Amazon, Starbucks and Google: not to pay taxes

Eldiario.es, 29/11/2012

“There is no shortage of examples of large multinationals with sophisticated global tax policies, which despite being perfectly legal, are questioned”

which go beyond the mere normative compliance. There is no shortage of examples of large multinationals with sophisticated global tax policies, which despite being perfectly legal, are questioned because at first sight its tax planning seems not to be contributing to local economy, but “taking advantage” of it.

The proceedings opened against prominent companies have certain characteristics that, from the communication point of view, require a professional treatment to minimize the impact on corporate reputation.

- **From the parallel to the circular judgment.** Judicial proceedings started to be also “judged” publicly in the media years ago. The pursuit of “appealing” news occasionally leads to headlines devastating for

companies’ reputation. Many times, the word “guilty” appears as a prior sentence, long before it can be proven.

Since any citizen can give its opinion in an immediate and open channel, as certain social networks, the process is more complex than the classic “parallel judgment” made by the media on judicial landmarks, because between each novelty in a process, there are many discussions, opinions and calls into action against companies. These are made by new and relevant opinion leaders that sometimes have more impact on reputation than the news in the media.

- **High sensitivity.** Topics related to money affairs at any level have become, due to the current economic

EXAMPLE *Change.org Campaign:*

**change.org**

6.953 signatures reached



A graphic for a Change.org petition. At the top is a red circle with a diagonal slash over a pair of scissors. Below this is the text: "Request to Cristóbal Montoro Romero: Say Montoro to cut in tax fraud, not in social investment #RecortaelFraude". At the bottom, it says "Petición creada por Alianza Española contra la Pobreza".

32.177 signatures reached



A graphic for a Change.org petition. At the top is a photograph of a hand holding a gold bar. Below this is the text: "Request to every European institution, national and local governments: Citizens demand actions against #corrupción and the secrets hidden in #Suiza". At the bottom, it says "Petición creada por #TrustCM TransparencyNow! Eto Suizos, Bélgica".

“Calls into action against companies, made by new and relevant opinion leaders, have sometimes more impact than the news in the media”

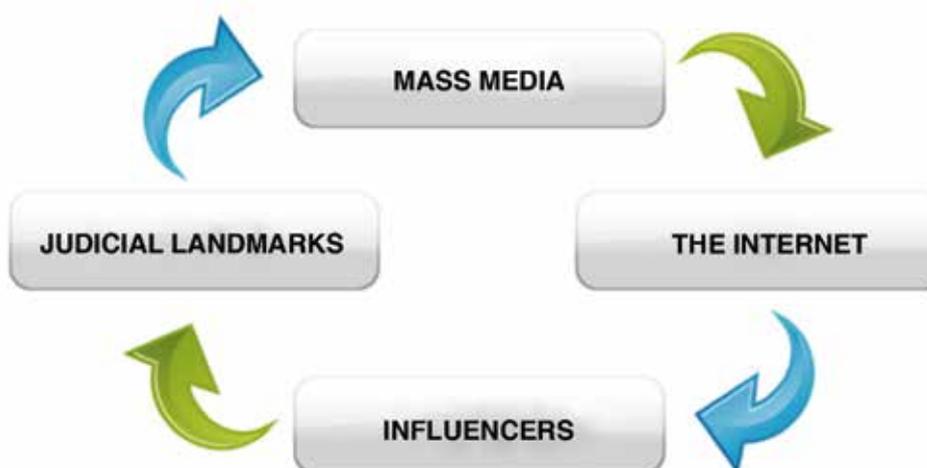
juncture, a high sensitive element for citizens. Although the called “spiral of silence” that led to silence minority voices has lost strength in recent years, generally very few stand up for a company when it is undergoing a process on tax matters. A wide part of society tends to publicly condemn any trace of tax abuse by large companies, despite it might not be real or proven, unless he has many powerful arguments showing the opposite.

- **Intensive surveillance.** The need to generate news by the media sometimes leads to stages of “intensive surveillance”. Until recently, open proceedings against companies had high audience peaks when there was a judicial landmark, while the rest of the time, during off-peak stages, had scarce visibility. Nowadays, audience peaks are prolonged beyond the landmark instead, and

new impacts on the media are observed –despite the scarce new content– due to the social sensitivity explained above.

- **Risk of leakage.** Some of the most relevant cases of previous months have proven that secrecy in summary proceedings is not always respected, thus proceedings of high-interest for the press generate many novelties by “sources close to the proceedings”. It is a fact to be taken into account due to the reasons aforementioned.
- **Positive resolutions do not get the same degree of attention** than the opening of proceedings or any action against companies. They should communicate directly with their stakeholders when a favorable final ruling is obtained, because the press and the social networks will continue to focus on those which are suspicious.

Those factors clearly influence the challenge that the commencement of any action related to their tax planning by tax or judicial authorities represents to the reputation of a company. The social and media scenario, and how the company acts in this field, apart from the communication management that the company does during the process, will mark the impact that may have on its reputation, and consequently on its outturn account. Yet, there is no need to leave everything to the time of crisis. In this scenario of



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public sensitiveness, companies have the chance to show the significance of tax contribution they made and the positive impact it has on the public Treasury.

### 3. WHAT CAN COMPANIES DO FACING THIS CHALLENGE?

Once taken the existing high risk scenario to certain profiles of companies and complex tax schemes, there are two differing fields where companies should work in parallel and concertedly in order to minimize the impact on their accounts and reputation: **an adequate communication management and a successful legal strategy.**

#### In legal and technical terms

A successful legal strategy requires an initial analysis on the possible questioning that a given tax planning might face, as well as an on-going review of such analysis, since the risk associated with a structure or transaction may vary substantially over the years.

Among the factors that may alter the possibilities that a structure can be questioned are, on the one hand, the ones that we describe as “traditional”, which are derived from the application of administrative doctrine and jurisprudence of law courts. In fact, it is clear that nowadays both have imposed plainly to the modification of standards as a review mechanism. It is possible therefore that the doctrine and jurisprudence

evaluated after the decision-making, alter the parameters over which the decision was taken in a certain moment.

On the other hand, and as a novelty of increasing significance, there is a whole set of guidelines, which are described as “soft law” –since they are not standards in the actual sense of the word, but criteria evaluated by bodies as diverse as the European Commission, the Committee of Tax Affairs of the OECD or the G-20, just to mention the most relevant–, and have an increasing influence both in applying the standards and, of course, regarding certain structures that may have been created before the publication of the guidelines.

Therefore, it is essential to carry out nowadays an on-going monitoring of the judicial and tax strategies and the potential risks associated to them, which will allow the companies to take the decisions required in any given moment, according to the situation.

#### In communication: prevention and management

It is important to consider that the tax planning represents a powerful competitive tool, thus a disclosure of a whole tax plan can endanger the current and future business of a company.

With such limitation, companies should be able to give a satisfactory explanation for the questions posed by relevant publics and the society, with a couple of characteristics which are apparently contradictory: it should be simple enough so

“The common factor of good managements is a thorough preparation before the risk turn into crisis”

that all the stakeholders (who usually do not have technical knowledge) understand it, as well as detailed and specific enough not to be questioned by experts or leave too many questions unanswered.

Once the explanation is defined, success will be determined by giving such explanation to each audience in the adequate moment, format and channel, after a proper analysis of doubts and criticism linked to each audience.

Additionally, as we have seen from experience in multiple similar cases, we should highlight that the common factor of good managements is a thorough preparation before the risk turn into crisis. The sooner the companies at risk are prepared for such contingency, the lesser the impact of a possible proceeding before the tax authority will be on their reputation. You will find certain keys related below:

- **Systematic risk monitoring.** Being aware of market trends, knowing what it is said in main forums –but also in small niche areas–, understanding the weaknesses. In a nutshell, conducting a systematic risk analysis to know which are the weaknesses of the organization, and the relevance

and likelihood of becoming reality, not only in the media, but also on the Internet or in parliamentary activity.

- **Comprehensive view in the management of the process.** The possible crisis situation derived from the opening of a proceeding, the leakage of an investigation by tax authorities or the commencement of any other action with legal repercussions should be always managed with the broadest view. Every company’s dimension can be affected, which forces to extend this management to every stage of the relation with stakeholders. It would be a serious mistake to think solely in the response to the media, or to restrict the explanations to tax policies, without placing it within the global corporate context.

In conclusion, both professionals of tax planning and those in charge of managing the relation of a company with its relevant audiences, face a major challenge to demonstrate that companies are always part of the solution when we speak about financial contribution, even when it may appear the opposite. The previous experience and the professional support can be then the key to success.

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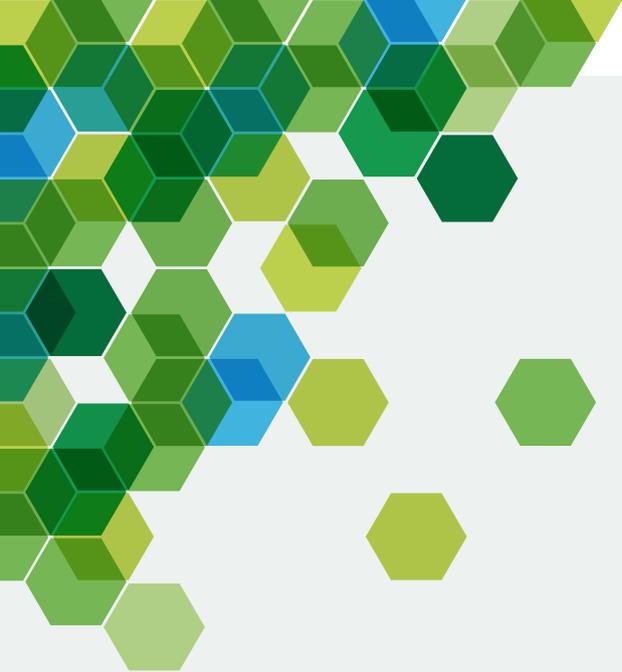
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