Chief Tax Officer Outlook

Top-of-mind issues for tax leaders — fourth global edition

April 2017

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Never before has the tax department played such an integral role in the success of the business. CTOs and other tax leaders are expected to align tax with business goals, drive strategic value, increase transparency, and improve the efficiency of tax operations. This publication is designed to highlight top-of-mind issues for tax executives and the ways tax leaders are addressing these opportunities and challenges.

Topics addressed in this edition[1]

- **Tax reform and international competitiveness: are we all on the same page?**
- **Regulations under section 385**
- **Tax disputes on the rise globally**
- **Tax department benchmarking offers key insights**
- **Senior management communications: real-time updates**
- **Responsible Tax: how can tax leaders confidently join the discussion?**

[1] This report was first published as 'Chief Tax Officer Insights' by KPMG LLP in the US, a limited liability partner and the US member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"). In its current form, the report has been expanded upon to provide a global context and address audiences in addition to those in the US. As with the original report, the information throughout is based on discussions between KPMG professionals and CTOs, as well as with government contacts.

Tax reform and international competitiveness: are we all on the same page?

In an age of increased global competition, the time is now to pay close attention to changes in corporate tax reform. We've recently seen various countries take different approaches to this topic. In turn, the level of international competitiveness within these countries will greatly differ.

Swiss tax reform

In Switzerland, multinationals have been paying much less than what they would likely have to pay in countries like the US, Japan, France, the UK and Germany. This has allowed Switzerland to be seen as an attractive hub for multinationals, holding companies and domiciliary companies. The recent corporate tax reform put forth a recommendation to increase the tax rate that these companies are paying. On 12 February, 2017, this reform was rejected in a surprising vote by the Swiss people. Until further notice, the tax rate that these larger companies pay will remain the same. However, with Switzerland operating on the policy that specific cantons can create their own tax systems, we will likely see a range in the tax rates offered across the country. Tax leaders must be aware of this when doing business across the country as the taxes they are obligated to pay will likely differ between cantons.

How does this affect global competition?

With uncertainty in Swiss tax policy, international firms may be hesitant to invest in the Swiss market until they are sure of the implications. With the chance that these firms may allocate their investment elsewhere, Switzerland may lose its competitive edge to another country.

US tax reform

Tax reform in the United States seems to be taking an opposite step. In June 2016, the House Republicans released their GOP 'blueprint on tax reform' that could lower the corporate income tax rate to 20 percent. An important feature, however, is the proposal to apply this tax only to imports and exempt exports. This is seen by Blueprint's proponents as a strong anti-base erosion measure and a proposal that would provide parity in the US with value added taxes employed by US trading partners. Donald Trump's campaign borrowed heavily from the Blueprint suggesting some consensus from the incoming Administration and Congressional Republicans. Not surprisingly, under Trump's new regime, there are plans to roll out a comprehensive tax plan including tax rate cuts for individuals and businesses.

? Questions to consider

— Will this spark a trend for corporate income tax to be on a steady decline across most countries?

— Is a country's corporate income tax rate the leading factor in determining their level of global competitiveness?

What about Brexit?

Well it's not a tax reform per se, but now that the UK government has officially started the countdown to the UK leaving the EU, companies are asking about the impact of customs duties and withholding taxes, leaving some to consider whether they should relocate operations to other EU countries or wait and see.

How does this affect global competition?

Many tax leaders are wary that this will deeply effect international competitiveness. The most immediate effect of these concerns has been the slowing or stopping of repatriation activity. Border adjustability could ultimately lower global competiveness and drive tax inequality between industries.

The next few months will be quite telling as we see how each Swiss canton approaches their corporate tax policy. Will Switzerland remain a hub for international investment and an attraction for multinationals or will we witness a change to its competitive edge?

Will the US be successful in boosting their economy through local production incentives and how will this affect its trade relations?

It will be important for tax leaders to stay ahead of these changes when evaluating movements in the operations of their companies and future investment plans.

Regulations under section 385

CTOs and other tax leaders have had a significant focus on section 385 recently with the release of the proposed regulations by the US Treasury and IRS in April 2016 and the final and temporary regulations in October 2016. As proposed, the regulations would have dramatically changed the treatment of cross-border and foreign-to-foreign intercompany debt. There were also potential difficulties for a number of current business practices, notably cash pooling, and an increased level of loan documentation required. The general sentiment of the proposed regulations was that they were rushed, overreaching, and highly politicized, with many believing the potential effect could be crippling to multinationals.

CTOs and other tax leaders took a number of steps to decrease the potential impact of the proposed regulations, including communicating with Treasury, compiling intercompany debt inventories, and conducting significant lobbying efforts. Many who typically avoid direct lobbying measures wrote comment letters signed by their organization's treasurer and CFO. Tax leaders were also meeting with contacts in Congress, the Senate and the IRS, and working with a range of trade groups. Internally, tax leaders focused communications efforts on explaining the proposal's impact to treasury teams, and many briefed senior executives, boards, and audit committees.

The final and temporary regulations address a much smaller universe of debt, and the changes to the proposed regulations have been welcomed by CTOs and other tax leaders. The changes in the final version mean the regulations are now targeted at base erosion concerns by US debt issuers, rather than massive changes around debt and equity for tax purposes. The largest change is the foreign issuer exception, which means that any debt issued by a foreign corporation will now fall outside the 385 regulations and the documentation and re-characterization rules. The final regulations also remove many of the initial concerns around cash pooling.

Because the US federal tax rate remains one of the highest in the world, non-US groups have historically leveraged their US operations to the extent permitted. The regulations continue to address such leverage, and thus continue to be a key risk item for non-US groups.

Questions to consider

- What practical steps are you taking in terms of 385 compliance?
- How are the US presidential election results altering your approach to section 385 regulations?
- What is your main concern regarding the impact of the 385 regulations?

Tax disputes on the rise globally

Companies around the world are seeing a significant rise in tax audits and disputes, and all signs point toward even more intense tax authority activity in the future. KPMG International's Global Tax Disputes Benchmarking Survey 2016 reveals steadily rising tax controversy as financially strained governments press for more revenue and media and public attitudes harden against perceived corporate tax avoidance. As a result, audit activity is rising across the board, from direct taxes and indirect taxes to employment and domestic compliance issues — and international tax in particular.

One factor fueling international disputes is the Organisation for Economic Co-operation and Development's (OECD) work on curbing tax base erosion and profit shifting (BEPS). With the proposals complete, countries worldwide are now putting them in place. From broader requirements for tax transparency through more stringent transfer pricing policies to greater scrutiny of business substance, the changing rules open the door to considerably more tax disputes — especially given differences in interpretations and timing as countries translate them into domestic laws.

International tax issues are by no means the tax authorities' only focus. The majority of the survey respondents also report more audit scrutiny related to direct taxes, indirect taxes and domestic compliance issues (e.g. income, expenses, reliefs).

The survey also confirms that behavior is changing among tax authorities worldwide. Feedback from tax executives suggests tax authorities have changed and intensified their approach, making them increasingly difficult to deal with. In this environment, it is not surprising that, over the past 3 years, survey respondents noted:

— more frequent requests for information

— more audit queries from tax authorities

— more aggressiveness in raising assessments

— more difficulty resolving disputes

— harder lines being taken by tax authorities in negotiations.

? Questions to consider

— Are you experiencing more audit scrutiny compared to years past?

— Is the level of difficulty in reaching resolutions with the tax authorities you deal with increasing?

— Are you seeing a rise in penalty amounts being applied?

— Is tax technology an area you are looking at closely?

Tax dispute management tips

In light of swelling levels of tax disputes and the significant reputational and financial losses they can cause, some forward-thinking companies are investing in processes and resources to strengthen their tax dispute resolution functions. For example:

— Twenty percent of the respondents have a specific group that handles tax audits and disputes exclusively, which can ensure the companies tax disputes are managed by dedicated, adequately staffed teams of professionals with experience relevant to the company and its industry.

— Two-thirds have an established internal process for managing and escalating tax disputes, which can ensure accountabilities are clear and promote consistency, quality and efficiency in tax dispute management activities, locally and globally.

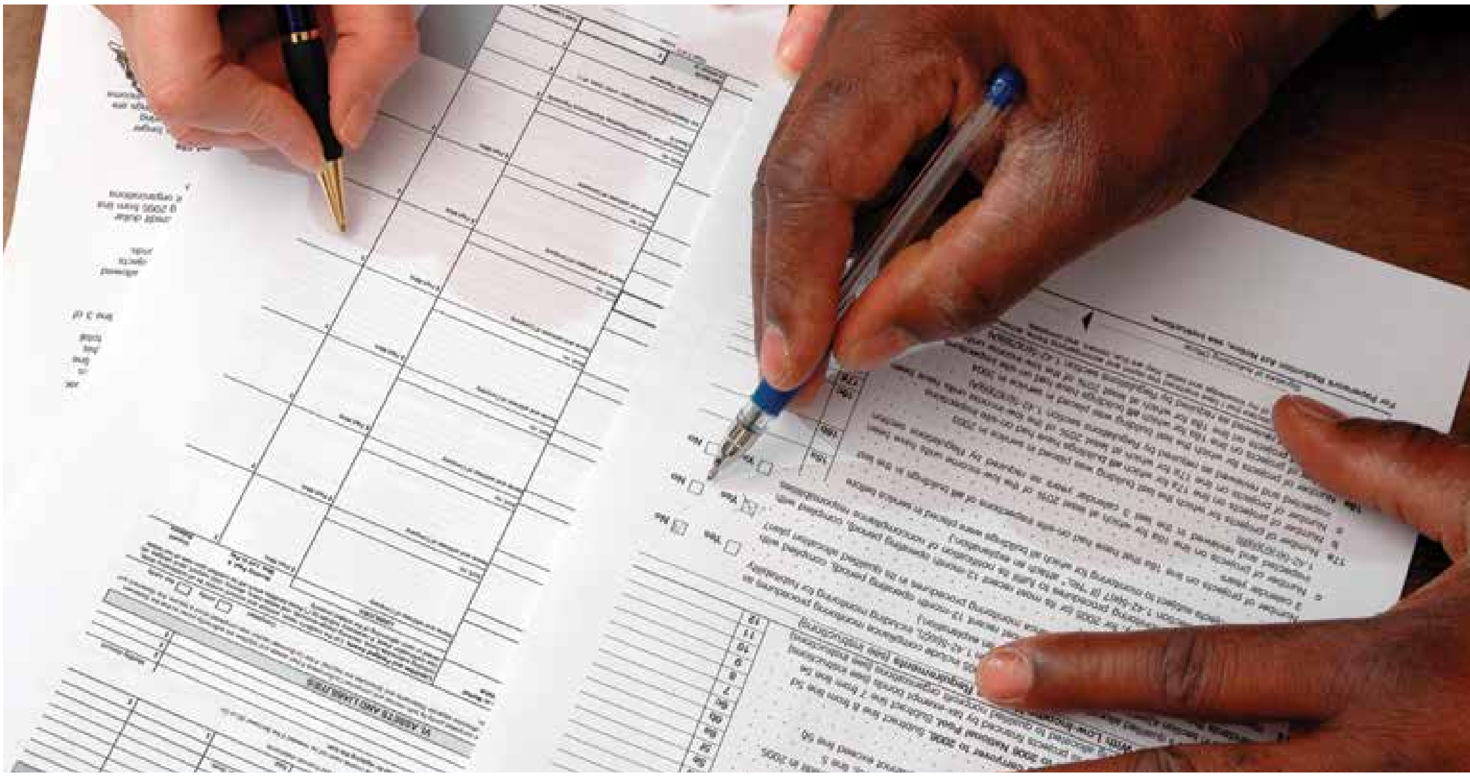
— More than half have a budget dedicated to tax dispute management, which can ensure all of the company's dispute management needs are covered and give the dispute management team some control over how the funds are deployed and invested.

Under 10 percent have a global head of controversy or equivalent who is responsible for the day-to-day management of tax disputes and who can help the dispute team to clarify accountabilities, centralize tax dispute monitoring and controls, provide strategic direction, and communicate with the board and senior management. Centralizing company-wide responsibility for tax disputes under one leader is expected to become a leading practice in the years to come.

Visibility is also key to identifying issues early in the process and developing a litigation or controversy strategy. A worldwide tax audit management software platform can deliver a complete view of all current disputes, as well as potential disputes in the pipeline, allowing dispute management teams to follow and compare cases and developments from country to country. This technology can also help reveal systemic issues within the organization that are giving rise to disputes and ensure the lessons learned are shared across the global organization's transfer pricing and compliance teams. While such systems are not yet widespread, about 40 percent of respondents expect their use of technology for managing and monitoring tax disputes to change in the next 2 years.

Tax dispute management take-aways

- Aggressive tax authority activity has been steadily rising and is expected to intensify in the coming years.
- Global tax department leaders say tax authorities are:
  - requesting more information from businesses
  - conducting more audits and taking longer to conclude them
  - increasingly reluctant to negotiate a settlement
  - moving more matters forward to litigation.
- All tax issues are coming under more audit scrutiny, with particular attention being paid to international tax issues.
- As tax authorities get better at risk assessment and share more information with other tax authorities, there is an increased potential for more aggressive tax adjustments, with a commensurate increase in the potential for tax controversy.
- Forward-thinking companies are investing in processes and resources to strengthen their tax dispute resolution functions.



Tax department benchmarking offers key insights

As a seasoned tax leader, you make key decisions every day to evolve your tax department in order to keep pace with unprecedented pressures, disruptive technological advancements, heightened compliance obligations and more — all while continually demonstrating value within your organization and beyond. Benchmarking against comparable tax departments can be a powerful tool for reflecting upon the department you have today, and thinking about how you will transform it for tomorrow.

An ongoing KPMG International study of tax departments around the world includes input from more than 300 tax leaders in terms of governance, priorities and performance measures of tax departments today. While the study continues, the data so far reveals some telling insights.

What do the current results tell us? Compliance and risk management are clearly top priorities for today's tax leaders, and the tax department's contribution to strategic value for the organization now seems to be overtaking priority over cost minimization in many areas.

Looking ahead, companies appear more-or-less satisfied with their current sourcing models but less satisfied with the ability of their companies' systems to provide meaningful tax data and insights. Most respondents expect their companies to invest more in technology changes in the years ahead, with the majority expecting to invest directly in tax-specific technology.

Questions to consider

- How do you benchmark against peers in terms of structure, resources, budget, etc.?
- Are you gaining the tax data you need from your company ERP?
- Does your department have a documented tax strategy in place?

Other highlights:

- Globally, most tax functions still fall within the finance function, although a significant number are independent. About one in 10 heads of tax report to the CEO directly.
- Many companies are moving toward greater centralization of tax resources and activities, especially in the area of transfer pricing.
- Companies may have opportunities to centralize accountabilities and activities further — for example, through greater use of shared service centers or other centralized sourcing models.
- Many companies have recognized and responded to the need to demonstrate strong frameworks for tax governance and risk management.
- Most tax leaders recognize the need to invest more in tax technology in the next 5 years.
- Over half of respondents have some form of documented tax strategy. Tax compliance, risk minimization, tax reputation and group tax rates are the most important objectives within the tax strategy's scope.
- Half of tax departments surveyed are well involved in operational business planning/business strategy, and this involvement has increased in the past 2 years in the majority of cases.

The KPMG Global Tax Department Benchmarking Survey is an ongoing initiative that is creating a comprehensive database of benchmarking insights for tax leaders around the world. Findings are updated regularly, and the survey remains open to tax leaders. You can learn more about the initiative, view the results to date and take part in the survey at kpmg.com/taxbenchmarking.

Senior management communications: real-time updates

Tax leaders around the world appear to be having more regular, real-time updates with senior management. One way they are approaching their leaders is with risk and opportunity scorecards that are updated monthly or quarterly. The updates are based on regular meetings between tax, financial planning, and other groups. One potential drawback of this approach can be that goals set by the tax leader can turn into expectations, which can diminish delivery achievements.

The reporting tools are sometimes referred to as a Tax Saving Report Card or a Tax Value Report. Given to the CFO, CEO, and the board, tools like these can address topics that are important to the organization and shows the value the tax department can bring.

In the recent KPMG International Tax Department Benchmarking Survey, tax leaders surveyed indicated that, while an overall effective tax rate is still important, management of risk, accuracy of returns and avoidance of penalties are considered even more important measures of their tax departments' performance.

Perhaps for this reason, more tax leaders are reporting on a broader range of criteria than they might have in the past, and tailoring their reports based on the interests of key stakeholders. For example, in terms of content on the scorecard, many tax leaders indicate that senior management interest appears to be most focused on cash tax savings and overall risk, while audit committees are felt to have broader interest in the general tax environment, including topics such as tax reform and the expected impacts, reputational risks and market trends.

Questions to consider

— Do you have a formal dashboard for meetings with senior leadership and how often do you review and display progress on these metrics?

— What metrics are your senior leadership most focused on today?

— Has the frequency of your meetings with leadership increased?

Responsible Tax: how can tax leaders confidently join the discussion?

As the world becomes more interconnected, discussion about who pays taxes, how, and when is likely to intensify. Though domestically developed and administered, tax is a global reality, and the evermore connected nature of the modern economy means tax now demands a global conversation and, where appropriate, global action.

Tax will always create a lively debate and differences of opinion. The issues become more complex in a global economy as different cultures have varying attitudes towards tax.

Yet, the Action Plan recommendations from the Organisation for Economic Co-operation and Development to eliminate BEPS and subsequent worldwide uptake by governments in response to the recommendations (even in non-OECD countries) is testament to the appetite for more consistent frameworks through which to address tax.

Meanwhile, tax leaders are, now more than ever, being called upon to help drive these conversations within their organizations, and to be able to articulate the organization's tax narrative externally in terms of the ways it aligns with the values of the organization, while contributing positively to society and also adding value to the business.

Understandably, some tax leaders may feel uneasy about their abilities to balance this message, particularly against the backdrop of the moral and political implications surrounding the tax debate. Some leaders, however, are starting to invest time in building their acumen in the areas of media and community relations and deepening their communications skills in order to confidently articulate their positions.

An informed discussion about Responsible Tax needs the voice of everyone involved in the debate — from governments to taxpayers to tax professionals and the larger civil society. The time is now for tax leaders to take the necessary steps to stay engaged in this conversation as it remains at the forefront of the global tax landscape around the world.

Interested in being part of the discussion on Responsible Tax? We welcome your thoughts. Join the conversation here responsibletax.kpmg.com/home.

? Questions to consider

— What tools do you need to start the conversation on Responsible Tax at the boardroom table?

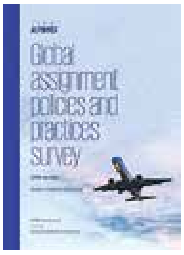
— How do you stay engaged in the conversation on Responsible Tax?

— Do Responsible Tax and tax transparency go hand-in-hand?

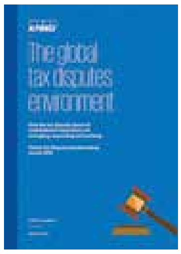
Further information

For further information and resources, please explore the links or visit kpmg.com/tax. You might also consider attending an upcoming webcast or event designed to address issues of interest to tax leaders. As always, please feel free to contact a KPMG professional to discuss these strategies and tools, or to speak about the tax issues you face today.

BEPS Action Plan: Taking the pulse publication series



Global assignment policies and practices survey



Global tax disputes department benchmarking

Global tax department benchmarking

Getting down to business with indirect tax

Notes

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Designed by Evalueserve.

Publication name: Chief Tax Officer Outlook — fourth global edition

Publication number: 134293-G

Publication date: April 2017