Managing Tax Risks: The Role of the Board

A top – down approach

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Tax risk management
A high level responsibility

- Intense public and private-sector scrutiny and demand for increased transparency has pushed tax risk squarely into the spotlight
- Factors such as rapid globalization are fuelling the calls for changes in tax operational strategy and execution across multiple jurisdictions
- Additionally, publicized tax accounting improprieties have made key stakeholders increasingly aware of the need for high-quality data computation and transparent tax planning and reporting processes
- The global recession and credit crisis has also made appropriate tax planning to conserve and manage cash a priority for all types of taxes
- Top company executives are faced with the responsibility of effectively managing tax risks facing the business, from the top down
- Tax is here to stay and the Board ignores it at its own peril

Tax risk
The need to manage it

- Staying abreast is a perennial challenge
- Cross border expansion is increasingly complex in all aspects including tax
- If left unmanaged one runs the risk of lagging behind and potentially losing the competitive edge
- The Board as final decision maker must understand the risks
- Intricate understanding of the issues that impact strategic decision-making and long-term success is critical

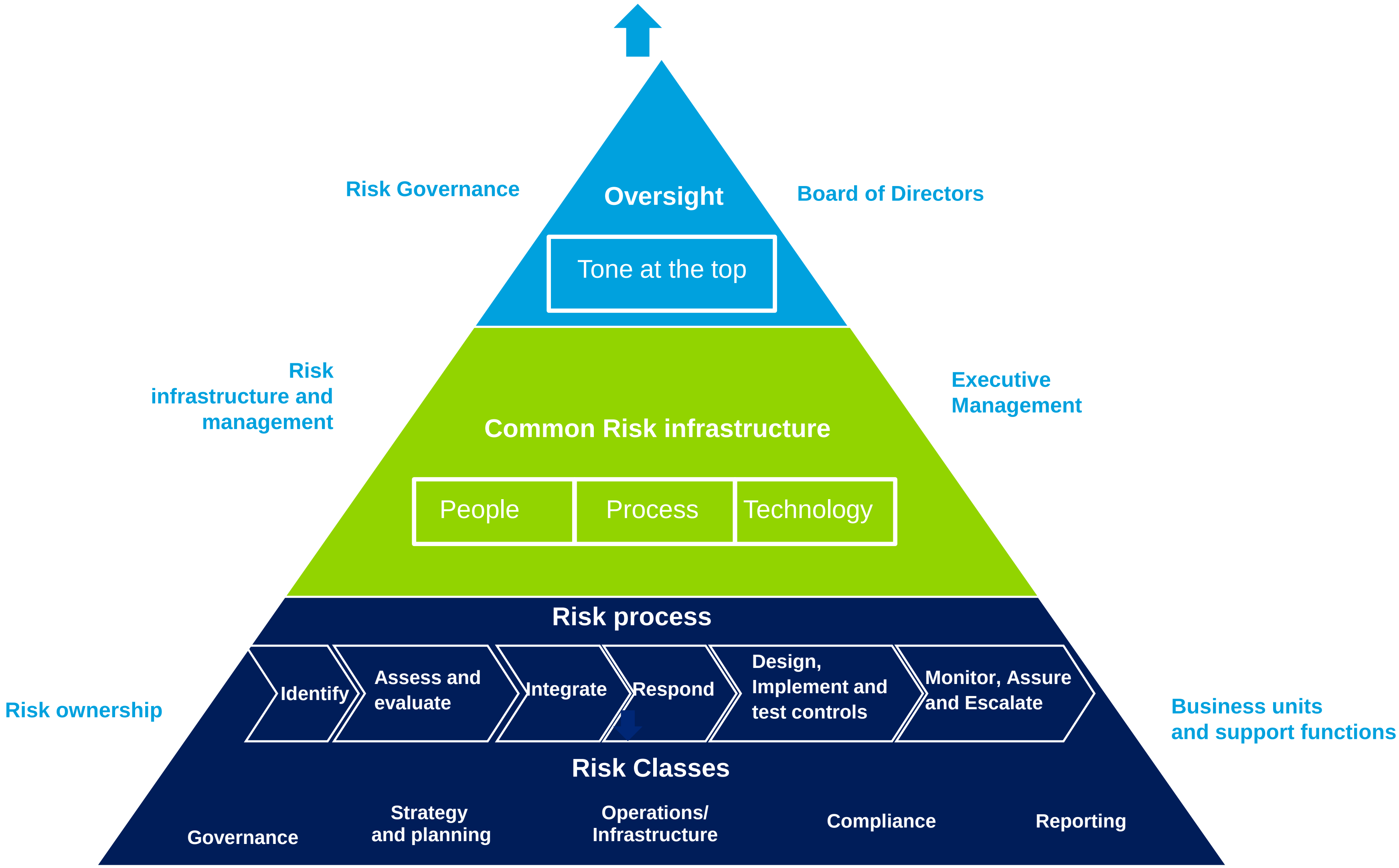
The changing scope of the tax function

- The tax function is evolving beyond its traditional reporting role
- Compliance issues have become more intricate and pressing
- The risk and cost of non-compliance is increasing
- Evolving and more complex legislation increases the risk of additional exposure
- Controls and processes throughout the enterprise needed
- Managing operational and cash-flow risks is critical
- Proactively seeking out which business decisions have significant tax impact
- The need to actively involve business units and the Board

The tax revolution

- Tax matters have always been on management's and the board's radar
- The traditional approach has been towards compliance issues with regard to potential downside tax implications
- Customarily, corporate tax is focused on avoiding penalties, assessments, and overpayments
- However, there is increasing interest in tax as a value contributor
- The trend is now to pursue value, in addition to mitigating risk through appropriate tax planning

Tax risk can arise at all levels of the organisation



Developing a tax risk framework

- Use a Risk Intelligent approach to tax not only to manage compliance risks but to build appropriate tax planning benefits

- Effective risk management depends on solid leadership in three areas:

  ✓ **Risk governance**: This includes strategic decision-making and risk oversight led by the board of directors

  ✓ **Risk infrastructure and management**: This includes designing, implementing, and maintaining an effective risk program, led by executive management

  ✓ **Risk ownership**: This includes identifying, measuring, monitoring, and reporting on specific risks, led by the business units and functions

- To effectively provide the leadership needed in effective risk governance, the board of directors need to ensure that the organisation has an appropriate risk framework in place

Developing a tax risk framework
Points to consider

- A strong framework for tax risk assessment and management can give the board a comprehensive snapshot of specific tax risks

- An in-depth framework sets guidelines, establishes metrics, and prescribes processes that potentially can help the board

- The use of an effective tax risk management framework can help companies develop policies, procedures, and processes that support the appropriate vetting of tax issues and help the tax department effectively communicate tax issues to top management and the board

- A strong tax risk management framework also actively supports efforts to achieve sustained compliance with tax-relevant laws and regulations

Managing tax risk
The Role of the Board

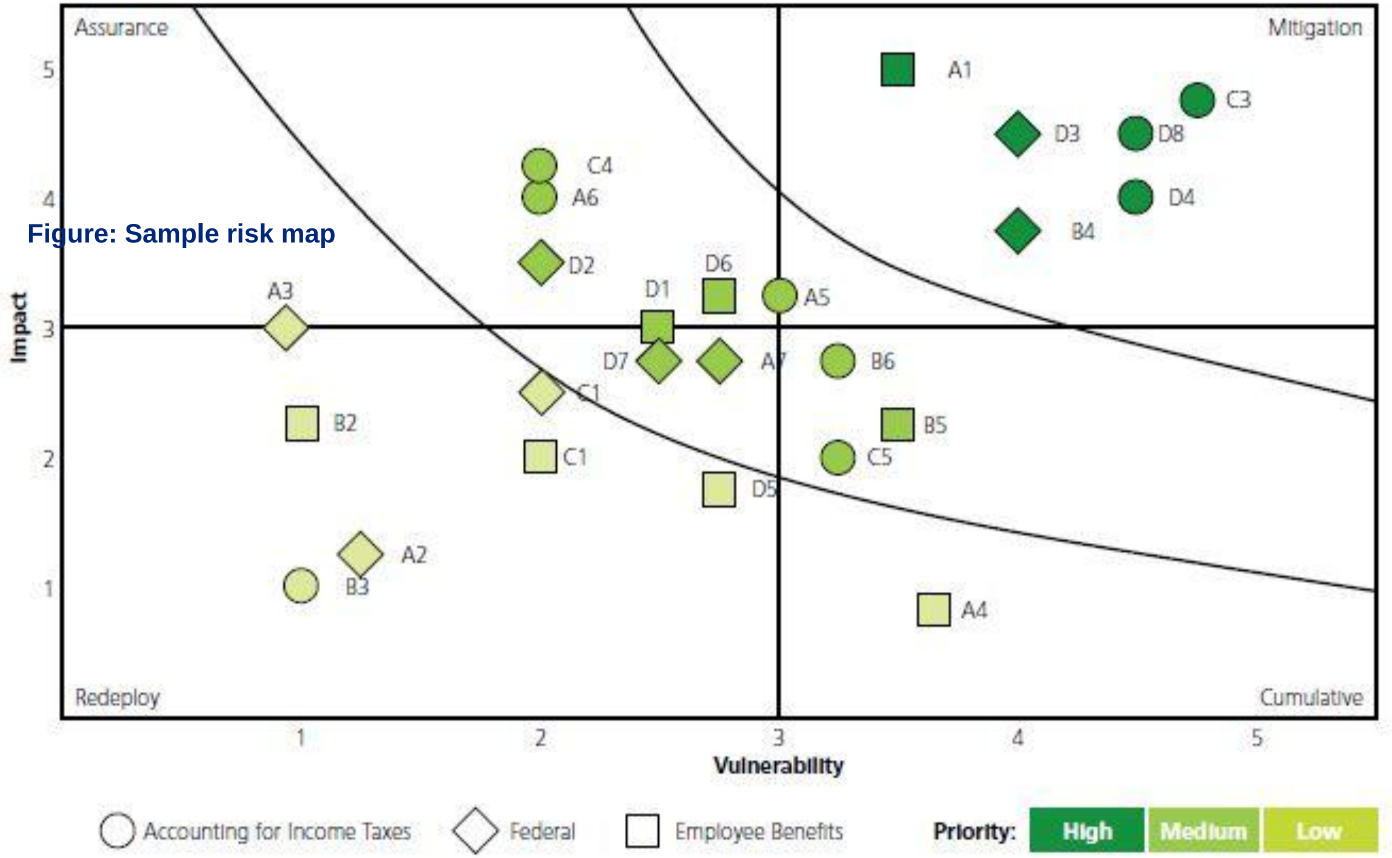
- Boards are under pressure
- Board members are unsure how to approach their risk-related responsibilities
- Steps the board can take to ensure that tax risks are being adequately addressed include:
- **Talk about it**
- **Team up with management**
- **Assess risk performance**
- Periodically assessing tax risks and seeking explanations
- Consider risks related to the following six areas:

1. **Operational**: planning and strategy
2. **Compliance**: process, technology, and positions
3. **Legislation**: governance and budget
4. **Deals**: corporate events and major transactions
5. **Corporate structure**: international tax presence
6. **Operations**: day-to-day processes, automation, and management decisions

Developing a tax risk framework
The Role of the Board

- Having identified and structured the risk use a Risk Map to:
  - ✓Outline the level of vulnerability to a tax risk as well as the potential impact
  - ✓Categorize the risks by tax type, department or entity

Figure: Sample risk map



Developing a tax risk framework
The Role of the Board

- A risk map assists in monitoring the effectiveness of risk management activities

- After identifying pressing risks, mitigation strategies can then be considered, weighing the costs of remediation against such overall risk factors as:
  - Tax risk category
  - Potential impact
  - Likelihood
  - Urgency
  - Mitigation strategy
  - Mitigation benefit (ROI)
  - Estimated cost to mitigate (as available)
  - Resources

- **The end result**: a systematic blueprint for tax risk mitigation that incorporates perspectives from both tax and the business and that is aligned with the company's overall risk management and strategic goals

Effective risk governance example:

The Risk Intelligent board partners with tax to provide top-down guidance

- A multinational company was struggling with an inconsistent set of global tax control processes and the absence of a global tax risk profile
- This lack of standardization across the global tax function not only contributed to inefficiencies, but kept tax from focusing on value-adding tax opportunities or proactively managing the criticism the tax function was receiving
- To drive greater standardization, the company developed global tax governance policies, controls, and procedures that drew on a benchmarking analysis of current corporate practices in tax policy, information, and risk management disclosure to both internal and external audiences
- After seeking and obtaining approval from the board and other major stakeholders, including tax authorities, the company then developed a tax operating model to execute the new governance policies, controls, and procedures
- This model articulated how the various groups in the global tax function would work together to execute their defined responsibilities, prescribing processes and tools to help the tax function connect with essential people, processes, technologies, and tax data, including tools to help identify and evaluate value-adding tax planning ideas

Effective risk governance example:
The Risk Intelligent board partners with tax to provide top-down guidance

The results

The benefits of the company's effort included:

- An agreed-upon tax risk management program that enhanced the board's confidence in tax risk management effectiveness
- Greater tax function efficiency due to enhanced access to essential high-quality information, people, and tools, as well as increased task standardization
- Improved clarity around accountabilities and delegations of authority
- Enhanced ability to identify and pursue value-added tax opportunities for the business