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FROM THE INSIDE OUT

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Tax & Corporate Transformation

Tax planning and tax performance improvement efforts are more important than ever in light of policy and technology disruption

Tax planning has never attracted so much controversy or been so critical to corporate transformation than now. Whether the issue is the increased reputational risk for companies that are not perceived to be paying their fair share, or the unfair competition posed by tax havens, or President Trump's flagship program of tax reforms in the U.S., corporate taxation issues are enjoying a high profile. New technology has also made tax arrangements more transparent. Boards and tax departments are challenged with addressing all these changes simultaneously.

This disruption has layered additional complexity to the fundamental role of tax planning, which is to allocate assets and place people and knowledge in the most tax-efficient way possible in order to maximize capital. This creates countless tax planning and tax operational improvement opportunities for organizations.

"If you're changing your operational model, you're changing the way you do things from a tax perspective," says Ernesto Perez, Managing Director and global leader of Alvarez & Marsal's Taxand practice. "It's a value component and an efficiency component of any transformation. If done in the right way, it can free up capital to achieve business goals. Furthermore, driven by the continuously evolving tax legislature, digitization, data analytics and process automation, internal tax organizations create 'white space' and open countless opportunities for value creation," adds Perez.

A global re-set in tax

Boards and their advisers must adapt to the new reality: technology is changing both the way compliance is monitored and disrupting business models to the extent that governments around the world are re-examining how companies should be taxed. The recent U.S. Supreme Court decision on the Wayfair case, which considers the duty of online retailers to collect state sales taxes, is a prominent example.

Over the last five years, governments have also worked hard to eliminate the tax advantages offered by jurisdictions such as Ireland and Switzerland and to increase transparency about where companies generate revenue, guided by the OECD's "base erosion and profit shifting" (BEPS) recommendations. Apple this month paid €14.3 billion ($16.7 billion) in back taxes and interest to Ireland, following a ruling by the EU that the company's tax deal in the country contravened European law.

The reputational risk of perceived tax avoidance is still less acute in the U.S. than in Europe, however U.S. companies face another form of uncertainty: they are still waiting for guidance to clarify parts of the sweeping tax reforms brought into law on January 1, 2018.

"We've seen a global re-set in tax," says Perez. "The same advantages are not there, so we have to be more purposeful in order to accomplish what we want to achieve, and within a different set of rules."

One way to do this is to ensure there is a degree of substance to tax planning decisions: there has to be a demonstrable link between where value is created and where tax is paid. Companies can no longer have one person in an office in Luxembourg and say 80 percent of their revenue comes from there, for example.

"As long as companies are willing to move regional headquarters, add capital and add manufacturing, then a lot of possibilities still exist – and a lot of multinationals today are doing that," says Perez.

M&A activity also provides companies with an opportunity to re-think their operations. This prompts them to think more critically about where they locate intangible assets, intellectual property (IP) and people, as well as take tax incentives and tax rates into consideration more often.

“We haven’t shied away from being creative in how companies can maximize their tax footprint and overall operating model,” Perez adds.

Repatriation questions
For U.S.-headquartered multinationals, one of the most significant changes in this year’s tax reforms was the elimination of deferring tax on foreign earnings until they are brought back into the country. From the point of view of transforming operations, there are two key questions:

1. How do you redeploy that capital (Moody’s estimated that Apple, Microsoft, Cisco, Oracle and Google parent Alphabet held $594bn in cash outside the US at the end of 2017)?; and
2. In the longer term, how does this change your operating model? Will U.S. tech companies continue to keep IP in Ireland, for example?

Awaiting further guidance from the U.S. government, companies are in “wait and see mode,” says Perez, adding that he does not expect a mass bringing back of IP. “Multinationals are operating across Europe, Asia and Latin America, and they need to be close to their markets,” he says. Political uncertainty also remains about how corporate tax rates, cut from 35 percent to 21 percent, would be treated under a different Congress or president.

In the face of such a degree of high-profile change, tax departments themselves are being disrupted: from ensuring compliance and answering questions as they arise, they are now looking at ways to automate compliance tasks and evaluating paths to work more pro-actively with outside advisers and the Board. The good news is, senior executives want to hear what they have to say:
“For the longest time, tax took a backseat at Board-level discussions,” says Perez. “However, it’s become a forefront issue now - Boards don’t want to be caught by surprise. Complexity creates real opportunities. “In addition to looking for value add using our traditional tax technical toolbox, we now also have the opening to play a role in cost takeout and optimization of the tax organization.”

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GOT A QUESTION? CONTACT AN INFLUENCER
ANSWERS ARE ONE CLICK AWAY

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