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Role of reputational risk in tax decision making by large companies

Dr Catriona Lavermicocca¹ and Dr Jenny Buchan²

Abstract

Companies are increasingly expected to contribute to the tax revenue in countries they operate in. This article explores the relationship between reputational risk and aggressive income tax decision making in large companies, focusing on the role of the tax risk management system. It shows that few Australian companies use a comprehensive definition of tax risk that includes reputational risk and that shareholders do not play a significant role in the determination of a company's tax risk profile. This article contributes to an understanding of the relationship between reputational risk and tax aggressive decision-making and the limitations in current tax risk management systems in their ability to consider this relationship in development of tax strategy.

Key words: tax aggressiveness, corporate social responsibility, companies, reputation, shareholders, tax risk.

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1. INTRODUCTION

Large companies are concerned with the impact of negative publicity on their reputation. Their tax minimisation strategies have been identified by lobby groups and governments as a cause of reduced government capacity, as well as a possible solution to filling an increasing shortfall in income tax revenue collected by governments around the world. This attention potentially places pressure on high profile companies to take a less aggressive tax position than they would otherwise adopt. As highlighted by Forbes in 2013 quoting tax practitioner Hadley Leach, “[t]here has definitely been a trend toward more conservatism among corporations on international tax strategy. We’re seeing a huge shift in perception around issues of reputational and audit risk and that’s really starting to affect how companies approach tax planning.”³

Disclosure requirements and community expectations increasingly place pressure on large companies to pay their ‘fair share of taxes’. For instance, the recent authority⁴ granted to the Australian Taxation Office (ATO) to publish data concerning a company’s income tax payments is likely to increase pressure on reputational risk as interested parties will now be able to discover and compare companies’ tax contributions. Likewise, Ernst and Young (EY) states in its international ‘2011–12 Tax Risk and Controversy Survey Report’ that in its view “[c]ompanies now face unprecedented scrutiny and reporting of their tax affairs by advocacy groups and the media, often hurting brand reputation and—in the worst cases—shareholder value, even when such coverage is unwarranted or inaccurate.”⁵ In the EY survey 57 per cent of tax directors reported that the threat of a negative media article about their company was a concern, with only 40 per cent reporting it was not a concern. A subset within the EY cohort, 58 per cent of tax directors from the largest companies (those with annual revenues in excess of \$US5b), reported that the threat of negative media was a concern.

Good tax governance today therefore requires the identification and management of tax risks,⁶ including reputational risk, yet limited research has considered the impact of the management of tax risks on large company tax aggressiveness.⁷ Governments, public policy advocates and the community generally consider that aggressive tax decision-making that results in the taxpayer contributing less to the revenue than the ‘spirit of tax law’ requires, is inconsistent with the government tax policy and on that basis is behaviour that needs to be understood and addressed.⁸ This article focuses on the tax risk management approaches taken by large Australian companies and the

3 Joe Harpaz, ‘Corporate Reputation Influences Tax Strategy’, Forbes (online), 20 November 2013
<<http://www.forbes.com/sites/joeharpaz/2013/11/20/corporate-reputation-influences-tax-strategy/>>

4 Treasury, Commonwealth, Improving the Transparency of Australia’s Business Tax System: Discussion Paper (2013); Part 1A s3C Taxation Administration Act 1953 (Cth).

5 Ernst and Young, ‘2011–12 Tax Risk and Controversy Survey Report’

6 Tax risk is defined for the purposes of this article as ‘any event, action, or inaction in tax strategy, operations, financial reporting, or compliance that adversely affects either the company’s tax or business operations or results in an unanticipated or unacceptable level of monetary, financial statement or reputational exposure.’ In accordance with Ernst and Young, ‘Tax Risk Management: The Evolving Role of Tax Directors’ (2004).

7 Grant Richardson, Grantley Taylor and Roman Lanis, ‘The Impact of Risk Management and Audit Characteristics on Corporate Tax Aggressiveness: An Empirical Analysis’ (Conference paper presented at the Journal of Accounting and Public Policy Conference at the London School of Economics, 25 May 2012, Session 1). This paper identified that the higher the firm’s level of tax risk management and internal control effectiveness, the lower the level of tax aggressiveness.

8 For the purposes of this article a ‘tax aggressive’ position may not necessarily constitute non-compliance with the tax laws.

extent to which they ensure that tax decision makers are fully informed concerning the impact of their tax decisions on the company, focusing on the increasing importance of reputational risk as a result of a particular tax strategy. A large Australian company is identified as one whose annual turnover exceeded \$AU250 million in 2011.

First the theoretical framework and its literature are introduced. In sections 3, 4 and 5 the research proposition is stated then research methods and results are presented. The implications of the results for the leadership, accountability and reputation of large companies as well as for the community and governments are discussed in section 6. Finally, brief conclusions are presented.

2. THEORETICAL FRAMEWORK AND LITERATURE

The legal and governance concepts underlying this tax risk governance research are the separation of ownership and control in a company including agency theory, the increased importance of corporate social responsibility and reputational risk as well as the tax disclosure rules. They provide a framework for the research proposition, analysis and conclusions.

2.1 Separation of ownership and control: the corporate veil, and the agency principle

A company is a separate legal entity and as a consequence a 'corporate veil' separates the company and its shareholders.⁹ Each shareholder's direct, personal financial exposure is limited to the contributed share capital. Directors and managers have a fiduciary duty to make decisions in the best interest of the company as a whole. The nature of a company, a shareholder's financial exposure, and the fiduciary duty that guides decision making by directors and managers impact on the position a company takes in terms of its income tax aggressiveness.¹⁰

Although income tax and any penalties payable by a company do affect the return to individual shareholders indirectly, through reduced dividends and lowered share price, the direct responsibility for taxes and penalties is with the company. A consequence of shareholders not being directly accountable for a company's tax strategy means that they may not be sufficiently concerned about a company's tax strategy to influence policy.¹¹ An analysis of company income tax strategy must therefore recognise the absence of a direct nexus between a company's tax decisions and its individual shareholders.

While a company is treated as a taxpayer, it exists only by virtue of legal rules. Its corporate governance policies determine which roles within the company are made responsible for ensuring the company meets its obligations and compliance

9 *Salomon v Salomon and Co Ltd* (1897) AC 22 recognises the legal concept of a 'corporate veil' in which the personality of a company is distinguished from the personalities of its shareholders and protects shareholders from being held personally liable for the company's debts and obligations.

10 In the case of a company group, any tax liability incurred by one entity may be distributed through a number of entities before it will be reflected in dividends paid to individual shareholders.

11 Yoram Keinan, 'Corporate Governance and Professional Responsibility' (2003) 17(1) *Tax Law Journal of Taxation and Regulation of Financial Institutions* 10; Catriona Lavermicocca and Margaret McKerchar, 'The Impact of Managing Tax Risk and the Tax Compliance Behaviour of Large Australian Companies' (2013) 28 *Australian Tax Forum* 707.

requirements under tax laws.¹² The individuals making the decisions with respect to tax strategy do so as agents of the company.¹³ As agents, as long as directors and managers are acting within the limits of their authority, the common law agency principle makes the company accountable for its income tax and penalties. Corporate governance practices may be used to align the interests of the agent with those of the principal to ensure that a company's tax strategy is consistent with corporate goals and risk preferences.¹⁴

While the goals and objectives of a company should be the primary consideration in directors' and managers' decision-making, directors and managers do not operate in a vacuum. Their scope for defining company goals and objectives is limited by laws and other regulations including accounting standards and professional codes of ethics.¹⁵

The decision control systems within a large company typically separate management strategy making (initiation and implementation) and control (ratification and compliance monitoring). This separation also acts as a mechanism that regulates the directors' and managers' decision-making scope and ability.¹⁶ The company's board of directors (the Board) has a key role in the ultimate financial performance of the company through its effective control of management decision-making to ensure the interests of shareholders are protected. In fulfilling its role, the Board appoints managers and company officers who together are the decision-makers with respect to the company's acceptable tax risk profile.

Until the 21st century focus on tax risk management, many directors of large companies were not informed about the tax implications or the risk profile of a tax position taken by their company.¹⁷ It was believed that only the tax department within the organisation had the technical skills to understand the issues involved.¹⁸ In many large companies, tax managers control the detailed tax information and still only provide superficial information and aggregated data to the Board. Others rely on the

¹² Wolfgang Schön, 'Tax and Corporate Governance: A Legal Approach', (Paper presented at the Symposium on Tax and Corporate Governance, Munich, 8–9 December, 2006) 3.

¹³ Arne Friese, Simon Link and Stefan Mayer, 'Taxation and Corporate Governance' in Wolfgang Schön (ed), *Tax and Corporate Governance*, MPI Studies on Intellectual Property, Competition and Tax Law 3 (Springer-Verlag, 2008).

¹⁴ According to Pamela Hanrahan, Ian Ramsay and Geof Stapledon, *Commercial Applications of Company Law* (CCH, 13th ed, 2012) 531 "corporate governance is concerned with the way in which companies are directed and controlled. The term corporate governance is often used to describe the way in which a company's internal arrangements, taking into account external factors such as legislation, commercial or market pressure, provide; for responsibility for decision making to be divided between the company's members, its board and its executive management, for decisions to be taken and implemented, for the monitoring and review of decision-makers, and incentives for decision-makers to act in the interests of the company and disincentives to act in a manner that harms the company."; see also OECD, 'Principles of Corporate Governance' (2004) <<http://www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/31557724.pdf>>; ASX, 'Corporate Governance Principles and Recommendations – 3rd Edition' (2014) <<http://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-3rd-edn.pdf>>.

¹⁵ Directors and managers are subject to regulation in making business decisions. To understand tax decision-making in a company, an understanding of the relevant regulatory provisions is required. In an effort to align the goals of the directors and managers with the legitimate expectations of the shareholders, a number of duties are imposed on directors and managers by the common law and the *Corporations Act 2001* (Cth).

¹⁶ See Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3 *Journal of Financial Economics* 305; Eugene F Fama, 'Agency Problems and the Theory of the Firm' (1980) 88(2) *The Journal of Political Economy* 288; Eugene F Fama and Michael C Jensen, 'Separation of Ownership and Control' (1983) 26(2) *Journal of Law and Economics* 301; Michael C Jensen, 'The Modern Industrial Revolution, Exit and the Failure of Internal Control Systems' (1993) 48 *Journal of Finance* 831 for a discussion of the role of the separation of management and control in company decision making.

¹⁷ Joel Slemrod, 'The Economics of Corporate Selfishness' (2004) Dec *National Tax Journal* 877.

¹⁸ Linda M Beale, 'Putting SEC Heat on Audit Firms and Corporate Tax Shelters: Responding to Tax Risk and Sunshine, Shame and Strict Liability' (2003–2004) 29 *Journal of Corporate Law* 210.

advice of external tax advisers for determining the tax position taken by the company.¹⁹ Times have changed. Now, in identifying tax risk management as a part of good corporate governance practices, directors are required to consider tax risk profiles and the tax implications of business decisions.²⁰ What is an acceptable tax risk profile for a particular company will ultimately be determined by shareholder objectives reflected in company goals including profit maximisation and perhaps, increasingly, a sense of corporate social responsibility ('CSR').²¹ Before discussing our research we note relevant aspects of corporate social responsibility.

2.2 Corporate governance and social responsibility

In Australia, the UK and the US, corporate governance has traditionally focused on the interests of the financial stakeholders, typically shareholders.²² In line with this, directors and managers seek to minimise taxes payable by a company (within the law) and to the extent that they do not, their actions could be considered inconsistent with shareholder objectives.²³ Increasingly, however, a sense of social responsibility is seen as important to large business and creates an expectation that company decision-makers should also act in a broader social context in making business decisions.²⁴ The appropriateness of aggressive tax planning and tax minimisation may be reappraised through the lens of CSR as companies that do not pay their 'fair share of taxes' risk hostility from the public and ultimately reputational damage.²⁵

Consistent with this thinking, Justice Neville Owen of the HIH Commission of Inquiry²⁶ portrayed "business decision-making [as] a moral exercise",²⁷ a perspective considered by the Supreme Court of New South Wales in *Australian Securities and*

¹⁹ Jim Killaly, 'Large Business and International (Case Leadership)' (Speech delivered at the Australian Taxation Summit, Sydney, 15–17 February 2006) 16.

²⁰ Michael Carmody, 'Large Business and Tax Compliance—A Corporate Governance Issue' (Speech delivered at the Leaders' Luncheon, Sydney, 10 June 2003); OECD Forum on Taxation Information Note 'General Administrative Principles: Corporate Governance and Tax Risk Management' (2009) <<http://www.oecd.org/tax/taxadministration/43239887.pdf>>.

²¹ Judith Freedman, 'Tax and Corporate Responsibility' (2003) 695 (2) *Tax Journal* 1; John Christensen and Richard Murphy, 'The Social Irresponsibility of Corporate Tax Avoidance: Taking CSR to the Bottom Line' (2004) 47(3) *Development* 37.

²² Reuven S Avi-Yonah, 'Taxation, Corporate Social Responsibility and the Business Enterprise' (CLPE Research Paper 19/2009, Vol 05, No 03); Reuven S Avi-Yonah, 'The Cyclical Transformations of the Corporate Form: A Historical Perspective on Corporate Social Responsibility' (2005) 30 *Delaware Journal of Corporate Law* 767; Mark J Roe, 'A Political Theory of American Corporate Finance' (1991) 91 *Columbia Law Review* 10; Lucian Bebchuk and Mark J Roe, 'A Theory of Path Dependence in Corporate Ownership and Governance' (1999) 52 *Stanford Law Review* 127; Mark D West, 'The Puzzling Divergence of Corporate Law: Evidence and Explanations from Japan and the United States' (2001) 150 *University of Pennsylvania Law Review* 527.

²³ Milton Friedman, 'The Social Responsibility of Business to Increase its Profits' *New York Times Magazine* (13 September 1970).

²⁴ Robert Baxt, 'The Dilemmas of the Modern Company Director', *Australian Corporations Commentary* (CCH, February 2011) [604–034]. This is consistent with the stakeholder model of the corporation articulated by R. Edward Freeman, 'Stakeholder Theory of the Modern Corporation' in *General Issues in Business Ethics*, 38–48 who identified that the stakeholders in the corporation are not only its owners, management and employees, but also include suppliers, local community and customers. Stakeholder theory and CSR is examined at Chapter 8 of R. Edward Freeman, Jeffrey S. Harrison, Andrew C. Wicks, Bidha L. Parmar, Simone De Colle *Stakeholder Theory: the State of the Art* Cambridge, 2010. Deeper discussion of this topic is beyond the scope of our article.

²⁵ Bernd Erle, 'Tax Risk Management and Board Responsibility' in Wolfgang Schön (ed), *Tax and Corporate Governance*, Springer, 2008 111.

²⁶ Commonwealth of Australia, The HIH Royal Commission, *Report on the Failure of the HIH Insurance Group in Australia* (2003).

²⁷ Neville Owen, 'Inaugural Lecture of the UTS Centre for Corporate Governance' (Speech delivered at UTS, Sydney, November 2003).

*Investments Commission v Macdonald [No 11]*²⁸ ('James Hardie'). The court in *James Hardie*²⁹ recognised that directors have moral responsibilities to a variety of stakeholders. The decision demonstrates that directors are required to make decisions after a consideration of the financial implications to the company as well as the moral implications. If this principle is also applied to the question of a director's stance on tax aggressiveness then directors should consider the company's moral requirement to make a 'fair contribution to the tax revenue' in making tax strategy decisions.

Following the line of thinking articulated by Justice Owen, and the decision in *James Hardie*, it could be argued that a company is expected to contribute to the revenue of a country in which they carry on business so that an aggressive tax position would be considered 'morally' unacceptable. To date no such moral responsibility exists under Australian law.³⁰

CSR itself imposes obligations on a company to a variety of stakeholders in addition to managers and shareholders including tax authorities, communities, political groups, customers and the public.³¹ For example, Muller and Kolk's research on multinationals operating in India found that taxation in developing countries is seen by multinationals as a CSR issue. Their research concluded that multinationals pay tax at considerably higher effective rates in India than do local companies.³²

Although no specific legislative provision requires an Australian company to be 'socially responsible' the ASX Corporate Governance Principles require ASX listed companies to "act ethically and responsibly" (Principle 3).³³ Accountability for the consequences of tax decisions is a likely consequence of Principle 3 which requires more than "mere compliance with legal obligations and involves acting with honesty, integrity and in a manner that is consistent with the reasonable expectations of investors and the broader community".³⁴ That there have been three separate inquiries into CSR in Australia over the past nine years reflects the topical nature of CSR.³⁵ In addition, the global financial crisis in 2008 added to the pressure on large companies to be socially responsible including the requirement to make a fair contribution to public revenue.³⁶

²⁸ [2009] NSWSC 28.

²⁹ Ibid.

³⁰ Andrew Lilico, 'Companies have a Moral Duty to Pay no More Tax than Legally Required' Telegraph Blogs 14 June 2013.

³¹ Robin W Roberts, 'Determinants of Corporate Social Responsibility Disclosure: an Application of Stakeholder Theory' (1992) 17 (6) *Accounting Organisations and Society* 595; Craig Deegan, 'Introduction: the Legitimising effect of social and environmental disclosures—a Theoretical Foundation' (2002) 15 (3) *Accounting, Auditing and Accountability* 282.

³² Alan Muller and Ans Kolk, 'Responsible Tax as Corporate Social Responsibility: The Case of Multinational Enterprises and Effective Tax in India' (2012) *Business and Society* 1.

³³ ASX, 'Corporate Governance Principles and Recommendations – 3rd Edition' (2014) <<http://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-3rd-edn.pdf>>.

³⁴ Ibid, 18.

³⁵ Parliamentary Joint Committee on Corporations and Financial Services (PJC), *Inquiry into Corporate Responsibility* (2006); Corporations and Markets Advisory Committee (CAMAC), 'Discussion Paper on the Inquiry into the Social Responsibility of Corporations' (November 2005); ASX, 'Corporate Governance Principles and Recommendations—3rd Edition' (2014).

³⁶ John Hasseldine, Kevin Holland and Pernill van der Rijt, 'The Market for Tax Knowledge' (2001) 22 *Critical Perspectives in Accounting* 39; OECD 'Moving Forward on the Global Standards of Transparency and Exchange of Information for Tax Purposes' (2009); Jeffrey Owens, 'Tax and Development: Why Tax is Important to Development' (2009) 4(4) *Tax Justice Focus* 1.

Traditionally the relationships between a company and other stakeholders have been ignored as the Board's focus has been on the company goal of profit maximisation. Consistent with this observation, Lanis and Richardson identify a surprising lack of research linking CSR with corporate taxation and argue that this may be due to the focus in accounting and business research relating to corporations, on agency theory and the relationship between managers and shareholders.³⁷

Henderson Global Investors surveyed 335 of the FTSE 350 companies in 2004 and noted that companies are increasingly required to "demonstrate to tax authorities (and also society) that they are complying with tax rules".³⁸

If a company is viewed as a 'real world entity', not just accountable to shareholders but to a variety of stakeholders, then addressing CSR would be considered legitimate.³⁹ In December 2012, for example, activists descended on Starbucks retail outlets in the United Kingdom (UK) to protest the company's failure to pay its required taxes, a failure that had been brought to light by a UK Parliamentary Investigative Committee.⁴⁰ Activists complained that as a consequence of Starbucks not paying the appropriate amount of taxes the less privileged and disadvantaged were not being looked after. Starbucks and other multinationals such as Google, Apple and Amazon have all been accused in recent time of failing to pay sufficient taxes and have accordingly been asked to explain their low rate of effective tax.⁴¹ Starbucks accepted that its reputation had been damaged by the accusation of tax dodging and that the perception had cost the company in terms of its viability to continue to carry on business in the UK.⁴² In response it announced that it would voluntarily pay £20 million in corporate tax in 2013 and 2014, regardless of whether the company was profitable.⁴³ The media continues to report on the low effective tax rates of high profile companies and the tax revenue implications of aggressive tax planning arrangements.⁴⁴

Starbucks' response indicates that community standards in relation to taxation can have an impact on a company's tax strategy. UK Uncut⁴⁵ has targeted other large businesses for failure to pay taxes in the UK and the public reaction indicates that "a social licence to operate has expanded beyond labour and environmental issues and beyond poor countries".⁴⁶ The impression that big business is not paying a 'fair

³⁷ Roman Lanis and Grant Richardson, 'Corporate Social Responsibility and Tax Aggressiveness: An Empirical Analysis' (2012) 31 *Journal of Accounting and Public Policy* 86.

³⁸ Henderson Global Investors, 'Tax, Risk and Corporate Governance' (2005) <<http://www.henderson.com/content/sri/publications/reports/taxriskcorporategovernance.pdf>>; Henderson Global Investors, 'Responsible Tax Report' (2005) <http://www.taxjustice.net/cms/upload/pdf/Global_Henderson_-_ResponsibleTax_-_OCT_2005.pdf>.

³⁹ Avi-Yonah, above n 22.

⁴⁰ Allison Christians, 'How Starbucks Lost its Social License—and Paid £20 million to Get it Back' *Tax Notes International* (2013) 71(7) 637.

⁴¹ Edward Kleinbard, 'The Lessons of Stateless Income' (2011) 65 *Tax Law Review* 99; James Hutchinson, 'Apple's tax falls to \$36m in Australia as sales hit \$6bn' *Australian Financial Review* (31 January 2014) <http://www.afr.com/p/technology/apple_tax_falls_to_in_australia_dWUlatWLWUYWD8XKa1Ln7K>; Jane Wardell, 'G20 Agrees on Push to Close Tax Loopholes, Make Multinationals Pay' Reuters (23 February 2014) <<http://in.reuters.com/article/2014/02/23/g20-australia-tax-idINDEEA1M05120140223>>.

⁴² Christians, above n 42; An IBE Survey (2012) found that tax avoidance was the second most important issue that the British public thought business needed to address.

⁴³ Christians, above n 42.

⁴⁴ Neil Chenoweth, 'International PwC Tax Schemes Exposed' *Australian Financial Review* (6 November 2014)

⁴⁵ UK Uncut is a grassroots movement taking action to highlight alternatives to the government's spending cuts.

⁴⁶ Christians, above n 42, 638.

amount of tax' encourages governments and bodies such as the OECD to look at taxation systems and provides support for a more heavy handed approach to corporate taxation.⁴⁷ The recent focus by the OECD on transfer pricing and tax base erosion, for instance, can be traced to a concern that multinational companies do not contribute sufficient taxes worldwide and that the current international tax agreements fail to address the shifting of profits to low tax jurisdictions.⁴⁸

Companies traditionally have not considered the payment of taxes to be an important part of their socially responsible behaviour⁴⁹ although the ownership structure of a company may moderate this.⁵⁰ Where a company's strategic goals include not just economic or financial goals but do also convey a sense of social responsibility it is expected that the company will place a higher level of importance on tax compliance and tax contributions to government.

Lobby groups including the The Tax Justice Network, Occupy Movement and Uncut UK and Uncut US all push for a larger contribution to tax revenue by big business.⁵¹ Publicised protests against alleged tax avoiders also have the potential to negatively impact on a company's reputation. Increasingly a social responsibility is recognised by companies in Australia and overseas and this may have an effect on a company's tax strategy.⁵²

A HMRC report highlights that large UK companies weigh up the potential impact on their reputation when considering whether to take a tax aggressive position.⁵³ As Christensen and Murphy argue the "[d]irectors now need to recognize that aggressive tax-planning strategies are not compatible with long term sustainability and therefore may not be in the shareholder's broader interests".⁵⁴

Difficulty exists in establishing whether a company is genuinely socially responsible. This in turn limits the ability to use published claims of socially responsible behaviour as indicators of tax aggressiveness. The role of CSR in reducing tax aggressive behaviour by large companies must be evaluated in the context of what Brunsson refers to as 'organised hypocrisy'⁵⁵ in which gaps arise between company talk, decisions and action. Sikka also argues that the CSR statements made by many companies are merely symbolic to "satisfy the demands from a critical external environment"⁵⁶ and the economic incentives for directors and management to increase

⁴⁷ OECD 'Action Plan on Base Erosion and Profit Shifting' (2013); OECD 'Addressing Base Erosion and Profit Shifting' (2013).

⁴⁸ Ibid.

⁴⁹ Angela K Davis, David A Guenther, Linda K Krull and Brian M Williams, 'Taxes and Corporate Sustainability Reporting: Is Paying Taxes Viewed as Socially Responsible' (Working Paper, Lundquist College of Business, University of Oregon, Eugene 2013).

⁵⁰ Susanne Landry, Manon Deslandes and Anne Fortin, 'Tax Aggressiveness, Corporate Social Responsibility, and Ownership Structure' (2013) *Journal of Accounting, Ethics and Public Policy* 14(3) 611.

⁵¹ Christians, above n42.

⁵² UTS Centre for Corporate Governance, 'The Changing Roles of Company Boards and Directors' (Final Report, September 2007).

⁵³ FDS International, 'Large Groups' Tax Departments: Factors that Influence Tax Management—A Qualitative Study' (Prepared for HMRC (UK), September 2006).

⁵⁴ John Christensen and Richard Murphy, 'The Social Irresponsibility of Corporate Tax Avoidance: Taking CSR to the Bottom Line' (2004) 47(3) *Development* 37, 43.

⁵⁵ Nils Brunsson, *Organised Hypocrisy: Talk, Decisions and Actions in Organisations* (John Wiley, 2003).

⁵⁶ Prem Sikka, 'Smoke and Mirrors: Corporate Social Responsibility and Tax Avoidance' (2010) 34 *Accounting Forum* 153, 156. Sikka examined a number of large companies that state they behave in an ethical and responsible way yet at the same time were involved in tax avoidance and in some cases tax evasion.

profits through the reduction of taxes remain paramount.⁵⁷ Accordingly statements made by a company as to social responsibility need to be evaluated with scepticism and may not indicate anything about a company's tax aggressiveness.⁵⁸

Preuss' study of offshore finance centres based in tax havens found that 38 per cent of the offshore finance centres claimed to engage in 'socially responsible business practices' despite the fact that they were resident in low tax jurisdictions.⁵⁹ The relevant offshore finance centres were found to present themselves as being socially responsible yet still avoid paying taxes by locating in low tax countries. Here again is evidence that CSR claims are in some cases mere 'window dressing'.⁶⁰

Hasseldine and Morris⁶¹ criticise the conclusions made by Sikka because, they argue, Sikka did not appropriately define tax avoidance, and that the inclusion of companies that simply take an aggressive tax position as tax avoiders is not appropriate. Companies that plan their tax affairs to minimise taxes are not tax avoiders but a case of directors meeting their obligation to maximise profits according to Hasseldine and Morris.⁶² Theirs may prove to be 'old thinking'. Whilst there is no requirement that companies make decisions in a socially responsible way Sikka argues that if companies claim they are socially responsible they should not be pushing tax aggressive positions that minimise their contribution to the public revenue.⁶³

Hoi, Wu and Zhang, using unrecognised tax benefits⁶⁴ (UTB) over the period 2003 to 2009 as an indicator of tax aggressive behaviour, found that companies that demonstrate irresponsible corporate social activities are more likely to enter into tax sheltering arrangements.⁶⁵ Watson compared the level of UTBs to a company's CSR position and concluded that socially irresponsible firms have larger UTBs.⁶⁶ That is, a socially responsible company is less likely to adopt a tax aggressive position (reflected in a lower level of UTB) compared to socially irresponsible companies.

Of particular relevance to this article, Lanis and Richardson identified that a company's CSR principles can influence the stance the company takes in terms of tax aggressiveness and that influence is via the Board of directors.⁶⁷ Lanis and Richardson use data from a sample of 408 publicly listed Australian companies and conclude that a company's CSR position says something about the lengths a company is prepared to

⁵⁷ Ibid.

⁵⁸ Ibid.

⁵⁹ Lutz Preuss, 'Responsibility in Paradise? The Adoption of CSR Tools by Companies Domiciled in Tax Havens' (2010) 110 *Journal of Business Ethics* 1.

⁶⁰ Ibid.

⁶¹ John Hasseldine and Gregory Morris, 'Corporate Social Responsibility and Tax Avoidance' (2013) 37(1) *Accounting Forum* 1.

⁶² Ibid.

⁶³ Prem Sikka, above n 56, 153; Prem Sikka, 'Smoke and Mirrors: Corporate Social Responsibility and Tax Avoidance—A reply to John Hasseldine and Gregory Morris' (2013) 37 *Accounting Forum* 15.

⁶⁴ A UTB is a tax position that a company's management is concerned will be challenged if examined by the revenue authority.

⁶⁵ Chun Keung Hoi, Qiang Wu and Hao Zhang, 'Is Corporate Social Responsibility (CSR) Associated with Tax Avoidance? Evidence from Irresponsible CSR' (2013) 88(6) *The Accounting Review* 2025.

⁶⁶ Luke Watson, 'Corporate Social Responsibility and Tax Aggressiveness: An Examination of Unrecognised Tax Benefits' (Paper presented at the American Accounting Association Annual Meeting—Tax Concurrent sessions Denver, Colorado US, August 2011).

⁶⁷ Lanis and Richardson, above n 37, 86.

go to reduce its tax liability.⁶⁸ Additional regression analysis demonstrates that social investment commitment, company strategy generally and the specific CSR strategy are all part of a firm's CSR activities and have a negative impact on tax aggressiveness.⁶⁹ The identification of a negative connection between social responsibility and tax aggressiveness suggests that companies that do address social responsibility are more concerned with ensuring compliance with the spirit of the tax laws than those companies that do not.

2.3 Reputational risk from tax decisions

As we have already noted in relation to Starbucks and other highly visible companies, the link between tax aggressive behaviour and a company's reputation could encourage companies to take a socially responsible approach to tax decision making where it is anticipated that the negative reputational impact outweighs any tax savings from an aggressive tax position. Negative media reporting of high profile multinationals that fail to contribute to the tax revenue in the jurisdiction in which they carry on business are increasingly common, having the potential to negatively impact that multinational's profitability.⁷⁰

Public opinion and perception, both directly and through the voice of the media, is a concern to large companies with 40 per cent of CEOs saying that the media had some influence on their company strategy and a further 12 per cent acknowledging that this influence was significant.⁷¹ In 2013, a US Government Accountability Office (GAO) Report on corporate tax rates highlighted that U.S. corporations paid on average a 13 per cent tax rate in 2010,⁷² a fact then widely reported in the media. The PricewaterhouseCoopers (PwC) Annual Global CEO survey, conducted in 2012 questioned 1038 CEOs in 68 countries about tax strategy and corporate reputation and the responses indicated that CEO's felt that corporate taxation has become a matter of public interest.⁷³

According to the PwC survey the single biggest danger that CEOs of large companies face in developing tax strategy is reputational.⁷⁴ As stated in the PwC report

[w]e're living in a world of 24-hour news and Twitter, a world where information is amplified and distributed in seconds and, most critically in the case of complicated tax arrangements, where complex issues are brutally summarised. Great damage can be done before a company has a chance to explain [its] position. Public opinion, even if it's based on inaccurate information, is powerful.⁷⁵

Further data that indicates the significance of reputational risk associated with tax decision-making by large companies was reported by ACE Group (one of the world's

⁶⁸ Ibid.

⁶⁹ Lanis and Richardson, above n 37, 105.

⁷⁰ Kleinbard, above n 41.

⁷¹ PricewaterhouseCoopers, 'Tax Strategy and Corporate Reputation—a Business Issue' (2013) 7.

⁷² United States Government Accountability Office, 'Corporate Income Tax—Effective Tax Rates Can Differ Significantly from the Statutory Rate' (May 2013) <<http://www.gao.gov/assets/660/654957.pdf>>.

⁷³ Ibid.

⁷⁴ Ibid, 8.

⁷⁵ Ibid.

largest property and casualty insurers).⁷⁶ The biggest source of reputational risk for 21 per cent of the 650 risk managers in the ACE survey report was aggressive tax avoidance/tax evasion in the business environment.⁷⁷ Similarly, the Thomson Reuters 2012 Australia and New Zealand Tax Survey sought the views of tax directors, corporate tax managers, heads of tax and Chief Financial Officers (CFO) at major companies in Australia and New Zealand and responses indicate that over half of the respondents (56%) were concerned about reputational risk with regard to non-compliance with tax laws and its effect on shareholder value.⁷⁸ The 2014 annual global survey of multinational CFOs conducted by Taxand, the world's largest global organisation of tax advisors to multinational businesses, indicates that 76 per cent of multinational CFOs felt that the focus in the media on corporate tax planning activity has had a detrimental impact on a company's reputation.⁷⁹ In fact 31 per cent of the Taxand survey respondents felt that the intense media focus on tax planning has had an impact on their approach to tax planning.⁸⁰

Whilst there is no clear and commonly agreed definition of 'company reputation' we use that proposed by Barnett, Jermier and Lafferty being "observers' collective judgements of a corporation based on assessments of the financial, social and environmental impacts attributed to the corporation over time".⁸¹ Because a company's reputation can affect its value and income earning potential, reputational tax risk concerns the impact on the company that may arise from its tax decisions and actions if persons outside the company were to become aware of it.⁸²

A potential negative impact on reputation as a result of a company adopting a tax aggressive position was not demonstrated in a pilot study of large companies in the UK in 2007.⁸³ Few of the respondents were concerned with the public's perceptions of their tax policy and planning behaviour. The authors suggest the lack of concern for negative publicity concerning tax aggressive behaviour could be due to the fact that in the UK at the time there was very little reporting of company tax strategy issues. In the light of the experience identified above of Starbucks, and others, it appears times have changed. Reputational risk is a "very real phenomenon facing multinationals if the public judges them to be too successful in reducing their tax bills".⁸⁴ The current view of the public can, to some extent, be ascertained from the results of a Gallup poll of US individuals in April 2013 that reported 66 per cent of respondents felt that companies pay 'too little' tax.⁸⁵

⁷⁶ ACE European Group, 'Reputation at Risk—ACE European Risk Briefing' (2013).

⁷⁷ Ibid, 11.

⁷⁸ Thomson Reuters, 'Thomson Reuters 2012 Australia and New Zealand Tax Survey' (2012).

⁷⁹ Taxand, 'Tax and Global Survey 2014—Navigating tax priorities: substance, reputational risk and reform' <http://www.taxand.com/sites/default/files/taxand/documents/Taxand%20Global%20Survey%202014.pdf>.

⁸⁰ Ibid.

⁸¹ Michael L Barnett, John M Jermier and Barbara A Lafferty, 'Corporate Reputation: The Definitional Landscape' (2006) 9(1) *Corporate Reputation Review* 26, 34.

⁸² Robert Booth, 'Starbucks Row Over Tax and Staff Contracts Could Squeeze Sales by 24 per cent' *The Guardian* (UK), 8 December 2012, 43.

⁸³ Judith Freedman, Geoffrey Loomer and John Vella, 'Moving Beyond Avoidance? Tax Risk and the Relationship between Large Business and HMRC' (Report of a Preliminary Study, Oxford University Centre for Business Taxation, June 2007).

⁸⁴ Christians, above n 42, 638

⁸⁵ Results are based on telephone interviews conducted April 4-7, 2013 with a random sample of 1000 adults, aged 18+ living in all 50 U.S. states and the District of Columbia; 'Gallup Poll (US)' 2013 <http://www.gallup.com/poll/161927/majority-wealth-evenly-distributed.aspx?ref=image>.

Community expectations also place pressure on governments and revenue authorities to do something about the failure (perceived or actual) of large companies to contribute to the revenue. In 2013, for example, the CEO of Apple was required to testify at the Senate Permanent Committee on Investigations in Washington, explaining why Apple manages to pay so little tax worldwide annually.⁸⁶ Other high profile multinationals, for example Amazon (6%), Boeing (7%), General Electric (16%) and Google (17%)⁸⁷ also demonstrate low effective tax rates. It is important to acknowledge that these multinationals are not necessarily involved in illegal activities rather they may be using legitimate tax-planning strategies to reduce their worldwide tax bill.⁸⁸

A number of researchers have considered the extent to which variables with an indirect impact on reputation drive tax decision-making. In analysing the tax planning activities of both public and private companies, Badertschera, Katzb and Rego note that because public companies are subject to greater financial reporting pressure, they tend to engage in more non-conforming tax planning.⁸⁹ In comparison, private companies are willing to adopt more book-tax conforming tax strategies which reduce their effective tax rates below those for public companies.⁹⁰

Badertschera, Katzb and Rego also considered private equity backed companies in the US that were involved in the management of investment funds and used, typically, to acquire mature businesses.⁹¹ Their research found that private companies, whose shareholders include private equity-based firms that were converted to public companies, engage in more tax avoidance than other public companies. This indicates that private equity ownership continues to influence the tax practices of a company after it becomes public.⁹² Badertschera, Katzb and Rego conclude that private equity backed companies view tax planning as an additional source of economic value to their firms, where the tax savings outweigh any potential reputational costs associated with company tax avoidance.⁹³ In a further dimension to the risk of reputation damage, Chen, et al (2010) found, not surprisingly, that family firms are more concerned about a potential tax penalty and/or potential damage to the family's reputation as a result of being found to be involved in tax avoidance than non-family firms.⁹⁴

Recent academic research has focused on the significance of company reputation in tax decision making. Specifically, Austin and Wilson⁹⁵ identify a set of firms with valuable consumer reputation and found no evidence that more highly rated consumer brands are associated with less tax avoidance but do find that managers of firms with

⁸⁶ Douglas S Stransky, 'US Tax Reform: Modern Tax Rules needed for the Modern Age of Business' *International Tax Review*, 18 June 2013.

⁸⁷ Ibid.

⁸⁸ Michelle Hanlon and Shane Heitzman, 'A Review of Tax Research' (2010) 50 *Journal of Accounting and Economics* 127.

⁸⁹ Brad Badertschera, Sharon P Katzb and Sonja Olhoft Rego, 'The Impact of Private Equity Ownership on Portfolio Firms' Corporate Tax Planning' (Unpublished working paper, University of Notre Dame, Columbia University and Indiana University 2011).

⁹⁰ Ibid.

⁹¹ Ibid.

⁹² Ibid.

⁹³ Ibid.

⁹⁴ Shuping Chen, Xia Chen, Qiang Cheng and Terry Shevlin, 'Are Family Firms More Tax Aggressive than Non-Family Firms?' (2010) 95 *Journal of Financial Economics* 41.

⁹⁵ Chelsea Rea Austin and Ryan Wilson, 'Are Reputational Costs a Determinant of Tax Avoidance?' (Working Paper, University of Iowa, February 2013).

valuable consumer brands use discretion inherent in financial reporting rules to report the benefits of tax planning more conservatively. In contrast Graham, Hanlon, Shevlin and Shroff⁹⁶ analysed survey responses from nearly 600 corporate tax executives to investigate firms' incentives and disincentives for tax planning and found that reputational concerns are important. Specifically 69 per cent of respondents rate reputation as important and rank reputation as second in order of importance among all factors explaining why they do not adopt a tax aggressive strategy.

Interdisciplinary research by Hardeck and Hertl links taxation, marketing and CSR and investigates the effects of media reports of aggressive or responsible corporate tax strategies on a company's success with consumers.⁹⁷ Hardeck and Hertl, using responses from a sample of German university students, found that a company's tax strategy can influence corporate success with consumers, in that a negative media report about a company's aggressive tax behaviour damages that company's reputation and lowers the likelihood that a customer will purchase that product.⁹⁸ In the alternative a media report on responsible tax behaviour has the opposite effect. Interestingly though, Hardeck and Hertl find that consumers are reluctant to pay higher prices for a product in order to induce responsible tax behaviour.⁹⁹ Arguably, increasing the level of disclosure of information about a company's tax compliance behaviour will increase the reputational risk, including the risk of consumer backlash, associated with aggressive tax decision-making by large companies. Yet on a more positive note increasing the level of disclosure of a company's responsible tax behaviour may enhance its reputation and provide benefits in the form of increased brand loyalty.

2.4 Disclosure of tax related information

The requirement to disclose information places pressure on company decision-makers to consider the implications of the disclosure on their relationship with stakeholders. The value that companies place on their reputation and the pressure to be more socially responsible suggests that disclosure of tax aggressive behaviour would be a concern to the Board and an important consideration in establishing a tax risk profile. Where a company is required to disclose detailed financial data, stakeholders have increased access to financial information about the company and are able to factor that information into decisions.

FIN48 including the disclosure of UTBs, s 404 of the *Sarbanes-Oxley Act of 2002* (US) ('SOX'), the ASX Principles of Good Corporate Governance, the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (Cth) ('CLERP 9') and the Continuous Disclosure Provisions¹⁰⁰ are measures that require primarily listed companies to justify and in some instances disclose details of the tax positions adopted.¹⁰¹ Revenue authorities have also been proactive in seeking greater

⁹⁶ John Graham, Michelle Hanlon, Terry Shevlin and Nemit Shroff, 'Incentives for Tax Planning and Avoidance: Evidence from the Field' (2014) 89(3) *The Accounting Review* 991.

⁹⁷ Inga Hardeck and Rebecca Hertl, 'Consumer Reactions to Corporate Tax Strategies: Effects on Corporate Reputation and Purchasing Behavior' (2013) 7 August *Journal of Business Ethics* 1.

⁹⁸ Ibid.

⁹⁹ Ibid.

¹⁰⁰ Companies listed on the ASX are subject to continuous disclosure obligations (with some exceptions) under ASX Listing Rule 3.1.

¹⁰¹ See also the *Dodd-Frank Wall Street reform and Consumer Protection Act* (US); PricewaterhouseCoopers 'Tax Accounting Services—Income Tax Disclosure' (Dec 2013).

transparency of material tax transactions. Australia requires taxpayers to notify the ATO of any reportable tax position¹⁰² and similar provisions exist internationally. Requirements to disclose information to the public are identified by Rice in an econometric study of small companies (assets between \$US1 million and \$US10 million) as encouraging tax compliant behaviour by a company.¹⁰³ Similarly, it is expected that increased regulation in terms of tax reporting will have an impact on company tax compliance as large companies are required to be transparent and accurate; they are becoming more accountable.

The research that links increased disclosure requirements to reduced tax aggressiveness is reflected in the 'OECD Report on Disclosure Initiatives' as it outlines the "importance of timely, targeted and comprehensive information to counter aggressive tax planning" and recommends that revenue authorities from OECD member countries introduce additional disclosure requirements to assist in the identification of tax aggressive behaviour.¹⁰⁴ Whilst the emphasis in the report is on the benefits to the tax administration of access to timely and detailed information for their review it is arguable that increasing the disclosure requirements will have an impact on the level of reputational risk faced by large companies that make the relevant disclosures.

The Head of the OECD's Global Transparency Forum, Monica Bhatia, stated in 2012 that "we are seeing a rise in transparency in policy, in incentives and in reporting, and it's only going in one direction: more transparency".¹⁰⁵ The introduction of country-by-country reporting requires companies to disclose a full consolidated profit and loss account for each and every jurisdiction in which it trades including full tax notes.¹⁰⁶ Some concern for information overload and public confusion as a result of the detailed information that will be available is noted.¹⁰⁷

The Australian Federal Government introduced legislation allowing the ATO to publish the corporate tax information of mining companies and businesses with \$AU100 million or more in total income.¹⁰⁸ An earlier Federal government discussion paper highlights that the publication of taxes payable by large business "... will enable the public to better understand the corporate tax system and engage in policy debates, as well as discourage aggressive tax minimisation practices by large corporate entities".¹⁰⁹ The ATO released, for the first time in May 2014, information showing where Australian companies shift revenues and analysts suggest that this is part of a

¹⁰² The reportable tax position schedule is the company income tax return to be lodged with the ATO. The schedule requires large businesses to disclose their most contestable and material tax positions.

¹⁰³ Eric Rice, 'The Corporate Tax Gap: Evidence on Tax Compliance by Small Corporations' in Joel Slemrod (ed), *Why People Pay Taxes: Tax Compliance and Enforcement* (University of Michigan Press, 1992) 125.

¹⁰⁴ Tackling Aggressive Tax Planning Through Improved Transparency and Disclosure Report on Disclosure Initiatives OECD, February 2011.

¹⁰⁵ Matthew Gilleard, 'The Dark Side of Transparency' (2014) February *International Tax Review* 12.

¹⁰⁶ Gilleard, Ibid; PriceWaterhouseCoopers (2013) Tax Transparency and country-by-country reporting- An Ever Changing Landscape <http://www.pwc.com/en_GX/gx/tax/publications/assets/pwc_tax_transparency_and_country-by-country_reporting.pdf>.

¹⁰⁷ Gilleard, above n105. See also the *Foreign Account Tax Compliance Act* US 2010 ('FATCA')

¹⁰⁸ Part 1A s3C *Taxation Administration Act 1953* (Cth) requires the ATO Commissioner to make public specific information relating to the tax affairs of all corporate tax entities that have a reported total income of \$100 million or more.

¹⁰⁹ David Bradbury, Assistant Treasurer Press Release No 40 'Improving the Transparency of Australia's Business Tax System', 3 April 2013; Improving the Transparency of Australia's Business Tax System—Discussion Paper, April 2013 Commonwealth of Australia; Australian Treasurer Arthur Sinodinos hinted that the Australian disclosure laws may be repealed on the basis of concern detracts from well informed debate.

‘scare campaign’ by the ATO to stop multinationals from shifting profits to countries with lower tax rates’.¹¹⁰ The increasing importance of social responsibility and the greater community awareness in relation to the tax contribution of large companies through tax reporting and disclosure requirements mean that the reputational risk associated with tax decision making will be a significant tax risk for many companies.¹¹¹

An additional concern identified, as a result of the disclosure of tax paid by large companies, is the risk that the information disclosed “may be misleading and it could do big damage unfairly”.¹¹² Large business, governments and the OECD highlight that the publication of simplified tax figures may give a distorted impression of a company’s tax contribution and result in misinformed impressions and decisions.¹¹³ Despite this concern, research commissioned by the Tax Justice Network in Australia, indicates that there is widespread support in Australia to make corporate tax more transparent and almost two-thirds of respondents to the survey in 2014 felt negative about companies such as Apple for using loopholes to avoid tax, increasing substantially from 2013.¹¹⁴

As demonstrated by Starbucks, it is anticipated that reputational risks are, for many industries, a substantial concern. Our research proposition is that the complex issue of reputational risk will have an impact on a large company’s tax risk management decisions and ultimate tax risk profile.

3. RESEARCH PROPOSITION

This article considers the research proposition that the impact of a large company’s tax aggressiveness on its reputation is a significant tax risk, and a comprehensive tax risk management system should include an evaluation of reputational risk. Further it is proposed that the consideration of reputational risk by a company’s tax risk management system will result in a company adopting a lower level of acceptable tax risk. Other recent research looking at the relationship between reputational risk and tax decision making was discussed in section IIC and supports this research proposition.¹¹⁵ We now detail the research methods underlying our results.

¹¹⁰ Jonathan Pearlman, ‘Aussie Firms target Singapore in Quest for Lower Taxes’ *The Straits Times* 9 May 2019

¹¹¹ Neil Chenoweth, ‘How Ireland got Apple’s \$9bn profit’ *Australian Financial Review* 6 March 2014.

¹¹² Nassim Khadem, ‘OECD Cool on Mandatory Disclosure of Tax Bills’ *Australian Financial Review* 30 January 2014; United Voice and Tax Justice Network, Australia, ‘Who Pays for our Commonwealth? Tax Practices of the ASX 200’ (2014) < file:///D:/Users-Data/mq92502857/Downloads/Who%20Pays%20-%20ASX%20200%20Short%20Report%20(1).pdf>.

¹¹³ *Ibid.*

¹¹⁴ Tax Justice Network, ‘Australian Public Outraged with Multinational Corporations Avoiding Tax’ (15 September 2014).

¹¹⁵ Lavermicocca and McKerchar, above n 11, 66; Ernst and Young, ‘2011–12 Tax Risk and Controversy Survey Report’.

4. RESEARCH METHODS—POPULATION AND DATA COLLECTION

The empirical research consisted of two phases: the initial qualitative phase followed by a quantitative phase.¹¹⁶ In the first, the relationship between tax risk management and tax compliance was explored through in-depth interviews. The responses to interview questions were then analysed, and key themes and relationships were isolated. These were then used to formulate specific research questions that were tested quantitatively using data collected in a survey of large companies in Australia during the second phase.

4.1 Phase One—In-depth interviews

In-depth interviews were conducted with tax managers from 14 large Australian companies.¹¹⁷ Each in-depth interview included 19 open-ended questions relating to tax risk and tax decision-making (See Appendix 1). A tax partner with a ‘Big 4’ international accounting firm was also interviewed during this first phase to obtain his view on the tax risk management practices of large company clients and the impact of those practices on tax compliance behaviour. The views of the tax partner provided an additional insight into the approach to tax risk management by large Australian companies.

Participation in the in-depth interviews was voluntary. Interviews were conducted face-to-face or via telephone between October 2009 and June 2010. The responses to open-ended questions were analysed by coding responses then isolating key concepts to develop themes and relationships.¹¹⁸ Ultimately, the themes and relationships identified were used to build a range of specific research questions to be tested empirically during Phase Two.

4.2 Phase Two—Survey instrument

In Phase Two a survey (See Appendix 2) was conducted to collect information about tax risk management practices in Australia and the variables that have an effect on a

¹¹⁶ David L Morgan, ‘Practical Strategies for Combining Qualitative and Quantitative Methods: Applications to Health Research’ (1998) 8(3) *Qualitative Health Research* 362; Abbas Tashakkori and Charles Teddlie, *Mixed Methodology: Combining Qualitative and Quantitative Approaches* (Sage Publications, 1998); Abbas Tashakkori and Charles Teddlie (eds), *Handbook of Mixed Methods in Social and Behavioural Research* (Sage Publications, 2003).

¹¹⁷ Large company for the purposes of this research includes both listed and unlisted companies with a turnover exceeding \$250million. The Australian Tax Office (ATO) ‘Large Business Group’ includes business groups with a turnover exceeding AUD250 million and it is this group that the ATO focuses on in correspondence and publications concerning the need to adopt a tax risk management system. For the purposes of this research a ‘large company’ is defined as a company with a turnover exceeding AUD250 million, as it is this subset of companies that contribute significantly to company tax revenue in Australia (58%) and are the target of the ATO tax risk management initiative. According to ‘Australian Taxation Statistics 2009–2010’ Chapter 3 Box 3.2, Table 3.3 and Table 3.9, companies with a turnover exceeding AUD250 million constitute 0.1 per cent of the total number of company taxpayers in Australia yet contribute 58 per cent of company tax revenue. Inconsistent with the definition used for the purposes of this research, the ATO defines a ‘large company’ as a company with a turnover between AUD100 million and AUD250 million and a ‘very large company’ as a company with a turnover in excess of AUD250. The decision to use the threshold of AUD250 million in this research, as opposed to the AUD100 million used by the ATO, is justified based on the ATO focus on tax risk management practices of companies with a turnover exceeding AUD250 million and the fact that according to ‘Australian Taxation Statistics 2009–2010’ Chapter 3 Table 3.9 companies with a turnover between AUD100 million and AUD250 million contribute only .05 per cent of company tax revenue and the indication in preliminary research is that company group is unlikely to have put in place a comprehensive tax risk management system.

¹¹⁸ Juliet Corbin and Anselm Strauss, *Basics of Qualitative Research* (Sage Publications, 3rd ed, 2008) 160.

large company's ability to manage tax risk. Company 360, a database of Australian companies, was used to obtain the contact details of Australian companies with a turnover exceeding AUD250 million.¹¹⁹ The CFOs of all companies identified, (approximately 1,200 companies) were sent the survey instrument by mail in December 2011 and January 2012. A postal survey, as opposed to an email survey was used as only the postal address of CFOs of large Australian companies was available on the Company 360 database. This survey constitutes a cross-sectional population survey rather than a sample survey as the survey instrument was sent to all Australian companies in the sample.

To maximise the response rate and minimise the potential for bias in responses, the survey responses did not identify the respondent company and accordingly respondents remained anonymous. A follow-up survey was sent to all potential participants three weeks after the first survey mail out to ensure participation in the survey was maximised.¹²⁰ The survey instrument included both closed and open-ended questions. A range of techniques were employed to minimise bias.¹²¹ Coded data was entered as a dataset into SSPS, producing statistics for analysis.

Based on the Company 360 database, 36.7 per cent of Australian companies in the population are public companies and 63.3 per cent are proprietary (referred to as 'private' in this article). One hundred and twenty three responses were received to the Phase 2 survey. Of these, 35.8 per cent were from people working in private companies and 64.2 per cent were from those working in public companies, as shown in Table 1.

Table 1: Population and respondents by company type

	Population %	Respondents %
Private company	63.3	35.8
Public company	36.7	64.2
Total	100.0	100.0

The fact that the majority of respondents were public companies is consistent with the ATO statement in the 'Compliance Program 2011–2012' that "the majority of entities in the large business sector are public companies".¹²²

There is a noticeable difference between the response rates for public and private companies. The response rate calculated for private companies is $44/737 = 6.0$ per cent while the response rate for public companies is $79/427 = 18.5$ per cent. While the response rate is lower than other Australian tax compliance mail surveys,¹²³ this

¹¹⁹ For the purposes of this research a 'large company' is defined as a company with a turnover exceeding AUD250 million, as it is this subset of companies that contribute significantly to company tax revenue in Australia (58%) and are the target of the ATO tax risk management initiative.

¹²⁰ Floyd J Fowler, *Survey Research Methods: 1 (Applied Social Research Methods)* (Sage Publications, 2009) 59; Don A Dillman, *Mail and Internet Surveys: The Tailored Design Method* (John Wiley, 2nd ed, 2007).

¹²¹ *Ibid*, 59.

¹²² ATO, 'Compliance Program 2011–2012' <<http://www.ato.gov.au/content/downloads/cr00284023compliance.pdf>>, 24.

¹²³ Ken Devos, 'An Investigation Into Australian Personal Tax Evaders—Their Attitudes Towards Compliance And The Penalties For Non-Compliance' (2009) 19(1) *Revenue Law Journal* Article 2

survey can be distinguished on the basis that the potential respondent is the individual in a large company responsible or familiar with the company's tax risk management practices. Previous Australian tax compliance mail surveys relate to individual tax compliance and the potential respondent was the individual taxpayer.¹²⁴ The response rate may also be low because surveys may not have reached the appropriate individual in the company.

Although the response rate is low there is no predetermined minimum response rate required for a mail survey.¹²⁵ The response rate should be judged in light of the specific nature of the survey recipients as complex and multifaceted entities, where tax compliance and tax risk management is handled by a number of staff in the entity with competing demands on their time. Certainly, the potential for bias associated with non-response needs to be considered as it is possible that those survey recipients who had an interest in tax risk management or who had actually addressed tax risk management in their governance practices are more likely to respond to the mail survey.¹²⁶ An analysis of non-response bias compared the characteristics of the early and late completers of the survey to determine whether there are significant differences between them and none were detected.

The percentage of all company taxpayers from the different industry categories shows that companies in a range of industries participated in the survey. As a result, the responses reflect tax risk management processes, approaches and outcomes for a variety of industries. In addition, comparisons with total company taxpayer and total company income do not highlight any substantial discrepancy in the industries reflected in the respondent group.

While the letter accompanying the survey was addressed to the CFO, the CFO did not necessarily complete the survey. Table 2 shows the position of the individuals who completed the survey.

<<http://epublications.bond.edu.au/rlj/vol19/iss1/2>> 14; Pauline Niemiowski, Alexander J Wearing and Steve Baldwin, 'Identifying the Determinants of Australian Taxpayer Compliance' in Adrian J Scott (ed), *XXVI IAREP Annual Colloquium on Economic Psychology: Environment and Wellbeing* (2001) 199; Pauline Niemiowski, Steve Baldwin and Alex Wearing, 'Chapter 18' in Michael Walpole and Chris Evans (eds), *Tax Administration in the 21st Century* (Prospect, 2001) 211.

¹²⁴ Fowler, above n 120.

¹²⁵ Ibid.

¹²⁶ Fowler, above n 120, 221.

Table 2: Position in the company of the individual who completed the survey

	Frequency	Per cent
CFO	47	38.2
Tax director	23	18.7
CEO	4	3.3
Tax manager	28	22.8
Assistant tax manager	1	0.8
Financial controller	9	7.3
Finance manager	4	3.3
Other	7	5.7
Total	123	100.0

The CFO, tax manager and tax director as a group make up 79.7 per cent of all respondents. The individuals in those positions are ordinarily responsible for ensuring that tax risk is managed in accordance with company policy. Importantly, not all companies in the large company sector have a dedicated tax director or manager. The nature and complexity of the tax issues that a large company faces is expected to also determine the structure of the tax function including the number of tax staff and level of responsibility.

Each survey question asked the respondent to provide information on behalf of their company that will contribute to answering a number of specific research questions. The frequency distribution for each of the responses to the closed questions and answers to open-ended questions were analysed and applied to the specific research questions to develop an understanding of tax risk management practices in large Australian companies and the impact on income tax compliance behaviour. A chi-square goodness of fit analysis was also used to determine any relationships between a company's characteristics and the survey responses regarding compliance and tax risk management.

The statistical analysis, together with the analysis of open-ended questions, provides a rich understanding of the tax risk management practices of large Australian companies and the views of individuals responsible for tax risk management. The responses offer a meaningful insight into the income tax compliance behaviour of large Australian companies.

5. RESULTS

Whilst the in-depth interviews and survey asked questions concerning tax risk management practices and their impact more broadly, this article focuses on the results that relate specifically to an understanding of the role of reputational risk in tax decision making in a large Australian company. Because reputational risk has been identified as being so important to large companies, the implications of the results for the leadership within and the accountability and integrity of large companies, cannot be discounted.

5.1 Results relating to reputational tax risk management

All interviewees commented on the importance of the company's reputation and believed that any negative publicity concerning tax compliance¹²⁷ would affect the company's profitability. All noted that the company and its senior management would be most concerned if it was perceived as non-compliant with the tax laws or considered to have taken an aggressive tax position. No interview participant indicated that they take an aggressive tax position, but rather, that they made every effort to comply. They identified one of the key motivators for taking a conservative approach to tax compliance as being their concern for the company's reputation. This concern was clearly articulated by the Board and filtered down to the operational tax decision makers.

Four interview participants stressed the importance of maintaining their reputation as good company taxpayers and further stressed that the potential impact on a company's reputation of any negative publicity concerning possible aggressive arrangements actually resulted in the company accepting a lower level of acceptable tax risk. Three interview participants felt that the importance of the company's good reputation is a key motivator in establishing a tax risk management system to identify tax risks.

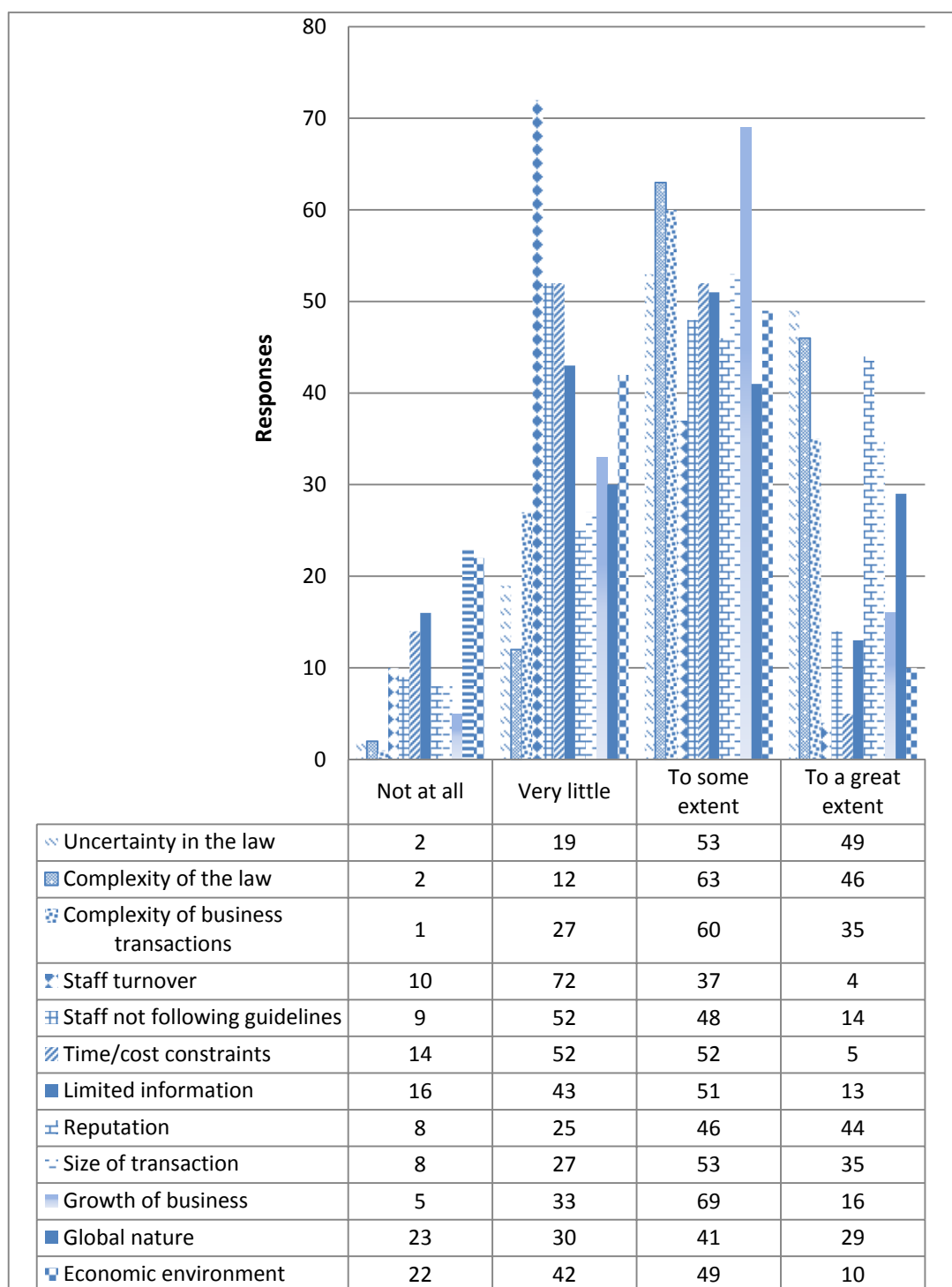
Survey Question 7 asked respondents whether certain factors increase or create tax risk for the company in carrying on its business activities including uncertainty and complexity in the tax laws, complexity of business transactions, staff turnover, staff not following guidelines, time and cost constraints, limited information flow to relevant staff, level of concern for reputation, size of the transaction, growth of the business, global nature of the business and economic environment. Figure 1 summarises the results for the relevant factors.

A significant number of respondent companies (73.2% as detailed in Table 3) indicated that concern for company reputation increases the level of tax risk that needs to be managed to some or a great extent. These respondents were concerned about the impact of tax non-compliance on their reputation.

Table 3: The extent to which the level of concern for reputation increases the level of tax risk (SQ7h)

	Frequency	Per cent
Not at all	8	6.5
Very little	25	20.3
To some extent	46	37.4
To a great extent	44	35.8
Total	123	100.0

¹²⁷ The interviews and survey asked about tax risk and tax decision making. Where the term 'compliance' was used it was meant and understood to mean *ex ante* tax strategy. No confusion was indicated by respondents about whether the questions related to *ex ante* strategic decision making or *ex post compliance* behaviour.

Figure 1: Factors that increase or create tax risk for large companies

5.2 Tax risk management system does affect the level of acceptable tax risk

Survey Question 16 asked the individual completing the survey on behalf of the respondent company whether in their view the current tax risk management system had an effect on the level of tax risk considered acceptable to the company. In addition, Survey Question 16 includes an open-ended component in which the individual on behalf of the respondent company can detail the actual effect on the level of acceptable tax risk and if it has no effect the reasons why. Only 68 of the 124 respondents did have a comprehensive tax risk management system.

While 82.4 per cent of respondent companies indicated that the tax risk management system did have an effect on the level of tax risk considered acceptable (detailed in Table 4 below) the comments by respondents in the open-ended component demonstrate that this is largely a result of the increased awareness and transparency of income tax risk. Potentially the increased awareness and transparency allows greater awareness of reputational risk. Tax decision makers are more informed of the relevant tax risks and possible consequences of their decisions as a result of the comprehensive identification and management of tax risks that the company faces, including reputational risk.

An increasingly global approach to the management of tax risk was identified by a number of respondent companies as ensuring a low level of acceptable tax risk, reflecting a conservative approach to tax risk globally. Some respondent companies indicated that acceptable tax risk is lower because the tax risk management system puts tax at the 'front of mind' of company executives when considering a business issue and staff have a better understanding of potential tax risk. Senior executives are increasingly committed to identifying and managing tax risk in recognition of the low tax risk profile.

Table 4: A Tax risk management system has an effect on the level of tax risk considered acceptable (SQ16)

	Frequency	Per cent
Strongly disagree	1	1.5
Disagree	5	7.4
Undecided	6	8.8
Agree	35	51.5
Strongly agree	21	30.9
Total	68	100.0

The results set out in Table 5 demonstrate that 73.5 per cent of respondent companies felt that the tax risk management system resulted in the lowest level of tax risk (Survey Question 23e). While 10.3 per cent disagreed with the view that the tax risk management system results in the lowest level of tax risk the remaining 16.2 per cent were undecided.

The large undecided component suggests that, in the absence of concrete evidence the tax risk management system results in the lowest level of tax risk, respondent companies were unable to respond to the question posed. As a substantial majority did feel that the tax risk management system results in the lowest level of tax risk it can be argued that a tax risk management system results in an improvement in tax compliance as company taxpayers take a more conservative and less aggressive approach in making tax compliance decisions.

Table 5: A tax risk management system results in the lowest level of tax risk (SQ23e)

	Frequency	Per cent
Strongly disagree	1	1.5
Disagree	6	8.8
Undecided	11	16.2
Agree	34	50.0
Strongly agree	16	23.5
Total	68	100.0

5.3 Statements and/or guidelines on what constitutes a tax risk

Table 6 details the percentage of respondent companies that have, and do not have statements and/or guidelines on what constitutes a tax risk that are used in the tax risk management process. A majority of respondent companies (54.5%) did not have statements and/or guidelines on what constitutes a tax risk. These results indicate that in many large companies there is a need for a clear definition of what constitutes a tax risk to ensure that all individuals involved in the tax risk management process have an understanding as to where and when a tax risk may arise.

Table 6: Companies that have statements and/or guidelines on what constitutes a tax risk (SQ6)

	Frequency	Per cent
No	67	54.5
Yes	56	45.5
Total	123	100.0

The open-ended component to Survey Question 6 enabled respondent companies that have statements and/or guidelines on what constitutes a tax risk to elaborate on the nature of those statements and/or guidelines. A respondent's definition of tax risk tended to focus on transaction risk, that is, the tax risk associated with specific transactions that the company enters into including "UTBs subject to a value threshold".¹²⁸ Some used the FIN48 criteria for UTB to determine the existence of a tax risk.¹²⁹

A number of respondent companies refer to policy guidelines that they use to determine the existence of a tax risk including not only transactional risk (the risk associated with specific transactions that a company enters) but also operational risk (the risk associated with the application of tax laws to the day to day operations) and compliance risk (the risk of failing to comply with all the various compliance requirements in the tax law). Only five respondent companies indicate that tax risk also includes the potential impact of more generic tax risk such as the impact on a company's reputation of negative publicity relating to tax aggressive decision making.

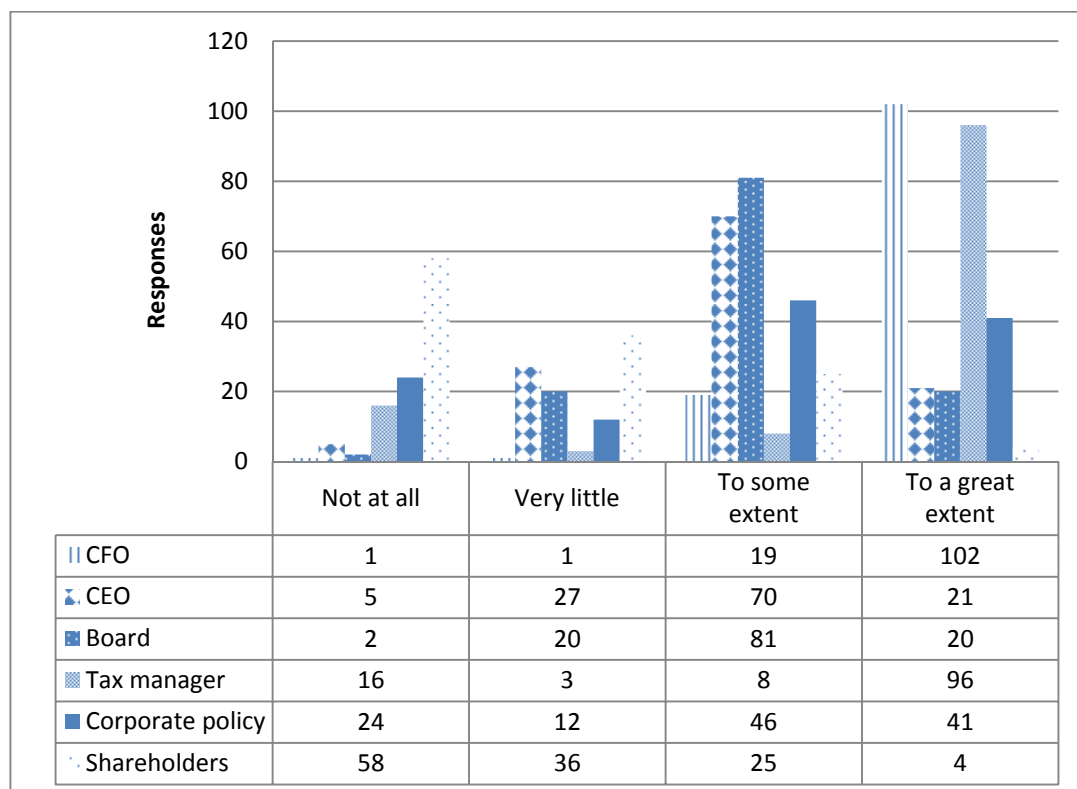
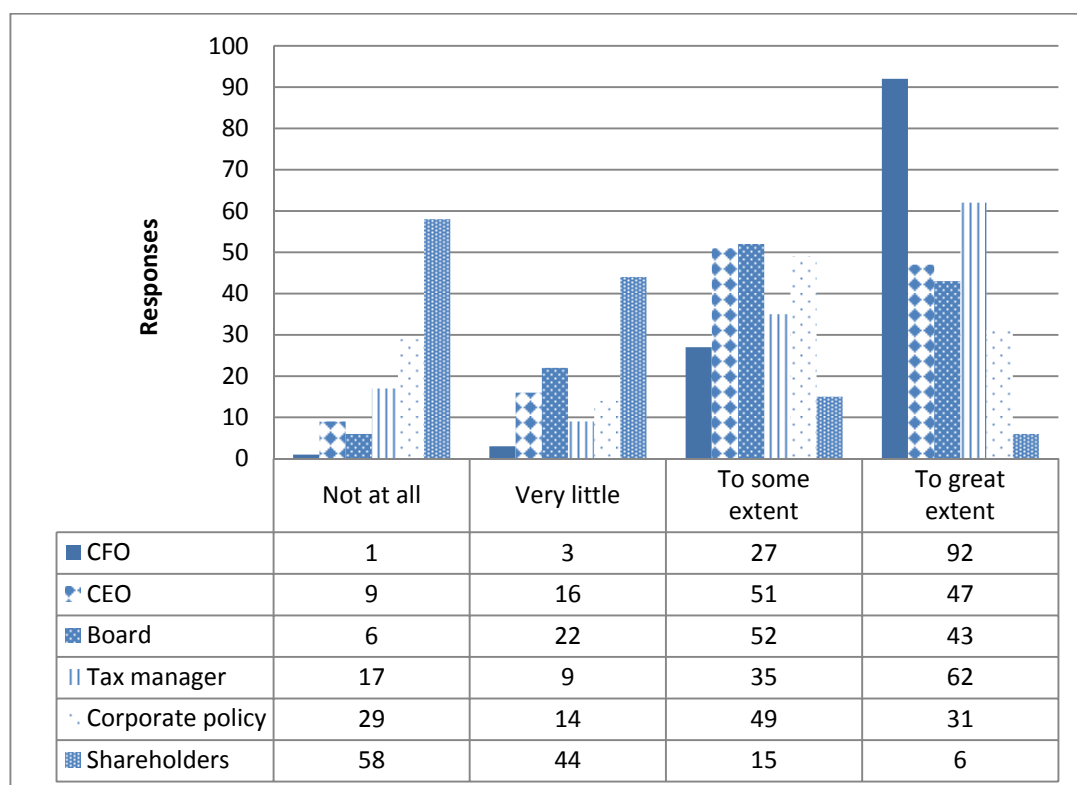
Only five respondent companies had a comprehensive definition of tax risk. A failure by the majority of respondents to use a comprehensive definition of tax risk may result in a number of tax risks, including reputational risk, being overlooked in the company's review process.

5.4 Individuals within companies who are involved and ultimately make the final decision on the acceptable level of tax risk

Figures 2 and 3 identify the individuals within respondent companies that are involved and ultimately make the final decision on their company's acceptable level of tax risk. The comparative figures demonstrate that the CFO and the tax manager are the most involved in the determination of acceptable tax risk and that the Board and the CEO also have a significant role. Company group policy was also shown to be a significant influencing factor. The shareholders were identified in only a few instances as having a significant role. The majority of respondents felt that the shareholders have very little or no involvement in the determination of an acceptable level of tax risk.

¹²⁸ Respondent Number 12.

¹²⁹ FIN48 states that firms should recognise in their financial statements the benefit of a tax position only after determining that it is more likely than not that the revenue authority would maintain the tax position after audit. In addition, the amount recognised in the financial statements should be the largest benefit that has a greater than 50 per cent likelihood of being realised upon settlement with the revenue authority.

Figure 2: Individuals involved in determination of acceptable tax risk**Figure 3: Individual who make the determination of acceptable tax risk**

Tables 7 and 8 show the extent to which the shareholders determine the acceptable level of risk. The shareholders in only 23.6 per cent of respondent companies were involved in the determination of the acceptable level of tax risk to at least some extent. The shareholders make only a small contribution in establishing the level of tax risk that will be tolerated and ultimately to at least some extent make the final decision on the acceptable level of tax risk in only 17.1 per cent of respondent companies.

Table 7: The extent to which the shareholders are involved in the determination of the acceptable level of tax risk (SQ4e)

	Frequency	Per cent
Not at all	58	47.2
Very little	36	29.3
To some extent	25	20.3
To a great extent	4	3.3
Total	123	100.0

Table 8: The extent to which the shareholders ultimately determine the acceptable level of tax risk (SQ5e)

	Frequency	Per cent
Not at all	58	47.2
Very little	44	35.8
To some extent	15	12.2
To a great extent	6	4.9
Total	123	100.0

5.5 Tax risk profile of respondents

Table 9 details the tax risk profile¹³⁰ of respondents with a majority (60.2%) indicating that they adopt a very low or low tax risk profile. Moderate tax risk is acceptable to 30.9 per cent of respondent companies and only 8.9 per cent of respondents are prepared to accept high or very high tax risk.

¹³⁰ Tax risk profile is defined in the survey and used in this article as 'the behavior of a taxpayer towards tax risk. The more aggressive the taxpayer's position with respect to tax risk, the higher the tax risk profile. The less aggressive the taxpayer's position with respect to tax risk, the lower the tax risk profile'.

Table 9: The tax risk profile of companies participating in the survey (SQ9)

	Frequency	Per cent
Very low	21	17.1
Low	53	43.1
Moderate	38	30.9
High	10	8.1
Very high	1	0.8
Total	123	100.0

The tax risk profile of respondent public companies (listed and unlisted) and private companies were analysed. The detailed cross tabulation set out at Table 10 below indicates that public companies are more likely to have a very low or low tax risk profile and private companies are more likely to have a moderate to very high tax risk profile.

Table 10: Cross tabulation company type and tax risk profile

Company type		Tax risk profile - Grouped responses (Survey Question 9)		
		very low/low	moderate/high/ very high	Total
Private company	Count	21	23	44
	Per cent private company	47.7%	52.3%	100.0%
	Per cent tax risk profile	28.4%	46.9%	35.8%
	Per cent of total	17.1%	18.7%	35.8%
Public company	Count	53	26	79
	Per cent public company	67.1%	32.9%	100.0%
	Per cent tax risk profile	71.6%	53.1%	64.2%
	Per cent of total	43.1%	21.1%	64.2%
Total	Count	74	49	123
	Per cent all companies	60.2%	39.8%	100.0%
	Per cent tax risk profile	100.0%	100.0%	100.0%
	Per cent of total	60.2%	39.8%	100.0%

The following section of this article discusses the research results detailed in this section looking specifically at the role of the tax risk management system, tax risk profile, reputational risk and tax aggressive decision making.

6. IMPLICATIONS

The results presented here demonstrate that, whilst a company's tax aggressiveness can have an impact on a company's reputation (as discussed in this article at section 2), most tax risk management systems used by large Australian companies do not systematically identify reputational risk as one of the tax risks that needs to be managed. That is the definition of tax risk used by large Australian companies does not include reputational risk yet a large majority of companies recognise their concern for reputation increases or creates tax risk.

Although a tax risk management system results in a lower level of acceptable tax risk it may not ensure that tax decision-makers are informed of the potential negative impact on reputation of a particular tax position taken. A company that has a comprehensive tax risk management system that identifies reputational risk will make more informed and potentially less aggressive tax decisions than a company that does not have a comprehensive tax risk management system that recognises reputational risk. The CFO and tax manager are most involved in the determination of the level of acceptable tax risk whilst shareholders have very little involvement. The results in relation to shareholders indicate that despite the increasing discussion and identification of CSR as a shareholder concern reflecting community values, few large companies consider the shareholders' views or preferences in relation to tax aggressiveness. This suggests that shareholders do not send clear messages concerning the level of tax aggressiveness they believe to be acceptable, and do not demonstrate an interest in 'their' company's income tax strategy *ex ante*. Currently it appears to be lobby groups that send messages to keep large companies accountable.

Private companies accept a higher tax risk profile than public companies and this result may be due to the fact that private companies are less exposed to share price fluctuation, requirements to disclose financial information and reputational risk generally. Research by Rice supports the relationship between company type and tax aggressiveness.¹³¹ Rice identified that tax compliance is positively correlated with being a publicly listed company and attributed this to the managers being more likely to be independent of the shareholders, and as a result under less pressure to reduce taxes.¹³²

Ultimately this research has identified that a comprehensive tax risk management system, one that considers all tax risks including reputational risk, results in more informed tax decision-making and constitutes good governance practice for a large company incorporated in Australia. This finding is of relevance not only to corporate taxpayers, but to tax policymakers and administrators who seek to understand the tax strategies adopted by this important taxpayer group. The extent to which the findings presented here apply to other jurisdictions is unclear, particularly in the light of differences in the legal and administrative frameworks that regulate company tax decision-making in other countries.

¹³¹ Rice, above n 103.

¹³² Ibid.

7. CONCLUSION

Given the importance of the large company taxpayers to revenue collections globally, it is believed that this research makes an important contribution. Notwithstanding, there is considerable scope for further research into the area of corporate tax strategy and the interconnected issues of tax risk management systems, reputational risk, CSR and increased tax disclosure requirements. The importance of reputational risk for large companies suggests that companies will most easily avoid adverse publicity about their tax if they systematically and routinely flag and address reputation as a tax risk and factor the need to be accountable to the public into their tax strategy.

8. APPENDICES

Appendix 1: In-depth interviews

Interviewer: Catriona Lavermicocca, PhD student, UNSW

This research project forms part of the data collection for the purposes of completion of a PhD in Taxation at the Australian School of Taxation (ATAX) at UNSW. The title of the PhD thesis is 'Tax Risk Management as a Corporate Governance Issue in Australia and the Impact on Income Tax Compliance by Large Company Taxpayers'.

Proposed questions for in-depth interviews concerning tax risk management:

1. To what extent does your organisation consider/evaluate tax risk?
2. Does your organisation have clear statements/guidelines on what constitutes a tax risk?
3. Who (not by name but by title) in the organisation determines the acceptable level of tax risk?
4. Do the organisation's corporate governance guidelines require tax risk to be managed?
5. Does your organisation have a tax risk management system?
6. What systems/procedures does your organisation have in place to ensure that tax risk is managed? To what extent are those systems/procedures documented and reviewed for compliance?
7. Have there been any recent changes in the approach the organisation takes to tax risk management?
8. What criteria are used to determine the acceptable level of tax risk in your organisation?
9. What factors do you consider have an impact on the level of tax risk that the organisation faces?
10. What limitations, if any, does the organisation face in managing tax risk?
11. What pressures do you believe have had an impact on the organisation's decision to adopt/not adopt a tax risk management system?
12. To what extent have the following had an impact on the organisation's decision to adopt/not adopt a tax risk management system?
 - ATO;
 - Shareholders;
 - Customers;
 - Stock market/listing rules;
 - Directors; and
 - SOX legislation.
13. What influence have the ATO announcements had on your organisation's tax risk management practices?
14. Have you received any correspondence from or entered into discussions with the ATO concerning tax risk management and tax decision-making practices?
15. Who (not by name but by title) are the key tax decision-makers in your organisation? Is there any board/director involvement in tax decision-making and, if any, what is the level of that involvement?
16. What are the performance measures in respect of the key tax decision-makers in your organisation?

17. What do you consider to be the impact of tax risk management systems on the determination of the acceptable level of tax risk?
18. Is the organisation more or less tax risk averse (or has there been no change) after the introduction of a tax risk management system?
19. To what extent does the organisation consider corporate social responsibility issues and if it does, does that include a consideration of the organisation's tax compliance profile?

Appendix 2: Survey of tax risk management practices of large Australian companies

Completing the Survey

You can answer most questions by ticking the appropriate box. In some instances further detail is requested. Please return your completed survey form in the reply paid envelope provided.

Definitions of some terms used in the survey

Compliance with the income tax laws - the taxpayer files all required income tax returns accurately and at the proper time, pays all outstanding taxes as they fall due and maintains all required records. The accuracy of the return and the records required are determined in accordance with the prevailing income tax laws, rulings, return instructions and court decisions.

Income tax liability - net income tax payable by a taxpayer in respect of a particular year of income

Large company - gross turnover exceeds \$250 million

Non-compliance with the income tax laws – the taxpayer does not file all required income tax returns accurately and at the proper time, and/or does not pay all outstanding taxes as they fall due and/or does not maintain all required records and/or the accuracy of the return and the records required are not in all instances determined in accordance with the prevailing income tax laws, rulings, return instructions and court decisions.

Operationalised - put in place and acted upon by decision makers as part of the ongoing and active business systems used by the organisation

Tax risk - any event, action, or inaction in tax strategy, operations, financial reporting, or compliance that adversely affects either the company's tax or business operations or results in an unanticipated or unacceptable level of monetary, financial statement or reputational exposure.

Tax risk management system - documented and operationalised systems and procedures to identify and manage tax risks

Tax risk profile - reflects the behavior of a taxpayer towards tax risk. The more aggressive the taxpayer's position with respect to tax risk, the higher the tax risk profile. The less aggressive the taxpayer's position with respect to tax risk, the lower the tax risk profile.

Please turn the page to commence the survey

Survey questions

1) Please indicate your company type

Public company ☐ Private company ☐
If your company is a public company is it listed on the Australian Securities Exchange?
Yes ☐ No ☐

2) In which of the following industries does the company carry on business? If your company operates in more than one industry please indicate the industry that best describes the industry in which the company carries on business.

Agriculture, forestry and fishing ☐
Mining ☐
Manufacturing ☐
Electricity, gas, water and waste services ☐
Construction ☐
Wholesale trade ☐
Retail trade ☐
Accommodation and food services ☐
Transport, postal and warehousing ☐
Information media and telecommunications ☐
Financial and insurance services ☐
Rental, hiring and real estate services ☐
Professional, scientific and technical services ☐
Administrative and support services ☐
Public administration and safety ☐
Education and training ☐
Health care and social assistance ☐
Arts and recreation services ☐
Other services ☐
Other ☐
Please specify.....

3) What is your position in the company?

Chief Financial Officer ☐
Tax Director ☐
Chief Executive Officer ☐
Tax Manager ☐
Assistant Tax Manager ☐
Other ☐
Please specify

4) To what extent are the following persons involved in the determination of the acceptable level of tax risk with respect to a transaction or series of transactions?

Tax risk - any event, action, or inaction in tax strategy, operations, financial reporting, or compliance that adversely affects either the company's tax or business operations or results in an unanticipated or unacceptable level of monetary, financial statement or reputational exposure.

a) CFO	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
b) CEO	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
c) Board of Directors	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
d) Tax manager	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
e) Shareholders	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
f) Corporate group policy	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
g) Other ☐ Please provide detail				

5) To what extent do the following persons in your company **ultimately make the final decision on the acceptable level of tax risk with respect to a transaction or series of transactions?**

a) CFO	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
b) CEO	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
c) Board of Directors	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
d) Tax manager	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
e) Shareholders	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
f) Corporate group policy	To a great extent ☐	To some extent ☐	Very little ☐	Not at all ☐
g) Other ☐ Please provide detail				

6) Does your company have **statements and/or guidelines** on what constitutes a tax risk?

Yes ☐ No ☐
If yes, what constitutes a tax risk according to your company's statements and/or guidelines?.....

7) Please indicate the extent to which each of the following factors increase the level of tax risk your company is exposed to in carrying on its business activities.

a) Uncertainty in the application of the income tax law To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
b) Complexity of the income tax law To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
c) Complexity of business transactions To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
d) Staff turnover To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
e) Staff not following guidelines To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
f) Time and/or cost constraints To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
g) Limited information provided to tax staff by other divisions within the company To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
h) Level of concern for reputation To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
i) Size of the transaction To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
j) Growth of the business To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
k) Global nature of the business To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
l) Economic environment To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
m) Other ☐ Please provide detail

8) How important is compliance with the income tax laws to your company?

Compliance with the income tax laws - the taxpayer does file all required income tax returns accurately and at the proper time, pays all outstanding taxes as they fall due and maintains all required records. The accuracy of the return and the records required are determined in accordance with the prevailing income tax laws, rulings, return instructions and court decisions.

Very important	☐
Important	☐
Moderately important	☐
Of little importance	☐
Unimportant	☐

9) Which of the following best describes the tax risk profile of your company?

Tax risk profile – reflects the behavior of a taxpayer towards tax risk. The more aggressive the taxpayer's position with respect to tax risk, the higher the tax risk profile. The less aggressive the taxpayer's position with respect to tax risk, the lower the tax risk profile.

Very high	☐	High	☐	Moderate	☐	Low	☐	Very low	☐
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10) Has there been a change in the tax risk profile of your company in the last three financial years?Yes ☐ No ☐

If yes what is the nature of the change and what do you believe to be the reason for it?

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11) Does your company have systems and/or procedures in place to identify and manage tax risks?Yes ☐ No ☐

If yes describe the systems and/or procedures in place to identify and manage tax risks and continue on to question 12)

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If you answered NO to question 11) the survey is now complete. Thank you**If you answered YES to question 11)
please turn the page and continue this survey.**

12) Considering the following factors please indicate the extent to which they limit the ability of your company to identify and manage the tax risks to which the company is exposed.

a) Uncertainty in the application of the income tax laws To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
b) Complexity of the income tax laws To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
c) Complexity of business transactions To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
d) Staff turnover To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
e) Staff not following guidelines To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
f) Time and/or cost constraints To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
g) Limited information provided to tax staff by other divisions within the company To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
h) Commercial pressure outside your tax department To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
i) Limitations of ATO staff To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
j) Country or countries where the company carries on business To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐
k) Other ☐ Please provide detail

13) Are the current systems and/or procedures used by your company to identify and manage tax risks documented?

To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐

14) Are the current systems and/or procedures used by your company to identify and manage tax risks operationalised in the company's business systems?

***Operationalised** - put in place and acted upon by decision makers as part of the ongoing and active business systems used by the organisation*

To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐

The following questions should only be answered if your company has systems and/or procedures in place to identify and manage tax risks that are to some extent documented and operationalised. If that is the case please continue.

If your company DOES NOT have systems and/or procedures in place to identify and manage tax risks that are to some extent documented and operationalised the survey is now complete.

Thank you

For the purposes of this survey systems and/or procedures that identify and manage tax risks that are to some extent documented and operationalised constitute a tax risk management system (TRMS).

15) When was the company's current tax risk management system introduced?

***Tax risk management system** – documented and operationalised systems and procedures to identify and manage tax risks*

In the 2011 financial year? ☐
In the 2010 financial year? ☐
In the 2009 financial year? ☐
In the 2008 financial year? ☐
Prior to the 2008 financial year? ☐
Progressively over a number of years ☐
If so please specify the relevant years
.....
.....
.....
.....

16) The current tax risk management system does have an effect on the level of tax risk considered acceptable by your company.

Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
If you agree, describe ways in which the current tax risk management system has an effect on the level of tax risk considered acceptable by your company.
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.....
If you disagree, why do you believe the current tax risk management system does not have an effect on the level of tax risk considered acceptable to your company?
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17) The current tax risk management system ensures compliance with the income tax laws by your company.

Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐

If you agree, describe ways in which the current tax risk management system ensures compliance with the income tax laws by your company.

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If you disagree, why do you believe the current tax risk management system does not ensure compliance with the income tax laws by your company?

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18) The current tax risk management system results in the identification of potential non-compliance with the income tax laws that would not otherwise be identified by your company.

Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐

If you agree, describe ways in which the current tax risk management system identifies potential non-compliance with the income tax laws that would not otherwise be identified by your company.

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If you disagree, why do you believe the current tax risk management system does not identify non-compliance with the income tax laws that would not otherwise be identified by your company?

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19) If you disagree with the statement at 18) above you can continue to 20).

If you agree with the statement at 18) above, does your company act to ensure potential non-compliance with the income tax laws identified by your current tax risk management system do not occur?

To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐

20) The current tax risk management system results in the identification of opportunities to minimise your company's income tax liability that would not otherwise be identified.

Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐

If you agree, in what way does the current tax risk management system result in the identification of opportunities to minimise your company's income tax liability that would not otherwise be identified?

.....

If you disagree, why do you believe the current tax risk management system does not result in the identification opportunities to minimise your company's income tax liability that would not otherwise be identified?

.....

21) If you disagree with the statement at 20) above you can continue to 22)

If you agree with the statement at 20) above, does your company act to ensure opportunities to minimise the company's income tax liability identified by your current tax risk management system are put in place?

To a great extent ☐ To some extent ☐ Very little ☐ Not at all ☐

22) The current tax risk management system ensures that the following persons are informed concerning the tax risks that your company is exposed to

a) Directors
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
b) Tax decision makers
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
c) Chief Financial Officer
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
d) Chief Executive Officer
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
e) Chairman of the Board
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
f) Other person Please specify
.....
.....
.....
.....

23) The current tax risk management system results in:

a) Better documented tax risks
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
b) More informed tax decision making
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
c) Greater range of tax risks identified
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
d) Improvement in the management of tax risks
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
e) The lowest level of tax risk
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
f) Improvement in compliance with the income tax laws
Strongly agree ☐ Agree ☐ Undecided ☐ Disagree ☐ Strongly disagree ☐
g) Other benefits Please specify
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24) Has your company been the subject of an adjustment to taxable income as a consequence of audit by the ATO relating to any of the last three financial years?

Yes ☐ No ☐

If yes, was the company aware of a tax risk associated with the issue that gave rise to the adjustment by the ATO before the audit commenced?

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25) Are you aware of a transaction or series of transactions in respect of which the income tax treatment adopted by the company was subsequently found to be incorrect relating to any of the last three financial years?

Yes ☐ No ☐

If yes, were you aware of any tax risk associated with that transaction or series of transactions when the transaction or series of transactions was entered into?

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The survey is now complete.

Thank you for participating