Why global tax inquiries and disputes are increasing

Our research reveals a sharp increase in the numbers of tax inquiries and disputes worldwide, with a broad range of issues giving rise to investigations

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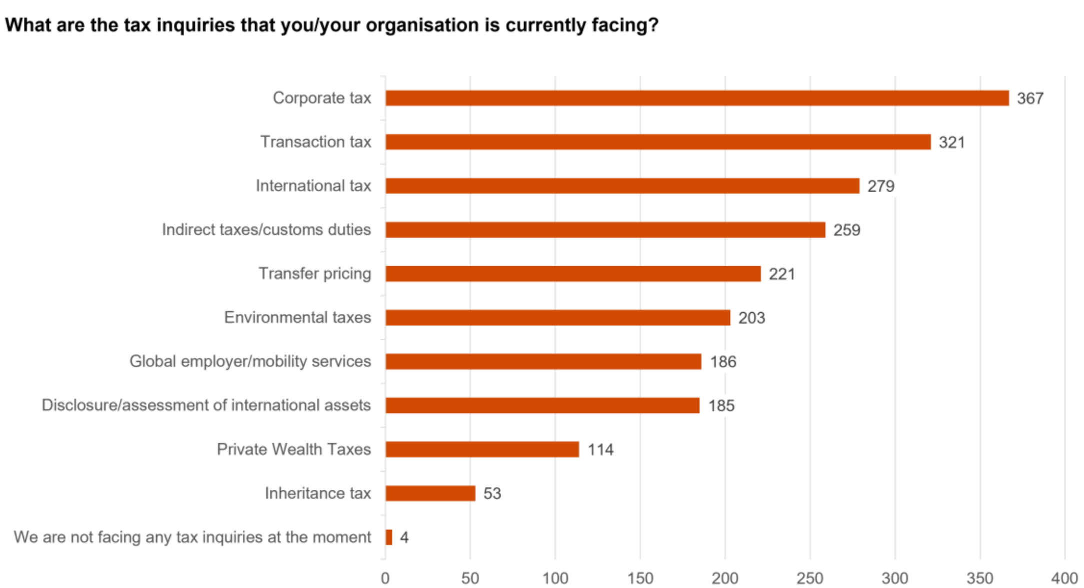
Increases in the numbers of tax inquiries and disputes worldwide reflect the reality that a broad range of issues is giving rise to investigations

The more interventionist and proactive stance of tax authorities in multiple jurisdictions is piling the pressure on to tax functions. And of the more than 2,000 inquiries faced by businesses taking part in this research, some 43% – more than 900 – have subsequently turned into full-blown disputes.

Inevitably, the nature of tax inquiries varies from one territory to another. But as Figure 1 shows, inquiries are spread across a broad range of taxes. While businesses are most likely to report they have received inquiries about their corporate tax affairs, transaction taxes, international taxes and indirect taxes have all given rise to significant numbers of inquiries too.

Tax functions dealing with such a broad spread of inquiries will need access to a wide range of specialist expertise. In addition, the increasingly tense interplay between national and international tax regulation – with individual jurisdictions increasingly competing for their share of the tax take – adds to the difficulty of dealing with tax inquiries.

Figure 1: What gives rise to tax inquiries



Moreover, while tax functions will want to resolve inquiries as quickly as possible, the fact that more than four in 10 cases are evolving into disputes with tax authorities will worry both Heads of Tax and CFOs alike. These disputes will demand further resources and potentially expose businesses to significant uncertainty and costs, as well as the potential for unexpected liabilities to tax.

In practice, no single area of tax appears to be much more likely to generate a dispute. At the top of the list, more than half of businesses (53%) say they have become embroiled in at least one dispute related to tax deductions (see Figure 2). One explanation for this may be the growing numbers of governments worldwide offering tax incentives to encourage businesses to invest in areas such as research and development; tax authorities are then tasked with ensuring that claims for such incentives are accurate and justified. The treatment of debt and debt interest may also be giving rise to disputes.

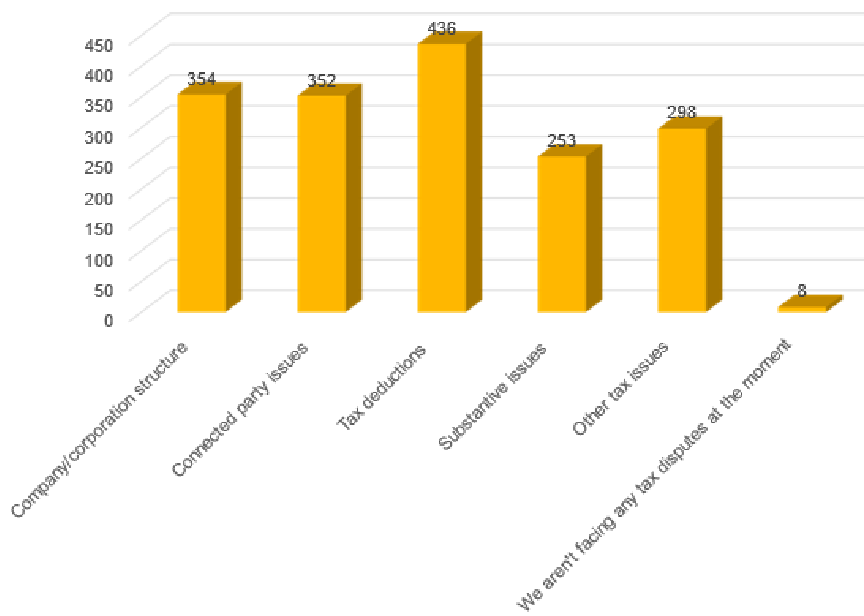
Elsewhere, 43% of businesses say they have suffered a dispute related to connected party issues. Transfer pricing issues, for example, are potentially troublesome, with service payment questions also escalating into disputes. On the former, 86% of businesses involved in a transfer pricing dispute say the issue is around methodology – the methods of calculation used by entities to determine their transfer prices; 41% cite transactional issues, pointing to disagreements about the underlying goods or services involved.

Meanwhile, the same proportion of businesses (43%) say they have been involved in disputes related to corporate structures. These include disputes in areas such as special purpose vehicles, residency, hybrid structures, permanent establishment and beneficial ownership, all of which often prove highly complicated to resolve.

As for other tax issues, PwC professionals point to a growing number of disputes over foreign tax credits; more broadly, increasing numbers of cross-border disputes may also reflect the potential conflict between national and international regulation. Future disputes, moreover, may reflect shifting tax regulation; in the UK, for example, the recent announcement of an increase in employers' national insurance rates is likely to lead to many businesses taking steps to mitigate higher costs, with disputes in some cases likely to follow.

Figure 2: Where tax disputes originate

What types of tax disputes (if any) is your organisation currently facing with regulatory authorities



Is there a way to head off inquiries and, particularly, disputes? With tax authorities under pressure to increase scrutiny of corporates, this may be difficult. However, businesses do now need to reflect on their appetite for risk – the extent to which an aggressive approach to tax is likely to give rise to a potentially time-consuming and expensive inquiry or dispute.

There is no one-size-fits-all answer to such questions. Specialist advisers with good understanding of the preoccupations of national and international tax authorities are well-placed to support businesses, offering guidance on where individual regulators ae most likely to take a rough line. This may help businesses identify areas of their tax affairs where caution is most advisable. Proactivity is important.

Ultimately, however, every organisation needs to take a view for itself on risk. Some businesses will prioritise minimising their liability – and will accept this leaves them more vulnerable to inquiries and disputes; that may require increased resourcing for their tax functions. Others will focus on avoiding such flashpoints to the greatest possible extent.

Thank you