Recent Tax Governance update in Australia

10 August 2017

Introduction

The global tax landscape is rapidly changing, and tax transparency has emerged as a key area of focus for governments and tax authorities around the world. Clearly, the OECD BEPS Project was designed to prevent and discourage multinational companies from having inappropriate tax outcomes and alsoartificial tax avoidance. Accordingly, tax authorities in various countries are now in the process of introducing their own new local-country regimes – some of which are aligned with the OECD's BEPS Report; others taking it even further. In addition, a huge degree of public awareness of BEPS and a desire for greater tax transparency by multinationals has occurred around the globe. Examples of this include the public protests in the UK against certain US multinationals that even led to a voluntary payment of UK tax, leaking of confidential taxpayer information to the public press, and ongoing articles in newspapers and media from special-interest groups campaigning against multinational tax avoidance. Given these prominence of issues in connection with tax transparency in the press and global community, managing tax risks and establishing tax governance structures has become increasingly relevant.

In Australia, tax transparency has increased exponentially in the last few years, and in some areas, Australia is a global leader in transparency. The Australian Taxation Office (ATO) have been raising tax governance from various perspectives since more than 10 years ago, culminating in the release of the Tax Risk Management and Governance Review Guide in January 2017. It is fair to say that this guide reflects the ATO's expectations of companies operating in Australia in terms of tax governance and sets the benchmark for ATO's future review of tax governance. Most recently, the ATO has announced that they will be reviewing tax governance frameworks of Australian Top 1,000 companies over next 4 years.

In this article, we highlight the recent movement of ATO with regard to tax governance, prospective influence to Japanese taxpayers and actions that could need to be taken.

Overview of the movement on tax governance in Australia

Following the release of the first iteration in 2015, the ATO has published a substantial update to its Tax Risk Management and Governance Review Guide, containing new guidance for directors of companies and recommended self-assessment procedures. The purpose of this latest update is to assist taxpayers to understand the ATO's shift beyond checking whether policies exist to actually testing whether tax risk management processes and procedures are operating effectively. It is clear that the ATO expects that large business can provide evidence of the fact that they are operating a robust tax risk management and governance framework. Further, where a formalized tax governance framework document is in place and periodic assessments of Board-level and management-level tax controls are carried out, this will provide the ATO with evidence that supports "Justified trust"(Justified trust is a concept from the OECD and is a reasonable conclusion based on sufficient evidence that the taxpayer is complying with their tax obligations and paying the right amount of tax on its economic activities connected to Australia.) and will influence the risk rating assigned to taxpayers by the ATO.

Most recently, the ATO announced the Top 1,000 Multinationals and Public Companies Tax Performance Program that the ATO will conduct a review of tax governance over next 4 years. Accordingly, now is the right time to perform (at the very least) a gap analysis (see below) of current tax governance policies, procedures and controls and document these taking into consideration the ATO's guideline.

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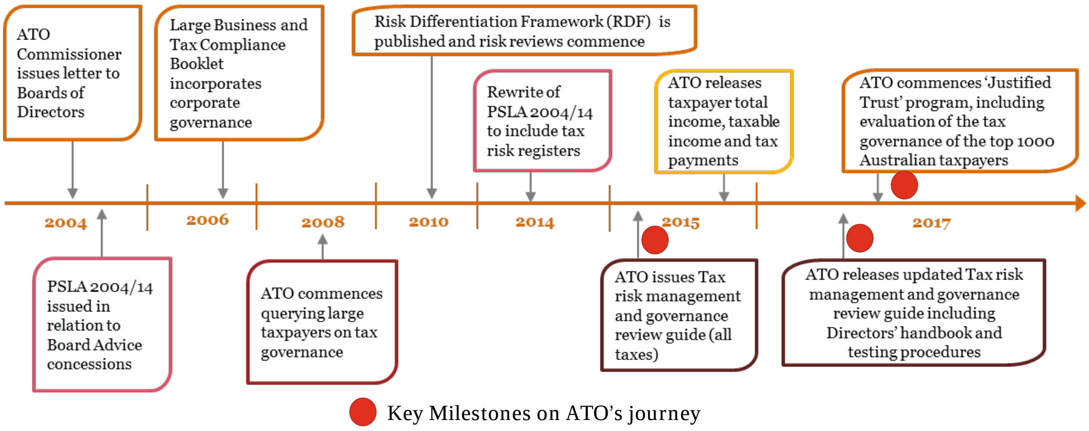
ATO's journey so far with regard to the tax governance



ATO's guideline – "Tax risk management and governance review guide"

"Tax Risk Management and Governance Review Guide" was issued in July 2015 and updated January 2017. The aim of the guide is to help taxpayers understand what the ATO believes better tax corporate governance practices look like, so the taxpayers can:

- Develop their own tax governance and internal control framework
- Test the robustness of the design of their framework against our benchmarks; and
- Understand how to demonstrate the operating effectiveness of their key internal controls to stakeholders.

The updated Guide clearly defines what the ATO considers to be "*better practice*" (see below example). It is therefore not expected that all taxpayers will satisfy all aspects of the Guide. However, taxpayers should be mindful that the ATO's assessment of an organisation's tax governance framework directly impacts on whether the ATO has "justified trust" which is about the ATO obtaining objective evidence that would lead a reasonable person to conclude a particular taxpayer paid the right amount of tax.

This new section of the Guide (self-assessment procedure) gives taxpayers a clear expectation of the ATO's approach to governance and highlights the types of questions the ATO may ask in a review of tax risk management and governance. Those taxpayers who comply with the Guide are more likely to be able to provide a level of "justified trust" to the ATO under the ATO's program and therefore maintain/lower their risk rating which in turn will determine the extent of tax audits/reviews.

The Guide also outlines key principles for tax risk management and governance, separated into board-level controls and management-level controls. These are summarised in the table below.

Board-level responsibilities	***Managerial-level responsibilities***
Formalised tax control framework	Roles and responsibilities are clearly understood
Roles and responsibilities are clearly understood	Senior management confident of capacity and capability
The board is appropriately informed	Significant transactions are identified
Periodic internal control testing	Controls in place for data - General IT controls
	Record-keeping policies
	Documented control frameworks
	Procedures to explain significant differences
	Complete and accurate tax disclosures
	Legal and administrative changes

Examples of better practice

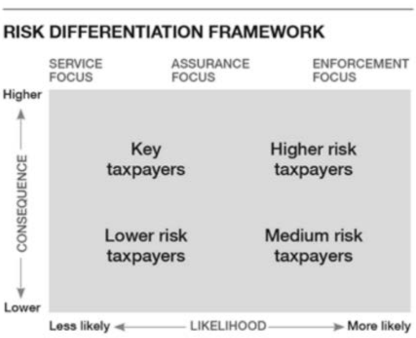
This Guide provides taxpayer with the opportunity to contrast their tax risk management and governance framework against the ATO better practices. During a governance review, taxpayers are encouraged to describe their compensating controls, to demonstrate how the entity manages their tax risks. If the framework does not align exactly with the ATO's better practices, taxpayers may be required to describe why these are not applicable to their circumstances. An 'if not, why not' approach is suggested in the Guide. The examples of better practice are set out in the Guide as follows;

- A formal tax strategy document that provides details of how the organisation identifies and manages tax risk.
- Documented role and responsibility descriptions for company directors.
- Programs for inducting new directors include briefings on key accounting and tax issues
- Annual reviews of the risk management framework at board meeting
- Regular to the board by management on how tax issues and risks are trending
- Evidence that the board (or sub-committee) has reviewed the results presented by management of control framework testing
- Formal documents including role descriptions for tax compliance, policies that specify methods and frequencies for reviewing and escalating risks in the tax risk register, including follow-up of identified tax risks.
- A policy for significant tax transactions that specifies the value of what would constitute a significant transaction, details the types of transactions to be escalated to senior management or the board, outline the threshold where independent external tax advice should be sought
- A formally documented record-keeping policy for tax, including appropriate timeframes for the retention of records
- Staff access to guidance notes via an intranet, or a set of procedures that are readily accessible
- Working papers reviewed and approved by management, indicating that they have checked the correct application of tax law to accounting transactions and accurate calculation of the tax return, etc.

ATO's program – Streamlined assurance reviews of the top 1,000 taxpayers

The ATO announced that they will undertake the Top 1,000 Multinationals and Public Companies Tax Performance Program over next 4 years. The ATO program is aimed at obtaining evidence that the top 1,000 multinational and public companies are paying the right amount of tax and identifying and addressing tax risks to help enable justified trust in large corporates by the ATO as well as the wider community. The program has commenced with the top 100 in 2017. Letters to these top 100 should have been received in relation to governance review. The remainder of the top 1,000 (some have already received letters) and the ATO seems to have focused on loss making companies as a starting point. Depending on the outcome, the ATO will review the taxpayer's risk rating based on the Risk-differentiation framework and reassess their engagement approach.

Risk Differentiation framework



The ATO issued "Risk-differentiation framework" (RDF) in October 2014 for large business taxpayers (the ATO defines large businesses as those taxpayers with turnover levels above $250 million). The RDF is based on ATO's perception of both the:

- estimated likelihood of you having a tax position that the ATO disagrees with, or you have misreported your tax obligations
- consequences of that potential non-compliance

Taxpayers might be re-categorized through the ATO's more recent program.

What are potential influences to Japanese taxpayers?

Considering the above, it is expected that whether or not to be able to provide a level of "justified trust" to the ATO under the ATO's program may affect you in terms of the perspectives below.

	Positive	**Negative**
Risk rating	Improve your chances of obtaining a low risk rating from the ATO	Increased chance of obtaining a higher risk rating from the ATO
Time & Cost	Reduce the likelihood of the ATO intervention, and the time spent dealing with tax authority queries	Increased the ATO intervention and time spent dealing with the ATO queries
Reputation Risk	Communicate transparently and with confidence, internally and externally on tax, thereby reducing the risk of tax reputational damage and unwanted tax exposures	Key tax risks not covered by effective controls create a greater risk of reputational damage and unexpected tax exposures arising
Tax exposure	Be confident that the mitigation of key tax risks is effective and efficient using appropriate tax controls throughout your organisation	Key tax risks not covered by effective controls create a greater risk of unexpected tax exposures arising

Our recommended approach

PwC has been heavily involved in the consultation process regarding both the original formulation of the Guide and in designing and testing tax governance frameworks, including tax operational controls. By applying our four-step approach you can provide senior management and the Board with a clear way forward in addressing ATO expectations.

Step1 **Gap Analysis**	**Step2** **Documentation**	**Step3** **Operationalise**	**Step4** **Periodic internal control testing**
Perform a gap analysis of current tax governance policy, procedures and controls against the ATO's expectations (Gap Analysis is suggested under the ATO's Guide)	• Define / amend the tax governance and risk management policy and supporting documentation • Document key tax controls and procedures manuals (i.e. CIT, GST, etc.)	• Implement / review tax software: ➢ Workflow management ➢ Computational ➢ Analytics and reporting ➢ Document management • Conduct training – staff and Board level • Improve/enhance existing processes (i.e. checklists, stakeholder involvement, existing software)	• Document an internal audit plan for tax • Test the control design and operational effectiveness of the tax governance policy content, CIT, GST and tax advice (3 year rolling programme)

If you have any questions or would like to know more details, please feel free to contact us.

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