

Trust and transparency with Tax Corporate Governance

Effective management of financial, regulatory and reputational risks associated with tax practices is increasingly being assessed. So far, lower hanging fruit, such as the management of carbon footprints and community work, falling under the environmental (E) and social (S) aspects of sustainability reporting have been addressed and managed. However, with borderless markets and insufficient data, companies are facing greater pressure from stakeholders like employees, customers, business partners, regulators and investors, to be more transparent about tax.

Historically, minimal regulation and insufficient reporting guidelines have led to limitations of tax disclosures and non-unified statements. These factors make it difficult to obtain correct and timely information for tax risk management in portfolios, as well as other investment and commercial decisions.

However, the Global Reporting Initiative (GRI) 207 for tax disclosures, which came into effect on Jan 1, 2021, has been a catalyst for more initiatives among stakeholders like regulatory bodies and industries that cut across borders. These initiatives include “carrots” such as accelerated tax refunds, dedicated tax officers, the absence of tax audits or reduction in the number of tax audits, investment opportunities based on global assessments and guidance on disclosures, as well as “sticks” like carbon taxes.

Over the last 18 months in Malaysia, we have seen the Tax Corporate Governance Framework (TCGF), updated in July 2022, and the Public Limited Companies Transformation (PLCT) programmes, implemented by the Inland Revenue Board (IRB) and Bursa Malaysia respectively. This has encouraged more companies to reassess and align their tax strategies with organisational corporate governance and risk management strategies and policies.

Addressing the needs of various stakeholders through good governance

All roads lead to comprehensive disclosure on how tax risks are being managed, while striking a balance between commercial and environmental, social and governance (ESG) strategies to build trust among stakeholders. The growing trend of moving away from just shareholder profit to meeting the needs of key stakeholders has driven changes in reporting. For instance:

- Investors such as Blackrock Inc apply an ESG lens when assessing their investments. This includes conducting ESG due diligence and referring to sustainability indices such as the FTSE4Good Bursa Malaysia and the Dow Jones Sustainability Indices (DJSI) that may be adopted in their potential investments.
- The Financial Times Stock Exchange (FTSE) proactively works with country regulators to promote sustainability reporting and activities, such as the launch of the FTSE4Good Bursa Malaysia and FTSE Blossom indices in Malaysia and Japan respectively.
- Non-profit organisations advocating for economic systems changes conducive to the environment, like the “B Team” led by philanthropists Sir Richard Branson and Jochen Zeitz.
- Steady rise of boycotts by consumers, and value chain partners, if an organisation's values or actions are not inclusive or environmentally friendly.
- Impact on business models due to sustainable supply chains that consider tax and ESG risks to their own, investors and supply chain partners' operations and their net zero commitments.
- The Australian Tax Office's Justified Trust Programme was established in 2016 to provide confidence to the community that large taxpayers are paying the right amount of tax.

Good governance has become an enabler for effective management and communication of issues that impact our social, economic and environmental ecosystems. With the introduction of the TCGF, this will enable companies to enhance their ESG reporting requirements.

Building trust among stakeholders

Never before has there been so much guidance on reporting and collaboration between regulators and industry to encourage cooperative compliance among taxpayers. In November 2021, Bursa, as part of its overall guidance on disclosures, made reference to the Malaysian Institute of Accountants (MIA) and the Malaysian Institute of Certified Public Accountants' (MICPA) Tax Corporate Governance (TCG) publication. Their expectations alongside MIA and MICPA were promoted extensively in the first quarter of 2022 in the form of public forums. This was further supported by Bursa's release, including road shows, of its second guidebook on ESG under the PLCT programme in June 2022, which has a section dedicated to tax.

The IRB issued its TCGF guidelines in April, which was further revised and updated in July. This adopts six key principles.

These are the building blocks identified in the Organisation for Economic Co-operation and Development's 2016 report on good governance, and they serve as the foundation for many other TCG frameworks, both locally and internationally.

The six key principles are:

- Establishment of a tax strategy;
- Consistent application of the tax strategy throughout the organisation;
- Clarity of roles and responsibilities in applying the tax strategy;
- Documentation of governance in place;
- Regular testing; and
- Assurance to stakeholders

The IRB will assess both the TCGF, that is, strategy and awareness to wider stakeholders and the Tax Control Framework (TCF) specific to the processes within a tax function. Key points to note include:

- Stakeholders such as business units, legal, procurement and finance need to be aware of tax risks and controls, which impact other business processes like procure to pay (P2P) and order to cash.
- Active involvement of the board in the organisation's tax risk and compliance management.
- Tax-aligned business processes to enable timely flow of relevant information among stakeholders like operating business units, legal, procurement, finance and tax that facilitate informed and effective decision-making, plus risk management. For example, a tax aligned P2P could enable timely information on carbon pricing implications on goods being exported to Europe, in consideration of the European Union's Carbon Border Adjustment Mechanism, which would impact the cost of supply, profit margins and delivery time.

In addition, having a comprehensive and robust TCGF in place enables an organisation to comply with other disclosure requirements, such as FTSE4Good and DJSI, that align with business and ESG strategies. We note that a growing number of companies have tax as a material action item for review in the coming financial year, as part of their adoption of sustainability indices and disclosures. This could also be driven by the expectations of their customers, employees and business partners or the need for financing.



TRUST IN Resilience

BY PAULINE LUM

Open lines of communication – Is this unlocking Pandora's box?

Cooperative compliance programmes promote mutual trust, transparency and understanding between tax authorities and taxpayers, which is made possible by open lines of communication.

While the TCGF programme is voluntary, we understand that organisations under the pilot are currently preparing their submissions for the IRB. Other triggers, such as ESG strategies or pressures from business partners, are causing others to assess whether to volunteer for the TCGF programme. Organisations that are keen to assess and enhance their disclosures can expect further guidance from the IRB (vide dialogues) and Bursa's second PLCT guidebook on ESG that includes tax considerations. To further strengthen the

lines of communication, the IRB will also discuss refinements and enhancements of an organisation's tax controls during the assessment of its TCGF, where relevant.

Transparency is an enabler in building good relations and trust. However, striking the right balance in an organisation's narrative is key. Particularly, when some may be apprehensive about opening their doors to stakeholders, like regulators and business partners. For instance, the IRB should continue to engage organisations to assure that their intent under the TCGF programme is to assess policies and processes in place to manage tax matters and risk for comfort, to build trust and two-way communication. One of the incentives of participating in the TCGF programme is that there will be no audits for the duration of three years, during the period of certification, if successful under the programme. This is not commonly available under other cooperative compliance programmes such as Singapore's CTRM and Australia's Justified Trust Programme.

What is your tax narrative?

Organisations need to proactively ensure that the narrative on their core values and purpose are aligned, and risk (including tax) is managed effectively. Activities to streamline corporate governance and risk management policies can be slightly expanded to include tax risk management and reporting obligations, with nominal additional time and cost. Leaders should consider:

- What their key stakeholders require, collaborate and leverage guidance provided and available initiatives to devise sustainable policies and processes to effectively manage their risk and compliance obligations.
- Regular engagement with key stakeholders to keep them abreast of progress to ensure that informed decisions can be made in real time.
- What are the “carrots” available and assess whether they can leverage any adopted sustainability indices, such as the FTSE100 and GRI to include tax disclosures, such as tax strategy and policy disclosure in the public domain, and participation in the TCGF programme.

In conclusion, organisations can no longer wait to see what is coming. Cooperative compliance is here and to remain relevant, they will need to jump on the bandwagon. It is time to harvest those “carrots”.

Pauline Lum is tax director at PwC Malaysia