A Conversation on the Current Environment with Joel Walters

By Lowell Yoder and Tadd Fowler

Joel Walters, leader of the U.S. inbound tax practice and leader of the global communications tax practice at PwC, recently spoke with Lowell Yoder, Editor-in-Chief of International Tax Journal (ITJ), and Tadd Fowler, VP of Tax for The Procter & Gamble Company and member of the Advisory Board of the ITJ, on his thoughts regarding the overall tax environment, public perception of multinational companies and the OECD/G-20 BEPS project.

ITJ: How does it feel to be back in an advisory role after spending many years as the head of tax at multinational companies and most recently at Vodafone? Is there a part of you that thinks ... "I sure got out at the right time"?

JW: I would say that I really enjoyed the 20 years I spent in the corporate world. There are many aspects to that environment that are really enjoyable and rewarding in terms of leading teams, impacting individual careers in the people around you and having direct tangible and measurable impact on the performance of the organization.

On the other hand, I am really enjoying being back at PwC where I feel like I bring a client perspective that is helping us be more successful in a variety of areas across the Firm. And I think we are really building something unique in our practice focused on foreign companies investing in the U.S. and am excited about where we are going in that space. Being part of building something that is different and

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lasting in how we make a difference for our clients as they deal with the complex U.S. tax environment within the context of a foreign-parented group is really exciting.

I understand though what you are asking in the second prong of your question about getting out at the right time. I guess I generally do have to agree there is a part of me that sounds like someone who has indeed been in the tax world for 30 years when I shake my head and say that this all used to be so much easier. And whether you have been doing this for a long time or just getting engaged in global tax matters, everyone can see that it is a more difficult world today, and the challenges to an in house tax executive are increasing exponentially. The escalation of focus on tax within the business all the way to the board and the policy and enforcement approaches in both emerged and emerging economies, as well as managing teams to deal with the changes, is certainly challenging and all indications are that this trajectory will continue upward.

But I think we would be missing a critical way to look at this if we simply viewed the changes as challenges and not as opportunities. Recall when we started, I mentioned that what I often miss about the corporate world is the opportunity to lead teams, impact individual careers in the people around me and having direct tangible and measurable impact on the performance of the organization. The changes increase the space in which senior tax executives can achieve these things.

ITJ: You mentioned the focus on tax to the board level, how have you seen that evolve over recent years?

JW: I'm glad you identified that specific point as worth further discussion because in my mind it is a really important trend which will continue and which also creates challenges and opportunities for senior tax executives.

First, I would say that focus on tax in the boardroom is not a new phenomenon, despite that suggestion over the past few years. It has always been an important aspect of the financial performance of the business and a material element on the balance sheet so it has never been left off the agenda. But I do think that the depth and breadth of the tax discussion in the boardroom has evolved.

This includes a deeper dialogue around the way tax decisions get made in the business, the commercial drivers of tax positions, the areas where disagreements might arise with tax authorities and how those disagreements are likely to be resolved. And, of course, there is the issue of how tax is perceived in the external environment and how best to explain the choices that have been made and why those choices are appropriate. A few years back the discussion around tax at the board level was along the lines of "what are the key elements of the tax position and looking out for several years what are the potential changes in that position for the better or the worse." Today the discussion would start with that and then go on to "and what are the principles and commercial objectives that guided the decisions we have made, who was involved in those decisions and are they consistent with the view and values of the organization, precisely where might there be disagreement with tax authorities and what is our expectation and plan to resolve any such disagreements in a positive transparent way, and what exactly can and should we say externally to create an understanding of the level of thought we have put into our tax position and why we are comfortable with what we have done and how we have done it?"

ITJ: This sounds challenging as you have said, but it also sounds like it requires a different skill set for senior tax executives than might have been required in the past?

JW: That is indeed true and very important. The challenges of this environment are certainly there, but think of the increasing opportunity for tax executives to have influence and impact in a deeper and broader way than was always the case previously. This includes everything from having a bigger role in commercial decision making to external communications strategies, which is really fantastic.

And yes, this requires enhanced skills in commercial strategy, influencing, leadership and communication. As the focus on and importance of tax evolves, so does the job description of senior tax executives. We will all need to change with the world in which we operate.

ITJ: As multinational businesses face these challenges in your experience have you seen any major philosophical differences on management of tax matters between U.S. and foreign multinationals?

JW: Actually, I do think there are significant differences in a number of areas. And I think it is a really important question to ask because I'm not sure all advisors, especially those in the United States, really take these differences into account in their approach and advice. Further, it is often a barrier to success even for U.S. corporate tax executives when joining foreign company tax teams or even dealing with foreign businesses when engaging with them in transactions or joint business interactions such as JVs.

Often the differences are really philosophical, as you say. In some cultures there is simply a fundamental difference in how tax is viewed. In the United States it is second nature to think of tax as a line on the P & L and cash flow statement that needs to be minimized in appropriate ways to enhance financial performance, while in many cultures the relationship with these lines on the financial statements is less clear and results in less focus on planning to reduce or defer tax. And, in some cases not really focused on it all to any material degree.

But the differences are often more executional. Foreign businesses usually have very different styles of decision making, both in terms of who is involved and the process for agreeing to strategies and actions. They also often have smaller budgets and smaller teams as compared to U.S. companies, which have been exposed to the enormous complexity and compliance burdens of the U.S. tax system and have developed an approach that includes more allocation of resources to tax functions.

While the global environment related to tax is creating change in all multinational businesses, these differences are still very much real. The important point in this, of course, is that those differences carry with them natural consequences related to how foreign businesses approach and execute tax, which requires different thinking in what they do, how they do it, how they influence within their businesses and how they communicate about tax both internally and externally.

ITJ: You mention the changing global tax environment. There is a lot we could talk about in that space but let's start with the public scrutiny of the tax affairs of businesses. Vodafone received a great deal of attention in the UK on a number of issues, including its settlement of the CFC dispute, while you were leading the tax function. What can you tell us about what you learned from that experience?

JW: I obviously can't speak on behalf of Vodafone or talk in detail about any specific company, but I can certainly give you my views of developments in this space and how I think business can best deal with the challenges and opportunities they present, which is unquestionably shaped by all my experiences of 20 years in the corporate world.

The first thing to be clear about is that tax is now the stuff of mainstream public debate, and that is not going to change soon. For most of my career it was a topic that got very little attention and when it did, was short-lived in terms of widespread public interest and debate. Why has that changed? I don't think it's because it has suddenly become a fascinating topic for the public at large. It's simply because we live in a world in which many, if not all, countries are dealing with difficult budget and sovereign debt situations, resulting in public debate about funding of welfare programs, infrastructure and social programs. It is to be expected that this focus on the spending side will increase interest in the revenue side and business would get attention. I think it's further to be expected that this public scrutiny of business taxation will only subside when these underlying sovereign fiscal drivers subside, which frankly isn't going to be soon.

The second thing to understand is that dealing with this kind of scrutiny when it turns to individual businesses is usually not in the natural skill set of tax or finance executives. Our natural tendency is to explain, usually in technical legal terms, the analysis that supports our position and why it is correct. The difficulty this creates is that the external challenge is often in the form of short, impactful, sound bites, often of questionable factual accuracy and always lacking in recognition of the complexity of the question at hand. A detailed legal analysis in rebuttal is materially less impactful.

So I think this is to say that senior tax executives need to understand that public scrutiny of their company's tax affairs is going to be part of the ongoing environment. To deal with that they need to develop personal skills and build a team that has the skills and experience to help their management communicate in a clear and impactful way why they believe they have an appropriate approach to tax generally and why they stand behind specific aspects of their tax planning and compliance. And my personal recommendation would be to start developing those communications before you find yourself in the spotlight so you can react quickly and effectively if and when needed.

ITJ: One of the challenges being put to business relates to the question of "paying your fair share" and sometimes even the obligation to pay a "moral" or "ethical" amount of tax in the jurisdictions in which they operate. What is the communications strategy to deal with this since that involves viewing tax obligations in a way that is at a minimum very difficult to define?

JW: That's a very good question and very difficult to answer. I boil this down to a couple things that I think businesses, and the business community as a whole, should be doing.

First, businesses should be comfortable that they have a clear standard as to how they manage their tax affairs, write this down and share it within the business as well as externally, as appropriate. Each business must decide how this looks, but an example might be:

- Everything we do must satisfy us that it is within not only the letter but also the intent of the law.
- Everything we do must be consistent with the values of our business.
- As professionals we must be proud of what we do and how we do it.
- We will be completely transparent with the tax authorities and work to resolve issues in an open and honest way.
- We must be comfortable that we will stand behind whatever we do should it become public knowledge.

I think a policy along these lines is an appropriate response by a business without needing to debate if a "fair," "ethical" or "moral" tax is being paid. In my view, this is an appropriate place to draw the line of the debate for a business.

The second thing is that both individual companies and the business community as a whole need to be better about explaining the total contribution that they make to a community. So much of this debate is focused on corporate income taxes. I think it would be useful if there was a deeper appreciation in the public consciousness of the contribution made to the economy of individual jurisdictions both in terms of all the types of taxes paid as well as job creation and charitable giving. I think this should be part of the ongoing communication strategy with the public, as well as the response when individual circumstances are debated in the public domain.

ITJ: Let's turn to the related topic of the OECD's activities to focus on international taxation as part of the BEPS project. What are your views on how we got to this point and what we might expect?

JW: I like to go back a few years and track through the road we've travelled to get here as it is instructive as to why we are here and what is likely to happen.

While I like to start with the Public Accounts Committee (PAC) engagement in this space since I was living in the UK at the time, I think you could find parallels elsewhere. If you look at the way the PAC thinking seemed to develop, you can see three key developments. First, there was a movement from what appeared to be a challenge of the legality of how business managed their tax affairs to a belief by members of the PAC that the appropriate challenge to business should be more focused on moral and ethical views of a fair tax obligation. Second, the PAC put forward the proposition that the way international operations of business are taxed is fundamentally broken. Third was a line of reasoning that it is appropriate to pressure business to pay a fair share of tax until the system for taxing international business is "fixed" though policy development and implementation.

These developments lead to what we are seeing in the BEPS project, which is an attempt to, first, refashion the policy and implementation of rules related to the taxation of international business and, second, to create transparency mechanisms designed to shine a light on the tax affairs of business.

ITJ: Do you believe that the OECD really can achieve consensus in these areas?

JW: I think the political imperative is too strong for the OECD not to achieve some consensus in each of these areas. So I expect there will be real actionable recommendations both in respect to international tax principles and transparency.

I also believe that, to the extent the OECD does not achieve consensus that satisfies all parties, we will see significant levels of unilateral action in many jurisdictions around the world. The risk of uncertainty and double taxation from unilateral action by individual countries will be something we are going to face for some time to come.

ITJ: Speaking of unilateral action, India is a place that is often accused of moving in directions that make it stand alone in terms of its approach to taxation of business operations and transactions. The *Vodafone* case related to the capital gains on its acquisition in India is pointed to as an example of this. Do you think that this case has diminished confidence of foreign investors into the country?

JW: Again, I don't speak for Vodafone in any way—nor can I discuss any particular company. I can only give my personal views based on dealing with India in a number of circumstances.

The simple answer is yes. My view is that the perception of the country as a destination for foreign investment is damaged by a number of unexpected and unprecedented actions. The uncertainty this creates in the environment makes it a much more difficult case for companies assessing investing into India as opposed to the many other investment destinations.

But I would actually come at this from exactly the other direction. I believe that India missed a real opportunity to send a positive message to potential investors. It had the chance to say to the world that when the Indian courts speak they can be relied upon as the rule of law without concern for retroactive changes in the law or new or different challenges. Not all jurisdictions can say that to the world, and it would have been a very powerful message. Not only would it have been the right thing to do in accordance with the rule of law, it would have given comfort to potential investors into India as they compared investing in India versus other countries.

ITJ: One last question about the environment. Some businesses have gotten out front on the transparency issue and have been providing more details around tax externally. What is your view on the balance of the potential risks and rewards in going down this road?

JW: This is a choice that each business needs to make and there are very good reasons why a particular business may choose to do more or less in the area. But in general I am in favor of moving towards more transparency if it is possible.

As you say there are many risks associated with this, including information put in the public domain that is either intentionally or unintentionally misinterpreted and even perhaps creating more confusion than benefit. But this is another tool to help explain the contribution that business makes to economies and communities. Further, I think it gives credibility and a foundation from which tax can be explained.

ITJ: We've covered a lot of ground so let's bring it back to your core focus today. As tax leader for PwC's Inbound tax practice, what developments do you feel are of most interest for foreign multinational taxpayers investing the United States?

JW: I think a lot of things we've touched on are important areas of focus for these businesses.

The challenges of the environment in terms of the complexity of the U.S. tax system create challenges and opportunities in their tax planning and compliance. But for foreign companies this can be even more challenging than for U.S. businesses due to the cultural, decision making and resource allocation characteristics of their parent country and senior management. We spend a lot of time helping these businesses assess whether they have the right people, systems and infrastructure to deal with the U.S. environment and how to manage the communication to foreign stakeholders.

The potential for legislative and regulatory changes in the United States through broad tax reform or more targeted provisions is a particular concern for these companies. The reason is that they can come both from changes that impact all businesses and those that can be focused specifically on foreign owned businesses. This necessitates an additional level of vigilance, focus and action for these businesses.

Finally, I would say that with the pressure for business performance on all businesses, including foreign companies, are increasingly resulting in them expanding their focus on tax beyond the more basic traditional compliance and risk management activities and international structuring areas. They are increasingly focused on the risks and opportunities in areas such as state and local taxation within the United States, how and where they operate their core U.S. business operations and how to achieve best practices in efficiency and effectiveness of their U.S.-based teams.

All of these factors are materially enhancing the ability of senior tax executives of U.S. businesses that are foreign-owned to have ever increasing impact on their people and the performance of their organization, which is very exciting.