WHEN YOUR TAXES ARE EVERYBODY'S BUSINESS

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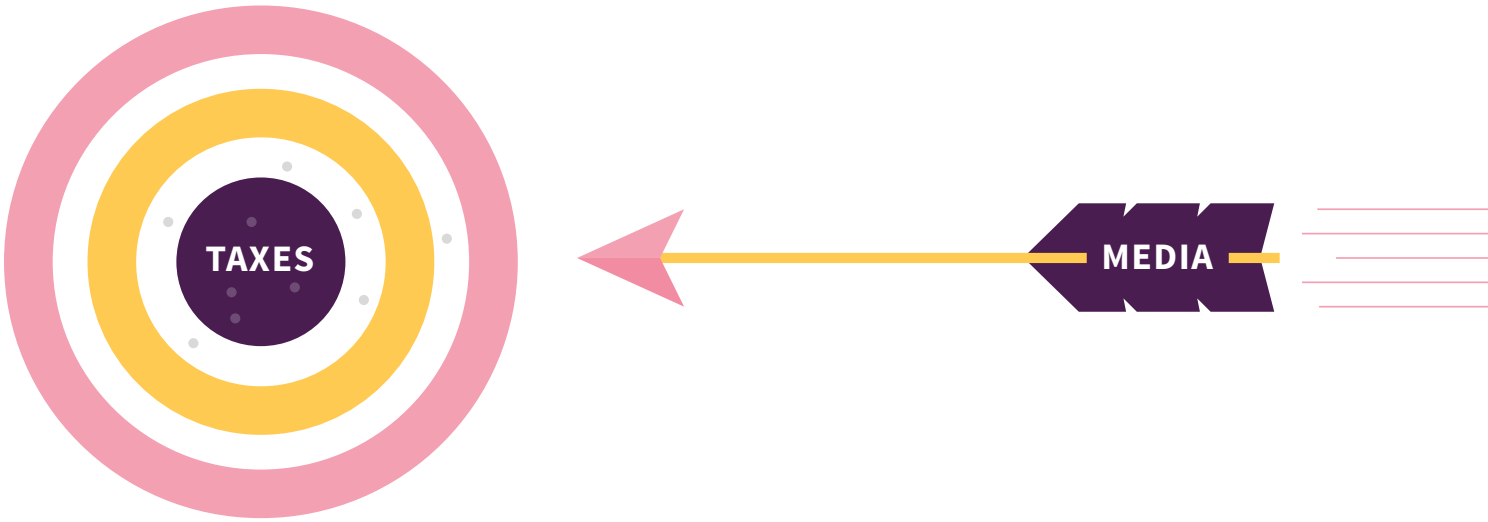
Executive Summary:

For a long time, when enterprises thought of taxes, it primarily was in terms of determining, paying and limiting them. Questioned about tax policies, the typical corporate response has been to say that the organization is complying with the law and is fulfilling its responsibilities to its shareholders.



But since the 2007 global financial crisis and the continuing sluggish recovery, political, consumer and media scrutiny of corporate tax behaviors has intensified. Companies, especially consumer-facing global organizations seeking to reduce their tax burdens, have become targets for media outrage and have found themselves cast in an unflattering light that has damaged their corporate reputation. In our view, this environment demands that tax policy development should become a more strategic process. If it does not already involve board-level decision makers, it should. Companies also must develop a broader rationale for their policies and be prepared to justify and communicate them in the public arena to all stakeholders. Companies that fail to do so will pay dearly on the streets where they do business.

How Your Taxes Became Everybody's Business

Corporate tax policies historically have been developed by the tax department in relative isolation from the rest of the business. The charge always has been to comply with the laws and standards in headquarter jurisdictions while leveraging those regulations to pay as little tax as possible. This long has been considered the proper way to conduct business and the best means to discharge the company's fiduciary responsibility to its investors and shareholders while maintaining as strong a financial position as possible to meet the challenges the business landscape presents in abundance.

However, following the 2007 global financial crisis, cash-strapped governments hungry for tax revenues to buttress their battered economy began to look more closely at corporate tax returns — especially those of large, global companies doing business in a variety of jurisdictions — and started calling for greater transparency in the reporting of the transactions that lie behind them. In the United States, the 2010 Foreign Account Tax Compliance Act (FATCA) has sought to hold non-U.S. financial institutions responsible for reporting their U.S. clients' activities to the Internal Revenue Service, thereby calling to task chief compliance officers and heads of the tax department at all financial institutions. There also have been calls for changes to the laws governing corporate tax behaviors in the Eurozone. At the autumn 2013 G20 meeting in St. Petersburg, Russia, the Organisation for Economic Co-operation and Development presented the G20 with a 15-point plan designed to prevent international tax avoidance. The plan,

in part, would require multinationals with offshore interests to pay taxes on profits from sales in those countries at the (generally higher) rate set by the jurisdiction in which they are headquartered.

At the same time that governments and non-governmental organizations began to campaign for greater regulation of corporate tax behaviors, the public, suffering from the effects of the downturn, responded positively to the view provided by dramatic films such as 2011's "Too Big to Fail" and documentaries such as 2010's "Inside Job" that an individual's own financial problems were caused by corporate greed and misbehavior. A suspicious mindset toward all corporate actions grew and was magnified by newly ascendant social media platforms that provided channels through which the public's displeasure could be magnified and disseminated. This intense level of scrutiny is unprecedented for most companies, and many have not been able to communicate successfully the reasons for current tax policies nor to cast them in a publically palatable light. The result has been that some companies — most notably public-facing, consumer-oriented enterprises — have suffered major reputational damage that has produced a broad variety of business challenges.

A number of companies now are examining their tax policies in this harsh light of political and consumer disapprobation and asking themselves:

- How should we design our tax policies?
- What should the goal of our policies be?
- How can we balance the public's concerns with our responsibilities to our business and shareholders?
- How can we improve the ways in which we engage with the public, media and shareholders to tell our side of the story?

Tax Follies in the UK

In the UK, Starbucks, Google and Amazon, despite their best efforts and with all the resources at their command, have become the public face of corporate tax avoidance.

In 2012, it was widely reported that Starbucks had paid no corporate tax in the UK, claiming no profit from its UK business between 2009 and 2012 on sales in excess of £1 billion. The absence of profit primarily was due to royalty payments for Starbucks' intellectual property made by Starbucks in the UK to Starbucks in Amsterdam and other jurisdictions. And although these payments were not unusual, nor in violation of any UK laws, the public did not take the news well nor did it respond positively to the actions Starbucks took after the revelations. At first, the company declined to engage in the public debate as online and offline protests grew. An organization

called UK Uncut arranged protests at 40 of the firm's branches, and various social media groups — such as #boycottstarbucks — sprung up. Soon more than 90 percent of the Starbucks comments on Facebook and Twitter contained a reference to tax. The company's BrandIndex reputation score tumbled from positive to sharply negative. Then, over the 2012 Christmas season, Starbucks offered to pay the UK Treasury £20 million, calling it a donation. And although Starbucks' stock did not suffer, the company experienced significant reputational damage during this period due to such high-volume, organized criticism.

This past June, HM Revenue & Customs accused Google — which reported $4.1 billion in UK sales in 2011 and paid just the equivalent of $9.6. million in UK taxes — with "aggressive tax avoidance." Google's response was that it was in compliance with the controlling tax laws and practices, and its chairman dismissed public concern in a manner deemed by some to be insensitive. "It's called capitalism," he explained to the media. "We are proudly capitalistic. I'm not confused about this." At the same time, Amazon, the giant Internet retailer and cloud services provider, was revealed to have routed billions of dollars of UK sales through Luxembourg, allowing it to pay Luxembourg's 3 percent value added tax on those sales rather than the UK's 20 percent rate. Amazon's response, like Google's, was that the company was in compliance with all relevant tax laws and practices, and, like Starbucks and Google, Amazon's response did little to quell the criticism of its actions.

While Starbucks, Google and Amazon are well-respected market leaders in their respective sectors and have not suffered immediate business harm by this public airing of each company's tax policies, all three have worked hard for decades to develop a sterling reputation as consumer-focused, consumer-friendly organizations. They cannot enjoy being perceived in a way that runs counter to their hard-won and largely deserved exemplary corporate image. And it will be difficult for each to forecast the consequences of what amounts to a public tarring and feathering in terms of future revenues and profits.

Transparency almost always is the best policy. Some companies have been very forward thinking in how they present their tax position and policies to the outside world.

There Has to Be a Better Way — and There Is

Developing a corporate tax strategy no longer can be left solely to the corporate tax department, as compliance and tax limitation cannot be the only rationale for a company's tax policies. Given the current environment of heightened regulatory scrutiny and public suspicion, tax strategies must be analyzed with an eye toward how they ultimately will be viewed by a broader set of stakeholders than just shareholders and equity analysts. This analysis must include consumers, the media and even company employees and drive toward an understanding of how the company's tax policies would appear to each constituency.

This requires the involvement of the board, as it involves a consideration of the company's core values and demands a frank assessment of how its tax policies could affect its public image.

Therefore, board members must ask themselves two key questions when weighing in on their company's tax policies:

- Are our company's stated values aligned with its tax strategies?
- If our company's tax policies are publicly examined, could they be construed to be taking unfair advantage of regulatory loopholes? As one UK plc chairman put it recently, "It has to pass the *Daily Mail* sniff test."

Once a company decides that its tax policies are what it wants them to be given the current climate and that they strike a good balance among business exigencies, fiduciary responsibilities and the demands of corporate good citizenship, the organization must consider its level of exposure should those policies be examined publicly and make sure there is a strong, integrated response plan in place. Such a plan would include a dedicated team, equipped with a single message, with each member's responsibilities documented and clearly communicated across the enterprise. Above all, the response team should be extremely knowledgeable and informed about the company's tax policies and activities and should include top leaders across the business, particularly the chief executive officer, chief financial officer, investor relations officer and chief communications officer.

Consideration then must be given to the level of disclosure that the company intends to provide. This very much will depend on the style of the company and its managers and also on the content of the company's tax story. Transparency almost always is the best policy. Some companies have been very forward thinking in how they present their tax position and policies to the outside world, developing microsites and even publishing brochures on the subject.

The response team leaders need to be trained to engage with critics in the public sector. This especially is crucial to consumer-facing companies as their continued success depends in large measure on how they appear to the buying public. In the UK, a number of reputations have been irreparably damaged due to insufficient preparation

in advance of a Public Accounts Committee grilling at the hands of members of parliament who, for the most part, are skilled communicators and are expert at appealing to public sentiment. It is not effective (and it often is counterproductive) to leave public communications in the hands of tax specialists — untrained in media relations — who are apt to get caught in the weeds explaining arcane regulations to a public that is not interested in such detail and may hear it as an attempt to obfuscate. Neither is it effective to leave these communications solely to the public relations department (either outsourced or in-house) as public relations executives, no matter how highly placed, never can have the same impact on the public as operational corporate leaders who are perceived to be the creators of policy, not simply its messengers. The public — and the media — wants to hear from the company's decision makers on these matters, not spokespeople who never can convey the same degree of gravitas or demonstrate the company's sincere wish to speak directly and openly with its customers on the issues.

Additionally, it is important that companies and their leaders engage with the media (both traditional mainstream journalists and key digital influencers) before problems emerge. Developing strong relationships with these groups will establish trust and encourage sympathetic ears when these issues surface. It also will reduce the chance that the company will be viewed as opportunistic or self-serving when it does reach out to those key opinion leaders.

This creation of allies in the media, both traditional and social, especially can be helpful when a company finds the fairness of its tax returns or policies questioned in public. The job of nurturing these allies should fall primarily to the investor relations and corporate communications departments. They can do this first by identifying key influencers through research and then by allowing them access to corporate leaders and supplying (properly vetted) information about the company's plans.

Increasingly, traditional media, both general interest and B2B, are getting information and leads from social media channels and influencers, as well as from corporate websites. In this way, bloggers often can set the agenda for mainstream media coverage, and it will serve companies well in times of reputational crisis to have good relationships with the media.

Once the tax strategy is aligned with the company's values and the organization has a roster of media allies willing to listen to its side of the story, the public conversation can begin. To guarantee that the communication follows paths that reflect well on the company and defuse (or contain) unjust criticism, the chief communications officer — as well as all C-level executives — must be conversant with the company's contributions to the welfare of the general economy, as well as corporate finance in general. This will enable the chief communications officer, or any other corporate leader, to educate the public on the relevant issues and place the company's tax policies in a broader industry context, thereby combating charges of exceptionalism. This also will relieve the company of the onus of representing all businesses by allowing the organization to focus on its own specific enhancements to the general economy in which it is headquartered. These contributions can include the company's role in job creation and economic development (two themes particularly resonant in these still-difficult economic times), as well as its philanthropic activities. Providing positive examples of a company's contributions to a society's welfare can help balance the picture the public receives via the media.

Don't Make Yourself a Target

There is a long tradition of portraying business as "the bad guy" when economic times get tough, as they have been since the waning days of 2007. Corporate tax policies, in their complexity and opacity to the general public, provide an easy target for politicians seeking to ingratiate themselves with a discomforted public. Corporate tax avoidance also has become a hot button issue for the media as it resonates with a public that sees its own taxes rising and regards corporations paying taxes at a lower rate than most citizens pay as unfair, simplistic as that view may be. Governments have responded by calling for new regulation of corporate tax-related activities, and there is no sign that any of these trends will slow or abate in the foreseeable future.

In our view, this situation can be met best by devising corporate tax policies with an eye to the eventual need to justify and explain them in the public arena. Enterprises that do so and develop a thoughtful and well-designed response plan can emerge from public debate with their corporate reputation preserved and, in many cases, even enhanced. Organizations that fail to implement the measures and strategies described in this article increase the risk to the corporate reputation and, perhaps, ability to conduct business as each would wish in both the home country and abroad.

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