Why tax governance is key in an era of more tax risk and controversy

2023 EY Tax Risk and Controversy Survey
Introduction

Global businesses will need robust tax governance to manage a new era of tax risk and controversy that is evolving after a pause in enforcement activity during the COVID-19 pandemic, the 2023 EY Tax Risk and controversy survey finds.

Among the 2,127 tax and finance executives in 47 jurisdictions who responded to the survey, 84% say that implementing or improving an existing global framework approach to tax risk and controversy management would add “some or significant” value to their business in the next two years. Yet more than six in 10 of those surveyed (61%) say their tax functions are only sometimes, rarely or never involved by executive leadership in significant changes to existing business activities such as business model changes, new products and new services – increasing the risk of unexpected tax exposure for those activities.

This juxtaposition is notable and a cause for concern because the most senior tax leaders among the respondents (holding the ranks of Vice-President of Tax, Global Tax Director or similar) are anticipating that the number and intensity of audits will grow by 79% in the next two years compared with the previous two. Despite this, 70% of the same group said their company doesn’t have complete visibility of all their ongoing disputes globally. This disconnect also has the potential to make it difficult to respond to new geopolitical, economic and tax policy changes that are adding unprecedented layers of tax risk that must be managed.

“Strong and effective tax governance has rapidly become essential for all businesses,” says Luis Coronado, EY Global Tax Controversy Leader. “This is partly because tax authorities around the world are using the absence or presence of good governance principles in tax as a way to segment taxpayers into different risk categories. It’s also because tax functions are recognizing that a good tax governance framework offers them many opportunities to help their organizations build long-term value for stakeholders, including in the important Environmental, Social and Governance (ESG) space.”

To navigate this new era of risk and controversy efficiently, businesses should strengthen their activity across three key areas:

- Enhancing their tax governance strategy, defining policies, roles, controls and accountabilities in clear, easily understood ways that better enable the effective management of both tax risk and tax controversy.
- Transforming their approach to tax and financial data management in a way that facilitates accurate and timely responses to ongoing reporting obligations, while also providing the tax function with awareness and valuable insight into both potential and ongoing tax disputes, mutual agreement procedures and tax litigation globally.
- Doing more to secure tax certainty at every opportunity, seeking out ways to manage tax risks while also taking advantage of the many proactive dispute prevention and resolution programs offered by tax authorities.

Informal requests, however innocuous they appear, may well be a harbinger of future tax controversy.

Luis Coronado
EY Global Tax Controversy Leader
More – and more detailed – information requests are driving tax audit activity

Expectations for more audit activity are being driven largely by an acceleration in the number of tax authority requests for more detailed information. Such requests – often informally sent and characterized as “voluntary” – can contain numerous detailed questions, posed over many pages, that require extensive time and resources to complete. While there is usually no legal compulsion to respond to these requests, practically speaking it is generally not in an organization’s best interest to ignore them, and increasingly, the use of formal information-gathering powers, as well as the exchange of information among tax authorities, may follow. “Informal requests, however innocuous they appear, may well be a harbinger of future tax controversy,” Coronado says.

More than half (56%) of tax and finance executives who said they anticipate more audits and more intense audits in the coming two years attribute that expectation to more numerous or detailed information requests and to ever increasing transparency and disclosure requirements.

Such information can and will be exchanged between tax authorities, of course; exactly half of respondents say that more information being exchanged between national tax authorities is also helping drive increased audit activity and intensity.

A litany of new tax risks

Meanwhile, a host of external developments are creating new risks for businesses and their tax functions.

Survey respondents cited a litany of concerns – inflation and higher interest rates that can affect intercompany financing transactions and transfer pricing, the ongoing conflict in Ukraine, and environmental sustainability issues chief among them. Across multiple areas these tax and finance executives report they are bracing for more complex and lengthy interactions with tax authorities in the next two years than in the previous two.

Tax function leaders are also anticipating more focus on indirect taxes and more risk from the digitalization of tax administrations. Many respondents also note concerns about tax-related reputational risk, especially considering the upcoming mandatory public disclosure in the European Union and other jurisdictions of country-by-country reports (CbCR).

Among the most senior tax leaders

50% are bracing for higher volumes and intensity of tax audits and disputes in the next two years. That’s a 79% increase over the proportion who reported an increase in the number and intensity of audits during 2021, when many tax authorities were focused on developing and delivering support and stimulus measures via the tax system.
Preparing for the global minimum tax

Pillar Two of the Organisation for Economic Cooperation and Development (OECD) and G20-sponsored project on Addressing the Tax Challenges Arising from the Digitalisation of the Economy was also cited as a major source of potential risk. This is likely due to two reasons: first, rapid preparations underway now to comply with the 15% global minimum tax could lead to future controversies. And second, once the laws are enacted by jurisdictions, they will interact with countless other areas of a jurisdiction's tax regime. This will need to be thoughtfully considered.

Audit activity around tax incentives, actively being reconfigured in many jurisdictions in light of Pillar Two was the second leading source of risk identified by survey respondents.

“Governments used to view tax as a largely sovereign concern but now they’re aligning in an unprecedented way to bring about another wave of global tax reforms,” says Marna Ricker, EY Global Vice Chair – Tax. “The world’s tax authorities are also working together in the same cooperative spirit to enforce both existing tax laws and get ready to enforce changes to come – and businesses need to prepare, if they want to avoid disputes.”

Survey methodology and demographic information

The 2023 EY Tax Risk and Controversy Survey questioned 2,127 respondents in 47 jurisdictions and 20 sectors and sub-sectors. Survey fieldwork was conducted in January and February 2023.

Across the survey population, 496 respondents were in a Functional Tax Head role (e.g., Tax planning, Tax reporting, Tax operations, International Taxes, Transfer Pricing, Indirect), while 456 were either Finance Directors or Finance Controllers with local responsibility for tax. 420 respondents were in a Global Tax Director, Global Head of Tax or Global Vice-President of Tax (or similar) role, while 376 respondents were Regional Tax Director, Regional Head of Tax or Regional VP of Tax or a similar role.

A wide spectrum of different-sized companies were surveyed. Twenty-one percent of respondent’s companies were in the US$750 million to US$4.9 billion annual global revenue band, 23% in the US$5 billion to US$9.9 billion annual global revenue band and 27% were in the US$10 billion to US$49.9 billion annual global revenue band. Ten percent (or 214 respondents) report annual global revenues in excess of US$50 billion.
Building a strategic approach to tax risk and controversy

The survey finds many companies are already proactively making changes to adapt to the post-COVID-19 tax risk and controversy environment. They are:

- Finding ways to further enhance tax governance
- Rolling out global framework approaches to tax risk and controversy management
- Adopting dedicated technology to help gather and assess tax risks, manage tax controls and track ongoing disputes
- Centralizing key collaborative processes, including the oversight and coordination of the most significant tax audits, disputes and litigation
- Making sure everything they do is “audit ready,” especially with regards to transfer pricing and changes made in response to new requirements prescribed by Pillar Two

But there is much more to do, particularly considering the dramatic evolution of the tax transparency and disclosure agenda. CbCR filings of how taxes paid in each jurisdiction relate to a company’s economic activity in those locations are on the cusp of becoming public in many countries\(^1\). Public disclosure of these reports may open new sources of risk for companies that don’t have a handle on how their tax policies and positions might be interpreted by broader audiences.

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\(^1\) Across the 27 European Union Member States as well as Australia.
Pillar Two is driving new risk areas
Pillar Two concerns propel incentives and deductibility toward the top of the tax risk list, but transfer pricing remains the top concern.

An increase in the number and intensity of audits, an increase in detail required in tax authorities’ information requests or the number of them, and greater risk or uncertainty around digital tax administration globally were the top three enforcement-related issues ranked by tax and finance executives overall as presenting the greatest tax risk to their enterprise in the coming two-year period.

Among those tax professionals who spend more than half of their time managing tax controversy, there were sharp increases in predictions for some areas of controversy. More than twice as many of this group anticipate more focus on cross-border tax issues (such as international tax and transfer pricing) compared with the previous two years, for example.

Transfer pricing, historically the biggest concern among tax and finance executives, once again secures the top spot in the 2023 survey, edging out tax incentives by some 12 percentage points. Among the most senior tax leader group, who arguably have best visibility of all tax risks faced by their business around the world, transfer pricing surpasses incentives by 28 percentage points (63% vs. 35%). That is to be expected; the impact of externalities including unprecedented business change, the continued global spotlight on transfer pricing as a result of both the original BEPS project and BEPS 2.0, and the enduring focus of tax administrations on cross-border transactions all result in heightened examination of transfer pricing.

These drivers (and more) are reasons why so many tax and finance executives – 84% – say that improving the contemporaneous documentation of transactions would help them increase their overall tax audit readiness. “Tax function leaders need to recognize that contemporaneous documentation includes gathering the evidence that proves you did what you say you did. Each tax authority is going to be looking for more detail, more evidence,” says Tracee Fultz, EY Global Transfer Pricing Leader. “That means you need to learn about exactly what each country is likely to demand and then create a systematic way to gather and retain evidence.”
Why tax governance is key in an era of more tax risk and controversy

Uncertainty and change amid Pillar Two’s introduction

Pillar Two is also a likely cause behind tax incentives being placed as the second-highest tax risk among all respondents, with many countries rapidly reconfiguring their incentives toolbox so they remain attractive to both inbound investment and outbound expansion. The deductibility of costs and interest ranked third and fourth respectively.

Almost half (45%) of tax and finance executives say Pillar Two will increase the likelihood of new tax audits and disputes while only 11% say it will result in a decrease. Also causing concern to respondents is how little is currently known about how dispute prevention and resolution programs will operate with regards to Pillar Two. That may in part be behind 55% of respondents saying that they think Pillar Two will increase their overall tax costs. “The multilateral dimensions of Pillar Two are likely to bring controversy in future years, so companies will need to be ready,” says Barbara Angus, EY Global Tax Policy Leader.

Survey results indicate that preparations are underway but not yet complete for many companies; almost half (49%) of respondents say they are already tracking how Pillar Two may be implemented in jurisdictions in which they operate, while 47% have educated themselves about its mechanics. Less than four-in-10 (38%) tax and finance executives say their companies have modeled Pillar Two’s impacts, and only 29% say they have started IT systems preparation.

Tax professionals have already presented to the OECD and national governments a multitude of scenarios where Pillar Two disputes could occur. Transfer pricing adjustments by tax authorities may also become more frequent – reflecting the fact that so many cross-border tax issues incorporate some element of transfer pricing. New global tax rules need new global dispute prevention and resolution mechanisms, and taxpayers will be keen to ensure that any such mechanisms are well-thought out, provide the desired levels of certainty and are available well in advance of the introduction of local legislation. Amendments to existing alternative dispute resolution tools are unlikely to be sufficient.

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Barbara Angus
EY Global Tax Policy Leader
Testing tax governance

The Pillar Two measures come on the heels of growing assertiveness of tax authorities, who are sharing information with one another at unprecedented levels. As a result, ideas that deliver results to one tax authority are quickly replicated among others. Primary in this regard is the adoption of new compliance assurance programs by more than a dozen countries in recent years.

These programs ask selected businesses — typically the largest enterprises in an economy — a series of detailed questions that, along with scrutiny of the company’s tax returns, help the tax authority to risk assess and segment taxpayers into different groups. While not audits, the questionnaires typically used in these programs demand detailed information around topics like the effective functioning of a business’s tax governance strategy, its approach to tax compliance and its use of tax technology, tools and systems.

Companies participating successfully in such compliance assurance programs may (or may not, depending on program specifics) be granted a range of benefits in return for their participation, the most important of which is typically a promise (but not a legally binding decision) from the tax authority that the company will not be audited for a set period of time after successfully completing the program.

More forensic detail

Survey respondents report seeing an increase in the use of informal questionnaires more recently that ask similar questions as the tax authority’s structured compliance assurance program, but in far greater detail and outside of the structured programs’ scope. For example, while the formal questionnaire may ask a company to describe its overall approach to tax governance, the informal one may ask how that governance works in practice in relation to indirect taxes, employment taxes or transfer pricing, among other topics.

Such requests for additional and more detailed information are one major reason why the most senior tax leaders, usually the typical recipients of such questionnaires, believe that more audits as well as more intense audits and disputes are likely in the coming two years. These compliance assurance programs are also starting to be applied to smaller companies, across both private and public dimensions. Tax and finance executives should therefore expect more programs of a similar nature to be deployed in the near future, as well as such programs being applied far more widely across different company sizes. The taxpayer-tax authority relationship is changing.

Whether structured, informal, mandatory or voluntary, collectively these programs aim to secure the same objective — to risk-rate taxpayers into different strata, allowing the tax authority to then focus its audit and dispute resolution resources more effectively. Complying — and complying well — will be paramount.
Returning to (a new) normal
During COVID-19, many tax authorities paused their normal auditing activities. That’s now over.

Survey results show tax authorities’ focus over the last two years – which included strong attention on auditing beneficiaries of COVID-19 relief measures – is giving way to a shift back to both traditional areas of scrutiny and examinations of compliance with newer tax laws, such as anti-hybrids legislation. Just 22% of respondents say they anticipate a tax audit related to a COVID-19 stimulus or support measure in the next two years, versus the 35% who say they experienced one in the previous two.

“Tax enforcement priority areas are quickly looking far more typical,” says Martin Caplice, EY Asia-Pacific Tax Controversy Leader. "Authorities are focused on the more familiar territories of transfer pricing, cross-border transactions and indirect tax compliance and enforcement is looking far more routine."

The work-from-anywhere phenomenon catalyzed by COVID-19 also generates concern among tax and finance executives. Twenty-nine percent of survey respondents say they expect new tax disputes over work-from-anywhere policies in the coming two years, including on issues such as the all-important question of whether a remote employee unknowingly creates a permanent establishment (PE) in a jurisdiction, triggering tax obligations. That is an increase from the 24% who say they experienced this in the previous two years, and an area to monitor.

Rising indirect tax risks

Tax and finance executives indicate that challenges around indirect taxes are also growing. Broader tax bases for value-added taxes, including a heightened focus on services and PE issues by tax authorities ranked as the top cause for concern, identified by 42% of respondents. Thirty-six percent said a lack of documentation to substantiate the application of lower or zero-rated supplies (such as proof of delivery or the licenses of customers) was a concern, while digital services taxes – theoretically set for withdrawal as a result of BEPS 2.0 negotiations – ranked as the third biggest indirect tax risk, securing 35% of responses.

"Tax enforcement priority areas are quickly looking far more routine."

Martin Caplice
EY Asia-Pacific Tax Controversy Leader
“Indirect taxes are often the go-to revenue source for governments during times of crisis,” says Kevin MacAuley, EY Global Indirect Tax Leader. “After loosening indirect tax rates and broadening exemptions during COVID-19, many countries are now swinging back to the other side of the pendulum and broadening the base, if not the rates, of these taxes, increasing the number of taxes and increasing enforcement.”

Survey results indicate that several other sources of tax risk and controversy still linger. For example:

› 24% anticipate warnings or actual use of criminal penalties and prosecution by a tax authority in the coming two years.
› 29% are worried about reputational risk to their business as the result of a tax dispute.
› 43% say a lack of clarity internally on how tax fits into their overall organization governance structure poses their biggest business risk as it relates to taxes.
› 37% say failure by local entity professionals to follow the organization’s tax processes is their second largest business-related risk.
› 32% said the tax implications of business restructuring pose challenges.
Getting tax governance right
Putting in place the right people, policies and controls can help better manage tax risk and limit new controversies.

All of these risks — whether they come from externalities or internal disfunction — can be better managed with improved tax governance. This is the first area on which global businesses hoping to better manage tax risk and reduce the incidence of tax controversies should focus.

Better tax governance – focusing on people, policies, processes and controls – can help accomplish three things.

• First, it underpins any global framework approach to managing tax controversy and better equips the business to identify tax risks earlier and manage any disputes that do occur more effectively.

• Second, it creates an opportunity to more closely link tax to the organization’s broader objectives, including those related to ESG, not only improving the level of confidence of multiple stakeholders but potentially even securing additional budget and resources for the tax function during the process.

• Third, it supports the enterprise in meeting the myriad governance-focused programs now being adopted by tax authorities globally.

Most tax and finance executives say their enterprise has many elements of tax governance in place, including tax policies, detailed policy and procedures manuals, and accountability matrices that define who does what, when, how, and where. Collectively, these elements are the keystone to any framework approach to managing tax risk and controversy more effectively.

Having the elements in place is one thing. Continuously executing them in harmony with each other, as well as with other parts of the business, is another. Here, survey respondents reveal several areas where harmonious execution is lacking.

First, from an operational standpoint, tax processes and protocols should tightly align and interact with an enterprise's lines of business and support functions, each of which will likely follow the enterprise-wide governance approach. Alignment with this wider strategy should therefore be an imperative for the tax function. But almost half (43%) of tax and finance executives say they lack clarity about how tax fits into their organization's broader governance structure. This can erode the tax function's effectiveness and was the leading business risk identified by survey respondents.

Good governance in tax

69% of respondents say they expect their organization’s overall focus on tax governance to grow in the coming two-year period.
# What good governance in tax looks like

| Name a tax controversy leader (or group, depending on the size of the enterprise) | Many companies are now putting in place new tax controversy roles or groups. Typically sitting independently from (but well engaged with) other parts of the tax function, this role helps to proactively manage controversy on a day-to-day basis. It relieves pressure on the tax function leader who would traditionally have had such activities in his or her remit. Fifty percent of tax and finance executives say their tax function has a named tax controversy leader, while 81% of respondents say that creating such a role would add “some or significant” value. |
| Create a tax risk committee or center of excellence | This group is typically made up of senior tax professionals, covering tax types and geographies. It performs tax risk and controversy-focused activities including defining decision-making thresholds, reviewing key transactions for risk, and defining the strategy for tax risk management, tax controls and cooperative compliance. Thirty-eight percent of tax and finance executives say they have created such a group in the past two years, while 34% say they plan to do so in the coming two years. |
| Maintain an effective Tax Control Framework (TCF) | A TCF is a key part of the system of internal controls, encapsulating a broad spectrum of content including tax policy, accountabilities, and all controls, processes and protocols to which tax and finance personnel should adhere. Many companies are now defining or enhancing their central TCF, localizing and customizing it wherever needed – often as a response to new tax authority requirements. |
| Centralize key processes | Many companies are currently setting defined thresholds at which a tax audit or dispute must be reported by local entity professionals to the central tax team. While the central team may not assume complete responsibility for such disputes, they will nonetheless provide higher levels of collaborative oversight and coordination, teaming with local resources. |
| Have clear communication and escalation protocols and providing the C-suite with regular tax briefings | Appropriately escalating matters for review and approval and updating the executive layer (and often the board and/or audit committee) on the tax risk environment and the company’s total exposure (both financial and reputational) is an important component of maintaining a relationship with senior decision makers. |
| Align with the enterprise’s broader ESG efforts | Good governance in tax – and specifically, tax controversy – is often the first step on the journey to meeting a company’s objectives as they relate to the “G” in ESG. But just 22% of respondents say that their tax function is completely integrated in their enterprise’s ESG strategy. |
Second, the tax function should maintain strong relationships and communication with wider business decisions and activities. But many of the most senior tax leaders say their tax function falls short of this goal. Sixty-one percent, for example, say that the tax function is rarely, sometimes or never involved in significant changes to business activities, including business model changes, new products and new services. Similarly, more than half (60%) of this group say they are rarely, sometimes or never involved in either changes to their own corporate structure or M&A deals pursued by their company (58%).

Finally, adherence to a corporation’s tax processes by local entity finance personnel is key to effective tax governance, and hence tax risk and controversy management. Without it, local entity personnel – often referred to as the “shadow tax function” – may be tempted to try to manage ongoing tax risks, disputes or litigation cases that may have wider implications for their company. Eighty-two percent of respondents say that gaining control in this area would deliver some or significant value to their enterprise.

Looking forward, 69% of tax and finance executives say they expect their organization’s overall focus on tax governance to grow in the coming two-year period. That is important because the new wave of risk and controversy, coupled with new revenue authority requirements around governance, will test the resiliency of organizations’ current tax governance models.

Tax and finance executives can test their tax governance model as it relates to tax risk and controversy in several ways. The first, which is definitely not recommended, is to wait and see whether new disputes arise. Second, companies already participating in mandatory tax compliance assurance programs (in jurisdictions including Australia, Germany, the Netherlands, New Zealand and the UK) can expect periodic feedback from the tax authority as to the rigor of their model. Third, they may choose to participate in one of the many voluntary tax authority programs that review and test the efficacy of their governance capabilities, such as in Singapore and Malaysia.

Tax and finance executives generally have positive outlooks on such voluntary programs. Fifty-nine percent say they are somewhat or very likely to participate in them where available, while 22% say they are already participating. Just 19% percent say they are somewhat or very unlikely to participate.
The right data enables effective tax risk and controversy management
Why tax governance is key in an era of more tax risk and controversy

Better data is a critical way to equip any tax governance model with the insights needed to effectively manage tax risk and controversy. This is the second key area of activity that should be prioritized.

While overall tax and financial data management is not a responsibility of tax controversy specialists, these professionals will have a vested interest in making sure that the right data is always available; a tax return based upon accurate data is always preferable to trying to source and explain additional data or evidence after filing has occurred.

Perhaps first and foremost, tax functions need to ensure that appropriate time is spent upfront identifying the right data and ensuring it can quickly be accessed if an audit or examination does occur. “Better data from a transfer pricing perspective centers upon a spectrum of different sources,” says Fultz. “Generally speaking, the tax function needs detailed and accurate financial information, legal agreements, business documents and more. The requests for this data come early in exams, and delays in responding to financial data requests can do irreparable harm to an exam relationship.”

Digital tools can help track audits globally and forecast where the next dispute may occur.

Second, tax functions need better data — and insights — around active tax audits and disputes. To accomplish this, data must be accurate, current, replicable and available.

“Tax function leaders also want full visibility of disputes in order to understand where their biggest or most urgent exposures lie,” Coronado says. Yet the survey results indicate many are falling short of this goal. Just 25% have complete visibility over all disputes globally, virtually the same number as in our 2021 survey (24%). Nearly half — 45% — say they have “substantial” visibility, defined as more than 75% of their disputes. Twenty-six percent have only partial visibility, defined as 25% to 75%.

One reason for this might be that gaining better visibility requires the right processes to be in place to communicate data to the right people who can interpret and manage it. In essence, more centralized tax functions need data around disputes to be communicated to them by local professionals who may often sit outside of the tax team.
Ideally, data captured from accurately tracking tax disputes can also be analyzed to produce new insights that can help predict where and on what topic a future audit may occur.

"Executing a robust data strategy doesn't just mean that audits and examinations can be responded to in a timely manner," says Joel Cooper, EY Global International Tax and Transaction Services Controversy Leader. "More broadly, the better an organization's access to clean, segmented and accurate data, the more time that can be dedicated to strategic issues — including being more proactive in identifying and managing new risks, stopping them from turning into disputes."

**Taxpayer data goes public**

The prospect that CbCR filings will soon become public in many jurisdictions was of particular concern to respondents, given the potential reputational risks that may occur as activists and the general public try to interpret this complex yet summary information. As a result, tax function leaders will need to create an ongoing process whereby all CbCR filings and existing public disclosures (such as narrative descriptions or total tax and social contribution models) are reviewed as and when new CbCR reports are published. This will represent a heavy burden on the tax function; automating some or all of the data-related tasks will be important.

Moving forward, tax controversy specialists will need to have a solid understanding of data science, clear visibility of what data is available to support their objectives and be empowered to mandate changes in the tax function's data strategy (and operations) as and when needed to support controversy management objectives.

"Tax function leaders also want full visibility of disputes in order to understand where their biggest or most urgent exposures lie."

*Luis Coronado*

EY Global Tax Controversy Leader
The quest for tax certainty
Why tax governance is key in an era of more tax risk and controversy

Not knowing how much tax will need to be paid in any given year is a common source of uncertainty, however large or small a business may be. That uncertainty, which the survey indicates will likely grow in the short-to-medium term, can often translate into the need to create a tax provision of substantial size for many companies. In extreme circumstances, a dispute or litigation can trigger a financial restatement.

As a result, most businesses seek to increase tax certainty whenever and wherever they can in an attempt to either prevent disputes in the first place or to better address disputes that do occur. Creating certainty involves both internal activities and the consideration of a spectrum of tools and programs offered by many tax authorities. Tax function leaders who have strong governance and better data in place will be in the best position to fulfill this quest for certainty.

“Businesses understand that they have tax obligations, but a lack of clarity around what those liabilities actually are can often be more impactful than the actual amount due,” says Cooper. “It may seem paradoxical that tax certainty can be achieved in such an uncertain world, but there are definitely ways to increase it.”

Looking at the tax function’s internal activities first, survey respondents say that being more proactive in identifying and managing tax risks before they turn into disputes would bring the highest value to their tax function in the next two years. The larger the enterprise, the more likely they were to subscribe to that view.

Managing tax risks is contingent on first being able to identify such risks, achieved via the establishment of effective tax risk assessment protocols. Again, success in this area requires the commitment of not only central tax function resources, but also collaboration with local tax and finance personnel.

Once emerging risks are identified, tracking them through the controversy lifecycle is critical. Businesses that are already actively moving in this direction typically complete three important activities, usually in a set order:

Consider being proactive earlier in the controversy life cycle by embracing government programs.

It may seem paradoxical that tax certainty can be achieved in such an uncertain world, but there are certainly ways to increase it.

Joel Cooper
EY Global International Tax and Transaction Services Controversy Leader
• First, they create a tax risk “register.” This helps alert tax leaders and controversy managers to new tax risks at both central and local entity levels. Eighty-three percent of tax and finance executives say that adopting such a risk register would deliver some or significant value.

• Second, they link tax risk assessment results to tax risk management processes. That might involve amending an internal tax control or utilizing a revenue authority tool such as an Advance Pricing Agreement (APA).

• Third, they use the risk assessment results to identify those transactions for which auditable, transparent and supporting documentation should be created. Eighty-four percent of tax and finance executives say that improving the contemporaneous documentation of certain transactions to increase overall tax audit readiness would deliver some or significant value to their organization.

Prevention is better than cure

Externally, many tax authorities offer a variety of programs that may help a taxpayer achieve higher levels of tax certainty (but not necessarily legal certainty) that the positions they take on their tax return won’t be audited.

These programs span both pre- and post-filing phases. Pre-filing programs include securing tax rulings or APAs, where 80% say that securing one or more APAs would deliver some or significant value. That’s not surprising given the number of companies that are actively trying to secure new APAs in advance of Pillar Two’s implementation.

Also available in the pre-filing period are various cooperative compliance programs, both at the national level (such as the Dutch horizontal monitoring program) and multilaterally, in the case of the OECD-supported International Compliance Assurance Programme (ICAP), now adopted by 22 jurisdictions. But less than half of respondents (48%) say they currently execute a clearly defined, proactive, cooperative compliance strategy.

Tax disputes will often occur even after all best efforts to prevent them have been exhausted. Here, the breadth and scope of documentation required by tax authorities is rapidly expanding, but tax and finance executives indicate that work remains if business is to keep pace with the authorities’ demands. Some 54% of respondents, for example, say they don’t currently create and maintain substance or business activity-based tax documentation files that can be called upon if a transaction is audited. Coincidentally, the same proportion say they select key transactions and periodically review the supporting documentation. This is one area in which survey respondents may wish to consider investing more time.

Tax risk “registers” gain popularity

83% of survey respondents said adopting a tax risk register would deliver some or significant value to their tax function.
Both the existence and the outcome of a tax dispute can dramatically reduce tax certainty. Proactive tax leaders therefore tend to consider what can be done to increase tax certainty at both the outset of and during a dispute itself. Survey respondents say, for example, that their leading priority is to try to better understand the tax authorities’ concerns and objectives before a tax audit commences. They will also put processes in place to help ensure that any settlement considers the potential multiyear, multijurisdictional “red flags” and knock-on effects. Finally, proactive tax leaders will enter each audit or dispute with as much knowledge of the local audit process and cultural approaches as possible.

It’s never too late to look for resolution

When disagreements do result in new tax assessments, dispute resolution programs can also contribute to higher levels of tax certainty. Central to resolving cross-border double taxation disputes and obtaining relief from double taxation is the Mutual Agreement Procedure (MAP).

MAP is one of the main tools available to companies for resolving such disputes, and peer reviews (under BEPS Action 14) have spurred changes regarding the structure and organization of competent authorities, streamlining their processes for resolving MAP cases in a timely manner.

The results of the OECD’s work are only slowly starting to be more visible; 37% of tax and finance executives (one percentage point higher than in our 2021 survey) say they use MAP, though this figure does grow among the largest companies. However, many businesses may not be aware that MAP can be used to address a spectrum of issues concerning taxing rights, beyond transfer pricing and profit allocation. Given Pillar Two and other developments, consideration of MAP will become even more important.

When agreement between taxpayer and tax authority is simply unachievable, tax litigation may be the only way to proceed. But nearly two-thirds (64%) of respondents say they don’t have a defined tax litigation strategy.

Looking ahead — to Pillar Two implementation, public CbCR and the implementation of a multitude of new local transparency and disclosure requirements — any efforts to achieve higher levels of tax certainty will be paramount.

Certainty in an uncertain world

Many tax functions are now moving to centralize and combine more of their controversy processes, localizing policies and controls and putting in place well-defined tax controversy roles. These activities are designed not to withdraw responsibility from local professionals, but to collaborate more closely in identifying and managing risks and avoiding exposures.

Any degree of tax certainty that can be secured in an uncertain world is safer, smarter and more strategic than sitting back and hoping for the best. A tax function that is better connected to the business through a robust tax governance framework and that makes use of the latest data capabilities will be in a position to contribute more value to the organization’s overall objectives, be they related to ESG, long-term value or protecting the enterprise. And that turns risk into opportunity.
The need for strong tax governance has emerged as a basic necessity in the effective management of tax risk and tax controversy, the EY 2023 Tax Risk and Controversy Survey finds. Strong tax governance, improved data capabilities and obtaining greater tax certainty can help the tax function provide more long-term value to their organization.

Summary

Contacts

Luis Coronado
Partner/Principal
EY Global Tax Controversy Leader
luis.coronado@sg.ey.com

Martin Caplice
Partner/Principal
EY Asia-Pacific Tax Policy and Controversy Leader
martin.caplice@ey.com

Paul Mulvihill
Partner/Principal
EY Americas Tax Controversy Leader - Canada
paul.f.mulvihill@ca.ey.com

Jorge Libreros
Partner/Principal
EY Americas Tax Controversy Leader - Latam North
jorge.libreros@lan.ey.com

Rodrigo Munhoz
Partner/Principal
EY Americas Tax Controversy Leader - Latam South
rodrigo.munhoz@br.ey.com

Bryon Christensen
Partner/Principal
EY Americas Tax Controversy Leader - United States
bryon.christensen@ey.com

Jean-Pierre Lieb
Partner/Principal
EY EMEIA Tax Policy and Controversy Leader
jean.pierre.lieb@ey-avocats.com

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