BoardMatters Forum
India

BoardMatters Quarterly

Insights for boards and audit committees

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Decision Analytics and the board's role in driving it

Big data is today seen as one of the biggest game-changers for business. But many organizations are still to view data as an asset and are therefore unable to source and manage it effectively. This article explores how boards can help the organization to seamlessly embrace data analytics and help derive optimum value.

BoardMatters Forum highlights

This edition of the *BoardMatters Quarterly* comes alongwith our *Viewpoints* publication. *Viewpoints* brings you the highlights of the 2nd EY BoardMatters Forum at Mumbai in November 2014. Featuring Mr M Damodaran on Board Performance Evaluation and a Panel Discussion on Effectively Managing the Audit Committee.

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For any business, corruption can potentially lead to significant financial loss and reputational damage. Every day, businesses in the country are confronted with numerous corruption-related risks. This feature discusses how organizations can create and deploy a dedicated anti-corruption program by strengthening internal controls.

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Amal Ganguli is one of corporate India's most respected independent directors, who serves on the boards of several leading organizations. As a board member, Mr Ganguli is also the Chair and Member of the Nomination and Remuneration Committees (NRCs) of several companies. In this exclusive interview with EY, Mr Ganguli tells us why he believes that NRCs will enhance transparency and governance, how the committee can play a meaningful role in the selection of both directors and key managerial personnel and the metrics that should be considered when evaluating the effectiveness of board members.

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Building a better working world

Decision Analytics and the board's role in driving it

The Age of Analytics

In the past few years, analytics has made a strong appearance and is touted to be the biggest game-changer across industries and functions.

While there is no doubt that harnessing analytics can offer step-function improvements in sales performance, revenue generation and quality management, it is equally critical that the organization understands the complexities and issues that come along with it.

Big data is a broad term to describe data which is substantial, complex and unwieldy to manage. It is a collection of very large data-sets which cannot be processed or analysed by traditional methods. This collection of data has been aided by the exponential reduction in storage costs, the emergence of interconnected digital devices, the internet of things and cheap and reliable communication networks.

The 3 V's of Big Data

i. Velocity : The frequency and speed in which data is processed and captured

ii. Volume: It is estimated that more than 2 zettabytes (1 zettabyte = 1021 bytes, the equivalent of more than 25,000 trillion documents) is being generated daily. This is only expected to increase.

iii. Variety : The texture of this data is also changing with more sources being made available – both structured and unstructured

The fourth 'V' – value, is imperative to unlock and harness the true potential of data.

Like human DNA, which has more than 98% of "Junk", a large portion of Big Data in any organization is low value. It is critical for the company to be able to segregate the most useful strands of data and utilise them to their maximum potential.

Data is an asset

Most organizations do not view their data as assets. Data offers a great source of potential income, a plug for revenue leakage and a control mechanism to prevent financial and reputational damage. A significant value can be generated by leveraging existing internal information.

Most organizations focus on the first aspect of analytics – as a driver for revenue. However, there are considerable opportunities in using analytics for risk, compliance, control and audit.

Analytics can help identify potential gaps by surveying all the data within the company to answer questions like "Has any employee been listed as a vendor, in violation of company policy?" "Are there ex- employees for whom expenses claims are still being processed?" or "Are there blacklisted customers or vendors for whom new identities have been created in the system and business continues to be done with them?"

Such queries require answers to be sought from multiple sources which can be effectively and scrupulously investigated with the power of analytics.

Analytics can also offer indispensable aid in litigation by surfing through millions of records, identifying instances that help bolster the organization's case.

The applications for analytics across functions are manifold.

How analytics can help different business functions

Sales	Marketing	Risk	Finance	Internal Audit	Human Resources
▸ Which is the best channel to reach out to a customer?	▸ How can marketing campaigns be generated and managed?	▸ How can fraudulent transactions be detected early on?	▸ How can periodic closings be made more efficient?	▸ Can audit be conducted on entire information periodically, quickly and accurately?	▸ What is the overall sentiment of the employees?
▸ Which products/ services to cross-sell to which customer?	▸ What is the optimal media-mix?	▸ What are the credit terms that should be offered to customers?	▸ Have lower tax credits than eligible been claimed?	▸ Can triggers be generated to identify control gaps?	▸ Can attrition be forecasted?

The board's role

Board members, as custodians of a company's assets, have to strive to enhance and protect the often-neglected asset of data. Underutilisation of this valuable asset puts the organization at a competitive disadvantage.

Board members need not understand or are expected to understand the intricacies of information management; however, they can provide guiding philosophies to maximise value from analytics.

Make data serve you – Many organizations look at the huge volume of data they generate and ask themselves what they can do with it. This is putting the cart before the horse. The data is an enabler for strategic decisions – to prove or disprove a hypothesis. Ask key questions on what decisions the organization needs to take and then have the team seek the relevant data. This directs the organization in a more focused search for the right data rather than sieving through millions of records in the hope of finding something.

Ensure information is used responsibly – In this day and age of privacy invasions and digital hacking, consumer trust in data-centric organizations is not very encouraging. Management needs to ensure that it maintains a long-term perspective towards customer engagement, enriching its information (and revenue) along with customer experience, and does not focus on short-term uni-directional financial gains. Strong data governance and resilient information infrastructure are key to ensuring this.

Nurturing a culture of analytics – While analytics can provide a bulwark for intuitive sense, it can also sometimes provide counter-intuitive revelations.

Board members have the opportunity to be "analytics evangelists" with CXOs, in driving this analytics sensibility, helping the organization embrace analytics to peel away qualitative judgement to find the kernel of quantitative truth beneath.

Statistics cannot be divorced from business intelligence – Numbers by themselves can tell a misleading story. Correlation does not imply causality. Have sales to a particular customer declined due to reduced sales interaction or is the sales officer engaging less due to reduced customer budgets? Business intelligence is the key to unlocking these answers. Board members, by their breadth and depth of experience, can call out logical fallacies and gaps and protect organizations from traversing on ill-conceived paths.

Data is never and always enough

Many organizations in India are reluctant to use analytics in the belief that they lack enough information. There is never an ideal condition to roll-out the data analytics processes. An early start will always give the organization an edge over its competitors. The analytics voyage can start with a simple assessment of what information is already available, irrespective of its form and structure.

These are very exciting times, where the power of information can radically swing fortunes. The new advances in technology and methodology are opening whole vistas for expense management and revenue opportunities.

This is true even for those organizations that have not seriously invested their resources or even mind-share in building their analytics capabilities yet.

There is no better time to start than now. And board members are uniquely positioned to relay this message

Questions to consider:

- What strategies and tactics can be supported by data?
- What are the key drivers for business and is the information available correctly, on time?
- How is information captured, stored, collated and disseminated? Is there a single version of truth across the organization?
- What stage of the analytics life-cycle is the company in? What is the road-map to achieve a higher maturity level?
- Which is the team or the key members who will be the custodians of the data?
- Is the right infrastructure, personnel, organizational culture and drive present to embed analytics?
- What are the investments in analytics initiatives and the expected ROI?

How to boost internal controls to tackle corruption

Everyday, businesses in India have to deal with numerous corruption-related risks. A majority of these are in the form of theft of physical assets and information, bribery, and internal financial frauds. This trend, combined with a stringent regulatory and enforcement environment, has brought risk management to the fore. It is not a choice anymore, but a necessity.

If you look at India Inc. in recent times, you will observe how scandals and frauds are increasingly becoming rampant. EY's 13th Global Fraud Survey, rates bribery and corporate fraud as the biggest risks, which affect Indian corporate entities this year. Businesses are required to develop a robust internal control program to assess and mitigate these risks. We now see Indian companies deploying targeted anti-corruption compliance programs, financial controls, trainings, internal audits and other monitoring mechanisms.

In fact, the anti-corruption watchdog, Transparency International, has rated an Indian conglomerate as the best in emerging markets for their measures to combat corruption.

Designing a suitable anti-corruption risk program

The starting point for designing an anti-corruption risk program is a holistic assessment of risks inherent in the business; the portfolio of projects in the pipeline; dealings with government entities and intermediaries; and complexity of the operational and regulatory environment.

For instance, a large Europe-based utility firm has a clearly laid out anti-corruption program called "Zero Tolerance of Corruption". It enlists guidelines for matters such as contributions to political parties, facilitation payments, and relations with third parties.

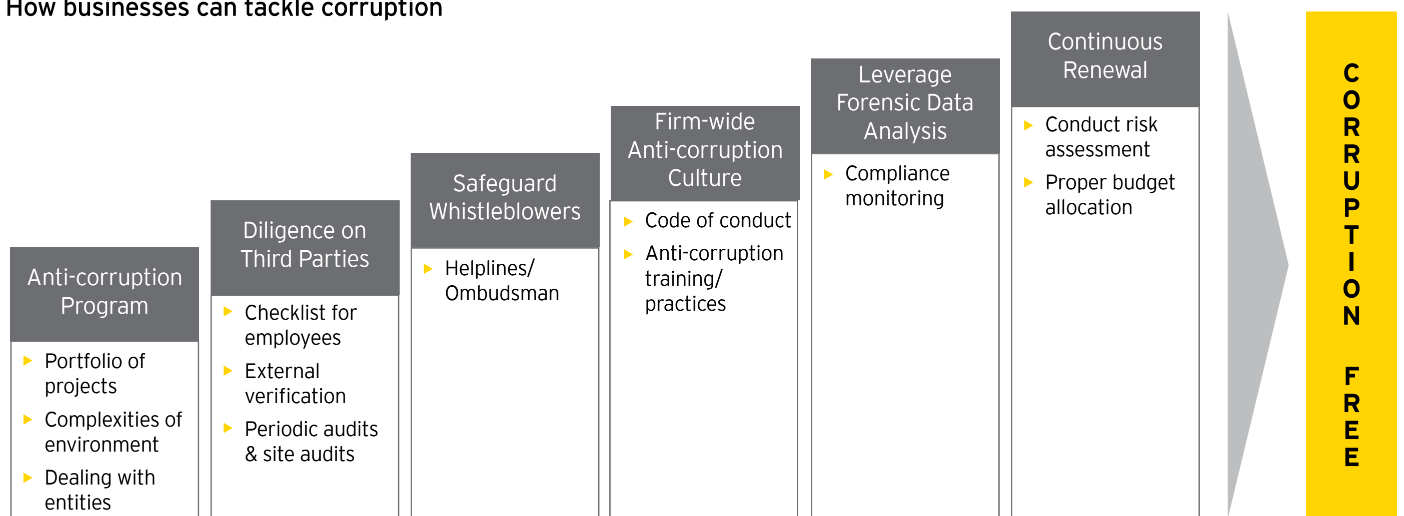
A "one-size-fits all" approach is not appropriate for India's diverse and dynamic business environment. Businesses are required to develop a program which is well-balanced between control policies and business necessities. This is especially relevant as there are vast differences in customer segments that companies serve. For instance, cash is a preferred mode of payment in rural India. A company that relies on the rural market cannot afford to have a control policy restricting the use of petty cash.

Due diligence on third parties

An essential element of an effective compliance program is third party due diligence. Companies are constantly put at risk due to their dealings with third parties and their exposure to corruption schemes.

Businesses should have a due diligence framework in place for third parties, that covers an assessment checklist for local employees, external verification, and periodic audits and site visits. It is also advisable to train local sales and finance personnel on how to identify "red flags" when offered/requested payments are over and above the services rendered.

How businesses can tackle corruption



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There should also be a well-defined policy regarding facilitation payments: Several times, corruption is disguised in the form of facilitation of payments. To alleviate such risks, companies should set in place a clear corporate policy on facilitation payments that dictates the extent to which such payments are allowed and ensures their accurate documentation.

Safeguarding whistle blowers

Turning a blind eye to violations can result in criminal and civil liabilities for the company as well as for individuals. However, several times, employees shy away from disclosing violations fearing negative implications of the disclosure.

As a response, companies should deploy mechanisms such as an ombudsman or helplines that facilitate and encourage its people to report any suspected malpractice. These mechanisms will initiate the necessary investigation while maintaining anonymity of the person.

Moreover, India's regulatory watchdog, the Securities and Exchange Board of India (SEBI) has made it mandatory for listed companies to have a whistle-blower mechanism for their employees and directors. To be effective, the whistle-blower policy should prompt timely action from the management and ensure protection of people who raise their voice against malpractices.

For instance, a leading Indian automobile company has a whistle-blower policy that sets a 15-day deadline for the Whistle Officer or committee to submit an investigation report about the complaint and ensure timely redressal.

Firm-wide anti-corruption culture through training

Employees are the face of a company and their conduct constantly exposes it to various types of risks. As fraud manifests itself in minor transactions across an organization, it is very important to drive anti-corruption as a cultural element.

It is essential for the senior leadership to motivate all its employees to be vigilant. Companies should introduce mandatory training on the company's code of conduct and anti-corruption practices.

One such example is a large computer networking products and services organization, which has made its global anti-corruption training a mandate for all its sales and marketing employees, channel partners, distributors, as well as sales supporting consultants.

A training module, which takes into consideration employees' roles and responsibilities and is periodically renewed for new as well as transitioning employees, can go a long way in creating a firm-wide anti-corruption culture.

Leveraging forensic data analytics

Companies can use data analytics as a tool for compliance monitoring. This can help in identifying high-risk vendors, track email communications carrying sensitive words, and determine which locations to audit.

A Fortune 500 company recently conducted an anti-fraud/anti-corruption review covering 15 countries and thousands of employees and vendors. The company analysed more than two terabytes of data, comprising more than 25 million documents, using forensic data analytics tools such as data visualization and text mining. The exercise resulted in improved project efficiencies and identification of high-risk vendors, customers and employees.

Continuous renewal

As the business environment becomes more dynamic than ever, companies will be constantly exposed to more regulatory changes and new types of risks. What is required from businesses is to periodically conduct risk assessments to ensure relevance and effectiveness of their anti-corruption programs.

In today's world, no organization is immune to bribery, corruption or fraud. Those that understand risks and implement proper controls will be best prepared to compete in the global economy.

However, businesses will also be required to measure the cost of implementing such measures and see that they do not overrun the benefits of risk control programs. Proper budget allocation and tracking of records are required for successful implementation of these programs.

It is clear that there are no quick fixes to manage corruption-related risks, but building best practices to deal with such risks is the need of the hour. The risk profile of a company changes with every strategic decision that it takes, and therefore, it is important to review and update risk assessment on a regular basis. Those who fail to do so will expose themselves to countless risks in this corruption-prone environment.

“Board performance should not be gauged only on monetary criteria”

In conversation with Amal Ganguli

Amal Ganguli is one of corporate India’s most respected independent directors, who serves on the boards of several leading organizations. As a board member, Mr Ganguli is also the Chair and Member of the Nomination and Remuneration Committees (NRCs) of several companies. In this exclusive interview with EY, Mr Ganguli tells us why he believes that NRCs will enhance transparency and governance, how the committee can play a meaningful role in the selection of both directors and key managerial personnel and the metrics that should be considered when evaluating the effectiveness of board members.

Q: The revised Clause 49 requirements mandate formation of a Nomination and Remuneration committee. Do you believe that this change will enhance governance on selection as well as remuneration of directors and Key Managerial Personnel (KMP)?

AG: After the 2008 global financial crisis there was significant focus on moderating remuneration of directors and KMPs globally. In response to the growing concern most major countries such as the USA, the UK and Australia came out with regulations requiring stronger review and oversight of remuneration of directors and KMPs.

Back home, I believe that the new requirements mandated by SEBI are a positive step to protect the interest of the business and shareholders, and to ensure that remuneration of directors and KMPs is fair and reasonable. It will also ensure that appropriate evaluation processes are followed such that remuneration levels are appropriate to the size and nature as well as the potential of each business and that the organization is able to retain, motivate and retain the talent that it needs. Remuneration committees play an important role in ensuring an objective approach in management of executive remuneration. The formulation of a selection and remuneration policy by the board should create transparency in the remuneration process and effectively enhance governance.

Q: Do you believe that there is adequate guidance available to Independent directors on formulating such policy and setting performance evaluation criteria? Is there any precedent available in other developed countries where such changes were adopted and successfully implemented?

AG: Most developed countries have adopted similar requirements on the formation of nomination and remuneration committees comprising independent directors. Some countries also encourage such committees to appoint independent compensation advisors to assist in the process of defining the compensation and performance evaluation policy that are in the organization’s best interests and aligned with its business vision and objective.

In India, the salaries of banking heads already need to be approved by the RBI. Moreover, several large companies as a best practice have formed compensation committees and defined clear compensation policies in line with global requirements. In my view, while there is a fairly good amount of precedence already available within and outside India where these committees have been effectively implemented, there is a need for more detailed guidance.

Q: What according to you should be the focus areas of this committee while setting selection criteria for KMP’s?

AG: Defining the selection criteria for KMPs will be one of the most challenging activities for this committee. Various KMPs require different skills and qualifications based on the role, which in turn will require enough flexibility in the selection criteria. The committee should set criteria to select a diversified group of KMP’s who can contribute in different ways to the effective functioning of the company. The selection criteria should be aligned with the business strategy and should focus on identifying the skills which will help a KMP achieve these goals. Apart from skills, the ability of the KMP to work constructively with the existing management and directors to enhance the efficiencies of the company should also be an important selection criterion.

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Q: Should the committee be directly involved in the selection, evaluation, remuneration decision making process of KMP and Directors or should it be providing criteria and guidance for such decisions?

AG: The Act requires the committee to formulate the criteria to determine qualifications, positive attributes and independence of a director and recommend to the board a policy, relating to the remuneration for the directors, KMP and other employees. The Act however does not stop at this stage, but also provides that the committee will identify persons who are qualified to become directors and who may be appointed in senior management positions in accordance with the criteria laid down and recommend their appointment to the board.

The committee is also expected to carry out performance evaluation of every director (executive, non-executive or independent). Hence, while the Act has cast much wider responsibility on the committee, it is also important for the committee members to ensure that their decision making is based on an objective criteria and their independence is not impaired while recommending a candidate for directorship or KMP position or while evaluating performance of the directors.

Q: What should be the component of the remuneration package of directors and KMP - should their package be linked to only monetary performance of the company?

AG: The Act prescribes that while formulating the selection, remuneration and performance evaluation policies, the committee will ensure that the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required for the company to run successfully. It further states that the relationship of remuneration to performance should be clear and should meet appropriate performance benchmarks. Moreover, most importantly, there should be a balance between fixed and incentive pay, reflecting short and long-term performance objectives of directors, KMPs and senior executives and ensure they are aligned to the working of the company and its goals.

In determining the remuneration policy, the committee also needs to take into account various factors such as local legal and regulatory requirements, the risk appetite of the company and alignment to strategic long term objectives. Linking remuneration purely to monetary performance may also increase risk of unethical business practices to obtain growth objectives, hence the right balance between monetary and non-monetary performance linkage is critical for a good remuneration policy. In addition, the policy needs to consider the expectations from various roles in formulating the remuneration package. Defining a good remuneration package for KMPs and directors can go a long way in achieving business objectives in the long run.

Q: Which non-monetary performance criteria should be linked to the performance of the KMP and directors and what should be the share of monetary and non-monetary criteria?

AG: Undoubtedly, monetary gains for a company are vital. However, the KMPs and directors should not be solely assessed by companies on this criterion. It can be beneficial to have an equal balance between monetary and non-monetary criteria to ensure that the performance of the KMPs and directors' is not directly dependent only on the monetary performance of the company. This will help them insulate against phases of financial downturns of the company.

Some of the non-monetary performance criteria can be factors such as good corporate governance processes, findings in Internal Audits and other review mechanisms, maintaining high quality standards in all dealings, contribution to creativity and innovation, ethical behaviour, strict adherence to the code of conduct, improving service patronage and successful operational delivery. The aim of selecting the non-monetary performance criteria can be two fold – to provide incentives to the KMP's and directors' giving equal emphasis to non-financial factors such as product quality, innovation, which contributes to a company's market value and to ensure that the management of the company satisfies the code of conduct, adheres to the legal compliances and ethics policies and adopts the best governance practices.

The committee must also consider benchmark remuneration for the same role by their peer and competition for retaining key executives. This becomes an important criterion when the company is not performing well compared to competitors and hence, key resources have to be incentivised to achieve benchmarked performance through a competitive or aggressive remuneration and reward policy.

Q: How should companies making losses or those not achieving their targeted earning remunerate KMP and directors?

AG: A good performance evaluation and remuneration structure will ensure that a fair balance is achieved between rewarding performance and penalizing non-performance. It is very critical to accurately link the KMPs goals with overall company

goals in order to ensure consistency between performance of company and rewarding the KMP.

What is important is to realize that just because a company is making a loss does not necessarily mean it has not met its goals for a particular year and that the KMPs have not performed as required. For example, a new company or a company which has undergone major changes could be making losses in line with the short-term business plans to achieve long term objectives. In such a case, it could be possible that the KMPs have performed well and may need to be rewarded. Moreover, to assume that a company is making profits and hence the KMPs should be rewarded would not be the right remuneration strategy. Hence, the right balance between fixed and variable compensation and linking of KMP performance with monetary and non-monetary performance of the company is very critical.

Q: What is your view on linking ethics, compliance and governance scores of the company to KMP and director's performance and remuneration?

AG: The current global financial landscape requires companies to be highly ethical, legally compliant and have strong governance. The new Companies Act in India casts specific responsibility on the directors to ensure that the Company achieves these standards. Moreover, modern day societies expect that companies operate ethically, be legally compliant and have good governance practices. In such circumstances, the companies have to incorporate the industry best practices and evolve to the next level. This can be driven by KMPs and directors by linking ethics, compliance and governance scores of the company to KMP and directors' performance and remuneration. The linkage can provide them an incentive to achieve the required standards which will also benefit the company, resulting in a win-win for all.

Q: How should the committee approach board diversity? Given the limited supply of women candidates, how should committees encourage diversity even at KMP and senior management levels within the company?

AG: Achieving diversity and inclusiveness in the workplace has several demonstrated benefits, including enhanced creativity, better and more productive communications and faster problem solving among others. A majority of companies profess that they are implementing measures to improve gender diversity. Despite this assurance, however, very few of these companies appear to have been able to achieve satisfactory results from their actions. Committees need to understand that bringing board diversity requires full implementation across the entire organization and it should be a sustained effort over a period of time. Furthermore, effective and continuous monitoring is also a key to achieving this diversity.

At a broad level, research also shows that the corporate culture and the mindset of KMPs and senior management level needs to change. To bring about this change, the committee can include board diversity as a priority on the strategic agenda, have programs to develop women as leaders and promote systematic inclusion of women in the recruitment and promotion cycles of the company.

Q: Do you believe that performance assessment criteria and remuneration model for CEO and CFO should be different? How should companies allocate the weightage among performance indicators for "grow the business"vs"protect the business"?

AG: Equality can be expected between two similarly placed individuals which is not the case here. The CEO and CFO perform different roles and discharge different responsibilities. The yearly targets for both are varied. In such circumstances, it is preferable not to equate the performance criteria and the remuneration for the CEO and the CFO. They should be assessed and remunerated based on the different expectations from them and their individual performance through the year.

Companies may, depending on the operating conditions and business circumstances, weigh the performance indicators "grow the business" vs "protect the business" equally or disproportionately as some situations will require emphasis on one of them and some on another. Both these indicators carry an equal amount of responsibility, risk and the need to comply with governance standards.

Trends in independent board leadership structures

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Board leadership structures have evolved dramatically over the past decade or so, with more companies separating the positions of chair and CEO, and appointing independent board leaders. Today around 90% of S&P 1500 companies have some form of independent leadership compared to only 10% in 2000. These leadership positions vary among companies and include independent chairs, lead and presiding directors. The responsibilities assigned to these positions vary among companies as well.

There is no consensus view on best practice. Directors have different thoughts on which leadership structure is most effective - and thoughts on what works best may change based on company specific circumstances. Views among investors differ too. For some investors, there is no substitute for an independent board chair, while others find lead or presiding directors to be sufficient, provided the responsibilities are clearly defined and robust.

Current Securities and Exchange Commission (SEC) rules require companies to disclose in the proxy statement whether and why they have chosen to combine or separate the CEO and board chair positions and why this leadership structure is the most appropriate.

Using the EY Center for Board Matters proprietary corporate governance database, this feature reviews evolving trends around independent board leadership structures, examines the key responsibilities most commonly assigned to these roles, and highlights investor initiatives in this area.

Independent board leadership landscape

The trend is clear — having an independent board leader has become standard practice. Most common are independent board chairs or lead directors with position responsibilities such as setting board meeting agendas and controlling the flow of information to the board.

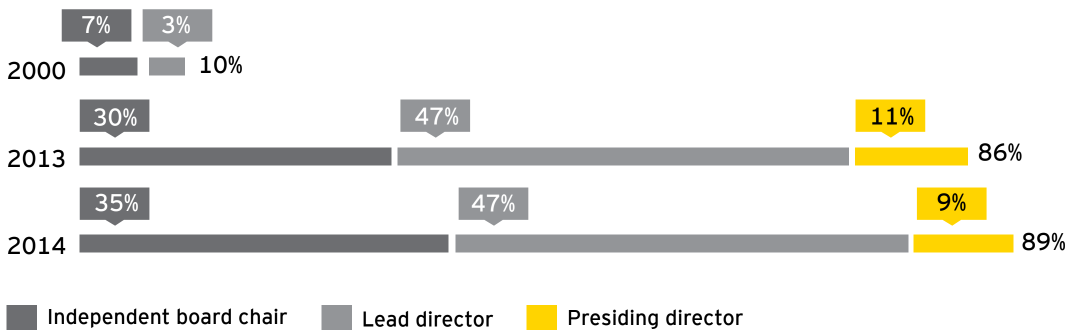
Fewer companies have presiding directors, likely because they are often viewed as having a more passive role. Larger companies are more likely to have independent lead directors, while independent board chairs are more common among smaller companies.

Board leadership debate plays out via shareholder proposals

Shareholder proposals seeking the appointment of an independent board chair, as well as company-investor engagement on this topic, are drivers of change in board leadership structures. The increase in independent board chair shareholder proposals from 2000 to 2013 mirrors the significant increase in the appointment of independent board leaders over the same time period.

Despite record numbers of shareholder proposals, support levels have declined in recent years. This may represent the general lack of consensus over a preferred structure.

Evolving independent board leadership practices at S&P 1500 companies



Source: EY Center for Board Matters

Global focus on tax base erosion and profit shifting

What boards should know about the OECD initiative

The tax landscape is clearly changing. As governments search for additional revenue streams, the focus on transparency is increasing and tax policies are being modified.

Boards and audit committees need to be well informed about tax policy developments and trends worldwide — in the markets they currently serve and those they may be considering.

A key project to monitor is an effort by the heads of state of the G20 countries to curb tax avoidance by companies. This initiative is driven largely by concern about the potential for multinational corporations (MNCs) to shift income to low- or no-tax jurisdictions.

The Organization for Economic Co-operation and Development's (OECD) base erosion and profit shifting (BEPS) project is meant to better coordinate how countries address tax strategies perceived as eroding countries' tax bases. The project is intended to spur governments to change their tax laws and treaties in order to reduce opportunities to shift profits to lower-taxed jurisdictions.

Based on a 15-point action plan issued in July 2013, the BEPS initiative focuses on several areas, including:

- Reporting and transparency
- Transfer pricing
- Deductibility of financing costs
- Entitlement to tax treaty benefits
- Tax treatment of companies operating in the digital economy
- Preferential tax regimes

The OECD plans to issue a series of reports, analyses and recommendations between September 2014 and the end of 2015.

Why are the OECD's recommendations important?

While not a governmental organization, the OECD is influential in setting global tax policy. Moreover, the BEPS project involves all of the G20 countries, including China and India, which are not OECD members.

Effects of the ongoing BEPS effort are already evident as individual countries have started implementing anti-BEPS policies through both legislation and enforcement activity, without waiting for the OECD's final recommendations.

For example, new tax laws in France and Mexico have included several BEPS-related changes, including fresh restrictions on the deduction of financing costs. Many other countries are also taking action.

The US Treasury has taken a lead role and has strongly supported some OECD BEPS action items and been more cautious or even critical in other areas. Anti-BEPS measures are also featured in some recent US international tax reform proposals, as well as in the Obama Administration's budget proposal.

Individual country responses to the OECD recommendations will vary, as will the timing of any legislative actions.

For this reason, companies and their boards need to carefully track BEPS-related developments, both at the OECD level and within the countries where the company has current or future operations, investment or activity.

By doing so, they can understand the trends and anticipate changes.

What is the expected outcome?

Ultimately, the OECD's recommendations are expected to play a role in reshaping country tax laws. The likely long-term result for MNCs will be more aggressive tax enforcement, heightened tax scrutiny, greater transparency requirements, increased compliance costs and, potentially, more taxes paid.

The OECD expects to release a number of items, including:

- A template for country-by-country reporting
- Guidelines on transfer pricing for intangibles
- Recommendations on hybrid mismatch arrangements (i.e., certain instruments or entities that are treated differently under the tax laws of two countries)
- Recommendations on options to address treaty abuse
- Report on the tax challenges of the digital economy
- Report on OECD member country preferential tax regimes
- Report on the feasibility of a multilateral instrument for amending bilateral tax treaties

In most of these areas, the OECD will work on implementation and other details into 2015. The OECD will also begin work on the action items with 2015 target dates, including treatment of interest expense, allocation of risk and capital, and controlled foreign corporation rules.

How should boards prepare?

A significant number of OECD recommendations are now in place, and countries are now assessing how to develop their local implementation. The timing is right for companies to review their business models and structures against each recommendation to identify possible pressure points.

Current reporting and compliance processes should be reviewed in light of the likelihood of expanded requirements in the future.

- Careful assessment includes preparing for the possibility of country-by-country reporting of financial and operating profiles for each country in which an MNC operates. Proactively managing global tax controversy is also important.
- Other steps companies can take to respond to BEPS-related developments include:
- Consider advance pricing agreements (APAs) and other early engagement with tax authorities to gain greater certainty
- Consider proactively communicating information regarding your company's total tax and economic contribution with key stakeholders, including regulators and shareholders
- Consider engaging with the OECD and country policymakers on these international tax issues

Given the many moving pieces of the BEPS initiative, relevant information that emerges from discussions with policymakers should be shared frequently with a company's management, board and other relevant stakeholders.

Source: EY Center for Board Matters

Questions for the board and audit committee to consider

- Has management conducted a strategic review of the implications of potential cross-border tax
- Has the board evaluated how the company can position itself for the evolving global tax landscape?
- Is the company ready for heightened scrutiny and tax audit risk, which can place increased pressure on cash tax and effective tax rate positions?
- Is the company prepared for the potentially substantial increase in global reporting requirements and the commensurate increase in compliance costs?

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