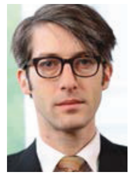
Comment

Views on topical issues

DOTAS and developing countries



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The DOTAS regime should be extended to include corporate tax abuse in the developing world.

As was reported by *Tax Journal* on 20 March, a consortium of development charities and anti-poverty campaigners, operating under the 'Enough food for everyone IF ...' banner, has proposed that the disclosure of tax avoidance schemes regime (DOTAS) be extended to include transactions effected by UK-headquartered multinational groups which threaten public revenues in poor countries.

The proposal takes as its starting point the proposition that certain jurisdictions are sufficiently poor, and have sufficiently unsophisticated tax systems, that they may properly be characterised as 'vulnerable'. These are places which suffer from endemic poverty and appalling under-investment in public health, education and infrastructure. We in the developed world are used to blaming such problems on corruption and conflict, but a tremendous volume of the wealth that flows out of these countries does so in the form of untaxed corporate profits.

In order for these profits to be properly taxed, the vulnerable jurisdictions need information as to how their tax is being avoided. If the corporate group avoiding tax in the vulnerable jurisdiction is headquartered in the UK, that information may be expected to be available in the UK, because the tax planning in question is invariably effected at group level. Fortunately, international mechanisms already exist to enable that information to be passed from the UK to the vulnerable jurisdiction – indeed, if the vulnerable jurisdiction is a signatory to the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, the UK has an *obligation* to pass such information over.

The only link that is missing from the chain is a disclosure obligation here in the UK, which is what has been proposed. The idea here is that, where a vulnerable jurisdiction-resident CFC of a UK-resident company enters into a transaction bearing the hallmarks of international corporate tax avoidance, the UK-resident company has an obligation to disclose the transaction to HMRC, which will pass the information to the affected jurisdiction. It is a carefully targeted, narrow spectrum measure that is perfectly feasible on a legal level and only applies where someone in the UK is effecting a transaction which looks like its purpose is to extract untaxed corporate profits from one of the world's poorest countries. To my mind, there is nothing there really for anyone to object to.

It is frustrating, therefore, that the UK government has chosen to reject this proposal without, it would appear, properly understanding it (see *Hansard*, HC debate, 25 February 2013, vol 559, col 197W). The objection appears to be that DOTAS is UK-specific and its existing hallmarks are specific to the UK tax avoidance game. This is certainly the case now, which is why what is proposed is an *extension* of DOTAS. But attaching the measure to DOTAS would be merely a matter of legislative convenience; there are extensions to DOTAS in the Finance Bill in any event, and its passage through parliament therefore provides a perfect opportunity for the proposal to be brought forward, debated and passed into law. The proposal, however, would work equally well as a stand-alone obligation.

The author provided technical advice on the proposal submitted by Action Aid, Oxfam, Save the Children and Christian Aid.

The tax director's trilemma

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How can the tax director cope with the seemingly impossible task of choosing between three equally unpleasant outcomes: becoming uncompetitive, failing to satisfy regulations and offending the moral judgement of the general community?

Tax directors could be forgiven for being confused. They are used to considering how to minimise the corporate tax burden and helping their firm complete in the market place, but they now must consider whether the tax affairs of the business satisfy the moral judgment of the wider community?

How should tax directors respond to this new 'trilemma'? One way to approach this issue is to use the analytical framework set out in 'The Shell Group Global Scenarios to 2025' (see lexisurl.com/s4iJM), which enables businesses to review their strategy in a changing environment. The scenarios outline a 'trilemma triangle', which is designed to illustrate three competing forces – competition, regulation and community – faced by businesses. Starting from the idea that society tends to hold these three forces in a kind of equilibrium or balance, we can form three basic alternative scenarios by assuming that one of the three forces becomes over time weaker than the others. The Shell scenarios describe them as follows:

- 'low trust globalisation'– which has stronger market forces and increased regulation but a weaker sense of community;
- 'open doors' – with stronger market forces and more cohesive (and demanding) civil societies but weaker regulation; and
- 'flags' – with stronger community values enforced through fiercer nationally-based regulation, with market forces and competition being weakened.

By working through a rigorous analytical process with the senior team, the tax function can examine how the business should take account of these potential futures and how the tax strategy needs to be adapted under each of them. For example, the likelihood that political (or community) representatives might call for more responsible behaviour from companies could arise as a possible outcome under the second 'open doors' scenario. But such an outcome would also be likely under the 'flags' scenario with politicians seeking to enforce community values through regulation, particularly on disclosure.

This approach will not provide a definitive solution, but it will put the tax director on notice that he needs to develop a response to these possible futures and not only have a response ready but, more importantly, to build the response into the strategy itself and hopefully avoid any negative exposure. The company might decide to prepare in advance a more solid public affairs management effort than we have seen in the UK in recent days, perhaps focusing on the benefits of tax competition for the consumer and the total tax contribution made by the company. Or the tax strategy might even be implemented at a lower tax efficiency, in order to leave a minimum amount of CT paid in the UK (as one company was reported as having done and which might also have avoided damage in recent cases). A third possibility would be simply to tough it out, concluding that the public expects companies to be tax efficient and that merely matching their expectations should not produce damage to the brand if they have complied fully with the law. In any event, it is clearly helpful to be able to identify the nature of the forces at play – in this case, community values – and therefore better understand them.