Abstract

This paper reviews tax risk management practices of large Australian companies to ascertain whether ethical considerations are an element of those practices. A company code of ethics or professional ethical principles do not appear to be applied by large Australian companies to set a standard for consideration and deliberation on acceptable tax risk. Statements around tax risk appetite do not generally refer to ethics and corporate social responsibility. Increasingly society demands a company justify their tax contribution and this paper considers whether a 'socially responsible' company would be expected to embed an ethical position in its tax risk management system, one in which there is a requirement to act in accordance with the 'spirit of the tax law' rather than the 'letter of the tax law'. It is anticipated that a focus on compliance with the 'spirit of the tax law' by large companies in making decisions about acceptable tax risk would discourage aggressive tax decision making and demonstrate a low tax risk appetite.

This research would be useful to revenue authorities as they seek to facilitate co-operative compliance, tax risk management and a mechanism to address uncertainty in the tax law.

Key words

Ethics, company tax, tax risk management

Over the last decade the nature of tax decision making by large companies[1] has changed substantially.[2] Revenue authorities around the world recommend all key decision makers in a large company be informed and consider the tax impact of their decisions.[3] A comprehensive tax risk management system, one in which all material tax risks are identified by a company in its decision making, is now considered good governance practice and something that the board of directors should initiate and participate in.[4] This paper considers the role of a company code of ethics and professional ethical principles in a comprehensive tax risk management system and ultimately tax decision making.

Tax transparency measures introduced by governments around the world have resulted in the detail of company tax contributions being made available to the public.[5] Whilst company decision makers have an obligation to maximise profit, ethical principles and reputational risk places pressure on tax decision makers to consider a variety of stakeholders including the community at large. The debate and commentary on company tax contributions in Australia has been extremely negative and media and lobby groups report on the tax compliance behaviour of high profile large companies that pay

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[1] The Australian Tax Office ('ATO') 'Large Business Group' includes business groups with a turnover exceeding AUD250 million and it is this group that the ATO focuses on in correspondence and publications concerning the need to adopt a tax risk management system. For the purposes of this research a 'large company' is defined as a company with a turnover exceeding AUD250 million, as it is this subset of companies that contribute significantly to company tax revenue in Australia (58 per cent) and are the target of the ATO tax risk management initiative. According to 'Australian Taxation Statistics 2009–2010' Chapter 3 Box 3.2, Table 3.3 and Table 3.9, companies with a turnover exceeding AUD250 million constitute 0.1 per cent of the total number of company taxpayers in Australia yet contribute 58 per cent of company tax revenue.
Inconsistent with the definition used for the purposes of this research, the ATO defines a 'large company' as a company with a turnover between AUD100 million and AUD250 million and a 'very large company' as a company with a turnover in excess of AUD250. The decision to use the threshold of AUD250 million in this research, as opposed to the AUD100 million used by the ATO, is justified based on the ATO focus on tax risk management practices of companies with a turnover exceeding AUD250 million and the fact that according to 'Australian Taxation Statistics 2009–2010' Chapter 3 Table 3.9 companies with a turnover between AUD100 million and AUD250 million contribute only .05 per cent of company tax revenue and the indication in preliminary research is that company group is unlikely to have put in place a comprehensive tax risk management system.

[2] Keinan, Y, 'Corporate Governance and Professional Responsibility' (2003) 17(1) *Tax Law Journal of Taxation and Regulation of Financial Institutions* 10.

[3] HMRC, 'HMRC Approach to Compliance Risk Management for Large Business' (March 2007) <http://www.hmrc.gov.uk/lbo/risk-update.pdf>; D Butler, 'Corporate Insolvency — Tax Risk Management' (Speech delivered at the New Zealand Law Society Taxation Conference, September 2006); D Shulman, 'Speech delivered at the National Association of Corporate Directors Governance Conference' (Washington, 19 October 2009, IRS News Release IR–220–95) <http://www.irs.gov/newsroom/article/0,,id=214451,00.html>; Ireland Revenue Authority, 'The Co-Operative Approach to Tax Compliance' (September 2005) <http://www.revenue.ie/en/business/running/large-businesses.html>; OECD Forum on Tax Administration, 'Seoul Declaration' (2006) <http://www.oecd.org/tax/taxadministration/37415572.pdf>; OECD Forum on Tax Administration, 'Good Corporate Governance: The Tax Dimension' (2006) <http://www.oecd.org/site/ctpfta/37207911.pdf>; OECD Forum on Taxation Information Note, 'General Administrative Principles: Corporate Governance and Tax Risk Management' (2009); s 93 and sch 46 to the *Finance Act 2009* (UK); Netherlands Tax and Customs Administration Co-ordination Group 2008, 'Tax Control Framework' (March 2008) <http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/vat_conferences/tax_control_framework_en.pdf>.

[4] M Carmody, 'Large Business and Tax Compliance — A Corporate Governance Issue' (Speech delivered at the Leaders' Luncheon, Sydney, 10 June 2003).

[5] Gilleard, Ibid; PriceWaterhouseCoopers (2013) Tax Transparency and country-by-country reporting- An Ever Changing Landscape http://www.pwc.com/en_GX/gx/tax/publications/assets/pwc_tax_transparency_and_country-by-country_reporting.pdf; Part 1A s3C *Taxation Administration Act 1953* (Cth) requires the ATO Commissioner to make public specific information relating to the tax affairs of all corporate tax entities that have a reported total income of $100 million or more.

very little or no tax in the country in which they have a substantial presence.[6] Increasingly corporate social responsibility and sustainability considerations impose a broader ethical obligation on company decision makers.[7]

What is an acceptable ethical position at any point in time reflects society's expectations (Doyle, Hughes and Glaister, 2008) and increasingly society expects a company to contribute an 'appropriate' amount to the tax revenue in countries where they have a presence.[8] As Doyle, Hughes and Glaister, note, an ethical approach is not just 'acting in a manner permitted by law' and goes 'beyond compliance with the law'. Interestingly ethical considerations were not identified as a key element of the tax risk management practices of large companies operating in Australia.[9] The recent focus on the tax contribution of large multinational companies worldwide, as well as tax transparency measures, may mean that compliance with the underlying tax policy may be the preferred approach of those firms concerned about reputational risk.

Whilst in the majority of large Australian companies the Chief Financial Officer ('CFO') and/or tax manager make the final decision on acceptable tax risk, a company code of ethics or professional ethical principles, are not typically applied in determining acceptable tax risk.[10] If a company code of code of ethics and professional ethical principles were a key consideration in tax decision making and tax risk management, it could be argued that a company's acceptable tax risk would be lower and something that governments, revenue authorities and professional bodies may want to facilitate/encourage to reduce aggressive tax decision making.

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[6] Christians, A. 'How Starbucks Lost its Social License – and Paid £20 million to Get it Back' *Tax Notes International* (2013) 71(7) 637; Taxand, 'Tax and Global Survey 2014 - Navigating tax priorities: substance, reputational risk and reform' http://www.taxand.com/sites/default/files/taxand/documents/Taxand%20Global%20Survey%202014.pdf.

[7] PricewaterhouseCoopers, 'Tax Strategy and Corporate Reputation – a Business Issue' (2013).

[8] Angela K Davis, David A Guenther, Linda K Krull and Brian M Williams, 'Taxes and Corporate Sustainability Reporting: Is Paying Taxes Viewed as Socially Responsible' (Working Paper, Lundquist College of Business, University of Oregon, Eugene 2013); [8] Edward Kleinbard, 'The Lessons of Stateless Income' (2011) 65 *Tax Law Review* 99; James Hutchinson, 'Apple's tax falls to $36m in Australia as sales hit $6bn' *Australian Financial Review* (31 January 2014) <http://www.afr.com/p/technology/apple_tax_falls_to_in_australia_dWUIatWLWUYWD8XKa1Ln7K>; Jane Wardell, 'G20 Agrees on Push to Close Tax Loopholes, Make Multinationals Pay' Reuters (23 February 2014) < http://in.reuters.com/article/2014/02/23/g20-australia-tax-idINDEEA1M05120140223>.

[9] Lavermicocca, C and McKerchar, M, 'The Impact of Managing Tax Risk on the Tax Compliance Behaviour of large Australian Companies' (2013) November *Australian Tax Forum* 707-723.

[10] Above n 9

Background

A company's income tax compliance behaviour reflects that company's position with respect to the level of, and approach to, tax aggressiveness and tax risk. A company whose preference is to take an aggressive or contentious tax position will typically demonstrate different income tax compliance behaviour than a company that takes a conservative approach to tax decision-making.[11] A company that invests in tax shelters or tax avoidance schemes demonstrates different income tax compliance behaviour to a company that does not consider that type of tax position acceptable.[12] Further, a company that always requires a private ruling from the Australian Taxation Office ('ATO') before making a decision in relation to a contentious tax transaction demonstrates different income tax compliance behaviour to a company that never seeks the ATO's opinion. In many instances it is a company's position along the tax planning behaviour spectrum, from aggressive to conservative that will determine whether a tax position taken will result in a failure to comply with the tax laws.[13]

Increasing pressure on governments to meet revenue demands places a focus on the effectiveness of the tax system. Governments, public policy advocates and the community generally considers tax avoidance arrangements, that result in the a company contributing less to the revenue than the 'spirit of tax law' requires, is inconsistent with government tax policy and on that basis is behaviour that needs to be understood and addressed.[14]

The need for large companies to have a tax risk management system[15], to meet reporting obligations, and to satisfy local revenue authorities that tax risk has been addressed, is evident in many countries including Australia.[16] International professional business advisory firms have targeted tax risk

[11] J Slemrod and S Yitzhaki, 'Tax Avoidance, Evasion, and Administration' in A J Auerbach and M Feldstein (eds), *Handbook of Public Economics* (Elsevier, 2002).
[12] Above n 9.
[13] Above n 9.
[14] Above n 9.
[15] The definition of a tax risk management system for the purposes of this research is having in place documented and operationalised systems and procedures to identify and manage tax risk.
[16] Above n 3

management as an area in which they can provide services to large business and have published a significant amount of material on the topic.[17]

The worldwide trend has been towards improved tax risk management, greater transparency in tax reporting and increased accountability of company decision-makers.[18] It is anticipated that these trends have had an impact on the tax departments within large companies. KPMG and Ernst and Young ('EY') have led the way in collecting information on tax decision making through international surveys of large companies.[19] Responses indicate that there is increasing pressure on tax departments to manage tax risk within a corporate governance framework. While globally the majority of a large company's tax department time is still spent on tax return compliance, tax risk management is an important part of large company's corporate governance practices.[20] Despite the fact that large companies indicate that tax risk management is an important aspect of risk management practices, this importance is not reflected in either the documented tax risk management procedures or in the amount of time tax departments devote to tax risk management.[21]

The ATO has advised large companies that do not have a comprehensive and documented tax risk management system that they will be considered a greater risk to the revenue and, as a result, will be subject to closer review. As part of good tax governance, the ATO has urged directors to be aware of the material tax positions relating to their company and to determine and approve a tax risk

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[17] Ernst and Young, 'Tax Risk Management: The Evolving Role of Tax Directors' (2004); Ernst and Young, 'Tax Risk: External Change, Internal Challenge, Global Tax Risk Survey' (2006) <http://www2.eycom.ch/publications/items/global_tax_risk_survey_2006/ey_global_tax_risk_survey_2006_e.pdf>.

[18] Lavermicocca, C. and Buchan, J., Role of reputational risk in tax decision making by large companies' eJournal of Tax Research (2015) Volume 13 (No 1) 5 50.

[19] Ernst and Young, 'Tax Risk Management: The Evolving Role of Tax Directors' (2004); Ernst and Young, 'Tax Risk: External Change, Internal Challenge, Global Tax Risk Survey' (2006) <http://www2.eycom.ch/publications/items/global_tax_risk_survey_2006/ey_global_tax_risk_survey_2006_e.pdf>; Ernst and Young, 'Tax Risk: External Change, Internal Challenge — The Australian Perspective, Global Tax Risk Survey' (2006–2007); 'Ernst and Young, Global Tax Risk Survey' (2008) <http://www.ey.com/GL/en/Services/Tax/Business-Tax/Tax-Accounting-and-Risk-Advisory/Tax_2008_Ernst-Young_tax_risk_survey>; Ernst and Young, 'Steady Course, Unchartered Waters — The Australian Perspective from the Third Ernst and Young Global Tax Risk Survey 2008'; KPMG, 'Tax Department Survey' (2005); KPMG, 'Tax Department Survey' (2006) <http://www.amr.kpmg.com/aci/docs/surveys/KPMG_Tax_Survey.pdf>; KPMG, 'The Rising Tide — Regulation and Stakeholder Pressure on Tax Departments Worldwide' (2006) <http://www.kpmg.com/Ca/en/WhatWeDo/SpecialInterests/Managing-Risk-Driving-Performance/Documents/Theper cent20Risingper cent20Tideper cent20-per cent20Regulationper cent20andper cent20stakeholderper cent20pressureper cent20onper cent20taxper cent20departmentsper cent20worldwide.pdf>; Henderson Global Investors, 'Tax, Risk and Corporate Governance' (2005) <http://www.henderson.com/content/sri/publications/reports/taxriskcorporategovernance.pdf>; Henderson Global Investors, 'Responsible Tax Report' (2005) <http://www.taxjustice.net/cms/upload/pdf/Global_Henderson_-_ResponsibleTax_-_OCT_2005.pdf>.

[20] 'Ernst and Young, Global Tax Risk Survey' (2008) <http://www.ey.com/GL/en/Services/Tax/Business-Tax/Tax-Accounting-and-Risk-Advisory/Tax_2008_Ernst-Young_tax_risk_survey>

[21] Above n 20.

management system and acceptable tax risk profile.[22] Other revenue authorities around the world have similarly identified the requirement to have in place a tax risk management system and have introduced measures whereby an individual or individuals are held accountable for tax decision-making in a large company.[23] Revenue authorities expect an improvement in income tax compliance and less aggressive tax practices by large companies as a consequence of the existence of a tax risk management system and the identification of directors as accountable for tax decision-making.

The categorisation of tax strategy and tax risk management as a corporate governance issue links tax compliance to directors' duties and may be effective in encouraging directors to take responsibility for a company's tax position. Directors are expected to establish a tax risk strategy and ensure compliance with that strategy through corporate governance practices and a failure to do so may not meet the standard of reasonable care that applies in s 180(1) of the *Corporations Act 2001* or similar provisions in company legislation in other jurisdictions.

An understanding of tax compliance behaviour of a large company requires a consideration of its tax risk profile, including the tax risk appetite and the extent to which a company is prepared to accept uncertainty in the tax position it adopts. Because tax legislation is complex and its application is at times unclear, a company may take a position where the ultimate tax treatment is uncertain.[24] The position a company adopts can range from conservative to aggressive. A company may comply with the literal words in the tax legislation but not its intended application. One tax expert may consider certain actions and decisions to comply with the income tax law while another may have a different

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22 ATO, 'Large Business and Tax Compliance Booklet' (2010) <http://www.ato.gov.au/content/downloads/bus33802nat8675072011.pdf>.

23 HMRC, 'HMRC Approach to Compliance Risk Management for Large Business' (March 2007) <http://www.hmrc.gov.uk/lbo/risk-update.pdf>; D Butler, 'Corporate Insolvency — Tax Risk Management' (Speech delivered at the New Zealand Law Society Taxation Conference, September 2006); D Shulman, 'Speech delivered at the National Association of Corporate Directors Governance Conference' (Washington, 19 October 2009, IRS News Release IR–220–95) <http://www.irs.gov/newsroom/article/0,,id=214451,00.html>; Ireland Revenue Authority, 'The Co-Operative Approach to Tax Compliance' (September 2005) <http://www.revenue.ie/en/business/running/large-businesses.html>; OECD Forum on Tax Administration, 'Seoul Declaration' (2006) <http://www.oecd.org/tax/taxadministration/37415572.pdf>; OECD Forum on Tax Administration, 'Good Corporate Governance: The Tax Dimension' (2006) <http://www.oecd.org/site/ctpfta/37207911.pdf>; OECD Forum on Taxation Information Note, 'General Administrative Principles: Corporate Governance and Tax Risk Management' (2009); s 93 and sch 46 to the *Finance Act 2009* (UK); Netherlands Tax and Customs Administration Co-ordination Group 2008, 'Tax Control Framework' (March 2008) <http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/vat_conferences/tax_control_framework_en.pdf>.

24 Tax compliance is defined as 'Taxpayer files all required income tax returns accurately and at the proper time, pays any outstanding taxes as they fall due and maintains all required records. The accuracy of the return and the records required are determined in accordance with the prevailing legislation (both tax and otherwise), rulings, return instructions and court decisions'; M McKerchar, *The Impact of Complexity Upon Compliance: A Study of Australian Personal Taxpayers* (Australian Tax Research Foundation, Research Study No 39, 2003), 34.

opinion. This conflict is seen in the degree to which the tax laws are the subject of litigation and dispute.[25]

A company code of ethics and professional ethical principles may be used to fill the void in application of the tax laws created by uncertainty and complexity and dictate where on the spectrum a company sits in terms of tax aggressiveness. A company ethics committee could oversee the ethical issues regularly and reporting would need to be transparent. Where professional accountants are involved in decisions concerning acceptable tax risk and the management of those risks, the ethical principle that require a professional accountant to act in the public interest should also be a relevant consideration.

The Code of Ethics for Professional Accountants in Australia, APES110 ('the Code') is the most relevant formalised code of ethics that may apply to a professional accountant making tax decisions as an employee or external adviser to a large Australian company.[26] A professional accountant, being a member of an accredited accounting body, including the Chartered Accountants Australia and New Zealand ('CAANZ'), CPA Australia, Association of Chartered Certified Accountants ('ACCA') or Institute of Public Accountants ('IPA') is required to comply with the Code. Whilst the Code was issued by the Accounting Professional and Ethical Standards Board (APESB), an independent body established by the professional accounting bodies in Australia, the Code is based on the Code of Ethics issued by the International Ethics Standards Board for Accountants ('IESBA') of the International Federation of Accountants ('IFAC'). Importantly the overarching responsibility of professional accountants, as set

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[25] J Freedman, 'Tax Risk Management and Corporate Taxpayers — International Tax Administration Developments' Chapter 4 in A Bakker and S Kloosterhof (eds), *Tax Risk Management: From Risk to Opportunity* (IBDF, 2010).

[26] APES110 Code of Ethics for Professional Accountants, issued by the Accounting Professional and Ethical Standards Board (APESB) is binding on members of CPA Australia and the Chartered Accountants in Australia and New Zealand. APES110 is principles based rather than rules based and identifies fundamental principles that a professional accountant must not compromise in carrying out their work. The fundamental principles identified in APES110 are:

- Integrity
- Objectivity
- Professional competence and due care
- Confidentiality
- Professional behaviour

APES220 'Taxation Services' also sets out standards for members in the provision of quality and ethical taxation services and arguably would impact on compliance behaviour where the tax position taken by a company involves decision-making by a member of the CPA Australia or the Institute of Chartered Accountants in Australia.

out in Section 100 of APES110, is the 'public interest' whilst also acting in the 'client's interest'. The responsibility of a professional accountant to act in the public interest, the professional accounting bodies argue, distinguishes the accountancy profession from other professions.[27]

In acting in the public interest, the Code states that professional accountants acting for their employer or client are also required to comply with the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour in advising their employer and/or their clients or both. In considering the public interest verses the employer/client interest a conflict arises where aggressive tax strategies that comply with the letter of the law rather than the spirit of the law, are in accordance with the obligation to act in the employer/client interest but not the public's interest.[28]

The various professional accounting bodies self-regulate their members conduct, undertaking their own disciplinary proceedings however recent pressure has been placed on the professional accounting bodies to enforce a higher standard of ethical conduct and provide more guidance on the application of the 'public interest' criteria.[29] Corporate failures, aggressive tax arrangements and international profit shifting by multinational companies including the accounting profession that advise with respect to these activities (Hasseldine, Holland and Van der Rijt, 2012) have been the focus of media attention and criticism.

Registered tax agents in Australia must also comply with the Code of Professional Conduct ('Tax Agent Code') as set out in Part 3, Div 30 of the *Tax Agents Services Act 2009* (Cth). The Tax Agent Code sets out the professional and ethical standards required of registered tax agents including the core

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[27] Shah, A, K. 'Public duty, private gain: professional ethics and tax' (2014) *Third Quarter* 9 (3) 4; APES110; IFAC policy position 5 June 2012 provides a definition of the public interest as 'The net benefits derived for, and procedural rigor employed on behalf of, all society in relation to any action, decision or policy'. 'Public ' in IFAC 5 'includes the widest possible scope of society' specifically investors, shareholders, business owners, consumers, suppliers, taxpayers, electorates and citizens.

[28] Goodall, A 'Analysis: PAC reignites tax 'code of conduct' debate' AccountanyAge 24 February 2015; Kaffash, J. 'Losing their moral compass: Should accountants uphold the public interest? AccountanyAge 24 February 2015; Steen, M. 'Ethical tax systems in a global economy' Markkula Centre for Applied Ethics Santa Clara University, November 2014; Institute of Business Ethics, 'Tax avoidance as an ethical issue for business' Business Ethics Briefing, Issue 31, April 2013.

[29] Walker, B. 'Do accountants act in the public interest' The Conversation 6 January 2012; Longstaff, S. 'What can accounting offer improved ethics' St James Ethics Centre – The Ethics Centre, 1 February 1995.

obligations of honesty and integrity, independence, confidentiality, competence and other responsibilities. Other responsibilities include the requirement that a registered tax agent must not knowingly obstruct the proper administration of the taxation laws. A tax decision-maker within a company or advising a company, who is a registered tax agent, is bound by these core principles that do not incorporate an obligation to the public.

The effectiveness of codes of professional ethics in guiding decision-making, focusing on auditors, has been the subject of some research in the US and Canada (Ponemon and Gabhert, 1993). This research indicates that an auditor's ethical judgment is most influenced by rule-based reasoning that focuses on compliance with standards. The application of ethics is generally limited to 'conventional moral reasoning' which suggests that any code of ethics for professional accountants will have limited impact on key tax decision-makers unless they are reflected as specific rules and requirements (Flanagan, 2006).

Professional accountants employed by a company have a legal obligation to act in the best interests of the employer company and if there is a potential tax saving available to the company, that complies with the tax legislation but is inconsistent with the legislative intention then it could be argued that the professional accountant has an legal obligation to take advantage of that potential tax saving.[30] The company goal of profit maximisation has seen aggressive tax planning arrangements proliferate whilst the public interest considerations take second place. [31]

Whilst professional accountants have a responsibility to uphold the law and to act in the best interests of the client/employer, where the application of the law is uncertain or subject to dispute, the public interest may dictate acting in accordance with the spirit of the law rather than a technical interpretation that would allow a client/employer to reduce tax payable (Myers (1990), Newberry, Reckers and Wyndelts (1993), Marshall, Armstrong and Smith (1998) and Cruz, Shafer and Strawser

[30] Sections 180 and 181 *Corporation Act 2001*
[31] Above n 28; Sikka, P, 'Smoke and Mirrors: Corporate Social Responsibility and Tax Avoidance' (2010) 34 Accounting Forum 153.

(2000)). Arjoon (2005) points out that legal compliance mechanisms are often insufficient and may not address the real and fundamental issues that inspire ethical behaviour.[32]

Law and ethics are a balancing act and to date, in the area of tax law, the focus has been on a client-centred approach where tax payable is minimised. Increasingly however we see media and lobby groups demonstrating moral activism in the area of tax ethics and companies judged on their tax contributions (Sikka and Hampton, 2005). Companies subject to reputational risk are forced to consider the law and their ethical position in making tax decisions. Tax advisors can at times face a conflict in satisfying professional codes, personal codes and also being financially successful in their profession (Sukurai and Braithwaite, 2001). A company code of ethics relating to tax decision making could assist in addressing these conflicts. What is ethical conduct for a particular company could be based on the underlying theoretical framework a company choses to adopt and explicitly stated in a company code of ethics.[33]

The positivist view that there is only one correct interpretation of the tax laws is not demonstrated in the many conflicts and appeals in the courts in Australia that relate to the tax laws. There is however little evidence of any overt consideration of ethical issues in tax decisions by judges and the ATO (Dabner and Burton, 2010). Dabner and Burton (2010) highlight 'tax ethics needs to be incorporated in the practice of tax law to ensure the goals and objects of the client are met' (p.775).[34] Ethics in tax decision making requires the consideration of not just the tax laws but the relevant individual and organisation's ethical position. It is important in managing tax risk that a company is upfront about its position in relation to tax ethics (Dabner and Burton, 2010). An ethical company is one where ethical conduct is promoted by the directors, managers, accountants, the systems and procedures and the reward system.[35]

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[32] Arjoon, S, 'Corporate Governance: An Ethical Perspective' (2005) 61 Journal of Business Ethics 343.
[33] A code of ethics may draw on one or more ethical theory including utilitarianism, deonotology, Confucianism etc.
[34] Dabner, J and M Burton, 'Weaving the Ethical Tapestry in these Changing Times- Contemporary Australian Discourses regarding the Ethical Obligations of Australian Tax Practitioners' (2010) UNSW Law Journal 33(3) 745.
[35] Preuss, L, 'Tax Avoidance and corporate social responsibility: you can't do both, or can you?' (2010) 10(4) Corporate Governance 365; Sikka, P, 'Smoke and Mirrors: Corporate Social Responsibility and Tax Avoidance' (2010) 34 Accounting Forum 153.

Not only is tax aggressive decision making an ethical issue for individual professional accountants in their role as a tax advisors and decision makers but also for the board of directors in establishing good governance practice and the appropriate tax risk appetite. One approach may be to develop and apply a tax risk management system that reflects a company's broad ethical principles ensuring that whilst the risk management process is important it requires the application of underlying ethical principles. Recent discussion concerning aggressive tax arrangements highlight that businesses have a choice about their approach to interpreting the tax law and as a result the amount of tax they pay. The tax laws are inherently complex and at times give rise to 'grey areas' of interpretation and an ethical position relating to the interpretation of the laws would require a company to adopt a conservative low risk position. Good tax governance would require a company to address tax as an issue or commitment in a company code of ethics.[36]

Research into business ethics indicates that the attitude of company managers toward company ethics will affect ethical decision-making processes within the company (Singhapakdi, Karande, Rao and Vitell, 2001). Shafer and Simmons (2008) surveyed tax professionals in both public accounting and private industry in Hong Kong and their responses support the view that tax professionals' attitudes toward ethics impact on their decision-making.[37] Shafer and Simmons (2008) conclude that tax professionals who place little importance on ethical and socially responsible conduct are more likely to facilitate aggressive corporate tax avoidance schemes.

Shafer and Simmons (2008) also look at a certain personality trait, which they refer to as 'machiavellianism' and its impact on attitudes of tax professionals to corporate ethics and social responsibility. 'Machiavellianism' for the purposes of the Shafer and Simmons (2008) research refers to a person who is manipulative, cold and calculating. Results of their research indicate that 'machiavellianism' has both a direct and indirect effect on a tax professional's ethical decisions. The

[36] Institute of Business Ethics, 'Tax avoidance as an ethical issue for business' Business Ethics Briefing, Issue 31, April 2013.
[37] Matten, D. 'Social Responsibility more than a business add-on' The Drum, Opinion 18 February 2014.

more pronounced a tax professional's manipulative, cold and calculating qualities the more likely the tax professional would judge an aggressive company tax avoidance scheme favourably.

While the individual personality traits of a company's managers are relevant to an understanding of large company tax compliance, the risk to the company in terms of its stance on ethics needs to be identified and dealt with. Where company goals include ethical conduct in relation to tax compliance, clearly stated procedures and practices must be enforced by the company to minimise the impact of inconsistent individual ethical preferences.

Listed companies in Australia are required to act ethically and responsibly and that would ideally include a company code of ethics setting out core values that address acceptable tax risk. Specifically the Australian Share Exchange ('ASX') Corporate Governance Council, Corporate Governance Principle 3 recommends that Australian listed entities 'act ethically and responsibly'. The commentary to Principle 3 says that 'ethically and responsibly' is more than just compliance with legal obligations and includes 'being, and being seen to be, a 'good corporate citizen''. In addition Principle 3 requires that a listed company's core values must appear in a company code of conduct that it is applied across the organisation's decision making.

Figure 1 and 2 detail the individuals within respondent companies that are involved and ultimately make the final decision on the acceptable level of tax risk and indicate that the CFO and the tax manager are the most involved in the determination of acceptable tax risk and that the board of directors, the CEO and company group policy also have a significant role. The CFO is involved in the determination of the acceptable level of tax risk to at least some extent in 98.3 per cent of respondent companies. The CFO has a key role in determining the level of tax risk that will be tolerated and many are members of professional accounting bodies that require compliance with a high standard of ethical conduct including a consideration of the 'public interest'.

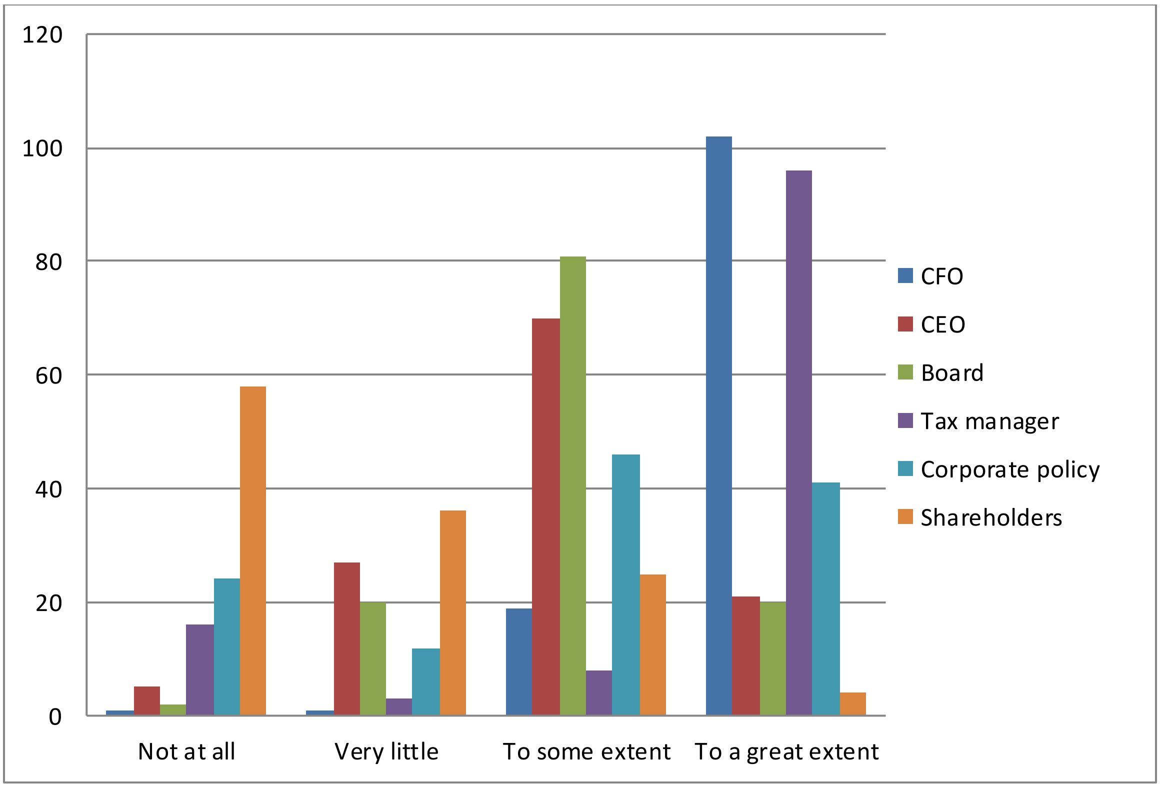

Figure 1 Individuals Involved in Determination of Acceptable Tax Risk

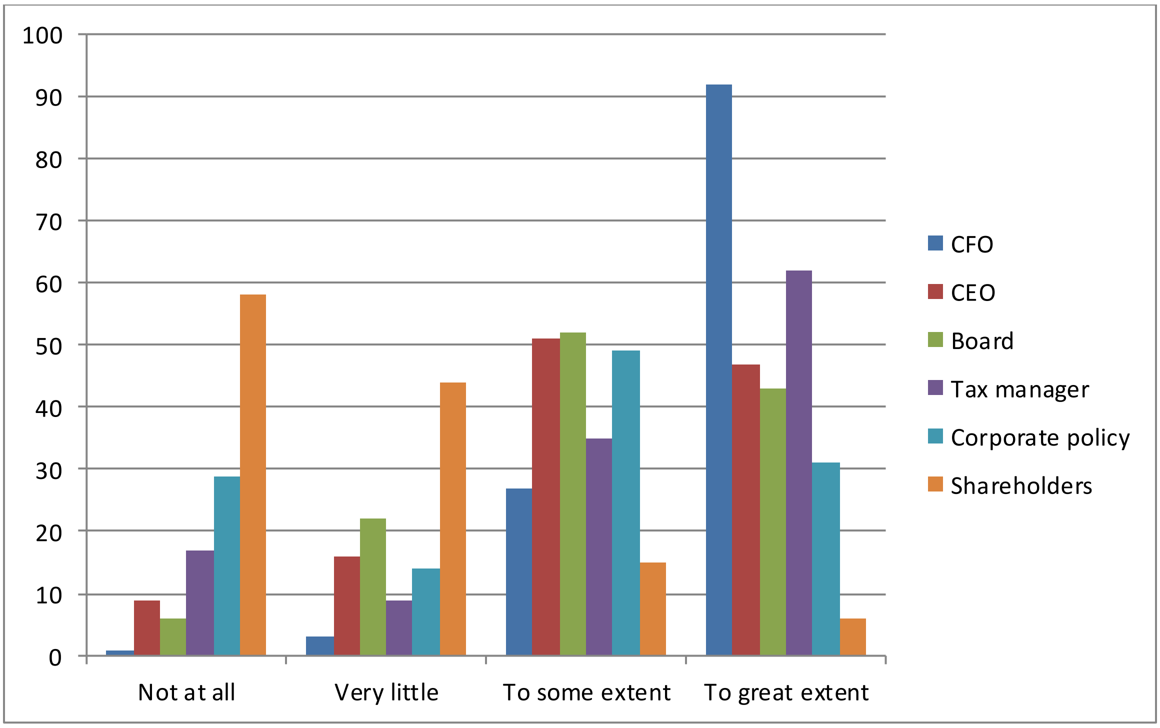

Figure 2 Individual who makes the Final Determination of Acceptable Tax Risk

The shareholders were identified in only a few instances as having a significant role and the majority of respondents felt that the shareholders have very little or no involvement in the determination of acceptable tax risk. The results in relation to shareholders suggest that despite the increasing discussion and identification of corporate social responsibility as a shareholder concern, few large companies consider their shareholders' views or preferences in relation to tax aggressiveness and ultimately tax compliance.

The commentary to Principle 3 says that 'ethically and responsibly' is more than just compliance with legal obligations and includes 'being, and being seen to be, a 'good corporate citizen''. It is important to note here that what constitutes a 'good corporate citizen' will vary depending on the underlying moral philosophy considered relevant in the jurisdiction, in this case Australia. Moral philosophies including utilitarianism, deontology, confucianism each apply a different basis to determine right or wrong and the degree of application of these approaches to business ethics also needs to be recognised. The approach to tax risk management that a company takes may, to some extent, reflect a variety of overarching moral philosophies and the regulator/courts may take a different view

Whilst the board of directors do have the overriding obligation to set the tax risk appetite and ethical position in relation to tax compliance a recent survey found that Australian's rate board chairs, foreign company directors, chief executives and senior executives are unethical on balance.[38] Responses also rate tax avoidance as the second biggest ethical issue for businesses after corruption. As senior company decision makers act as gatekeepers they are so crucial in setting the 'tone at the top' and it appears there is work to be done in embedding ethics and ensuring it flows through the organisation. Tax ethics is part of that mix.

[38] Ethics Index 2016, Governance Institute of Australia July 2016

A recent six country survey of banking and financial industry practitioners indicates that 'company policies and legal requirements are the most influential factors driving ethical decisions'.[39] Decision makers need a clear set of guiding values and principles to ensure principled reasoning so that 'ethical' and 'legal' are clearly defined by the board, typically included in a code of conduct, with examples provided and demonstrated at all levels of the organisation.[40] A review of tax strategy statements by large Australian companies set out at Appendix One indicates that the focus in tax risk management and tax strategy generally is on 'legal' compliance with the tax law as opposed to 'ethical' compliance.

Conclusions

The recent inquiry into corporate tax avoidance by the Senate Economics References Committee in Australia[41] and media reporting of low effective tax rates paid by high profile companies reveal aggressive tax arrangements have the potential to damage a company's reputation.[42] Greater and broader disclosure of a company's tax contribution can reduce the financial benefits to a company of aggressive tax arrangements (due to reputational damage) and encourage improved alignment between the public interest and the company's best interest. Of some concern is that companies that are not exposed to reputational risk (low public profile), will not be subject to the same pressures from the community on their tax decision making as companies that are required to disclose their tax contribution and have a high public profile.

The pressure on large companies to contribute to tax revenue, not just to comply with the technical detail of the tax laws, means that tax decision makers and tax reports need to 'tell a story' about the company's tax contribution so as to convince relevant stakeholders that the company is paying its 'fair

[39] CAANZ 'A Question of Ethics- Navigating Ethical Failure in the Banking and Financial Services Sector' Chartered Accountants Australia and New Zealand August 2016.
[40] Above n 38.
[41] 2 October 2014 the Senate referred an inquiry into corporate tax avoidance to the Senate Economics References Committee for inquiry and report.
[42] Edward Kleinbard, 'The Lessons of Stateless Income' (2011) 65 Tax Law Review 99; James Hutchinson, 'Apple's tax falls to $36m in Australia as sales hit $6bn' Australian Financial Review (31 January 2014) <http://www.afr.com/p/technology/apple_tax_falls_to_in_australia_dWUIatWLWUYWD8XKa1Ln7K>; Jane Wardell, 'G20 Agrees on Push to Close Tax Loopholes, Make Multinationals Pay' Reuters (23 February 2014) < http://in.reuters.com/article/2014/02/23/g20-australia-tax-idINDEEA1M05120140223>.

share of tax'. It is no longer enough for the tax function to ensure compliance with the tax laws but instead companies are expected to take an ethical position. What that ethical position is will be informed by regulatory provisions, shareholders, directors, tax decision makers, professional accounting bodies, consumers and any other stakeholders whose view of the company's tax contribution would impact on their relationship with the company.

The tax risk management system could be used to protect a company's reputation by facilitating an ethical approach to tax decision making and a lower level of acceptable tax risk. In fact the tax risk management system could be used to build a company's tax reputation by ensuring that the tax contribution is detailed and explained to a broad range of users of that information. Ultimately in encouraging large companies to disclose the detail of their tax contribution and ethical position with respect to tax, the tax risk management system would facilitate informed decision making, not just by decision makers within the organisation but also decision makers external to the organisation. Reputational benefits of a company's tax contribution could be exploited to win community acceptance and support (Morse, 2012). In addition the link between ethical performance, financial performance and financial reporting quality would also be used to support a company code of ethics that is applied in substance across the organisation (Elayan, Li, Liu, Meyer and Felon, 2013).

Ethics was not identified, in survey responses of large Australian companies, as playing a role in tax risk management systems.[43] Whilst a tax risk management system allows the company decision makers to better match company objectives with ultimate tax outcomes it appears from the results that large companies in Australia, operating in a variety of industries, are not guided by a particular ethical position embodied in the acceptable tax risk profile adopted. This research identifies that complexity and uncertainty in the tax laws limit the effectiveness of a tax risk management system and suggests that a company position on ethics in managing tax risk could be used to guide tax decision makers in dealing with uncertainty and complexity.

[43] Above n 9.

In a survey of large Australian companies, the CFO and tax manager are most involved in the determination of acceptable tax risk[44]. Although the Code would apply to professional accountants employed as the CFO and/or tax manager, and should guide their decision on the acceptable tax risk spectrum no respondent identified ethical issues as a guiding factor in determination of the acceptable tax risk profile. The professional accounting bodies do provide guidance and direction to its members in relation to ethical decision making and yet further guidance is required in relation to how ethics would apply to their members in making decisions about aggressive tax arrangements.

The ethical principles, determined by a company itself or a professional body, do not currently have a significant role in the management of tax risks. A company's position on ethics as well as the ethical position of the professional bodies should be a key element in a comprehensive tax risk management system to ensure that the tax decisions made recognise the company goals are balanced as against the public interest. Increased tax transparency requirements in Australia, and around the world, demand a consideration of ethical principles in the identification and management of tax risk.

[44] Above n 9.

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