How tax can emerge as a trust center in the wake of Covid-19

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The view

The COVID-19 pandemic has been an undeniably difficult time for governments, businesses, non-profits and news media that were already struggling with declining levels of trust among citizens, consumers, clients and audiences.

Crises always test leaders, and leaders who respond with fortitude, agility and compassion will ultimately see their organizations through this crisis and position them for future success. They will have the opportunity to win back confidence and close the widening trust gap. This is particularly true for businesses that listen to the ideas of younger employees who care deeply about environmental, social and governance (ESG) issues.

Defining the trust gap

The trust gap is very real. Despite a mostly strong global economy for two decades, businesses, NGOs and the media are not enjoying the high levels of trust that typically accompany an economic expansion, according to the 2020 Edelman Trust Barometer. Somewhat more unsettling is that the survey, with its January release, predates the pandemic and more recent social unrest. Trust in key organizations has the potential to be another calamity of 2020.

The trust gap also affects how employees view their own organizations. The EY Global Integrity Report 2020 shows that, even before the pandemic, 53% of junior employees weren't very confident that their management abided by relevant laws, codes of conduct or industry regulations. This is perhaps unsurprising when you consider that 14% of board directors admitted they would be willing to mislead external parties such as regulators.

Increased focus on ESG

But every crisis has seeds of opportunity – rebounding to a "new normal" might be an ideal window to define and create a better normal. Even before COVID-19, positive social changes were beginning to take shape, led in part by younger generations. Global climate change protests, for instance, galvanized millennials and Generation Z (among others), and employers have begun to incorporate these concerns into company values and purpose.

Generation Z values diversity and fairness and is "deeply socially aware", according to Forbes. Millennials, meanwhile, "value social issues over institutions; like using their collective voice and supporting others and the greater good," according to the Millennial Impact Report. These two groups will increasingly dominate workforces, making investment decisions and leading organizations.

But businesses cannot wait until the supporters make it to the C-suite. Companies should continue to take cues from the youngest members of their workforce and act now, starting with paying attention to ESG issues.

In terms of the environment, steps include:

- Reducing the amount of energy a business consumes: In the wake of the pandemic, air pollution has fallen due to declines in flights and automobile traffic and reductions in manufacturing. This has stirred many to consider how they can conduct their businesses in more sustainable ways.
- Purchasing as much renewable electricity as possible and offsetting what can't be reduced: Whether that's from essential travel or for countries where it is not currently possible for an organization to purchase renewable electricity.

A focus on sustainability also means focusing on people. The need for businesses to put their people's well-being front and center has become clear during the pandemic. Regular, open two-way communication with employees is also crucial. Businesses will need to retain this people-centric approach as the workplace evolves, with more being done virtually and people having more say over where and when they work. Virtual working models will also help boost diversity and inclusion by expanding the talent pool. This will provide new opportunities for people of all backgrounds, including those who find the physical workplace inaccessible.

In terms of governance, a proposal released by the World Economic Forum (WEF) in January 2020 created 22 core metrics – now updated to 21 core and 34 expanded metrics and disclosures – that companies should consider in ESG reporting across industries and across the globe. Directors and CEOs must understand that ESG is now a mainstream business practice. It's being measured; it has to be overseen; and it's crucial to trust. Organizations will need to think about how ESG metrics are operationalized and disclosed, and make certain they are meaningful across corporate strategy, risk oversight and board engagement.

The WEF work, which includes contributions from EY, aligns with conversations the EY Center for Board Matters had with 60 institutional investors representing US$35 trillion in assets under management. When asked which factors are most critical to the strategic success of a portfolio company over the next three to five years, their most common responses were environmental issues, climate change, corporate culture, talent management, board composition and diversity.

The EY Global Integrity Report 2020 reinforces this message that operating with corporate integrity can deliver major benefits for organizations. Respondents cited strengthening reputation (50%), attracting new customers (41%) and retaining talent (40%) as key benefits.

Where does tax fit in?

Trust in a business is closely linked with its actions as a taxpayer. Companies that are perceived as less than transparent about their tax strategies and reporting are more likely to struggle with trust deficits.

Looking at tax through a COVID-19 lens, US$27 trillion has been spent globally by governments – via more than 2,700 new provisions – to provide support and stimulus to ease the economic pain of shutdowns and quarantines. Tax leaders are overwhelmed with the complexity of this new fabric of relief measures, many of which operate through the tax code.

Thus, tax professionals will have an important role in making sure their organizations commit to doing the right thing. With the tax code changes, the tax profession is going to be in the spotlight like never before.

The tax function was seen as a cost center in the early 1980s. By the 1990s, some saw it as a value center, which triggered public backlash. This set the stage for the early 2000s, when the tax function became a risk management center.

Now, with the pandemic as a backdrop, tax has the opportunity to emerge as a trust center. The tax function is more tied to business unit leaders than ever before. It is imperative that it is a trusted member of the C-suite.

Summary

Relief measures and tax code changes can help the tax function close the trust gap when paired with a focus on ESG issues. ■

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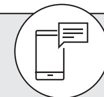

TAX ALERT!

Ghana publishes Transfer Pricing Regulations 2020

Executive summary

Ghana's Minister of Finance1 submitted new Transfer Pricing Regulations (new Regulations) before Parliament on 10 August 2020. In accordance with Article 11(7) of the Constitution of the Republic of Ghana, 1992, the new Regulations2 matured after 21 sitting days for Parliament. Thus, the new Regulations – which also repealed the Transfer Pricing Regulations, 2012 (L.I. 2188) (old Regulations) – entered into force on 2 November 2020.

The new Regulations incorporate many of the revisions introduced by the July 2017 edition of the Organisation for Economic Co-operation and Development (OECD)'s Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines), but with significant variations in certain cases.

The 19 paragraphs and two schedules of the new Regulations introduce significant changes in the compliance obligations for affected taxpayers as compared to the 10 paragraphs of the old Regulations.

This Alert summarizes the key provisions of the new Regulations.

Detailed discussion

Application

The new Regulations apply to "arrangements" between "persons who are (regarded as being) in a controlled relationship under...the Act3 and any other tax law."

Demonstrating arm's-length considerations

Allocation of risk: The definition of what constitutes an arm's-length transaction has not changed in accordance with the long-established global practice. In line with the new guidance in the OECD Guidelines, however, the new Regulations now specifically require the consideration of the allocation of the economically significant risks in determining the comparability of transactions. Assumption of risk, performance of mitigation functions and financial capacity to bear risk are explicitly required to be considered in determining transfer prices.

Aggregation of transactions: Recognizing the ways of modern business, the new Regulations explicitly permit the aggregation of "two or more controlled arrangements that are economically

closely linked with one another or that form a continuum such that they cannot reliably be analysed separately."

This is a positive development that should both make compliance more certain for impacted businesses and also make compliance more cost effective.

Intangible property: While the old Regulations provided for transactions involving intangible property, the new Regulations enhance the factors that should be taken into account in determining whether the transactions comply with the arm's-length standard, including the so-called DEMPE factors – the arrangements regarding the Development, Enhancement, Maintenance, Protection and Exploitation of the intangible asset.

Financing transactions: One new Regulation is dedicated to financing transactions. It contains specific provisions guiding what factors need to be considered in determining an arm's-length price for a financing transaction.

Among these, it is interesting to highlight that the new Regulation requires interest to be charged on related party trade payables which remain unpaid for 12 months.

Business restructuring: The new Regulations cover business restructurings. The objective is to ensure that, in any transfer of functions, rights, interests, assets and risks between persons in a controlled relationship, the amount received for the transfer reflected the amount an independent person in comparable circumstances would pay.

Documentation

Ghana's new Regulations, a sequel of the OECD Guidelines, now define the "Documentation" to be maintained as

(a) Master File and (b) Local File, and they are required to be maintained contemporaneously. This is a change from the requirement under the old Regulations to maintain only the "Local File" as documentation.

"Contemporaneous documentation" is defined as documentation which "...exists or is brought into existence at the time the person is developing or implementing any arrangement that might raise transfer pricing issues."

Safe Harbors

Taxpayers who are parties to a controlled arrangement with a value of up to US$200,000 are automatically exempted from the requirement to maintain contemporaneous documentation.

Additionally, taxpayers involved in low value-adding intra-group services which satisfy the Commissioner

General's (CG) set criteria may, by written notice to the CG, elect to be exempted from the requirement to maintain contemporaneous transfer pricing documentation.

The third safe harbor for documentation purposes is available by election to persons involved in controlled arrangements pursuant to a technology transfer agreement (TTA) which:

a. Is registered with the Ghana Investment Promotion Centre (GIPC); and
b. For which the applicable charges are less than or equal to 2% of net profit.

Mandatory disclosure filings: Similar to the old Regulations, the new Regulations require affected taxpayers to submit an annual transfer pricing return no later than four months after the end of each basis period.

However, the new Regulations also require the documentation to be filed with the tax authority no later than four months after the end of each basis period. This is a significant change from the old Regulations which only required submission of the documentation upon request by the CG.

Similarly, the filing of a Country-by-Country (CbC) report is a new compliance requirement introduced by the new Regulations. This requirement will, however, only apply to multinational enterprise groups with annual consolidated group revenues of 2.9b Ghana cedis or above in the fiscal year immediately preceding the Reporting Fiscal Year. On 2 November 2020, when the new Regulations entered into force, the threshold amount was approximately equivalent to €420 million, significantly below the €750 million that is recommended by the OECD Guidelines.

Recharacterization of debt financing as equity financing: The Minister has provided guidance on the factors that the CG should consider in recharacterizing a debt financing as equity financing as he is authorized to do under section 31(5)(a) of the ITA 2015. This will, generally, be triggered during an audit.

No Advance Pricing Agreements (APAs)

The new Regulations, like the old Regulations, do not contain provisions on APAs. Private rulings, therefore, remain

the only available route for entities requiring certainty for particularly sensitive or high value related party transactions.

Drafting error: It is important to note a drafting error in the new Regulations. Regulation 13(1) inadvertently refers to the "requirements of sub-regulation (6)" instead of sub-regulation (7) which contains the requirements for a CbC report. It is anticipated that the Treasury will address this soon.

Implications

The new Regulations introduce significant changes in the compliance obligations for taxpayers. Affected taxpayers should review their transfer pricing compliance procedures to ensure that they can demonstrate the requisite arm-length considerations and meet their documentation obligations.