

CFO'S ROLE IN TAX COMPLIANCE IN THE BUSINESS ENVIRONMENT

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1.0. Abstract

Taxation is a major source of revenue for most Governments of the world. It provides the needed resources for government developmental projects at local, state and federal levels. The importance of taxation is well acknowledged globally as a vehicle for economic development and transformation. Considering the importance of taxation, non-compliance is usually treated as a great offence in most nations of the world. The compliance level in developed economies has been very high while compliance level in developing countries is generally poor. Hence, there is need for the CFOs to drive compliance in their firms.

The Chief Financial Officer (CFO) is a top executive responsible primarily for financial reporting of his firm. The financial report prepared by the CFO reveals the financial position and performance of the enterprise. It shows the financial health status of the firm and serves as a basis for key management decisions. Other stakeholders such as shareholders, bankers/lenders, government, public, employees, customers and suppliers, e.t.c all rely on the financial statement presented by the CFO for their decision making. For example, the government uses the financial report as a starting point in the process of determining corporation tax to be paid by the firm. The financial statement being the final output from the CFO must comply with the relevant standards and statutory requirements, including appropriate provisions for tax and other statutory deductions.

2.0. Introduction:

The business environment across sectors and human endeavours is beset with risk of varied proportions and nature all the time. These range from risk of an operating nature to financial, transactional or systemic risk to mention but a few. These risks contribute, by no small measure, in shaping or reinforcing the performance of the business or organisation over time and this is also why Managers of resources must continue to pay attention to those risk pools that directly or

otherwise affect their bottom-line leading to profound sub-optimal utilisation of resources and poor returns on shareholders' fund.

There is an established link between government tax revenue and economic development. A country with low tax revenue profile will be lacking necessary funds needed for economic development and transformation. Therefore all responsible corporate citizens would seek to ensure compliance with tax laws. Most developmental projects in developed countries have been attributed to proper utilization of tax revenue. The nation will remain under developed, if it lacks financial resources to provide basic infrastructures, health care services, quality education and services to the rural areas. We should not expect good roads, good healthcare system, stable power supply, well-funded educational system devoid of ASUU's strike, rural transformation etc if the level of tax compliance remains low in the country.

So also in today's business world, one of the areas where a firm can suffer consequential financial haemorrhage is from lack of proper planning and inadequate provisions for tax liability of the firm or business. The firm/business, as a taxpayer, owes itself an obligation to pay only what is required of it as tax and nothing more under the tax laws. Tax planning and compliance strategies need to be evolved in ensuring that this happens.

2.0. Meeting the Chief Financial Officer

As other paper presenters here may have noted, the Chief Financial Officer of a firm is saddled with lots of activities of both financial and non-financial nature as well as identifying risks as they impact on activities necessary for the delivery of broad goals and targets through the adoption of appropriate measures to meet the challenges in today's business world. As the demands on the finance functions continue to expand, he must maintain a delicate balance between collaborating closely with individual business units and simultaneously ensuring that there is no over centralisation. In order to appreciate this further, it is pertinent, at this juncture to understand the place of the Chief Financial Officer and his relevance in the business environment.

3.0. Redefining the Position of a CFO

As mentioned earlier, the traditional role of the CFO is the preparation of financial statements. As a financial manager, the CFO makes some critically important decisions such as investment decisions, financing decisions, dividend and operating decisions. Other functions of the CFO will include ensuring regulatory /statutory compliance. Thus one important function of the CFO is ensuring that the financial reports prepared by him have fully complied with all statutory

requirements and regulatory standards as well as ensuring that appropriate amount of tax has been provided for in the financial statements. The CFO ensures that the right amount of tax is deducted and timely remitted to the relevant tax authority. The modern day CFO is not just responsible for financial reporting but also engages in key decisions on projects, funding, cash flows, taxes, regulatory and statutory compliance. He plays significant role in ensuring that his firm is in compliance with all relevant tax laws. Depending on the size of the organization and the structure used, the CFO may be solely responsible for tax matters. Bigger organizations may have the office of a tax manager who drives tax compliance. Other firms may engage the services of tax consultants to help them plan, monitor and ensure tax compliance. Whichever approach is used, the CFO plays a key role in the entire process of tax compliance.

4.0. Role of CFO in Tax Compliance

It is the duty of the CFO to ensure that his firm/business/company voluntarily discharges its tax obligations by subjecting its profits, businesses and assets or expenditure to the demands of the tax laws. A situation where a tax assessment is received and paid by the company without taking account of allowances and reliefs that can bring about lower tax liabilities does not augur well for such a company and its performance.

Studies reveal that all operational activities and decisions made by managers carry their own risks and uncertainties thereby contributing to a firm's overall risks, one of which is Tax Risk. The discourse regarding Tax Risk as an essential part of corporate governance has become so germane in organisations of today that the question now is how an issue that might encourage a corporate reorganisation or influence the payment of dividends to shareholders, or which might affect a merger or take-over could possibly stay out of the board room. Examples that are so fresh in memory are those of Enron and WorldCom with their weak governance system. In days of old, the mantra of "the lower the tax charge the better" as a simple rule is no longer sustainable today. Rather, stakeholders are in demand for sufficient long term information on how tax risks are being controlled through an effective tax risk management system implementation and corporate conduct supervision.

In the words of Will Egin, CFO of IEM and RTP CFO Forum Board Member, failure to properly identify and comply with the tax laws across states over which a business has 'Nexus' opens doors for fines and penalties just as it negatively impacts on the firm's eligibility for government contracts or grants. This is more so telling when unliquidated liabilities come with penalties and interest from revenue authority against the firm.

In addition, regulatory and accounting standards, as well as tax regimes, are changing rapidly, putting pressure on finance to collect timely and accurate information from the business units for control and compliance purposes. The upshot is that the links between all of these groups are tightening and in some cases, this has led managements to bring tax and internal audit inside finance.

The need to ensure compliance with all tax regulations is more real today than in previous years. In the United States, the finance function now focuses intensively on compliance! Tax and audit in many U.S. companies since the 2002 passage of the Sarbanes-Oxley Act governing public-company reporting. Stricter enforcement of the Foreign Corrupt Practices Act is also another regulation of note. Basel III, the latest version of the global capital adequacy and liquidity standards negotiated following the 2008 market crash, creates new compliance responsibilities for financial institutions. In the United States, financial firms also await a series of new regulations pursuant to the Dodd-Frank Act.

Non-compliance with extant tax laws exposes the firm to a risk of financial loss, in the form of penalty charges, interest e.t.c. Non-compliance also paints a picture of an irresponsible corporate citizen and leads to loss of goodwill. The consequences of non-compliance are so great that no good CFO would want to ignore it. Ensuring compliance will entail:

- ❖ Ensuring timely rendition of tax returns
- ❖ Self-Assessment
- ❖ Tax provisioning
- ❖ Accurate deduction of relevant taxes e.g withholding tax, PAYE and VAT
- ❖ Timely payment of tax deducted e.g VAT, WHT and PAYE
- ❖ Ensuring timely resolutions of all tax disputes
- ❖ Liaison with relevant tax authority on tax issues
- ❖ Responding timely to tax queries
- ❖ Ensuring the firms comply timely with new tax regulations

For example, the Transfer Pricing and Self-Assessment Regulations which had been introduced will pose great challenges for unprepared CFOs and that could lead their firms to a path of danger resulting from additional tax liabilities. All CFOs are expected to initiate a process of Transfer Pricing documentation so as not to be caught unawares. The first Transfer Pricing filing will be due by this current year 2014. CFOs should look into their firms' financial transactions and identify areas of related party transactions that may be subject of Transfer Pricing adjustments.

All existing and new tax regulations must be factored into transactions and financial reporting processes to ensure compliance as well as ensure that their firms are not made to pay excessive taxes.

In recent reports also, it is said that non-compliance with the host of new regulations covering all aspects of financial services has become a serious risk for firms. The price of getting compliance wrong is getting larger as headline-grabbing fines in both the United States and UK recently have demonstrated. Surely firms want to avoid being hit with fines such as the ones handed to the likes of Coutts, Credit Suisse, and Greenlight Capital. One way to manage that is to treat compliance issues as a risk category just like credit or market risk, for example. Risk officers need to understand the risk of non-compliance and assess their firms' performance in compliance as part of the bigger risk management picture.

Tax evasion is a criminal offence punishable by imprisonment should a Risk Manager/CFO be found in default by failing to make necessary tax returns at stipulated periods or failure to disclose in a return the true amount of tax payable. Recently in the U.S District Court in Chicago, the billionaire creator of Beanie Babies, TY Warner would serve two years of probation following guilty pleas to a tax evasion charge. Of note is the fact that some social and sport celebrities have in recent times been found guilty of tax evasion.

5.0. The Foreign Account Tax Compliance Act (FATCA)

The Foreign Account Tax Compliance Act (FATCA), is a new US law which is generally known as FATCA. It was passed in 2010. FATCA should not to be confused with FACTA (the Fair and Accurate Credit Transactions Act) just as the IFRS should not be confused with FIRS. FATCA was derived from the Hiring Incentives to Restore Employment (HIRE) Act of 2010, enacted March 18, 2010, H.R. 2847). HIRE is a law in the 111th United States Congress to provide payroll tax breaks and incentives for businesses to hire unemployed workers. FATCA aims to combat tax evasion by US tax residents using foreign accounts. It includes certain provisions on withholding taxes and requires financial institutions outside the US to pass information about their US customers to the Internal Revenue Services (IRS). Failure to meet these new reporting obligations would result in a 30% withholding tax on the financial institutions.

FATCA creates a new information reporting and withholding regime for payments made to certain foreign financial institutions and other foreign entities. The FATCA rules become effective with respect to certain payments made on or after January 1, 2014. On 12 July 2013 the US announced

a delay of 6 months before the commencement of FATCA. The effect of this delay is that there will be no reporting with regard to 2013, and all current deadlines for undertaking due diligence e.t.c will be pushed back by 6 months.

5.1. Objective of FATCA

The Foreign Account Tax Compliance Act (FATCA) is aimed at foreign financial institutions (FFIs) and other financial intermediaries to prevent tax evasion by US citizens and residents through use of offshore accounts. The FATCA provisions were included in the HIRE ACT which was signed into US law on March 18, 2010. FATCA is intended to increase transparency for the Internal Revenue Service (IRS) with respect to U.S. persons that may be investing and earning income through non-U.S. institutions. While the primary goal of FATCA is to gain information about U.S. persons, FATCA imposes tax withholding where the applicable documentation and reporting requirements are not met.

5.2. Requirements of FATCA

FATCA requires foreign banks to find any American account holders and disclose their balances, receipts, and withdrawals to the US (IRS), or be subject to a 30-percent withholding tax on income from US financial assets held by the banks. Owners of these foreign-held assets must report them on US tax returns if they are worth more than \$50,000 and those who do not would be subject to a 30-percent penalty on the balance of the account in question. FATCA also closes a tax loophole that investors had used to avoid paying any taxes on dividends by converting them into dividend equivalents. The CFOs should note this act and guide their organisation accordingly.

5.3. FATCA and its Implication on Businesses

Although FATCA will certainly affects U.S. withholding agents and U.S. multinational companies, the greatest impact will likely be on Foreign Financial Institutions (FFIs) in which Nigerian is not immune. Under FATCA, the United States will seek information not only on all US residents but also on all US persons living overseas because of its unique citizenship-based taxation (CBT). The immediate consequence is that foreign financial institutions do not want US clients, and are advising against investment in US securities. FATCA will have a far-reaching impact on US-based companies as well as foreign companies with US assets or clients. Under the new provisions, a FFI may enter into an agreement with the Internal Revenue Service, or IRS requiring it, among other things, to report information on the FFI's US accounts. A FFI that enters into such an agreement becomes a "participating FFI."

5.4. Safeguards provided by Inter Governmental Agreement (IGA)

5.4.1. Intergovernmental Agreement Model 1

In July 2012, the U.S. Treasury Department issued the first model for an Intergovernmental Agreement (IGA) which makes it easier for partner countries to comply with the provisions of FATCA. The IGA provides for a partnership agreement between the U.S. and a FATCA Partnership jurisdiction, namely France, Germany, Italy and Spain with the United Kingdom first to sign the IGA agreement.

Under this agreement, FFIs in partner jurisdictions will be able to report information on U.S. account holders directly to their national tax authorities, who in turn will report to the IRS.

5.4.1.1. IGA highlights and benefits

- Relaxation of deadlines
- Simplified due diligence
- Increased clarity around due diligence with country specific provisions

Annex II of the Model 1 IGA includes a country-specific list of financial institutions, products and accounts that are exempt or deemed compliant, thus reducing some of the remediation work for FFIs.

- Reduced withholding requirements
- Increased clarity around insurers
- Clearer definitions with respect to pension annuities and more favourable rules applicable to new insurance contracts.

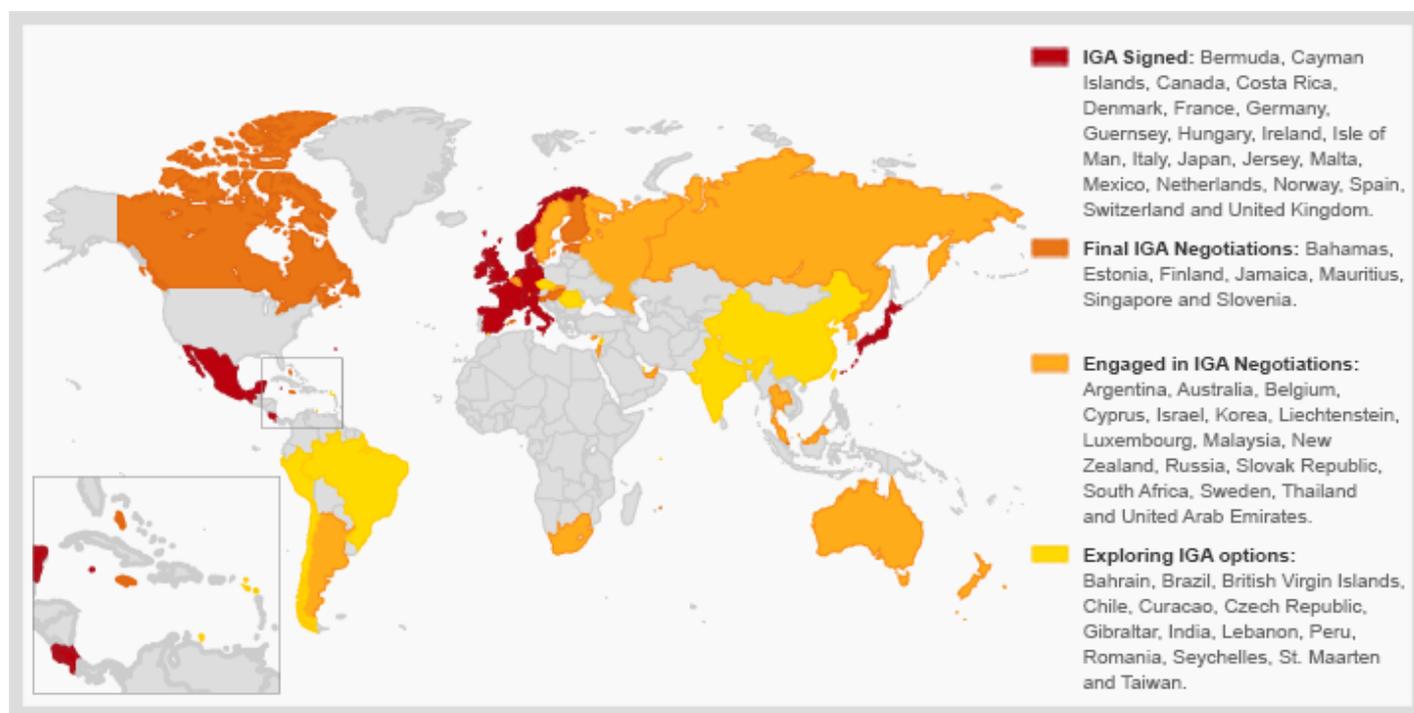
5.4.2. Intergovernmental Agreement Model 2

On November 15, 2012, the U.S. Treasury Department issued the second model of the Intergovernmental Agreement (IGA) for complying with the FATCA provisions. The model 2 IGA reflects the framework that was described in the joint statements by U.S. and Switzerland as well as U.S. and Japan issued earlier in the year.

Model 2 IGA was designed to address potential conflicts of national and local laws that would make it difficult, for Financial Institutions in some jurisdictions, to comply with FATCA.

The most notable differences between Model 1 and Model 2 IGA's,

- In Model 2, financial institutions will report information directly to the IRS rather than their local jurisdictions
- There is no ‘reciprocal’ version of the Model 2 IGA.



6.0. Relationship with Chartered Tax Practitioners

Members of the Chartered Institute of Taxation of Nigeria (CITN) are statutorily recognized tax professionals in Nigeria. They add value to their organizations by their professional and ethical handling of tax matters. Whether they work in-house as tax managers or outside as tax consultants, they help their firms/clients in tax planning, advisory services, compliance issues and tax dispute resolutions. Therefore CFOs are strongly advised to work hand in hand with professional tax practitioners in their bid to ensure tax compliance in their firms. Where the CFO is a member of CITN, it is not out of place for him/her to work with other tax professional colleagues, to enable him share the burden of ensuring compliance and help him focus on his core function of accurate and timely financial reporting.

The relationship between the CFO and the professional tax practitioner therefore must be cordial and collaborative. It is of note that most of the CFO in Nigeria are also members of CITN which qualify them to handle tax related matters.

Ethical Considerations

As members of professional bodies, tax practitioners are bound by the code of ethics of their professional institutes. Tax practitioners play an important role in the tax system. They act as catalysts between the taxpayer who may or may not be knowledgeable in taxation and the tax administrator who is knowledgeable in the area. They are saddled with the responsibility of advising their clients and representing them on issues of taxation. In broad terms, tax practitioners are expected to perform their duties in adherence with the following fundamental principles; viz

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

7.0. Conclusion

In the final analysis, tax planning viz-a-viz initiatives required to keep track with compliance are as much a long term value adding strategy as with the existence of the risk of falling short of regulations put in place for the enforcement of the tax laws.

As the CFO continues to build capacity in the finance function and evaluating available strategy options in building a virile Corporate Governance structure, he should also consider the probability or risk of compliance failure as a risk factor in the decision making process by board and management.

Finally, it pays in the long run to pay taxes and comply with the extant tax laws as failure to do so only leads to incremental cost burden over and above the tax burden. These are the issues to which CFOs must pay attention and for which they must also rally the board, management and staff in achieving.

Thank you for listening!

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Death, taxes and childbirth! There's never any convenient time for any of them!

Margaret Mitchell (1900–1949), U.S. novelist.

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