The Role of the Tax Advisor in the Changing World of Global Tax Administration: The 2012 Erwin N. Griswold Lecture Before the American College of Tax Counsel

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I am, of course, deeply honored by the invitation to deliver the Griswold lecture to my friends and colleagues. It is traditional and, in my case personally appropriate, to pay homage to the man who I always knew as "the Dean." He went off to Washington to become the Solicitor General while I attended the Law School, but his presence was felt nonetheless. Those of you from the Boston area also know that regularly in April and December—no matter where he otherwise was—the Dean would make the pilgrimage to John Hancock Hall to preside over the meetings of the Federal Tax Institute of New England. These were memorable events, not only for the clam chowder at lunch, but, if you were a presenter, there was always a post-Institute dinner as part of the festivities. The places of honor for a female were on either side of the Dean as he presided over that event as well—quizzing everyone on the topics of the day. My wife, Anne, well remembers her evening "in the sun."

I could not do justice to the Dean's legacy by trying again to summarize it. He was simply a towering figure in the tax community. I would like to think that he would be very interested in what I will discuss, as his interests in the tax law went well beyond technical matters and reached to issues of efficient administration of the system—a system which at the time was far less global and complicated than it is today. And in matters of administrative efficiency, his views were consequential, if not always welcomed by all. My own special memory goes back to my days in the Treasury, 1977–1980, and to the vigorous debate at the time over the provision of the 1976 Tax Act that provided a carryover basis for assets that passed from a decedent. I believed then—and I believe now—that there is no policy rationale for allowing the unrealized appreciation in property held at death to escape income tax. The question then, as now, was how to achieve that goal efficiently and fairly. The Dean had a view on that issue—as I am sure at least some of you remember.

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In 1977, he submitted a letter to the Senate Finance Subcommittee on Taxation and Debt Management in connection with a hearing that was being held on the carryover basis provisions.[1] The Dean wrote that he had collected stamps since he was eight years old. He had come to view stamps as a good investment to assure adequate financial resources to care for his wife after his death and at the time of the letter he had over 10,000 of them. He pointed out the practical difficulty of ascertaining the basis of each stamp, noting that he had not kept records of the purchase price because he had no expectation of selling the stamps while he was alive. The letter was principally about the difficulties created by the application of the provision to assets acquired prior to the enactment of the statute. However, it was constantly cited by opponents of the provision to buttress their case that carryover basis could not be made to work and, as we know, at the end of the day the provision was repealed. Of course, the real issue was transition relief as to which, in retrospect, we in the Treasury were much too unyielding. Time has taught me that the important thing is to achieve the substantive result and not worry unduly about transition issues. But to this day I wonder how the Dean would have reported his gain if he had actually sold one of those stamps.

Enough nostalgia. It has been difficult to find a topic appropriate for this group. While tempting, I decided that it was not necessary to remind this audience about the deficiencies of the current tax code and the flawed process by which tax laws are enacted. I did that in my Woodworth lecture in 1999[2] and the issues I cited then remain unresolved today—unfortunately without the luxury of projected budget surpluses to cushion the revenue impact of change and without any honest discussion of the distributional consequences of change. Revenue estimating,[3] the consequences of reducing or eliminating tax expenditures (a concept that has at last been recognized universally as a tool to identify those features of the tax law that provide the substantive equivalent of a direct government expenditure),[4] how we think about "competitiveness" (the subject of a recent ATPI conference in which I participated),[5] and how we measure the incidence of taxation in order better to understand the economic consequences of tax changes—each is a subject

[1] *The Tax Reform Act of 1976: Hearing Before the Subcomm. on Tax'n and Debt Mgmt. Generally of the S. Comm. on Finance*, 95th Cong. 147 (1977) (statement of Erwin N. Griswold).

[2] Harry L. Gutman, 5th Annual Lawrence Neal Woodworth Lecture, *Reflections on the Process of Enacting Tax Law*, 86 Tax Notes 93 (2000).

[3] *See, e.g.,* Staff of Joint Comm. on Tax'n, 109th Cong., Overview of Revenue Estimating Procedures and Methodologies Used by the Staff of the Joint Committee on Taxation (Comm. Print 2005).

[4] S*ee, e.g.*, Staff of Joint Comm. on Tax'n, 112th Cong., Background Information on Tax Expenditure Analysis and Historical Summary of Tax Expenditure Estimates (Comm. Print 2011).

[5] *Conference on International Taxation and Competitiveness*, American Tax Policy Institute (Oct. 17, 2011).

worthy of discussion.[6]

But there is something else going on about which I would like to talk and that is the role of the tax practitioner in the changing landscape of global tax administration. It is a subject that is especially visible to me from my platform as an attorney in a major, global accounting firm. It raises issues that are extremely relevant to us as practitioners, but which do not surface regularly in our day-to-day practice. In particular, I want to discuss the different ways that jurisdictions around the world are approaching the question of the most efficient use of limited resources to enhance tax compliance and the resulting changes to the role of tax advisors.

The topic is timely. Just last Wednesday and Thursday over 375 participants attended a Tax Council Policy Institute Symposium on the subject.[7] The Commissioner of Internal Revenue addressed tax risk management in the keynote address and the entire senior leadership team of the Service—the Deputy Commissioner for Enforcement, the Chief Counsel, the Commissioner of LB&I and the Deputy Commissioner of LB&I for International—as well as the UK Permanent Secretary for Tax—appeared on various panels to discuss the perspective of tax administrators. This is clear evidence that the topic is "top of mind" today.

In this context the role of the tax lawyer is evolving—not in a liability sense, but more broadly as "an officer of the court" in ensuring the sound functioning of domestic tax systems. I am not naïve and I fully recognize the real and potential conflicts between the duty to provide zealous representation of clients and a more abstract responsibility to the "system," a subject fully discussed in the classic, "Standards of Tax Practice," coauthored by two former Griswold lecturers, Jim Holden and Bernie Wolfman.[8] Nonetheless, as lawyers—and more specifically as a part of the class that has been identified in the literature as "tax intermediaries"—we have to pay attention to these developments. And as we do, we may find our roles as counselors altered with respect to interactions with revenue bodies and, potentially more significantly, expanded to assist clients in the development of tax risk management and compliance structures and informed business decisions that will satisfy the requirements of the global tax administrators.

We have already begun to see some of these changes in the tax administrative process in the United States. The CAP program and the introduction of Schedule UTP are examples of domestic adaptations of administrative initiatives that are occurring in other forms around the world, just as the codification of the economic substance doctrine can be seen as reflecting one element in our own unique legislative response to controlling tax avoidance,

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[6] *See, e.g.*, Staff of Joint Comm. on Tax'n, 103rd Cong., Methodology and Issues in Measuring Change in the Distribution of Tax Burdens (Comm. Print 1993).

[7] *13th Annual Tax Policy & Practice Symposium—The New Realities of Tax Risk Management: Navigating Risk in a Complex World*, Tax Council Policy Institute (Feb. 15–16, 2012).

[8] Bernard Wolfman, James P. Holden & Kenneth L. Harris, Standards of Tax Practice § 101.2 (6th ed. 2004).

an exercise that has manifest itself in other countries by the enactment of both General and Specific Anti-Abuse Rules.

So here is what I intend to do. I will review the background that has produced these developments; the specific interest in the role of tax intermediaries in influencing tax compliance; the evolution of that examination into the more relevant inquiry of the interaction between taxpayers and tax authorities that led to the concept of the "enhanced relationship"; how that concept has been adopted in a number of countries; the consequent focus on managing tax risk and what that means for taxpayers; and finally some thoughts on how these developments affect the tax advisors. It is an ambitious agenda.

I. Background

The United States legislative and administrative actions are not occurring in a vacuum. Rather, they are responsive to a phenomenon that took on global significance in 2002 when the OECD's Committee in Fiscal Affairs established the Forum on Tax Administration (the FTA) to promote dialogue between tax administrators and identify good tax administration practices.[9]

The Final Declaration of the FTA's meeting in 2006 (the Seoul Declaration) noted that international tax compliance was "a significant and growing problem" and specifically cited "continued concerns about corporate governance and the role of tax advisors."[10] The Declaration stated that the FTA would examine "the role of tax intermediaries (for example, law and accounting firms) in relation to noncompliance and the promotion of unacceptable tax minimization arrangements."[11] The FTA created a study team[12] to pursue those questions and to identify strategies to strengthen the relationship between tax intermediaries and revenue bodies.[13] The clear assumption of the Seoul Declaration was that much of the fault lay on the "supply" side—that the tax intermediaries were culprits and something had to be done to redress that situation. While acknowledging that tax advisors do play a positive role in the tax system, principally by increasing compliance, the study team's working papers nonetheless cautioned that tax authorities needed to be alert to tax advisors who "design, identify or provide favorable opinions on tax planning options leading to unintended or unexpected tax revenue conse-

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[9] Organization for Economic Co-operation and Development (OECD), Final Seoul Declaration 2 (2006) (issued at the Third Meeting of the OECD Forum on Tax Administration, Sept. 14–15, 2006). The FTA now includes the tax administrators of over 45 jurisdictions. It is currently chaired by the United States Commissioner of Internal Revenue.

[10] *Id*. at 3.

[11] *Id*. at 4.

[12] The team comprised the U.K. and OECD Secretariat and senior representatives from Australia, Canada, Chile, France, Ireland, Mexico, South Africa, Spain and the United States. Organization for Economic Co-operation and Development (OECD), Tax Intermediaries Study Working Paper 1: How the Study Team is Working (2007), *available at* www.oecd.org/dataoecd/57/13/38393150.pdf.

[13] Organization for Economic Co-operation and Development (OECD), Study into the Role of Tax Intermediaries 7 (2008) [hereinafter Final Study].

quences; and/or act as advocates for their clients where there is disagreement over the interpretation of the law."[14] The working papers proposed a formal system of risk profiling for tax advisors on the basis of the extent to which the advisors engaged in those activities.[15]

The study team received and took into account numerous comments directed at the assumption that the supply side dictated the market, as well as severe criticism of the notion of risk profiling tax advisors. Recognizing that tax intermediaries do not work independently from their clients but supply services that clients demand, the Study Team ultimately concluded that revenue bodies needed to consider the taxpayer's role—the 'demand side' of the market.[16]

This was an important insight. The recognition that the primary relationship from both a statutory and practical perspective is between the taxpayer and the revenue body[17] shifted the focus of the exercise and became the driver of the principal recommendation of the report—the creation of an "enhanced relationship" between taxpayers and revenue bodies in which tax intermediaries play a distinctly subordinate direct role. The prior prescription of aggressive risk profiling for tax advisors was replaced by a more limited approach that emphasized the traditional tools of regulation and registration, advance disclosure, compliance agreements, and penalties and other sanctions to deal with tax intermediary risk.[18] The study also encouraged more dialogue with the advisor community in an effort to promote a more extensive appreciation of the role each plays in the efficient administration of the tax system.

At this point you may well ask—where's the beef? Having started out by focusing on tax advisors the FTA got it right and put its principal focus on taxpayers. Why should I care? Well, here's why. The notion of an "enhanced relationship" has taken hold in many jurisdictions, although how that is expressed differs. A "tripartite" relationship that involves tax advisors as well as taxpayers and revenue bodies poses new and different challenges for tax advisors. It is not about how revenue authorities regulate tax advisors. Rather, it is about the role of the tax advisor in the new system. So, let's turn to that.

II. The Evolution of the Enhanced Relationship Concept

We are all aware of the traditional, adversarial relationship between the revenue body and the taxpayer. I am going to call that the "basic relationship." That relationship creates both rights and obligations for taxpayers and tax administrators. Taxpayers have the obligation to be honest, co-operative, provide accurate information and documents on timely basis, keep records and

[14] Organization for Economic Co-operation and Development (OECD), Tax Intermediaries Study Working Paper 5: Risk Management 7 (2007), *available at* www.oecd.org/dataoecd/59/59/39003865.pdf.

[15] *Id.* at 9.

[16] Final Study, *supra* note 13 at 7.

[17] *Id.* at 11.

[18] *Id.* at ch. 4.

pay their tax liabilities.[19] They have the right to be informed, assisted and heard, appeal, pay no more than the correct amount of tax, achieve certainty and have privacy and confidentiality.[20]

In practice, this relationship does not require taxpayers to do more than file an accurate and timely tax return. Revenue authorities have the traditional enforcement tools that enable them to get supporting information, determine whether the appropriate amount of tax has been declared and collect that tax. As the OECD has observed, the obligation-based nature of the relationship means that there is no incentive for taxpayers to disclose additional information to revenue bodies, particularly regarding areas of tax uncertainty or risk.[21]

In an increasingly global economy, with a myriad of different tax laws and shrinking resources with which to administer their tax systems, individual governments and tax administrators have sought ways to improve the efficiency of tax collection. One of those ways has been for revenue officials to recognize "the different factors that influence taxpayer" compliance and adopt strategies to achieve improved compliance. In practice this has meant that tax authorities take on a broader servicing role in exchange for taxpayers adopting a more open, interactive approach. This is the "enhanced relationship."[22] It is based on a "carrot and stick" model of tax administration in which the regulator's enforcement approach is determined by an assessment of the conduct of the regulatee. It is grounded in the premise that if the parties understand each others' needs and trust each other to observe them, the approach will yield positive enforcement results.

What then are the parties' needs? To ensure that taxpayers meet their tax obligations voluntarily and accurately the tax authorities will expect taxpayers to be "fully transparent in their communications and dealings and to disclose all significant risks in a timely manner." In essence, the taxpayer is being asked to provide a "self-risk-assessment."

The goal of taxpayers is "to have tax matters resolved quickly, quietly, fairly and with finality." To achieve this, tax authorities need to demonstrate: commercial awareness—that is, understanding the business of business; impartiality—which involves the culture, attitude and mindset that the revenue authorities bring to the issue resolution process; proportionality—which involves how the revenue body goes about determining which aspects of, and to what extent, a taxpayer's return is to be examined; disclosure and transparency—which principally involves the revenue authority being open about why particular positions are being scrutinized; and finally, responsiveness—which requires the tax authorities to provide prompt, efficient and professional

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[19] Organization for Economic Co-operation and Development (OECD), Taxpayers' Rights and Obligations—Practice Note (2001).

[20] *Id.* The OECD practice note on *Taxpayers' Rights and Obligations* expands the definition of these basic elements.

[21] Final Study, *supra* note 13 at 40.

[22] John Braithwaite, Restorative Justice and Responsive Regulation (2002).

responses to legitimate inquires made during the course of an examination.[23]

The anticipated results of meeting these reciprocal requirements are that taxpayers would achieve earlier resolution of tax issues with less extensive audits and lower compliance costs and revenue authorities would achieve more efficient collection of the correct amount of tax.

What about the tax advisor? Unless the tax advisor is representing the taxpayer pursuant to a power of attorney, he is not a direct participant in the system. However, the "enhanced relationship" structure envisions tax advisors facilitating the disclosure and transparency demanded by the new system and it is here that traditional views of professional responsibility may collide with the expectations of the new system. Less radical inputs involve assisting the revenue agency (as a part of achieving its goal of commercial awareness) to understand the business of tax advisors and in particular how and the extent to which they influence the tax decisions of their clients. Tax advisors can also assist the revenue body in understanding the business of the taxpayers. The overall hope is that tax advisors will ultimately function more effectively in advising clients, particularly with respect to tax control frameworks and appropriate levels of transparency and disclosure.

What happens to taxpayers or advisors who are unwilling to go beyond the traditional obligations of disclosure and transparency dictated by the "basic relationship." The answer with respect to taxpayers is "risk assessment," which is at the core of the enhanced relationship and the place where tax advisors may have their most significant impact in ways that are different from the traditional tax counseling role.

With respect to tax advisors, the study makes a general recommendation that revenue bodies should use a risk-based approach to focus attention on tax advisors who are unwilling to engage in the enhanced relationship and continue to promote aggressive tax planning without transparency. The objective is to make it apparent that there are consequences in failing to cooperate. A number of suggestions, including civil penalties or other sanctions, are mentioned but no specific action is recommended. To the extent the "enhanced relationship" requirements are aspirational, counselors will have to weigh compliance against their other professional obligations. The situation would change if the requirements became statutory.

Can the "enhanced relationship" achieve its objectives? The jury is still out on that question. But the more significant point is that some form of it is being adopted around the world. Whether it will ultimately be successful in achieving its goal does not affect the fact that as tax advisors we must be cognizant of and react to its development. Thus, the experience of a number of countries that have implemented its principles is instructive.

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[23] Final Study, *supra* note 13, chs. 7 and 8.

A. *Australia*

Australia embraced the principles of the "enhanced relationship" model in the late 1990s, before the concept had a name. Since then, it has been in the forefront of refining the model. The basic elements are this. The level of the tax administration's engagement with taxpayers is determined by an assessment of the taxpayer's compliance approach and how the taxpayer manages its tax risk.[24] Large businesses are profiled twice a year, comparing the results of a number of risk filters with the company's previous results and data from other businesses. After review the company is placed in one of four risk categories. The risk category classification dictates the resources that the ATO will devote to the company, ranging from continuous review for higher risk taxpayers to periodic monitoring for lower risk taxpayers.

The ATO uses a Risk Differentiation Framework to assess a taxpayer's tax risk. Factors that are considered include past compliance behavior, tax risk management governance, business performance compared to tax outcomes of the taxpayer and peers, as well as special factors that relate to the company, such as significant transactions, and intelligence from other agencies (both domestic and international). The ATO is specifically focused on financial or tax performance that varies substantially over time or varies from the industry norm, unexplained variances between economic performance and tax liability, commercially uneconomic losses, tax outcomes that appear inconsistent with the policy of the tax statute, a history of aggressive tax planning, and weaknesses in corporate governance structures.[25] The protocols for conducting risk review analyses and audits are publicly available and taxpayers have an opportunity to discuss the outcomes with the agency.[26]

While not explicitly a part of the risk analysis, the ATO has recognized that tax advisors play an important role in influencing tax compliance. Consequently it has explicitly solicited tax advisors to become partners in the enterprise and it has proactively engaged in conversations with the tax profession to develop working relationships to further this goal. Not surprisingly, the outcome of this outreach has been described as "patchy."[27] The reasons for this are, to a large extent, not specifically related to Australia, but rather reflect the tax advisor's conflict between client responsibility and responsibility to the system. Moreover, the playing field between the advisors and the ATO may not be level. As much as the revenue authority may want to create a partnership with advisors, its ability to do so is limited by the fact that it has to administer the law as written and thus its flexibility to accommodate

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[24] Australian Taxation Office, Large Business and Tax Compliance (2010).

[25] Australian Taxation Office, Compliance Program 2010–11 at 27 (2010).

[26] Inspector-General of Taxation, Report into the Australian Tax Office's Large Business Risk Review and Audit Policies, Procedures and Practices (2011) (Austl.) [hereinafter I-G Report].

[27] Justin Dabner & Mark Burton, *Lessons for Tax Administrators if Adopting the OECD's "Enhanced Relationship" Model—Australia's and New Zealand's Experiences*, 63 Bull. for Int'l Tax'n 321 (2009).

the reasonable requests of the advisors may be limited. Limited survey data indicate that advisors to large entities have begun to enjoy a more cooperative relationship with the ATO, but that other tax professionals did not have the same experience. The survey indicated that to some extent this result occurred because not all levels of the ATO had bought into the system.

The role of enterprise tax risk management as an component of overall risk assessment cannot be over-emphasized. It has been the theme of a number of speeches by the Australian Commissioner of Taxation and it is a matter to which I shall return.

The ATO's large business risk review and audit policies, procedures, and practices were subject to an extensive recent review by the Inspector-General of Taxation.[28] On balance the report indicated that the ATO program has been successful in making the review and audit processes more efficient, cooperative and less intrusive. Nonetheless, issues remain with respect to communication and engagement and transparency in the risk review and audit processes, particularly focused on a perceived lack of even application of the ATO's articulated policies and procedures. The report identified three broad areas for improvement: greater transparency in the risk review and audit processes and procedures, more consistent and proportionate application of the risk review and audit principles and "greater engagement and dialogue and aspiring to a greater level of trust."[29] For our purposes, what is important is that the enhanced relationship approach to compliance has become imbedded in the Australian tax administration process.

B. *The United Kingdom*

The core of the UK program, adopted in 2006, is the Business Risk Review (BRR) pursuant to which companies are awarded a risk rating that determines the extent to which HMRC will get involved in the company's affairs and the working relationship between the two.[30] The "risk" to which the program is directed is tax compliance. The current iteration of the program is set out online in the "Tax Risk Compliance Management Process" document that is revised periodically.[31] The program is designed to foster efficient allocation of limited HMRC resources. However, it is also expected to provide an incentive for companies to alter their behavior with respect to transparency, governance and planning.

Companies are classified as either Low Risk or not Low Risk. The Risk Rat-

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[28] I-G Report, *supra* note 26.

[29] *Id.* at 35.

[30] Sir David R. Varney, HM Revenue & Customs (HMRC), 2006 Review of Links with Large Businesses (2006) [hereinafter Varney Review]; HM Revenue & Customs (HMRC), Approach to Compliance Risk Management for Large Business (2007) [hereinafter Risk Management Report].

[31] *See* Tax Compliance Risk Management Manual, HM Revenue & Customs (HMRC), http://www.hmrc.gov.uk/manuals/tcrmanual/index.htm (last visited June 14, 2012) [hereinafter TCRM].

ing is confidential. Low Risk taxpayers are generally subject to risk review only every three years and their tax returns will not be challenged. Taxpayers who are not Low Risk can expect more frequent BRRs, HMRC-initiated "interventions," and, if the taxpayer represents a "significant" risk, more intensive actions are deployed to produce a "rapid" reduction in their risk profile.

The BRR involves assessing the taxpayer against seven factors, three of which are deemed "inherent" and four of which are deemed "behavioral." The former relate to the risks that are inherent in the company's structure and operation: complexity—the potential risks in the size, scope, and depth of the business interests; boundary—the level of complexity in international structures, financing and related parties; and change—the degree and pace of change in factors (such as mergers or acquisitions) that could affect the tax profile of the business.[32] The behavioral factors, which are the principal focus of the risk determination, relate to: corporate governance—management accountability for managing tax risk; delivery—delivering the right tax through systems, processes and skills; tax strategy—the extent to which the taxpayer engages in tax planning that does not support commercial activity; and contribution—the tax paid in comparison to what HMRC thinks should be paid based on the level of the company's activities and a comparison with its competitors.[33]

Survey data and anecdotal evidence indicate that the program has been helpful.[34] Moreover, HMRC has engaged in a continuous public dialogue with the business community over implementation of the program.[35] One issue, similar to that identified in Australia, is how to ensure consistent treatment by HRMC officials. However, the most significant issue, which has not been fully resolved, relates to the definition of suspect tax planning and its effect on Risk Rating. The relevant HRMC guidance states that taxpayers must not structure transactions in a way that "gives a tax result contrary to the intention of Parliament" and must report to HMRC "transactions that rely upon innovative interpretation of tax law and fully disclose any legal uncertainty." These criteria pose some difficulty for taxpayers and their advisors because they rely on standards that are not found in the UK statutes or case law.[36] The business community has indicated that "transparency, disclosure, and robust compliance are . . . reasonable requirements, but engaging in tax planning is . . . something that the company has a right to do," particularly

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[32] TCRM, *supra* note 31, at § 3320.

[33] TCRM, *supra* note 31, at § 3330.

[34] Judith Freedman, Geoffrey Loomer & John Veller, Analyzing the Enhanced Relationship Between Corporate Taxpayers and Revenue Authorities: A U.K. Case Study, IRS Research Bulletin: Proceedings of the 2009 IRS Research Conference, *available at* http://www.irs.gov/pub/irs-soi/09rescon.pdf; Judith Freedman, Geoffrey Loomer & John Veller, Corporate Tax Risk and Tax Avoidance: New Approaches, 2009 British Tax Rev. 74.

[35] Business Tax Forum, HMRC, http://www.hmrc.gov.uk.

[36] Judith Freedman, *Responsive Regulation, Risk and Rules: Applying Theory to Tax Practice*, 44 Univ. Brit. Colum. L. Rev. 627 (2011).

since, under the program, there is full disclosure.

Obviously, taxpayers have the choice to cooperate in the enhanced relationship initiative and if they do not see a real benefit to the promised "lighter touch" they will not engage in the program (risking a visit to their Board by HMRC). Also, companies that participate cooperatively in the HMRC initiative give up some of the "rights" they possessed under the "basic relationship." Does it matter? Survey results conclude the BRR leads to a better allocation of resources within HMRC and a possible change in behavior with respect to transparency and openness, but that it is unlikely to alter taxpayer planning behavior.

The initiative has not been without its problems. The House of Commons Committee of Public Accounts has been engaged in an investigation of the interaction of HMRC with large corporate taxpayers.[37] While in part politically motivated, the tentative conclusions of the inquiry have raised concerns about HMRC transparency and consistency in the application of its rules. In particular, the Committee has noted that HMRC has left itself open to suspicions that its relationships with large companies are too cozy.

These criticisms are not unexpected. Indeed they may be inevitable. HMRC leadership is taking steps to address them. However, if in fact the program has led to more efficient deployment of resources it follows that avoidance is being identified more systematically and from that perspective the program has begun to accomplish its objective.

C. *The United States*

It would not seem practical in the United States to introduce an "enhanced relationship" program in which the Service would explicitly categorize taxpayers as high or low risk. As we have seen in the UK, that could result in adverse publicity (and probably some sort of Congressional investigation). Rather, the Service has turned to other methods to achieve the goal of attempting to maximize the efficiency of tax collection while at the same time altering taxpayer behavior. One initiative, available to a limited number of taxpayers, is the Compliance Assurance Process (CAP) program. The second is Schedule UTP, the requirement for corporations with more than $100 million in assets to include with their tax return a schedule of their "uncertain tax positions."

1. *The CAP Program*

In 2005, the Service selected 17 taxpayers to participate in a pilot program pursuant to which the taxpayer fully discloses information concerning completed transactions and its proposed tax return treatment of all material issues. In return, the Service conducts a near real-time audit of the disclosed tax positions and the parties attempt to reach and record agreement on return positions. If the returns are filed consistent with the agreed positions the return

[37] Committee of Public Accounts, HM Revenue and Customs 2010–11 Accounts: Tax Disputes, Sixty-First Report of Session 2010-12, H.C. 1531.

is accepted by the Service as filed. Acceptance can be full or partial and unresolved issues are dealt with in the traditional audit mode.

There are now some 160 taxpayers enrolled in CAP and the Service has expanded its scope and made it permanent. There are now three phases of CAP; pre-CAP in which the parties agree on a plan to eliminate open audit years by a date certain and during which the taxpayer has to demonstrate transparency and cooperation; CAP itself in which the objective is to resolve all material issues prior to filing; and CAP maintenance which occurs once a positive track record has been established and the Service understands the taxpayer's accounting, internal control, and risk management processes. At that point the examination team can lower its level of review. Periodic meetings occur to assure there is no change in the taxpayer's risk profile.

Participants in CAP generally report that their experience is preferable to the typical Service large case audit, but note that at least initially CAP requires a significant resource commitment. In deciding whether to participate in the program companies need to determine the importance of early certainty and greater predictability and understand and be willing to commit to a high level of transparency. Tax advisors can assist in this assessment, including the evaluation of exposures in open years.

The tax advisor role can be significant in other areas as well. For example, advice will be needed with respect to the level of disclosure that will have to be made to the government as a company is planning, structuring and executing transactions. The advisor can also play a role in enhancing the government's commercial awareness. And finally, the advisor can be a positive factor in encouraging trust between the parties—the concept that lies at the core of the enhanced relationship.

2. *Schedule UTP*

Schedule UTP is explicitly designed to inject efficiency into the audit process. Here is what the Commissioner had to say, "Guided by the fundamental principle that transparency is essential to achieving an effective and efficient self-assessment tax system, the I.R.S. [will require] business taxpayers to report basic information regarding their uncertain tax positions when they file their tax returns."[38]

The stated goals of the Service are to create greater certainty for taxpayers, reduce the time required to find issues and complete audits, prioritize the selection of taxpayers and issues for examination, increase consistency of taxpayer treatment and systematically identify issues where their uncertainty makes them ripe for Service guidance.

Starting with tax returns for 2010 companies with assets over $100 million had to file Schedule UTP on which they disclosed uncertain tax positions

[38] Douglas Shulman, Comm'r, I.R.S., Prepared Remarks to the American Bar Association in Toronto, Canada (Sept. 27, 2010); *see also* Douglas Shulman, Comm'r, I.R.S., Prepared Remarks to the New York State Bar Association in New York, N.Y. (Jan. 26. 2010).

for which they had created a reserve under the applicable financial reporting system (or for which no reserve was created because the taxpayer expects to litigate the position if challenged). The asset threshold declines to $50 million in 2012 and $10 million in 2014. The schedule requires the taxpayer to rank the uncertain positions based on the actual reserve amount, but that amount is not required to be stated, nor is the company's risk evaluation. The schedule also requires a concise description of the position that provides the Service with sufficient facts to identify the issue. The taxpayer's rationale or analysis of the position is not required.[39]

The introduction of the notion of requiring taxpayers to disclose their uncertain tax positions created a bit of a firestorm,[40] even though these positions in the aggregate were already disclosed in the financial statements. In particular taxpayers objected that the schedule would provide an audit roadmap. That is a curious objection because that was the objective of the schedule. More to the point, taxpayers feared that agents would simply write up disclosed issues without any examination of the merits of the position. The Service has responded to these concerns by issuing guidance that reflects an intention to monitor carefully the ways in which the information is used in the examination process.[41] In particular, the Service has said it will create a centralized process to review and analyze the disclosures and has reminded examiners to conduct examinations consistent with the understanding that UTPs are uncertain for various reasons. In other guidance it has limited the types of questions that examination teams may ask. For example, the taxpayer cannot be asked to explain its rationale for determining that the position was uncertain, information about the hazards of litigation or an analysis of support for or against the position. Significantly, the team cannot ask why the position is uncertain, nor can the team ask the taxpayer for copies of

[39] The Service received approximately 1,900 Schedules UTP for the 2010 filing season containing approximately 4,000 UTP disclosures. Seventy-nine percent of the returns that disclosed uncertain tax positions came from corporations not currently in the Coordinated Industry Case (CIC) program, the Service procedure that that examines the largest and most complex business entities. The non-CIC returns averaged 1.9 uncertain position disclosures; the CIC returns that included uncertain positions averaged 3.1 UTPs per schedule. Fifty-three percent of all companies filing the schedule disclosed only one or no uncertain positions. The most frequently reported issues involved transfer pricing, the research and experimentation tax credit and various business expense issues.

[40] *See*, *e.g.*, Comments of ABA Tax Section, 2010 Tax Notes Today 104-66 (June 1, 2010); Comments of ABA, 2010 Tax Notes Today 105-19 (June 2, 2010); Comments of the New York State Bar Association, 2010 Tax Notes Today 60-27 (Mar. 30, 2010); Comments of the State Bar of Texas Tax Section, 10 Taxcore (BNA) 105 (June 3, 2010).

[41] *See, e.g.*, Memorandum from Heather C. Maloy, Commissioner, Large Business & International Division (LB&I) to LB&I Employees (Aug. 31, 2011), *available at* http://www.irs.gov/businesses/corporations/article/0,,id=245494,00.html (regarding "UTP Guidance and Procedures for the Compliance Assurance Process (CAP) Program"); Memorandum from Heather C. Maloy, Comm'r, Large Business & International Division (LB&I) to LB&I Employees (May 11, 2011), *available at* http://www.irs.gov/businesses/corporations/article/0,,id=245494,00.html (regarding "Centralized Management of LB&I Returns with UTP Schedules").

workpapers used to prepare the Schedule UTP, any tax accrual workpapers, or any documents that are privileged under the Service's modified policy of restraint—the Service policy that states that although it is legally entitled to examine tax accrual workpapers it will not request them unless the taxpayer has claimed a benefit from a listed transaction or a transaction similar to a listed transaction or there are "unusual circumstances."

Although in theory these actions by the Service limit how the Service may obtain and use the information provided by the schedule, taxpayers remain curious and skeptical about what will really happen in the field. In the context of our examination of deviations from the "basic relationship," however, this innovation is significant. It clearly enhances the objectives of the tax collector, but it provides only conjectural future benefits for taxpayers. These conflicting objectives may become more sharply focused as the filing threshold decreases in the future.

The introduction of Schedule UTP provides opportunities for the tax advisor. As an example, consider the following. An uncertain tax position is a position that has been recorded in the entity's tax reserve. Determining whether a position is to be included in the tax reserve requires a decision as to the level of certainty that the position will be upheld. That comfort level is a legal judgment. With the new emphasis on disclosing uncertain tax positions there will likely be increased attention paid to the level of comfort with respect to questionable positions.

III. Tax Risk Management

Managing tax risk is explicitly or implicitly at the core of all the initiatives I have mentioned. And the tax authorities in many jurisdictions have made this abundantly clear. For example, Commissioner Shulman, noting that taxes are one of the biggest expenses of a corporation, has said that boards of directors should play an important role in overseeing tax risk and tax strategies of corporations.[42] The Australian Tax Commissioner has said that the "increasing focus by regulators on the need for robust risk management frameworks . . . [has brought] many companies' tax risk management into the public arena."[43] The HMRC has made it clear that robust tax management policies are a key to Low Risk rating and that the Boards of noncompliant taxpayers can expect a visit. That should be enough to get one's attention. But, in truth, satisfying the tax administrators is only one of the many reasons an entity should consider implementing formal tax risk management policy and the tax adviser can and should have a role to play in that process.

Outside the tax arena there is an increased focus on corporate governance generally, and with it, tax risk management. This focus has resulted in greater

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[42] Douglas Shulman, Comm'r, I.R.S., Speech to National Association of Directors (Oct. 19. 2009).

[43] Michael D'Ascenzo, Comm'r, Austl. Tax'n Office, What's Tax Got To Do With It?, Speech to Australian Institute of Company Directors (Feb. 16, 2010).

demands for transparency and disclosure. The Sarbanes–Oxley legislation, FIN 48 in the accounting area, heightened media attention on the complexity and significant impact that taxes can have on a corporation's reputation and value all combine to emphasize the need for a corporation to focus on managing tax risk.

What does managing tax risk entail? First, we need a definition of tax risk. Then we need to identify where the risks arise. Finally, we need to implement a plan to integrate the tax risk management policy with the entity's enterprise risk management policy.

Broadly speaking, tax risk encompasses all sources of risk that may create an unexpected outcome from a tax position. The potential for tax risk is imbedded in all aspects of the business. Risks may arise in operations, transactions, compliance, financial accounting and controversy management.

Analysis of the scope of the risk requires a more granular examination of the sources of risk within each of those categories. For example, transactional risk includes the risks associated with the application of the tax laws, regulations and interpretations to specific transactions. In assessing the scope of tax risk in relation to transactions, one can identify the following areas of concern: a challenge to the technical basis for the tax treatment of the transaction, a change in law that affects the transaction, a change in facts or circumstances, insufficient tax planning, or failure to implement the planning. A similar list can be prepared for each of the other categories.

The nature of these risks will vary from company to company, but it important to understand that tax risk is substantially more than getting the numbers wrong on a tax return and the areas in which tax risks can arise are not limited to the tax department alone. The challenge is to create an internal matrix that will not only identify these risk areas but also create a framework in which they can be monitored. This is not an insignificant challenge. It involves the active collaboration of the tax department, the "C Suite" and the responsible committees of the board. It should be obvious that outside advisors can play a significant role.

The benefits of this in-depth analysis are manifold. It is not just that the tax administrators are satisfied; rather it can result in increased confidence that the tax function is operating in a manner that is consistent with the organization's overall business goals, that there is control from the organization's center and that there is clarity on the roles, responsibilities and accountability for each element of the plan.

IV. Conclusion

I have outlined for you a number of significant developments in the realm of global tax administration. In particular I have highlighted the role that the examination of the role of tax intermediaries played in the development of the "enhanced relationship" concept of tax administration. I have described how that model is being applied explicitly in Australia and the UK and the United States. I have also described the emphasis that those enforcement

models place on managing tax risk. And this is not the whole story. Other countries, such as the Netherlands, Ireland, Canada, New Zealand, and Korea have adopted similar programs.

And there is more. Each of these jurisdictions has introduced other initiatives, illustrated in the United States by the Industry Issue Resolution program, pre-filing agreements, Fast Track Settlement and the CIC program, designed to advance the objectives of consistency, certainty and efficiency. The FTA has identified high net worth individuals and banks as targets for further examination and has published reports on each.[44] The Service has created a global high wealth industry initiative to look at the entire web of business entities, including global activities, controlled by wealthy individuals, to assess tax compliance risks.[45] Australia, Canada, Germany, and Japan have created similar groups. The UK requires banks to execute a Code of Conduct in which the bank commits to act within the spirit of the law.[46] The UK has also assembled a huge data base to which risk filters are applied to identify targets for examination. Countries are sharing information and engaging in joint audits. This scrutiny will only intensify, particularly as the focus expands beyond large corporations.

To be sure, the ultimate success of the enhanced relationship approach will depend upon whether each party can deliver on its commitments—transparency and disclosure by taxpayers; commercial awareness, impartiality, proportionality, disclosure and responsiveness by tax authorities—and establish the level of mutual trust upon which the program depends. At the TCPI Symposium the leadership of the Service reiterated its commitment to those principles and invited taxpayers to the table.

These developments provide new and different opportunities for tax advisors. It is incumbent upon us to recognize and react positively to them. Understanding the requirements is the first step. Recognizing specific opportunities is the second. There will be a need to consult with respect to the benefits and costs of the transparency demanded by the enhanced relationship, as well as what the practical requirements entail. And finally, opportunities abound in the general area of counseling with respect to managing tax risk, but they will require a re-thinking of our traditional role. It is a new world and we must be prepared to confront it.

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[44] Organization for Economic Co-operation and Development (OECD), Building Transparent Tax Compliance by Banks (2009); Organization for Economic Co-operation and Development (OECD), Engaging with High Net Worth Individuals on Tax Compliance (2009).

[45] *See* Douglas Shulman, Comm'r, I.R.S., Remarks at AICPA National Conference on Federal Taxation in Washington, D.C. (Oct. 26, 2009).

[46] *See*, HM Revenue & Customs, www.hmrc.gov.uk.