"You must pay taxes. But there’s no law that says you gotta leave a tip.”

The striking and epochal 2006 advertising payoff line in an advertising campaign by multinational financial services giant, Morgan Stanley, was viewed as much an avowal of the industry’s attitudes toward paying taxes as it was an encouragement to use their experts in determining the correctly calculated statutory tithe.

But the Morgan Stanley sentiment, intended or no, is a subliminally accepted norm for many multinational corporations, who have created complex structures aimed at aggressively minimising their effective tax rates – often to rates which are negligible in comparison to the profits generated by these entities. In the past few years, there has been increased interest from governments, revenue collectors, journalists, NGOs and the general public, in ensuring that these entities pay their fair share of tax – and media buzz around the so-called ‘Panama Papers’ and the tax strategies of companies like Apple and Google in Ireland, have highlighted such perceived ‘kick serve’ conduct.

While in many cases the strategies and policies that these taxpayers employ are technically legal, the result of these strategies can be viewed negatively, with unintended consequences in respect of that company’s reputation. Against this background, the King IV Report on Corporate Governance™ for South Africa (the Code) released this week specifically includes the formulation of tax policy and strategy within the ambit of a board of directors’ responsibilities.
According to King IV™, the board of directors of an entity must now balance the requirement of ‘Responsible Corporate Citizenship’ with the expectation of shareholders, and other stakeholders of the organisation, that tax costs are minimised as far as possible. In many cases, the board will need to carefully consider the reputational repercussions of a tax strategy (bearing in mind that the Code not only requires the organisation to be a responsible corporate citizen but also to be seen to be a responsible corporate citizen) against the profit generating ability of that tax strategy.

The mere fact that a corporate’s tax structure or strategy is technically legal does not necessarily reduce the reputational damage caused by the publication of such strategies. It is worth noting that these requirements do not only apply to the overarching tax strategy of the organisation, but also to any transaction which the organisation concludes, seeing as each such transaction will have tax consequences particular to that transaction.
In general, the tax provisions of the Code aligns South African corporate governance requirements with international trends. In addition, with the proliferation of automatic exchange of information agreements between the South African revenue authorities and other revenue authorities, it is important that South African organisations ensure that their tax corporate governance complies with international best practice. Application of the Code principles should ensure that South African organisations become compliant in this regard.

Accordingly, where in the past the board of directors may have taken a more passive role in respect of the tax strategy of an entity, the Code now requires the board of directors to actively engage on tax governance decisions. The “stakeholder” approach of the Code requires that the board now has to consider whether the tax strategy employed by the entity is for the benefit of all stakeholders of the entity.

Queries regarding the application of King IV™ to your corporate structure and strategies may be directed to André Visser (Partner) and Shmuel Moch (Associate).