CORPORATE GOVERNANCE AND TAX: STRONGER TOGETHER

Max Schofield
LLB (Exeter), LLM (Durham), LLM (CGSL Lisbon), JD Exchange (Cornell)

Working Paper No.01/2015

January 2015

Keywords: tax law, corporate governance.

CORPORATE GOVERNANCE AND TAX: STRONGER TOGETHER

Max Schofield[1]

mjpschofield@gmail.com

Abstract

Executive Summary

Until recently there has been relatively little attention paid to the relationship between corporate governance and tax rules. The two disciplines do not exist in a vacuum, instead there is a complex interplay and symbiosis that can dramatically effect the efficiency of corporate structures and strategy. This paper hopes to provide a compendious analysis of the overlaps between the general corporate income tax system and corporate governance, concluding that the two fields are not exclusive. The regulatory effects of tax can be direct or accidental, both influence a broad spectrum of commercial decisions ranging from managerial remuneration to the (global) market for corporate control. Tax may not be the most effective way of improving governance, however there is value in charting the effects. With a deeper understanding, legislators may acknowledge the possibility of more effective regulatory or Pigouvian measures, and corporate governance experts become educated in the wider consequences of business strategy. A greater appreciation of tax policy and tax management is required in future corporate governance literature. When working towards a common goal the two areas of law complement each other and may provide more efficient alternatives than implementing separate schemes.

[1] This paper was written as part of the European Corporate Governance Seminar of the Católica Global School of Law LL.M. taught by Prof. Paulo Câmara, by Max Schofield LLB (Exeter), LLM (Durham), LLM (CGSL Lisbon), JD Exchange (Cornell).

1. INTRODUCTION

"In the complexity of today's business and tax jungle, a corporate president who does not obtain tax advice before a substantial dollar transaction, ought to be fired."[2]

The corporate tax system, as with most taxes, has the primary purpose of raising revenue however, the regulatory effects of the CIT[3] are widely overlooked in company law literature. As Avi-Yonah notes, much of the complexity of the tax system stems from the government's attempt to use CIT to achieve regulatory goals.[4] It is hard to deny that tax issues have made their way into the board room, shifting the role of the tax director from tax specialist to business manager.[5] Yet until recently there has been relatively little attention paid to the relationship between corporate governance and tax rules.[6] Schizer wrote recently for the Oxford Handbook on Corporate Law and Governance that tax experts rarely focus on agency costs, while corporate experts seldom have detailed knowledge of tax.[7]

There are regulatory effects for the sake of the agency problem and managerial constraints, as well as incentivising or penalising activities as a means of behavioural regulation (to a large number of individuals indirectly through a relatively small number of companies which lend themselves to accessible monitoring). Recently taxation has collided with corporate governance in regard to the duties of directors. Whilst considering to whom the duties are owed, it may elicit the question of whether there exists a duty to minimise the tax burden in line with the risks that tax planning imposes. Tax avoidance is undoubtably a zeitgeist issue with potentially harmful effects on a company's reputation. The recent tax scandals involving companies like Starbucks or Amazon highlight the significance of the connection between tax management from the board, and reputation. It would hardly be a huge leap to include the relationship between a corporation and the

---

[2] *Plains Petroleum Co. v. Commissioner*, (1999), T.C. Memo 1999-241, in: Hoard, V., *Corporate Tax Shelters*, (2000), Tax Practice & Procedure, 24

[3] Corporate Income Tax.

[4] Avi-Yonah, R., *Taxation as Regulation: Carbon Tax, Healthcare Tax, Bank Tax and Other Regulatory Taxes*, (2011), Acct. Econ. & L. 1, Art.6; Also available as: Draft 8/23/10, *U of Michigan Law & Econ, Empirical Legal Studies Center Paper No. 10-020, U of Michigan Public Law Working Paper No. 216*, <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1664045> accessed 07/14.

[5] Minnick, K., Noga, T., *Do Corporate Governance Characteristics Influence Tax Management?*, (2010), Journal of Corporate Finance 16, 705

[6] Owens, J., *Good Corporate Governance: The Tax Dimension*, (2006), OECD Seoul, Korea, 1, <http://www.oecd.org/site/ctpfta/37207911.pdf> accessed 07/14. See also: Schizer, D., *Tax and Corporate Governance: The Influence of Tax on Managerial Agency Costs*, (2014), Columbia Law Working Paper No. 491, 2. ["Yet although the tax system influences managerial agency costs in a number of ways, many of these effects have attracted only limited scholarly attention."]

[7] Schizer, D., *Tax and Corporate Governance: The Influence of Tax on Managerial Agency Costs*, (2014), Columbia Law Working Paper No. 491, 2.

revenue authorities such as HMRC[8] within the purview of enlightened shareholder value or stakeholder considerations. Additionally, if one were to consider the redistribution of wealth from the tax collected; the Pigouvian taxes against negative externalities; tax treatment of bribes; and the research suggesting that good tax management can be a driver for long-termism,[9] taxation may even be argued as relevant to Corporate Social Responsibility.[10]

2. REGULATORY EFFECTS

The current CIT system is a hybrid realisation-based income tax separately levied on corporations at rates unrelated to those of shareholders.[11] The philosophy behind this decision to tax is the modern understanding that a corporation is a real entity separate from its owners as opposed to merely an aggregate of its owners or a creature of the state.[12] This understanding of a company,which is contested in corporate governance literature[13] has two justifications: the first is that independent corporations have separate ability to pay; and secondly that taxation is required to control and regulate the power of management.[14] The regulatory consequences are elucidated fully by Correia,[15] I shall merely outline the concepts.

The deterrent effect regulates the accuracy (and thus fraudulence) of accounting due to the tension and comparability of tax and financial accounting. A separate corporate tax on corporate profits works as a friction against the propensity for corporate management to seek investment by reporting inflated profits or reduced losses for investment purposes, and makes wrongful tax disclosure easily identifiable. This has obvious market benefits as well as improving the quality and accessibility of company information which is crucial for mitigating agency problems. Yet the opposite can also be true - where the need for greater tax and book conformity induces firms to report less

---

[8] (In the UK) Her Majesty's Revenue and Customs
[9] Op cit (5), 703
[10] See: Freedman, J., *Tax And Corporate Responsibility*, (2003), Tax Journal 695, 2. ["Tax has figured surprisingly little in this [CSR] debate"]
[11] Correia, M., *Taxation of Corporate Groups*, (2013), Kluwer Law, 9
[12] Barker, W., *A Common Sense Corporate Tax: The Case for a Destination-Based, Cash Flow Tax on Corporations*, (2012), Legal Studies Research Paper No.1-2012, 46, 47; Also in: (2012) 61 Catholic University Law Review 4.
[13] *See*, for example: Millon, D, *Theories of the Corporation*, (1990), Duke Law Journal 1990:201; O'Kelley, C, *Coase, Knight, and the Nexus of Contracts Theory of the Firm*, (2012), Seattle Uni. L. Rev. 35(4); Butler, H., *The Contractual Theory of the Corporation*, (1989), Geo. Mason U.L. Rev. 11(4), 99-123; and, *Merchandise Transport v British Transport Commission* [1962] 2 QB 173, 206-207.
[14] Ibid., 48
[15] Op cit (11), 23

accurately or conservatively such that shareholders are left with less reliable information.[16]

Next is the reversal of the clientele effect, removing the tax policy from shareholders or investors thus equalising diverse individual shareholder circumstances.[17] There is some evidence that CEO's in weakly governed firms are much more likely to maximise their short-term wealth[18] but since tax management has a long horizon, the disparities of shareholder's intentions is reduced. This additionally inhibits agency problems for example, if the management were also shareholders they would act selfishly for their own tax burden as opposed to the other shareholders or company itself.[19] (This relates to the issue of executive's equity incentives and pay-performance sensitivity discussed below).

Lastly, the control effect states that a separate corporate level tax allows society to limit or control corporate behaviour and managerial power.[20] The rationale is thus: levying a tax on corporate income slows down the accumulation of corporate resources which constitute the base of managerial power.[21] This also aids in the reduction of costs of monitoring the management. These tax considerations may encourage management to make fiscal decisions on behalf of the shareholders that are contrary to the long term interests of the company or *vice versa*. For example, management may be induced to act inefficiently by retaining assets beyond the optimal period or selling them before the optimal time under the so-called lock-in or lock-out effect.[22] (It should be noted that this somewhat makes assumptions on the incidence of CIT.[23])

[16] Hanlon, M., Maydew, E., Shelvin, T., *Book-Tax Conformity and the Information Content of Earnings*, (2005), U. Mich. Working Paper.
[17] Levmore, S., Kanda, H., *Taxes, Agency Costs and the Price of Incorporation*, (1991), 77 Virginia Law Rev., 211, 213
[18] *See:* Bertrand, M., Mullainathan, S., *Are CEOs rewarded for luck? The ones without principles are*, (2001), Q. J. Econ. 116, 901-963; and, Gravey, G., Milbourn, T., *Asymmetric benchmarking in compensation*, (2006), J. Fin. Econ. 82, 197-225
[19] Op cit (17)
[20] Avi-Yonah, R., *Corporations, Society, and the State: A Defense of The Corporate Tax*, (2004), Va. L. Rev. 90(5), 1244
[21] Ibid., 1247
[22] Op cit (11), 14
[23] Whether the burden of the corporate income tax falls on capital, labour or consumption is an unsettled issue in the tax literature.

3. OVER-LEVERAGING AND THE MARKET FOR CORPORATE CONTROL

The beneficial treatment of debt over equity by the tax code is a further consideration for corporate governance. Corporate debt plays an important role in monitoring management and thus reducing agency costs.[24] There are substantial non-tax costs to over-leveraging which results from favourable treatment of debt.[25] Added debt may increase the risk of financial difficulty and bankruptcy and will affect credit ratings[26] - this will have a knock-on effect on the "company and its members as a whole".[27] It may restrict the management flexibility however, the requirement of repayments may also encourage prudent and efficient practice. Jensen argued that the increased commitments to pay interest serves as an incentive to elicit greater efforts from entrenched mangers.[28] Schizer agrees that the need to pay interest pressures managers to generate earnings, and with regards to agency costs, bankruptcy can be more costly for managers than shareholders.[29] This means debt (and thus the prospect of bankruptcy) can motivate managers to perform better. Schizer posits that these factors could help explain why share prices habitually rise when firms issue debt to buy back equity.[30]

The more favourable treatment of debt than equity, and other tax policies can encourage or dissuade takeover (or M&A) activity and may entice firms to pursue ill-advised debt-heavy acquisitions. Tax law can stifle growth if it inhibits flexible business restructuring and "should not be setting the parameters in the market for corporate control".[31] The US for example, imposes a Pigouvian tax on 'golden parachutes', or payments to managers when their employer is sold.[32] The fear may be that managers will not drive a hard enough bargain and too willingly accept acquisitions.[33] This tax may penalise managers for a deal premium that benefits shareholders, and impose costs on the

---

[24] *See:* Jensen, M., *Agency costs of free cash flow, corporate finance and takeovers*, (1986), Am. Econ. Rev. 76, 323-329; and, Grossman, S., Hart, O., *Corporate financial structure and managerial incentives*, (1982) in: McCall, J., (Ed.), *The Economics of Information and Uncertainty*, University of Chicago Press, 107-140

[25] Interest accrued on corporate debt is deductible from corporate profits. Therefore, to the extent of interest payments, the profit earned through the use of debt is not subject to corporate tax.

[26] See: Edwards, C., *Replacing the Scandal-Plagued Corporate Income Tax*, (2003), Policy Analysis 484, 1-44

[27] Companies Act 2006, s.172(1) (UK)

[28] Op cit (24)

[29] Op cit (7), 17 - "Senior executives are likely to lose their jobs and could have trouble finding another […] managers of levered firms might shy away from especially risky investments."

[30] Shah, K., *The Nature of Information Conveyed by Pure Capital Structure Changes,* (1994), 36 J. Fin. Econ. 89. See: Ibid.

[31] Op cit (26)

[32] Op cit (7), 12

[33] Leebron, D., *Games Corporations Play: A Theory of Tender Offers*, (1986), 61 N.Y.U. L. Rev. 153, 183 n.105

firm instead of on management.[34] "Inversions" also repeatedly made the news in 2014 on both sides of the Atlantic, even under the guises of patriotism and corporate responsibility.[35] The process of a U.S. entity that has been the multinational's parent becoming a subsidiary of a new non-U.S. parent is made to reduce tax obligations.[36] This arguably allows [ex-]US companies to be more competitive in the global marketplace however, shareholder protections can change depending upon where the new firm is incorporated and what its new charter provides.[37] The initial choice of entity or whether to incorporate has always presented a tension between corporate governance and taxation; that tension now permeates through the global platform of corporate ownership. Again, tax affects multiple areas of the governance of companies, for better or worse.

There may be a policy consideration for the legislator as the incentive to add debt is stronger when corporate tax rates are high.[38] (Yet, this incentive is weaker when the firm already has enough debt to shelter its profits).[39] This likely contributes to international tax planning, whether it be thin capitalisation, profit shifting or the use of foreign tax credits.

4. TAX AVOIDANCE, MANAGEMENT REMUNERATION AND COMPOSITION

The benefits of tax avoidance can be economically large[40] and tax avoidance can be a relatively inexpensive source of financing.[41] Whether a duty to avoid tax exists is worthy of a thesis itself and is rather too expansive for this paper's limits. The matter rests on the interpretation of domestic company law regarding the directors' duties. In the UK, the

[34] "Section 4999 imposes a 20% excise tax on "excess parachute payments," which generally are the excess over three year's salary.[…] Section 280G disallows the firm's deduction for excess parachute payments (as well as payments "grossing up" managers for the excise tax)." Op cit (7), 13, 25. (Also option for "greenmail" tax to discourage techniques managers use to resist acquisitions.)

[35] See: <http://www.accountingtoday.com/news/tax-essentials/patriotism-corporate-responsibility-politics-tax-inversion-controversy-73281-1.html>; and, <http://www.ft.com/cms/s/0/b66af9ae-429f-11e4-9818-00144feabdc0.html>.

[36] Desai, M., Hines, J., *Expectations and Expatriations: Tracing the Causes and Consequences of Corporate Inversions*, (2002), 55 Nat. T. J. 410

[37] Kun, O., *Corporate Inversions: The Interplay of Tax, Corporate, and Economic Implications*, (2004), 29 Del. J. Corp. L. 313

[38] Graham, J., *Taxes and Corporate Finance: a review*, (2003), 16 Rev. Fin. Stud. 1075

[39] Han Kim, E., *Optimal Capital Structure in Miller's Equilibrium*, in: Bhattacharya, S., Constantinides, G., eds. (1989).

[40] *See:* Scholes, M., et al., *Taxes and business strategy*, (2009), Prentice Hall

[41] See: Armstrong, C., et al., *The incentives for tax planning*, (2012), Journal of Accounting and Economics, 53(1), 391-411

'Farrer opinion'[42] concluded that it was not possible to construe a director's duty to promote the success of the company as constituting a positive duty to avoid tax. This concluded with a suggestion for companies to issue a formal policy document[43] regarding its approach to responsible corporate taxpayer conduct providing factors that the directors must take into account when promoting the success of the company.[44] The issue is fraught with definitional hurdles. What constitutes tax avoidance or responsible conduct are added on to the list alongside 'success'[45] and 'the company'. Underhill responded by saying that if it means directors have no fiduciary duty to their shareholders to avoid tax, this position is no more defensible than stating they should pursue every opportunity to save every penny of tax.[46]

The opportunity for tax avoidance could be removed with sweeping reform so that the initial premise is nullified.[47] Or one could accept currently, there is no legal duty to avoid tax, however it would be amateurish to not consider lowering one's tax burden for the profit of the company but only following a cost-benefit analysis in relation to the risks (financial and reputational). It would be expected that companies take advantage of low risk legislative tax incentives such as the Patent Box regime to incentivise commercialisation in the UK. And *this* is the important tax consideration for corporate governance: "[It] is not a question of whether or not a corporation should seek to minimise its tax burden, but more an issue of the Board's responsibility to assess the financial and reputation risks associated with any particular tax strategy."[48] Aggressive tax planning can create significant financial risks (adjustments, legal fees, penalties etc.) as well as repercussions for reputations.[49] In general, shareholders have reason to value tax planning even more than managers, since shareholders do not bear the same downside risks.[50]

---

[42] Farrer & Co, *Fiduciary Duties and Tax Avoidance, Opinion*, (2013), Tax Justice Network, 1, <http://www.taxjustice.net/cms/upload/pdf/Farrer_and_Co_Opinion_on_Fiduciary_Duties_and_Tax_Avoidance.pdf> accessed 07/14.

[43] Although, potentially an oath may suffice for SMEs? This idea of an oath has been proposed for the banking industry in lieu of the global financial crisis, see: Shah, A., *Bankers should look eastwards for ethical guidance*, (2014), The Conversation, <http://theconversation.com/bankers-should-look-eastwards-for-ethical-guidance-27747> accessed 07/14.

[44] Op cit (42), 6

[45] Issues such as: Short-term or Long-term?; or, for the entity, shareholders, stakeholders or the corporate group? etc.

[46] Underhill, W., *Tax and Directors' Fiduciary Duties*, (2013), Company Secretary's Review 37(14), 105

[47] *See:* Devereux, M., de la Feria, R., *Designing and Implementing a Destination-Based Corporate Tax*, (2014), OUCBT Working Paper 14/07

[48] Op cit (6), 2

[49] Ibid.

[50] Op cit (7), 34

(Schizer writes that if the firm is caught being too aggressive, shareholders are unlikely to bear high reputational costs, while managers could lose their jobs and even go to jail.[51])

Minnick and Noga note that tax planning can be a complex and opaque possibility for managerial opportunism and may have long and short term benefits or costs.[52] Their study concluded that governance plays an important role in tax management; companies with different governance structures choose different tax management strategies.[53] Higher (long-term) pay-performance sensitivity provides incentives for directors and CEO's to focus on better tax management.[54] Rego and Wilson found that firms where managers have high risk-taking equity incentives engage in more tax avoidance:[55] management expect greater personal payoffs from increased tax avoidance.[56] Corporate governance mechanisms may therefore wish to consider methods of tackling this problem whereby high levels of risk-taking equity incentives have the potential to motivate managers to over-invest in tax avoidance relative to the level desired by shareholders.[57] In general managers should earn more for doing good work, but equity compensation can motivate executives to raise the stock price - this may tempt managers to use accounting gimmicks or even fraud.[58] Other forms of compensation can also encourage risk or create different incentives even if managers tend to be more risk-averse than shareholders.[59] The right mix of stock, options, and bonuses then, depends on a broad range of context-specific factors; one-size-fits-all answers will not be optimal, and are sometimes flawed.[60] Tax rules can also weaken the constitution of the board itself. In Germany, director compensation is only partially deductible (as a way to keep it from serving as disguised, and thus untaxed dividends).[61] Schön suggests that this rule discourages firms "from hiring and paying high-class people" for the board.[62]

A 2014 study suggested that more financially sophisticated and independent boards recognise the potential agency problems that would otherwise give rise to extreme

---

[51] Ibid.
[52] Op cit (5), 703
[53] Ibid., 717
[54] Ibid.
[55] Rego, S., Wilson, R., *Equity Risk Incentives and Corporate Tax Aggressiveness*, (2012), Journal of Accounting Research 50, 775-810
[56] Armstrong, C., et al., *Corporate Governance, Incentives, and Tax Avoidance*, (2014), 22, available at <http://ssrn.com/abstract=2252682> accessed 07/14.
[57] Ibid.
[58] Op cit (7), 7
[59] Ibid.
[60] Ibid.
[61] Op cit (7), 32
[62] Schön, W., *Tax and Corporate Governance*, (2008), 60

levels of tax avoidance and thus they constrain manager's tax avoidance decisions.[63] They also contrast previous studies, finding that corporate governance appears to be related to managers' tax avoidance decisions, but only for high levels of tax avoidance.[64] Robinson reported evidence that the proportion of accounting experts on the board is associated with more general, but less 'risky', tax planning.[65]

Despite modern literature which posits that the relationship between board composition and performance may be tenuous,[66] tax education has the ability to improve company performance. Perhaps reform to the provision of directors' duties regarding diligence (care and skill) so that either a working knowledge of tax law or the compelling of directors to seek tax advise could therefore be included. And as stated earlier, within the UK concept of Enlightened Shareholder Value and the shift, academically, towards stakeholder-centric pluralism[67] - inclusion of HMRC as a group with an interest in the affairs of a company that can be affected by the activities of the business in supporting society beyond its shareholders, is certainly a valid argument that is yet to be expounded.

However, the biggest problem from this author's point of view is that by acknowledging the extensive research in this area into corporate governance codes or legislations, it affirms the economic fact that there is an optimum level of tax avoidance. An efficient locus that changes from company to company and from quarter to quarter that balances cost and benefit. The regulators and the government seek complete tax compliance and would therefore never adopt or condone legislation for governance that encourages efficient tax avoidance.

5. CORPORATE SOCIAL RESPONSIBILITY

The possible collusion of tax avoidance and corporate social responsibility regulation has been briefly discussed by leading tax academics.[68] A recent study concluded that firms with excessive, irresponsible CSR activities have a higher likelihood of engaging in tax sheltering activities, lending credence to the idea that corporate culture affects tax

---

[63] Op cit (56), 3
[64] Op cit (56), 4
[65] Robinson, J., et al., *Tax Planning and Financial Expertise in the Audit Committee*, (2012), Uni of Texas Working Paper.
[66] "There is not a single optimal structure; rather, that structure depends on the industry." See: Bhagat, S., Black, B., *The Uncertain Relationship between Board Composition and Firm Performance*, (1999), Business Lawyer 54, 921-963; or: "Boards vary with characteristics of the company." Coles, J., et al., *Boards: does one size fit all?*, (2008), J. Financ. Econ. 87, 329-356
[67] See for example: Freeman, R., *The Politics of Stakeholder Theory*, (1994), 4 Bus. Ethics Q. 413.
[68] See: Avi-Yonah, R., *Corporate Social Responsibility and Strategic Tax Behavior*, (2006), Law & Economics Working Papers Archive 2003-2009; and Freedman, J., at Op cit (10), for example.

avoidance.[69] Fisher, regarding the U.S., wrote in 2014 that the doctrine of corporate social responsibility provides a logical rationale for multinational corporations to adopt anti-avoidance practices.[70] She argues that the same mechanisms that helped turn environmentally sustainable and human rights practices[71] into corporate social responsibility "norms" can be implemented to lead multinational corporations away from tax avoidance practices.[72]

There are many other areas of tax which deserve mention for infringing into the realms of CSR. (Interestingly, in India there is currently debate over whether CSR spending made by companies should or should not be tax deductible.[73]) But I am constricted by word limits so, offer merely a few examples of the amalgamation of tax law, corporate practice and CSR. As a result of the OECD's work on the bribery of foreign officials, all OECD countries deny a tax deduction for bribes and other illegal payments, thus increasing the cost of such payments.[74] There are definitional problems with the term "bribe." Sometimes a payment may be tantamount to a gift or potentially it is merely an unwritten local custom that is uniformly observed without legal consequence. The bribe however, is usually conducted without the knowledge of the Principal, and may allow action which is counter to the interests of the Principal.[75] It may also cause market distortions, aid monopolisation and if revealed, lead to 'observable and unobservable' costs.[76] Discouraging bribes is an example of the two legal disciplines converging via anti-bribery legislation written into company and criminal law, and the utilising of tax mechanisms as a financial disincentive. This success can be compared with the inability to tax or alter the performance of mangers where utility is gained but may be unquantifiable. It is hard to tax the utility that managers derive from light hours, long lunches, lavish offices, and nepotistic hiring practices.[77] Unfortunately, though a manager may favour these benefits, they are hard for shareholders to see[78] and the cost or benefit, risk or

---

[69] Hoi, C.K., Wu, Q., Zhang, H., *Is Corporate Social Responsibility (CSR) Associated with Tax Avoidance? Evidence from Irresponsible CSR Activities*, (2013), Accounting Review (Forthcoming), available at: <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2280558> accessed 07/14.

[70] Fisher, J.M., *Fairer Shores: Tax Havens, Tax Avoidance, and Corporate Social Responsibility*, (2014), Boston University Law Review 94, 337-338

[71] For example: "Consumer activism, investor influence, and voluntary corporate leadership"

[72] Op cit (70)

[73] Srivats, K., *CSR Spend: India Inc raise taxation issue with Jaitley*, (2014), The Hindu Business Line, available at: <http://www.thehindubusinessline.com/economy/policy/csr-spend-india-inc-raise-taxation-issue-with-jaitley/article6217924.ece> accessed 07/14

[74] Op cit (6), 2

[75] Op cit (42), 6

[76] Op cit (56), 1 - 'observable' (e.g., fines and legal fees) and 'unobservable' (e.g., excess risk and loss of corporate reputation).

[77] Op cit (7), 16

[78] Ibid.

reward is impossible to establish. Asserting that the tax system therefore encourages these activities is, I believe, tenuous.[79]

6. <u>Conclusion</u>

The paper presents a multitude of areas where tax has trumped corporate governance considerations and *vice versa*, such that their partition and disaffiliation is no longer defensible. Having an understanding of the issues discussed and other specificities of the tax code can be a useful safeguard of the wellbeing of a company; recent guidance recommends greater awareness in the boardroom of the importance of tax issues.[80] The tax system's regulatory functions deserve, in my opinion, greater recognition in corporate governance academia and practice. The inverse is additionally an unappreciated opportunity - to receive suggestions from the field of corporate governance expertise on reforms to the tax system to broaden tax authorities' constricted mission beyond revenue collection - providing a win/win situation whereby revenue collection is improved and companies are better governed in terms of profit and CSR.

There are problems, for example in tax planning and avoidance. Interpreting the remit of directors' duties is contentious and internationally varied, and crucially (in the author's opinion) efficient tax planning from the managers involves a degree of optimum, low risk tax avoidance which would not be approved by regulatory codes or legislators. However, when the two disciplines have a common goal, the combination of tax and corporate governance mechanisms can be far more effective together than individually. This will be increasingly important with CSR and sustainability where taxes may actually offer regulation to a large contingent at the lowest cost and highest neutrality,[81] thus imposing less impact to the governance structure and managerial pressures.

---

[79] Ibid. "Administrability also explains why the tax system does not tax some perquisites and thus inadvertently encourages them."
[80] Op cit (6), 2
[81] Op cit (4)