IAFEI QUARTERLY

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Message from the Chairman

From the start of this year, the International Association of Financial Executives Institute(IAFEI) has been very busy.

I am happy to note that Mr. Carlo Locatelli has been elected as IAFEI Treasurer and we welcome him to this very important role. Mr. Locatelli brings a wealth of experience as he has been the treasurer of ANDAF for many years and of the Italian Insurance Broker Association. With this, I wish to thank Mr. Saiful Haq Manan for the outstanding services he has provided IAFEI as Treasurer since 2016.

It is indeed an exciting year as IAFEI explores many opportunities to expand our members and partners globally. We have many projects underway and our Executive Committee Members are responding remarkably and continue to contribute to the success of IAFEI.

As we are fast approaching the date to the IAFEI World Congress in Matera, Italy on October 25-26, 2019, I encourage you to regularly check the IAFEI website at www.iafei.org to get updated information regarding this important event.

I hope you enjoy reading this 44th Issue of the IAFEI Quarterly and we would certainly welcome any suggestions you may have to help us improve this communication tool. You can share your views by sending an email to the IAFEI Secretariat at secretariat.iafei@gmail.com.

Sincerely,

EDUARDO “Ed” V. FRANCISCO
Chairman

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Tax Competitiveness: Business Relevance

by **Piergiorgio Valente**, *Chairman, IAFEI International Tax Committee, Founding and Managing Partner, Valente Associati GEB Partners / President, CFE Tax Advisers Europe*

Tax competitiveness or competitive taxation is increasingly attracting the attention of the business world and of tax policy makers. If nothing else, it is the area of taxation where the interests of both groups meet: Business needs a tax environment that allows it to grow, that knows to boost entrepreneurship with perspective. Equally, tax policy makers need business to flourish in order to increase their tax revenue and implement broader initiatives.

Lately the debate has become fiercer due to the rise of digital economy and new business models. Change in business must be met by corresponding change in tax policy to adapt the tax framework and ensure that it can promote current business. Under these circumstances, it is critical that both business and tax policy makers engage in the debate in an interactive manner. It is the opportunity for progress towards taxation that favors development and welfare.

What is a competitive tax system?

A competitive tax system can be defined as a tax system that is appropriate to enhance productivity and economic welfare and that contributes to raise living standards at a sustainable level and rate.

Yet, tax competitiveness is often seen from a narrow lens, focusing on the tax legislation. In this respect, "competitive" is used in the International Tax Competitiveness Index to refer to tax legislation that keeps marginal tax rates low. Assuming that in principle investment can be considered to the extent the cost of holding the capital exceeds the return after tax and risk costs, the marginal tax rate refers to the threshold situation where effective taxation of the return shall be determinant.

Which of the two types of competitiveness should then be sought?

In a 2011 report entitled "What is a Competitive Tax System?" , the OECD seems to clearly favor the broad notion of tax competitiveness.

In particular, in the aforementioned report, the OECD concludes that "if the competitive pillars of an economy are strong, it is generally more able to impose corporate income tax without discouraging investment." In other words, taxation should be treated as a constituent element of a broader landscape that reaches the whole of economy and the relevant legal system.

Twelve key pillars of competitiveness are identified: 1. institutions, 2. infrastructure, 3. macroeconomic environment, 4. health and primary education, 5. higher education and training, 6. goods market efficiency, 7. labor market efficiency, 8. financial market development, 9. technological readiness, 10. market

size, 11. business sophistication, and 12. innovation.

Furthermore, the tax system is found to have a significant impact to the majority of these pillars. Indicatively, the perceived fairness of the tax system, i.e. the just distribution of the effective tax burden on taxpayers, is held to promote tax compliance. Tax compliance in turn enables the effective collection of tax revenue with minimal resource allocation. Another example relates to effective tax administration that does not permit tax evasion while favoring cooperative relations with taxpayers. Effective tax administration is then an important advantage of a tax system.

The EU is also prioritizing the tax competitiveness debate, especially in the light of increasing international tax competition. Thus, in September 2018, the European Commission put forward a discussion paper entitled "Competitiveness and Tax Competition" to initiate the dialogue in the context of the Platform for Tax Good Governance. Centre of the discussion was how to use taxation for a more competitive Single Market.

In the discussion paper, competitiveness is approached as "an environment that promotes investment and innovation by businesses and allows them to compete in international markets, while also attracting investment from international companies." It is then acknowledged that the decision for the location of the enterprise involves a number of factors, beyond taxation, such as strong institutions, good infrastructure, skilled workforce, rule of law. Thus, at the EU level, tax competitiveness seems to be perceived in the broad sense, as well.

As a result, lowering the tax rates or limiting the tax base would not be sufficient to enhance the competitiveness of the Single Market. Instead, attention should be paid:

- to increase legal certainty, stability and predictability;
- to simplify tax legislation;
- to provide employment incentives;
- to prevent double taxation and resolution of disputes; and
- to reduce compliance burden.

Conclusions

What seems certain is that the debate shall continue to attract attention, and no less in the EU context. In this regard, a key question is whether the EU should seek to increase competitiveness of the Single Market on the basis of ex ante coordinated initiatives or Member States should be let to compete among themselves – hopefully – towards positive coordination.

On the one hand, it might be too early to pursue the first option, taking into account the unanimity required for the EU Member States to take decision in the area of direct taxation. On the other hand, the risk of delays entailed by the second option could have harmful effects on Single Market competitiveness, which should not be underestimated.

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[1] *Matthews, S. (2011), "What is a "Competitive" Tax System?", OECD Taxation Working Papers, No. 2, OECD Publishing, Paris, https://doi.org/10.1787/5kg3h0vmd4kj-en.*

[2] *European Commission, Platform For Tax Good Governance, Competitiveness and Tax Competition, Discussion paper for the Platform on Tax Good Governance, Meeting of 12 September 2018, https://ec.europa.eu/taxation_customs/sites/taxation/files/document_of_com_competitiveness_andtaxation_docx_en.pdf*

Piergiorgio Valente, Founding and Managing Partner, Valente Associati GEB Partners / President, CFE Tax Advisers Europe

RECESSION EXPECTED BY LATE 2020

by **John Graham**, *D. Richard Mead Jr. Family Professor of Finance, The Fuqua School of Business, Duke University and*
Philippe Dupuy, *Associate Professor, Accounting, Law and Finance, Grenoble Ecole de Management*

IAFEI (International Association of Financial Executives Institutes) and a group of partners among which Duke University and Grenoble Ecole de Management surveyed CFOs across the world. For the first quarter of 2019, the survey was running from 5th March to 29th March 2019.

- Two-thirds of CFOs predict a recession by the third quarter of 2020, according to the latest Duke University/CFO Global Business Outlook.
- Despite that prediction, CFOs expect capital spending and revenue to increase moderately this year.

The Global Business Outlook CFO survey has been conducted for 92 consecutive quarters and spans the globe, making it the world's longest-running and most comprehensive research on senior finance executives.

Recession Likely Next Year

Sixty-seven percent of U.S. CFOs believe that the U.S. will be in recession by the third quarter of 2020, and 84 percent believe that a recession will have begun by the first quarter of 2021. The survey found 38 percent of CFOs predicting recession by the first quarter of 2020.

A recession is on the horizon, but the expected start date for the next recession has been pushed back by 6 to 9 months, relative to what we heard in our previous survey. This likely reflects substantial economic uncertainty about the risks inherent in the global economy.

We asked the CFOs which economic variables will provide the most accurate indication that their own firms are experiencing a slow-down. Almost half (47 percent) of CFOs said they consider GDP growth to be one of the three most important indicators of their own firm's fortunes. Consumer spending (39 percent), commodity prices (31 percent) and interest rates (29 percent) were also highly-ranked indicators.

Outlook for 2019

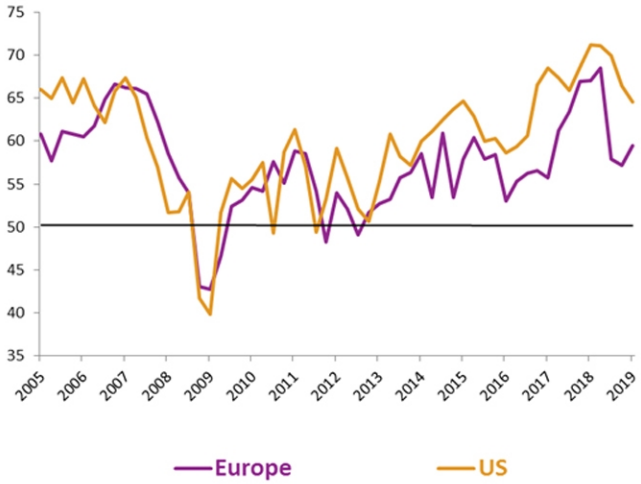
CFOs expect their capital spending and revenue to increase by 5 percent over the next 12 months. CFOs predict hiring to increase by 2 percent and wages to grow by 3 percent. Wage inflation has picked up due to the tight labor market.

Optimism Falls

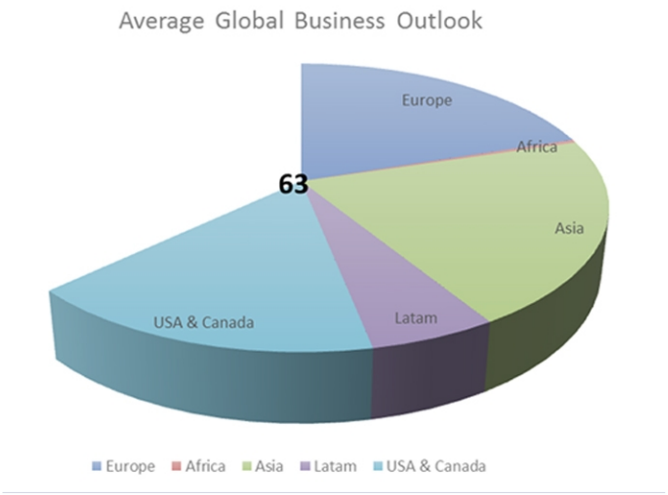
The Optimism Index for the U.S. Economy continued its downward trend, falling to 65 this quarter, down one point from December's 66 and down five points from the value in September 2018. Over the past 20 years, CFO optimism has averaged 60 on a 100-point scale.

The survey's CFO Optimism Index has historically been an accurate predictor of future hiring and overall GDP growth.

CFO survey: Optimism index



CFO survey: Optimism index



GDP weighed Average Global Business Outlook
(World Bank GDP constant prices in USD)

Global Results

Optimism outside the U.S. rebounded this quarter in many parts of the world. Optimism in Europe climbed two points to 59, on a scale of 0 to 100. Capital spending is expected to grow by about 3 percent and employment about 2 percent over the next year.

Optimism in Asia climbed sharply to 65 this quarter. Capital spending is expected to grow about 5 percent, and employment 3 percent, over the next 12 months.

Overall Latin American optimism is 65 this quarter. The Optimism Index is highest in Brazil, at 66, though it dipped three points since December. Optimism is 55 in Mexico, 65 in Chile, 66 in Peru, and 63 in Ecuador.

Business optimism in Africa climbed this quarter, though remains somewhat low at 55. Employment is expected to increase by 2 percent in Africa over the next 12 months.

The survey generated responses from almost 1,500 CFOs, including 469 from North America, 145 from Asia, 261 from Europe, 590 from Latin America and 42 from Africa.

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Duke's Fuqua School of Business / CFO Magazine Global Business Outlook

Results for 261 European firms (own-firm changes expected during the next 12 months)

	Mar 2019	Dec 2018	Sept 2018	Jun 2018	Mar 2018
Weighted Averages for	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months
Earnings growth*		6.2%	7.6%	3.1%	7.2%
Capital spending	8.5% Median=5.0%	2.2% Median=0%	1.5% Median=2.0%	6.2% Median=3.0%	7.0%
Advertising and marketing spending		0.7%	1.0%	4.5%	2.5%
Technology spending		3.5%	4.8%	6.6%	4.0%
R&D spending		1.7%	2.9%	1.4%	2.4%
Employment – full-time	1.8% Median=1.0%	1.6% Median=1.0%	1.6% Median=1.0%	2.9% Median=1.0%	-0.1% Median = 2%
Wages and Salaries	2.9% Median=2.0%	3.1% Median=2.0%	2.2% Median=2.0%	3.1% Median=2.0%	2.4%
Inflation (Chg in prices of own-firm products)		1.5%	1.2%	1.1%	2.8%
Health Care Costs		1.8%	0.7%	2.1%	1.1%
Revenue	3.5% Median=3.0%	5.4%	3.8%	8.3%	4.5%

* indicates public firms only. All other numbers for all survey respondents (including private)

European BUSINESS OPTIMISM

	Mar 2019	Dec 2018	Sept 2018	Jun 2018	Mar 2018
	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.
Optimism about the country's economy	More opt: 26.2% Less opt: 38.3% No chg: 35.5%	More opt: 11.0% Less opt: 54.9% No chg: 34.1%	More opt: 23.6% Less opt: 37.8% No chg: 38.6%	More opt: 38.4% Less opt: 22.2% No chg: 39.4%	More opt: 60.0% Less opt: 10.5% No chg: 29.5%
Country optimism level	59.5	57.2	57.9	68.5	67.0
Optimism about own company	More opt: 42.4% Less opt: 25.1% No chg: 32.5%	More opt: 32.1% Less opt: 33.3% No chg: 34.6%	More opt: 32.3% Less opt: 26.0% No chg: 41.7%	More opt: 45.9% Less opt: 24.5% No chg: 29.6%	More opt: 52.0% Less opt: 21.0% No chg: 27.0%
Own company optimism level	67.5	64.1	62.5	69.1	65.9

Results for 469 U.S. firms (own-firm changes expected during the next 12 months)

	Mar 2019	Dec 2018	Sept 2018	Jun 2018	Mar 2018
Weighted Averages for	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months
Earnings growth*		4.5%	12.8%	9.5%	8.5%
Capital spending	8.2% Median=5.0%	1.0% Median=2.0%	5.7% Median=5.0%	8.3% Median=5%	11.0%
Advertising and marketing spending		1.3%	3.6%	1.9%	3.5%
Technology spending		4.3%	6.3%	7.2%	9.0%
R&D spending		1.4%	2.7%	3.1%	3.0%
Employment – full-time	4.6% Median=2.0%	3.6% Median=3.0%	3.9% Median=2.0%	4.5% Median=3.0%	3.0%
Wages and Salaries	5.1% Median=3.0%	4.2% Median=3.0%	4.8% Median=3.0%	4.1% Median=3.0%	3.9%
Inflation (Chg in prices of own-firm products)		2.7%	3.0%	3.8%	3.0%
Health Care Costs		6.0%	7.8%	7.6%	7.2%
Revenue	6.3% Median=5.0%	4.9%	7.5%	6.9%	7.0%

* indicates public firms only. All other numbers are for all survey respondents (including private). The reported averages are weighted by revenue or number of employees, so that large firms are weighted more heavily.

Duke's Fuqua School of Business / CFO Magazine Global Business Outlook

	Mar 2019	Dec 2018	Sept 2018	Jun 2018	Mar 2018
	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.
Optimism about the U.S. economy	More opt: 24.1% Less opt: 36.8% No chg: 39.1%	More opt: 16.6% Less opt: 45.0% No chg: 38.4%	More opt: 43.6% Less opt: 23.0% No chg: 33.3%	More opt: 47.1% Less opt: 21.3% No chg: 31.6%	More opt: 53.3% Less opt: 16.4% No chg: 30.3%
U. S. optimism level (0 to 100)	64.6	66.4	70.0	71.1	71.2
Optimism about own company	More opt: 48.3% Less opt: 21.9% No chg: 29.9%	More opt: 35.1% Less opt: 32.7% No chg: 32.2%	More opt: 48.6% Less opt: 21.4% No chg: 30.0%	More opt: 54.0% Less opt: 17.3% No chg: 28.8%	More opt: 55.9% Less opt: 16.3% No chg: 27.8%
Own company optimism level	70.4	68.5	71.4	71.0	70.1

Results for 145 Asian firms (own-firm changes expected during the next 12 months)

	Mar 2019	Dec 2018	Sept 2018	Jun 2018	Mar 2018
Weighted Averages for	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months	Expected growth in next 12 months
Earnings growth*		6.4%	14.7% Median=5.0 %	5.7%	3.4%
Capital spending	11.0% Median=5.0 %	10.0% Median=3.4 %	4.6% Median=0%	7.0% Median=5.0 %	11.9%
Advertising and marketing spending		3.0%	2.5%	3.9%	10.5%
Technology spending		4.6%	4.1%	6.0%	8.5%
R&D spending		3.2%	3.8%	4.7%	8.0%
Employment – full-time	3.0% Median=1.0 %	2.0% Median=3.0 %	3.5% Median=2.7 %	3.6% Median=5.0 %	3.0%
Wages and Salaries	6.1% Median=5.0 %	2.2% Median=2.0 %	4.3% Median=3.0 %	4.1% Median=3.0 %	5.3%
Inflation (Chg in prices of own-firm products)		1.5%	3.6%	4.3%	4.5%
Health Care Costs		2.1%	2.4%	2.0%	6.0%
Revenue	10.4% Median=7.4 %	5.1%	6.7%	4.8%	9.5%

* indicates public firms only. All other numbers for all survey respondents (including private)
** numbers in the bracket are GDP-weighted results

ASIA BUSINESS OPTIMISM

	Mar 2019	Dec 2018	Sept 2018	Jun 2018	Mar 2018
	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.	Compared to last qtr.
Optimism about the country's economy	More opt: 47.4% Less opt: 29.6% No chg: 23.0%	More opt: 16.2% Less opt: 64.3% No chg: 19.5%	More opt: 21.8% Less opt: 43.4% No chg: 34.7%	More opt: 36.5% Less opt: 36.6% No chg: 26.9%	More opt: 40.9% Less opt: 26.3% No chg: 32.8%
Country optimism level	64.9	51.9	59.5	60.3	61.0
Optimism about own company	More opt: 60.7% Less opt: 19.3% No chg: 20.0%	More opt: 20.6% Less opt: 50.2% No chg: 29.1%	More opt: 20.4% Less opt: 35.7% No chg: 43.9%	More opt: 38.0% Less opt: 25.4% No chg: 36.5%	More opt: 39.8% Less opt: 29.6% No chg: 30.6%
Own company optimism level	69.6	58.8	59.8	64.8	61.2

DUKE THE FUQUA SCHOOL OF BUSINESS | CFO | DUKE CFO GLOBAL BUSINESS OUTLOOK | GRENOBLE ECOLE DE MANAGEMENT TECHNOLOGY & INNOVATION

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ASIA

To build resilience against global trade tensions, ASEAN's fate lies in its own hands

by Euben Paracuelles

by **Euben Paracuelles**, *Chief ASEAN Economist at Nomura*

Just when we thought the two largest countries in the world were close to an agreement to resolve the trade wars, tensions have re-escalated. The US raised the tariff rates of USD200bn worth of imports from China to 25% from 10% effective on 10 May. China retaliated and seems to have upped the ante on its rhetoric in response.

Financial markets reacted negatively, reflecting concerns that nobody wins in a trade war and the risk that it could derail global growth. The ASEAN region is not insulated, and will likely suffer more from rising risks of protectionism and de-globalisation. After all, ASEAN is home to some of the most open economies in the world including Singapore, Malaysia and Thailand, and is heavily reliant on exports.

Despite the dimming outlook as a result of the trade tensions, the ASEAN region has scope to respond to this threat and turn it into an opportunity to strengthen its own resilience over the long-run, regardless of when we get a clear resolution in the trade conflict.

First, trade diversion is starting to happen with companies operating in the US and China increasing their imports from elsewhere to avoid the tariff increases slapped on them by both countries. A study by Nomura late last year showed that of the top 10 countries in Asia that are potential beneficiaries from this "import substitution effect," six are ASEAN countries, most notably Malaysia, Thailand, and the Philippines. This is based, among others, on metrics such as the country's comparative advantage in products affected by the tariffs, geographic distance and existing trade linkages with both the US and China.

Beyond this short-term effect, multinational companies may eventually relocate their production facilities to suitable jurisdictions. Here, recipient countries can play a more proactive role in attracting foreign direct investment (FDI) via, for example, policies to liberalise ownership restrictions and improve the business climate. To some extent, this process of rising FDI inflows is arguably already taking place in ASEAN, in part because of ageing demographics in China and Japan. But the uncertainty brought about by the trade tensions may accelerate this process, creating an opportunity for ASEAN countries. The trick is to continue to implement the right policies and capitalise on "pull" factors such as the availability of low-cost labour, political stability and rising infrastructure spending. On this count, Nomura's Production Relocation Index shows that Vietnam, Malaysia and Singapore stand out to be potential winners, followed closely by Thailand, while Indonesia and the Philippines appear to be also catching up.

Second, ASEAN countries can trade more with each other. For a region that has a 50-

year old grouping with ambitions to build an economic community, ASEAN has a relatively small share of intra-regional trade at between 20% and 25%. To put this in perspective, this is less than half the equivalent share in the European Union, even after accounting for the fact that the EU is a monetary union. A well-known reason for this low ratio is that while tariff rates are already set at zero for nearly all ASEAN products, non-tariff barriers have remained, although maybe less so for more open economies such as Singapore and Thailand.

ASEAN, therefore, has plenty of scope to increase trade within the region. Breaking down trade barriers, complemented by freer movement of labour and capital, is an effective way for ASEAN countries to help lift each other's growth potential and strengthen resilience from broader external risks at the same time. ASEAN is very diverse not just in its levels of economic development, but also in its product markets (e.g., it has both commodity producers and large commodity importers), pointing to large benefits of increased trade. In addition, the region's total population of more than 630 million is home to some of the fastest-growing economies in the world, due in part to internal reforms that are gaining traction, such as in Indonesia and the Philippines. With growth this strong, demand for exports from within should naturally pick up.

The good news is that ASEAN leaders appear to be increasingly cognizant of this, and the sense of urgency has perhaps increased due to rising risks of protectionism from their two largest trading partners. ASEAN cannot control the outcome of the ongoing trade conflict, but it can do more to attract FDI and seize the opportunities from trade diversion.

The writer is Chief ASEAN Economist at Nomura. This article first appeared on May 28, 2019, in the Opinion pages of Business Times newspaper in Singapore.

Euben Paracuelles
Chief ASEAN Economist at Nomura

AFRICA

The Auditor: Quo Vadis?

by **Linda de Beer**, *Chartered Accountant, South Africa*

Introduction

In July 2018 a US Federal Judge awarded the biggest claim to against an auditor - $625 million. In the UK, partly fuelled by the Carillion failure, the regulator is considering the 'break up' of the Big 4 (Deloitte, EY, KPMG and PWC), by splittng the audit practices from the firms' advisory arms. The Bank of England also initiated an investigation against the Carillion auditor. In South Africa there was an almost overnight demise of KPMG, after reputational concerns led to not only a wholesale walk out of clients, but also an unprecedented retrenchment of staff across all levels.

These are examples of only three countries where the auditing profession is experiencing severe pressure. Similar pressures occur across many jurisdictions, ranging from audit firms being banned from audit for a period of time, massive monetary claims against auditors for corporate and alleged audit failures threatening the financial existence of firms, as well as audit regulators piling up more severe and restrictive rules on the audit profession.

These concerns, added to a myriad of other challenges such as the inability, after more than 40 years, to bridge the auditor expectation gap and the investment required of audit firms to stay ahead of the technology and information game, begs the question whether audit has become a sunset profession.

In 2016 Mervyn King, my South African countryman and colleague, who is internationally renowned for his work in corporate governance, asked me to write a book with him on the future of the audit profession. Then already, this auditor extinction threat was a matter of grave concern to us, especially the potential repercussions thereof on the effectiveness of capital markets.

Our objective was to bring important aspects regarding audit and auditors to the attention of business people, executive and non-executive directors alike, to assist in better understanding what audit is and what it is not. We also offered some ideas to ease concerns caused by unlimited auditor liability.

Key aspects of the book

The Auditor: Quo Vadis? provides a short history of the birth of accounting during the time of the merchants of Venice and thereafter the birth of the loan stock company that impacted to the need for auditors. Interestingly, the very original role of the auditor was to detect and avoid fraud. Over time this role changed and narrowed in a way, to that of an assurance provider on financial statements. However, despite many years of the audit profession trying to bridge the

expectation gap of what their statutory role is versus what the public at large expects this role to be, there is still an outcry after a corporate failure questioning 'where were the auditors'.

We also discuss the key threats that the audit profession is facing, affecting its ability to meet the demands of the 21st century, as further expanded upon in this article.

The demands of the 21st century on audit

The 4th industrial revolution

Many conversations and speculations surface on the future of jobs, skills, companies and even industries. The well-known company, Kodak, which is in a way still a household name (despite it being extinct now that we all have cameras in our smartphones and hardly ever print photographs anymore), was once the employer of more than 170 000 workers and sold 85% of the photographic paper in the world. IBM Watson, which can be described as a legal advisory algorithm, provides 'run of the mill' legal advice faster and more accurately than humans. Audit is considered as one on the fobs that will fall victim to technological unemployment in future. Audit firms are already 'off shoring' more routine audit work to centres in the East, where labour is less expensive and productivity higher.

Social justice

Decades after the phrase 'the auditor expectation gap' was first coined, it is still as high a cliff as ever. The expectation gap in short is the gap in understanding or expectation by users of financial statements, clients and society at large in respect of the audit service and the assurances that it provides versus the legal duty of an auditor. The largest gap is potentially in respect of the auditor's legal duty which does neither include the pro-active seeking and identification of fraud, nor a whistle-blower role to flag concerns in respect of the viability of the company, its business model and strategy.

One the one hand investors and the companies being audited are also seeking assurance on more than just financial statements, demanding a stronger commercial and value-add mind set in respect of big data and benchmarking information from auditors. Audit standards are not necessarily yet aligned to support auditors addressing these needs. On the other, social media and generational differences, clearly noticeable in the millennials, are putting auditors in a spotlight that was never shone on them by past generations. Social justice beyond legal compliance is the order of the day and has become the yardstick applied by society on the conduct of auditors.

These demands by business and society are adding costs to the structures within the audit firms and putting extra strain on already restrictive auditor independence requirements.

Ultimately all of this have a detrimental effect on the audit profession's ability to attract and retain the best and the brightest talent in the market – a luxury that belonged to the big firms in bygone eras.

Enhanced regulation

Enhanced regulation came about since the rise of the International Federation of Independent Audit Regulators (IFIAR), and its member bodies, as a reaction by governments to the corporate failures early in the 21st century (Enron, Woldcom, etc). This heightened regulation leads to pressure mounting on auditors, to enhance their technical and ethical competencies. Audit quality and auditor independence have become key focus areas of audit regulators and audit committees alike.

Audit firms, in particular the Big 4, are forced

to change their business and audit execution models to become more efficient and cost effective and to absorb the costs associated with regulation.

Restrictive independence rules also impact the business model of audit firms in so far as the provision of consulting services are concerned. Some audit regulators are giving serious consideration to 'audit only' firms, hence putting a ban on consulting services by auditors to their audit clients.

These rules put strain on the audit firms' investment in technology and skills development, but also create opportunities for pyramid staffing models and an environment where highly qualified and expensive skills can be more focused at the strategic and higher risk aspects of the audit.

Furthermore, regulators and society are calling for greater insight into audit firms, their quality control processes, disclosure regarding audit firm and engagement partner inspection findings and how the firms ensure independence. Some investors are even suggesting that audit firms should have their own financial statements independently audited and made publicly available and also have a minimum capital requirement to protect the firms against liability claims.

The litigation crisis

The auditor liability regimes in most jurisdictions are of such a nature that auditors are potentially liable for both criminal offences and civil wrongs. The trends with corporate failure has mostly been that companies, prefer to claim against auditors only for losses suffered, without considering the contributory roles that management, the board of directors and others have played. Audit firms, especially the Big 4, are seen to have deep pockets, both from and asset base and an insurance cover perspective, hence this practice.

This, added to the lack of apportionment of liability between joint wrongdoers linked to a corporate failure, mean that the full amount of loss being claimed from the auditor. This has resulted in settlement of litigation claims against the Big 4 over the past two decades running into billions of dollars.

A study in the UK indicated that a claim of between £600m and £1.2bn can potentially cause a Big 4 firm to fail, considering that damages claim are mostly settled at approximately 25% of the original claim.

Some strides have been made by individual auditor regulators in addressing the need for a limitation of auditor liability, either through statutory capping or apportionment. In our book we also present a view in respect of the need to implement an auditor judgment rule, similar to the business judgement rule (or reasonable director test), applied to company directors.

In conclusion

An audit is seen by many as a grudge purchase, and by some as a necessary evil. More and more investors are asking why an audit is still needed. An audit well executed though, is an invaluable seal of comfort for investors and other decision makers on a set of financial statements.

Quo vadis – where to? The audit profession is at a tipping point, running the risk of a sudden death and, in a way, becoming a dinosaur.

It will need to step up to meet the needs of the public it serves by addressing the credibility gap in so far as its role as protector of the public interest is concerned. Furthermore, the audit firms will need to rethink how it upskills itself, through its education and training models, transformation efforts and anti-competitive risk management. Without significant innovation in its business model, staff recruitment strategies and audit execution processes, the audit profession may not remain relevant in the 21st century.

About Linda de Beer:

Linda is a Chartered Accountant (South African) and holds a Chartered Director designation. She serves as an independent non-executive director on a number of South Africa listed company boards. She also acts as a reporting and corporate governance adviser, is a member of the King Committee on Corporate Governance in South Africa, a visiting professor at the University of Johannesburg and a member of the Investor Advisory Group of the Public Company Accounting Oversight Board (PCAOB) in the US. She was previously the chairman of the Consultative Advisory Group of the International Auditing and Assurance Standards Board.

Linda de Beer
Chartered Accountant, South Africa

GREECE

Leaders manage their Energy, not Time!

by **Anastasios Rodopoulos**, *General Manager, HMA*
Area President EME, IAFEI

Most people complain how there isn't sufficient time or how they are always running behind the schedule. It shouldn't come as a surprise, because time is finite. However much they wish, the day cannot be lengthened or the hours cannot be stretched.

On the other hand, real leaders do not run a race against time; they do not burn the midnight oil trying to meet daunting deadlines. Instead, they manage their energy. With enthusiasm and verve, they fill each moment of time with perfection. So, how do they do it?

To manage energy is to conserve energy – to replenish and recharge yourself with positive energy so that your journey as a leader is filled with health, rigour and gratitude.

There are 4 energy sources in each one of you. If you manage them wisely, they can prove to be inexhaustible energy sources.

1. **Physical:** You may not believe it, but the first source of energy is your body itself. If you give your body sufficient sleep (8 hours), provide it good nutrition and keep it fit through discipline and exercise, it can help you manage energy.

2. **Emotional:** Next comes the emotional source of energy. Feed your feelings and trust your intuition. Spend time with your family and catch up with your friends from time to time. These time outs are very important for maximizing your energy levels.

3. **Mental:** Indulge in activities that stimulate your brain. They keep you happy, alert and efficient. Remember, energy creates energy.

4. **Spiritual:** Stick to your values and beliefs

and pursue your passion. A person driven by passion can create and manage his energy skillfully.

Here are some tips in which leaders manage their energy in their day-to-day life. You can too, if you adopt them!

• During long commutes, listen to your favorite music or read something positive. Or connect with old friends with whom you've been postponing a conversation for long.
• As far as possible, never carry work, home.
• Allot some time for regular meditation. Do rhythmic and deep abdominal breathing which would replenish your tired brain cells with life-giving oxygen.
• Set your morning alarm clock 20 minutes earlier. Use this extra time to your advantage by exercising or doing your favorite activities. As you stick to this routine, you may be surprised that you stay as alert at 5 pm as you were at 8 am.
• Hit the sack at the same time, every night!
• Instead of rushing through lunch in your cabin, once in a while, have lunch in the canteen along with the people who work for you. Talking about people's families and their dreams creates a bond of trust and spreads positive energy.

People talk about time management all the time. However, it is only energy management that really counts. And leaders do it, efficiently.

Installing a Growth Mind-Set

Alexander the Great tamed a wild horse at age 13. Mohammed Ali won 19 of 19 Boxing Matches by Knockout between the age of 19 and 21. Bobby Fischer was playing chess at age 6. Mozart wrote his first symphony at 8.

Everything I know from experience about achievement in life or in business, whether it be my personal experience or that of others, tells me one very important thing. Success is difficult. Anyone who has achieved true sustainable success (even the crooks of the world) will surely attest to this. Every quick-fix pill out there!

Anastasios Rodopoulos
General Manager, HMA
Area President EME, IAFEI

SWEDEN

"We are not expecting a weak first half year"

Interview with **Mr. Carl Mellander,** CFO Ericsson-Group, Sweden, from Börsen-Zeitung, Frankfurt am Main, Germany, article provided by GEFIU, the Association of Chief Financial Officers Germany, the German IAFEI Member Association.

Mr. Mellander, Ericsson is still writing read numbers, but so far it has grown for the first time since years in 2019. Has it been possible to push the growth at the Mobile World Congress this year with additional orders?

We are talking already since long about 5G, but in this year we experience for the first time a strong demand for this new network-technology. 5G has become in a way a commercial reality. We have started in many regions to build up this new network-technology, especially in North-America, in Australia, partly also in Asia and in Europe.

Where in Europe?

Swisscom is an example in Europe. And we have won further orders in Middle-East, for example Etisalat or Tele2 in Russia as well.

Will sales also grow in 2019? The competitor Nokia was warning recently for a weak first half year, how are things looking for Ericsson?

We are not expecting a weak first half year 2019. Indeed, business is presently going well, especially in North-America, where the telecom-network-operators have already issued 5G-orders and are building them. This in a way is the first wave. The second one will then come in Japan, South-Corea and China, Europe will follow as third wave. Here, capital expenditures are deferred among other things because Spectrum has not yet been distributed.

What do you expect for 2019 then?

The total market for new network-technology is said to increase in the current year by 3 %. This is encouraging because the market researcher Dell'Oro, on the forecasts of which the industry is counting, has recently increased his expectations from 2 to 3 %, and we will participate in this accordingly.

The CEO Börje Ekholm has said that gaining back market share continues to be the most important objective, and Ericsson for this purpose has also envisaged so called "strategic contracts". What does that mean exactly?

Yes, we have indeed decided with the view to the total picture of our market-share to enter into such contracts, where we give away a little bit of margin, in order to secure the position for the future. Such compromises, however, are not reaching at all the order of

magnitude like in past years, where the industry underwent a painful hard competition for the “modernization of Europe”. We presently move very selectively.

This means, that your financial objectives are not impacted by this?

No, we want to show in 2020 an operating margin of more than 10 %, and more than 12 % in 2022, before restructuring-costs.

When will these restruction-costs have been digested, so that Ericsson will also make profits on an unadjusted basis?

We have had very high restruction-costs for years. This is true for Ericsson, but also for other corporations in the telecommunication-industry. In 2019, it will be again 3 – 5 billion Swedish Crowns. After this, however, we want to reduce this number to roundabout 1 % of turnover, or around 2 billion Swedish Crowns.

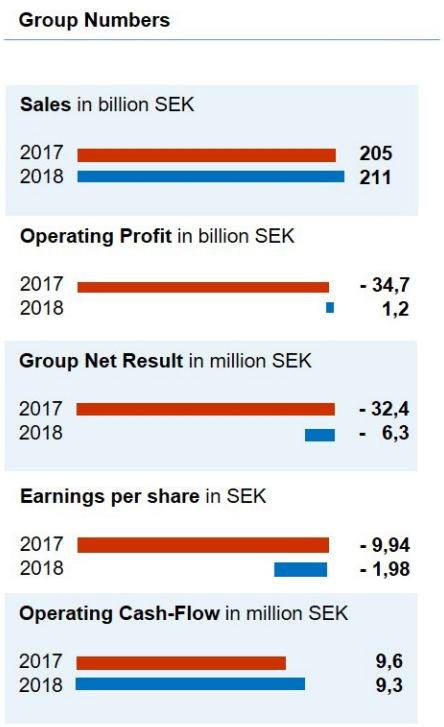
The demand for 5G develops very slowly in Europe. Formerly, it was customary in the industry to enhance sales with suppliers credits, for example when the UMTS networks were being built. Are you giving out such loans also for 5G and to what extent?

We are very active to arrange financings for our customers, but other than formerly we are incurring only a very limited own risk. We are working with banks, export credit suppliers, especially with the Swedish Export Credit Agency, which ordinarily is bearing the entire risk. Very rarely, we take over a very small portion of the loan, for a limited time. But we are engaging us not at all like in the times after the turn of the millennium, when supplier credits occasionally amounted to 150 % of the contract value.

Last year, the liquidity was your first worry, with a view to your balance sheet. How did it develop, and what is your target number?

We have gross cash reserves of 69 billion Swedish Crowns and net of 35 billion Swedish Crowns. This is a solid cushion which we need as long as we are still in this turnaround phase. We have achieved much, but we still have a section of our way before us. Moody’s has already recognized our progress and has changed the outlook “negative” to “stable”. The rating is still at “Ba2”. Investment grade we are presently only at Fitch, not at Moody’s and S&P.

Ericsson at a glance

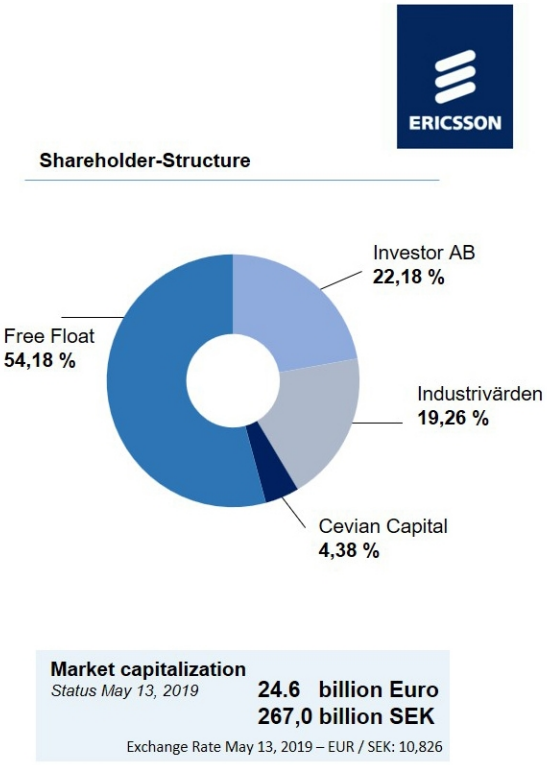


But this is your objective?

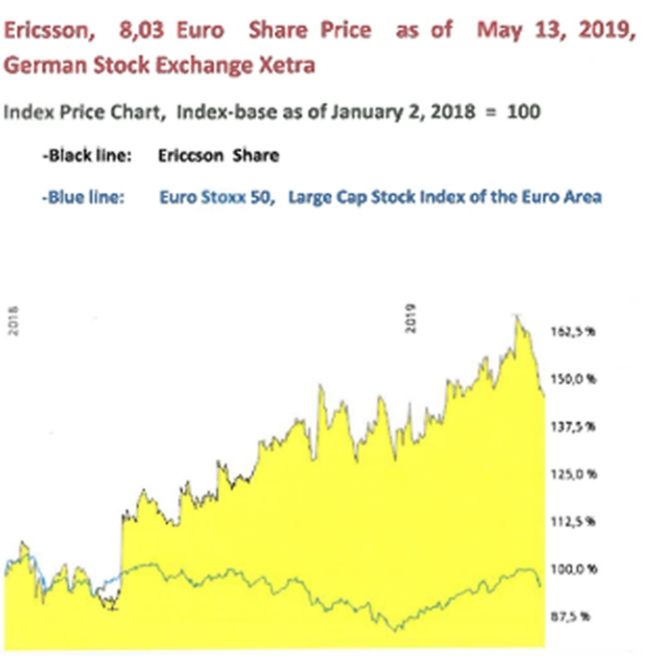
Yes, but not yet. At first, we want to be profitable again in 2020 and earn a strong free-cash-flow. After this, we will cope with the objective of investment-grade. This is a long term-objective.

What is a strong free-cash-flow?

At the free-cash-flow we are expecting in the year 2020 an order of size of 17 – 18 billion Swedish Crowns. At this, we exclude with our expectations possible acquisitions.



Source: Corporation, Thomson Reuters



You have just bought the antenna-business of Kathrein. Has this acquisition been financed from cash flow?

Yes, but this was a limited amount.

Will you in 2019 tap the bond market, in order to re-finance, or if applicable finance new acquisitions?

We are keeping the eyes open for acquisitions, where mostly we are looking at targets with which we can enlarge our portfolio. This industry is developing very quickly, sometimes one has to add to own competencies and technologies.

Will you tap the capital markets?

This is possible. Basically we are fully financed in 2019.

There are no maturities any more in this year, but possibly we will go to the market opportunistically, in order to re-finance debt which matures in 2021.

For this, we are looking as well at Euro as also to the US-Dollar market, because we are active in both currency-areas. In addition, we have taken up in the past year a loan from the European Investment Bank, a first tranch of 250 million Euro, which serves specifically the research and development at 5G. This, possibly, we will repeat.

With regard to the business units, which have been restructured in the past two years, also the business with the Managed Services especially and also parts of the Digital Services, are you through with this?

We have concluded a restruction program of 10 billion Swedish Crowns, already in mid 2018. But we are not yet ready with this. We have especially at BSS, a part of Digital Services, just started a restructuring, at which a part of the business will be completely abandoned. This is included in the restructuring costs planned for this year.

Is the business with Managed Services, where in the past losses have occurred and where contracts have been stopped or renegotiated, for the future an area, which Ericsson wants again to expand, or do you rather cut back here?

On the contrary, we are very satisfied with the business. It was profitable again in 2018 and it is very well positioned for the future. We are

investing here in automisation and in artificial intelligence as an example, where we then make a very good offer to the customers.

How are margins here typically?

They are lower than in the network business, however, also capital needs are lower here, the capital return here is thus looking very good.

One of the competitors is regarding the Enterprise-Business presently as very promising and has for this even just now established a new division. Especially in Germany it is said that soon on the basis of a local Spectrum, so called Campus-nets will be created. Will Ericsson also build such ones, for example for the large automobile-producers?

It is priority for us to support our customers, the telecom-network-operators. It is never a good idea to go into the market as competitor of the customers. It is imaginable that in individual cases we will also build networks for our corporate customers, for example platforms for the internet of things. But as a matter of principle we will rather endeavour to develop together with the telecom-network-operators business models at our corporate customers.

Well then, when will Ericsson again make profits, which will justify an increasing dividend?

It is our objective at first to reach a healthy profitability in 2020. It is my task to make sure that we attain the cash flow in order to pay the dividend which the shareholders want. I want to emphazise however, that our shareholders do accept the decrease of the dividend to the level of 1 Swedish Crown per share, and this now already for three years in a row.

The interview was made by Heidi Rohde.

About the person

Storm-proofed

Carl Mellander has taken over the position of the CFO at Ericsson in stormy times, in crisis-year 2016 at first as interim-manager. The 55-year old was chosen, who for the first time in 1994 became employed by the Swedish telecommunication equipment producer and who, apart from a brief departure, worked continually in different areas of the group, may be also because there, he had already experienced quite different crises. For example in 2002, when Ericsson stood at the brink and could be saved only with a billions heavy capital increase. Quite that badly it didn't go this time, but Mellander has nevertheless as guard of the finances no easy job. Always relaxed and with a sense of humour he lately commented the operating progresses which brought Ericsson in 2018 the turnaround at the sales, with the words: "We are on the right way, but we have not yet put the champaign in the refrigerator." This the critical finance expert will rather do only, when also at the bottom line black numbers will show up.

From Börsenzeitung, Frankfurt am Main, Germany, February 27, 2019. Responsible for English translation: GEFIU, the Association of Chief Financial Officers Germany, the German IAFEI Member Association, translated by Helmut Schnabel

ITALY

The Data Economy: On Evaluation and Taxation

by **Piergiorgio Valente**, *Chairman, IAFEI International Tax Committee, Founding and Managing Partner, Valente Associati GEB Partners / President, CFE Tax Advisers Europe*

While data-centred business models are claiming an ever-growing share of worldwide revenue, regulatory efforts to identify proper tax rules for the relevant activities are intensifying. It is questionable whether or not the proposals currently on the table capture the distinctive features of the data economy. The formulation of appropriate tax rules requires a thorough understanding of the mechanics of data processing activities and due consideration of the difference between information, which is an intangible asset, and tangible assets.

1. Introduction

It is widely acknowledged in the areas of business, legislation and policymaking, as well as administration and human rights protection, that the dominion of data is increasing.[1] This is clearly illustrated by the series of legislative initiatives launched and/or adopted in order to provide a legal framework applicable to the unstoppable flow of data.[2]

Data collection and analysis are not, however, new processes. In particular, data processing is deemed to encompass:[3]

> any operation or set of operations which is performed on personal data or on sets of personal data, whether or not by automated means, such as collection, recording, organisation, structuring, storage, adaptation or alteration, retrieval, consultation, use, disclosure by transmission, dissemination or otherwise making available, alignment or combination, restriction, erasure or destruction.

It is clear from this definition that data processing is an age-old procedure that underlies all economies. In fact, business and trade are borne from the observation of people's needs and preferences, i.e. from the collection of data, which is then analysed (by more or less automated means) to identify how best to address such needs and preferences.

What is different today is the technology used in data processing and the vast possibilities such technology promises. The virtual network of modern communication technologies enables the release and exchange of huge amounts of personal data every second on a global scale. Such data can be collected and recorded regardless of quantity, something that human memory and non-automated means of recording (such as documentation) could never achieve on their own. In addition, new technologies can analyse data effectively in different ways, as well as combine, summarize and draw conclusions from any quantity and type of data. And such conclusions can be communicated to any number of interested persons in a comprehensive and timely manner. Using artificial intelligence, such conclusions can also take the form of (i) decisions taken on behalf of decision makers, based on data analytics to evaluate alternatives and probabilities of success and considering the specific interests to be served or (ii) options of decisions, including pros and

cons. In other words, today, data is a key driver in the design of business strategy, whereas it used to simply act as a source of information.[4]

Although it is arguable that the intrinsic value of data used to be ignored, the increase in the amount of data, the ways of processing it and the potential of artificially intelligent systems to activate business processes on the basis of data analytics has turned data into a goldmine. The question of data evaluation is thus becoming more prominent, together with the issue of the proper and effective taxation of transactions involving data. Indeed, national and international policymakers are now concentrating their efforts on designing a tax regime for data-centred business models. A prime example is the European Commission's short-term proposal for a digital services tax on business, which draws its main value from user participation (through user data processing or user content exploitation).[5] Another line of development is being developed at an international level through the BEPS Inclusive Framework within the context of the effort to identify an appropriate system to tax the digital economy.[6]

In light of the above, the present article focuses on the evaluation of data and the urgent need to enact tax rules for the fair and effective taxation of income from data-centred business models. The article contains six sections. Section 2. illustrates some of the most common business models in respect of the data-centred economy. Section 3. aims to reconstruct the data-processing value chain, seeking to identify the different ways to extract value. Section 4. addresses the method used to assess the value of the data and the value drawn from data processing, while section 5. addresses tax regimes that have been proposed for the taxation of the data economy. Finally, section 6. concludes that a prerequisite to fair and effective taxation of the data economy is a thorough understanding of the data economy.

2. Data-Centred Economy: Business Models

2.1. Introductory remarks

There are various ways to extract value from big data,[7] create new value and capture value.[8] In recent years, which have been marked by digitalization, data analytics has become a core aspect of several industries, such as healthcare, retail, marketing and advertising, publishing, gaming, accounting, etc. These industries have become so data-focused that there is hardly an industry left that has not integrated big data analytics into its processes. If there is such an industry, it will soon be forced to change its practices.

There are three basic classifications of data-centred business models through which enterprises monetize big data. The distinction is based on the principal purpose for which the enterprise processes the data:

- differentiation of a company's offering;
- brokering of information; and,
- delivery of data exchange networks.

Under each category there are sub-classifications. Hence, businesses can differentiate their offering by (i) creating a completely new product or service; (ii) identifying new ways for the existing offer to create more satisfaction for the buyer; and/or (iii) ensuring more contextual relevance for the buyer during his experience with the existing product or service (i.e. have a more intense and positive effect on his feelings).

Information-based brokering might take place through(i) the sale of raw data; (ii) the supply of benchmarking services; and/or (iii) data analysis and the extraction of targeted input. Finally, networks can be delivered by (1) providing the (online) marketplace; (2) intermediating the conclusion of agreements between a provider and purchaser and (3) permitting marketing/advertising activity.

2.2. Differentiation – Online retail sector

The online retail sector provides illustrative examples of how data analytics can be used to differentiate the products or services

offered.

First, customer and potential customer data[10] is processed to identify market trends. The input that arises is then funnelled to the manufacturing department, which identifies a trend. Provided that the data analytics systems employed are fast and effective, the enterprise can respond in an informed manner to market needs at their peak, aligning production rate with foreseeable market demand and minimizing the risk of unsold items.[11]

Second, the retailer can differentiate the customer's purchase experience, for example, through tools combining the specific customer's data with other stored data. For instance, online fashion platforms seek to enable customers to virtually try on clothes that they are interested in buying.[12] Offer differentiation can also be achieved through the elaboration of the content created or released by users online for several other industries not connected with the one using the data to differentiate its offer.[13]

2.3. Brokering information – Benchmarking

It has been argued that the value of data is maximized at the time of sale.[14] Evidence of this is the sale of various databases that range from raw data to targeted multi-level data analytics.[15] Briefly, such databases gather data of interest to a specific customer target group and provide access to the data so gathered. It could also include data analytics services tailored to the customer's purpose or a combination of data with other data provided by the customer or stored in the database. Such services are, in principle, provided in exchange for a subscription or access fee. Apart from benchmarking databases, data can be sold, for example, the data of users of an online platform and/or the content created thereby.

2.4. Delivery of networks – Marketing

The third category of data-centred business models aims to extract value from the communication of data between the holder of the information and the interested purchaser/user. Such communication can lead to value for:

– a person who provides the communication route, or facilitates the meeting of the interested parties by providing a targeted context or marketplace, for example, a housing rental website;

– a person who facilitates the conclusion of an agreement between the interested parties, for example, by certifying the quality of the products/services of the provider or by enabling the collection and publication of customer input on products/services; and,

– a person who speeds up identification of the targeted product/service by the customer, for example, through the performance of advertising activities.

Marketing is one of the sectors that has benefitted the most from big data analytics. Advertisers can now direct their promotional activity to the targeted/interested customers, which saves costs and maximizes success. Interestingly, the advertiser can analyse the same data multiple times for multiple products/services to be promoted and from different angles.

3. Reconstructing the Data-processing Value Chain

From section 2., it is apparent that there are several ways to derive value during the different stages of data processing. Such value can also be derived multiple times from the same data source.

Identifying the persons that contribute to value creation and gain value from relevant processes and assessing the relevant value share is a condition precedent to designing suitable tax rules. The new business models have different mechanics than the brick-and-mortar economy in respect of which the current tax rules have been tailored.[16] It is therefore crucial to understand the new, data-centred ways of doing business to properly adjust the rules.

A breakdown of the activities performed under the business models outlined in section 2. would allow for the identification of the key players involved in data processing who can hence claim rights over such value. These key players include:
– the data subject, i.e. the user or consumer to whom the data refers (initial possessor of the
personal data–passive user) or who creates the digital content (initial holder of the content – active user);
– the provider of the automated data processing technology, including manufacturers and maintenance service providers that design and ensure the operation of the technology needed to process the data in a specific manner;
– the data collector, i.e. any person who employs the necessary technology and uses it in order to collect specific data for a business purpose;
– the data analyser, i.e. any person who disposes of the necessary technology and of the collected data and know-how and engages in specific data analysis or a data combination for a specific business purpose;
– the purchaser of the data or of the outcome of a data analysis process, i.e. any person who identifies a profit-making use of the raw data or of the conclusions drawn therefrom and seeks to use such information in order to create a new offer or enhance an existing one; and,
– the provider of any services relevant to data collection and processing, i.e. any person who activity enables, facilitates or speeds up the communication and analysis of the data.

Furthermore, it can be concluded that data processing, including digital content, involves various stages, as follows:
– ownership of raw data by the data subject;
– release of raw data from the data subject/user on a system/platform that can record it;
– recording and saving the individual data released by the system/platform, while applying the necessary data protection mechanisms;
– collection of the data by an appropriate system/platform;
– removal of data that can be considered useless;
– archiving and primary grouping of data;
– primary processing of the data collected in order to draw targeted conclusions, create new content or improve existing content;
– combining the conclusions drawn from a primary analysis of the data (or the content primarily created/ improved) with new data or conclusions from the processing of other data (or with different content) to draw further conclusions;
– use of the raw data or the conclusions drawn through an analysis of the data (at different stages) or of the content created or improved to differentiate a certain product or service;
– sale of raw data;
– sale of conclusions drawn from the elaboration of data at different stages of data processing; and,
– sale of content created or enhanced on the basis of data.

4. Location and Measurement of Value from Data

Having analysed the data processing value chain and the key actors in the data economy, the next step is to construct suitable tax rules to identify the place of relevant value creation and the rules to measure the value created. In fact, the central principle underpinning the ongoing overhaul of the international tax framework is that profit should be taxed where value is created.[17] This principle is the driver of the proposals on the taxation of the digital economy currently under discussion in the European Union[18] and internationally.[19] Value creation can be defined as the "process of creating something which did not exist before, of which the outcome is better than the closest alternative available, for which individuals are willing to exchange a monetary amount".[20] Unclear rules on this matter risk ignoring and leaving untaxed important value or enable transfer pricing practices that

allocate the value to the place where taxation is most favourable.[21]

Furthermore, the need for data evaluation can arise, for example, in the context of mergers and acquisitions, where the entities involved must be accurately evaluated or in the context of bankruptcy, where the assets of the entity need to be assigned a specific value.[22] In any event, being aware of the value of the enterprise's assets is a prerequisite to making investment decisions, enhancing the quality of the asset and drawing maximum benefit therefrom.[23]

The evaluation of data, however, is a tricky question due to certain special features that distinguish data from the assets of the enterprise. Such features may be deemed to coincide with the seven "laws" that have been identified in relation to information.[24] These seven laws differentiate information from other assets in terms of the application of the laws of economics:

– information can be shared infinitely without losing its value;
– share and use has positive effects on the value of information;
– time can have a negative impact on the value of information and the extent of such impact depends on the type of information;
– the more accurate a piece of information is, the more value may be assigned to it;
– the combination of different pieces of information can add value;
– the amount of information is not necessarily relevant to its value – in fact, it can imply a decrease in value; and
– information is not exhaustible with use but is a self-generating resource that increases through use.

The above factors imply that the known framework for the assessment of the value of assets cannot be applied, as such, to information, including data, but needs to be adjusted to take these differences into account.

In addition, as regards the location of value creation, it needs to be duly considered that data and information, in general, is an intangible asset.[25] This means that it is not of a physical nature and does not have a location per se.[26] Also, it does not have any value in and of itself due to its mere presence, which is the main difference in comparison to gold.

Owning data as an intangible asset does not imply profits and does not lead to returns. Something else must take place for the intangible to generate value and produce profit: it must be used.[27] In this respect, it can be concluded that value creation does not stem from ownership of the intangible asset of data but the exploitation activity, i.e. its development, updating, maintenance, protection, expansion, etc. In other words, amongst the players, identified in section 3. above, involved in data processing and having a claim on any value created are those taking part in the exploitation activity. It follows that the discussion on relevant allocation of taxing power is restricted to the jurisdictions where these players are located.

User contribution to value creation in the context of data-centred business models must hence be considered in light of the above conclusions. Such a contribution is deemed to fall within the heart of digital business activities and the special features thereof. New technologies have enabled (mere) consumers to be upgraded as consumers/producers. Yet, if the consumer is part of the value production, he should be entitled to claim part of the value, which would subsequently justify taxing rights of the jurisdiction where he is located.[28] In fact, there is currently a debate on the taxation of digital business centres that revolves around identifying the extent to which consumers/users actually contribute to the creation of value from data processing.

User contribution to value creation can be divided into two broad categories: passive and active contribution, which trigger a

different assessment from a valuation– and subsequently from a tax – perspective. On the one hand, active users are deemed to be those who provide digital content (for example, users uploading videos on YouTube or information on Wikipedia) or actively network (for example, users concluding contracts online for the purchase of products/services or users commenting on/rating the products they have purchased on an online retail platform). On the other hand, passive users include those who release their personal data, for example, on the online platforms they use, hence permitting them to be profiled and the platform to be expanded, through the accumulation of increased amounts of data. This second type of user is the most common.

In respect of active users, the user consciously puts effort into and produces content that is made available to the platform and its other users; thus, the value of the platform is increased as a result of the effort of the user. In respect of passive users, the main contribution of the user is the communication to the platform of personal data; there is no effort and there is no new content. Such personal data does not have a value on its own as a result of its mere ownership but can gain (important) value if elaborated on in a profitable manner. It is therefore clear that there is a difference in the level of contribution in each of these scenarios, which implies that their evaluation and subsequent taxation cannot be the same.[29]

Beyond the contribution of users, the same pattern can be applied in relation to other players involved in value creation from data processing. Their contributions must be distinguished and assessed on a case-by-case basis, taking into account the relevance of each contribution to the creation of the specific value. In this regard, it has been observed that recording, saving, collecting and the general grouping of raw data should not be considered to create significant value because this does not lead to new information. This is not the case in relation to other data processing activities, including targeted analysis, as well as combining and compiling statistics; such activities can lead to new content and actually create value.[30]

5. proposals for the Taxation of the Digital Economy

From a tax perspective, the special characteristics of the data-centred economy, and its growing share of worldwide revenue, have triggered a series of efforts to adjust the international tax framework to the data reality. The proposals for the taxation of the digital economy, including the data-centredbusiness models that are currently under discussion, have, however, been criticized repeatedly for not reflecting the above findings. These proposals include mainly:
– the EU Digital Tax Package, which encompasses two directive proposals, i.e. regarding the short-term provision of a digital services tax (DST)[31] and the long- term establishment of a digital permanent establishment (PE) concept;[32] and
– the OECD new nexus approach outlined in the context of the BEPS Final Report on Action 1.[33]

More specifically, the European Commission has suggested that the PE concept be extended to a significant digital presence, regardless of physical presence. Factors indicating such a significant remote presence would include:
– the number of users of digital services provided in a specific jurisdiction;
– the number of business contracts for the supply of digital services with users of a certain jurisdiction; and
– the annual business revenue from the supply of digital services to users of a certain jurisdiction.[34]

There is no distinction between active and passive users or in relation to the specific data processing activity performed. In addition, it seems to be highly debatable whether or not the existence of a user base,

where the use of digital services does not involve a charge to the user, should be considered evidence of substantial activity in a given jurisdiction. In this respect, it is argued that such a user base should be distinguished from a customer base, in respect of which there is a "transfer of financial means" and hence a real exchange of value.[35]

Similar remarks can be made in relation to the short-term solution promoted in the European Union, i.e. the application of a DST to specific business activities. These activities have allegedly been distinguished from others (falling outside the scope of the DST) on the basis that user contribution is at the core of relevant value creation. Based on this premise, DST would, in principle, be subject to additional conditions applicable to marketing, intermediation services and sales of user data. Once again, the type of user contribution does not seem to be relevant. Interestingly, the majority of the services identified do not refer to active user participation but to passive contribution through the release of the personal data of users.

At the international level, a relevant proposal has been made in the context of the BEPS Project.[36] A new nexus approach is in the preliminary stages of discussion and would achieve better alignment between value creation and taxation. This new nexus would take into account user contributions in identifying economic substance even in the absence of physical presence. The indicative factors differ from those in the EU digital PE case. They are, namely: (i) revenue generated from a certain jurisdiction (regardless of the connection with digital services); (ii) digital indicators, such as the existence of a local domain name, a local website using local language and the availability of local payment options; (iii) user-related factors, including the number of active users, the number of contracts concluded online with users from a certain jurisdiction, and the volume of data collected from users residing in a certain jurisdiction. Under the OECD proposal, however, the lack of a specific distinction between the various types of user contributions may be considered to have a marginal impact since user-based factors simply fall under one of three categories of indicators of economic substance. In any event, this solution is not considered workable at this point. It requires further elabora- tion,[37] which is expected to be concluded in 2020 with the release of a consent-based proposal by the more than 100 jurisdictions forming part of the Inclusive Framework.[38]

6. Conclusion

To sum up, this note has focused on the ever-growing data-centred economy and has sought to shed some light on the proper method for the evaluation of data and data processing activities. Such evaluation is a prerequisite to the attribution of taxing power in relation to data processing and the determination of the correct method to allocate such value amongst the different jurisdictions involved. To this end, this note examined some of the more dominant business models deemed to exploit user contribution in order to reconstruct the value chain thereof and the key players involved. It went on to provide some remarks on the application of taxation-at-the-place-of-value-creation principle in respect of the data economy and the content of the proposals on the taxation of the digital economy currently under discussion.

Information, including data, constitutes an intangible asset. Most importantly, the value of information, in principle, increases with its distribution and use, while the opposite is true for material assets. While use and diffusion of data adds value, such value added must be considered ad hoc, taking into account the particular circumstances of each case. Hence, the contribution of users of digital services may lead to more or less value for the respective provider depending on the type of contribution. Equally, data processing activities must be distinguished and

evaluated on a case-by-case basis, considering that certain activities tend to produce more value than others in the data economy context.

The European Commission has taken an important step forward in an effort to identify proper rules to tax value created over the web.[39] The OECD is moving in the same direction, although it is following different steps, starting from the 2015 Final Report onBEPS Action 1, continuing with the 2018 Interim Report and culminating in a commitment to release a consent-based final report on the matter by 2020.[40] With regard to the solutions proposed up until this point, it is arguable whether or not they sufficiently take into account the particularities of data as an intangible asset.

The data-centred economy needs to be understood plainly and thoroughly and this is a prerequisite to building an appropriate international tax system. Its unique characteristics demand an adjustment to the existing tax rules, i.e. a targeted elaboration on the rules in order to suit the new concepts. The variety of business models out there and the ongoing development of new means of user interconnection and participation demand flexible rules and a case-by-case examination.

In this respect, there are two important lessons to be learned from international taxation's past history. First, issues that have a cross-border reach, such as the activities of multinationals or the sharing economy, cannot be efficiently dealt with in a local context. New technologies have resulted in a global marketplace that is at odds with the existing fragmented international framework. Any solutions need to be widely acceptable in order to be enforceable. Second, regulatory action to establish the coordinates for the new activities must be timely if fragmentation is to be prevented and to ensure that the rules keep pace with the economy. If these steps are not taken, the tax world risks being led back to the pre-BEPS situation. This second time around, there will be no excuse for failing to keep up with economic developments.

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1. This is also acknowledged in the literature. According to Yuval Noah Harari, "science is converging on an all-encompassing dogma, which says that organisms are algorithms and life is data processing". This dogma lies at the foundation of the techno-religion alleged as distinguishing the modern era. Harari also contends that people "want to be part of [this] data flow, even if that means giving up their privacy, their autonomy and their individuality". See Y.N. Harari, Homo Deus: A Brief History of Tomorrow (Harvil Secker 2016).

2. By way of an example, the European Union, in April 2016, adopted the General Data Protection Regulation (GDPR) in order to address concerns regarding the protection of personal data (Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 Apr. 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC, OJ L 119 (2016), EU Law IBFD [hereinafter GDPR]). See B. Krähenbühl, Personal Data Protection Rights within the Frame- work of International Automatic Exchange of Financial Account Infor- mation, 58 Eur. Taxn. 8 (2018), Journals IBFD.

3. Art. 4 GDPR.

4. T.C. Redman, 4 Business Models for the Data Age, Harvard Bus. Review (20 May 2015), available at https://hbr.org/2015/05/4-business-models-for-the-data-age (accessed 29 Mar. 2019).

5. European Commission, Proposal for a Council Directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services (DST Proposal), COM(2018) 148 final (2018), EU Law IBFD.

6. Inclusive Framework on BEPS, Tax Challenges Arising from Digitaliza- tion – Interim Report 2018 (OECD 2018), available at https://bit.ly/2rX 9elD.

7. Big data is described as a "situation where the volume, velocity and variety of data exceed an

organization's storage or compute capacity for distinguishable and timely decision making" (Y. Perwej, An Expe- riential Study of the Big Data, 4 Int. T. Electr. Energy 1 (2017)).

8. The value captured must be distinguished from the value created. There is value creation whenever an action or course of action leads to a benefit that exceeds the cost. Although value creation is a pre-condition to value capture, it does not necessarily imply it. Capturing value is connected with the profit actually made by the enterprise and depends mainly on the selling price. M. Ryall, Don't Just Create Value; Capture It, Harvard Bus. Review (6 June 2013), available at https://hbr.org/2013/06/dont-just-create-value-capture-it (accessed 29 Mar. 2019); M. Lennard, Act of Creation: the OECD/G20 test of "Value Creation" as a basis for taxing rights and its relevance to developing countries, 25 TNCS 3 (2018).

9. R. Wang, What a Big-Data Business Model Looks Like, HBR (6 Dec. 2012), available at https://hbr.org/2012/12/what-a-big-data-business-model (accessed 29 Mar. 2019).

10. Such data may be gathered from sales, blogs and social media platforms.

11. J. Brownlow et al., Data and Analytics – Data-Driven Business Models: A Blueprint for Innovation. The Competitive Advantage of the New Big Data World (University of Cambridge 2015).

12. Another example is Project Muze, which enabled customers to design their own clothes online using artificial intelligence, the processing of data from the fashion industry and aesthetic parameters. See M. Veitch, Zalando relies on technology to aid fashionistas (IDG Connect 2016), available at https://www.idgconnect.com/idgconnect/interviews/1018942/zalando-relies-technology-aid-fashionistas (accessed 29 Mar. 2019); see A. Rietze, Project Muze: Fashion inspired by you, designed by code, The Keyword (2 Sept. 2016), available at https://blog.google/around-the-globe/google-europe/project-muze-fashion-inspir ed-by-you/ (accessed 29 Mar. 2019).

13. By way of example, journalists and bloggers can collect digital content and information available online in order to analyse it, elaborate on it and produce new content for their targeted readers. Similarly, soft- ware providers can use such content in order to produce new software or enhance the quality of existing software, feeding them an increased amount of information relevant to consumers.

14. A. Lewis & D. McKone, To Get More Value from Your Data, Sell It, Harvard Bus. Review (21 Oct. 2016), available at https://hbr.org/2016/10/to-get-more-value-from-your-data-sell-it (accessed 29 Mar. 2019).

15. Examples of such databases include Bloomberg and Bureau van Dijk.
See Wang, supra n. 9.

16. P. Valente, Taxless Corporate Income: Balance Against White Income, Grey Rules and Black Holes, 57 Eur. Taxn. 7 (2017), Journals IBFD and OECD, Action Plan on Base Erosion and Profit Shifting (OECD 2013), International Organizations' Documentation IBFD.

17. OECD, id.

18. European Commission DG TAXUD, Fair Taxation of the Digital Economy (2018), available at http://www.europarl.europa.eu/cmsdata/152963/Commission_powerpoint.pdf.

19. Inclusive Framework on BEPS, supra n. 6.

20. T. Theunis, Profit Allocation Based on Value Creation in the Digital Economy, HARN60 Master Thesis, Lund University (2017/2018).

21. Valente, supra n. 16.

22. J. Short & S. Todd, What's Your Data Worth?, MIT Sloan Management Review (Spring 2017).

23. Reply Glue, The valuation of data as an asset: a consumption-based approach, available at https://www.reply.com/Documents/13903_img_The-valuation-of-data-as-an-asset.pdf.

24. D. Moody & P. Walsh, Measuring the Value of Information: An Asset Valuation Approach, Seventh European Conference on Information Systems (ECIS), Copenhagen Business School (1999).

25. It has been held that information falls under the category of assets, since it: (i) has service potential or future economic benefit potential, (ii) is subject to control, and (iii) is a product of a transaction (three key ele- ments of an asset). Moody & Walsh, supra n. 24.

26. In addition, intangibles can easily be transferred through mere contrac- tual arrangements without the need for substantive action. This makes intangibles vulnerable to manipulation in the context of (aggressive) tax planning and hence they are not a reliable indicator of the place of value creation. See Valente, supra n. 16.

27. W. Haslehner, Taxing Where Value is Created in a post-BEPS (digitalized) world?, Kluwer International Tax Blog (30 May 2018).

28. To this effect, however, consumption taxes, including value added tax (VAT) should be duly taken into account.

29. T. Theunis, supra n. 20 and Haslehner, supra n. 27.

30. Y. Brauner & P. Pistone, Some Comments on the Attribution of Profits to the Digital Permanent Establishment, 72 Bull. Intl. Taxn. 4a/Special Issue (2018), Journals IBFD.

31. DST Proposal, supra n. 5.

32. European Commission, Proposal for a Council Directive laying down rules relating to the corporate taxation of a significant digital presence, COM(2018) 147, EU Law IBFD [hereinafter SDP Proposal].

33. OECD/G20, Addressing the Tax Challenges of the Digital Economy – Action 1: 2015 Final Report (OECD 2015), International Organizations' Documentation IBFD [hereinafter Action 1 Final Report (2015)].

34. Art. 4 SDP Proposal.

35. W. Schoen, International Tax Coordination for a Second-Best World (Part 1), 1 WTJ 4 (2009), Journals IBFD.

36. P. Valente, Digital Revolution. Tax Revolution?, 72 Bull. Intl. Taxn. 4a/ Special Issue (2018), Journals IBFD.

37. Other potential solutions that could be considered according to the Action 1 Final Report (2015) include (i) a withholding tax on remote sales (where the seller is not located in the country of the purchaser and the sale is concluded online) and (ii) an equalization levy appli- cable to non-resident enterprises with significant economic presence. The equalization levy would take into account the factors mentioned in sec. 5. as indicators of a digital PE, hence also user-related factors. It would nevertheless function differently from the EU DST: while the former would seek to remedy any differences in the tax treatment of resident and non-resident providers, the latter would seek to remedy the fact that user contribution is not sufficiently taken into account in allocating taxing rights.

38. OECD, Brief On The Tax Challenges Arising From Digitalisation: Interim Report 2018 (OECD 2018), available at https://www.oecd.org/tax/beps/brief-on-the-tax-challenges-arising-from-digitalisation-interim-re port-2018.pdf (accessed 29 Mar. 2019).

39. R. Petruzzi & V. Koukoulioti, The European Commission's Proposal on Corporate Taxation and Significant Digital Presence: A Preliminary Assessment, 58 Eur. Taxn. 9 (2018), Journals IBFD.

40. OECD, supra n. 38.

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