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# Four Visions of the Future: Scenario Planning for Tax Departments in Multinational Companies

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In this article, the author engages in a general scenario planning exercise and discusses how companies, particularly tax departments in multinational organizations, can use similar exercises to prepare for the future and improve their operations in the present.

In the late 1960s, a pair of innovative Shell executives began developing long-term planning reports that described distant "alternative futures" that might become reality in the decades ahead.[1] Not surprisingly, oil supplies, oil prices, and geopolitical conflicts involving oil-rich countries featured prominently in these futures. While it is standard practice today, scenario planning wasn't commonly embraced before Shell's exercise. Now, global tax policies and other tax trends feature just as prominently as energy prices, technological advancements, and other potential disruptors when leadership teams examine scenarios to better equip their organizations for an increasingly uncertain future.

The future of tax is now a major strategic concern for multinational enterprises. Global CEOs have begun to recognize that tax strategy can no longer be treated as merely a tax issue; it now qualifies as a genuine business issue of concern to the C-suite and the board.[2] Top executives also cite a growing tax burden and increasing tax complexity among the top threats to their organizations' growth prospects and globalization agendas.[3]

Tax has been thrust into the strategic spotlight. But what will global tax policies look like in the future, and how will corporate tax departments change as a result?

Scenario planning can help companies address this daunting question. Given the rising importance of tax issues in strategic planning activities, it makes sense for companies to integrate more tax expertise into scenario planning exercises. This was a prime impetus behind the Global Tax Futures (GTF) project, which used scenario planning methods and practices to produce two iterations of reports featuring four plausible scenarios for what the world will look like in 2035.

The purpose of this effort is to stimulate strategic conversations about these future scenarios and their likely effect on companies and their stakeholders. This article highlights four future scenarios and briefly discusses what each might portend for global tax policy and for tax functions.

For example, many governments are likely to face greater difficulty paying their bills in the decades to come, given demographic trends (that is, aging populations, particularly in Japan, Europe, and the United States). As a result, the need for tax revenue to service government debts seems likely to increase. But how will governments and taxing authorities generate this revenue? What types of taxes will be used? Transaction taxes are likely a major part of the answer, and this would comport with the global trend of moving away from an emphasis on

[1] Angela Wilkinson and Roland Kupers, "Living in the Futures," 91(5) *Harvard Business Review* 118-127 (May 2013).

[2] Deloitte Tax LLP, "The Global Tax Reset: Summary Results of the 2017 Annual Multinational Survey" (Aug. 2017).

[3] PwC, "20th CEO Survey: 20 Years Inside the Mind of the CEO . . . What's Next?" (2017).

corporate income tax toward a more active use of indirect taxes.

As tax leaders and their teams assume a more active role in corporate scenario planning activities, it is important to keep in mind that these efforts have highly practical applications. Companies routinely apply these practices and techniques to strengthen operational planning, budgeting, and forecasting activities.[4] It is also important to keep in mind that scenarios are not static forecasts but guideposts that necessarily move and evolve over time.

### How to Chart the Future

While there are different scenario planning methods, most organizational approaches follow similar steps and address the same three questions:

- What could plausibly occur?
- How would each future affect organizational strategy, planning, and investments?
- How would the organization respond?[5]

The first question requires selecting a time frame to examine, identifying the key drivers of change and trends and collecting and analyzing relevant data and expert insights to assess how these forces and changes are likely to play out during the time frame.

### Four Plausible Futures

The Vertex GTF project identified 16 interrelated business, political, social, technological, environmental, and tax policy trends that will shape the 2035 business environment. The project team's analysis concluded that these 16 trends will produce two high-impact uncertainties. The first uncertainty concerns whether (and to what degree) the relationships between governments will become more cooperative or more protectionist. The second uncertainty concerns the degree to which the relationship between governments and the business sector will become more complex or more simplified.

[4]David A.J. Axson, "Scenario Planning: Navigating Through Today's Uncertain World," *Journal of Accountancy* (Mar. 1, 2011).

[5]*Id.*

The following four scenarios depict possible combinations of the cooperative/protectionist and complex/simplified uncertainties.

### Scenario 1: Stalled Engines

In this complex and protectionist scenario, the U.S. and Europe have turned inward, globalization has stalled, and governments act unilaterally to protect their interests in the face of persistent global conflicts and environmental challenges.

Foreign direct investment, international lending, and overall international trade decline significantly in this future, which, in many ways, is an extension of current international taxation trends.

These dynamics intensify under the stalled engines scenario. By 2035, assuming this scenario ensues, mature economies in the West have become consumption oriented while a growing middle class creates real economic growth in China, India, and other parts of Southeast Asia. Overall, global GDP continues to grow, but at an extremely low rate. The long-awaited U.S. economic reinvention never materializes. The U.S. also takes a wait-and-see approach to most global conflicts.

Public debt in Europe and the U.S. has ballooned, making it increasingly difficult to fund infrastructure projects needed to fuel innovation. The majority of global citizens have grown skeptical of their governments' capability to govern.

The financial situation becomes dire for some Western governments that cannot overcome their fiscal shortfalls or rebound from their financial woes. Municipal bankruptcies proliferate. Russia, Venezuela, and some oil-rich countries in the Middle East and Africa make little progress in reducing their long-standing dependence on oil exports as the primary source of economic growth. Periodic drops in oil prices are especially harsh on these economies, helping stall globalization. Power moves away from traditional national governments toward new, nongovernmental coalitions and networks.

The big success stories in this scenario involve an empowered global citizenry and the emergence of new and smart cities, primarily in the East, that carry their own economic power and can resist national pressure to confirm to regulatory standards and tax regimes that run counter to their interests. Eventually, cities like Chicago and Lagos, Nigeria, mount efforts to gain statehood within their respective federal governments.

In the Stalled Engines future, several tax and fiscal policy trends emerge:

- Tax administration practices of nations and existing municipalities remain a labyrinth of rules and exceptions.
- Governments compete for tax revenues, both at the international level and internally at the state and local levels.
- Audit pressure from struggling national governments increases.
- Nations strapped for revenue become more aggressive, escalating their adversarial tension with corporations over compliance.
- MNEs exploit tax givebacks, regulatory loopholes, and profit-shifting strategies, pitting jurisdictions against one another. MNEs also lobby successfully against transnational tax agreements.

### Scenario 2: Gated Globalization

Despite the anti-trade backlash of the past few years, global trade has delivered proven benefits, including higher wages among major export industries, massive increases in product choice, and lower prices for basic goods in the United States of 2017.[6] Gated Globalization is a 2035 scenario in which the engines of global trade are not stalled but are not firing on all cylinders, either.

In this less complex and protectionist scenario, trade has shifted from a global marketplace to large regional trading blocs. MNEs and other businesses find it easier, faster, and cheaper to trade within their trade bloc.

These trading blocs are defined by trade barriers, such as high import tariffs and complicated customs procedures, that hinder commerce across blocs and increase trade within blocs. Barriers to commercial activity within blocs are reduced or eliminated. The lack of simplified taxation, long considered the last real barrier to trade, is largely removed, and goods and services move freely within blocs.

Most trading blocs are regional, while others link countries that have similarly sized GDPs. China might form a trading bloc with resource-rich, but investment-poor, African countries. Europe may fortify trading partnerships with Russia and parts of the Middle East, helping to secure their energy needs. The Association of Southeast Asian Nations exists to promote cultural, economic, and political development, while North American and Latin American countries (minus Mexico) build on the North American Free Trade Agreement to form their own blocs. In this scenario, national governments have less power, as blocs create their own economic systems, environmental rules, and shared energy reserves.

Smart cities in the East experience rapid growth as people migrate from the countryside and small towns to seek employment opportunities and the services that are expected for a middle-income lifestyle. These urban areas will resemble extensions of present-day Songdo, South Korea — a planned urban area the South Korean government began building in 2003. As of 2017, Songdo features one of the highest percentages of park space of any city on the planet, ubiquitous video-chatting technology, an automated garbage-removal system that negates the need for outdoor trash bins and garbage trucks, abundant urban farming, bicycle commuting lanes, and pedestrian thoroughfares.[7]

The following tax and policy trends dominate the Gated Globalization future:

- Tax revenues increase for countries in North America and Europe as a result of robust trade within these blocs. This shift reduces public debt. Credit markets make more capital available for infrastructure and construction projects.
- Tax complexity is reduced, allowing goods and services to move more freely within the blocs.

[6] Peter S. Goodman, "More Wealth, More Jobs, but Not for Everyone: What Fuels the Backlash on Trade," *The New York Times*, Sept. 28, 2016.

[7] Ross Arbes and Charles Bethea, "Songdo, South Korea: City of the Future?" *The Atlantic* (Sept. 27, 2014).

- Trade across blocs, however, continues to be hindered by high import tariffs, complicated customs procedures, and the usual convoluted universe of tax rules, including both transaction taxes and business activity taxes.

### Scenario 3: Interconnected World

In this low-complexity, highly cooperative scenario, a combination of marketplace coordination, regulatory reform, and regulatory standardization has created what many call the best of economic times.

People in most countries enjoy an improved standard of living, which is attributed to the economic benefits of significantly increased trade, the stabilizing effect of a rise in foreign direct investments, and a business-friendly regulatory environment. In addition to products and services, workers are also flowing more freely — a majority of Fortune Global 500 employees work outside their country of citizenship.

This marketplace-driven world is not without its economic downside. A labor strike in India can have ripple effects on mining operations in Bolivia, which in turn can roil stock markets and result in dramatic market adjustments across the globe. In the hypercompetitive Interconnected World, strong GDP growth, lowered trade barriers, fickle customers, churning markets, and periodic recessions are accepted parts of economic life.

Fewer and greatly simplified business regulations serve more as guideposts to facilitate trade and foreign direct investment than as speed bumps that slow it down.

The Interconnected World is relatively free of armed conflict. Nations and territories tend to work out their differences in negotiations with the formation of trade agreements. Economic sanctions trump hostile actions. More noticeable than armed conflict is the nonstop social activism on issues like food, energy, and water shortages. Activist groups around the world have become very skilled at shining a 24-hour spotlight on hypercompetitive corporations and the effect their actions have on people and communities, especially when it comes to environmental issues.

The surge in GDP, foreign direct investment, and trade leads to uneasy alliances between rivals. These and other forms of cooperation pay off. Aside from periodic market crises, GDP expands at a healthy pace, with growth in Europe, the U.S., and China fluctuating between 2 and 5 percent. Confronted with rising labor costs in China, India, and other Asian countries, corporations respond by shifting some production to Africa, where low-labor-cost countries such as Nigeria and Zambia offer attractive investments.

The rate of technology adoption accelerates, stimulating digital trade that is subject to uniform global tax rules.

This Interconnected World is marked by the following tax and policy trends:

- Tax reporting gets easier and less costly for corporations in most parts of the world. The trend toward funding government operations through indirect taxes continues.
- The tax transparency movement makes significant gains as governments adopt advanced information technology and innovative social media tools. Tax transparency is a social and political issue. MNEs are not competing for effective tax rates; rather, they focus on efficiency of information sharing between business and governments.
- Many G-20 governments pass some form of legislation allowing them to analyze and make public tax information collected from corporations. Companies that appear to be "good citizens" with fair effective tax rates receive positive feedback from social media, while those with negative reputations become mired in social politics that threaten their brand and market share.
- Tax reforms continue to materialize in most economies as the cost of compliance continues to fall.
- With the OECD's various standards gaining wide adoption, sharing information on global income attribution becomes the norm for MNEs.
- The steady increase in the use of information technology creates an increasingly automated and frictionless environment for both businesses and tax agencies. This drives down the total cost of tax administration (for governments and MNEs), stimulating further efforts to simplify it.

### Scenario 4: Corpocracy

This is the complex but cooperative scenario, and the traditional relationships between corporations, governments, and citizens has truly transformed.

A highly influential group of global corporations assumes some of the functions traditionally performed by the increasingly ineffective sovereign governments. Though clearly driven by profit, these "super-corporations" also exhibit a sense of responsibility for addressing critical global issues.

This scenario seems particularly plausible considering the structure and behaviors of the world's largest companies today. As a special report in *The Economist* recently noted, these "superstar" companies are skilled in applying their "creative excellence to rule-bending," and they possess the capabilities necessary to "build up impregnable advantages, giving them growing monopoly power."[8]

If superstar companies continue to press these advantages, it is easy to imagine how a small number of very large corporations could exert an unprecedented level of influence in politics and society by 2035. In this Corpocracy scenario, super-corporations harness technology and the digital economy, opening global markets and responding to shareholder pressure to drive profits and value. Their rising influence comes at the expense of government authority, as governments struggle to provide needed services and reduce debt. The global citizenry, frustrated by years of governmental ineffectiveness, generally accepts the shift in power because of the vast increase in the availability of consumer goods and the public's ability to directly influence what the super-corporations produce.

Super-corporations walk a fine line between maximizing profits and being perceived as robber barons. Their hyper-sophisticated legal teams provide just enough transparency, competition, and compliance to continue to meet their business targets. Governments are seen as necessary but not essential: They may need to be propped up, but they should never stand in the way of corporate growth and expansion. A significant component of corporate power is its mastery of IT, particularly social media and big data. Citizens, as consumers and investors, provide the greatest check on corporate power through their wallets and their collective influence via social media.

These companies deftly use tax structures to not only to deliver superior returns to stakeholders but also to strengthen their position relative to traditional competitors and regulatory bodies. Many of these companies begin providing public services at a lower cost and higher quality than governments do, leading to the privatization of many government services. As the super-companies' influence grows, they discover that they must address food, water, and energy scarcity issues because governments cannot do so. Corporations increasingly influence education and social agendas, as well.

Tax and fiscal policy trends in the Corpocracy future include the following:

- The unprecedented adoption of technology in all sectors, coupled with the steady march of globlization, leads to significant changes in tax policy regarding who and what should be taxed.
- Constant pressure from the super-corporations and their shareholders to minimize taxation of income at both the corporate and personal levels leads to a far greater emphasis on consumption and transaction taxes.
- The proliferation of technology into the infrastructure makes the processing and taxation of consumption far easier. The overall volume of transactions across the globe increases significantly.
- Within the tax departments of these super-corporations, critical issues such as carbon emissions, precious resource consumption, legal entity restructuring, and the age-old transfer pricing arrangements are monitored with laser focus, given their potential impact on financial performance.
- Revenue authorities simply cannot match the sophistication of these super-corporations, so they focus their attention on auditing smaller corporations and monitoring consumption/transaction processing systems.

[8] "The Rise of the Superstars," *The Economist*, Sept. 17, 2016.

### Questions for Future Tax Functions

How will the tax policy trends described above affect companies and their tax functions in 2035? The question, and the process of tracking down answers, can deliver present-day value for tax leaders and their companies.

A successful scenario planning exercise encompasses more than just the development of plausible futures. It also involves analyzing the effect of key variables (including tax policy) within each scenario, creating action plans for addressing those effects and monitoring those key variables, and taking actions on those variables that seem more plausible.

The present-day benefits of these activities are not hypothetical. Companies routinely gain real value from scenario planning. A primer on scenario planning published by Bain & Co. indicates that the activity allows companies to: challenge widely held assumptions about businesses and their strategic direction; identify levers that can help improve performance in the near term; boost overall organizational learning; and integrate more change management considerations into their strategic planning.[9]

Any organization would be uniquely affected by the tax policy trends within each of the four scenarios. The precise results would depend on the company's industry, size, and geographic footprint, along with a host of structural and operational characteristics. Nonetheless, tax departments can begin to assess these unique situations by addressing a similar set of questions for each scenario:

- *How would this scenario and the tax trends that follow affect how the tax department collaborates with the rest of the organization?* The extreme tax transparency in the Interconnected World scenario would likely foist most, if not all, of a company's tax data into the public domain and subject it to instant social media feedback from stakeholders. This dynamic poses major potential brand and reputational risks, which would likely require tax functions to collaborate closely with their risk management and external communications colleagues. In a Stalled Engines scenario, tax strategy would likely become a full-fledged mainstream business capability. Chief tax officers would report directly to CEOs, tax-function budgets would increase dramatically, and tax officers at companies of all sizes would require larger dedicated IT teams.
- *How would this scenario and the tax trends that follow affect the degree to which the tax function is centralized or decentralized?* In the low-complexity scenarios (Gated Globalization and Interconnected World), a highly centralized tax function would be possible and efficient; outsourcing would also be more attractive when possible. In the high-complexity scenarios (Stalled Engines and Corpocracy), a decentralized tax function would be more viable (as MNEs whose tax chiefs work with government officials in developing countries may already know).
- *How would this scenario and the tax trends that follow affect the type of talent the tax function needs and its access to that talent?* In one or more of the scenarios, tax policy would vary, sometimes wildly, by region and country. This complexity would require tax functions within global companies to employ, or at the very least externally source, a wider range of region- and country-specific tax expertise. The widespread need for this expertise would drive competition for talent, drive up salaries, and create other talent-management challenges for tax functions. Other scenarios would cause a spike in demand for tax technologists.

### Conclusion: Preparation Outdoes Prediction

For tax departments, the value of addressing these questions (and others) extends well beyond planning and forecasting. Shell has remained a scenario planning exemplar for more than four decades because it continues to derive a wide range of benefits from the discipline it launched:

> Shell-style scenario planning has never really been about predicting the future. Its value lies in how scenarios are embedded in — and provide vital links between — organizational processes such as strategy making, innovation, risk management,

[9] Bain & Co., "Scenario and Contingency Planning" (June 10, 2015).

public affairs, and leadership development. It has helped break the habit, ingrained in most corporate planning, of assuming that the future will look much like the present . . . Scenarios enable Shell executives to open their minds to previously inconceivable or imperceptible developments.[10]

By participating in corporate scenario planning efforts — and developing their own tax-specific futures that include likely effects and possible responses — tax leaders can open their minds, and their teams' minds, to new ways of thinking about the future. In the process, they may also discover new ways of improving their companies today. ■

[10] Wilkinson and Kupers, *supra* note 1.