

Webcast series 'State of Tax'

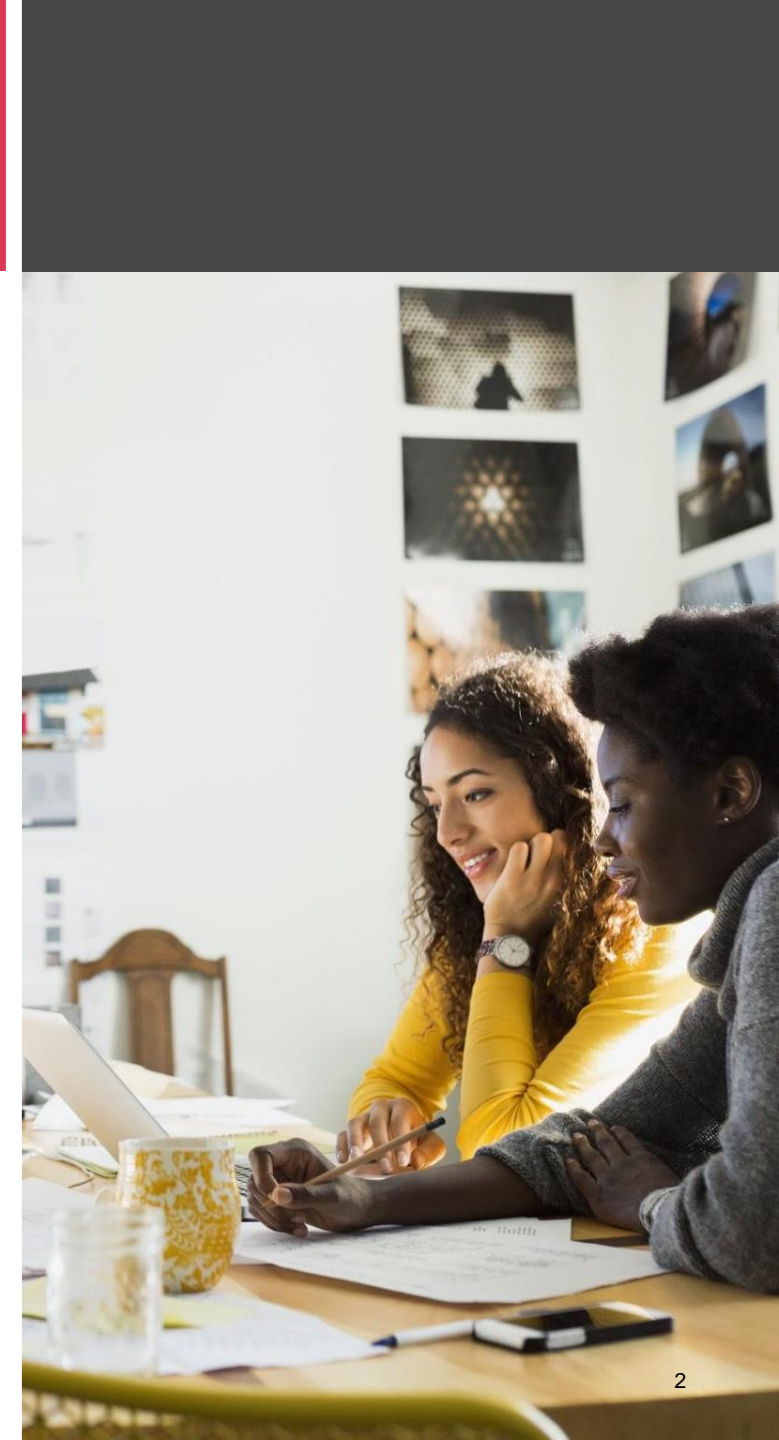
Tax impact of changes in your supply chain & operations



Presentation by Jeroen Schmitz, Claudia Buysing Damsté
and Richard Hiemstra
2 July 2020

Introduction

- Webinar works best via Google Chrome
- The button '**[Ask a question]**' allows you to ask a live question via chat
- Any other questions via your PwC advisor or fill in the form on pwc.nl
- View this webcast or presentation at a later stage
- Slides will become available afterwards
- Evaluation form afterwards



Agenda

1. Introduction
2. Trends in supply chain and operations
3. Role of tax in supply chain and operations developments
4. Case study and how can technology support?
5. Key takeaways
6. Closing



Here with you today



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The past 20 years



Winners
2000 - 2008



Winners
2008 - 2012



Winners
2012 - 2020

Market Disruption

From Physical, Banking and Oil

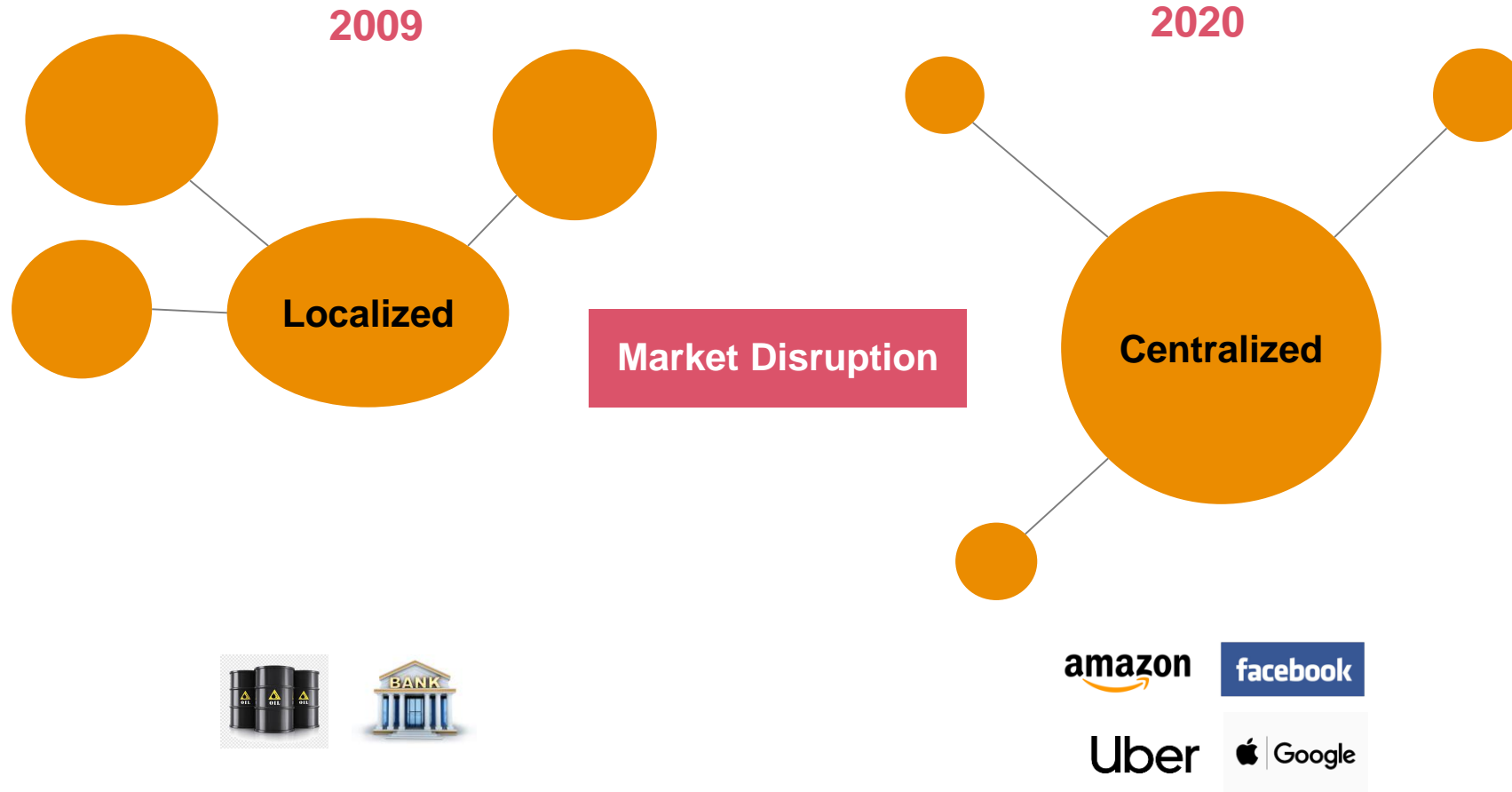
to Technology and Data

And the winner was...

After the financial crisis of 2009, a clear disruption occurred in the global market. Data and content driven technology startups dominated the market by the end 2019, as they were (almost) unconstrained by the physical laws. This allowed them to quickly adapt to the post-crisis business environment with the use of intangibles driven centralized supply chain models.

Pre-crisis companies held their winning streak if involved in Technology.

From 2009 to 2020 Market Disruption



Market disruption

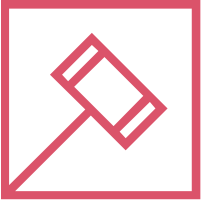
The post-financial crisis environment allowed the Winners to benefit from the advantages of world-wide centralized business models.

The key entrepreneurial activities of developing and creating the valuable intangibles were centrally managed and conducted.

Whilst the worldwide expansion only required limited routine support functionalities.

This opened the door to tremendous scale without expensive mass.

Uncertainty adjusting to reforms and trends



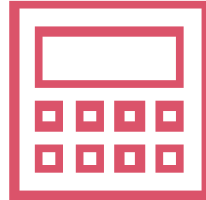
Regulatory reforms

GDPR

Data Restriction

Environmental restrictions

Anti-takeover rules



Tax reforms

Sustainability

Transparency

Profit allocation

Funding



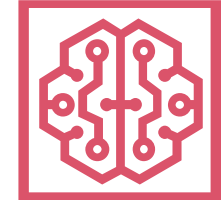
Geopolitical trends

Climate / Population

Trade Wars / Protectionism

Sanctions

State Aid



Structural trends

Industry 4.0

Sustainability

Uncertainty causing a shift in location

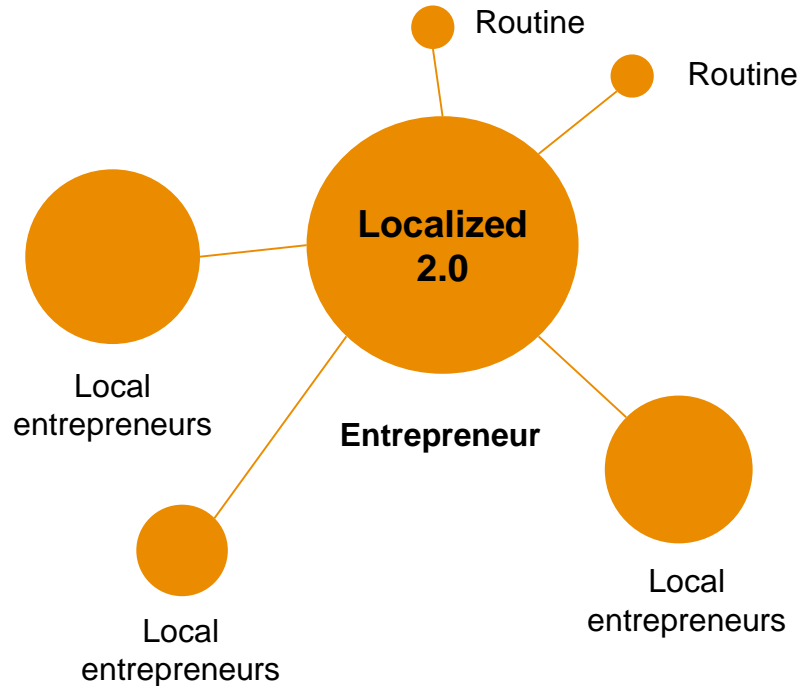
Uncertainty

Regulatory reforms

Tax reforms

Geopolitical trends

Structural trends



Changes

Future of Work

Legal and Economic ownership of assets

People Locations

Intercompany flows

Operating Systems

Customer experience

Entity/branch functionality

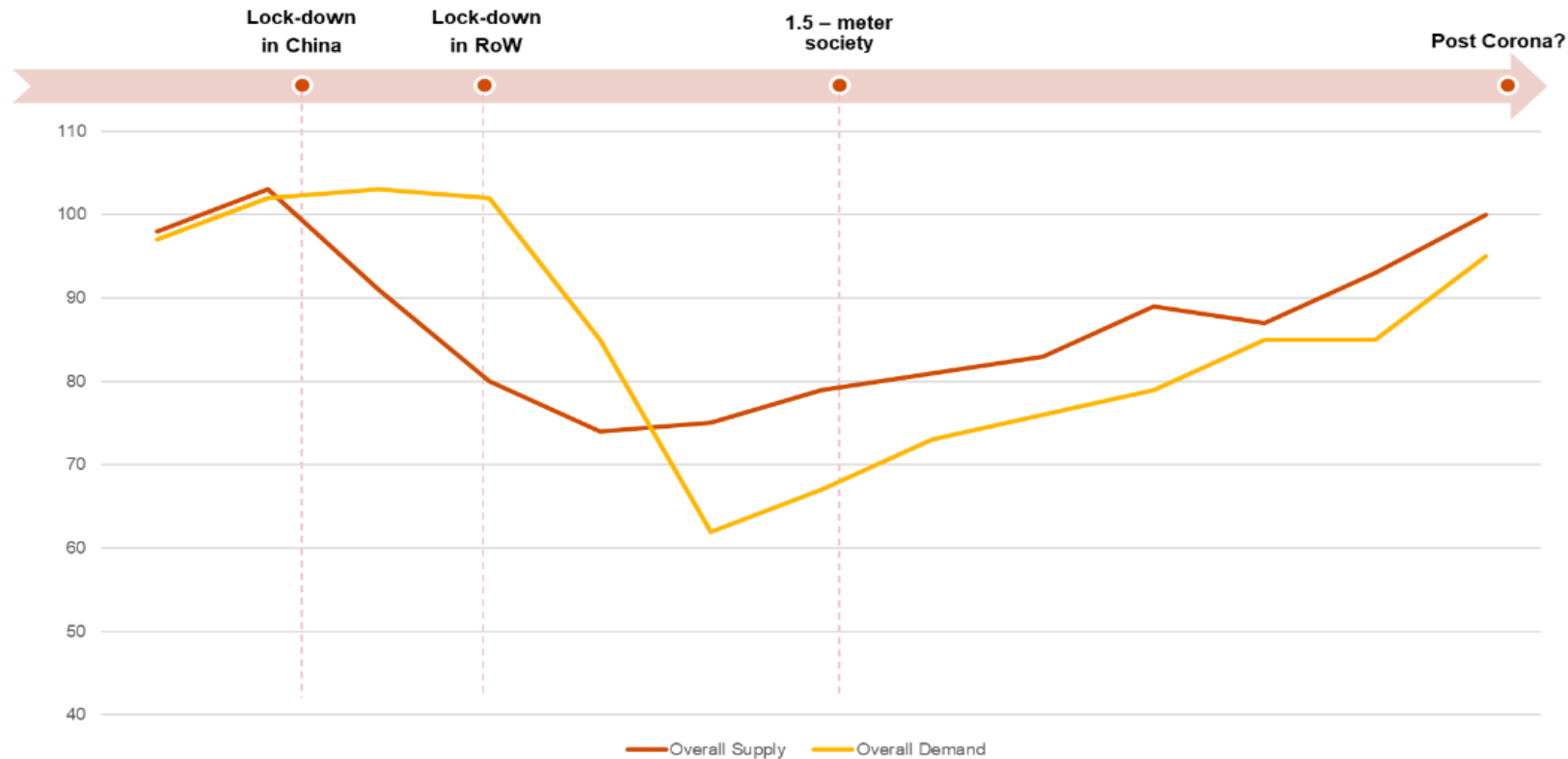
Technology

Localized 2.0

Localized 2.0 is a hybrid of the previous models. It will require due to the identified trends and reforms a stronger local physical presence whilst the digitalization based on technology and data of the supply chain will have to advance rapidly to stay ahead of the herd.

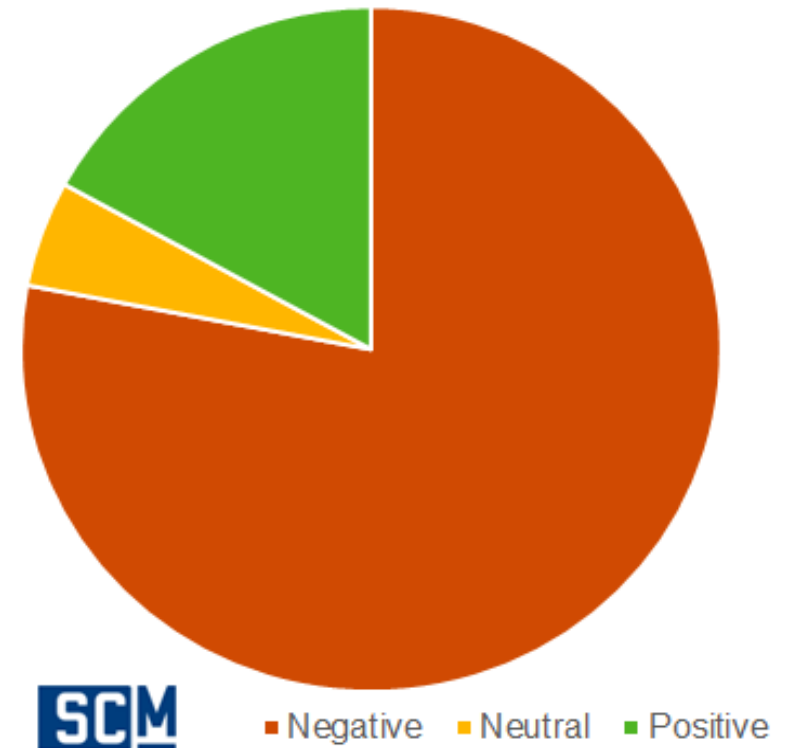
Further accelerated by the COVID-19 crisis

The Demand – Supply mismatch



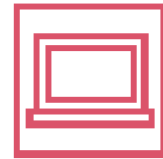
- SC Diversification
- SC Transparency

Short-term impact of Coronacrisis
survey supply chain decision-makers in Europe



Other COVID-19 consequences

- Travel ban
- Working at 1.5 meter distance
- Inability to do physical shopping
- Closing down bars, restaurants and clubs



Leads to:

- Working and shopping from a distant place



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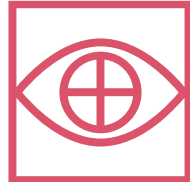


Tax trends within the uncertainty tax drivers



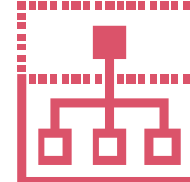
Sustainability

- Co2 emission tax
- State & Local environmental taxes



Transparency

- GRI
- (Public) Country by Country Reporting
- Tax Policy reporting
- 3 tier TP documentation
- Ruling exchanges
- ICAP
- DAC6
- Real Time digital government



Allocation

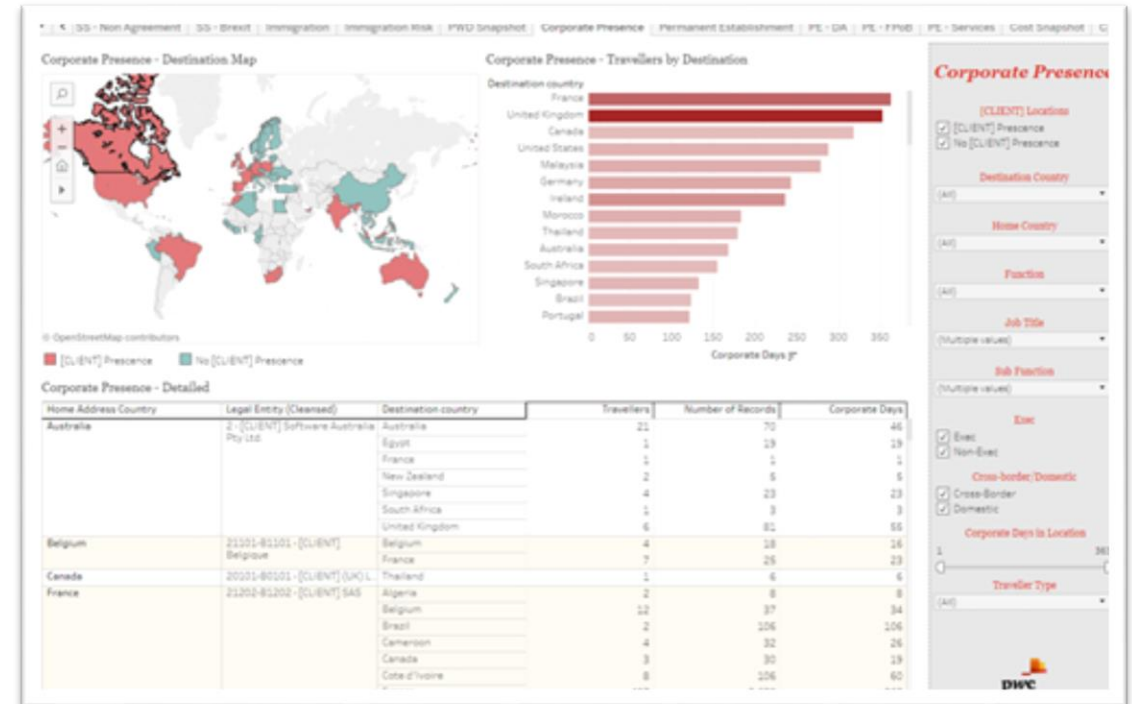
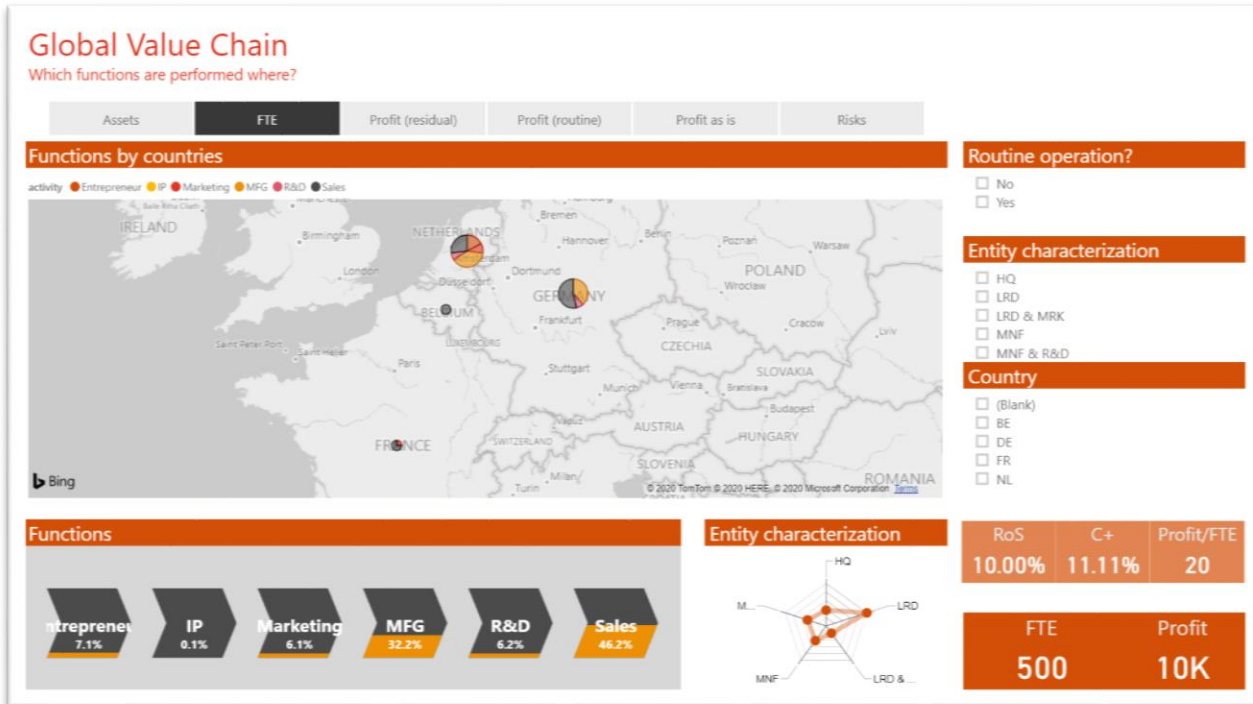
- Pillar 1 Unified Approach
- Pillar 2 – minimal tax
- DSTs
- Other Local Taxes
- VAT platform taxes
- (Digital) permanent establishments



Funding

- Stricter EBITDA interest deduction rules
- Higher equity (buffer) requirements – not only at central group level

Data Driven Approach



Insights tooling

An efficient, data-enabled approach utilising available data in systems (ERP, CRM, HR) to provide insights into the tax position. Allowing for tax risk management and identifying tax optimisation of the changes made to the supply chain and operations.

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Case study

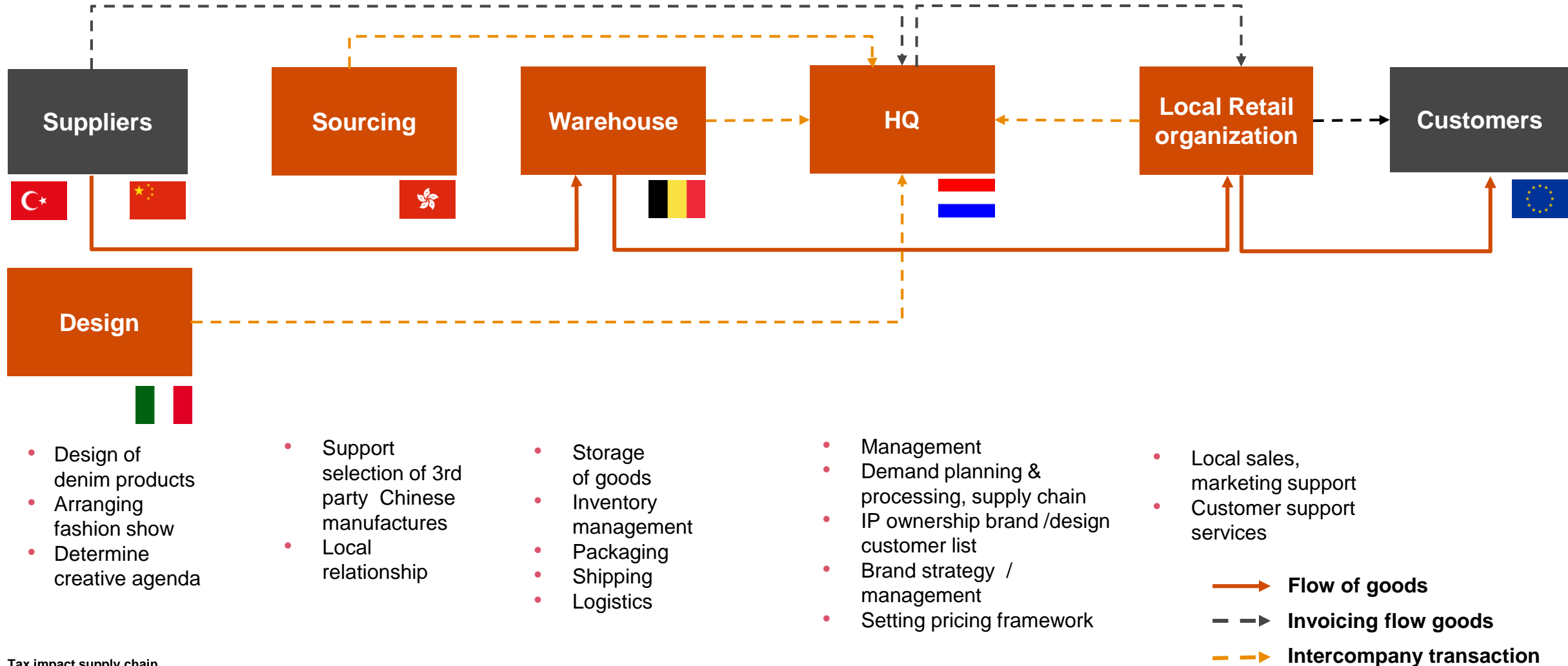
December 2019

- Group A is a premium fashion house with a centralized business model.
- The HQ is located in the Netherlands (**supply chain and IP principal**)
- Team of **high-profile designers** located in hub in Milan
- Procurement from one supplier with plants in China and Turkey
- Sales in own flagship stores or by shop-in-shop concept with local stock
- The **customers** are mainly located in the EU.
- Brand gets traction in US and Asia via sponsored influencers and artists.
- Local in-market teams involved in local campaigns and customer support.
- There is a regional Belgian **warehouse** owned by HQ
- The warehouse manages inventory, stores, packages and shipment to stores. Logistics is performed in-house – own fleet of trucks.



Transactional flows 2019

Case study



Case study

June 2020

A perfect storm?

- End of February - **supply from China stops** – still finished goods at the docks.
- Mid March - **supply from Turkey stops too**.
- Mid March - **Stores close**. Complete hold of transport.
- Mid March - **Design center Milan closed** – no design new collection.
- End of March – **Dutch HQ closed**. All employees working from home – executives also outside Netherlands.
- April – Multi-lateral tax audit announced including exchange of Dutch rulings.
- April - **On-line demand** via third parties increases.
- April - **Stock still at central warehouse** and local retailers.
- April - Additional funding required to pay for stock and down payment for new collection.
- May - **NGO-s publish report** on the environmental impact of denim production.
- Begin of June - Chinese Manufactures restart and ship supplies. Turkey starts as well.
- Begin of June - Physical stores slowly opening. Regional warehouse full of stock.



Case study

July 2020

- **What is next?**
- Management Board meeting first week of July.
- Question on the table - What strategy is required to come to an agile and resilient operational model?
- Solutions suggested by the Board:
 1. **generate cash** by selling stock at discount to third parties
 2. make sure that a **new collection** will be designed
 3. create **online channel** via own web shop
 4. arrange for **working from home** infrastructure



Question 1

Do you believe that the strategy determined by the Management Board is holistic enough?

A) Yes

B) No

Question 2

Which of the tax drivers should be considered most as part of the strategy?

- A) Sustainability
- B) Transparency
- C) Allocation
- D) Funding

Question 3

Who are the main stakeholders to the strategy?

- A) The board and the designers
- B) The customers, the local governments and the suppliers
- C) Employees

Question 4

Which element is key and should be added to the strategy?

- A) Arrange for higher capital buffer
- B) More environmental friendly production
- C) Redesign supply chain and pricing policy
- D) Expansion to North America / Asia

Case study

September 2020

Group A decides the following strategy:

- Redesign supply chain – Sustainable, transparent, agile and resilient
 1. **Regional online sales** organizations with regional customer support
 2. Reducing physical stores in Europe
 3. **Regional sourcing** (Singapore, Netherlands, US) and warehouses
 4. **Online design platform** with teams in Singapore, Italy and US
 5. Collecting local and **analyzing customer data** in the Germany
 6. Cloud solutions developed by Germany with a **server in Denmark**
 7. 3rd party logistics



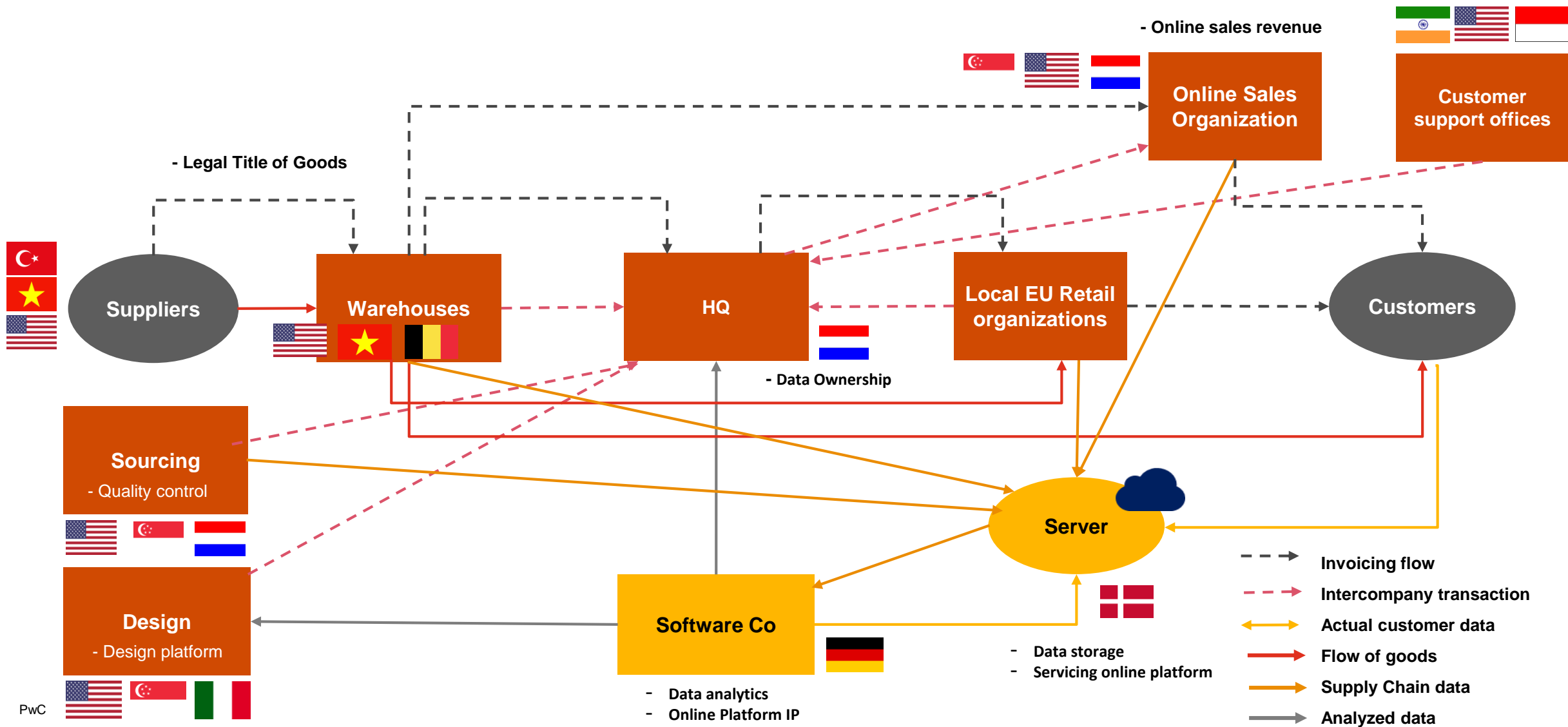
Question 5

What is a realistic timeframe to implement the changes?

- A) 12 months
- B) 18 months
- C) 24 months

Transactional flows 2022

Case study



Transfer pricing considerations

Case study

HQ

Are all strategic and risk controlling functions at HQ?
Legal and/or full economic ownership of all intangibles, including (analyzed) data?
All residual income after routine remunerations? Or profit split?

Design

Service provider or key value contributor?
Cost plus, license or profit split with HQ and other group entities?
How to allocate amongst design platform entities?
Which allocation key?

Local Retail organization

Distributor with a limited or full risk profile?
Fixed Return on Sales or not?

Sourcing

Support versus center of excellence?

Historically the key value drivers. Changed in new model?

Transfer pricing considerations

Case study

Software Co

Is data analytics a key value driver?
Is Germany strategically driving the online business?
Does Germany own the online customer base?
Cost plus versus license or profit split model?

Server

Is the storage of data and buffering a website a routine function?
Should a cost plus remuneration be sufficient?

Online Sales Organization

Does handling of customer payment flows create a customer list?
A cost plus or sales based remuneration?
To bring additional functionality in-market in case sales based remuneration?
Does the remuneration reflect the in-market value creation?

Warehouse

Does the fact that warehouse takes title and arranges for transportation impact the remuneration level?
Role of warehouse in online business model?

Technology and data a new value driver?

Data value location:
server, analytics hub,
HQ, consumer market?

Taxation rights:

- Local marketing intangibles
- Digital PEs
- Digital Services Tax

Transfer pricing considerations

Data driven analysis



Footprint
Global presence

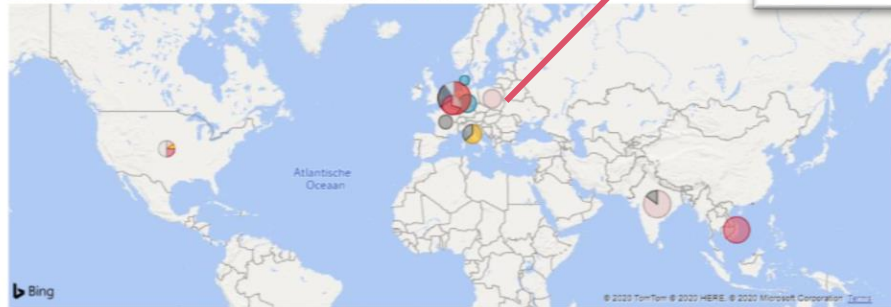
Global Value Chain

Which transactions take place and how are they remunerated?

Assets P&L **People** Profit (as is) Profit (calculated)

value by Country ISO and function_key

function_key Cust. Serv. Design Entrepreneur Logistics Marketing Sales Soft Dev Sourcing



Product

- ☐ Offline
- ☐ Online

Entity characterization

- ☐ De Rol
- ☐ Design
- ☐ HQ
- ☐ NL role
- ☐ Sales
- ☐ SP Role

RoS	C+	Profit/FTE
10,50%	11,73%	11

People	Profit
186	2K

Functions



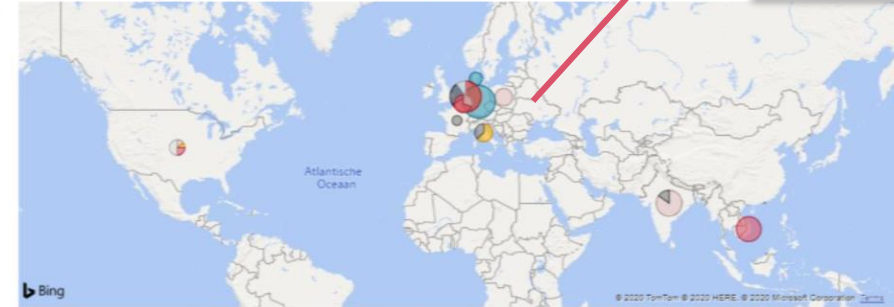
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Product

- ☒ Online

Entity characterization

- ☐ De Rol
- ☐ Design
- ☐ HQ
- ☐ NL role
- ☐ Sales
- ☐ SP Role

RoS	C+	Profit/FTE
5,13%	5,40%	5

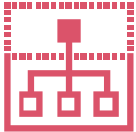
People	Profit
84	410

Functions



Transfer pricing considerations

Data driven analysis

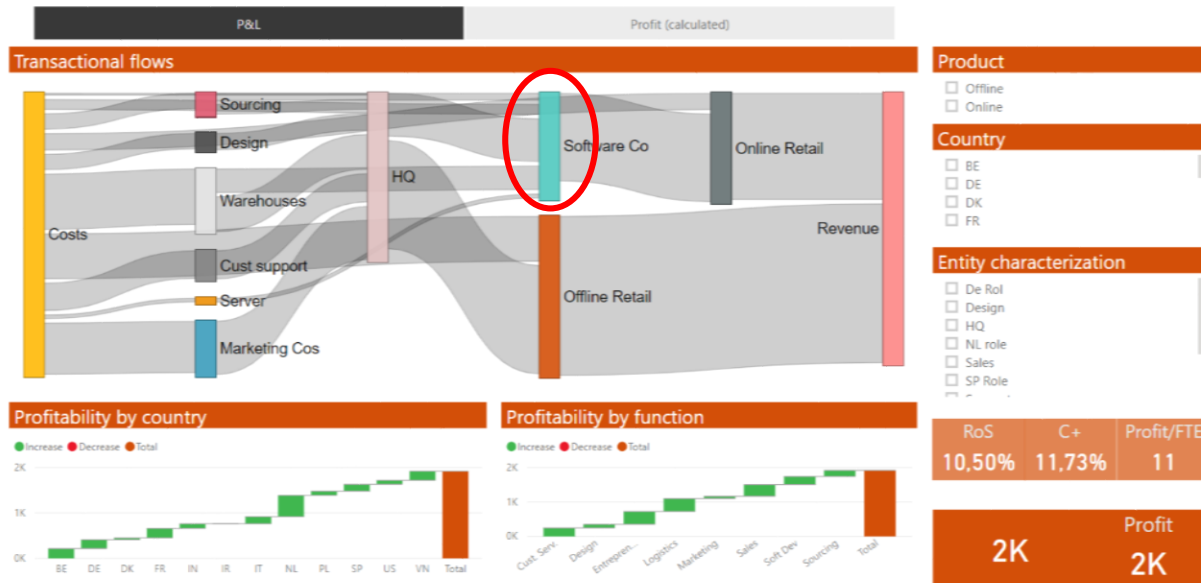


TP Model

Transactions and profit allocation

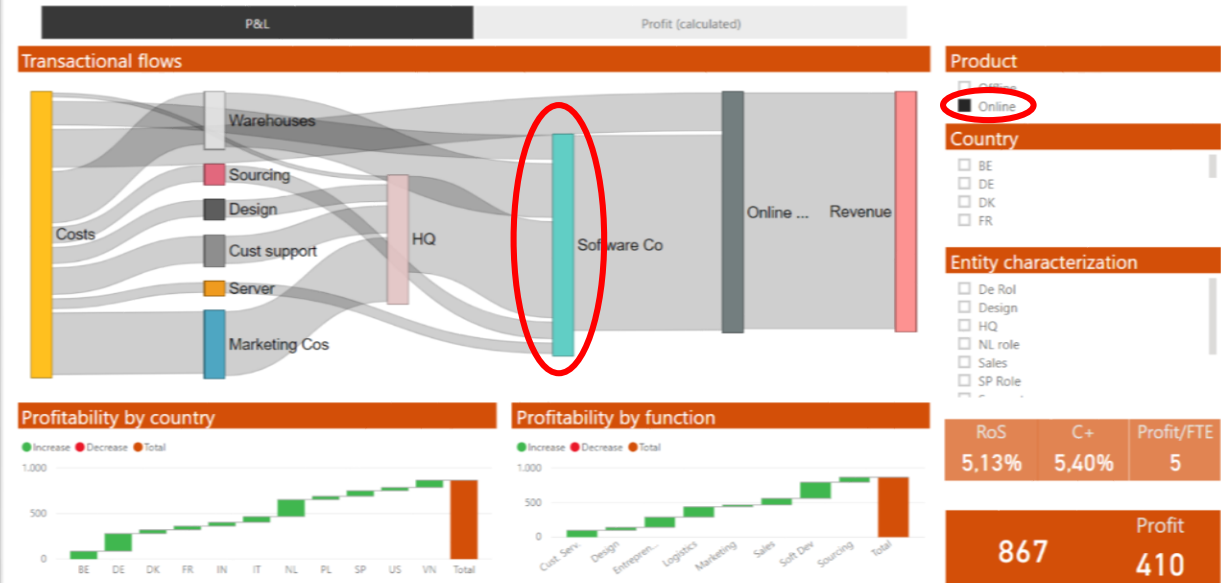
Internal transactional flows

Which transactions take place and how are they remunerated?



Internal transactional flows

Which transactions take place and how are they remunerated?



Transfer pricing considerations

Data driven analysis



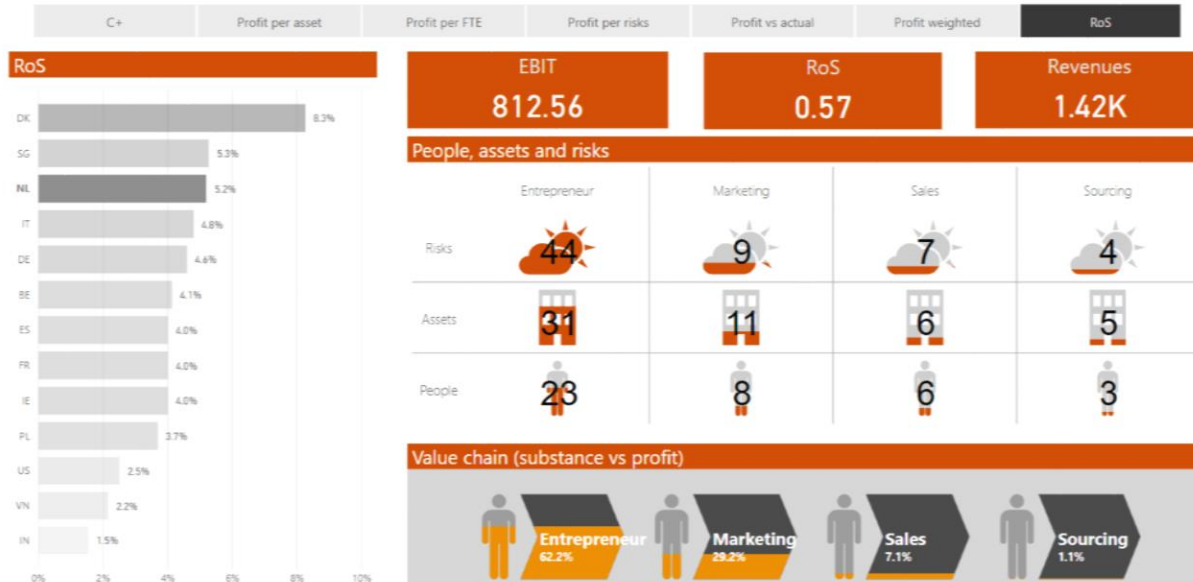
Control
Margin monitoring



Sustainability
Profit alignment with value creation

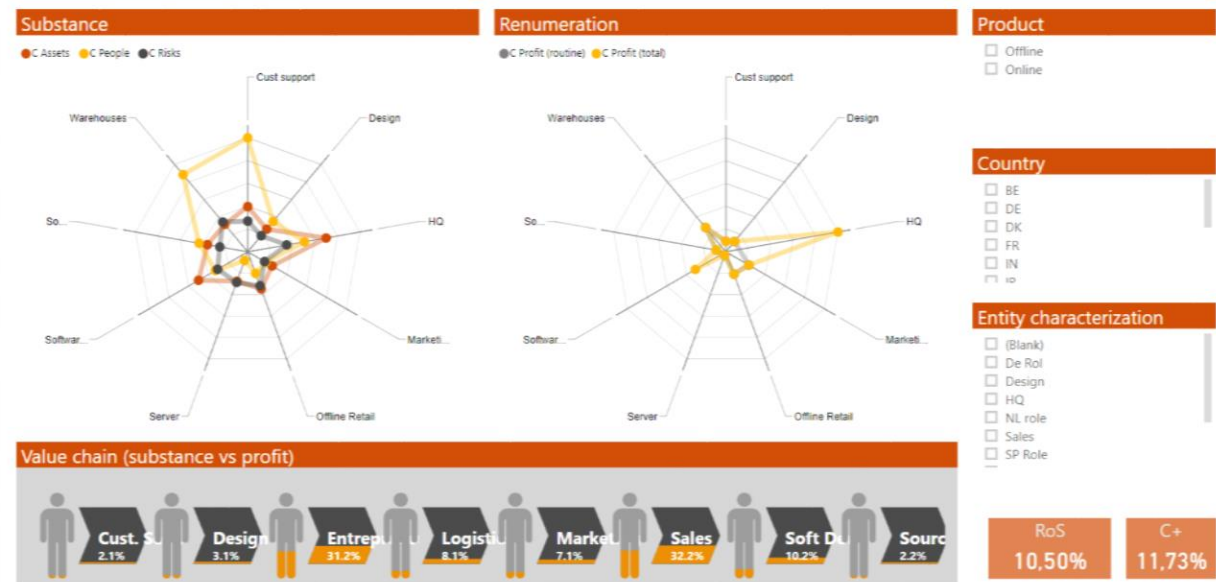
Financial analyses

Select a KPI, find anomalies and analyse functions



Functional analysis

Compare substance (people, assets and risks) with remuneration (routine, total) by entity characterizations



Phase I – Services

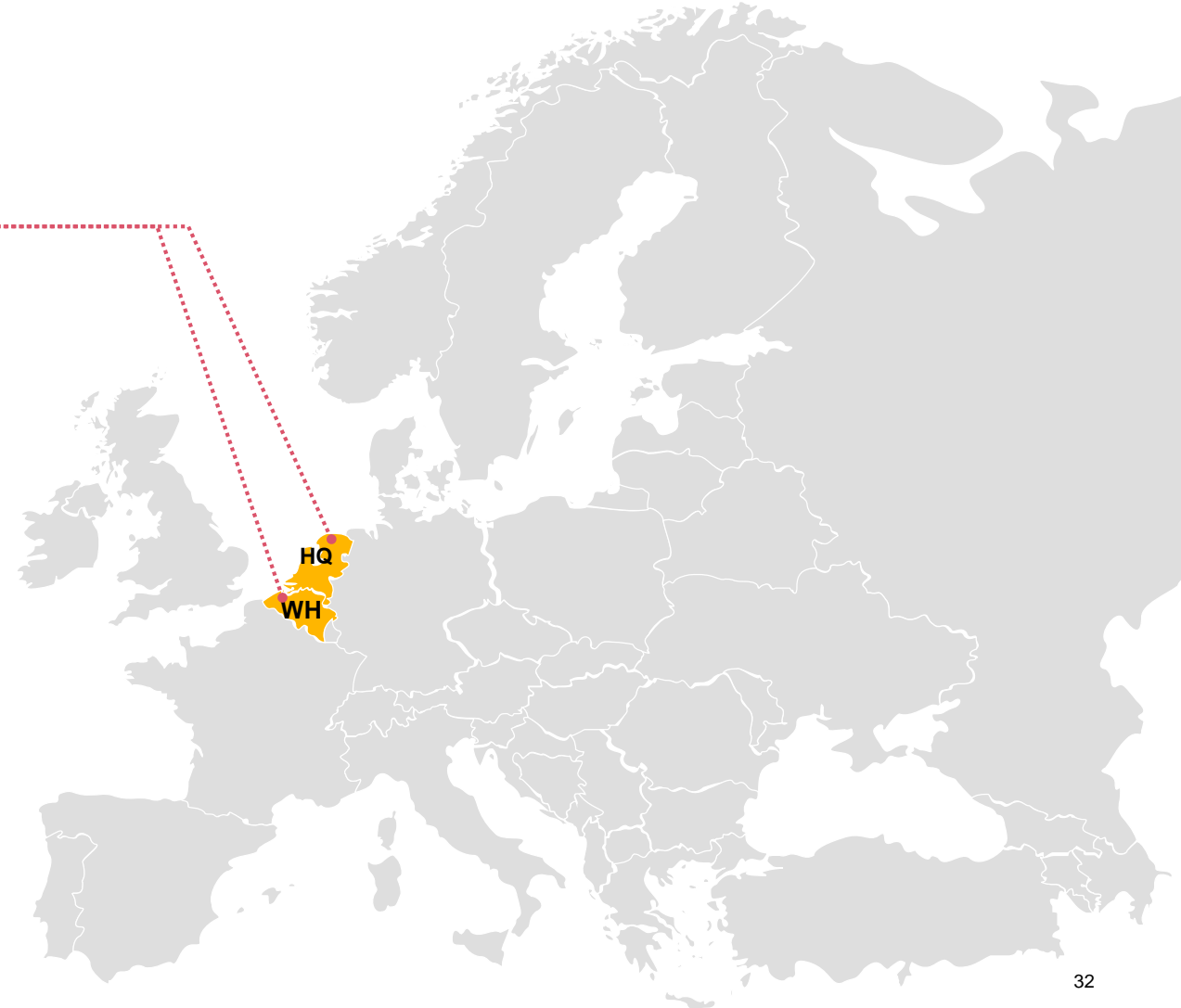
Customs considerations



- At which time in the supply chain does the transaction occur?



- Review the customs value used – align with TP strategy
- Would it be possible to benefit from preferential origin?
- Would storing the products under a suspension regime reduce duties due?



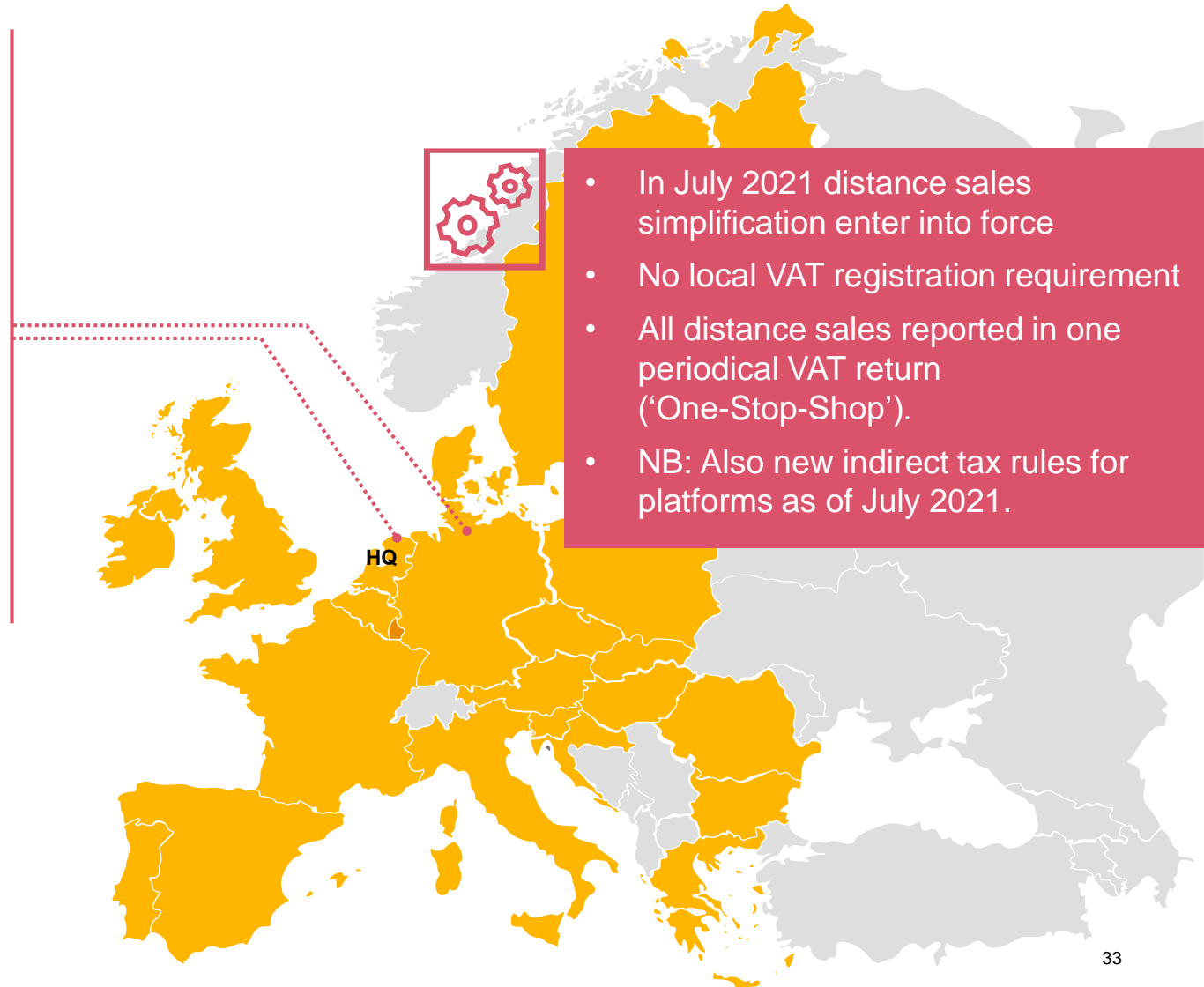
Phase I – Supply of goods

VAT considerations

- If B2C supply of goods from BE to other EU countries, in principle BE VAT due
- However, if certain thresholds are exceeded, local VAT may be due (distance sales regime)
- VAT registration & VAT reporting in all EU countries where distance sales threshold is exceeded.
- When thresholds are exceeded, also invoices should be issued meeting local invoicing requirements.

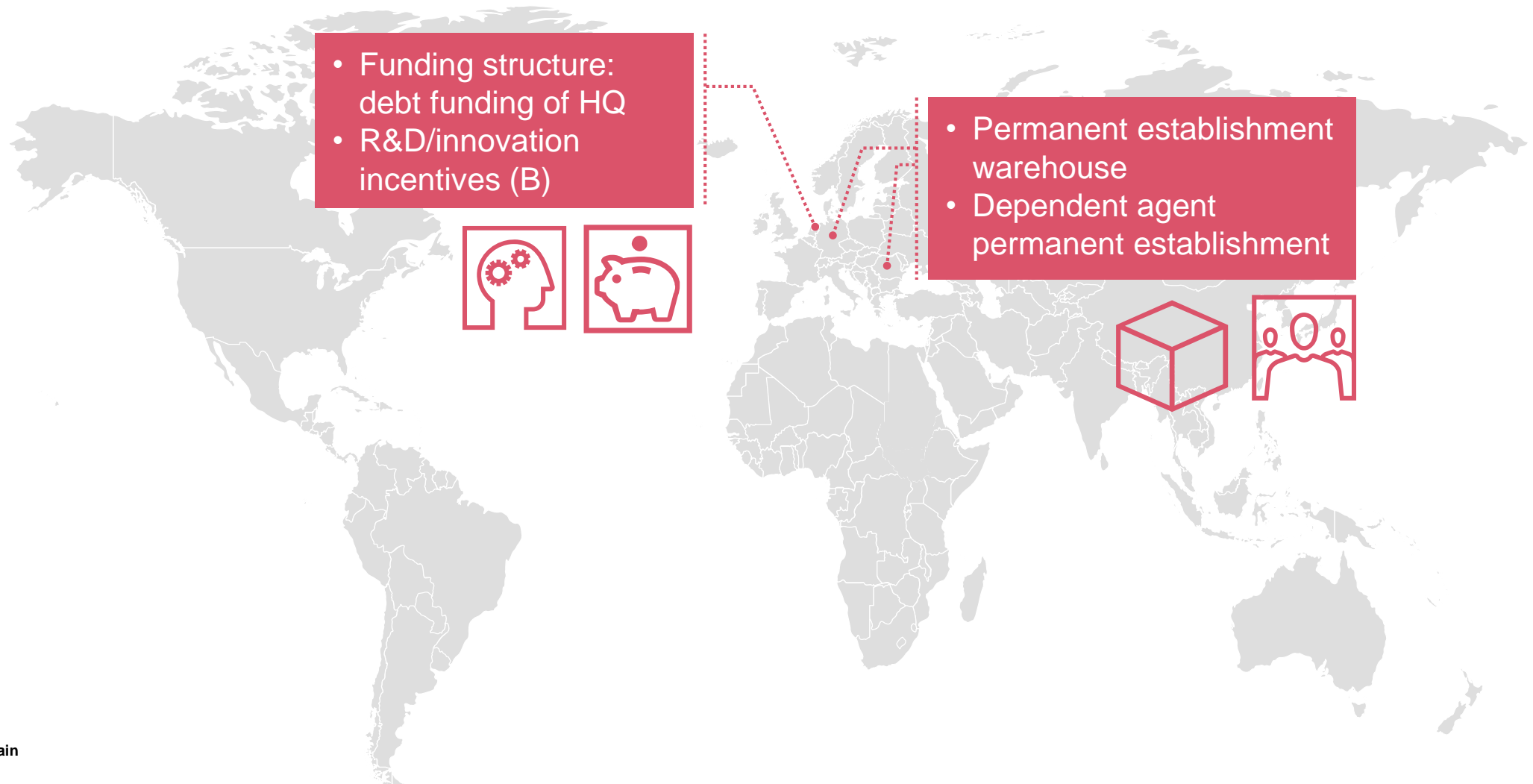


- Due to the various local reporting obligations, this model is more difficult to manage (and less cost efficient) from both an indirect tax as IT perspective.

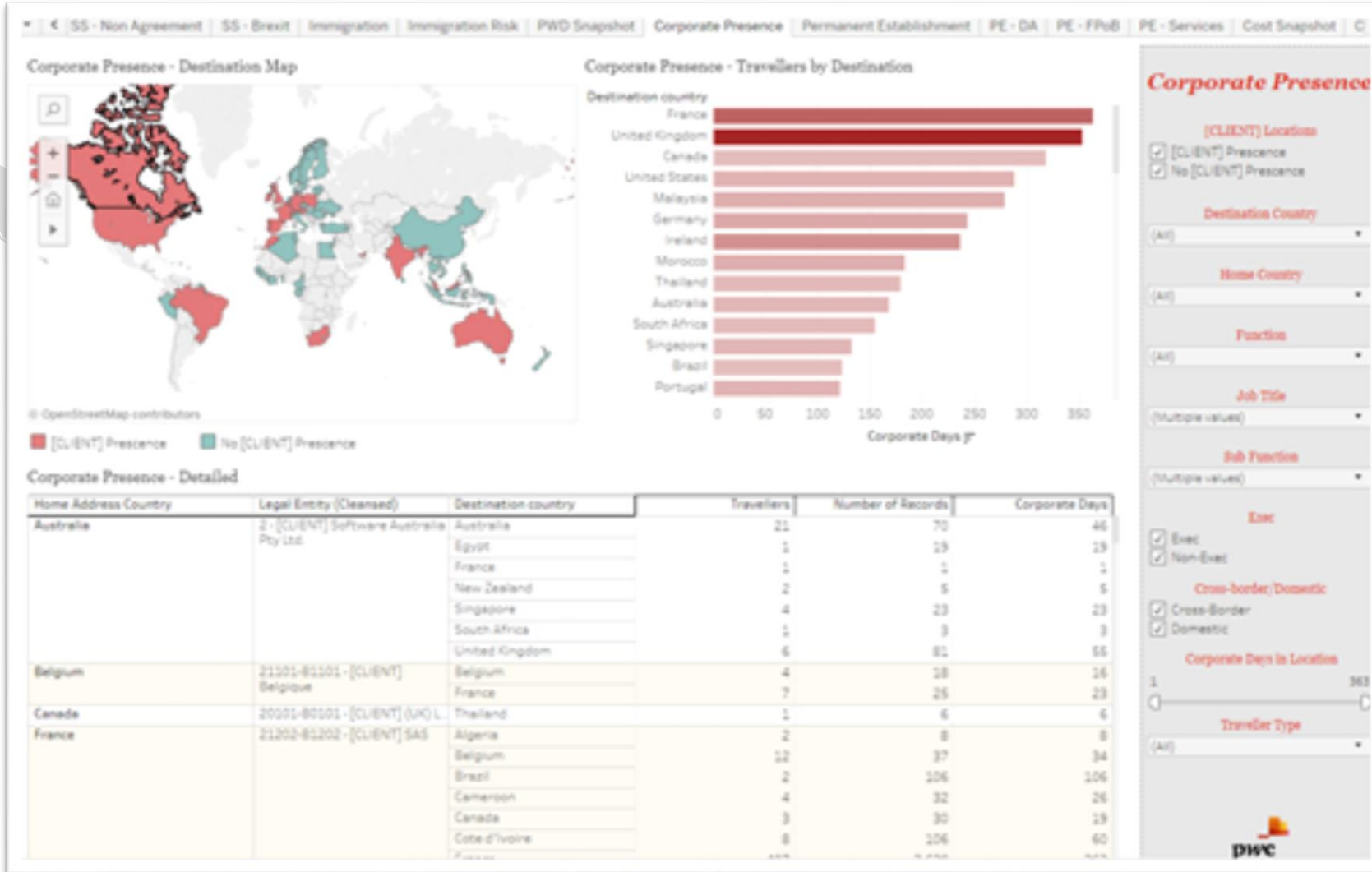


Phase I

CIT considerations



CIT considerations – Travel Data analysis



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Key takeaways

- Holistic approach required to determine a “Winners” strategy
- Consider the relevant reforms and trends
- Identify and manage all key stakeholders
- Overlay the tax drivers
- Translate to supply chain/operating model changes
- Apply a cross tax approach aware of all (non-tax) interdependencies

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Closing

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