



Developing a common framework for disclosing tax information

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The case for a framework

Background

There can be little doubt that the debate around greater tax transparency by companies is becoming increasingly prominent. There are a growing number of calls from various parts of civil society for companies to be transparent about where they operate around the globe, where they make their profits, where they pay their taxes and how much tax they pay.

It would appear that at the same time there are an increasing number of regimes with varied scopes, which require different levels of tax disclosures by companies, some to the public and some to tax authorities. For example:

- The Commissioner of Taxation publicly disclosed information about certain corporate tax entities with annual total income of \$100 million or more in December 2015 for the first time. A flurry of legislative changes prior to the first disclosure exempted privately owned Australian companies with a total income of \$200 million or less from the requirement. Private companies with more than \$200 million of income will have their data disclosed early in 2016.
- On 11 December 2015, the Board of Taxation (BoT) released a consultation paper on the development of a proposed tax transparency code (Code). The Code is to facilitate greater public disclosure of tax information by business.
- Late amendments to the recent Multinational Anti-Avoidance Law (MAAL) Bill, passed by Australian Parliament in December 2015, would appear to require all companies with global (consolidated) income of more than \$1 billion to prepare general purpose financial statements, although there is some uncertainty surrounding the law.
- The Australian Senate Economics Reference Committee Inquiry into Corporate Tax Avoidance made a number of recommendations in its interim report in August 2015, including the implementation of a Country by Country (CbCr) reporting standard based on the EU and OECD standards, implementation of a mandatory tax reporting code, and a public register of tax avoidance settlements. The final report of this inquiry is scheduled to be released in February 2016, and will likely focus on transfer pricing, profit shifting and transparency.

KPMG Australia's view is that the direction of travel in respect of tax transparency is clear – there will be increased disclosure requirements with more information becoming public

- The Organisation for Economic Co-operation and Development ('OECD') template for CbCR, which will be adopted by countries from 2016, requires reporting to tax authorities.
- The Australian Taxation Office's (ATO) Tax Risk Management and Governance Review Guide which contains the suggestion of publishing tax policies both internally and in the annual report.
- The EU's Capital Requirements Directive IV and Accounting Directive Chapter 10 requiring certain financial institutions and energy and natural resources groups in the EU to publicly report additional information on taxes and payments to governments.
- In the US the *Dodd-Frank Act*, which is currently being redrafted, may require SEC registered ENR entities to report similar information in coming years.
- In December 2015, the European Parliament Economic and Monetary Affairs (ECON) Committee voted to adopt its report *Bringing transparency, coordination and convergence to Corporate Tax policies in the Union*. The report recommends a number of tax transparency measures, including introduction of CbCR for all sectors by multinational companies, and the creation of a 'Fair Tax Payer' label for companies that engage in good tax practices.
- The United Kingdom (UK) is planning to introduce legislation on a requirement for large businesses to publish their tax strategies as they relate to or affect UK taxation.

There is also an increasing interest from certain stakeholders in the tax risks that companies face and how they manage these risks – both financial and reputational. In addition, in December 2015 the ATO published tax data for many of the largest businesses in Australia.

The ongoing tax transparency debate rests against a backdrop of high-profile media stories, in which the tax affairs of a number of groups have been brought into the public arena – and this has served to damage public trust in companies, particularly in relation to the conduct of their tax affairs.



Tax transparency code

Background

On 11 December 2015, the Board of Taxation (BoT) released a consultation paper on the development of a proposed tax transparency code. The Code is to facilitate greater public disclosure of tax information by businesses.

The Code is divided into two parts which set out the minimum standards of information for companies. 'Large businesses' which earn an aggregated turnover of more than A\$500m should adopt both parts. 'Medium businesses', earning A\$100m to A\$500m in revenue, should adopt Part A.

The Code has been designed to meet the requirements of 'interested users' (social justice groups, media, analysts and shareholders) and 'general users' (the person on the street), rather than the ATO. The BoT suggests appointing the ATO or another government agency as 'the responsible agency' for the Code. The responsible agency will establish a central website providing links online to the various taxes paid reports to be prepared by companies. There is no provision to limit the obligations for Australian private companies. Superannuation funds, partnerships and trusts do not have to comply but may volunteer to adopt it.

The BoT considers that the Code should be in operation in time for the reporting period for 2015-16 financial statements or annual reports. A Government review should take place three years from the commencement of the Code.

KPMG observations

KPMG believes the proposed Code represents a sensible balance of the different interests in the transparency debate. By adopting a principles based approach rather than a template and by allowing differential requirements for medium and larger businesses, the BoT has sought to keep cost proportionate for Australian companies. The proposal for a consistent approach to effective tax rates will be important in enhancing trust in the disclosures.

Although the Code is currently voluntary, and so compliance with it will not be enforced, the proposed Code implicitly reads as a positive obligation on business to adopt 'at the earliest opportunity'. The proposed Code also effectively introduces a new concept of local Australian tax materiality. The minimum standard set by the proposed Code of a local and global effective tax rate will be a clear point of reference for stakeholders.

Code disclosure	Who	Minimum standard of information
Part A: Improvements to disclosures of tax information in financial statements	'Large' and 'medium' businesses*	<ul style="list-style-type: none"> A reconciliation of accounting profit to tax expense and to income tax paid or income tax payable Identification of material temporary and non-temporary differences Accounting effective company tax rates for Australian and global operations (pursuant to AASB guidance)
Part B: 'Taxes paid' report	'Large' businesses	<ul style="list-style-type: none"> Approach to tax strategy and governance Tax contribution summary for corporate taxes paid Information about international related party dealings, financing and tax concessions



KPMG Australia's perspective

KPMG Australia's view is that the direction of travel in respect of tax transparency is clear – there will be increased disclosure requirements with more information becoming public. It is also the case that, as well as several reporting regimes existing side by side, different stakeholder groups will look for different forms of disclosure and so there is a real challenge for companies in how they manage this.

KPMG Australia believes that Australian companies should engage in an open and constructive debate on tax transparency to establish what content can, and might be produced to meet the demands of the different stakeholder groups while balancing the cost to businesses. However, a prescriptive set of rules, that is a 'one size fits all' approach, is not the right way to proceed with transparency.

We have therefore engaged with a number of leading multi-national groups headquartered in Australia and overseas on this issue. From those discussions several common themes have arisen which might form a platform or framework for disclosing tax information. We have summarised these key themes into the five broad areas below:

- Strategy/policy and approach to tax
- Tax risk governance
- Business model
- Tax contribution
- Specific information in relation to material issues

The framework is intended to prompt Australian companies to evaluate their own position and is not intended as a definitive checklist.

We also recognise that the issue of tax transparency is of international significance. However, given different cultural backgrounds and legal frameworks, reaching a global consensus will be difficult and, at the very least will take time. Consequently, our comments relate only to businesses operating in Australia.

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Purposes of a tax disclosure framework

The purpose of a tax contribution statement of greater transparency is to:

- Help build trust by enabling the stakeholders to hold companies to account; and
- Provide increased assurance to stakeholders over the level and management of tax risk.

The objectives of the disclosures should be to give an understanding of:

- A company's approach to how they manage tax and how this fits with their corporate ethos; and
- Where they pay tax and what drives this given their business, business model and the choices they make.

It is key that no information should be disclosed if this would either impact on an organisation's competitive position or would be commercially sensitive. In line with accepted practice in other areas of financial disclosure, a concept of materiality (based on revenue and tax in each jurisdiction) should also be adopted in relation to any disclosure. This concept of local materiality is also introduced in the BoT's proposed Code.

Depending on the nature of a particular business, such as the sector in which they operate, the focus and emphasis on disclosures may be different. Our experience and discussions with corporate groups, however, suggest that there are some common areas that might be included in a framework.







Business model

The purpose of a tax contribution statement is to give a greater context of the business model and the implications for tax. Areas which could be covered include:

- A broad outline of where the business operates and what this means for tax, especially corporate income tax.
- A broad description of the business model and tax attributes that impact the company's reported effective tax rate and its cash tax position.
- A high level description of the company's approach to transfer pricing.
- An explanation, where relevant, of business presence in low tax jurisdictions.
- Other explanations that might help to address apparent anomalies in published information, for example relating to taxes paid versus the number of employees in a jurisdiction.

Organisations should reflect on the level of local and global detail to provide on the overall business model. For example, the proposed Code suggests a qualitative approach to international related party dealings only as they affect the Australian business. Increasing consideration will need to be given to a holistic view of the global value chain as tax transparency requirements and expectations continue to expand worldwide.

It is critical that disclosures on the business model complement, support and reconcile with disclosures and publications such as the Annual Report and Operating and Financial Review.



Tax contribution

The purpose of a tax contribution statement is to give stakeholders an understanding of where profits are earned and taxes paid and to provide a picture of the total amount of taxes generated by a company. Considerations might also be given to other payments to governments not necessarily defined as a 'tax' including, for example, royalties and licence fees. This could be achieved by:

- Presentation of data (subject to overriding concerns about commercial sensitivity) and supporting narrative in relation to turnover, profits and taxes paid.
- A statement of taxes borne (and taxes collected) by different types of tax to give a fuller picture of the company's economic contribution (total tax contribution).
- Infographics to illustrate how a company's profits are put to use (e.g. reinvestment in the business, payments to shareholders, payments to employees, taxes paid).

The proposed Code also follows this approach as it relates to Australian taxes but suggesting that the core element be corporate income tax, with other taxes as optional additional elements as required.

Specific information in relation to material issues

The purpose of the specific information is to explain areas which might otherwise give rise to questions or misunderstandings. Such issues might include:

- Use of losses or other tax attributes brought forward from earlier periods.
- Availability of targeted tax incentives, such as research and development.
- Availability of franking credits.
- Availability of tax holidays.
- Other significant items impacting the tax paid in that territory, such as pensions contributions, impairments, or concessionary arrangements, for example, the Offshore Banking Unit regime in Australia.

The purpose of a tax contribution statement is to give stakeholders an understanding of where profits are earned and taxes paid

Is there a standard way to present data?

Different companies have divergent views on how to present tax data. Many already have to produce data under existing reporting regimes and the OECD CbCR template will soon become mandatory. Companies will want to minimise the cost and administrative burden of disclosure and therefore wish to avoid having to produce yet another set of data in a different way. A pragmatic approach is therefore for businesses to choose the form which is considered most appropriate to explain their tax position in their commercial circumstances.

Two themes emerged from our discussions. First, the general view is that simply making the OECD CbCR template public once the rules are in force is not the best approach. For example, the definition of revenue is different to the accounting definition and the template does not contain a reconciliation to the consolidated accounts as it is produced for a different purpose to the accounts. Concerns have also been expressed that, because it has been negotiated at an international level with agreement that it will only be shared amongst tax authorities under exchange of information procedures, making the template public would undermine that international process.

Secondly, some companies thought the right approach might be for accounting rules to be changed to include CbCR. The main advantage of such an approach is that it would be consistent. Disadvantages, however, include that it could create another set of rules on top of existing ones, so increasing the administrative burden. It would also likely increase the cost of external audits, and it would go against current initiatives to try to simplify accounts to make them more accessible. Changes to accounting rules also have a track record of taking a long time to take effect.

The BoT's proposed Code currently suggests increased transparency around Australian and global tax and operations in the financial statements but more limited disclosure than is contemplated for CbCR.

In conclusion

KPMG Australia's opinion is that transparency is an essential pillar in building trust. We recommend that Australian companies engage proactively with all stakeholders in the debate.

Establishing a single comprehensive framework that best serves all businesses and stakeholders is a real challenge. The different sectors in which businesses operate, how they operate, and their different stages of maturity mean that there cannot be a 'one size fits all' approach. It is clear though that the quality of the narrative is as important, if not more so, than the publication of tax-related data.

Our experience and discussions with large corporate groups strongly point towards areas of commonality regarding what might be disclosed as part of a framework, and we are seeing this borne out in practice as groups prepare their tax information and policy documentation.

This framework does not therefore attempt to answer all of the questions an organisation may have, nor does it put forward a definitive template for disclosing tax information. What it aims to do is to prompt companies to evaluate where they are in the overall tax transparency debate, and to consider how they might approach this area.

KPMG Australia's opinion is that transparency is an essential pillar in building trust. We recommend that Australian companies engage proactively with all stakeholders in the debate.

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