

# Perspective

This is one of a series of articles where experts in assurance, reporting and regulatory matters discuss recent technical and policy developments in these areas.



## Tax transparency - a new era in reporting?

**Jonathon Moss, CA, Partner, PwC**

**John Ratna, CA, Director, PwC**

**Grainne O'Halloran, Senior Accountant, PwC**

**Timothy Murphy, Accountant, PwC**



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In the past year, taxes paid have attracted global regulatory and media scrutiny. From the recent EU decision to claim \$14bn from Apple to Australia's focus on introducing new multinational anti-avoidance laws to Australian Senate hearings, companies have been under heavy and constant scrutiny over their tax affairs.



Transparency of tax contributions has been at the forefront of media attention, particularly with the OECD focusing on multinational tax arrangements. Globally, the starting point has been for companies to report taxes paid by country. With governments worldwide in budget deficit, what was originally simply a regulatory requirement for information has now, with media pressure, become an issue of corporate social responsibility. A number of non-government organisations have been active in calling for public scrutiny of taxation arrangements.



The snapshot below provides insight into the global acceptance and adoption of OECD-style private country-by-country reporting requirements, as well as the shifting focus to public disclosure.

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## Australia

- OECD country-by-country **private** reporting has been adopted.\*
- Tax authorities **publicly** release limited amounts of tax data for certain entities.
- A voluntary **public** tax transparency code has been introduced.

## Canada

- OECD country-by-country **private** reporting has been adopted.\*
- A form of country-by-country **public** disclosure is required for certain businesses in the extractive industry.

## European Union

- OECD country-by-country **private** reporting has been adopted.\* It has been further proposed to subject these requirements to **public** disclosure.
- A form of country-by-country **public** disclosure is required for certain businesses in the extractive industry as well as credit institutions.

## Scandinavia (Denmark, Finland, Norway and Sweden)

- OECD country-by-country **private** reporting has been adopted.\*
- Tax authorities **publicly** release limited amounts of tax data for certain entities.

## United Kingdom

- OECD country-by-country **private** reporting has been adopted.\* The government has the power to subject these requirements to **public** disclosure; however, this is unlikely in the absence of an international consensus.

## United States

- The United States has not ratified the OECD policy; however, similar country-by-country **private** reporting requirements have been proposed.
- A form of country-by-country **public** disclosure is required for certain businesses in the extractive industry.

*\*Note that "adopted" refers to the ratification of the OECD Country-by-Country Reporting agreement. Local legislation may range from proposal stage to implementation stage.*

## Where are we at?

In Australia, increased scrutiny of tax arrangements has resulted in the federal government, via the Board of Taxation, introducing a 'Tax Transparency Code' (TTC). The TTC is a voluntary code that companies have been asked to sign up to. To date, 33 companies representing more than 50% of the taxable income and tax payable by corporates across the ASX have undertaken to present the required information. However, the TTC is a voluntary disclosure regime. No plans have been announced by the AASB or the federal government to build the disclosures into law or into mandatory financial reporting requirements.

However, with the critical mass of companies committing to voluntarily publish the required information, questions may increasingly be asked of companies that have not yet committed to the TTC.

So, let's take a look at what the TTC actually requires companies to disclose compared with current AASB112 *Income Taxes* required disclosures.



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The TTC itself focuses on effective tax rates, being accounting income tax expense as a percentage of accounting profits. To bring the TTC to life, we've set out the TTC guidelines and included some relevant extracts from SEEK Limited.

## TTC disclosure guidelines

### Part A – minimum standard for large (>\$500M Australian turnover) and medium (>\$100M Australian turnover) businesses

#### Requirement:

A reconciliation of accounting profit to income tax paid or payable, and from income tax expense to income tax paid or payable.

#### How the requirement may be applied:

This disclosure would normally already be partly provided under the requirements of AASB 112, being accounting profit reconciled to income tax expense. Critically, this reconciliation is now extended from tax expense to tax paid/payable. In our example, SEEK Limited highlight this by providing an additional incremental reconciliation between income tax expense and current tax liability.

#### Reconciliation of income tax expense to current tax liability

	2016 \$m	2015 \$m
Income tax expense in the consolidated income statement	157.4	68.7
Add/(subtract):		
Deferred tax assets charged to income	0.9	(0.9)
Deferred tax liabilities charged to income	2.3	2.8
Over/(under) provision in prior years (current and deferred tax)	0.1	(0.7)
<b>Current tax included in income tax expense</b>	<b>160.7</b>	<b>69.9</b>
Add/(subtract):		
Tax payments made to tax authorities	(51.0)	(72.2)
Under provision in prior years (current tax)	(1.3)	(1.8)
Items recognised directly in equity	(2.2)	(10.6)
Acquisition of subsidiary's tax payable	-	1.8
Foreign exchange	0.3	1.9
Other	(0.5)	0.6
Net opening balance carried forward	7.8	18.2
<b>Net current tax liability</b>	<b>113.8</b>	<b>7.8</b>
<b>Net current tax liability comprises:</b>		
Current tax asset in the consolidated balance sheet	-	(9.3)
Current tax liability in the consolidated balance sheet	113.8	17.1
<b>Net current tax liability</b>	<b>113.8</b>	<b>7.8</b>

The Australian capital gains tax of \$84.5m from the disposal of IDP (refer to note 3 for further details) is due and payable in December 2016.

#### Requirement:

Identification of material temporary and non-temporary differences within the reconciliation.

#### How the requirement may be applied:

This already forms part of the AASB 112 disclosures within the income tax expense reconciliation.

#### Requirement:

Disclosure of the accounting effective tax rates for Australian and global operations.

#### How the requirement may be applied:



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This is an incremental disclosure. AASB 112 only requires disclosure of the consolidated reconciliation, typically with a reconciling item being the effect of foreign tax rates. The new disclosure breaks out the Australian profit and effective Australian tax rate as distinct from the global effective tax rate. Additionally, companies should endeavour to provide robust narrative if the Australian tax expense is affected by intercompany transactions where applicable.

By way of example in breaking out the effect of foreign tax rates, SEEK Limited shows the applicable statutory tax rate in each relevant foreign jurisdiction to assist readers in understanding their global effective tax rate. This expands on the single line in the consolidated income tax expense reconciliation being the overseas rate differential line item.

## (a) Income tax expense continued

### Reconciliation of income tax at the standard rate to actual income tax payable

	2016 \$m	2015 \$m
Profit from ordinary activities before income tax expense	556.8	383.9
Income tax calculated @ 30% (2015: 30%)	167.0	115.2
Tax effect of amounts that are not deductible/(taxable) in calculating income tax:		
Net taxable gain on disposal of equity accounted investment (a)	4.6	-
Fair value gain on step acquisitions (b)	-	(30.1)
Taxable unfranked dividend (c)	5.4	2.0
Financing, transaction and legal costs (d)	3.1	4.9
Tax deductible goodwill (e)	(2.4)	(3.8)
Post tax associate earnings (f)	(3.7)	(6.5)
Research and development claim (g)	(7.0)	(4.4)
Overseas tax rate differential (h)	(11.3)	(10.8)
(Over)/under provision in prior year	(0.1)	0.7
Other	1.8	1.5
<b>Income tax expense in the consolidated income statement</b>	<b>157.4</b>	<b>68.7</b>

#### Explanation of key items

- The difference between the accounting and tax gain on SEEK's disposal of its interest in IDP.
- Non-taxable gain realised as part of the JobStreet transaction.
- The unfranked portion of dividends received from IDP during the period is taxable to SEEK.
- Non-deductible financing, transaction and legal costs within the SEEK Group.
- Goodwill amortisation is tax deductible in Brazil.
- SEEK's share of profit from associates and joint ventures is taken up net of tax expense.
- Research and development incentives utilised throughout the SEEK Group.
- SEEK Group's international profits are taxed at local statutory or preferential rates varying from the Australian statutory tax rate (as shown below):

#### Local tax rates

Country (Business)	2016	2015
Australia (SEEK Australia)	30.0%	30.0%
New Zealand (SEEK NZ)	28.0%	28.0%
China (Zhaopin excluding Beijing Wangpin)	25.0%	25.0%
China (Beijing Wangpin)	15.0%	15.0%
South East Asia (SEEK Asia)	16.5%-30.0%	16.5%-30.0%
Brazil (Brasil Online)	34.0%	34.0%
Mexico (OCC)	30.0%	30.0%

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## Part B – applies only to large businesses with >\$500M Australian turnover

### *Requirement:*

Tax policy, strategy and governance summary

### *How the requirement may be applied:*

This is an incremental disclosure to what AASB 112 requires. The TTC require, at a minimum, some narrative on a company's:

- approach to risk management and governance arrangements
- attitude towards tax planning
- accepted level of risk in relation to taxation and
- approach to engagement with the ATO.

Practically, this may include disclosure of the tax payer's risk categorisation and engagement strategy with the ATO. It might also comment on the Board's involvement including whether a Board approved tax risk policy exists. Other items of narrative might include:

- the extent, if any, of group companies in low tax jurisdictions (or a positive statement if none)
- overview of transfer pricing arrangements
- extent of any foreign hybrid or related party funding structures (or a positive statement if none) and
- the extent to which tax outcomes are not aligned to economic outcomes.

Businesses also have the option of including an overview of operations, approach to engagement with other tax authorities and a description of applicable assurance regimes. Companies may wish to draw out here any particular arrangements such as use of historical tax losses or the applicability of particular tax law that results in a specific treatment - for example, trust structures that are taxed at the level of the unit holder or infrastructure companies where an effective tax rate may be lower in the early stages of project operation due to start-up costs.

### *Requirement:*

Australian tax contribution summary

### *How the requirement may be applied:*

The minimum required disclosure is an outline of Australian corporate income tax contributions.

Additionally, corporates may also choose to include details of other Australian taxes and imposts paid to governments. These would include royalties, levies, stamp duties, state taxes and all other indirect taxes. For a resources company, such taxes would be significant. Corporates may also disclose taxes and imposts collected by the business on behalf of others. For example, GST and PAYG withholdings would be included if disclosed.

### *Requirement:*

International related party dealings summary

### *How the requirement may be applied:*

This is an incremental disclosure that aims to provide a qualitative disclosure of key categories of dealings with offshore related parties which have a material impact on the business's Australian taxable income. Such disclosure would be incremental to AASB 124 *Related party disclosures* as such transactions are eliminated in a consolidated group.



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## Difficulties companies face in providing TTC information

If a company chooses to adopt the TTC disclosures, two areas of challenge arise.

First, there are no accounting standards governing the TTC disclosures. Specifically, the TTC disclosures are intended to address the total tax impost paid by a corporation. The effective tax rate disclosures within the accounting standards only focus on corporate income tax for a consolidated worldwide group.

As such, each corporation adopting the TTC would need to establish its own definition of effective tax rate for the TTC reconciliation. Pro forma adjustments, significant items, policy choices and changes in standards may all affect the resultant effective tax rate calculation. Benchmarking against industry practice will be critical for any corporate considering TTC.

Additionally, any public disclosure of an effective tax rate below the 30% statutory rate will naturally invite scrutiny. While the TTC does encourage narrative commentary, it is challenging to concisely articulate exactly why a lower effective tax rate may apply. Investor relations teams will need to be well prepared and briefed to respond to the inevitable media and stakeholder questions. In particular, they'll need to ensure that transfer pricing arrangements and narrative explanations can withstand public scrutiny.

## What's coming – political pressures on companies; transfer pricing becoming part of tax considerations

The increasing focus on taxes paid is not expected to diminish. Tensions within the OECD on how to manage multinational taxation arrangements have increasingly seen governments introducing new taxation regulations designed to catch income that flows offshore.

While the regulators have, to date, largely signalled that TTC disclosures will only be voluntary in Australia, the continuing budget crisis will only intensify pressures on companies that choose not to provide such disclosures. With a critical mass of companies already publicly committed to the code, Australian corporates should start to plan now as if they may need to adopt the TTC in the future. Complexities of transfer pricing will also increasingly come into the spotlight and a company's ability to tell its story of how its foreign and domestic units work together will be critical.

## What should companies do?

We believe the debate on tax transparency has firmly shifted. What was, five years ago, a regulatory requirement to privately share information with tax regulators has transformed into pressure to publicly share information on taxes paid. Already, the EU and the US (through Dodd-Frank legislation) are moving toward imposing similar disclosure regimes. Australian corporates should be giving serious consideration to the reputational risk in treating the TTC as simply voluntary disclosures. Getting on the front foot and raising the matter internally with stakeholders should be an immediate concern for all finance teams.