

The tax transparency code

February 2016

1 INTRODUCTION

The following Tax Transparency Code (TTC) has been extracted from the Board of Taxation report to Government “*A Tax Transparency Code*” dated February 2016.

The TTC disclosure is divided into two parts. A summary of the content of Part A and Part B is set out below.

TTC disclosure	Who	Minimum standard of information
Part A	'Large' and 'medium' businesses	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	'Large' businesses	Approach to tax strategy and governance
		Tax contribution summary for corporate taxes paid
		Information about international related party dealings

'Large businesses' should adopt Part A and Part B of the TTC. 'Large businesses' are defined as businesses with aggregated TTC Australian turnover of AUD 500 million or more.

'Medium businesses' should adopt Part A of the TTC. 'Medium businesses' are defined as businesses with aggregated TTC Australian turnover of at least AUD 100 million but less than AUD 500 million.

2 WHO SHOULD DISCLOSE?

The TTC is targeted to larger businesses. Most of the public interest is focussed on the tax affairs of large business, including both Australian-headquartered businesses and foreign multinationals.

For the purpose of the TTC:

1. An Australian-headquartered business is generally taken to mean an Australian company (or entity that is treated as a company for Australian tax purposes), or an accounting consolidated group headed by an Australian parent.
2. A foreign multinational business is generally taken to mean an accounting consolidated group headed by a non-Australian parent.

There may be a number of entities within an accounting consolidated group which are subject to the TTC. The TTC does not specify the means by which these disclosures should occur therefore groups can choose the level of aggregation or grouping of entities for disclosures under the TTC and which entity is the discloser(s). For example, groups can choose to produce one disclosure covering all relevant entities, individual disclosures by entity or aggregations of entities. This will enable groups to produce the disclosures in a manner which best matches the natural accounting and reporting systems of that organisation to mitigate compliance costs in adoption of the TTC.

2.1 LARGE BUSINESSES

The full content of the TTC (Part A and Part B) should be disclosed by 'large businesses'. 'Large businesses' are defined as businesses with a 'TTC Australian turnover' of AUD 500 million or more, calculated as follows:

- In respect of an Australian-headquartered business: the TTC Australian turnover is the turnover of the Australian entity, or the income tax consolidated group headed by an Australian parent; and
- In respect of a foreign multinational business: the TTC Australian turnover is the turnover of the accounting consolidated group headed by a foreign parent to the extent that the turnover relates to:
 - any Australian entities or an Australian tax consolidated group; and
 - any foreign entities to the extent that the turnover is attributable to a permanent establishment in Australia.

2.2 MEDIUM BUSINESSES

In addition, businesses with a TTC Australian turnover greater than AUD 100 million but less than AUD 500 million ('medium businesses') should adopt Part A of the TTC. Specifically, 'medium businesses' can adopt Part A either in their Australian general purpose financial reports or via publication of a 'taxes paid' report or another document at their option.

3 TYPES OF ENTITIES COVERED BY THE TTC

Most large businesses in Australia operate through company structures or through entities that are treated as companies for Australian tax purposes. The Board has designed the TTC with these types of structures in mind.

Unlike companies, most partnerships and trusts are 'tax transparent'. That is, the tax on profits is typically paid by the partners, beneficiaries or unit holders, rather than by the business entity. In addition, superannuation funds are taxed under special rules that significantly differ from the taxation of companies, partnerships and trusts.

Further, these types of businesses are generally not subject to the same reporting requirements as companies. In light of these differences, the code extends only to companies and entities taxed like companies.

Nonetheless, a superannuation fund, trust or partnership may wish to voluntarily adopt the TTC, by adapting its principles as far as possible. For example, it could reconcile its accounting profits to taxable income, rather than to tax paid, with an explanation as to the tax treatment of that taxable income to material categories of recipients of income.

4 WHAT INFORMATION SHOULD BE DISCLOSED?

4.1 PART A

A reconciliation of accounting profit to income tax paid or income tax payable

Minimum standard for 'large businesses' and 'medium businesses'

Businesses should disclose a reconciliation of accounting profit to income tax expense, and from income tax expense to income tax paid or income tax payable.

The reconciliation should identify material temporary or non-temporary differences.

In the interests of minimising compliance costs, inclusion of a reconciliation in the 'taxes paid' report or another document prepared at a global level is acceptable provided that reconciliation identifies material temporary and non-temporary differences. Where Australian general purpose financial statements are not prepared the rate reconciliation should be in a 'taxes paid' report or another document.

Effective tax rates for Australian and global operations

Minimum standard for 'large businesses' and 'medium businesses'

Businesses should disclose an Australian accounting effective tax rate (ETR) and a global ETR for the worldwide accounting consolidated group calculated based on company tax expense.

The ETRs should be calculated as company income tax expense divided by accounting profit. Calculation of the ETR based on company tax expense only will enable the users of the disclosure to make comparisons both to the company tax rate and to other companies.

ETRs can be calculated on different bases, inviting possible criticism that they can potentially be misleading to those seeking to understand how a given ETR compares to

the company tax rate. Businesses should clearly define the basis on which the disclosed ETR was calculated and any underlying assumptions.

Businesses in certain industries may choose to publish an additional ETR based on a 'total tax expense' figure that includes taxes other than income tax. Where businesses choose to do so, the basis on which the additional ETR has been calculated should be clearly identified.

The TTC specifies that the global ETR should be calculated 'for the worldwide accounting consolidated group' of which the Australian operations form a part.

The Board's report does not recommend that businesses publish ETRs calculated using the ATO's 'effective tax borne' methodology as part of the TTC disclosure. The Board's consultations revealed little support for publication of effective tax borne calculations, as they are too complex and not suitable for public disclosure under the Tax Transparency Code (TTC).

Role of the AASB

The Board also considers that the AASB should play a broader role in the effective operation of the TTC by developing guidance material to assist businesses in meeting the minimum standards required by the TTC. In particular, the AASB can assist the process by establishing a common definition of ETR to ensure consistency and comparability of disclosures made under the TTC. The definition should address such issues as the treatment of amended assessments, impairments, foreign currency translation, refunds and penalties.

Development of guidance by the AASB may take a period of time after the release of the TTC before it is available. This should not delay the release of disclosures under the TTC by businesses. Until this guidance is available business should adopt commonly accepted methodologies for the calculation of the ETR's based on the broad parameters outlined above (ie ETR to be calculated as company income tax expense divided by accounting profit), clearly defining the basis on which the calculation has been made and the underlying assumptions used.

4.2 PART B

Minimum standard for 'large businesses'

As set out below, Part B should include information on the business's:

- tax policy, tax strategy and governance;
- total tax contribution; and
- international related party dealings.

Tax policy, tax strategy and governance summary

Minimum standard for 'large businesses'

The tax policy, tax strategy and governance summary should provide information on the business's 'tax policy' or 'tax strategy' including its:

- 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.

The minimum standard is consistent with the proposed UK legislative tax transparency measure for all qualifying entities to publish a tax strategy on the internet.

Businesses have the option of including the following information which the Board identified as of interest to the community:

- an overview of the business's operations (perhaps adapted from directors' reports);
- its approach to engagement with other tax authorities; and
- a description of the assurance regimes it is subject to, for example, internal audit, external audit, Advance Compliance Agreements, Advance Pricing Arrangements (APAs) and ATO pre-lodgement compliance reviews.

The Board did not find it is necessary to disclose disputes with revenue authorities as part of the TTC. These will be subject to accounting or ASX disclosures if material.

Australian Tax contribution summary

The tax contribution of a business to Australia includes more than just corporate income tax.

Minimum standard for 'large businesses'

The tax contribution summary has core and optional elements, as follows:

- [Core element] disclosure of Australian corporate income tax;
- [Optional element] disclosure of other Australian taxes and imposts paid to Government, for example Petroleum Resources Rent Tax, royalties, excises, payroll taxes, stamp duties, fringe benefits tax and state taxes;
- [Optional element] disclosure of Government imposts collected by the business on behalf of others, for example, GST and Pay As You Go withholding taxes.

The Board suggests that businesses consider the use of charts, diagrams and trend data to improve communication of this information to the public.

The optionality of disclosing taxes other than corporate income tax reflects differing views between stakeholders about the merits and compliance costs involved.

International related party dealings summary

A business's dealings with international related parties have particular relevance for the 'interested users' of the TTC. There is public interest in ensuring that international related party dealings are being conducted in a manner consistent with Australian tax law and international taxation norms (the arm's length principle).

The Board considered a quantitative approach that would involve the detailed disclosure of the dollar amount of international related party dealings. However, the Board considers the disclosure of this information, apart from raising issues of commercial sensitivity, may not be meaningful to the intended users of the TTC.

The Board also considered an approach which would involve disclosure of the key categories of related party dealings as defined by the International Dealings Schedule. However, the Board considers the disclosure of this information may not be meaningful to the intended users of the TTC as these transactions may not be tax sensitive. That is they may have limited effect on the Australian tax position of the relevant business.

The Board considers that the public interest is better served by a qualitative explanation of the nature of related dealings and measures that have been put in place to manage the associated tax risks. This qualitative explanation would include, but would not be confined to, dealings which have a material impact on the business's Australian taxable income.

Minimum standard for 'large businesses'

The international related party dealings summary should 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, including the nature of material categories of dealings and the country in which the related party is located.

The Board acknowledges the risks of businesses publicly disclosing the information noted above, including the risk of reputational damage caused by misunderstanding of this information. However, the Board believes it is necessary for the TTC to include this information in light of community concern and media coverage of tax issues. Businesses may address these risks by carefully explaining the commercial context of these arrangements.

As noted above, the OECD's recommendations on Country-by-Country reporting have been implemented in Australia. Although this is an important initiative to provide the ATO with enhanced information in relation to transfer pricing, it should be noted that Country-by-Country reporting is designed as a risk management tool for revenue authorities rather than a public disclosure regime. The Board recommends against any component of the OECD Country-by-Country reporting being made the subject of mandatory public disclosure under the TTC.

International sales to Australians by foreign multinationals

The Board considered an approach under which international supplies to Australians by foreign multinationals would be disclosed in the 'taxes paid' report under the TTC.

Foreign multinational businesses can in some instances sell goods or services to Australian customers without being subject to Australian income tax. However, while there may be a public interest in the tax payments of these entities, the Board does not consider that this interest would be served by requiring foreign multinationals to disclose sales to Australian customers.

In coming to its view, the Board has had regard to the Government's Multinational Anti-avoidance law (MAAL) to combat artificial or contrived arrangements to avoid the attribution of profits to Australia through a taxable presence in Australia. The rules, took effect from 1 January 2016, create an incentive for relevant foreign multinationals to restructure their Australian-connected activities to create a taxable presence in Australia. When this occurs, these businesses will be subject to the TTC, as appropriate, in accordance with the eligibility test set out below.

For foreign multinational businesses selling to Australian customers from outside Australia in circumstances that are not a target of the MAAL, recommending disclosure of Australian-connected sales under the TTC would impose an unnecessary compliance burden, in circumstances where they are not subject to Australian income tax.