Title

What do Tax Transparency Reports tell us about tax governance and tax decision making by large corporations in Australia?

Author

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Abstract

A variety of international and domestic initiatives require companies to disclose their tax contribution and facilitate information sharing between tax authorities in different countries. The extent of international co-operation and sharing of tax details of multinational companies is unprecedented and is expected to continue to increase. Ultimately transparency expectations are not static, nor are societal demands for accountability, and as a result the expectations for tax transparency continue to shift. Tax transparency impacts the risks associated with the tax position a corporation takes and this research examines Tax Transparency Reports published by Australian companies in accordance with the Voluntary Tax Transparency Code (the Code) developed by the Board of Taxation (Australia). The Code is a set of principles and ‘minimum standards’ to guide disclosure of tax information by businesses. This examination of Tax Transparency Reports, published in accordance with the Code, examines the different approaches to tax policy, tax strategy and governance disclosed and what those Tax Transparency Reports tell us about tax governance and tax decision making by large corporations in Australia. Currently there are over 60 Tax Transparency Reports published in respect of Large Australian corporations.
The extent of international co-operation and sharing of tax details of multinational companies is unprecedented and is expected to continue to increase. Ultimately transparency expectations are not static, nor are societal demands for accountability, and as a result the expectations for tax transparency continue to shift. A variety of international and domestic initiatives require companies to disclose their tax contribution and facilitate information sharing between tax authorities in different countries. Tax transparency impacts the risks associated with the tax position a corporation takes and this research examines Tax Transparency Reports published by Australian companies in accordance with the Voluntary Tax Transparency Code (the Code) developed by the Board of Taxation (Australia).1 The Code is a set of principles and ‘minimum standards’ to guide disclosure of tax information by businesses. This examination of Tax Transparency Reports, published in accordance with the Code, examines the different approaches to tax policy, tax strategy and governance disclosed and what those Tax Transparency Reports tell us about tax governance and tax decision making by large corporations in Australia. Currently there are over 120 Tax Transparency Reports (‘TTR’) (over 3 years) published in respect of Australian company’s both medium and large as well as some non-corporate entities.

**Tax Transparency in Context**

More than ever before reports concerning alleged tax avoidance by large corporations are reported in a range of media and the public takes an interest.2 Some recent examples of aggressive tax arrangements that were reported in the media include the Panama papers, Luxembourg Leaks, Apple Euro tax decision, Google tax, Singapore sling, Uncut protests re Vodafone, Starbucks and the list could go on. Community expectations require a corporation to act responsibly with respect to taxation and corporations are concerned that they explain the basis of tax arrangements especially if reported publicly. Managing a company's

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legitimacy in the eyes of a broad stakeholder group can act as an incentive to the company executive to make voluntary disclosures relating to tax contributions.

The recent Senate Economics References Committee of the Australian Parliaments 2015-2018 (expected to report May 2018), investigating corporate tax avoidance, made publicly available transcripts of interviews and submissions for review. Whilst there is the sense that the ‘public’ require tax strategy and tax reconciliations be visible, different stakeholders in a company will have different expectations as to the essential requirements of tax transparency. Ultimately companies will need to balance the transparency of tax data with the danger of information overload and public confusion. The Code sets out a framework for what should be made publicly available with some flexibility based on company size but ultimately what a corporation does make publicly available is very much a reflection of that company’s approach to tax decision making.

Tax transparency impacts the risks associated with the tax position a corporation takes. The tax governance framework/tax risk management system of a corporation must incorporate an awareness of the relevant transparency requirements. Arguably the extent of reporting of the detail of a company’s tax strategy will impact the risk assessment of a tax position adopted. The Australian Taxation Office publishes a Report of Entity Tax Information annually detailing total income, taxable income and income tax payable of public and foreign-owned corporate tax entities with total income exceeding AU$100 million and Australian-owned private companies with total income exceeding AU$200 million. The Australian Financial Review conducted a live news feed capturing the public’s reaction to the first release of this data for 2015.³

The ATO reporting of entity tax information is a step forward for corporate tax transparency but does not explain why an entity paid little or no tax in that year. The ATO’s General Guidance provides some context (no tax doesn’t necessarily mean tax avoidance)⁴ but the onus is on the named taxpayer to provide explanations. Whilst small and medium companies may not have the resources or time to manage their tax risk comprehensively, tax decision

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³ Australian Financial Review, *Which of Australia’s biggest companies are not paying tax*, 17 December 2015
⁴ Australian Financial Review, *Companies plead with ATO to publish tax losses*, 1 March 2018
making may result in unanticipated outcomes and the exclusion of small and medium size companies from ATO reporting of entity tax information creates an uneven 'playing field'.

Recently introduced Australian measures require Significant Global Entities (‘SGEs’), for years beginning on or after 1 July 2016, to lodge general purpose financial statements with the ATO if they don’t already lodge them with the Australian Securities and Investments Commission.\(^5\) SGEs are defined as corporate tax entities that have, or are part of a global group that has, annual global income greater than AU$1 billion. These financial statements will be made available to the public and should provide a structured representation of the financial position, financial performance and cash flows of the relevant entity who prior to these rules were not required to make the financial information available. As the first SGE reporting is relatively recent, its success in enhancing corporate tax transparency remains to be seen.

In May 2016, the Board of Taxation published the Code, a set of principles and ‘minimum standards’ to guide public disclosure of tax information by businesses. The aim is for large businesses to become more transparent and educate the public about their compliance with Australia’s tax laws. The success of this voluntary Code, in achieving its stated aims, will depend on the extent to which companies see the TTR as an additional reporting burden rather than embracing the disclosures required to explain the detail of its tax contribution. Further the tax disclosures seek to change reporting habits of large business more broadly.\(^6\) In addition, the Australian Accounting Standards Board (‘AASB’) has provided guidelines on the meaning of terms such as effective tax rate (‘ETR’) for the purposes of TTR voluntary reporting.

The ATO has urged directors to be aware of the material tax positions relating to their company and to determine and approve a tax risk management system and acceptable tax risk profile as part and parcel of good tax governance. The categorisation of tax strategy and tax risk management as a corporate governance issue links tax compliance to directors’ duties and may be effective in encouraging directors to take responsibility for a company’s tax position. Directors are expected to establish a tax risk strategy and ensure compliance with that strategy through corporate governance practices and a failure to do so may not meet the

\(^{5}\) Section 3CA of the Taxation Administration Act 1953 (TAA 1953)

\(^{6}\) A Tax Transparency Code: A Report to the Treasurer, Board of Taxation, February 2016
standard of reasonable care that applies in s 180(1) of the *Corporations Act* or similar provisions in company legislation in other jurisdictions.

A variety of factors determine the level of tax risk that a large Australian company is exposed to, including uncertainty and complexity of the income tax laws, reputational concerns, and the complexity and size of business transactions. Tax transparency reporting should be part of the risk management process, involve regular checking and surveillance. Companies need to invest in technology that collects data, provides oversight of compliance and automates accurate reporting of, where relevant, income earned and tax paid country-by-country.

The tax risk management system could be used to protect a company’s reputation. The pressure on large companies to contribute to tax revenue, not just to comply with the technical detail of the tax laws, means that tax decision makers and TTRs need to ‘tell a story’ about the company’s tax contribution and convince relevant stakeholders that the company is paying the appropriate amount of tax.

It is no longer enough for the tax function to ensure compliance with the tax law but instead high-profile companies are expected to take an ethical position. What that ethical position is will be informed by regulatory provisions, shareholders, directors, tax decision makers, professional accounting bodies, consumers and any other stakeholders whose view of the company’s tax contribution would impact on their relationship with the company.

Other international initiatives require large companies, particularly multinational companies, to detail their tax contribution and facilitate information sharing between tax authorities in different countries. Initiatives include OECD Common Reporting Standards, requirements under the Reporting for Extractive and Financial Institutions guidelines, Base Erosion and Profit Shifting ("BEPS") Mandatory Disclosure requirements, automatic exchange of tax information between tax authorities and reporting on the beneficial ownership of a

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8 Base erosion and profit shifting (BEPS) refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations. Under the inclusive framework, over 100 countries and jurisdictions are collaborating to implement the BEPS measures and tackle BEPS.
corporations. In relation to information exchanged between tax authorities it is essential that the information is kept confidential by the tax authorities, unless otherwise required or agreed. Accordingly, technology has a significant impact on the effectiveness of information exchange, and the OECD offer assistance to developing countries to ensure they can implement an effective and secure tax exchange framework.

The Australian government signed up to the G20 and OECD’s BEPS recommendations including the new transfer pricing documentation standards (BEPS Action 13) and, as a result, specific entities are required to provide country-by-country tax details to the ATO. The ATO provides guidelines on the required reporting as well Master File report templates assist entities in meeting these reporting obligations. Australian Local File design differs from the OECD Guidelines, with much emphasis on collecting detailed information on international related party dealings as well as the relevant agreements in an electronic form.

Tax Transparency Reports

A review of the publicly available Australian company tax transparency reports for the tax years 2016 – 2018 indicate that 120 TTRs have been lodged voluntarily by companies and other entities and are listed in an excel spreadsheet on the ATO website. Whilst Australia has a voluntary code developed by the Board of Taxation other countries and organisations are also calling for an increase in the transparency of tax information of large businesses.9

The disclosure requirements of the Code include two parts, A and B. A summary of the content of Part A and Part B is set out in table 1 below:

<table>
<thead>
<tr>
<th>Table 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>TTR disclosure</td>
</tr>
<tr>
<td>Part A</td>
</tr>
</tbody>
</table>

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Table 1

<table>
<thead>
<tr>
<th>TTR disclosure</th>
<th>Who</th>
<th>Minimum standard of information</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>‘Large’ and ‘medium’ businesses</td>
<td>income tax paid or income tax payable</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Identification of material temporary and non-temporary differences</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Accounting effective company tax rates for Australian and global operations (pursuant to AASB guidance)</td>
</tr>
</tbody>
</table>

Part B

<table>
<thead>
<tr>
<th>Who</th>
<th>Minimum standard of information</th>
</tr>
</thead>
<tbody>
<tr>
<td>‘Large’ businesses</td>
<td>Approach to tax strategy and governance</td>
</tr>
<tr>
<td></td>
<td>Tax contribution summary for corporate taxes paid</td>
</tr>
<tr>
<td></td>
<td>Information about international related party dealings</td>
</tr>
</tbody>
</table>

‘Large businesses’ should adopt Part A and Part B of the Code. ‘Large businesses’ are defined as businesses with aggregated Australian turnover of AUD $500 million or more. ‘Medium businesses’ should adopt Part A of the code. ‘Medium businesses’ are defined as businesses with aggregated Australian turnover of at least AUD $100 million but less than AUD $500 million. In drafting the Code, the potential users of information disclosed in the TTR were broadly grouped into two categories by the Board of Taxation including ‘General users’ (the ‘person in the street’ and the community at large) and ‘Interested users’ (shareholders, analysts, investors, social justice groups, media and politicians). In evaluating the effectiveness of a TRR a consideration of the potential users is relevant.
Some descriptive details relating to the 120 TTR reports published to date are detailed in Table 2 below:

<table>
<thead>
<tr>
<th>Table 2</th>
<th>Tax Transparency Report details</th>
<th>2016</th>
<th>2017</th>
<th>2018 to date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of TTRs</td>
<td>55</td>
<td>51</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Part A only</td>
<td>5</td>
<td>4</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Part B only</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Part A and B</td>
<td>47</td>
<td>47</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Part A and partially B</td>
<td>2</td>
<td>0</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>55</td>
<td>51</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Large entity</td>
<td>43</td>
<td>44</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>Medium/other entity</td>
<td>12</td>
<td>7</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>55</td>
<td>51</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Australian and dual listed parent company</td>
<td>2</td>
<td>2</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Foreign parent company</td>
<td>1</td>
<td>10</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Australian ultimate parent company</td>
<td>52</td>
<td>39</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>55</td>
<td>51</td>
<td>14</td>
<td></td>
</tr>
</tbody>
</table>

Research Method

Leximancer, a text analytics tool, was used to analyse the content of the TTRs and to display the extracted information visually. The information is displayed by means of a conceptual map that provides a view of the TTR’s, representing the main concepts contained within the text as well as information about how they are related. This map allows the researcher to view the conceptual structure of the various documents, as well as perform a directed search of those documents. The interactive nature of the map permits the user to explore concepts, their connections to each other, as well as links to the original text. The concept maps produced quantify and display the conceptual structure of the text and can be used as a means of exploring interesting conceptual features.
TTR’s over the period 2016 to 2018 were uploaded to Leximancer and a set of ‘seed’ words were identified. Words highly relevant to the seed are continuously updated and eventually form a thesaurus of terms for each concept. Apart from adding highly relevant words to a concept, Leximancer may also add words that are negatively correlated with the concept (i.e. words that rarely appear in sentence blocks containing the concept and frequently appear elsewhere). The aim of concept learning is to discover clusters of words which, when taken together as a concept, maximise the relevancy of all the other words in the document. The Concept Map produced contains the names of the main concepts that occur within the text. These are shown as grey labels on the map.

**Results**

The automatically generated concept map produced in Leximancer, after scanning all TTR’s for the years 2016 to 2018 (as at April 2018), is set out in Figure 1 below and includes the following themes:

- Tax
- Year
- Financial
- Business
- Group
- Management
- Continued
- Share
- Australia
- TSR (Total Shareholder Return)
- Customers
- People
A second user generated concept map run in Leximancer sought to identify the extent to which TTR’s refer to ethical principles. After scanning all TTR’s for the years 2016 to 2018 the concept map is set out in Figure 2 below and includes the following themes identified:

- Ethical
- Responsibilities/responsible
- Values
- Engagement
- Disclosures
- Risk
- Sustainable
Conclusions

Not surprisingly the automatically generated concept map identifies the terms ‘tax’, ‘year’, Total Shareholder Return (‘TSR’) and ‘financial’ as key themes of the TTR’s however the importance of the business context and characteristics of the company is highlighted in themes including ‘business’, ‘management’, ‘customers’ and ‘people’. Drilling down and focusing on the references to ethical principles in TTR’s, figure 2 demonstrates that an ethical approach to tax decision making is referred to and identified in 61 hits across all documents and linked to a sense of responsibility, values, engagement, disclosure obligations, risk and
sustainability. Whilst ‘ethical’ is referred to 61 times, the reference is not comprehensive across all 120 TTR’s and in some cases the reference occurs multiple times in the one document.

In terms of participation in the voluntary code, a total of 120 TTR’s over almost three years, does indicate that a substantial majority of large and medium companies are not choosing the participate in this transparency initiative, especially as ATO data indicates that there are over 2,000 companies above the relevant turnover thresholds for voluntary publication of a TTR.