

KPMG submission

Board of Taxation

Tax Transparency Code

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Executive Summary

KPMG welcomes the opportunity to lodge a submission to the Board of Taxation (**Board**) on the development of the voluntary Tax Transparency Code (**Code**).

We support the Board's work in developing the voluntary Code for disclosing company tax related information to interested stakeholders. In preparation for our submission, we benefited from a discussion with members of the Board and its Secretariat on the Consultation Paper.

We make the following key observations in our submission:

- We broadly embrace the balance reached between transparency and the compliance burden proposed in the Code.
- The final Code could, however, articulate more clearly its envisaged flexibility (i.e. the *how* or *when* a business discloses the Code's information is left up to the judgement of the business).
- We broadly agree with the target medium and large businesses for the Code. However, given the Parliament has chosen a different revenue threshold for Australian owned private businesses in relation to the existing tax transparency regime, the Code should follow suit. As such, Australian owned private companies with annual turnover of less than \$200 million should be excluded from the Code.
- In connection with *what* a business discloses, we support, inter alia, disclosures of Australian and global effective tax rates. However, the formula of 'company income tax expense' over 'accounting profit' would benefit from greater clarity on both the numerator and denominator, not just the numerator.
- Whilst acknowledging the Code is voluntary, the Code should only apply in respect of financial year ends ending after a formal government endorsement of the Code is made public.
- We support the proposition that the Code's effectiveness should be subject to a review three years after implementation. However, we consider the final Code should articulate what might be some of the measurable criteria for assessing the success of the Code.

Detailed comments

1 Overall comments

1.1 In preparing our submission, we have benefited from a discussion with members of the Board and its Secretariat on 19 January 2016. We wish to acknowledge our appreciation of having those discussions, given that certain aspects of the proposed Code were not entirely clear to us following a review of the Consultation Paper.

1.2 Some of the key insights we gleaned from those discussions were as follows:

- (a) The key objective of the proposed Code is transparency by the relevant businesses, as opposed to comparability across businesses.
- (b) The proposed Code identifies the type of information to be disclosed, but deliberately does not prescribe *how* the information is collated or *when* and *how* the information is presented. For example, businesses are free to choose to have all the additional disclosures in a separate taxes paid report rather than in any financial statements, irrespective of whether they are preparing Australian general purpose financial statements (GPFS) or not.
- (c) This flexibility extends to the intended ‘discloser’ under the Code. Businesses have the option to choose from any of the following possibilities:
 - A tax report for each relevant entity in Australia;
 - A single Australian taxes paid report covering all operations in Australia;
 - For foreign multinationals, any existing global taxes paid report can be used to include the relevant Australian tax information desired in the Code; or
 - Any other option the business feels is most informative to the intended end users.
- (d) Businesses also have flexibility to decide *how* to present a reconciliation from accounting profit to tax expense to tax payable or tax paid. The basic disclosure principle is that there should be an expansion of the standard tax reconciliation note normally found in a set of GPFS, such that accounting profit is reconciled to income tax expense and then to income tax payable/paid. However, this later amount might be estimated income tax payable as per the financial statements, or

the tax payable amount as per the tax return, or tax paid as per any cashflow statement.

(e) Notwithstanding the flexibility discussed above, some comparability is viewed as important for effective tax rate (ETR) disclosures. That is, the Board envisages businesses should be disclosing 'company income tax expense' divided by the relevant 'accounting profit', as opposed to 'total income tax expense' divided by the relevant 'accounting profit'. This will allow greater comparability against the statutory company income tax rate and as between companies.

(f) All this flexibility is premised on the basis that the business would clearly explain how the information has been collated.

1.3 Overall, we support a voluntary code for disclosing company tax related information to provide tax transparency for interested stakeholders.

1.4 In this regard, KPMG broadly embraces the Board's approach under the proposed Code to balance end user expectations of greater tax transparency with the additional compliance burden for businesses.

1.5 We note, however, we were much better informed on the way the proposed Code is intended to operate having regard to the abovementioned insights.

1.6 Accordingly, we recommend that the final Code should more clearly articulate these insights to assist businesses and end users better understand the scope of the Code.

2 Who should disclose?

2.1 We broadly support the target businesses who should disclose under the proposed Code. We make two submission points for the Board's consideration.

2.2 **Articulation of flexibility.** This recommendation represents a specific example of the recommendation made in paragraph 1.6 above. That is, the Code would benefit from better articulation of the flexibility for businesses to choose the discloser(s) within an economic group. The Consultation Paper currently leaves open, who within an Australian-headquartered business or a foreign multinational business should disclose the requisite information under the Code.

2.3 The discussion with the Board was informative of the Board's intention to leave this choice open depending on what best fits an economic group's existing systems. The final code would benefit from this clarity.

2.4 **Treatment of certain private companies.** The Consultation Paper does not distinguish between public and private businesses. The same turnover thresholds apply to determine if such businesses are within the ambit of the proposed Code. Whether there should be a different threshold between private companies and public companies is debateable. However, given the Parliament has chosen a different threshold in relation to the Australian Taxation Office (ATO) website publication of tax return data, the Code should follow suit. We therefore submit that Australian owned private businesses with annual turnover of less than \$200 million should be excluded from the voluntary Code.

2.5 Whilst acknowledging that the proposed Code and the ATO tax transparency rules will always have inconsistencies, in the case of Australian owned private businesses, we recommend alignment in the interests of simplicity for Australian private businesses.

3 What should be disclosed – Part A?

3.1 **‘Rate reconciliation’ and temporary and non-temporary differences.** We support the disclosure of a rate reconciliation and an explanation of material temporary and non-temporary differences by all impacted medium and large businesses.

3.2 **Effective tax rates.** We are also supportive of a standard definition of the company ETRs. Indeed, we make the observation that disclosure of three sets of ETRs would probably be required to the extent that the Code’s disclosures are embedded within a set of Australian GPFS. That is, a combination of the mandatory requirements of the Australian accounting standards¹ and the voluntary requirements of the proposed Code are likely to require disclosure of the following:

- (1) **Total tax expense ETR:** total income tax expense divided by global accounting profit, which would be disclosed in a GPFS pursuant to relevant accounting standard requirements;

¹ We recognise there are two ways that a company can explain the relationship between tax expense and accounting profit: (1) numerical reconciliation between tax expense and accounting profit multiplied by the applicable tax rate (e.g. 30%), or (2) numerical reconciliation between the average effective tax rate and the applicable tax rate. Where a company chose option (2), three sets of ETRs would probably be required under the Code to the extent disclosures are embedded within GPFS.

- (2) **Total company income tax expense ETR:** global company income tax expense divided by global accounting profit. This appears necessary under the Code; and
- (3) **Australian company income tax expense ETR:** Australian company income tax expense divided by Australian accounting profit. This appears necessary under the Code.

3.3 The Consultation Paper argues it is important that the numerator in (3) above should *not* include taxes that are not company income taxes (e.g. various resources rent taxes). We observe that guidance on the numerator and denominator in (1) above can come from the accounting standards, but in the case of (2) and (3) above, these are the product of the proposed Code.

3.4 We recommend the proposed Code should provide guidance on both the numerators and denominators in (2) and (3) above, not just the numerator in (3). If it is the Board's view that there is some degree of choice in some of the numbers, then the Code should expressly state so. For example, if the accounting profit number can come from consolidated financial statements, or standalone financial statements, or even tax return disclosures of profit, then the final Code should say so.

4 What should be disclosed – Part B?

4.1 We are broadly supportive of recommended Part B disclosures by large businesses.

4.2 As part of the final Code, it would be useful to point out that not all entities that may fall within the scope of the Part B disclosures would have an ATO risk rating and, in some circumstances, there would be multiple ratings for multiple taxpayers in the economic group.

5 Other comments

5.1 The Consultation Paper considers that the Code should be in operation for the 2015-16 financial reporting season. We consider that it would be fairer if the Code was only applicable for financial years ending after a formal government endorsement of the Code is made public.

5.2 Finally, we support the proposition that the Code's effectiveness should be subject to a review three years after implementation. However, we recommend the final Code should set out criteria for assessing the success of the Code. As a simple example, one measure of success will be the percentage of relevant businesses that have

adopted the relevant Code over the three years and the trends over that period.
Another example might be comparing disclosures under Australia's Code as against other international disclosure regimes, three years on.