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Responsible Tax

Tax transparency – developments in 2014

Contents

Executive summary

More tax reporting to more stakeholders

Companies are under increasing pressure to report more about their taxes through various channels, as the public debate around the tax contribution of large corporates rumbles on and regulators respond. Indeed, individuals responsible for reporting taxes not only need to keep an eye on mandatory requirements as they expand and evolve, but also trends in additional, voluntary reporting. Doing all this while grappling with existing processes and systems presents a key tax management challenge for 2015.

Mandatory reporting became more challenging in the year as corporate reporting bodies such as the Finance Reporting Council (FRC) and Securities and Exchange Commission (SEC) have further defined their expectations in relation to tax disclosures. The bar rose still further for many large groups that are affected by the new reporting regimes that have been introduced or are under consideration within the OECD, European Union, the US and certain industry bodes. In responding to these requirements, many have done the minimum necessary to comply.

Going beyond what must be reported, however, is becoming increasingly common. FTSE 100 companies have voluntarily increased tax disclosure in their financial reporting by 33% and some have responded to new reporting requirements by including additional tax information in these targeted disclosures. The result of the ongoing call for tax transparency is in some cases also seeing tax become part of a corporation's social responsibility reporting.

In responding to this evolving agenda, tax professionals within companies are clear that the need for high quality mandatory tax reporting should be their prime focus. At the very least, companies should understand what is required to comply, engage with stakeholders across the business and have well-oiled processes to do so. In many cases, this will require changes to systems, as making do with what may have served old requirements becomes too difficult.

Most will want to consider what new risks such additional reporting may give rise to – one option increasingly being considered is the use of analytics to pre-empt the thinking of tax authorities and other users of the information. Some are reviewing their current tax disclosures through a non-tax audience lens and assessing whether there might be benefits to their business from increasing, or at least refining, what they disclose voluntarily.

Looking forward, it seems unlikely there will be a let up in the demands for increased tax reporting. In the UK political will supports more tax reporting outside the financial statements, which can be expected to feature as a popular topic in the lead up to the election in May 2015. Many new regulatory reporting requirements will become live with more in the pipeline. More companies are likely to be asked to report tax in more detail and in an increasingly globally consistent way.

In this update to our 2013 tax transparency paper, part of Deloitte's Responsible Tax series, we:

- Discuss the developments in the reporting of taxes in the financial statements across the FTSE 100 during 2014;
- Comment on trends in how large corporates are responding to increasing demands for information; and
- Look ahead to how the reporting environment may evolve yet further in 2015 and beyond.

Looking forward, it seems unlikely there will be a let up in the demands for increased tax reporting

2. A look back at 2014

The pressure to manage taxes effectively continues to grow.

In our previous paper – *An integrated approach to tax transparency* – we observed that there had been an increase in the profile of tax with an ever widening spectrum of stakeholders taking an interest in what has historically been seen as a niche technical subject. Businesses responded by reporting more, establishing or revisiting their tax policy and strategy, and critically assessing how much comfort they could have in their numbers by reviewing the underpinning processes and controls.

The trend continued in 2014 with companies facing interest from a number of directions. The expectation has not lowered in respect of basic, mandatory tax reporting. But in addition, increased attention is being given to decide how much tax information should be reported on a voluntary basis.

Companies have voluntarily increased the amount of tax commentary in their financial reports. There is a more global flavour, driven by various 'country-by-country' reporting requirements, and an increasingly social and political element. The pressure to manage taxes effectively continues to grow.

There are also various tax transparency initiatives – the table in the appendix to this paper contains a comparison of these initiatives and the reporting criteria they include.

Mandatory reporting

While the Responsible Tax agenda is often associated with the choice to report tax in a variety of ways, we should not forget that accounting standards require tax to be reported in the financial statements. The mandatory requirement to report tax was not new for 2014 but bodies such as the FRC and SEC are examples of important stakeholders expressing views on the way tax should be disclosed.

The FRC issued its annual Corporate Reporting Review on 14 October 2014. The FRC's assessment is based on a review of 271 sets of reports and accounts in the year to 31 March 2014, of which 100 (37%) companies were approached for further information and explanation. One of the ten areas of common challenge identified by the FRC is taxation. The FRC noted that many of its questions were prompted by a lack of availability of sufficient information for a reasonably informed reader.[1]

Similarly, SEC officials recently said at an American Institute of Certified Public Accountants conference on 9 December 2014 that many US public companies are not providing sufficient information regarding their foreign earnings in corporate financial filings.

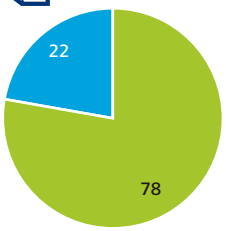
1 © The Financial Reporting Council Limited (FRC). Adopted and reproduced with the kind permission of the FRC, 8th Floor, 125 London Wall, London EC2Y 5AS. All rights reserved. For further information, please visit www.frc.org.uk or call +44 (0) 20 7492 2300.

Voluntary reporting

Following a review by Deloitte of this year's UK FTSE 100 group's financial statements, we noted an increase of 33% in instances of voluntary tax disclosure across the various categories. The biggest changes were the increase in commentary on tax policy and strategy, an increase in disclosure of taxes paid (sometimes positioned as 'contribution' to government), and some explanation of what has driven the Effective Tax Rate (ETR).

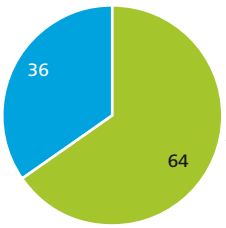
Voluntary tax disclosures in publicly available FTSE 100 accounts as at 31 July 2014

ETR drivers



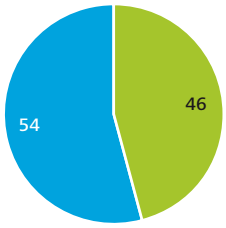
- 78 (2013: 62) groups provided narrative disclosure explaining why the effective tax rate differed from the expected statutory rate and/or explained variances year-on-year.

Governance



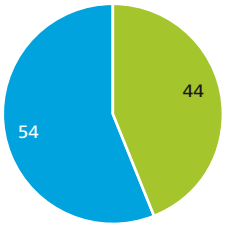
- 64 (2013: 60) groups made some disclosure of tax-related governance. Of these:
- 7 (2013: 8) made partial reference (e.g. mentioning that the Audit Committee had reviewed tax accounting judgment areas).
- 57 (2013: 52) provided fuller details, setting out processes for setting and monitoring adherence to tax policies and strategies.

Taxes paid/contribution



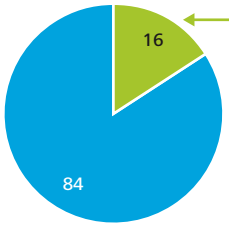
- 46 (2013: 32) groups disclosed total taxes paid/tax 'contribution'. Of these:
- 6 (2013: 12) made partial disclosure, setting out total taxes paid with no further analysis.
- 40 (2013: 20) disclosed the split between various categories of tax.

Uncertain tax positions



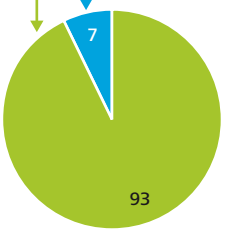
- 44 (2013: 32) groups commented on uncertain tax positions, either those for which a provision had been recorded, or those deemed to be a contingent liability.

Geographical split



- 16 (2013: 8) groups split tax payment disclosures on a geographical basis. Of these:
- 8 disclosed payments on a regional basis.
- 8 disclosed payments on a jurisdictional basis.

Tax havens



- 93 (2013: 96) groups made no reference to the use of tax havens.

Of the 7 that do:
- 2 groups made oblique reference to overseas operations being trading in nature.
- 2 groups specifically stated that they did not undertake tax planning involving the use of havens.
- 3 groups mentioned they had operations in countries that would commonly be described as tax havens.

Deloitte member firms are undertaking similar reviews across Europe, with early indicators suggesting a slightly different trend. While tax reporting is increasing, the additional disclosure is less prevalent in financial statements and more commonly disclosed in statements via other reporting media such as the company website.

In Deloitte's EMEA Dbrief webcast 'Reporting tax transparency – trends in public disclosure' on 9 December 2014, 60% of attendees polled felt there was an increase in the level of interest in their tax reporting and broader tax communications in the last 12 months, and only 11% expected not to change the way in which they report and otherwise communicate their tax position over the next 12 months.

Describing your tax position is not limited to the tax content of your financial disclosures. The OECD, industry regulators, US legislators and the European Union have new and emerging reporting requirements which incorporate tax.

The liberal use of the term 'country-by-country reporting' for a variety of different measures is a source of some confusion.

Country-by-country compliance (to tax authorities only)

The G20 countries asked the Organisation for Economic Cooperation and Development (OECD) to propose measures to tackle base erosion and profit shifting (BEPS). One of the 15 actions is for enhanced transfer pricing documentation, including a new requirement for reporting income, tax and some economic measures by country to tax authorities. The country-by-country information is intended to act as a high level risk assessment tool for tax authorities to help them prioritise their resources for audits. The intention is that the template (the format of which is now known) will be shared with tax authorities, although the mechanism for this has yet to be confirmed.

The template will provide a combination of financial and economic factors by country, including turnover, profit, taxes paid and accrued, together with number of employees and capital.

Some companies are responding by carrying out a dry run in 2014 or 2015 to assess the data gathering process and to see what their data looks like. The first reporting period has not been announced but is thought likely to be 2016, which means there is a need to act quickly to allow time to make changes should any be required. It is expected that the OECD will set the first dates for BEPS documentation when the sharing mechanism is agreed by February 2015.

Public disclosures at country and project level

The EU has introduced public country reporting requirements for banking and capital markets under article 89 of the EU Directive 2013/36/EU, commonly referred to as the Capital Requirement Directive IV (CRD IV). At present, tax information is not made public, pending a review by the European Commission. Extractive and forestry industries have a different requirement for public payment accounting under the EU accounting directive.

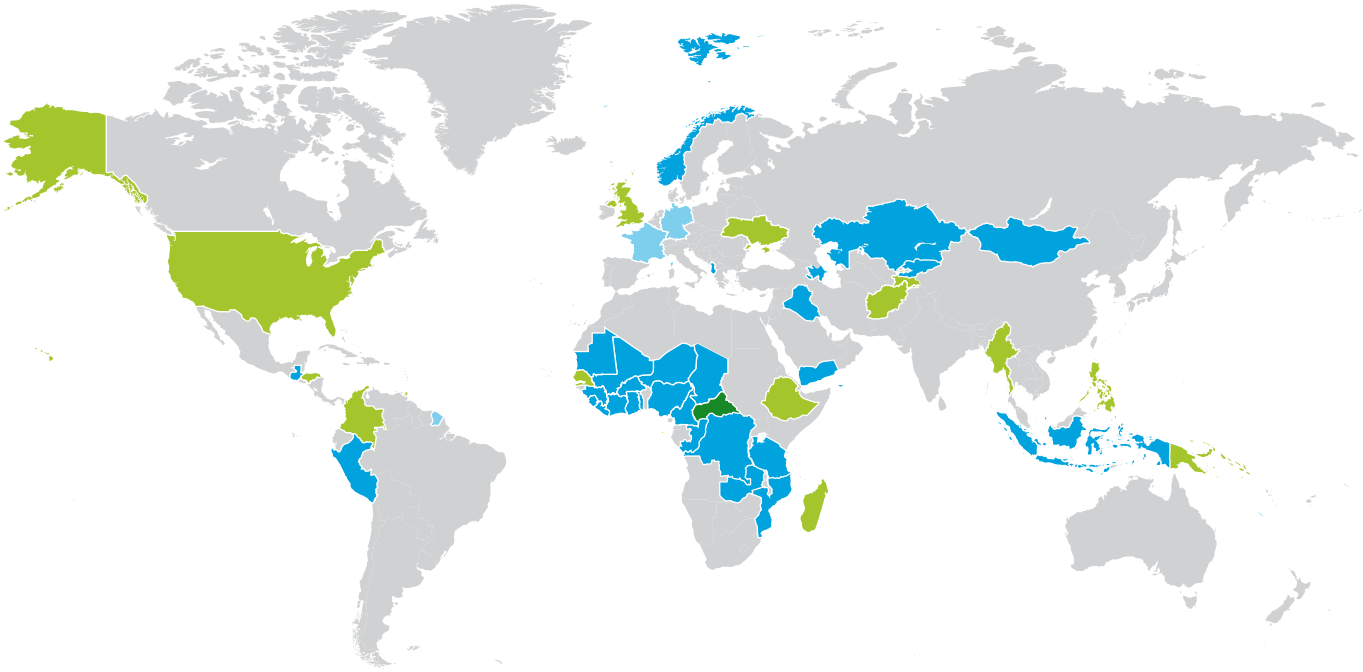
Describing your tax position is not limited to the tax content of your financial disclosures. The OECD, industry regulators, US legislators and the European Union have new and emerging reporting requirements which incorporate tax.

The first disclosures under CRD IV were due by 1 July 2014. Companies took different approaches, with some choosing to disclose extensive country breakdowns well beyond CRD IV requirements, while the majority chose to limit disclosure to the requirements prescribed.

The first disclosures under the EU accounting directive for extractive and forestry industries are generally expected to come into effect from 1 January 2016, although the UK government has accelerated this by a year to 1 January 2015 with the UK regulations coming into force on 1 December 2014. Meanwhile, other non-EU jurisdictions such as Canada and Japan have also progressed similar regimes. Payment accounting is established by a calender year and is intended to make it clear how much revenue is received by resource-rich countries from companies licenced to extract minerals, oil and gas, and timber.

The Extractive Industries Transparency Initiative, or EITI, accepted the UK on 15 October 2014 as a candidate country during its board meeting in Myanmar. The EITI provides a standard for transparency in the governance of a country's oil, gas and mining resources. The standard covers issues such as contracts, the awarding of licenses and the tax regime governing the sector. It requires separate reporting from governments on revenues received and from companies on the payments made. An independent administrator – usually an accounting firm – reconciles these figures under the guidance of a multi-stakeholder committee with representatives from government, industry, and civil society. The information on the sector and its impact on the economy is widely published.

EITI countries



- EITI Candidate Country – implementing EITI, not yet meeting all requirements
- Suspended – Compliant/Candidate status is temporarily suspended
- EITI Compliant Country – meeting all requirements in the EITI standard
- Other

Source: https://eiti.org/countries

The trend for regulators and other bodies to seek increased tax disclosure seems set to continue.

A number of other draft European regulations covering country reporting for all companies, irrespective of industry, were prepared during 2014, although these have yet to progress.

The trend for regulators and other bodies to seek increased tax disclosure seems set to continue. A significant challenge for companies is to keep track of all the requirements emerging globally.

Tax in other areas of reporting

Other areas of corporate reporting now include tax.

On 11 September 2014, The Dow Jones Sustainability Indices (DJSI) report was released, which included 'tax strategy' as a criterion for the first time. The index is intended to help investors take account of sustainability when assessing their portfolios. For some companies, the index has become an important benchmark of their sustainability credentials, with some including a target rating in their published KPIs.

Tax Strategy Questions in the Dow Jones Sustainability Questionnaire

1. Tax Strategy – Does your company have a tax policy/principles/strategy in place which indicates your approach towards taxation? Please indicate if this policy is publicly available and provide supporting evidence.

2. Tax Reporting – Does your company publicly report on key business, financial and tax information for regions or countries in which you operate? Please provide the weblink for where this information can be found.

3. Do you provide a public explanation of your effective tax rate which addresses why your tax rate may differ from the expected tax rate in the respective countries where you generate profits? Please provide supporting references.

4. Do you evaluate the risks of taxation on future company value creation? If you do risk evaluation, please indicate which risks you have identified as being material, also including business risks, and provide supporting evidence.

Source: http://www.robecosam.com/images/sample-questionnaire.pdf

The Lloyd's Risk Index 2013 identified tax as the highest risk (up from number 13 in 2011) in their survey of global business leaders' perceptions of the greatest risks to their business and the level to which they feel prepare to deal with them. Evidence from 2014 supports this as the increase in board interest in tax suggests.

CORPORATE TAXATION – A NEW GLOBAL PRIORITY

The public scrutiny given to corporate taxation has become increasingly intense over the last two years, with governments and the taxpayer alike demanding greater transparency and changes to legislation. Since 2011, this pressure has clearly been felt by respondents, who now rank the risk of high taxation as their highest overall risk, up from number 13 in 2011. In the US, the priority scores given to this risk are particularly high.

Source: http://www.lloyds.com/~/media/Files/News%20and%20Insight/Risk%20Insight/Risk%20Index%202013/Report/Lloyds%20Risk%20Index%202013report100713.pdf

The concept of a 'Fair Tax Mark' has been introduced in the UK by a non-governmental organisation seeking to raise the profile and importance of companies explaining their tax position clearly. The first companies were awarded the Fair Tax Mark in 2014, including FTSE 100 energy company SSE, who has publicised this in recent advertising.

The Lloyd's Risk survey of global business leaders' perceptions of the greatest risks to their business identified tax as the highest risk.

3. The evolving response of business

Finding ways to do more with less

Ask any tax department if they have more tax reporting to do today than 12 months ago, and the answer will be a consistent 'yes'. Ask whether they have had a chance to improve the quality of their source data, reengineer their processes or implement new systems, then the answer is likely to be less consistent.

There is greater opportunity to leverage the high profile tax now holds to help deliver improvements to make the tax reporting burden more manageable and efficient. Indeed, the improvement may be a necessity as the new reporting regimes continue to come on-stream.

Finance functions are increasingly taking account of tax requirements in their large transformation projects and tax departments should make sure they are involved closely to mitigate risks and drive efficiencies.

HMRC is seeking evidence of how the tax policy is 'lived and breathed'.

Manage the stakeholders

Formalising an approach to both traditional and the newer breed of stakeholders is generally a new exercise for tax departments. The financial community and tax authorities are the traditional focus, albeit now with increased demands. Employees, customers, suppliers and broader society collectively represent the more recent public interest in tax and require new and deliberate consideration.

Non-executive directors increasingly bring tax matters to the board's attention, prompting companies to seek input from a range of departments including public relations, investor relations, internal audit and other internal functions. The tax department is generally expected to manage messaging across these functions appropriately, in a strategically consistent way.

Revisit tax policy and strategy

In light of the broader attention on tax, companies are taking a fresh look at their tax disclosures. With new audiences come new risks. Does the tax policy anticipate these new risks? Should the tax strategy change in light of them?

Companies are certainly taking stock of their current approach to tax matters, the governance infrastructure and external communication. There are so many routes to communicate externally from a business that a strong governance framework, embedded in the way the business operates, is the only realistic way to keep on top of it.

HMRC agrees and Customer Relationship Managers are routinely asking for the organisation's tax policy, and seeking evidence to show how it is 'lived and breathed' by the relevant parts of the business.

Increase confidence in the numbers

Ultimately there may come a point where the reporting of tax to the tax authorities and others externally cannot be delivered on data, processes and systems that were set up only for tax compliance and year end calculations.

The benchmark is higher and so tax departments are seeking ways to feel more able to rely on the numbers they collect as early in the process as possible. In a recent poll[2] the top priority from the audience of over 120 CFOs in respect of tax reporting was to improve tax data accuracy. Where they are successful, they are able to cut out numerous checks and balances which are so often in place, especially where the process is very manual or data re-work heavy.

Analytics is one window to data that may not previously have been assessed in detail or which has demanded too many resources to analyse, with the result that it may be hiding risk or over prudent assumptions. By opening that window, companies can increase confidence by better understanding what lurks beneath an otherwise impenetrable volume of data. This unlocks the potential to save time spent manually trawling through account codes or invoices and instead provide evidence that the organisation, and by extension the tax authority, can have confidence in the numbers. This may give rise to a commercial benefit where greater accuracy proves that the previous position was too prudent.

Accepting risk or a prudent commercial position is less acceptable as the microscope now passes over the way the tax department functions.

2 The Future of Tax Provisioning webcast on cfo.com http://pages.cfo.com/the_future_of_tax_provisioning_register_webcast.html?p=ARCHIVE

4. Where next?

The proliferation of reporting requirements seems set to continue with any hope for sensible consolidation between the various regulators and legislators a longer term target.

Financial Secretary to the Treasury David Gauke MP has confirmed that the UK will adopt the OECD's Transfer Pricing Documentation proposals, including country-by-country reporting. The current coalition government has not made any suggestion that companies should be required by statute to enhance public reporting of taxation, although the opposition Labour party has proposed additional (unspecified) reporting.

The European Council of Finance Ministers has decided not to extend public reporting beyond the banking sector – but has asked the European Commission to conduct a review in 2018. At the same time many of the long talked about transparency initiatives continue to come on stream as they become live reporting obligations. CRD IV will also come into its second phase with additional reporting requirements and decisions with regard to the public vs. private disclosure of some of that information.

The OECD's BEPS project continues to broaden its reach with new discussions with non-OECD countries each week. The target appears to be as close to a global consensus as possible. The BEPS project recommendations are expected to be finalised by December 2015 and there will then be a discussion about a multilateral convention. However, it is widely expected that the transfer pricing documentation rules will be finalised in Spring 2015, ready for countries to put into legislation with the likely aim for the first reports to be submitted in 2017.

There is arguably a tax reporting revolution underway that is set to gather pace, to modernise outdated legislation, and to seek greater global co-ordination than ever before. Companies need to work hard to keep up with the changes and reflect on the reputational and organisational impact both internally and externally.

Appendix: Comparison of tax transparency initiatives

Reporting requirement category	Reporting requirement detail	Tax Transparency Initiative						
		Base Erosion and Profit Shifting	Capital Requirement Directive IV	Extractive Industries Transparency Initiative	Dodd-Frank	European Union Accounting Directive	Publish What You Pay	Tax Justice Network
Audience for reporting	Reported to tax authorities	✔	✗	✗	✗	✗	✗	✗
	Reported publicly	✗	✔	✔	✔	✔	✔	✔
Scope of companies		All multinational companies	Financial services	Extractive industries				All companies
Names of countries of operation		✔	✔	✔	✔	✔	✔	✔
Names of companies trading in each country		✔	✗	✗	✗	✗	✔	✔
Financial performance by country:	Sales: total only	✗	✔	✗	✗	✗	✗	✗
	Sales: to third parties	✔	✗	✗	✗	✗	✔	✔
	Sales: to other group companies (downstream ops for PWYP)	✔	✗	✗	✗	✗	✔	✔
	Purchases/costs: third party	✗	✗	✗	✗	✗	✗	✔
	Purchases/costs: intra-group	✗	✗	✗	✗	✗	✗	✔
	Finance costs: third party	✗	✗	✗	✗	✗	✗	✔
	Finance costs: intra-group	✗	✗	✗	✗	✗	✗	✔
	Production costs (extractive industries)	✗	✗	✗	✗	✗	✔	✗
	Development costs (extractive industries)	✗	✗	✗	✗	✗	✔	✗
Labour costs		✗	✗	✗	✗	✗	✗	✔
Employee numbers		✔	✔	✗	✗	✗	✗	✔
Pre-tax profit		✔	✔	✗	✗	✗	✗	✔
Tax charge in detail by country:	Current tax charge	✔	✗	✗	✗	✗	✗	✔
	Deferred tax charge	✗	✗	✗	✗	✗	✗	✔
	Liabilities owing for tax and equivalent charges (opening & closing)	✗	✗	✗	✗	✗	✗	✔
	Deferred tax liabilities (opening & closing)	✗	✗	✗	✗	✗	✗	✔
	Corporate Income tax paid (cash basis)	✔	✗					
	Tax payments to government (corporate income tax and other taxes on income or profit)	✗	✔	✔	✔	✔	✔	✔
	Subsidies received	✗	✔	✗	✗	✗	✗	✗
Additional tax payment detail for extractive industries:	Production entitlements: host government's	✗	✗	✔	✔	✔	✔	✔
	Production entitlements: national state owned company	✗	✗	✔	✔	✔	✔	✔
	Other taxes on production	✗	✗	✔	✔	✔	✔	✔
	Royalties	✗	✗	✔	✔	✔	✔	✔
	Dividends	✗	✗	✔	✔	✔	✔	✔
	Production, signatory, discovery and other bonuses	✗	✗	✔	✔	✔	✔	✔
	Licence fees, rental fees, entry fees and other considerations for licences and/or concessions	✗	✗	✔	✔	✔	✔	✔
Physical fixed assets:	Costs and net book value by country	✗	✗	✗	✗	✗	✗	✔
	Names and locations of property in each country	✗	✗	✗	✗	✗	✔	✗
	Tangible assets other than Cash and Cash Equivalents	✔	✗	✗	✗	✗	✗	✗
Details of gross and net assets in total by country		✔	✗	✗	✗	✗	✗	✔
Stated capital		✔	✗	✗	✗	✗	✗	✗
Accumulated earnings		✔	✗	✗	✗	✗	✗	✗
Production volumes (extraction)		✗	✗	✗	✗	✗	✔	✗
Reserves volumes (extraction)		✗	✗	✗	✗	✗	✔	✗
Will these disclosures be audited?		✗	✔	✗	✗	✗	✔	✗

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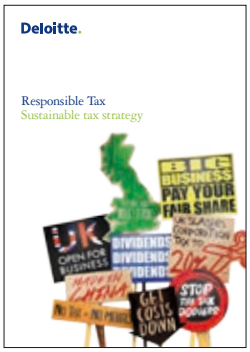
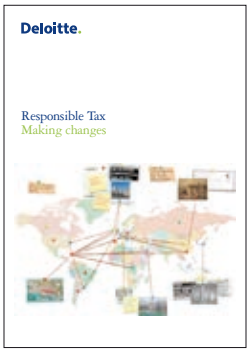
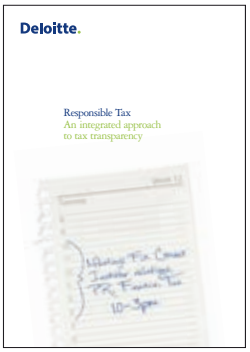


Sustainable tax strategy



Making changes



An integrated approach
to tax transparency

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