Tax and Financial Policy

Position Statement

Tax transparency: The EU proposal for general country-specific reporting requirements

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At the G 20's initiative the OECD has submitted an Action Plan on Base Erosion and Profit Shifting (BEPS) which, amongst others, includes the creation of transparency in the field of tax evasion. In this regard G20 together with the OECD support a bilateral and/or multilateral system of automatic exchange of information between tax authorities as from 2015. BDI is broadly supportive to increase tax transparency and welcomes the plans to introduce a bilateral and/or multilateral system of automatic exchange of information between the tax authorities.

Regardless of this initiative, a proposal for an expanded country-by-country reporting (CBCR) for all entities over a certain size is currently being prepared by the EU institutions upon Council's request to introduce it to the new Accounting Directive (2013/34/EU in the following DIR 34) in addition to CBCR rules already introduced for undertakings active in the extractive industry and the logging of primary forest. With such a proposal on a broad tax transparency the EU is aiming to restore public confidence in a fair and efficient tax system. The proposal is supported both by the European Commission and the European Parliament. Already in the course of consultations on the implementation of the country-by-country reporting for extracting industry, the European Parliament has required a further expansion towards other industrial sectors. The current debate in the European Parliament shows that this option will continue to receive support. An expanded CBCR requirement possibly will be included in the proposal of introducing mandatory reporting on non-financial information.

1. Proposal for a general country-specific reporting requirements

The proposal possibly requires additional disclosures for large undertakings and public-interest entities with the average number of employees during the financial year exceeding 500 as follows on

- turnover
- number of employees on a full time equivalent basis
- profit or loss before tax
- tax on profit or loss
- public subsidies received.

The required information has to be disclosed in notes of the financial statements and has to be audited in line with existing European audit

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rules (Directive 2006/43/EC). This proposal is based on requirements already in place for financial institutions' reporting (CRD Directive for Basel III implementation), whereupon these reporting requirements are introduced as an Annex to the financial statements and should be published and audited in line with existing European audit.

In addition to that, there are plans to introduce a supplement reporting requirement on tax planning arrangements.

2. Accountants' assessment of the country-specific reporting requirements

2.1 Required data/figures would not be comparable with one another

The required figures are not available under the same accounting regimes. Not all entities within the scope apply the same accounting principles. Furthermore, there is no clear evidence on the companies to be consolidated within a group that could fall under the reporting obligation. Information on tax expenses of non-fully consolidated companies is not available. Whereas accounting information could be translated to international agreed standards the information on tax expenses based on current tax legislations is not comparable in itself. Another aspect of non-comparability concerns deferred taxes which have to be accounted for under IFRS but maybe not under local accounting regimes. These figures per se would therefore not be comparable. Thus the required data won't be comparable within one group, different companies and different countries with the consequence of misinterpretations.

In addition, non-comparable standards would be set if companies were obliged to describe tax planning arrangements as proposed by the Committee on Economic and Monetary Affairs. This description to be disclosed to the financial statements should include "aggressive tax planning arrangements", "transfer pricing arrangements", and "permanent establishment decisions". Although there is an on-going public discussion about "aggressive tax planning", there is currently no definition available and there is not even a common understanding of exactly what this term means. As a result, different meanings are attributed to the above mentioned term due to different languages and cultural characteristics.

2.2 Required data will not be available in the requested quality

The reporting requirements in conjunction with the consolidated financial statements have to be performed, analysed and audited in a Fast-Close-Processes' limited timeframe. A country-specific reporting request in the required quality will stretch existing resources. As such, the whole financial reporting as well as the data quality might suffer. Furthermore the required data suggest a mere spurious accuracy. Considering that final tax assessments are only available years later by the time of publication and that deferred taxes will be added to the figures, the quality of the transparency achieved is far questionable.

2.3 Required data will impose costs on business

The provision of supplement audited data from other accounting regimes than IFRS will lead to unmanageable tasks and supplement expenses. Existing systems, time and organizational framework of the year-end closing must be adjusted. Already today companies are struggling to streamline the reporting in order to improve the communication with investors and other constituents. Any requirement to report selected audited figures of separate legal entities would lead to a compulsory audit of these entities, while currently these entities without material effects for group reporting may be out of the regular audit and consolidation scope. Thus specifically for those companies being not relevant from an investor perspective there would be an increase in time efforts and costs for the company without justifiable benefit for the decision-usefulness of the financial statements. Therefore delays in reporting would not be accepted by investors.

2.4 Required data will expose companies to competitive disadvantages and criminal penalties

An introduction of mandatory CBCR for large undertakings will put European companies in a competitive disadvantage compared to companies in other jurisdictions that will not fall under similar reporting requirements. This point was recognized by the Commission in their own Impact Assessment of the introduction of CBCR for the extractive and forestry industry and is certainly valid for a proposal to introduce a general CBCR requirement for large undertakings. It is also obvious that required information to be disclosed could be commercially very sensitive, especially in those cases where a company has only one or few customers in a particular country. Furthermore, it could put companies at risk in third countries where contractual or even legal prohibitions may exist.

For that reason the exemption rule in Article 18 (2) DIR 34 should applicable for the required information of an expanded CBCR. Similarly, the breakdown of net turnover by the field of activity or geographical markets- where this would likely cause significant harm to undertakings- is not mandatory. Moreover, the breakdown of revenues, gains, losses and taxes by Member States/third countries by an expanded CBCR shouldn’t be mandatory under the same circumstances. Bearing in mind existing conflicts in legal systems with transparency requirements, it should be possible to omit the information when an affected undertaking is threatened by the reporting obligation penalties in a particular country.

3. Tax experts’ assessment of the country-specific reporting requirements

3.1 Misleading data

The provided information can be widely interpreted, or even misleading, whereas the aim is to give clear rather than complex information to stakeholders including the general public. BDI fears that instead of improving transparency, expanded country-by-country reporting will force entities to disclose certain data out of context. This would neither improve tax compliance in general- an increased understanding of the underlying tax issues - nor the understanding of the tax position of the specific company. This is especially the case if profits are combined with either none or relatively low tax expenses.

Amount-related data on country-specific tax expenses itself, as a general rule, is not self-explicable. In this regard it should be borne in mind, that determination of tax expenses - in contrast to the consolidated financial statements – does not follow international standards but the country-specific taxation law with number of national particularities. Country specific tax rates would not be enough to understand the amount-related data on tax expenses, since they depend on the tax determination base respectively. In order to understand tax expenses more detailed presentation of tax calculations with explanation of complex country-specific regulatory arrangements for e.g.: increased depreciation, creation of provisions or offsetting losses is necessary.

3.2 Required data will mislead public opinion

A substantial risk exists for the undertakings regarding misinterpretation of the disclosed tax data by the public. This is particularly applicable to the current tense political and public debate on international tax competition, the appropriate involvement of undertakings in the community financing and the general outrage over unfair tax structuring/planning of foreign undertakings. Numerous examples of inaccurate press reports about alleged tax avoidance strategies show that enormous subsequent explanation and communication efforts to rectify shortened statements are required. The basis for these questionable press reports on tax expenses is already as of today publicly available information due to regulatory requirements in the Annual Financial Statements. It is unclear how an expanded CBCR should provide clearer information. Positive economic profit of a subsidiary can trigger misinterpretation due to non-taxation as a result of consolidation within a tax group. Hereby, clarifications are made to the general public which are almost inexplicable because of the complex tax regulatory arrangements and thus could significantly damage undertakings' reputation.

3.3 Required data can only be analysed by tax authorities

International taxation is not harmonized across jurisdictions. As a consequence to the current diversity of taxation approaches only the competent authorities can conduct detailed assessment of tax data. In this context it should be noted that in Germany internal tax declarations, which would need to be disclosed in order to understand tax expenses, are in general subject to tax secrecy according to § 30 German Federal Tax Law.

Constitutionally tax secrecy is enshrined in the general right of privacy**;** it guarantees the protection of the right to informational self-determination in the field of taxation. The guarantee of protection is only permitted to breach in exceptional cases like, e.g. overriding public interests. The tax secrecy according to § 30 Federal Tax Law in principle obliges only officials; however, it sets high demands towards existing internal tax declaration disclosure. As a result, the constitutionally embedded protective effect of tax secrecy would be lifted by the country-specific reporting requirement of tax expenses by disclosing tax data which is necessary to understand the amount-related data.

4. Conclusion

The Accounting Directive is not the right instrument, as the intended scope covers neither financial nor non-financial reporting issues on which investors would base their decisions.

BDI calls upon the EU to carry out an impartial and comprehensive impact assessment, before adopting any kind of legislative requirements on country-by-country reporting. A robust impact assessment is needed before any decision is taken, demonstrating a consistent and proportionate policy decision making with consideration of relevance, efficiency and cost-effectiveness, instead of rushing a proposal through without any consideration of the impact on EU businesses.

Given the evolving nature of the international tax debate, the EU should not adopt a stand-alone rule on country-by-country reporting. BDI urges the EU to focus on coordinating tax initiatives at international level – such as the OECD/G20 BEPS Action Plan[1] – to promote international consistency. BDI believes that a preferred way forward is to submit the required information only to the Tax Authorities.

EU approaches that avoid “aggressive tax planning” should be harmonized with respective measures at OECD and G20 level respectively (see the OECD Action Plan on Base Erosion and Profit Shifting). We believe that not globally applied measures would lead to significant disadvantages for EU-based companies (including the risk of double taxation) rather than a level playing field.

The introduction of a bilateral and/or multilateral system of automatic exchange of information between the tax authorities according to the OECD plan for more transparency is a better solution. Tax secrecy must be maintained.

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[1] The OECD/G20 BEPS (Base Erosion Profit Shifting) Action Plan includes Action 13 as follows: “*Develop rules (...) to enhance transparency for tax administration, taking into consideration the compliance costs for business. The rules to be developed will include a requirement that MNE’s provide all relevant governments with needed information on their global allocation of the income, economic activity and taxes paid among countries according to a common template.”*