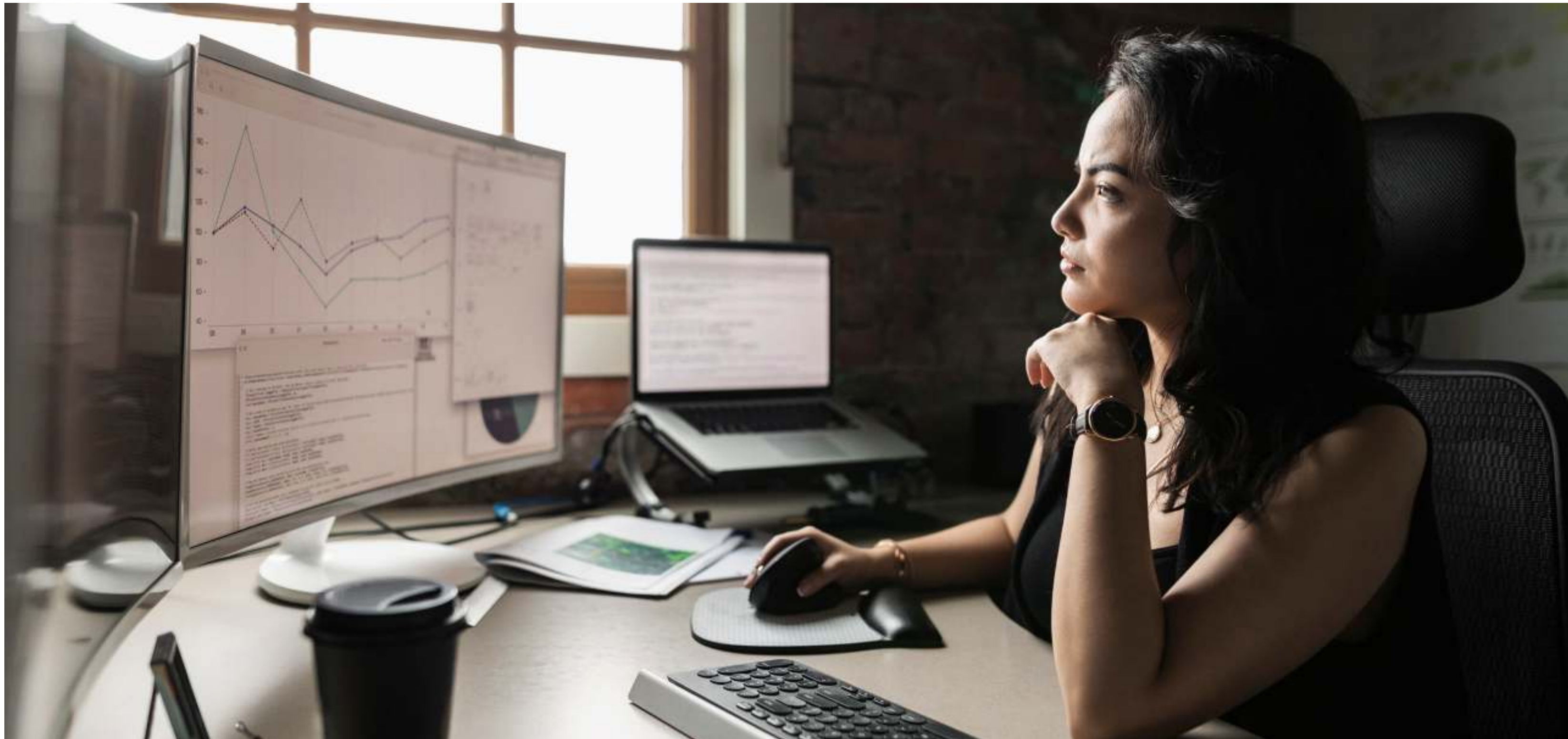
Tax transparency: A shift in focus – tax as a sustainability issue

Trends in voluntary tax reporting

Seventh edition

May 2020: A review of the FTSE100 for 2019 year ends



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Highlights of the seventh edition of 'Trends in voluntary tax reporting'

Welcome to the seventh edition of trends in tax transparency, released as the COVID-19 pandemic creates an economic crisis of unforeseen proportions. The implications for tax and tax transparency are wide ranging. The government support for businesses, on a scale not seen for over a century, is likely to result in a revaluation of the relationship between the private sector and the state. One outcome already evident is greater scrutiny over the tax affairs of businesses receiving state support, for example:

- Denmark, Poland and France have announced that COVID-19 government assistance would not be available for companies registered in tax havens;
- In both the US and the EU, proposals requiring firms receiving government assistance to publish country-by-country reporting data (CbCR) data were made if not pursued.

COVID-19 aside, we have seen increased interest over the last year from Environmental, Social and Governance (ESG) investors. There is a view that a company's tax affairs could generate risks to long term value creation and a number of ESG analysts (e.g. DJSI, FTSE Russell) are incorporating tax transparency into their assessments. For some companies, this can lead to tension between tax teams and sustainability teams. Sixteen companies in the FTSE100 have linked tax to the UN's Sustainable Development Goals.

The recent sustainability standard on tax (GRI-207: Tax 2019) released in December 2019 includes a requirement for public CbCR. Sustainability teams that are keen to follow GRI standards can place pressure on tax teams for greater transparency and careful discussions are needed in this sensitive area. Inclusion of the GRI tax standard in the International Business Council paper 'Toward Common Metrics and Consistent Reporting of Sustainable Value Creation' resulted in further attention on public CbCR.

How are companies responding to these developments?

Our review of 2019 year ends revealed an increase in voluntary tax disclosures. Twenty two companies published a stand alone tax report (up from 18 in 2018 and 7 in 2017). We found large increases in disclosures relating to the tax risk control framework (up by 10 FTSE100 companies) and Total Tax Contribution (up by 8 companies). A tax risk control framework provides comfort that a company's tax strategy has been followed, so is an important disclosure. The increase in Total Tax Contribution disclosures, highlighting taxes paid in addition to corporation tax, is perhaps a reflection of the attention on public CbCR since it provides a broader context of the contribution made through taxes. We found seven countries in the FTSE100 with a voluntary public CbCR disclosure.

One output of our review is an individual tax transparency feedback report. Please let one of the team know if you would like to receive a bespoke report and if you have any comments on the content of this paper.

Have you considered?

- Total Tax Contribution disclosures in a time when profit taxes may be low
- How your voluntary tax disclosures compare to your peers?
- How your CbCR data would be interpreted when compared to other publicly available CbCR data?
- What ESG analysts are looking for in relation to tax?
- Are you linked in with your sustainability team on tax disclosures?

Approach to tax and governance over tax

2018
2019

Tax havens

30
+6
36

Tax havens were discussed by 36 companies in this year's review, which represents an increase of 20% on the 2018 year-ends, where 30 companies mentioned them.

Tax havens have been an area of intense scrutiny over the years, and continue to attract strong interest from NGOs, ESG analysts and the wider public. In response to this increased attention, more companies are voluntarily offering additional data to support their explanations for why they use tax havens – including details around the number of subsidiaries they have operating in low tax jurisdictions and why.

Tax incentives

61
+9
70

Tax Incentives were mentioned by 70 companies, an increase of 15% on the 2018 year-ends.

A tax incentive is a government measure designed to promote specific corporate behaviours – such as investment in technologies, R&D, and employment-generating schemes. Incentives have become an increasing area of focus for many stakeholders, and in response, a number of companies are voluntarily disclosing information which emphasises how they are utilising incentives – including data concerning how much the incentives are worth, and how this is shaping their overall tax policy.

Transfer pricing

40
+6
46

Transfer pricing was discussed by 46 companies in this year's review, an increase of 15% on the 2018 year-ends.

The price at which companies carry out intra-group transactions, transfer pricing is an area where numerous companies are now providing either a brief statement to acknowledge their conformity with OECD principles, or expanding on these narratives to provide additional voluntary information about their business model and why transfer pricing is an important element of their operations.

Board approval

51
+7
58

Board approval of the company's tax strategy has increased in this year's review by 14% on the 2018 year-ends.

HMRC guidance on large business tax strategies was updated in June 2018, and indicates that there should be board approval of the strategy. Many companies have responded since this guidance was introduced by making explicit reference to board approval of the tax strategy, or approval of an individual board member specifically – often the CFO via delegation through the audit committee. Either way the increasing trend highlights responsibility for, and involvement with, the tax strategy at the highest levels of the business.

Risk framework

73
+12
85

85 companies have a risk framework in place specific to tax in this year's review, up 16% on the 2018 year-ends.

Risk frameworks are increasing important – as demonstrated by the high number of companies referring to them – as stakeholders look for assurance that the company tax strategy, alongside public statements on tax, are followed in practice. Tax risk frameworks set out the activities, tools, techniques, and organisational arrangements to ensure tax risks are identified, assessed, understood, and that appropriate responses are in place to mitigate the impact of all risks.

The numbers above shows the number of FTSE100 companies reporting in each area.

Tax numbers and performance, total tax contribution, and the wider impact of tax

Cash tax reconciliation

19

+1

2018
2019

20

In this year's review, the number of companies providing a cash tax reconciliation increased by 5% on the 2018 year-ends.

Cash tax reconciliation is a voluntary disclosure which sets out the difference between the tax charge disclosed in the financial statements and the corporation tax paid by the company. This disclosure is less common, but it is provided by companies seeking to explain and clarify to stakeholder groups, how the tax charge in the accounts relates to actual cash tax paid to the authorities.

Tax reconciliation narrative

41

+5

46

We found 46 companies providing additional narrative around their statutory/effective rate reconciliation, an increase of 12% on the 2018 year-ends.

This continuing increase is likely to be attributable to the thematic paper published by the Financial Reporting Council in 2016, which encouraged companies to provide more narrative in this area for stakeholders.

Total tax contribution

34

+6

40

40 companies provided some kind of information or data concerning their total tax contribution, an 18% increase on the 2018 year-ends.

Often broken down geographically, by type or tax, and distinguishing between taxes borne and collected, it is clear that more companies are interested in emphasising and showcasing the wider contributions they make to society – beyond simply focussing on the corporation tax they pay on profits. This voluntary disclosure of a company's total tax contribution is more prevalent in the financial services and extractive industries, where public disclosure of information on a country-by-country basis is already required.

The numbers above shows the number of FTSE100 companies reporting in each area.

Have you considered:

- Whether additional voluntary disclosures would create value for your business?
- The benefits of disclosing your Total Tax Contribution?
- How your published tax strategy compares to your peers?

Public Country-by Country Reporting (CbCR)

What is CbCR?

CbCR is a term that is used broadly, but in simple terms it means reporting on certain financial information (e.g. revenue, profit, employees, assets, tax paid) on a country basis rather than a global basis. Under OECD BEPS Action 13, over 80 countries have passed legislation requiring companies to disclose this information privately to tax authorities, for use in risk assessment.

Latest developments

GRI (Global Reporting Initiative) are widely adopted standards for sustainability reporting. The standard, **GRI 207 : Tax 2019**, which was released in December 2019, includes a requirement for public CbCR. The standard is effective for publications after 1 January 2021.

The International Business Council (IBC) of the World Economic Forum (WEF) issued a consultation document ‘Toward Common Metrics and Consistent Reporting of Sustainable Value Creation’ at the 2020 annual meeting in Davos. GRI 207: Tax 2019 is included in the IBC document as a core (required) metric.

[1] https://www.globalreporting.org/standards/gri-standards-download-center/gri-207-tax-2019/

GRI standard on Tax (GRI 207)[1]

The content of the GRI public CbCR disclosures is shown below. Seven companies in the FTSE100 have voluntarily disclosed public CbCR. All have included additional narrative to aid understanding of the data and avoid misinterpretation.

Disclosures required:

The reporting organisation shall report the following information:

a. All tax **jurisdictions** where the entities included in the organisation’s audited consolidated financial statements, or in the financial information filed on public record, are resident for tax purposes.

b. For each tax jurisdiction reported in disclosure 207-4-a:

1. Names of the resident entities;
2. Primary activities of the organisation;
3. Number of employees, and the basis of calculation of this number;
4. Revenues from third-party sales;
5. Revenues from intra-group transactions with other tax jurisdictions;
6. Profit/loss before tax;
7. Tangible assets other than cash and cash equivalents;
8. Corporate income tax paid on a cash basis;
9. Corporate income tax accrued on profit/ loss, and
10. Reasons for the difference between corporate income tax accrued on profit/ loss and the tax due if she statutory tax rate is applied to profit/loss before tax.

c. The time period covered by the information reported in Disclosure 207-4.

Differences between GRI CbCR and OECD

	GRI 207-4	OECD
Domestic party transactions	Only cross-border related party transactions are to be consolidated at a country level.	Aggregates all related party transactions, including those within the same territory.
Revenue	Taken directly from the audited financial statements.	Revenue includes other income received and interest receivable.
Withholding tax	Separate disclosure of withholding tax paid or to be included in the corporate tax paid.	To be included in income tax paid figures.
Corporate income tax	**Excludes** provisions for UTP’s that have been booked in the year. Reconciliation between the effective tax rate and the statutory tax rate.	**Includes** provisions for UTP’s that have been booked in the year.

What else could you consider?

- The risks and benefits of disclosing CbC data and the format of any disclosure
- The potential questions raised if CbC data were published
- The narrative around the CbC disclosure to better interpret the data
- Whether Total Tax Contribution data would provide useful context alongside or instead of CbC data

What does tax transparency mean for me?

Our research shows a small number of companies leading in the area of tax transparency but the majority with more limited voluntary disclosures.

In the aftermath of COVID-19, with tax as part of the sustainability story and the increasing interest from ESG investors, more companies are now considering their approach to tax transparency.

It may be that voluntary disclosures would not add value to the business. Whatever your approach, it is important to have briefed internal stakeholders on this sensitive area.

The **PwC Tax Transparency Framework** helps to guide companies through the thought process needed to develop an approach that maximises the benefit of tax transparency for the company. It consists of a series of questions to help manage the risks and benefits of voluntary tax disclosures.

We suggest focusing on four areas:

Approach to tax 1	Governance over tax 2
Tax numbers and performance 3	Total Tax Contribution and the wider impact of tax 4

Transparency to whom and for what purpose?	This is the central question of the framework and takes into account the full range of internal and external stakeholders.
What are the views around the business?	Internal consensus on approach is key. Prepare a briefing paper for the board, public relations, investor relations, sustainability, corporate reporting teams setting out latest developments in tax transparency and how your current tax disclosures compare to your peers.
What do stakeholders want to know and why?	For your external stakeholders, identify what they want to know, why they want to know it and therefore what information might be useful to them. Whether or not you choose to disclose that information is a separate question. You might consider disclosures around **tax havens, transfer pricing** and **tax incentives**.
What are the risks and benefits of providing additional information?	The risks of additional transparency is an important consideration for internal stakeholders. Once disclosures have been made, it is difficult to withdraw them in subsequent years. What are the risks and benefits of providing or withholding information?
What disclosures would create value?	For a company operating 'business-to-business' with limited presence in developing countries, no voluntary public disclosure may be most appropriate. For others, a relatively straightforward statement could add considerable value. **Total Tax Contribution** disclosures can help highlight the contribution made to the public finances beyond corporation tax.
Are the disclosures understandable?	Once decisions on disclosures have been made, consider whether they are understandable by the target audience. Is there a business case for providing additional narrative to 'explain tax'? **Additional narrative for the tax reconciliation** and an **explanation of the difference between the tax charge and tax paid** are areas to consider.
Do you have systems to support your disclosures?	The final element of the framework is to consider whether there are controls and processes in place to support any disclosures. Details of **board approval** of the tax strategy and the **tax control framework** can help provide comfort that statements made are followed in practice.

Our methodology

We reviewed the annual reports for financial years ending between January and December 2019, for all companies listed in the FTSE 100 at 31 December 2019. Figures for 2018 are for all companies listed in the FTSE 100 at December 2018, therefore the trends shown represent the FTSE 100 group at the time of review, and are not on a like-for-like basis year on year.

We reviewed the most recent publicly available corporate reports, social responsibility reports, and additional tax reporting documents publicly available at 30 April 2020. We explored each company's website, searching for any other information that relates to tax reporting.

Our review uses the PwC Tax Transparency Framework, a set of more than 40 broadly defined tax transparency indicators, to assess the disclosures made. Eight of these indicators are discussed in detail in this publication.

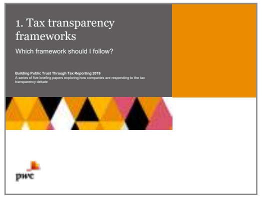
Building Public Trust Awards for Tax Reporting

Winners of our fourteenth Building Public Trust Awards for Tax Reporting – recognising companies making leading voluntary tax disclosures – will be announced in November 2020.

Explore how the tax transparency debate is evolving through our short briefings on our website. Each addresses a different topic and contains extracts from leading companies. **There will also be a repository of extracts published here throughout the year.** Scan the QR code below, search for **'Building Public Trust Through Tax Reporting'** or visit **https://www.pwc.co.uk/services/tax/insights/building-public-trust-through-tax-reporting.html**

1

Tax Transparency frameworks:
Which framework should I follow?



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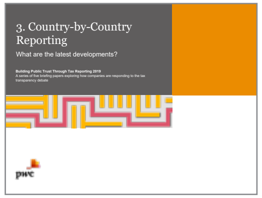
Tax strategy:
Is anyone reading published tax strategies?

3

Country by country reporting:
What are the latest developments?



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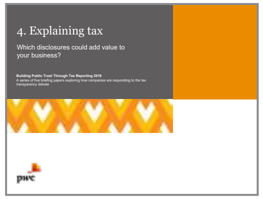
Explaining tax:
Which disclosures could add value to your business?



How can we help?

As this report shows, tax disclosures are changing. We can assist you in understanding how your current and proposed disclosures compare to your peers using a benchmarking report.

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