


Tax Reporting and ESG: Does Tax Belong in the “S”?

Professor Kerrie Sadiq, QUT, Brisbane Australia
(presenter and corresponding author)

Dr Rodney Brown, UNSW, Sydney, Australia

Dr Bronwyn McCredie, QUT, Brisbane Australia



The Importance of MNEs Paying Their 'Fair Share' of Tax

- + Multinational enterprises (MNEs) have a responsibility to pay their 'fair share' of tax.
- + Tax revenues are essential for funding public services and infrastructure.

The Impact of MNEs Not Paying Their Fair Share of Tax



- + Tax avoidance and tax evasion by MNEs harm economies, governments and societies.
- + Tax avoidance by MNEs leads to revenue loss for governments.
- + Revenue loss can lead to underfunding of public services and infrastructure.
- + Underfunding can have negative social and economic consequences.

Rationale for Corporate Tax Disclosures: ESG Framework

- + ESG considerations are becoming increasingly important for investors
- + Tax strategies are a material ESG issue
- + Transparent tax disclosures can help companies demonstrate their commitment to responsible corporate behavior



A hand holding a blue pencil is positioned over a document. The document contains a table with multiple columns of numbers, some of which are highlighted in blue and red. The background is a blurred image of a person's face, suggesting a focus on the document and the hand. The word "Overview" is written in a large, white, sans-serif font on the left side of the image.

Overview

- + Increased tax transparency initiatives aimed at MNEs in the last decade.
- + Initiatives in the form of voluntary and mandatory tax disclosures.
- + Primary purpose is to achieve tax transparency.
- + Desired outcome is increased intra-jurisdictional and global tax revenue.
- + Studies suggest that this intended outcome may not be achieved for five broad reasons.

Rationale for Corporate Tax Disclosures

- + Various rationales are provided, either mandating or providing voluntary tax reporting and disclosure guidance.
- + The most common reasons associated with voluntary disclosures are:
 - + to encourage MNEs to highlight that they are paying their fair share of tax, to encourage all businesses to refrain from engaging in aggressive tax avoidance; and
 - + to become more transparent and educate stakeholders about their compliance with tax laws.
- + Organisations are encouraged to publicly report on tax under the GRI Standards to show the contribution that they make to the countries in which they operate, promote confidence and credibility in the tax practices of organisations and the tax system, enable stakeholders to make informed judgements about an organisation's tax practices, and to help inform public debate and support the development of socially desirable tax policy.

How does it reduce tax avoidance?

- + According to Muller, Spengel, and Vay (2020), tax transparency is expected to reduce MNE's tax avoidance through three channels:
 1. Tax authorities could use the incremental information to enhance their audit scrutiny and efficiency;
 2. Legislators could discover legal loopholes and subsequently adjust the law;
 3. In the case of public disclosures, firms may be disciplined by increased accountability to the general public, which may exercise pressure on companies to pay their “fair share” of taxes.
- + A fourth channel: investors. Institutional investors are now starting to raise shareholder resolutions against MNEs pushing them to adopt public CbCR (for example) and to encourage the firm to reduce tax risk through aggressive tax positions.

Are the underlying principles correct?

- + Is the target of transparency:

- + The public – the disclosure of additional information (the ‘S’ in ESG); OR
- + Companies – for accountability purposes (the ‘G’ in ESG)?

- + Is the objective of tax transparency to:

- + Provide additional information; or
- + For companies to pay more tax; or
- + Both 1 and 2?



Current Reporting Mechanisms

- + Paradigm shift towards greater tax transparency
- + Mandatory reporting requirements
- + Voluntary reporting
- + EU Parliament and Council agreement on mandatory public CbCR for all industries
- + Australian government draft legislation for public CbCR
- + Well-known voluntary disclosure regimes such as GRI 207, B-Team Principles, and UN-PRI principles

5 Reasons why Current Reporting Mechanisms Fail

- + MNEs view tax as a legal obligation, not a moral one
- + MNEs have the power to influence and shape policy
- + Inconsistencies exist within and between reporting regimes
- + Shareholders have a social conscience but don't extend it to investment
- + Broader stakeholder groups pay little attention to MNE tax practices



Tax is a Legal Obligation

+MNEs regard tax as a legal obligation rather than a moral one and will minimise taxes accordingly to ensure that their statutory obligations are met but go no further.



Regulatory Capture

- + Regulators may be influenced by the businesses they are meant to oversee
- + Lobbying can lead to rules that benefit corporations
- + Regulatory capture can lead to less effective enforcement of tax laws





Interpreting Data

- + Different countries have different reporting requirements
- + Inconsistencies in reporting can make it difficult to interpret data
- + Comparing data between companies can be challenging

Profit Motivation

- + Companies may take advantage of loopholes to reduce their tax liabilities
- + Some companies use aggressive tax planning strategies
- + Tax competition can lead to lower tax rates and reduced revenues



Stakeholder Concern

- + Stakeholders expect companies to act responsibly
- + ESG factors are becoming increasingly important
- + Transparent tax disclosures can help companies demonstrate their commitment to responsible behavior

BUT

- + broader stakeholder groups, such as debt holders, financial analysts, and society (the public, media, non-government organisations, and tax justice campaigners), may pay little attention to MNE tax practices and/or do not have a high level of expertise required to understand the information reported.



Focus on Country-by-Country Reporting and the Shift to a Governance Emphasis

- + Country-by-country reporting (CbCR) requires MNEs to disclose financial information by country.
- + CbCR increases transparency and accountability.
- + Shift from compliance-oriented to governance-oriented approach.



The Need for Tax Transparency to Extend Beyond Country-by-Country Reporting



- + CbCR is a start, but it is not enough.
- + Greater transparency is needed to address tax avoidance and evasion.
- + Tax transparency should be embedded into corporate strategy and culture.

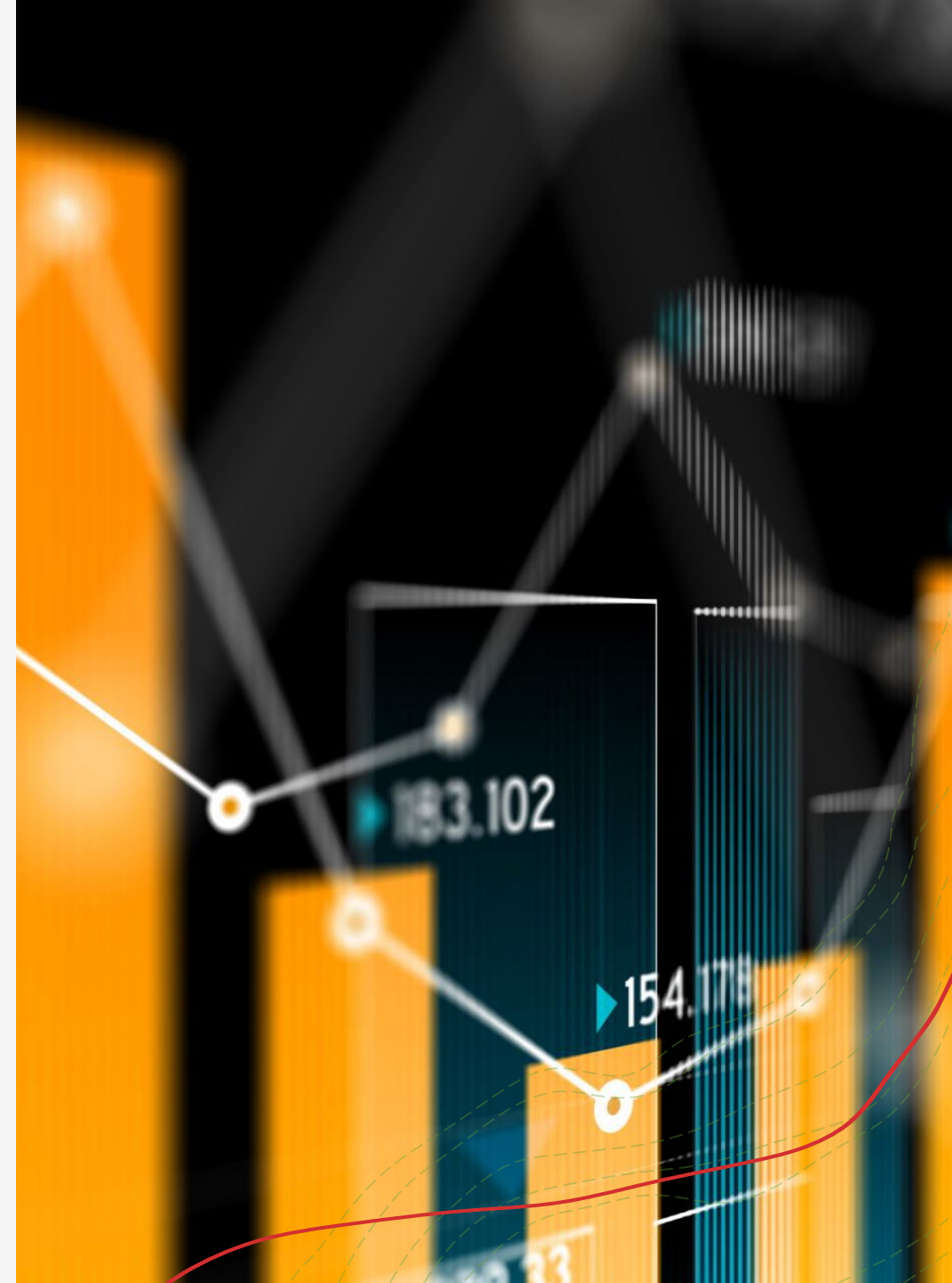
The Way Forward

- + Tax disclosures contribute to ESG, but current limitations may limit their effectiveness
- + A more robust and harmonized approach to reporting can lead to better performance and commitment to social responsibility
- + Incorporating tax into the 'S' of ESG can be achieved through greater transparency and accountability
- + Tax compliance is important for governments and taxpayers, and can lead to more responsible behavior



GRI 207: Tax 2019

- + Contains disclosures for organizations to report information about their tax-related impacts, and how they manage these impacts.
- + The disclosures enable an organization to provide information on how it manages tax, and information about its revenue, tax, and business activities on a country-by-country basis.



Disclosure 207-1 Approach to tax

The reporting organization shall report the following information:

- a. A description of the approach to tax, including:
 - i. whether the organization has a tax strategy and, if so, a link to this strategy if publicly available;
 - ii. the governance body or executive-level position within the organization that formally reviews and approves the tax strategy, and the frequency of this review;
 - iii. the approach to regulatory compliance;
 - iv. how the approach to tax is linked to the business and sustainable development strategies of the organization.

Disclosure 207-2 Tax governance, control, and risk management

The reporting organization shall report the following information:

- a. A description of the tax governance and control framework, including:
 - i. the governance body or executive-level position within the organization accountable for compliance with the tax strategy;
 - ii. how the approach to tax is embedded within the organization;
 - iii. the approach to tax risks, including how risks are identified, managed, and monitored;
 - iv. how compliance with the tax governance and control framework is evaluated.
- b. A description of the mechanisms to raise concerns about the organization's business conduct and the organization's integrity in relation to tax.
- c. A description of the assurance process for disclosures on tax including, if applicable, a link or reference to the external assurance report(s) or assurance statement(s).

Disclosure 207-3 Stakeholder engagement and management of concerns related to tax

The reporting organization shall report the following information:

- a. A description of the approach to stakeholder engagement and management of stakeholder concerns related to tax, including:
 - i. the approach to engagement with tax authorities;
 - ii. the approach to public policy advocacy on tax;
 - iii. the processes for collecting and considering the views and concerns of stakeholders, including external stakeholders.

Disclosure 207-4 Country-by-country reporting

The reporting organization shall report the following information:

- a. All tax jurisdictions where the entities included in the organization'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:
 - I. Names of the resident entities;
 - II. Primary activities of the organization;
 - III. Number of employees, and the basis of calculation of this number;
 - IV. Revenues from third-party sales;
 - V. Revenues from intra-group transactions with other tax jurisdictions;
 - VI. Profit/loss before tax;
 - VII. Tangible assets other than cash and cash equivalents;
 - VIII. Corporate income tax paid on a cash basis;
 - IX. Corporate income tax accrued on profit/loss;
 - X. Reasons for the difference between corporate income tax accrued on profit/loss and the tax due if the statutory tax rate is applied to profit/loss before tax.
- c. The time period covered by the information reported in Disclosure 207-4.

A potential Solution?

+ Stop thinking of tax as part of the 'S' and start treating it as part of the 'G'.



An aerial photograph of a long, multi-lane highway bridge spanning a body of water. The bridge has several lanes in each direction, with white dashed lines marking the lanes. Several vehicles, including cars and trucks, are visible on the bridge. The water is a deep teal color with visible ripples. In the top left corner, there are white dashed contour lines. In the bottom right corner, there is a solid red line and some white dashed contour lines. The text "THANK YOU" is overlaid in the center of the image in a large, white, sans-serif font.

THANK YOU