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Country-by-Country Reporting

The pros and cons of more tax transparency

The European Commission will present its proposal for more corporate tax transparency these days. The so-called Country-by-Country Reporting will force large multinational enterprises to publish country specific profits and tax payments. By emphasizing positive aspects such as disclosing the tax contributions of global corporations, the European Commission forgets to look at the increasing red tape burden for companies and to address tax loopholes established by the national governments in the EU member states. It also risks competitive disadvantages and reputational damage for MNE by publishing sensitive company data.

Establishing a level playing field in corporate taxation is a priority for the EU Commission and crucial for a fair and efficient tax system in the European Union.

According to the European Commission “the public has become more sensitive to tax fairness issues in the context of increased pressure on public finance at times when large multinational enterprises can reduce the amount of corporate income tax to single-digit percentages.” (European Commission, 2015).

More transparency plays a key role

The current efforts for changes in the EU tax policy are directly linked to the OECD project on Base Erosion and Profit Shifting (BEPS). Among the 15 action points of BEPS, transparency plays a central role. Action point 13 – “Transfer Pricing Documentation and Country-by-Country Reporting” – addresses the issue of more transparency explicitly (OECD, 2015). A first step by the European Commission refers to the so-called “Anti Tax Avoidance Package” presented in January (European Commission, 2016a).

Country-by-Country Reporting (CbCR) is seen as a powerful tool to fight profit shifting by multinational enterprises (MNE). They shall be obliged to provide financial figures such as turnover, profit before tax and number of employees as well as taxes paid and taxes accrued separated by each country they are operating in via the company’s website. However, for legal reasons the CbCR will be limited to EU countries while for the rest of the world only aggregated figures will be provided. The purpose of gathering all the information is to show the full picture of a company’s global activities and tax burden.

Search results for Germany

	EU definition of large companies:	
	Solvent companies with ...	
1	… revenues of minimum 40 million Euro	
2	… a balance sheet amount of minimum 20 million Euro	
3	… minimum 250 employees	
4	Solvent companies fulfilling at least two of the three thresholds 1-3	**15,547**
	OECD recommendation based on the BEPS project:	
1	Solvent companies with revenues of minimum 750 million Euro	**1,214**

Remarks: Since these results are only based on a quantitative search, the precise number of companies might differ in both cases for several reasons:

- The database does not contain all solvent companies or does not provide all data.
- Companies do not fulfil the criteria on a stand-alone basis in Germany and are therefore not detected in the database. Nevertheless, many companies operating in Germany will be concerned since their company group will fulfil the criteria on a consolidated basis.
- Double counting might occur since large enterprises such as listed company can have more than one local company fulfilling the criteria. However, they are regarded as one MNE.
- Not all companies fulfilling the criteria have necessarily a multinational company structure.

Source: Dafne Database

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Transparency towards whom?

Even if EU and OECD both argue in favour of more transparency, the two institutions follow different strategies. While the OECD is convinced that the availability of the company data should be restricted to the tax authorities, the EU seems to be in favour of publishing the CbCR. While there is a broad consensus that more transparency is a reasonable approach in international taxation, the central questions in this context is “Transparency towards whom?” (European Commission, 2015, p 3).

Business representatives and company owners are afraid of losing competitive advantages when sensitive company data become known to the public and thus to competitors. Consequently, they are concerned about distorted competition. Furthermore, the inappropriate interpretation of the CbCR might lead to a reputational damage (European Commission, 2016b, p 15). Therefore, the CbCR should only be provided to tax authorities.

Number of companies captured by the EU proposal

With regard to the number of companies having to comply with the new transparency rules, the OECD proposes to capture MNE groups with a consolidated turnover of at least 750 million Euro. According to the OECD this is an adequate threshold since it would exclude 85 to 90 percent of MNE groups from the burdensome bureaucratic requirement to file the Country-by-Country Report. At the same time, the remaining 10 to 15 percent represent about 90 percent of global revenues (OECD, 2015, p 21). There are more than 100,000 MNE registered worldwide with approximately 900,000 affiliates.

So far, the European Commission defined company groups as large if they fulfilled two of the following three criteria on a consolidated base: balance sheet amount of 20 million Euro, net sales of 40 million Euro, number of employees of 250 (European Union, 2013, p 28). However, it now seems likely that the European Commission will follow the OECD approach when presenting its directive the next days.

This is an important issue since the two options would concern a significantly deviating number of companies. From a German perspective, the EU definition of large company groups would apply to many companies belonging to the "Mittelstand". According to a data evaluation, more than 15,000 German companies would potentially be affected by the more narrow EU approach and would have to comply with the transparency rules. In contrast, following the OECD approach with a minimum consolidated turnover of 750 million Euro, approximately 1,200 German companies meet the requirement (table).

However, German affiliates not fulfilling the criteria on a stand-alone basis but belonging to a large company group are not covered by this approach. Hence, it is evident that these numbers underestimate the actual number of companies having to comply with the CbCR.

In fact, nearly all subsidiaries of MNE exceeding the threshold on a consolidated basis will be obliged to provide the CbCR for their operating business in countries of the European Union even if the headquarter is located outside the European Union.

Only small local companies will be exempted from filing the CbCR, i.e. companies which do not fulfil at least two of the following criteria: a balance sheet amount between 4 and 6 million Euro, turnover of 8 to 12 million Euro and at least 50 employees. There will only be very few global corporations with a consolidated turnover above 750 million Euro but without any relevant operating business in the European Union.

Therefore, the expected CbCR proposed by the European Commission will increase the red tape burden for thousands of MNE and their subsidiaries in Germany and the whole European Union even if the threshold is set to revenues of minimum 750 million Euro.

Tax loopholes established by EU member states

According to EU law, the national governments will have to apply the directive to national tax law. It will be interesting to see how the different governments will interpret and implement the directive. As a result of the EU plan, a large number of MNE worldwide will have to publish sensitive financial figures in the future. By focusing on the compliance rules for MNE, the European Commission completely ignores the role of the national governments and their disharmony with regard to offering loopholes and other tax incentives in order to attract corporate business. However, for a fair tax competition between the member states and thus a level playing field, harmonised tax rules in the whole European Union are needed.

Literature

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