Country-by-Country Reporting Goes Public – Cui Bono?

After the introduction of CbCR – pursuant to the BEPS Project (Action 13) in 2015 –, which was established to reduce the information asymmetry between MNEs and tax authorities of the countries they operate in, now public CbCR – as suggested by the EU Commission in 2016 – is discussed as a next step. Here, the objective is to overcome information asymmetries between MNEs and the general public of the countries they operate in. Starting from the assumption that regulators care about the legitimacy of tax laws, this article evaluates pros and cons of public CbCR. The authors find that from the perspective of information asymmetries, public CbCR increases tax transparency only marginally at best. Accordingly, it is concluded that democracies that are based on the rule of law seem to rely on pillars in terms of public CbCR to enforce fair tax payments.

1. Introduction

Country-by-Country Reporting (CbCR) has received much attention among tax professionals and tax researchers since its initial conceptualization in the course of the

BEPS Project led by the OECD during 2013 to 2015. As an innovative element and cornerstone of the so-called three-tiered documentation approach in transfer pricing, CbCR was designed to reduce the information asymmetry between large multinational corporate taxpayers and tax authorities of the countries they operate in by providing tax information aggregated on the country level and in turn increasing tax transparency. CbCR is often deemed a transfer pricing-related documentation. However, this does not seem to be really the case due to the fact that only one out of eight financial performance indicators that have to be reported is directly connected to intercompany transactions. Rather, it has been designed as a simple instrument for fiscal authorities’ analyses enabling a “quick and dirty” high-level BEPS-risk assessment regarding tax planning of reporting multinational enterprises (MNEs) on a global level.

Unfortunately, numerous ambiguities and uncertainties exist regarding the required information to be reported.


These shortcomings have frequently been discussed in tax literature and are also reflected by the growing volume of guidance and additional clarification provided by the OECD with respect to CbCR over the years. However, it cannot be denied that CbCr data, be they considered as a good or poor fit for tax risk assessment purposes, provide an unprecedented level of information that enables tax authorities to identify targets for a detailed subsequent tax audit investigation on a unilateral or multilateral scale.

Aiming for further transparency, the EU Commission suggested in April 2016 public CbCr as an additional measure to impact tax compliance behaviour of European-based MNEs. Interestingly, this initiative was introduced in the shape of a revised Accounting Directive and not in the realm of tax directives. This approach has prolonged the political debate and slowed down the legislative decision-making process regarding the actual introduction of public CbCr to date. A turning point was reached when Germany – represented by its current Finance Minister Olaf Scholz – finally gave up its previous opposition to the introduction of public CbCr, as this additional transparency initiative had already been advocated for some time by other EU Member States, especially France. However, no qualified majority vote upon the introduction of public CbCr for European-based multinationals could be achieved among the (then) 28 EU Member States end of November 2019. The demand for public CbCr is not entirely new. In the banking sector, it was already implemented in 2013 by way of EU Directive 2013/36. A similar directive was implemented in the same year, to provide more transparency with respect to a public disclosure of payments to governments made by companies operating in the extractive industry sector (gas, oil, mining). This development seems to have gone more or less unnoticed and without much debate by the general public over the last couple of years. This lack of debate on introducing more extensive disclosure regulations may be due to the fact that after the financial and economic crisis from 2008 to 2010, the reputation of banks and other financial institutions was at an all-time low. Therefore, publicly disclosing tax-related data was expected to ease the negative public awareness and to meet the repeated demand by the general public for a better-informed view of the business practices of major players in the financial sector. This is true, even though it did not add much to the already “well known” and accessible facts provided by general financial reporting of banks and other financial institutions. In the extractive industry, most of the public attention was directed at this industry’s environmental footprint and sustainability considerations, rather than its financial transparency.

For all other industries, CbCr data have been maintained as confidential corporate taxpayer information according to unambiguous OECD guidance and the respective national tax law so far. However, it is argued by various stakeholders that the general public needs to know more about the actual tax-compliance behaviour of MNEs, in order to be able to judge whether to invest in a company, to buy its products or use its services. Implications regarding public access to taxpayer CbCr information in view of the proposed EU directive have been discussed in literature. The subsequent section takes an alternative approach. It

---

16. See OECD Guidelines, supra n. 2, at ch. V, paras. 5.44 and 5.45.
explores several aspects of public CbCR from different stakeholder perspectives and in relation to the data itself.

2. Considerations on Public CbCR

As a starting point, the differentiation between legality and legitimacy needs to be considered as an underlying premise. Even though legitimacy as perceived by the general public is a decisive factor in constitutional democracies with respect to the acceptance of and adherence to applicable laws and their enforcement, the actual exercise of executive power and governance by the state always needs to be firmly grounded on a legal basis.

In the discussion in this article, the authors employ the well-known sender-signal-receiver model. In particular, this means that initially the MNE (the sender) has private knowledge about its tax data. The MNE is responsible for generating and recording these tax data by means of its bookkeeping. The CbC report (the signal) is generated by selecting, aggregating and commenting on these data and thus assembling pieces of information to be reported. Fraudulent reporting is excluded from the scope: for purposes of the discussion it is assumed that reported information is always true (truth-telling constraint known from disclosure theory). In the given setting, the extent of information provided and thus the quality of the signal is determined by regulation. Furthermore, it is assumed that the firm tells the truth whenever it reports, but it may conceal information by aggregation or reporting management. Finally, the focus is on the general public as receiver of this aggregated information. Given that the currently confidential (henceforth: private) CbC report according to chapter V of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations has already been established in the European Union and beyond, and the debate on public information provision is ongoing, it is not unlikely that public CbCR could become a mandatory requirement for MNEs in Europe. However, the outcome of decoding the reported information by the receivers depends, for example, on factors such as their tax expertise and the initial information endowment allowing the receivers to interpret the newly received signal, as well as the cognitive capacity, effort and technology expended by receivers on the decoding process. The complexity of this perception process implies that misperceptions of the signal are likely.

In the following, the authors argue in line with the sender-signal-receiver model, i.e., it starts with presenting arguments from the sender’s perspective. Then aspects concerning the signal itself are considered, followed by a presentation of arguments from the receiver’s perspective. All listed arguments represent individual opinions that have been raised during a workshop of the Transfer Pricing working group of the Schmalenbach Gesellschaft in Germany.

2.1. MNEs’ (sender’s) perspective

From the sender’s perspective, data collection is crucial, as it is time consuming and costly, and determines the quality of the signal. A naive view is that the information required for public CbCR does not need to be generated, because it exists already for the purpose of private CbCR. In real-world tax accounting, global allocation of revenues, income, income taxes paid and accrued, and further required indicators like stated capital, tangible assets and number of employees can be easily determined and have to be prepared for private CbCR in any case. Furthermore, some MNEs offer public tax reports voluntarily. However, private CbC reports need to be prepared and annotated for public CbCR purposes, to ensure and increase the understandability and avoid ambiguity of the information provided. A prominent example for the effort made to generate a public CbC report is provided by Vodafone. That report’s total length is 89 pages, with 27 pages of introduction and explanation followed by 42 pages of country-related information. The report concludes with a further 20 pages including several appendices. Obviously, in the years to come, a comprehensive public tax reporting strategy is likely to trigger additional compliance costs for MNEs when preparing such reports, and further compliance costs due to more discussions with different stakeholder groups, several thereof with discussions on non-tax specialists.

In contrast to the cost-related argument, a second argument refers to the allocation of responsibilities between the tax authorities and MNEs. The standard argumentation in favour of public CbCR reads as follows.

Tax laws cannot perfectly address all kinds and characteristics of cross-border transactions. Moreover, inconsistencies between various national tax laws exist. MNEs are deemed to exploit these shortcomings. Thus, by presenting real business cases in a certain accounting way, MNEs gain an unfair advantage form their internationality, because they can shift profits across countries. These extra tax-planning opportunities result in undesired low effective tax rates and in an unfair allocation of taxes across countries. Providing more tax information to the public will reduce MNEs’ appetite for profit shifting because they are concerned about reputational loss (shame and blame). These reputational damages are expected to generate economic disadvantages like lower revenues, lower profits or reduced liquidity in capital markets.

This standard argumentation line calls for corporate social responsibility (CSR) in the realm of corporate taxation. MNEs should not only earn profits for their shareholders, but also act in the interest of other stakeholders.

18. See, for example, K.J. Arrow, The Economics of Information: An Exposition, 23 Empirica 2, pp. 119-128 (1996).
19. For this refined version of the truth-telling assumption, see, for example, M. Ebert, J. Stecher & D. Simons, Discretionary aggregation, The Accounting Review, pp. 73-91 (2017).
Therefore, MNEs have to serve the interest of all citizens and are therefore required to pay their “fair share in taxes”. This understanding of CSR can be challenged. MNEs compete in markets regulated by law. In general, competition in markets and the rule of law work in favour of public welfare and the common good. It goes against this common understanding of the market order to demand a behaviour that could be harmful for a competitor because it creates a competitive disadvantage. In particular, the collection of taxes is based on the rule of law. And from a legal perspective, a taxpayer does not have an obligation to pay more taxes than the law demands.  

One may argue that MNEs have more market power than national enterprises and that CbCR is justified as an instrument to address competitive distortions and to level the playing field in terms of taxation. However, competitive distortions caused by tax law have to be addressed by the tax legislator. Continued profit shifting will only take place if anti-avoidance regulations are ineffective. Enforcing tax rules and closing gaps in tax legislations is a more promising way of establishing a fair and reasonable tax allocation. Instead, appropriate anti-avoidance regulations and enforcement corroborate the idea that the responsibility should be shared by MNE taxpayers and national tax authorities. Moreover, establishing a legal framework for a fair allocation of taxes across countries is not an issue for a single country but a matter of international cooperation. The OECD has recently proposed several measures targeted at international profit shifting, among them an international minimum taxation regime. When negotiating countries achieve an agreement along the lines of the OECD proposals, this sets effective limits to international profit shifting. If countries’ national tax laws are adapted accordingly, following the terms of an international agreement, public information and public pressure definitely cannot longer be taken into account as legitimate elements of tax enforcement.

Above all, the argument in favour of CSR and the reputational effect of CbCR critically relies on the ability of the general public to perceive the reports correctly and exert pressure in a justified way. This requires that the public understands the data properly, as described above. However, the data do not reveal whether the reporting company has actually adhered to applicable tax law. This can only be assessed by way of a detailed investigation conducted by fiscal authorities, which is their legal obligation in terms of national sovereignty. Additionally, the public would have to abstain from a strictly nationalist view and populist behaviour. In other words, public pressure in different countries is by no means an effective instrument to achieve an overall fair allocation of MNEs’ profit taxes across countries. And beyond possible misconceptions of the general public and correspondingly biased stakeholder responses, the decisive question is whether the appropriate reference system for fair taxation is the regulatory framework, i.e. (hard and soft) tax law, or rather public opinion about tax morale. Although the authors cannot find a convincing argument in favour of mandatory public CbCR, there is room for CSR in the area of taxes as a business case. It may be in the MNEs’ best interest to provide more tax information along the lines of CbCR. MNEs presenting themselves as “good corporate citizens” paying their fair share in taxes may hope to avoid negative market reactions. Moreover, positive incremental revenue or cost effects of increased tax transparency may outweigh the negative effect of higher tax payments. CSR could improve customer relations. Consumers, in particular, may appreciate MNEs’ commitment to CSR in taxation.

potentially applicable EU regulations in future. However, the key figures provided in a CbC report are only weakly linked to the calculation of the tax base.25 Related data can be gathered from other sources like financial reports, especially segment reports, or investor relations material.26 Accordingly, it is doubtful whether a legal breach of tax secrecy could actually exist.

In a similar vein, arguments of fairness and comparability issues need to be discussed. Obviously, MNEs are treated differently than wholly domestic firms. However, from a legal perspective only equals need to be treated equally. Moreover, MNEs located in the European Union are treated differently than their international competitors. With public CbCR, competitors could exploit the information provided and obtain an unfair competitive advantage, which, in particular, could be the case for MNEs not located in the European Union and therefore not subject to mandatory publication of their data. Given the above-mentioned information sources are already available, these additional effects of public CbCR may not be overly relevant either.

2.2. CbCR report (signal)

Regarding the signal itself, several issues need to be considered. Firstly, the appropriateness of CbCR data can be challenged. In order to generate reputational concerns in MNEs, the general public needs to be in a position to form justified expectations about a fair tax share. The global allocation of an MNE’s revenues, income and employees is only a rough indicator for the economic activities and does not enable conclusions about “fair tax allocation”. Secondly, definition and content of the various numbers to be reported initially varied across legislations and are still being debated (tax accounting, IFRS, local GAAP, etc.). Thus, comparability is impaired.27 Finally, under the EU proposal not every country needs to be displayed individually. Non-EU jurisdictions may be aggregated unless they are considered tax havens. Thus, the informational value added by public CbCR is questionable. Even if all these issues were solved, the question regarding the appropriate benchmark (regulatory or moral framework) is still open.

Neither economic theory nor other sources provide an appropriate benchmark for a “fair” allocation of taxation rights among countries. The request for public CbCR data is based on the assumption that this reporting obligation can support the goal of achieving an improved allocation of an MNE’s profit and corresponding tax payment to each country where that multinational group does business.28 From an economic perspective, it is essentially unclear what the “fair or adequate” share of profit in a country might be. Income or profit is economically defined as a

natural or legal person’s change in net assets in a certain period of time. However, this definition does not refer to locations where income or profits may come from. Therefore, public CbCR lacks a clear-cut theoretical concept of the adequate amount of profit in a certain country. Given this lack of theory, the definition of a fair share of profit is purely a matter of debate and arbitrary value judgments.

Nevertheless, one argument in favour of public CbCR is that, if not yet considered originates from international politics. Given that multilateral negotiations can suffer from a lack of willingness to cooperate, public CbCR can be interpreted as a necessary tax policy tool that represents the smallest common denominator for fiscal authorities. However, this argument speaks for private CbCR. The argument’s support for public CbCR is negligible, because public CbCR is not a substitute for a lack of international cooperation.29 By means of international cooperation, countries may agree upon an allocation of profit taxes that they consider to be fair and to be in their common interest. This is not necessarily the case with public CbCR. Even if public CbCR is effective and exerts the expected pressure on MNEs’ international profit shifting, MNEs have the choice to adapt their international tax planning. In the end, it is not the countries but the MNEs that decide about profit tax allocation across countries, based on their business and corresponding investment decisions.

2.3. General public’s (receiver’s) perspective

From the receiver’s perspective, three key questions need to be answered. Firstly, what is the objective of public CbCR? Secondly, is the information provided understandable and appropriate for achieving this objective? And thirdly, what are the decisions to be taken by the general public?

Regarding the purpose of public CbCR, two potential objectives are obvious: On the one hand, the existing/perceived informational gap of the general public concerning tax information availability could be bridged, entailing potentially positive political side effects. Following, for instance, the example of the Nordic countries regarding higher tax transparency could strengthen the perception of democratic equality in terms of a fair tax system. In that case, the requirements for the appropriateness of the data are quite limited. Given that hitherto unknown information is disclosed, the impression of improved transparency is supported. However, introducing public CbCR could also be interpreted as a cheap way to achieve political publicity; because politicians send a signal to the general public that they take effective action, thereby concealing their difficulties to apply or develop appropriate tax law instruments and simultaneously burdening the MNEs with additional compliance costs.

On the other hand, reducing an MNE’s appetite for tax planning, and thus undesired corporate behaviour, by means of public pressure or reputational concerns could be another objective. From a theoretical perspective, the

25. For example, due to an aggregation of figures on the country level.
27. This aspect is adding to the comparability issues already created by the aggregation of CbCR data on the country level only.
28. See Remeur, supra n. 11, at p. 2 et seq.
29. Nonetheless, public CbCR might be considered an additional signal to certain countries, calling for an improved international cooperation on their part.
key CbCR figures provided should be sufficient indicators for the MNEs’ financial position indicating their appropriate tax payment. In section 2.1., doubt has been expressed, however, that the current set of key figures to be reported under public CbCR achieves this outcome. For EU financial institutions, public CbCR is already mandatory. Here, the empirical evidence on the effects of public CbCR is mixed: early empirical evidence casts doubts on public CbC reporting as an instrument to prevent international profit shifting. At least, average effective tax rates are not altered significantly.\textsuperscript{30} Another recent study, however, provides evidence for higher effective tax rates of European-based multinational banks in the post-CbC reporting periods compared to their domestic peers.\textsuperscript{31} Moreover, evidence has been provided that after the introduction of mandatory public CbC for European banks, tax haven presence has declined as compared to non-reporting industries.\textsuperscript{32} Obviously, extant research shows inconclusive findings. Furthermore, no investor reactions can be observed, which may be explained by an anticipation effect. However, for banks doing business in tax havens and for banks with a customer orientation, evidence for a negative effect on firm values has been observed.\textsuperscript{33} Moreover, the EU regulation which mandates companies in the extracting industries (gas, oil, mining) to publicly disclose their tax payments has resulted in decreasing firm values, investments abroad, and extraction licences.\textsuperscript{34}

Recent empirical evidence suggests that private CbC is working properly, as it may prevent aggressive tax planning by involvement in tax havens and accrual-based profit shifting.\textsuperscript{35} This, however, is not the end of the story. Given that MNEs refrain from profit shifting to tax havens or low-tax countries, MNEs may substitute profit shifting by investment shifting. Empirical evidence suggests that MNEs react by allocating revenue, employment, assets and corresponding tax payments to low-tax countries.\textsuperscript{36} Although one can only speculate about the size of this effect, it seems likely that MNEs’ reaction to mandatory public CbC would essentially be the same. When MNEs shift real investment to other countries, they report profits and taxes in countries where they do business. This may be perfectly in line with the purpose of public CbC. Therefore, high-tax countries that promoted CbC in the first place may find themselves in an uncomfortable position once public CbC comes into effect: MNEs reacting to public pressure reduce not only their tax payments (as they may have done before), but also cut back investment and employment in high-tax countries.

3. Conclusion

In order to answer the question of who benefits from the introduction of public CbC, two perspectives have to be distinguished – the informational and the political perspective.

To start with the informational perspective, improving transparency is not automatically achieved by publishing more reports. What could help, however, is a better understanding of the underlying facts by disseminating the information to a broader set of stakeholders at a cost that is not over-compensating the informational advantage. From the informational perspective, it is hard to identify who would actually benefit from the introduction of public CbC. It is likely that MNEs would face higher compliance costs due to preparing a new tax report, i.e. the annotated public CbC. Tax authorities do not necessarily benefit either, as they do not receive new information, since private Cbc data are already at their disposal. The general public would receive more information. However, a cost-benefit analysis reveals many drawbacks of public CbC that have to be considered. As it is the tax authority rather than the general public that is responsible for collecting taxes, public provision of tax data has to be justified by other benefits. And whether end consumers’ procurement decisions are improved by the availability of tax data may well be doubted. On the other hand, from an informational perspective, certain beneficiaries strongly advocating public CbC may be NGOs, like Tax Justice Network or Transparency International.\textsuperscript{37} In summary, from an informational perspective, the authors do not see conclusive theoretical or empirical evidence supporting the notion that public CbC provides additional benefits beyond private CbC.

Turning to the political perspective, the answer to the above question is not clear-cut. The law demands compliance with national tax regulations. However, “mere” adherence to applicable tax law may – in an environment dominated by tax morale debates – not be sufficient for preventing reputational loss from perceived tax avoidance.

\begin{thebibliography}{9}
\bibitem[*]{} Martin Lagarden, Ulrich Schreiber, Dirk Simons, Caren Sureth-Sloane et al.
\end{thebibliography}
From a political perspective, MNEs will not benefit from public CbCR at first glance. They will be facing more discussions with different public stakeholders beyond their ongoing discussions with fiscal authorities and other tax professionals. These additional discussions will increase their communication costs. However, MNEs may benefit from presenting themselves as “good corporate citizens”. Separating themselves from the “bad firms” could be a means of improving customers’ and investors’ perception of them. Tax authorities might benefit from MNEs’ reputational concerns and collect higher tax revenues. Furthermore, for those MNEs that present themselves as good corporate citizens, tax enforcement may become easier and thus cheaper. And the general public might value an improved access to more information about potential employers, suppliers and neighbours.


Overall, the major political questions are the following. Should democracies that are based on the rule of law rely on pillories to enforce fair tax payments? What does “fair share of taxes” mean – is perceived moral behaviour an appropriate benchmark for determining tax payments? Will public CbCR data leave even more room for interpretation, tax morale considerations and diverging understanding than tax law and related commentaries in an expert discussion? Are there better ways to strengthen citizens’ trust in the fairness of the tax system, for example, by enabling tax authorities to better identify and collect taxes that are legally defined as appropriate?

Enhanced transparency regarding MNEs’ tax planning may be considered an overriding goal. However, it is obvious that many questions around public CbCR remain unanswered in this regard. As a consequence, it seems doubtful that this additional reporting requirement for MNEs is “fit for purpose”.

The University of Amsterdam and IBFD have combined their expert knowledge to introduce a unique advanced master’s programme: “International Tax Law: Principles, Policy and Practice”. This one-year, full-time programme is based in Amsterdam, the Netherlands.

- Access, including dedicated support, to the IBFD Library, with unrestricted access to the IBFD Tax Research Platform
- International network and opportunities that develop long-term contacts
- Study facilities at both the University of Amsterdam and IBFD
- Each year, a scholarship covering half the tuition fee is awarded to two exceptional candidates

The programme starts every September. Applications must be received by 1 April of the same year. For more information or to apply, visit: uva.nl/lmisinternational-tax-law