

Country-by-Country Reporting: A New Dimension in Taxpayer Compliance Obligations

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Abstract

This paper critically examines country-by-country reporting requirements according to the Australian legislation, and the impact of compliance on large multinational consolidated groups in Australia. The paper analyses the taxation framework on country-by-country reporting in Australia and examines issues that transcend the taxation sphere, such as general business reporting and corporate governance. Using institutional theory, this paper demonstrates the implications of country-by-country reporting for Australian corporate entities.

Keywords: Country-by-Country Reporting; Compliance; Accounting; Institutional Theory; Australia

1. Introduction

In the search for greater tax transparency and accuracy in reporting, the efforts of the G20/Organisation for Economic Co-operation and Development (OECD) and European Union (EU) have led to shifts in the global tax landscape with the introduction of base erosion and profit shifting (BEPS) (OECD, 2016) and the 'Action Plan on Base Erosion and Profit Shifting' (OECD, 2013a). The Action Plan contains a number of actions designed to address the issue of BEPS. In particular, Action Plan 13 focuses on the issue of transfer pricing documentation and country-by-country reporting (CbCR) (OECD/G20, 2015). Under the CbCR requirements outlined in the BEPS Action Plan 13, multinational enterprises (MNEs) are required to provide and report financial and tax information detailing their global allocation of income and taxes. Since the introduction of CbCR, approximately 50 countries, including Australia, have agreed to incorporate the OECD's CbCR recommendations into their domestic legislation to varying degrees. Furthermore, 40 countries have signed the OECD's Multilateral Competent Authority Agreement on CbCR, which will facilitate the automatic exchange of CbCR information among signatories. CbCR compliance requirements may have varying effects on MNEs, and in particular, impose certain challenges and obstacles. The strategic responses of MNEs will be central to preparing them for compliance and helping CbCR become established as authoritative guidelines for tax behaviour.

This analytical paper considers the implications of CbCR requirements and how MNEs can respond as organisations. In particular, this paper considers how corporate entities may change their systems, structures and procedures in response to this legislation to equip them for compliance and receive legitimacy from tax authorities. As explained by institutional theories, organisations exist in specific physical, technological, cultural and social environments to which they must adapt (Scott, 1998) to gain legitimacy (Meyer & Rowan, 1977) and continued societal support. Consequently, certain institutional structures, such as rules, routines, norms and schemes become authoritative guidelines for organisations by shaping their structures, systems, cultures and behaviours. As CbCR becomes institutionalised in Australia, Australian corporate entities may adapt their systems and structures and undertake strategic behaviours in order to support their compliance and secure their legitimacy with national and international tax authorities and other external stakeholders. This paper contributes to the very limited academic literature on CbCR by first outlining the global implications of CbCR for reporting entities, and then alluding to the various strategic and calculative considerations reporting entities will need to consider in preparing themselves for CbCR compliance. The key matters and issues of CbCR and the possible responses outlined in this paper will provide fruitful guidance for reporting

entities in preparing them for CbCR as well as alerting them to various organisational challenges and opportunities.

This paper is organised as follows. Section 2 explains the introduction of CbCR in Australia. Section 3 discusses how MNEs may account and prepare for CbCR requirements. Section 4 examines accounting for CbCR reporting, Section 5 contains a critical perspective on CbCR reporting and Section 6 presents the conclusions.

2. Background—The Global Context

The erosion of the tax base by artificial shifting of profits to low tax or no tax jurisdictions is a serious issue, which affects most developed and developing countries. Profit shifting and base erosion practices are possible where there is low tax transparency associated with inadequate or outdated tax legislation and poor international coordination between tax authorities. As highlighted by Longhorn (2015), ‘BEPS is a complex and multifaceted problem perceived to be facilitated by the non-transparent reporting practices of multinational entities as enabled by existing regulations’ (Longhorn, 2015, p. 1).

According to estimates from the OECD, base erosion results in an annual revenue loss of between USD \$100 and \$240 billion (OECD, 2015a). Among other factors, lack of tax transparency, lack of coordination between tax administrations and poor interaction with domestic tax rules have been mentioned as some of the main causes for these losses. However, the consequences of BEPS go much beyond loss of revenue. BEPS minimisation strategies undermine the notion of tax justice, where the wealthiest entities pay little or no tax, while individuals and smaller entities bear the bulk of the tax burden. In order to address this issue, tax and policy specialists from the OECD and G20 countries analysed the tax planning strategies utilised by multinational companies to identify the loopholes that allowed opportunities for BEPS. The findings were published in the 2013 report entitled ‘Addressing Base Erosion and Profit Shifting’ (the BEPS Report) (OECD, 2013b). Following the BEPS Report, and as noted above, the OECD/G20 group issued the ‘Action Plan on Base Erosion and Profit Shifting’ (the BEPS Action Plan), which comprised 15 action points with recommendations to address the issues of each particular area. The BEPS Action Plan final reports were published in 2015 and contained a number of recommendations for legislative changes in the relevant areas of concern. CbCR was introduced in Action 13 as part of the transfer pricing documentation recommended actions designed

to increase tax transparency (OECD, 2015b). Action 13 is specifically aimed at MNEs with annual consolidated group revenue equal to or exceeding EUR 750 million (or equivalent in domestic currency), requiring that they provide annual statements detailing their business activities and allocation of profits to the tax authorities of the countries where they do business (OECD, 2015a, pp. 6–7).

As highlighted in the ‘OECD/G20 Base Erosion and Profit Shifting Project Explanatory Statement’:

Standardised country-by-country reporting and other documentation requirements will give tax administrations a global picture of where MNE profits, tax and economic activities are reported, and the ability to use this information to assess transfer pricing and other BEPS risks, so they can focus audit resources where they will be most effective (OECD, 2015a, p. 6).

Action 13 was further developed into two subsequent reports, the 2015 ‘Action 13: Guidance on Transfer Pricing Documentation and Country-by-Country Reporting’ (Guidance on TP Documentation and CbCR, OECD, 2015c), which outlined the three-level reporting system, and the 2015 ‘Action 13: Country-by-Country Reporting Implementation Package’ (later updated in November 2017, OECD, 2017a), which presented a legislative template to be used by countries in the process of introducing CbCR into their domestic legislations. The findings and recommendations of the three initial reports were consolidated in the 2015 ‘Transfer Pricing Documentation and Country-by-Country Reporting, Action 13—2015 Final Report’ (the 2015 Final Country-by-Country Report, OECD, 2015b), according to which:

- The revised standards for transfer pricing documentation and CbCR incorporated a master file, local file, and a country-by-country report which would outline revenues, profits, taxes paid and certain measures of economic activity.
- The standardised approach meant that (i) taxpayers will need to review and articulate their transfer pricing positions and (ii) the information will be provided to the tax authority in a standardised format, thus facilitating the risk assessment and audits processes.
- Some CbC reports will be automatically exchanged (or exchanged at request) between tax authorities.

Under the recommendations of Action 13, the statements to be provided by relevant MNEs under the CbCR requirements are:

- a) The master file: The master file will contain high-level information regarding the MNE's global business operations and transfer pricing policies, and will be made available to all relevant tax administrations.
- b) The local file: The local file will be lodged with the local tax authority and will include detailed transactional transfer pricing documentation, identifying material-related party transactions and their respective amounts, as well as the MNE's analysis of the transfer pricing determinations made in relation to those transactions.
- c) The CbC report: The CbC report will typically be prepared by the MNE's parent entity and will provide, on an annual basis, details on revenue, before tax profits, income tax paid and accrued, number of employees, stated capital, retained earnings and tangible assets for each country in which the MNE does business. It also requires that the MNE identifies and explains the business activities undertaken by each entity within the group in each jurisdiction (OECD, 2015e, p. 37).

As the legislative template refers to automatic exchange of reports between tax authorities, the implementation of CbCR is also related to the application of the Multilateral Convention on Administrative Assistance in Tax Matters (OECD & Council of Europe, 2011), as well as to the double taxation agreements and information exchange agreements in force between the countries involved. Therefore, the process of implementing CbCR legislation may require further amendments to existing double taxation agreements and information exchange agreements to accommodate the new reporting requirements.

Since the 2015 Final CbC Report was published many countries have made considerable progress in introducing CbCR into their domestic transfer pricing regulations. Alongside other OECD countries, Australia has recently enacted CbCR legislation, which has applied since 1 January 2016, with the first round of CbC reports expected on 30 June 2018.

3. Country-by-Country Reporting in Australia

Following the OECD recommendations of BEPS Action 13, in December 2015 the Australian Government enacted amending legislation introducing CbCR obligations to certain categories of large multinational consolidated groups, effectively implementing the recommendations of Action 13 of the OECD/G20 BEPS Action Plan (Action 13) (OECD, 2015b, 2017a). The new legislation, introduced into

the Australian Income Tax Assessment Act 1997 as Subdivision 815-E (Subdiv 815-E ITAA97), applies to years starting 1 January 2016 and demonstrates the Australian Government's commitment to global tax transparency and Australia's engagement with other tax jurisdictions in fighting international tax avoidance by profit shifting (Commonwealth of Australia, 2015 a,b).

The Australian CbCR requirements reflect most of the recommendations of Action 13 (with the exception of the particular format adopted for the local file) and target a group of entities legally referred to as 'significant global entities' (SGEs), comprising Australian resident corporate entities that are either 'global parent entities' (GPEs) or members of consolidated multinational groups with an annual global income exceeding AUD \$1 billion (Commonwealth of Australia, 2015b). The concept of SGE also includes cases where the global group's annual income exceeds the \$1 billion threshold due to an extraordinary transaction in one year only, unless the group is granted an exemption upon written application to the Commissioner (ATO, 2017; Commonwealth of Australia, 1997).

The main reason why only SGEs are required to comply with CbCR obligations is related to the belief that large MNEs have more opportunities to engage with aggressive international tax avoidance schemes (Commonwealth of Australia, 2015b, paras 2.4–2.5) involving related party international dealings (OECD, 2015a, p. 4). In these cases, tax is avoided (or evaded) generally through artificial shifting of profits to lower tax or even to no tax jurisdictions, effectively eroding the tax base through exploitation of gaps and mismatches in the tax legislation, ultimately undermining the principle of tax justice and the fairness of tax systems (Cortellese, 2016, p. 5; Nethercott & Gonzaga, 2016). For example, multinational groups often have subsidiaries in several countries, meaning that they do not necessarily have to engage third parties to finance their transactions. By utilising intra-group loans multinational entities can easily claim excessive interest deductions on intra-group debts. Analysing the introduction of the new Australian Multinational Anti-Avoidance Law (MAAL) and the introduction of CbCR, Antony Ting explains that the creation of intra-group debt is a tax avoidance tool which is both relevant and relatively simple to implement. The simplicity is because it does not require the involvement of third parties or movement of personnel or assets. This type of arrangement only requires a legal agreement between the Australian subsidiary and the overseas subsidiary whereby the interest on the loan repayments is claimed by the Australian subsidiary while the overseas subsidiary who receives the interest is subject to low (even zero) tax on this income. Furthermore, as intra-group loans are not subject to the constraints that would generally apply to amounts, interest

rates and credit securities in an unrelated-party transaction, such intra-group loans open an avenue for manipulation and flexibility. (Ting, 2016)

SGEs are also much more likely to be regarded as being at high risk of obtaining a transfer pricing benefit, and as such, producing the CbCR statements would allow such entities to properly justify their intra-group international dealings (Cortellese, 2016, p. 24). Ultimately, CbCR is relevant not only for tax purposes, but as highlighted by Murphy (2012), Longhorn (2015) and Cortellese (2016), it is mostly important for the purposes of general transparency affecting global corporate social responsibility, corporate governance, accountability, and on a macro-economic scenario, prevention and combating of corruption, political stability, economic development and fair trade.

The Australian CbCR requirements require that SGEs lodge three separate statements, being (i) the CbC report, (ii) the master file and (iii) the local file (see Appendix 1 for detailed explanations of each statement) with the Australian Taxation Office (ATO) within 12 months after the end of their income tax year. While the Australian CbC report and the master file closely follow the OECD template both in terms of content and structure, the Australian local file departs from the OECD model both in relation to content and structure. On what concerns the structure and format, the Australian local file is closely related to the International Dealings Schedule (IDS), which forms part of the Australian transfer pricing documentation requirements (see Appendix 1 for detailed explanations of transfer pricing documentation). Having said that, the Australian local file follows a two-tier structure, which aims at facilitating compliance by entities with less complex transfer pricing affairs. The first tier is the 'short form local file', which must disclose data on the reporting entity's organisational structure, including business strategies and restructures affecting the entity in the current or previous income year; the entity's management reporting hierarchy, indicating the countries to which local managers report, as well as a description of any transfers of intangibles in the current or previous year, and finally, a list of key competitors. However, as the eligibility requirements are extremely limited and the materiality thresholds are very low (ATO, n.d.), in practice very few entities will benefit from this simplified reporting option.

The 'full local file' is the standard report for any entity not eligible to lodge the short form local file, and it must include all the data required in the short form local file plus two additional parts. In the local file 'Part A', the entity will disclose information regarding all controlled transactions for the relevant income year, including the names of the Australian and foreign counterparties (and their countries of residence), category of transaction and the income and expenses associated with such

transactions (including transactions of capital nature), the transfer pricing method (or capital asset pricing method) relied upon, and finally, the transfer pricing documentation code. The local file 'Part B' will further extend the information from Part A and will require that the reporting entity provides copies of all intercompany agreements underpinning all material international intra-group transactions, as well as any advance pricing agreements in relation to the Australian transactions and general purpose financial statements.

It is the local file Part A which is substantially similar (although with a much deeper level of detail) to the IDS Part A. Due to this relative overlap, the ATO authorises entities who voluntarily lodge the local file Part A together with their income tax returns to skip the majority of the questions of the IDS Part A. Where this is the case, the local file Part B must still be lodged by the relevant deadline. Most importantly, SGE global management teams wishing to prepare their global CbC statements based on the OECD templates will need to keep in mind the peculiarities of the Australian local file and make sure it is prepared in accordance with the Australian model, or otherwise they could be at risk of failing to comply with the Australian CbC requirements and therefore be subject to heavy penalties (PwC, 2016).

Notwithstanding, the clear interface between the transfer pricing documentation and the CbCR statements, it is important to clarify that the CbCR statements and the transfer pricing documentation (which includes the Transfer Pricing Report [TPR]) and the IDS constitute independent compliance requirements based on separate legislative bases. For this reason, even though there are similarities between the two sets of statements, they are not substitutes for one another. The transfer pricing documentation, although technically not mandatory, is required for the purposes of establishing a reasonably arguable position and for penalty protection.¹ However, all SGEs operating in Australia must lodge CbCR statements regardless of volume of operations or materiality of international related party dealings (PwC, 2017). Failing to comply (including by late lodgement) would lead to the application of high penalties to the SGE.

a. Compliance Challenges

Even though CbCR obligations represent a major effort to increase tax transparency and to improve the risk assessment of SGEs, complying with such legislation may pose significant challenges to Australian SGEs. For example, CbC reporting requirements apply to income year beginning on or after

1 January 2016. Considering that in Australia the income year runs from the 1 July until 30 June, and considering that SGEs may lodge their documentation up to 12 months after the end of the income year, the first CbC deadline is 30 June 2018. However, the operations developed during this period of time might not necessarily have begun exactly on or after 1 January 2016. On many occasions, the reports may contain several entries of intra-group loans taken before January 2016, which might not have been documented in accordance with the CbCR obligations because there were no such obligations at the time the underlying legal agreements were entered into. Therefore, it is possible that entities may face the challenge of having to report on structures and operations that may be missing information that was not originally recorded because there was no legal obligation to do so. This represents a challenge insofar as failing to produce adequate evidence, especially for the purposes of elaboration of the local file, may place the entity at risk of heavy penalties. On other occasions a SGE may find itself in a position of not being able to produce documents where such documents are supposed to be provided by subsidiaries located in countries that do not have CbCR requirements in place, or simply because the relevant information might never have been available or documented in the foreign jurisdiction. This may also represent an exposure to possible penalties for non-compliance.

As highlighted by Nethercott and Gonzaga (2016), one particularly relevant challenge concerns the interpretation of the materiality thresholds for the purposes of the local file. The problem here is that there is no consensus as to what parameters are to be used in defining materiality: qualitative outcomes or quantitative data? These authors state:

Moreover, it is important to consider that, while some information relating to a reportable transaction may be immaterial when it is considered in isolation, this may not be the case when considered in relation to other transactions undertaken, which, in aggregation, may be material. In this respect, a quantitative guideline viewed in isolation may not reflect what is truly material. (Nethercott & Gonzaga, 2016, p. 4)

The risk here is due to the fact that even though there is no consensus regarding materiality thresholds, penalty provisions will still apply if the information provided by the entity is considered inaccurate. Some of those issues have already been addressed by the ATO in several guidance documents, such as the 'Law Companion Guideline (LCG) 2015/3' (ATO, 2015), where the ATO outlines how the CbCR legislation will be applied. Relevant practical guidance is also provided in other documents such as the 'Country-by-Country Reporting: Questions and Answers' (ATO, 2017), which

address common issues and frequent questions regarding difficulties in complying with CbCR obligations. For example, the 'Country-by-Country Reporting: Questions and Answers' (ATO, 2017) explains that the Australian entity may apply for aligning its reporting period with that of the SGE's GPE where it produces the CbC report and the master file. In a different scenario, the Australian entity may apply for a one-year exemption in relation to lodging the CbC report where the SGE's GPE country of residence does not have CbCR legislation in force.

Finally, it is important to note that in some exceptional and very limited circumstances, a SGE may apply for a temporary exemption from CbCR obligations and, in any case, any exemption would depend on formal, written and well-substantiated application. The one-year temporary exemption regarding the master file (see Appendix 1) is one example. From a different perspective, SGEs headquartered in Australia with no IRP dealings that would need to be disclosed in the CbC report could potentially have good grounds for applying for an exemption (KPMG, 2016b). However, where the SGE has an Australian GPE but has IRP dealings, it would not qualify for an exemption. Considering a purposive interpretation of the Australian CbCR legislation, it could be argued that tax exempt multinational entities operating in Australia would be good candidates for an exemption from CbCR requirements. This is because such entities, being tax exempt, would not be expected to engage in tax avoidance or profit shifting schemes, and as such, would be outside the scope of the CbCR legislation. This could arguably be the case of some multinational civil society groups, multinational charitable entities and foreign universities operating in Australia, among others. In any case, no SGE would ever be automatically exempt, meaning that even tax exempt SGEs would, in principle, have the obligation to comply with CbCR requirements and would potentially be subject to penalties in case of non-compliance or late lodgement.

b. Penalty Protection (Establishing a Reasonably Arguable Position)

Lodging the CbCR statements as well as the transfer pricing documentation on time will offer protection against the increased administrative penalties announced in the 2017 Budget, which came into effect on 1 July 2017. The recently enacted amendment will substantially increase the non-compliance and late lodgement penalties applicable to SGEs by a factor of 100. These penalties were further increased as a result of the adjustment of penalty unit from \$180 to \$210 (Commonwealth of Australia, 2016), effectively pushing the highest possible penalty that can be applied to a SGE to \$525,000 (See Appendix 2).

The failure to lodge on time (FTL) penalties were substantially increased to compel SGEs to comply with their CbCR obligations on time. Where the entity is an SGE the base penalty for late lodgement will be multiplied by 500. As a result, the minimum FTL penalty will start at \$105,000 where the documentation is up to four weeks late, potentially reaching \$525,000 where the entity is more than 16 weeks late. Importantly, the FTL penalties apply to all statements required from SGEs, including income tax and fringe benefits tax returns, business activity statements, CbCR and general purpose financial statements. However, SGEs may be protected by administrative safe harbour provisions where there is evidence that the SGE provided all relevant information to their tax agents and that due to their lack of reasonable care, there was a false or misleading statement or a late lodgement penalty (Woellner, Barkoczy & Murphy, 2016). Notwithstanding, safe harbour provisions may not be argued where it is a case of reckless behaviour or intentional disregard of the law.

c. Tax Auditing Risk Policy and Compliance Burden

CbCR statements represent an important tool both for entities and for the ATO for the purposes of tax auditing risk policy. In its 'Guidance on Transfer Pricing Documentation and Country-by-Country Reporting' the OECD has advised that 'the specific content of the various documents reflects an effort to balance tax administration information needs, concerns about inappropriate use of the information, and the compliance costs and burdens imposed on businesses.' (OECD, 2015c, p. 10). As the three statements will contain a substantial amount of detailed information about the entire group's IRP dealings and allocation of income, the Australian entity will be able to identify and review those arrangements that may be regarded by the ATO as at 'high risk' of raising a transfer pricing benefit.

Much of the information to be utilised in assessing CbCR and transfer pricing risks will come from the data and documents provided in the local file, especially in the documents lodged in the local file Part B, due to the substantive overlap with the information required for the IDS Part A. Therefore, it is extremely important that SGEs keep their intercompany agreements up to date in order to correctly reflect the transactions that they formalise. Even though the ATO has indicated that it will not require SGEs to produce intercompany agreements solely for the purpose of substantiating IRP transactions in the local file, where such agreements did not previously exist the reporting entity must be able to provide enough documentation to substantiate the transaction as well as to evidence the observance

of the arm's length principle. In view of this, it is of utmost importance that Australian reporting entities keep proper tax and accounting records, as well as proper records of their practices, processes, standards and evidence of any reviews thereof.

4. Accounting for Country-by-Country Reporting

As authoritative guidelines for reporting entities, the rules, requirements and routines of CbCR can have certain implications for reporting entities' extant organisational arrangements. As espoused by institutional theories (see for example, Meyer & Rowan, 1977), changes to organisations' social environments and institutional arrangements can lead to them to adapt their structures, processes, people or culture to continue to receive societal support and legitimacy from various stakeholders (Scott, 1998). Therefore, in response to the introduction and implementation of CbCR, SGEs will need to consider, generate and apply a range of effective and timely tax and accounting measures and processes to help support compliance, secure legitimacy (Meyer & Rowan, 1977) with national and international tax authorities and other external stakeholders and manage associated risks.

Although there is no universal or best way approach established to guide and prepare SGEs for CbCR, companies will need to start planning for CbCR with respect to entity-specific needs and circumstances. Undoubtedly, this will require SGEs to take a proactive approach to various tax, accounting and accountability considerations and practices to prepare themselves for CbCR compliance and achieve legitimacy from tax authorities. To prepare and safeguard themselves against these challenges, SGEs may need to review and adjust their strategies, data management, risk management, governance and reporting structures and all other CbCR compliance-related practices. This section of the paper discusses the significance of these considerations in preparing and adapting SGEs for CbCR.

a. Corporate and Local Strategies

The introduction of CbCR presents SGEs with both challenges and opportunities. SGEs can prepare themselves for CbCR compliance and any (un)anticipated challenges by developing flexible CbCR approaches and strategies (KPMG, 2016a). A coordinated and consistent response strategy reflecting the interests of the reporting entities and the tax authorities is likely to generate greater benefits for SGEs (KPMG, 2015). Certain strategic frameworks developed at the corporate level with the input of the GPE and its subsidiaries can help determine appropriate reporting governance structures, provide

greater reporting synergies among SGEs, promote voluntary disclosure and dissemination of information across corporate reporting systems and achieve a degree of standardisation in preparing and submitting CbC reports. Corporate CbCR strategies can also facilitate revisions and adjustments to tax strategies and policies across the SGEs, leading to the (re)development of authentic and transparent tax structures and policies across entities, which may be effective in strengthening SGEs corporate tax communication internally and externally. If corporate CbCR strategies and approaches are not able to be established, then it is essential that business strategies are developed at local entity levels to help govern reporting entities. As mentioned earlier in this paper, an inability to comply with all reporting requirements may not only result in penalties, it can also have adverse effects on companies' public image, compliance burdens and competitive edge. Therefore, whether it is at the corporate or local business level, clearly defined strategies and approaches to CbCR will be a stepping-stone in preparing reporting entities for compliance and responding to possible risks and opportunities.

SGEs' strategic responses to the introduction and implementation of CbCR may vary. For example, some SGEs have begun articulating the magnitude and complexity of CbCR requirements and in response are taking immediate action (i.e., diagnostic reviews and strategic planning) to evaluate their tax business policies and reporting structures in line with CbCR expectations (KPMG, 2015). As part of these contemplations, companies will need to assess and determine how to treat certain items for CbCR, such as branches, minority investments, permanent establishments, joint ventures, and subpart F income (Deloitte, 2016a, p. 5). Companies have also begun evaluating their existing IT systems, data collection and aggregation processes, as well as their financial reporting systems by performing dry-run CbC reporting using data from previous years in preparation for the real reporting period (Deloitte, 2016a, PWC, 2015) and to determine how the CbC report will be interpreted by tax authorities. While some companies are proactively articulating the possible effects of CbCR, other companies are taking a 'wait and see' approach to CbCR (Deloitte, 2016a). Instead of planning for what is ahead of them, these companies are waiting for the reporting period to near first. However, as reporting deadline nears, companies will eventually need to confront and respond to compliance expectations and burdens as well as the challenges imposed on their current processes, systems, structures and people.

Regardless of the timing and extent to which strategies are developed, proactive development of clear philosophies and strategies for CbCR at the corporate and business level, combined with corporate values, will assist reporting entities' compliance with CbCR expectations. CbCR strategies can also

support corporate reputation management through the consistency achieved in information disclosures and reporting across all SGE groups (KPMG, 2015). Planning and strategising for CbCR will be pivotal in preparing companies for compliance without significant burdens and difficulties. Non-compliance may also be an obvious strategy for some entities. However, the cost (high penalties) of non-compliance is likely to redirect SGEs to the correct path of planning and preparing for CbCR compliance.

b. Governance and Reporting Structures

The introduction and requirements of CbCR may require SGE boards to not only strategise, but also to reconsider their corporate governance structures and financial reporting arrangements. Incoherent or inappropriate structures and practices may inhibit companies from retrieving vital information and generating the reports required by CbCR. Governance structures and reporting systems tailored for CbCR will be effective for identifying and assigning key CbCR responsibilities and accountabilities among the SGE group. The establishment of clearly defined reporting structures and systems will help facilitate the generation and gathering of the information required for CbCR. If explicit governance structures and reporting streams are not determined in advance, reporting entities may face certain difficulties or conflicts in retrieving data required to prepare their CbC reports. This may be the case if, for example, GPEs or certain subsidiaries are residing in countries that have not implemented CbCR or are delayed in doing so.

Without the collaboration and support from the GPE and other subsidiaries, the reporting entity may encounter difficulties in gathering all required information and providing complete reports to its tax authorities. For instance, specific CbCR-relevant information may be omitted from the reports if the information resides with the GPE or another subsidiary in different realms and could not be retrieved and reported due to foreign jurisdiction privacy concerns or delays in information transfers. Regardless of whether GPEs or other subsidiaries are exempt from reporting, local reporting entities will still be required to supply the master file and local file to their tax authorities. A key question then arises as to who is accountable for producing and filing these reports. Although the OECD recommends that all SGE groups file CbC related reports, if the GPE or a subsidiary operates in a jurisdiction where CbCR is not mandated then they may not be motivated to fulfil such requirements. In addition to the establishment of intra-subsidary reporting and governance structures, reporting entities will also need to determine their own entity's reporting and governance structures. For instance, the reporting entity will need to consider who within their own organisation (i.e., senior managers, tax division,

board of directors, middle managers) is responsible for generating and managing the information required for CbCR and preparing the CbC report. Clearly defined roles, responsibilities and accountabilities within the organisation will allow the reporting entity to better prepare itself for CbCR and meet all the requirements for compliance. Therefore, reporting entities should be considering who within their organisation will be responsible for what in relation to CbCR expectations, and who will be held responsible if requirements are not met.

In preparation for CbCR, SGEs should clearly assign accountabilities among the GPE group to determine who is responsible for preparing and submitting the reports and files required by CbCR. Clearly defined roles and responsibilities will be effective for determining which group of the SGE will be exempt from submitting the CbC report and master file and ensuring that local files are prepared accurately and are consistent with the CbC report and master file. An inability to assign roles and clarify responsibilities may result in the omission of significant data and submission of incomplete reports to tax authorities.

c. Managing Data

The vast amount of information required for CbCR will necessitate the need for appropriate and efficient data collection and management systems and staff expertise for the generation, collection and aggregation of relevant data from multiple sources in a timely manner. Developing and implementing consistent data management systems suitable for CbCR across all SGE groups will require time, effort and expertise. It can take six to nine months for an entity to implement a new centralised data collection process (Deloitte, 2016b). Therefore, corporate entities and their professional advisers should assess their current data management system capabilities and perform data mapping to identify and determine if any changes will be required to enhance existing data collection systems or implement completely new ones. Entities should also assess their tax functions and perform legal entity and jurisdiction mapping to ensure consistency of tax policies, approaches and reporting across cross-border operations. Inconsistencies in tax policies may result in the collection and reporting of inappropriate data, leading to the misinterpretation of reported data by tax authorities when local reports are exchanged among different jurisdictions and reconciled with the main CbC report.

To help compile the various information required for CbCR, a standardised (i.e., use of SharePoint, Excel or MS Office) and consolidated approach (Deloitte, 2016b) across all entities can ease the burden of combining information from multiple groups and sources, especially if data is available across corporate systems. According to Nethercott and Gonzaga (2016), the development and implementation of joint reporting systems and adoption of same definitions among SGE groups can help minimise the time involved in gathering and reporting information. A centralised approach can also ensure that all entities involved in collecting and reporting data have the same understanding about the parameters around the requested information. Potential misunderstandings among entities may hinder the integrity and certainty of information collected and reported. Therefore, reporting entities should deviate from their current standalone processes to collecting and reporting local tax data and embrace data harmonisation and aggregation at the SGE country level to ensure consistency and integrity of reported data across all reporting SGE groups. They should also establish simple and routine approaches that can manage voluminous data and gather important information on a regular basis. For instance, Deloitte (2016a) suggests the integration of tax data analytics into entities tax compliance systems to gauge CbCR readiness by assisting entities with the collection and interpretation of data and the prevention of data anomalies and unintended consequences. Effective and appropriate data management systems and processes will be vital to help alleviate the burdens of preparing CbC reports and achieving greater synergies across all corporate entities, which will help support CbCR compliance.

d. Managing Risks and Exposures

CbCR may give rise to certain risks and exposures for reporting entities. CbCR-related risks may range from compliance risks to reputational risks. CbCR will provide tax authorities with detailed and transparent financial information about SGE group operations and tax strategies. This information can give tax authorities opportunities to undertake high-level transfer pricing risk assessments, and therefore, help them to allocate tax audit resources accordingly. The detection of data anomalies, non-arm's length behaviour and high-level transfer pricing risk across entities may lead to tax authorities raising concerns and wanting to interrogate the entity's transfer pricing and tax practices, which may lead to audits or more extensive compliance burdens for entities (i.e., adjusting transfer pricing methods). Reporting entities can manage and mitigate (un)anticipated risks relating to CbCR by undertaking timely risk assessments and developing well-constructed tax risk management systems and frameworks across all SGE groups. A lack of risk management can be costly for SGEs, both

financially and non-financially. Aside from incurring penalties and further costs, SGEs may risk damage to their reputation and competitive advantage (Evers, Meier & Spengel, 2014).

SGEs can begin identifying and assessing the impact of possible risks of CbCR by undertaking dry-run simulations using historic data. Diagnostic review tools (KPMG, 2015) can also help evaluate readiness for CbCR compliance and ability to respond to likely risks and opportunities. As part of these simulations, companies should also consider whether their existing risk management frameworks are sufficient to track and manage CbCR-related risks. The extensive requirements of CbCR may require the adoption of more advanced and proactive data analytic approaches (Deloitte, 2016a) and processes that can help detect and rectify various risks. Analytical techniques can help validate and benchmark the data required for the CbC report. It can also help reporting entities to understand risks associated with events and practices that have already occurred. Additionally, it can provide opportunities for foresight by allowing scenario planning for possible tax outcomes and considering alternative strategies and approaches to CbCR. These qualitative deliberations facilitated by data analytics can detect data errors and identify the root cause of errors and anomalies in transfer pricing policies prior to reporting, which can be rectified prior to the CbCR submission deadline. Therefore, companies should begin devising effective risk management strategies and practices to manoeuvre CbCR-related risks.

e. Compliance Costs

Evers and colleagues (2014) classify CbCR-related costs as direct and indirect. Direct costs relate to the compliance burdens such as outlays incurred for updating or adjusting extant data, financial reporting and IT systems and processes. Direct costs also relate to the ongoing preparation and reporting of CbC reports, as well as costs incurred for employing external tax expertise to undertake a diagnostic review of current systems and capabilities for CbCR and provide guidance on preparing CbC reports. On the other hand, indirect costs may arise because of the disclosure of corporate sensitive tax information, which may become public. If no legal protections are enforced by jurisdictions to ensure the confidentiality of local reporting entities reported information, the availability of commercially sensitive tax data to competitors may affect the competitive advantage of SGEs. The disclosure of tax payments by reporting entities in certain jurisdictions may also violate the principle of tax secrecy governed by tax law (Evers et al., 2014). CbCR may also give rise to double taxation for a reporting entity if relative tax authorities use the CbC reports to claim additional tax payment from the company (Evers et al., 2014). Another potential indirect cost may be reputational costs. If certain entities do not

fully meet their CbCR requirements or if their CbC reports unveil information that leaves the entity's tax affairs under further scrutiny, then the entity may face reputational harm from tax authorities as well as the public. Therefore, to minimise direct and indirect compliance costs, it is essential for reporting SGEs to develop and implement proactive strategies, appropriate governance and tax structures, reporting systems and risk management frameworks that facilitate CbCR compliance and reduce (un)anticipated burdens and costs.

Overall, the introduction of CbCR in Australia will require Australian SGEs to evaluate their organisations in the context of a new tax institutional environment, and to some extent, adapt their organisational arrangements to help prepare themselves for CbCR expectations and achieve compliance. A lack of consideration of the possible implications of CbCR on organisational interpretive schemes (i.e., corporate and local strategies) and design archetypes (such as organisational structure, data management system, roles and accountabilities and risk framework) may threaten SGEs' ability to fulfil the demands of CbCR, and potentially impair their reputation with various stakeholders, including legal tax authorities. An inability to comply with CbCR expectations and fulfil all reporting requirements may leave certain stakeholder questioning the credibility of GPEs and their legitimacy in terms of maintaining appropriate transparent and accurate tax reporting. Therefore, in order to continue to receive societal support and legitimacy, GPEs should plan and prepare themselves for the opportunities and challenges of CbCR and adapt their organisations where appropriate (Meyer & Rowan, 1977).

5. A Critical Perspective

From the above analysis, it can be seen that the CbCR issue is not only important from a tax perspective, but it also is a reflection of the change in regulatory authorities and social perspectives at a local and global level arising from fiscal leakage. Furthermore, it should be seen as only part of the BEPS action plans designed to address the issue of BEPS (OECD, 2013b). While the implementation of such a policy can be viewed through a local prism such as that in Australia, effective implementation is dependent upon global co-operation with the appropriate policies as evidenced by the BEPS action plans but also on an administrative process that is able to implement and monitor compliance. In this sense, and from an Australian perspective, the amendments to the ITAA97 contained in Subdivision 815-E may be seen as a welcome addition to the ATO armoury in reducing fiscal leakage arising from international transactions that lack commercial substance. However, the practical outcome will be dependent on local compliance by the affected SGEs as well as the ability of the ATO to access

information offshore by related parties where necessary. While at first instance this will rely on voluntary disclosure of information by Australian SGEs, in a global sense there may also be a need for the effective exchange of information through the multilateral exchange of information between relevant overseas jurisdictions (OECD, 2017b). Without such an agreement, there is a concern that the appropriate information required under the CbCR provisions may not be obtained.

Australia has been actively involved in the BEPS project for some time, and has been supportive of the recommendations contained in the BEPS Action Plans. The legislation contained in Subdivision 815-E very much mirrors the Action Plan 13 outlined in the BEPS Action Plan. However, with the introduction of Subdivision 815-E there may be some concern whether various countries may introduce their own legislation, which may not be consistent with the BEPS Action Plan recommendations. A lack of consistency by way of information, disclosure requirements or operative and penalty provisions may undermine the effective operation of Action Plan 13 at a global level and especially reduce the effectiveness of any information exchange of information between countries.

As a reflection of the above, some of the following issues arise with the Australian legislation relating to CbCR. First, it is not clear whether there is a need for overseas financial statements to comply with Australian accounting standards. If overseas countries are compliant with International Financial Reporting Standards (IFRS) as released by the International Accounting Standards Board (IASB) there may not be a significant issue. Nevertheless, it cannot be assumed that there is an immediate compliance by countries adopting IFRS with Australian accounting standards. This is because some Australian standards contain additional disclosure requirements. In the case of entities affected by the CbCR rules (such as a corporate limited partnership, or where the taxpayer is a foreign resident operating a permanent establishment, and did not lodge a general purpose financial statement [GPFS] with the Australian Securities and Investment Commission [ASIC], etc.), there may be a need to formalise information that is compliant.

In addition, in the case of large multinational corporations the question arises as to whether the consolidated statements of the parent entity would be compliant. Given the earlier comments, it may be possible that such consolidated statements are not compliant. It is understood that that the ATO is seeking feedback on the issue. A main example of where such a difficulty would arise is in the situation where the parent entity is a USA company. As such, for reporting purposes in the USA the entity would be required to adopt USA Generally Accepted Accounting Principles (GAAP). As the USA

GAAP is not compliant with IFRS such disclosures would not meet the requirements of the CbCR provisions in Subdivision 815-E. If such an outcome arises there would be a significant cost in making such reports Australian compliant and very much raise the issue of penalties being imposed. While an immediate solution would be for the legislation to require disclosure-based non-IFRS compliant reports the issue of USA GAAP is a major issue. It is understood the ATO has indicated that as part of a transitional process for the first year SGEs may comply with their respective countries' accounting standards. However, this is not enshrined in any legislative process.

In relation to CbCR requirements, the ATO has indicated that the financial statements lodged with the ATO will not be required to be audited. This is quite an anomaly. While it is a requirement that the CbCR financial statements must be compliant with Australian standards there is no process to verify the veracity or integrity of the data other than through the penalty provisions relating to false and misleading statements. In an attempt to address some of these issues, the ATO has released the 'Law Companion Guideline 2015/3' (ATO, 2015). However, the guideline is somewhat dated and does not adequately resolve the matters raised above. Furthermore, it is a questionable outcome that uncertainly in legislation is addressed by the release of a law companion guideline, only part of which is designated as a public ruling (see paragraphs 1–39). It can be seen from the discussion above that the issue of CbCR is an important issue for SGEs. According to Nethercott:

...it is suggested that a proactive awareness and implementation of an appropriate policy concerning CbCR requirements is a prudent course of compliance and risk management for MNEs to adopt (Nethercott, 2017).

The task of compliance with the provisions in Subdivision 815-E is onerous and time consuming, especially where there are a number of overseas entities that may come within the scope of the provisions. In this respect, given the urgency of compliance with such statements recasting to the financial year ending 30 June 17 required to be lodged with the ATO by 31 March 2018, there is a degree of urgency to ensure affected companies are compliant and avoid any related penalties. Although it is the SGE's responsibility to ensure compliance, the question arises as to whether the entity will undertake this task, delegate it or outsource it to their professional adviser. Where such a task is delegated, it will be critical that the appropriate advisers and the entity concerned have an engagement letter or formal process established to ensure the relevant financial information is documented in a timely and accurate manner.

6. Conclusion

With the release of the OECD Action Plan 13 concerning CbCR disclosure and the formalisation of the Australian requirements in Subdivision 815-E it is suggested that the local Australian and global environment concerning fiscal leakage through BEPS has become much more aware and concerned. In this sense, institutional theory may also have some importance and relevance in understanding and addressing the issue of BEPS. As stated earlier, organisations need to be aware of the cultural and social environment in which they act in order to gain legitimacy and the continued support of society (Meyer & Rowan, 1977). However, it should be noted that in order for such an issue to be satisfactorily addressed it would require a cohesive and global effort to resolve the issue in the context of all the BEPS Action Plans. While an individual country may attempt to address the matter by implementing domestic legislation, caution is needed to ensure there is no fragmentation of the appropriate global policies as outlined in all of the BEPS action plans and in particular Action Plan 13. In addition, it should be noted that without effective operation of the multilateral treaties on the exchange of information such information might be lacking in integrity or timeliness to address the issue of BEPS.

Appendices

Appendix 1: Outline of Transfer Pricing Documentation and Country-by-Country Reporting Statements

Transfer Pricing Documentation
<p>Transfer Pricing Report: The TPR comprises a detailed analysis of the entity's IRP transactions, with clear identification of the arm's length conditions applicable to each relevant transaction and the comparable circumstances relevant to identifying the arm's length conditions, supported by a functional analysis and benchmarking study in accordance with the applicable transfer pricing methods (ATO, 1998). Even though it is not mandatory to lodge a TPR, lodging it before lodgement of corporate tax returns (Commonwealth of Australia, 1953) allows the reporting entity to establish a reasonably arguable position (ATO, 2014) and provides penalty protection. Having adequate TP documentation has become especially important in view of the recent substantial increase in the penalties for non-compliance with reporting obligations, in force from 1 July 2017.</p>
<p>International Dealings Schedule 'Part A': The IDS is a mandatory part of Australian corporate entities' tax return where the taxpayer is engaged in IRP dealings above the threshold of AUD \$2 million. It follows a questionnaire structure and provides information about the nature and size of a company's IRP dealings for the purposes of risk and materiality assessment; however, it does not require an analysis of the arm's length principle or the transfer pricing methods used by the taxpayer.</p>

Country-by-Country Reporting Statements

Country-by-Country Report: The CbC report follows the OECD recommended model. It is a statement relating to the SGE's global operations and activities, including its transfer pricing policies. This statement is to be prepared and lodged by the GPE at their own jurisdiction and must include data relating to all other members in the global group. In other words, the CbC report is filed by the parent entity but relying on information provided by its subsidiaries. Where there is an information exchange agreement between Australia and the GPE's country of jurisdiction, the CbC report will be automatically exchanged between tax authorities. However, if the parent entity is based in a country that does not automatically exchange information with Australia, or if the GPE's country of residence does not have CbCR legal requirements, the Australian entity becomes responsible for lodging the CbC report with the ATO. In this case, the Australian entity will electronically lodge the CbC report using the OECD XML schema, separately from the local file and master file, which must be lodged using the XML schema designed by the ATO. Finally, if there are discrepancies in the reporting periods, the Australian entity is required to request a replacement of reporting period.

Local File: The Australian local file is substantially different from the OECD recommended model both in relation to its format and in its content. As such, it will require careful preparation and attentive management by reporting entities.

The Australian local file follows a two-tier structure, which aims at facilitating compliance by entities with less complex transfer pricing affairs. The first tier comprises the 'short form local file', which is a simplified version of the 'full local file' and is available to reporting entities with few international intra-group transactions, provided they meet certain eligibility conditions.² The short form local file must contain information on the reporting entity's organisational structure, including business strategies and restructures affecting the entity in the current or previous income year; the entity's management reporting hierarchy, indicating the countries to which local managers report; as well as a description of any transfers of intangibles in the current or previous year, and finally, a list of key competitors. However, because the eligibility conditions reflect very low materiality thresholds, in practice it is expected that very few reporting entities will be able to lodge the short form local file.

Reporting entities not eligible to lodge the short form local file will need to lodge a full local file. This will include all the information required in the short form local file plus two additional parts. In the local file 'Part A' the entity will disclose information regarding all controlled transactions for the relevant income year, including the names of the Australian and foreign counterparties (and their countries of residence), category of transaction and the income and expenses associated with such transactions (including transactions of capital nature), the transfer pricing method (or capital asset

pricing method) relied upon, and finally, the transfer pricing documentation code. The local file 'Part B' will further extend the information from Part A and will require that the reporting entity provides copies of all intercompany agreements underpinning all material international intra-group transactions, as well as any advance pricing agreements in relation to the Australian transactions and GPFS.

The information required in the local file Part A is substantially similar (although with a much greater level of detail) to that required in the IDS Part A. Due to this relative overlap, the ATO authorises entities who voluntarily lodge the local file Part A together with their income tax returns to skip the majority of the questions of the IDS Part A. Where this is the case, the local file Part B must still be lodged by the relevant deadline.

Most importantly, SGE global management teams wishing to prepare their global CbC statements based on the OECD templates will need to keep in mind the peculiarities of the Australian local file and make sure it is prepared in accordance with the Australian model, otherwise they could be at risk of failing to comply with the Australian CbCR requirements and therefore subject to heavy penalties (PwC, 2016).

Master File: The master file will follow the OECD template and will provide information on the allocation of income between countries where the group operates, the activities of and taxes paid by the SGE parent entity and by the other members of the global group. Generally, the master file will be prepared by the foreign parent entity and the Australian entity will lodge a copy of it with the ATO together with the local file. However, if the GPE is not mandated to prepare the master file, then the local reporting entity will be required to prepare and submit the master file and the local file.

In some cases, a temporary one-year exemption (concessional treatment) may apply to reporting entities meeting the following criteria:

- The taxpayer has a foreign global parent entity; and
- Neither the global parent entity nor any other entity in the group is required to prepare a master file prior to the due date in Australia; and
- The reporting entity commits to providing the master file for the second reporting period.”

(PwC, 2017)

However, these cases are expected to be very limited, given that a significant number of OECD countries already have legislated CbCR obligations and in most cases, the deadlines recommended by the OECD are followed, just as they are in Australia.

Appendix 2: Outline of Recently Enacted Increased Penalties

Source: www.ato.gov.au

Administrative Penalties (False or misleading statements resulting in tax shortfall)	Culpable behaviour		Former base penalty (% of shortfall/penalty units)		Current base penalty (% of shortfall/penalty units)	
	Making a false or misleading statement		25%, 50%, 75%		50%, 100%, 150%	
	Making a statement that treats a law as applying in a way that was not reasonably arguable		25%		50%	
	Failing to provide a document as required		75%		150%	
Administrative Penalties (False or misleading statements not resulting in shortfall)	Intentional disregard of the law		60 penalty units (\$10,800)		120 penalty units (\$25,200)	
	Reckless behaviour		40 penalty units (\$7,200)		80 penalty units (\$16,800)	
	No reasonable care		20 penalty units (\$3,600)		40 penalty units (\$8,400)	
Failure to Lodge on Time (FTL)	Days late	<28	29>56	57>84	85>112	112+
	Current large entity penalties	\$900	\$1,800	\$2,700	\$3,600	\$4,500
	Large entity penalties (increased penalties)	\$1,050	\$2,100	\$3,150	\$4,200	\$5,250
	SGE penalties (increased penalties)	\$105,000	\$210,000	\$315,000	\$420,000	\$525,000

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