Why Investors and Multinationals Should Push The U.S. for Public CbC Reporting

by Ryan Gurule


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In this article, Gurule compares emerging financial transparency rules in Australia and the United States that would affect how U.S. multinationals publicly report tax and other operating information.

Canberra, Australia, is 15 hours ahead of Washington, D.C., and is moving even further ahead of Washington in providing greater transparency for investors and other stakeholders that use financial statements to understand the international operations of the world's largest multinational enterprises. Under rules set forth by the U.S. Securities and Exchange Commission and the independent body it relies on to create U.S. generally accepted accounting principles — the Financial Accounting Standards Board — investors, policymakers, academics, activists, and other stakeholders that use financial statements to allocate capital or craft global tax policy are underinformed by reporting that generally lumps together the totality of MNEs' offshore operations.

On October 25 the Australian Treasury formally introduced a proposal requiring large MNEs, including those headquartered outside Australia, to report public country-by-country tax and operating data.[1] These rules, if implemented (as is expected when the Australian Parliament reconvenes in February, given the makeup of the Australian Parliament), will require reporting for income years beginning in July 2023. The Australian proposal is expected to cover a variety of U.S. MNEs. This announcement comes on the heels of FASB[2] asking members of its Advisory Council to weigh in on potential improvements to the ways that U.S. companies disclose their income taxes in financial statements. If advanced, FASB's proposals would result in public MNEs disclosing information regarding income taxes paid for the jurisdictions in which the most tax is paid, as well as additional detail regarding how companies lower (or increase) their overall tax exposure in a "rate reconciliation table."[3]

This article briefly identifies key improvements to each of FASB's proposals that are necessary to best inform investors and other stakeholders about tax and other operating risks stemming from international practices of MNEs.

However, in light of Australia's efforts, as well as other international updates, the United States should instead require large public companies to engage in public CbC reporting in line with international best practices to best inform investors and other stakeholders of relevant risks. MNEs should also push for standardized, best-practices disclosure because doing so will improve information symmetry across jurisdictions and minimize global compliance costs in a world filled with a patchwork of standards.

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[1] *See* Treasurer of the Commonwealth of Australia, Budget Paper No. 2: Budget Measures 2022-23, at 17 (Oct. 25, 2022) ("Australian proposal").

[2] Financial Accounting Standards Advisory Council, Meeting Recap (Sept. 20, 2022).

[3] *See* FASB, FASAC Meeting Agenda (Sept. 20, 2022) ("FASB agenda").

However, it is possible, given FASB's U.S. GAAP standard-setting role, that it is reticent to advance public CbC reporting in full without some outside push. That is no problem for the SEC, which has clear statutory authority to require public CbC reporting for public filers. The SEC can and should work alongside FASB to see public CbC reporting through in the coming year via notice and comment rulemaking.

I. Background

A. Public CbC Reporting Origins

As the Financial Accountability and Corporate Transparency (FACT) Coalition recently noted in its report, "A Material Concern: The Investor Case for Public Country-by-Country Reporting," investors need an understanding of where revenues are generated, where taxable income is booked, and how business is being conducted in global jurisdictions to truly understand an investment's risks and opportunities.[4] This information would provide greater insight into real cash flow risks stemming from aggressive tax planning strategies, as well as geopolitical risks affecting supply chains, immobile assets, and access to potentially material markets.

Also, to create international policies, including tax policies, that work for all stakeholders, more symmetrical information is needed regarding the international operations of MNEs. MNEs are (or should be) increasingly recognizing public CbC reporting as an opportunity to better engage in these policymaking efforts.

Investors, policymakers, advocates, and other users of financial reports are largely in the dark on the ways that multinationals operate globally in response to tax policy. In the United States, public MNEs often only report their global income and accrued taxes in two buckets: domestic and international.[5] MNEs following SEC and U.S. GAAP rules typically present even less detailed information about where global revenues are earned.[6]

The lack of transparency on tax and other country-based practices reduces investors' ability to understand a firm's tax and operating risks that affect the bottom line and its governance mechanisms affecting those risks. For example, oversight of accounting and tax strategy is the province of not only the CFO and CEO, but also the board. It is an important element in evaluating board structure and leadership, as well as the board's oversight of a company's management team and its propensity to engage in risk-causing activities. For investors, this lack of insight increases the risk of modeling and valuation inaccuracies, potentially leading to inefficient capital allocation decisions — needlessly requiring guesswork when information is readily available. Creditors are also denied insights that can affect cash flows available to repay any outstanding amounts owed and the ability to evaluate risk of default. In turn, this could lead to greater volatility in the market, bond spreads, and other negative market outcomes.

Opacity regarding international operations also denies other users of financial statements, such as policymakers and the public, key data necessary to tackle some of the most important global challenges. These include climate change, a global pandemic, and the "race-to-the-bottom" competition for attracting investment. The latter of these challenges undermines the ability for governments to address the first two, creating incentives for MNEs to shift profits and erode the tax base of the nations in which they actually operate. These profit-shifting and base-erosion practices also politically entrench financial secrecy, and the corruption and other ills that come with it.

Over the long term, the failure for governments to appropriately address these

[4]FACT Coalition, "A Material Concern: The Investor Case for Public Country-by-Country Tax Reporting" (July 28, 2022) ("FACT investor report").

[5]*See, e.g.*, 17 C.F.R. section 210.4-08(h) (detailing tax disclosure requirements for public MNEs).

[6]Some filers, such as bank holding companies, may have some jurisdiction-based reporting requirements, as detailed in the FACT investor report, and others may include detail for different regions or markets (such as developing). *See* FACT investor report, *supra* note 4, at 13-14; *see also* 17 C.F.R. section 210.9-05. Reporting by regions — like Europe — hardly clarifies tax risks relating to transfer pricing practices between France and Luxembourg, for example, or clarifies risks relating to Russian operations (if classified as Europe in the applicable report). *See* Juliette Jabkhiro, "McDonald's Agrees to Pay $1.3 Bln to Settle French Tax Dispute," Reuters, June 16, 2022.

challenges may create unstable operating environments, hurting MNEs operating globally. This impact will ultimately harm MNE investors, creditors, and other stakeholders, and it helps to explain an eroding public faith in our tax systems and the democratic institutions they support.[7] This vicious spiral is in no one's interest, and we are watching it play out in real time.

In response to base erosion and profit shifting, as well as other deleterious tax practices, some global governments have worked together in recent years to better exchange tax information on MNEs' CbC operations under the OECD's BEPS action 13.[8] Under this action, the United States requires MNEs generating more than $850 million in global revenues to provide CbC reporting directly to the IRS.[9] However, the results of this information remain strictly in the hands of the IRS for its auditing purposes and those governments with whom the United States has a bilateral exchange agreement.[10] This leaves investors, policymakers, and other users of financial statements without the full picture, though they are able to access aggregate compilations of this data on a delayed basis.[11]

Limited access to this data has proved vexing in informing, creating, and implementing multilateral and unilateral solutions to BEPS practices by MNEs. For example, a lack of public information on a firm level has complicated an understanding of the global minimum corporate tax and reallocation of taxing rights created by the two-pillar[12] solution agreed to by 137 jurisdictions in 2021.[13] Public CbC reporting can help to address these information gaps for policymakers and other advocates that use financial statements, as well as help investors understand whether and how these conversations might affect capital allocation decisions.

MNEs should also recognize that greater transparency, not less, provides an opportunity to promote competition based on real operations and to demonstrate responsible engagement in markets. Concerns that public CbC reporting will reveal competitively sensitive information confuse competition based on real operations of MNEs with the sophisticated tax planning practices of tax advisers.[14] On the other hand, with greater transparency, MNEs can demonstrate more sustainable profits and good governance practices to their investors and other stakeholders. Shell, which reports under the Global Reporting Initiative (GRI) standard (discussed below), put it this way:

> When we first started considering the report, we thought through all the possible risks, downsides and unintended consequences. I can tell you now that in reality these concerns did not play out. In fact, being more transparent has strengthened trust in Shell, and it continues to strengthen our relationships with our customers, investors, policymakers and others.
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> So, I would encourage more companies to open their books and show their financial contributions to society. Because meeting society's expectations will earn them trust . . . and because more transparency can support the development of fair, stable and effective tax systems which are always important . . . but today perhaps more than ever.[15]

[7] *See* Pew Research Center, "Domestic Policy: Taxes, Environment, Health Care" (Dec. 17, 2019) ("Most Americans have doubts about the fairness of the federal tax system.").

[8] *See* OECD, "Action 13: Country-by-Country Reporting."

[9] Reg. section 1.6038-4.

[10] *See* U.S. Department of the Treasury, "Tax Information Exchange Agreements (TIEAs)" (last accessed Nov. 15, 2022).

[11] *See* IRS, "SOI Tax Stats — Country by Country Report" (last accessed Nov. 15, 2022); *see also* U.S. Bureau of Economic Analysis, U.S. Department of Commerce, "Activities of U.S. Multinational Enterprises (MNEs)" (last accessed Nov. 15, 2022) (providing applicable information regarding offshore operations of U.S. MNEs).

[12] *See, e.g.*, OECD, "Statement on a Two-Pillar Solution to Address the Tax Challenges Arising From the Digitalisation of the Economy" (Oct. 8, 2021).

[13] *See* Julie McCarthy, "A Bad Deal for Development," Brookings Global Working Paper No. 174, at 11 (May 2022).

[14] Similarly, the idea that public disclosure of supply chain information might somehow disclose the key to a competitive advantage in our globalized economy seems less likely to hurt MNEs (or investors and other stakeholders) than it does to affect a consulting industry that is dedicated to these questions.

[15] Alan McLean, Royal Dutch Shell plc Executive Vice President, Taxation and Controller, introductory remarks at the European Parliament FISC Committee Public Hearing on Tax Transparency (Sept. 9, 2021).

B. Public CbC Reporting Momentum

For these reasons, investors and stakeholders across the globe, working alongside forward-looking MNEs, have increasingly been pushing for public CbC reporting in line with international best practices. The gold standard for user-friendly public CbC reporting is the GRI standard. GRI 207-2019 represents intensive consultation from global investors, business leaders, academics, civil society members, policymakers, and other users of financial statements to create a user-friendly public CbC reporting framework.[16] However, because of the standard's voluntary nature, GRI reporting requirements are insufficient to yield symmetrical data necessary to reliably provide meaningful insights to investors and other users of financial statements or across companies and sectors.

In the United States, investor support encouraged the House of Representatives to pass the Disclosure of Tax Havens and Offshoring Act, part of the Corporate Governance Improvement and Investor Protection Act (H.R. 1187), in July 2021.[17] Investor support has also pushed FASB toward greater tax disaggregation and led to increased shareholder activism at the SEC in support of implementing public CbC reporting on a company-by-company basis for brand-name U.S. multinationals. Most recently, shareholders have urged Amazon, Microsoft, and Cisco Systems to implement public CbC reporting.[18] In support of the Amazon shareholder filing, investors with $3.6 trillion in assets under management wrote to the SEC, encouraging it to reject Amazon's efforts to squash the vote.[19] The SEC did and noted that the tax information sought wasn't ordinary course business that can be excluded from vote. Independent investors representing 21 percent of Amazon's outstanding shares voted for these efforts at Amazon's annual meeting on May 25, while 27 percent of Cisco's shareholders voted in favor of increased transparency measures on December 8, demonstrating an increasing familiarity and momentum for these issues among investors in a short time span.[20]

Meanwhile, the EU and Australia have advanced public CbC reporting requirements that will cover U.S. multinational corporations. Although the EU adopted only a partial public CbC reporting requirement, U.S. multinationals with sufficient EU operations will be required to report on EU jurisdictions and jurisdictions gray-listed and blacklisted by the EU beginning as early as 2024 (with the earliest reports coming in 2025).[21]

Australia, on the other hand, has proposed more extensive public CbC reporting requirements.[22] It is imperative that these requirements be finalized to incorporate full public CbC reporting disclosure and commentary in line with GRI best practices. Given its composition, the Australian Parliament is likely to adopt the requirements. These Australian reporting obligations are expected to cover U.S. and other foreign MNEs with established taxable contacts with Australia. As discussed in more detail below, the United States should act as a leader to avoid proliferation of differing reporting and disclosure requirements.

Access to greater disaggregated tax information can improve capital allocation, reduce volatility in the market, and promote more sustainable global economic growth to the benefit of all investor types and other stakeholders.[23] The FACT Coalition's analysis also shows that greater disaggregation of tax information cannot be considered in isolation. That is, it should occur alongside greater disaggregation of information on revenue, income (or loss), and other key operating metrics so that investors and other stakeholders can best understand the

[16] *See* GRI, "GRI 207: Tax" (2019).

[17] "66 Investors With $2.9 Trillion in Assets Under Management Show Support for the Disclosure of Tax Havens and Offshoring Act," FACT Coalition (May 17, 2021); "House Takes Historic Step in Advancing Corporate Tax Transparency," FACT Coalition (June 16, 2021).

[18] Nana Ama Sarfo, "Microsoft and Cisco Face Shareholder Pressure Over Public Disclosures," *Tax Notes Int'l*, July 4, 2022, p. 7.

[19] *See* Chris Boose, "Investors Score Huge Win at the SEC in the Fight for Greater Tax Transparency From Amazon," FACT Coalition blog, Apr. 7, 2022.

[20] "Amazon Investors Push Company on Global Tax Transparency," FACT Coalition, May 27, 2022; *see also* Cisco Systems Inc., SEC Form 8-K, at 2 (Dec. 8, 2022) (proposal 4). The Microsoft vote also occurred on December 13, but results had not yet been published when this article went to press.

[21] *See* KPMG, "Country-by-Country Reporting" (2022).

[22] *See* Australian proposal, *supra* note 1, at 17.

[23] *See, e.g.*, FACT investor report, *supra* note 4.

comparative risks facing an MNE and a tax system. These risks may stem from aggressive profit shifting. They may also involve risks relating to other geopolitical factors — such as exposure to Russia's invasion of Ukraine.

U.S. MNEs, increasingly facing a patchwork of disclosure obligations, should also recognize the tide of transparency and seek a clear U.S. framework for disclosing this information to promote competition based on operations and to minimize compliance costs. Hess Corp. and Newmont Corp. became the first U.S.-headquartered public filers to produce public CbC reports in line with GRI standards late this summer.[24] Some MNEs operating in the United States are now facing up to three different proposals for greater tax and operating information disaggregation — the EU partial public CbC reporting rules that are law, the more extensive Australian proposal that is likely to become law, and FASB's recent proposal.

Based on IRS reporting requirements and good governance principles, none of these different proposals should result in overly burdensome compliance costs. However, by requiring public CbC reporting in line with international best practices and coordinating with international partners, the United States can minimize reporting costs across jurisdictions for MNEs and provide a more useful framework for users of financial statements at the same time.

II. FASB Proposal Responses

FASB's proposals potentially revise the ways that companies: (1) disaggregate information regarding income taxes paid (or cash taxes) on a jurisdictional basis by top jurisdictions or some quantitative threshold ("cash tax proposal");[25] and (2) in the case of only public companies, provide additional detail regarding the difference between the statutory tax rate faced by and the effective tax rate paid by the filer in the rate reconciliation table (the "rate reconciliation proposal").

Problematically, FASB's cash tax proposal ignores the incidence of risk facing investors that arises out of multinational tax and operational practices. Comparing this data side-by-side with the rate reconciliation proposal, without additional information, does not necessarily clarify the nature of these risks. Further, while FASB's rate reconciliation proposal can represent an important step toward greater transparency relating to both domestic and international tax risks affecting an MNE, it ignores tax-related risks to investors resulting from international tax enforcement and reform. Requiring public CbC reporting in line with GRI standards in lieu of the cash tax proposal and maintaining the rate reconciliation proposal — at least for large filers already reporting confidential CbC tax information to the IRS — can address each of these challenges.

A. Cash Tax Proposal and Risk

FASB's cash tax proposal would require that MNEs disaggregate their income taxes paid by jurisdiction based on:

- top jurisdiction status (such as top five or top 10, or otherwise by income taxes paid); or
- some other quantitative threshold (such as 5 percent or 10 percent of the total amount of income taxes paid).[26]

MNEs are not necessarily required to publicly report their revenues or income on a jurisdictional basis, and FASB's proposal would seemingly not

[24] *See* Hess Corp., "Sustainable Tax Practices" (2022); Newmont Corp., "2021 Taxes and Royalties Contribution Report" (2022).

[25] At the time of drafting this article, FASB has agreed to advance the process under which these proposals would revise U.S. GAAP reporting requirements. However, a formal proposal is not expected until March 2023, at which time FASB is expected to seek public comment for a 75-day period. *See* Mark Maurer, "FASB Again Aims for More Disclosure on Taxes From U.S. Companies," *The Wall Street Journal*, Nov. 30, 2022. Accordingly, the author understands that these proposals may be subject to revision and clarification.

[26] *See* FASB agenda, *supra* note 3, at Attachment 2. Recent indications from FASB seem to indicate that any formal proposal will peg disclosure based on a particular jurisdiction comprising more than 5 percent of cash taxes paid. *See* Maurer, *supra* note 25.

change this.[27] FASB's cash tax proposal fails to recognize that an investor understanding of tax-related and other potential geopolitical risks is contingent not only on the incidence of paid taxes but also on where and how taxes are paid (or aggressively avoided) based on a comparison of the jurisdiction of an MNE's book revenues, income (or loss), tangible and human capital investment, and income taxes paid. FASB's proposal can be improved by requiring this information to be presented in a coordinated fashion or requiring MNEs to report public CbC information.

As the FACT Coalition detailed in its recent report,[28] aggressive international tax planning by large MNEs can create risk for investors, such as by increasing investor exposure to the impacts of tax enforcement or international tax reform efforts. MNEs create this risk by relocating highly mobile profits — hundreds of billions of dollars, based on the most recent numbers — to tax haven jurisdictions that have near-zero effective tax rates.[29] The more aggressive the tax planning for a multinational, the more increased the risks may be.

But FASB's cash tax proposal doesn't inform these risks. Consider the Coca-Cola Co., which according to a U.S. Tax Court ruling owes the IRS $3.3 billion in underpaid taxes and penalties because of transfer pricing activities from 2007 to 2009 that the court deemed to be inconsistent with applicable regulations.[30] Coca-Cola could end up owing as much as $13 billion in taxes if the IRS uses the same logic in analyzing later years of tax payments.[31] Public CbC reporting may have highlighted the nature, scope, and governance implications of the risks associated with these transfer pricing practices.

Consider, also, the following example.

A large U.S. multinational corporation generates $500 million in annual income from activities of a French subsidiary operating in France, a country with a corporate tax rate of 27.5 percent. For tax purposes, however, the U.S. multinational has located relevant intellectual property and some minimal operations to Bermuda (or to an entity with Bermuda tax residency) — a territory with an effectively 0 percent corporate tax rate. Under internal agreements, the French subsidiary pays the Bermuda entity $450 million as part of its other operating costs, such that the French subsidiary has only $50 million in taxable income (or a 10 percent profit margin). The U.S. multinational must pay French taxes on this $50 million ($13.75 million). The U.S. multinational pays no corporate taxes in Bermuda, and the multinational has a foreign effective tax rate of 2.75 percent.[32]

Under this example, would the FASB cash tax proposal provide investors a clearer picture of tax risks facing the MNE? Not really. Investors and other stakeholders would not see any information regarding where revenues are actually generated or where, and how aggressively, profits are being shifted. As a result, investors would continue to have limited insight into capital risks relating to potential tax enforcement or international tax reform risks. Based on total taxes paid or the number of jurisdictions profits are being shifted from, investors may or may not see that taxes are paid in France, and very little insight might be gleaned from this information. The investor would have no idea that huge amounts of profits

[27] As detailed above, large MNEs may be required to disclose this information to the IRS, making this simply a question of whether the information is publicly disclosed (not whether the information-gathering and reporting costs are incurred). *See* reg. section 1.6038-4 and *supra* text accompanying note 9. FASB does promulgate separate U.S. GAAP standards regarding the disclosure of revenue and income (loss), and under certain circumstances, this information may be reported with additional geographic detail. *See, e.g.*, FASB agenda, *supra* note 3, at "Segment Reporting" and "Disaggregation of Income Statement." However, investors and other users of financial statements seeking to better understand tax and geopolitical risks would be benefitted by this information being presented in a coordinated manner.

[28] *See* FACT investor report, *supra* note 4.

[29] *See* IRS, *supra* note 1; *see also* Steve Wamhoff, "Unfinished Tax Reform: Corporate Minimum Taxes," Institute on Taxation and Economic Policy (Oct. 4, 2022).

[30] *See* Richard Rubin, "Coca-Cola Improperly Shifted Profits Abroad, Tax Court Rules," *The Wall Street Journal*, Nov. 19, 2020.

[31] *See* The Coca-Cola Co., "Annual Report on Form 10-K for the Year Ended December 31, 2021," at 90-92 (2022) ("Note 11: Commitments and Contingencies").

[32] Although a U.S. multinational may be responsible for U.S. taxes because of this arrangement — such as the global intangible low-taxed income tax or subpart F taxes (with either poor or very purposeful planning) — these taxes would likely be deemed cash taxes paid to the United States under the cash tax proposal. These taxes would therefore not clearly identify the abuse of any tax haven at the expense of any particular foreign operations.

are being shifted to Bermuda *because no, or little, taxes are paid in Bermuda, which is the point of a tax haven*.[33]

Investors would also remain in the dark regarding other operational risks for where revenues are actually generated and where profits are booked. Mathematically, it would be impossible for investors to accurately back out information regarding real operations in France or other countries by only using income taxes paid, without also knowing information regarding revenues or income (including information regarding interparty revenues that reduce marginal returns for high-tax operations).[34] In the example, an investor could assume that the multinational was making anywhere from $50 million to $500 million, or significantly more, in French revenues — resulting in very different exposure to the French market (and increasingly aggressive French tax authorities).[35] Under FASB's cash tax proposal, investors would be forced to make similar assumptions about the nature and degree of tax and geographic operating risks, as well as governance practices, as they might make today — potentially perpetuating increased market volatility or inefficient capital allocation.

The example isn't too far off from reality. Consider that Microsoft — facing a shareholder proposal for public CbC reporting in line with GRI practices[36] — writes in its most recent annual report that in "fiscal years 2022, 2021, and 2020, our foreign regional operating centers in Ireland and Puerto Rico, which are taxed at rates lower than the U.S. rate, generated 71 percent, 82 percent, and 86 percent of our foreign income before tax."[37] In earlier years, Microsoft investors may have seen Singapore on that list of tax havens, or entirely missed that when Microsoft said Ireland, sometimes it really may have meant Bermuda for tax purposes.[38] Under the FASB proposal, investors might be left scratching their heads while trying to compare statements regarding where profits are located and where cash taxes are paid without additional information.

Instead, a more meaningful approach for investors would be to require reporting on income taxes paid to each of the jurisdictions in which a minimum threshold amount of revenue and income are booked (say, $1 million, adjusted for inflation). This information should include for each applicable jurisdiction:

- information regarding intraparty and third-party revenues;[39]
- information regarding net income (or loss), with adjustments to exclude double-counted items; and
- information regarding cash taxes paid.[40]

[33]Similarly, the investor might have no real concept of how much revenue is generated in France, and thus how much exposure the entity might face regarding French geopolitical risks. For France, this risk might include the ongoing imposition of its digital services tax in light of delays implementing the two-pillar tax solution negotiated at the OECD. *See, e.g.*, "US Compromises With the UK, France, Italy, Spain and Austria on Digital Services Taxes and Trade Actions," PwC Tax Policy Alert (Oct. 25, 2021). This calculus might be entirely different if the example replaced French operations with Chinese or Russian operations, as highlighted by the FACT Coalition in its recent report making the investor case for public CbC reporting. *See* FACT investor report, *supra* note 4.

[34]Consider that assuming a 6 percent profit margin for French operations would indicate a very different exposure to French markets, for example. Without further information, investors would have no other choice but to continue making random assumptions that may increase volatility and improperly affect capital allocation decisions.

[35]While the amount of income taxes actually paid may fluctuate for a variety of reasons, this article accepts the FASB proposal's reliance solely on income taxes paid as a reasonable indicator of firm tax liability across an appropriate time horizon. The GRI standard would also include information on income taxes accrued and allow for an explanation for discrepancies between income tax accrual and the amount of taxes that would be owed if the statutory rate were applied. *See* GRI, *supra* note 16, at section 207-4(b)(x).

[36]Sarfo, *supra* note 18 and accompanying text. At the time of drafting this article, the Microsoft annual meeting had not yet occurred.

[37]*See* Microsoft Corp., "Form 10-K for the Fiscal Year Ended June 30, 2022," at 85 (2022).

[38]*See* Microsoft Corp., "Form 10-K for the Fiscal Year Ended June 30, 2020," at 71; *see also* Rupert Neate, "Microsoft's Irish Subsidiary Posted £220bn Profit in Single Year," *The Guardian*, June 3, 2021 (distinguishing between corporate and tax residency for tax purposes in Ireland).

[39]For more information on these distinctions, see GRI, *supra* note 16, at 12 ("Guidance for Disclosures 207-4-b-iv and 207-4-b-v"). Disaggregating revenue by intraparty transactions between the relevant jurisdictions and other jurisdictions (and identifying and correcting for dividend income) can help to ensure local revenues are not double counted and that the true operating activities in a jurisdiction are better understood. Currently, U.S. GAAP accounting may aggregate many intraparty transactions for purposes of reporting, and the GAAP's focus on these issues tends to be more concerned with ensuring fair dealing. *See* FASB ASC 850. However, because this information may clearly demonstrate the incidence of tax risk, guidance should be promulgated to more clearly identify and disclose intraparty transactions between jurisdictions in accordance with the recommendations in this article.

[40]This information might similarly be helpful on a state-by-state basis, as FASB highlights. *See* FASB, *supra* note 26.

Alternatively, public CbC reporting in line with international best practices would also include this information, and for large MNEs, would require minimal additional compliance costs compared with current IRS reporting requirements.

B. The Rate Table Proposal

FASB's rate reconciliation proposal would dramatically improve the rate reconciliation table in public filings. By way of background, public U.S. filers taxed as corporations use a rate reconciliation table to demonstrate key categories of activity that increase or decrease their effective tax rates, requiring filers to "reconcile" from the tax that they would have paid if taxes applied at the statutory U.S. corporate tax rate of 21 percent to their actual effective tax rate for the reporting period.[41] The FASB rate reconciliation proposal would require greater disaggregation in the rate reconciliation table (1) for items having a greater quantitative effect than an established threshold or (2) on a list of specific categories that would be required by FASB.

FASB's proposed quantitative threshold approach would require disclosure of any item having an effect of greater than 5 percent (or some other threshold, subject to comment) of total tax if the statutory tax rate applied without adjustment to pretax income.[42] FASB's proposed specific category approach would, among other categories simplified here, require additional detail regarding: (1) foreign tax rate differential (by jurisdiction, and excluding the effect of foreign tax credits); (2) state and local taxes; (3) the enactment of new tax laws (perhaps like the new corporate alternative minimum tax passed in the Inflation Reduction Act); (4) the effect of cross-border tax laws (such as differentials related to the global intangible low-taxed income regime); (5) tax credits (including FTCs); (6) valuation allowances; (7) nontaxable or nondeductible items; (8) tax position changes; and (9) other adjustments.[43]

[41] For foreign headquartered filers, a different statutory rate might apply (such as the statutory corporate rate where the MNE is headquartered).

[42] *See* FASB, *supra* note 26.

[43] *See id.*

This discussion will evaluate the impact of this proposal in light of information that FASB seems to be forgo were it to implement public CbC reporting.[44] This subsection of information might relate to FASB's proposed information on jurisdiction-by-jurisdiction foreign tax differential; new tax laws; the effect of cross-border provisions; and tax credit provisions, as applicable.

1. Missing Data, Missing Risks

Theoretically, the rate reconciliation proposal may provide users of financial statements with information regarding the nature and scale of tax risks stemming from profit shifting. Read alongside information regarding income taxes paid as a result of the cash tax proposal, a jurisdiction-by-jurisdiction foreign tax differential might identify for users that MNEs are shifting large amounts of profits, potentially indicating aggressive tax strategies that may be subject to greater tax enforcement or reform risks. Nonetheless, exposure to some foreign jurisdictions may remain difficult to determine without minimal thresholds and disclosure regarding taxable income, effective tax rates, or revenues on a jurisdiction-by-jurisdiction basis.

Returning to the example, users of financial statements might see the following regarding the MNE's $500 million in profits using something similar to FASB's rate reconciliation proposal template[45] (which would otherwise be taxed in the United States at 21 percent for a total tax of $105 million) (see table).

Beneficially, the information provided under FASB's reconciliation rate proposal will make it apparent that the MNE is booking a large portion of profits in Bermuda in a way that is substantially lowering its effective tax rate. This may make investors aware that some tax enforcement and tax reform risks may apply for this MNE. However, it remains facially unclear from looking

[44] This discussion only comments on those provisions of the rate reconciliation proposal that would provide insight into multinational tax and operating strategies in light of international tax policies or geopolitical risks, because this disaggregation proposal has been compared to public CbC reporting. However, transparency concerning other tax policies is most welcome and merited in light of the increasing amount of policy that occurs — at least in the United States — through the tax code.

[45] *See* FASB, *supra* note 26.

solely at this table how much income or revenue and what types of revenue (that is, intraparty or third-party) are actually being booked in Bermuda.

In simple cases, one might be able to back out income for the countries that have an identified impact on effective tax rate in the rate reconciliation proposal if we can make key assumptions regarding the applicable tax rate in the jurisdiction. For example, if we assume zero (or close to zero) taxes are paid in Bermuda because the corporate tax rate is effectively zero percent, then we can back out income in France and Bermuda from the information in the table by knowing the overall income.[46]

Further, if filers are required to disclose additional information for those jurisdictions that have a reportable impact on effective tax rate — such as impact on deferred tax assets and deferred tax liabilities, then investors and other users might be able to extrapolate income reported in a given jurisdiction with reasonable accuracy by simply knowing the statutory rate of that jurisdiction (versus effective tax rate).[47] Without this additional information, or additional insight into the effective tax rate that applies in each jurisdiction, investors might still be left with questions regarding the nature and scope of multinational tax strategies given that a taxpayer's effective tax rate in any given jurisdiction might vary wildly from the statutory rate in the jurisdiction. An additional complication may arise, even with additional information regarding deferred tax assets and liabilities, if a jurisdiction has multiple applicable tax rates (for example, because of a patent box). In this case, investors would either need additional disclosure regarding the effects of such foreign regimes, or would still need to make key assumptions about the nature of profits being shifted.

Rate Reconciliation Proposal Example

	Amount (in millions of dollars)	Percent
Net income	$500	—
U.S. statutory	$105	21
France[a]	$3.25	0.65
Bermuda[b]	($94.50)	(18.9)
Total	$13.75	2.75

[a]This assumes that FASB would provide guidance for weighing the impact of each jurisdiction by the comparative income associated with that jurisdiction. This also assumes that the number being disclosed is the difference between what would have been paid using the statutory rate versus what was paid in the applicable jurisdiction. These assumptions could be varied based on any final FASB proposal. FASB has indicated that more information for each jurisdiction may be disclosed, such as impact regarding deferred tax liability/assets. This would be very helpful, as discussed below; illustrative examples from FASB regarding the rate reconciliation table proposal would be very useful in any formal proposal.

[b]Under the rate reconciliation proposal, an additional line for GILTI (given that offshore profits are taxed at less than 50 percent of the domestic rate) or subpart F income, if applicable, might appear or be blended into the impact of the respective countries based on additional guidance. Included in these numbers or separately, the impact of FTCs might be disclosed. For simplicity, these items are not included here.

Finally, consider that given France's limited impact on tax paid for the MNE in the example in light of regimes like GILTI, France may not be included in the rate reconciliation table based on FASB's proposal. Problematically, if profits stemming from activity in many different jurisdictions were moved to Bermuda, the cumulative impact of these shifts may appear large in Bermuda, without any corresponding information to reveal from where profits are being shifted. This is particularly true given that CbC revenue information is also still missing. Without the revisions proposed in this article, information from both the cash tax proposal and the rate reconciliation proposal would still fail to provide adequate insight into where real MNE operations are occurring and to what extent the disconnect, if any, between these operations and the MNE's tax

[46]In this case, with a zero percent income tax rate in Bermuda, the taxpayer is lowering its effective tax rate by $94.5 million, allowing us to divide $94.5 million by 21 percent to determine that $450 million in profits must be taxed at zero percent in Bermuda. This might allow an investor to better understand how a 15 percent effective corporate minimum tax rate might impact the MNEs cash flows.

[47]Although it is not clear from investor advisory committee materials whether this additional information will be required, this information would be particularly useful if a jurisdiction has only a single corporate tax rate (that is, not distinct rate for intellectual property, or similar).

strategy may create risks related to tax enforcement or tax reform.[48]

a. International Tax Enforcement Risks

It is not only the U.S. government that has a vested interest in making sure that large MNEs play by international tax rules. In the example above, France has a big interest in making sure that the MNE is not being overly aggressive in its transfer pricing strategies to move profits ultimately generated by French revenues away from France.[49] McDonald's $1.3 billion settlement with French tax authorities this summer — relating to its Luxembourg-centered transfer pricing practices in the EU — serves as a reminder of this fact for international investors.[50]

By reconciling only to the U.S. statutory rate, the rate reconciliation proposal largely ignores foreign enforcement risks. In the example, profit shifting to Bermuda would seem even more egregious compared with the French statutory rate. If a different country with a slightly lower rate than the United States were the subject of the MNE's operations, the potential foreign tax enforcement risk would similarly be obscured. If the MNE generated its revenue from operations in the United Kingdom — where there is a 19 percent corporate tax rate — the rate reconciliation table would also make it appear as though the U.K. operations were lowering the U.S. effective tax rate and might make it seem like the United Kingdom would have a lesser tax enforcement interest in profits shifted away from there.

Full public CbC reporting or the suggested improvements relating to the cash tax proposal resolve these ambiguities by allowing users to see where large MNEs are booking revenues and where they are moving profits. This is true even when the effective tax rate impact of higher-tax jurisdictions is minimized, as is the intent of corporate tax planning. As a result, investors and other financial statement users have much better insight into foreign tax enforcement risks, as well as domestic tax enforcement risks when additional information regarding revenue and income, as well as other key operational metrics, are provided alongside the rate reconciliation proposal.

b. International Tax Reform Risks

One obvious reason for greater disaggregation of tax information has to do with the international momentum to work unilaterally or multilaterally to better tax MNEs in light of a digitalized economy. For example, we know from aggregated CbC information produced by the IRS that U.S. MNEs will likely face substantial increases in taxation of foreign profits if pillar 2 of the OECD agreement discussed above, creating a minimum corporate tax rate equal to an effective rate of 15 percent applied on a CbC basis, is implemented in key jurisdictions. However, investors may be keen to know exactly which MNEs may be affected by such a reform. The rate reconciliation proposal provided by FASB may prove helpful in this regard as it would demonstrate how MNEs are locating profits in specific jurisdictions to lower their overall effective tax rate. Public CbC reporting would certainly also address this information gap in a more detailed way, because it would clearly show effective tax rates in each jurisdiction (versus just reconciling back to the U.S. rate).[51]

However, the lack of information about where revenue is generated is a significant drawback of both the cash tax proposal and the rate reconciliation proposal. As a simple example, consider that digital economy and aggressive tax planning strategies may frustrate countries' ability to effectively tax MNEs, forcing countries to explore the use of digital services taxes and other gross receipts taxes. Without additional CbC revenue information, investors and other stakeholders will continue to have very little insight into how current or threatened gross

[48]If you think about the same issues and substitute China and the British Virgin Islands for France and Bermuda, then, in addition to tax, country risk considerations also relevant to investors are implicated.

[49]Using the facts of the example, one might argue convincingly that these profits are, in fact, generated by activity related to the intangible property and rightly accrue to wherever activities relating to the creation of the intangible property accrued. Likely that is still not whatever tax haven is chosen to host the IP for strategic tax purposes. This is not the subject of this article, however.

[50]Jabkhiro, *supra* note 6; *see also* William Hoke, "McDonald's to Pay France €1.245 Billion to Settle Tax Dispute," *Tax Notes Today Int'l*, June 16, 2022.

[51]For a more fulsome discussion of these issues, see FACT investor report, *supra* note 4.

receipts taxes might affect the bottom line for MNEs operating in applicable jurisdictions.

It is also no secret that the increase in unilateral gross receipts taxes helped drive the United States and other countries to the multilateral negotiation table to hash out the two-pillar framework.[52] Pillar 1 of the framework represents a fundamental shift to the way that corporations have been taxed for the last 100 years. By reallocating limited taxing rights to market jurisdictions, pillar 1 (tepidly) addresses the ability of MNEs to essentially choose where profits are booked for tax purposes. Without more information regarding where MNEs' revenues are booked, investors, policymakers, and advocates alike remain slightly in limbo in understanding the potential ramifications of pillar 1.

And what happens if pillar 1 fails? DSTs and other unilateral gross receipt taxes will certainly not go away. Regardless, more detailed public CbC information regarding where MNE revenues are generated is needed, and neither the cash tax proposal nor the rate reconciliation proposal can currently address this need.

2. Geopolitical Considerations

Besides informing tax risks, public CbC reporting also gives investors and other users of financial statements greater insight into geopolitical risks that are otherwise missing in financial statements. By providing detailed CbC revenue information, public CbC reporting also informs investors and other stakeholders where real third-party revenue and supply chain exposure exists for MNEs. The FACT Coalition's recent report highlights how reporting guidelines made it nearly impossible for investors to understand their exposure to Russian and Ukrainian operations, for example, before Russia's invasion in February.[53] Improving the cash tax proposal as suggested in this article (or adopting public CbC reporting) can ensure that investors and other stakeholders have more insight into these material risks.

3. Additional Considerations

As a baseline, FASB will need to issue detailed technical guidance regardless of the approach it takes on the rate reconciliation proposal. It has already begun this task by identifying the complicated ways that U.S. international tax policy intersects with strategic MNE tax planning (for example, by separately identifying the impacts of FTCs and cross-border tax laws from a foreign tax rate differential). The FACT Coalition previously flagged consideration of these intersections in its report making the investors' case for public CbC reporting.[54] In light of these technical considerations, the rate reconciliation proposal should not slow down other efforts to advance the cash tax proposal, as revised by suggestions in this article (or public CbC reporting implementation).

In all cases, FASB will need to ensure that MNEs are making clear, consistent, and comparable disclosures that identify the cash flow implications of distinct tax policies in a way that avoids selective or misleading disclosure. MNEs should not be able to combine the effects of multiple jurisdictions or offsetting tax policies to create selective or misleading disclosure. If, and to the extent, a quantitative (or top-jurisdiction) approach is taken, a low threshold that would provide a more complete picture of international operations yields far more benefits to investors and other financial statement users than the marginal cost savings to MNEs, if any, of streamlined reporting.[55] A narrative description explaining the rate reconciliation table may also be merited, consistent with public CbC reporting best practices.

III. The Need for SEC and FASB Action

Investors and other users of financial statements will welcome prompt FASB action on these transparency proposals, revised as suggested in this discussion. Information provided by these proposals, as revised, would

[52] *See* Alexander W. Koff and Friedemann Thomma, "Digital Service Tax Update: OECD Talks Continue Amid U.S. DST Investigations," Venable LLP (Feb. 9, 2021).

[53] *See* FACT investor report, *supra* note 4.

[54] *Id.*

[55] Assuming proper internal governance controls are put into place to determine which jurisdictions are reported, it seems unlikely that reporting costs would materially increase simply as a result of having to report specific jurisdictions. Again, for large MNEs, this information is already at hand. *See* reg. section 1.6038-4 and *supra* text accompanying note 9.

improve capital allocation decisions, reduce market volatility, and improve MNE and international governance. Yet, with Australia's recent actions to implement public CbC reporting in a way that is likely to require full GRI-consistent disclosure from many U.S. MNEs when finalized, it would be better policy to require U.S. MNEs (or at least large MNEs) to produce public CbC reporting in line with GRI requirements in lieu of FASB's cash tax proposal. To fast-track public CbC reporting requirements to align with Australian reporting requirements and promote information symmetry, the SEC should work alongside FASB, take matters into its own hands, and pursue notice and comment rulemaking.

Australia's public CbC reporting proposal is broad enough to apply to any multinational with ties to Australia, regardless of where it is headquartered, and this scope will likely stick. This will likely include many U.S. MNEs, and it is currently proposed to begin requiring reporting for periods beginning July 2023.[56] Meanwhile, U.S. MNEs operating in the EU may also need to begin filing limited public CbC reports with the EU shortly thereafter.[57] As discussed above, this burden will be minimized because these U.S. MNEs already report this data to the IRS under rules meant to implement the OECD's BEPS action 13. For these MNEs — along with any other U.S. MNE[58] with annual revenues exceeding $850 million — there will be minimal additional burden.

With competing standards evolving across jurisdictions, the United States can minimize MNE reporting burdens by implementing its own gold standard in public CbC reporting. If the United States fails to do so, then compliance costs for U.S. MNEs could increase because of having to parse between different reporting practices in varying jurisdictions — whether in Australia or the EU. To the extent that the same information may be covered by the cash tax proposal and portions of public CbC reporting requirements, for example, it would be more efficient to have consistent reporting obligations across jurisdictions.

Given the global appeal of public CbC reporting and IRS reporting requirements, it would be most efficient to simply require full public CbC reporting in line with international best practices in lieu of partial proposals, like the cash tax proposal or the EU's limited public CbC reporting rules. U.S. MNEs should consider joining Hess Corp. and Newmont Corp. in embracing public CbC reporting in line with GRI standards, as well as the opportunity this might create to highlight for investors that their competitive advantage is from their products and services — not where they are moving paper profits.

FASB may be concerned that full public CbC reporting may include references to non-GAAP metrics. As an independent standard-setting body for U.S. GAAP, FASB is justified in avoiding requiring disclosure of non-GAAP metrics. For example, although employee head count by jurisdiction may be helpful to understanding global MNE operations, FASB may seek to avoid defining who constitutes an employee. Rather than ditching public CbC reporting that could otherwise minimize information asymmetries and compliance costs because it views some of the details as non-GAAP, FASB should identify those details and proceed without them, passing the torch back to the SEC to define the specifics.[59]

The SEC is well positioned to finish the job and require public CbC reporting for all large U.S. MNEs in line with the Australian approach without any additional action by Congress. The SEC already has clear authority to determine how filers present accounting information, as well as

[56] Australian proposal, *supra* note 1, at 17.

[57] "Amazon Investors Push Company on Global Tax Transparency," *supra* note 20 and accompanying text.

[58] The previous administration exempted some "national defense" businesses from this requirement if "more than 50 percent of the U.S. MNE group's annual revenue, as determined in accordance with U.S. generally accepted accounting principles, in the preceding reporting period is attributable to contracts with the Department of Defense or other U.S. government intelligence or security agencies." *See* Notice 2008-31, 2008-11 IRB 592. Assumedly, the justification for this exemption is to protect the confidentiality of supply lines for the nation's defense contractors; however, this justification should not protect the disclosure of profit-shifting practices unrelated to actual operations. FASB's rate reconciliation table revisions would help to bring transparency to these companies without necessarily compromising the confidentiality of supply lines.

[59] These instances should not be confused with areas in which increased GAAP guidance may be merited (such as to more clearly delineate what might constitute intraparty and third-party revenues and income on a CbC basis, in each case without "double-counting"). *See supra* note 6 and accompanying text.

human capital information.[60] The SEC has also routinely indicated that it is committed to reducing information asymmetries between actors and across markets to help investors and other users of financial statements better understand internal governance standards for filers, more efficiently allocate capital, and minimize market volatility.[61]

Whether as a result of Australia's new public CbC reporting rules, IRS reporting requirements, other mandatory or voluntary disclosure rules, or the strategic nature of tax planning, MNEs should be creating the internal governance control mechanisms needed to produce public CbC reporting information. Investors and other stakeholders should not be kept in the dark on this information, and uniform public CbC reporting rules should require consistent, comparable information in the United States.

The time is right for the SEC to begin a rulemaking process to require full public CbC reporting disclosures consistent with GRI principles for all large MNEs subject to SEC oversight. These efforts should occur alongside FASB's proposals and preempt the cash tax proposal for applicable filers.

IV. Conclusion

FASB should be commended for taking a concrete step toward greater financial transparency that can highlight tax-related and other risks for investors and other users of financial statements. However, parts of its proposal could be improved. FASB should continue to carefully consider requiring large public companies to engage in public CbC reporting in line with standards put forward by the GRI to best inform investors and other stakeholders. This has many advantages, including to better inform investors on real tax and operations risks for large MNEs; improve international tax policy conversations between policymakers, the business community, and other stakeholders; and minimize global compliance costs for filers that already generate this data for IRS filing purposes and are increasingly facing a patchwork of public disclosure regimes. The SEC can and should work alongside FASB to see public CbC reporting through in the coming year. ■

[60] *See* 15 U.S.C. sections 78(l)(b)(1)(A), (J), (K), (L), and 78(m)(a)(1).

[61] *See* Gary Gensler, Chair, SEC, Speech at the Annual Conference on Financial Market Regulation: A Century With a Gold Standard (May 6, 2022) (addressing, among other topics, the benefits of transparency in reducing asymmetric information in markets).