Multinational tax transparency legislation

Disclosure of tax residence of subsidiaries in the financial report

Mandatory for 30 June 2024 annual reporting periods

At a glance

On the 27th of March 2024, the Federal Government passed the *Treasury Laws Amendment (Making Multinationals Pay Their Fair Share – Integrity and Transparency) Bill 2023*. The legislation amends the *Corporations Act 2001* to require Australian public companies to disclose information (including place of incorporation and tax residency) about themselves and their subsidiaries in their annual financial reports by way of a 'consolidated entity disclosure statement' (CEDS or statement).

The amendments were made as part of the Government's commitment to protect the integrity of the Australian tax system and improve tax transparency. The legislation also includes significant changes to the existing thin capitalisation tax rules which apply to certain foreign controlled or outbound multinational groups. See our Tax Alert *Australia's new thin capitalisation regime* for further information about those changes and their potential impact on taxable income.

The legislation will apply for the first time for financial years ending 30 June 2024. Companies should begin to consider what the new reporting disclosures mean and how the necessary information will be gathered. Some of the required information may not be readily available, in particular in relation to the tax residency status for each subsidiary of a large global group. Tax specialists may also be needed where the tax residency of an entity is not immediately apparent, or an entity is operating in multiple locations.

This publication provides our current views on a number of questions in relation to the legislation and how it may be interpreted and applied. It was updated on 18 September to add further guidance on the disclosure of the tax residency of trusts and to explain why we recommend including a basis of preparation.

Which entities are required to comply with the new legislation?

The new requirement applies to all public companies that are required to prepare consolidated financial statements under accounting standards, regardless of size and whether or not they are listed. However, it does not apply to proprietary limited companies, trusts, registered schemes, registrable superannuation entities or public companies that report under the *Australian Charities and Not-for-profits Commission Act 2012*.

pwc

What information is required to be included in the Consolidated Entity Disclosure Statement?

The CEDS is a new component or section of the annual financial report. That is, the annual financial report of a public company now comprises the financial statements, notes to the financial statements, the CEDS and the directors' declaration. The CEDS will be required to set out the following information for each entity (parent and subsidiaries) in the consolidated financial statements at the end of the financial year:

- The entity's name
- Whether
  - The entity was a body corporate, partnership or trust
  - The entity was a trustee of a trust, partner in a partnership or a participant in a joint venture where the trust, partnership and joint venture are consolidated
- If the entity is a body corporate
  - The place of incorporation
  - The percentage of the entity's issued share capital that was held by the public company at the end of the financial year
- Whether, at the end of the financial year
  - The entity was an Australian or foreign tax resident
  - If the entity was a foreign resident, a list of each foreign jurisdiction in which the entity was a tax resident

For illustrative disclosures, refer to our *Value Accounts Annual Financial Reporting 2023* publication (page 263).

Should the CEDS include a 'basis of preparation'?

The legislation does not require the inclusion of a basis of preparation for the CEDS. However, because of the judgement involved in determining the tax residency of certain entities, we recommend explaining the basis on which this information has been determined. This would be the case in particular if there was significant judgement involved in determining tax residency status. To see what this might look like, refer to our *Value Accounts Annual Financial Reporting 2023* publication (page 263)

Do public companies that are not required to prepare consolidated accounts need to do anything as a result of the legislation?

Yes. If a public company is not required to prepare consolidated financial statements (for example, because it meets an exception in AASB 10 Consolidated Financial Statements (AASB 10), it is still required to prepare a separate CEDS. The legislation requires the CEDS to include a statement that the company is not required to prepare consolidated financial statements. For illustrative disclosures, refer to our Value Accounts Annual Financial Reporting 2023 publication (page 265).

What is the impact on the directors' declaration?

The directors will have to confirm in their directors' declaration that the information disclosed in the CEDS is 'true and correct'. CEOs and CFOs of listed entities have to include the same statement in their declaration to the directors. This is different to the 'true and fair' declaration that applies to the other parts of the financial report. While 'true and correct' is not defined in the legislation, the explanatory memorandum states that the confirmation is meant to ensure that the disclosures in the CEDS are complete and accurate.

Companies will therefore need to establish a governance structure as part of their annual financial reporting obligations to provide directors with the necessary information to declare that the CEDS is true and correct.

The directors' declaration must include this confirmation regardless of whether the entity is disclosing a table with information about all of their subsidiaries, or whether the CEDS is simply a statement that says that the requirements do not apply to the entity (as per the previous question).

Are the auditors required to audit the CEDS?

Given the CEDS will form part of the annual financial report, it will need to be audited. Auditors will need to provide reasonable assurance over the information in the statement.

Are there any new disclosure requirements for interim reporting periods?

No. The new requirements apply only to annual reporting periods.

Is any information required to be disclosed with respect to comparative periods?

No. The information is only required to be disclosed based upon the entities in the consolidated group at the end of the financial year. There is no requirement to disclose the same information for the comparative period.

Can the CEDS be included in the notes to the financial statements and integrated with the current list of subsidiaries as required by AASB 12 *Disclosure of Interests in Other Entities* (AASB 12)?

No. Because the directors must make a 'true and correct' declaration over the CEDS, as opposed to 'true and fair', it is important that the CEDS can be clearly distinguished from other information in the financial report. The legislation lists the CEDS as a new component of the financial report that is separate from the notes. As such, we would generally expect that the statement is included as a separate section after the notes. ASIC has confirmed in *Information Sheet 284* that the CEDS cannot be combined with the note on controlled entities that is required by accounting standards.

If a public company is not allowed to prepare consolidated financial statements because it is an investment entity and is required to measure all of its interests at fair value through profit and loss, does it still need to provide the information in the CEDS for its unconsolidated subsidiaries?

No. A parent entity only needs to provide the detailed information about each entity if the accounting standards require the parent to prepare consolidated financial statements. Therefore, if an entity does not consolidate any subsidiaries because it is an investment entity under AASB 10, it will only need to state that section 295(3A) does not apply to it.

For illustrative disclosures, refer to our *Value Accounts Annual Financial Reporting 2023* publication (page 265).

Does information in the CEDS need to be provided for investments that are accounted for as equity accounted associates and joint ventures or other financial investments?

No. The reference in the legislation to disclosures is regarding entities that are part of the consolidated group which we consider refers to consolidated subsidiaries and the parent entity. There is no requirement to provide information on investments in entities that are not consolidated. The legislation requires indication of whether any consolidated subsidiary in the group was a trustee of a trust, partner in a partnership or an investor/participant in a joint venture – in the case where the trust, partnership or joint venture are consolidated.

Does the CEDS need to include information on all entities in the group or is it limited to only those entities that are direct subsidiaries of the parent entity of the group?

The legislation does not restrict the disclosures to only direct subsidiaries of the parent. As such, all subsidiaries in the consolidated group must be included in the statement, as well as the parent entity.

Can immaterial subsidiaries and/or dormant subsidiaries be excluded?

No. ASIC has confirmed in Information Sheet 284 that materiality does not apply to the CEDS, because it is a separate legal requirement under the Corporations Act 2001. This means that all controlled entities must be included in the CEDS, regardless of whether they would otherwise be excluded from consolidation and disclosures because of materiality.

How is the tax residency of subsidiaries determined?

The legislation requires companies to firstly disclose whether each entity is an Australian tax resident within the meaning of the *Income Tax Assessment Act 1997*. Foreign incorporated companies can still be considered to be a tax resident of Australia if their central management and control is in Australia. This determination is not always straightforward under the Australian tax legislation and associated guidance from the Australian Taxation Office.

Where the entity is not an Australian tax resident but is a foreign tax resident, each foreign country in which the entity is a tax resident is required to be disclosed. For entities operating in foreign jurisdictions, reference will need to be made to the relevant foreign tax laws.

Treasury's media release confirms that entities that determine tax residency in good faith and in accordance with the Commissioner of Taxation's *public guidance*, may declare that the tax residency status of a subsidiary is true and correct for the purposes of CEDS. It is important to note that the ATO's public guidance on corporate residency refers to both a practical compliance guideline and a tax ruling which outlines the Commissioner's interpretation of the relevant law.

What should be disclosed as tax residency for consolidated trusts?

Given the absence of a specific residency test applicable to flow-through trusts in the context of the CEDS requirements, groups will need to determine what useful and appropriate disclosure should be included with respect to their trusts. Some of the approaches we have observed include:

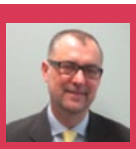
a) Whether a trust is an Australian resident or foreign resident within the meaning of the ITAA 1997 is disclosed as 'N/A' on the basis there are no specific residency tests applicable to trusts.
b) A trust is disclosed as an Australian resident on the basis that it has an Australian resident trustee.
c) A trust is disclosed as an Australian resident on the basis that it is flow-through for tax purposes, but has Australian resident unitholders.
d) A trust is disclosed as an Australian resident on the basis that it is a member of an Australian tax consolidated group.

In all cases, we recommend explaining the basis for the residency disclosures relating to trusts in the basis of preparation, having regard to the specific facts relevant to the trusts

Erin Craike
0415 598 440
erin.craike@au.pwc.com

Meina Rose
0432 320 540
meina.rose@au.pwc.com

Sarah Saville
0421 052 504
sarah.saville@au.pwc.com



Chris Vanderkley
0412 170 744
chris.g.vanderkley@au.pwc.com

PWC200871291