

4.6 Taxation

4.6.1 What is at stake?

In a democratic society, tax revenues are essential to finance public goods such as healthcare, infrastructure and social security. Multinational companies (including banks) benefit from the public facilities in the countries where they undertake activities and therefore have a responsibility to pay their fair share of taxes and be transparent about their tax payments. As such, tax compliance can be considered as the bottom line of Corporate Social Responsibility.²⁰⁷

Unfortunately, stimulated by global competition, the liberalization of capital markets and developments in information and communication technologies, multinational corporations are increasingly pursuing aggressive tactics to avoid or sometimes even evade paying taxes. While aggressive tax avoidance is abhorrent, tax evasion is both unethical and illegal. Due to international differences in tax rates and loopholes in national tax regulations, companies with operations in different countries have the possibility to decrease their tax burden considerably.²⁰⁸

Tax avoidance and tax evasion often involve complex corporate or financial structures that use *shell* or *mailbox* companies in tax havens. The use of tax havens is attractive because, apart from very low corporate tax rates, these locations are also characterized by limited or no transparency, which makes it very difficult for foreign tax authorities and civil society organisations to understand what is exactly going on - let alone take action to combat tax dodging.

The [Tax Justice Network \(TJN\)](#) estimated that as much as US\$ 255 billion is lost every year by governments around the world because of low or zero taxation of funds held by individuals in tax havens. This amount would be more than sufficient to plug the financing gap identified for one of the [UN Millennium Development Goals \(MDG\)](#), aiming to halve world poverty by 2015. Figures on how much tax income is lost by governments around the world due to corporate tax planning are even more difficult to estimate, but will certainly be in the same order of magnitude.

Companies should pay the appropriate taxes in the countries they are operating in to finance public goods such as healthcare, infrastructure and social security. Companies should also be transparent about their tax payments. The bank's policy should ensure that it will only offer financial services which live up to these principles. In developing such a policy, the bank could make use of the best international standards available as described below.

4.6.2 Best standards available

Acknowledging the negative effects of tax havens and other countries with harmful tax regimes, there have been several international initiatives to address this issue:

Government tax measures

Governments in various countries try to attract corporate investments by offering favourable tax regimes. These types of measures stimulate tax avoidance by multinational companies, harming the tax income of other states. Several international initiatives have been taken to set standards for the tax measures a government can rightfully take without harming the tax income of other states. Although meant for governments, these guidelines do offer some guidance for businesses as well.

The European Union has drafted a [Code of Conduct](#) on business taxation, which focuses on taxation measures which "affect, or may affect, in a significant way the location of business activity in the Community". More specifically, the Code states that "tax measures which provide for a significantly lower effective rate of taxation, including zero taxation, than those levels which generally apply in the member state in question are to be regarded as potentially harmful and therefore covered by this code".²⁰⁹

In 1998, the OECD initiated a project against [harmful tax practices](#).²¹⁰ The OECD makes a distinction between tax havens and countries with a harmful preferential tax regime. In contrast to tax havens which are often very small countries, almost fully dependent on income from tax related practices, the latter are characterised by a diversified economy and normal tax system, but with certain, often very lucrative, exceptions for specific activities or types of corporation.²¹¹ The OECD has identified [38 jurisdictions](#) as tax havens.²¹²

The Tax Justice Network has drafted its own list of tax havens. The list includes 72 jurisdictions including the OECD tax havens, the majority of countries with harmful preferential tax regimes and others like Hong Kong, Dubai, New York and the City of London.

Tax planning

A first important international standard on this issue are the [OECD Guidelines for Multinational Enterprises](#). Chapter X on Taxation states that "enterprises should comply with all tax laws and regulations in all countries in which they operate and should exert every effort to act in accordance with both the letter and the spirit of those laws and regulation".²¹³

The Tax Justice Network and the [Association for Accountancy and Business Affairs](#) have issued a *DRAFT Code of Conduct for Taxation*²¹⁴. The code states that "taxable transactions are recorded where their economic benefit can be best determined to arise." This means that companies should report income to tax authorities where it undertakes economic activity and refrain from shifting income earned in the country to locations with lower tax rates, mainly tax havens, to avoid taxation. Section 3 of this *DRAFT Code of Conduct for Taxation* provides general guidelines on how companies should deal with the issue of tax planning:

- Tax planning seeks to comply with the spirit as well as the letter of the law;
 - Tax planning seeks to reflect the economic substance of the transactions undertaken;
 - No steps are put into a transaction solely or mainly to secure a tax advantage.
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The British investment manager Henderson Global Investors has published [Responsible Tax](#), a very useful publication which describes a set of principles that should guide tax decision-making at leading companies, proposes ways of improving disclosure on tax to investors and others, and suggests a framework companies could use to assess their approach to tax.²¹⁵

Transparency and country-by-country tax reporting

Apart from paying their due share of taxes, multinationals should also report on the amount of tax they pay annually to hold them accountable. Generally, only companies listed on a stock exchange are obliged to publish their annual tax payments in their annual accounts. The problem is that these tax figures are only presented at the group level (on a consolidated basis) and not per country in which the multinational is active. In this way it is impossible to determine to what extent the company is shifting money to low tax jurisdictions or is involved in other forms of tax avoidance or evasion.

This issue has gained some attention within the extractive industry under the [Extractive Industries Transparency Initiative](#), a coalition of governments, companies, civil society groups and investors which established criteria for full publication and verification of company payments and government revenues from oil, gas and mining.²¹⁶ The [Publish What You Pay](#) coalition has a similar focus and additionally advocates for extractive companies to publish what they pay to governments. This also includes the reporting on what a company pays in taxes in countries where it operates.

This call for companies to disclose country-by-country data on commercial performance and taxes can be applied to all companies and sectors. [Global Witness](#) has issued a submission to the International Accounting Standards Board to expand and update the [International Accounting Standard 14 on Segment Reporting](#). Most important element suggested for this update is the obligation for corporations to disclose country-by-country data on (among other points):²¹⁷

- profit before tax;
- tax charge on profits split between current and deferred tax;
- other taxes or equivalent charges due to the government of the territory in respect of local operations;
- the actual payments made to the government of the country and its agencies for tax and equivalent charges in the period;
- the liabilities owing locally for tax and equivalent charges at the beginning and end of each period as shown on the balance sheet at each such date;
- deferred taxation liabilities for the country at the start and close of the period.

The G3 Guidelines of the [Global Reporting Initiative](#) also have a [performance indicator on tax](#) which also stresses the need for country-by-country reporting. Companies should report: "all company taxes (corporate, income, property, etc.) and related penalties paid at the international, national, and local levels. This figure should not include deferred taxes because they may not be paid. For organizations operating in more than one country, report taxes paid by country. The organization should report which definition of segmentation has been used."²¹⁸

4.6.3 Content of a bank policy

For banks, tax compliance is relevant in two ways. On the one hand, international banks themselves are multinational companies and therefore should pay taxes in accordance with the letter and spirit of the tax laws of the countries in which they operate as well as being transparent about it.

On the other hand, nearly all financial services offered by banks to companies bear a tax component. Given the large sums of money that are involved in corporate loans, project finance and investment banking, tax planning strategies may result in saving enormous amounts for the client. Hence, financial institutions and their clients have a strong incentive to organize their financial transactions in such a way that tax payments are minimized. Therefore international offerings of bonds or corporate loans are frequently structured via tax havens. This is often done by establishing a mailbox company to benefit from the low tax rates in tax havens. Managing and administrating such *Special Purpose Entities* is referred to as *trust banking* and is undertaken by divisions of large banks as well as specialized companies.

Although this report deals mainly with the services offered by banks to corporate clients, services offered to private clients need to be mentioned as well when dealing with tax issues. Many banks offer their wealthy private clients *offshore banking services*. These services are offered by subsidiaries of the banks which are deliberately located in tax havens. Banks should refrain from offering this type of *offshore* services to their private clients.

Both as a multinational company and provider of financial services, banks have a duty to pay their fair share of taxes and refrain from fiscal structures which are predominantly guided by tax motivations. The following elements should therefore be incorporated in the bank's tax policy:

- All financial services and products offered by the bank should be in compliance with the letter as well as the spirit of tax laws;
- Refraining from transactions which main (or only) goal is to secure tax advantages;
- Refraining from the use of tax havens;
- Full country-by-country reporting concerning the bank's tax payments.

4.6.4 Scoring table

The considerations in the previous paragraphs lead to the following scoring table with regard to bank policies on tax compliance. Bank policies are only evaluated on issues related to their financial services, as is the case with other policies. Issues related with the tax payments of banks themselves are important, but not included in the scoring table.

0. *The bank has no policy on tax compliance;*
 1. *The bank's tax policy is vaguely worded or aspirational, with no clear commitments other than that the bank ensures legal compliance (no tax evasion);*
 2. *The bank ensures its financial services are compliant with the letter and the spirit of tax laws (no tax avoidance);*
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3. *The bank ensures its financial services are compliant with the letter and the spirit of tax laws. The bank also refrains from products or transactions which main or only goal is to secure tax advantages OR from the use of tax havens.*
4. *The bank ensures its financial services are compliant with the letter and the spirit of tax laws. The bank also refrains from products or transactions which main or only goal is to secure tax advantages AND from the use of tax havens.*

4.6.5 Results

In advisory services, banks often support their clients (individuals or corporate) in such a way that they pay as little tax as possible. This is likely to encourage behaviour that is on the edge of what is legally and/or socially acceptable. Almost all banks state that they only do business with clients that abide to the law. This of course cannot be considered a policy, but is merely ensuring that the bank will not get involved in criminal transactions.

However, many banks do have offshore branches in tax havens, which help their clients to evade taxes levied by legitimate authorities. Only BBVA (Spain) states that it does not support activities related to tax evasion by its clients. Whether it also restricts lending to these clients is not known.

Scores on Taxation policies					
BBVA	1	Deutsche Bank	0	Rabobank	0
ABN AMRO	0	Dexia	0	RBS	0
ANZ	0	Fortis	0	Royal Bank of Canada	0
Banco Bradesco	0	Goldman Sachs	0	Saudi-American Bank	0
Banco do Brasil	0	HSBC	0	Santander	0
Banco Itaú	0	ICBC	0	Scotiabank	0
Bank Mandiri	0	ING	0	Société Générale	0
Bank of America	0	Intesa Sanpaolo	0	Standard Bank	0
Bank of China	0	JPMorgan Chase	0	Standard Chartered	0
Barclays	0	KBC	0	State Bank of India	0
BNP Paribas	0	Merrill Lynch	0	Sumitomo Mitsui	0
China Construction	0	Mitsubishi UFJ	0	UBS	0
Citi	0	Mizuho Financial	0	Unicredit	0
Crédit Agricole	0	Morgan Stanley	0	WestLB	0
Credit Suisse	0	Nedbank	0	Westpac	0