THE CHURCH OF ENGLAND
Ethical Investment Advisory Group

Church of England Ethical Investment Advisory Group

Corporate tax ethics: engagement policy

July 2013

The EIAG has considered the role of the national investing bodies with regard to tax ethics and the companies in which they invest.

The EIAG recommends that tax ethics should be a subject for investor engagement where it appears that a company's approach is blatantly aggressive or abusive.

Definitions

The Glossary of Tax Terms, OECD Centre for Tax Policy and Administration, offers the following definitions:

- **TAX EVASION:** "A term that is difficult to define but which is generally used to mean illegal arrangements where liability to tax is hidden or ignored, i.e. the taxpayer pays less tax than he is legally obligated to pay by hiding income or information from the tax authorities"

- **TAX PLANNING:** "Arrangement of a person's business and /or private affairs in order to minimize tax liability"

- **TAX AVOIDANCE:** "A term that is difficult to define but which is generally used to describe the arrangement of a taxpayer's affairs that is intended to reduce his tax liability and that although the arrangement could be strictly legal it is usually in contradiction with the intent of the law it purports to follow"

In 2012, the UK Government issued a consultation document on the institution, through legislation, of a General Anti-Abuse Rule ('GAAR'), the intention of which would be to combat abusive tax arrangements:

- **ABUSIVE TAX ARRANGEMENTS:** "Tax arrangements are "abusive" if they are arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action, having regard to all the circumstances including (a) the relevant tax provisions, (b) the substantive results of the arrangements, and (c) any other arrangements of which the arrangements form part."

The EIAG's concerns about corporate tax ethics relate not only to illegal tax evasion but also to aggressive tax planning and avoidance, particularly where a company's approach may be regarded as abusive.

Introductory remarks

1. This policy relates to corporate tax ethics. Corporate tax ethics are a matter of interest to the national investing bodies because of their shareholdings in companies.

2. Corporate tax is a complicated area, more so in a globalised business world. The national investing bodies cannot and should not attempt to police the payment of corporate tax. This is the responsibility of the boards of companies and the tax authorities.

3. Part of the reason for the complexity of the corporate tax landscape is the use of taxation policy by governments to compete for investment, encourage particular corporate behaviours (e.g. capital investment) and support business (e.g. tax deductability of losses). The payment of low rates of corporate tax does not necessarily indicate abuse.

4. Low rates of tax collection by low income countries can be (but are not only) the result of poor tax codes and poor implementation of them. Such problems cannot be solved by companies alone and will require additional support e.g. technical assistance from international development agencies.

Policy analysis

5. Boards of companies have a fiduciary responsibility to their shareholders, which implies some tax planning. However, the EIAG rejects the view that corporate tax planning is *only* a matter of legal compliance. The way in which tax planning is conducted is both a business risk and an ethical issue.

Business risk

6. The way in which a company approaches tax planning affects business risk. A preoccupation with aggressive minimisation of tax liabilities can lead to activities or transactions that serve no useful purpose for the business and confuse its operation. Aggressive attempts to minimise tax liabilities may lead to new regulations that are damaging to a company's interests or to disputes with tax authorities.

7. Disputes with tax authorities are not an automatic sign of abusive tax arrangements. They may arise from the aggressiveness of the tax authorities, rather than the taxpayer. But disputes divert management focus, soak up staff time and require expensive professional advice. They lead to accounting and investor uncertainty, and may result in costly fines and demands for back payment of tax. They may even hamper a company's ability to continue to operate successfully in a jurisdiction.

8. Finally, negative perceptions of a company's approach to tax may lead to brand and reputational damage, potentially jeopardising the company's continuing ability to create economic value for shareholders.

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Ethics

9. The way in which a company approaches tax is part of its relationship with the societies in which it operates.

10. Corporate activity brings benefits to society (e.g. jobs, prosperity), but companies also derive benefits from society (e.g. limited liability, security, infrastructure, an educated workforce). The payment of corporate tax acknowledges companies' responsibility to society. Societies should resolve for themselves what constitute appropriate government activities and tax regimes. Christians believe that the payment of tax in such circumstances contributes to a good society.

11. Companies neglect their corporate social responsibility when they engage in aggressive tax avoidance or abusive tax arrangements. Such practice:

- reduces tax yield decided by government, making government trim its expenditure plans or consider raising taxes, which in turn has the potential to damage incentives
- redistributes the tax burden on a do-it-yourself basis, which is not open to everyone, so is unfair and misallocates incentives provided through the tax system
- undermines the integrity of the tax system by being perceived to be unfair by those taxpayers who want to pay their fair share, eventually becoming corrosive by persuading the compliant that they too should pay less tax
- creates horizontal and vertical inequities between both individuals and corporate entities; and
- diverts resources to the artificial activity of creating avoidance schemes and away from developing enterprise and growth.

12. No tax code will be perfect and the global patchwork of tax codes is certainly far from perfect. As a result, tax planning involves constant ethical decisions for companies e.g. about the extent to which they obey the spirit of the law (assuming the intent of the legislature is clear), where they choose to domicile corporate activities and how they use their negotiating strength with the governments of low income countries (e.g. with regard to the terms for extractive projects).

Policy recommendations

13. The business risk and ethical dimensions of the management of corporate tax both point in the same direction: eschewing aggressive tax planning and avoidance, and abusive tax arrangements.

    The EIAG recommends that tax ethics should be a subject for investor engagement where it appears that a company's approach is blatantly aggressive or abusive.

14. Payment of significantly lower levels of tax than peers may indicate that a company is an outlier and should be the subject of engagement.

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15. In the context of low income countries, the EIAG has particular concerns about companies extracting profits resulting from economic activity without paying appropriate corporate tax in those countries. Corporate negotiating power should not be deployed in such a way that it prejudices a low income country's ability to improve the welfare of its citizens.

16. Concern may relate not only to a company's approach to its own tax liabilities but also to corporate promotion of, or support for, tax avoidance by others e.g. businesses, individuals, employees or other parties associated with the company.

17. Engagement should start with fact-finding and exploration. The objective of engagement should be to encourage the development of and alignment with good practice. Good practice includes board-level reviews of tax policy, maintenance of a documented tax policy and voluntary public disclosure of tax paid accompanied by information to help interpret the data disclosed.

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