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# DEVELOPMENT FINANCE INSTITUTIONS AND RESPONSIBLE CORPORATE TAX BEHAVIOUR

WHERE WE ARE AND THE ROAD AHEAD

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## SUMMARY

Development Finance Institutions (DFI) are not doing enough to avoid becoming accomplices in harmful corporate tax practices. This is the finding of an analysis of publicly available policies of nine DFIs related to corporate tax payments, which suggests that DFIs are doing too little to encourage responsible corporate tax behaviour. This analysis highlights the role DFIs should play in promoting responsible tax practices by companies.

This briefing paper outlines how a selection of DFIs are largely failing to use their influence as investors in companies operating in developing countries to ensure that those companies restrict or eliminate their use of tax havens or to reduce the risk of corporate tax avoidance. While others have taken important steps forward. There is a particular need for DFIs to play this role, given the scale of global tax dodging, the fact that DFIs largely use public money and since DFI investments in developing countries are significantly increasing.

DFIs are government-owned institutions that invest in private sector projects in developing countries. In Europe, 15 bilateral DFIs are members of the Association of European Development Finance Institutions (EDFI) and are among the bodies that implement their governments' development cooperation policies. Several multilateral DFIs are also major investors in the private sector, notably the World Bank's International Finance Corporation (IFC), the EU's European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD) and the regional development banks in Africa, Asia and Latin America.

This analysis of DFIs' publicly available policies on tax finds that some DFIs are significantly lagging behind in preventing their funds supporting aggressive tax planning albeit unintentionally. Some aspects of their investments remain shrouded in secrecy, although transparency is crucial in order to establish public confidence, as DFIs are using tax payers' money. All DFIs need to still make improvements in public access to information to ensure accountability.

European governments are making private finance central to their international development efforts, and DFIs are playing an ever more central role in channelling investments from north to south. The role of DFIs in development finance has increased dramatically. Globally, the IFC is the biggest player in this field and its investment commitments have increased six-fold since 2002. In Europe, the consolidated portfolio of EDFI members increased nearly four-fold between 2003 and 2015, from €10bn to €36bn.

Investees of DFIs include both small- and medium-sized enterprises and large transnational corporations (TNCs). The latter are a particular focus for this report because, due to their cross-border nature, they have a greater ability than domestic companies to practice tax avoidance, especially by using tax havens.

Tax revenues form the basis of a sustainable economy and are crucial for developing countries that seek to invest in poverty reducing services while also becoming less dependent on foreign aid. Yet the United Nations (UN) trade body, the UN Conference on Trade and Development (UNCTAD), estimates that developing countries lose at least \$100bn a year due to one type of corporate tax avoidance alone.

Corporate tax dodging by TNCs and the persistent presence of tax havens in the international system represents a major obstacle to combatting a modern scourge – that of deep and rising global inequality. One of the most effective ways of fighting inequality in societies is through greater tax justice, and dedicated efforts by governments to realize human rights and achieve the

Sustainable Development Goals (SDGs). There will be a significant need for more public finance to be mobilized domestically to help deliver the SDGs in all countries. This will require national tax systems that are efficient and fair, ensuring that taxpayers, including corporations, contribute according to their means.

Under their human rights obligations, states are required to mobilize the maximum available resources to finance the progressive realization of economic, social and cultural rights, as well as to advance civil and political rights and the right to development. The financing gap to achieve the SDGs is estimated at \$2.5 trillion. Undoubtedly the private sector will need to play a role to complement public financing for sustainable development. The private sector will also need to contribute to domestic resource mobilisation through corporate tax payments. DFIs and private sector lending by publicly backed banks should play a crucial role in ensuring this.

This research analyses the policies of nine DFIs, assessing them against some key indicators that would help ensure they promote responsible tax practices and avoid possible complicity in company tax avoidance strategies. Key findings include the following:

- Eight of the nine DFIs list their entire portfolios of investments on their websites. None of the DFIs report what proportion (or which) of their investments goes to TNCs.
- Seven of the nine DFIs fail to routinely state the country of incorporation of all their investees. Four of the nine DFIs do not list these at all, while three list the domicile for only some of their investees, usually the funds in which they invest, and two lists all countries of incorporation. At least seven of the nine DFIs invest in companies or financial intermediaries incorporated in tax havens, such as Mauritius and the Cayman Islands. In addition, DFIs invest in many companies that use tax havens in their corporate structures.
- Eight of the nine DFIs have some sort of policy and standards in place specifically regarding their tax policies and use of tax havens. However, most are reliant on the ratings put forward by the Organisation for Economic Co-operation and Development (OECD) Global Forum on Transparency and Exchange of Information for Tax Purposes, argued for many years by NGOs to be insufficient. Only a few take steps beyond legal compliance and the Global Forum.
- DFIs vary in having tax risk and impact assessment and few provide public information on this. Most DFIs have some framework for monitoring tax payments as part of their projects, but this is usually not situated in a framework of monitoring key tax risk factors that can result in abusive practices.
- Eight of the nine DFIs include tax as an indicator when measuring their development impact. However, those DFIs reporting the tax payments of the companies in which they invest provide only limited information publicly.
- DFIs hardly highlight the importance of tax in their public annual reporting at all. In their most recent (2015) annual reports, four DFIs make no mention of tax at all. Others make brief mentions of taxes paid by their investees while only one (Swedfund) has a considerable section on its tax policy and payments.
- This research has not been able to identify any of the nine DFIs that is encouraging or requiring concrete, responsible tax practices by its investees. As a general rule, DFIs simply require investees to abide by the law.
- All nine DFIs require their private sector clients to identify their beneficial owners as part of their screening process. Yet none of the DFIs appear to make this information public.
- None of the DFIs require the companies it invests in to report publicly (or to the DFIs) on a country-by-country basis on the profits, losses, number of employees, taxes paid and other forms of economic performance.

# Recommendations

The following set of recommendations contains a wide range of actions DFIs can undertake to secure more responsible corporate tax behaviour from their clients and business partners. Some are immediately implementable (and perhaps already being implemented for some), while others may only be implemented over a longer time. For all recommendations, DFIs can take the first step of acknowledging publicly the challenges related to TNCs and aggressive tax planning and their commitment towards continuously improving practices to meeting these.

## Use of tax havens

- ✓ DFIs should not use tax havens to channel their investments to developing countries. When an intermediary jurisdiction is used, DFIs should demonstrate that the use of a third jurisdiction was superior in advancing its development mandate when compared with a targeted developing country for domiciliation.
- ✓ When tax havens appear in the corporate structure of a client or partner of DFIs, heightened tax due diligence should be applied in addition to the regular requirements. DFIs should deliver an impact assessment to document that development effects are not negatively affected including documenting impacts on domestic resource mobilization.
- ✓ DFIs should ensure that these and other recommendations outlined here apply to financial intermediaries through which DFIs invest as well as investee companies and sub-clients of financial intermediaries.

## Tax behaviour of client companies

DFIs should:

- ✓ Require all clients to have and publish a responsible corporate tax policy approved by its board. The policy should be published on the company's website. This should acknowledge the important role of tax in society and commit the company to avoid engaging in harmful tax practices, including avoiding the use of tax havens.
- ✓ Require all clients to make the following elements available to the DFI risk assessment team and subsequently to be made public, if eligibility for investment is granted:
  - a commitment not to practice aggressive tax planning, and to engage in tax risk and tax impact assessment in key identified areas;
  - country-by-country information on the turnover, assets, full-time employees, profits and tax payments in each country in which it operates;
  - information about beneficial ownership and company structure and purpose;
  - all discretionary tax treatment they receive that affects the tax base or taxable profits, including tax incentives, any tax planning schemes that are under mandatory notification (e.g. UK DOTAS) in any country where the company operates, advance pricing agreements or advance tax rulings that substantially affect either the tax base or taxable profits;
  - tax risk and tax impact assessment in their analysis of challenges to domestic resource mobilization to prevent aggressive tax planning, irresponsible tax behaviour as well as its potential for negative impact on human rights.
- ✓ Ensure that these and other recommendations outlined here apply to financial intermediaries through which DFIs invest, as well as investee companies and sub-clients of financial intermediaries.

## **Transparency and reporting**

DFIs should:

- ✓ Develop, in consultation with civil society organizations (CSOs), and publish a tax-responsible investment policy, which includes a commitment to promote domestic resource mobilization and responsible corporate tax behaviour. Once adopted, this should be applied to existing as well as new investments.
- ✓ Publish a full list of investments that includes: (a) the investee companies (and sub-clients of financial intermediaries); (b) their countries of incorporation; (c) their corporate structure; and (d) their beneficial owners.
- ✓ Publish figures on what proportion of the DFI's portfolio goes to: (a) transnational corporations (including through financial intermediaries); and (b) small- and medium-sized enterprises (SMEs).
- ✓ Giving the reporting of tax payments a prominent place in annual reports, and/or developing a separate tax responsibility report, including analysis of their development impacts.
- ✓ Reporting the tax payments of investee clients and each investment's expected and actual tax payments and asking companies to explain deviations in relation to economic activities.
- ✓ Engaging openly and in a transparent manner with stakeholders on tax issues and tax impacts of its investments. This could include assessing and reporting on the impacts of tax practice, assessing whether value creation corresponds to economic reality, how to prevent and mitigate potential negative impacts, and tracking performance and communicating on this.

## **Measuring development**

DFIs should:

- ✓ Include tax in the development indicators and explain how they are measured, and what importance is attached to tax indicators in relation to other indicators for development.
- ✓ When evaluating projects ex-ante, periodically and ex-post, include corporate tax payments as a separate indicator in addition to total payments to governments. Measure tax risk and impact based on key themes where practices have the greatest impact on revenue, human rights and good governance. Measure tax payments in absolute numbers and relative to the investment.

## **Internal issues**

DFIs should:

- ✓ Devote sufficient resources to develop optimal policies and implement best practice.
- ✓ Enable full transparency toward and constructive engagement with CSOs on new policies and evaluation of existing policies.
- ✓ Ensure in-house capacity to oversee these activities to ensure there is no dependency on external advisers, who might have a conflict of interest. This could include hiring capacity to look at taxes beyond legal compliance and to improve engagement of staff to help contribute to sustainable development and human rights.

# INTRODUCTION

Development Finance Institutions (DFIs) are not doing enough to avoid becoming accomplices in harmful corporate tax practices. This is the finding of an analysis of publicly available DFI policies related to corporate tax payments, which suggests that DFIs are doing too little to encourage responsible corporate tax behaviour. This analysis highlights the role DFIs should play in promoting responsible tax practices by companies.

The briefing paper outlines how a selection of DFIs are largely failing to use their influence as investors in companies operating in developing countries to ensure that those companies restrict or eliminate their use of tax havens or to reduce the risk of corporate tax avoidance. Meanwhile other DFIs are taking very important steps forward. There is a particular need for DFIs to play this role given the scale of global tax dodging, the fact that DFIs largely use public money and since DFI investments in developing countries are significantly increasing.

Although the role of the private sector in global development is increasingly accompanied by discussions on tax and domestic resource mobilization, DFIs are lagging behind in preventing their funds from becoming complicit in supporting aggressive tax planning. This has been demonstrated to be at odds with stated development objectives. While often considered to be highly immoral, international tax avoidance is often, technically speaking, legal. Tax evasion, on the other hand, is illegal and DFIs should also be vigilant in ensuring their investments flows are in no way associated with tax evasion. However, some aspects of DFIs' investments remain shrouded in secrecy, although transparency is crucial in order to establish public confidence, as DFIs are using tax payers' money. Today it seems that investors' interests overrule transparency.

DFIs must take on the increased role that governments and the tax-paying public envisioned for them by redefining sustainable finance and developing new standards for responsible corporate tax behaviour that go beyond legal compliance. They must recognize the intrinsic connection between financing development and mobilizing domestic resources, including through the effective fight against aggressive tax planning so that they can play a leading role in securing more transparency in the use of public funds.

While the international community is taking important steps to ensure collaboration in tax matters, much more can be done to ensure individual companies adhere to the highest standards of responsibility and transparency when it comes to their corporate tax payments. DFIs must become more transparent themselves about their investments and they should act as catalysts for a more progressive global agenda on transparency and tax justice. Policy makers should ensure that DFIs are at the forefront of sustainability standards and the realization of human rights. This means that they should in no way support private sector actors that compromise these objectives by promoting tax avoidance. In the European Union (EU), ensuring that DFIs promote responsible tax behaviour should be considered a key aspect of Policy Coherence for Development, which is meant to ensure that all EU policies contribute to sustainable development.<sup>1</sup>

## The increasing role of DFIs

DFIs are government-controlled institutions that invest in private sector projects in developing countries. Some have multilateral governance and shareholding structures between representa-

tives of regional member countries and non-regional member countries in Europe, Asia and North America, global and regional donor agencies. Others, as bilateral agencies have simpler structures. In Europe, 15 bilateral DFIs are members of the Association of European Development Finance Institutions (EDFI) and are among the bodies that implement their governments' development cooperation policies. Several multilateral DFIs are also major investors in the private sector, notably the World Bank's International Finance Corporation (IFC), the EU's European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD) and the regional development banks in Africa, Asia and Latin America.

Some DFIs are wholly owned by the public sector, while others have mixed public and private ownership. Most DFIs are funded by donors' development agencies but can raise additional funds on capital markets. DFIs support private sector companies in developing countries, either directly by providing loans or buying shares, or indirectly by supporting financial intermediaries such as commercial banks and private equity funds, which subsequently on-lend or invest in enterprises.<sup>2</sup>

The financing gap to reach the sustainable development goals (SDGs) is estimated at \$2.5 trillion. Undoubtedly the private sector will need to play a role to complement public financing for sustainable development. European governments are making private finance central to their international development efforts, and DFIs are playing an ever more central role in channelling investments from north to south.<sup>3</sup>

The role of DFIs in development finance has increased dramatically. Globally, the IFC is the biggest player in this field and its investment commitments have increased six-fold since 2002.<sup>4</sup> In Europe, the consolidated portfolio of EDFI members increased nearly four-fold between 2003 and 2015, from €10bn to €36 bn.<sup>5</sup> However, leveraging private financing is not only about size but is also about the quality of the investment.

Financial markets have gained increasing prominence in DFIs' commitments. On average, over 50 percent of the public finance flowing from DFIs to the private sector goes to the financial sector, including banks, in the form of loans and equity.<sup>6</sup> The IFC has made investments of over \$50bn in the financial sector during 2010-15, which have risen by 45 percent during that same period.<sup>7</sup> Recent research by non-governmental organizations (NGOs) has shown that, in addition to problems associated with direct investments in companies, the use of financial intermediaries comes with significant challenges regarding management and effective implementation of due diligence, which can have quite severe negative impacts on the communities affected.<sup>8</sup> Development impacts from the funds channelled through financial intermediaries can be hard to monitor and the use of third parties is problematic because there is a lack of knowledge about who the beneficiaries of the funds are and, sometimes, who the beneficial owners are. This creates a significant risk as it does not allow DFIs to identify aggressive tax planning schemes or financial crimes such as money laundering and tax evasion.<sup>9</sup>

All of these concerns call into question the appropriateness of the private sector as a major channel of development finance, and raises questions about whether the use of third-party financing undermines people-centred, inclusive models of development. This paper does not address this more structural issue related to publicly backed private finance,<sup>10</sup> but rather focuses on how accountability and development impact in relation to responsible corporate tax behaviour and the use of tax havens can be ensured when development financing is channelled through the private sector.

## DFIs and corporate tax payments

Investees of DFIs include both small- and medium-sized enterprises (SMEs) and large transnational corporations (TNCs). The latter are a particular focus of this report given that, due to their cross-border nature, they have a greater ability than domestic companies to adopt tax avoidance schemes. They do this in particular by using tax havens with high levels of financial secrecy, which



can be the conduit through which money illicitly flows out of developing countries. Equally, the use of financial intermediaries raises particular concerns related to tax issues, as the intermediaries can be TNCs themselves and also lend on to their clients, which might be TNCs too. Furthermore, making sure that development ends are achieved and preventing negative impacts on human rights in the end use of the funds have proven to be particularly challenging in several cases.<sup>11</sup>

Tax revenues form the basis of a sustainable economy and are crucial for developing countries that seek to invest in poverty reducing services while also becoming less dependent on foreign aid. Alongside job creation and technology transfer, paying taxes is one of the most important contributions that a foreign business can make to its host country. This is severely challenged by the use of tax havens and aggressive tax planning schemes by TNCs. For example, UNCTAD has estimated that one type of corporate tax avoidance alone is costing developing countries \$70-120bn per year.<sup>12</sup>

After reviewing publicly available data on more than 200 companies, Oxfam has found evidence that nine out of ten of them have a presence in at least one tax haven.<sup>13</sup> In addition to depriving countries of much-needed resources, tax dodging by TNCs also creates an uneven playing field in countries by undermining the competitiveness of domestic businesses, which are usually key to national economic development. It significantly challenges the ability of states to realize their human rights obligations and meet the SDGs.<sup>14</sup>

Corporate tax dodging by TNCs and the persistent presence of tax havens in the international system represents a major obstacle to combatting a modern scourge – that of deep and rising global inequality. One of the most effective ways of fighting inequality in societies is through greater tax justice, and dedicated efforts by governments to realize human rights and achieve the SDGs. There will be a significant need for more public finance to be mobilized domestically to help deliver the SDGs in all countries. This will require national tax systems that are efficient and fair, ensuring taxpayers, including corporations, contribute according to their means. The recognition of the importance of good tax policies and practices is slowly embedding itself in the international community and it is influencing discussions about how to finance the development agenda post-2015.<sup>15</sup>

In the run-up to the third UN Financing for Development Conference in Addis Ababa, held in July 2015, the need to build a fairer international tax system was higher on the agenda than ever before. It was supported by global NGO campaigns, several side-events were held and global tax governance – as well as global corporate taxation – became a key part of the final negotiations.<sup>16</sup> G77 countries were calling for fairer global corporate tax reforms and pushed this issue to the top of the agenda, as they recognize that tax revenues are essential in terms of financing their development. The Addis Tax Initiative was announced at the conference and was supported by about 30 donors and 10 international organizations, including the World Bank Group. It includes several elements to support domestic resource mobilization, including a call for the UN Global Compact to develop an 11th Principle on Responsible Corporate Taxation.<sup>17</sup>

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## Box 1: Research on DFIs and corporate taxes by NGOs

In recent years, NGOs have scrutinized DFIs' policies and practices related to corporate tax payments and corporate tax behaviour in various publications. The present report draws on these analyses, as well as on new research.

In 2016, Oxfam commissioned research to analyse the investments of the IFC regarding tax havens, gauging the extent to which the IFC invests in TNCs in sub-Saharan Africa and considering financial intermediaries as well as direct investments in companies.<sup>18</sup> It found that the IFC is a substantial investor in companies using tax havens and urged the DFI to update its offshore policy and improve transparency.

In two separate reports in 2014 and 2015, Oxfam IBIS (formerly IBIS) analysed the tax policies of three Scandinavian DFIs – Denmark's IFU, Sweden's Swedfund and Norway's Norfund. It also looked at three multilateral DFIs – the IFC, the Inter-American Development Bank (IDB, but now IIC) and the African Development Bank (AfDB).<sup>19</sup> The research sought to gauge how well these DFIs report on tax in their development results frameworks, and highlighted several gaps. It urged the DFIs to improve their transparency, eliminate the use of tax havens for tax planning purposes and require investee companies to promote responsible tax policies.

The NGO network Eurodad has also produced several reports on DFIs in recent years. Its principal report on tax, *Going Offshore*, published in 2014, assessed the extent to which a sample of European DFIs are investing in companies domiciled in tax havens and analysed the internal standards these DFIs have in place regarding tax havens. It found that some DFIs – notably the UK's CDC Group and Belgium's BIO – routed a large proportion of their investments via tax havens and that internal standards were insufficient to reduce or prevent this.<sup>20</sup>

A group of NGOs, including Oxfam IBIS, published an analysis of DFIs' use of tax havens in 2010.<sup>21</sup> Another NGO group, including Re:Common and Counter Balance, analysed the tax policies of the European Investment Bank in 2015.<sup>22</sup> In 2016, Counter Balance also critically analysed the EIB's use of private equity funds. The research showed that the EIB supports private equity funds incorporated in tax havens and problematic jurisdictions and that there is a systematic lack of transparency involved in these types of operations, both from the EIB and the investment funds' side.<sup>23</sup>

Joint analysis by Oxfam, ActionAid and Christian Aid in 2015 outlined a range of ways in which corporations could become responsible tax payers. It also urged them to improve tax transparency and conduct better impact evaluations of their tax policies and practices, among other areas.<sup>24</sup> While not directly addressing the role of investors, the report highlights that investors are starting to adopt tax-responsible investment policies due to concerns about financial and reputational risks associated with tax avoidance practices. The report also notes that investors need to ask the right questions and that, when they engage, they can improve corporate practices in terms of tax-responsible practices.

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# ANALYSIS OF DFI POLICIES ON TAX

This research analyses the policies of nine DFIs, assessing them against some key indicators that would help ensure they promote responsible tax practices and avoid possible complicity in company tax avoidance and evasion strategies. This research has only analysed publicly available material. There are some gaps in the research owing to lack of publicly available information; nevertheless, a clear picture emerges regarding the positive and negative aspects of current DFI policies.

The following sections are structured around key questions of relevance to assess the extent to which DFIs can reduce the risk of their investments being complicit in irresponsible tax behaviour, whether they report sufficiently on this and finally what role, if any, they take in actively encouraging responsible corporate tax practice. Some of the questions relate to transparency, and whether investments can be publicly scrutinized; some relate to existing mechanisms for securing development effectiveness; and a few are new suggestions based on how the area of corporate responsible tax practice is developing. Please find a summary of key questions asked in the annex.

The DFIs we have chosen to look at represent both multilateral and bilateral institutions that vary in size and experience. They are:

- African Development Bank (AfDB)
- CDC Group of the UK
- European Investment Bank (EIB)
- FMO of the Netherlands
- Inter-American Investment Corporation (IIC), part of the Inter-American Development Bank (IDB) Group
- International Finance Corporation (IFC)
- IFU of Denmark
- Proparco of France
- Swedfund of Sweden

## Transparency in portfolio and monitoring what type of companies benefit from the funds

Public funds need to be held to the highest standards of accountability and transparency. Therefore, it is important that there is clear information available for the public, media and researchers regarding which companies DFIs invest in and where these are incorporated.

Eight of the nine DFIs list their entire investment portfolio on their websites. However, the EIB does not list its entire portfolio: it lists only some current projects and some but not all projects 'to be' financed.<sup>25</sup> In addition, the EIB does not always state who the investee actually is for its investment projects.<sup>26</sup>

Monitoring what types of companies are receiving the investments is also important. Many DFIs state it is their aim to reach small- and medium-sized enterprises (SMEs), which necessitates monitoring. However, for risk management purposes it is also important to identify whether the companies have subsidiaries in other countries. As mentioned above, TNCs have a greater possibility for engaging in aggressive tax planning schemes than domestic companies. Our research found that none of the nine DFIs shows what proportion of their investments goes to TNCs. However, recent research on the IFC's investments in sub-Saharan Africa shows that the IFC invests *primarily* in TNCs, and that the vast majority of those TNCs have a corporate structure that includes tax havens.<sup>27</sup>

This research has not focussed on the sub-clients of financial intermediaries, but stresses that information on the on-lend of financial intermediaries is a particular concern and that currently access to information is highly inadequate.

## Beginning to gauge the risk: countries of incorporation

In order to gauge the risk of whether DFI investments could be complicit in tax avoidance, even unintentionally, as a starting point it is important for DFIs to state the country of incorporation of the investee company, the financial intermediary and the clients of the financial intermediary benefiting from the DFI funds. Yet none of the nine DFIs routinely state the country of incorporation of all their investees. Four of the nine DFIs – AfDB, IIC, FMO, and Swedfund – do not list these at all, while three – Proparco, IFU<sup>28</sup> and EIB – list the domicile for only *some* of their investees, usually the funds in which they invest, and two appear to list all countries of incorporation - IFC, CDC.

By individually checking the country of incorporation of each DFI investment, this research found that at least seven of the nine DFIs invest in companies or financial intermediaries incorporated in tax havens.<sup>29</sup> FMO and EIB, for example, have investments in financial intermediaries incorporated in Mauritius,<sup>30</sup> while CDC has investments in companies incorporated in, for example, the Cayman Islands.<sup>31</sup> The number of DFI investments in companies incorporated in tax havens varies: for example, our research found that only one of 56 investees of Swedfund is incorporated in a tax haven.<sup>32</sup> For IIC and Proparco, this research was not able to establish whether they invest through tax havens.

In addition to investments in companies incorporated in tax havens, DFIs might well invest in companies that use tax havens in their corporate structures. Recent Oxfam research found that 51 of the 68 companies that were lent money by the IFC in 2015 to finance investments in sub-Saharan Africa use tax havens. In total, these companies – whose use of tax havens has no apparent link to their core business – received 84 percent of the IFC's investments in the region in 2015.<sup>33</sup> Oxfam also found that more than 80 percent of the dollars invested by IFC in sub-Saharan Africa in 2015 were channelled to companies that are present in at least one tax haven, without any apparent link to their core business and with a very low level of transparency on such sophisticated structures.<sup>34</sup>

Between 2007 and 2013, Proparco channelled more than \$505m intended for developing countries through tax havens.<sup>35</sup> Research by Eurodad also found that, at the end of 2013, 118 out of 157 fund investments made by CDC went through jurisdictions that featured in the top 20 of Tax Justice Network's Financial Secrecy Index – an index that ranks jurisdictions according to their levels of secrecy.<sup>36</sup> Between 2000 and 2013, these funds received a total of \$3.8bn in original CDC commitments.<sup>37</sup> Eurodad argued that CDC's portfolio as of 31 December 2013 'shows that both its direct and its indirect investment model rely heavily on secrecy jurisdictions', including Mauritius, Guernsey and Luxembourg.<sup>38</sup>

In 2016, Counter Balance critically analysed the EIB's use of private equity funds. The research showed that the EIB supports private equity funds incorporated in tax havens and problematic jurisdictions. They highlighted a systematic lack of transparency involved in these types of operations, both from the EIB and the investment fund's side. From 2011 to 2015, the EIB invested €470m in investment funds located in secrecy jurisdictions.<sup>39</sup>

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## Box 2: Oxfam's definition of tax havens

Tax havens are jurisdictions or territories that have intentionally adopted fiscal and legal frameworks allowing non-residents (physical persons or legal entities) to minimize the amount of taxes they should pay where they perform a substantial economic activity.

Tax havens tend to specialize and most of them do not tick all of the boxes. However, they usually fulfill several of the following criteria (which can be used in various combinations):

- They grant fiscal advantages to non-resident individuals or legal entities only, without requiring that *corresponding* economic activity should be made in the country or dependency.
- They provide a significantly lower effective level of taxation, including zero taxation for natural or legal persons.
- They have adopted laws or administrative practices that prevent the automatic exchange of information for tax purposes with some or all other governments.
- They have adopted legislative, legal or administrative provisions that allow the non-disclosure of the corporate structure of legal entities (including trusts, charities, foundations etc.) or the ownership of assets or rights.

In January 2016, to create an updated list of tax havens, Oxfam used lists drawn up by other organizations,<sup>40</sup> and found that these combined identified 58 jurisdictions.<sup>41</sup> Note that many more countries could be added to such a list and/or could be expected to join a list in the future as they adopt harmful tax practices. Furthermore, some jurisdictions/countries may need to be removed from the list when they no longer meet tax haven criteria.

Oxfam calls for the setting up of integrated, binding, exhaustive and objective monitoring exercises of tax havens at a global level, in order to assess the risks posed by these jurisdictions. These exercises should be held regularly and their outcomes should be made public.

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## DFIs' own policies on tax or tax havens

Having a publicly available policy related to corporate tax payments and the use of tax havens can be a good starting point. However, it fundamentally depends on the content of such a policy or guideline. Our research found that eight of the nine DFIs have some sort of policy or standard in place regarding tax (with our focus being on corporate tax payments) or the use of tax havens (often referred to by DFIs as offshore financial centres (OFC)).

However, these policies vary in terms of comprehensiveness. In addition, all are reliant on the ratings put forward by the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes (hereafter the Global Forum) in one shape or another. The Global Forum has severe limitations, as it uses unambitious criteria for determining what constitutes a tax haven (see Box 2 and 3).<sup>42</sup> A key point of the analysis have been to check whether DFI policies go beyond the standard set by the Global Forum, and enable a position on responsible corporate tax practice beyond legal compliance from their clients.

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### Box 3: Problems with the Global Forum

The current Global Forum peer review process is not fit for purpose for several reasons, including:

#### **Unambitious standards:**

The Global Forum uses a relatively low standard to judge which jurisdictions are ‘non-cooperative’ and should therefore be excluded by investors. For example, the Global Forum regards Luxembourg and the Isle of Man as compliant with its standards and Mauritius, the British Virgin Islands (BVI) and Cayman Islands as ‘largely compliant’.<sup>43</sup> However, half of the companies in the Panama Papers database were registered in the BVI, so behaviour shows that BVI remains an attractive location for offshore non-resident company transactions. In addition, the Forum’s standards are mainly focused on exchange of bank account information and, to a lesser extent, on who owns which company. However, they exclude indicators of other harmful tax haven practices, such as whether they publicly disclose the beneficial owners of companies and require them to practice country-by-country reporting. Finally, it does not assess harmful tax features such as offering fiscal advantages to non-residents, or low effective tax rate on corporate income taxation. The Global Forum is thus currently not well placed to seriously address corporate tax dodging and its list should not be used as the standard by which DFI investments are assessed.

#### **Information exchange – not for everyone**

The Global Forum long used the system of ‘upon request’. This standard is based on governments sending specific case-by-case requests for information about companies to each other. This system has been widely used internationally, but has also been strongly criticized for being ineffective, especially when it comes to obtaining information from countries with strong financial secrecy regulation, such as Switzerland. In many cases it has proven very difficult, and often impossible, for governments to obtain information on companies, not least because information requests often have to be very specific.

Today the Global Forum is facilitating the system of ‘Automatic Information Exchange’. However, not all countries are eligible to take part in this. In particular, developing countries are often left out, at best with the old system of information ‘upon request’.

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The European DFIs jointly agreed ‘Guidelines for Offshore Financial Centres’ in 2013.<sup>44</sup> These Guidelines are, however, non-binding; it is left to each DFI to adopt binding standards. Moreover, the Guidelines do not attempt to prevent DFIs from investing in tax havens; rather, they highlight ‘acceptable’ offshore centres that are deemed to be those that have ‘substantially implemented’ the Global Forum’s standards of transparency, among other criteria.<sup>45</sup> Thus they do little to address the concerns raised in this briefing.

**Proparco’s policy**<sup>46</sup> rests primarily on the Global Forum list and standards. However, for the jurisdictions triggered by this list the policy outlines ways to ensure due diligence also through out the investment period. However, it is not clear, how this policy enables Proparco to go beyond legal compliance and really gauge the risk of tax havens as defined broader than by the Global Forum (see box 2 and 3).

**CDC’s policy**<sup>47</sup> openly allows it to continue using tax havens, although it states that it only uses offshore financial centres to meet its priority to mobilize capital into developing countries. It argues that:

‘Offshore financial centres can provide straightforward and stable financial, judiciary and legal systems which facilitate investment. We will therefore often introduce such jurisdictions

into transactions for non-tax related purposes. This may include insulating companies from legal risk, insulating classes of security from cross-default or improving the financial terms or security for different investors. Certain investments may include structures that reduce the tax burden on investors. CDC will only acquiesce to such structures in order to facilitate a developmental impact, increasing investment and consequent job creation and economic growth.'

CDC notes that it only 'prefers' to use offshore financial centres that are successfully participating in the Global Forum and that it will not invest through a jurisdiction that does not adequately exchange tax information internationally. However, failing to comply with the Global Forum's already low standards does not appear to be mandatory. Furthermore, even if these structures are introduced for 'non-tax related' purposes, they can still have a substantial impact on the tax payments due in the country of the end investment, as CDC notes themselves that 'it may reduce the tax burden on investors'. This appears to completely fail to capture how payment of taxes is an important indicator, which can indirectly lead to development impacts through its redistribution. It appears that mobilizing capital and securing growth and investments takes precedence over supporting domestic resource mobilization.

**Swedfund** has a stronger policy, stating that it 'only invest[s] in sound and clear corporate structures not contributing to tax evasion'<sup>48</sup> and that it 'works to ensure that tax revenues are paid in the countries where portfolio companies do business'.<sup>49</sup> Swedfund is one of the few DFIs to state that 'it's not sufficient to rest on what is legal' and that tax is part of its due diligence. It adds:

'If we detect structures that mean companies in which we intend to invest will pay less tax in a country they do business in than what they should be paying, then there must be strong legitimate reasons not related to tax for us to accept such a structure... Neither may investments be made in intermediary jurisdictions which have been assessed within the framework of the OECD Global Forum Peer Review Process and that have thereby not been approved in phase one or been deemed non-compliant or partly-compliant in phase two'.<sup>50</sup>

**IFU's** tax policy<sup>51</sup>, dating from December 2015, also tackles more issues than simply relying on the Global Forum. Where it does mention that holding company structures can only be in jurisdictions that comply with OECD's Global Forum, it also notes that these 'structures must in all cases be legal, transparent and not designed to work against the spirit of the law'. The policy also notes that 'the companies in which IFU invests must at all times comply with local tax laws and pay taxes where they have their economic activity', which can be understood to support the fight against aggressive tax planning.

**FMO's** tax policy requires its clients to comply with the law but also:

'where FMO identifies an unbalanced tax situation, FMO will, within its power, take appropriate steps to assure that FMO acts according to its development goals. FMO considers an unbalanced tax situation where there is a clear situation of tax avoidance, base erosion by the tax payer or opposite, an unfair tax treatment towards the taxpayer. This will be comprehensibly determined by FMO's tax department'.<sup>52</sup>

FMO has also developed an assessment methodology called the Tax Transparency Tool 'to systematically appraise whether its clients show responsible tax behaviour'. This began only in January 2016 and its 'ultimate aim is to identify possible tax base erosion activities, which are considered problematic since they jeopardize the contribution made to local government revenues'.<sup>53</sup>

Of the multilateral development banks, the **IIC** have by far taken the most significant step in the right direction. In 2016, the IIC developed an 'Integrity Framework'<sup>54</sup>, which allows it to conduct a 'tax review' when investments that include cross-border transactions present risks, which are listed as: using complex or opaque structures, shell companies, entities in low or no-tax jurisdictions and entities in a jurisdiction that presents tax information exchange risk. The latter is assessed by ref-

erence to the jurisdictions identified by the Global Forum. The inclusion of an indicator related to ‘low or no-tax jurisdictions’ seems particularly appropriate, as it allows taking a risk-based approach to all cross-border structures with a special focus on corporate tax payments.

The **IFC**’s policy on offshore financial centres<sup>55</sup>, however, relies primarily on the Global Forum. It can exclude companies if they are domiciled in tax havens (which it calls ‘offshore financial centres’) according to the Global Forum standards. The IFC’s policy itself speaks of a commitment to ‘advancing the international tax transparency agenda’ and ‘addressing potential risks to its private sector operations’, including by ‘jurisdictions with low or no tax’. However, as the Global Forum lists appear to be the one concrete tool to screen and select projects in relation to tax practices, it is not clear how the IFC actively contributes to the tax transparency agenda or is able to capture the risk from low or no tax jurisdictions, many of which are not rated non-compliant according to the Global Forum standards.

On the other hand the IFC has a relatively strong set of environmental and social performance standards,<sup>56</sup> which its clients must adhere to. However, these standards do not cover issues related to tax payments or tax transparency, despite its significant impact on sustainable development. As recent Oxfam research argued, IFC policies need significant revision to ensure that responsible corporate tax policies – beyond legal compliance – are included in sustainability policies and development impacts.<sup>57</sup>

The **EIB** is similarly falling behind best practices. It was the first international financial institution to adopt a public policy explicitly addressing the issue of offshore financial centres, then referred to as non-cooperative jurisdictions<sup>58</sup>, but have failed to improve over time despite calls for revision. The EIB’s tax policy – first promulgated in 2010, and updated in 2014<sup>59</sup> – is largely based on the Global Forum. Counterparties located in these jurisdictions also have to disclose information on their beneficial owners, the economic rationale of the structure and the economic requirements that make the use of the jurisdictions necessary, as well as providing a description of the tax regime applicable. However, a major problem is that the EIB’s policy does not prohibit counterparties from registering in a country other than in which they are economically active and produce economic value. This implies that counterparties are still permitted to move to offshore financial centres to benefit from lower taxation and/or higher secrecy. In addition, counterparties can still operate in a prohibited jurisdiction if this jurisdiction offers a level of ‘corporate security’.<sup>60</sup> NGOs have advocated strongly for a revision of this policy and for the EIB to develop a ‘responsible tax policy’.<sup>61</sup>

The one exception to DFIs in regard to tax policies is the **AfDB**, which appears to have only an Integrity Due Diligence Policy on non-sovereign operations (IDD), but not an OFC or tax policy. The IDD promotes ‘transparency and openness in Bank operations to ensure the full disclosure of information on counterparties thereby limiting the misuse of its funds for criminal and illicit activities such as fraud, corruption, money laundering, terrorist financing, trafficking and other offenses’.<sup>62</sup> However, this has not been published and the media release accompanying the announcement noted above does not mention that the policy covers tax.

FMO, Swedfund, IIC and IFU have taken important steps to express the need to go beyond legal compliance explicitly in their policies. These are very welcome steps forward at a crucial time. For the majority of the DFIs analysed, whose policies still rely mainly on the Global Forum standard, this is a significant gap and continues to place these DFIs at the risk of allowing public funds being complicit in tax avoidance and thereby undermining domestic resource mobilization and the ability of developing countries to meet their human rights obligations by financing essential services and achieving the SDGs.

## Risk assessments on corporate tax payments

Conducting risk assessments on tax before making investments would help to ensure that investee companies are not likely to engage in tax evasion or avoidance. Continuing such tax risk and tax



impact analysis periodically as part of investee monitoring would allow for developing benchmarks in reducing the risk of tax avoidance also for those companies that pass the initial risk assessment. At the end of an investment period, one would expect that in an ex-post assessment of the tax risk would have been reduced and tax impact would have increased. Publication of this type of information is crucial to allow for scrutiny and greater accountability of the public funds channelled through DFIs.

DFIs vary in having ex-ante indicators on tax and some provide little public information on this. Many DFIs have some framework for monitoring tax payments as part of their projects but only some have indicators for measuring this ex-ante. However, simply monitoring tax payments is not equivalent to conducting a risk assessment, as one would need to analyse the likelihood that a company engages in potentially harmful tax practices or structures.

Rather the type of tax integrity framework of the IIC more significantly captures the essence of a risk assessment. The simple screening for the Global Forum list of non-compliant jurisdictions, on the other hand, does not amount to an appropriate risk assessment tool. As mentioned, the IIC's tax integrity policy provides a concrete way of screening investments that include the cross-border behaviour of TNCs and what triggers heightened due diligence. This effectively constitutes the first steps of a risk assessment, and it appears to go beyond merely asking for legal compliance, but taking a critical view on the tax impacts of cross-border activity of the client. A crucial next step is transparency of the findings and continuous monitoring and improving the policy. None of the other multilateral DFIs analysed in this research indicate any in depth risk assessment beyond legal compliance.

Of the bilateral agencies, also FMO's policy on tax base erosion screens appears to be the first step of a risk assessment that goes beyond legal compliance. It is complemented by the FMO Tax Transparency Tool, which is developed 'to systematically appraise whether its clients show responsible tax behaviour'.<sup>63</sup> These constitute significant improvements and a very welcome approach to the question of corporate tax behaviour. However, as this work is in its initial stages, limited information is available and the tool itself is not publicly available.

Swedfund states that tax is part of its due diligence and that 'prior to making an investment we check any structures in place to make sure that they are sound'.<sup>64</sup> However, referring to their ownership instructions, the concrete measures are restricted to not contributing to tax evasion (which is illegal) and screening for jurisdictions deemed non- or partially compliant by the Global Forum.<sup>65</sup> In a similar vein, does the tax policy of the IFU allude to a risk assessment beyond legal compliance screening for alignment between real economic activity and corporate tax payments, but no further information on the steps involved is publicly available.

Finally, CDC states that its ex-ante tool for measuring development impact includes assessing the payment of local taxes,<sup>66</sup> but it is not clear whether any contextual key account data is collected to screen for aggressive tax planning behaviour. It is quite clear, however, that it only screens for legal compliance and does not assess for aggressive, but legal, behaviour.

This research has not been able to locate any publicly available material outlining risk assessment efforts concerning tax planning behaviours of TNCs by IFU, the IFC, the ADB, the EIB or Proparco, beyond the policies mentioned above. From the information available it appears that CDC and Swedfund rest solely on legal compliance aspects. In order to really understand the process of how those policies are put in practice, and whether they manage to take on board practices that might be technically legally compliant, but undesirable or harmful in nature, much more information would need to be made available by these DFIs. The IIC and FMO on the other hand appear to be taking practical steps in the direction of more thorough risk assessment that goes beyond the Global Forum standard and focuses on ensuring tax payments in the beneficiary country. These are much welcome steps that other DFIs could learn from. However, a continued challenge is to ensure adequate transparency and consultation also with NGOs in the process of formulation and continued improvement and accountability of the implementation of these policies. Publishing information on

risk assessment outcomes can form a valuable part in monitoring policies effectiveness and send a strong signal to future potential clients to ensure a responsible corporate tax practice.

## Reporting on tax payments

As development institutions, DFIs should have the highest standards for reporting on the development impacts (results) of their investments. One would expect company tax payments to governments to be an obvious part of the results reported by DFIs. This means taxes paid by companies themselves, and should not include taxes paid by the employees of those companies (which some companies like to include as ‘their’ tax payments).

In 2013, 25 bilateral and multilateral DFIs, including all nine under consideration here, agreed on a set of harmonized development results indicators. These indicators include one related to tax, on ‘payment to government’. It states:

‘All transfers to the government made by [the] client company over the reporting period. At a minimum, this includes payments to the government in the form of corporate income or profit taxes. Additional forms of transfer to be reported as appropriate include (i) sales taxes, (ii) net VAT, (iii) royalties, (iv) dividends and related taxes, (v) management and/or concession fees, (vi) license fees, (vii) tax on payment of interest, and (viii) other material payments net of any direct subsidies received.’<sup>67</sup>

This means that all DFIs should be collecting information from investee companies on their tax payments. However, this does not commit them to publishing this information.

All Scandinavian DFIs include company tax contributions in their sets of indicators to measure development impact. IFU, for example, states that ‘taxes paid to host countries are an important element of the development effect of IFU’s investments. IFU annually discloses the aggregate amount of tax expenses as reported in the accounts of companies in which IFU invests.’<sup>68</sup> IFU states that it has information on taxes paid from 140 companies, which amount to a total of DKK 336m in corporate and other taxes.<sup>69</sup> IFU’s indicator framework also applies through the investment lifetime and ex-post. Monitoring tax payments continuously is an important tool to complement ex-ante assessments.

Since 2013, Swedfund has reported the taxes paid by its investee companies *by country*, but it does not break these payments down by each investee company. These tax payments cover only corporate income tax paid by the companies, not other taxes.<sup>70</sup> Swedfund states that its investee companies paid SEK 502m (2013: SEK 347m, 2012: SEK 367m) in tax in 2015.<sup>71</sup> Swedfund has dedicated considerable space in its annual report to the issue of taxes, and appear to seriously consider the usefulness of its reporting on taxes. This is a very welcome step.

Others have more basic reporting. The IFC and IIC include taxes paid in their ex-post indicators.<sup>72</sup> Tax revenues also appear to be one of the indicators that the AfDB uses to measure project performance, but it does not appear to publicly report these figures.<sup>73</sup> Proparco includes tax as an indicator when measuring its development impact and reports on it in its annual reporting on impacts.<sup>74</sup> CDC also has an indicator for tax payments and reports the results by country of operation and by sector.<sup>75</sup>

The EIB, as the only DFI found in this research, does not appear to include tax as an indicator when measuring its development impact. The EIB’s report on results, produced as part of its Results Measurement Framework, does not mention tax, for example, although it is not clear whether an indicator exists at project level.<sup>76</sup>

It is important for tax issues to be mentioned in DFIs’ annual reporting on results since this highlights the extent to which tax is being measured in policy making and how seriously it is being taken by the DFI. It also communicates the importance of tax to other DFI clients and stakeholders.

However, our research finds that DFIs barely highlight the importance of tax in their public annual reporting. In their most recent (2015) annual reports, IIC, AfDB, EIB and FMO make no mention of tax at all. Some others, such as Proparco, CDC and IFC, make brief mentions of taxes paid by their investees while IFU has little more, but only Swedfund has a significant section on its tax policy and payments.

Overall, much more could be done to rethink indicators and to communicate the importance of the contribution that the private sector makes to domestic resource mobilization in developing countries, particularly through corporate tax payments. For example, no DFI currently publicly provides a meaningful indicator of how significant these company tax payments are compared to other companies in the country or compared to the country's overall revenues from tax. Neither do any provide details of companies' effective corporate tax rates nor how these compare to the national level.

## Requirements for responsible corporate tax practice from clients

DFIs should be doing much more to encourage their investees to have responsible corporate tax policies and practices. For example, they could require each company to develop and publish its own corporate tax policy, enabling consumers and partners to be aware of this and to be able to hold the company to account. This could include company policy towards aggressive tax planning, use of tax havens, tax incentives and the use of artificial corporate structures (see Box 4). Other key elements of responsible corporate tax practice include public transparency of corporate structure, beneficial ownership and full country-by-country reporting<sup>77</sup> - these elements should also be integral parts of the DFIs risk assessments. Our research shows that currently none of the DFIs are actively requiring their clients with cross-border structures to take steps to demonstrate their responsibility in corporate tax practice.

Our research suggests that all the DFIs require their private sector clients to identify their beneficial owners as part of their screening process. Yet none of the DFIs appear to make public this information. This information can be important, particularly in relation to prevention of money laundering and tax evasion, and would allow for public scrutiny and a reality check in terms of implementation of a DFI's policy.<sup>78</sup>

If DFIs were to require their investees to publicly report their tax payments and key account data publicly on a country-by-country basis, this would enhance their tax transparency and reduce the risk of company complicity in aggressive tax planning. It would also function as a standard for responsible corporate tax practice as well as assisting in the risk assessment for the DFIs on corporate tax payments.<sup>79</sup> Some companies are already voluntarily publishing this type of data and in the European Union the finance and banking sector are required to publicly report this type of data.

The IFC and EIB collect information from their client companies on their corporate taxes paid, profits and losses and the number of employees and staffing costs. However, this is not being done on a country-by-country basis.<sup>80</sup> For example, Proparco does not require its client companies to report on a country-by-country basis, even though France's development law, adopted in 2014, requires that the Agence Française de Développement Group, which includes Proparco, should promote financial transparency on a country-by-country basis for companies operating with them.<sup>81</sup>

CDC has a 'Code of Responsible Investing', which sets out 'requirements for all businesses' in which CDC invests. However, there is only one mention of tax – companies are simply required to 'properly record, report and review financial and tax information'.<sup>82</sup> This code also recommends practices for CDC clients which include the OECD guidelines for multinational enterprises<sup>83</sup>, which has a chapter on taxation, however, this is not a requirement. FMO actually requires adherence to

these guidelines, but the chapter on taxation does not require specific activity and remains a set of recommendations.

The risk assessment tools by FMO and IIC do have elements of screening for responsible corporate behaviour beyond legal compliance. However, it is not clear if there are any specific requirements for clients in terms of taking particular steps for responsible corporate tax practice. It is clear that they do not require a publicly available responsible tax policy or publication of beneficial ownership information, corporate structure or country-by-country reporting as a pre-requisite as such, which would be the natural next step.

As mentioned IFU and Swedfund monitor tax payments by their clients, but not in a way that amounts to full country-by-country reporting or acts as a requirement for responsible corporate tax practice. Neither of them appears to have additional requirements from their clients for responsible tax behaviour.

This research has not been able to identify any among the nine DFIs that are encouraging, let alone requiring, sufficiently responsible tax practices by its investees. As a general rule, DFIs simply require investees to abide by the law in terms of reporting and transparency and do not ask them to have higher standards of transparency or reporting, despite this being so crucial for accountability of DFIs funds, showing that these are not going to tax dodgers. In addition to risk assessment, DFIs should require high standards of responsible corporate tax practice and improvements over the time of the investment to support domestic resource mobilisation and to meet the challenges related to corporate tax revenue gathering in developing countries through greater transparency.

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#### **Box 4: What is responsible corporate tax behaviour?**

Recent work by Oxfam, ActionAid and Christian Aid seeks to highlight standards regarding what constitutes ‘tax-responsibility’ on the part of companies. This includes the following processes for reducing tax risk and improving the positive impact of tax practices in developing countries, whereby the company:

- is radically and proactively transparent about its business structure and operations, its tax affairs and tax decision-making
- assesses and publicly reports the fiscal, economic and social impacts (positive and negative) of its tax-related decisions and practices in a manner that is accessible and comprehensive
- takes steps – progressively, measurably and in dialogue with its stakeholders – to improve the impact of its tax behaviour on sustainable development and on the human rights of employees, customers and citizens in the places where it does business.<sup>84</sup>

The report subsequently discusses eight thematic areas where such risk and impact assessment should take place, and proposes positive actions to improve tax practices. For instance, a tax-responsible company or group should be able to:

- show it is taking progressive steps to align its economic activities and tax liabilities
  - publicly justify its tax planning choices against the reality of its operations
  - progressively improve the international equity of its tax payments, i.e. ultimately to aim to pay a larger proportion of the group’s overall global tax bill in poorer countries, where that is consistent with transfer pricing rules and the reality of the group’s operations.<sup>85</sup>
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# RECOMMENDATIONS

The following set of recommendations contains a wide range of actions DFIs can undertake to secure more responsible corporate tax behaviour from their clients and business partners. Some are immediately implementable (and perhaps already being implemented for some), while others may only be implemented over a longer time. For all recommendations, DFIs can take the first step of acknowledging publicly the challenges related to TNCs and aggressive tax planning and their commitment towards continuously improving practices to meeting these.

## Use of tax havens

- ✓ DFIs should not use tax havens to channel their investments to developing countries. When an intermediary jurisdiction is used, DFIs should demonstrate that the use of a third jurisdiction was superior in advancing its development mandate when compared with a targeted developing country for domiciliation.
- ✓ When tax havens appear in the corporate structure of a client or partner of DFIs, heightened tax due diligence should be applied in addition to the regular requirements. DFIs should deliver an impact assessment to document that development effects are not negatively affected including documenting impacts on domestic resource mobilization.
- ✓ DFIs should ensure that these and other recommendations outlined here apply to financial intermediaries through which DFIs invest as well as investee companies and sub-clients of financial intermediaries.

## Tax behaviour of client companies

DFIs should:

- ✓ Require all clients to have and publish a responsible corporate tax policy approved by its board. The policy should be published on the company's website. This should acknowledge the important role of tax in society and commit the company to avoid engaging in harmful tax practices, including avoiding the use of tax havens.
- ✓ Require all clients to make the following elements available to the DFI risk assessment team and subsequently to be made public if eligibility for investment is granted:
  - a commitment not to practice aggressive tax planning, and to engage in tax risk and tax impact assessment in key identified areas;
  - country-by-country information on the turnover, assets, full-time employees, profits and tax payments in each country in which it operates;
  - information about beneficial ownership and company structure and purpose;
  - all discretionary tax treatment they receive that affects the tax base or taxable profits, including tax incentives, any tax planning schemes that are under mandatory notification (e.g. UK DOTAS) in any country where the company operates, advance pricing agreements or advance tax rulings that substantially affect either the tax base or taxable profits;
  - tax risk and tax impact assessment in their analysis of challenges to domestic resource mobilization to prevent aggressive tax planning, irresponsible tax behaviour as well as its potential for negative impact on human rights.
- ✓ Ensure that these and other recommendations outlined here apply to financial intermediaries through which DFIs invest, as well as investee companies and sub-clients of financial intermediaries.

## Transparency and reporting

DFIs should:

- ✓ Develop, in consultation with CSOs, and publish a tax-responsible investment policy, which includes a commitment to promote domestic resource mobilization and responsible corporate tax behaviour. Once adopted, this should be applied to existing as well as new investments.
- ✓ Publish a full list of investments that includes: (a) the investee companies (and sub-clients of financial intermediaries); (b) their countries of incorporation; (c) their corporate structure; and (d) their beneficial owners.
- ✓ Publish figures on what proportion of the DFI's portfolio goes to: (a) transnational corporations (including through) financial intermediaries; and (b) SMEs.
- ✓ Giving the reporting on tax payments a prominent place in annual reports, and/or developing a separate tax responsibility report, including analysis of their development impacts.
- ✓ Reporting the tax payments of investee clients and each investment's expected and actual tax payments and asking companies to explain deviations in relation to economic activities.
- ✓ Engaging openly and in a transparent manner with stakeholders on tax issues and tax impacts of its investments. This could include assessing and reporting on the impacts of tax practice, assessing whether value creation corresponds to economic reality, how to prevent and mitigate potential negative impacts, and tracking performance and communicating on this.

## Measuring development

DFIs should:

- ✓ Include tax in the development indicators and explain how they are measured, and what importance is attached to tax indicators in relation to other indicators for development.
- ✓ When evaluating projects ex-ante, periodically and ex-post, include corporate tax payments as a separate indicator in addition to total payments to governments. Measure tax risk and impact based on key themes where practices have the greatest impact on revenue, human rights and good governance. Measure tax payments in absolute numbers and relative to the investment.

## Internal issues

DFIs should:

- ✓ Devote sufficient resources to develop optimal policies and implement best practice.
- ✓ Enable full transparency toward and constructive engagement with CSOs on new policies and evaluation of existing policies.
- ✓ Ensure in-house capacity to oversee these activities to ensure there is no dependency on external advisers, who might have a conflict of interest. This could include hiring capacity to look at taxes beyond legal compliance and to improve engagement of staff to help contribute to sustainable development and human rights.



# NOTES

<sup>1</sup> See, for example, CONCORD, 2015, *Spotlight report 2015 policy paper: the role of the EU in ensuring global tax justice* <http://library.concordeurope.org/record/1632/files/DEEEP-PAPER-2016-001.pdf>

<sup>2</sup> Eurodad, *Going Offshore: How Development Finance Institutions Support Companies Using the World's Most Secretive Financial Centres*, 2014, p.8, <http://www.eurodad.org/files/pdf/5457b8e273cfa.pdf>

<sup>3</sup> IBIS, 'Scandinavian Development Financial Institutions: Leading the way on responsible taxation?', *IBIS Briefing*, November 2014, p.1, [http://thetaxdialogue.org/sites/default/files/media/pdf\\_global/the\\_tax\\_dialogue\\_pdf/ibis\\_briefing\\_scandinavian\\_dfis\\_and\\_responsible\\_tax.pdf](http://thetaxdialogue.org/sites/default/files/media/pdf_global/the_tax_dialogue_pdf/ibis_briefing_scandinavian_dfis_and_responsible_tax.pdf)

<sup>4</sup> Eurodad, *Going Offshore: How Development Finance Institutions Support Companies Using the World's Most Secretive Financial Centres*, 2014, p.8, <http://www.eurodad.org/files/pdf/5457b8e273cfa.pdf>

<sup>5</sup> Homepage, <http://edfi.be/>

<sup>6</sup> Eurodad, *A Private Affair: Shining a light on the shadowy institutions giving public support to private companies and taking over the development agenda*, 2014, p.11, <http://www.eurodad.org/files/pdf/1546237-a-private-affair-shining-a-light-on-the-shadowy-institutions-giving-public-support-to-private-companies-and-taking-over-the-development-agenda.pdf>

<sup>7</sup> Oxfam, *Owning the Outcomes: Time to Make the World Bank Group's Financial Intermediary Investments More Accountable*, October 2015, p.2, [https://www.oxfam.org/sites/www.oxfam.org/files/file\\_attachments/bn-ifc-owning-outcomes-031016-en\\_0.pdf](https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/bn-ifc-owning-outcomes-031016-en_0.pdf)

<sup>8</sup> See [https://www.oxfam.org/sites/www.oxfam.org/files/file\\_attachments/ib-suffering-of-others-international-finance-corporation-020415-en.pdf](https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/ib-suffering-of-others-international-finance-corporation-020415-en.pdf) and <http://www.inclusivedevelopment.net/wp-content/uploads/2016/09/Outsourcing-Development-Introduction.pdf>

<sup>9</sup> IBIS, *Development Finance Institutions and the Responsible Tax Agenda: Fit for Purpose?*, 2015, p.7, [http://thetaxdialogue.org/sites/default/files/media/pdf\\_global/the\\_tax\\_dialogue\\_pdf/dfi\\_brief\\_final.pdf](http://thetaxdialogue.org/sites/default/files/media/pdf_global/the_tax_dialogue_pdf/dfi_brief_final.pdf)

<sup>10</sup> See more on this debate here: [https://www.actionaid.org.uk/sites/default/files/delivering\\_sustainable\\_development.pdf](https://www.actionaid.org.uk/sites/default/files/delivering_sustainable_development.pdf)

<sup>11</sup> See [https://www.oxfam.org/sites/www.oxfam.org/files/file\\_attachments/ib-suffering-of-others-international-finance-corporation-020415-en.pdf](https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/ib-suffering-of-others-international-finance-corporation-020415-en.pdf) and <http://www.inclusivedevelopment.net/wp-content/uploads/2016/09/Outsourcing-Development-Introduction.pdf>

<sup>12</sup> UNCTAD, *World Investment Report 2015*, p.200, [http://unctad.org/en/PublicationsLibrary/wir2015\\_en.pdf](http://unctad.org/en/PublicationsLibrary/wir2015_en.pdf)

<sup>13</sup> Oxfam, *An Economy for the 1%*, 2016, <http://oxf.am/Znhx>

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<sup>28</sup> IFU's portfolio is not currently listed on its website, which says that this is 'currently unavailable' (<http://www.ifu.dk/en/investments/portfolio>). In the past, however, IFU has disclosed the domiciles of the funds in which it has invested and in some cases direct investment domiciles. Eurodad, *Going Offshore: How Development Finance Institutions Support Companies Using the World's Most Secretive Financial Centres*, 2014, p.16, <http://www.eurodad.org/files/pdf/5457b8e273cfa.pdf>

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<sup>31</sup> Frontier PE (Cayman) LP, <http://www.cdcgroup.com/What-we-do/Our-Investments/>; Gulf Resources, [http://www.gulfresourcesinc.com/images/pdf/e613413\\_10k\\_gulf\\_rev5.pdf](http://www.gulfresourcesinc.com/images/pdf/e613413_10k_gulf_rev5.pdf)

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<sup>36</sup> See more on <http://www.financialsecrecyindex.com/>

<sup>37</sup> Eurodad, *Going Offshore: How Development Finance Institutions Support Companies Using the World's Most Secretive Financial Centres*, 2014, p.4, <http://www.eurodad.org/files/pdf/5457b8e273cfa.pdf>

<sup>38</sup> Eurodad, *Going Offshore: How Development Finance Institutions Support Companies Using the World's Most Secretive Financial Centres*, 2014, p.10, <http://www.eurodad.org/files/pdf/5457b8e273cfa.pdf>

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[http://www.cdcgroup.com/Documents/Country%20by%20Country%20information%20\(31.12.15\).pdf](http://www.cdcgroup.com/Documents/Country%20by%20Country%20information%20(31.12.15).pdf) and by sector here

[http://www.cdcgroup.com/Documents/Sector%20by%20Sector%20information%20\(31.12.15\).pdf](http://www.cdcgroup.com/Documents/Sector%20by%20Sector%20information%20(31.12.15).pdf)

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