THE BUSINESS'S COMMERCIAL SUCCESS SUBSTANTIALLY DEPENDS UPON:

RED FLAG NO.

24

RED FLAGS IN THE COST STRUCTURE AND THE REVENUE MODEL

Aggressive strategies to minimize taxation, particularly with respect to operations in developing countries.

HIGH-LEVEL DECISION-MAKING

RISK TO PEOPLE

RISK TO THE BUSINESS

UNGPs & SGDs ANALYSIS

TAKING ACTION

Such as: Undue use of the following such that governments may be deprived of the resources needed to address poverty and to finance programs seeking to protect and fulfil rights:

- transfer (mis-)pricing
- negotiation of tax holidays
- (non-)taxation of natural resources
- offshore investment accounts

HIGHER-RISK SECTORS:

- Tech industry and other highly digitized business models
- Extractive industry in the context of natural resource acquisition and use
- Various industries with operations in countries that are particularly vulnerable to the consequences of low revenue from taxes

KEY QUESTIONS FOR LEADERS TO ASK OR BE ASKED:

- How does the company assess whether its taxation strategy is aligned with, and not undermining, its responsibilities and commitments to respect human rights?
- Does the company publish a tax strategy? Does it disclose the entities it owns, its overall tax rate and the taxes paid where it does business?
- Has the company endorsed the B Team's Responsible Tax Principles?

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RISKS TO PEOPLE

- The International Bar Association's Human Rights Institute (IBA-HRI) found that in the context of the developing world, tax practices considered most relevant to potential human rights impacts include transfer-pricing and other cross-border intra-group transactions (see Lipsett). Multi-national enterprises may "take advantage of gaps in the interaction of different tax systems to artificially reduce taxable income or shift profits to low-tax jurisdictions in which little or no economic activity is performed" (see OECD). The Task Force also identified the following as areas of greatest concern: the negotiation of tax holidays and incentives, the taxation of natural resources, the use of offshore investment accounts and, finally, secrecy jurisdictions due to their role in facilitating tax abuses. (See Lipsett).

- Highly digitized business models have been associated with challenges to existing taxation frameworks, including where the business is highly involved in the economic life of a jurisdiction without any significant physical presence, as well as where a high number of assets are intangible (such as algorithms and software). (See OECD).

- Aggressive taxation practices such as those identified above can "deprive governments of the resources required to provide the programmes that give effect to economic, social and cultural rights, and to create and strengthen the institutions that uphold civil and political rights." (See Lipsett). Lost revenue from taxation can lead to decreased funds available for spending on "services such as health, education, housing, access to water and other human rights." It has been noted that countries in the global south lose much more money to tax evasion and illicit financial flows than they receive in international aid.

- The connection between tax and **inequality** has been explored by the IBA-HRI, which has noted that "the global shadow economy is contributing to a growth in global inequality, which is also having a major impact on democracy."

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RISKS TO THE BUSINESS

- **Reputational Risks:** "Over recent years, the tax affairs of major businesses have been subject to unprecedented levels of scrutiny, debate and controversy." The FT, has noted that despite the "dry, complex nature of corporate tax planning," campaigners have begun to focus on the issues with "zeal."

- **Regulatory Risks:** Concerns over the facilitation of base erosion and profit shifting through uneven legislation has led to a multilateral international tax policy initiative under the OECD, resulting in a multilateral convention, the sharing of information between tax administrations, disclosure of previously secret tax rulings and "legislative changes made to amend/abolish 110+ ['harmful preferential tax regimes']."

- **Operational Risks:** Public outcry over taxation inequality has "contributed to significant political instability in many developing countries" which has also been to the detriment of companies operating in these areas. Such outcry has not been limited to developing countries: in the UK several companies have appeared before the Public Accounts Committee or had their high street stores occupied by protestors, and US companies have been the subject of major news investigations.

- **Legal, Financial and Operational:** Risks also arise where public outcry leads to a re-examination of tax settlements. Calvert Investments, referencing the International Accounting Standards Board, has noted: "Reputational damage [from a perception that a company is not paying its fair share of tax to a host country] may lead to liabilities for external costs associated with a company's operations, greater difficulty in permitting that could lead to project delays or cancellation or the loss of favourable tax status or other forms of government financial assistance."

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WHAT THE UN GUIDING PRINCIPLES SAY:

**For an explanation of how companies can be involved in human rights impacts, and their related responsibilities, see here.*

- The "corporate responsibility to respect," the second pillar of the UNGPs, "exists independently of States' abilities and/or willingness to fulfil their own human rights obligations, and … exists over and above compliance with national laws and regulations protecting human rights." (Principle 11, Commentary). In other words, "all business enterprises have the same responsibility to respect human rights wherever they operate" (Principle 23, Commentary), whether or not they have a domestic legal obligation to do so. As such, undue or aggressive use of taxation strategies may infringe companies' responsibility **even where actions are legal under local taxation laws**.

- The UNGPs note that companies should "strive for coherence between their responsibility to respect human rights and policies and procedures that govern their wider business activities …" (Principle 16, Commentary), which would be relevant where aggressive tax strategies undermine efforts to respect rights in jurisdictions of operation.

- Where a company is benefiting from an unduly aggressive tax strategy or unusually generous taxation deal in a particular location, it may be **directly linked** to impacts that result from a lack of public services for local populations. Where it is aware of this situation and does nothing, it may be judged to **contribute** to such impacts. This may be a contribution in parallel with other companies benefiting from similar tax arrangements, such that they collectively deplete state revenues needed to fulfil people's human rights. If the company lobbies in favor of tax deals that undercut state revenues with similar results, it may be seen as contributing by incentivizing the government to favor corporate benefits over the human rights of the population.

- The connection between taxation planning and human rights is complex, but receiving increased attention. Mauricio Lazala, Deputy Director of the Business and Human Rights Resource Centre has noted that "[t]he State duty to protect human rights in its corporate tax policies, the business responsibility to respect human rights and carry out due diligence in their tax practices, and the need for effective remedy for tax abuse are all relevant, yet still emerging dimensions of the UN Guiding Principles on Business and Human Rights."

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POSSIBLE CONTRIBUTIONS TO THE SDGS:

Taxation policy is a key element in facilitating the achievement of the SDGs. As such, this red flag indicator is relevant for a range of SDGs, including:

1 NO POVERTY

SDG 1: No Poverty, including

- **Target 1.2:** By 2030, reduce at least by half the proportion of men, women and children of all ages living in poverty in all its dimensions according to national definitions
  - The IBA-HRI has noted that "greater tax revenues have the potential to reduce poverty, provided that they are properly spent on programmes that contribute to infrastructure, development and human rights." (See IBA-HRI p.89).

10 REDUCED INEQUALITIES

SDG 10: Reduced Inequalities, in particular

- **Target 10.4:** Adopt policies, especially fiscal, wage and social protection policies, and progressively achieve greater equality. Income redistribution through taxation can contribute to reducing inequality and promoting inclusive growth.

17 PARTNERSHIPS FOR THE GOALS

SDG 17: Partnerships for the Goals, in particular

- **Target 17.1:** Strengthen domestic resource mobilization, including through international support to developing countries, to improve domestic capacity for tax and other revenue collection.

Shift

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DUE DILIGENCE LINES OF INQUIRY:

- Do we have a policy on tax planning that includes a human rights perspective? Do we have a considered and disclosed position on use of "tax havens"?
- How transparent are we about our taxation strategy including as regards our operations in developing countries? Do we disclose how our approach to taxation planning aligns with our business purpose and sustainability strategy?
- To what extent do we review the structures and practices of tax planning through the lens of our responsibility respect human rights, (rather than merely the **amount** of tax paid, which is an outcome of these practices).
- Are we involved in projects for which tax rules are being created? Is our approach to these negotiations aligned with our sustainability commitments/ responsibilities?
- How meaningful is the interaction between our departments and external advisors responsible for taxation strategy and our corporate responsibility/ sustainability/human rights teams, with a view to internal alignment?

MITIGATION EXAMPLES:

**Mitigation examples are current or historical examples for reference, but do not offer insight into their relative maturity or effectiveness.*

- **Allianz** states that it "seeks to be a responsible tax payer... Our attitude is that tax planning is not a goal in itself, but should be undertaken to support the business strategy while being both tax-efficient and legally compliant." (*Ralf Chalupnik, Director of Tax Policy, Allianz,* in B Team: "A New Bar for Responsible Tax"). The company reports that it does "not engage in aggressive tax planning or artificial structuring that lacks business purpose or economic substance," does not use tax havens and "refrain[s] from discretionary tax arrangements." Allianz has a comprehensive "Standard for Tax Management" which requires that tax planning be based on valid business reasons.
- **Unilever** reports on its "total tax rate" in its annual report "which they see as a key indicator that they pay tax on 100% of their profits aligned to the countries where they do business." **Vodafone** has published an annual tax report setting out their total contribution to public finances, country-by-country, on an actual cash-paid basis, since 2013; **Maersk** began to include taxation in their sustainability report in 2016 and have conducted a gap analysis against the B Team Responsible Tax Principles, aiming for implementation in 2020. (From B Team: "A New Bar for Responsible Tax")
- The Extractive Industries Transparency Initiative (EITI) is a coalition of governments, companies and civil society working "*to improve openness and accountable management of revenues from natural resources*."

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ALTERNATIVE MODELS:

- In 2012 **Starbucks** announced that following "loud and clear" messages from customers, the company would make "changes which will result in Starbucks paying higher corporation tax in the UK – above what is currently required by law".

OTHER TOOLS AND RESOURCES:

- The B Team's *Responsible Tax Principles* were developed through dialogue with a group of leading companies, convened by The B Team with contributions from civil society, institutional investors and international institution representatives.
- The International Bar Association's Human Rights Institute released a 2013 report entitled Tax Abuses, Poverty and Human Rights. The Report addresses tax abuses from the novel perspective of human rights law and policy. It is based on extensive consultation from diverse perspectives and offers insight into the links between tax abuses, poverty and human rights.
- The Business and Human Rights Resource Centre portal on Tax Avoidance.
- Oxfam (2017) *Making Tax Vanish: How the practices of consumer goods MNC RB show that the international tax system is broken*. Contains an in-depth analysis and critique of the taxation planning practices of one company as well as the company's response.
- M Lazala, Business & Human Rights Resource Centre (2015) *Tax avoidance: the missing link in business & human rights?*
- Tax Justice Network is a UK-based international research and advocacy network focusing on the link between taxation and, inter alia, human rights. It publishes the Corporate Tax Haven Index.
- OECD (2019) *Tax and Digitalization* discusses the tax challenges that arise from digitalization in furtherance of a work program to culminate in 2020 with an agreed global, long-term solution.
- The OECD's Tax portal includes its Action Plan on Base Erosion and Profit Shifting and Inclusive Framework.

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