committee on workers' capital

research briefing

Investor Brief on Tax Evasion and Avoidance

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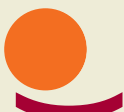

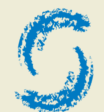

About the CWC:
The Global Unions Committee on Workers' Capital, established in 1999, is a joint initiative by the International Trade Union Confederation (ITUC), the Trade Union Advisory Committee to the OECD (TUAC) and the Global Union Federations.

Why it matters for long term investors

The series of tax evasion scandals – UBS, HSBC, 'offshoreleaks' among others – concerns about the aggressive tax planning schemes by some multinational enterprises (MNEs) – Amazon, Google, the 'Luxleaks' scandal – as well as public concern about the low effective tax rate of some MNEs, are dire reminders that much must still be achieved to effectively put an end to tax evasion and "aggressive" tax planning worldwide. Civil society groups have been doing their part to keep the spotlight on tax evasion, including the Tax Justice Network and individual NGOs such as ActionAid, Oxfam, the French CCFD, Brussels-based EURODAD and the Washington-based Global Financial Integrity. Public sector trade unions have also been very active, including the European EPSU and, at the global level, the PSI.

Governments have started to take action. At the international level, the G20 countries, accounting for 80% of world GDP, adopted an Action Plan in October 2015 to eliminate Base Erosion and Profit Shifting (BEPS) tax practices by MNEs. The Action Plan, which is the outcome of a two-year negotiation process, represents to most far reaching attempt in modern history to reform the global tax system and the taxation of MNEs in particular. In Europe, the European Commission has revived discussion on a Common Consolidated Corporate Tax Base and has taken action along the lines of the BEPS Action Plan.

The emerging international consensus to curb aggressive tax planning by MNEs is welcome, but needs to be followed by effective action and implementation. It would also require the active participation and support in the market place and among all corporate stakeholders, including investors.
Despite the visibility of tax issues in the international forums such as the G20, there is still a lot of caution among institutional investors on the subject. The notion of "responsible tax practices" has yet to make inroads in the

responsible investment world. However, there is a rising interest in the topic. In March 2015 the UK Local Authority Pension Fund Forum (LAPFF) launched a Corporate Tax Transparency Initiative and sent a questionnaire to all FTSE100 companies with technical questions on their respective taxation and governance policies. For its parts, in November 2014 the ITUC and the TUAC helped coordinate a Global Union Call for Action for Pension Fund Responsible Tax Practices[2].

Tax evasion and tax avoidance in figures

Measuring the impact of tax evasion is a challenging task. However, official statistics on current accounts and on foreign direct investment (FDI) stocks and flows reveal some surprising figures:

- With less than 30 000 inhabitants (but with more than 40000 registered trusts), the British Virgin Islands (BVI) are the second largest "investor" in China, while Mauritius is the top investor in India. Cyprus, BVI, Bermuda and the Bahamas are among the top five investors into Russia;
- In 2012, the Netherlands attracted more foreign direct investment (FDI) from Bermuda (64,000 inhabitants), Curaçao (150,000) and Cayman Islands (56,000) combined than from the entire Nordic countries (Denmark, Norway, Sweden, Finland and Iceland)[3]. Of the total USD3.5tr in FDI in 2012, just USD573bn ended up in the real Dutch economy, while Luxembourg booked USD2.28tn in FDI but just USD122bn entered the real economy[4];
- According to calculations by Oxfam, when taking into account the use of empty shell companies abroad, Spain becomes the second largest "foreign" investor in Spain[5].

The measurement of the effective tax rate (ETR) of MNEs (as opposed to the nominal tax rate) is another indication of the size of the problem:

- According to a joint report by UnitedVoice & the Tax Justice Network, the effective tax rate of Australian ASX 200 companies over the last decade is 23%, below the statutory rate of 30% and nearly one third of companies have an average effective tax rate of 10% or less. The report also shows that 57% of ASX companies have subsidiaries in secrecy jurisdictions (as defined by the Tax Justice Network) and 60% report debt levels in excess of 75%, which may artificially reduce taxable profits[6];
- According to a trade union report prepared by EPSU, EFFAT and the SEIU, with only 13 employees, between 2009 and 2013, McD Europe Franchising Sarl (Mc Donald's Luxembourg entity) made €3.7bn in revenues and paid €13m in taxes[7];

According to OECD estimates released as part of the final BEPS packages of October 2015[8]:

- Between 2007 and 2011, reported profit rates of MNE affiliates in lower-tax countries were, on average, almost twice as high as their group's worldwide profit rate;
- Between 2000 and 2010, the ETRs for large MNE entities (with more than 250 employees) was estimated to be between 2.7 to 4.5 percentage points lower than similar non-MNE ETRs;

For the OECD aggressive corporate tax planning "affects everyone"

"Globalisation has opened up opportunities for MNEs to greatly reduce the taxes they pay. The use of legal arrangements that make profits disappear for tax purposes or allow profits to be artificially shifted to low or no-tax locations is referred to as Base Erosion and Profit Shifting (BEPS). (...) BEPS affects everyone. It harms governments because it reduces their tax revenues and raises the cost of ensuring compliance. It harms people because, when some MNEs pay low or no tax, individual taxpayers must shoulder a greater share of the tax burden. And finally it harms businesses themselves: MNEs face significant reputational risk from the public focus on their tax affairs while domestic companies face an uneven playing field when competing with multinationals". OECD statement on the release of the final package of the G20/OECD BEPS Action Plan, 5 October 2015[1]

Tax planning and business restructuring, what is the impact on workers?

Tax avoidance harms government finance and the right to public services through the net loss in tax revenues. But it also directly affects workers' rights. The Trade Union Advisory Committee to the OECD has held regular meetings on corporate tax planning and its impact on workers[10]. Trade union experience shows that aggressive tax planning is just another form of corporate "regulatory planning" with short termist goals. For example, abusive transfer pricing typically reduces profit levels in subsidiaries that are employment intensive. When a business restructuring for tax planning purpose splits a single company into separate entities, workers' access to important company information is reduced. A trade unionist of the French subsidiary of Colgate captured why tax planning matters for trade union action: "the farther you are from where tax is being declared within the MNE group structure, the higher the risk for worker misery". For trade unions, aggressive tax planning and tax evasion schemes are manifestations of corporate short-termist behaviour that harms the interest of the company and its stakeholders.

- Overall, revenue losses from BEPS are conservatively estimated at USD 100-240 billion annually, or anywhere from 4-10% of global corporate income tax;

Investor risks

Aggressive tax planning and tax evasion practices may increase profits – and hence shareholder returns – on the short term. But these corporate practices are detrimental to the interest of the company, its stakeholders, and the broader economic environment, because of multiple forms of risk that they generate.

Company-specific risks:

- *Corporate governance and transparency risk:* Investors rely on sound corporate accountability at every step of the investment chain. Aggressive tax planning implies a lack of transparency for institutional investors and a greater risk of corporate wrongdoing.
- *Government relations and litigation risk:* Governments are no longer taking a passive view on aggressive tax planning. Companies who engage in such behaviour risk exorbitant legal fees to respond to tax compliance audits and the loss of lucrative government contracts.
- *Reputational damage:* Aggressive tax planning and tax evasion may harm a company's reputation with its customers and the public. This risk to a company's brand names may be particularly acute for retail and consumer product companies.

Economy-wide risks:

- *Impact on availability and quality of public services and infrastructure:* tax evasion and planning contribute to the gradual reduction in the traditional sources of finance for public services, health, education, and social security – a problem that has become exacerbated in times of public budget constraints. Tax revenues are essential to the entire macroeconomic system as they provide for crucial government spending and investment;
- *Impact on market competition:* tax avoidance and evasion practices lead to unfair competition in the private sector, between MNEs and the rest of the economy. As noted above, the effective tax rate of large MNEs has been estimated to be on average 5% lower than that of comparable domestic companies;
- *Impact on public governance and rule of law:* tax evasion practices may contribute to a broader institutional environment that is conducive to weak rule of law, corruption, and organised crime – particularly in developing countries;
- *Impact on society:* compliance is also important for upholding human rights in countries of operation. For the International Bar Association, "tax abuses – defined as practices contrary to the letter or spirit of global or national tax laws and policies – have a significantly negative impact on the human rights of those living in developing countries, by depriving governments of the resources they require to alleviate poverty"[9].

Tax evasion versus tax avoidance

A primary distinction needs to be made between aggressive tax planning (tax avoidance) and tax evasion. While tax evasion is by definition illegal, tax avoidance is by definition the use of legal means to reduce tax liabilities. The following table explains the main differences between the two and how to deal with them. To give a practical example, the "offshoreleaks" and "Swissleaks" scandals involve pure tax evasion issues, while the "Luxleaks" scandal (involving secret deals, called "rulings", between tax authorities and MNEs on an individual base) is a case of tax avoidance.

Tax evasion

Combatting tax evasion by MNEs requires greater information sharing between tax authorities. There are several international forums and initiatives which aim is promote tax transparency within the corporate and financial sector and between tax authorities. At the international level, the authoritative body is the Global Forum on Transparency and Exchange of Information for Tax Purposes. At the regional level, the European Commission published a list of 30 "non-cooperative jurisdictions" in June 2015[11]. On NGO side, the Tax Justice Network has produced a rating system, the Tax Secrecy Index[12].

The Global Forum on Tax Transparency

The main international initiative to curb tax evasion is the OECD-hosted Global Forum on Transparency and Exchange of Information for Tax Purposes, with 127 member countries13. At the request of the G20, the Forum previously published a "grey list" and "black list" of "non-cooperative jurisdictions." This mechanism had positive effects… perhaps "too" positive. The number of countries on the "grey list" fell from 44 in 2009 to 5 in 2011), while the black list – which included 4 countries in 2009 – was emptied during that period. After 2009 however, the Forum replaced this "naming and shaming" technique with a peer review[14] system against a "standard" for tax transparency. This standard covers 10 elements and is grouped in three categories:

- A: Availability of information, including access to beneficial ownership, record keeping of banking & accounting information;
- B: Access to information, including granting authorities enforcement power;
- C: Exchange mechanisms, including a minimum of 12 bilateral agreements covering "relevant economic partner" countries.

The Forum's peer review process consists of two consecutive phases: legal compliance with the standard (Phase 1) and its effective implementation through enforcement and practices (Phase 2). The Countries are "rated" accordingly: fully compliant, partially compliant, or non-compliant. According to the Forum annual report,

TABLE 1 DISTINCTION BETWEEN TAX EVASION & AVOIDANCE

	Tax evasion	Aggressive tax planning & tax avoidance
Legal compliance	Illegal	Legal
Problem	Opacity of information on tax; Non-cooperative jurisdictions	Inadequate & "outdated" tax regulation; Mismatch between jurisdictions
High profile scandals	"Offshoreleaks" and "Swissleaks"	"Luxleaks"
Policy issue	Tax transparency; Automatic exchange of information between tax authorities	Tax treatment of transfer pricing, debt, foreign operations, etc. International harmonisation
Key international forum & agenda	The Global Forum peer review process, OECD Standard for automatic exchange of information	G20/ OECD BEPS action plan

TABLE 2 LIST OF TAX JURISDICTIONS AT-RISK

		Included in the EU list of tax havens (June 20125)	Not included in the EU list, but with a TJN secrecy score of 65 or above (November 2015)	TJN Secrecy Score below 65 or not rated by the TJN
Status of the Global Forum peer review (October 2015):	Phase 1 failed because of "serious deficiencies in the legal framework"	Liberia (83), Nauru (79), Vanuatu (87)	Guatemala (76), Lebanon (79),	Kazakhstan (n.a.), Micronesia (n.a.), Trinidad & Tobago (n.a.)
	Phase 1 successful, but not compliant with A1 criteria (beneficial ownership)	Marshall Islands (79)	Dominican Republic (65-73), Switzerland (73)	Mauritania (n.a.), Morocco (n.a.), Romania (n.a.)
	Phase 1 successful	Brunei (83), Panama (72), Niue (n.a.)	Botswana (71), Dominica (76),	
	Partially compliant (Phase1&2)	Antigua & Barbuda (81), Andorra (77), Anguilla (69), Barbados (78)	Curacao (68), Samoa (86)	Costa Rica (55), Indonesia (n.a.), Israel (53), St Maarten (n.a.), Turkey (64)
	Largely compliant (Phase1&2)	Bahamas (70), Belize (79), Bermuda (66), British Virgin Islands (60), Cayman Islands (65), Cook Islands (76), Grenada (76), Guernsey (64), Hong Kong (72), Liechtenstein (76), Mauritius (72), Monaco (74), Montserrat (67), St Kitts & Nevis (78), St Vincent & Grenadines (78), The Seychelles (71), Turks & Caicos (71)	Aruba (68), Bahrain (74), Ghana (67), Malaysia (75), Gibraltar (67) Jersey (65), Macao (70), St Lucia (83), San Marino (80), Singapore (69), Uruguay (71)	
Not reviewed by the Forum		Maldives (76-84), US Virgin Islands (69)	Bolivia (72-80), Gambia (73-81), Macedonia (66), Paraguay (75-83), Tanzania (73-81), Taiwan (67-75), Venezuela (64-72)	

jurisdictions' compliance with the standard is "generally high". Over 80% of jurisdictions are considered fully compliant or "largely compliant" with the standard. However, when looking at the compliance rating for each of the three categories, some serious differences emerge. In particular less than 50% of the rated jurisdictions scored a "fully compliant" rating regarding "availability of ownership information" (category A).

Although the Global Forum no longer produces an official list of "tax havens", its peer review rating process provides some indication of countries where tax opacity remains of concern, including jurisdictions that (i) failed the Phase 1 review because of "serious deficiencies in the legal framework" and therefore "cannot move to Phase 2", or (ii) are rated as non-compliant after having completed both Phase 1 & 2. Countries that pass Phase 1 successfully but are non-compliant with the Standard's A1 criteria (access to beneficial ownership) should also be treated with concern.

The European Commission list and the Tax Justice Network Secrecy Index

In June 2015, the European Commission published its first list of 30 non-cooperative jurisdictions as part of a new Action Plan for Fair and Efficient Corporate Taxation in the EU[15]. This list does not consist of a comprehensive assessment, but rather a compilation of the countries listed on at least 10 of the national tax haven lists submitted by EU member countries.

The Tax Justice Network (TJN) "Financial Secrecy Index" rates jurisdictions based on their lack of transparency but also their scale of activities. This index gives a quantitative "secrecy score" from 1 to 100 which is based on 15 secrecy indicators[16] where 100 represents maximum secrecy. A score of 65 or above qualifies the country as a secrecy jurisdiction. Secrecy scores are then weighted based on the share of the financial services industry in order to calculate an overall financial secrecy ranking. The top ten ranking of the 2015 results is:

1. Switzerland;
2. Hong Kong;
3. USA;
4. Singapore;
5. Cayman Islands;
6. Luxembourg;
7. Lebanon;
8. Germany;
9. Bahrain;
10. United Arab Emirates (Dubai).

Based on different combinations between the outcome of the Global Forum rating process (update October 2015), the EU list (June 2015) and the TJN Secrecy Score (November 2015), Table 2 identifies the jurisdictions where tax opacity remains of concern – hence "tax jurisdictions at-risk".

Aggressive tax planning

Unlike tax evasion – which is illegal – tax avoidance is by definition the use of legal means to reduce the amount of tax that is payable. Aggressive tax planning strategies include various accounting and financial transactions that aim at (i) artificially reducing the taxable income base of the company and/or (ii) moving profits away from economically relevant (but high tax) jurisdictions to economically irrelevant (but low-tax) jurisdictions. An example is the "Double Irish": the legal ownership – and the allocation of revenues – of an intangible asset created in country A (say, in Palo Alto, California) is domiciled in an empty shell company in an unrelated country B (Ireland).

The G20/ OECD BEPS Action Plan

The OECD Action Plan on Base Erosion and Profit Sharing (BEPS) is the primary initiative at the international level to counter tax avoidance and aggressive tax planning[17]. The deliverables of the Action Plan agreed to in October 2015 includes 15 action points, covering the most common forms of aggressive tax planning techniques such as:

- *Transfer pricing*, most frequent case of tax avoidance. For example a subsidiary of an MNE (typically located in a high tax jurisdiction) is charged well above market value for spare parts provided by another subsidiary (located in a low tax jurisdiction);
- *Artificial allocation of debt services, of intangibles and of other profitable risk-related assets* to low-tax jurisdictions and away from economically relevant jurisdictions.
- *Exploiting "treaty shopping"* (and treaty abuse) whereby an MNE uses an empty shell company to unduly access the tax benefits of a bilateral tax treaty (i.e. the "Dutch sandwich");
- *Exploiting "hybrid mismatches"* between two or more jurisdictions with regard to the tax treatment of debt and equity (for example the USD700m tax evasion schemes set up by Barclays and KPMG between 2002 and 2007 under a US-based scheme called "STARS");
- *Avoiding "permanent establishment"* status for local economic activities and hence escaping paying corporate income tax locally;
- *Benefiting from government "harmful tax practices"* to shift income away from economically relevant jurisdictions such as aggressive tax incentives to attract foreign investors (i.e. "patent box" regimes) and the secretive "rulings" between a tax authority and an individual MNE (i.e. the "Luxleaks" scandals, and the tax deal between Apple Inc. and the Irish tax authorities);

Country-by-country reporting framework

A key achievement of the BEPS Action Plan is the agreement on a new country-by-country reporting framework[18]. From 2016 onward, MNEs with annual revenues equivalent to USD750m or above will have to report on 8 items: revenue, profit (or losses), income tax paid (on cash basis), income tax accrued, capital, accumulated earnings, number of employees, and

tangible assets (other than cash). In addition, MNEs are to report the business activities of each corporate entity located in each country (e.g. manufacturing, sales, marketing, R&D, financial, etc.). OECD experts had initially considered a more comprehensive reporting framework (also including: employee remuneration, royalties, interest, service fees). The list was cut down following pressure by business groups and some countries

The new country-by-country reporting framework is necessary to enhance transparency for national tax administrations and allow them to properly monitor the tax avoidance strategies of MNEs. However, only national tax administrations will have access the reports. Corporate stakeholders, including shareholders, will not. The strict confidentiality rules surrounding the reporting is a serious disappointment, considering that the information contained does not inherently confidential, such as business secrets or otherwise private knowledge.

Private equity funds under scrutiny?

In a study of 523 private firms between 1978 and 2005, a Harvard Business School paper has shown that private equity backed firms "engage in significantly more nonconforming tax planning and have lower marginal tax rates than other private firms"[22], Specifically, private equity-backed portfolio firms paid 14.2% less income tax per each dollar of pre-tax income than other portfolio firms. These results hold even after controlling for factors that are known to cause variation in tax avoidance across firms.[23]

Aggressive tax planning is even alluded to as a legal obligation within the wording of limited partnership contracts. In a legal document of a US limited partnership, for example, the general partner is called to prepare all necessary fillings in order to obtain "any available exemption from, reduction in the rate of, or refund of, any material withholding or other taxes imposed by any non-US (whether sovereign or local) taxing authority."

Public reporting on a country-by-country is already a requirement in a number of jurisdictions in Europe and in the US. In the US, the Dodd-Frank Act (section 1504) has such a requirement for the extractive industry. In the EU, the country-by-country requirement for the extractive industry and the banking sector are under revised Accounting and Transparency Directives (2013) and the Capital Requirement Directive (CRD IV, 2013) respectively. The implementation of the CRD IV reporting requirements in 2014 in France is being monitored by a joint NGO platform on tax transparency[19].

Measuring tax avoidance: the "6+2" OECD quantitative indicators

While recent corporate scandals have shed light on specific sectors – such as the extractive industry, the IT sector and the banks – it is clear that the risk for aggressive tax planning to occur is an issue for any sector of the economy and for any company involved in international transactions. There simply is no sufficient comprehensive data available to conduct sector-specific analysis. As part of the BEPS Action Plan n°11 on "Measuring and Monitoring",[20] the OECD has identified six quantitative indicators to measure the importance of aggressive tax planning and for which data is currently available. In addition, the OECD has identified two indicators for which data are not necessarily currently availably but could be so in the future and/or at the company level:

TABLE 3 MACRO- AND FIRM-LEVEL OECD INDICATORS

Category	OECD indicator	Data
Disconnect between financial and real economic activities	1. Concentration of high levels of foreign direct investment (FDI) relative to GDP	macro-level
Profit rate differentials within top (e.g. top 250) global MNEs	2. Differential profit rates compared to effective tax rates	firm-level
	3. Differential profit rates between low-tax locations and worldwide MNE operations	firm-level
MNE vs. "comparable" non-MNE effective tax rate differentials	4. Effective tax rates of large MNE affiliates relative to non-MNE entities with similar characteristics	firm-level
Profit shifting through intangibles	5. Concentration of high levels of royalty receipts relative to R&D spending	macro-level
Profit shifting through interest	6. Interest expense to income ratios of MNE affiliates in high-tax locations	firm-level
Future indicators	#7. Profit rates compared to effective tax rates for MNE domestic (HQ) & foreign operations	firm-level
	#8. Differential rates of return on FDI investment related to special purpose entities (SPEs)	macro-level

Source: Measuring and Monitoring BEPS, Action 11 - 2015 Final Report, October 05, 2015[21]

TABLE 4 EXAMPLES OF VOTING RECOMMENDATIONS ON NON-AUDIT FEES

Constituency	AGM recommendation to vote 'no' on the ratification of an auditor if:
Labour & civil society:	
AFL-CIO	The auditor provides tax advice or strategies for tax avoidance or non-audit services are more than 20% of total fees[24].
Episcopal Church	The sum of "tax fees" and "all other fees" exceeds 5% of total fees[25].
Pension funds:	
Ontario Teacher's Pension Plan Ontario Municipal Employees Retirement Fund	Non-audit fees are greater than audit fees[26]
The Ohio Police and Fire Pension Fund	Non-audit fees are greater than audit fees, audit-related fees, and permitted tax service fees combined, or if non-audit fees are "excessive"[27]
Suffolk Pension Fund advises	Non-audit fees exceed 25% of total fees, unless special circumstances are explained[28]
West Yorkshire Pension Fund	Non-audit fees are greater than 25% of total fees
Proxy Voting Firms:	
Glass Lewis advises	Tax fees and/or other fees are greater than audit and audit-related fees for more than one year in a row and if audit fees include fees for tax services for senior executives[29]
ISS	US: non-audit fees exceed 25% of total fees, or if non-audit fees are excessive / Continental European: non-audit fees exceed standard annual audit-related fees (for main index listed companies)[30]
Dimensional Fund Advisors	Non-audit fees are "excessive" and if no explanation is given to show that independence is maintained when non-auditor services are given[31]

What to look for & what to ask

Compared with other non-financial risk – environmental, social and corporate governance – corporate tax planning is a relatively unexplored domain for corporate research and long term investors. However there are a number of relatively simple indicators, most being drawn from the company's annual report, that can be used to help measure the extent to which a company is exposed to corporate tax planning risk. Two sets of indicators are proposed below: those that are corporate governance related and those related to the financial statements of the company.

From a corporate governance perspective, the primary quantitative indicator for measuring the presence of aggressive tax planning practices may be found in the size of "non-audit" fees taken by auditors. A large proportion of non-audit fees not only threatens the independence of the auditor but may also provide for a good indication of the level of resources spent by the company on aggressive tax planning schemes.

A number of "qualitative" corporate governance indicators can help inform investors, including: the extent to which the Board of directors treats tax planning practices as a potential but significant risk for the company, what the drivers are of any large business restructuring, mergers & acquisitions, and executive compensation.

Last but not least, several indicators can be drawn from the consolidated financial statement of the company. Some of the 6+2 OECD indicators presented above may be precious in this regard. As well, the country-by-country reporting may help spot any inconsistency in the transactions and distribution of assets within the group.

Non-audit fees

"Non-audit" fees refer to the amount of auditor fees spent on services that are not directly related to the basic responsibilities of an independent auditor. An independent auditor is required to review a company's financial statements each year to ensure that the company abides by fiscal laws. Companies are in turn required to report the cost of this external auditor as an expense for accounting purposes. Auditor expenses are publicly available in a company's annual financial statements.

If the company has hired an auditor to perform tax services as well, namely advising in tax planning, this service will be recorded as a "non-audit" service. Several investors and proxy advising services have, in their proxy voting policy, specific recommendations on when to vote 'no' on the ratification of an auditor, based on the amount of non-audit fees. The AFL-CIO advises voting no if the auditor provides advice on abusive tax avoidance strategies. In addition, proxy voters should consider voting against the auditor if the fees for non-audit services (audit-related fees, tax services, or other fees) are more

Shareholder activism preventing corporate inversion

The AFL-CIO advises voting to "support proposals to block or prohibit companies from reincorporating in tax havens and support proposals urging companies to reincorporate in the US". Walgreens, a U.S. pharmacy and drugstore, is a case in point. The company announced plans in 2014 to merge with the European company Alliance Boots and transfer its residence to Switzerland, despite the fact that the vast majority of its operations would remain in the U.S. The deal was heavily supported by hedge funds with short-term stakes in Walgreens, who stood to gain from higher temporary profits. However, the corporate inversion would have harmed long-term investors including pension funds. The deal would have cost U.S. taxpayers USD4mn over 5 years, according to a report by Americans for Tax Fairness and Change to Win. Such a move would have negatively impacted Walgreens' reputation with customers and the U.S. government (over 40% of Walgreens' revenues come from the government through Medicare and other programs). Several pension funds launched a resolution to challenge the inversion, and the inversion was ultimately rejected by Walgreens' board.

Reporting "on earnings indefinitely reinvested outside of the US"

US accounting standards require publicly held companies to disclose the US tax they would pay upon repatriation of their offshore profits. Offshore profits that an American corporation repatriates are subject to the U.S. tax rate of 35% minus a tax credit equal to taxes paid to foreign governments. However, accounting standards provide a loophole allowing companies to assert that calculating this tax liability is "not practicable." As reported by the Citizens for Tax Justice[32], almost all of the 243 non-disclosing companies use this loophole to avoid disclosing their likely tax rates upon repatriation—even though these companies almost certainly have the capacity to estimate these liabilities. According to the securities filings of 304 US corporations surveyed Bloomberg, profits held abroad account for some USD2.1tr. Of which over a fifth is held by Microsoft, Apple, Google and five other tech companies[33].

than 20% of total fees. Non-audit fees over 50% should be considered “a serious threat to auditor independence.”

Other corporate governance indicators

In addition to non-audit tax fees, several qualitative indicators on the governance of the company may be of relevance to measure the extent to which tax evasion and aggressive tax planning is an issue.

- *Board policy & management reporting*: best practice calls for the board of directors to have direct oversight of the company’s risk management system, including tax risks. As noted by the OECD, “jurisdictions are increasingly demanding that boards oversee the finance and tax planning strategies management is allowed to conduct, thus discouraging practices, for example the pursuit of aggressive tax avoidance, that do not contribute to the long term interests of the company and its shareholders, and can cause legal and reputational risks”.

- *Business restructuring, mergers & acquisitions*: large business restructuring and mergers and acquisitions may pose significant risk for the company’s stakeholders, including substantial social and employment costs for workers and local communities, and destruction of shareholder value for long-term investors. Investors should be particularly concerned when a restructuring involves splitting a company or part of it in several entities (fragmentation) or shifting operations into a foreign jurisdiction (inversion). Such a move may be an attempt to reduce taxes and increase short-term profits, at the expense of long-term stability.

- *CEO & executive management compensation*: Although executive compensation is not directly related to aggressive tax planning, it is an important indicator for corporate governance best practices. Investors should be aware of a company’s policies on executive compensation, as they are an important part of a comprehensive approach to long-term growth and sustainability.

Quantitative indicators from financial statements

An in-depth analysis of the consolidated financing statements, including information drawn from the new country-by-country reporting can help investors make informed judgments about the exposure of the company to aggressive tax planning practices. Corporate reporting can indeed reveal the presence of subsidiaries in a number of countries where tax opacity remains of concern. In the same vein, corporate reporting that reveals a marginal number of staff employed in a low tax jurisdiction with disproportionate levels of revenues would merit further engagement with the management of the company. In the US context, information about “earnings indefinitely reinvested outside of the US” may also provide for an indication of the level of aggressive tax planning.

Investors could make use of the official OECD indicators of tax avoidance for which data is currently available at firm-level (indicators n°2, 3, 4 & 6) as well as requesting disclosure of additional data for the “future” indicator which is also based on firm-level data:

- Differential profit rates compared to effective tax rates (OECD “BEPS” indicator n°2);
- Differential profit rates between low-tax locations and worldwide MNE operations (OECD “BEPS” indicator n°3);
- Effective tax rates of large MNE affiliates relative to non-MNE entities with similar characteristics (OECD “BEPS” indicator n°4);
- Interest expense to income ratios of MNE affiliates in high-tax locations (OECD “BEPS” indicator n°6); and
- Profit rates compared to effective tax rates for MNE domestic (HQ) & foreign operations (OECD future indicator).

Roadmap on responsible tax practices

Tax evasion and aggressive tax planning are still emerging issues in the responsible investment world. The international landscape on tax cooperation is changing fast. But, pension fund trustees can anticipate and take proactive steps to begin integrating tax risks —the risk for being exposed to tax evasion or tax avoidance behaviour by invested companies—into their investment policy.

DEVELOP A FORMAL STATEMENT

1 Analyse the risks associated with aggressive tax planning and tax evasion from the fund's perspective;

2 Determine the fund's in house management capacities and expertise to address tax risks, as well as the role and possibility of outside consultants;

3 Establish a formal statement, including how to vote and/or how to engage with individual companies. The statement could address:

- Corporate governance related indicators
  - non-audit fees;
  - companies' domicile of incorporation;
  - exposure to countries for which tax secrecy remains of concern;
  - integration of tax in the risk management oversight by the Board of directors;
  - tax drivers of business restructuring, mergers and acquisitions;
  - tax treatment of executive compensations.
- Economic and financial indicators
  - public disclosure of country-by-country reporting;
  - use of the OECD BEPS indicators at firm-level.

COMMUNICATE

4 Communicate the statement and goals with plan members;

5 Survey investment managers and other relevant service providers regarding their capacity and commitment to effectively observe the fund's statement.

ENGAGE

6 Engage with key companies to encourage voluntary disclosure of tax payments, including country-by-country breakdowns of revenue, tax and use of subsidiaries in secrecy jurisdictions.

7 Review the fund's portfolio holdings in light of the expectations contained in the Statement,

8 With due regard for the fund's internal capacity, conduct a screening process identifying portfolio companies where tax risk may be significant;

9 Engage with the management of companies at risk.

REPORT BACK

10 Report annually on the observance of the statement and on any other specific measure taken to address or mitigate tax risks.

Key resources for trustees

Trade unions

- Global Union Call for Action for Pension Fund Responsible Tax Practices, November 2014 http://www.tuac.org/en/public/doc/tradeunions/index.phtml
- AFL-CIO ⟶ Corporate Watch ⟶ Avoiding Their Fair Share of Taxes http://www.aflcio.org/Corporate-Watch/Avoiding-Their-Fair-Share-of-Taxes
- EPSU ⟶ Tax Justice Campaign http://www.notaxfraud.eu/
- ITF ⟶ Chevron investigation launched at global labour tax summit http://www.itfglobal.org/en/news-events/news/2015/september/chevron-investigation-launched-at-global-labour-tax-summit/
- PSI ⟶ Public Funding/Tax Justice http://www.world-psi.org/en/issue/public-fundingtaxation

NGOs

- Global Alliance for Tax Justice http://www.globaltaxjustice.org/
- ActionAid ⟶ Tax Power http://www.actionaid.org/tax-power
- BEPS Monitoring Group https://bepsmonitoringgroup.wordpress.com/
- Global Financial Integrity (GFI) ⟶ Tax Havens / Bank Secrecy http://www.gfintegrity.org/issue/tax-havens-bank-secrecy/
- SOMO ⟶ Economic Justice / Tax Justice http://somo.nl/dossiers-en/economic-justice/tax-justice
- Tax Justice Network Financial Secrecy Index http://www.financialsecrecyindex.com

Investor groups

- LAPFF ⟶ Investor Statement G20 Global Tax Reform, November 2014 http://www.lapfforum.org/LNews/Investor StatementTransparencyG20TaxReform12th-Nov2014.pdf
- UN PRI ⟶ PRI addresses multinational tax avoidance, November 2014 http://www.unpri.org/whatsnew/pri-addresses-multinational-tax-avoidance/

International initiatives

- G20/OECD Action Plan on Base Erosion and Profit Shifting http://www.oecd.org/tax/beps.htm
- Global Forum on Tax Transparency and Exchange of Information http://www.oecd.org/tax/transparency/
- European Commission ⟶ Taxation and Customs Union ⟶ Fight against tax fraud and tax evasion http://ec.europa.eu/taxation_customs/taxation/tax_fraud_evasion/index_en.htm

Business & tax advisors

- BIAC ⟶ Taxation http://biac.org/policy_groups/taxation/
- Deloitte ⟶ Global Tax Alerts http://www2.deloitte.com/global/en/pages/tax/articles/global-tax-alerts.html
- EY ⟶ Tax Services ⟶ OECD BEPS http://www.ey.com/GL/en/Services/Tax/OECD-base-erosion-and-profit-shifting-project
- PwC ⟶ Global Tax ⟶ BEPS http://www.pwc.com/beps
- KPMG ⟶ Tax News Flash ⟶ BEPS https://home.kpmg.com/xx/en/home/insights/2015/03/beps-in-taxnewsflash.html

Notes

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3. http://dotstat.oecd.org/
4. Figures shed light on tax avoidance haul, ft.com, April 28, 2013, http://www.ft.com/intl/cms/s/0/aad0297e-b020-11e2-8d07-00144feabdco.html#axzz2S20gaTUh
5. LA ILUSIÓN FISCAL - Demasiadas sombras en la fiscalidad de las grandes empresas - INFORME DE OXFAM INTERMÓN– Oxfam Intermón Nº 36 MARZOMarzo 2015 https://oxfamintermon.s3.amazonaws.com/sites/default/files/documentos/files/InformeLailusionFiscal2015.pdf
6. Who pays for our common wealth? Tax practices of the ASX 200, UnitedVoice / Tax Justice Network Australia, September 2014 http://www.unitedvoice.org.au/news/who-pays-our-common-wealth
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9. Tax Abuses, Poverty and Human Rights - IBAHRI Task Force report, October 2013 http://www.ibanet.org/Article/Detail.aspx?ArticleUid=4A0CF930-A0D1-4784-8D09-F588D-CDDFEA4
10. 13/05/2015| TUAC meeting on Corporate Tax Planning, 20 March 2015 http://www.tuac.org/en/public/e-docs/00/00/10/6B/document_doc.phtml & 20/12/2013| Report on a global unions meeting on corporate tax planning http://www.tuac.org/en/public/e-docs/00/00/0D/FE/document_doc.phtml
11. http://ec.europa.eu/taxation_customs/taxation/gen_info/good_governance_matters/lists_of_countries/index_en.htm
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16. Secrecy indicators include: banking secrecy, trusts and foundations register, recorded company ownership, published company ownership, published company accounts, country by country reporting, fit for information exchange, efficiency of tax administration, avoids promoting tax evasion, harmful legal vehicles, anti-money laundering, automatic information exchange, bilateral treaties, international transparency commitments, and international judicial co-operation. http://www.financialsecrecyindex.com/PDF/FSI-Methodology.pdf
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18. http://www.oecd.org/ctp/transfer-pricing/beps-action-13-country-by-country-reporting-implementation-package.pdf
19. 2014 : Que font les plus grandes banques françaises dans les paradis fiscaux ? Plate-forme paradis fiscaux et judiciaires, Novembre 2014 http://www.stoppa-radisfiscaux.fr/IMG/pdf/etude-banques-PPFJ-13-11-2014.pdf
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24. http://www.aflcio.org/Corporate-Watch/Capital-Stewardship/Proxy-Voting
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33. http://www.bloomberg.com/news/articles/2015-03-04/u-s-companies-are-stashing-2-1-trillion-overseas-to-avoid-taxes

The CWC brings together representatives of the international labour movement to share information and develop strategies for joint action in the field of workers' capital.

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