TAX AND ESG

By Nupur Jalan

Background

- More and more stakeholders have started demanding increased visibility over the details of the tax footprints of the multinationals in different countries.

- GRI 207: Global Reporting Initiative (GRI) issued GRI 207 which sets out standards for tax disclosures

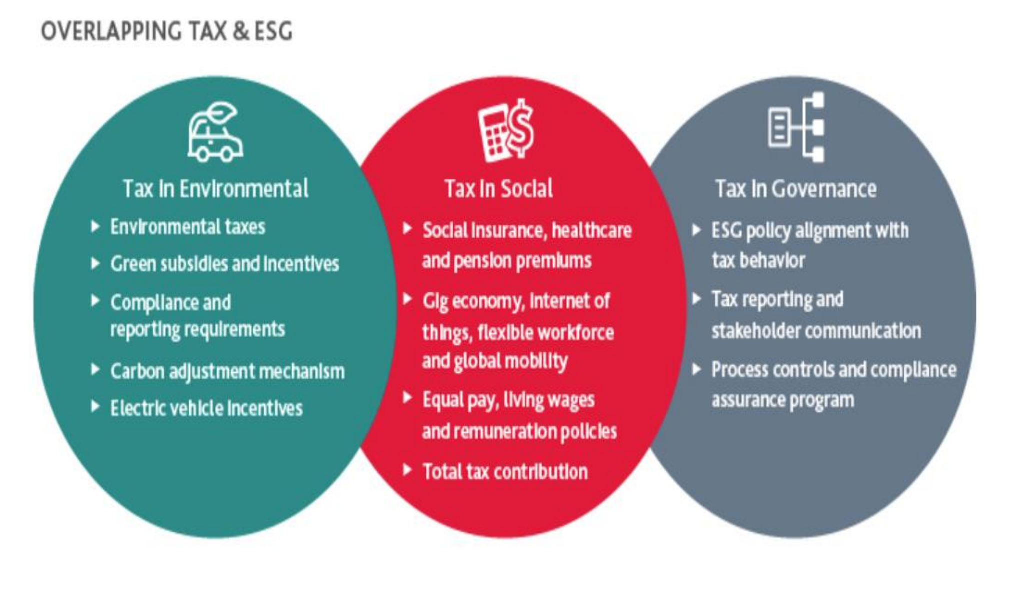
GRI 207: Tax

1. **Management approach disclosures**
   Disclosure 207-1 Approach to tax
   Disclosure 207-2 Tax governance, control, and risk management
   Disclosure 207-3 Stakeholder engagement and management of concerns related to tax
2. **Topic-specific disclosures**
   Disclosure 207-4 Country-by-country reporting

- World Economic Forum's (WEF) International Business Council made tax disclosures a core component of ESG reporting metrics and discussed about the tax metrics in 'Measuring Stakeholder Capitalism Towards Common metrics and Consistent Reporting of Sustainable Value Creation' white paper published by the WEF in 2020.

- Some companies like Anglo-American were early starters and have been publishing the Tax and Economic Contribution Report from many years. Similarly, Vodafone have been releasing tax contribution report.

What ESG means for tax



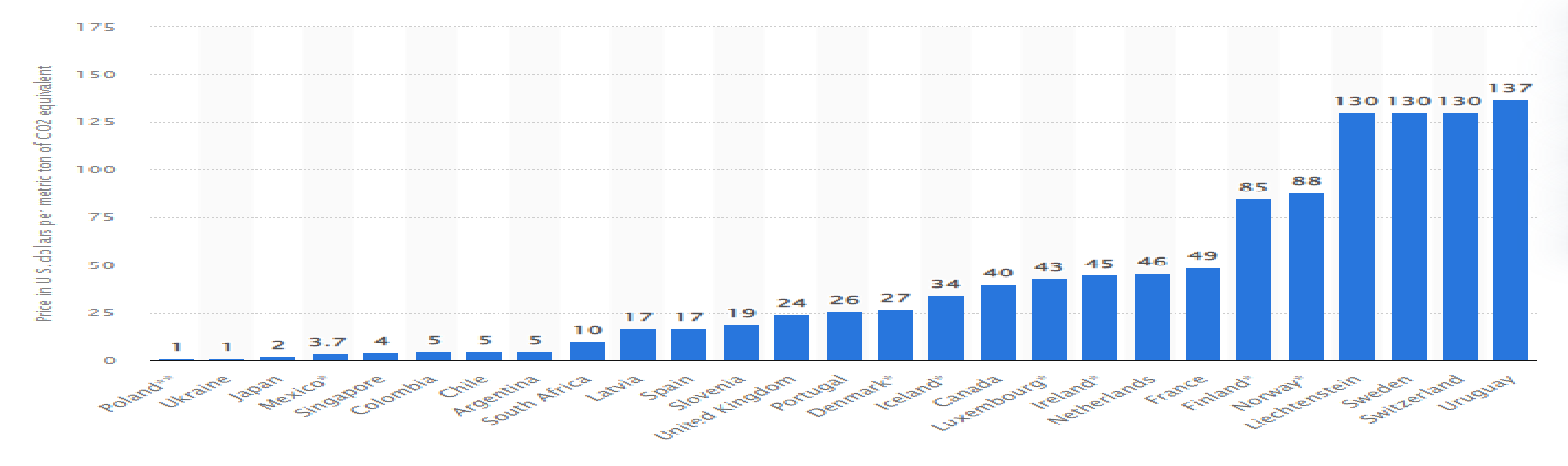
Source: Daniel Fuller and Jonathon Geisen, Navigating the intersection of tax & ESG, BDO (2022); available at *https://www.bdo.com/insights/tax/federal-tax/navigating-the-intersection-of-tax-esg* *https://www.bdo.com/insights/tax/federal-tax/navigating-the-intersection-of-tax-esg*

Environment	Governments across the countries are introducing a range of taxes, levies and other measures over the last couple of years as a mechanism to charge environment behavioral taxes or to incentivize organisations to adopt sustainable strategies. Some of these strategies (like offering incentives to adopt sustainable strategies) help in driving behavioral shift towards adopting more sustainable practice. For ex. – - Europe Green Deal, also known a FitFor55, where the continent expects to reduce carbon by 55 % in 2030 also includes revision in the energy taxation directive. - R&D tax credit of 12% to 13% for certain climate-related investments in the UK. - Production linked incentives for solar PV modules in India.
Social	For organisations, tax plays an important role for companies to contribute to the society and building trust amongst the stakeholders at large and being a responsible actor of the society. Appropriate revenue mobilization is essential for the states to promote social welfare. For ex. - European Commission has recognised the role taxation can play in achieving the 2030 Agenda for Sustainable Development.
Governance	Appropriate governance can help in aligning tax strategy and disclosures with the stakeholders demand of appropriate tax reporting (One step in this direction could be board having overview of tax strategy & risk; so that timely actions can be taken where needed and appropriate communications are made to the stakeholders). This could help stakeholders in believing that company is transparent and pays its appropriate fair of taxes.

Carbon taxes

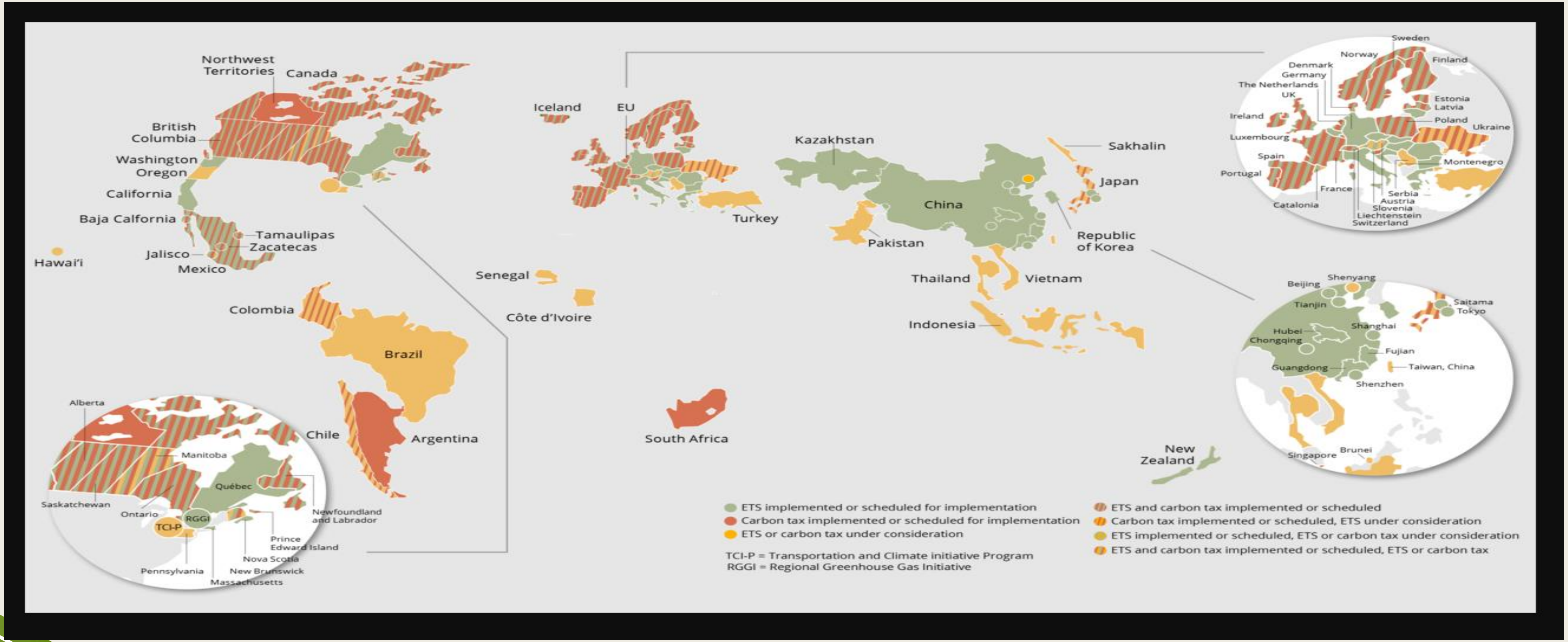
As stated earlier, countries have started levying several form of environmental taxes/ levies. Carbon-pricing measures (like carbon taxes and the carbon border adjustment mechanism) is amongst one of them.

Carbon tax rates worldwide as of April 1, 2022, by country *(in U.S. dollars per metric ton of CO2-equivalent)*



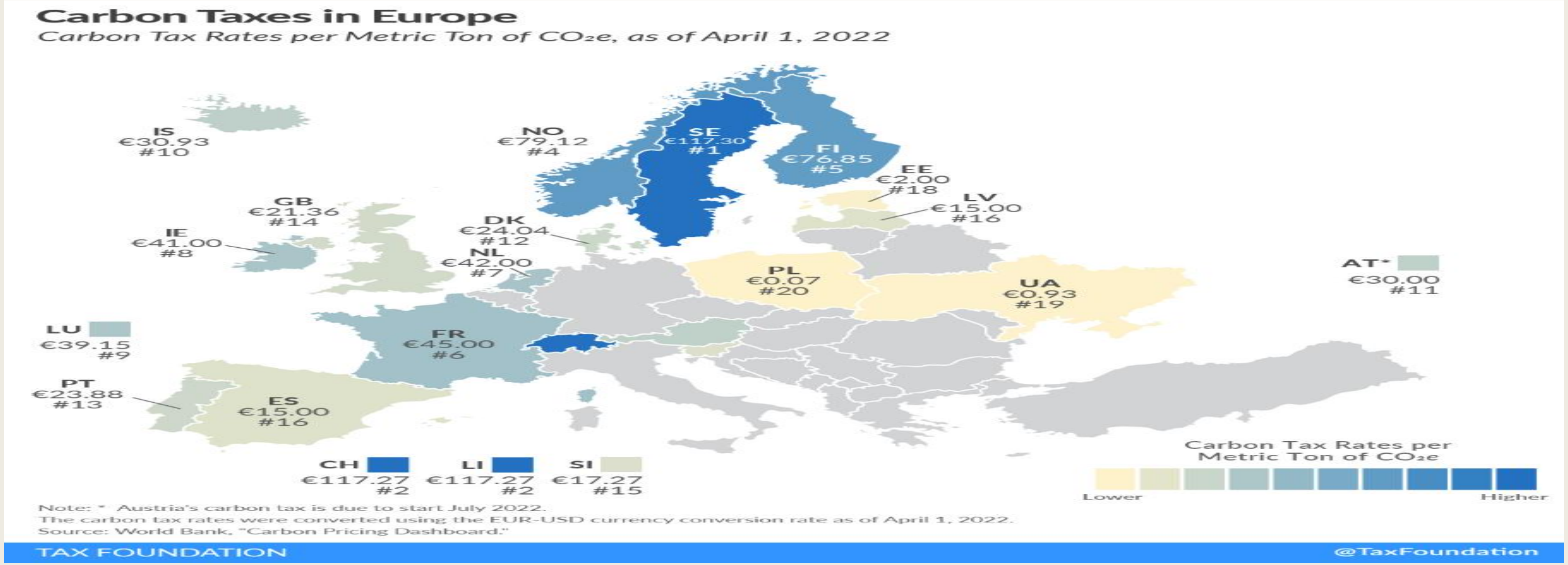
Source: Statista 2022

Carbon taxes



Source: https://en.wikipedia.org/wiki/Carbon_tax

Carbon taxes



Source: Sean Bray, Carbon Taxes in Europe (2022); available at https://taxfoundation.org/carbon-taxes-in-europe-2022/

Country-by-country reporting

- Country-by-country reporting (CbCR) was introduced as part of OECD’s base erosion and profit shifting (BEPS) initiative. The Country-by-Country Report provides aggregate data on the global allocation of income, profit, taxes paid and economic activity among tax jurisdictions in which a company operates. Several companies have started voluntary making CbCR publically available.
- On December 1, 2021, the public CbCR directive was published in the Official Journal of the European Union. According to the published text, the directive will enter into force on 21 December 2021 and Member States will have to transpose the directive into national legislation by 22 June 2023.
- Table 1 & Table 2 from Action plan 13 depicting the disclosures to be made in CbCR is presented below:

Table 1. Overview of allocation of income, taxes and business activities by tax jurisdiction

Name of the MNE group:
Fiscal year concerned:
Currency used:

Tax Jurisdiction	Revenues			Profit (Loss) Before Income Tax	Income Tax Paid (on cash basis)	Income Tax Accrued – Current Year	Stated capital	Accumulated earnings	Number of Employees	Tangible Assets other than Cash and Cash Equivalents
	Unrelated Party	Related Party	Total							

Table 2. List of all the Constituent Entities of the MNE group included in each aggregation per tax jurisdiction

Name of the MNE group:
Fiscal year concerned:

Tax Jurisdiction	Constituent Entities resident in the Tax Jurisdiction	Tax Jurisdiction of organisation or incorporation if different from Tax Jurisdiction of Residence	Main business activity(ies)												
			Research and Development	Holding or Managing intellectual property	Purchasing or Procurement	Manufacturing or Production	Sales, Marketing or Distribution	Administrative, Management or Support Services	Provision of Services to unrelated parties	Internal Group Finance	Regulated Financial Services	Insurance	Holding shares or other equity instruments	Dormant	Other[9]
	1.														
	2.														
	3.														
	1.														
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	3.														

Considerations for organisations from a tax perspective to align with ESG

<u>Some of these can be:</u>

- Alignment the tax strategy with the overall sustainability strategy of the organization
- Being tax transparent and disclosing relevant tax related information to all stakeholders
- Paying ‘fair share of taxes’ and following the practice of tax integrity

Separately, there should be tax code of conduct and appropriate tax risk management strategies in place.

A transparent tax policy can help businesses to outlay their contribution towards ESG and build trust among various stakeholders.