Discussion Summary

Responsible Tax - Investor roundtable #1 (Aug/Sep 2022)

INTRODUCTION

ESG. Responsible investing. Tax. Three topics that have been gaining significance and connection as institutional investors navigate the role, demands and opportunities that responsible investing from a tax perspective can and should play. Whilst some see responsible tax investing as an emerging discipline, others have been grappling with the issues for sometime.

In Late August / early September 2022 we gathered some of Australia's largest investors to discuss what progress, or lack of progress, is being made in Australia compared to their global counterparts; and to discuss as investors what are the issues and the measures that are being applied to 'walk the walk' on responsible investing for tax.

It was a fascinating discussion. As expected, there were different perspectives and different stages of the journey in understanding and applying principles that respond to the dynamics at play. But it was clear it is a live topic and one that will only become more important.

Reflecting on the discussion it was apparent it will be increasingly impossible to have an ESG investment strategy without also having a responsible tax investment strategy. However, rather than it only being a risk management issue, is it also a value creation opportunity for funds as well as tax professionals?

DISCUSSION

What is driving the increased emphasis on responsible investing including tax?

For some investors the need to consider and expand responsible tax practices is grounded in risk management, specifically reputational risk issues, for instance high profile examples of investors and portfolio / investee companies investing through the use of low tax jurisdictions, but also more nuanced and complex tax issues.

With a lens of risk management, the opportunity exists to expand the methodologies, sign-off rigour and the quantification of tax risks as part of ROI calculations. This is not always easy because what might be considered an appropriate tax structure can change over time, but not tackling this difficulty is increasingly not an option.

Some investors add to this risk management perspective objectives of encouraging better practices in investees reflecting broader ESG concerns for improved practices and outcomes for society and the environment. In essence tax is seen as a sustainability issue not just a financial risk issue.

Members of funds and other consumers are concerned about the tax practices of companies they are invested in. A survey by Responsible Investment Association Australasia ranked concerns with 'tax fairness' the same as gambling and tobacco and just lower than human rights abuses.

It could be said this level of concern by consumers underlines the view that it will be increasingly difficult for funds to have an ESG / responsible investing strategy and profile more broadly that is not combined with a responsible tax investing strategy. Potentially this consumer concern creates value creation opportunities over time. If nothing else funds will need to be careful they are not accused of 'green washing' when it comes to their tax practices. A reason for investors to undertake tax transparency reporting.

Clarifying what is meant by 'responsible tax' and 'tax fairness

Discussion in respect to ESG and tax often is associated with 'tax fairness'. For instance the survey mentioned above by Responsible Investment found a significant a significant number of consumers want to avoid in their investments include "Companies that don't pay their fair share of tax".

The concept of fairness was acknowledged, however so too was the difficulty in defining 'fairness' as different stakeholders in different parts of the world can have very different, legitimate, views on 'fairness'.

Some take the view that it is better to avoid getting 'bogged down' in these conceptual issues and approach it in terms of more concrete attributes. One such approach might be to consider:

1. A public policy on the principles to be applied for responsible tax investing;
2. The tax governance framework and operating controls in place; and
3. Preparing tax transparency reports.

We are now in a much better position to define a strategy

Global organisations such as the UN PRI and GRI have prepared over more recent years guidance which contributes meaningfully to a process of establishing global practices that may become norms. In addition, jurisdiction specific initiatives such as the ATO's guidance on tax risk management and governance, and similar initiatives in other countries in Europe and more recently in Singapore and Malaysia add further instances of better practices. We have also seen global examples of publicly available tax investment principles by funds. It was suggested that rating agencies also include tax attributes as part of some of their sustainability indices.

This increasing body of better practices is helpful. However, we are still not in a position of global norms. There are key markets like the US where practices on tax governance and transparency are not aligned with other regions.

As a result, investors need to define their own view and their own 'norm' and aspiration. The norms they would like to see applied should include investing principles and accountabilities - in addition to transparency related practices.

Emerging practices of stewardship

Larger Australian investors, especially in joining with 'like-minded' investors in more direct investment have been increasing their consideration and scrutiny of tax risk management and governance practices of investees. In some cases, this also includes seeking to influence through encouraging the application of better practices by portfolio companies.

The 'activism' of Australian funds to influence behaviours in respect of listed companies headquartered outside of Australia has perhaps been less than many of the European and North American funds. There are practical reasons for this, including where a fund holds a small stake in a listed company and therefore has limited if any practical influence. However, as the recent Amazon shareholder initiative to push for greater tax transparency showed, combining efforts with like-minded investors is also possible to drive change in the listed environment.

Capacity building to enable more mature practices

Many investors are engaged in responsible investing and the opportunity to evolve how tax is considered and embedded as part of responsible investing processes. However, gathering the imperfect data and analysing it, in sometimes confined timeframes, requires resourcing, skills and a programme to improve practices. Resources and capabilities that don't necessarily exist currently.

Building the business case for additional resources or different skills might be an initial task for investors to enable real progress in the area. Much like the uplift in tax governance may have required a business case.

That capacity building also includes improving how tax and ESG / responsible investing teams collaborate. Applying and expanding mechanisms to integrate tax qualitative and quantitative parameters into ESG assessment and decision making.

Being on the journey is an outcome in itself?

Given the somewhat nascent nature of the discipline of responsible tax investing and the inherit difficulties and permutations in tax technical issues and behaviours by investees, there is merit in recognising the positives of just being on the journey.

That journey however needs to recognise that outcomes will likely encompass both tax risk and sustainability perspectives, and be backed by concrete measures and actions to demonstrate progress.

It is clear that to demonstrate 'walking the walk' on responsible investing when it comes to tax, more is required than a tax risk management policy and a couple of checklists.

The future focus and new measures the journey necessitates also provides a platform for a systems wide recognition of the role of taxes (and the complexities) and for tax teams to contribute to a bigger picture and a more profound legacy.

For questions on the roundtable, contact:

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