Responsible tax at Finnfund

Finnfund's mission is to promote economic and social development in developing countries. For this to take place, target countries require tax revenue and payments of other fees. Thus, tax revenue and other tax-like fees paid by companies to the public sector in developing countries constitute one of the development aims of Finnfund's work with the companies it finances. Such revenue allows a country's government to structure and provide services such as education, health care and infrastructure for its people.

Projects financed by Finnfund must be both economically viable and responsibly implemented, and must generate development effects in the target countries. Finnfund requires the projects it finances to act responsibly with regards to taxation and to comply with the local tax legislation.

In addition to the tax aspects, Finnfund also evaluates the other effects on the economic and social development of the target country, as well as factors such as the likelihood of the project's success, compliance with environmental and social responsibility, and observance of human rights. The investment decisions are based on a consideration of such issues as a whole.

Finland has committed to the goals of the OECD's Base Erosion and Profit Shifting (BEPS) project that aims to eliminate profit shifting, which erodes tax base and non-taxation due to asymmetry of tax regimes.

Through its operations, Finnfund supports the development of international tax regulation and complies with current legislation and the guidelines issued by its majority shareholder, the Government of Finland. Through is operations, Finnfund also supports the tax responsibility of the companies it finances.

Principles for a responsible tax practice and international financial centres

1. Finnfund finances responsible businesses in developing countries which pay taxes on their profits to the developing countries, in which the work and financial activities generating the income occur. One goal of Finnfund's operations is to increase the tax revenue of developing countries.

    - The companies that Finnfund finances, either directly or through a fund-structure, pay taxes and other tax-like fees to the governments of their target countries. Finnfund monitors these payments annually.
    - Finnfund assesses the tax responsibility of the investments it finances, and monitors the realisation of tax responsibility. The corporate, financing and ownership structures of the projects Finnfund finances must be made known to Finnfund
    - Finnfund is statutorily obligated to investigate the ownership structure of the projects. Finnfund requires that the corporate structure of the project company and its company group be transparent to the tax authorities of the relevant countries.
    - Finnfund also investigates the background of the co-investors and the ultimate beneficiaries, but it cannot be responsible for the tax arrangements of its co-investors.
    - Finnfund seeks to promote transparency of information on tax revenues in the target countries, while respecting the confidentiality of client information.

Finnfund publishes annually and on country-by-country basis the amount of taxes and fees in aggregate that the companies it finances pay to governments.

- Developing countries need investments, and they have the right to use taxation to steer business activities. Such measures, for example tax holidays, should be available to everyone on similar grounds in similar situations. Finnfund requires the project companies to act transparently towards the target country authorities, but does not expect them to pay more taxes than what is required by the local tax laws and authorities.

- Finnfund complies with the Finnish government ownership steering guidelines that require taxes to be reported on a country by country basis. Finnfund's corporate social responsibility report includes the taxes it has paid annually in each country. In accordance with the Finnish Income Tax Act, Finnfund does not pay income tax in Finland or dividends to its shareholders. All monies and profits returned by the projects to Finnfund are reinvested in new projects.

2. Finnfund does not support aggressive tax planning, which prevents the accumulation of tax revenue from profitable business activities in developing countries.

- Finnfund follows the government policy on aggressive tax planning. The policy (12 March 2014, available in Finnish), states that there is no unambiguous definition of what constitutes aggressive tax planning and that drawing the line is not always simple. Aggressive tax planning can mean using arrangements that in themselves are legal, but are nevertheless in conflict with the fundamental intent of the law. According to the policy, Finnfund does not accept the use of artificial economic substance or structures or taking advantage of the differences between tax systems which diminish the impact of the taxation rules of developing countries, causing them to lose tax revenue.

- Finnfund examines in particular the income tax accrued from the operating result of the project company located in a developing country. Finnfund evaluates before an investment decision, and monitors during the project, whether the project company's result, and thereby the taxes paid to the developing country, are artificially reduced. For example, Finnfund examines whether there is thin capitalisation and whether the interest on shareholder loans as well as other transfer prices are at arm's length (see: processes and tools).

- Finnfund requires that the companies it finances act responsibly and transparently in matters related to taxation, and encourages them to maintain a tax policy that is disclosed to the public.

- The taxation capacity of developing countries and international taxation regulations develop continuously. Finnfund monitors the development of regulation and contributes to the increase in tax information transparency through its own operations as well as to the debate on tax issues. Finnfund is engaged in co-operation with European development finance institutions and other bodies.

3. In respect of investments in funds, Finnfund requires that the fund's investment policy complies with Finnfund's mission and principles in respect of both the investee companies and the acquisition and management company structures used.

- Finnfund also requires the companies that are a part of the fund's administrative structures and their shareholders to report their income related to the compensation paid by the fund in accordance with the tax legislation of each country.

4. Foreign holding companies can be used in projects funded by Finnfund, if there are sufficient commercial reasons to do so.

   - Finnfund does not accept the use of holding company structures, if their only objective is to exploit asymmetry of taxation. Asymmetry of taxation means a situation where countries treat the same object differently for tax purposes, and this asymmetry can be exploited to avoid taxes in the developing country.

   - Finnfund can only invest through holding companies and funds registered in countries that comply with the progressively tightening standards of OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes. Finnfund also cannot make investments via holding companies registered in countries listed in the list of non-cooperative jurisdictions published by the Council of the European Union on 5 December 2017. However, direct investments can be made in all developing countries regardless of how the countries in question have been classified or if they have been classified at all by OECD's Global Forum, or whether or not they have been included in the list of the Council of the European Union mentioned above.

Process and tools

The practical tools of Finnfund's responsible tax policy comprise three sections: investment criteria, agreement terms and conditions, and monitoring.

A) Investment criteria and process: Finnfund must understand the corporate, ownership and financing structures of the financed project

- Assessment of tax practices and financing structures during the preparatory phase
- Describing and understanding the financing and group structures and their purpose
- Transparency of the financing and ownership arrangements of the financed project and rest of the company group to the local tax authorities (e.g. transfer pricing documentation in the manner required by each state)
- Ensuring interest on shareholder loans and transfer prices are at arm's length
- Checking the grounds of the received tax benefits

B) Agreement terms and conditions

- Terms and conditions (representations and warranties, undertakings) on tax structures and reporting are included in the agreements. Finnfund wants to be informed if changes occur in e.g. company structures or internal financing structures as well as an opportunity to react to such changes
- The aforementioned information must be transparent to the tax authorities and Finnfund
- In the projects it finances, Finnfund's role is to assist the companies to develop their corporate responsibility; emphasis being on the promotion of best practices whilst the company's operations develop

C) Monitoring and reporting

- Finnfund monitors the projects it finances and encourages them to prepare their own tax policy
- Finnfund encourages the companies it finances to report to Finnfund annually on a country-by-country basis the taxes and tax-like fees paid. This is a requirement in respect of new projects which is also recorded in the agreements.
- Finnfund publishes the tax footprint of the projects it finances on portfolio level on a country-by-country basis, while respecting client information confidentiality.
- When participating in the corporate governance of its investees, Finnfund seeks to promote increasing responsible tax practices and transparency in these companies
- Finnfund follows the development of international tax regulations and develops its own capacities in tax issues. This tax policy and related practices are updated when necessary.

This tax policy is valid starting from 1 January 2018 and it shall apply to all projects approved by the Board of Directors after this date.