



Article

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Responsible Investment: Taxes and Paradoxes**

<https://doi.org/10.1515/ntaxj-2017-0010>

Received Jun 01, 2017; accepted Oct 30, 2017

Abstract: Taxes have become an issue of corporate social responsibility (CSR), but the role of taxation is to some extent an ambiguous and controversial issue in the CSR framework. Similarly, another unclear question is what role investors who are committed to sustainable and responsible investment (SRI) see taxes as having on their environmental, social, and governance (ESG) agenda. Corporate taxes have an inverse relationship with the return of the investors: taxes paid directly affect what is left on the bottom line, reducing the return of investors. However, investors are now more aware of tax-related risks, which can include different forms of reputation risk. Corporate tax planning may increase the returns, but those increased returns are riskier. This study focuses particularly on the relationship between SRI and taxation. We find that tax matters are considered to be on the ESG agenda, but their role and significance in the ESG analysis is unclear.

Keywords: corporate taxes, sustainable and responsible investment (SRI), ESG, corporate social responsibility (CSR), aggressive tax planning, corporate governance

1 Introduction

Traditionally, corporate social responsibility (CSR) has been divided into economic, ecologic, and social elements. One of the best-known theoretical models exempli-

fying these elements, is Elkington's (1997) triple-bottom-line framework, and many researchers have adopted this framework to evaluate CSR from the perspective of different stakeholders. For example, society expects companies take into account the economic, environmental, and social effects of their businesses and operations.¹

In many ways, sustainable and responsible investment (SRI) is a mirror image of CSR. When making their investment decisions, investors evaluate how companies (whether current or prospective investments) handle their responsibilities (Hyske *et al.* 2012; Sparkes and Cowton 2004).

Regarding responsible investments, the key letters are *ESG*, referring to environmental, social, and governance factors used in measuring the sustainability impact of an investment in a company or business (e.g., Hoepner 2013). Two first letters mirror the two elements of CSR, namely *environmental* and *social*, very well. However, "G" standing for *governance* is not conceptually equivalent to economic responsibility. In this context, governance refers to corporate governance (see Bebchuk and Weisbach 2010).

This mismatch can be explained by the fact that from the viewpoint of responsible investments, an investor as a shareholder is self-evidently the primary stakeholder. The main (or often only) reason for an individual or an institutional investor like pension funds or asset managers to invest in a company is economic return. Investors seek returns for themselves, to finance the pensions they manage, or for their clients. For many institutional investors, ESG analysis is a means to achieve a better risk-return profile (Clark *et al.* 2015; Hoepner 2013). However, in CSR discussions and argumentation, the shareholder is only one stakeholder, albeit a very important one.² The company and its directors have to be aware of a range of expect-

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** This article is a part of the Sustainable Market Actors for Responsible Trade (SMART) project (smart.uio.no). Reijo Knuutinen is a member of the SMART project and Matleena Pietiläinen has collaborated with the project. The SMART project has received funding from the European Union's Horizon 2020 research and innovation program under grant agreement No 693642.

¹ The terms 'company' and 'corporation' are often used interchangeably. In this article we primarily use the term 'company' when speaking about them as legal entities and investment objectives. The term 'corporate' is used in the context of CSR, as well as speaking about corporate taxes, as it is established. We view terms like 'firm', 'enterprise' or 'business' to primarily refer to something which is physical, like production facilities, operations, or actions. See also Posner 1992, p. 409.

² Regarding the shareholder/stakeholder debate, see e.g. Clark *et al.* 2015.

tations and requirements among the company's different stakeholders. The review and evaluation of responsibilities is not in the same way locked to one stakeholder only.

Taxation has become a real CSR issue during the last decade or two, though with some vague features.³ In the framework of *3P* ("planet, people, profit"), it is natural to perceive taxation as a part of economic responsibility, albeit very often it is considered a self-contained issue. It is also possible to look at taxation from the broader perspective, since taxes allow many social goals to be achieved through public finances and operations.

Despite the increasing awareness, the role of taxes is to some extent ambiguous and that can make it a controversial issue. This is demonstrated by the fact that many companies reporting on their CSR do not include tax issues on the reporting list. Furthermore, the concept of CSR is defined in many different ways in different contexts, and sometimes it may be difficult to see tax issues to be included in the definitions.⁴ One of the aims of this study is to gather information on whether taxes are a similar (or an even more) ambiguous issue within SRI. How do investors committed to SRI view tax issues on their ESG agenda?

In their ESG analyses, investors use public information about environmental, social and governance issues. First, tax matters are clearly involved in any governance agenda. Second, taxation has an indirect impact on how society can fulfill its tasks and obligations. Therefore, tax issues can be included on the social factors agenda as well. Furthermore, taxation is one of the most important tools in environmental protection as well. Although this link is very strong at the level of tax policy, it is harder to see that in ESG analyses taxes would have any particular role when assessing a company's environmental responsibility.

³ According to survey by FIBS (Finland's leading corporate responsibility network), 37% of the largest Finnish companies have actively worked for tax transparency and tax reporting within their CSR activities. The survey was executed in January–March 2017 by interviewing 200 CEOs and CSR directors among the top 1000 companies in Finland. In 2015 the respective share was 25%.

⁴ See e.g. COM(2011) 681 final (A renewed EU strategy 2011-14 for Corporate Social Responsibility), p. 3 (referring further to COM(2001) 366): "The European Commission has previously defined Corporate Social Responsibility (CSR) as 'a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis.'" See also http://ec.europa.eu/growth/industry/corporate-social-responsibility_en: "Companies can become socially responsible by: following the law; integrating social, environmental, ethical, consumer, and human rights concerns into their business strategy and operations."

The current study attempts to clarify and understand the role played by corporate taxes in the context of SRI. First, while the relationship of SRI and taxes is an almost unexplored area of research, we initially approach the issue by reviewing the relationship of CSR and taxes. Although this matter is not very well studied either, there is literature available to refer to. Second, we investigate the issue through empirical interviews with Finnish institutional investors.

Our article structure is as follows: Section 2 deals with previous research on the relationship between taxation and CSR or taxation and SRI. Section 3 deals with the role of corporate taxes within CSR, which is used to refine the research questions in Section 4. Section 5 examines the methodological issues of the empirical part of our study. In Section 6, the results of our empirical research are presented and analyzed. Section 7 concludes.

2 Prior research and setting the research questions

This section reviews prior research on the relationship between CSR and taxation and the relationship between responsible investing and taxation. The review informs our choice of research questions and the approaches and research methods we adopt.

Approaches to and perspectives on the research on the relationship between *CSR and taxation* vary. Studies are typically sited in the economic and legal interface disciplines. Some studies concern the boundaries and limits of the law, while others relate to business ethics. It is also possible to take a purely economic perspective and, for example, look at the issue from a risk-return point of view.

Some studies on CSR and taxation have approached the issue from the standpoint of company law, or even more precisely, the theory of company law and the essence of the company. That viewpoint involves accepting that how we understand a company may be decisive in how we see its responsibility to pay taxes (Avi-Yonah 2006). As a topical theme, the aggressive tax planning of corporate taxpayers, especially of multinational enterprises, and the assessment of its impact on society has been of interest to researchers for some years (see e.g., Shafer and Simmons 2008; Sikka 2010; Preuss 2012; Finér and Ylönen 2017). Some studies have been very critical of tax planning by corporations (see, e.g., Ylönen and Laine 2015), while others have emphasized the legality of taxation as a main criterion for companies to make use of tax planning options; according to this approach, responsibility

lies mainly within the framework of tax legislation (HJI Panayi 2015). The issue has also been examined from the perspective of law and philosophy, and research has addressed, *inter alia*, the moral obligations of the company in relation to tax standards (Ostas 2004; Knuutinen 2014b; Gribnau 2015). In addition, at least one monograph has been written examining the relationship between corporate responsibility and taxation more widely from a variety of perspectives (Knuutinen 2014a).

In contrast, the relationship between *SRI and taxation* is an almost unexplored area of research; an exception being Scholtens' (2005) study of special tax regulations relating to responsible investments. The aforementioned study finds that a lightened form of tax regulation applied to the investments has positively affected the growth of SRI in the Netherlands. Indirectly, the relationship between SRI and taxation has been examined somewhat more frequently. Studies are linked, for example, to increasing transparency and reporting requirements (Fernandez-Feijoo *et al.* 2014), to the investment activity in connection with changes in tax legislation (Moore 2014), compliance with corporate tax laws (Alon and Hageman 2013), or assess the connection between national corruption level and foreign investments (Robertson and Watson 2004). Beyond the examples provided above, the link between SRI and taxation seems to have rarely been directly or even indirectly addressed in earlier research, either from a broader perspective or from the specific perspective of investors.

However, in SRI guidelines, factors and practices, tax issues have begun to take their place during the last years (see *e.g.*, UN PRI 2015a; Berry and Junkus 2013). But what is the precise role of taxes? What is the relevance, weight, or effect of tax issues? Is the role of taxes controversial on the ESG agenda and in practice? What kind of role could or should taxes have on the ESG agenda and in practice?

According to the definition of Eurosif (2016)⁵

Sustainable and Responsible Investment (SRI) is a long-term oriented investment approach, which integrates ESG factors in the research, analysis, and selection process of securities within an investment portfolio. It combines fundamental analysis and engagement with an evaluation of ESG factors in order to better capture long-term returns for investors, and to benefit society by influencing the behaviour of companies.

However, this definition of SRI does not specify exactly which factors should be included in the ESG analysis. Therefore, it prompts the question of whether tax matters

are among the required ESG factors and, if so, in what way, and for what purpose. If tax issues are there on the ESG agenda, how are they being explored and analyzed, and how do they influence investment decisions?

SRI strategies⁶ including influencing, such as *engagement and voting* and impact investing are popular ways for institutional investors to affect the ESG issues in investments. For example, according to Eurosif (2016), *impact investing*, as a strategy of SRI combining economic productivity and social impact has recently been adopted by Finnish institutional investors.⁷ Has this kind of influence been in some way reflected in tax issues, and what form might that influence take?

As the role of responsibility becomes more important in the activities of institutional investors, it can be assumed that Finnish (and other) institutional investors will at least to some extent proactively (*i.e.*, not only reactively) take account of corporate taxation practices in their investment activities. After all, taxation is vital to the functioning of society. In addition, among the key players in the SRI arena, corporate tax issues have been raised as one of the most important global themes for SRI in the foreseeable future (see *e.g.*, UN PRI 2015b). This motivates us to look at taxation as an analysis criteria and factor for SRI, specifically from the point of view of Finnish investors, and examine whether, and if so to what extent, taxation is a part of the SRI activities of Finnish institutional investors.

This study seeks answers to the questions raised above. In particular, the questions are examined with regard to institutional investors managing the funds, not those private investors investing for their own benefit, or who have transferred their funds to an asset management firm. The various research questions posed above can be combined to form a single question: *How do institutional investors committed to SRI see the role of tax matters in their responsibility analysis, and how does this analysis of tax matters affect their investment decisions or other activities?*

This study can be located at the interface of the legal and economic disciplines. From a legal research point of view, however, the question is not a matter of dogmatic legal research, but rather one of setting the boundaries of law. From an economic research point of view, this study could be located mainly in the accounting and financing realm, as it involves clarifying information use and the

⁶ See Eurosif's (2016) categorization of all SRI strategies and their definitions.

⁷ According to Eurosif (2016, 67) "impact investment has also reached the Finnish market. There have been product launches and other events linked to this topic."

⁵ Eurosif 2016, 9.

needs of institutional investors, and evaluating the links between CSR reporting and ESG analyses. Consequently, the study responds to identifications to incorporate accounting aspects into taxation research (Boden *et al.* 2010; see also Finér and Ylönen 2017).

The current research is also multidisciplinary in terms of the methods used. The research is conceptually based and justified, and the research questions or statements formulated in a way that may be more typical of legal research. The research questions are refined in the form of statements and then evaluated through data elicited from empirical interviews and supporting documents used to assess how clearly the empirical and the other available material validates the set statements. The execution of the empirical part may be closer the methods of qualitative research used in the accounting discipline.

3 What are the arguments made for CSR generally and especially regarding tax issues?

Since corporate social responsibility and responsible investment can be seen as mirroring concepts, we next look at what are the arguments made for CSR generally and especially regarding tax issues. The main arguments for CSR are very well-known: sustainability, a moral obligation, reciprocity (companies' "license to operate"), and the reputation of companies (Porter and Kramer 2006). Nevertheless, the relevance of these arguments in the context of taxation is not equally obvious and accepted. We next offer a brief overview of these arguments generally, while also suggesting how they can be interpreted in the context of taxation, not only for CSR but also for SRI.⁸

The best-known definition for the term *sustainability* was developed in the 1980s by the World Commission on Environment and Development, headed by Norwegian Prime Minister Gro Harlem Brundtland, it describes sustainability as: "Meeting the needs of the present without compromising the ability of future generations to meet their own needs."⁹ Sustainability is often connected to environmental development, but sustainable development requires socially and economically sustainable solutions and actions as well. In turn, companies are expected to op-

erate in ways that secure long-term economic performance by avoiding short-term behavior which is environmentally wasteful or socially detrimental (Porter and Kramer 2006). Sustainable development is also related to taxation. Tax havens, for instance, distort the inter-nation equity (Musgrave and Musgrave 1972). Profit shifting and base erosion as a result of aggressive tax planning activities have been one of the main concerns occupying OECD and G20 countries in recent years.¹⁰

A company that acts in a way so as to secure sustainable development can be considered a responsible company. But is there any *moral obligation* for the company to bear this kind of responsibility? The first morality aspect is that the company as such, as an abstract legal phenomenon, cannot have any real and independent moral thoughts and views; only natural persons can. All natural persons certainly have some basic idea of right and wrong. In the case of the company, the natural persons making decisions include the Board of Directors, the CEO, and also the shareholders or their representatives. This observation does not mean, however, that the company cannot formulate, as a part of its corporate culture, some kind of collective perceptions of right and wrong. Similarly, institutional investors as a legal entity do not have moral considerations, but the investment managers and portfolio managers as natural persons may have.

The relationship between law and morality is a classic legal philosophy issue. From the perspectives of legal history and philosophy, the question is also about the relationship between natural law and legal positivism. Further, this relationship is dissimilar in different legal fields. For example, fundamental human rights are considered to be valid everywhere, regardless of the legal system and jurisdiction, while tax law is based on the rule of law and legal positivism, and consequently tax systems differ from one state to another. States are also engaged in tax competition, which can at least to some extent be considered both acceptable and desirable. It would however be considered unacceptable if countries were to compete over the establishment and investments of companies without regard to occupational safety and health regulations, or by having no environmental protection regulations, for example.

The idea of *reciprocity* is based on the fact that any enterprise or company needs public goods and infrastructures, or at least the legal system, to continue to exist. In

⁸ Regarding the argumentation, see also Knuutinen 2014b, pp. 53–58.

⁹ World Commission on Environment and Development: Our Common Future (1987).

¹⁰ OECD/G20 Base Erosion and Profit Shifting Project. See Addressing Base Erosion and Profit Shifting (2013) and Actions 1–15 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project (2015).

return, companies pay corporate income taxes. As a result, it can be argued that companies have corporate social responsibilities when society can be seen as a partner or even as a class of investor in a company through the influence of the public infrastructure (see e.g., Kanninen 2003). Companies have to pay for their “license to operate” (Porter and Kramer 2006). Regarding tax behavior, reciprocity may be considered as requiring companies to comply not only with the letter of law, but also with the principles of fair tax compliance.

The strongest argument is that the company’s way of operating and acting in relation to the requirements and expectations of society may significantly affect the company’s *reputation*. Today, tax planning activity is a relevant issue. In practice, taxation matters can be assessed with respect to CSR from the point of view of whether a certain type of tax planning is not only lawful but also generally acceptable.

Tax planning that is lawful but generally frowned upon, is often called aggressive tax planning. However, aggressive tax planning is not a legal concept so the term has no legal definition. From the CSR point of view, aggressive tax planning can be defined as actions taken by taxpayers that accord with the legal requirements of tax law, but that do not meet the reasonable and justified expectations and requirements of the stakeholders involved (Knuutinen 2014b).

Adopting aggressive tax planning can help a company improve its financial position in the short term, but in the longer term, the approach could harm the company’s financial interests. Actions or omissions that negatively affect a company’s reputation are risk factors affecting the company’s success and value. One of the tasks of management is to identify and evaluate the various risks involved and to seek to eliminate or hedge them if necessary. This risk assessment might incorporate the overall acceptability of tax planning activities and any potential reputational risks arising from it.

If corporate tax planning activity passes beyond a critical point (which could be called L_1) in the eyes of a company’s stakeholders, it moves into the realm of aggressive tax planning where such activity risks having adverse impacts, for example, in the eyes of customers or potential employees. The area beyond L_1 , can be called the *critical area* of tax planning (Knuutinen 2014b). From this point forward, it may still be possible to secure tax benefits through aggressive tax planning, but at the same time the action may trigger reputational risk. Theoretically, the company should seek further tax planning opportunities until the point L_2 , where the advantages of tax planning (i.e., tax savings) equal the expected losses due to repu-

tational risks.¹¹ However, responsible companies are unlikely to be willing to go that far.

These are the main arguments for the requirements and expectations of CSR. However, it is worth noting that these are not legally binding arguments. Instead, they are moral and ethical justifications, arguments for equity and justice. However, the emergence of reputational risk broadens the scope of the issue, in that the question has come to involve economic and financial arguments as well. Consequently, CSR, at least in view of the reputation risk, may not conflict with shareholder value thinking (see Friedman 1970).

Responsibility can also confer direct or indirect economic benefits. There is at least some evidence that CSR has a role in attracting good employees, reducing undesirable employee turnover, increasing customer satisfaction, and generally improving corporate reputation (see e.g., Weber 2008 and Galbreath 2010). However, the results do not seem completely unambiguous. In particular, the benefits of adopting responsible tax behavior are not necessarily clear. In the first place, taxes paid always and immediately come out of the company’s earnings and assets. It is also quite obvious that companies operating in different business sectors may see completely different potential reactions on the part of employees and customers.

4 Refining and focusing the research questions

The research statements of this study are derived from the general discussion on the subject of the research, the research reports and publications of civil society players like NGOs¹², the juridical and economic literature, and preliminary expert interviews. It is interesting to note that these statements contain what are close to paradoxes or inconsistencies. If the empirical evidence confirms these statements or some of them, it gives reason to consider the investors’ views regarding the tax issues in the SRI frame-

¹¹ The critical area can either be defined as an area between points L_1 , and L_2 , or it can be defined to proceed until the limits set by the norms of the expressly stated law.

¹² For example, the Finnish NGO Finnwatch (see <https://www.finnwatch.org/en/>) has published several research reports concerning responsibilities in the area of corporate tax behavior and responsibility for tax payments. See the example from the disquisition about Finnish state-owned companies’ tax reporting practices and their shortcomings (<https://www.finnwatch.org/en/news/336-country-by-country-reporting-lessons-from-finland>).

work somewhat inconsistent and vague. On the other hand, that kind of criticism may provide the basis for understanding and developing the roles of taxes in the SRI framework in the future.

1. The first statement is that responsible tax behavior is considered to be paying the taxes required by the relevant tax legislation. Taxes must be paid when the law requires, and to the extent the law requires. However, if this is all that is required in a company's ESG analysis, the situation invites the question of whether taxation is a real responsibility theme at all. Acting according to the requirements of the law of the land should be a self-evident responsibility. If an equivalent requirement or criterion were set for social responsibility, for example, it could mean that acting in accordance with local labor law standards in each country would be sufficient.

Obviously, from the legal point of view the fact is that the duty to pay taxes can only be based on law.¹³ Therefore this has been the most common argument proposed when some companies have been criticized by the media or NGOs for implementing aggressive tax planning activities. But what is legally acceptable, may not always be seen as responsible. For example, using holding or other offshore companies in tax havens may be fully legal, although not necessary responsible tax behavior.

In order to be a genuine responsibility issue, tax behavior and corporate tax policy issues should therefore be something beyond just fulfilling the requirements of the law. This might mean tax reporting beyond the requirements laid down by law, for example. From this point can we proceed to the next statement.

2. Companies are subject to both requirements and expectations regarding reporting on their tax payments and other tax issues. Reporting cannot, however, be a final goal in itself, but is a step toward improving tax transparency. But what exactly is it that investors are looking for in the context of discussions of and demands for tax transparency?

If the purpose of better transparency were only to ensure that taxes are paid in accordance with the tax law, then comprehensive reporting to tax authorities should be sufficient. If, however, investors want to assess whether taxes have been paid in accordance

with some other criteria, that is, non-legal criteria, what would those criteria be?

With respect to environmental responsibility, transparency makes it possible for shareholders and other stakeholders to assess the ecological effects exerted by the business, and in the context of social responsibility. For example, transparency would reassure observers that human rights have been respected, irrespective of the legal requirements of whichever states the company operates in. But what would this mean in connection with taxes?

3. Sometimes it is considered by companies and investors that complying with tax laws is the minimum requirement to discharge responsibility, and any action beyond mere compliance is a bonus. But if this is the minimum level, what is the "good thing" above it? Does it mean more taxes or more information, for instance?

The paradox of the third statement is that if companies pay taxes to a certain country above the level strictly required by the tax code and appropriate tax planning activities, the effect will be to reduce the company's after-tax profit and thus reduce the return to investors. From an economics point of view, this can only be justified through a desire to offset the reputation risk; the company may choose not to take advantage of all the tax planning tools allowed by law, if doing so could expose the company to reputation risk.

To sum up, the refined research questions are as follows:

If a company's tax responsibility is limited to ensuring the legally required level of taxes is paid, are taxation issues a *real responsibility theme* at all?

Responsibility with tax issues is often linked to tax reporting, but is it clear what this *transparency* is intended to deliver?

If investors are of the opinion that paying taxes according to the tax laws is the minimum requirement for responsibility, what would be the *optimal level* above the minimal (or economically justified) level?

5 Methodology and material of the empirical research

The empirical part of the research involves institutional investors located in Finland, where SRI practices have developed considerably in recent years (Eurosif 2010, 2012,

¹³ This principle (the rule of law, the principle of legality) is ingrained in the constitution in many countries.

2014, and Eurosif 2016). The aim of the empirical research is to find out if Finnish institutional investors take taxation (which is reported to be a topical responsibility theme among institutional investors)¹⁴ into account in their SRI practices and factors.

The research is based on a qualitative research methodology (Eriksson and Kovalainen 2008; Eskola and Suoranta 1998; Chi 1997) which has been used in research on both SRI (e.g., Sievänen 2014) and taxation (e.g., Ylönen and Laine 2015). The empirical research consists of interviews with Finnish institutional investors, who are committed to abiding by the United Nations' principles for responsible investment (UN PRI¹⁵).¹⁶ Using this group of investors to inform the research means we can trust that the investors involved are aware of their responsibilities and of ESG issues (e.g., Jemel-Fornetty *et al.* 2011) as laid out in the UN PRI (see UN PRI 2017b). Those responsibilities include incorporating topical responsibility issues on to their ESG agenda and also being broadly committed to the principle of SRI.

We did not allow investors' total amount of investments (cf. Sievänen 2014) or possible use of external ESG service providers (see e.g., Guyatt 2016) to limit our choice of research subjects. In this research, the overarching factor is the fact that institutional investors are UN PRI signatories and their registered offices are located in the same country.

We made interviews in Finnish institutional investment companies, including those managing pension funds and asset managers. We did not decide the number of the research subjects in advance but continued sending interview requests and conducting interviews until we detected theoretical saturation (Eskola and Suoranta 1998). There were total of nine interviews and had eleven representatives. Interviewee's number per interview were not ordered in forehand, instead the companies chose their own representatives. Two of the interviews were with two and the rest were with one representatives. Eight of the interviews were face-to face and one by telephone. The representatives interviewed played a key role in implementing SRI practices (see e.g., Eurosif 2016) and had a long working experience in the area of investment or banking. Their job titles included Head of Asset Management and Portfolio Manager. The respondents therefore possessed vital in-

formation on SRI practices and ESG issues (see e.g., Sievänen 2014), such as that vital to the context of the current research like taxation as a part of the SRI process and ESG information.

The interviews were conducted in October to December in 2016 and were audio recorded before being transcribed for detailed analysis. The interviewees were assured of anonymity, and the transcriptions redact information that could be used to identify the subjects, such as references to the date of signing the UN PRI. The interviews lasted between 45 and 90 minutes. We prepared semi-structured interviews to understand the role of taxation as a part of the ESG agenda in SRI and thus, to identify support or otherwise for our statements and research questions. The structured sections of the interviews consisted of questions asking how investors see taxation as a part of CSR, SRI, and specifically their ESG agenda. In addition, we left time for open discussion to encourage the interviewees to freely express their own perceptions of the topic.

We used the content analysis method to analyze the interview material (Eskola and Suoranta 1998), following Chi's (1997) suggestion for processing qualitative research material. First, we independently examined the transcripts of the interview material and the institutional investors' published SRI documents. Doing so meant each researcher formed a subjective impression of the role of the taxation as an evaluation issue of SRI. Analyzing the content of the interview material involved a trawl for repeated and vital issues and the preliminary combination of congruent themes of research. After that, we assembled to review the interview material in regularly convened research meetings. In those meetings, we discussed the observations in an endeavor to connect subjectively reviewed themes and establish segmentation. As an outcome of the collective analysis, we converged themes for each refined research question that illustrate the role of taxation and its dimensions as part of an ESG analysis. For example, themes connected to the first refined research question were *legislation, tax planning, tax avoidance* and *tax evasion*. The themes connected to the second refined research question were *tax reporting, transparency, and reputation*. The themes connected to the third refined research question were *engagement, influencing, risk, and opportunity*. Themes observed at the limits of the refined research questions were not subordinated but all themes were also observed with respect to the other refined research questions if necessary. Nevertheless, the above segmentation process clarified the analysis of the interview material when we analyzed each refined research question individually within the limits of the relevant themes. These themes and

¹⁴ See Werner and Morrow (2017).

¹⁵ See UN PRI 2017a.

¹⁶ All the interviews were conducted in Finnish, because both the interviewer and the interviewees were Finnish. Interviewees' quotes in this article have been translated from Finnish to English.

how they related to each other were analyzed more closely when we observed their positioning in relation to the context of SRI and the refined research questions. To assist content analysis, we read the interview material several times.

In addition to interviews, we familiarized ourselves with how institutional investors integrate taxation issues and their ESG analysis by researching documents retrieved from the internet, such as SRI reports and overviews, annual reports, blog posts, and other publications. This research involved document analysis, in that we strove to find confluences to the refined research questions among the documentary material—either to confirm or reject them. The use of triangulation and multiple research methods (see *e.g.*, Eskola and Suoranta 1998) was intended to deepen the understanding of the connection between SRI, taxation, and ESG information with the framework of Finnish institutional investors and to enhance the reliability of the research (see *e.g.*, Eriksson and Kovalainen 2008). In addition, we would support the contention of Finér and Ylönen (2017) based on the findings of prior studies that flaws in taxation should be investigated with a qualitative approach and based on triangulation.

6 Answers to the research questions derived from the empirical results

Question 1: If the obligation to pay taxes is based only on a legal requirement, is taxation a genuine ESG theme at all?

In this section, we look at the role of taxation as an ESG analysis factor on the basis of the interview results, and thus strive to answer our refined research questions. We analyze the interviews by addressing one statement/question at a time, after which, in the final section of our article, we draw conclusions.

Concerning question 1, the results of the empirical material indicate a clear consensus among institutional investors assessing taxation as an ESG factor that the minimum requirement is that a company complies with the tax laws of the relevant state of operation. As a matter of fact, all interviewees mentioned that as a minimum re-

quirement for tax compliance.¹⁷ This, however, does not indicate, for instance, how investors are concerned with (i) *aggressive tax planning* that is conducted within the limits of the legislative framework (*i.e.*, the letter of the law of tax statutes), while not yet being acceptable in the opinion of all stakeholders, (ii) how investors are concerned with *tax avoidance* schemes which are not illegal as such, but could possibly be tackled by general or special anti-avoidance rules, or (iii) even *tax evasion* which is prohibited and incurs criminal law sanctions.¹⁸ Therefore, we asked the interviewees to clarify their views on the topic.

Legally enforced tax planning was mainly addressed by the investors in two ways. For a majority of the interviewees, there was still no clear line on how to deal with tax planning cases in a critical area, if such is revealed by the media or in their ESG analysis. Nor did the interviewees offer a clear view of how far the tax planning or avoidance activities could go before they would adversely affect investment in the firm or lead it to be excluded from the investors' portfolio¹⁹, or when it would have an impact, for example, on the risk/return requirement of the investment.

However, the absence of a clear policy regarding the above-mentioned issues does not mean that institutional investors do not monitor the approach to taxation of the companies at all. Four interviews included a mention that the effective tax rate of companies is monitored in the ESG analysis, for example, as in the following:

The thing what I would check out is effectively how much tax the company pays and how much is legislated for, and what is the difference between the two. That explains a lot. (Institutional Investor D)

One issue and way that can be observed, is the difference between the theoretical tax requirement and the realistic payments. (Institutional investor A)

¹⁷ Institutional investors can influence the election of the company's board and its auditors (corporate governance). It is their role to make sure that the company behaves in compliance with the tax law. In other respects, institutional investors have to trust that tax authorities and other authorities will intervene if the company's behavior over taxation is not compliant with the law.

¹⁸ Regarding these levels of acceptability, see *e.g.* Uckmar 1983, p. 23 "tax avoidance can be defined as a way of removing, reducing ,or postponing the tax liability, otherwise than by means of tax evasion and tax saving ."; Thuronyi 2003, p. 156, "Tax minimization (tax mitigation, tax planning) is behavior that is legally effective in reducing tax liability." See also Knuutinen 2014a.

¹⁹ From the perspective of influencing, this disinvesting/excluding approach may be inadequate, because the issue of aggressive tax planning or avoidance practices does not vanish but would move to other investors. Effectuation of the positive change concerning this flaw could be more helpful.

Additional issues mentioned as meriting inclusion in ESG analysis were the tax strategies and policies of companies and their tax footprint. That is, investors have to monitor several tax factors and consider them as part of the ESG analysis. Several interviewees also described how they would ask companies for additional information whenever they detected any ambiguities or obscurity regarding taxation.

Nevertheless, most of the interviewees did not adequately specify what is actually analysed in terms of tax strategies, tax policies, or the tax footprint, or how they could compare companies on these issues. Such a comparison was considered challenging, for instance, because of the different practices in tax reporting and the fragmentation of information. Consequently, we could not be sure that the investors interviewed would expressly take account of tax-related issues in the ESG analysis.

We also asked the investors to supply more detail on corporate taxation as part of the ESG analysis. One interviewee reported that the ESG analysis involved consideration of corporate tax strategy, the accountable party behind the strategy, the board's possible approval of the strategy in its entirety, and the application of the tax strategy. However, the interviewee in question did not specify exact requirements for a tax strategy to support the ESG analysis. This might suggest either of two situations: perhaps investors do not necessarily know which criteria to evaluate corporations' taxation/tax strategies upon; or they assume that it is an essential task of a company board to align corporate tax payments and thus, investors do not find it necessary to analyze the tax affairs of the beneficiaries of their investment more closely.

However, we found some exceptions to the main line outlined above. One interviewee offered his more detailed policy views in relation to aggressive tax planning: if a multinational enterprise, for instance, has aggressive tax planning practices, the cash flow from that company can be considered at risk, and therefore of less value in the discount cash flow (DCF) analysis, even though such a tax planning takes place within the framework of tax and criminal law. Consequently, such a company may face more rigorous taxation in the future through the tightening of tax legislation, for example. On the other hand, if a multinational enterprise (MNE) adopts tax behavior or practices that make it likely that additional taxes will be imposed based on tax avoidance (e.g., on the basis of general anti-avoidance rule), then it will lead to conversations with the company, even if that happens only occasionally. Repeated occurrences may lead to the investor dropping the company, or at least the course of action will result in a higher risk premium in the DCF model.

The above observation indicates that tax-related factors are observed and criteria for exclusion can be related to cases where there is a need for subsequent correction of taxation collected afterward, even if there is no violation of the criminal law. In other words, in this respect, the expectations and requirements of investors for responsible tax behavior by companies can be considered to be at least to some extent above the minimum level, that is, the limits set by the taxation legislation. Our results do not, however, provide a broader or more detailed picture of what exactly are the expectations and requirements for responsible tax behavior above the minimum standards. Several interviewees responded that it is not possible to give a more general answer or a description of what would be *the optimal level*, as opposed to the minimum level, for tax planning measures or with regard to taxes more generally. Three interviewees mentioned that the question of an optimal level is company-specific and hence difficult to define at a general level.

The literature suggests, and there were also indications in some of our interviews, that the optimal level regarding tax policies and tax behavior of the companies would be that not only the letter of the law, passively, but also the spirit of the law, actively, would be followed. Ostas (2004) uses the concept pair *compliance with the (letter of) law* and *cooperate with the (spirit of) law*. The spirit of law refers to the purpose of the law. In the taxation context, the spirit of the law can mean, for example, that the companies do not fully exploit the loopholes in the law or mismatches between the different tax jurisdictions in their tax planning, when such tax planning advantages were clearly not intended by the legislators of the states concerned.

The attitude toward exceeding the limits of criminal law was more stringent than breaching the limits of tax laws, as was expected. However, several interviewees estimated that the incidence of tax evasion or tax fraud was at most very low among the kind of companies they invest in. Specifically, the investments in question are mainly directed at listed companies whose taxation on a large scale meets the clear and strict legal requirements of the countries in which they operate.

In two interviews, respondents also questioned whether it would be possible for any company to conduct illegal tax evasion or tax fraud without invoking action from the tax authorities. Consequently, tax evasion or tax fraud were considered principally harmful from the investor's point of view, but the practical significance of the issue was considered to be small. Tax planning cases within the law were considered more challenging to eval-

uate, but on the other hand, their effects were assessed as short-term and less significant.

Investors felt increased media attention on aggressive tax planning was useful because it provides them with background information to support their analysis, although they were clearly aware that the information reported by the media as such is no reason to react to the cases, and that the onus is on the investors to procure relevant information through their own information channels. One interviewee mentioned using media information in assessing tax cases but then considering in each case whether the information obtained is sufficient, and of sufficient quality, to be a driver of potential exclusion. The investors also reported that they could consult tax specialists if necessary.

Some of the interviewees mentioned that while tax issues have attracted publicity, that has increased the public discussion and debate on tax matters within the companies, and also activated thinking about how taxation might be better taken account of in the ESG analysis. However, we did not gather any concrete examples of the development steps in this regard.

Our findings suggest the interviewees are aware of the tax legislation determining tax liability and rely heavily on that being obeyed in their ESG analysis. Aggressive tax planning, conducted within the letter of the law, is not a reason to disinvest or exclude the investment from the portfolio immediately, but if such activity continues over a longer period of time, an exclusion may be involved, or it may provide a reason to raise the risk premium of the investment (and thus the yield requirement), or at least lead to discussions with the company. We found that as a minimum requirement for appropriate tax behavior, investors require that companies comply with tax laws, and at least do not repeatedly violate the limits set by law in their tax planning activities. All the investors interviewed seemed to think that taxation is an issue in ESG analysis. Some of the interviewees possessed a more structured outline of how to deal with aggressive tax planning and tax evasion cases. On the other hand, investors seemed also to be well aware of the fact that the more corporate income taxes are paid, the less return the investors will get.

Question 2: Tax transparency – what investors want to see, what they want to find out?

Tax reporting has been one of the main issues around CSR and tax activities. Tax reporting may not be a goal itself, but it is an instrument for increasing the transparency of taxation. If tax transparency is a goal for stakeholders, it

seems sensible to assume that particularly investors, given their shareholder role, would have explicitly defined criteria for what they want to see or find.

Regarding our second research question above, we observed what investors look at and what they would like to see included in the tax reporting of companies. Tax reporting has become a very topical theme; during the last few years, a great deal of effort has been made to change the tax reporting practices of MNEs, and many changes have already taken place, for instance, within the European Union. There have been stated aims to harmonize, unify, and maintain corporate tax bases, as well as to close the loopholes in tax legislation.²⁰ Stakeholders, especially NGOs and politicians, have over the last few years demanded that country-by-country reporting of taxes be compulsory for companies, in particular for MNEs. Furthermore, from an investor's perspective, country-by-country reporting will promote and facilitate tax analysis as it is easier for investors to evaluate issues like country-specific risks and thus to manage their investments (Wójcik 2015).

Generally speaking, tax reporting issues can be divided into either compulsory reporting based on legal norms and requirements or voluntary reporting. Regarding compulsory reporting, the legal requirements for large multinational companies have changed through EU-level regulation. The changes are based on the recommendations of the OECD's BEPS (*Base Erosion and Profit Shifting*) project and EU Directive 2016/881/EU²¹, both of which reflect international efforts to increase the transparency of tax information relating to MNEs.

The action plans of the OECD's BEPS project were published on October 2015. Action plan 13 concerns transfer pricing documentation and tax reporting.²² It aims to increase the transparency of transfer pricing and other tax relevant information between the tax administrations in different countries. The report includes guidelines on transfer pricing documentation and on the contents and implementation of country-by-country reporting measures. The European Union has ensured the implementation of the guidelines in the Member States by way of EU Directive 2016/881/EU.

²⁰ See COM (2016) 685 final. Proposal for a council directive on a Common Corporate Tax Base.

²¹ Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation.

²² BEPS (Base Erosion and Profit Shifting), Action 13: Final Report. Transfer Pricing Documentation and Country-by-Country Reporting.

Although country-by-country reporting (and other relevant information related to it) has become mandatory, for some businesses and situations, much remains to be done on voluntary reporting. First, the reporting obligation required by Directive 2016/881/EU is not a matter of public information, but the information is provided to the tax administration, after which the tax administrations in the various countries exchange information among themselves. Secondly, compulsory country-by-country reporting only applies to large multinational companies. As a general rule, the reporting requirement is limited to companies with at least one foreign party (or permanent establishment) in their group abroad that is not controlled by any other party, in other words, those who are the parent company of the group. In addition, it is required that the group's global turnover reported during the previous financial year is at least EUR 750 million. In Finland, for example, there are fewer than 100 companies that meet those conditions.²³

For research question two, the results of the empirical interviews are somewhat vague at best. We base that observation on the fact that in almost all the interviews the respondent stressed that transparency and openness through increased reporting and new reporting requirements is a good thing. However, with a few exceptions, the interviewees did not precisely define what transparency and openness mean in practice, or in other words, in what form those qualities are evident.

Investors did however mention some points relating to tax reporting where they expect to be furnished with more than just numerical information: the overall description of corporate tax policies or tax strategies, and the description of the tax footprint. With regard to these issues, investors were expecting a more detailed description, but the interviews did not reveal how investors use that information in the ESG analysis, or whether it is sufficient merely to ensure that the above-mentioned issues are included in the reporting. None of the interviews revealed, for example, that investors had their own internal approaches or methods for analyzing, measuring, comparing, or otherwise evaluating tax-related information as part of their ESG criteria.

Those institutional investors who rely on an external service provider to support their ESG analysis stated that taxation is currently a small part of the ESG criteria the service provider relies on to complete its analysis. In three interviews, it was also mentioned that in the (near) future the role of taxation is expected to increase in the ESG analysis

carried out by service providers and, presumably, the analysis will then be based on the joint comparison of companies. In this respect, the difficulties seen were largely the same as in the analysis of tax/responsibility issues in general. The following quotation reflects the above situation:

Currently service providers are developing indicators for their ESG analysis to measure taxes paid as an ESG issue. It is moving that way, and actually now we are at the stage when it will come here little by little, but they will confront the same problem, that of where it is based and where the boundary is drawn. But clearly there are attempts already and we are already seeing theoretical taxes per GNP... and are there factors that explain that, and why they diverge from each other. If it is not found, then we can think that there is some form of aggressive country-by-country tax planning or something else in the background, but something like that." (Institutional investor A)

In many studies and discussions, tax transparency has been linked to the company's reputation and image, in that the more transparent and detailed is tax reporting, the greater the positive effect it creates for the company's reputation and image, and vice versa (EY 2015). In this context, the interviewees considered the factors linked to reputation, for example, as follows:

And of course benefits for those who want to be as open as possible and grow to trust, so this (tax reporting) of course offers a way to do that. Certainly, nobody is forbidden to do this kind of reporting before and some are nevertheless doing it a bit. Therefore, it is possible, that it will grow trust and in that way present a positive picture of the company. (Institutional investor B)

So, let's say that there is very aggressive tax planning in question, it is a reputational risk to the company, it needs to be evaluated, and if there is such advanced tax planning, then we may have to exclude that investment. But these cases demand advanced analysis and procurement of the information before this kind of conclusion can be made, because we have to know every regions' tax legislation practices, corporate structures, and how the business is organized, to analyze where the profits are entered as income and where the profits are located after earning. In this respect it is important to get information and transparency but it is very challenging work that we try to do. (Institutional Investor C)

As the above quotations illustrate, in the interviewees' view, the reputation associated with tax reporting is combined with transparency, increased confidence, and a positive corporate image. In addition, the UN PRI suggests that these elements will be consequences of more detailed tax reporting and will thus help investors evaluate tax-specific risks more closely (UN PRI 2015a).

Asked about the disadvantages of tightening tax reporting requirements, such as implementing country-by-country reporting, investors spoke of the increasing costs to companies and the disclosure of competitive factors.

²³ See Government Proposal 142/2016.

These issues were also raised in the study prepared by PwC for the European Commission, which did also identify some positive impacts as well (European Commission 2014).²⁴ As a challenge, from the investors' perspective, our interviewees mentioned the difficulties of comparing companies and their tax reports. In Europe, however, the country-by-country reporting requirements set by the EU directive are expected to harmonize tax reporting and thus improve comparability (European Commission 2016).

When asked about the implications of these legislative changes for the role of taxation as an ESG factor, all respondents welcomed this change from the legislators, as the following quote reflects:

For each company, it is possible to get a better view of how the company pays its taxes and where, and when in principle we can begin to think about the upcoming political change for example, then it is easier to analyze what it means to the company, when we have more detailed information. Company analysis will sharpen in many ways, responsibility for one but in other ways too. (Institutional investor D)

More stringent tax reporting requirements and improved information as a consequence were seen as a potential factor heightening the analysis of tax issues. On the other hand, no concrete examples of how to use this improved information in the ESG analysis were presented, even though examples were requested in the interviews.

In evaluating the benefits of tightening the tax reporting requirements, it was also noted in several interviews that the estimates of the effects of tightened tax requirements are only hypothetical, which would suggest that investors have no clear picture of what is actually expected of tax reporting—or if they have, they are not willing to tell outsiders.

²⁴ Regarding the positive impacts, the report noted: "The results from our analysis provide some evidence that disclosure quality has a positive impact on capital market outcomes (by lowering a firm's effective cost of equity capital), improves transparency (by improving the accuracy of analysts' forecasts) and reduces the likelihood of earnings management, thereby improving accounting quality. There is also some evidence to suggest that the public availability and granularity of financial information reduces a firm's effective cost of equity capital, which provides support for CBCR to lead to beneficial outcomes for banks. However, it should be noted that the magnitude of the potential impacts are likely to be small."

Question 3: Minimum level vs. optimum level: would "something else" mean more taxes or more information?

Concerning question 3, we investigated the role of investors in influencing corporations' approaches to their tax responsibilities. In this regard, we found that the interviewees did not actively aim to influence tax practices such as tax policy, tax strategy, tax reporting, or material issues of taxation. The interviewees did not, for instance, give any examples of their own role, or the role of investors in general, in combating tax avoidance, aggressive tax planning, or other issues for the investors. Instead, interviewees highlighted the role of legislators and authorities in combating aggressive tax planning and other tax-related disadvantages.

Almost all of the interviewees reported that in their ESG analysis they consider whether the company has a corporate tax policy or tax strategy, but they did not clarify what content elements are required in the policy or strategy. One interviewee mentioned explicitly, and others mentioned indirectly, that regarding the companies and their tax issues, something else beyond merely the legal requirement is expected, however, the interviews failed to elicit a more detailed definition or examples of that.

All of the interviewees welcomed the increasing volume and improving quality of tax information, as a result of a pressure for increased reporting. The position of the investors interviewed can be explained by the fact that investors have specifically been found to be the main user group for tax reporting information (Murphy 2016). Nonetheless, our detailed analysis did not find signs that investors would like to influence the tax practices of the companies, although they showed interest in evaluating tax information in their ESG analysis. The interviewees highlighted the strategies of *engagement and voting* and *exclusions* (see e.g., Eurosif 2016); if cases or suspicions of aggressive tax planning emerge among existing investment clients, it serves as a basis for heightening the discussion on influencing, whereupon further information and clarification is requested. We did not see any concrete tax-related indicators, beyond the legal requirements, that would be monitored for the purpose of influencing efforts within the limits of the strategy of *engagement and voting*. For some investors, aggressive tax planning might be a reason to exclude the company concerned, if such tax planning is consciously planned and occurring continually in the long term. However, such an outline did not come out in all interviews.

Our perceptions of the responsible investment strategies presented above support the research findings stating that the engagement and voting strategy was the third

most commonly applied, and exclusion was the most common SRI strategy used by the Finnish institutional investors in 2015 (Eurosif 2016). In addition, tax issues can be seen as an ESG factor or component of those strategies. Our observations suggest that in terms of tax issues there might be some influencing, if tax compliance were uncertain or there were signals that compliance with the legislation was not being maintained. However, we did not elicit evidence of aims to influence tax behavior or other tax issues from the interview data, be that in its wider societal context or in a situation where no actual tax compliance problems have been observed.

Consequently, we do not really see taxation to be an issue on the impact investing agenda of institutional investors. The interviews did not show that investors play an active role in changing the tax behavior or tax practices of companies through pushing a responsible investing process, which is typically associated with impact investing. This rather passive role may arise from the fact that investors do not have an exact benchmark on how this kind of influencing in taxation terms should be implemented. Generally, with impact investing practices, investors strive to promote the positive realization of ESG factors, and also to observe the performance and measure the progress in terms of ESG along with their economic return targets (see e.g., Hebb 2013; Hyske *et al.* 2012). Our observation concerning tax issues thus runs counter to the topical consensus on SRI strategies and ESG issues, which is that impact investing is likely to play a greater role across Europe and thus also among Finnish institutional investors (Eurosif 2016).

In summarizing the findings from the interviews it can be noted that regarding the investment process and ESG analysis, the institutional investors observe and consider that tax policies and strategies of the companies exist, the legal requirements of tax and criminal laws are adhered to, and there is tax reporting on relevant issues. In addition to this, we found little evidence that investors actively feel the need or desire to affect the taxation policies of companies. Based on the interviews, we did not get any clear picture as to whether “something else” beyond the legal minimum requirements would mean more (or different) information or more taxes.

When responsible investing is conducted in a proactive manner, investors strive to achieve a positive impact on the environment, society, and governance, and they monitor and control both the risks and the opportunities connected to those ESG factors (Hebb 2012). Moreover, taxation is identified as an ESG factor (e.g., UN PRI 2015a; Hyske *et al.* 2012). However, the contradictory observations of our study compared to previous research raise

the question of whether taxation really is an ESG issue. As many research articles have noted, responsibility is something that goes beyond compliance with legislation (Sparkes and Cowton 2004, see also Sievänen 2014).

What does our study thus say about how Finnish responsible institutional investors think and act toward the tax issues of the companies they are investing in?

The following quotes are addressed by the arguments below:

There is a nation state based, kind of a world political order, and on the other hand there is a global market economy, so it is in my opinion quite obvious, that it causes conflicts between two different systems, and one of the reasons is this taxation of the multinational enterprises. It won't necessarily affect us, because we are quite a small investor and invest also in the local companies rather than multinational enterprises...so it means that this problem, it will not exist in the same scale for us than if our investment portfolio were full of multinational enterprises. (Institutional investor E)

We thought that many or some of these cases [tax planning]... In the listed companies, where we work, these cases are notably few in number. And maybe the general situation has gone in the direction where companies also pay more attention to the taxation issues. (Institutional investor F)

I don't know if that is possible... either taxes are paid or not, am I right? Either they are paid according to legislation or something other is done. It is binary in my opinion, there is not the kind of continuum as in social issues. But taxes are taxes and there are certain constitutions for them and those constitutions have to be followed (Institutional investor D)

As the excerpts convey, an investor's absolute size, the volume of assets under management, and the challenges in analysis concerning tax issues may explain the current relatively low weight of tax issues in the ESG analysis. In international terms, Finnish institutional investors are comparatively small investors and the extent of their investment operations are not substantial. In many cases investments are first made in local companies or larger international listed companies whose tax compliance is assumed to follow the legal requirements. (On the other hand, one could add here that many companies with the largest market value in the world, even among top 10, have been criticized for aggressive tax planning schemes.²⁵) Furthermore, a relatively small volume of assets under management may constrain an individual investor's options to exert influence. Finally, but importantly, regarding tax issues, it is often hard to say what is right and what is wrong. That creates challenges for an ESG analysis as well.

²⁵ See e.g. Christians 2013; Fisher 2014.

7 Conclusion

Responsible Finnish institutional investors seem very much to equate corporate responsibility with ensuring taxes are paid in accordance with the tax laws. This is generally considered to be the minimum level of responsibility. However, it is not clear what activity could lead to an optimum level beyond the minimum level. Would it be more information, improved or more versatile information, or would it be more taxation, that is a greater economic contribution to a country a company operates in?

The paradox is that if the minimum level of responsibility means more taxation, then the result would be lower returns for the investors. If that minimum level of responsibility instead means providing more information, however, it is not clear what reaching the optimal level would require. Very often the tax responsibility is connected to tax reporting, but according to our interviews it is not quite clear what the ultimate goal of transparency is. Even though taxation seems to be part of the ESG agenda, its role is still unspecified, and on occasion even contradictory and paradoxical.

If the tax responsibility only equates to compliance with taxation legislation, then one might ask whether taxation is a realistic independent SRI issue at all. Is it just a question of tax matters being treated properly as part of good governance? Is taxation a theme with *content elements*, or just related to good governance in the sense that the formalities have been adhered to?

Based on interviews and other research material used we can draw some conclusions on the alternative approaches to SRI and taxes. The level of *legal requirement* is the basic level of responsibility. Companies must conduct in their tax affairs within the framework of law and pay their taxes to the extent required by law. This approach does not directly exclude forms of tax planning that do not violate the absolute limits of criminal law, or which cannot be tackled with legal means like general anti-avoidance rules or doctrines. It is worth noticing that undertaking so-called aggressive tax planning would constitute acting within this framework.

Nevertheless, aggressive tax planning may cause problems to companies, and as a consequence to the investors as well. Reputational risk can materialize as a behavior among customers or, for example, as the dissatisfaction of existing and potential employees. Furthermore, those cash flows that have been obtained through aggressive tax planning may be more risky than usual, which is worth considering in DCF models. For those reasons, it is worth assessing the risks and impacts of aggressive tax

planning in ESG analyses. Whenever a company is conducting tax planning *in the critical area*, that kind of risk-based evaluation makes sense only from a financial point of view, without any moral or ethical dimensions being involved.

Tax issues also provide a potential theme for *engagement and voting* and also for *impact investing*. At this level, however, there may be contradictions between the influence objectives and the investor's financial objectives, at least in the short term; specifically, paying more in taxes means less profit. Supporting good tax practices, or tackling some of the disadvantages, can be productive for all investors in the long run. The contradiction between these objectives means that balancing skills may sometimes be needed.

Such balancing skills would include both companies and institutional investors—while acting professionally and carefully—taking into account, especially in cross-border situations, a variety of tax issues. That means implementing tax planning. International taxation with many jurisdictions and tax systems, and with thousands of tax treaties is not an automated integrated entity, and nor does it constitute an integrated and coherently functioning system. Therefore, failures in tax planning can lead to, for example, double taxation situations.

On the other hand, the return requirements of investors cannot mean that responsible business directors and managers should take advantage of the full benefit derived from mismatches, distinctions, and discontinuities between different tax systems. This could be one tangible goal of SRI strategies including influencing engagement and voting and impact investing in the context of taxes.

There are some signals that big international investors are actively influencing the taxation practices of companies. Norges Bank Investment Management (NBIM) responsible for managing the Norwegian Government Pension Fund Global, with assets worth about 850 billion euros (which probably makes it the largest stock owner in Europe) in April 2017 set out its expectations of companies in terms of tax and transparency. The document states NBIM will, as a starting point and where appropriate, base its practices on internationally recognized standards such as the UN Global Compact, the UN Guiding Principles on Business and Human Rights, the G20/OECD Principles of Corporate Governance, and the OECD Guidelines for Multinational Enterprises.²⁶ In the United Kingdom, the Local

²⁶ See Norges Bank Investment Management: Tax and Transparency: Expectations Towards Companies. The Norwegian Government Pension Fund Global (“The Oil Fund”) has been regarded as a

Authority Pension Fund Forum has raised corporate tax transparency as one of its engagement themes.²⁷ It remains to be seen how extensively other institutional investors in different countries follow these kinds of approaches.

For companies and investors, there will always be a need for some tax planning. However, as stated earlier in the article, it may not be easy to say what kind of tax planning is socially responsible and what is not. It may be that investors need a second opinion; ratings or certifications, like the UK's Fair Tax Mark²⁸ could be helpful when this line is drawn in the future.

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²⁷ See http://www.lapfforum.org/engagement-themes/corporate_tax_transparency/. The Local Authority Pension Fund Forum (LAPFF) is a collaborative shareholder engagement group that consists of over 70 Local Government pension scheme funds from across the UK).

²⁸ See <https://fairtaxmark.net/>. A business with the Fair Tax Mark is certified as paying the right amount of tax in the right place at the right time and applying the gold standard of tax transparency.

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