ESG ON TAXATION
THE ROLE OF LEGISLATORS AND TAX AUTHORITIES

VIEIRA DE ALMEIDA

by Francisco Cabral Matos
Managing Associate of the Tax practice

Contacts:
fcm@vda.pt
Rua Dom Luís I, 28
1200-151 Lisboa
Portugal
(+351) 21 311 3400

Francisco Cabral Matos joined VdA in 2007. Managing Associate of the Tax practice where he has been involved in several corporate transactions, namely in corporate restructuring, banking and finance, international tax planning and tax litigation.
Francisco has also been providing tax and legal assistance in numerous private wealth transactions and private client planning.

It is beyond questioning that the way tax matters are collectively perceived is rapidly changing. The Principles for Responsible Investment (PRI) are a game changer for tax transparency, as they give the floor to companies and their stakeholders to establish what is (or should be) the level playing field for taxation. By linking fair taxation with reputational risks, Environmental, Social, and Corporate Governance (ESG) trend brings the discussion from *tax legality* to *tax morality*.
This is a much bigger challenge, as tax morality is hardly consensual and depends on the relevant social, economic and political context. Therefore, although the media spotlight is mainly on taxpayers, it is key that national legislators and tax authorities are also part in the ESG movement.
Companies are welcomed to disclose their tax planning strategies, to improve reporting towards investors and to publicize their position on tax risk management and interaction with tax authorities on a country-by-country basis[1]. For this self-assessment process, it is interesting to note that ESG guidelines measure the "tax risk appetite" by reference to the likelihood of a tax dispute with tax authorities[2], rather than the likelihood of losing a dispute at court. ESG seek to promote fair(er) taxation, but also to less litigation.
To that end, it is critical that tax authorities enhance cooperation with taxpayers and collaborate with each other on a cross-border basis. Quite often, cross-border tax disputes are

1. The author refers to the *Explanatory Notes on Investors' Recommendations on Corporate Income Tax Disclosure*, available at https://www.unpri.org/download?ac=4655.

2. The unrecognised tax benefits or UTB are characterized as "tax positions being taken by a company that management believes are less than 50% likely to be upheld by a tax authority" (see *Explanatory Notes on Investors' Recommendations on Corporate Income Tax Disclosure)*.

questioned only in one of many jurisdictions involved. In this regard, ESG guidelines underline that "*[s]ome jurisdictions with statutory tax rates that are in line with global averages will provide companies with individual incentives, to entice investment into the country.*"[3] ESG guidelines put said tax incentives side-by-side with the use of tax havens and shelf companies, as potentially abusive/aggressive planning. This means that ESG is also inviting sovereign States to review their own tax policies. The inability of sovereign States to set common terms for business taxation highlights how challenging the task is for companies – ESG invites taxpayers to search for tax morality, while countries are unable to set the standard for fair taxation – and how important it is for having all parties onboard.

Notably, the world economic recovery in the post-pandemic requires all companies to be as efficient as possible, notably regarding their tax strategy. Thus, it is crucial that national legislators and tax authorities improve legal certainty and participate in drafting a cohesive international tax framework. In this regard, the implementation of the Mandatory Disclosure Directive (DAC 6)[4] was a milestone in EU, improving tax transparency. The extensive guidelines issued by European tax authorities on how taxpayers should comply with reporting obligations[5] contrast with the lack of guidelines or harmonized positions on core tax issues, such as the application of EU Directives and double tax treaties. It also contrasts with the fact that EU Member States have been discussing business taxation since at least 2011 (with the first proposal for a *Common Consolidated Tax Basis* or CCCTB)[6] and remain unable to reach consensus. The *Business in Europe: Framework for Income Taxation* (or BEFIT) has been included in the EU tax agenda for the coming years[7] and intends to reform of the (European) international corporate tax framework.

Taking into consideration the deterring effect on investment that results from increasing tax compliance costs and uncertainty on legal frameworks, it is of essence that the EU legislator and EU tax authorities also undertake to abide by the ESG spirit and promote clarity (not complexity) in the European tax framework.

There is no question that tax transparency is a common goal and that companies (especially MNE) have a relevant role in promoting it, namely through ESG policies. But one should expect a similar, if not higher, commitment from EU authorities, national legislators and tax authorities, towards setting common grounds for fair taxation.

3. See *PRI Engagement Guidance on Corporate Tax Responsibility*, available at https://www.unpri.org/download?ac=5601.

4. Council Directive (EU) 2018/822, of 25 May 2018.

5. E.g. German guidelines exceeded 70 pages; Irish guidelines exceeded 60 pages.

6. The initial proposal dates back to 2011 (see the Proposal for a Council Directive on a Common Consolidated Corporate Tax Base available at https://ec.europa.eu/taxation_customs/system/files/2016-09/com_2011_121_en_0.pdf).

7. Available at https://ec.europa.eu/commission/presscorner/detail/en/ip_21_2430.