NORGES BANK
INVESTMENT MANAGEMENT

Ministry of Finance
Akersg. 40
Postboks 8008 Dep

Date: 24.01.2018
Your ref.: 17/439 - 12
Our ref.: 18/00100

Expectation document on tax and transparency

We refer to the Ministry's letter of 14 June 2017 on the Storting's consideration of Report to the Storting No. 26 (2016-2017) on the Management of the Government Pension Fund in 2016.

In its letter, the Ministry refers to the Standing Committee on Finance and Economic Affairs' Recommendation 357 S (2016-2017) on the white paper. In this recommendation, the Standing Committee notes that Norges Bank has prepared a new expectation document on transparency in international corporate taxation. The Standing Committee states that it has high hopes for the follow-up of the expectation document and looks forward to reading about this work in the spring 2018 white paper. Against this background, the Ministry asks Norges Bank to report on its work on the expectation document on tax and transparency.

Responsible investment supports the overall objective of safeguarding the fund's assets for the long term. We work on standard setting, ownership and risk management as an integral part of our management of the fund. We communicate our expectations and positions as an investor to the companies the fund is invested in through public documents, voting and other direct engagement. As well as tax and transparency, we have published expectation documents on climate change, water resources, children's rights and human rights.

This letter provides a status for our work on tax and transparency in the management of the fund. This is a long-term undertaking. Norges Bank will continue to report on its work on the expectation documents in its annual report on responsible investment, in line with established practice.

The goals for our work on tax and transparency

The expectation document on tax and transparency was published on 7 April 2017. Norges Bank stresses the importance of transparency and good reporting at portfolio companies in building trust, counteracting the consequences of secrecy and supporting fair taxation across jurisdictions. As a long-term global investor, Norges Bank wishes to promote standards and practices that contribute to a level competitive playing field and are long-term sustainable.

The topics covered by the document are also the target of regulatory changes in many countries, and general expectations of companies when it comes to tax are evolving.

First of all, Norges Bank would stress that tax levels and the enforcement of tax legislation are matters for the authorities rather than investors. Taxation is a matter of national sovereignty. It is not natural for Norges Bank to take a position on an individual country's tax policies. At the same time, the taxation of multinational enterprises must take place within the framework of global collaboration between nation states. Taxation across jurisdictions affects competition between companies. Investors therefore have a role to play in promoting good international standards, transparency and better practices at multinational enterprises, so contributing to legitimate and well-functioning markets.

International work on co-ordination to avoid erosion of tax bases therefore deserves support from an investor perspective. In time, Norges Bank assumes that national implementation of the likes of the OECD's Base Erosion and Profit Shifting (BEPS) package will create a more predictable and consistent international framework for corporate taxation. The BEPS project was launched at the G20 summit in Los Cabos in June 2012 and has since been followed up with various reports and action plans. The actions developed by the BEPS project were unveiled on 15 October 2015 and have now moved into an implementation phase. Norges Bank supports this work under the auspices of the OECD. More than 100 countries have signed up. It will contribute to a more level playing field and make the creation of complex tax structures less attractive. It is further expected to reduce the use of secrecy jurisdictions and the potential negative consequences thereof. Greater transparency can also make it easier for investors to assess companies' strategy and any risks associated with international taxation.

The expectation document on tax and transparency

Norges Bank's ownership work takes advantage of the fund's long-term investment horizon and is constantly evolving. The expectation document forms a point of departure for our dialogue with multinational enterprises on tax and transparency. Norges Bank takes a principles-based approach and emphasises the importance of transparency and good reporting for building trust, counteracting the consequences of secrecy and supporting appropriate taxation across jurisdictions.

Norges Bank's expectation documents are directed at company boards and serve as a starting point for dialogue. As a long-term global investor, Norges Bank supports standards and practices that contribute to fair competition. We promote well-functioning, legitimate markets and market solutions that are long-term sustainable. A company's board and management are responsible for its strategy and operations. We are particularly interested in companies' governance processes and reporting. As a shareholder, we may raise concrete issues and elaborate on our expectations at meetings with companies. On the other hand, our dialogue with company representatives must not extend to micromanagement.

The aim of the expectation document on tax and transparency is to communicate how Norges Bank, as a financial investor, expects multinational enterprises to exhibit appropriate, prudent and transparent tax behaviour. Corporate taxes provide public revenue the world over and may be particularly critical in emerging markets. Companies for their part benefit from society's legal and financial infrastructure.

The expectation document is rooted in international principles, including the OECD Guidelines for Multinational Enterprises and the G20/OECD Principles of Corporate Governance. The document was drawn up in a process with broad input from external stakeholders, including NGOs, experts and academics.

The expectation document is based on three main principles. The first is that taxes should be paid where economic value is generated. The second is that company tax arrangements are a board responsibility. The third is that public country-by-country reporting is a core element of transparent corporate tax disclosure. The document's emphasis on public country-by-country reporting can be seen in the light of ongoing regulatory changes in many places.

In the document, we stress that corporate tax strategies may pose a risk to investors, especially in periods of regulatory change. We also emphasise that boards should ensure that strategic decisions are driven by long-term value creation. We wish to support boards in their work on creating long-term value. We expect companies to be prepared to explain publicly the business case for locating subsidiaries in secrecy jurisdictions or in significantly low-tax environments where any local operations are limited in relation to the economic value attributed to them.

As a minority shareholder, we can take a systematic and principles-based approach, but it is not possible for us to force companies to modify their tax behaviour. In parallel with our own work, we find that tax issues are currently the subject of growing investor interest. However, investors rarely have an opportunity to closely monitor the tax strategies that companies adopt.

Our work on the expectation document

In 2017, we worked both specifically with various companies on particular issues and more generally with our largest investments. The expectation document lists nine expectations that we believe companies should address, divided into two main categories. It is these expectations that we follow up with companies. As part of this work, we sent letters about the expectation document to the 500 largest companies in the fund's portfolio. We have received replies from about 50 of them.

This correspondence has provided us with information and opinions from these companies, including on the two main categories defined in the expectation document, the first being board responsibilities and policies. In line with our expectations, many of the companies confirmed that tax is a board responsibility. We have received more information on how the boards of these companies follow up tax matters, and on tax management policies at the companies. Some multinational enterprises have begun to publish their tax policies.

The second main category defined in the expectation document is disclosure. The companies have given us a range of opinions in this area, particularly on public country-by-country reporting. Many plan to share country-by-country information with national authorities, but some are reluctant to disclose such information publicly until new legislation is in place. Some companies cite commercial challenges associated with public country-by-country reporting, but they also state that they will comply with official requirements in this area when the time comes.

The expectation document also raises questions about the use of secrecy jurisdictions. In our correspondence, some companies stated that they are opposed to the use of such jurisdictions. This dialogue with companies has also provided confirmation that our support for the BEPS project is appropriate.

Some of the companies we contacted say that they share our position on tax and transparency, and a number confirm taking a strategic approach to corporate taxation at board level. We recognise, however, that our expectations far from reflect current corporate practices, and we believe that clarity from us as an investor could send an important governance signal about what kinds of tax practices create value for companies and society in the long run.

The replies we have received will form part of the basis for our active ownership work and further follow-up of tax and transparency at the companies we invest in. We expect corporate practices in this area to continue to develop, and we will support company boards in their work on meeting investors' expectations. In 2018, we will work further on the concrete input from companies responding to our letter. We will also contact companies that have not replied. We will attach importance to disclosure in our interaction with companies.

Our managers build up significant specific knowledge of companies and taxation. Understanding individual companies' situation and opportunity set is important when assessing more general data. We are keen to obtain sufficient information so that we can better assess the risk associated with companies, sectors and markets. The starting point for such information is corporate reporting. This information can then be compared with third-party analyses. We included third-party information on tax in our data set in 2017. This information is relevant for investment and ownership purposes as well as for risk management. It does not, however, extend to all of the areas covered by our expectations, or to all of the companies in the portfolio. We will continue to work on improving the information we have on companies' tax practices, and also, over time, our own analyses. We have found that information from independent organisations can be useful in this work.

One goal for us is to encourage portfolio companies to address developments in international tax rules. In addition to the work targeting individual companies described above, we have taken part in conferences and panel discussions on tax and transparency, including the PRI annual conference, in order to present our expectations. We participate in these fora to contribute to a better understanding of key issues in the relationship between company and investor, and better practices.

We have seen considerable interest in our document, and that the position underlying our expectations is shared by many institutional investors. In December, we submitted a consultation response to the EU on the taxation of the digital economy. We are keen to contribute to a framework that is predictable, consistent and appropriate given new economic structures and dynamics across markets.

We will use the means available to us as an investor to help further increase corporate transparency on tax policies and reporting, in line with the topics highlighted in the expectation document. We will develop our analyses and emphasise this issue in our ownership work. In time, we expect to see changes in both regulatory requirements and corporate disclosure that result in more consistent information across sectors and markets, and further examples of good practices among the companies in the portfolio.

Yours faithfully

Yngve Slyngstad   Carine Smith Ihenacho