



# **Tax responsibility principles in Finland's development cooperation funding to the private sector**

**Policy paper**

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# Tax responsibility principles in Finland's development cooperation funding to the private sector

Prime Minister Sanna Marin's Government Programme (10 December 2019) committed Finland to support active and proactive solutions for combating and hindering the operation of tax havens, both within the European Union and throughout the world. According to the Government Programme, companies in which the state has a controlling interest will have to show an example of corporate responsibility by reporting their tax footprint in each country in accordance with ownership steering guidelines. Aggressive tax planning will not be tolerated. Companies that receive development cooperation funds will be obligated to meet tax responsibility and transparency criteria, promote human rights and advance Finland's development policy goals.

On 9 June 2020, the Ministry for Foreign Affairs of Finland published the *Taxation for Development Action Programme 2020-2023* to implement the Government Programme's objective to contribute to improvements in the taxation systems of developing countries. One part of the programme is to ensure the tax responsibility of companies receiving Finnish

development cooperation funding (i.e. official development assistance, ODA<sup>1</sup>), as required in the Government Programme.

The objective of this policy paper is to outline the key principles of tax responsibility in Finland's official development cooperation funding to the private sector. This policy paper also provides general guidance on the implementation of these principles in the main channels of Finnish ODA to the private sector; Finnish private sector instruments and funding through multilateral development banks and other international organizations and funds. Based on this policy paper, the strategy or guidance as well as implementing guidelines will be created or updated for each Finnish private sector instrument. This policy paper has its foundations in international standards set by the UN, OECD and the EU. It is aligned with Finland's domestic policies such as the State Ownership Steering Policy (8.4.2020) and the Action Programme against Aggressive Tax Planning (12.3.2014).

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1 Development cooperation funding and official development assistance (ODA) are used interchangeably in this policy paper. Finland adheres to the OECD DAC definition of official development assistance (ODA) ("official development assistance flows are defined as those flows to countries and territories on the DAC List of ODA Recipients and to multilateral development institutions which are provided by official agencies, including state and local governments, or by their executive agencies; and each transaction of which is administered with the promotion of the economic development and welfare of developing countries as its main objective and is concessional in character." (<http://www.oecd.org/development/financing-sustainable-development/development-finance-standards/officialdevelopmentassistance-definition-and-coverage.htm>))



## Contents

1. Taxes play a vital role in achieving the SDGs .....	3
2. Key principles.....	4
3. How the principles can be implemented.....	5
3.1. Instruments or funds in which the Finnish government is the largest or only funder .....	5
3.2. Private sector funding through ODA projects and programmes directly financed by Finland.....	8
3.3. Private sector funding through multilateral development bank operations or other global funds.....	8
4. The monitoring and evaluation of the policy .....	9

# 1. Taxes play a vital role in achieving the SDGs

Finland is committed to the achievement of the Sustainable Development Goals (SDGs) and supports economically, socially and environmentally sustainable development in its actions both at home and abroad. Achieving the SDGs requires both national and international public and private funding. Developing taxation, fighting corruption and combatting illicit financial flows are key components in this endeavor.

Taxes are typically the most important source of government revenue in nearly all countries, as well as central to fiscal policies and macroeconomic stability. Taxes are also a key mechanism by which businesses contribute to the economies and societies of the countries in which they operate. Their contributions can be, for instance, in the form of corporate tax, income tax and social security contributions of employees that companies help to collect, various licence fees, levies and customs duties, or value-added tax on the consumption of goods and services provided by companies. Tax revenue allows a country's government to structure and provide services such as education, health and social care and infrastructure for its people, thereby reducing poverty and inequality.

Aggressive tax planning and illicit financial flows are serious matters given the major impact they have on the domestic

revenues of developing countries. If companies seek to minimize their tax obligations in a jurisdiction, they might deprive the government of revenue, hence reducing the availability and access to some key public services the country needs to achieve the SDGs. Perceptions of tax avoidance by companies could also undermine tax compliance more broadly, by driving other companies to engage in aggressive tax planning based on the view that they might otherwise be at a competitive disadvantage. Awareness of tax avoidance or other unfair tax practices may also negatively impact citizens' morale to pay taxes.

Taxes, social security contributions<sup>2</sup> and other tax-like fees paid to the government are key building blocks in the development of well functioning societies which is one of the four focus areas of Finland's development policy. The Government of Finland supports the private sector in its official development cooperation in various ways. Therefore, the Government Program requires the Ministry for Foreign Affairs of Finland to obligate all companies benefiting from Finland's official development assistance (ODA) funds to commit to the tax responsibility principles presented in this policy paper.

<sup>2</sup> These include, for instance, employers' share of compulsory social security payments. A more thorough definition is provided by the OECD (<https://data.oecd.org/tax/social-security-contributions.htm>).



## 2. Key principles

All companies receiving Finland's official development cooperation funding (ODA funding) are required to act in a tax responsible way. This includes following the key principles set out in this document, as well as other UN, OECD and EU principles of good governance and fight against all forms of corruption. The companies are also encouraged to integrate corporate responsibility more broadly into their business practices and show results-based corporate responsibility leadership.

Good tax management of companies is understood as described in the OECD guidelines for Multinational Enterprises. This includes that the companies should comply "with both the letter and the spirit of the law and regulations in all countries in which they operate" as well to cooperate "with authorities and making information that is relevant or required by

law available to them".<sup>3</sup> Other additional good international practices are also encouraged to be followed.

National tax laws and regulations are not always sufficient to ensure responsible tax behaviour, especially when it comes to regulating international operations of companies. Therefore, in addition to the above-mentioned OECD guidelines, the Finnish Government requires a commitment to the following key tax responsibility principles from all companies receiving Finnish ODA funding. This is in line with the requirements from all state-owned companies as defined in the Government Resolution dated 8.4.2020. In addition, the companies receiving funding are strongly encouraged to choose partners that respect these principles in their operations.

**NO AGGRESSIVE TAX PLANNING:** The Finnish Government does not tolerate aggressive tax planning by any of the companies receiving Finnish ODA. The Finnish Government uses the OECD definition of international aggressive tax planning (profit shifting). This refers to tax base erosion and profit shifting (BEPS) of multinational enterprises that can establish intra-group arrangements achieving no or low taxation by shifting profits away from jurisdictions where the activities creating the profits are taking place<sup>4</sup>. Aggressive tax planning can e.g. involve arrangements that shift profits from a developing country, where they have been generated, to a tax haven.

**TAX HAVENS:** To combat and hinder the operations of tax havens, the Finnish Government does not allow investing its ODA funds through investment funds or holding companies registered in countries on the evolving EU list of non-cooperative tax jurisdictions<sup>5</sup> and/or that are not compliant or are only partially compliant with the progressively tightening standards<sup>6</sup> of OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes.<sup>7</sup>

**TAX HOLIDAYS:** Governments use tax incentives to attract foreign investments into desired sectors and technologies. Such measures, for example tax holidays, should be available to everyone on similar grounds in similar situations. Companies receiving Finnish ODA should not distort fair competition by requiring or encouraging tax holidays and other similar tax incentives that are not available to all other potential investors considering or making similar investments. This does not require them to pay more taxes than what is required by the local legislation and authorities.

**TRANSPARENT REPORTING:** To ensure tax responsible behavior, companies receiving Finnish ODA must operate transparently and report their economic activity, income, profit and taxes paid in each tax jurisdiction in which they operate<sup>8</sup>

3 See the full description in the [OECD Guidelines for Multinational Enterprises, chapter on taxation](#)

4 OECD: Measuring and Monitoring BEPS, page 18. See: <https://www.oecd.org/tax/measuring-and-monitoring-beps-action-11-2015-final-report-9789264241343-en.htm>

5 The EU list is available on [https://ec.europa.eu/taxation\\_customs/tax-common-eu-list\\_en](https://ec.europa.eu/taxation_customs/tax-common-eu-list_en).

6 The OECD list is available at <http://www.oecd.org/tax/transparency/documents/exchange-of-information-on-request-ratings.htm>

7 Direct investments can be made in all developing countries and the companies and financial institutions operating in them as long as there is no profit shifting involved.

8 State-owned companies show an example of transparent reporting by reporting their tax footprint on a country by country basis in accordance with the guidelines provided by the Prime Minister's Office.



## 3. How the principles can be implemented

Finland supports the private sector in its official development cooperation in various ways, ranging from large funding through multilateral development banks, investments in companies or funds to small grants for piloting new business ideas or assessing environmental and social impacts. In addition, the mixed-credit instrument PIF, although it is an instrument to support public sector investments, in practice facilitates private sector exports as well.

The Ministry for Foreign Affairs of Finland (MFA) can directly influence the policies and management practices of Finnish private sector instruments and bilateral ODA projects and programmes, whereas the operations of international organizations, multilateral banks and various funds as well as multi-donor programmes are guided by their own policies that Finland can aim to influence in the long term. Therefore, the general implementation guidance of this policy is divided into three sections covering the Finnish private sector instruments, support to the private sector through ODA programmes directly financed by Finland and, the support to the private sector through other organizations.

The Ministry for Foreign Affairs procures services from private sector companies using funds classified as ODA and private companies also implement Finland's development cooperation programmes as service providers. Procurements from the private sector are not understood to constitute receiving ODA funds in the context of this policy paper.<sup>9</sup>

### 3.1. Instruments or funds in which the Finnish government is the largest or only funder

At the time of writing this policy paper in 2020, the instruments channeling ODA funds to the private sector<sup>10</sup> in which the Finnish government is the largest or only funder include:

<sup>9</sup> However, the Ministry for Foreign Affairs does include tax responsibility principles in its exclusion criteria and service agreements, as provided by national public procurement legislation. As part of the implementation of the Government Resolution on the Strategy of National Public Procurements (10.9.2020) the possibilities for checking and monitoring of the fulfillment of tax responsibilities of the companies by Finnish public officials will be expanded to promote tax responsibility through public procurements.

<sup>10</sup> The funding provided by the instruments is either fully (Finnpartnership, PIF) or in part (other instruments) Finnish ODA funding. DevPlat may also channel Business Finland financing that is not classified as ODA. The companies that apply for ODA funding from DevPlat with a separate form and are thus informed of the ODA funding decision separately.



**FINNFUND** is a development finance institution majority-owned by the State of Finland. It invests in profitable business projects advancing sustainable development in developing countries. The financing is in the form of equity, mezzanine finance or debt. Finnfund gets its funding from the Finnish Government and the private capital markets, as well as retained earnings from its investments.

**FCA INVESTMENTS (FCAI)** is an impact investing company that provides equity, mezzanine finance, debt, cost-plus financing and capacity building services for small and medium size companies operating in developing countries and fragile states. It is a subsidiary of the Finn Church Aid. The Finnish Government has provided a significant loan to start FCAI's operations and a representative of the MFA is a Member of its Board.

**THE PUBLIC SECTOR INVESTMENT FACILITY (PIF)** is a mixed-credit funding instrument that aims to support public sector investments in developing countries that comply with the sustainable development goals of the UN and utilise Finnish expertise and technology. ODA funds are used to support the investment project's purchase price and interest, whereby expenses incurred to the developing country from the investment are markedly reduced. The Ministry for Foreign Affairs of Finland directly manages this funding instrument and can influence the project planning phase, but it is not a party to the contract agreements of the projects between the the Finnish company and the public sector client (project owner) in the developing country. However, the Ministry for Foreign Affairs will enter into a PIF framework agreement with the developing country Government where the project takes place.

**FINNPARTNERSHIP** provides grant-based, small scale funding support to organizations registered in Finland or to organizations registered in other countries that have substantial Finnish ownership. The Ministry for Foreign Affairs is responsible for the overall steering of Finnpartnership. The Ministry also makes all of the funding decisions based on the Act on Discretionary Government Transfers (688/2001). Finnfund manages the day-to-day operations of Finnpartnership<sup>11</sup>.

**Developing Markets Platform (DevPlat)** is a platform that combines Business Finland services with those of the Ministry for Foreign Affairs, Finnpartnership and other key partners. DevPlat helps Finnish companies and their partners access African and Asian growth markets in ways that are compatible with UN Sustainable Development Goals (SDGs), for example in the form of funding, part of which may be ODA funding from the Ministry for Foreign Affairs of Finland.

<sup>11</sup> The managing organization of the Finnpartnership program is selected via a competitive process. The current agreement with Finnfund is valid until the end of 2021.





All of the above-mentioned instruments shall ensure that the principles of tax responsibility laid out in this document are included in their relevant decision-making, monitoring and reporting processes. General guidance on how to do this in prac-

tice is given below. The Ministry for Foreign Affairs will agree separately with each instrument on the more specific requirements, processes and details of implementation and will provide support as needed.

Each private sector instrument shall prepare a **PUBLIC POLICY OR GUIDANCE FOR TAX RESPONSIBILITY** or integrate tax responsibility issues to its existing corporate responsibility policies, guidance or criteria **by 31.5.2021**<sup>12</sup>. This is important to demonstrate how Finland's key principles on tax responsibility are implemented and monitored in each instrument.

The prepared or updated policy or guidance shall include the general tax responsibility principles of this policy and **LAY OUT THE IMPLEMENTATION PROCESS** that is relevant for the instrument and proportionate to the size of of the financing provided by the instrument and the available resources.

The organization managing the funding instrument shall indicate to MFA which **GOVERNANCE BODY** within the organization is accountable for compliance with the prepared or updated policy or guidance.

The document shall be made **PUBLICLY AVAILABLE** on the website of the instrument and/or the organization managing the instrument.

After each instrument's decision making mechanisms have approved the prepared or updated policy or guidance, tax responsibility issues are required to be integrated in the full funding and/or investment cycles of the instrument. This includes:

**DUE DILIGENCE:** As part of the due diligence process commensurate with the size and type of the proposed investment or funding, each company considered for financing shall be reviewed from a tax perspective to assess how it adheres to the tax responsibility principles set out in this policy paper.

**TERMS AND CONDITIONS OF FINANCING AGREEMENTS AND DISCRETIONARY GOVERNMENT TRANSFERS:** Terms and conditions implementing the tax responsibility principles shall be included in all agreements and/or discretionary government transfer decisions made by the instruments<sup>13</sup>. Each instrument should explore available options on potential action to take in case of non-compliance with the terms and conditions after the decision or agreement has been made.

**MONITORING:** Tax responsibility issues shall be incorporated in the monitoring mechanisms of each instrument.

**REPORTING AND TRANSPARENCY:** Each instrument shall include tax responsibility issues, including how the key principles of this policy are being implemented, in their reporting. In addition, to enable monitoring of impact and effectiveness of ODA, the instruments shall gather information on the paid taxes and other tax-like fees by the companies they finance and include the aggregated information in their reporting. The aim is to have tax information available on a country-by-country basis.

<sup>12</sup> The main guiding documents of Finnpartnership will be updated as a part of the tendering process of the management of the instrument and they will become effective on 1.1.2022.

<sup>13</sup> In the case of the PIF, MFA is not a contracting party.



In addition to direct investments in companies, Finnfund and FCAI also invest in funds. Investments should only be made to funds that are managed in a tax responsible and transparent way. The investment policies of such funds should be in line with these principles in respect of the investee companies and the acquisition and management company structures used. Prior to the investment, the investor must conduct proper due diligence regarding the structure and practices of the fund. This includes confirming that the fund does not promote any such practices and structures that would artificially reduce taxable income in its target countries.

### **3.2. Private sector funding through ODA projects and programmes directly financed by Finland**

Discretionary government grants and other types of financing may also be provided to the private sector as a part of the implementation of other ODA projects and programmes financed by the Ministry for Foreign Affairs. In bilateral programmes where Finland is the only donor, the implementation of the key principles of this policy paper will be ensured in the design and grant and procurement processes of such new programmes, proportionate to the size of the financing provided and the available resources. Practical guidance will be drafted as needed.

In programmes where Finland is one of many donors and/or that are implemented by international organizations or development banks, the safeguards and practices of that organization will be utilized. Finland advocates for these principles in their respective governing bodies as described in section 3.3.

### **3.3. Private sector funding through multilateral development bank operations or other global funds**

Multilateral development banks (MDB), international organizations and funds set up by them implement their own safeguards and sustainability practices. Due to their considerable size and operational relationships with the private sector, they are in a position to influence and lead global standards and practices regarding corporate governance. Finland will advocate for the principles outlined in this document in the governing bodies of the multilateral development banks in which it is represented. The purpose of this policy is to draw attention to the most critically important ways to ensure that countries adopt policies of responsible taxation, and that companies benefiting from ODA through these banks and funds act according to them. These means of promoting tax responsibility can be developed further, as relevant, together with the various international organizations and MDB constituencies in their respective operational contexts.



## 4. The monitoring and evaluation of the policy

The Ministry for Foreign Affairs will work together with each private sector instrument as they develop their instrument specific tax responsibility policies. After that, the Ministry will monitor the implementation of the policy in each funding instrument as part of the existing monitoring and guiding

processes. The instruments should include the implementation of the key principles of this policy in their reporting to the Ministry. An overall evaluation of this tax responsibility policy will be conducted in 2023.



## RELEVANT SOURCES FOR MORE INFORMATION

[Government Programme, section "Taxation in a Changing World"](#)

[Government Programme, section "Globally influential Finland"](#)

[Valtioneuvoston omistajapoliittinen periaatepäätös 2020 \(only available in Finnish\)](#)

[Kansallinen julkisten hankintojen strategia 2020 \(only available in Finnish\)](#)

[Hallituksen kansainvälisen veronkierron vastainen toimintaohjelma \(only available in Finnish\)](#)

[Taxation and Development Action Plan 2020-2023](#)

[OECD Guidelines for Multinational Enterprises, chapter on taxation](#)

[Measuring and Monitoring BEPS](#)

[GRI tax standard](#)





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