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Tax Policy

FCA Investments LTD.

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Introduction

FCA Investments (FCAI) is a subsidiary of Finn Church Aid (the largest international aid organisation in Finland). FCAI's primary objective is to make funding and technical support available for economically viable, socially and environmentally sustainable Small and Medium-Sized Enterprises (SME's) that work to improve livelihoods in target countries (e.g. least developed countries 'LDCs' and fragile states 'FS') for more resilient and productive communities. Therefore, FCAI considers the sustainable development goals (SDGs) as the main compass that guides its operation and decision-making processes.

Despite a tremendous increase in the number of initiatives dedicated to sustainable development since the adoption of the 2030 Agenda in 2015, a persistent $2.5 trillion annual financing gap stands in the way of achieving the Sustainable Development Goals (SDGs)[1]. In this context, FCAI believes that achieving the SDGs requires both a qualitative and quantitative shift in approaching development with more emphasis on the role of the SME sector in developing countries. A vibrant and responsible SME-sector along with the associated job creation and tax revenues are the backbone of any sustainable economy; however, in LDCs and fragile contexts, SMEs are largely absent and suffer from limited access to finance and low productivity levels.

FCAI deeply believes in the role of tax revenues as a key source of mobilizing domestic resources and channelling them towards sustainable development to help close the financing gap. Conversely, aggressive tax planning and tax evasion practices are perceived by FCAI as a threat that could undermine the progress of achieving the SDGs, especially in developing countries.

Tax Management Approach

FCAI's tax management follows a two-tier approach with FCAI holding itself and investee funds to a higher tier (Tier A) than its direct investments (Tier B), which are broadly SME's. This is in recognition of the different levels of complexity of these entities and the inherent technical and capacity challenges faced by SME's. However, this tax policy may not be applicable to treasury management activities like bank's deposits and parking cash in liquid funds.

Tax Management approach for Fund Investments (Tier A)

In all its Tax affairs and investments in other funds, FCAI is guided by the following key guidelines.

1- OECD's Guidelines for multinational enterprises – Taxation
2- Tax responsibility principles in Finland's development cooperation funding to the private sector

In practice, this means that any instances of deviation from the guidelines above (if at all) must be documented, clearly justified and need the approval of the board to proceed. On the other hand, material deviations by funds seeking investment would lead to a rejection of the investment request unless the fund can come back into compliance prior to the investment.

In addition to the international tax laws, FCAI complies with the local tax laws and regulations of the countries/jurisdictions in which it operates. For that reason, FCAI will not

[1] https://www.weforum.org/agenda/2020/01/unlocking-sdg-financing-decade-delivery/#:~:text=Despite%20a%20tremendous%20increase%20in,Sustainable%20Development%20Goals%20(SDGs).

engage with or participate in activities that aim at tax evasion or unjust profit shifting across countries or jurisdictions for tax minimization purposes.

Holding company structure(s):

As part of its fund investments, FCAI may invest in a fund that has a "holding company structure" or use a holding company structure for its own investments. The holding company structure (where it is used) must be fully aligned with the OECD inclusive framework on base erosion and profit shifting (BEPS). FCAI does not invest through third jurisdictions that are on the EU list of non-cooperative jurisdictions for tax purposes; in addition, FCAI prefers to avoid investing through third jurisdictions that are not compliant or only partially compliant with the OECD global forum on Transparency and Exchange of Information for Tax Purposes.

Tax Management Approach for Direct Investments (Tier B)

FCAI's tax management approach for its direct (SME) investments takes into account the local context in each of its target markets. Overall, it aims to ensure that investee SME's apply best practice and are fully compliant with local tax legislation during or at least by the end of the investment period. In this regard, SME's that seek to receive FCAI's investment or support need to commit to FCAI's tax policy for direct investments, demonstrate an ability to come into compliance by the end of the investment period and agree to continuous assessment of their progress via active due diligence, engagement, and reporting.

In many of FCA's target markets, tax legislation is not fully developed, tax administration and collection is done haphazardly and taxes are many times perceived as unfair. A lack of tax compliance is therefore not always wilful and is most often the result of a combination of factors including inadequate knowledge of the various taxes, poor or inadequate records that may make tax determination and compliance almost impossible, irregular cash flows that force a delay in payment and extremely low tax morale.

Verification and Compliance Practices

As part of its investments across the board, FCAI will carry out verification and compliance checks to ensure that the tax status of the investees is identified, there is a clear monitoring plan to ensure the investee moves towards compliance and reporting on tax is transparent.

1- Tax due diligence: Responsible tax practices in-line with local tax laws are a prerequisite for FCAI's investments.

As part of the screening and due diligence process, FCAI demands transparent communication and disclosure of the tax structure, practices, and historic tax data of the potential investee to improve and ensure compliance with local tax laws and FCAI's tax management approach during the investment tenor. Given the weak regulatory frameworks in some target markets, FCAI will design a post-Investment action plan that seeks to address any tax non-conformance issues.

It is acknowledged that local tax regulations in some fragile states or least developed countries may not live-up to the EU or OECD tax-compliance requirements. Therefore, FCAI may make investments in an intermediary or SME in a certain developing country despite being on the EU list of non-cooperative tax jurisdictions and regardless of the country's classification by

OECD's Global Forum as long as there is no profit shifting or tax evasion practiced at the investee level.

2- Active engagement: commitment to responsible tax practices and zero-tolerance to aggressive tax planning or tax evasion[2].

As per the investment agreement and in-line with the post investment action plan agreed to by FCAI and each investee, the FCAI portfolio companies and funds have to be committed to and held accountable for tax compliance and responsible tax practices. The portfolio companies/funds shall not engage in any aggressive tax planning or tax evasion practices. As part of the annual audit, FCAI will request each investee company to report on their tax compliance and any liabilities outstanding at the year-end.

FCAI adopts a zero-tolerance policy on all forms of illegal and unjust[3] activities including irresponsible tax practices. As per its active engagement, the unjustified failures in implementing the post investment action plan and/or new tax non-conformance issues that may occur during the investment period will be treated as a breach of contract (in accordance with the investment agreement). Thus, the failure to address those tax non-conformance issues when brought to the attention of the investee company will open the door to possible sanctions e.g. penalties, blacklisting, immediate exit, or litigation in court.

3- Transparency and reporting: fundamental part of the impact measurement and management process

At the end of each reporting period, quantitative data received from each portfolio company will be analysed, aggregated, and combined with any related qualitative data that might be collected during that reporting period. According to the investment agreement and the associated reporting requirements, each portfolio company has to report on its taxation and all payments to the government on an annual and country-by-country basis. The tax-reporting requirement is part of FCAI's impact measurement and management process and it must be included in the investment agreement.

Tax revenues generated in host countries are an important element of the development impact of FCAI's investments. FCAI therefore annually discloses in its impact report the aggregate amount of tax payments as reported by the companies in which FCAI invests, classified by country (or continent if there are less than 3 portfolio companies per country).

[2] According to EU, aggressive tax planning (ATP) consists in taxpayers' reducing their tax liability through arrangements that may be legal but are in contradiction with the intent of the law. ATP includes exploiting loopholes in a tax system and mismatches between tax systems. It may also lead to double non taxation or double deductions

[3] intentionally not aligned with FCAI's investment principles and guidelines