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Aggressive Tax Planning Indicators

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Agenda

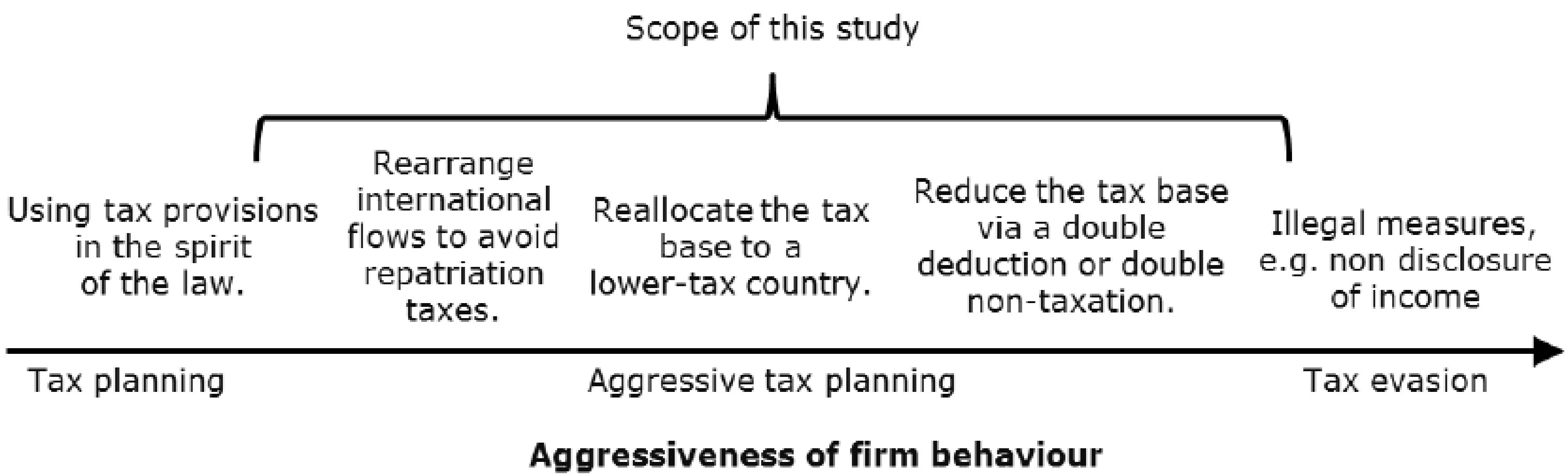
- Aim of the study
- Definition of Aggressive Tax Planning (ATP)
- Indicators
  - General indicators: Country-level, MNE-group level
  - Specific indicators: Subsidiary-level, Country-pair-level
  - Combination of indicators
- Aggregation and Key results
- Conclusion

Aim of the study

- **Provide a set of country-level indicators for all EU28 countries, which…**
  - **… measure the extent of ATP**
  - **… indicate the main channels (interest payments, royalty payments, transfer pricing) of ATP**
  - **… indicate whether a country is mainly target (i.e. losing tax base), conduit (i.e. not winning or losing but instrumental to ATP) or a lower tax (i.e. attracting tax base) country**

Definition of ATP

- **There is no well-accepted definition of ATP**
- **Firm behavior can be seen as a continuum**



- **Broadly: "*behavior of MNEs, which substantially reduces their tax burden and runs against the spirit of the law*"**

General Indicators: country-level

- Statutory tax burden
  - Rates, patent boxes, CFC rules…
- Corporate tax revenues/base
  - Corporate income tax revenues + decomposition
- Exposure to aggressive tax planning
  - FDI (unexplained), foreign controlled activities, market concentration
- Treaty shopping indicators
  - No. of tax treaties, average repatriation taxes, attractiveness for treaty shopping

General Indicators: MNE group-level

- Ownership structure
  - Headquarter in country without CFC rule
  - Presence in low tax country
  - Presence in country with patent box
  - Presence in country favourable for treaty shopping
- Consolidated Effective tax burden and profitability
  - Effective tax burden (tax/profit) consolidated accounts, MNEs vs. Domestics
  - Profitability (profit/assets) consolidated accounts, MNEs vs. Domestics

Specific Indicators: firm-level (I)

- Profitability measures
  - Pre-tax profit or loss/total assets
  - Earning before interest and taxation/total assets
  - Financial profits or loss/total assets
- Interest payments/debt shares
  - Interest payment/total assets
  - (Current +non-current liabilities)/total assets
- Intangible assets/patents
  - Intangible assets/total assets
  - No. of granted patents

Specific Indicators: firm-level (II)

- For all firm-specific indicators we calculate two "gaps"
- Gap within MNE
  - Value is lower/higher than average of the rest of the MNE group
- Gap to domestic companies
  - Value is lower/higher than average of domestic companies

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Specific Indicators: country-pair level

- Bilateral import price anomalies
  - Import prices too high/low for at least one good in the industry
  - Export prices too high/low for at least one good in the industry
  - Matched with firm ownership structure to identify relative tax position
- Bilateral royalty flows
  - Royalty inflows/outflows and net flows in % of GDP
  - Matched with firm ownership structure

Combination of indicators

- Relative tax situation within a MNE group
  - Classify the location of a subsidiary as low tax (5%p gap to other parts of MNE group)
- Combine indicators to allocate each entity to a role in ATP
  - E.g. ATP through interest payments
  - Target entity: lower profitability, higher debt share,…
  - Lower tax entity: higher profitability, lower tax rate, …
  - Conduit entity: Neither target nor lower tax entity, but part of a MNE group with target entity

Aggregation to country level

- Type specific averages and medians
  - Split the firm-level data into subsamples according to the ownership and relative tax status:
  - Stand-alone, lower tax firms and NOT-lower tax firms
- Aggregate the roles within ATP structures
  - Share of entities in each category (by country)
- Identification of outliers, high and low value countries
  - Values two (one) standard deviation(s) above/below average

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Key results (I): Distribution of indicators at country level

- Tax rates and revenues
  - High tax revenues: CY, MT, (LU)
  - High profitability of corporate sector: IE, (RO, GR)
  - Low profitability of corporate sector: (FR, HR, SI, UK)
- Foreign direct investment stock
  - (unexplained) High values for: (LU, MT, CY, IE, NL, HU)
- Distribution of MNE entities by type
  - Lower tax entity elsewhere: BE, DE, HU, LU, IT
  - Lowest tax entity: CY, BG, IE, LT, LV
  - Strongest link to zero tax entity: IE, UK, NL, FR, BG

Key results (II): Consolidated profitability and tax burden in MNEs

- Effective tax rates for MNEs are higher than for domestic companies
  - Inconsistent with ATP
- MNE groups are more profitable (EBIT/total assets)
- Profitability gap no longer visible in pre-tax profit and loss
  - MNE groups appear to have more financial losses

- Overall: Consolidated accounts perform poorly as indicators for ATP

Key results (III): ATP-specific indicators at entity level

- Profitability is highest for MNE entities which are in relatively low tax countries, followed by domestic companies and the relatively high tax countries
  - PLBT/Assets: 4.5% vs. 3.6% vs. 2.9%
  - EBIT/Assets: 4.7% vs. 3.8% vs. 3.1%
- No clear picture for financial profit/loss
- No clear picture for debt share/interest payments
- Intangibles assets/patents are only relevant for MNEs
- Overall: Type specific profitability measures appear to work as indicators for ATP

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Key results (IV): Royalty flows, import price anomalies and treaty shopping

- Royalty flows are very skewed
  - Very high inflows in MT, NL, (IE, LU)
  - Very high outflows in IE
  - Bilateral data not reliable enough
- Import price anomalies provide no clear picture
  - More detailed data would be necessary
- Treaty shopping indicators show that the UK is on many optimal repatriation routes
- **Overall: Bilateral royalty flows and trade data could be useful, but more detailed data needed**

Key results (V): Roles within ATP structures

- The allocation of MNE entities to roles within ATP structures is challenging
  - Using a strict classification, few entity can be clearly classified
  - Using a less strict classification, we find that…
  - … target entities are most often found in FR, BE
  - … lower tax entities are most found in BG, SI, PL
  - … "usual suspects" are often classified as conduit entities: IE, NL, CY
- Overall: Classification into roles within ATP structures not really feasible for EU 28 countries

Conclusion

- ATP is a firm/MNE-group-level phenomenon, aggregation to country-level is difficult
- Consolidated accounts (so far) bear little information for identification of ATP
- Investigating only EU 28 countries is most likely not sufficient
- Reliable data about bilateral royalty flows could be useful
- So far, the most promising indicators appear to be firm type-specific profitability measures