Organizing Tax Avoidance in Large Corporations

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Definition

- Tax avoidance (Stiglitz, 1985): Explicit reduction of tax liabilities

- Tax evasion: Illegal practice to avoid paying tax liabilities

What would happen if people like **you / me** violate the tax law in Sweden?

→ Tax offender (Criminal)

→ Skatteverket / Polisen

What would happen if **IKEA / Starbucks / Google** violates the tax law in Sweden?

→ Tax planning / Tax avoidance

→ Investigation ???

→ **Tax avoidance is a Legal practice to avoid paying tax liabilities**

A problem for whom?

Oxfam

Christian Aid

#occupiedwallstreet movement, 2011

ActionAid

GLOBAL ALLIANCE FOR TAX JUSTICE

Crimes of globalization

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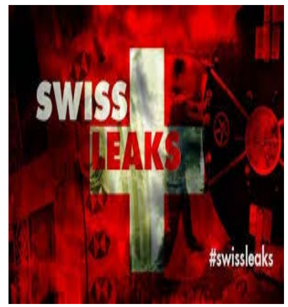
"Crimes of globalization are those demonstrably harmful policies and practices of institutions and entities that are specifically a product of the forces of globalization, and that by their very nature occur within a global context".

(Rothe and Friedrichs 2015, p. 26)

Increasing attention to tax avoidance

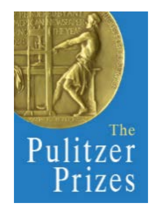
PWC: 548 tax rulings in favour of 340 MNC



HSBC: 106.000 clients, 203 countries +$100 billion

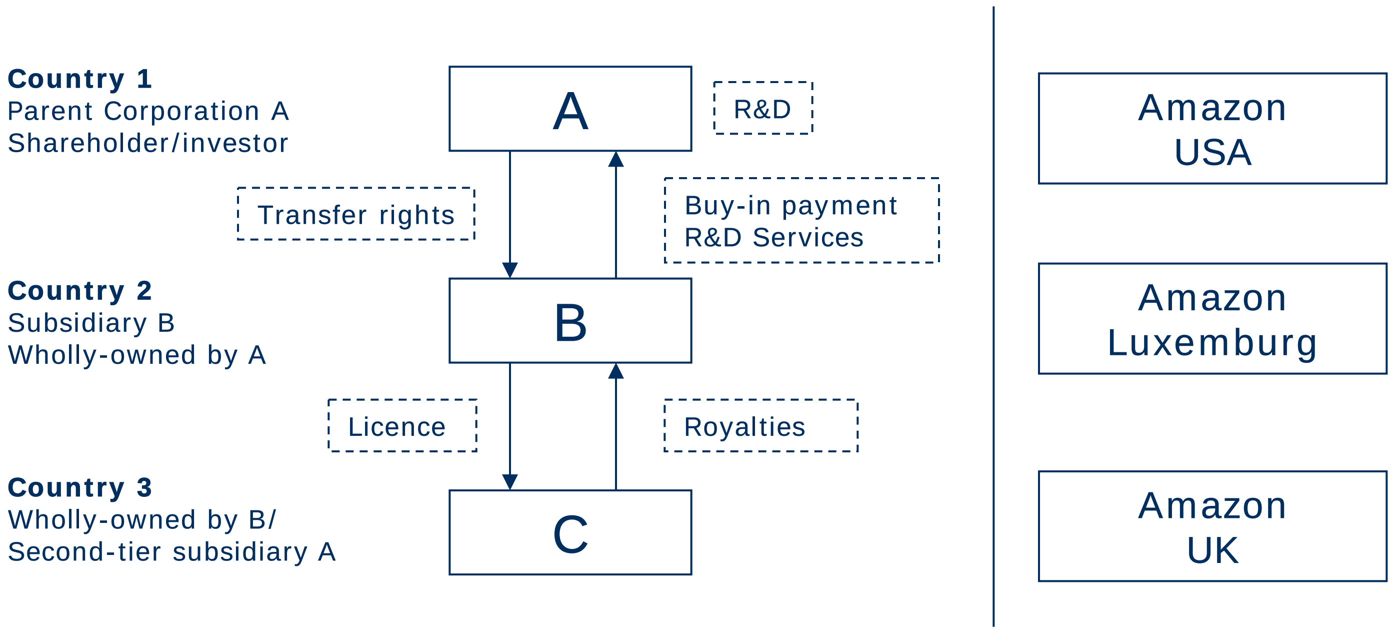
Liechenstein Leaks: 170 countries, 120,000 offshore companies + individuals

"But Nobody Pays That,"
David Kocieniewski,
The New York Times, 2012



http://www.nytimes.com/video/business/100000000870844/inside-the-accountants-playbook.html

Methods of tax avoidance - Basic schema



Methods of tax avoidance

- Profit shifting: Operational activities (higher-tax state) move to a subsidiary (lower-tax state)

  Ireland → Corporate income tax rate: 12.5%;

  Switzerland → Corporate income: 0% non-residents

  Bermuda→ 0% (total exemption), Government fee
- Payment for intangibles: Include royalties for the use of licences, brands, patents

  Netherlands → Innovation Box regime: 5% corp income
- Transfer pricing: Payments for goods (and loans) between a parent company and subsidiary

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The Starbucks case

Royalties brand

Coffee beans

Loan interest

Starbucks Manufacturing EMEA BV
(Netherlands)

Starbucks Mfg
(Netherlands)

Starbucks Coffee Tradind SarL
(Switzerland)

Rain City CV, Emerald City CV
(Netherlands)

Starbucks Coffee International Inc.
USA

Schema based on Edward Kleinbard, 2013. Through a Latter, Darkly: Starbucks's Stateless Income Planning.
USC Gould School of Law

The Google case

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Royalties: 99.4% profits

Sales locally, invoices Ireland

Google
Incorporated
USA

Tax paid: 0
No double taxation

Google
Algorithms
Bermuda

Tax paid: 0
No double taxation

Google
Ireland Limited
Ireland

Tax paid: £6m
12% rate (0.6% profits)

Methods of tax avoidance (Cont…)

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- Conduit: A corporation channels money through a country with low corporate tax rate

  Mauritius → India; BVI → China; Cyprus → Russia

- Hybird entities: Obtain a deduction for the same cost in two different countries

  Switzerland: Capital income for non-residents 0%;

  Witholding tax for royalties: 0%

  Belgium: 95% Dividends are exempt

  Luxembourg: Treaty with Belgium → no taxed

Offshore territories

Source: http://visual.ly/locations-offshore-tax-jurisdictions

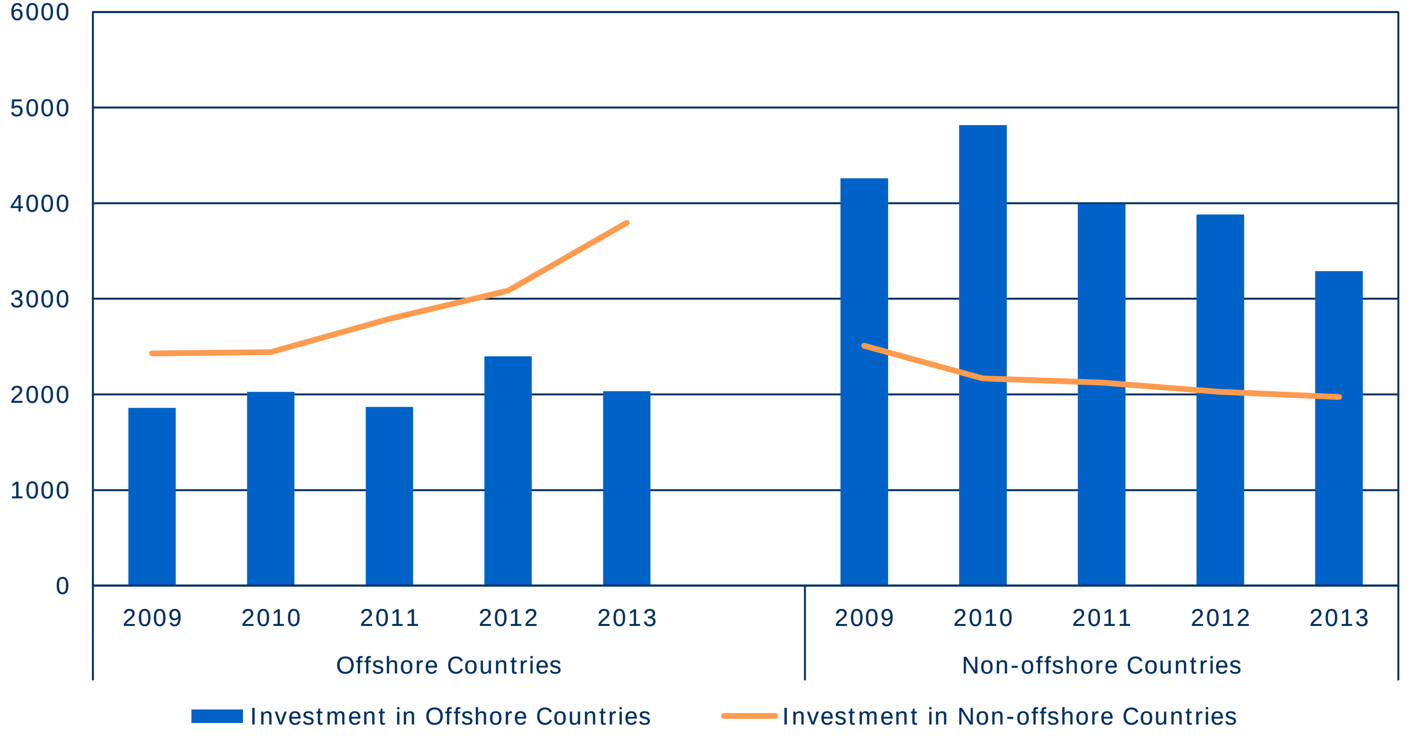
IMF: 46 territories
OECD: 70 territories
TJN: 82 territories

Cayman Islands (June,2015):

- 58,238 inhabitants
- Second Financial Center (Portfolio invest. assest)
- 96,554 companies
- 196 banks
- 11,061 mutual funds
- 752 insurance companies
- 144 trust companies

→ Ugland House: 18,000 companies

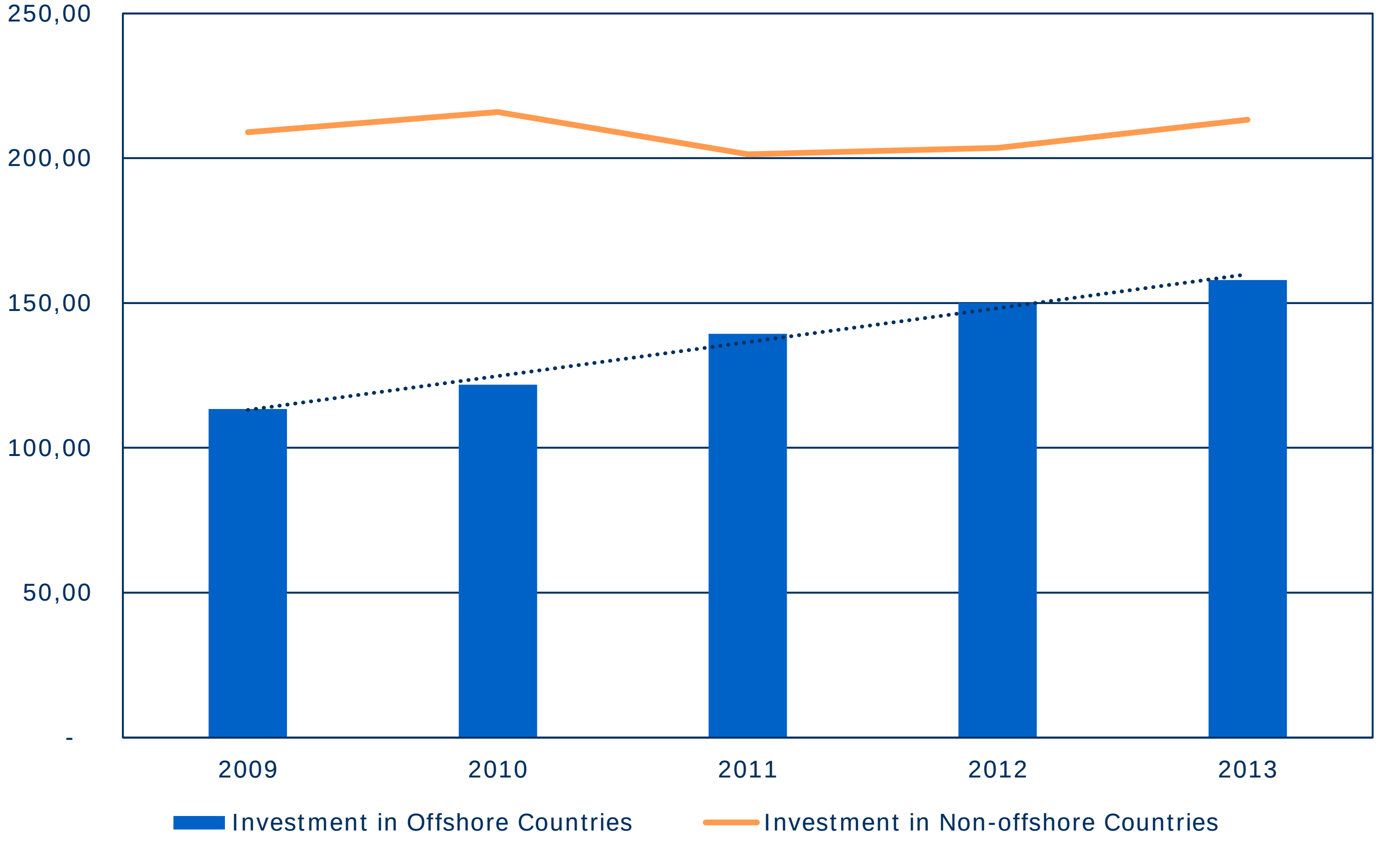
Inward direct investment of top ten economies



Offshore countries: China, P.R.: Hong Kong, Netherlands, Luxembourg, Japan, Switzerland, Virgin Islands, British
Non-offshore countries: Brazil, Canada, China, P.R.: Mainland, France, Germany, Spain, United States, United Kingdom

Source: Coordinated Direct Investment Survey (CDIS) by the IMF
Available at: http://data.imf.org/?sk=40313609-F037-48C1-84B1-E1F1CE54D6D5&sId=1410469433565&ss=1390030109571

Swedish inward direct investment



Top ten Swedish investment countries include:
Offshore Countries: China, P.R.: Hong Kong, Luxembourg, Netherlands, Singapore, Switzerland
Non-offshore Countries: China, P.R.: Mainland, France, Germany, United States, United Kingdom

Source: Coordinated Direct Investment Survey (CDIS) by the IMF
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Total inward direct investment – Sweden Vs. Top 10 economies (%)

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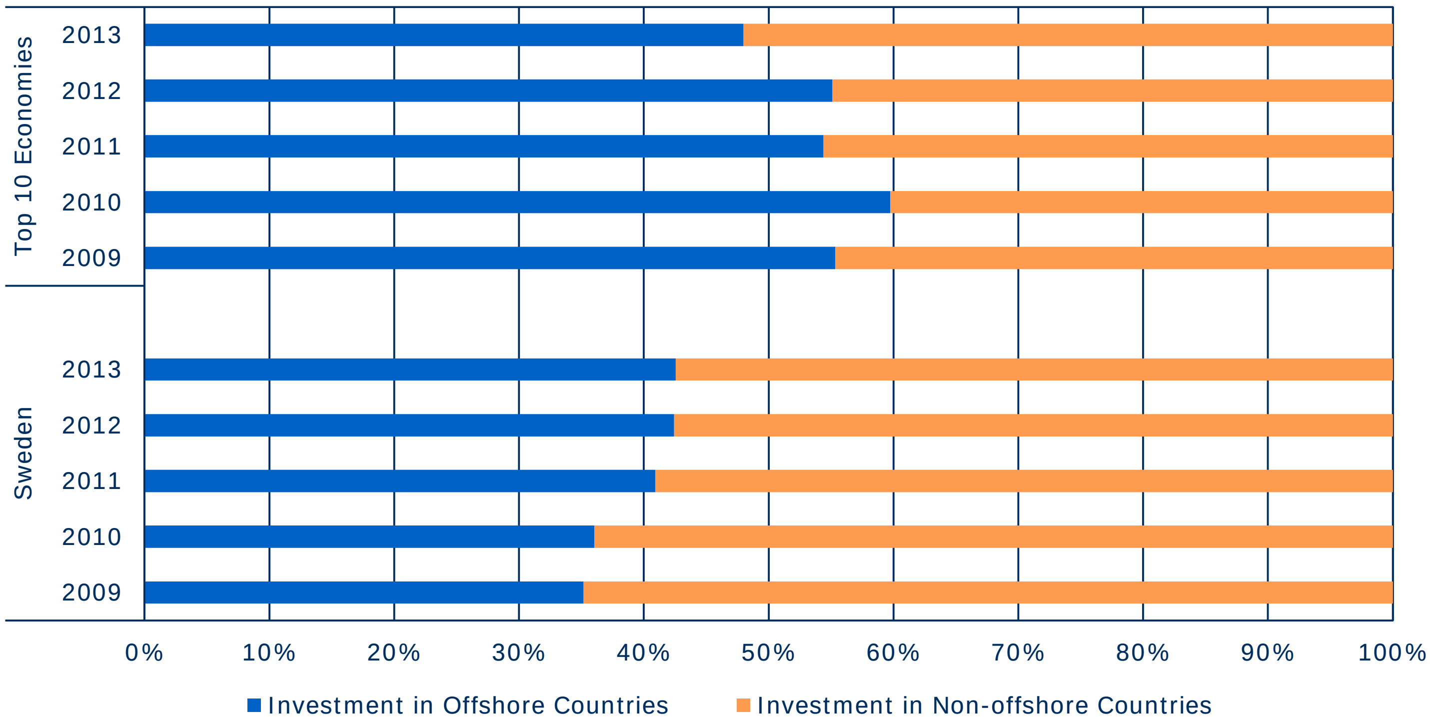

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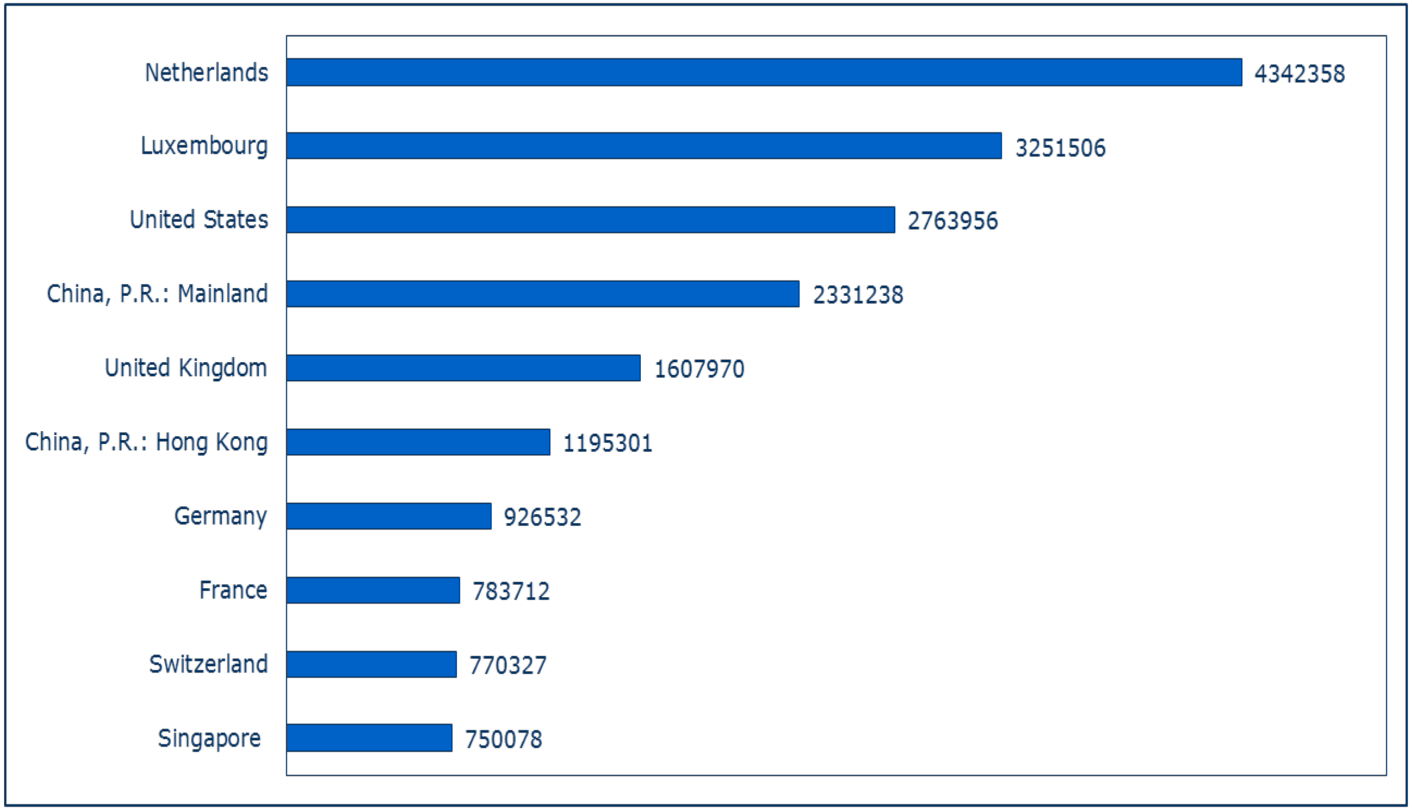
Top 10 direct investment countries in Sweden (2013, US$, Millions)



Source: Coordinated Direct Investment Survey (CDIS) by the IMF
Available at: http://data.imf.org/?sk=40313609-F037-48C1-84B1-E1F1CE54D6D5

What do we know about tax avoidance…

- Who uses it?

  Multinational companies (Halmon, 2010)

- Who decides?

  CEOs (Dyreng, Hanlon and Maydew, 2010)

- When to use it?

  High quality governance (Desai, 2009)

  Non-family firms (Chen, 2010)

  Risk-takers [fine/scandal] (Hanlon, 2009)

  Spend on auditing firms (Dyreng, 2010)

Is the top leadership of the organizations promoting tax avoidance?

- Cross-national analysis
- Sample size: 22 countries (including Sweden)

  → High-income: 15; Medium-income: 6; Low-income: 1
- Data:
  - Global Competitiveness Report 2012-2013 (Reports 99 indicators base on surveys with 100 CEOs in 144 countries)
  - Atwood et al. (2012) ”Home country tax system characteristics and corporate tax avoidance: International evidence”. *The Accounting Review 87(6)*

Hypotheses tested

- H1: CEOs who report that their firms have a strong ethical behaviour are less likely to adopt tax avoidance mechanisms.

- H2: Corporate boards and investors who demand that management be highly accountable tend to reduce the use of tax avoidance mechanisms in their corporations.

- H3: In countries with strong auditing standards, corporations are less likely to adopt tax avoidance strategies.

Results of OLS regression on the nature of tax avoidance

	Hypothesis	Predicted	Final Model
Independent variable			
EthicBehav	H1	Negative	-0.171 (0.030)**
EfficCorpBoard	H2	Negative	-0.520 (0.077)**
StregthAudit	H3	Negative	0.404 (0.056)**
Control variables			...
Constant			3.813 (0.493) **
Adjusted R^2			0.940
Observations			22
F			18.366*

*, **, *** indicate significance at 10%, 5%, and 1%, respectively.
Dependent variable: Tax Avoidance (ETR)

H1: Accepted CEOs can contribute to reduce tax avoidance

H2: Accepted Boards can help to reduce tax avoidance

H3: Rejected Strong auditing increasing tax avoidance

How does tax avoidance work?

IKEA and tax avoidance

- Mr. Ingvar Kamprad
- Fourth-wealthiest individual in the world (2013, Forbes)
- Personal Fortune $ 57 billion
- Personal Fortune in Sweden (2013) $ 88 million
- Tax Sweden $1.3 million

Source: http://www.svenskbladet.se/ekonomi/index.php?alias=ingvar_kamprad_annu_rikare_an_du_trodde_nar_du_inte_ens_kunde_fantisera_om_hur_rik_han_ar.html

http://www.svd.se/sa-mycket-kommer-kamprad-att-skatta

IKEA

- Created 1958
- "Småland legacy"
- 361 stores in 49 countries (Franchise)

High income countries
Australia, Austria, Belgium, Canada, Croatia, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hong Kong, Hungary, Iceland , Ireland, Israel, Italy, Japan, Kuwait, Lithuania, Netherlands, Norway, Poland, Portugal, Puerto Rico, Qatar, Russia, Saudi Arabia, Singapore, Slovakia, Spain, Sweden, Switzerland, Taiwan, United Arab Emirates, United Kingdom, United States
Upper middle income countries
Bulgaria, China, Dominican Republic, Malaysia, Jordan, Romania, Thailand, Turkey
Lower middle income countries
Egypt, Indonesia
Lower income country
South Korea

- 1982 → Residence in Leiden, Netherlands
- Charity foundation

IKEA became a charity

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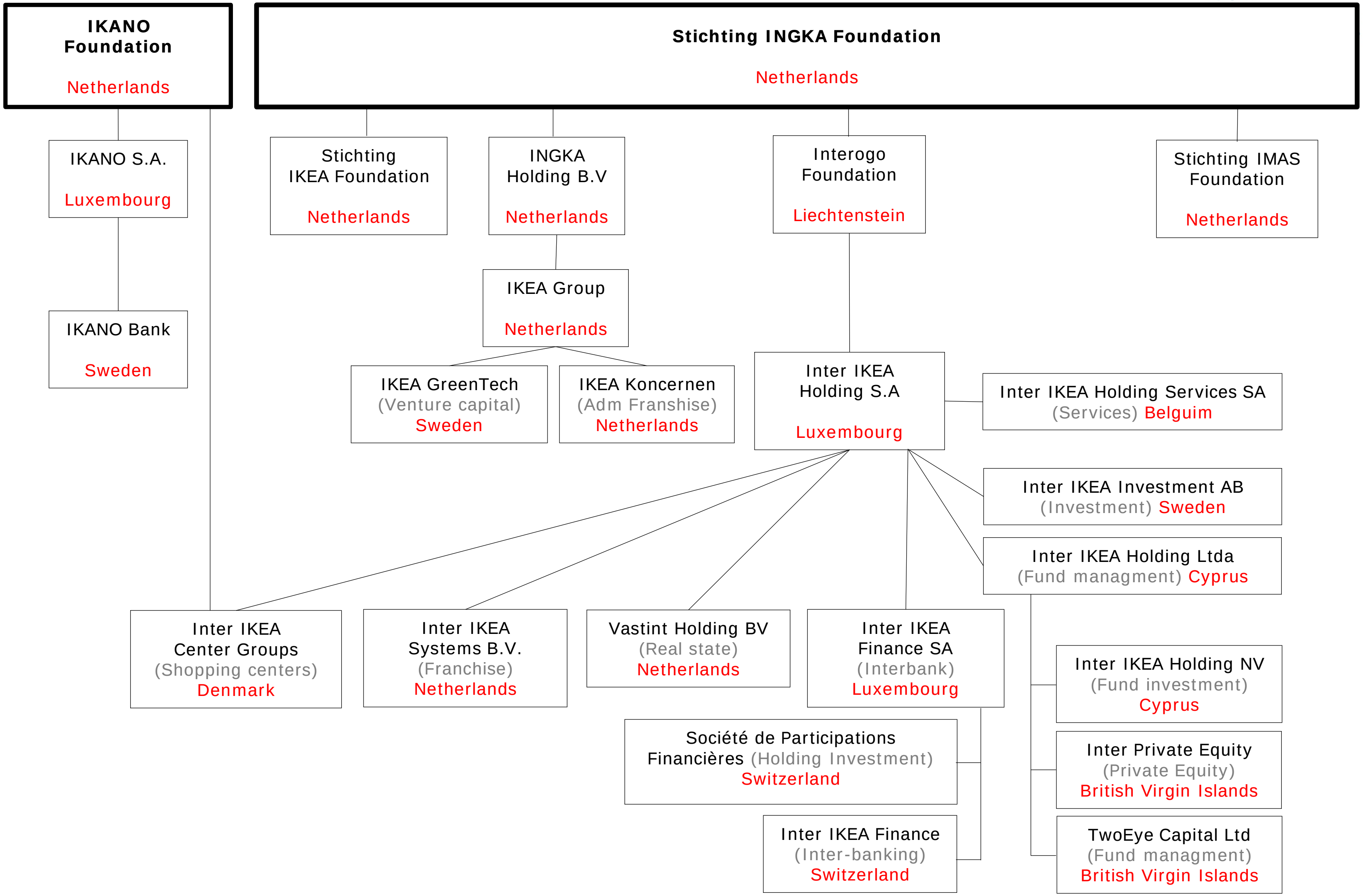
"Ingvar Kamprad spends a lot of time thinking about how to secure longevity and independence for his business and concept. He seeks for an ownership structure [...] that would be sustainable over many generations. The answer was to separate the ownership of the retail operation from the ownership of the concept and the IKEA brand. Ingvar Kamprad therefore donated a large number of the operating companies to a Dutch Foundation – the INGKA Foundation - which today owns a large number of the IKEA franchisees".

(IKEA Foundation 2015)


IKANO Foundation
Netherlands
Stichting INGKA Foundation
Netherlands
IKANO S.A.
Luxembourg
IKANO Bank
Sweden
Stichting IKEA Foundation
Netherlands
INGKA Holding B.V
Netherlands
Interogo Foundation
Liechtenstein
Stichting IMAS Foundation
Netherlands
IKEA Group
Netherlands
IKEA GreenTech
(Venture capital)
Sweden
IKEA Koncernen
(Adm Franshise)
Netherlands
Inter IKEA Holding S.A
Luxembourg
Inter IKEA Holding Services SA
(Services) Belguim
Inter IKEA Investment AB
(Investment) Sweden
Inter IKEA Holding Ltda
(Fund managment) Cyprus
Inter IKEA Center Groups
(Shopping centers)
Denmark
Inter IKEA Systems B.V.
(Franchise)
Netherlands
Vastint Holding BV
(Real state)
Netherlands
Inter IKEA Finance SA
(Interbank)
Luxembourg
Inter IKEA Holding NV
(Fund investment)
Cyprus
Société de Participations Financières (Holding Investment)
Switzerland
Inter Private Equity
(Private Equity)
British Virgin Islands
Inter IKEA Finance
(Inter-banking)
Switzerland
TwoEye Capital Ltd
(Fund managment)
British Virgin Islands

IKEA taxes and donations

- In 2014 the Stichting INGKA Foundation informed that:
  - IKEA Group reported sales for €28.7 billion
  - Paid taxes for €801 million
  - Corporate income tax rate 19.3%

- In 2014 Stichting INKEA Foundation informed that:
  - Gave donations for €104 million
  - Reached 170 million children around the world through 40 partner organizations (i.e. UNICEF, UNDP, Save the Children)
  - Received the 2015 THANKYOU award from the World Childhood Foundation

IKEA's tax approach

"The operations comply with all relevant laws and regulations and thus pay taxes accordingly. However, we have always viewed taxes as a cost, equal to any other cost of doing business. An optimized tax structure allows us the flexibility to use funds, that have already been taxed in one market, in new markets for further business development without the additional burden of double taxation". (Kamprad 2011)

IKEA tax avoidance strategies

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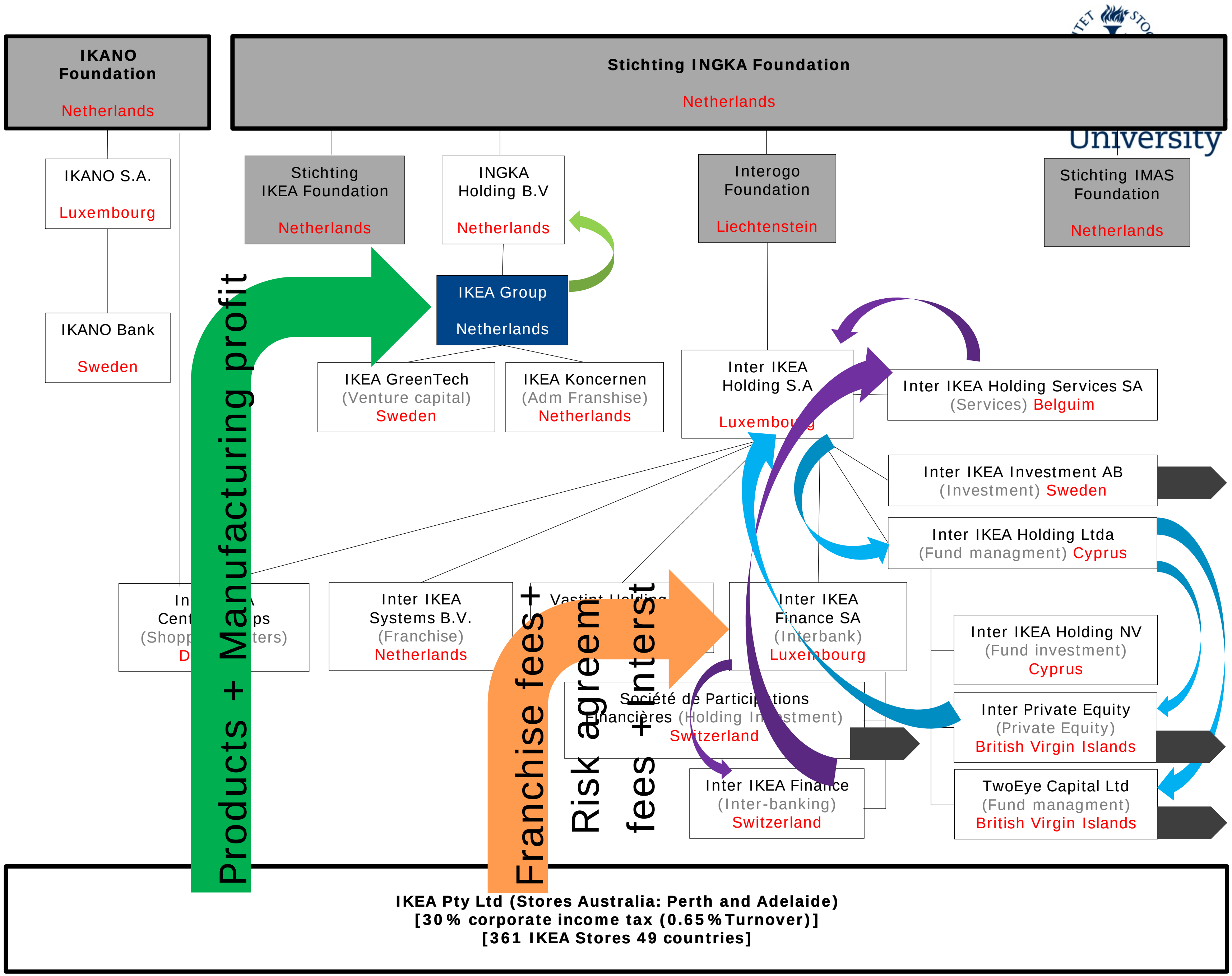
- Payment for intangibles
- Profit shifting
- Use double treaty (Luxembourg-Belgium)
- Use exemptions (Netherlands)
- Use exemptions + Avoid double treaty (BVI)

- Charity: ”[T]o support individual IKEA retailers experiencing financial difficulties”. (Kamprad 2011)



IKANO Foundation
Netherlands
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Luxembourg
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Netherlands
INGKA Holding B.V
Netherlands
Interogo Foundation
Liechtenstein
Stichting IMAS Foundation
Netherlands
University
IKANO Bank
Sweden
IKEA Group
Netherlands
IKEA GreenTech
(Venture capital)
Sweden
IKEA Koncernen
(Adm Franshise)
Netherlands
Inter IKEA Holding S.A
Luxembourg
Inter IKEA Holding Services SA
(Services) Belguim
Inter IKEA Investment AB
(Investment) Sweden
Inter IKEA Holding Ltda
(Fund managment) Cyprus
Inter IKEA Systems B.V.
(Franchise)
Netherlands
Inter IKEA Finance SA
(Interbank)
Luxembourg
Inter IKEA Holding NV
(Fund investment)
Cyprus
Société de Participations Financières (Holding Investment)
Switzerland
Inter Private Equity
(Private Equity)
British Virgin Islands
Inter IKEA Finance
(Inter-banking)
Switzerland
TwoEye Capital Ltd
(Fund managment)
British Virgin Islands
Products + Manufacturing profit
Franchise fees +
Risk agreem
fees + Interst
IKEA Pty Ltd (Stores Australia: Perth and Adelaide)
[30% corporate income tax (0.65% Turnover)]
[361 IKEA Stores 49 countries]

Conclusion

- IKEA’s tax avoidance structure harms society in the 49 countries they operate.
- IKEA uses tax avoidance to expand their global operation
- IKEA is involved in crimes of globalization

Cont….

Conclusion

Understanding IKEA's crimes of globlization:

1. Rational choice theory: Profit, opportunity
2. Neutralization techniques: Stick to regulations
3. Learning theories: MNC
4. Anomie theory: Goals, egoism
5. Organizational theory: Structure, differential association
6. System criminality theory: global ”experts”
7. Regimes of truth: Legislation in offshore territories
8. Political economy theories: Interaction politics & economics