Multinationals operating in tax havens avoid reporting specifics, study finds

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In the era of a renewed spotlight on offshore tax havens, a new study suggests U.S. tax reporting rules still make it easy for corporations to quietly shift and shelter profits in low-tax jurisdictions, avoiding public scrutiny.

Reviewing 12 years of public reporting data for U.S. multinationals, researchers found companies with more extensive operations in known tax havens were much more likely to group and report their foreign earnings by broader categories, rather than reporting by individual country. It is perfectly legal. U.S. corporate tax rules require companies to disclose which countries they are operating in. But the companies don't have to provide details as to how much they are earning in each place. Instead, they are allowed to—and usually do—report their foreign earnings more generally, such as by region, continent or even "total foreign earnings."

That makes it harder for watchdogs and other stakeholders to track earnings and ask hard questions, including which companies may be attempting to dodge higher taxes, by claiming more earnings in lower-tax havens.

Rather than pointing out potential tax cheats, "we are more interested in whether outsiders can learn anything about these activities from the information companies must provide. I think the quick answer to that is, 'Not too much, unfortunately,'" says Ole-Kristian Hope, the Deloitte Professor and a professor of accounting at the University of Toronto's Rotman School of Management. Prof. Hope conducted the study with Herita Akamah of the University of Nebraska-Lincoln and Wayne B. Thomas of the University of Oklahoma.

The researchers are not aware of any other large-scale study like theirs. The study analyzed financial reporting data between 1998 and 2010 for every company incorporated in the U.S. Researchers manually sifted through the information to catalogue the countries where firms said they operated and compared that to how they disclosed and grouped their earnings.

In addition to their main finding, the study also found that larger companies, those working in natural resources, retail, or in industries with low competition were especially likely to stay vague about where they were claiming their earnings.

The results support calls by some policymakers and non-governmental organizations for U.S. tax authorities to require country-by-country earnings reporting in order to identify companies' tax avoidance practices.

"Just as in other aspects of firms' disclosure practices, most multinationals are loath to disclose something that may work against them, unless they are absolutely forced to," Prof. Hope said.

Reports show the use of tax sheltering has grown significantly over the last 20 years. The use of sheltering in key tax havens has shifted from just over 13 percent of foreign earnings among U.S. multinationals in 1998, to nearly 26 percent in 2010, according to U.S. Bureau of Economic Analysis data. An estimated $100 billion a year has been lost in tax revenue due to use of tax havens by Fortune 500 companies, reports the U.S.-based Citizens for Tax Justice.

The paper will be published in the *Journal of International Business Studies*.

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