Corporate Tax Haven Index explained

ABOUT THE CORPORATE TAX HAVEN INDEX

The Corporate Tax Haven Index is a ranking of countries most complicit in helping multinational corporations underpay corporate income tax. The index evaluates how much wiggle room for corporate tax abuse a country's laws and regulations provide - this is the country's 'Haven Score'. The index also monitors how much financial activity by multinational corporations enters and exits the country - this is the country's 'Global Scale Weight'. These two factors are then combined to determine how big of a role the country plays in enabling global corporate tax abuse - this is the country's 'CTHI value' and is what the country is ranked on.

18 CORPORATE TAX HAVEN INDICATORS EXPLAINED

Lowest Available Corporate Income Tax

When a country makes special tax arrangements for multinational corporations, they pay far less than the statutory corporate income tax rate on profits. This also may trigger a race to the bottom in tax rates across the world.

This indicator measures the country's lowest available corporate income tax rate for any large, tax-resident for-profit company. It takes the statutory corporate income tax rate as a starting point and then analyses legal gaps and loopholes that result in lower tax rates, such as those based on sector, company size, region of operation or individual arrangements. The indicator compares the lowest available corporate income tax rate with the highest available corporate income tax rate in a democracy to assess negative spillovers.

Foreign Investment Income

When a country introduces local rules to prevent multinational corporations from being taxed on their income elsewhere in the world - for example, in the country where they are registered - this often results in corporations paying no or little tax anywhere.

This indicator assesses if the country includes worldwide capital income in its corporate income tax base and if its domestic law grants unilateral tax credits for foreign tax paid on certain foreign capital income.

Loss Utilisation

When a country permits multinational corporations to carry losses backwards and forwards for years, corporations may create artificial losses in years of great profit to avoid paying any corporate income tax at all.

This indicator assess if the country allows companies to carry backwards and forwards ordinary and trading losses, and checks what limits are put in place, such as a set time frame or annual ceiling.

Capital Gains Taxation

When a country chooses not to tax capital gains multinational corporations make from selling domestic or foreign financial securities, such as shares or bonds, multinational corporations ca underpay tax by setting up a holding company in that country to own shares in its own affiliates. Tax havens actively seek to attract such holding companies with low or zero tax rates, which
may lead other countries to reduce their own rates in a race to the bottom.

This indicator assesses if the country taxes corporate capital gains for large, resident, for-profit corporations on the disposal of domestic and foreign securities. It examines the lowest available tax levied on corporate capital gains in the country compared to the highest available rate in a democracy.

Sectoral Exemptions

When a country gives corporate income tax breaks to multinational corporations operating in specific economic sectors, this special treatment can be abused to shift profit and underpay ta owed elsewhere in the world.

This indicator measures if the country gives profit-based tax exemptions to companies in certain economic sectors, such as manufacturing or agriculture, and for passive income through investment activities, including financial and real estate investments. To avoid unfairly penalising countries with sector-specific industrial policies, the indicator differentiates between less harmful cost-based exemptions (granted based on real capital investment or staff salaries and tax-abuse prone profit-based exemptions (given simply because a
company engages in for-profit activities).

Economic Zones and Tax Holidays

When a country sets up special economic zones and offers tax holidays to multinational corporations to encourage local investment, these incentives can be easily abused by corporations to shift profits and underpay tax elsewhere. This often comes with little local economic benefit to the country, leading to large, wasteful tax losses.

This indicator measures if the country provides time-bound or geographically confined tax incentives to multinational corporations. It measures if these incentives offer partial or full exemptions from corporate income tax and/or capital gains tax. This includes temporary tax holidays and special tax incentives (temporary or permanent) given to corporations in designated economic zones.

Patent Box Regimes

When a country offers multinational corporations special tax incentives for intellectual property, such as patents, the intended goal of stimulating innovation can often be thwarted. These incentives are often abused to shift profit and underpay tax elsewhere, without leading to significant innovation. Countries can often follow suit in offering these "patent box regimes", sparking a race to the bottom.

This indicator measures if the country offers corporations preferential tax treatment for income related to intellectual property rights (eg patent boxes). It also considers whether the country applies the OECD's (Organisation for Economic Co-operation and Development) test of genuine nexus between the income generated and the underlying innovation that led to that income.

Fictional Interest Deduction

When a country allows multinational corporations to deduct fictional interest from their taxable income, instead of discouraging corporations from using excessive debt to finance their operations, these rules provide multinational corporations with a way to shift their profits and underpay tax.

This indicator assesses if the country offers a company fictional interest deduction regime to lower income tax.

Transparency of Company Accounts

When a country does not require all companies to publish annual accounts, multinational corporations can conceal their financial activities, limiting regulatory oversight and making it impossible for government authorities and other stakeholders to evaluate the risks of doing business with a company, such as for public procurement.

This indicator assesses if the country requires all available types of companies with limited liability (except small companies) to keep accounts per the international standard, file their accounts with a government authority, and make them accessible online for free or at a low cost.

Public Country By Country Reporting

When a country does not require all multinational corporations to report their revenue, profits, taxes, staff and tangible assets for each country where they have affiliates, corporations can shift their profits to tax havens, conceal this information within their consolidated accounts at the group level, and underpay tax.

This indicator assesses if the country requires multinational corporations incorporated within its borders, listed on national stock exchanges, or involved in certain sectors to make public their worldwide financial reporting data on a country by country basis.

Tax Rulings and Extractive Industries' Contracts

When a country keeps hidden its specially negotiated arrangements with companies, including tax rulings it issues to companies and contracts it signs in the extractive industries, it gives large multinational corporations an unfair advantage, increases the risk of weakened financial, environmental and social obligations, may erode government revenue, and makes enforcement more difficult - especially when there are many hidden agreements and tax authorities don't have access to them.

This indicator assesses if the country publishes online unilateral cross-border tax rulings and, where relevant, contracts in the extractive industries.

Reporting of Tax Avoidance Schemes

When a country does not require taxpayers and tax advisers to report tax avoidance schemes and uncertain tax positions, multinational corporations are more likely to use these schemes, and tax administrations find it more difficult to prioritise audits and pinpoint ambiguities in the tax law.

This indicator assesses if the country has mandatory disclosure rules for both taxpayers and tax advisers to report any tax avoidance schemes they have used and uncertain tax positions for which reserves have been made in annual corporate accounts.

Deduction Limitation of Interest Payments

When a country allows resident companies to deduct from their tax base the interest payments they have made to affiliates in other countries, this encourages intra-company debt financing. The more debt a company assumes from an affiliate, the more interest it will pay, reducing its tax bill where it is resident. This often results in multinational corporations issuing itself loans and paying high interest rates back to itself purely to shrink profits and underpay tax.

This indicator assesses if the country restricts or disallows the deduction of interest payments paid to non-resident group affiliates from the corporate income tax base. It assesses if a fixed ratio rule for debt-to-equity is used to limit the deduction of interest payments.

Deduction Limitation of Royalty Payments

When a country allows resident companies to deduct from their tax dues the royalty payments they pay to affiliates in other countries for the right to use intellectual property, this allows multinational corporations to abuse intra-group royalty payments to shift profit and underpay tax. They register their intellectual property in affiliates tax havens, then charge fees to use their own intellectual property, paying their profits into tax havens to avoid tax.

This indicator assesses if the country restricts or disallows the deduction of royalties paid to non-resident group affiliates from the corporate income tax base.

Deduction Limitation of Service Payments

When a country allows resident companies to deduct from their tax base the service payments they have made to affiliates in other countries, this encourages multinational corporations to abuse intra-group service payments to shift profits from a profitable subsidiary to one located in a tax haven, and underpay tax as a result.

This indicator assesses if the country restricts or disallows the deduction of intra-group services payments (management fees, technical fees, consulting services fees) to non-resident group affiliates from the corporate income tax base.

Withholding Taxes on Dividends

When a country does not withhold tax on dividend payments made by resident subsidiaries of multinational corporations to affiliates outside the country within the same group, it reduces the government's tax revenue collection associated with income generated within a country's borders. It also creates an incentive for profit shifting, which may cause other countries to lower their tax rates in response in a race to the bottom.

This indicator assesses the country's lowest withholding tax on outbound dividends and compares it with the highest available unilateral withholding tax rate on dividends worldwide.

Controlled Foreign Company Rules

When a country has lax rules on taxing the profits booked in low-tax countries by foreign companies owned and controlled by local parent companies, these local parent companies can exploit loopholes to shift their profits into corporate tax havens through their foreign-controlled companies and underpay tax. They can also reinvest their profits in their foreign companies, indirectly enriching themselves with profit that should have been taxed at home before being reinvested.

This indicator assesses if the country applies robust non-transactional controlled foreign company rules to protect against tax abuse. The rules treat the profits of a local parent company's foreign companies as income directly earned by the local parent company, even when the profits are not distributed up the ladder.

Tax Treaty Aggressiveness

When a country agrees tax treaties with very low or zero tax rates with other countries, it allows multinational corporations to shift their profits out of countries where they operate, employ staff, or make sales, and underpay tax as a result.

This indicator assesses the aggressiveness of a country's tax agreements with other countries by examining the withholding tax rates on dividends, interests and royalty payments.

New rollout approach

The Tax Justice Network has made changes to how the Corporate Tax Haven Index is published. Up until now, the index was updated once every two years. For each update, all the indicators on the index – against which countries' laws and regulations are assessed – were updated simultaneously. Going forward, the index will be updated on a rolling basis in batches. Each batch will include updates to a set of indicators, following the index's new update cycle.

The new approach allows the Corporate Tax Haven Index to capture regulatory change closer to when it occurs and to offer a more dynamic view of countries' complicity in enabling global corporate tax abuse.

This update of the index consists of updates to the following 7 of the index's 18 indicators:

- **Public Country By Country Reporting**
- **Deduction Limitation of Interest Payments**
- **Deduction Limitation of Royalty Payments**
- **Deduction Limitation of Service Payments**
- **Withholding Taxes on Dividends**
- **Controlled Foreign Company Rules**
- **Tax Treaty Aggressiveness**

This update also consists of a number of "supplementary updates" – ie, regulatory changes pertaining to indicators that are not part of the current batch, but were brought to the Tax Justice Network's attention, verified by its researchers and updated on the index as part of the current batch ahead of cycle. Lastly, this update also includes new data on the scale of corporate financial activity entering and exiting countries – this metric (ie the "Global Scale Weight") is updated annually.