



# Name and shame? Evidence from the European Union tax haven blacklist

Aija Rusina

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Platform for Tax Good Governance



The blacklisted countries: American Samoa, Bahrain, Barbados, Grenada, Guam, South Korea, Macau, the Marshall Islands, Mongolia, Namibia, Palau, Panama, St Lucia, Samoa, Trinidad and Tobago, Tunisia and the United Arab Emirates

# First tax havens blacklist published by EU

BBC

NHH

By Jamie Robertson  
Business reporter, BBC News



© 5 December 2017

## EU blacklists 17 tax havens, avoids sanctions

euobserver

### EU puts 17 countries on tax haven blacklist

Almost 50 nations in 'grey' zone given more time to comply

FINANCIAL TIMES

### Europe: EU Releases List of Tax Havens

Published: Tuesday, 05 December 2017 18:29 WRITTEN BY SINEAD CAROLAN



OCCRP

ORGANIZED CRIME AND CORRUPTION REPORTING PROJECT

BUSINESS NEWS DECEMBER 5, 2017 / 12:14 PM / 8 MONTHS AGO

## EU adopts tax haven blacklist, British territories spared



REUTERS



*"The unveiling of the EU tax haven blacklist was covered in our Alert dated 12 December, 2017. While the consequences of a jurisdiction being on the blacklist remain largely unclear, clients may wish to review whether they have transactions which involve blacklisted jurisdictions and to consider carefully the uncertainty and possible reputational consequences of undertaking new transactions involving blacklisted jurisdictions."*

Ropes & Gray  
January 18, 2018



*"For companies, the EU's move creates several new risks. Multinationals with operations in the countries on the blacklist could see EU jurisdictions apply more scrutiny and withholding, and that may mean a re-examination of financial flows and the development of plans to move some operations from countries that are likely to remain on the list."*

## EY Tax Insights



*"It's important to know where your company stands on the risk spectrum. If governments are going to reform their systems, you've got to know the effect the changes will have on your organization and communicate concerns to governments if you believe the effect is unreasonable. Companies' audit risk might be much higher."*

Mat Mealey, EY Europe, Middle East, India and Africa  
International Tax Services Leader



*"The public has had enough of governments saying they will do better. Real action is needed. It is completely pointless to have a blacklist with no sanctions. Tax avoiders, and the countries that sponsor them will all be letting out a sigh of relief today."*

Alex Cobham, chief executive of the Tax Justice Network  
December 5, 2017



**What effect did publication of the EU tax haven blacklist have on share prices of multinational firms with subsidiaries in the blacklisted countries?**





## Hypothesis: Negative market reaction due to EU shaming

- Reputational costs (Graham et al. 2014; Akamah et al. 2018)
  - Damage to firms' brand value
  - Public pressure or backlash against the firm or its products
  - Losing customers to a boycott
  - Diminished prospects for recruiting and retaining employees
  - Weakened ability to raise capital
- Audits and monitoring of transactions involving affiliates in tax havens
- Tax havens face countermeasures and might change their tax laws, jeopardising firm's tax saving strategies
  - Blacklisting damages states' reputations among investors, and thus produces pressure to comply through actual or anticipated capital flight (Sharman, 2009)



## Results

- Significantly negative stock returns following publication of the EU tax haven blacklist for firms with tax haven affiliates
  - Publication of the blacklist reduced value of firms connected to the blacklisted tax havens by 0.6% relative to other firms
  - Publication of the blacklist reduced the overall market capitalization of firms connected to the blacklisted tax havens by 18 billion USD
- More negative stock returns for firms with a large proportion and number of tax haven affiliates
- More negative stock returns for firms with affiliates in tax havens that were listed unexpectedly
- Differences in the market reaction (corporate citizenship, tax aggressiveness and expropriation)



## Data

- Subsidiary and financial data of all listed firms in Bureau van Dijk's Orbis database
- Market data from Datastream and Orbis
- BNY Mellon, KPMG, Property Rights Alliance, PRS Group, RepRisk Transparency International and the World Bank, among others



## Sample selection

All publicly listed active firms as of December 2017	67 113
Less:	
Stocks with less than 100 non-missing return observations during estimation window	15 926
Purely domestic firms with no foreign affiliates	10 613
Firms with no share price data for the event period	8 923
Firms with missing data for total assets	7 982
Stocks not actively traded (no price changes between December 4, 2017 and December 8, 2017)	3 940
Penny stocks with prices below 0.10 \$	3 315
Firms with total assets below 5 mln \$	1 849
<u>Remaining firms for the final sample</u>	<u>14 537</u>



## Event study methodology

$$ActualReturn_{it} = \ln(Price_{it}) - \ln(Price_{it-1}) = \ln(Price_{it}/Price_{it-1})$$

$$ActualReturn_{it} = \alpha_i + \beta_i MarketReturn_{mt} + u_{it}$$

$$ExpectedReturn_{it} = \hat{\alpha}_i + \hat{\beta}_i MarketReturn_{it}$$

$$AbnormalReturn_{it} = ActualReturn_{it} - ExpectedReturn_{it}$$

$$CAR_i(T_1, T_2) = \sum_{i=T_1}^{T_2} AbnormalReturn_{it}$$



## Identification strategy

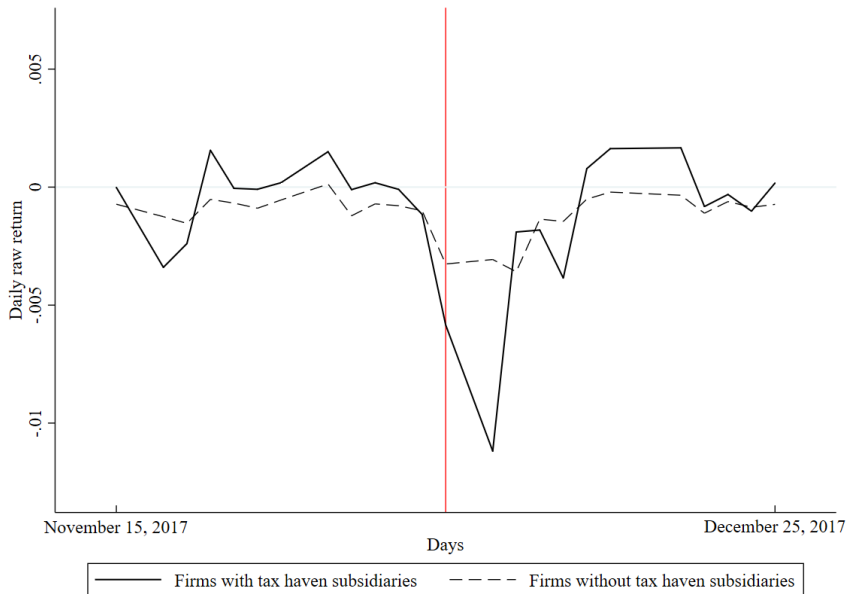
$$CAR_i = \alpha + \beta TaxHavenExposure_i + \mathbf{X}_i\gamma + \epsilon_i,$$

- $CAR_i$ : cumulative abnormal return
- $TaxHavenExposure_i$ : dummy=1 if firm has affiliates located in tax havens
- $\mathbf{X}_i$ : controls, including country and industry fixed effects
- Two-way clustering of standard errors (country and industry)



## Summary statistics

	Firms with tax haven exposure	Firms without tax haven exposure	Difference all	Difference matched
	Mean	Mean		
Total assets (th USD)	8 786 724	1 835 130	6 951 594***	230 4115
Number of subsidiaries	81.41	18.54	62.88***	5.41
Proportion of foreign subsidiaries	0.61	0.49	0.12***	0.006
Corruption exposure (1/0)	0.62	0.23	0.40***	0.17*
Effective tax rate	0.165	0.237	-0.07***	-0.03
Foreign institutional ownership	0.57	0.50	0.08***	0.03
Property rights	0.85	0.82	0.03***	0.01
Rule of law	0.56	0.5	0.05***	-0.02







## Main result: Summary statistics on cumulative returns

	Firms without tax havens	Firms with tax havens	Full sample		Matched sample	
	Mean	Mean	Mean	Diff	Mean	Diff
CRR (%)	-0.64**	-1.15***	-0.7***	0.51***	-1.14**	0.49**
<b>Market model</b>						
CAR (%)	-0.74	-1.29***	-0.8*	0.56***	-1.07*	0.34**
<b>Market-adjusted model</b>						
CAR (%)	-0.69	-1.2***	-0.75*	0.51***	-1.21*	0.43**
<b>Mean-adjusted model</b>						
CAR (%)	-0.81	-1.37***	-0.88*	0.55***	-1.32	0.46*
<b>Capital asset pricing model</b>						
CAR (%)	-0.53	-1.66***	-1.03*	1.13***	-1.13*	1.07**



## Differences in market reaction: Part 1

- Retail firms experienced a larger stock price decrease
  - Negative consumer reaction to bad corporate citizenship
- More tax aggressive firms had more negative returns
  - More to lose if tax haven preferential treatment is limited or countermeasures are applied
  - Firms might be audited or fined for past or overly aggressive tax avoidance
  - Potential future costs of restructuring to keep corporate tax payments low



## Differences in market reaction: Part 2

- Firms facing high expropriation risk had less negative returns
  - The underlying secrecy of tax havens can be used for expropriation purposes
  - Managers who support tax avoidance activities might be aggressive with reporting firm's accounting earnings
  - Suspicion of accuracy of firm's financial statements
  - News on firm's tax avoidance might be perceived as evidence not only about firm's behaviour towards tax authorities, but also about insiders' willingness to be aggressive with investors
  - Blacklisting should contribute towards increased auditing, monitoring, scrutiny and transparency and less shareholder expropriation



## Conclusion

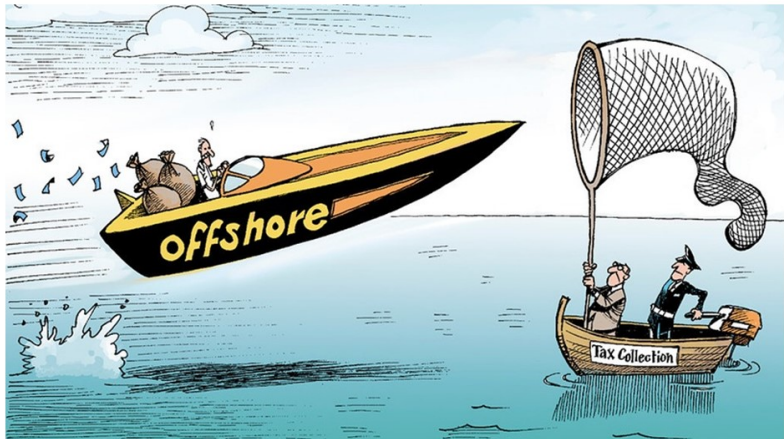
- Publication of EU tax haven blacklist on December 5, 2017 led to negative stock returns of firms with tax haven affiliates
  - Publication of the blacklist reduced value of firms connected to the blacklisted tax havens by 0.6% relative to other firms
  - Publication of the blacklist reduced the overall market capitalization of firms connected to the blacklisted tax havens by 18 billion USD
- More negative stock returns for firms with a large proportion and number of tax haven affiliates
- More negative stock returns for firms with affiliates in tax havens that were listed unexpectedly
- No market reaction to large exposure to grey-listed countries
- Retail firms faced particularly large share price decrease
- More tax aggressive firms faced more negative returns
- The negative effect was less pronounced in countries with low levels of investor protection and weakly governed firms



## Policy implications

- **The bark is the bite**
- Many countries have been cooperative to avoid public shaming
- Investors care about public tax haven shaming by international organisations and news media
- Negative stock returns after publication of the blacklist, despite lack of any specific sanctions or penalties
- Potential negative investor reaction might deter firm's management to engage in tax avoidance or increase costs of tax avoidance
- **Are these spotlights followed by improvements in firm's corporate tax strategies?**
- **Do these spotlights contribute towards less tax avoidance in the future?**

# Thank you for attention!



NORWEGIAN SCHOOL OF ECONOMICS



## Sample firms by country and tax haven exposure

Country	Number of firms	Fraction of tax haven exposure	Country	Number of firms	Fraction of tax haven exposure
Kuwait	78	64.10%	Norway	65	10.77%
Switzerland	129	31.78%	Greece	66	10.61%
South Korea	729	29.06%	Brazil	137	8.76%
Netherlands	92	28.26%	Turkey	173	8.67%
Bermuda	475	27.79%	Singapore	307	8.47%
United Kingdom	426	25.59%	China	1 069	7.23%
Chile	51	23.53%	Canada	263	6.46%
Japan	1 361	23.42%	Australia	269	6.32%
Egypt	74	22.97%	Russia	72	5.56%
Hong Kong	196	21.94%	Spain	61	4.92%
Germany	244	20.90%	Malaysia	238	4.62%
Italy	59	18.64%	Israel	167	4.19%
Belgium	61	16.39%	Pakistan	190	3.68%
Finland	107	15.89%	Thailand	182	2.20%
Denmark	76	15.79%	Poland	72	1.39%
France	272	15.44%	Indonesia	163	1.23%
Taiwan	745	14.23%	Sri Lanka	121	0.83%
Cayman Islands	945	13.76%	Bangladesh	199	0%
India	1 316	12.25%	Vietnam	135	0%
USA	2 506	11.97%	Rest of world	305	21.97%
Sweden	268	11.19%			
Mexico	73	10.96%	<b>Total</b>	<b>14 537</b>	<b>14.61%</b>



## Sample firms by industry

Industry	Number of firms	Fraction of tax haven exposure	Industry	Number of firms	Fraction of tax haven exposure
Shipbuilding, Railroad	41	33.90 %	Printing, Publishing	104	15.23 %
Defense	7	30.00 %	Wholesale	722	15.11 %
Electronic Equipment	981	27.10 %	Construction Materials	576	15.02 %
Apparel	164	25.52 %	Candy, Soda	66	14.58 %
Automobiles, Trucks	351	25.05 %	Construction	446	14.47 %
Measuring, Control	162	24.58 %	Pharmaceutical Products	603	14.01 %
Recreation	115	24.55 %	Electrical Equipment	306	13.90 %
Aircraft	34	24.49 %	Food Products	402	13.14 %
Transportation	461	24.44 %	Rubber, Plastic Products	205	12.75 %
Machinery	712	24.30 %	Personal Services	138	11.94 %
Tobacco Products	17	24.00 %	Metal Mining	154	11.61 %
Consumer Goods	302	21.14 %	Retail	526	11.49 %
Computers	190	20.65 %	Restaurants, Hotels	266	11.08 %
Chemicals	659	20.63 %	Fabricated Products	78	9.73 %
Steel Works	427	20.42 %	Agriculture	176	9.38 %
Shipping Containers	59	19.77 %	Textiles	304	8.58 %
Almost Nothing	31	17.78 %	Trading	612	8.08 %
Petroleum, Natural Gas	262	17.54 %	Utilities	308	7.57 %
Communication	326	16.84 %	Real Estate	551	5.49 %
Entertainment	165	16.67 %	Precious Metals	80	5.17 %
Computer Software	605	16.57 %	Insurance	29	4.76 %
Beer, Liquor	100	16.55 %	Healthcare	124	4.44 %
Medical Equipment	133	16.49 %	Banking	170	3.64 %
Business Supplies	192	16.43 %	Coal	43	3.23 %
Business Services	1 036	16.11 %			
			<b>Total</b>	<b>14 537</b>	<b>14.61 %</b>





## Affiliates of sample firms in tax haven countries

Country	Number of tax haven subsidiaries	Fraction of all tax haven subsidiaries
South Korea	7 157	40.88%
United Arab Emirates	3 309	18.90%
Marshall Islands	1 381	7.89%
Panama	1 282	7.32%
Tunisia	932	5.32%
Namibia	663	3.79%
Macau	655	3.74%
Barbados	559	3.19%
Bahrain	542	3.10%
Samoa	483	2.76%
Trinidad and Tobago	238	1.36%
Mongolia	174	0.99%
Saint Lucia	120	0.69%
Grenada	10	0.06%
Palau	2	0.01%
<b>Total</b>	<b>17 507</b>	<b>100%</b>



## Main result I: Cumulative raw returns

	(1)	(2)	(3)	(4)	(5)	(6)
Tax haven exposure	-0.00008 (-0.073)	-0.00134*** (-3.205)				
Proportion of tax havens			-0.00510*** (-3.627)	-0.00567*** (-5.398)		
Number of tax havens					-0.00003 (-0.433)	-0.00009*** (-3.118)
Log(Number of foreign subsidiaries)		0.00077** (2.623)		0.000615** (2.577)		0.000655** (2.645)
$R^2$	0.076	0.076	0.076	0.076	0.076	0.076
Observations	14537	14537	14537	14537	14537	14537



## Main result II: Cumulative abnormal returns

	(1)	(2)	(3)	(4)	(5)	(6)
Tax haven exposure	-0.00031 (0.272)	-0.00145*** (-2.948)				
Proportion of tax havens			-0.00707*** (-3.244)	-0.00881*** (-3.791)		
Number of tax havens					-0.00005 (-0.599)	-0.00015*** (-3.370)
Log(Number of foreign subsidiaries)		0.00105** (2.670)		0.00100** (2.602)		0.00101** (2.526)
$R^2$	0.155	0.157	0.155	0.157	0.155	0.157
Observations	14537	14537	14537	14537	14537	14537



# Robustness

	(1)	(2)	(3)	(4)	(5)
Proportion of tax havens	-0.00881*** (-3.791)	-0.01230*** (-7.279)	-0.01168*** (-3.988)	-0.01282*** (-4.564)	-0.00882*** (-3.601)
Proportion of grey tax havens					-0.00088 (0.762)
Log(Number of foreign subsidiaries)	0.00100** (2.602)	0.00117 (0.955)	0.00094 (1.593)		0.00128** (3.226)
Fixed effects	Yes	Yes	Yes	No	Yes
	Main	Matched on number of foreign subsidiaries	Matched on total assets	No controls	Grey list
$R^2$	0.157	0.107	0.035	0.003	0.157
Observations	14537	485	3247	14537	14537



## Previous tax haven lists

	(1)	(2)
Likely to be on EU list · Was on EU list	-0.00418 (-0.747)	
Likely to be on EU list · Was not on EU list	-0.00271 (-0.637)	
Not likely to be on EU list · Was on EU list	-0.00680*** (-9.162)	
Was on all lists · Was on EU list		-0.003071 (-1.318)
Was on all lists · Was not on EU list		-0.00095 (-0.092)
Was on no lists · Was on EU list		-0.00632*** (-6.478)
Log(Number of foreign subsidiaries)	0.00071 (1.440)	0.00070 (1.543)
$R^2$	0.076	0.076
Observations	14537	14537



## Firm-level cross-sectional variation

	(1)	(2)	(3)	(4)	(5)
Proportion of tax havens	-0.00881*** (-3.791)	-0.00834*** (-3.627)	-0.00107*** (-2.967)	-0.00887*** (-2.985)	-0.00683*** (-3.93)
Proportion of tax havens · Retail		-0.03570*** (-15.264)			
Proportion of tax havens · Tax aggressiveness			-0.01391*** (-2.884)		
Proportion of tax havens · Cash effective tax rate				0.03900*** (8.828)	
Proportion of tax havens · Governance					0.04843*** (-3.21)
	Main	Retail	Tax aggressiveness	Cash ETRs	Governance
$R^2$	0.157	0.157	0.157	0.158	0.157
Observations	14537	14537	14537	14537	14537



## Country-level governance

	(1)	(2)	(3)	(4)	(5)
Proportion of tax havens	-0.00118*** (-2.604)	-0.00177*** (-2.798)	-0.00665*** (-2.704)	-0.00431*** (-4.939)	-0.00829*** (-2.794)
Proportion of tax havens · Governance	-0.01162*** (-3.450)	-0.00831*** (-8.556)	-0.00536*** (-3.797)	-0.00517*** (-3.353)	-0.00577 (-1.556)
$R^2$	0.157	0.157	0.156	0.157	0.156
Observations	14537	14537	14537	14537	14537
	Property rights	Country risk	Rule of law	Minority shareholder protection	GDP per capita