EU Banks' Country-by-Country Reporting

A synthesis of the Tax Research LLP Report

June 2015

1. General assessment

- The report summarises and interprets country-by-country reporting data from 26 European Union banks available in early June 2015, 17 of which have published the full data now required by the time the report was prepared[1].

- The report highlights that the banks surveyed have been systematically over-reporting their profits in some low tax jurisdictions or places identifiable as tax havens[2], whilst appearing to under-report them in those places where they have major centres of operation. The study shows a potential reallocation of profits - for the purpose of reducing tax liabilities - exceeding €100 million[3] into or out of 39 jurisdictions.

- There appears to be above expected relocation of profits to jurisdictions where this might have been anticipated including Belgium, Luxembourg, Ireland, Singapore, Hong Kong, UAE, Jersey, Mauritius and the Isle of Man, all of which have a reputation for acting as offshore tax locations for various reasons.

- The top 10 of banks showing the highest risk of base erosion and profits shifting[4]

    1. Deutsche Bank
    2. Barclays
    3. Rabobank Group
    4. Standard Chartered
    5. Banco Bilbao Vizcaya Argentaria, S.A
    6. Royal Bank of Scotland
    7. BNP Paribas
    8. KBC Bank
    9. ING
    10. Credit Agricole

2. Country assessment

a. Germany

[1] This data is required to be reported by Article 89 of the Capital Requirements Directive IV. Under the terms of that Directive full disclosure is not required for 2014 until 1 July 2015. Some banks (e.g. Lloyds) have made it clear that they will not publish full data for 2014 before being legally required to do so even though their accounts for that year are now available. As a result for nine banks the limited data of the type required to be published in 2014 has been used in preparing this report.

[2] To say it differently: there appears to be very consistent relocation of profit from EU states to tax havens.

[3] Assuming that many banks have not integrated intra-group transactions in their data reported per jurisdiction (see the conclusion section below), this could explain why the total figure suggested by the report for potential reallocation of profits into or out of the analysed jurisdictions seems relatively low.

[4] This overall ranking for the surveyed banks combines the results achieved by applying four different methods assessing potential profit shifting within individual banks.

- The report suggests that banks' declared profits tend to be under-reported in Germany;

- **Deutsche Bank** comes first in the overall ranking of banks showing the highest potential risk of base erosion and profits shifting. Using the "*unitary taxation risk assessment*" method, the report suggests that DB might have reallocated 28.5% of its total declared profits (i.e. by overstating its profits in non EU member states that are either tax haven states or non- tax haven states[5] whilst under-reporting them in EU member states where it has major centres of operation).

  It is also interesting to note that DB records its highest profit per head in Malta, which is known to be a significant tax haven for German companies. The ratio between DB's highest profit per head and its average profit per head is extremely high (see the table at the bottom of page 2 of the report), which suggests that DB largely over-reports its profits in Malta for tax benefit purposes. The ratio suggests that profits reallocated to Malta have very little commercial substance. Another ratio used to analyse the data - which compares real economic activity (as represented by the combined turnover and people employed ratio) with profit – also suggests that DB has a high risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

- **Commerzbank AG** comes thirteenth in the overall ranking of banks showing the highest risk of base erosion and profits shifting. Using the "*unitary taxation risk assessment*" method, the report suggests that Commerzbank has reallocated 19.1% of its total declared profits (i.e. by overstating its profits in non EU member states that are either tax haven states or non- tax haven states whilst under-reporting them in EU member states where it has major centres of operation). It is also worth noting that this bank records its highest profit per head in the Netherlands, which is known to be a tax haven[6]. Furthermore, Commerzbank's ratio comparing the combined employee and turnover ratio with profit suggests that it has a relatively high risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

- **DZ Bank AG, LBBW Landesbank Baden-Württemberg, KfW, and Württemberg** have not yet published their full data - including profit before tax and corporate tax paid by country.

b. France

- France appears to enjoy over-reporting of bank profit. At present it is not clear why this is the case.

[5] The report states that much of the profits that are being reallocated out of the EU to non-tax haven states are to the USA. Yet, the report also points out that the high profit reporting enjoyed by the USA could be partly due to the fact that some EU banks - such as BNP Paribas - report their income from the Cayman Islands in the US. Furthermore, it is also possible that some of the profits that are being reallocated to the USA are actually recorded in state of Delaware, which is known to be a tax haven. But, given the lack of information, it is not possible to draw any firm conclusions on this issue.

[6] However, in the case of Commerzbank AG, the ratio of difference between that level of profit and that for the bank as a whole is relatively low compared to other systemic banks (see the table at the bottom of page 2 of the report).

- The four biggest French banks - i.e. **BNP Paribas**, **Crédit Agricole**, **Société Générale** and **BPCE SA** - are ranked amongst the EU banks showing the highest risk of base erosion and profits shifting.

- **BNP Paribas** is the only one of the four above-mentioned banks which always remains within the 'top ten' ranking regardless of the methodology used to analyse the data. Like BPCE SA, BNP Paribas records its maximum profit per head in Ireland, which is known as a tax haven. The fact that BNP Paribas' maximum profit per head as a ratio of average profit per head is relatively high tends to indicate that it may over-report its profits in Ireland. Another ratio used to analyse the data - which compares real economic activity (as represented by the combined turnover and people employed ratio) with profit - confirms that BNP Paribas has a high risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

- As for **Crédit Agricole** and **BPCE SA**, they register their highest profit per head respectively in Australia[7] and Ireland: the latter is on the TJN Financial Secrecy Index. Although their highest profit per head as a ratio of average profit per head is much lower compared to BNP Paribas as well as other EU systemic banks, the analysed data suggests nonetheless that Crédit Agricole and BPCE may have over-reported their profits respectively in Australia and Ireland; it is not clear why this might be the case in Australia.

- **Société Générale** and **Crédit Mutuel** have not yet published their full data - including profit before tax and corporate tax paid by country;

c. United Kingdom

- The data suggests that banks' declared profits tend to be under-reported in the UK. However, UK data is likely to be distorted by losses resulting from fines for financial misdemeanours charged on many UK banks. If this is the case it may be hard to draw conclusions on profit shifting to and from the UK because this other factor may be bigger in its impact.

- **Barclays**, **Standard Chartered plc** and **Royal Bank of Scotland plc** (RBS) are ranked amongst the 'top 10' EU banks showing the highest risk of base erosion and profits shifting. HSBC appears to have a low risk but has yet to publish full data to permit analysis.

- Using the "*unitary taxation risk assessment*" method, the report suggests that **Barclays**, **Standard Chartered plc** and **RBS** have reallocated respectively 26.4%, 40.5% and 15.5% of their total declared profits (including by overstating large part of their profits in identifiable low tax jurisdictions).

  It is also worth noting that **Barclays** and **Standard Chartered plc** record their highest profit per head respectively in Luxembourg and Ireland, which are known to be tax havens. The ratio between Barclays' highest profit per head and its average profit per

[7] Australia is not indeed on the FSI. The Australian data appears quite off and needs explanation.

head is extremely high (see the table at the bottom of page 2 of the report), which indicates that this bank largely over-reports its profits in Luxembourg for tax benefit purposes. Standard Chartered's ratio between its highest level of profit per head and its average profit per head - although much lower than that of Barclays - also indicates that this bank may over-report its profits in Ireland.

As for **RBS,** the report points out quite surprisingly that this bank has more than likely over-reported to a large extent its profits in Finland, a country which is not on the TJN Financial Secrecy Index. Another ratio - which compares real economic activity (as represented by the combined turnover and people employed ratio) with profit - confirms that RBS has a high risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

- **HSBC Holdings plc** and **Lloyds Banking Group plc** have not yet published their full data - including profit before tax and corporate tax paid by country. Furthermore, the report points out that **Barclays** has not disclosed data for all the jurisdictions in which it appears that it trades, offering 'unallocated' data in its place. This creates real problems with data credibility in the case of this bank.

d. Spain

- The data suggests that Spain comes first in the ranking of tax jurisdictions where bank profits tend to be under-reported. However, the report underlines that such data might be distorted as a result of the impact of the economic crisis on the Spanish economy. As with the UK, this over-riding economic impact may be bigger than any impact of profit shifting.

- **Banco Bilbao Vizcaya Argentaria S.A** is ranked 5th in the 'top 10' EU banks showing the highest risk of base erosion and profits shifting amongst Spanish banks. Using the "*unitary taxation risk assessment*" method, the report suggests that BBVA has reallocated 35.8% of its total declared profits (i.e. by overstating its profits in non EU member states that are either tax haven states or non- tax haven states whilst under-reporting them in EU member states where it has major centres of operation).

  It is also interesting to note that BBVA records its highest profit per head in Ireland, which is known to be a tax haven. The ratio between BBVA's highest profit per head and its average profit per head is relatively high (see the table at the bottom of page 2 of the report), which indicates that this bank may over-report its profits in Ireland for tax benefit purposes. Another ratio used to analyse the data - which compares real economic activity (as represented by the combined turnover and people employed ratio) with profit - confirms that BBVA has a higher than average risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

- **Santander** and **Caixa Bank SA** have not yet published their full data - including profit before tax and corporate tax paid by country. Caixabank SA has also clearly failed to disclose data for all the jurisdictions in which it appears that it trades, offering 'unallocated' data in its place[8]

e. The Netherlands

- The data suggests that banks tend to largely under-report their profits in the Netherlands. In other words, it doesn't seem to pay for this country to host bank headquarters in terms of potential tax yield and despite the fact that banks not registered in the Netherlands do tend to overstate their apparent profits earned in that country. There are answers needed to resolve this paradox;

- **Rabobank Group** and **ING** are ranked amongst the 'top 10' EU banks showing inflated risk of base erosion and profits shifting. Depending on the methodology used to analyse the data, the position of these two banks within the 'top 10 ranking' varies accordingly. **ABN AMRO** is ranked 15th in the overall ranking.

- Using the "*unitary taxation risk assessment*" method, the report suggests that **Rabobank Group** has reallocated 18.9% of its total declared profits (i.e. by overstating its profits in non EU member states that are either tax haven states or non- tax haven states whilst under-reporting them in EU member states where it has major centres of operation).

  Rabobank Group records its highest profit per head in Curacao, an island in the southern Caribbean Sea that is a constituent country of the Kingdom of the Netherlands. This location has long been associated with tax haven activities when linked to the Netherland Antilles.

  The ratio between Rabobank Group's highest profit per head and its average profit per head is very high (see the table at the bottom of page 2 of the report) suggests that this bank may over-reports its profits in Curacao for tax benefit purposes. Another ratio used for data analysis - which compares real economic activity (as represented by the combined turnover and people employed ratio) with profit - confirms that Rabobank Group has a high apparent risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

- As for **ING**, the report suggests that it has reallocated 43.3% of its total declared profits (i.e. by overstating its profits in non EU member states that are either tax haven states or non- tax haven states whilst under-reporting them in EU member states where it has major centres of operation). ING records its highest profit per head in Ireland[9], which is known to be a tax haven. Furthermore, its ratio comparing the combined employee and turnover ratio with profit suggests that it has a relatively high risk of significant profit shifting, from jurisdictions where real economic activity appears to be occurring towards those where little such actual activity appears to be arising;

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[8] For example, Caixa has not disclosed its income per head by country. Such information is crucial as it would enable citizens and decision-makers to identify by location where potential mis-statement might be arising and the potential scale of that mis-statement and to then express this as a ratio and so produce a ranking;

[8] In the case of ING, the maximum profit per head as a ratio of average profit per head is however relatively low compared to other systemic banks (see the table at the bottom of page 2 of the report).

f. Belgium

- Belgium is ranked amongst the 'top 3' tax jurisdictions where EU bank profits tend to be over-reported for tax benefit purposes. The implication is that Belgium may be providing a favourable environment in which banks might wish to declare profits, and this perception accords with its known behaviour;

- **KBC Bank** is ranked amongst the 'top 10' EU banks showing the highest risk of base erosion and profits shifting. Using the "*unitary taxation risk assessment*" method, the report suggests that it has reallocated 15.3% of its total declared profits (including by overstating part of its profits in non EU tax haven states).

  KBC Bank records its highest profit per head in Luxembourg, which is known to be a tax haven. The ratio between KBC's highest profit per head and its average profit per head is moderately high (see the table at the bottom of page 2 of the report), which indicates that its may over-report its profits in Luxembourg for tax benefit purposes;

3. Conclusions

- **Some countries are seriously losing out** in terms of revenue and profit reporting as a result appears to be high. This is particularly true of states that host bank head office locations, France excepted;

- **Some EU countries appear to be gaining** from tax competition in ways that appear inconsistent with the level playing field required by the internal market. Tax haven activity appears to be significant.

- Broadly speaking **larger banks appear more likely to be profit shifting**;

- Some European Union jurisdictions emerge as very clear potential destinations for the relocation of profits in these surveys. In particular Ireland seems to be a particularly likely destination whilst Malta also stands out. Some other destinations, such as Finland, are harder to explain.

- **Country-by-country reporting data is useful**, and powerful. **Nevertheless, there are considerable limitations in the data published** for the following reasons:

  - **Not all banks surveyed have reported full data yet**. For example, some of them have not yet published profits and tax paid data;

  - **The Article 89 of the Capital Requirements Directive IV is too broadly drafted**. In particular, the demand made on corporate tax disclosure is for tax payments made (or received) in a year. This makes little accounting sense since such payments and receipts are heavily influenced by the financial performance of the bank in earlier years, but that earlier year performance may have little relationship to the currently declared profits and the consequence is that information declared on profits and tax payments need have very little correlation to each other.

→ CRDIV Article 89 should therefore be consistently interpreted across all EU jurisdictions. What should be demanded is tax data for the year for which profits or losses are disclosed split into three parts. The first is the current tax liability for the year for each jurisdiction; the second is the deferred tax liability for the year for each jurisdiction and thirdly the figure for corporation tax paid in the year by jurisdiction. This would remove the anomalies in the current data disclosure which at present creates the risk that like is not being compared with like either within one banks data (this definitely being true in the case of the UK where tax paid largely relating to a prior year is compared to a current year's profit) or between states (where France requires current year provision disclosure but the UK does not, for example)

- **It is unclear whether data reported per jurisdiction includes or excludes intra-group transactions**[10]. This ambiguity produces uncertainty and reduces the value of the data available.
  → CRDIV Article 89 should be consistently interpreted across all EU jurisdictions, so that: (i) turnover includes intra-group sales in a jurisdiction (with a reconciling adjustment to reported group turnover being provided); (ii) profit reported includes the consequence of intra-group transactions (and is then reconciled to group reported profit);

- **Some banks** (e.g. Barclays and some Spanish banks) **have not disclosed data for all the jurisdictions** in which it appears that they trade, offering 'unallocated' data in its place.
  → Data should be reported for every jurisdiction in which a bank trades, without exception;

[10] If only third party data are reported, this implies that intra-group transactions - in which much of the likely base erosion and profits shifting takes place - is suppressed for reporting purposes.