

Key Corporate Tax Haven Indicators

Haven Indicator 3:

Loss Utilisation

What is measured?

This indicator measures whether a jurisdiction provides unrestricted loss carry backward and/or loss carry forward for ordinary and trading losses. Capital losses fall outside the scope of this indicator. Accordingly, we have split this indicator into two components.

1. **Loss carry backward:** we assess whether a jurisdiction provides loss carry backward provisions in its rules determining the corporate income tax base.
2. **Loss carry forward:** we assess whether a jurisdiction offers unrestricted loss carry forward (independent of change of ownership rules) in its rules determining the corporate income tax base.

The overall haven score for this indicator is calculated by the simple addition of the haven scores of each of these two components. The scoring matrix is shown in Table 3.1 and full details of the assessment logic are presented in Table 3.3 below.

Table 3.1. Scoring Matrix Haven Indicator 3

Regulation	Haven Score [100 = maximum risk; 0 = minimum risk]
Component 1: Loss carry backward (50)	
<p><u>Loss carry backward is available</u></p> <p>Corporates are allowed to transfer losses accrued in the current (or a later) tax year to a previous tax year, and thereby to obtain a tax reduction of corporate income taxes assessed and/or paid in the previous tax year (so as to obtain a reimbursement).</p>	50

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<p><u>Loss carry backward is not available</u></p> <p>Losses accrued in the current tax year cannot be transferred back to previous tax years.</p>	0
<p>Component 2: Loss carry forward (50)</p>	
<p><u>Unrestricted loss carry forward</u></p> <p>Losses accrued in the current tax year can be carried forward to reduce taxable income in future tax years without any restrictions.</p>	50
<p><u>Loss carry forward is restricted to a maximum of more than five years</u></p> <p>Losses accrued in the current tax year can be carried forward only for a certain number of years, but this number is higher than five.</p> <p>Or</p> <p><u>Loss carry forward is restricted by an annual ceiling ("minimum tax")</u></p> <p>Losses accrued in past tax years can be carried forward for an unlimited number of years, but the extent to which these losses can be used to reduce income taxes is restricted in each current tax year.</p>	37.5
<p><u>Loss carry forward is restricted to a maximum of more than five years, and by an annual ceiling</u></p> <p>Losses accrued in the current tax year can be carried forward only for a certain number of years, but this number is higher than five, and there is an annual ceiling.</p> <p>Or</p> <p><u>Loss carry forward is restricted to a maximum of five years or less</u></p> <p>Losses accrued in the current tax year can be carried forward only for up to five subsequent years.</p>	12.5
<p><u>Loss carry forward is restricted to a maximum of five years or less, and by an annual ceiling</u></p> <p>Losses accrued in the current tax year can be carried forward only for up to five subsequent years and there is an annual ceiling.</p> <p>Or</p> <p><u>No loss carry forward is available</u></p>	0

Ordinary companies generate revenue by selling goods or providing services and expenses, such as for paying salaries and buying intermediate goods and services. When company revenues exceed expenses in a given tax year, the company makes a taxable profit. If, however, the expenses exceed revenue, the company makes a loss. Normally, if a company is loss making, no corporate

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income taxes are due in that tax year. In addition, most jurisdictions allow this loss to be carried forward. Carrying forward losses allows a company to use the losses of the past to offset or reduce taxes due in future years when the company may be making a profit.

Carrying losses backward allows a company to go back in time to whenever it made a loss to reduce, retroactively, the profits booked in an earlier tax year in which it made a profit. Thus, tax due on profits in earlier years is reassessed and adjusted accordingly. Assuming a company will have paid more tax in the past than what it owes after carrying back losses, the company would expect to receive a corresponding reimbursement.

Most jurisdictions do not allow loss carry backward, or they allow it only for a limited time.¹ According to the Organisation for Economic Co-operation and Development (OECD), loss carry backward provisions have a more severe impact on reducing government budgets and are more difficult to administer than carry forward provisions.²

To avoid abuse of such provisions by multinational companies,³ jurisdictions generally place limits on the time and value of loss carry forward rules. The strictest time limitation for loss carry forward we have found in the literature is five years (such limitation is found in Argentina, China, Poland, Portugal, Turkey).⁴

This time limit threshold refers to the period within which revenue administrations are permitted to reopen tax assessments.⁵ For reopening an assessment, tax administrations must rely on company records. According to the OECD Global Forum Joint Ad Hoc Group on Accounts, the necessary accounting record retention period and the accessibility to accounting records are as follows:

Accounting records need to be kept for a minimum period that should be equal to the period established in this area by the Financial Action Task Force. This period is currently five years. A five-year period represents a minimum period and longer periods are, of course, also acceptable.⁶

Thus, we have chosen a five-year threshold in assessing the haven risk of loss carry forward provisions.

The data for this indicator was collected primarily from the country analyses and country surveys in the International Bureau of Fiscal Documentation (IBFD) database.⁷ In some instances, we have also consulted additional local websites and reports.

All underlying data can be accessed freely in the CTHI [database](#).⁸ To see the sources we are using for particular jurisdictions please consult the assessment

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logic in Table 3.3 and search for the corresponding info IDs (IDs 509 and 510) in the database report of the respective jurisdiction.

Why is this important?

By carrying forward billions in losses to future tax years, global businesses have gamed the system with loss to generate colossal deductions and pay no or very little tax. The use of artificial losses to minimise tax has been a core element of Apple's tax strategy in Ireland. In 2015, the artificial inflation of debt and a multibillion-dollar purchase of Apple's own intellectual property generated billions in recognised losses for Apple's subsidiary in Ireland.⁹ In other words, Apple Ireland borrowed heavily to purchase Apple's intellectual property from an Apple subsidiary tax-resident in Jersey (which applies nearly zero tax). As a result, Apple Ireland had billions in deductible interest payments, billions in deductible intellectual property purchase expenses, and billions in capital allowances; enough to write off all profits from European sales for years. Similarly, Apple's offshore entity in Jersey earned billions from the sale of intellectual property and interest repayments which went untaxed.¹⁰

The Apple case illustrates the damage that multinational corporate practice has on public revenues. While Apple's business in Europe is thriving and its sales continue to [rise worldwide](#),¹¹ Apple declares losses. While piles of cash continue to accumulate in Jersey, Ireland's subsidiary is heavily in debt.

These tax avoidance games would not have been possible if comprehensive limitations were in place. Both this indicator (Haven Indicator 3) and our indicators on intra-group payments deductibility ([Haven Indicators 15](#), [16](#) and [17](#)) present measurements and alternatives towards a financially consistent and fiscally responsible environment for multinational corporations.

Annual tax accounting systems are a basic feature of modern income taxation. Income tax is calculated and charged on the income earned in the preceding fiscal year, which consists of 12 consecutive months. However, this system involves an intrinsic unfairness: "taxpayers whose incomes fluctuate from year to year should receive tax treatment equivalent to those with stable incomes".¹² To eliminate this intrinsic unfairness, countries provide tax relief on profits to reflect losses. Losses may be carried forward and set off against future profits and/or carried backward and relieved against profits in earlier or subsequent years. The basic rationale behind the loss carry-over rules is income averaging.

However, companies might use losses as an aggressive tax planning tool by increasing or accelerating tax relief on their losses. Unrestricted loss carry forward and loss carry backward are in effect a profit-based tax incentive because they only take effect once a company declares profits. It increases those profits further by showering taxpayer's money onto those private sector profits. Unrestricted loss carry forward and backward thus enables profit shifting,

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investment round tripping and corporate (re)structuring for tax avoidance purposes.¹³

Countries may deny or restrict the use of losses for tax purposes to eliminate or reduce tax compliance risks. Countries should consider introducing or revising carry-over limitations, especially those countries that have introduced or are planning to introduce a fixed-ratio rule or a group ratio rule, which are other anti-base erosion and profit shifting measures for limiting interest deductibility. These rules establish a limit on the ability of an entity to deduct net interest expenses that in turn result in an entity either incurring an interest disallowance (i.e., where its net interest expense exceeds the maximum permitted), or having unused interest capacity (i.e., where its net interest expense is below the maximum permitted).¹⁴

Several kinds of limitation on loss relief exist. The OECD has captured some of these based on country practice¹⁵:

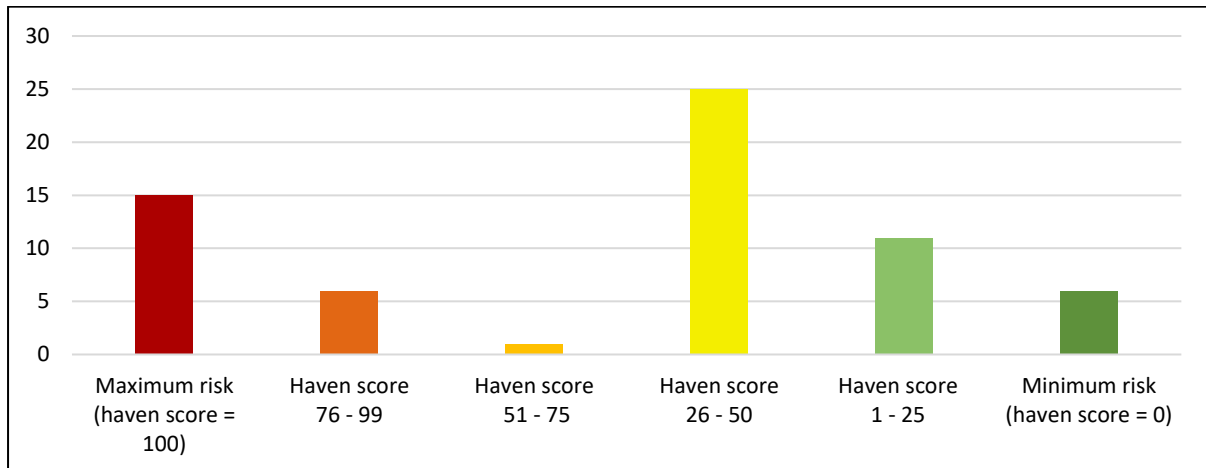
- The number of years for which disallowed interest expense or unused interest capacity may be carried forward, or disallowed interest expense may be carried back, could be limited.
- The value of carry forwards could reduce over time, such as by 10% each year.
- The value of a carry forward or carry back could be capped at a fixed monetary amount.
- The amount of a carry forward or carry back that may be used in a single year could be limited. For example, providing that no more than 50% of current net interest expense may be set against unused interest capacity carried forward from previous years.
- Carry forwards should be reset to zero in certain circumstances, following normal practice applied to loss carry forwards, such as where a company changes ownership and also changes the nature of its economic activity. Countries impose this kind of limitation especially to ensure that the loss relief is granted exclusively to the person that economically incurred the losses.

Nonetheless, a study showed a growing tendency of relaxing the loss offset provisions before the 2008 financial and economic crisis by comparing 41 country practices. According to the study, 31 countries restricted the loss carry forward in 1996 while only 25 countries restricted the loss carry forward in 2007.¹⁶ In light of the magnitude of global corporate losses and growing tax compliance risks associated with loss-making corporations since the 2008 crisis, this indicator evaluates the current state of play.

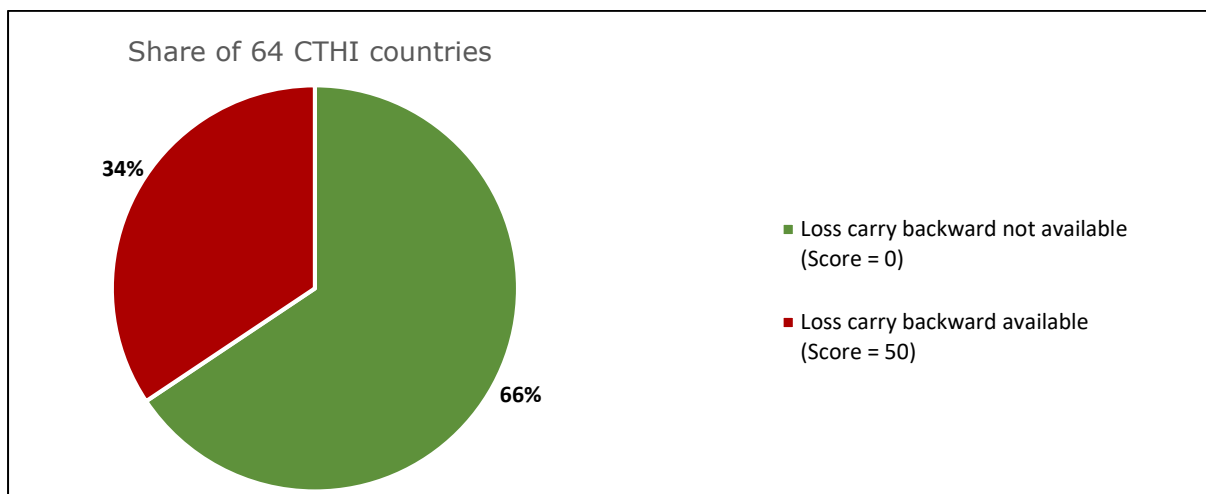
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Results Overview

Graph 3.1. Loss Utilisation Overview

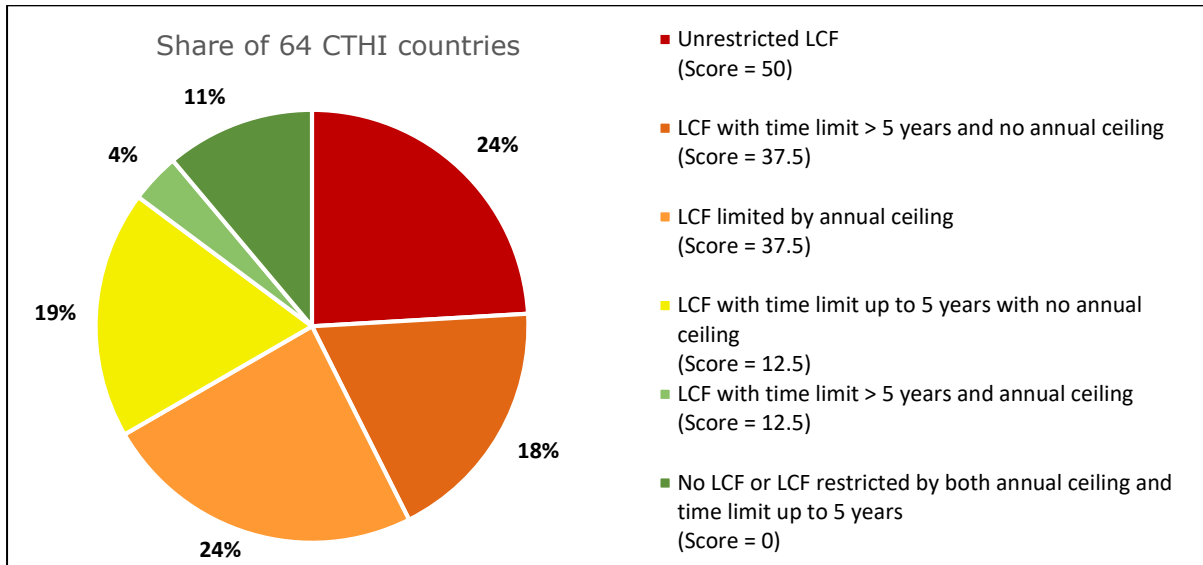


Graph 3.2. Loss Carry Backward



Graph 3.3. Loss Carry Forward

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Results Details

Table 3.2. Loss Utilisation – Haven Indicator Scores

ISO	Country Name	Final Score	Loss Carry Backward	Loss Carry Forward
AD	Andorra	37.5	0.0	37.5
AI	Anguilla	100.0	50.0	50.0
AW	Aruba	50.0	0.0	50.0
AT	Austria	50.0	0.0	50.0
BS	Bahamas	100.0	50.0	50.0
BE	Belgium	37.5	0.0	37.5
BM	Bermuda	100.0	50.0	50.0
BW	Botswana	50.0	0.0	50.0
VG	British Virgin Islands	100.0	50.0	50.0
BG	Bulgaria	12.5	0.0	12.5
KY	Cayman Islands	100.0	50.0	50.0
CN	China	37.5	0.0	37.5
HR	Croatia	12.5	0.0	12.5
CW	Curacao	50.0	0.0	50.0
CY	Cyprus	12.5	0.0	12.5
CZ	Czech Republic	12.5	0.0	12.5
DK	Denmark	37.5	0.0	37.5
EE	Estonia	0.0	0.0	0.0
FI	Finland	37.5	0.0	37.5
FR	France	87.5	50.0	37.5
GM	Gambia	37.5	0.0	37.5
DE	Germany	87.5	50.0	37.5
GH	Ghana	62.5	50.0	12.5
GI	Gibraltar	37.5	0.0	37.5
GR	Greece	12.5	0.0	12.5

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ISO	Country Name	Final Score	Loss Carry Backward	Loss Carry Forward
GG	Guernsey	100.0	50.0	50.0
HK	Hong Kong	50.0	0.0	50.0
HU	Hungary	12.5	0.0	12.5
IE	Ireland	100.0	50.0	50.0
IM	Isle of Man	100.0	50.0	50.0
IT	Italy	37.5	0.0	37.5
JE	Jersey	100.0	50.0	50.0
KE	Kenya	100.0	50.0	50.0
LV	Latvia	0.0	0.0	0.0
LB	Lebanon	12.5	0.0	12.5
LR	Liberia	37.5	0.0	37.5
LI	Liechtenstein	37.5	0.0	37.5
LT	Lithuania	37.5	0.0	37.5
LU	Luxembourg	37.5	0.0	37.5
MO	Macao	12.5	0.0	12.5
MT	Malta	50.0	0.0	50.0
MU	Mauritius	50.0	0.0	50.0
MC	Monaco	87.5	50.0	37.5
MS	Montserrat	12.5	0.0	12.5
NL	Netherlands	87.5	50.0	37.5
PA	Panama	0.0	0.0	0.0
PL	Poland	0.0	0.0	0.0
PT	Portugal (Madeira)	0.0	0.0	0.0
RO	Romania	37.5	0.0	37.5
SM	San Marino	0.0	0.0	0.0
SC	Seychelles	12.5	0.0	12.5
SG	Singapore	100.0	50.0	50.0
SK	Slovakia	12.5	0.0	12.5
SI	Slovenia	37.5	0.0	37.5
ZA	South Africa	50.0	0.0	50.0
ES	Spain	37.5	0.0	37.5
SE	Sweden	100.0	50.0	50.0
CH	Switzerland	87.5	50.0	37.5
TW	Taiwan	37.5	0.0	37.5
TZ	Tanzania	100.0	50.0	50.0
TC	Turks and Caicos Islands	100.0	50.0	50.0
AE	United Arab Emirates (Dubai)	100.0	50.0	50.0
GB	United Kingdom	87.5	50.0	37.5
US	USA	37.5	0.0	37.5

Final Score

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Maximum Risk (Haven Score 100)	Haven Score 76 - 99	Haven Score 51 - 75	Haven Score 26 - 50	Haven Score 1 - 25	Minimum Risk (Haven Score 0)
Component score					
Maximum Risk (Haven Score 50)	Haven score 26-49		Haven Score 1-25		Minimum Risk (Haven Score 0)

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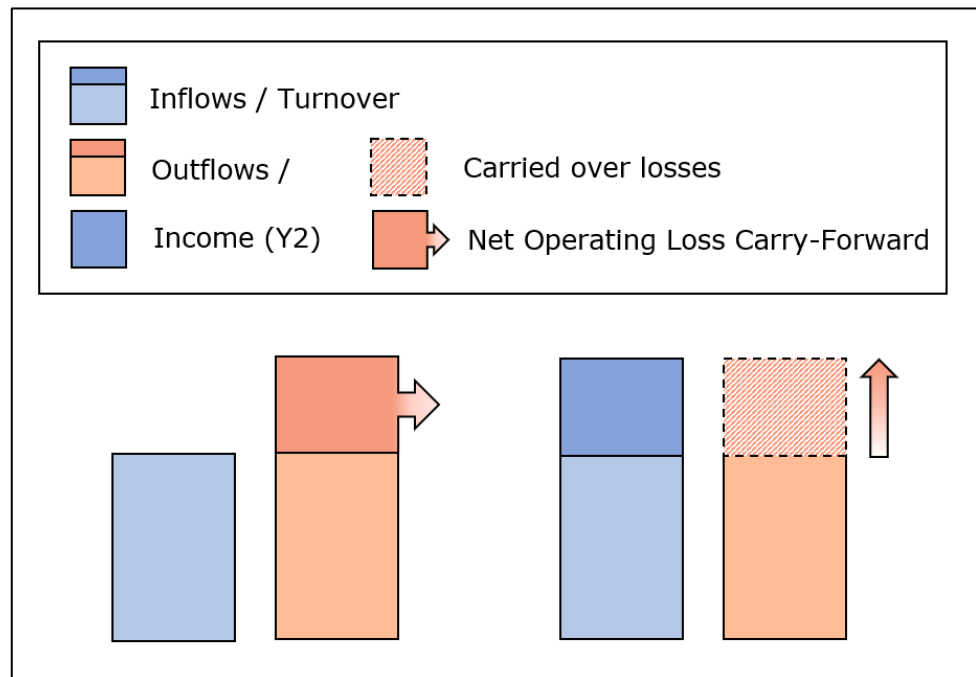
Table 3.3. Assessment Logic

Info_ID	Text_Info_ID	Answers (Codes applicable for all questions: -2: Unknown; -3: Not Applicable)	Valuation Haven Score
509	Loss Carry Backward: Does the jurisdiction allow loss carry backward?	0: No; 1: Yes	0: 0 1: 50
510	Loss Carry Forward: Does the jurisdiction restrict loss carry forward independent of change of ownership?	0: No, unrestricted loss carry forward is available; 1: Yes, loss carry forward is available with a time limit of more than 5 years but there is no annual ceiling; 2: Yes, loss carry forward is limited only by annual ceiling (minimum tax); 3: Yes, loss carry forward is available with a time limit of up to 5 years but there is no annual ceiling; 4: Yes, loss carry forward is limited by an annual ceiling and a time limit of more than 5 years; 5: Yes, either there is no loss carry forward available or it is restricted by an annual ceiling and a time limit of 5 years or less.	0: 50 1: 37.5 2: 37.5 3: 12.5 4: 12.5 5: 0

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ANNEX 1. Loss Utilisation Explanatory Diagrams

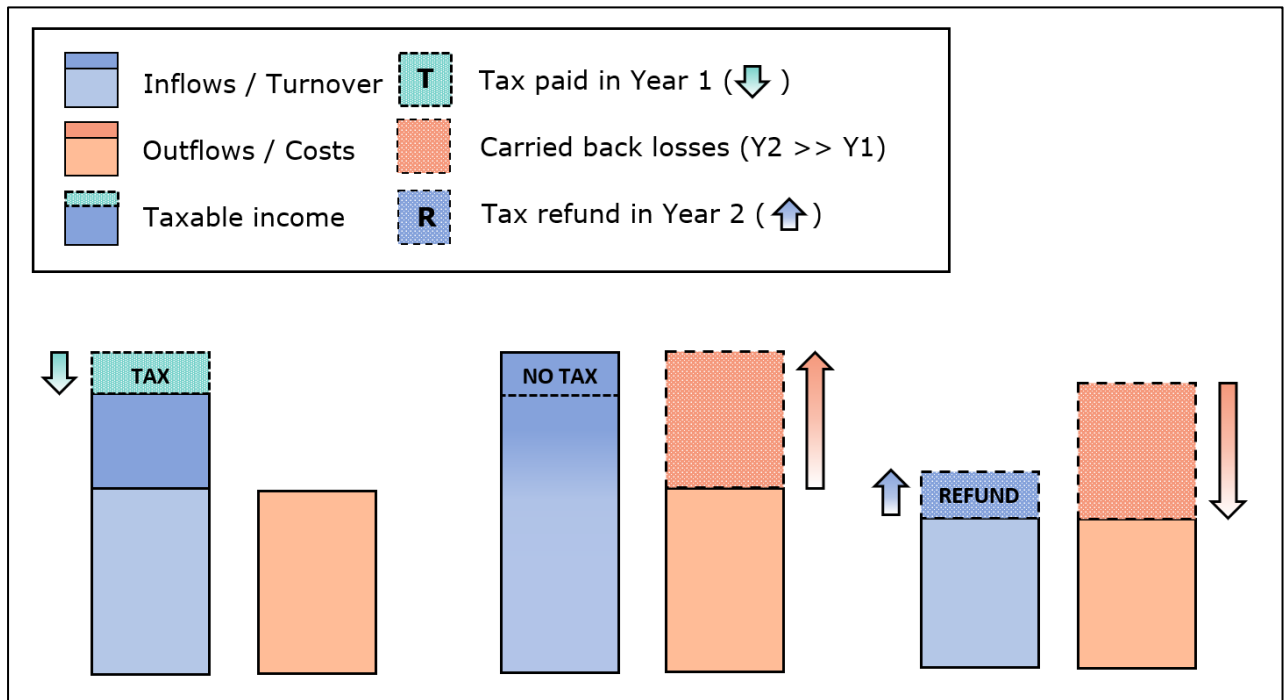
Figure 3.1. Loss Carry-Forward: Economics and Tax Consequences



	Year 1 : Net Operating Losses	Year 2 : Loss Carry-Forward
Economics	Outflows are larger than inflows, the company makes losses (i.e. net operating losses). Such losses can be met using cash reserves. Otherwise, losses might be expensed (paid to creditor) in following years. Sustained losses may trigger dissolution of the company.	Losses incurred in a previous tax year offset income generated in current tax year. The tax system attenuates cyclical losses of corporations, ensuring reduced taxation for companies having suffered losses in previous years.
Tax consequences	The company does not have income (profits) and thus no corporate income tax is due. The company may be able to carry forward the losses to offset future income.	If losses incurred in a previous year (Y1) are allowed to be deducted against the current year's (Y2) income, the company may be able to reduce or eliminate its tax liability in current year (Y2).

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Figure 3.2. Loss Carry-Backward: Economics and Tax Consequences



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- ¹⁴ OECD, *Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 - 2015 Final Report* (Paris, 2015), 69, para. 164 <<https://www.oecd-ilibrary.org/docserver/9789264241176-en.pdf?expires=1557996390&id=id&accname=guest&checksum=4C61C67D7652BE5C0ABF0421567F6774>> [accessed 16 May 2019].
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¹⁶ Daniel Dreßler and Michael Overesch, 'Investment Impact of Tax Loss Treatment— Empirical Insights from a Panel of Multinationals', *International Tax and Public Finance*, 20/3 (2013), 513–43.