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Tax Motivated Transfer Pricing

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Summary

Title: Tax Motivated Transfer Pricing

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Purpose: To study tax motivated transfer pricing from the perspective of stakeholder theory and legitimacy theory in hope of finding out the motives for corporations to engage in transfer pricing manipulation and whether tax avoidance behavior via manipulating transfer pricing will cause a legitimacy problem.

Method: This paper predominantly employs the qualitative method with a complement of quantitative method. A small survey and interviews with seven major Swedish media companies are conducted in order to find out the public attitude towards tax planning.

Theoretical perspective: This study is based on transfer pricing theory, stakeholder theory and legitimacy theory. A brief introduction of the concept of tax planning, tax haven and "fairness" social norm are also presented.

Empirical data: Multinational corporations' tax avoidance mechanism is presented via four cases. The general public's attitudes towards corporations' tax avoidance behavior in any form are also presented through various survey results. Our own survey and interviews with seven major Swedish media companies are also presented in order to reveal the fact – the lack of public concern on corporations' tax planning behavior in the society.

Conclusion: Multinational corporations have both internal and external motives to manipulate transfer pricing in order to shift their profits between high- and low-tax jurisdictions. Theoretically, multinational corporations' tax avoidance behavior will cause legitimacy problem. However, in reality such a behavior does not really endanger their legitimacy and thus legitimacy theory is not applicable for the issue of tax planning.

Abstract

Multinational Corporations (MNCs) or Multinational Enterprises (MNEs) are of great importance in the global economy. A great amount of international trade is either between multinational corporations or within a multinational corporation, which is called intra-firm trade. Therefore, intra-firm trade is also of importance in the global economy. The price used in intra-firm trade is called transfer price. The process of deciding the transfer price refers to transfer pricing, which is an important strategy for multinational corporations to shift their global pre-tax profit from high tax jurisdictions to low tax jurisdictions for the purpose of tax avoidance.

As major participants of the global economy, multinational corporations and governments view transfer pricing differently. Corporations regard transfer pricing strategy as an important tool for tax planning, which is consistent with their professional ethics, because the ultimate goal of the corporation is profit maximization. Therefore, corporations have strong motivations to manipulate transfer pricing for the tax purpose. However, tax avoidance behavior is a conflictual behavior. From the government's perspective, it is harmful because such a behavior causes loss of tax revenue, which could be used to fulfill public spending obligations such as financing public infrastructure, national defense, education, health care, social security and other public services.

The purpose of this paper is to study tax motivated transfer pricing from the perspective of stakeholder theory and legitimacy theory in hope of finding out the motives for corporations to engage in transfer pricing manipulation, and whether tax avoidance behavior via manipulating transfer pricing will cause a legitimacy problem. In order to do so, we examined both cases related to tax avoidance via transfer pricing manipulation and regulations involving transfer pricing, OECD guidelines in particular. We also conducted a small survey and telephone interviews with seven Swedish media companies in order to find out the public attitude towards tax planning.

We try to analyze corporations' conflictual behavior from both a theoretical and practical perspective, and then compare them with each other. We also try to provide an explanation for the result of the comparison and extend our analysis to the question: Is legitimacy theory applicable to the issue of tax planning? Last but not least, some suggestions about reducing tax motivated transfer pricing manipulation are presented.

Table of Contents

Summary 2
Abstract 3
Table of Contents 4
Abbreviation 6
1. Introduction 7
1.1. Background 7
1.2. Problem discussion & Purposes 9
1.2.1. Problem discussion 9
1.2.2. Purposes 10
1.3. Structure 11
2. Method 12
2.1. Choice of Topic 12
2.2. Data 12
2.2.1. Primary Data and Secondary Data 12
2.2.2. Data Collection and Processing 13
2.3. Qualitative and Quantitative method 14
2.4. Choice of Theory 15
2.5. Research Procedure 15
2.6. Source Criticism 16
2.7. Limitations 17
3. Literature Overview 18
3.1. Transfer Pricing 18
3.1.1. Transfer Price and Transfer Pricing 18
3.1.2. Objectives of transfer pricing 18
3.1.3. Transfer pricing in global context 19
3.1.4. Transfer Pricing methods As Per OECD Guideline 20
3.2. Legitimacy Theory 24
3.2.1. Legitimacy and legitimation 24
3.2.2. Public Expectations, Social Contract and Legitimacy Gap 24
3.2.3. Gaining, Maintaining or Repairing Legitimacy 25
3.2.4. Reputation Risk Management 26
3.3. Stakeholder Theory 26
3.3.1. Similarity and Difference between Stakeholder Theory and Legitimacy Theory 26
3.3.2. Stakeholder Concept 27
3.3.3. Normative and Positive Branch of Stakeholder Theory 27

3.4. Fairness and Social Norms 29
3.5. Tax Planning and Tax Haven 31
3.5.1. Three forms of Tax Planning 31
3.5.2. Tax Haven 31
4. Global Regulations related to Transfer Pricing 35
4.1. OECD Guidelines – OECD's Work on Transfer Pricing 35
4.2. Action Plan on Base Erosion and Profit Shifting 37
5. Empirical Data 40
5.1. An Overview of Multinational Corporations' Tax Avoidance Behavior 40
5.2. Cases of Tax Avoidance Through Transfer Pricing Manipulation 42
5.2.1. Forest Laboratories Inc. Case – The Double Irish 42
5.2.2. Apple Case 44
5.2.3. Caterpillar Case 46
5.2.4. SABMiller Case 47
5.3. Public Attitudes to Tax Avoidance in Any Form 48
5.3.1. World Value Survey 2005-2006 48
5.3.2. ComRes Tax Avoidance Survey and IBE Business Ethics Survey 50
5.3.3. Survey and Interview About Multinational Corporations' Tax Planning 50
6. Analysis 53
6.1. Internal and external motivation for transfer pricing manipulation 53
6.2. Tax Induced Transfer Pricing Manipulation and Legitimacy Problem 55
6.2.1. The Negative Effects of Tax Avoidance 55
6.2.2. Tax Avoidance Behavior and Social Contract 56
6.2.3. Tax Avoidance and Legitimacy Problem 58
6.2.4. Is Legitimacy Theory Applicable for the Issue of Tax Planning? 59
7. Conclusion and Discussion 62
7.1. Conclusion 62
7.2. Discussion 62
Bibliography 66

Abbreviation

APA	The advance pricing agreement process
BEPS	The Action Plan on Base Erosion and profit Shifting
CUP Method	Comparable Uncontrolled Price Method
DISA	Du Pont International S.A.
EBITA	Earnings before interest, tax, amortization and exceptional items
FATF	Financial Action Task Force
FTSE 100	The 100 biggest groups listed on the London Stock Exchange
GAO	Government Accountability Office of the United States
HMRC	Her Majesty's Revenue and Customs
IBE	Institute of Business of Ethics
IMF	The International Monetary Fund
MNC / MNE	Multinational Corporation / Multinational Enterprise
OECD	Organization for Economic Co-operation and Development
OFC	Offshore financial center
TPM	Transfer pricing manipulation
UNCTAD	United Nations Conference on Trade and Development
WVS	World Value Survey

1. Introduction

Introduction presents a background and problem discussion about transfer pricing, which leads to the purpose of this paper. The structure of this paper is also presented in the later part of introduction.

1.1. Background

Multinational Corporations (MNCs) are of great importance in the global economy. In the past half century, the number and economic influence of multinational corporations have grown steadily (Ghemawat & Pisani, 2013). According to World Investment Report 2010 (UNCTAD, 2010, p.16), there are 889,416 multinational corporations worldwide in 2009, among which 82,053 mother corporations each have almost 10 affiliates. Since 2009, the world has seen the great economic recession as a result of the global financial crisis. However, large multinational corporations are still playing the predominant role in international trade because trade between and within MNCs represents a large share of the global trade. World Investment Report 2013 (UNCTAD, 2013: XV) states that "FDI stocks rose by 9 per cent in 2012… Foreign affiliate of TNCs (transnational corporations) generated sales worth $26 trillion … increasing 7.4 per cent from 2011. They contributed value added worth $ 6.6 trillion, up 5.5 per cent, which compares well with global GDP growth of 2.3 per cent."

Furthermore, a large amount of international trade involves foreign affiliates of multinational corporations. Ernst & Young's 2013 global transfer pricing survey mentions that "according to the OECD (Organization of Economic Cooperation and Development), around 60% of world trade actually takes place within multinational enterprises" (Ernst & Young, 2013, p.3). Trade within a multinational corporation refers to intra-firm trade and the price related to intra-firm trade is transfer price. Anthony and Govindarajan (2007, p.230) mentioned in their book *Management Control Systems* that "79 percent of Fortune 1,000 companies transferred products between profit centers". As per World Investment Report 2010 from UNCTAD (United Nations Conference on Trade and Development), exports of goods and services by multinational corporations and their affiliates account for one third of global exports in 2009 (UNCTAD, 2010, p.16). 48 percent of goods imports and 30 percent of goods exports in United States were intra-firm trade in 2009 (Lanz, R. & S. Miroudot, 2011, p.5). "58% of US goods imports from OECD countries were intra-firm." (Lanz, R. & S. Miroudot, 2011, p.6) In Sweden, one of the countries with the highest share of intra-firm trade, 51 percent of total manufacturing exports were intra-firm trade (Lanz, R. & S. Miroudot, 2011, p.5).

Multinational corporations can set price for intra-firm trade, i.e. transfer price. Transfer pricing is the process of establishing price for a transaction of goods or services between two parties within one organization (Benari, 2009, p.2). How multinational corporations set their transfer prices has been a

hot topic for decades. Transfer pricing has an inherent problem, which is the difficulty for setting a fair price in absence of two unrelated parties in a transaction. Price of goods and services in transactions between unrelated parties is usually affected by certain market factors, for example, supply and demand, tariffs or political conditions, while intra-firm trade often ignores these market factors (Benari, 2009, p.2).

Looking from a global view, transfer pricing between affiliates across borders brings about further complications related to tax planning (Benari, 2009, p.2). Different regulations and taxation systems in different countries make it possible for multinational corporations to exploit the differences in tax rates and to maximize their profits via manipulating transfer pricing. A great many cases of tax planning related to transfer pricing manipulation are reported. A classic case of profit shifting via transfer pricing strategy is Du Pont de Nemours. Investigation about EF Education First led by Swedish TV program “Uppdrag granskning” in 2013 is another example.

Du Pont de Nemours Case

Du Pont de Nemours was a chemical company and it created a marketing and sales subsidiary – Du Pont International S.A. (“DISA”) – in Switzerland in 1959. The subsidiary distributed chemical products outside America. Du Pont’s internal memoranda kept records of tax advantages, especially in planning prices of goods to be sold to DISA. According to court documents, the tax strategy was that “Du Pont sold its goods to DISA at prices below fair market value. DISA, upon resale of the goods, would recognize the greater part of the total profit (i.e. manufacturing and selling profits). Since this foreign subsidiary could be located in a country where its profits would be taxed at a much lower level than the parent Du Pont would be taxed here, the enterprise as a whole would minimize its taxes.” (Leagle, 1979)

EF Education First

EF Education First, founded in the Swedish university town – Lund 1965, is nowadays the biggest privately owned international education company, which offers culture exchange, educational travel and language study programs worldwide. The organization has more than 400 schools in over 50 countries. As per Uppdrag granskning, EF Education First generates millions of revenue but presents only minimum of profits and thus hardly pays any taxes. (Aftonbladet, 2013)

Uppdrag granskning asserts that the corporation’s foreign affiliates and daughter companies are transferring profits to different central accounts (central konton) and then receive just enough capital for covering the cost of business operations. In addition, the company’s headquarters, which is located in Lucerne, Switzerland, distributes the overhead costs to foreign affiliates and daughter companies with the aim of minimizing the profits which would be taxed in the host countries.

Anonymous sources within EF Education First claim that the effective tax planning via transfer pricing is credited with the profit maximization of whole organization (Ljunggren & Sandelin, 2013).

1.2. Problem discussion & Purposes

1.2.1. Problem discussion

Multinational corporations and governments are major participants in the global economy and they view transfer pricing differently.

Multinational corporations

Transfer pricing per se is just about setting price for the transactions within an organization. It does not say anything about whether the price is over-priced, underpriced or set according to arm's length principle. Multinational corporations have an incentive to misprice transfer price for the purpose of minimizing tax in view of their primary goal of profit maximization. Therefore, transfer pricing, from the perspective of organization's' top management, is a significant strategic decision due to its importance in creating shareholder wealth.

Governments

For a long time, the world has known and worried about the dark side of transfer pricing, especially when it is related to developing countries. One of the most discussed problems is related to taxation. Many million dollar tax disputes, such as Xilinx and Veritas Software tax fraud case share one common question – Is abusive manipulation of transfer pricing employed for tax evasion or tax fraud purposes (Leone, 2011)? After the Du Pont case in 1979, companies were required to record their transfer pricing strategies. A guideline about transfer pricing by multinational corporations and income taxation was made by OECD (Organization for Economic Co-operation and Development) and is reviewed on a regular basis. Many countries built up various bilateral and/or multilateral agreements involving transfer pricing based on the OECD guidelines (Eden & Murphy, 2011, p.3). The primary norm involving transfer pricing is arm's length principle, which refers to that the transfer price should be based on the price that two unrelated parties negotiate for the identical or similar product traded on the active market (Eden, Dacin & Wan, 2001).

The focus of regulations and taxation laws are on aggressive or abusive transfer pricing manipulation which most probably leads to tax evasion or tax fraud. Tax planning involving tax avoidance is considered to be legal, or more exactly, not illegal. Multinational corporations' tax avoidance behavior is morally acceptable to government and tax authorities, at least based on the interpretation of current regulations and taxation laws.

Insomuch as multinational corporations and intra-firm trades are of importance in the world economy; major players (multinational corporations and government) in the global economy have different views on transfer pricing, it is necessary to further the study of transfer pricing manipulation.

Stakeholders of multinational corporations are paying more and more attention to transfer pricing risk management. Ernst & Young's 2013 Global Transfer Pricing Survey stated that "the 2011-2012 Tax Risk and Controversy Survey found 57% of tax administrators identified transfer pricing as their top risk focus" and almost 40 percent of companies "identified transfer pricing as their leading risk" (Ernst & Young, 2013, p.4). There has been a sharp increase in tax controversy worldwide, especially regarding transfer pricing. Transfer pricing and tax "fairness" nowadays have become hot topics in the news around world. British Prime Minister David Cameron thinks that multinationals' aggressive tax avoidance is like illegal evasion. Cameron said on February 18, 2013:

"*There are some forms of tax avoidance that have become so aggressive that I think there are moral questions we have to answer about whether we want to encourage or allow that sort of behavior."*

(Bloomberg, February 18, 2013)

In order to achieve shareholder wealth maximization, multinational corporations are in need of reducing cost as much as possible, including minimizing the tax costs in all manner of ways such as transfer pricing strategies. On the other hand, tax avoidance behavior in any form and in any measure is becoming more and more intolerable to government, tax authority and the general public. Multinational corporations need to operate within the bounds and norms of society, i.e. to legitimate their business activities in order to win the "license to operate". Therefore, multinational corporations' tax avoidance behavior via transfer pricing manipulation is a conflictual behavior which could endanger corporations' legitimacy.

1.2.2. Purposes

The aim of this paper is to study multinational corporations' tax avoidance behavior via transfer pricing manipulation, especially profit shifting from a high-tax jurisdiction to a low-tax jurisdiction. From the perspective of stakeholder theory and legitimacy theory, we will try to understand multinational corporations' conflictual behavior – tax avoidance via transfer pricing manipulation by providing the answers to the following questions.

- What are the motives for multinational corporations to engage in transfer pricing manipulation?

- Will tax avoidance behavior via manipulating transfer pricing eventually lead to legitimacy problem for multinational corporations?

1.3. Structure

After this part, we will introduce the method of our study. After that, followed by empirical data, related theories such as transfer pricing, stakeholder theory and legitimacy theory will be introduced. Empirical materials are focusing on two aspects. One is multinational corporations' profit shifting mechanism by taking advantage of transfer pricing and tax haven. This will be presented in the form of case description. Another focus of empirical data is on the public's attitudes to tax avoidance.

In our analysis part, we will discuss transfer pricing manipulation from four aspects. First, we will analyze the motives for multinational corporations to engage in transfer pricing manipulation. Secondly, from the perspective of stakeholder theory and legitimacy theory, we try to understand and explain the legitimacy problem involving tax motivated transfer pricing manipulation. Thirdly, compared with the theoretical result about legitimacy problem, we present a different result in reality: tax motivated transfer pricing manipulation does not cause a legitimacy problem. Fourthly, in order to find out whether legitimacy theory is applicable for the issue of tax planning, we try to analyze the difference between theory and reality and provide an answer for it.

The conclusion and discussion part summarizes the analysis and offers answers to the questions mentioned in the purpose section. A discussion about reducing multinational corporations' tax motivated transfer pricing manipulation is also presented.

2. Method

This part discusses and motivates which research methods are used in our study. The methods for data collecting and data analyzing are presented; the credibility/reliability of empirical data is discussed; and in the end, limitations for this paper are described.

2.1. Choice of Topic

As an important tool for internal management control, transfer pricing is considered to be a strategic decision. Numerous research on transfer prices have been done and multitudinous studies have focused on business ethics and business sustainability. However, there are not many studies focusing on the conflict between multinational corporations' profit maximization goal and the legitimacy of tax avoidance behavior involving transfer pricing strategies. Therefore, this conflict deserves a further study. In addition, we think it is interesting and important to understand the possible legitimacy problem caused by the tax motivated transfer pricing manipulation.

2.2. Data

2.2.1. Primary Data and Secondary Data

Primary data is the first-hand data which researchers collect in person through, for example, interviews or surveys. Secondary data is what is already in databases, archives and other forms of materials such as academic papers, journals, literature books, newspapers, etc.

Our study is based on both primary data and secondary data. However, most of the work is based on the research of secondary data, because the topic of the study – tax avoidance via transfer pricing manipulation – is a hot but very sensitive topic. Thus it is, on one hand, hard for us to get access to the fresh first hand data through the normal primary data collecting methods; on the other hand, a large amount of related second hand data is available for our study, since it is now such a hot topic among academic researchers and politicians.

Two decisive factors can explain our difficulties. First, transfer pricing is considered to be a significant corporate strategy and it is often regarded by most corporations as an important secrecy. Secondly, transfer pricing strategy is a prominent source of tax controversy. Multinational corporations use tax haven to shift profits for the purpose of avoiding corporate income tax. Such a behavior has an elaborate disguise and the lack of transparency for the transactions through "Tax Haven" often makes it difficult even for tax authorities to identify or find solid proofs for corporations' actual process of operation. Hence, we think, it is better to use the secondary data from trustworthy sources as the ground for our study, since it can avoid the problem that analysis and conclusion are jeopardized because of unsound or even false data.

In order to analyze whether tax avoidance behavior will create a threat to corporations' legitimacy, we complement our study with primary data by conducting a small survey involving 50 randomly selected people in different lines of business with various academic backgrounds. We also conducted telephone interviews with seven major Swedish media companies. The detailed information about the survey and interviews will be presented in 2.2.2 Data Collection and Processing.

Out of the reasons mentioned above, we decided to ground our study on both primary and secondary data and we read widely about theories, research papers and newspaper articles, as well as regulations and laws related to transfer pricing. Information is collected with the help of course literature, database of Lund university library and google search engine on the internet.

2.2.2. Data Collection and Processing

Global Regulations and Cases of Transfer Pricing Manipulation

As our aim is to understand the tax avoidance by shifting profits between high- and low-tax jurisdictions via transfer pricing strategies, we are focusing on searching for data on how multinational corporations actually operate in practice. That is to say, how do multinational corporations manipulate transfer pricing to shift their pre-tax global profits through tax havens for the purpose of tax avoidance? We also study the general global regulations involving transfer pricing, especially the arm's length principle.

In order to elaborate multinational corporations' tax avoidance behavior via transfer pricing manipulation, we choose altogether four cases to show how corporations actually operate in practice. Even if all cases share the same characteristic – profit shifting through tax havens by manipulating transfer pricing, each case has its individual focus. That is the negative effects of tax avoidance exerted on different aspects. We think that, combined with stakeholder theory and legitimacy theory, those cases could provide a revealing insight for understanding multinational corporations' conflictual behavior (tax avoidance behavior) and the possible legitimacy problem arising from it. We also chose to present those corporations' current financial performances for the purpose of gauging the effect of the possible legitimacy problem induced by tax planning.

Survey and Interviews about General Public's View towards Tax Planning

In order to study the possible legitimacy problem, we need to know the public attitudes towards multinational corporations' tax planning behavior. Therefore, we conducted a small survey involving 25 randomly selected people from various lines of business in a common Swedish community and 25 students with various academic backgrounds at Lund University. 25 people are regular Swedish citizens and except two retired persons, all others have different types of jobs, such as office workers, sales representatives, electrical engineers, craftsmen and entrepreneurs. Among the 25

students from Lund University, there are four students from Business Administration and two students from Economics. Others are from different majors, such as Engineering, Math, Psychology, Biomedicine, and Chemistry.

We chose to conduct the survey in a form of conversation with people randomly passing by in the community and in the campus. In order to know where tax planning lies in the general public's ranking and why it lies in that position, we first asked them to rank four issues, environmental problem, low salary, child labor and tax planning, in today's society. Then, we asked them to motivate the reason for why they rank it in this way.

The result of survey motivated us to further our study by interviewing the major Swedish media outlets. We conducted telephone interviews with five newspapers, Dagens nyheter, Sydsvenskan, Aftonbladet, Svenska Dagbladet and Metro. We also interviewed two TV stations, SVT Nyheter and TV4 Nyheter, because many people access news via television. The interview questions are listed as following:

1. How do you rank the news reporting interest for the following alternatives?
   a) Environment problems (such as pollution)
   b) Low wages (than allowed)
   c) Child labor
   d) Tax planning (with a focus on tax avoidance)
2. Why do you rank them in this way?
3. Please motivate the reasons for why tax planning has not been widely reported in Swedish media?

Data collection is a repeated ongoing process during our writing. We collect the data and then assess, process, group and analyze the data. Based on the data available, we adjust the angle of research and if necessary, we continue the data collection and processing work during the analysis stage.

2.3. Qualitative and Quantitative method

Quantitative method refers to that the reality is observed with the help of certain mathematical measures and statistics study. Qualitative method does not use mathematical measures and statistics study as a tool for research, i.e. qualitative method uses word description instead of using numbers (Backman, 2008, p.33).

We choose to predominantly employ the qualitative method with a complement of quantitative method. We choose to do so, because there are many research materials suitable for our study, such as cases of tax avoidance via transfer pricing manipulation, laws and regulations related to transfer pricing as well. Even if the mathematical or statistical data in a broad range is hard to get access to, a

small survey and seven telephone interviews with the major Swedish media companies were conducted in order to find out the public attitudes towards tax planning, which we think, is necessary and beneficial to our study.

2.4. Choice of Theory

Choice of Theory has to fulfill the requirement of research paper's purpose. One of the purposes of our paper is to understand the possible legitimacy problem which is created by multinational corporations' tax avoidance behavior involving transfer pricing manipulation. We think it is necessary to give a brief introduction about transfer price and transfer pricing theory. An important part of transfer pricing is the OECD guidelines, the arm's length principle in particular. Laws and regulations related to transfer pricing in a lot of countries are based on the guidelines. It would be impossible for us to go through every country's legislation. We therefore chose to use the OECD guidelines, because it gives us a general understanding of laws concerning transfer pricing in most countries.

One question we try to answer in this paper is: "what are the motives for multinational corporations to engage in transfer pricing manipulation?" Transfer pricing is an important tool for tax planning and tax havens provide the arbitrage opportunities for corporations' tax planning behavior. Thus, we think it is necessary to introduce the concept of tax planning and tax haven.

In order to analyze the legitimacy problem for multinational corporations' tax motivated transfer pricing behavior, we choose to do our analysis based on stakeholder theory and legitimacy theory with a complimentary introduction about the social norm "fairness" in hope of proving there should be a legitimacy problem for corporations' tax avoidance behavior.

Out of above reasoning, we think our theory framework is appropriate and suitable to conduct the study for understanding multinational corporations' tax motivated transfer pricing manipulation.

2.5. Research Procedure

Our research procedure includes 7 phases: 1) choosing topic; 2) formulating problem; 3) literature study; 4) collecting data; 5) processing data; 6) analysis based on theory and empirical data; and 7) conclusion and suggestions.

1) *Choosing Topic*: In the starting phase, we discussed about various choices of topic which we are interested in for our study. We decided to choose tax motivated transfer pricing as our topic, because on one hand, it is interesting to us; on the other hand, there are enough resources available for conducting our study.

2) *Formulating Problem*: Based on a broad reading of various literatures and academic papers, we formulated the problems on which we would like to do further study. This stage of work also makes a good preparation for the next stage of work. With the development and deepening of our study, the purpose of the study has undergone several minor adjustments in order to provide a better understanding of the research topic.

3) *Literature Study*: During the stage of literature study, we reviewed literatures and academic studies carefully and selected theories that, we think, are necessary and most relevant to combine with the empirical data for the analysis work.

4) *Collecting Data*: Data (majorly empirical data) collection was separated into two stages. First, we collected all the empirical data related to multinational corporations' actual mechanism for manipulating transfer pricing for tax purpose and the general public attitudes towards tax avoidance through various sources, such as newspapers, web pages and academic papers. The second stage of empirical data collection work (survey and interviews about tax planning) was triggered by questions raised during the analysis work. Therefore, we decided to conduct a small survey and interviews with the major Swedish media companies in order to solve our confusions and complete our analysis.

5) *Processing Data*: During the stage of data processing, we organized all the collected data and discussed how we should combine it with selected literatures for the analysis.

6) *Analysis*: Analysis can be divided into two parts. First, we analyzed multinational corporations' tax motivated transfer pricing manipulation behavior and its possible legitimacy problem based on the selected theory and empirical data, especially four cases of the actual mechanism for shifting profits between high- and low-jurisdictions; Then we compared the situation in reality and furthered the study of the possible legitimacy problem in reality and provided an answer for the difference between the theoretical and practical results.

7) *Conclusion and Suggestion*: Conclusion is the product of the analysis. In this stage, we also furthered our discussion about the research topic in hope of providing useful and practical suggestions.

2.6. Source Criticism

Credibility / Reliability of Empirical Data

The topic of this paper, transfer pricing manipulation for tax planning, is a very sensitive topic. It is understandable that most companies would not like to reveal their actual operational mechanism related to tax motivated transfer pricing strategies. It then creates the difficulty for us to get access to

primary data through any first-hand data collecting methods such as survey or interview with companies. Therefore, we choose to research on previous studies related to transfer pricing manipulation.

While we were reading widely about all kinds of materials from various sources, we found that there are a large amount of literatures about transfer pricing and multinational corporations' profit shifting behavior. But few studies actually present empirical evidence of the profit shifting mechanism by manipulating transfer pricing. On the other hand, cases for explaining how multinational corporations work with their transfer pricing strategies always make the headlines on various newspapers. Besides academic research papers, we thus decided to select some cases reported in newspapers as our empirical data for showing multinational corporations' actual profit shifting mechanism via transfer pricing manipulation.

We understand the importance of credibility/reliability of empirical data, since it has a direct bearing on the correctness of our analysis and results. Therefore, we carefully selected cases reported by the big and reputable newspapers and news reports based on the actual law cases in the hope of ensuring the credibility of our empirical data.

2.7. Limitations

This paper focuses only on tax motivated transfer pricing manipulation with the purpose of shifting profit from a high jurisdiction to a low jurisdiction. We will not discuss other issues related to profit shifting via transfer pricing manipulation out of motivations such as tariffs, export taxes, foreign exchange risks or political risks.

As for the analysis of the related global regulations of transfer pricing, we are primarily focusing on OECD's Transfer Pricing Guidelines, the arm's length principle in particular. The study is mainly taking a global perspective and it is not focusing on any specific country.

Our study is majorly based on secondary data through various books, academic papers and newspaper articles. The main disadvantage of using secondary data is the data collected might not be a perfect fit for supporting the purpose of the study. For example, as for the public attitude towards tax avoidance in OECD countries, data for all OECD countries are not available. We choose to present the result of Tekeli's (2011) study based on World Value Survey 2005-2006, because it is the most complete data available for showing the public attitudes to tax cheating.

3. Literature Overview

This part first presents theory about transfer price and transfer pricing in global context and then transfer pricing method as per OECD guideline, the arm's length principle. Legitimacy theory and stakeholder theory are presented with a complementary description of fairness and the social norm. In the end, a brief description of tax planning and tax haven are presented.

3.1. Transfer Pricing

3.1.1. Transfer Price and Transfer Pricing

The thinking of the business world has long been decentralization and one of essential feature of decentralized organization is responsibility center, which is often evaluated based on various accounting numbers, as well as certain non-accounting measures. One primary challenge for decentralized organization is attaching those accounting numbers to transactions between various responsibility centers, i.e. an appropriate method of accounting for intra-firm trade should be constructed if a significant amount of such trade exists (Heath & Slotta, 2009, p.1). Transfer prices are constructed for internal management control of various responsibility centers, especially for cost and profit centers (Eden & Smith, 2011, p.10). In a broad sense, transfer price refers to "the amount used in accounting for any transfer of goods and services between responsibility centers" (Anthony& Govindarajan, 2007, p.230). A narrow definition of transfer price given by Anthony and Govindarajan (2007) in *Management Control System* is "the value placed on a transfer of goods or services in transactions in which at least one of the two parties involved is a profit center" (Anthony & Govindarajan, 2007, p.230). Transfer pricing is used to describe intra-firm pricing arrangement between related business entities (Bairstow, 2011, p.3).

3.1.2. Objectives of transfer pricing

Transfer price is a mechanism for distributing revenue when more than one business unit is involved in the development, manufacturing, marketing and sales of a product line. There are several predominant objectives for constructing an appropriate transfer price scheme according to some researchers (Heath & Slotta, 2009, p.2; Anthony & Govindarajan, 2007, p.230; Lanz, Ceder & Larsson, 2002, p.7).

- Help coordinate different units responsible for different functions involving developing, producing, marketing and sales of a specified product line; help coordinate their pricing decisions and minimize risk of conflicts.
- Each unit generates profit or cost separately via transfer pricing, which thereby acts as a ground for their economic performance measurement.

- Induce goal congruent decisions – transfer price scheme should be constructed on the basis that decision of individual unit for profit maximization will be consistent with the profit maximization goal of organization as a whole.
- Transfer pricing system should be "simple to understand and easy to administer" (Anthony & Govindarajan, 2007, p.230).

3.1.3. Transfer pricing in global context

Globalization can be interpreted as a new word of "internationalization". According to Scholte (2005) *" Globalization is a process which diminishes the necessity of a common and shared territorial basis for social, economic, and political activities, processes and relations"* (Crane & Matten, 2010, p.19).

Globalization makes it possible for resources to move freely cross borders. Organizations can establish affiliates, subsidiaries, joint ventures, etc without territorial limitations. Globalization creates new complexities for transfer pricing policy making, because multinational corporations can take advantage of low taxes in different geographical locations (Sikka & Willmott, 2010, p. 345). The International Monetary Fund (IMF) proclaims that globalization causes taxation problems related to "potential use and abuse of transfer prices" by multinational corporations (Tanzi, 2000, p.10).

Internalization benefit of transfer prices

With the development of a global value chain, intra-firm trade across borders is growing at a tremendous pace. Multinational corporations can take advantage of the incompletely integrated world market and semi-globalization to create additional values via cross-border intercompany transactions. (Eden, 2003, p.3). An appropriate transfer price scheme can help enhance multinational corporations' competitiveness in the international market, facilitate management of cash flow, motivate subsidiary managers and thereby induce goal congruence (Bairstow, 2011).

Intercompany transactions nowadays involve more contents such as tangible, intangible property and finance transfers. Issues related to transfer pricing are becoming more and more complex. Tax planning is one principal issue related to transfer pricing. Sikka and Willmott (2010, p. 343) mentioned in their research paper that Ernst & Young proclaimed in its *transfer pricing global reference guide 2005* as following:

"Transfer pricing continues to be, and will remain, the most important international tax issue facing MNEs" (Ernst & Young, 2006, p.5).

Different taxation regulations in various countries offer opportunities for multinational corporations to reduce taxes and tariffs. Eden (2003) stated that an appropriate transfer pricing system helps avoid

tax conflicts with home and host governments and minimize foreign exchange risks. Through transfer pricing manipulation, multinational corporations can shift profit artificially from a high-tax jurisdiction to a low-tax jurisdiction and thereby present a better financial performance. Moreover, organization can reduce capital cost and achieve higher after-tax profit via transfer pricing system. Therefore, transfer pricing manipulation is a value adding activity which can create additional benefit from internalizing markets and shareholder wealth (Eden, 2003, p.3).

Problems of transfer pricing manipulation

Resource allocation is another issue related to transfer pricing. Researchers discovered long time ago that transfer pricing manipulation can result in resources misallocation. In a global context, besides loss of income tax and custom duties, transfer pricing manipulations can have other potential negative impacts for the host country, such as "depletion of natural resources, environmental damage, health hazards, increased national debt and poverty, psychological feelings of betrayal and loss of trust in MNEs, and economic colonialism" (Eden & Smith, 2011). Some researchers state that transfer pricing is a tool for capital flight. It is "not just an accounting technique but also a method of resource allocation and avoidance of taxes that affects distribution of income, wealth, risks and quality of life" (Sikka & Willnott, 2010, p.352). Capital shifting and tax avoidance raise questions about the quality of national economic statistics because most governments steer the economy based on the "data of imports, exports, national income, corporate profitability, balance of payments and terms of trade", which is problematized by multinational corporations' transfer pricing policies (Sikka & Willnott, 2010, p. 353).

3.1.4. Transfer Pricing methods As Per OECD Guideline

Arm's Length Principle

Arm's length principle is the accepted international transfer pricing standard by OECD member countries for taxation purposes of MNEs (Multinational Enterprises). In article 9 of the OECD Model Tax Convention the arm's length principle is stated as follows:

"Conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly." (Article 9 of the OECD Model Tax Convention)

When MNEs do intra-firm trade between countries, they should use transfer prices as it would be used between unrelated independent companies. But how should the transfer price be calculated as per the arm's length principle?

1) Comparable Uncontrolled Price Method (CUP Method)

This method compares the price charged for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances. If a difference in the two prices indicates that the pricing is not according to arm's length principle, the controlled price might need to be substituted by the uncontrolled price. This is the most direct way to apply the arm's length principle. (OECD, 2010 p 63)

An uncontrolled transaction is considered to be comparable to the controlled transaction if one of either two conditions are met: " *a) none of the differences (if any) between the transactions being compared or between the enterprises undertaking those transactions could materially affect the price in the open market; or, b) reasonably accurate adjustments can be made to eliminate the material effects of such differences*." (OECD, 2010, p.63)

Problems with using this method are that it's not always easy or possible to find a similar transaction to compare with. Even if there is one, it could materially affect the price. It may also be difficult to determine the adjustments that need to be made in order to eliminate the effect of the price difference. When determining the adjustments, there are lots of things that need to be considered. For example, are the products being sold the same or very similar? Do they have the same quality and quantity? Are they in the same time frame, in the same stage of the production/distribution chain and under similar conditions? This is, however, dependent on the available data. If no accurate data is available then a different method should be chosen. (OECD, 2010, p.63-65)

2) Resale price method

Resale price method changes the perspective to for which price a product in intra-firm trade would be resold to an independent enterprise without taking the gross margin into account. This means that the arm's length price is considered to be the price of the product after subtracting profit, risk coverage, selling and operating expenses as well as costs for the actual purchase such as customs cost. (OECD, 2010, p.65-66)

One way to figure out the resale price margin of the reseller in the controlled transaction is by using the resale price margin that the same reseller would use in an uncontrolled transaction. Another way is to use an independent enterprise in a comparable uncontrolled transaction as a reference point. If the resale price margin is related to a brokerage fee, then it should follow the same principles as the CUP method. The difference is that the resale price margin is used instead of the price. (OECD, 2010, p. 66-67)

An uncontrolled transaction is considered to be comparable to the controlled transaction if one of either two conditions are met: "*a) none of the differences (if any) between the transactions being*

compared or between the enterprises undertaking those transactions could materially affect the resale price margin in the open market; or, b) reasonably accurate adjustments can be made to eliminate the material effects of such differences." (OECD, 2010, p.66)

Generally speaking, minor product differences have a smaller effect on the profit margin as they do on price. This means that using resale price method tends to require fewer adjustments for product differences than using the CUP method. For example, if a distribution company is performing the same task, whether it is selling toaster or blenders, the gross profit margin could be comparable. If we are focusing on the products themselves, toasters and blenders obviously are not substitutes for each other. It is however important to remember that comparing similar products will give a better comparability and when comparing things like valuable or unique intangibles, it may be harder to get a good comparison and a high attention might need to be paid to the product. This also means that if the circumstances are similar in all aspects except the product itself, then resale price method can give a more reliable comparison then using CUP method. (OECD, 2010, p.67-68)

There are two instances where the resale price method would be a bad choice. One is when a resale adds a lot of value to the product, such as when they are further processed or incorporated into something. The other is when intangible property is associated with the product, such as trademarks, and the reseller substantially contributes to the creation or maintenance of this. Another important factor is time between the original purchase and the resale, the more time that passes, the higher the risk that other factors affect the price. (OECD, 2010, p.67-69)

If there is a chain of distribution within the MNE and if an intermediate company is involved, tax administrators are urged to not only look at the resale price of the goods but also to look at the price such a company paid to its own supplier as well to look at the activities and role of the intermediate company to see if it bears an economic risk or adds value to the goods since independent enterprises would otherwise not normally let such a company share in the profits. Another important point is that adjustments need to be made if the accounting practices used by the companies between the controlled and uncontrolled transactions differ. An example of this is how gross profit margin is affected by the way research and development can be reflected in operating expenses or cost of sales. (OECD, 2010, p.67-69)

3) Cost Plus Method

The cost plus method takes the perspective from the costs incurred by the supplier and then applies cost plus markup to the cost that the supplier would need in order to make an appropriate profit considering the functions performed and the market. The marked up costs can be considered as the arm's length price of the original controlled transaction. One way to establish the cost markup of the

supplier in the controlled transaction is by using the cost markup that the same supplier would use in an uncontrolled transaction. Another way is to use the cost markup from an independent enterprise in a comparable uncontrolled transaction as a reference point. The same principles concerning product differences for resale price margin can be applied to the cost plus method. By doing so, cost plus method can be used in a broader sense and fewer adjustments need to be made comparing with using the CUP method. Companies can have differences in how effective they are at manufacturing and such differences need to be taking into account when comparing the cost markup price between different companies. (OECD, 2010, p.70-71)

An uncontrolled transaction is considered to be comparable to the controlled transaction if one of either two conditions are met: *"a) none of the differences (if any) between the transactions being compared or between the enterprises undertaking those transactions materially affect the cost plus markup in the open market; or, b) reasonably accurate adjustments can be made to eliminate the material effects of such differences."* (OECD, 2010, p.71)

Sometimes it can be problematic to apply the cost plus method since the level of costs is not always linked to the market price. Another difficulty is that the comparable markup must be compared to a comparable cost basis. If one supplier is using leased business assets while the other is using owned, then the costs might not be comparable with each other if there are no adjustments. Factors that can have an effect on the markup size need to be analyzed in order to be able to do the proper adjustments. That is why it is so important to consider different types of expenses, such as operating and nonoperating expenses including financing expenditures, associated with functions performed and risks assumed by the parties or transactions being compared. (OECD 2010, p.72-75)

As with the resale method, it is important, when using cost plus method, to look at the accounting practices of the enterprises being compared as well as the accounting consistency. The same types of costs need to be used in each case. Generally speaking, direct costs and indirect costs of production will be used in the cost plus method. However, besides those two costs, the net profit method would count the operating expenses as well. Variations in practice among countries may therefore cause problems when using cost plus method. (OECD 2010, p.72-75)

Historical costs should be attributed to individual units of production. However, some costs such as materials, labor, manufacturing and transport vary over time, it is therefore most probably appropriate to average the costs over a period of time. The cost plus method is limited to the supplier's costs which can cause problems if overhead costs are not properly split among the buyer and the supplier in an MNE. The buyer could carry some of the supplier's costs, thereby diminishing the supplier's cost base. A follow up problem here is how to properly split the overhead costs. Should we use turnover, number of employees or something else? (OECD 2010, p.72-75)

Sometimes a good basis could be only using marginal or variable costs because transactions represent a disposal of marginal production. This is however dependent on factors such as information on the percentage of the production that is claimed to be marginal production; whether the MNE could sell the products at a higher price in a foreign market; and whether they have sales of other or similar products. (OECD 2010, p.72-75)

3.2. Legitimacy Theory

Legitimacy theory states that organizations strive towards being perceived as legitimate by operating within the bounds and norms of the society. Bounds and norms of the society are changing over time, thus organizations have to "be responsive to ethical (or moral) environment in which they operate" (Deegan & Unerman, 2011, p. 323).

3.2.1. Legitimacy and legitimation

What is legitimacy? Deegan and Unerman (2011) agree with Lindblom's idea of distinguishing between legitimacy and legitimation. Legitimacy is "a status or condition"; while legitimation is "the process that leads to an organization being adjudged legitimate" (Deegan & Unerman, 2011, p. 324). In their book *Financial Accounting Theory*, Deegan and Unerman (2011) quote Lindblom (1993, p.2) that legitimacy is "a condition which exists when an entity's value system is congruent with the value system of the larger social system of which the entity is part."

Legitimacy theory treats legitimacy as a resource that is necessary for an organization's survival (Deegan & Unerman, 2011, p.324). Thus organizations will pursue the appropriate legitimation strategies for a continued supply of such a necessary resource in order to gain, maintain or repair legitimacy (Deegan & Unerman, 2011, p.324). The importance does not lie in what the organization actually does but rather in "what society collectively knows or perceives about the organizations conduct" (Deegan & Unerman, 2011, p.324).

3.2.2. Public Expectations, Social Contract and Legitimacy Gap

Social Contract

Social contract, in legitimacy theory, is a theoretical contract between the organization and the society in which it operates. The social contract incorporates the society's norms and expectations, both implicit and explicit, about how an organization should conduct its operations (Deegan & Unerman, 2011, p.325-328).

Traditionally, the optimal corporate performance is considered to be profit maximization. However, as social expectations have evolved over time, the focus of society's expectations has shifted towards some social issues such as environment, health and safety of consumers and employees (Deegan &

Unerman, 2011, p.325). Failure to comply with those "heightened social expectations" (Deegan & Unerman, 2011, p.325) brings a breach of the social contract, which may lead to sanctions being imposed by society on the organization (Deegan & Unerman, 2011, p.325).

Legitimacy theory stresses that an organization should consider "the rights of the public at large, not merely those of its investors" (Deegan & Unerman, 2011, p.325). "Organizations are not considered to have an inherent right towards resources" and they need to earn this right (Deegan & Unerman, 2011, p.325). Therefore, "license to operate" and legitimacy go hand in hand. (Deegan & Unerman, 2011, p.325-326).

Social Contract and Law

Social contract has both explicit and implicit terms. Explicit terms are often related to legal requirements; while the implicit terms are those non-legislated societal expectations (Deegan & Unerman, 2011, p.328). According to Deegan and Unerman (2011), "there is an imperfect correlation between the law and social norms (as reflected by the social contract)". Based on the research work of Dowling and Pfeffer (1975), Deegan and Unerman (2011) summarized the following three reasons for the difference (Deegan & Unerman, 2011, p.328).

- "Even though laws are reflective of societal norms and values, legal systems are slow to adapt to changes in the norms and values in society."
- "Legal systems often strive for consistency whereas societal norms and expectations can be contradictory."
- "While society may not be accepting of certain behaviours, it may not be willing or structured enough to have those behavioural restrictions codified within law."

Legitimacy Gap

The term "legitimacy gap" is used to describe situations where there is "a lack of correspondence between how society believes organization should act and how it is perceived that the organization has acted" (Deegan & Unerman, 2011, p.329). The sources of "legitimacy gap" are mainly 1) societal expectations have changed, while the organization is still operating in the same old way; 2) the news media discloses certain previously unknown information about the organization. (Deegan & Unerman, 2011, p.329-330)

3.2.3. Gaining, Maintaining or Repairing Legitimacy

When it comes to the issue of gaining, maintaining or repairing legitimacy, organizations will choose different legitimation tactics depending on their different needs to do with their current legitimacy (Deegan & Unerman, 2011, p.331). "Gaining legitimacy occurs when an organization moves into a

new area of operations in which it has no past reputation." (Deegan & Unerman, 2011, p.331) Strategies for maintaining legitimacy include both forecasting future changes and protecting past accomplishments (Deegan & Unerman, 2011, p.331). The greater extent an organization's trade is dependent on legitimacy, the stronger the need that the organization will have to maintain its current legitimacy (Deegan & Unerman, 2011, p.332). Strategies for repairing legitimacy are often the reactive response to unforeseen crises (Deegan & Unerman, 2011, p.332). Organizations can employ legitimation strategies through using accounting reports, since annual reports is a way of public disclosure of information (Deegan & Unerman, 2011, p.333-334).

Deegan and Unerman (2011) quotes Lindblom's (1993) four courses of actions to gain, maintain or repair legitimacy:

- An organization can educate and inform its 'relevant publics' about changes of its actions which are consistent with society's values and expectations;
- An organization can try to change the society's perceptions of its actions without actually changing its behavior;
- An organization can try to manipulate the society's perception by deflecting the attention away from the issue of concern to other issues;
- And an organization can attempt to change the society's expectations of its actions (Deegan & Unerman, 2011, p.333).

3.2.4. Reputation Risk Management

In recent years, gaining and maintaining legitimacy is more about building or maintaining an organization's reputation. Reputation risk management is a notion created under such circumstances. It indicates the financial importance of legitimacy to organizations (Deegan & Unerman, 2011, p.336). A corporation's reputation is considered to be "a resource of considerable (if normally unquantified) value in generating future profits" (Deegan & Unerman, 2011, p.333). Any damage to this reputation will have negative impacts on the corporation's future profitability (Deegan & Unerman, 2011, p.333). Therefore, threats to corporate legitimacy can cause damage to the value of a corporation's reputation, which must be minimized through active management (Deegan & Unerman, 2011, p.334).

3.3. Stakeholder Theory

3.3.1. Similarity and Difference between Stakeholder Theory and Legitimacy Theory

Deegan & Unerman (2011) states in their book *Financial Accounting Theory* that legitimacy theory and stakeholder theory should not be treated as two separate theories and they complement each other (Deegan & Unerman, 2011, p.348). As Deegan (2002, p. 295) indicates, stakeholder theory and

legitimacy theory have many similarities – "both theories conceptualize the organization as part of a broader social system wherein the organization impacts upon, and is impacted by, other groups within society." (Deegan & Unerman, 2011, p. 348)

There are also differences between stakeholder theory and legitimacy theory. Deegan & Unerman (2011) point out that "legitimacy theory considers interactions with 'society' as a whole" and it "discusses the expectations of society in general (as encapsulated within the 'social contract')" (Deegan & Unerman, 2011, p.348-349). Stakeholder theory is "focusing on how an organization interacts with particular stakeholders" and it "provides a more refined resolution by referring to particular groups within society (stakeholder groups)" (Deegan & Unerman, 2011, p.348-349).

3.3.2. Stakeholder Concept

Freeman & Reed (1983) proposed to understand the concept of stakeholder from two perspectives, a wide sense and a narrow sense, and they defined the stakeholder concept as:

"The Wide Sense of Stakeholder: Any identifiable group or individual who can affect the achievement of an organization's objectives or who is affected by the achievement of an organization's objectives. (Public interest groups, protest groups, government agencies, trade associations, competitors, unions, as well as employees, customer segments, shareowners and others are stakeholders, in this sense.)" (Freeman & Reed, 1983, p.91)

"The Narrow Sense of Stakeholder: Any identifiable group or individual on which the organization is dependent for its continued survival. (Employees, customer segments, certain suppliers, key government agencies, shareowners, certain financial institutions, as well as others are all stakeholders in the narrow sense of the term.)" (Freeman & Reed, 1983, p.91)

Freeman's wide sense of stakeholder concept includes another two different stakeholder concepts – primary stakeholders and secondary stakeholders (Clarkson, 1995, p. 106). Primary stakeholders are those whose continuing participation is a matter of survival for the corporation; while secondary stakeholders are those who can influence or affect positively and negatively the corporation, or those who are influenced or affected by the corporation's business operations. They do not take part in the transactions with corporation and they are not essential for a corporation's survival (Clarkson, 1995, p.106-107).

3.3.3. Normative and Positive Branch of Stakeholder Theory

Based on the different interpretations about stakeholder concept, stakeholder theory can be broken into two branches – normative (ethical/moral) branch and positive (managerial) branch (Deegan & Unerman, 2011, p.348).

The Normative/Ethical Branch of Stakeholder Theory

According to Deegan & Unerman (2011), stakeholder theory from moral perspective argues that "all stakeholders have the right to be treated fairly by an organization" and "the impact of the organization on the life experiences of a stakeholder should be what determines the organization's responsibilities to that stakeholder, rather than the extent of that stakeholder's (economic) power over the organization" (Deegan & Unerman, 2011, p.349).

Hasnas (1998) states in his paper *The Normative Theories of Business Ethics: A Guide for The Perplexed*:

"Managers should manage the business for the benefit of all stakeholders. It [stakeholder theory normative branch] views the firm not as a mechanism for increasing the stockholders' financial returns, but as a vehicle for coordinating stakeholder interests, and sees management as having a fiduciary relationship not only to the stockholders, but to all stakeholders." (Hasnas, 1998, p. 32)

Deegan and Unerman argue that "stakeholders have intrinsic rights" and "these rights should not be violated" (Deegan & Unerman, 2011, p.350). Both primary stakeholders and secondary stakeholders have their minimum rights, which can be interpreted as "the right[s] to be provided with information about how the organization is affecting them (perhaps through pollution, community sponsorship, provision of employment safety initiatives, etc.), even if they [stakeholders] choose not to use the information, and even if they cannot directly have an impact on the survival of the organization" (Deegan & Unerman, 2011, p.350-351).

Stakeholders' rights to information, as per Gray et al.s (1996) "accountability model", are reporting as a responsibility rather than demand driven (Deegan & Unerman, 2011, p.351). The role of corporate social responsibility report is to provide the society with information about whether or to which extent a corporation has met the responsibilities that are imposed upon it by the society (Deegan & Unerman, 2011, p.351).

The Positive/managerial Branch of Stakeholder Theory

The positive branch "explicitly considers various groups (of stakeholders) that exist in society, and how the expectations of particular stakeholder groups may have more (or less) impact on corporate strategies" (Deegan & Unerman, 2011, p.349); and it considers also "how they [stakeholders] should best be managed if the organization is to survive" (Deegan & Unerman, 2011, p.353).

Stakeholder theory from the managerial perspective argues that an organization should not respond to all stakeholders equally, but should respond to the most powerful stakeholders. A stakeholder's power is defined as "the extent that a stakeholder can exert its influence on the organization" (Dee-

gan & Unerman, 2011, p. 354) or "the stakeholder's degree of control over resources required by the organization" (Deegan & Unerman, 2011, p.353).

The role of management is to "asses the importance of meeting stakeholder demands in order to achieve the strategic objectives of the firm" (Deegan & Unerman, 2011, p.354). "The level of stakeholder power increases, the importance of meeting stakeholder demands increases." "Various activities undertaken by organizations, including public reporting, will be directly related to the expectations of particular stakeholder groups." (Deegan & Unerman, 2011, p.354) Thus the aim of information disclosure is to inform respective stakeholder groups that organizations are "conforming with those stakeholders' expectations" (Deegan & Unerman, 2011, p.354). Information becomes a major element employed by organizations to manage or manipulate their stakeholders, to gain their support or approval, to distract their opposition and disapproval as well (Deegan & Unerman, 2011, p.354-355)

Stakeholders have various conflicting interests and expectations. Empirical studies indicate that some corporations will choose to provide information to those most powerful stakeholders who are important to the survival of the organization (Deegan & Unerman, 2011, p.355). On the other hand, some other corporations will elect to be more ethical/morally aware. However, in most cases, there will be most likely a combination of both aspects (Deegan & Unerman, 2011, p.360).

3.4. Fairness and Social Norms

Hechter and Opp (2005) illustrated in their book *Social Norms* that there are no unified definition about social norms because researchers "disagree about what norms are" (Hechter & Opp, 2005, p.3). They pointed out that "several key elements are widely acknowledged as essential" for defining norms (Hechter & Opp, 2005, p.5). Based on those essential elements, they defined social norm as rules "that are enforced through social sanctions" and that specify what people should and should not do in certain social surroundings or under certain circumstances (Hechter & Opp, 2005, p.5). Norms are created and become "statistically expected and socially prescribed", if "most people behave in certain ways" (Hechter & Opp, 2005, p.278).

According to Hechter and Opp (2005), there are two types of norms: moral norms and coercive norms. They emphasize that "all norms might ultimately be moral norms" (Hechter & Opp, 2005, p.297).

Moral norms "*prescribe behavior that most people would do anyway or proscribes behavior that most people would not do anyway, even in the absence of such norms and the accompanying threat of sanctions*" (Hechter & Opp, 2005, p.281). For example, norms against rape or murder belong to

the category of moral norms and people tend not to violate moral norms (Hechter & Opp, 2005, p.281).

Coercive norm "*prescribes behavior that most people would not otherwise do or proscribes behavior that most people would otherwise do, in the absence of such norms*" (Hechter & Opp, 2005, p.281). Most of the specific coercive norms often have fairness as their moral ground (Hechter & Opp, 2005, p.297). For example, speeding and tax evasion are violations against coercive norms (Hechter & Opp, 2005, p.281) and fairness "necessitates the coercive norms of speed limits or tax contribution" (Hechter & Opp, 2005, p.297).

According to Moral Foundations Theory, fairness is one of the five moral foundations (Care/harm, Fairness/cheating, Loyalty/betrayal, Authority/subversion and Sanctity/degradation) for social norms. Each culture builds up its virtues, narratives and institutions, and thereby its unique moralities based on those five moral foundations. Moral Foundations Theory aims at understanding the differences and similarities of morality under the cross-cultural circumstances. According to Jonathan Haidt (2012), fairness/cheating foundation refers to "profiting from someone else's undeserved loss" (Haidt, 2012, Chapter 7, p.1).

In the field of social dilemma research, fairness is regarded as a social norm which acts as "an important motive in social dilemmas" (Biel, Eek, Gärling & Gustafson, 2008, p.76). Social dilemmas refer to the situation when self-interest conflicts with collective interest. Biel, *et al*. (2008) pointed out that fairness, as a strong societal norm, plays "a paramount role for how people behave in social dilemmas" (Biel, Eek, Gärling & Gustafson, 2008, p.76). It gives guidance to cooperation between individuals and "downplays the role of self-interest in social dilemmas" (Biel, Eek, Gärling & Gustafson, 2008, p.76).

Biel, *et al*. (2008) mentioned also that fairness is important for "self-presentational concerns. People are striving for maximizing their own gains. Simultaneously, they are trying to be seen as fair", because fairness is considered to be a moral virtue (Biel, Eek, Gärling & Gustafson, 2008, p.76).

Bicchieri (2006) examined social norms including fairness norm in his book *The Grammar of Society*. She categorized fairness, together with reciprocity and trust, into the category of local norms, because "their interpretation and the expectations and prescriptions that surround them vary with the objects, people, and situations to which they apply" (Bicchieri, 2006, p.76). However, both reciprocity and trust norms are partial and local in a stronger sense. By using rules against nepotism as an example of avoiding "personalizing fairness", she stated that fairness norms, in most societies, are considered as impartial, "in the sense that they are meant to apply to everyone who is in a given posi-

tion" (Bicchieri, 2006, p.76). Moreover, she emphasized that "we ought to be fair in all of our interactions" (Bicchieri, 2006, p.76).

3.5. Tax Planning and Tax Haven

3.5.1. Three forms of Tax Planning

The tax planning industry is thriving and many international tax accountants and lawyers are helping various multinational corporations to minimize their global tax burden (Eden, 2011, p.14-15). Shifting profit to tax haven through transfer pricing manipulation is one of the golden tools for helping tax planning, which includes three forms: tax avoidance, tax evasion and tax fraud (Eden, 2011, p. 15). Tax planning is perceived as compliant behavior when it is not concerned with the aggressive tax avoidance behavior that usually leads to tax evasion and tax fraud.

Tax evasion refers to "the situation where a company tries to reduce tax liability by falsely suppressing income or inflating expenditure, recording fictitious transactions, etc" (IBE, 2013, p.1). Tax fraud is tax evasion by hiding relevant facts, creating nonexistent facts, or which is "covered by a criminal provision in national tax law" (Eden, 2011, p. 16).

3.5.2. Tax Haven

Tax haven is a growing economic phenomenon and its growth rate is enormous. However, there are various definitions for tax haven. According to Assogbavi and Azondékon (2008), "the term 'tax haven' is not always easy to interpret, mainly because it has taken on so many different connotations" (Assogbavi & Azondékon, 2008, p.2). They quoted Colin Power's (2002) description about tax haven in her book *Tax Havens and Their Uses:*

"What … identifies an area as a tax haven is the existence of a composite tax structure established deliberately to take advantage of, and exploit, a worldwide demand for opportunities to engage in tax avoidance." (Assogbavi & Azondékon, 2008, p.2)

Based on Powell's description, Assogbavi and Azondékon gave their own definition of tax haven: "a country or territory where a wealthy individual either physically (having a local presence) or indirectly (meaning that he oversees operations from his resident country), may establish a legal tax shelter with advantages that extend further than those offered in his originating country. This individual may benefit by reducing his tax burden to benefit from a less tax-abrasive society by either self-managing an account or by forming a trust." (Assogbavi & Azondékon, 2008, p.2)

Gravelle (2009) proposed two definitions for the concept of "tax haven" – a broad definition and a narrow definition. In a broad sense, tax haven is defined as "any low-tax country with a goal of attracting capital, or simply any country that has low or non-existent taxes on capital income" (Grav-

elle, 2009, p.729). On the other hand, a narrow definition limits tax haven concept to " those countries that, in addition to having low or non-existent tax rates on some types of income, also are characterized by a lack of transparency and information sharing, allow for bank secrecy, and require little or no economic activity for an entity to obtain legal status" (Gravelle, 2009, p.729).

Report of Organization for Economic Co-operation and Development (OECD) in year 1998 defines tax haven as following:

- "No or only nominal taxation combined with the fact that a country offers itself as a place, or is perceived to be a place, to be used by non-residents to escape tax in their country of residence may be sufficient to classify that jurisdiction as a tax haven." (OECD, 1998, p.22)
- "No or only nominal taxation combined with serious limitations on the ability of other countries to obtain information from that country for tax purposes would typically identify a tax haven." (OECD, 1998, p.22)

According to the definitions given above, OECD adopts the narrow definition of tax haven proposed by Gravelle.

United States Government Accountability Office (GAO) stated in its report to congressional requesters (2008) that "there is no agreed-upon definition of a tax haven or agreed-upon list of jurisdictions that should be considered tax havens" (GAO, 2008, p.2). Based on various governmental, international and academic sources, GAO defines the characteristics of tax haven as:

"No or nominal taxes; a lack of effective exchange of information with foreign tax authorities; and a lack of transparency in legislative, legal, or administrative provisions." (GAO, 2008, p.2)

The report also pointed out that "offshore financial centers" and "financial privacy jurisdictions" have the similar characteristics as tax haven has.

Generally speaking, within the context of this paper, tax haven is perceived to be a jurisdiction that creates attractive tax rules, systems of regulation and veils of secrecy in order to benefit non-resident individuals and companies (Hearson & Brooks, 2012, p.2).

Similar to the concept of Tax Haven, there is not any unified list of tax havens. With a certain degree of subjectivity, different organizations or entities have their own criteria or interpretations of the Tax Haven concept (THG, 2014). The following Table 1 shows a list of tax havens which are used in various studies of tax haven.

Caribbean/West Indies	Anguilla, Antigua and Barbuda, Aruba, Bahamas, Barbados,[a,e] British Virgin Islands, Cayman Islands, Dominica, Grenada, Montserrat,[a] Netherlands Antilles, St. Kitts and Nevis, St. Lucia, St. Vincent and Grenadines, Turks and Caicos, U.S. Virgin Islands[a,e]
Central America	Belize, Costa Rica,[b,c] Panama
Coast of East Asia	Hong Kong,[a,b] Macau,[a,b] Singapore[b]
Europe/Mediterranean	Andorra,[a] Channel Islands (Guernsey and Jersey),[a] Cyprus,[a] Gibralter, Isle of Man,[a] Ireland,[a,b,e] Liechtenstein, Luxembourg,[a,b,e] Malta,[a] Monaco,[a] San Marino,[a,e] Switzerland[a,b]
Indian Ocean	Maldives,[a,d] Mauritius,[a,c,e] Seychelles[a,e]
Middle East	Bahrain, Jordan,[a,b] Lebanon[a,b]
North Atlantic	Bermuda[e]
Pacific, South Pacific	Cook Islands, Marshall Islands,[a] Samoa, Nauru,[c] Niue,[a,c] Tonga,[a,c,d] Vanuatu
West Africa	Liberia

Table 1: Countries listed on Various Tax Haven Lists

(Source: Gravelle, Jane G. (2009). Tax Havens: International Tax Avoidance and Evasion. pp. 729)

According to the latest prominent OECD list of Tax Havens (2012), the last seven jurisdictions (Andorra, The Principality of Liechtenstein, Liberia, The Principality of Monaco, The Republic of the Marshall Islands, The Republic of Nauru and The Republic of Vanuatu) on the list of unco-operative tax havens have been excluded. Therefore, there are no countries currently listed as unco-operative tax havens (OECD, 2012). Instead, OECD coined a term "Other Financial Centers" which includes countries officially regarded as tax havens and other jurisdictions that have similar characteristics in tax incentives as tax havens have. Table 2 is a list of offshore financial centers (OFC) according to OECD (2012) (THG, 2014).

list of offshore financial centres

Alderney	Gibraltar	Nauru
Andorra	Grenada	Netherlands Antilles
Anguilla	Guatemala	Niue
Antigua and Barbuda	Guernesey	Norfolk
Aruba	Hong Kong	Oman
Antillas Holandesas	Ireland	Panama
Aruba	Israel	Philippines
Bahamas	Jersey	St. Kitts and Nevis
Bahrain	Jordan	St. Vincent
Barbados	Labuan	St. Lucia
Belize	Lebanon	Samoa
Bermuda	Liberia	San Marino
Botswana	Liechtenstein	Sark
British Virgin Islands	Luxembourg	Seychelles
Brunei Darussalam	Macau	Singapore
Cayman Islands	Madeira	Switzerland
Campione D'Italia	Malta	Turks and Caicos
Cook Islands	Isle of Man	UAE
Costa Rica	Marshall Islands	United Kingdom
Cyprus	Mauritius	Uruguay
Dominica	Monaco	USA
Ghana	Montserrat	Vanuatu

Table 2: List of Offshore Financial Centers

(Source: Tax Havens Guide. http://www.taxhavensguide.com/list-of-offshore-financial-centres.php)

In order to understand multinational corporations' transfer pricing manipulation, we have already presented theories related to transfer pricing, stakeholder theory and legitimacy theory with a complementary brief introduction of "fairness" social norm. The concept of tax planning and tax haven are also presented. In the next chapter, we are going to examine 1) the regulations about transfer pricing, especially OECD guidelines; 2) the practical mechanism of profit shifting via manipulating transfer pricing by presenting several cases; and 3) the attitudes of the general public towards tax avoidance behavior by showing the results of surveys and interviews. Afterwards, we will conduct the analysis from both theoretical perspective and practical perspective.

4. Global Regulations related to Transfer Pricing

This part presents the global regulations related to transfer pricing, especially OECD's work on transfer pricing.

4.1. OECD Guidelines – OECD's Work on Transfer Pricing

The arm's length principle dates all the way back to the first half of the century, when the League of Nation Model Tax Conventions formed the international consensus and in 1963 found its way into article 9 of the OECD Model Tax Convention. In 1980 it was adopted by the United Nations Model Double Taxation Convention between Developed and Developing Countries. Today the arm's length principle is used in bilateral income tax treaties between OECD member countries as well as between OECD member countries and non OECD economies. It is currently part of the transfer pricing rules in over a hundred countries domestic legislation (Ruiter, 2012, p. 1).

OECD has been continuously developing, revising and updating practical guidance for the implementation of the arm's length principle since the year 1979 via The OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. The increasingly globalized economy creates huge challenges and in 2010 the guidelines were revised with a focus on comparability and profit methods. Among other things, this led to new guidance on transfer pricing aspects of business restructurings. During 2011, two new projects dealing with the transfer pricing of intangibles and the simplification of transfer pricing were launched by the OECD. (Ruiter, 2012, p.2)

Intangibles in connection to transfer pricing related matters such as transfer pricing aspects of business restructuring were considered to be a key area of concern to governments and taxpayers, because there is a lack of sufficient international guidance in particular on the definition, identification and valuation of intangibles for transfer pricing purposes. (Ruiter, 2012, p. 2)

The project concerning transfer pricing simplification was considered to be a high priority project and was aimed at streamlining the administration of the transfer pricing system in areas such as transfer pricing documentation and understandability of the guidelines themselves. (Ruiter, 2012, p. 2)

OECD held its first annual meeting in March 2012. The meeting was about transfer pricing under the auspices of global forum on treaties and transfer pricing. This enabled government officials from 90 countries to discuss transfer pricing issues (Ruiter, 2012, p. 3).

OECDs Task Force on Tax and Development identified transfer pricing as one of its high-priority areas and aims to help developing countries introduce and implement transfer pricing rules by

providing support on policies issues for administrative structures, regulations and guidance and building practical auditing skills. Other aspects that will be looked over are availability of comparable data and access to financial data that is sometimes needed in order to apply transfer pricing rules. (Ruiter, 2012, p. 3-4)

OECD, the European Commission and World Bank formed an international partnership in order to provide support. During May 2012 The Task Force on Tax and Development launched "Tax Inspectors without Borders" which is an initiative to help developing countries make their tax systems fairer and more effective. Plans were made by the OECD to establish an independent foundation to provide international auditing expertise and advice to help developing countries combat tax base erosion such as tax evasion as well as avoidance. (Ruiter, 2012, p. 4-5)

Over 40 Commissioners or Heads of Taxation of OECD and non OECD economies make up OECD's Forum on Tax Administration. The aim of this forum is to produce outputs of significant relevance to developing countries and in 2012 the forum published the report "Dealing Effectively with the Challenges of Transfer Pricing" which focused on practical administration of transfer pricing programs. (Ruiter, 2012, p. 4-5)

On November 12th to 14th, 2012, a conference took place. During the conference, transfer pricing experts met more than 100 private sector representatives. OECD had a discussion related to Intangibles, Safe Harbors and Timing Issues. There was a discussion about how to improve the transfer pricing compliance and enforcement, and the implementation of targeted safe harbor provisions. According to Business Dictionary, safe harbor is a “provision in an agreement, law, or regulation that affords protection from liability or penalty under specified circumstances of if certain conditions are met” (Business Dictionary, 2014). Furthermore, the meeting focused on how to clear up the transfer pricing rules for transactions regarding intangibles and rules related to limiting the opportunities for applying the transfers of intangibles for tax advantage by attributing income to parties that only hold the legal title to the intangible, with the absence of economical contribution towards development and maintenance. (OECD, 2012)

During 2013 new guidelines were introduced, concerning safe harbors in order to relieve some of the compliance burdens as well as to provide a greater certainty when involving smaller taxpayers and less complicated transactions, making developing countries able to make optimal use of the limited resources available. Some of the old guidelines concerning safe harbors were revised to better reflect the practices of OECD Member countries, as the way they are viewed have somewhat changed to a more positive view. Among some of the changes are bilateral agreements leading to safe harbors. A proposed draft recognizes that properly designed safe harbors can help relieve compliance burdens and provide taxpayers with greater certainty. (OECD, 2013)

OECD has historically placed a lot of focus on eliminating double taxation. The Model Tax Convention serves as a basis for over 3000 bilateral tax treaties.(OECD, 2014, webcast) Pascal Saint-Amans, Director, OECD Centre for Tax Policy and Administration has stated during a 23 January 2014 OECD webcast, that OECD might have been so effective in eliminating double taxation that they may have facilitated double non taxation. The recognition of double non taxation practices such as tax avoidance has led to OECD focusing on Base Erosion and Profit Shifting (BEPS) and publishing two reports: "Addressing Base Erosion and Profit Shifting" in February 2013 and later in July "Action Plan on Base Erosion and Profit Shifting, OECD Publishing". (OECD, forum, 2013) OECD is working together with the G20 countries on the BEPS project in order to develop rules to rehabilitate the global taxation system. (Saint-Amans, 2013)

4.2. Action Plan on Base Erosion and Profit Shifting

The Action Plan on Base Erosion and Profit Shifting (BEPS) is a plan for the actions that OECD wants to take in order to restrain base erosion and profit shifting. It also sets timelines for the implementation of the BEPS project (OECD, 2013). According to the action plan, the rules in the area of transfer pricing need to be revised with a larger emphasis on value creation in highly integrated groups, tackling the use of intangibles, risks, capital and other high-risk transactions to shift profits. (OECD, 2013, p.13)

According OECD's Action Plan on Base Erosion and Profit Shifting, governments are deregulating the business environment and competing on offering lower tax in order to attract or retain economic activities. Such behaviors often take "the form of across the board corporate tax rate reductions on particular types of income (such as income from financial activities or from the provision of intangibles)" (OECD, 2013, p.17). They can be harmful for the taxation in many countries, because they help drive the applicable tax rate on certain mobile sources of income to zero not only for countries that employ this type of taxation policies but also for those who do not. OECD plans to tackle these issues by putting more emphasis on transparency and substance in the regulations. (OECD, 2013, p.17)

Action five "Counter harmful tax practices more effectively, taking into account transparency and substance" (OECD, 2013) in the Action Plan on Base Erosion and Profit Shifting states:

"Revamp the work on harmful tax practices with a priority on improving transparency, including compulsory spontaneous exchange on rulings related to preferential regimes, and on requiring substantial activity for any preferential regime. It will take a holistic approach to evaluate preferential tax regimes in the BEPS context. It will engage with non OECD members on the basis of the existing framework and consider revisions or additions to the existing framework." (OECD, 2013, p. 18)

A major purpose of transfer pricing rules, the arm's length principle in particular, is to allocate multinational corporations' profits in order to make them taxed in the countries where corporations conduct their business. In many cases, the transfer pricing rules based on the arm's length principle are able to achieve this aim effectively and efficiently. In other instances however, this might not always be the case. Multinational corporations are able to manipulate the rules to separate the income from the economic activities which generate the income by moving the income to low-tax jurisdictions such as tax havens. Some of the more common ways of doing so are: "transfers of intangibles and other mobile assets for less than full value, the over-capitalisation of lowly taxed group companies" and "contractual allocations of risk to low-tax environments in transactions that would be unlikely to occur between unrelated parties", i.e. an uncontrolled transaction. (OECD, 2013, Action Plan on Base Erosion and Profit Shifting, OECD Publishing p19-20)

OECD has recognized that the current regulatory systems need to be changed. However, due to the practical difficulties regarding the implementation and the importance of concerted action, the best course of action is to directly address the flaws regarding returns related to intangible assets, risk and over-capitalizations in the current transfer pricing system rather than replacing it with an entirely new system. To this end, special measures either within or beyond the arm's length principle may be required. (OECD, 2013, p. 20)

Actions eight, nine and ten (OECD, 2013, p. 20-21) in the Action Plan on Base Erosion and Profit Shifting state:

"**Assure that transfer pricing outcomes are in line with value creation"**

"Action 8 – Intangibles Develop rules to prevent BEPS by moving intangibles among group members. This will involve: (i) adopting a broad and clearly delineated definition of intangibles; (ii) ensuring that profits associated with the transfer and use of intangibles are appropriately allocated in accordance with (rather than divorced from) value creation; (iii) developing transfer pricing rules or special measures for transfers of hard-to-value intangibles; and (iv) updating the guidance on cost contribution arrangements." (OECD, 2013, p. 20)

"Action 9 – Risks and capital Develop rules to prevent BEPS by transferring risks among, or allocating excessive capital to, group members. This will involve adopting transfer pricing rules or special measures to ensure that inappropriate returns will not accrue to an entity solely because it has contractually assumed risks or has provided capital. The rules to be developed will also require alignment of returns with value creation. This work will be co-ordinated with the work on interest expense deductions and other financial payments." (OECD, 2013, p. 20) "

“Action 10 – Other high-risk transactions Develop rules to prevent BEPS by engaging in transactions which would not, or would only very rarely, occur between third parties. This will involve adopting transfer pricing rules or special measures to: (i) clarify the circumstances in which transactions can be recharacterised; (ii) clarify the application of transfer pricing methods, in particular profit splits, in the context of global value chains; and (iii) provide protection against common types of base eroding payments, such as management fees and head office expenses." (OECD, 2013, p.20-21)

The above changes are set to take place during September 2014 and September 2015 (OECD, 2013, p.33). A starting point for the BEPS project is that OECD’s work needs to be inclusive and effective, which means that OECD’s work should “take into account perspective of developing countries and benefits from input of business and the civil society at large” (OECD, 2013, p.25). As a result, in light of the strong interest and support expressed by the G20 governments, even non OECD member countries of the G20 are invited to be part of the BEPS project as associates. Moreover, they will be on equal footing with OECD member countries, and thereby they “will expected to associate themselves with the outcome of the BEPS Project” (OECD, 2013, p.25). An important aim for the BEPS project is that it needs to be in line with the political expectations from most countries (OECD, 2013, p.26). However, consultations with non-governmental stakeholders are also of key importance. Therefore, business and civil society representatives are also invited to comment on different proposals. (OECD, 2013, p.26)

5. Empirical Data

This part describes multinational corporations' tax avoidance mechanism via presentation of several cases. The general public's attitudes towards corporations' tax avoidance behavior in any form are also presented through various survey results. Our own survey and interviews with the major Swedish media outlets are also presented here in order to reveal the fact – the lack of public concern on corporations' tax planning behavior in the society.

5.1. An Overview of Multinational Corporations' Tax Avoidance Behavior

Many multinational corporations operate successfully around the world. But they are paying little or even no local corporate tax at all. According to the 2011 ActionAid report (2011), the 100 biggest groups listed on the London Stock Exchange (FTSE 100) "comprise 34,216 subsidiary companies, joint ventures and associates". "38% (8,492) of their overseas companies are located in tax havens." 98 of FTSE 100 companies use tax havens in order to reduce their corporate tax bills (ActionAid, 2011, p.1).

Her Majesty's Revenue and Customs (HMRC), a non-ministerial department of the UK government which is responsible for the collection of taxes, estimated that during 2010 and 2011 the gap between the amount of actually collected corporation tax and the amount which should be collected is £4.1 billion. Some researchers believe that this tax gap is as big as £12 billion (IBE, 2013, p.2). ActionAid (2011) mentioned in its report "Addicted to tax havens: The Secret Life of the FTSE 100" that the U.K. government could be losing as high as £18 billion a year to tax havens (ActionAid, 2011, p. 6).

According to a U.S. Senate report (2009), "offshore tax abuses cost the U.S. Treasury an estimated $ 100 billion each year in lost tax revenues, … Abusive domestic tax shelters cost tens of billions of dollars more." The report also presents that more than 80 percent of the U.S. largest companies have offshore subsidiaries in tax havens (Levin, 2009).

Multinational corporations' tax avoidance behavior by taking advantage of tax haven "add[s] to the soaring budget deficit and shift[s] the tax burden to small businesses and families, who play by the rules". Carl Levin, the U.S. Senator of Michigan, claims that "Offshore tax haven and tax shelter abuses are undermining the integrity of our tax system and increasing the tax burden on middle income families" (Levin, 2009).

According to the Bloomberg journalist Jesse Drucker (2010), transfer pricing manipulation causes almost $60 billion dollars loss yearly for the U.S. Treasury. And it takes almost seven years for the U.S. government to generate $60 billion tax on certain financial institutions and this "lost revenue could pay the federal government's share of health coverage for more than 10 million uninsured Americans" (Drucker, 2010).

Crisea and Nguyen (2013) conducted a study to prove, with new empirical evidence, multinational corporations' profit shifting mechanism through transfer pricing manipulation. They use data for the period 1999 – 2006 from Denmark and find significant evidence that Danish multinational firms shift profits from high-tax jurisdictions to low-tax jurisdictions by using transfer pricing manipulation. They find that "a 10 percentage point decrease in the foreign tax rate below Denmark's rate induces a MNC to lower its export price by 5.7 percent when selling to a market with established foreign ownership, relative to non-affiliated exporters" (Crisea & Nguyen, 2013, p. 4).

Their research also points out that "the fall in the MNC's export price is even larger when estimated on the subsample of firms who establish new affiliates during the sample period." (Crisea & Nguyen, 2013, p. 4) The result indicates "a 10 percent fall in the export prices of MNCs relative to non-affiliated exporters" (Crisea & Nguyen, 2013, p.4). These findings prove that Danish multinational corporations shift profit to low-tax jurisdiction by using low export prices in order to avoid taxation.

Action Aid's report (2011), *Addicted to Tax Havens*, claims that corporate tax avoidance is "one of the main reasons companies use tax havens" (ActionAid, 2011, p.1). Such a behavior has "a massive impact on developing and developed countries alike" (ActionAid, 2011, p.1). Yet, the developing countries suffered more from multinational corporations' tax avoidance behavior, because such a behavior cuts off "the only sustainable source of funding for [developing countries'] governments to invest in reducing poverty and inequality" (ActionAid, 2011, p.1). "The OECD estimates that developing countries lose almost three times more to tax havens than all the aid they receive each year" (ActionAid, 2011, p.1).

Ernst & Young 2013 Global Transfer Pricing Survey

According to Ernst & Young's 2013 global transfer pricing survey which is based on interviews with professionals at 878 corporations in 26 countries, "66% of companies identified 'risk management' as their highest priority for transfer pricing". There is "a 32% increase over surveys conducted in 2007 and 2010" (Ernst & Young, 2013, p.3). The results of the survey also show that "28 % of companies reported using the mutual agreement procedure; 26% of companies reported using the advance pricing agreement process (APA); 15% of companies reported having referred a case to litigation in the past year; 28% of companies report unresolved transfer pricing examinations; 60% of companies report having been subject to an interest charge when they had a transfer pricing adjustment; 24% report having been subject to penalties when they had a transfer pricing adjustment" (Ernst & Young, 2013, p.7).

The growing concern for transfer pricing issues leads to increasing amount of work for supranational organizations. OECD has recently carried out a project on BEPS (Base Erosion and Profit Shifting)

which is focusing on harmonizing tax authorities' approaches to eliminate inappropriate tax avoidance. In BEPS project report, some indicators show that "tax practices of some multinational companies have become more aggressive over time, raising serious compliance and fairness issues." (Ernst & Young, 2013, p.6) Report points out that transfer pricing is "key pressure area", especially when it comes to "the shifting of intangibles, the artificial splitting and ownership of assets between entities within a group, and transactions between such entities that would rarely take place between independents" (OECD, 2013, p.6).

5.2. Cases of Tax Avoidance Through Transfer Pricing Manipulation

The following cases are collected from companies' web pages and other various sources, such as Fobes, Bloomberg, the Guardian, and Action Aid's reports.

5.2.1. Forest Laboratories Inc. Case – The Double Irish

Forest Laboratories Inc., a pharmaceutical company, has its headquarters in New York City. The company is known for licensing European pharmaceuticals in order to sell those medicines in the United States. For example, Forest sells Lexapro, the world's third bestselling antidepressant, in the United States. Since Lexapro's debut in 2002, $13.8 billion revenue has been generated and 58 percent of Forest's sales were from Lexapro (Drucker, 2010). In 2009, Lexapro alone generated $2.3 billion in revenue. But most of its profits are not taxed in the U.S. and company pays little tax elsewhere (Drucker, 2010).

The profit from Lexapro makes a journey across the Atlantic Ocean first to Dublin, Ireland. Lexapro are produced and tested in the Forest subsidiary, Forest Laboratories Ireland Ltd. The Irish subsidy controls the patents of Lexapro for the U.S. market; while Forest licenses the use of patent from a Danish pharmaceutical company, H. Lundbeck A/S and the Irish subsidy pays for Lexapro's U.S. clinical trials (Drucker, 2010). The Irish subsidiary sells Lexapro to the parent company in the U.S. The secondary processing, such as bottling and blister-packing, is carried out in the U.S. Each tablet the parent company buy helps shift profit to Ireland, where the corporate tax rate is between 10 percent and 12.5 percent (Drucker, 2010). However, the corporate tax rate in the U.S. is 35 percent, which is one of the world's highest tax rates on corporate income. In fiscal year 2009, the Irish subsidy reported $2.5 billion in sales which accounted for 70 percent of parent company's net sales ($3.6 billion) (Drucker, 2010).

The profit from Lexapro does not stay in Ireland. Taking advice from Ernst & Young in 2005, the Irish subsidiary "Forest Laboratories Holdings Ltd" started reorganizing and registered a one-person law office in Hamilton, Bermuda which has no corporate tax (Drucker, 2010). This law office is claimed to be the corporation's tax residence and then controls licensing of the patents. A second

subsidiary in Ireland was established to deal with the manufacturing and sublicensing the rights to the patents (Drucker, 2010). This arrangement helped the Irish subsidiary reduce its effective tax rate from 10.3 percent to 2.4 percent, because the license fees which went to Bermuda were deducted from the corporation's taxable income (Drucker, 2010). Those license fees did not need to pay any corporate income tax in Bermuda. This type of structure has a special name: the Double Irish (Drucker, 2010).

In order to avoid another Irish tax, the profit from Lexapro did not go directly to Bermuda. Before it finally flied to Bermuda, it stayed in Amsterdam temporarily via passing through another subsidiary (Forest Finance BV in the Netherlands) where Forest has no employees. Forest's annual report in 2007 presented that Forest Finance paid out 99.6 percent of its $1.19 billion licensing income as licensing expense (Drucker, 2010). According to Richard Murphy, the director of Tax Research LLP, this route helped Forest bypass a 20 percent tax in Ireland on certain royalties for patents by taking advantage of "an exemption from the levy if payments go to a company in another EU member state" (Drucker, 2010).

This Irish-Dutch-Bermudan international operation doubled Forest's income tax saving. In 2007, the company's effective tax rate was reduced by 21.8 percent. By using transfer pricing manipulation, Forest saved more than one third of its tax payments in 2009, which accounted for $183 million. As a result, Forest's net income was boosted by 31 percent in 2009. (Drucker, 2010)

Current Financial Performance

Table 3 presents selected financial data of Forest Laboratories, Inc. from 2009 to 2013. There were continuous increases in corporation's net sales during four years from 2009 to 2012 (4% in 2009, 7% in 2010, 8% in 2011 and 4.3% in 2012). The corporation's most significant product, Lexapro, achieved a sale of $2,315,880 in fiscal 2011, which indicated an increase of $45,527 compared with the sales in fiscal 2010 (Forest Laboratories, Inc., 2011, p.13).

In fiscal 2013, the corporation's net sales decreased 33.9 percent and Lexapro also met its waterloo with a significant decrease of 90.9 percent in net sales (see Table 3 & 4 below) (Forest Laboratories, Inc., 2013, p.12). The 2013 Annual Report blames the sharp decline of the corporation's net sales to the dramatic decrease in Lexapro sales, which, as per the 2013 Annual report, is the result of "the expiration of its [Lexapro's] market exclusivity in March 2012" (Forest Laboratories, Inc., 2013, p.12). The report also points out that "excluding Lexapro sales, net sales increased $448.1 million or 19.8% for fiscal 2013 compared to fiscal 2012" (Forest Laboratories, Inc., 2013, p.12).

(In thousands, except per share data)	Year Ended March 31, 2013	2012	2011	2010	2009
Summary of operations:					
Net sales	$2,904,936	$4,392,548	$4,213,126	$3,903,524	$3,636,055
Contract revenue and other	221,189	193,496	206,574	289,338	286,727
Costs and expenses	3,170,983	3,348,356	3,081,964	3,242,176	2,952,248
Income (loss) before income tax expense	(44,858)	1,237,688	1,337,736	950,686	970,534
Income tax expense (benefit)	(12,755)	258,630	290,966	268,303	202,791
Net income (loss)	(32,103)	979,058	1,046,770	682,383	767,743
Net income (loss) per share:					
Basic	$ (0.12)	$ 3.58	$ 3.60	$ 2.25	$ 2.52
Diluted	$ (0.12)	$ 3.57	$ 3.59	$ 2.25	$ 2.52
Weighted average number of common and common equivalent shares outstanding:					
Basic	266,807	273,561	291,058	303,386	304,363
Diluted	266,807	274,016	291,175	303,781	305,121

Table 3: Forest Laboratories, Inc. Selected Financial Data (2009-2013)

(Source: Forest Laboratories, Inc. (2013). 2013 Annual Report – Financial Data. P.1)

(In thousands)	Year Ended March 31, 2013	2012	Change	% Change
Key Marketed Products				
Namenda	$1,520,640	$1,390,307	$ 130,333	9.4 %
Bystolic	455,092	347,772	107,320	30.9
Viibryd	162,511	56,507	106,004	187.6
Savella	104,587	102,812	1,775	1.7
Daliresp	77,924	31,203	46,721	149.7
Teflaro	44,010	22,449	21,561	96.0
Linzess	23,728	--	23,728	--
Tudorza	22,996	--	22,996	--
Lexapro	194,939	2,130,624	(1,935,685)	-90.9
Other Products	298,509	310,874	(12,365)	-4.0
Total	$2,904,936	$4,392,548	$(1,487,612)	-33.9 %

Table 4: Net Sales of Key Products of Forest Laboratories, Inc.

(Source: Forest Laboratories, Inc. (2013). 2013 Annual Report. P.12)

5.2.2. Apple Case

By using transfer pricing manipulation, Apple successfully cuts its U.S. corporate tax by an average of $10 billion yearly for four years. We all know that almost all the value of Apple's products is in its patents and other intellectual properties. Apple minimizes the U.S. mother company's intellectual

property income by charging little to its foreign affiliates for using the intellectual property. This helps Apple shift the profit to its foreign subsidiaries by maximizing their profits (Gleckman, 2013).

Apple has two firms in Ireland and they are the core of Apple's tax arrangements. These two firms helped Apple funnel two-thirds of its pre-tax global income (Gleckman, 2013). In 2011, Apple generated $34 billion in pre-tax income in total, of which $22 billion was shifted to these two firms in Ireland. However, these incomes did not return to Apple. It disappeared into the deep blue. That is, the "ocean income" as Harvard University tax professor Steve Shay says (Gleckman, 2013).

According to Australian Financial Review, Apple has moved $8.9 billion in profits from Australia to Ireland in the past 10 years (Farrell, 2014). In 2013, Apple Sales International in Ireland was reported to help Apple shift $2 billion income from Australia to Ireland and Apple only reported $88.5 million in pre-tax earnings in Australia (Farrell, 2014).

Current Financial Performance

Table 5 presents the three-year (2011-2013) financial history of Apple Inc. As per the data in table 4, both domestic and international net sales of Apple are increasing continuously every year. Domestic and international net sales in financial year 2012, compared with 2011, have increased 45.77 percent and 43.83 percent respectively. The increase of net sales in financial year 2013 is 8.61 percent for domestic and 9.53 percent for international, compared with sales in 2012. The yearly increase of total net sales is 44.58 percent for 2012 and 9.20 percent for 2013.

Results of Operations *($ millions, except shares in thousands and per share amounts)*	FY 2013	FY 2012	FY 2011
Net sales:			
Domestic	$66,197	$60,949	$41,812
International	104,713	95,559	66,437
Total net sales	170,910	156,508	108,249
Cost of sales	106,606	87,846	64,431
Gross margin	64,304	68,662	43,818
Operating Expenses:			
Research and development (R&D)	4,475	3,381	2,429
Selling, general and administrative (SG&A)	10,830	10,040	7,599
Total operating expenses	15,305	13,421	10,028
Operating income	48,999	55,241	33,790
Other income/(expense), net	1,156	522	415
Income before provision for income taxes	50,155	55,763	34,205
Provision for income taxes	13,118	14,030	8,283
Net income	$37,037	$41,733	$25,922
Diluted earnings per share	$39.75	$44.15	$27.68
Shares used in computing diluted earnings per share	931,662	945,355	936,645
Cash dividends declared per common share	$11.40	$2.65	$0.00

Table 5: Apple Three-Year Financial History

(Source: Apple Website (http://investor.apple.com/financials.cfm). (2014). Apple Three-year Financial History. p.1)

	2014 Q 2	2014 Q 1	2014 Q 2	2013 Q 1
Quarterly Revenue	$45.6	$57.6	$43.6	$54.5
Quarterly Net Profit	$10.2	$13.1	$9.5	$13.1

Table 6: Apple Quarterly Reports

(Source: Apple Website (http://investor.apple.com/results.cfm). (2014). Earnings Releases.)

According to Apple's first quarter 2014 (ended December 28, 2013) report, record quarterly revenue was $57.6 billion, which is an increase of 5.69 percent compared to the same quarter the previous year at $54.5 billion (Apple, 2014). Quarterly net profit is $13.1 billion (Apple, 2014). International sales account for 63 percent of the quarter's revenue (Apple, 2014). Both iPhones (51 million) and iPads (47.8 million) sales during the first quarter 2014 created the all-time quarterly records (Apple, 2014).

Apple's second quarter 2014 (ended March 29, 2014) report shows quarterly revenue of $45.6 billion and net profit of $10.2 billion (Apple, 2014). Compared to the year-ago quarter ($43.6 billion in revenue and $9.5 billion in net profit), both revenue and net profit are increasing (Apple, 2014). The increases are 4.59 percent for quarterly revenue and 7.37 percent for net profit. International sales in the second quarter account for 66 percent of the quarter's revenue, which increased by 3 percent compared to the previous quarter in 2014 (Apple, 2014).

5.2.3. Caterpillar Case

Caterpillar Inc. is one of the world's largest manufacturing companies which designs, manufactures, markets and sells machinery and engines. It is reported that the company moved more than $8 billion in profits to Switzerland for the reason of tax avoidance (Roberts, 2014).

The majority of Caterpillar's manufacturing, R&D and employment are in the U.S. The company's most profitable business is the international spare parts business. There are 54 manufacturing facilities, 10 warehouses and 4900 parts employees in the U.S. Caterpillar company which ships around 1.5 billion parts around the world. The Company has also an offshore subsidiary in Switzerland which has only 65 staff members and has no parts manufacturing or warehouses. The Swiss subsidiary is established only for the tax avoidance purpose, according to a senior tax official who works for the company. It is reported that 85 percent of profit from the international spare parts business were routed through Caterpillar's Swiss subsidiary (Roberts, 2014). By making a deal with Swiss tax authorities, the company succeeded in avoiding paying more than $2.4 billion in U.S. tax over a decade. And Caterpillar's Geneva-based subsidiary only paid 4% tax on the profits of international spare parts sales (Roberts, 2014).

Caterpillar is accused of employing aggressive transfer pricing manipulation in order to avoid tax on purpose, since the company's parts business is mostly based in a high-tax jurisdictions instead of at its offshore Swiss subsidiary (Roberts, 2014).

5.2.4. SABMiller Case

SABMiller is one of the FTSE 100 corporations and it is the world's second-biggest brewer and one of the world's biggest bottlers of Coca-Cola products. SABMiller has more than 200 beer brands and over 70,000 employees in 75 countries around the world. The headquarters of the company is situated in London, United Kingdom. (SABMiller, 2014)

SABMiller has been involved in many tax affairs in the developing world. One example is the corporation's tax dispute case in Delhi High Court, India. SABMiller is accused of evading tax when buying intangible assets (Forster's brand name and patent in the Indian branch) from Forster's Australia, one of SABMiller's subsidiaries (Padmakshan, 2009). In 2011, SABMiller was sentenced to pay tax on the deal of purchasing the Indian assets from Foster's. According to the report "Calling Time – Why SABMiller Should Stop Dodging Taxes in Africa" conducted by ActionAid, there are more than 10,000 people around the world taking actions to urge SABMiller to take responsible measures to deal with these tax affairs (Hearson & Brooks, 2012, p.4).

Accra Brewery, SABMiller's subsidiary in Ghana, Africa, is the second-largest brewer in Ghana. Hearson and Brooks (2012) described in their report that company generated £29 million of beer yearly but it recorded a loss in the past two years. Moreover, company "paid corporation tax in only one of the four years from 2007-10". A small retailer of SABMiller's Club beer in Ghana with £220 in profit monthly paid more income tax than its supplier, SABMiller's subsidiary in Ghana, during the past two years (Hearson & Brooks, 2012, p.7).

The Action Aid's report presented four ways SABMiller used to avoid tax. Among these four tax dodging strategies, two of them are too new to find solid data to show the tax lost for the African countries. The other two strategies – going Dutch and the Swiss Role – are presenting a huge tax loss to African countries (Hearson & Brooks, 2012, p.7-8).

Going Dutch

SABMiller has a subsidiary in the Netherlands which is in charge of the company's local beer brands sold in African countries where the beer is produced. The subsidiary in the Netherlands "takes advantage of a novel set of tax rules offered by the Netherlands that enables companies to pay next to no tax on the royalties they earn" (Hearson & Brooks, 2012, p.8). According to the Action Aid report, SABMiller's African subsidiaries paid £25 million in royalties in 2011 and this directly led to "an estimated tax loss to African countries of £10 million" (Hearson & Brooks, 2012, p.8).

The Swiss Role

The Action Aid's report revealed that "SABMiller's African and Indian subsidiaries pay whopping 'management service fees' to sister companies in European tax havens where effective tax rates are lower, mostly to Switzerland" (Hearson & Brooks, 2012, p.8). Hearson and Brooks (2012) quoted the words from the head of the Ghana Revenue Authority in their report, "management fees is an area that we know is being used widely [to avoid tax], and it's mainly because it's difficult to verify the reasonableness of the management fee" (Hearson & Brooks, 2012, p.8). It is estimated that SABMiller's African and Indian subsidiaries pay £47 million in management fees yearly and this helps SABMiller successfully dodge £9.5 million in tax payment (Hearson & Brooks, 2012, p.8).

Current Financial Performance

During the tax dispute period (from 2009 to 2011), SABMiller's financial performance was not affected at all. Its group revenue and EBITA (earnings before interest, tax, amortization and exceptional items) continued to increase. According to SABMiller's Annual Report 2009, 2010 and 2011, corporation's group revenue growth was 9%, 4% and 7%; corporation's EBITA growth was 5%, 6% and 15% (SABMiller, 2009, p.1; 2010, p. 1; 2011, p.1).

According to SABMiller plc Annual Report 2012, the corporation's "reported EBITA grew 12%, with organic, constant currency EBITA growth of 8%; EBITA margin increased by 10 basis points (bps) to 17.9%" (SABMiller, 2012, p.7). Except for a slight EBITA decline in the European market, strong EBITA increases dominated all the other markets, among which Asia Pacific had the highest EBITA increase with 30%. The African market had an EBITA growth of 16% and the other two markets, Latin America and South Africa, both had 14% in EBITA growth (SABMiller, 2012, p.7). North America EBITA increased by 2% (SABMiller, 2012, p.7).

SABMiller plc Annual Report 2013 shows a "reported group revenue growth of 10%" with organic, constant currency group revenue growth of 7% (SABMiller, 2013, p.38). EBITA had an increase of 14% with 9% on an organic, constant currency basis and EBITA margin increased by 70 basis points (bps) to 18.6%, compared with the previous year (SABMiller, 2013, p.38). The adjusted profit before tax had an increase of 11 percent (SABMiller, 2013, p.38).

5.3. Public Attitudes to Tax Avoidance in Any Form

5.3.1. World Value Survey 2005-2006

World Value Survey (WVS) is a global survey of socio-cultural and political change. The latest survey, WVS 2005/2007, collected data from 57 countries, including most of the OECD countries (WVS, 2011). The national sample each involves more than 1000 individuals. "The World Values

Surveys have produced comparative data on what people value, what their beliefs are, what they want out of life and the facts of life.” (Tekeli, 2011, p.8)

In the questionnaire of WVS 2005, question number 200 is about the general public’s attitudes towards cheating on taxation. Similar question has been surveyed altogether four times during two decades (from 1981 to 2005). The question in the latest survey is:

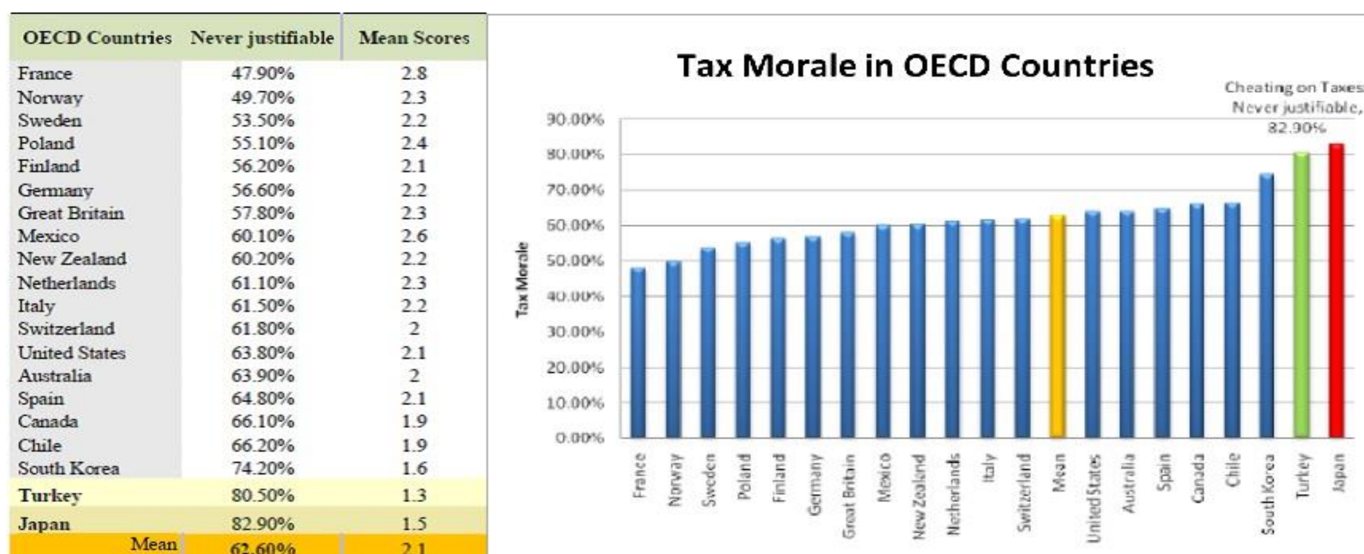
“Please tell me for each of the following actions whether you think it can always be justified, never be justified, or something in between, using this card.”

	Never justifiable								Always justifiable
V200. Cheating on taxes if you have a chance	1	2	3	4	5	6	7	8	9	10

Table 7: Question 200 in the questionnaire of WVS 2005

(Source: WVS 2005-2006 Wave, OECD-Split Version – Ballot A)

As shown above, the attitude to cheating on taxes is measured with a one to ten scales. A one represents that cheating on taxes is never justifiable; a 10 indicates that cheating on taxes is always justifiable. Many researchers use the data from this survey to analyze how views change over time globally. Tekeli (2011) tried to “link the tax morale and high degree of tax compliance” (Tekeli, 2011, p.2) and to find out the determinants of tax morale based on the data from the question listed above. According to his study, the attitude of individual in OECD countries towards cheating on taxes is shown in Figure 1. On average 62.6 percent of individuals in OECD countries agreed that “tax cheating is never justifiable.



OECD Countries	Never justifiable	Mean Scores
France	47.90%	2.8
Norway	49.70%	2.3
Sweden	53.50%	2.2
Poland	55.10%	2.4
Finland	56.20%	2.1
Germany	56.60%	2.2
Great Britain	57.80%	2.3
Mexico	60.10%	2.6
New Zealand	60.20%	2.2
Netherlands	61.10%	2.3
Italy	61.50%	2.2
Switzerland	61.80%	2
United States	63.80%	2.1
Australia	63.90%	2
Spain	64.80%	2.1
Canada	66.10%	1.9
Chile	66.20%	1.9
South Korea	74.20%	1.6
Turkey	80.50%	1.3
Japan	82.90%	1.5
Mean	62.60%	2.1

Figure 1: Tax Morale in OECD Countries

Note: Data for public attitudes to tax cheating was not available for all OECD countries. (Source: Tekeli (2011). The Determinants of Tax Morale: the Effects of Cultural Differences and Politics. Page 12-13)

5.3.2. ComRes Tax Avoidance Survey and IBE Business Ethics Survey

From February 15 to February 17, 2013, Christian Aid (ComRes) conducted a survey about the public attitudes to tax avoidance which was based on an online interview with 2,270 adults in the U.K. According to this tax avoidance survey, public anger on tax avoidance increased in 2012 and 80 percent of Britons felt anger over multinational corporations' tax avoidance behavior. The survey also showed that one third of the Britons are boycotting companies that avoid tax in the U.K.(ComRes, 2013). Another survey conducted by ActionAid showed that 72 percent of Britons agreed that "companies should pay their full share of tax, and it is not acceptable for them to use loopholes in the law to avoid paying their share" (ActionAid, 2012).

An IBE briefing "Tax Avoidance as an Ethical Issue for Business" (2013) concluded based on Christian Aid's tax avoidance survey that 75 percent of respondents of the survey think that the British government has "a responsibility to ensure that all UK-based companies pay the proper amount of tax in every country in which they operate". 85 percent respondents of the survey claim that "it was 'too easy' for multinational companies in the U.K. to avoid paying tax" (IBE, 2013, p.2).

5.3.3. Survey and Interview About Multinational Corporations' Tax Planning

Survey about Multinational Corporations' Tax Planning

As mentioned earlier in 2.2.2. Data Collection and Processing, survey was conducted in a form of conversation with 50 randomly selected people, among whom there are 25 Swedish citizens from a typical Swedish community and 25 students from Lund University. 88 percent of respondents (44 respondents out of 50) claimed that tax planning is their least concern or is the least interesting topic compared with the other three alternatives. 60 percent of correspondents (30 respondents out of 50) chose to rank the issues as 1) Environmental Problem; 2) Child Labor; 3) Low Salary; and 4) Tax Planning. The detailed ranking information about the top issue on the list is presented in the following Table 8.

The Top Issue on the List	25 normal Swedish Citizens	25 students from Lund University	Total	Percentage
a) Environmental Problem	18	12	30	60%
b) Low Salary	2	1	3	6%
c) Child Labor	5	6	11	22%
d) Tax Planning	0	6	6	12%

Table 8: Result of Survey: Issue positioned at the Top of the List

All the respondents in the community rank tax planning last on the list and their reasons for such a ranking are unanimous: there is a lack of media publicity about multinational corporations' tax planning behavior. As for the students, depending on different academic backgrounds, they have certain biases towards different issues. Four students from Business Administration and two students from Economics, for example, regarded tax planning as the most interesting topic. Other students all ranked tax planning last on the list due to a lack of publicity. Furthermore, they claimed that tax planning was simply not as close to the heart as the other subjects were, especially compared to child labor and environmental issues.

Interviews with Media

With the aim of finding out why there is so little media publicity about tax planning, we conducted interviews with seven major Swedish media companies. The interview questions are listed in 2.2.2. Data Collection and Processing. Answers to the questions are various and some of the answers related to issues other than tax planning are not of interest to us, since our focus is tax planning. The result shows that most Swedish media placed tax planning at the bottom of the list. It should, however, be noted that no one said tax planning was uninteresting, but it was considered to be a bad choice for news reporting. The relevant information from the interviews is summarized as follows:

Relevance to the Readers / Viewers

Relevance is something mentioned by all of our interviewees. Newspapers and news stations want to report issues in the society that their target audiences care so much about that they would like to do something about them. The problem with news reports about tax planning is that it doesn't touch the emotions of the target audience as much as other subjects, such as child labor. Another problem is that it does not affect the audience directly. If a company in Sweden is using transfer pricing strategy to shift profits to the tax haven in order to avoid corporation tax in Sweden, the general public is only indirectly affected by such a behavior. News about tax planning simply doesn't evoke the same strong emotion as other subjects (e.g. environment problems or child labor) do. After all, people would probably think: "It's only the government's money; it's not ours! The government would just waste it anyway".

Needs of Being Actual News

The word "new" is not part of the word "news" due to coincidence. One of the important points mentioned by both TV stations and two newspapers (Metro and Dagens Nyheter) is that news need to be something that is previously unknown or uncovered. There is, after all, little point to report about things that everyone already knows about. Tax planning and tax avoidance via various methods, such as transfer pricing manipulation, has been going on for a long time. It is no longer some-

thing that could be considered "news". If the media is to report about it, they need to find a new angle to report it, i.e. an angle to make it more appealing to the public.

Could Be Too Complicated

All five newspapers pointed out that tax planning and tax avoidance can be so complicated that it is hard for the general public to understand. Both TV stations mentioned that tax planning, besides being kind of “old news”, is so complicated that it will take up too much air time in the news for a thorough report. Moreover, journalists themselves sometimes are not experts in this field, either. This means that it is troublesome for journalists to report about tax planning, if they want to have some depth in their reports. These two factors lead to tax planning generally not being considered as the best choice for news, because neither the general public nor the journalists have enough knowledge to be able to make proper judgment.

6. Analysis

Based on the literature overview and empirical data, this part presents the analysis of transfer pricing manipulation by answering the questions: 1) What are the motives for multinational corporations to engage in transfer pricing manipulation? 2) Will tax avoidance behavior via manipulating transfer pricing eventually lead to legitimacy problem for multinational corporations?

6.1. Internal and external motivates for transfer pricing manipulation

The trend of the business has long been internalization, which is one of the advantages for a multinational corporation over a domestic company (Eden, 2011, p. 7). The benefits from internalization, such as reduced transaction costs and free mobility of tacit resources, provide the ground for intra-firm trade (Eden, 2011, p. 7-8). Multinational corporations can have both internal and external motives to manipulate transfer pricing in the intra-firm trade. Corporations' profit maximization goal characterizes the internal motive for transfer pricing manipulation and tax-induced motives explain their external motives.

Internal motive – profit maximization goal

Multinational corporations mostly have decentralized organizational structure based on profit centers which have strengthened profit consciousness. For example, the foreign subsidiaries of four multinational corporations (Forest Laboratories Inc., Apple, Caterpillar Inc., and SABMiller) presented in the empirical data are considered to be profit centers which generate profits or costs separately via transfer pricing in the transactions within the corporation. The goal for each subsidiary is obviously maximizing its own profit. From the perspective of the whole corporation, the optimal goal has always been maximizing the corporation's profit.

As an effective tool for internal management control, a corporation's transfer pricing strategy has an important objective – to induce goal congruent decisions, i.e. the profit maximization goal of each profit center should be consistent with the whole corporation's profit maximization goal. Empirical data shows that four multinational corporations managed to maximize the whole corporation's profits by maximizing their subsidiaries' individual profits in the intra-firm trade. It is done through shifting the corporations' pre-tax income to their offshore subsidiaries in tax havens via manipulating transfer pricing, which minimizes the corporations' tax costs.

According to stakeholder theory managerial branch, the role of management is to meet the most powerful stakeholders' demands in order to achieve the strategic objectives of the corporation. Maximizing stakeholders' profits is the "one best way" to serve their interests. It is thus reasonable for those four corporations to maximize their profits by minimizing their tax cost via transfer pricing manipulation.

The primary norm of transfer pricing – the arm's length principle – indicates that intra-firm trade should be conducted just like the transactions between unrelated partners on the open active market. The relation between unrelated trading partners is competitive, because their goals are maximizing their individual profits. However, in intra-firm trade, trade partners are related and their goals are consistent and cooperative – maximizing the whole corporation's profit. The individual profit maximization goal of the "arm's length principle" conflicts the cooperative goal of intra-firm trade. Therefore, multinational corporations have strong incentives to manipulate transfer pricing and deviate from the prominent transfer pricing norm.

External Motives – tax-induced motives

It is a universal truth that globalization makes it easier to exchange capital, goods and services across international borders or territories. Ghemawat (2003) pointed out that we are "in a state of semiglobalization" and we will "stay there for the next few decades" (Ghemawat, 2003, p.5-6). Semi-globalization indicates that there are still many big differences between countries, for example, differences in price and resources and differences in law and regulations.

Beneficial tax regulations for the purpose of attracting foreign direct investments and tax haven are such economic phenomena under the circumstances of semi-globalization. Beneficial tax regulations induce tax differences which make regulatory arbitrage possible. Low or zero tax rates and a veil of secrecy for transactions via tax havens provide strong incentives for multinational corporations to shift their profits by manipulating transfer pricing in order to avoid corporate income tax, which is probably the most important motivation for corporations' profit shifting behavior.

The four cases presented in the empirical data share the same characteristic: tax planning via regulatory arbitrage, especially via shifting profits between high- and low- tax jurisdictions by using transfer pricing strategies and by taking advantage of the different tax regulations. Four corporations mentioned in the cases all established offshore subsidiaries in "Tax Haven" countries or "Offshore Financial Centers" (OFC) (Forest Laboratories Inc.'s Irish subsidiary and law office in Bermuda; Apple's Irish subsidiaries; Caterpillar Inc.'s Swiss subsidiary; SABMiller's subsidiaries in Netherlands and Switzerland). Those offshore subsidiaries are either claimed to be the corporations' tax residence (e.g. Forest's law office in Bermuda and Caterpillar's Swiss subsidiary) or in charge of the intangible assets (e.g. Forest's Irish subsidy, Apple's Irish firms, and SABMiller's subsidiary in Netherlands), such as trademarks, patents and other intellectual properties. Moreover, some subsidiaries provide management services (e.g. SABMiller's subsidiary in Switzerland) and charge management fees to sister companies. In order to avoid or evade corporate taxation, four multinational corporations (Forest Laboratories Inc., Apple, Caterpillar Inc., and SABMiller)

successfully shifted their pre-tax global income through their offshore subsidiaries by maximizing those foreign subsidiaries' profits either through patents' licensing fees or management fees.

Another external factor which makes the transfer pricing manipulation possible is the disadvantage of the arm's length principle, when it comes to pricing intangible assets such as patents and other intellectual properties. One reason is that the arm's length principle has an inherent problem: finding comparable intangible assets when the transaction involves intangible assets such as patents or trademarks. That is to say, how to distinguish the value of the trademark from the value of the product or service. Calculating a transfer price based on the arm's length principle by using for example the CUP method means to set a price as if it was between independent contractors. However, setting an appropriate price for an intangible asset is difficult because, for example, no trademarks in the world are at the same value; and how should people value patents. This is therefore problematic.

The disadvantages of the arm's length principle make it possible for corporations to shift profits to tax havens by mispricing the intangibles during the transaction. OECD has acknowledged that, today, the arm's length principle by itself might not be enough and further revisions of the regulations need to be done. For example, regulations related to definition of intangibles, regulations concerning the allocation of the profits from intangibles not being divorced from the value creation of the assets, regulations about developing special measures for hard-to-value intangibles and regulations involving cost contribution arrangements. But for now, the inherent disadvantage of the arm's length principle still exists with regard to the current regulations. And this is an important external factor for corporations' motivation to engage in transfer pricing manipulation for tax purposes.

6.2. Tax Induced Transfer Pricing Manipulation and Legitimacy Problem

Multinational corporations under globalization "can benefit from integration and arbitrage in ways that domestic firms cannot" (Eden & Smith, 2011, p.8). As per our analysis above, they have both internal and external motivations to manipulate transfer pricing for the purpose of tax avoidance. Governments and authorities have long been aware of and are on full alert for the negative effects of multinational corporations' inherent behavior of arbitraging international tax burdens via transfer pricing strategies.

6.2.1. The Negative Effects of Tax Avoidance

Among three forms of tax planning, tax evasion and tax fraud are fundamentally illegal, while tax avoidance lies in a grey area. It is a sort of legitimate form of tax planning which uses loopholes in laws and regulations for avoiding taxes. Moreover, there is a fine line between tax avoidance and tax evasion.

No matter which form of tax planning multinational corporations are using, their tax payments are minimized, which causes a huge cut on the government's tax revenue. As the finance minister of South Africa stated, "aggressive tax avoidance" is "a serious cancer" which is "eating into the fiscal base of many countries" (Hearson & Brooks, 2012, p.6).

Governments of developed countries are losing billions of dollars annually in tax revenue because of multinational corporations' tax avoidance behavior via transfer pricing manipulation. According to OECD estimation, "developing countries lose almost three times more to tax havens than all the aid they receive each year" (ActionAid, 2011, p.1). Very aggressive tax schemes aiming at dodging tax in developing countries, such as in SABMiller case, bring even more serious issues. Empirical evidences also show that developing countries suffered more from multinational corporations' tax avoidance behavior via shifting profit out of those developing countries.

Even if tax avoidance is not illegal, it brings the same or even more severe negative impacts on the society. It leads to welfare loss to the society and it discourages other tax compliant firms and individuals.

6.2.2. Tax Avoidance Behavior and Social Contract

According to legitimacy theory, the social contract includes both explicit and implicit terms. Explicit terms usually refer to laws and regulations; while implicit terms are related to social norms and non-legislated societal expectations. Tax evasion and tax fraud via aggressive transfer pricing manipulation are against the laws and regulations of transfer pricing. Such behaviours will receive sanctions according to law and regulations and thereby are violations of the explicit terms in the social contract. However, multinational corporations' tax avoidance behavior is not illegal, which means it does not breach the explicit terms of the social contract. But, does tax avoidance behavior breach the implicit terms of the social contract?

Fairness is conceived by many philosophical researches as either the moral foundation for social norms or a strong societal norm. Moral Foundations Theory defines fairness as "profiting from someone else's undeserved loss" (Haidt, 2012, Chapter7, p.1). Hechter & Opp (2005) pointed out clearly that fairness "necessitates the coercive norms of speed limits or tax contribution" (Hechter & Opp, 2005, p.297). Therefore, multinational corporations' tax avoidance behavior is against fairness, which indicates that such a behavior is a violation of the implicit terms in the social contract and thereby is a breach of the social contract.

Tax Avoidance and Fairness

Every country is facing public spending obligations and constraints such as financing public infrastructure, national defence, education, health care, social security, and other public services.

Expenses on those essential goods and services in various aspects are majorly financed by the government's tax revenue. Tax avoidance behavior of the four corporations mentioned in empirical data diverts resources used for these public spending obligations to the hands of a few individuals. In the long run, the welfare loss caused by their tax avoidance behavior would suffocate the hosting country's economic development.

When Caterpillar establishes a subsidiary in a tax haven – Switzerland only for the purpose of tax avoidance, while the majority of its key business activities are remaining in the high-tax jurisdiction – the U.S. as the home country with 35% corporate tax rate, Caterpillar becomes a "free rider" who enjoys the benefits from the public spending in the home country without contributing to financing it.

On the other hand, governments of tax haven countries like Switzerland in the Caterpillar case can be regarded as "free riders" as well, since they are benefiting from consuming other countries' (e.g. the U.S. in Caterpillar case) resources without paying for them. It is not fair to consume one country's resources while avoiding contributing to the national development of that country. It is not fair either when benefiting from consuming other countries' resources without payments.

For the developing world, multinational corporations' profit shifting behavior through transfer pricing manipulation (e.g. in SABMiller case) has caused huge losses which those poor countries' governments can hardly afford. Developing countries like Ghana in Africa are trying very hard in order to develop the national economy and improving their tax systems in order to generate additional revenues for the national development. However, SABMiller's profit shifting behavior undermines such efforts from Ghana's government. According to Action Aid's report (2011), the tax payment that SABMiller avoid in Africa can afford to educate more than 250, 000 African children (ActionAid, 2011, p.6). Tax avoidance behavior of multinational corporations like SABMiller in developing countries can be compared to an action of exploitation under the new circumstances. It is obviously unfair and immoral.

Moreover, multinational corporations' tax avoidance behavior is not fair to those who are voluntarily paying their fair share of tax strictly complying with the spirit of law. As the U.S. senator Carl Levin (2009) pointed out that tax avoidance behavior redistributes the tax burden, because the compliant taxpayer will eventually bear the whole tax burden. Just as Carl Levin (2009) emphasized in his report, the unfair distribution of tax burden will discourage the compliant tax paying behavior and will make compliant taxpayers distrust the tax system. In order to compete favorably in the market, tax compliant corporations will most probably choose to engage in the tax avoidance schemes as well, which will induce more tax revenue loss to the government and more welfare loss to the society. Therefore, multinational corporations' tax avoidance behavior can induce a vicious circle.

6.2.3. Tax Avoidance and Legitimacy Problem

Multinational corporations try to minimize their tax via transfer pricing manipulation in order to achieve shareholder wealth maximization. This is a part of good governance as per stakeholder theory managerial branch. However, from the perspective of stakeholder theory normative branch, corporations should consider the interests of all the stakeholders which refer to anyone who is affected by a corporation's business activities. Legitimacy theory also emphasizes that corporations should have "the rights of the public at large" (Deegan & Unerman, 2011, p.325) or the whole society's best interests at heart and do as what society expects them to do.

Her Majesty's Revenue and Customs (HMRC) stated that corporate tax "is not a voluntary tax" and that "the public expects businesses to pay their fair share [of tax]" (BBC, 2012). All corporations have a moral obligation to pay their fair share of tax. This is also supported by the result of World Value Survey 2005 – 2006, which presented that no form of cheating in tax is justifiable.

According to legitimacy theory, corporations have to earn their rights towards resources. In order to do so, they try very hard to build up positive images and get legitimated by the society through engaging in activities which contribute to improve the social welfare, such as community development projects or donation to the charity. However, tax avoidance behavior makes their efforts wasted.

Multinational corporations' tax avoidance behavior via aggressive transfer pricing manipulation can be treated as a breach of the social contract, since it is a violation of both explicit and implicit terms in the social contract. Such a behavior would eventually induce sanctions from the society, such as declined sales volume. To make it worse, the corporations' public image would be destroyed and their legitimacy would be questioned.

Christian Aid's survey about public attitudes to tax avoidance shows clearly that most British citizens are angry about multinational corporations' tax avoidance behavior and there are public actions to boycott corporations who do not pay their fair share of tax. It is a proof that multinational corporations' tax avoidance behavior is not consistent with the social contract that corporations agreed upon and the society is imposing sanctions on their breaching behavior.

A corporation's image or reputation is a resource for generating future profit. When a corporation's image is damaged and its legitimacy is questioned, its future profitability will be negatively affected. In worst case scenario, it can lose its "license to operate". Tax avoidance by any means will eventually cause damage to a corporation's reputation and bring threats to its legitimacy, since it is against the social norm as "fairness" and thereby a breach to the social contract between the corporation and the society.

As per our analysis above, theoretically tax avoidance behavior will eventually cause legitimacy problem for multinational corporations. But in reality, will such a conflictual behavior of multinational corporations' really bring threats to corporations' legitimacy?

Empirical data shows a very different story. Sales of those corporations previously mentioned in the empirical part (Forest Laboratories, Inc., Apple Inc. and SABMiller) did not go down because of their tax avoidance behavior via transfer pricing manipulation. Among these financial data in the empirical part, Apple's financial performance is very eye catching, even if the corporation is accused of shifting two-thirds of its pre-tax global income for the purpose of tax avoidance. Apple's domestic and international net sales increased continuously during 2011 to 2013 and the first two quarter reports in 2014 present increases on both quarterly revenue and net profit. The international sales in the second quarter, which accounts for the greater part of the second quarter's revenue, has also increased. Sales for iPhones and iPads in the first quarter even created the all-time quarterly records.

An endangered legitimacy can be indicated by the declining sales due to the general public's boycott against the products from corporations which do not pay their fair share of tax. However, our empirical data shows that those multinational corporations' tax avoidance behavior does not threaten their legitimacy in reality, because their net sales and revenue are still increasing. Theoretically, tax avoidance behavior should eventually cause legitimacy problem, but why does it not bring threats to corporations' legitimacy in reality? An obvious answer is that the general public are not concerned enough about corporations' tax planning behavior to take actions such as boycotting their products.

As per our survey, the prominent reason for the general public not being very interested in corporations' tax planning is a lack of publicity. Our interviews with the major Swedish media companies showed that there are three main reasons for not having a wide media coverage about tax planning: 1) It is not interesting enough to arouse the emotions of the public; 2) Tax planning is kind of "old news" and it's troublesome to find attractive angles to report; 3) Tax planning is such a complicated issue that it is hard for both the public and journalists to understand properly without professional knowledge. Out of the reasons mentioned above, the media often does not regard tax planning as a good topic, which leads to a lack of public awareness about tax planning. Therefore, there is not enough public concern to create a threat against corporations' legitimacy.

6.2.4. Is Legitimacy Theory Applicable for the Issue of Tax Planning?

To advance further with our analysis, another issue of concern is whether legitimacy theory is applicable and appropriate for the subject of tax planning via transfer pricing manipulation. Assume that corporations' tax avoidance behavior will lead to legitimacy problem, the first question to be addressed is: When would corporations actually start to face the legitimacy problem? Our answer is:

when people get to know the negative effects of corporations' tax avoidance behavior and start to boycott their products. Based on this assumption, we would like to further our study by separating the possible occurrence of the legitimacy problem induced by tax avoidance behavior into two phases as showing in figure 2.

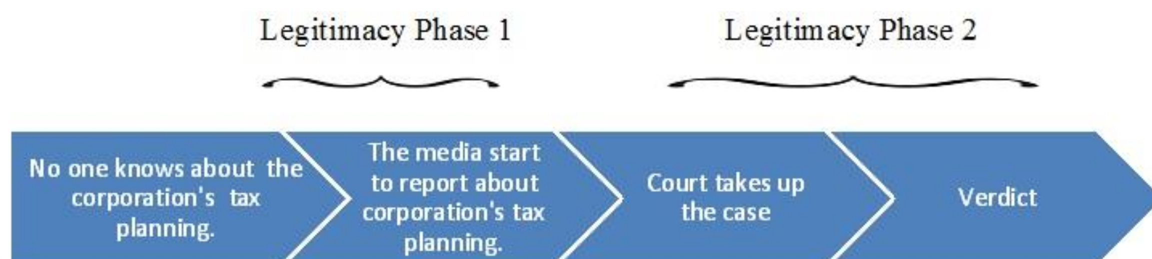


Figure 2: Basic Flow Chart about the Occurrence of the Legitimacy Problem

In figure 2, our assumption in phase 1 is that a corporation's tax avoidance behavior would lead to the legitimacy problem which would be presented in the form of such as declining sales. However, the empirical data about corporations' financial performances and our analysis based on the empirical data do not support this assumption. We think that the main reason for a lack of consistence between the legitimacy theory and the reality might lie in the products themselves, namely the brands and patents. For example, people will choose to buy an IPhone, even if there are phones of other brands with similar technology and performance. The reason behind this choice is the strong brand effect of Apple which makes IPhone a unique product. And thus there will be no clear substitutes for it. As a result, people will not stop buying IPhones just because Apple avoids paying their fair share of tax. A similar argument can be made for customers' continuous purchasing of certain medicine from corporations, such as Forest Laboratories Inc., that hold exclusive rights to the patents of the medicine, especially when the medicine is considered to be the best or the most effective of its kinds.

Additionally, our survey shows that there is a lack of concern among the general public for tax planning. We consider this to be another major cause for why the sales of these four corporations in the empirical data do not correspond well with the legitimacy theory. This is however something that should have been included into the scope of the legitimacy theory; something that could shed light on the fact that social expectations might not have yet heightened enough to make tax avoidance behavior be considered as a serious breach of the implicit terms in the social contract.

During phase 2, a corporation's tax planning scheme becomes a court case and the ruling is not in the favor of the corporation. In such circumstances, the corporation's tax avoidance behavior breaches the explicit terms in the social contract. Theoretically speaking, corporations involving in tax dispute should face legitimacy problem and receive sanctions from society, for example in the form of falling sales. However, our empirical data shows that the sales of such corporations have not

decreased, no matter whether they are in the middle of court process of tax dispute or they have been found guilty of tax avoidance. For example, from 2009 to 2011, SABMiller had a tax dispute case in the Delhi High Court, India, which is involving the transferring of intangible assets, such as Foster's brand name and patent, to SABMiller.

A guilty verdict for a corporation's tax dispute case denotes that the corporation's tax avoidance behavior is considered to be illegal. Such a behavior is a breaching of the explicit terms in the social contract and there should be a change of the corporation's behavior related to tax planning. An important thing to point out here is that the breach of the social contract is mainly between government and corporations. Our survey and interviews about the public attitudes towards corporations' tax planning behavior reveal that the general public does not care about tax planning to the extent that they will regard it as a serious breach of the social contract. Therefore, they continue to buy the company's products. In reality, therefore, legitimacy problem does not exist in phase 2, either.

Furthermore, convicted corporations will change their tax planning behavior due to the punishments imposed on them according to law. However, due to their internal motives of manipulating transfer pricing – profit maximization goal, corporations will continue to find loopholes in the laws and regulations related to transfer pricing and practice regulatory arbitrage for the tax purpose, as long as the social expectations have not heightened enough to regard tax avoidance behavior as a serious breach of social contract. Based on our analysis above, we conclude that corporations' tax avoidance behavior via transfer pricing manipulation will not cause legitimacy problem for corporations and thus legitimacy theory is not applicable for the issue of tax planning.

7. Conclusion and Discussion

This part presents the conclusion based on the analysis. Furthermore, suggestions about reducing multinational corporations' incentive to engage in tax motivated transfer pricing manipulation are given.

7.1. Conclusion

Multinational corporations have both internal and external motives to manipulate transfer pricing in order to shift their profits between high- and low-tax jurisdictions. The profit maximization goal characterizes the internal motive for transfer pricing manipulation; globalization, tax haven, different practices of tax regulations and the difficulty to appropriately apply the arm's length principle provide external environment for multinational corporations to manipulate transfer pricing in order to avoid corporation taxes.

Corporations' aggressive manipulation of transfer pricing often leads to tax evasion and tax fraud, which obviously breach the social contract and such behaviors will induce the sanctions according to laws and regulations. Tax avoidance behavior lies more in a grey area. From the perspective of legitimacy theory, it is a breach of the social contract, since it is against the norm of fairness and thereby violates the implicit terms in the social contract. Theoretically, multinational corporations' tax avoidance behavior will cause legitimacy problem for them. However, in reality such a behavior does not really endanger their legitimacy due to a lack of public concern, which is majorly caused by a lack of media exposure. The brand effect and the uniqueness of the products also explain the lack of consistence between legitimacy theory and reality.

No matter whether the general public knows about corporations' tax avoidance behavior or not; no matter whether corporations are in the middle of the court process of tax disputes or have been found guilty, tax avoidance behavior via transfer pricing manipulation will not cause legitimacy problem for corporations and thus legitimacy theory is not applicable for the issue of tax planning.

7.2. Discussion

Even if multinational corporations' tax avoidance behavior via transfer pricing manipulation will not cause legitimacy problem, it is still unethical and harmful to the society. How can we stop such a behavior or, at least, reduce multinational corporations' incentives to engage in such a behavior?

Elliott (2013) argues that corporations will only change for one of three reasons: 1) forced to change due to the pressure from customers; 2) forced to change because of compliance with law and regulations; 3) spontaneous change in order to operate in accord with moral sentiments (Elliott, 2013).

We suggest, as per Elliott's arguments, giving greater publicity to multinational corporations' tax avoidance behavior; reducing the arbitrage opportunities for transfer pricing manipulation and changing the rationalization of tax avoidance behavior via transfer pricing manipulation. Lessening of arbitrage opportunities will involve strengthening and harmonization of regulation such as changing of tax policies and accounting standards at both national and international level. Changing rationalization requires strengthening of the ethical training related to tax planning via transfer pricing manipulation.

Greater Publicity to Tax Avoidance Behavior

Based on Theory of Moral Sentiments by Adam Smith, Elliott (2013) argues that "it is up to consumers and voters to change the lousy behaviour" of big companies (Elliott, 2013). He points out that according to Adam Smith, many problems "would be solved if only people could hold up a mirror and see themselves 'in the light in which others see us' (Elliott, 2013). Therefore, corporations would like to "be held in high esteem by their customers" (Elliott, 2013).

We suggest a greater publicity to corporations' tax planning in order to make the general public know those severe negative impacts tax avoidance behavior brings about. Corporations' behavior can be forced to change due to the pressure from the attitudes of their customers. Starbucks' volunteering to pay extra corporate tax in the UK is a good example. BBC News reported in June 2013 that Starbucks started to pay UK corporate tax for first time since 2009 after avoiding UK corporation tax for 14 years. Furthermore, Starbucks decided to pay an extra £5 million later in 2013 due to "the bad publicity and the pressure from politicians and campaigners" (BBC, 2013). Starbucks spokeswoman claimed that Starbucks listened to customers and responded to the public anger (including the proposal of boycotting Starbucks) over the revelation of the corporation's tax avoidance behavior. Thus, Starbucks decided to pay £10 million in corporate tax in 2013 and another £10 million in 2014 (BBC, 2013).

Reducing the Arbitrage Opportunities

Our analysis concluded that tax avoidance, from corporations' perspective, most probably will not cause legitimacy problem, since the sales did not decline, which is because the general public are not concerned enough about corporations' tax planning behavior to boycott the products. However, it does not mean that the governments are happy about multinational corporations' tax planning behavior. The G20's strong support towards OECDs BEPS project and the continuous revisions of old regulations as well as the creations of new regulations are proofs for governments' actions to tackle tax avoidance behavior. We suggest and call for more similar actions which aim at harmonizing and strengthening the laws and regulations related to transfer pricing, in order to reduce the arbitrage op-

portunities for transfer pricing manipulation. The co-operation between both governmental and non-governmental representatives takes into account not only the government's point of view but also the perspective of business and civil society. This may lead to better harmonized regulations.

Changing the Rationalization of Tax Avoidance Behavior

Multinational corporations' tax avoidance behavior via transfer pricing manipulation is a conflictual behavior and it is categorized as business ethical issue. Such a conflictual behavior can be viewed from two different perspectives. Seen from the corporation's perspective on one hand, the tax avoidance behavior is merely a way to reduce costs, which is part of a sound business plan. It is thus consistent with the corporation's professional ethics, because it fits well for the primary goal of the corporation as a whole – profit maximization. According to Hansen, Crosser and Laufer (1992), tax avoidance is allowed by the law and it therefore gives practitioners the right to choose it as an alternative (Hansen, Crosser & Laufer, 1992, p. 683).

On the other hand, seen from the perspective of the whole society and from the ethical perspective, following laws, regulations or rules is not always equivalent to being ethical – "doing the right thing" (Hansen, Crosser & Laufer, 1992, p. 684). It is not illegal to bend the rules and regulations of the tax system, but such a behavior is inconsistent with the spirit of the law. Companies have choices for interpreting the tax law and they draw their ethical line concerning the interpretation of tax law and their business arrangements. Corporations' tax avoidance behavior is regarded as an immoral and unethical practice which negatively affects the integrity of the tax system (IBE, 2013, p.1).

Moreover, multinational corporations' tax avoidance behavior via transfer pricing manipulation is harmful to the society because it causes loss of social welfare; it is against the moral ethics, since such a behavior is against the social norm of "fairness", which thereby breaches the "social contract"; and it is an evasion to corporate social responsibility.

There should be no distinction between professional and moral ethics. Tax practitioners should be driven by doing right thing and not just blindly do what is allowed by the law (Hansen, Crosser & Laufer, 1992, p. 684). Eden and Smith (2011) emphasized that it is important to include ethical training related to transfer pricing manipulation as "part of the tax planning community's professional recertification activities" (Eden & Smith, 2011, p. 26). They also pointed out that this type of training should focus on "comparing tax and moral ethics, determining the 'bright line' where a TPM [transfer pricing manipulation' action becomes unethical, and taxation in the context of corporate social responsibility" (Eden & Smith, 2011, p.26-27). They also recommend that ethics of transfer pricing should be included in business school teaching agenda, "particularly in accounting and MBA courses" (Eden & Smith, 2011, p.27).

The tax payment is not just a legal issue; it should be regarded as a moral and ethical issue. Researchers call for "a development of a transfer pricing hypernom", which transfer pricing manipulation is regarded as corporate fraud and socially irresponsible (Eden & Smith, 2011, p.27). Eden and Smith proposed two ways for developing such a hyper-norm: 1) regarding abusive transfer pricing as corrupt behaviors of firms and including it into the principles of the UN Global Compact (UN Global Compact provides a series of standards or hyper-norms for corporations); 2) extending the work of Financial Action Task Force (FATF) and Wolfsberg Group about trade finance principles (Eden & Smith, 2011, p. 28). The principles from both organizations are designed only for stopping money laundering activities by trade mispricing. Eden and Smith (2011) suggested extending FATF's work and Principles in order to create "a set of more general norms for transfer pricing" (Eden and Smith, 2011, p.28).

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