Discussion: The Globalization of Corporate Control by Gur Aminadav, Luis Fonseca and Elias Papaioannou

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Road map

Overview

Comment #1: Comparison to official sources

Comment #2: Complex Hierarchies

Comment #3: Empirical Results

Closing Remarks

Overview

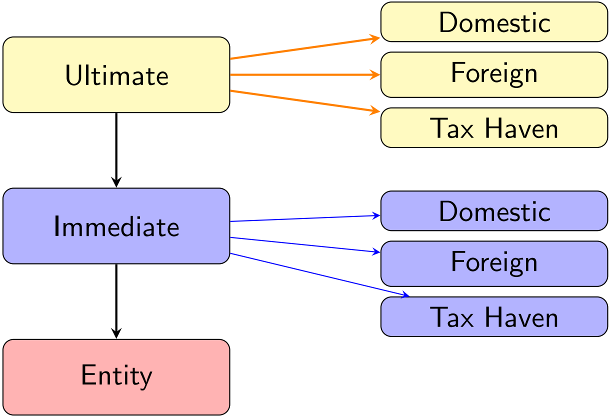
- The paper provides an anatomy of international corporate control based on information on the ownership structure of listed firms from 86 countries.
- Careful treatment of the data, distinguishing between immediate and ultimate ownership as well as the nationality of the owner (including those incorporated in tax haven countries).
- Important contribution to the existing literature that until very recently had mainly relied on aggregate country-level information based on *residence principle*.
- Recent efforts to improve upon this literature:
  - Bond and equity issuance (Coppola, Maggiori, Neiman and Schreger (2021))
  - Real and "phantom" FDI channeled through Special Purpose Enterprises, SPEs (Damgaard, Elkjaer, and Johannesen (2019)).
  - The Missing Profits of Nations (Tørsløv, Wier and Zucman (2021)).

Overview

- Build a new database: construction
  - Complement BvD ORBIS ownership database with company reports, government publications, regulatory agencies, financial data providers and media (Bloomberg, Dun & Bradstreet, Google Finance, Credit Risk Monitor, and Forbes).
  - One cross-section in 2012: Over 25,000 listed firms in 86 countries with over 84,000 shareholders and ultimate owner from 86 countries.
  - The sample accounts for 87% of the total value of market equity in Datastream and 81% of global market capitalization reported by World Bank.

Overview

- Corporate control: a shareholder (individual, family, state, another firm, mutual fund) with over 20% voting rights.



Overview

- Findings:
  1. Controlled firms represent around 42% of market capitalization. Among controlled firms, individuals and governments account for 60% of the market capitalization (equally distributed).
  2. In terms of nationality:
     - Domestic (UO)-Domestic (IMM) is the most frequent form of control (72%).
     - Foreign (UO) - Foreign (IMM) represents 10%.
     - Tax havens (UO) involved in 11% of market cap or firms of either domestic or foreign (IMM).
  3. Empirical results: International corporate control is more prevalent in **common law** countries; **Corruption** is negatively related to foreign ownership and control; **Taxes** are only weakly related to cross-border ownership and control (foreign investors often bypass using tax code provisions or incorporating in offshore financial centers).

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Official Information of Foreign Investment

- What happens when there are more than one owner with 20% control? How is control allocated? Are there instances in which the full ownership structure of the firm is unknown?(i.e., stakes do not add up to 100)
- Use 10% threshold for control instead of a 20% threshold → possible to compare to aggregate official data on international capital flows.
- Official source for total FDI: **IMF-Balance of Payments Statistics** (flows and stocks)
- Official sources on <u>bilateral</u> foreign investment:
    - **Coordinated Portfolio Investment Surveys (CPIS)**: Bilateral portfolio equity investment positions (less than 10% of ownership stake).
    - **OECD International Direct Investment Database**: Bilateral foreign investment positions (more than 10% of ownership stake in general, sometimes majority).
        - **OECD BMD4** framework distinguishes between direct investment, ultimate investment and SPEs.

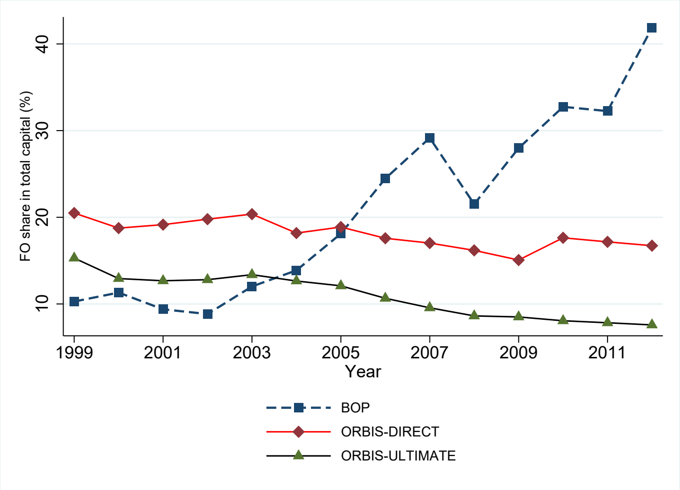
OECD BMD4 Framework

- Complex corporate ownership structures often involve the use of special purpose entities (SPEs) to channel investments through several countries before reaching their final destinations.
- SPEs can distort foreign direct investment (FDI) statistics:
  - A country hosting a significant number of SPEs can appear as receiving investment from countries whose investors are just passing capital through SPEs.
  - Likewise, it can appear that investors from this country are investing abroad when that investment really reflects the funds that have been passed through.
- To address these issues, the OECD developed the 4th edition of its Benchmark Definition of Foreign Direct Investment (BMD4): countries should compile FDI statistics separately for SPEs and non-SPEs.

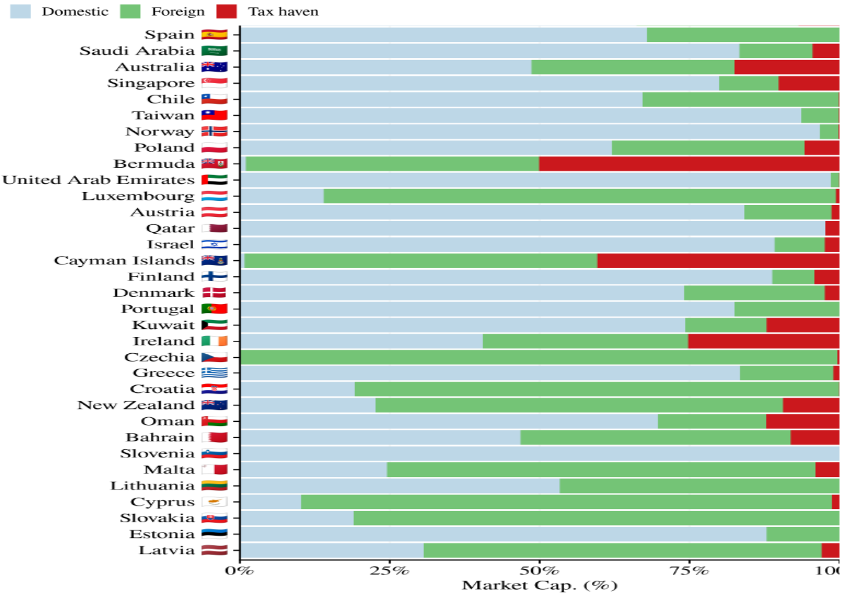
- The comparison to official sources will serve two purposes:
  - External validation of the exercise.
  - Further highlight the contribution $\rightarrow$ since very different results if one were to use official BoP data vs firm level.

Euro Area BoP compared to Direct and Ultimate Ownership

- Source: Kalemli-Ozcan, Sorensen, Villegas-Sanchez and Volosovych, 2018, "Who Owns Europe's Firms? Foreign Investment in Europe and Implications for Risk Sharing"



Nationality of UO (Aminadav, Fonseca and Papaioannou (2021))

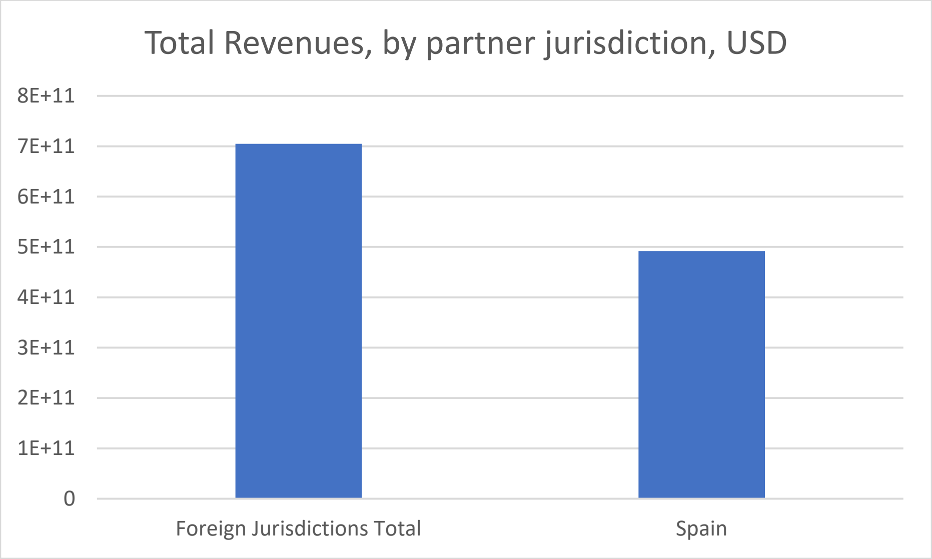


OECD BEPS Project

- Under BEPS Action 13, all large multinational enterprises (MNEs) are required to prepare a country-by-country (CbC) report with aggregate data on the global allocation of income, profit, taxes paid and economic activity among tax jurisdictions in which it operates.
- Country by Country Reporting (CbCR) applies to multinational companies (MNCs) with a combined revenue of euros 750 million or more.
- This CbC report is shared with tax administrations in these jurisdictions, for use in high level transfer pricing and BEPS risk assessments.

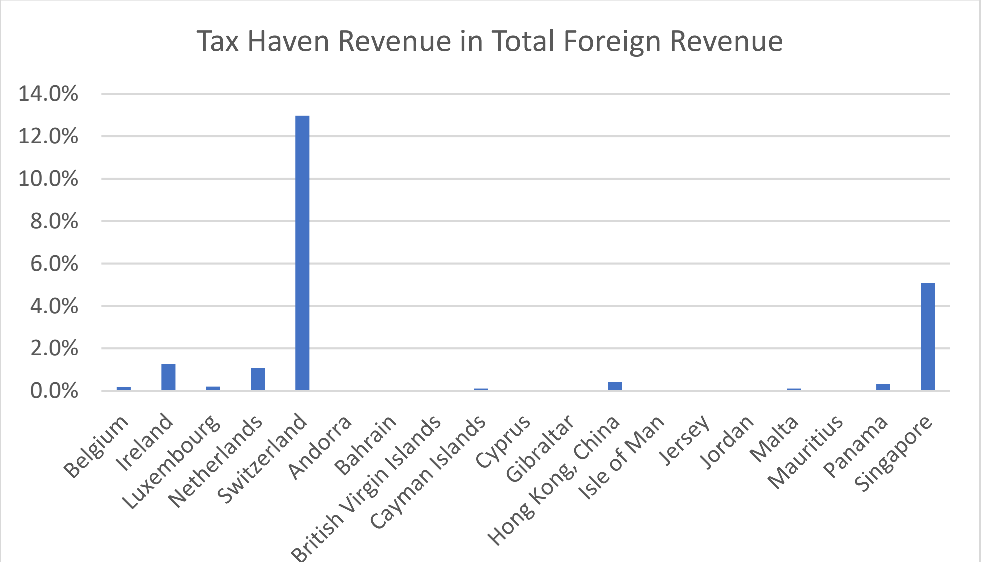
OECD - BEPS project

- Ultimate jurisdiction Spain: Spain's MNCs report more revenues abroad.



OECD - BEPS project

- Of all foreign revenue, 26% is reported in tax haven countries.



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Complex Hierarchies to identify the use of Tax Havens

- Most countries have tax incentives in certain regions (Domestic - Tax Haven (i.e., Delaware) or financial vehicles that allow for low tax rates (i.e., SICAVs in Spain)
- SICAV is a collective investment scheme common in Western Europe, especially Luxembourg, Switzerland, Italy, Spain, Belgium, Malta, France, and the Czech Republic. SICAV is an acronym in French for société d'investissement à capital variable, which can be translated as "investment company with variable capital".

Complex Hierarchies to identify the use of Tax Havens

- Sicavs in Spain are subject to 1% tax rate vs the general 25% corporate rate.

Drop driven by potential change in regulation, many changing incorporation to Luxembourg.

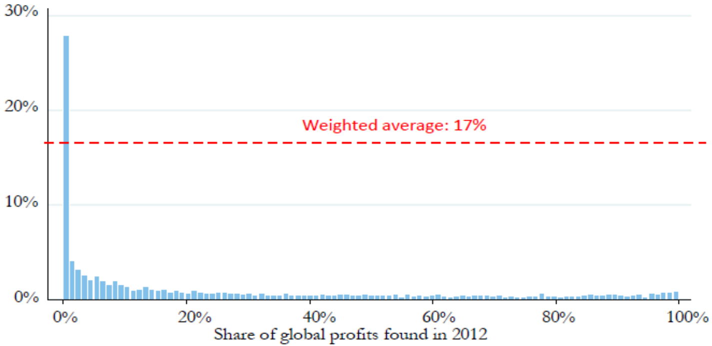
Complex Hierarchies to identify the use of Tax Havens

- Why is this important in the context of the current paper?
- The ultimate owner might be classified as NON-Tax Haven however:
  - The domestic tax treatment of these firms close to that of a foreign tax-haven.
  - The UO will show-up as domestic owner and will not be classified as foreign tax haven even if incorporated abroad.

Complex Hierarchies to identify the use of Tax Havens

- Tørsløv, Wier and Zucman (2021) "The Missing Profits of Nations"
- Orbis relies on information in public business registries. However, in many countries public registries either do not exist (e.g., Bermuda), or contain no income information (e.g., United States, Switzerland).

Figure 1: Fraction of Global Profits That Can be Observed in Orbis



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Empirical Results

- Controls included one at a time, but interesting to explore conditional correlations.
- Expanding the time series to improve identification.
- Exploit bilateral information.
- Are there differences across sectors? 30% of corporate control in the hands of governments, we would expect different results in heavily regulated markets.
- Can the data be used to shed light on cross-ownership evidence?

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- Very careful treatment of firm level data that documents trends in global corporate ownership.
- Nicely explained and documented with concrete examples of how different types of ownership are treated.
- Important contribution to our understanding of the determinants of global corporate ownership control.