FOUR CASES OF TAX OPTIMIZATION – CAN REVISED IFRS CHANGE THEM?

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DECLARATION

I hereby declare that no portion of the work referred to in this thesis has been submitted in support of an application for another degree, or qualification thereof, or for any other university or institute of learning.

I declare that this thesis is my independent work. All sources and literature are cited and included.

I also hereby acknowledge that my thesis will be made publicly available pursuant to Section 47b of Act No. 552/2005 Coll. and AAU’s internal regulations.

Yuliya Andreeva ______________________

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ABSTRACT

The thesis investigates the topic of tax avoidance and the impact which revised IFRS may have on the implementation of tax avoidance practices by companies. The author provides an overview of the key theoretical aspects related to tax avoidance, and explains the legal and ethical sides of corporate tax avoidance practices. Based on the case studies of major transnational corporations such as Apple, Google, Amazon, and Starbucks, the author explains how tax avoidance can be used by companies with the aim of minimizing their tax payments, and reveals the potential consequences of such activities. Based on the findings of the research, the author provides recommendations for revisions to IFRS in order to minimize the volume of international tax avoidance. The thesis should be of interest to researchers dealing with the topic of tax avoidance and its different aspects.

KEYWORDS:

Amazon, Apple, financial reporting, Google, IFRS, Starbucks, tax, tax avoidance, tax evasion, tax optimization.

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1 INTRODUCTION

Taxes have been playing a key role in the effective operation of any country's economy since as the ancient time, constituting one of the main sources of state budget proceeds. All economic entities or agents running their economic activities are liable to pay taxes to the state, and this means that their direct profits are decreased.

As a result, companies might seek way to reduce the tax burden borne, and may use tax optimization or avoidance schemes with this aim. Such schemes are beneficial to economic agents, but bring major harm to the state through lower tax proceeds.

International Financial Reporting Standards commonly referred to as IFRS are destined specifically to provide all economic agents around the globe with common grounds for the maintenance of their accounting procedures and preparation of financial statements. The adoption of IFRS in the national practice of individual jurisdictions allows eliminating the existing differences in different states' national accounting systems, and thus allows for the better comprehension between counterparties in international cooperation.

Taking into consideration the progressively growing adoption of IFRS as the financial reporting system around the globe, the issue of IFRS in the accounting and financial reporting practice of companies is particularly important and relevant as of today, and thus deserves particular attention in theoretical and empirical research. Moreover, the application of IFRS is particularly important in the context of tax regulation and the activities of tax authorities.

In this thesis, one particular aspect of the revised and up-to-date version of IFRS will be investigated, namely the treatment of tax optimization based on the case studies of particular companies.

The relevance of the chosen topic as of today can be explained by the fact that the tax optimization schemes used by major corporations may be compliant with the legislation and international regulations, but may be unethical. Therefore, it is important to investigate how the revised IFRS standards can address the ethical issues of the aforesaid tax optimization and tax avoidance activities.

The main aim of the thesis is to reveal how revised IFRS could affect tax optimization or avoidance, and what consequences they could have for commercial entities.

The goals of the thesis are to investigate the key theoretical aspects related to the definition of tax and taxation systems, tasks and functions of taxes, types of taxes, etc.; to analyse the definition of tax optimization and avoidance and to asses the role of those phenomena for the national economy; to investigate the different schemes and methods of tax optimization and tax avoidance; to analyse the case studies of four companies running their tax optimization activities; to reveal how the revised IFRS might affect the aforesaid companies' business activities; to discuss the findings of the thesis and to draw comprehensive conclusions on the impact of the revised IFRS on tax optimization and tax avoidance activities.

Different bibliographic sources will be used for writing this thesis, namely scientific research publications and articles, sources available in the Internet, official publications and explanations of the International Accounting Standards Board, etc. Among other publications, the following bibliographic sources will be investigated: De Broe, L. (2008). *International tax planning and prevention of abuse*; Brown, K. (2012). *A comparative look at regulation of corporate tax avoidance*; Cordes, J., Ebel, R. and Gravelle, J. (2005). *The encyclopedia of taxation & tax policy*; McGee, R. (2004). *The philosophy of taxation and public finance*; Murray, R. (2012). *Tax avoidance*; etc.

The methods used for writing this thesis will include theoretical overview (for the investigation of the key theoretical aspects related to taxes and taxation systems, the different types of tax optimization and tax avoidance tools and methods, their role for the national economy, etc.), case study (for the empirical analysis of the practical cases of companies which have performed tax optimization activities in the course of their business practices), modeling (for investigating the impact which revised IFRS might have on the tax optimization or avoidance practices of the companies investigated within the case study), and deductive thinking (for drawing conclusions in line with the research topic).

The findings of this thesis should explain the role of the revised IFRS in the current business practice of companies, namely in the field of taxation and tax optimization, and should also provide grounds for the subsequent research of this topic.

2 THEORETICAL PART

2.1 Definition of tax and taxation systems

When proceeding to the investigation of taxes and taxation, it is first of all worth understanding the definition of tax. Although there might be different definitions of tax in the bibliographic sources and the legislative practice in different countries, the general commonly used definition of taxation states that tax is "*a compulsory levy made by public authorities for which nothing is received directly in return*" (Lymer and Hasseldine 2002, p. 2). Therefore, based on the above definition, it can be stated that any tax is a levy which the public authorities impose on individuals and corporations with the aim of obtaining funds to be subsequently invested in the performance of public functions and needs.

Any tax has its inherent characteristics and features which shape the role played by taxes in the existence of any states. Thus, the main features of taxes are as follows:

- mandatory nature. Taxes are inherently mandatory, and therefore the companies and individuals subject to pay taxes are not allowed to refuse any such payment, and moreover, are legally prosecuted for the non-fulfillment of their tax liabilities;
- change in the form of income ownership. When taxation procedures are implemented, part of income generated by the respective economic agent becomes the property of the state without any compensation. Such amounts are the state's budget proceeds which the government may use for the performance of its public functions;
- irreversibility. Taxes are not returned to the individuals or entities on which they are imposed;
- legitimacy. This characteristic means not only that taxes are collected under the legislation in force in the respective states, but also that taxes are collected only from legitimate operations and transactions (Hildreth and Richardson 1999, pp. 5-7).

Tax systems can be defined as sets of regulations, standards and tools which shape the imposition and charging of taxes in the respective jurisdictions, and which shape the existence of taxation bodies responsible for such activities (Lymer and Hasseldine 2002, p. 3). The choice of the particular tax system and the creation of conditions under which the tools and mechanisms used within it would generate the greatest benefits for the state belong to the direct responsibility of the government. Furthermore, it should be understood that no state can operate without charging taxes, and therefore the effectiveness of the taxation system chosen preconditions directly how effectively the respective state is able to perform its tasks and functions not only in the long-term perspective, but also in the context of daily activities (Ibáñez and Martinez-Vazquez 2011., pp. 1-2).

Taking into account the above facts, it can be stated that taxes play an essential role in the operation of the entire economic system formed within any particular state. Historically, taxes have been known to humanity since the ancient times. As confirmed by available historical sources, taxes were used in Ancient Egypt at least in 3000 BC, and since then, they have been rapidly spreading around the globe and changing in form. If initially, taxes used to be collected mostly in natural form, with the development of money and credit relations, countries started implementing more developed taxation systems which became the prototypes of the modern taxation systems used as of today (Blankson 2007, pp. 1-3).

The social and economic nature of taxes can be explained through the set of relationships which emerge between the state and the economic actors within it in terms of taxation. Thus, as any tax assumes that the government takes a portion of income from the residents for the purpose of ensuring the fulfillment of its public functions, such actions can be deemed unilateral expropriation of funds. In order to perform taxation, the government of any state acts under the legislation in force and evaluates the taxation base, i.e. the respective amounts subject to taxation. For instance, when speaking of the income tax or corporate profit tax, the taxation base will be the entire amount of taxable income or corporate profit, respectively. Thereafter, the tax rate established by the state is applied. Such tax rate may be stipulated in the legislation either in the form of percent to be paid to the state budget or in the form of lump sum. The multiplication of the tax base by the tax rate gives the ultimate amount which the respective individual or corporate is liable to pay to the state as compulsory tax (Arnold 2008, pp. 235-236).

Due to the fact that by performing taxation procedures the state in fact expropriates part of economic actors' income, discussions may exist on whether such actions on the part of the state are justified from the economic perspective, and part of the economic agents may seek ways not to pay their taxes for maximizing their profits. In this case, the state should find the optimum level of tax rates at which the population and the corporate sector would bring the greatest amounts of income to the state budget. Excessive decrease in the rates of taxes might lead to smaller benefits for the state budget, while excessively raised tax rates might lead to the growth of the shadow sector of the national economy, and thus to the budget's deprivation of a major part of its proceeds (Gwartney 2009, p. 100).

Thus, the operation of an effective taxation system is a key precondition for the effective development of any state. Therefore, it is worth investigating more in detail the mechanisms through which taxes contribute to the development of the national economy and the social sector. In the next chapter of the thesis, the tasks and functions of taxes will be investigated more in detail.

2.2 Tasks and functions of taxes

Due to the complex nature of tasks and their essential role in the provision of the effective operation of any country's national economy and social sector, taxes perform a number of different tasks and functions which of which is destined to ensure the fulfilment of particular tasks and goals of state government.

The main functions of taxes are as follows:

1. Fiscal function

The fiscal function of taxes is inherent of any taxes due to their very nature. Thus, the fiscal function of taxes consists in the fact that they ensure the opportunity for any state to exist. In practice, public financial resources are formed through the charging of taxes from individuals and corporations. Such financial flows are directed to the state budget, and under the governmental policies adopted in the field of public administration, decisions are made on how the respective funds should be re-distributed and how they should be used for achieving the best results for the state in financial terms. However, the fiscal function of taxes is not limited only to the effective performance of national budgets, and is broader, ensuring the effective operation of the entire public government apparatus (Hansen 1999, p. 77).

Taking into account the specificities of the fiscal function of taxes, it should be understood that it has some inherent limitations. For instance, in case that the level of tax proceeds to the state budget is insufficient for covering the existing expenditures or the planned public programs, the state is forced to seek other ways to replenish the budget, for instance by raising loans from international organizations, foreign countries or domestic economic agents. In order to service such debts (i.e. to pay interest on them), the government might be forced to increase taxes for raising budget proceeds, but this may induce lower payments by economic agents, and thus growth of the shadow economy. Therefore, this testifies that any government should be able to oversee effectively its activities, and thus to develop its fiscal policies so that the expenditures to be made would match the existing resources (Pickhardt and Prinz 2012, pp. 3-6).

2. Regulatory function

The regulatory function of taxes plays a particularly prominent role as of today, taking into account the growing level of turbulence of the international market under the impact of globalization, and thus the high risks of occurrence of international crises. The regulatory function consists in the time, geographic and sectoral re-distribution of the population's income. Thus, the funds collected by the state to its budget in the form of taxes are used by the government in order not only to regulate the activities of the different economic branches or to ensure the public functions of state administration. In addition to this, it also allows regulating the income of different population groups.

The state may use a developed system of taxation for the purpose of varying the ultimate tax burden borne by various groups of the population. For instance, with this aim, different tax rates can be applied to individuals and corporations depending on their level of income or depending on the products they manufacture or sell, etc. Moreover, the government may also provide tax privileges to different groups of the population, and so on. All this is destined to ensure the effective regulation of the national economy and to achieve the results sought by the state in its activities. Tax credits and tax discounts may be other tools used by the state in the context of its tax regulation. Therefore, the regulation function of taxes has its greatest consequences not only in the field of production, but also in the context of the regulation of consumers' purchasing power in the market (Cullis and Jones 2009, pp. 53-55).

3. Social function

The social function of taxes is tightly interconnected with the two previous functions, as it is associated with the government's provisions of sufficient and favourable living conditions for the entire population of the respective state. Namely, in the first turn, the fulfilment of the social function of taxes is associated with the government's provisions of subsidies, aid and assistance to the poorest layers of the population. On the one hand, the state may establish basic tax exemption, so that individuals with earnings below a particular level would not be liable to pay any contributions to the state budget. On the other hand, the state operates system of social provisions and privileges which it redistributes among the population using the tax collection mechanisms within the existing taxation system.

The role of the social function of taxes becomes particularly important in the conditions of crises where the least wealthy population suffers most due to the negative economic conjuncture and negative tendencies in the national economy. The effectiveness of the performance of the social function preconditions to a large extent the state's ability to ensure the even development of society across all population groups and layers (Andersson et al. 2007, p. 73).

4. Control function

The control function of taxes ensures all economic agents' compliance with the regulatory requirements of the national legislation and the compliance with the existing price proportions formed under the impact of market demand and market supply, with the involvement of the government's regulation. Through the process of collection and re-distribution of part of the population's and the corporate sector's income, the government ensures not only the effective fulfilment of its public functions and thus the needs of the state, but also the supervision of and control over the activities of each and every economic agent. Through this function, the state may ensure the greatest transparency of the government's activities in all sectors, and at the same time the greatest transparency in the relationships between the state and all residents running their activities, and the application of similar control and supervision to all economic agents makes them comply with the legislative and regulatory framework existing within the state (Khakhonova 2013, pp. 160-161).

5. Other functions

In the scientific literature, other functions of taxes can be classified. For instance, such functions may include the containment of inflationary growth (through the limitation of prices in the economy and limitation of the population's income under balanced GDP composition and growth), antimonopoly function (through the charging of greater taxes from companies gaining greater market shares leading to the uneven market competition), and so on (Paul et al. 2006, p. 12).

Taking into account the above functions of taxes, it can be stated that taxes perform the following main tasks:

- replenishment of the state budget with income, which is a key task on the way to the government's opportunity to ensure the full-fledged fulfilment of the population's and national economy's needs;
- re-distribution of national income with the aim of ensuring the effective development of all population groups;
- creation of equitable conditions for all economic agents within the states to run their activities;
- achievement of the greatest transparency and legitimacy in all operations and transactions run within the state;
- control over all economic processes within the states;
- containment of inflationary growth;
- prevention of monopolist tendencies;

- stimulation of economic activities;
- formation of effective international economic cooperation, etc. (Pickhardt and Prinz 2012, pp. 3-6).

Therefore, it can be stated that taxes play an important role in the effective operation of the national economy in all respects, far beyond the simple replenishment of the budget with tax proceeds. Using the system of taxation, the government puts all economic agents operating within the state in the same equitable conditions in which everyone would operate in a legitimate way, and would be able to comply with the existing tax legislation on the same conditions as the other economic agents. Moreover, taxes are indispensable for any state to get the opportunity to ensure the even development of its society, namely in the context of the re-distribution of the existing financial flows with the aim of ensuring the high standards of living of all population groups, including the least wealthy ones.

Taking into consideration the aforesaid essential role of taxes and the functions performed by them in the national economy and in society in general, in the next chapter of the thesis, the different types of taxes will be investigated more in detail.

2.3 Types of taxes

When investigating the different types and forms of taxes, it should be understood that although all taxation systems are similar in terms of the functions they perform and the tasks they fulfil, all such taxation systems may use the different forms of taxes, tax rates, specificities of their application, and so on. All this is preconditioned by the particular economic conditions existing in the respective state on the one hand and by the economic policies adopted by the respective state's government on the other hand. Conditionally, all tax systems can be divided into two main types: schedule and global. Under global tax systems, all taxes are charged from the respective jurisdiction's economic agents on the same conditions, while under the schedule system, the entire population is divided into groups called schedules, and different tax conditions thereafter apply to each such different schedule with the aim of achieving the most positive financial result for the state (Ault et al. 2010, p. 198).

Proceeding to the classification of taxes, it can be stated that there might be a great variety of approaches in the scientific literature and economic practice of states to the classification of taxes. Such differences in the classification of taxes may be preconditioned by the specificities of the respective researcher's approach to the investigation of the underlying issues, the particular aspects of taxes analysed and so on.

Taking into account the aforesaid, it can be stated that the main classifications of taxes are as follows:

1. By form of charging:

- direct taxes. Such taxes are charged directly from the source of income or from the respective property. For instance, such taxes include the individual income tax, corporate profit tax, property tax, and so on. The key distinction of direct taxes is the fact that they are paid by the respective economic agents directly using their own funds, and the amount of such taxes to be paid is preconditioned directly by the amount of the respective gains (in either financial or any other material form) earned by the respective individual or entity;
- indirect taxes. Such taxes are contrary to direct taxes due to the fact that they are charged in the form of extra charges or additions to the respective price or tariff. This means that, in contrast to direct taxes where the taxpayer pays them from his own gains, the ultimate payer of indirect taxes is the consumer. This is due to the fact that indirect taxes are added to the ultimate value of the product by the manufacturer or seller, so that the consumer purchasing such products or services already pays the amount of the indirect tax which is thereafter transferred to the state budget under the regulations in force. Namely, indirect taxes include the value added tax, excise taxes, customs duties, and so on (Creedy 1999, p. 100).

2. By type of impact:

- proportional taxes. The rates applied to such taxes are proportional, which means that the same percentage or amount of taxes is charged from the respective income or property, regardless of the financial value of such income or property. This means that all individuals or corporations pay the same amount of taxes, regardless of their level of wealth, social status, gains, and so on;
- progressive taxes. For this type of taxes, an inherent feature is the growing tax rates with the growing amount of income or any other material proceeds. The application of progressive tax rates might be appropriate in the case where the government seeks charging greater funds from wealthier persons or greater corporations, so that the abovementioned income charged to the state budget in the form of taxes would be subsequently re-distributed for the sake of the rest of the population. Each government may develop its own scale of the application of progressive tax rates depending on the particular economic situation and the economic policies implemented;
- regressive taxes. In contrast to progressive taxes, regressive tax rates assume that the rates of taxes drop with the growing value of the tax base. For instance, when speaking of the income tax, it can be stated that individuals or corporations earning particular amounts of funds are liable to pay less, if they start earning more. This option might be used by the state, when there is a need to stimulate the economic activities of its residents and to boost the growth of the national economy, as economic agents might be interested in raising the scope of their activities in order to be charged smaller amounts of taxes (Bardes et al. 2010, p. 511).

3. By type of economic agent:

- taxes charged from individuals. Taxes of this type are charged from individuals, and aren't applicable to corporate entities. For instance, the most widely spread type of taxes charged from individual is the individual income tax which assumes that each person gaining a certain amount of earnings through his or her professional activities is liable to pay a portion of such income to the state budget in the form of taxes. It should also be noted here that the state may establish basic exemption for the population below which the individuals aren't liable to pay taxes at all. This may be done with the aim of ensuring the minimum standards of living for the poorest part of the population, in order to ensure the even and effective development of society in all respects;

- taxes charged from entities. In addition to charging taxes from the population, the state also charges taxes from the corporate sector, as entities are among the main contributors to the state budget. The taxes charged from the corporations are more varied. For instance, the government charges the corporate profit tax from the profits generated by entities. In addition, manufacturers and service providers are liable to pay the value added tax which is an indirect tax charged from the value added to the products through processing. Companies working with products such as cigarettes, alcohol, petrol, and so on, are liable to pay excises which are included in the prices of the respective products as indirect taxes. In addition, companies pay payroll taxes from the salaries and wages provided to their employees, and pay contributions to the Pension Fund and other social funds existing in the state (Block 2004, pp. 3-6);

4. By aim of taxation:

- general-purpose taxes. General-purpose taxes include taxes which are collected by the state to the state budget without fixing the precise direction of the subsequent expenditures. For instance, such taxes include the individual income tax and corporate profit tax. The funds collected by the state to the budget through such taxation are thereafter re-distributed by the government within the framework of its existing policies, and may be directed do different public functions. For instance, such funds may be directed to healthcare, education, military, energy sector, and so on, and the source and direction of use of such funds aren't in any way regulated in legislative terms within that context;
- special taxes. In contrast to general-purpose taxes, the directions of use of special taxes collected to the state budget are regulated in the legislation in force, and

therefore the government collects such taxes from the population and the corporate sector for funding particular vectors of its public expenses. For instance, such special taxes include the contributions to social funds by both the population and the corporations. Such funds are thereafter used for the payment of retirement benefits and other similar work benefits to the employees. Such taxes collected within special funds cannot be directed to any other expenses (Bardes et al. 2010, p. 511).

5. By object of taxation:

- property taxes. Property taxes are charged from the respective individual's or entity's property available to them, for instance, such as buildings, premises. Such taxes are collected directly from the respective tax agent based on the area of the respective property in his ownership. Such property tax is calculated on a regular timely basis, most often once a year. The tax rates may vary depending on the area of the respective property in line with the taxation system in force in the respective country;
- resource taxes. Resource taxes are rental payments which companies pay for their use of national resources. Such rental payments are collected from companies involved in the operations with oil, natural gas, gold, diamonds, and any other important natural resources. For the state, collecting resource taxes is an opportunity to get the just and sufficient compensation for the use of its national resources by the economic agents;
- income taxes. Incomes taxes have been described in detail earlier in this chapter. They are charged directly from the income source, and are collected from both the population's and the corporate sector's earnings;
- consumption taxes. Consumption taxes are indirect taxes which are paid directly by consumers. Such taxes include VAT, excise taxes, and so on (Creedy 1999, p. 100).

6. By level of budget

- federal taxes. Federal taxes are collected on the state level and are directed to the state budget. Such taxes are used by the state directly for funding the existing government programs and for ensuring the effective operation of the state apparatus;
- regional taxes. Regional, land and other similar taxes exist in countries with federative systems, and are destined to ensure the regions' ability to effectively fund their particular development vectors, and allow expanding the opportunities of the regional authorities. This may be more effective, as the central government may not be always totally aware of the particular needs of the regions, and therefore may distribute funds rather ineffectively on the regional level;
- municipal or local taxes. Municipal or local taxes are collected on the local level, and are directed to the budgets of the respective cities, communities or villages. Their main aim is to ensure the effective funding of city development programs in line with the needs and preferences of the local population. It should also be noted here that the government may leave part of the state taxes collected from the population on the regional or local level, so that the local communities would benefit from the most effective choice of the development programs to be implemented (Raabe 2012, p. 288).

Therefore, it can be stated that there are a great number of taxes which government may apply within the framework of its fiscal policies, and the entirety of such taxes existing within the framework of the respective taxation system preconditions the actual tax burden borne by the jurisdiction's population and corporate sector. The ultimate tax burden in its turn predefines the economic benefits which an economic agent might generate in the long turn through his activities. Therefore, in case that the tax burden is excessive for an economic agent, or that the economic conditions in the respective state are unfavorable, such economic agent might seek avoiding taxes by means of transferring his activities to other countries, or seek evading taxation using either legal loopholes in the legislation or illegal activities within the shadow economy.

In the next chapter of the research, tax optimization and tax avoidance will be investigated more in detail.

2.4 Theoretical overview of tax optimization and tax avoidance

When investigating the issues of tax avoidance, it is worth clearly understanding the methodological differences in the construction of the terms tax optimization, tax avoidance, and tax evasion, as their construction preconditions the respective regulatory consequences applied to the companies running the respective activities.

Tax avoidance can be constructed as "*an act of dodging tax without breaking the law. It means when a taxpayer arranges his financial activities in such manner that although it is within the four corners of tax law and takes advantage of loopholes which exists in the tax law for reduction of tax liability"* (Agrawal 2008, p. 5). According to Hoffman (2008, p. 45), tax avoidance "*is merely tax minimization through legal techniques. In this sense, tax avoidance becomes the proper objective of all tax planning.*"

Therefore, based on the definitions above, it can be stated that tax avoidance involves legal techniques that companies may use for the purpose of reducing their ultimate tax burden, and thus for preserving the amount of their earnings generated through commercial business activities. From the legal point of view, tax avoidance doesn't imply any legislative consequences for the respective companies involved, and it is based on the use of the loopholes or drawbacks existing in the national or international legislation which allow companies benefiting from different channels and tools for minimizing their tax expenses.

Tax optimization should be understood as "*a very popular way of cost saving… Tax optimization and tax planning are not "forbidden terms" at all*" (Valinurova 2013, p. 102). Therefore, it can be stated that the term tax optimization is identical to tax avoidance, and they may be used equally for designating the same economic phenomena and activities run by corporations. Tax optimization is therefore totally legal, and companies resorting to tax optimization perform such activities within the framework of their tax planning and budgeting procedures, and do not imply any negative consequences for corporations, as no regulations are violated.

Tax evasion can be constructed as the "*general term for efforts by individuals, firms, trusts and other entities to evade taxes by illegal means. Tax evasion usually entails taxpayers deliberately misrepresenting or concealing the true state of their affairs to the tax authorities to reduce their tax liability, and includes, in particular, dishonest tax reporting (such as declaring less income, profits or gains than actually earned; or overstating deductions). Any illegal method which leads to reduction of tax liability is known as tax evasion*" (Agrawal 2008, p. 6).

Therefore, based on the definitions given above, it can be stated that tax evasion is contrary to tax avoidance and tax optimization, as it implies different aims and goals pursued by companies within the framework of their activities in the field of taxation, and also implies different consequences borne by companies as a result of the aforesaid activities. Namely, while tax optimization and tax avoidance are legal under the regulations in force, tax evasion is inherently illegal, as companies resorting to tax evasion violate the legislation of the respective country or international regulations or arrangements.

The differences between tax avoidance or tax optimization and tax evasion can be generalized as follows: on the one hand, the use of tax optimization or tax avoidance is inherently legal (which means that companies running such activities benefit from the existing loopholes in the legislation, and do not undertake any unlawful activities) while tax evasion is inherently illegal (companies use unfair means for running such activities, and thus violate the legislation in force, and are prosecuted), and on the other hand, tax avoidance or optimization activities are performed before a tax liability arises (which means that such activities exist in the form of tax planning, and assume the respective company's forecasting of its subsequent economic activities, and thus use of options to achieve the most effective cost optimization), while tax evasion most often occurs after a particular tax liability arises, and takes the form of tax fraud (Agrawal 2006, p. 9).

From the economic point of view, it should be noted that both tax evasion and tax optimization/avoidance imply negative consequences for the state due to the fact that, regardless of the legitimacy of any such activities, they lead to the contraction of budget proceeds through taxation. Therefore, the reduction in the tax proceeds generated by the state leads to reduced opportunities for the government to fund public development programs.

However, while tax optimization leads to negative consequences for the state only in the context of decreased budget proceeds, the scope of negative consequences associated with tax evasion is much broader. Namely, in addition to negative financial effects, tax evasion brings the following negative consequences:

- tax evasion promotes rise in the respective jurisdiction's shadow economy. This means that the transparency of economic operations and transactions within the state gets impaired, and as a result, the black market of the respective state tends to grow. As a result of the growing black market, inflationary pressures within the state tend to rise, and this leads to the subsequent negative consequences for the national economy in the context of the decreased value of the national economy, the population's impaired purchasing power, and the overall decreasing standards of the population's living;
- social dissatisfaction. The high level of social dissatisfaction as a result of tax evasion may induce the fact that fair taxpayers complying with the legislation in force in the respective jurisdiction (including both individuals and corporate entities) would be dissatisfied with the growing level of tax burden as a result of the state's contracted budget proceeds. Therefore, the may require the state to change its tax policies, and such conflict between the state and the population might lead to major negative consequences in terms of both the state's image and the social situation in it;
- hidden loss to society due to the great scope of legal disputes. The tax evasion activities performed by companies may require the government to undertake a number of difficult legal procedures to return the funds illegally withdrawn from the respective state to the budget. This means the use of part of the respective state's intellectual potential for the achievement of those goals, and thus losses associated with the potential alternative applications of the aforesaid human potential (Agrawal 2008, pp. 6-7).

Although companies may use their tax avoidance and tax evasion practices in all countries around the globe, according to the tendencies currently persisting in the international economy, it can be stated that the scope of such activities is broader in developing countries. This is preconditioned by several key facts. Namely, in developed states, the legislation governing the field of taxation is more developed, and the legislation governing the business activities of economic agents is more fair and transparent, thus ensuring the equitable conditions for all individuals and corporate entities in the respective jurisdiction. At the same time, the favourable conditions of doing business in developed countries may be more advantageous to companies as compared to lower tax burden, and therefore such corporations may opt toward running their activities in such countries and paying greater taxes, instead of moving their activities to other jurisdictions where the respective risks incurred might be significantly greater (Mo 2003, pp. 1-2).

Often, tax optimization or avoidance and tax evasion activities can be hard to track and monitor on the level of the government, and can be hard to identify unambiguously. The main way to distinguish tax optimization/avoidance from tax evasion is the concealment or non-disclosure of information on the use of the respective mechanisms on the one hand, and the use of purely unlawful practices on the other hand. However, due to the sophisticated nature of the tax optimization tools and methods currently available to corporations, such corporations may use the respective activities in a way to effectively hide them from the government, and therefore the state needs to use effective mechanisms and special services in order to reveal such cases and to eliminate them. Also, it should be understood that the state is interested in eliminating or reducing not only illegal tax evasion, but also legal tax avoidance activities, with the aim of raising budget proceeds. In contrast to tax evasion which is criminally prosecuted, tax avoidance can be reduce or limited using only the mechanisms of effective public governance, and the creation of the fair market economy in the respective jurisdiction (Mo 2003, pp. 2-3).

Therefore, it can be stated that tax avoidance/optimization and tax evasion activities play an essential role for any national economy, and may significantly affect the effectiveness of the respective government’s public activities. At the same time, tax optimization and tax evasion play an essential role for the corporate sector, as such activities may contribute to the maximization of the financial results generated through business activities.

In the next chapter of the research, the different types and methods of tax optimization will be analysed more in detail.

2.5 Types and methods of tax optimization

Taking into account the importance of tax optimization in corporate activities, it should be understood that such tax optimization schemes are widely used in the business practice of corporate entities. Therefore, companies tend to use such schemes very extensively in their business activities, and there are a wide variety of tools and mechanisms which allow them benefiting from the lower tax burden borne. Such main types and methods of tax optimization are as follows:

1. Use of legal loopholes

Under this type of tax optimization, a key task of the respective company is to analyse thoroughly the legislation in force, namely as applied to its taxation, and to reveal where legal options exist to avoid such taxation. Under this method, companies may find options to optimize their tax burden using different mechanisms such as change in the form of ownership, registration of companies in other jurisdictions for the more complex transfer operations, and so on. All such operations are required to be legal, and to be based only on the existing loopholes which the legislation fails to take into account. The main advantage of this method is its legality, and the opportunity to effectively reduce corporate taxes without the performance of any risky activities. However, its major drawbacks are the fact that it requires significant financial and time expenditures for the analysis of the legislation in force on the one hand, and the fact that the state constantly seeks eliminating such existing loopholes, and therefore their use might often bring only short-term positive effects to the respective companies seeking optimizing their taxation (Agrawal 2008, p. 5).

2. Identification of errors in corporate activities and their elimination

An option to achieve tax optimization is to ensure the effective monitoring and identification of the respective company's errors and omissions in its activities. For instance, major errors which might lead to excessive taxation might be managerial errors such as the failure to make a timely application for tax privileges, failure to use the opportunities provided by the state (transfer of operations to free economic zones within the country, tax privileges for innovations, and so on), etc. Therefore, companies might improve their taxation simply by improving their operational activities and managerial practices as regards taxation.

3. Choice of organizational form

Companies may benefit from the optimum tax regime applied to them by means of choosing the right organizational form. For instance, in some cases, companies might benefit from being registered as a limited liability company or a joint-stock company, partnership, and so on. Moreover, some companies may conclude agreements with their employees as individual entrepreneurs, and provide services to their customers on the part of such individual entrepreneurs, which might allow reducing the aggregate tax burden borne. Also, companies might prefer choosing the scope of their activities in terms of the number of employees hired or the financial results generated: in some cases, companies might be divided with the aim of diminishing their size, and thus for lowering the tax burden borne (Cordes et al. 2005, p. 212).

4. Correct formation of accounting policies

The use of the right accounting policies is one of the key preconditions for the effective achievement of tax optimization. In order to ensure the minimization of the tax burden borne by them, companies need to select the most appropriate accounting system. The optimum selection of the reporting of expenses and income should be used with the aim of achieving the smallest amount of the tax base. Also, the formation of the ultimate tax base is greatly affected by the accounting and reporting of debts, and namely bad debts, depreciation of equipment and property as part of expenses, and so on (Elliott and Elliott 2008, pp. 379-380).

5. Use of offshore tax havens

Offshore tax havens can be seen as jurisdictions at which no taxes are imposed on corporations in association with their business activities, or where the tax rates applied to such companies are extremely low. In order to reduce their income paid to the state under the form of taxes, companies may transfer their activities abroad, or may enter their subsidiaries or parent corporations in such offshore jurisdiction, so that the entire tax base would be diminished. Although the choice of tax jurisdiction most often belongs to the will of the respective company, and therefore doesn't violate any legislative or regulatory norms, tax havens are often used by companies for illegal purposes, namely for money laundering. This is due to the fact that the level of public control over corporate business activities in tax havens is very low, and therefore funds may be concealed there. Therefore, tax havens are often used not only for tax avoidance, but also for tax evasion (Schmitt 2008, pp. 15-17).

6. Lobbying

Lobbying may be an effective way for tax avoidance or optimization for companies having significant political powers or able to affect the decisions of the national authorities due to their scope of economic activities and importance for the respective jurisdiction's national economy. In case that such lobbying activities do not violate the legislation, they might be used as a way to achieve the reduction in taxes for the entire corporate sector, for particular industries, or for particular companies depending on their size, role for the economy or any other important factors whatsoever. However, in most cases, lobbying is associated with unlawful activities, and the lobbying of legislative decisions is performed by major transnational corporations in violation of the existing regulations and rules (Mooij and Nicodème 2014, p. 127).

Thus, it can be stated that the diversity of the types of tax avoidance is quite broad, and therefore companies wishing to optimize the structure of their taxation have a great number of alternatives available. Based on the application of the above types of tax avoidance activities, companies may use different tax avoidance methods or schemes. Among such schemes, the most widely used ones are the following:

1. Double Irish arrangement

Under the double Irish arrangement, a company transfers its intellectual property right to an offshore company established in a jurisdiction abroad. Therefore, the offshore company exploits such intellectual property rights, and isn't liable to pay any taxes in the corporation's jurisdiction of residence. Under this scheme, two companies in Ireland are required for making it viable. At this, one of such companies is tax resident in an offshore tax haven (for instance, such as the Cayman Islands), but holds its management and control bodies in Ireland. The first Irish company obtains the rights transferred from the corporation's jurisdiction of residence. The second company obtains the profits generated outside the corporation's jurisdiction of residence based on the use of its assets. The second Irish company pays royalties or fees to the first Irish company, which fess are tax-deductible. As a result, most of the second Irish company's profit isn't subject to taxation, while only part of it is taxed at the Irish corporate profit tax rate of 12.5%. The payments between the two Irish companies aren't taken into account in the jurisdiction of the company's residence, and thus such corporation achieves the minimization of its tax base (Schroeder and Chester 2013, p. 180).

2. Dutch sandwich

This scheme is very often used together with the double Irish scheme. Using this scheme, a shell company (company used for running business transactions, without having any considerable assets or equity) is established in the Netherlands. Sales revenues (often from the second Irish company, if the double Irish scheme is used first) are directed to such Dutch company, as the Netherlands' tax climate is favourable. The rest of the profits are thereafter transferred to an offshore tax jurisdiction. As a result, the taxation in Ireland is avoided, and the ultimate tax burden is minimized (Schroeder and Chester 2013, p. 180).

3. Bermuda black hole

Under this scheme, corporations may establish a shell company in the Bermuda Island. The intellectual property rights which the corporation has in its jurisdiction of residence are thereafter transferred to such shell company. The profits generated by the company in its jurisdiction of residence are accounted for the Bermuda-based company, and its profits are exempted from tax under the legislation of the Bermuda Islands, which allows avoiding any amounts to be charged from companies' income.

4. Singapore sling

Under this scheme, a corporation establishes a subsidiary in a country with lower tax rates. Thereafter, it sells its products and services to such subsidiary in the abroad jurisdiction. This subsidiary then sells the respective products or services to the end customers. As a result, a lower tax rate applies to corporate profit, and the parent corporation's tax burden is diminished. The name of this scheme is due to the fact that Singapore may often be used as the hub jurisdiction due to its favourable tax regime (Woolrich 2015).

Taking into account the specificities of tax optimization and its different types and methods, in the next chapter of the research, the focus will be put on the investigation of the main legal and ethical aspects associated with tax optimization.

2.6 Tax optimization: legal and ethical aspects

Within the investigation of the legal and ethical aspects related to tax optimization and tax evasion, it is worth differentiating the two terms as described earlier in this research. Namely, while tax evasion is equal to tax fraud, and thus is illegal, tax optimization can be regarded from different perspectives: namely from the legal points of view on the one hand, and from the ethical perspective on the other hand. This means that although tax optimization may be legal, this doesn't necessarily mean that it is ethical. Therefore, it is worth analysing the difference between those two approaches more in detail for understanding the different ways in which tax optimization and tax avoidance can be constructed.

As stated by Thuronyi (1996, p. 45), "most countries recognize the right of the taxpayer to arrange his or her affairs in such a way as to pay less tax… Therefore, in some countries some constructions or transactions that constituted tax avoidance, although not a criminal offense, are not recognized either by the courts, or by general or specific antiabuse provision." Based on those arguments, it can be stated that the nature of tax minimization is inherently legal, where there is no tax fraud. Companies are free to seek their greatest benefits, including in terms of the minimized tax costs, and thus are free to choose their suitable tax jurisdiction with the aim of maximizing their financial performance results.

However, the legality of any tax optimization operations or transactions doesn't necessarily mean their ethicality or morality, which means the aspect of tax avoidance associated with the consequences borne by society.

As for the ethicality of tax avoidance, it should be noted that discussion has long persisted in society on whether such activities should be allowed or not, and on whether they break social moral norms. Therefore, different researchers may adopt different approaches to the investigation of this particular topic. According to McGee (2011, pp. 6-23), taking into account the fact that companies seek tax evasion for the purpose of reducing their tax burden and thus limiting their aggregate costs, all views regarding the ethicality of tax evasion can conditionally classified into three groups:

1. Tax evasion is never ethical

Under this approach, it is believed that taxes can never be excessively high for economic entities due to the fact the level of taxes is set by society itself. This can be explained by the fact that national authorities are elected directly by people. Thereafter, they develop and implement their strategies of national development under which they set the level of taxes for the economic sectors based on the assessment of the current economic situation and market conjuncture. In case that people are unsatisfied with the policies of the government, they choose new authorities through elections, and so on. Therefore, the proponents of the affirmation that tax evasion is never ethical stress that the level of taxes within a particular state is inherently fair, and therefore companies shouldn't have any reason to evade those taxes using any tax avoidance schemes or mechanisms.

2. Tax evasion is always legal

This affirmation opposes the previous approach, and is what McGee (2005, p. 11) calls "anarchist". Under this approach, it is believed that the state is always unfair in its policies and acts “as a thief”. Therefore, companies do not have any reasons to believe the authorities of their respective state, and being led by their economic motives and reasons, may seek better conditions abroad in terms of taxation and the financial burden borne by them.

3. Tax evasion is sometimes ethical

Under this approach, it is believed that tax evasion may be justified from the ethical perspective in some particular cases. For instance, as stated by McGee, there may be situations in which the state fails to implement its effective national economic development policies, and only runs activities associated with the redistribution of income. A major part of such income is concentrated in the hands of a very limited number of families, and thus corruption occurs. In those conditions, companies do not have any ethical liabilities to pay higher taxes which are consumed by corruption mechanisms, and are not directed to the development of society, and therefore companies have the moral right to transfer their activities to foreign jurisdictions for avoiding taxes.

The proponents of the approach under which the ethical consequences of tax optimization and tax avoidance activities are deemed negative argue that any such activities lead to the decrease in the actual gains of the respective state’s budget. As a result, such state’s national authorities are deprived of the opportunity to effectively run all state programs associated with education, healthcare, public development, and so on. Therefore, regardless of the goals pursued by firms in the course of their tax avoidance, the population of the respective country suffers (Said et al. 2014, p. 111).

Lately, corporate social responsibility activities have been growing on the global scale on the part of major corporations. Such activities are not associated directly with the respective companies’ business activities, and they are destined to ensure positive brand image among the customers. Such activities are undertaken by companies in order to overcome their activities through the better contribution to social development. Under the CSR approach, tax avoidance is considered unethical, even regardless of its legality, as companies seeking tax avoidance act for the sake at their own benefits to the prejudice of society (Haynes et al. 2013, p. 119).

Another argument used by the proponents of the unethical nature of tax avoidance is the fact that due to the diminished budget income as a result of tax avoidance, public authorities may seek other sources to replenish the treasury, and thus may increase the ultimate tax burden borne by both the domestic corporate sector and the population, thus contributing to the subsequent deterioration of life quality in the country (Bagley 2002, p. 41).

Thus, overall, it can be stated that although tax optimization is generally deemed legal under the international regulations and national legislation of most states, the ethicality and morality of such activities is much debatable.

Taking into consideration the findings of the theoretical part of the research, in the next chapter of the research, the case study analysis of tax optimization activities will be run.

3 PRACTICAL PART

3.1 Tax avoidance in the United States

The scope of tax avoidance activities run by transnational corporations has been steadily growing on the global scale in recent years in terms of the total amount of taxes which are re-routed from host countries to low-tax offshore jurisdictions. In this context, a particularly important role is played by American multinational companies which are among the world's pioneers in the development of new and effective tax avoidance tools and schemes.

According to expert estimates, the tax optimization activities run by American multinationals, cost the American budget as much as USD 57 to 90 million in 2008, the year of the global financial and economic crisis (Keightley 2013, p. 3). In 2012, the estimated losses of the American budget due to the tax avoidance activities run by US-based multinational corporations made up USD 77 to 111 billion in aggregate, which made up almost 40% of the total estimated amount of tax optimization activities on the global scale (Clausing 2016).

The main offshore tax jurisdictions which are used by American multinational companies with the aim of declaring their profits with lower taxation rates applied include Ireland, Bermuda, Luxembourg, the Netherlands, and Switzerland. The amount of overseas profits declared by major American transnational corporations in such jurisdictions is approximately 4 times greater as compared to the profit declared in high-tax jurisdictions such as Germany, the UK, or Canada. The recent trends in the field of American companies' tax optimization testify that there is a tendency toward the geographic shifting of profits with greater share accounted for by low-tax foreign jurisdictions. This proves that major American companies indeed tend to maximize their use of tax optimization/avoidance schemes for the purpose of contracting their tax base, and this brings further greater losses to the American budget (Keightley 2013, pp. 4-5).

The abovementioned trends become even more negative for the American economy taking into account the fact that major American transnational companies actively use state support in their activities, and moreover, resort to lobbying with the aim of increasing their political and economic impact. As stated by Oxfam (2016), "*from 2008 – 2014 the 50 largest*

US companies collectively received $27 in federal loans, loan guarantees and bailouts for every $1 they paid in federal taxes. From 2008 – 2014 these 50 companies spent approximately $2.6 billion on lobbying while receiving nearly $11.2 trillion in federal loans, loan guarantees and bailouts. Even as these 50 companies earned nearly $4 trillion in profits globally from 2008 – 2014, they used offshore tax havens to lower their effective overall tax rate to just 26.5% 8 , well below the statutory rate of 35% and even below average levels paid in other developed countries. Only 5 of 50 companies paid the full 35% corporate tax rate." This information proves that the aggregate scope of American multinational corporations' tax optimization/avoidance activities is large, and the effects brought to the American budget are much detrimental. Thus, those tax optimization activities require to be addressed by the American authorities with the aim of achieving the best economic opportunities for the state.

As of today, the American authorities are foreseeing different scenarios in profit shifting activities undertaken by major multinational corporations. There have been different proposals with the aim of ensuring the minimization of profit outflows from the country's budgets. Among other proposals, the opportunity to reduce the tax rate applied to American corporations' business profit has been taken into consideration. However, there are currently no effective mechanisms to eliminate or at least significantly reduce the total amount of tax optimization activities run by the American companies due to the fact that they are inherently legal, and therefore do not breach any regulatory provisions (Clausing 2016).

In this context, it is worth noting in Particular the recent scandal with tax avoidance on the global scale commonly referred to as the Panama Papers scandal. It occurred in March 2016 when the internal documentation of the Panama-based legal entity entitled Mossack-Fonseca was disclosed to the public, and it was found out that a number of major international officials and corporations, including American MNCs, had their business registered in foreign offshore tax jurisdictions with the aim of minimizing their tax burden. "*The US president said the leak from Panama illustrated the scale of tax avoidance involving Fortune 500 companies and running into trillions of dollars worldwide.*" (The Guardian 2016). This situation proved that the current level of control over corporate tax avoidance/optimization practices in the US is insufficient, and thus requires major improvement.

In addition, the Panama Papers also revealed the fact that the tax optimization/avoidance activities undertaken by translational corporations cannot be always effectively monitored and identified by the state. Even though such activities do not include any illegal practices, they are much sophisticated and are based on the use of much complex tax avoidance schemes (The Guardian 2016). Due to this, the public authorities might be unaware of where such particular activities are undertaken, and therefore this only further emphasizes that the field of tax avoidance/optimization requires further greater attention on the part of national and international authorities with the aim of achieving the minimization of tax outflow from high-tax jurisdictions such as the United States.

Taking into consideration the great scope of the American multinational corporation's tax avoidance/optimization activities and the effects which such activities bring to the state, in the next chapter of the thesis, the case studies of major American companies which have been involved in profit optimization activities lately will be investigated more in detail.

3.2 Case study of tax optimization

3.2.1 Case 1. Apple

Apple is an American multinational corporation specialized in the production of computer hardware and software and a wide range of consumer electronics. The company has been running its activities in the international market since the 1980's, and its name has been steadily tied with tax avoidance practices throughout the company's lifetime. However, the greatest scandal occurred in 2013 when the American Senate discovered that Apple had established a network of foreign subsidiaries in offshore jurisdictions holding over USD 67 billion in the form of cash funds. According to the findings of the Senate's investigation, Apple "*avoided at least $3.5bn (£2.3bn) in US federal taxes in 2011 and $9bn (£5.9bn) in 2012*," and the firm didn't commit any illegal activities, which means that it used legal tax avoidance schemes. However, as a result of the scandal, the company was blamed as the largest tax avoider in the US, and its reputation significantly deteriorated (Losh 2013).

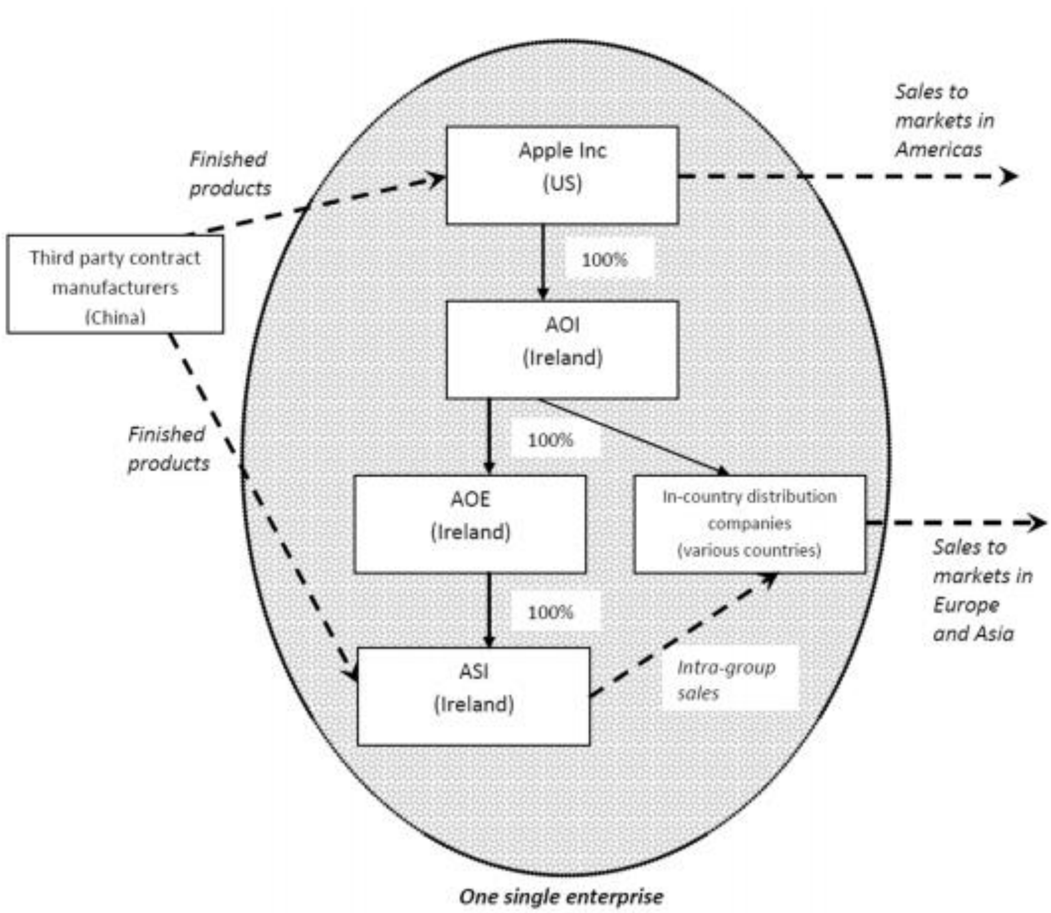
Only four years after its establishment, Apple established subsidiaries in Ireland to which 60% of the company's profits are attributable. However, despite being registered in

Ireland, the profits of Apple's Irish subsidiaries aren't taxed anywhere. This is possible thanks to the sophisticated tax avoidance scheme used by the company. Namely, Apple Inc. has an Irish holding entity which doesn't run any business operation and doesn't have any staff. As stated by Sheppard (2013), "*This company also serves as a group finance company. Apple Inc., the U.S. parent of the whole group, pays U.S. tax on the investment earnings of this company. Otherwise, the holding company pays no tax to any government, and has not paid tax for five years. It claims tax residence nowhere.*" Beneath the holding entity, Apple also has an Irish principal corporation which has entered into agreements with the American company's Chinese contractors, and thus receives the inventory manufactured by such contractors under the order placed by Apple. This company and the other Irish subsidiary of Apple have the foreign rights to Apple's American-based technologies (Sheppard 2013).

The income tax rate in the United States is high, while in Ireland, it constitutes only 12.5%. Through the use of the network of its subsidiaries, Apple allocates the largest part of its income to Ireland, while the largest part of its costs is allocated to the United States. Furthermore, thanks to the special calculations used for evaluating the company's income, Apple's income in Ireland is taxed at a rate even lower than 12.5%. Here, the abovementioned right to Apple's American technologies attributable to Irish subsidiaries plays a major role. Namely, as stated by Gleckman (2013), "*For a company like Apple, nearly all the value of its products is in its patents and other intellectual property. By charging a relative pittance to a foreign subsidiary for use of that IP, it can maximize that affiliate's profit and minimize its IP income in the U.S.*"

However, it is worth understanding how the company further minimizes the amount of taxes it pays when the profit flows are attributed to the Irish subsidiaries in their major part. This is achieved by Apple Inc. thanks to the differences in the American and Irish legislation in the context of organization of companies. Namely, under the American law, a company is resident of the country where it was organized. Under the Irish legislation, a company is tax resident in the country where it is managed and controlled. Therefore, Apple Inc. doesn't file any documents confirming the Irish subsidiaries' belonging to any particular tax jurisdiction. As a result, the companies are not considered as tax residents of any jurisdiction under the Irish legislation. This allows Apple's Irish subsidiaries avoiding the tax treaty between Ireland and the US (Sheppard 2013). Therefore, while the companies are registered in Ireland, the profit attributable to them in fact doesn't belong to any jurisdiction, and moreover, it isn't covered by the US tax legislation, which allows Apple avoiding taxes (Gleckman 2013).

Figure 1. Apple's tax avoidance Double Irish scheme



Source: Ting 2014, p. 43

Figure 1 above illustrates the Double Irish taxation scheme used by Apple in its business activities with the aim of minimizing the company's tax expenses. This tax optimization scheme is often referred to as iTax similarly to the common name structure inherent of Apple's corporate products. As can be seen from the chart, Apple actively uses intracorporate transactions implemented through the application of transfer pricing, and thus re-allocates its profits to tax jurisdictions with lower tax rates as illustrated earlier in this thesis (Ting 2014, pp. 40-43).

However, those are not the only methods used by the corporation to avoid the high taxation rate in the US and to minimize the ultimate tax expenses borne. Namely, while the company's intellectual property is located in the United States, and isn't attributable to any tax haven, Apple has a cost-sharing agreement with its Irish principal holding entity. This company gets the income from foreign sales of inventory, which sales are not taxable under the US law. Moreover, the abovementioned cost-sharing agreement, Apple's expenses associated with research and engineering activities are divided between the parent company in the US and its Irish subsidiaries proportionately to the total amount of sales. Apple's Irish holding company pays small royalty fees to the American parent corporation for the use of its intellectual property rights, while it collects much greater revenues from sales from Apple's other foreign subsidiaries. As a result, a major part of the company's income is passed through the network of foreign subsidiaries without any tax jurisdiction, and the company pays high taxes only on a small part of its income (Sheppard 2013).

In recent years, Apple has even increased the share of its profits attributable to the Irish subsidiaries for achieving even greater benefits derived from tax optimization. The US Senate's investigations against the company continued, and new claims appeared. Namely, in 2015, the Senate argued that Apple was concealing over USD 74 billion in Ireland which would otherwise be subject to taxation under the US laws. However, the company's managers rejected all those claims, and stated that the corporation didn't violate any American laws. This is indeed true, as the investigations of the Senate only proved tax avoidance, and not any illegal tax evasion. Therefore, the state cannot prosecute the company, and initiated negotiations with Ireland for the purpose of preventing American companies from using this jurisdiction for minimizing their income taxable under the US laws (Bolton 2015).

As a result of the tax avoidance activities run by Apple Inc. and other American companies, there has lately been much debate in American society, and namely among American economists on whether the company's activities are ethical. While ones argue that the corporation is required to pay its taxes in the US with the aim of developing the country's economy, others claim that insofar, the entity's activities have remained totally legal, and using loopholes in the legislation is natural for all companies, as they run their commercial activities for maximizing their ultimate financial profits (Johnson 2016).

Against the background of those accusations and litigations, the managers of Apple Inc. continue developing new schemes for the purpose of ensuring the best tax avoidance results. Namely, in 2016, the American corporation issued its bonds for a total amount of USD 12 billion. The profits were attributed to the company's subsidiaries in offshore jurisdiction, and were used for paying dividends to Apple's shareholders and for purchasing back the company's shares from foreign investors. As a result, the company avoided paying US corporate profit tax at a rate of 35%. According to estimates, throughout the year, the company will able to save at least USD 6.5 billion using only this tax avoidance scheme through bond issues (Bates and Newton 2016).

Therefore, overall, it can be stated that Apple Inc. uses quite sophisticated tax avoidance schemes which allow the company minimizing its ultimate costs associated with the payment of taxes. In the next chapter of the thesis, the case study of another corporation, namely Google, will be run for investigating in detail its corporate tax avoidance practices.

3.2.2 Case 2. Google

Google Inc. is an American multinational corporation specialized in the development and sales of a wide range of software and online-based services. The company' greatest profits are generated through AdWords, Google's service for the placement of online advertisements shown to people running search queries using Google's search engine. The recent surge in the number of claims and accusations directed against Google Inc. is due to the investigations run by the UK authorities which prove that Google avoids the payment of full taxes under the legislation in force. The company uses a number of different tax avoidance schemes, but it is able to ensure the greatest amount of tax avoidance through the routing of its profits to offshore jurisdictions (Schutte 2016).

The example of Google UK is very illustrative due to the fact that it is the company's largest subsidiary in Europe in terms of the number of staff employed and the amount of revenues generated. For the period from 2005 to 2015, the company paid only approximately GBP 130 million to the state budget as corporate profit tax, while the company's total revenue made up approximately GBP 3.9 billion. The investigation run by the UK tax authorities revealed that such discrepancies in the ultimate amount of profit tax paid by the entity against the amount it is liable to pay under the British legislation is due to the fact that the company operates subsidiaries in Ireland, and attributes its profits from sales in the United Kingdom to its subsidiaries located in Ireland (Cole 2016).

Calculations estimate that the effective tax rate by Google in the United Kingdom makes up approximately slightly over 2.5%, while the corporate profit tax rate in the UK makes up 20%. To the largest extent, such tax optimization is achieved through the localization of advertising activities in other jurisdictions and through sophisticated licensing schemes (Savov 2016).

The greatest part of Google's profits are generated through the company's operations with intellectual property rights. The company's intellectual property rights are attributable to its company located in Bermuda, an offshore tax jurisdiction, and not in the US or any European countries. In Bermuda, foreign companies are not liable to pay any corporate income tax or tax on capital gains, and as a result, the business profits of companies are re-routed for avoiding the high tax rates in the US (35%), the UK (20%) or any other developed states. In Bermuda, Google has absolutely no staff, and the company's subsidiary in fact acts as a shelter for its income generated through business activities. However, the company doesn't direct its profits right to the subsidiary in Bermuda. The company uses the Double Irish and Dutch Sandwich scheme for achieving the greatest minimization of profits (Faccio 2016).

The corporation's sales performed in the United Kingdom and other European countries are routed to Ireland where the taxation rate amounts to 12.5% for corporate profit tax. The Irish subsidiary pays royalties to Google Netherlands Holdings BV, Google's subsidiary incorporated in the Netherlands, for the use of the company's intellectual property rights. Such operations are not imposed by taxes. Thereafter, the Dutch company pays royalties to the subsidiary incorporated in Bermuda. Such payments of royalties are accounted for as costs, and therefore they minimize the tax base of the Dutch subsidiary. Furthermore, such royalties are accounted for as income by the company incorporated in Bermuda, and due to the lack of income tax in the jurisdiction, the entirety of such income is exempted from tax, thanks to which the corporation spares much through tax avoidance (Sterling 2016).

In the above scheme, Google uses transfer pricing for ensuring the re-distribution of its income. "*Google has a very strong case to make that its intellectual property (in other words, the sophisticated algorithms that make its search engine so useful) is something for which its subsidiaries worldwide should be paying for — thereby transferring a portion of their revenue back to Google elsewhere.*" (Gumbel 2012). Therefore, it can be stated that the tax optimization activities run by Google rely largely upon its broad business network embracing a number of different subsidiaries located in different jurisdictions around the globe. The transfer-pricing tool serves the company's use of its tax avoidance mechanisms and allows minimizing the amount of income attributable to high-tax jurisdictions such as the US or developed Western European states.

Google has been under growing tensions in the United Kingdom and other EU member states in recent years due to the allegations of tax avoidance. Although no illegal activities were found in Google's tax optimization procedures, the findings of the British tax authorities' investigation gave birth to major debate in British society due to the claims that Google was cheating the British taxpayer. The corporation didn't negate the accusations of tax avoidance, and even further confirmed them, claiming that the company was proud of its effective tax management. As a result of the findings revealed by the British authorities, the country initiated negotiations between the EU member states for the elimination of the existing loopholes in their legislation with the aim of preventing the great outflow of funds to foreign offshore tax jurisdictions (Evans 2013). The findings revealed on Google's tax avoidance in the United Kingdom raised a wake of subsequent investigation in Italy France and other jurisdictions in the European Union. However, Google cooperates with the authorities and provides all data on their tax avoidance, without concealing the transfer-pricing mechanisms used, which again proves the legality of Google's tax optimization operations, but further ignites the social dispute on the moral side of such activities and their impact on social development (Drucker 2012).

Overall, it can be stated that Google is an effective tax avoider, as the company is able to significantly minimize its tax burden through the legal tax avoidance mechanisms based on the use of the loopholes existing in the international legislation and national regulations of different countries. In the next chapter of the thesis, the tax optimization case of Amazon will be investigated.

3.2.3 Case 3. Amazon

Amazon is an American multinational corporation specialized in electronic commerce and cloud storage service technologies. Lately, the corporation has been accused of massive tax avoidance through sales outside the United States. This was revealed in 2013, when the authorities of EU member states initiated investigations to reveal Amazon's involvement in tax optimization practices. According to the findings of the investigation run by the British officials, the company generated almost USD 6 billion of sales in the United Kingdom in 2013. However, the total amount of taxes paid by the company made up only USD 3.3 million for the year. Despite running its sales in the UK and other countries of the European Union, the company recorded its sales in other jurisdictions with lower taxation rates, and as a result, it was able to achieve significant contraction of its aggregate tax base (Kamran 2016).

The tax avoidance scheme applied by Amazon relies on the operation of its subsidiaries incorporated in Luxembourg. The company's servers through which sales are performed in Europe are located in a number of states, including the UK, France, Italy, etc. However, the corporation's profits are recorded for its subsidiary registered in Luxembourg. This subsidiary records the greatest part of the company's net profit in Europe. Thereafter, this subsidiary pays royalty fees for the use of intellectual property rights to another subsidiary located in Luxembourg. Such expenses are recorded as costs borne by the first subsidiary to which European income is attributable. As a result, the tax base of Amazon gets decreased, and the company is liable to pay a smaller amount of taxes. However, the corporate profit tax rate in Luxembourg is still considerable, and it amounts to as much as 29.22%. The investigation of the European authorities showed that Amazon and the authorities of Luxembourg had agreed upon a preferential tax regime under which the corporation became tax exempt from the largest part of its profit, and remained liable to pay only the smaller part of the tax liabilities it would otherwise be due to pay to the budget. As stated by the conclusions stipulated by the European Commission, "*At this stage we consider the amount of this royalty, which lowered the taxable profits of Amazon, was not in line with market conditions. Luxembourg agreed to limit the amount subject to tax.*" However, both Amazon and the authorities of Luxembourg denied the existence of any preferential tax regime and claimed that the corporation was still imposed by the same taxation rate as all other entities incorporated in the jurisdiction of Luxembourg (BBC News 2014).

The scheme used by Amazon with the involvement of two subsidiaries in Luxembourg allowed the company avoiding taxation in the United States. This was ensured thanks to the company's minimization of the profits repatriated to the US. To the contrary, it recorded almost all of its European profit to be re-invested in the development of Amazon business and its subsequent growth. As a result, this profit was never taxed under the American legislation. Given the proofs provided by the European Commission as regards the existence of a preferential tax regime for Luxembourg in the European Union, it can be stated that Amazon was paying its value added tax in Luxembourg, which rates are much lower as compared to other countries (3% for e-book purchases and 15% for music downloads). Therefore, the deal was beneficial not only to the corporation, but also to the state of Luxembourg, as Luxembourg gained an opportunity to boost its budget proceeds thanks to greater VAT income, as well as thanks to greater corporate profit taxation (of part of Amazon's profit was still taxed in Luxembourg) (Borec 2015).

The scheme used by Amazon for avoiding excessive taxation through the use of subsidiaries in Luxembourg is quite complex and sophisticated. It is based on the use of loopholes existing in the American legislation. Namely, the corporation's subsidiary in Luxembourg which records the largest part of its European profits, Amazon Europe Technologies Holding SCS, is a limited liability partnership (LLP). Unless it pays dividends to its shareholders, the company's profits aren't subject to any US taxes, which is due to the discrepancies in the tax legislations of the US and Luxembourg. Amazon Europe Technologies Holding SCS is the owner of all licenses and intellectual property rights which it sells to the second subsidiary in Luxembourg, namely Amazon EU Sarl, as described earlier in this thesis chapter. Amazon Europe Technologies Holding SCS provides commercial loans to other subsidiaries of Amazon for interest payments. As a result, the company allocates loans to its affiliated structure, which thereafter have to repay greater funds due to the existence of interest. Such interest payments are recorded as costs on the part of the parent corporation in the US, and they diminish the company's ultimate amount of profit, which leads to the smaller tax payments due. As a result, this scheme allows feeding the business expansion of Amazon by leaving almost all of the company's profits generated in the European Union within the corporate business framework of Amazon (Borec 2015).

The policies implemented by Amazon as regards taxation and tax avoidance caused a wake of negative reactions both among European officials and among the population, as activists called for the boycott of Amazon's services. As a result, the company undertook to change its business policies in 2015. Since 2015, the company has been recording its sales in the UK for its British branch, and not for the subsidiary located in Luxembourg. According to the official representatives of Amazon, this was done for the purpose of satisfying the public requirements and the needs of society. However, according to experts, this may be associated with the punitive tax at a rate of 25% which entered into force in the United Kingdom in April 2015. This tax is applied to corporate entities using artificial re-routing of their taxes through tax optimization and tax avoidance schemes to other jurisdictions, thus diminishing the benefits attributable to states where their yield-generating commercial activities were performed. As stated by the headquarters of Amazon, "*We regularly review our business structure to ensure that we are able to best serve our customers and provide additional product and services. More than two years ago we began the process of establishing local country branches of Amazon EU Sarl, our primary retail operating company in Europe.*" This means that the company plans to further develop its business network in Europe and to attribute its sales and thus revenues to those states in which they were performed. However, this does not mean that the entity will refrain from tax optimization or will not use other tax avoidance alternatives currently known to it and available in the market (Bowers 2015).

Therefore, Amazon is another example of successful tax optimization activities, even though the corporation was forced to modify its tax avoidance policies in line of the stricter requirements imposed on it in European Union member states.

In the next chapter of the thesis, the case study of Starbucks will be investigated more in detail in the context of the corporation's tax avoidance practices.

3.2.4 Case 4. Starbucks

Starbucks is an American multinational corporation specialized in the production and sales of coffee through retail outlets and a developed network of coffee shops around the globe. The company's extensive tax avoidance volumes were first revealed in 2012 when the British authorities revealed that the company had paid only GBP 8.5 million of corporate profit tax for the 14 years of its business activities in the country with the operation of over 750 outlets across the UK. In 2009-2012, the company achieved a total of USD 1.2 billion of sales in the UK, but did not pay any corporate profit tax at all (Bergin 2015). The detailed investigation of the corporation's activities showed that the company was using a developed network of subsidiaries in different states and intracorporate transfer pricing with the aim of minimizing its ultimate tax burden (Szabo 2012).

The reason for the investigation run against Starbucks in the UK was due to the fact that company had been declaring net losses for several years subsequently, despite constantly raising its total sales and despite declaring the British unit's profitability to the investors. The findings of the investigation revealed that the company had been using a sophisticated scheme with the aim of routing its profits to other subsidiaries beyond the UK for lowering the total tax base. Namely, the company had a subsidiary operating in Switzerland employing only 30 persons. The subsidiary located in Switzerland purchases coffee, which is thereafter, sold in the EU member states. However, it re-sells coffee beans to other subsidiaries, namely the on in the United Kingdom, at a premium of approximately 20% over the initial price. According to the affirmations of Starbucks' officials, this is due to the fact that the company further selects the best coffee beans, and is also liable to incur costs for its ordinary course of activities (Szabo 2012).

Therefore, the UK-based subsidiary of Starbucks incurs additional expenses for the purchase of coffee beans from the company's Swiss subsidiary. Furthermore, the company pays large amounts of costs associated with advertising to other associated located in the Netherlands, which allows Starbucks further reducing its aggregate tax burden. At the same time, the unit responsible for coffee roasting operations is located in the Netherlands, and is another subsidiary making part of the Starbucks Group. Throughout the previous years, the British subsidiary had been paying the value of coffee bean roasting to the Dutch subsidiary at a premium of 4.7% to 6%, thus further increasing its costs. Finally, it is worth noting that the company declared great research and development costs. All in all, this made the corporation's expenses high, and thus allowed significantly decreasing its total profits generated through sales in the United Kingdom (Bergin 2015).

The revelation of Starbucks' tax avoidance practices became largely known in society, and the company needed to react to the accusations regarding its unethical corporate practices. Initially, the officials of Starbucks negated any use of illegal practices, and therefore claimed their tax optimization to be the corporation's natural desire to minimize its taxes paid to the budget. Namely, the CEO of Starbucks' British branch claimed that "*Fundamentally, the piece that was aerating was around royalties – the fact a brand is paying a royalty to an entity outside the UK, and to me that's very, very ordinary. It happens across the sector and therefore it didn't bother me at all. There was nothing abnormal about the way Starbucks is run in the UK. What is abnormal is that we haven't been making a profit.*" Such explanations were treated negatively in society due to the fact that the company washed out its profit from the UK. As a result, initiatives appeared in social networks for protesting against Starbucks' tax avoidance policies and the corporation's attitude toward the customers in the United Kingdom (Campbell 2014).

After the great resonance in society caused by the British authorities' investigation and the company's accusations of tax avoidance, Starbucks decided to change its business policies as regards taxation, and started declaring positive net profits. Thus, in 2014, it paid a total of GBP 8.1 million as corporate profit tax, which figure was almost equal to the entire amount of profit tax by the corporation for the last 14 years of its business operations in the UK. Moreover, Starbucks also closed one of its subsidiaries acting in the United Kingdom which was used with the aim of minimizing the company's taxes through its network of business entities located in foreign jurisdictions (Davies 2015).

Therefore, it can be stated that Starbucks is another bright example of successful corporate tax avoidance activities. However, the corporation is also an example of how the public opinion and the perception of the ethical side of tax optimization by society affect the activities of transnational corporations and make them change their tax avoidance policies.

Taking into consideration the findings of the four case studies described above, in the next chapter of the thesis, the four companies and their tax avoidance practices will be analysed from the perspective of revised IFRS.

3.3 Analysis of the analyzed cases from the perspective of revised IFRS

For the purpose of analysing the above case studies from the perspective of revised IFRS, it is worth first of all summarizing the findings of the previous chapters of this thesis, and revealing the key similarities and differences in the four analysed companies' performance of their tax optimization procedures.

A common point in each of the above cases is the fact that the investigated international corporations rely heavily upon the use of two main mechanisms for ensuring the minimization of their tax burden, namely use of subsidiaries in foreign jurisdictions with lower corporate profit taxation rates and application of transfer pricing mechanisms with the aim of raising the actual amount of costs borne by the companies. The different entities' schemes are characterized by different levels of sophistication, different countries used as offshore jurisdiction, and different number of subsidiaries used as intermediaries in the process of tax burden minimization. However, generally, it can be stated that companies involved in different markets use intensively the payment of royalty fees to their subsidiaries with the ultimate goal of minimizing their corporate profit.

At the same time, a key common point in the analysed companies' business avoidance is the fact that they seek the reduction of the tax burden borne in the United States or Western European jurisdictions due to the high corporate profit tax rates set in those countries' legislation. Furthermore, none of the investigations run against Google, Amazon, Apple or Starbucks has revealed any violations of the national tax legislation or any international tax agreements, which means that the companies didn't use any illegal tax evasion practices, didn't conceal their profits or use offshore jurisdictions for money laundering. To the contrary, as revealed by the findings of the investigations, their activities were based purely on the loopholes existing in the applicable taxation regulations.

However, in each of the analysed cases, the use of legal tax optimization practices has caused major social resonance, and therefore prompted the companies to react in order not to let their image deteriorate. The reaction of different companies differed. While Starbucks and Amazon started recording their profits in the respective high-tax jurisdiction with the aim of avoiding any deterioration in their brand image, Apple and Google didn't undertake any major corrective actions, and moreover, Google even declared that its activities were ordinary for a company wishing to achieve financial prosperity.

Therefore, as such activities are legal, a question arises on how the tax optimization practices should be approached form the moral and ethical perspective, and how revised IFRS could contribute to the resolution of this issue.

In 2015, the Organization for Economic Cooperation and Development and the G20 states started a project to address the issue of base erosion and profit shifting. According to this project, the developed states aim to achieve the recording of profits generated by commercial entities in tax jurisdictions where their respective business activities are run, which should allow eliminating the practices of profit recording for offshore jurisdictions. At the same time, the European Commission launched a project for ensuring greater tax transparency in the European Union, and for creating a more fair tax environment in the region. Those initiatives were promoted in particular by the cases of the four analysed companies, namely Apple, Amazon, Google, and Starbucks, as they became illustrative examples of how the loopholes and drawbacks in the existing tax regulations allowed companies minimizing their tax burden (Deloitte 2015).

Due to the fact that tax avoidance/optimization comprises only legal activities, it can be stated that the International Financial Reporting Standards (IFRS) can deal only with the ethical side of those activities, as they do not violate any norms or regulations on either the national or international level (in contrast to illegal tax evasion constituting tax fraud).

There are several main accounting standards and international financial reporting standards which deal with the issues related to tax avoidance. Namely, International Accounting Standard 12 deals with the key issues related to income taxes. Under IAS 12, all corporate profits can be divided conditionally into accounting profit and taxable profit. Accounting profit is "*profit or loss for a period before deducting tax expense*", and profitable tax is "*the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable)*". This International Accounting Standard also investigates temporary differences and tax liabilities occurring in different periods recognized as either liabilities or assets depending on the time of their recognition (European Commission 2012).

However, the standard which deals most closely with the schemes which international corporations use for their tax optimization activities is IAS 24 "Related Party Disclosures" investigating in detail transfer pricing. In contrast to GAAP, the application of IFRS to transfer pricing affects significantly the actual value of transfer price and the respective costs to be reflected in corporate financial statements. Namely, as stated by Deloitte IAS Plus (2015), "*For companies that use the comparable uncontrolled transaction (CUT) method to determine their transfer pricing for intangible property, the effect on their pricing will depend on the exact details of their contracts with related parties, as well as the contracts of their comparables. The total amount of gross royalty charges or license fees may change for several reasons. Royalty rates charged to or from unrelated parties may be determined by using financial statement data. This could affect the range of arm's length royalty rates. Additionally, an income statement item to which a royalty rate may be applied, such as net revenue, has the potential to change under IFRS.*"

This finding is important taking into account the fact that the companies analysed in this thesis, namely Amazon, Google, Starbucks and Apple, use actively transfer-pricing mechanisms for the purpose of minimizing their actual costs. Therefore, IFRS affect the actual value of royalty rates which the abovementioned and other multinational corporations may use in their business practice with the aim of paying to their subsidiaries for the provision of intellectual property rights. Although as of today IFRS provide significant width to companies in terms of their opportunity to record costs in financial statements, potential revisions to IFRS for closer control over the recognition of royalty fee payments in corporate financial statements may be important for reducing the level of tax avoidance.

Next, as stated by Deloitte IAS Plus (2015), "*For companies that use the resale price method (RPM) or the cost plus method, the calculation of gross profits is essential to determining the appropriate transfer price. In calculating the margins/markups or the base to which those margins/markups are applied, financial earnings generally form the basis of these calculations, which are directly affected by the accounting standards used. It is feasible that a company's overall taxable results using the RPM or the cost plus method may change, solely because of the conversion to IFRS even though there has been no change in the underlying economics of the transactions.*" Therefore, this further confirms the fact that the use of common standards for financial reporting, namely IFRS, leads to the creation of the same conditions for all companies to reveal their costs incurred as a result of transfer pricing, and this may provide financial authorities on the national and international level with greater opportunities of control over all respective transactions.

IAS 24 also deals with the ethical aspects related to the disclosure of arm's length operations run by transnational corporations with their related parties. Namely, under the provisions stipulated in the Standard, "*Regardless of whether there have been transactions between a parent and a subsidiary, an entity must disclose the name of its parent and, if different, the ultimate controlling party*" (Deloitte IAS Plus 2011). This means that all companies involved in economic activities are required to disclose the full structure of their ownership. This is important to take into account as an ethical aspect due to the fact that companies implementing tax avoidance procedures do not breach any legislative norms. Therefore, their transparency in business ownership allows the authorities of the respective states investigating in detail how the aforesaid tax minimization activities are run, and in its turn this allows the public authorities developing improvements to the legislation for eliminating the existing loopholes, and thus for preventing the subsequent outflow of tax funds.

The above facts prove that the ethical side of IFRS is particularly important in the current conditions of international business development. Although tax optimization activities cannot be prohibited under the current legislation and international regulations, they may be effectively controlled. As shown by the examples of Starbucks and Amazon, international corporations may react well to the existing social resonance with the aim of avoiding any major brand reputation impairment. Therefore, IFRS can contribute to the spreading of reliable and accurate information on corporate tax avoidance practices among society, which thus would create social tensions on the respective entities, and thus may make them revise their business policies in the direction of recording of their profits in the jurisdiction here they were generated.

In the next chapter of the thesis, the findings revealed above will be discussed more in detail, and the ethical side of IFRS in the context of corporate tax optimization practices will be investigated with the aim of developing suggestions and recommendations for the possible amendments and revisions of the existing IFRS with the goal of minimizing tax outflows from the respective jurisdictions.

3.4 Discussion of results

The findings of the research prove that tax optimization activities play an important role in the corporate business practices of entities, and particularly of major transnational corporations. Such activities in fact represent a legal way for multinational companies to minimize their costs through the minimization of tax burden borne. The main benefit of tax optimization is the legality of those activities. However, their main drawback is that even though they do not breach any national regulations or international standards, such activities may lead to negative response on the part of society, as they bring to major outflows of funds from the national economies of countries where economic activities are carried out by companies for the purpose of generating profits.

The investigation of loopholes existing in the national legislation of states and in international regulations provides much wider opportunities for companies to build up their effective tax optimization policies. In this context, the activities of international corporations in this context may be particularly effective thanks to the availability of a wide international business network, and thus foreign legal entities through which companies can re-route their profits, thus deriving financial benefits through the minimization of costs.

The analysis run within the framework of this thesis has revealed that transnational corporations may use different tax optimization/avoidance schemes in their activities, and the selection of the particular scheme is preconditioned by the specificities of the respective entity's business activities, their scope, and the opportunities which the company may find for minimizing its tax burden. However, the two tools which are used most often are the recording of profits for a foreign subsidiary incorporated in a foreign offshore jurisdiction with low level of taxation or no corporate profit taxation on the one hand, and intensive use of transfer pricing on the other hand.

The case studies analysed in this research are illustrative as examples of corporate tax avoidance practices and their potential consequences for corporations in terms of their financial results on the one hand and the effects on their brand image on the other hand. Thus, it has been revealed throughout this research that Amazon, Google, Apple and Starbucks are companies which use effectively tax optimization. Each of the abovementioned companies has a developed international network of subsidiaries, and uses them effectively for achieving the best results in terms of tax optimization. The schemes used by these transnational corporations are quite sophisticated, and they had succeeded disguising their tax avoidance for a great number of consecutive years, until a series of investigations finally revealed those operations.

The fact that the companies concealed their tax avoidance practices can be explained by their desire not to let their brand image deteriorate as a result of negative reaction on the part of society. However, the responsive actions undertaken by the abovementioned transnational corporations differed. Namely, while Amazon and Starbucks started declaring their profits in the high-tax jurisdictions where they are generated, Apple didn't make any changes to its business policies, and Google even claimed that it would continue running its tax optimization, as those activities are indispensable for the company to achieve successful business results.

Those findings are important due to the fact that they help understand the essence of the legal and ethical sides of tax optimization. On the one hand, such activities are legal and cannot be prosecuted, and the corporations are aware of it. As a result, they may leave their business policies unchanged without fearing any sanctions. On the other hand, without effectively addressing those issues, companies risk of losing their positive brand image. And this effect is due to the ethical side of corporate tax avoidance practices.

So, when speaking of International Financial Reporting Standards and their impact on tax optimization activities run by companies, a question arises on how they can affect such practices. IFRS impose requirements on the disclosure of data by commercial entities, including as regards arm's length operations with related parties. This means that there are clear and explicit requirements applied to companies in terms of how they must report their financial results. Therefore, IFRS cannot address the legal aspects associated with tax optimization, and focus only on the general guidelines to be followed by corporations in their accounting and financial reporting practices.

However, while IFRS cannot address or have only limited effect on the legal side of corporate tax optimization practices, the importance of IFRS is particularly high in the ethical context. The findings of this thesis reveal that IFRS play an essential role in the imposition of requirements for the full disclosure of all operations associated with transfer pricing and transactions with related entities on transnational corporations. As a result, such corporations are forced to disclose the information on all their particular operations, and this makes the information on their tax optimization mechanisms available to the public. In this case, companies risk of losing their positive brand image in the eyes of customers, and therefore are forced to undertake some actions.

Taking into account the impact of IFRS on the ethical side of tax avoidance activities, in the next chapter of the thesis, suggestions and recommendations will be developed for IFRS to address tax avoidance more effectively.

3.5 Suggestions and recommendations

Due to the fact that as of today, companies tend to use corporate tax avoidance practices very often with the aim of minimizing their tax burden and maximizing their ultimate profits, there is a need to develop a framework within which companies would be discouraged to use tax avoidance. As of today, this cannot be done in the legal field due to the fact that corporations use loopholes existing in the national legislation and international regulations. However, such framework can be created in terms of the ethical perception of tax optimization, and International Financial Reporting Standards may be the regulatory documents where improvements should be sought in this context.

For the purpose of ensuring companies' less intensive use of tax avoidance due to ethical considerations, IFRS should create a framework within which companies would be promoted to show their transparent statements, thus providing the financial authorities and the public with the opportunity to monitor all operations and transactions aimed for tax optimization.

Although IFRS already require the disclosure of corporate structure in terms of the network of subsidiaries on the international scale, this may not be enough for understanding the actual amount of their financial transactions aimed at tax minimization using transfer-pricing methods. This is due to the fact that companies only disclose data on their transactions on arm’s length with related parties, and do not justify how such transactions are used with the aim of avoiding taxes.

IFRS could elaborate more on the mandatory disclosure of related-party transactions by companies. For instance, revised IFRS could include provisions on the mandatory justifications of how particular transactions are used for minimizing taxes. Namely, such provisions could require companies to show how much taxable profits they would have had in case that they hadn’t used corporate tax avoidance practices. This would allow understanding in detail how much profits the respective companies would have been required to pay as taxes on the level of particular countries where commercial activities of countries were run, and thus would allow understanding how much profits the respective companies were able to re-route to other jurisdictions by increasing their costs, and thus minimizing their tax base.

The disclosure of such data under the requirements of IFRS would make them available to the public. Due to the great impact of the media, such data would be widely highlighted and explained to the public (without any investigations on the part of national authorities, but only through the use of data disclosed by corporations under IFRS). As shown in the case studies of Amazon and Starbucks, such disclosure may have great social resonance due to ethical considerations, and therefore companies may be required to undertake actions with the aim of avoiding their brand deterioration, and such actions would be connected with the start of declaration of profits in the respective jurisdictions.

So, revised IFRS with greater focus on the prevention of arm’s length operations with related parties associated with tax optimization could indeed encourage companies to minimize the amount of their tax optimization practices with the aim of avoiding social resonance connected with ethical considerations. However, it should also be remembered in this case that the schemes applied by transnational corporations with their subsidiaries with the aim of minimizing the tax base are often sophisticated and hard to track. As revealed by the Panama Papers scandal, such activities can often remain unnoticed by the public authorities, even if the companies disclose the full information on all related parties. Therefore, further improvements should be sough in revised IFRS for minimizing tax outflows from host countries.

Next, in my opinion, major improvement in the control over tax avoidance/optimization on the global scale could be achieved through revision of IFRS with the focus on the establishment of a mandatory tax schedule to be applied to consolidated corporations. Within such schedules, consolidated companies would be required to disclose which particular amount of which tax they paid under the legislation in force. As a result, this would allow tracking the payment of taxes made by corporations in the breakdown into particular types of taxes. As a result, the public authorities would get greater opportunities to benefit from improve supervisions and control over the payment of taxes, and thus would be able to undertake the required amendments to the legislation for boosting budget proceeds as associated with the payment of particular taxes on the part of transnational corporations.

In this context, it should also be noted that the Statement of Cash Flows which replaced Source and Uses of Funds (sometimes called “Statement of Changes in Financial Position”) as a type of corporate financial statements under the IFRS standards, was implemented with the aim of reducing companies’ opportunities to adjust any of their cash flows in their reporting with the aim of minimizing the applicable tax base. Therefore, further reducing the opportunities for artificial adjustment of cash flows within IFRS could be another important direction to be followed in the revision of International Financial Reporting Standards for the purpose of reducing the total turnover of tax optimization/avoidance on the international scale.

In addition to the above suggestions and recommendations, it can be stated that revised IFRS could further elaborate on the detailed construction of all elements of income and profits. The clear distinction between taxable profits generated in the respective states and recorded in them and in other foreign jurisdictions could be another important aspect of revised IFRS which would allow minimizing the level of tax outflows from states as a result of tax optimization activities undertaken by corporations.

However, it should be understood that as soon as revised IFRS will be dealing only with the ethical aspects related to tax avoidance/optimization, they will not be able to prevent the performance of such activities by companies, and thus may be ineffective in the long run. For instance, as shown by the examples of Apple and Google illustrated in this thesis, transnational corporations may resist any social resonance and not take it into consideration due to the great economies achieved through tax optimization.

Therefore, the improvements made to revised IFRS may be insufficient for achieving the maximum effects of corporate tax avoidance practices. In order to achieve the greatest effects in those terms, the authorities of states need to enhance their work on legal, and not only ethical, aspects of tax avoidance, and namely on the improvement of national legislation through the elimination of existing loophole, and on the improvement of the system of international regulations with the aim of preventing tax avoidance through international operations and transactions.

The fulfilment of the above suggestions and recommendations should allow significantly improving IFRS as regards corporate tax avoidance practices, thus minimizing the amount of tax optimization activities on the international scale.

4 CONCLUSION

In the current conditions of international business development, companies need to achieve their maximum effectiveness in terms of cost management with the aim of minimizing the expenses borne through their commercial activities, and thus with the aim of achieving the greatest possible profits, which is the ultimate aim of any commercial entity's business.

Companies incur a great number of different costs in the course of their business activities, and such companies' ability to minimize their costs is preconditioned by a great number of internal and external factors which affect the reserves available to companies, and their ability to identify and use all such reserves.

In this context, a particularly important role is played by tax expenses which constitute costs borne by companies due to the requirements of the legislation to pay part of their profit to the state budget. When running their activities in jurisdictions with high tax rates, companies are required to direct a great portion of their profits for tax payments, and this impairs the ultimate financial effectiveness of their business operations. Therefore, in order to maximize their profits, companies are interested in minimizing their tax base, and thus the ultimate value of tax payments to the budget.

The minimization of taxes imposed on corporations can be achieved by companies through two main types of activities: tax optimization/avoidance on the one hand and tax evasion on the other hand. Tax evasion comprises illegal practices applied for minimizing taxes, and constitutes violation of laws through tax frauds, concealment of profits, and so on. At the same time, tax optimization/avoidance stands for the legal practices of tax minimization which are based on loopholes existing in the national legislation of individual states and international regulations.

The case studies of major transnational corporations such as Apple, Google, Amazon, and Starbucks investigated in this research testify that the application of tax optimization/avoidance practices is very widely spread among transnational corporations, particularly the ones incorporated in the US and other high-tax jurisdictions. Companies may use different methods and tools with the aim of achieving minimization of their tax payments. Namely, such tools may include the use of foreign offshore tax jurisdictions with low tax rates for recording of profits in countries where low taxes are imposed, and the use of transfer pricing within the international business networks of corporations for the purpose of raising their levels of costs and thus minimizing the ultimate tax base.

Due to the fact that corporate tax avoidance/tax optimization practices cannot be eliminated using legal mechanisms (as such activities do not breach any regulations on either national or international level), they should be tackled from the ethical perspective. In this context, an important role may be played by International Financial Reporting Standards. As of today, IFRS already contain provisions on the mandatory disclosure of international corporate structure, which allows financial authorities tracking the re-routing of financial flows between related parties, which is one of the main tax avoidance methods.

Here, one of the main focal points is the fact that the information on how a company performs within its business activities and how much it pays for the public services consumed in the form of taxes should be available to all actors in society, and first of all to public authorities which protect the rights of society. This is a key precondition for the most effective public monitoring of corporate financial activities of businesses and thus the most effective interaction between society and the corporate sector.

In addition, revised IFRS could include provisions on the mandatory disclosure of companies' information on their tax payments in the breakdown into particular taxes. This could allow public authorities of states to have greater control over the particular taxes paid by such companies and over how they may manipulate their reporting with the aim of minimizing such tax payments.

Revised IFRS could also allow maximizing the effectiveness of cooperation between the governments of individual states with the aim of eliminating any tax avoidance practices leading to impaired effectiveness of public policies in the field of taxation, and thus to the overall impaired opportunities of states' economic and social development.

However, this is not enough. Revised IFRS could benefit from the inclusion of provisions on the mandatory disclosure of data related to tax optimization transaction and their impact on the amount of taxes paid, as well as from the clear distinction between taxable profits recorded in different jurisdictions. This could maximize the availability of the respective information to the public, and thus could lower the volume of tax avoidance activities run by companies due to their fear of social resonance.

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