

CHALMERS



Global Tax Efficient Company Structures

Master of Science Thesis in the Master Degree Programme,
Entrepreneurship and Business Design

EINAR EMILSSON

Department of Technology Management and Economics
Division of Management of Organizational Renewal and Entrepreneurship
CHALMERS UNIVERSITY OF TECHNOLOGY
Gothenburg, Sweden, 2014
Report No E2014:001

Abstract

This thesis presents the current tax situation for corporations in Sweden, the US and the Cayman Islands.

The purpose of this thesis is to answer the questions:

- What options are there for a Swedish startup company with global investors to structure themselves to optimize owners' ROI?
- How do the options available to a company starting in Sweden differ from starting in the U.S.?

Through literature readings and discussions with the Swedish tax agency the following results have been achieved:

Today intellectual property as well as the use of transfer pricing, internal borrowing and licensing are extremely important for tax avoidance. The location of physical and legal activities also makes a big difference for ROI for the investor as well as for the Entrepreneur.

The best options for a Swedish startup company with global investors to structure themselves to optimize owners' ROI are two-fold. The best one for the global investor is to set up a holding company in a low-tax jurisdiction. And the best one for the entrepreneur (through LLC) is to own stock directly in the startup company.

The difference between starting in Sweden and the US is for the entrepreneur. In Sweden they are tax-exempt if they own more than 10% of the company (through LLC), and then they only have to pay corporate taxes in the startup company. In the US the entrepreneur has a legal way of keeping the money away from any taxation by funneling profits to an offshore company and then not repatriating the profits.

Overall, the Swedish model is competitive, but tax havens still present a fairly tempting alternative.

Table of Contents

1. INTRODUCTION.....	4
1.1 CONTEXT AND DEFINITIONS.....	5
1.2 PURPOSE.....	8
1.3 METHOD.....	8
1.4 SCOPE AND/OR LIMITATIONS.....	9
1.5 OUTLINE.....	9
2. FRAME OF REFERENCE.....	10
2.1 BUSINESS TACTICS AND TRENDS.....	10
2.2 GOVERNMENT TACTICS AND TRENDS.....	11
4. EMPIRICAL FINDINGS.....	12
4.1 THE TAX SITUATION IN SWEDEN.....	12
4.2 THE TAX SITUATION IN THE US.....	15
4.3 THE TAX SITUATION IN CAYMAN.....	19
5. ANALYSIS.....	22
6. CONCLUSION.....	30
7. REFERENCE LIST.....	32
8. APPENDICES.....	39

Abbreviations

CFC: Controlled foreign company

CRS: Congressional Research Service (United States)

EEC: European Economic Community

EU: European Union

GDP: Gross domestic product

GOP: Grand Old Party, also known as the Republican Party (United States)

GST: Goods and Services Tax

IRS: Internal Revenue Service

FJE: Foreign juridical entity

LLC: Limited liability company

MORE: Management of Organizational Renewal and Entrepreneurship, Department of

OECD: Organization of Economically Developed Countries

PE: Permanent establishment

ROI: Return on investment

VAT: Value-added tax

1. Introduction

Why tax efficient structures are necessary for startups today.

Most fast growing start-up companies typically take in capital to be able to expand as quickly as reasonable. Experts say that the market is fast-moving today and rapid expansion is often needed to reach a leading market position. Economies of scale are becoming more and more important in a global economy that has made the market much bigger for most companies (Ernst and Young, 2013).

Usually investors want a good return on investment (ROI) and tax levels have a big impact on it. In most jurisdictions companies pay corporate tax before dividends and therefore the corporate tax level is important, as is the capital gains tax. Some jurisdictions are not as willing to let money cross borders without taxation as others are. As a result, there are competitive differences resulting from in which jurisdiction the start-up is located. Since the precedent was set to consider intellectual property, brands, and human capital as assets in the past 20 years, (Groves and King 1997, p. 135) the possibilities for moving assets to other jurisdictions seems to have increased, and thereby the possibilities for shifting tax liability have also seemed to increase.

Entities pay different amounts of tax depending on in which jurisdictions they are active and where their constituent parts are registered. Sovereign states around the globe have different tax rates and opportunities for deductions and exemptions. With industrialization and globalization the hindrances for movement of assets have eased. Capital as well as large companies and SMEs can today be located in places where taxes are favorable, even if most of the operations take place within the borders of high tax jurisdictions. When it comes to big companies almost all operate this way. Apple, Google (Bloomberg 2012) and G.E. (Buffet 2012) are some examples of such companies.

Different governments have chosen to act differently within their jurisdictions. Countries such as Sweden, Japan and Canada have corporate taxes in the twenties whilst countries like Russia, the Bahamas and Hong Kong have corporate taxes that are ten percent or lower. Some jurisdictions have specialized in specific industries to draw companies. Panama, for one, has specialized in boating.

There are cross-border organizations that try to oversee allocation of assets and tax liability such as the OECD and the EU.

The geographical shift in taxes from high-tax jurisdictions to low-tax jurisdictions has undoubtedly taken away funding for education, healthcare and infrastructure from high-tax countries. To prevent this, many countries have both made their laws in regards to tax avoidance stronger and they have also lowered profit taxes. The sharpening of laws has turned earlier tax avoidance into tax evasion. The overall trend in taxation has become to lower taxes that are based on movable incomes, such as corporate taxes, and increase taxes that are related to physical presence, such as sales tax and property taxes.

Since many companies work on minimizing taxes through planning, it becomes a factor when investors are making decisions on in what companies to invest. It's an area where there is no reason to lose a competitive edge.

1.1 Context and Definitions

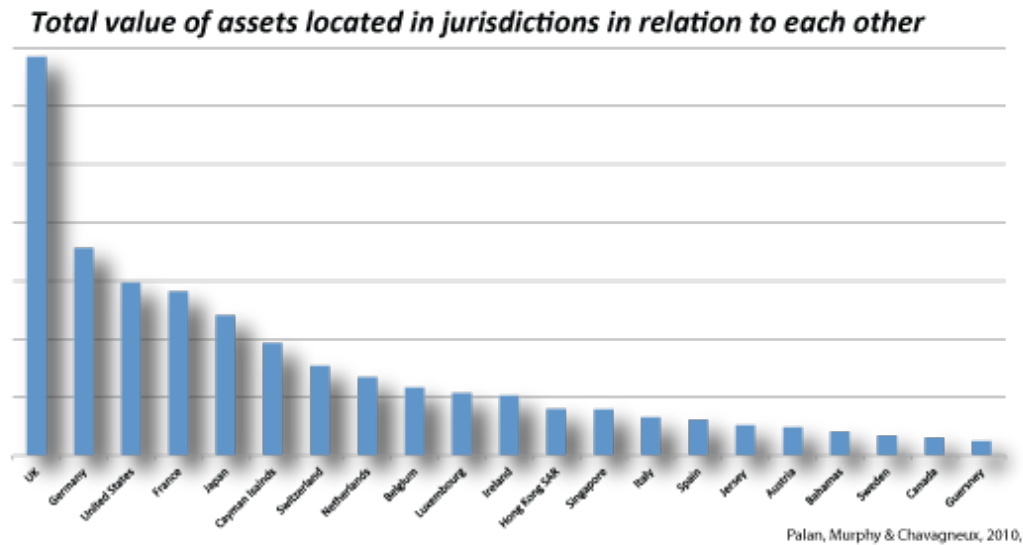
Tax Havens

If companies were unable to shift assets and capital across borders, the fact that there are jurisdictions with varying levels of tax and regulation would be irrelevant. However, recent decades have generally made such movement easier, and thus states that developed societal systems with relatively little or almost no taxation of companies have been able to benefit from companies' desire to minimize their tax bills. Countries that engage in this process are popularly known as tax havens.

It is difficult to define exactly what a tax haven is due to all the aspects that need to be taken into account. Low tax rates are perhaps the primary characteristic. However, other definitions also emphasize secrecy and weak regulations. After all, if a country has low tax levels but shares information with other countries then it may not be useful for tax avoidance. As one definition puts it: "[Tax havens are] jurisdictions that deliberately create legislation to ease transactions undertaken by people who are not resident in their domains, with a purpose of avoiding taxation and/or regulations, which they facilitate by providing a legally backed veil of secrecy to obscure the beneficiaries of those transactions". (Palan, Murphy & Chavagneux, 2010, p53)

The number of countries considered to be tax havens has been growing rapidly the last 30 years and they are nowadays-important players in the capital market. While it is clear that these tax havens play an important role in corporate planning, it's very difficult to estimate how much tax is actually avoided. (Palan, Murphy & Chavagneux, 2010, p. 67) Available US data recognizes that profits allocated to tax havens have increased over the last decades.

Lists of tax haven countries can appear to be an odd mix. Many are countries with a small population that once used to be part of a bigger country, such as the Cayman Islands, Jersey, and the Bahamas. However, some larger countries are also typically considered to be tax havens, such as Switzerland, the Benelux countries, Ireland, and even the UK due to its generous taxation laws for foreigners. Looking at the diagram below which describes assets located with the specific jurisdictions, there are some odd countries there. Cayman islands has the fifth most assets in the world. This makes it very interesting to look at. (HM Revenue & Customs, 2013).



Competition is intense between tax havens and as a result, many have developed different niche strategies to attract investment and transaction flows through special policies and laws. (Palan, Murphy & Chavagneux, 2010)

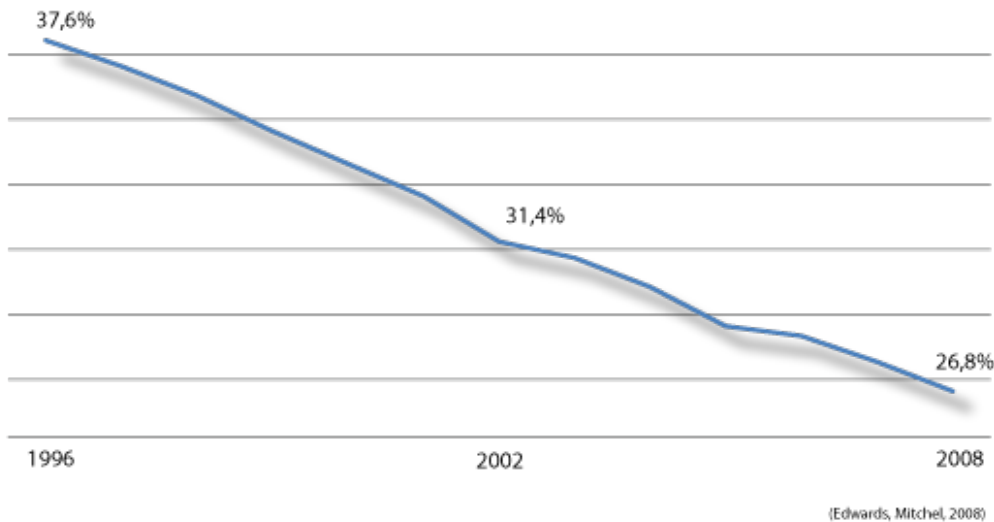
Types of Taxes

In order to understand why and how the variation in tax levels and regulations between jurisdictions matters, a brief overview of the types of taxes that exist in high-tax jurisdictions is necessary. In most developed countries, the main taxes for companies are corporate tax, corporate capital gains tax, sales tax and withholding tax (Berk & DeMarzo 2011, p. 6).

In this section, I will present these taxes and their evolution in recent decades.

Corporate tax is a tax on the annual profits that a corporation makes. These taxes are usually applied after a company's expenses are deducted. This includes interest, deductions and depreciations. Sixty years ago the world experienced a lot higher corporate tax levels overall than it does today. Due to several liberal political decisions this has changed. Between 1960 and 1980 the corporate tax averaged above forty percent in OECD area. During the 80s rapid change began. The United Kingdom took the first major step in the tax revolution and the Conservative Party's leader, Margaret Thatcher, led cutting corporate rates from a whopping 50% to 35%. Many other nations followed suit, including Australia, Canada, France Germany and Japan. (Edwards and Mitchell 2008, p. 43)

Corporate Tax Development 96-2008 in OECD countries



Looking at the countries within the EU the pattern is very clear. Likely due to internal competition, rates went down from 38% in 1996 to 24% in 2007. This is an average decline of close to two percent per year. (Edwards, Mitchel, 2008, p46)

If you look at different regions in the world they differ substantially in numbers. In the 2007 statutory corporate tax rates graph, the United States really sticks out. It's important to remember that deductions also play a big role, though. In the United States there are a lot of deductions that companies use to bring down the effective tax rates.

Corporate capital gains tax occurs when a company sells shares they own of another company (Edwards and Mitchell 2008, p. 50). European countries provide full or partial exemption of capital gains taxes when companies sell shares of subsidiaries (Washington report 2007, p. 68). Some of these nations are big industrial nations such as Germany (who very recently changed its rules to be more competitive), Ireland, the Netherlands, New Zealand, Spain, Switzerland and the United Kingdom (Warbuton and Hendy p. 158, p. 189). These countries make a tax efficient place to have corporate headquarters (Edwards and Mitchell 2008, p. 62). This is due to that an investor can make a profit on one company, sell that one and invest the money in another company, tax-free.

The capital gains tax differs from country to country. For example, in the U.S. there is no distinction between capital gains taxes for corporations or individuals, both of which are under most circumstances 15 %. In Sweden they are zero for corporations. Also, behind the company there is in the end a private person or a foundation that owns the corporation. Thus, there is yet another layer of tax and the effective tax rate is higher.

Withholding taxes are a tax on cross-border investments. It can be applied to royalties, capital gains, payments of interests and dividends to as well as foreign businesses as individuals. Over the years these taxes have decreased mainly by global tax competition.

Very often withholding taxes are regulated in tax treaties between countries. (Taxes on Cross-Border Investment, p. 51, Reuven Avi Yonah)

The Global Battle for Taxes

It is primarily high-tax jurisdictions, which typically are also wealthy industrialized nations that stand to lose from creative tax planning for tax evasion. The past couple of decades have seen an ongoing battle between governments, international organizations, and companies over tax havens and planning. As soon as governments figure out how to stop or discourage one tactic, companies seek out another.

The OECD has been particularly active in fighting tax havens and tax avoidance. They have developed a model bilateral tax treaty and facilitate the process for many countries to adopt these treaties. They also publish regular shaming lists -- white, grey, or black -- to publicize what they consider to be a given country's status in regards to tax avoidance and evasion.

1.2 Purpose

In this thesis I have taken the perspective of an entrepreneur and an investor, looking at how their ROIs are affected by where they operate and are domiciled.

The purpose of this thesis is to highlight the big differences in taxation and policy and the importance for startup companies to consider their corporate structure to be able in a competitive way are able to compete for capital. By providing this study I hope to be able to level the playing ground a bit between the big companies with unlimited resources and the startup companies mainly based in Sweden.

With this background I have come to ask the following questions for this thesis.

- What options are there for a Swedish startup company with global investors to structure themselves to optimize owners' ROI?
- How do the options available to a company starting in Sweden differ from starting in the U.S.?

1.3 Method

I have chosen to do a literature study on the legal tax situations in three different jurisdictions to be able to determine if Sweden is competitive for investments in startup companies. The literature reviewed includes books, articles legal documents as well as government documents. I also have interviewed the foreign department of the Swedish tax agency. I choose to do three jurisdictions to be able to compare two western countries and to have space for a low-tax jurisdiction.

The results of the literature studies are presented in Chapter 2 as well as in Chapter 4. The later mentioned chapter goes through a brief overview and history of the current

jurisdiction as well as the tax situation for companies. The analysis and the conclusion are based on the information presented in Chapter 4.

Based on the information in the empirical findings I set up 5 scenarios where I compare the tax burden and ROI over a five-year period for an global investor and a entrepreneur. To be able do this I chose to run the numbers over a fictional company. The numbers are based on a small startup with decent success.

I chose to compare the US and Sweden due to that Sweden is the country that I write my thesis in and US is the country where there are the most money available for start-ups. I chose Cayman Islands due to that it's the biggest tax haven, measured by assets located there.

1.4 Scope and/or limitations

This business plan is written as a 30 ECTS master's thesis in business design and its limitations are set by the timeframe and academic demands from the department of MORE. Due to this I have chosen to limit this theses to only look at the competitiveness of operating a company from Sweden versus an American company. Also, I have chosen to only look at one low-tax jurisdiction. These countries can be used as an example and the principles are to a big extent similar in most jurisdictions.

I am also limiting the thesis to only look structures that are strictly legal. The grey-area tactics will remain in shadows. I am a businessperson and I will take the perspective of a businessperson not a legal person. Due to the time-scope I have chosen to use the rates and context of 2012.

I have chosen to essentially exclude discussion of social security taxes and VAT. The reason for this is that social security works very differently in Sweden and the US but the costs for health are similar. Since VAT affects the sales on a specific market and has nothing to do with the owner-structure I have chosen not to look at VAT. I am of the opinion that corporate tax and corporate capital gains works very well to describe the principles.

I have only looked at holding company situations and thereby excluded insurance schemes and foundations. Both of those schemes are questionable from a Swedish legal perspective. This is also the case with advanced schemes to go around CFC regulations.

I have unfurtunately also not had time to write about how the situation would be for private people, but that would be a good subject for a PhD within the area.

1.5 Outline

This thesis contains 7 chapters. The introduction chapter with background, purpose, research questions and scope and limitations will first describe the current state of tax competitiveness. It will also introduce the questions for the theses. Chapter 2 contains

the frame of reference and some of the current literature. Chapter, 3, will describe the way I have gone about with doing my research. Chapter 4 is my empirical findings, where I will present the tax-situations and the context for companies operating in Sweden, the US and on the Cayman islands. In Chapter 5 will present a number of key factors that affects the overall tax rate. Chapter 6 will be my analyses and discussion with an example of a Swedish company and a US company in a five-scenario setup. Chapter 7 Conclusions and chapter 8 are my reference list and chapter 9 contains appendices.

2. Frame of reference

This chapter is dedicated to presenting some of the current written material in regards to the current tactics and trends regarding tax avoidance from the business perspective as well as the government perspective. It will also present some relevant terms in regards to the subject.

2.1 Business Tactics and Trends

During my research it's been hard to find concrete examples and recommendations to answer my questions. In the thesis presented by James Butler (2009) it's possible to read very vaguely about available structures and that they affect taxation levels but it is very difficult to understand how to actually go about the problem and which taxes affect the overall taxation level of the company.

There are, however, some existing materials on the topic. I will break down this existing research by reviewing some of the most commonly discussed strategies.

Broadly speaking, companies typically practice tax avoidance either shifting income and profits from high-tax jurisdictions to low-tax jurisdictions. There are two essential categories of tactics that are practiced across the world.

The first category is *transfer pricing* (Palan et. al 2010). To perform transfer pricing, companies usually play with the values of goods and services sent across borders between parent companies and subsidiaries (one located in a high-tax jurisdiction and the other in a low-tax one).

This can be achieved by undercharging for exports to subsidiaries in low-tax jurisdictions, or vice versa, by overcharging for imports. On the export side, companies can misreport quality or quantity and/or the price of the good or service. The goods are then sold from the tax haven at full value, the excess earned on onward sale being the value of the flight capital. Another way is creating fictitious transactions for which payment is made.

On the import side, assets are commonly owned in a low-tax jurisdiction and then leased, rented out to the high tax jurisdiction. This can be the case with things like ships and oilrigs as well as brands and logos. (Palan, Murphy & Chavagneux, 2010, p. 69)

The licensing of intellectual property like brands is particularly common because the rules in place to prevent transfer pricing are difficult to apply against it. The OECD has the concept of “arm’s length pricing” This is fairly straightforward for something like an oil rig, but it’s basically impossible to pin down the market value of something like the Starbucks logo. As a result, companies have a lot of flexibility here and it’s an excellent tactic for reducing tax liability.

To regulate the exploitation of transfer pricing, the OECD has released guidelines for jurisdictions and multi-national corporations. In the Transfer Pricing Guidelines they define “the arms-length principle” which is that sections of a company in different jurisdictions should pay each other the same for goods and services as they would get from other, unrelated companies.

In theory this should prevent transfer pricing and to some extent it does. The principle regulates both buying and selling transactions as well as deals and money transfers that are contractually regulated. (Transfer pricing guidelines, p. 32). However, Gravelle describes in her report, “Tax Havens: International Tax Avoidance and Evasion” (2010) how companies get around this. Though the OECD requires in principle that such goods transferred between affiliates should be at market value, in practice it is tricky to know what would be a market price for many of these goods and assets. This is particularly easy for companies when it comes to intellectual property, which is typically not comparable to anything else. (Gravelle 2010, p. 9)

The second category is to shift income is through *debt allocation* to high-tax jurisdictions, in part because increased debt decreases profits and equally important, because many of high-tax countries allow deduction of interest paid on debt, according to Berk and DeMarzo in the book *Corporate Finance* (2011). This is called the interest tax shield. These rules can be used to a company’s advantage by lending money from a subsidiary in a low-tax country to one in a high-tax country. The high-tax-based company pays interest, which then brings down their profit and tax liability whilst income in the low-tax jurisdiction goes up. (Berk & DeMarzo, 2011 p.157, p. 480)

2.2 Government Tactics and Trends

To give a sense of the scope of global tax avoidance, Gravelle’s report, written for the U.S. Congressional Research service (2010), estimates the size of global tax evasion by comparing the fact that the G8 countries have 32% of the world’s pre-tax profits and 38% of GDP. The tax havens together with the Netherlands have 6% of the world’s GDP and 44% of the world profits.

The future of the distribution of profits and GDP is not clear however, because several trends show that countries are pushing to compete with tax havens on the one hand and fight them on the other.

In terms of competing with tax havens, there is an ongoing trend of countries decreasing tax rates on moveable income, like the corporate tax rate, while increasing tax rates on immovable income, like taxes on sales, property, and natural resources, according to Loughlin’s report for KPMG (2010). Hickey also talks about this trend. Niall Cambell of

KPMG Ireland speaks directly to the trend on immovable income, observing that that many countries are introducing or increasing national VAT/GST regimes. Some of these countries are UK, Spain, Greece, Finland, Poland, Romania, New Zealand and Portugal. He also mentions that the US might consider a full VAT system, but politicians are not fully there yet.

In terms of fighting tax havens, there seem to be a few trends/predictions observed by people knowledgeable on the topic. Kennekens predicts that companies will more aggressively go after transfer pricing adjustments. He also foresees changes in the deductibility of interest in countries like Sweden and Germany, as common tax avoidance tactics become better known. Another less common trend that he observes and predicts, mostly limited to Oceania and South Korea, is a breakdown of the global system of bilateral tax treaties – that in order to protect domestic tax revenues, countries will instead violate tax treaties with other countries through court cases.

Another major actor in fighting tax havens is the OECD, which James Butler focuses on in his Master's thesis, "Illojal skattekonkurrens: OECDs arbete gentemot skatteparadis." James Butler claims that the OECD and the EU have now put a lot of resources in facing the harmful tax competition happening in the world. Like many other authors, his opinion is that the amounts of money flowing through tax havens are steadily increasing, often by invoicing of services from a low-tax country to a high-tax country.

Despite the increased work of the OECD and the EU, however, Butler claims that the question of whether countries will be able to better limit tax avoidance depends also on the action of American politicians, who are not particularly aggressive in targeting tax avoidance.

In response to these trends, KPMG's report also highlights how business should prepare for these trends. Regarding the shift in taxation types, Loughlin says that active management of the increasing indirect taxes will be important. Ways of doing this he says are making tax efficient supply chain management decisions as well as making sure not to have any unrecovered VAT/GST that a given company is entitled to.

At the same time, KPMG's companies should try to influence indirect tax reforms, respond after the market impact, increase automation by the use of new technology and understand local cultures and tax environments.

Overall, it will continue to be extremely important for companies to be highly aware of tax regulation in the jurisdictions where they are active as these regulations continue to involve.

4. Empirical findings

4.1 The tax situation in Sweden

Sweden is a relatively small country located in northern Europe. It has a population of nine and a half million people (SCB 2012) and GDP of \$475 Billion, (Skatteverket 2011,

p. 104) with a corresponding GDP per capita of about \$50,000. Most of its economy is made up of services, media and manufacturing. It is considered to be one of the most stable countries in the world. It is parliamentary and there are a clear right and left wing alternatives. Both the right and the left wing are pretty close to each other when it comes to taxation. There is a civil legal system. There are three stages where the "Högsta Förvaltningsdomstolen" has the final say in tax questions. (Wikipedia 2013, "Förvaltningsdomstol")

Sweden is very active in the OECD and has tax agreements with most other countries in the organization. This has led to that a lot of people and companies with high incomes move away from the country since it's difficult to successfully place money in tax havens. IKEA, for example, is run through a Dutch company that is owned by entities in Liechtenstein and the Dutch Antilles. (Wikipedia 2013, "Ikea")

The country was poor in the beginning of the 20th century and there were high levels of emigration. Sweden stayed out of both the world wars and by that kept much of its production capacity. During the 50s, 60s and 70s the country built the social model it still has today. It is egalitarian with high taxes and high levels of redistribution. With highly developed infrastructure and investment, it is also one of the few countries that has a balanced budget. The total tax revenue makes up 45.5% of GDP. The total tax borne by juridical entities in 2009 was \$21.5 Billion. Of that amount, limited liability companies, banks and insurance companies paid 89%. In Sweden there are a lot of small companies, very few mid-sized companies, and a few big ones. 0.03% of the companies pay 24% of the total corporate tax (Skatteverket 2011, p. 8)

Mapping of the tax situation from a legal perspective

The statutory corporate tax rate in Sweden is currently 26.3% (2012). Until 1989 the tax was 52% but when the tax code was restructured in 1990-91 it was first lowered to 40% and then to 30%. 1994 it was once again lowered to 28%. Then it was not touched until 2009 when it went down to 26,3% (Ekonomifakta 2012). Together with social security and the other forms of income tax it makes up 75% of the tax revenues.

The Swedish Government has now lowered the corporate tax to 22% starting on January 1, 2013. This would once again make Sweden's corporate tax lower than the OECD average (Regeringskansliet, 2012). In 2011, total corporate tax revenue was equal to 3,2% of GDP. (Skatteverket 2012b, p21) In terms of basic principles of taxation, it's important to note that in Sweden, companies' losses can be carried forward indefinitely as a deduction from subsequent years' profits.

The sales tax rates in Sweden range between 6% and 25% (Skatteverket 2012a). Everything is taxed at 25% except food items (12%) and transportation and literature (6%). Sales taxes are a major factor of total taxation in Sweden, with total revenue of close to 10% of the Swedish GDP. It has steadily risen from mid 1960s when made up around 5% of GDP. The sales tax functions as a value-added tax (VAT), meaning every step in the value chain pays their difference between sales and purchases.

The corporate capital gains tax is 26.3%, generally speaking. However, there is a very important exception, which is when a company residing in Sweden is a shareholder of stock in another Swedish or EU company and the relationship fulfills at least one of the three following conditions: first, that the shareholding company owns at least 10% of the company, second, that they are considered as being in control of the other Swedish or EU company, or third, that the other Swedish or EU company is public (FaktaBank 2001). If any of these are fulfilled, then the Swedish shareholding company is exempt from taxation on dividends and sales of that stock. This makes the corporate capital gains tax only apply to smaller investments (Deloitte 2012).

In the case where a Swedish company owns a part or all of a company that resides outside of the EU, the applicable tax law becomes more complicated. These companies are called foreign juridical entities (FJE). An FJE is an association that in its home jurisdiction can take on responsibilities and liability and act in front of a court and other institutions, and individual owners cannot individually make decisions over the assets in the association. Foundations are normally not considered to be associations because specific people do not own them. (Skatteverket 2011b, p. 165)

Foreign companies that have operations or do business in Sweden are, generally speaking, tax subjects of Sweden only for dividends or sales of stock. Corporate tax is paid in their home jurisdiction. However, this is only the case if the company is taxed in a similar way and amount as it would have been in Sweden, meaning corporations in jurisdictions that apply revenue taxes, fixed yearly fees or jurisdictions that have a low or no corporate tax are liable for corporate tax in Sweden. To determine the level, the actual amount of taxes paid should be about 15% of profits (Skatteverket 2011b, p. 167). Companies residing in countries that have full tax agreements with Sweden are considered foreign (Skatteverket 2011b, p. 167). If a company qualifies to be in this category, then there are no special taxes applied. There are exemptions, for example holding companies in Luxembourg are more or less tax-exempt.

Investment funds that invest in Sweden have limited liability for taxation. Thus they are subject to taxes on income from permanent establishments (PEs) or property in Sweden, both from ongoing revenue as well as income from one-time sales; income from dividends in economic associations; income from that derives from income reinstated from periodic funds, reinstated deferral amounts and imputed income. Compensation in royalty or periodical fees for property as shall be looked on as income from a PE in Sweden. (Skatteverket 2011b, p. 57)

Swedish entities that are fully liable for tax in Sweden are taxed on the income of the FJEs that they own. The profits are considered liable for taxation according to Swedish standards, no matter if the profit has actually been distributed as dividends or not (5 kap. 3 § IL). If the shareholder has been taxed continually on the income of the company, then the shareholder is not subject to additional tax when and if dividends are distributed.

A shareholder with limited tax liability in Sweden is not taxable for their part of the income even if the juridical foreign entity has income in Sweden (5 kap. 2 a § IL)). Instead, the tax is put on the foreign entity with operations in Sweden or property in Sweden. (6 kap. 7 och 11 §§ IL) (Skatteverket 2011b, p. 168)

For Swedish entities that own FJEs that own other, where the owner-company is in a low-tax jurisdiction (judged as a corporate tax rate lower than 14.5%), the Swedish juridical person gets taxed continually on the income from both these companies. This only applies if the Swedish juridical person controls 25% of that company, either by themselves or in partnership with other companies to which they have direct or indirect ties (through other foreign companies). If the foreign company is similar to an economic organization or a limited liability company then the company can be considered to obey under the 3:12 rules. As a result, the Swedish juridical person's income would be taxed as income of service rather than capital. These are what are called the CFC rules. There are countries that are exempt from the main rules; these countries are listed under the attachment 39a in IL (the US is among these, but the Cayman Islands are not). If the holding/owning company is within the EES and there is a real establishment (at least an office and some basic office supplies) then they are exempt from the CFC rules. (Tax Rate Guide 2012b; Skatteverket 2011b, p. 169)

Foundations are usually not considered an association because they don't have any owners or members. Thus, they are generally speaking exempt from CFC taxation. (Skatteverket 2011b, p. 165)

Withholding tax revenue is equivalent to 0.1% of Swedish GDP (Skatteverket 2012b, p. 21) if dividends are paid to from a Swedish company to a foreign company or person; a 30% withholding tax is applied. There are tax-treaties with some countries that lower this. In the particular case of cross-border investment with the U.S., the two countries have settled on a 15% withholding tax (Skatteverket 2012c). There is no withholding tax on payments of interest or royalties. A royalty payment to a foreign recipient, however, may be deemed to constitute a PE for the foreign recipient and be taxed at the corporate rate. This tax only applies to company profits calculated on an annual basis.

4.2 The tax situation in the US

The US is the world's biggest economy and it has been so for the last 50 years. Its GDP is a bit over \$15 trillion (CIA 2012) and the population is 314 million (Census 2012). This makes the GDP per capita \$47,700. Considering GDP composition, 1.2% is agriculture, 19.2% is industry, and 79.6% is services (CIA 2012). In 1984, the top one percent of income earners received 8.4% of national income, while following tax reform 1989 it had increased to 13.5%. The effect of the 1986 reform on this shift has been subject to several economic studies. (Altig and Carlstrom 1999)

The United States is a federal constitutional republic. The power of governance is shared both between the federal government and the fifty states, and between the three branches of the federal government itself. The three branches are the executive, the

judiciary and the bi-cameral legislature known as Congress and the Senate (U.S. Constitution, 1789). The states have nothing to do with tax law when it comes to international, multinational or even multi-state companies (Wikipedia, "Commerce Clause," 2012).

While Congress has the primary responsibility for writing laws, the President and the executive branch have certain powers which have particularly evolved in recent decades that allow them to legislate. Even if the Congress writes the law regarding taxes and tax collection, it is the Internal Revenue Service that interprets the laws and issues specific rules and instructions for how the law is to be carried out. (Wikipedia, "Internal Revenue Service," 2013)

The U.S. has bilateral tax treaties with dozens of countries. Thus, if the residents of these countries invest or earn money in the U.S., they are subject to lower tax rates than they might otherwise be if their home countries did not have a treaty with the U.S. However, there is only one country with which the U.S. mutually shares information, which is Canada (IRS, 2012). As a result, the rest of the treaties that the U.S. has do not contribute a great deal to limiting or inhibiting offshoring of money and accounts.

Mapping of the tax situation from the legal perspective

The total tax burden is about 15,3% of GDP. If social security and other programs its 22% of GDP (2001 estimate). The U.S. has the 193rd highest tax burden in the world. (CIA 2012)

Though the statutory tax rates of the US are one of the highest in the world, the actual tax collected is low compared to the average among OECD countries. In 2006, the revenue from corporate taxes was 189,4 billion or 1,6% of GDP (U.S. CBO 2005, p. 11) on top of this there is another .5 % on average of local corporate taxes. In 2010 the corporate tax revenue made up 1,3% of GDP (Kocieniewski 2011) and 9% of the total of US federal tax revenue. The statutory corporate tax brackets ranges between 15% and 40% (IRS 2010). It has been the same since 1986 (TRA 1986). There are eight brackets, with profit over \$75,000 taxed at 34% or more (IRS 2010).

It's not just low relative to other countries' corporate tax burdens. Citizens for Tax Justice claim that America effectively has one of the lowest corporate income taxes of any developed country, despite having one of the highest statutory rates. They have examined 280 profitable Fortune 500 companies and found that the average effective corporate tax rate paid was 18,5%. This is lower than the OECD average (CTJ 2012a). There are a couple of reasons for this. First, there are a large amount of deductions and subsidies on taxes, which vary by industry. Depreciation and investment rules can also play a major role. Perhaps most importantly, there is a special rule about profits made and kept abroad. (CTJ 2011)

If a U.S. company has its headquarters inside of US borders are liable for income tax on all its income; it does not matter where in the world it has been earned. However, they only technically have to pay these taxes once they repatriate the profits. If a company decides to hold those profits abroad, they can delay payment of these taxes indefinitely.

As a result, there are a lot of companies that choose never to repatriate profit to the US or do so only when there are tax exemptions or holidays for repatriation. This brings down the overall rate. (RPC 2012)

A lowering of the statutory tax rates is likely within the next few years. Both the Republican Party as well as the Democratic Party has in their election platforms for 2012 to lower them (RATE 2012). In the Democratic platform for the 2012 election we can read: "We are also committed to reforming the corporate tax code to lower tax rates for companies in the United States, with additional relief for those locating manufacturing and research and development on our shores, while closing loopholes and reducing incentives for corporations to shift jobs overseas." (Democrats, 2012). Similarly, in the Republican platform for the 2012 election, "American businesses now face the world's highest corporate tax rate. It reduces their worldwide competitiveness, encourages corporations to move overseas, lessens investment, cripples job creation, lowers U.S. wages, and fosters the avoidance of tax liability – without actually increasing tax revenues. To level the international playing field, and to spur job creation here at home, we call for a reduction of the corporate rate to keep U.S. corporations competitive internationally, with a permanent research and development tax credit, and a repeal of the corporate alternative minimum tax. We also support the recommendation of the National Commission on Fiscal Responsibility and Reform, as well as the current President's Export Council, to switch to a territorial system of corporate taxation, so that profits earned and taxed abroad may be repatriated for job-creating investment here at home without additional penalty". (GOP 2012)

For both domestic and multinational corporations, another important rule is that net operating losses can be applied both backwards and forwards (IRS 2013, "Publication 536") but since all companies engage in this it is not particularly distinguishable for international investment and business development.

Since the "Bush tax cuts" between 2001-2003, the taxation rate for both dividends and long-term capital gains has been at 15% (Carroll and Prante 2012, p. 1). A big difference to many other countries is that companies in the U.S. are taxed first on the dividends or capital gains, and then that income also counts towards taxable corporate income. This creates double taxation.

Withholding tax is 30% if there are no specific tax agreements with a given country (U.S. IRS, 2008).

Common practices / Loopholes

Despite high statutory rates, many big American companies pay almost no corporate tax in the US. This includes companies like General Electric, Boeing and Wells Fargo. Citizens for Tax Justice (CTJ) released a report where they disclosed numbers for some companies. General Electric paid during the period 2002 to 2011 an average corporate income tax of 2.3%. (CTJ 2012b). Other companies take it even further, for example was Boeing's effective federal tax rate over those ten years was negative 6.5% (CTJ, 2012c).

A report from the Congressional Research Services (CRS) report brings up several of the above-mentioned methods of tax avoidance as some of the main ones used by major companies. Multinational companies are not taxed on their income until they repatriate the profits to the US parent company as dividends. Also, when repatriating money, the foreign tax credits are paid on an overall basis. Which means that taxes paid in a high-tax jurisdiction can offset the offsets from income in a low tax jurisdiction. One study observed by the CRS claims that shifting of profits between high and low-tax jurisdictions are due to transfers of intellectual property, intangibles and through the allocation of debt. (Gravelle 2010, p. 8)

In general, interest is deductible like in many other countries. There is an exemption if the IRS assumes that lending/borrowing to a related foreign company are for tax evasion reasons. This happens if the debt to equity is more 1.5 to 1 in the borrowing company and the net interest of those loans exceeds 50% of adjusted income and the interest is bigger than half of the income plus depreciation. (Gravelle 2010, p. 9)

Since interest is deductible in the US, companies can borrow in the US to finance operations abroad, make money on that investment abroad and then keep the profits of the mainland. In this way they don't have to pay US corporate taxes but they get the deductions on lending. (RPC 2012)

To be able to transfer profits abroad transfer pricing is used a lot by American companies. The US has a similar definition of transfer pricing as the OECD does. The CRS describes it as, "To properly reflect income, prices of goods and services sold by related companies should be the same as the prices that would be paid by unrelated parties. By lowering the price of goods and services sold by parents and affiliates in high-tax jurisdictions and raising the price of purchases, income can be shifted" (Gravelle 2010, p. 9). CRS also acknowledges that intellectual property and intangibles such as inventions and new drugs are hard to value.

In the US there are tax credits for research and development and deductibility for advertising to establish brand names. The CRS believes that the combination of these two things makes overall tax rates for investment in intangibles low, zero or negative. They also believe that when companies cost-share the development of products it's more difficult for the tax surveyors to know where assets should be located (Gravelle 2010, p. 11)

Another major category for evasions is something called the "check-the-box" provisions. The concept was created to make it easier to define if an entity is a corporation or a partnership in regards to US tax law. When applying this to foreign companies a loophole have appeared and a lot of hybrid entities have been created through the "disregarded entity" hole. This means that an entity is a recognized corporation in one jurisdiction but not in another. One common way of using this setup, CBR claims, is that a parent company in a low tax-country lends money to a subsidiary in the high-tax jurisdiction. This common method results in deductible interests for the high-tax jurisdiction company, due to that the high-tax jurisdiction recognized the two companies as separate corporations. Under normal circumstances the high-tax

jurisdiction would consider the two entities being one and then the interest would not be deductible.

4.3 The tax situation in Cayman

The Cayman Islands are located in the Caribbean Sea, south of Cuba. It is a British Overseas Territory. In total there are three islands: Grand Cayman, Cayman Brac and Little Cayman, which together make up a land mass roughly the same size as Washington D.C. (Wikipedia, 2013, "Cayman Islands"). According to legend the islands became free from taxation by their British rulers after an incident on the February 8, 1794. On that day, Cayman sailors rescued 10 English ships that had struck a reef (known as Wreck of the Ten Sails). One of the ships had onboard Prince William, son of King George III. As a reward King George III promised that the islands would never have to pay taxes to the Commonwealth. This was the starting point for what was to become the biggest tax haven in the world (Wikipedia, 2013, "Cayman Islands"). Over the years the Cayman government has made sure to preserve and specialize this competitive advantage. It has served the country well and made it one of the richest in the world. When telecommunications and flights developed in the 1950s the international finance and tourism really took off. Today there are more than 85,000 companies licensed or registered on the Cayman Islands. (U.S. Dept. of State, 2012)

The Cayman Islands has the fourth highest purchasing power parity in the world, with 131.6% of the American dollar's purchasing power (Economist 2012, p. 27). One of the reasons for this is the high employment, almost all adults work. The proportion of the population in working force is 68.4% (Economist 2012, p. 58), which is after only Qatar and Guam (each particular for different reasons) on the world list of this metric. In spite of that the Caymans are a financial powerhouse, they are tiny in terms of population. There are 54,878 (Wikipedia 2013, "Cayman Islands") people living on the islands and, interestingly, 170 of them are working at the central bank, the highest per capita percentage in the world (Economist 2012, p. 22). The country has managed to attract a lot of wealthy people from other countries: 63% of the population is foreign. (Economist 2012, p. 22)

The Cayman Islands have two registered companies for every resident and \$41 million dollars in bank assets per resident. They also have one mutual fund or hedge fund per 5 residents. (U.S. Senate Committee on Finance, 2008)

The Cayman Islands have specialized in banking, hedge fund formation and investment, structured finance and securitization, captive insurance and general corporate activities (Wikipedia 2013, "Cayman Islands"). This strategy has made them the fifth largest banking center in the world with branches from 40 of the 50 biggest banks in the world (Economist 2007). Total banking liabilities are \$1.5 trillion spread over 279 banks. Only 19 banks have a license to do business domestically. The rest are only allowed to do business with international customers. (U.S. GAO 2008b, p. 7)

Overall, the financial service sector employs 36% of the workforce and generates 40%

of the government's revenue (CIMA 2008). Other industries are tourism (30-40% of GDP), construction and furniture. The tourism industry is mainly based on scenic beaches, scuba diving and turtles. When it comes to export the main products are turtle products and manufactured consumer goods. Total export is estimated to \$17 million and total import of goods is estimated to \$795 million. A big part of that is food and consumer goods. (U.S. Dept. of State, 2012)

The Caymans are often seen as a prominent option for offshoring due to that's its stable, complies with international standards and that it has a friendly regulatory environment. Starting a company on Cayman usually costs less than \$600. (U.S. GAO 2008a, p. 4)

The political system is democratic parliamentary. They are self-governed but also a British overseas territory (U.S. Dept. of State, 2012). The current constitution was written in 2009. The country has a cabinet containing 20 seats where the members serve for four-year terms. There are two main parties, the people's progressive movement and the united Democratic Party (U.S. Dept. of State, 2012). The ruling power is split between the cabinet and the legislative assembly and the government. The head of the government is a governor that is appointed by the United Kingdom. The governor's area of responsibilities is civil service, defense, security and external affairs. On top of this, he also appoints the Chief Secretary, the financial secretary and the attorney secretary. He also is the chairman of the cabinet. (U.S. Dept. of State, 2012)

The Premier is an elected politician that leads the country and is also the minister of financial services, tourism and development. The chief secretary, indirectly appointed by Britain, is the highest civil servant. The UK government has the right to veto bills. The law system is built on the UK system and then mixed with local statutes. The highest court on the island is the Cayman Islands court of appeals and above that is Her Majesty's Privy Council in London. (U.S. Dept. of State, 2012)

Companies that choose to incorporate on the island are regulated under the "company's law". The same law controls foreign entities that do business on the Cayman Islands. (Tax Rate Guide 2012a)

Mapping of the tax situation from the legal perspective

The Cayman Islands are a major offshore center as they have no direct taxes (U.S. GAO 2008b). There is no corporate tax, withholding tax, sales tax, income tax or corporate capital gains tax. (PKF 2010). There are no estate or death taxes payable on Cayman Islands real estate or assets held in the Cayman Islands (Wikipedia 2013, "Cayman Islands").

All companies are obliged to pay a fee that is levied on the share capital of the company (Tax Rate Guide 2012a). All local businesses in Cayman Islands require a license and an annual payment is made dependent on the type and size of the business (Tax Rate Guide 2012a). Financial institutions are charged flat fees that range between \$3000 and \$500.000 (PKF 2012) as well as that they have to pay for work visas for the foreign workforce that are active on the islands. The visa fees ranges from \$500 to \$20.000 (Tax

Rate Guide 2012a).

Instead Cayman Islands government receives the lion's share of its revenues from indirect taxation. There are different kinds of stamp taxes, for example import duties from 5% to 22% (Wikipedia 2013, "Cayman Islands") levied on goods imported into the islands. Some items are tax-exempt like baby formula, books and cameras but taxes on automobiles can reach up to 40% for exclusive models (Tax Rate Guide 2012a). Real estate has a stamp duty between 7.5%-9% and a 1.5% tax on mortgage duties when a transfer exceeds a certain value (PKF 2010). There are flat licensing fees on financial institutions and there are work permit fees on foreign labor.

The Cayman Islands have tax treaties with the UK, New Zealand and Japan. They also have many tax information exchange agreements. In 2002 they entered a legal assistance treaty with the US, though it does not cover fiscal matters, as well as a tax information exchange treaty. The treaty allows among other things the countries to exchange information in regards to people that are suspected of tax evasion.

In 2009 Sweden signed an information treaty with Cayman and in 2009 and 2010 Cayman signed with G7 and the OECD members. By this Sweden can request information about suspected tax criminals (Lowtaxnet, 2013). In recent years the Cayman Islands has entered into various international anti-narcotics trafficking and anti-money-laundering agreements (Tax Rate Guide 2012a).

The use of Cayman Islands for tax avoidance and evasion.

According to Max Baucus, a US Senator, tax evasion through Cayman costs the US tens of billions each year (U.S. GAO 2008a, p. 2). Former U.S. Senator John Kerry described the strange situation that is the Caymans: "Here, you have this island area, 1.5 miles, something like that. It is about the size of Washington, DC. There are 47,000 residents, a lot of water, and a lot of sand, not a heck of a lot of production of anything. Yet, you have, what is it, 277 licensed banks, over 80,000 registered companies, more than 9,000 registered investment funds, 760 captive insurance companies, and, according to the Department of Treasury, U.S. investors held \$376 billion in Cayman-issued securities". (U.S. GAO 2008a, p. 18)

In George Town on Cayman island, the law firm Maples and Calder owns a house called the Uglund house. The building has 18 857 entities registered at its address (Davis 2009). BBC writer Nick Davis quoted U.S. President Obama as commenting, "That's either the biggest building in the world or the biggest tax scam in the world" (2009).

The building came to the world's knowledge in 2008 when it was the object for an investigation of tax evasion. Maples and Calder estimate that 5% of the registered entities in the building are fully owned by Americans and that 40-50% have some kind of US connection. Most of the entities are related to investment funds or structured finance. These kind of financial vehicles registered there are typically not present on the owner's balance sheet and are therefore hard to track. They are often owned by a trust; another offshore entity or ownership is spread over the world. The main reason for establishing companies in Cayman is to gain business advantages, including the advantage of minimizing tax. The registration also offers a way for investors that do not

want to have any direct business in the US. (U.S. GAO 2008a, p. 4)

There are very few of the Uglund entities that carry out any business activities on the Caymans. A matter a fact, 96% of all entities there (18.857) were classified as exempted entities by Cayman law. This meant that they are not allowed to do any business on Cayman, but instead they are tax exempt. (U.S. GAO 2008a)

A foreign company has a few different kinds of types of companies to choose between when registering in Cayman. The two most common ones are ordinary Nonresident Company and Exempt Company. The main differences between these two types of company are that an Exempt Company is allowed to issue bearer shares, use foreign terms in its name, and has fewer filing formalities. (Tax Rate Guide 2012a)

Other differences are that the ordinary non-resident company must hold a register of members in the registered office, which is open to a public inspection and its name must end with Ltd or Limited. The financial authority issues a certificate of a non-residence status and information on such a company's shareholders must be provided. Financial accounts must be kept, but they need not be audited. (Tax Rate Guide 2012a)

An exempt company may issue bearer shares, it need not hold shareholders' meeting in the Cayman Islands. There are no obligationS to send in a list of shareholders to the authorities on an annual basis. A certificate of Tax Exemption for 20 years may be obtained, this works as a protection if laws change within Cayman. It's important especially due to that the UK has such influence on the island. The certificate can be renewed by 10 years on expiry. This type of company is often chosen for the purposes of collective investments. The annual upkeep for the company is \$1932. (Higgs & Johnson, 2013)

Cayman Islands Trust

Trust legislation of the Cayman Islands is based on English trust law. Only a company that has obtained a trust license must offer trust services on the Cayman Islands. Cayman Islands Trusts need not be registered. However, those trusts, which want to obtain an exempt status, must be registered with the Registrar of Trusts. (Tax Rate Guide 2012a)

5. Analysis

I have found some aspects that a Swedish startup company with global investors should consider when structuring themselves to achieve highest possible ROI. My research only covers a very specific case, but the principles should be similiar in other cases as well.

I have found that the movability of assets to low-tax districts is key to tax optimization. Some assets are easier to move and while others are more difficult. The way companies

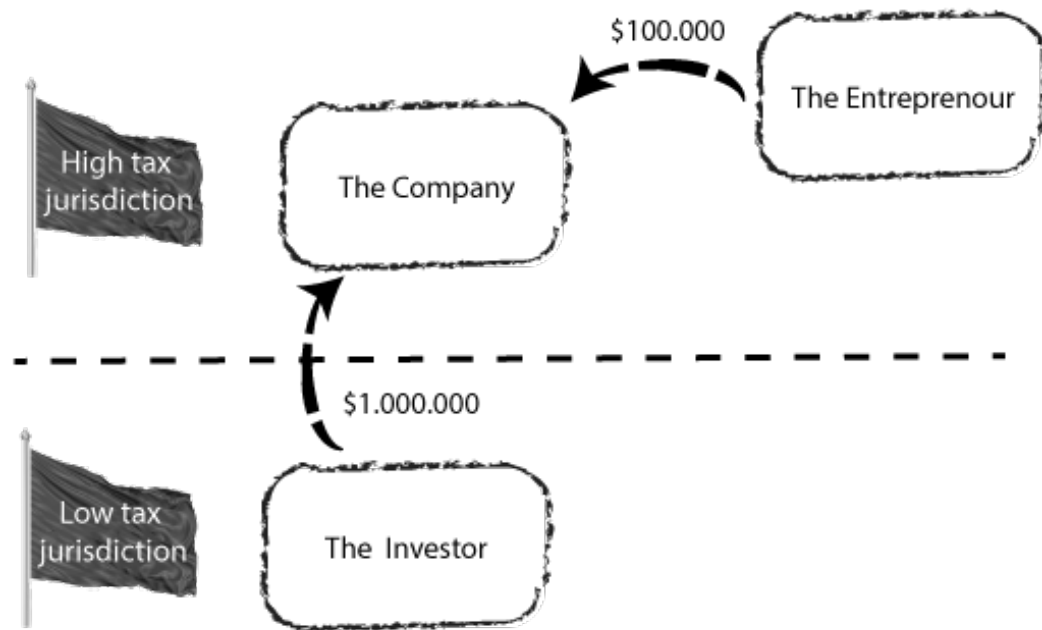
are financed can make a huge difference to the total tax burden. This is because interest is often deductible in high-tax jurisdictions and thereby it brings down profits and then withholding taxes as well.

As seen in the literature study there are a lot of companies that uses not only lending but also transfer pricing, allocation of intellectual property, leasing and even made up invoices to be able to move profits and thereby pay less corporate and withholding tax. The principle is mainly to lower the profits in the high-tax jurisdiction and move them to low-tax jurisdictions.

Tax treaties can play a very important role in where to allocate the different parts of the company but also in what form to do it. But at the same time the treaties only works to a limited extend due to that there at least in the case of Cayman and Sweden, must be a suspicion about illegal activities on a entity or person for information to be exchanged. Also, due to that you can register companies in for example the Cayman Islands without registering who owns it with the state (must be registered with the firm) its very difficult to track who owns what anyways.

The two biggest tax exemptions that I have found in is that in Sweden if a company own more then 10% of another company they don't have to pay any tax on dividends and sales of that particular stock and that in the US companies can chose not to repatriate profits and then they don't have to pay taxes on it. None of these seems to be changing any time soon.

The options I have found that are available and sensible for tax optimization, for a Swedish company as well as for an American company are either to be directly located in Sweden/USA, or to set up a holding company in a foreign low-tax jurisdiction. I will give an example of how the tax implications can look like for a Swedish or American entrepreneur ("the Entrepreneur) and a global investor ("The Investor) when starting a company in Sweden/the US. The Entrepreneur has a local limited liability company and the investor has an exempt company in the Cayman Islands. The entrepreneur has put in \$0.1 million in equity and the investor has put in \$1 million. The entrepreneur and the investor own equal parts of the stock. The company's value is based on a movable, protected intellectual property.



In the example I used the following number: After five years the company has \$10 million in revenue and a 10% pre-tax profit. The revenue has grown for each year and so has the profit margin. The revenue has doubled each year with the first year revenue of \$1 million. Profit has grown five-fold, as the pre-profit margin was 2% the first year. Each year half of the profit has been taken out as dividends. Sales are all over the world. After these five years, the company gets acquired for five times its after-tax earning plus its own equity.

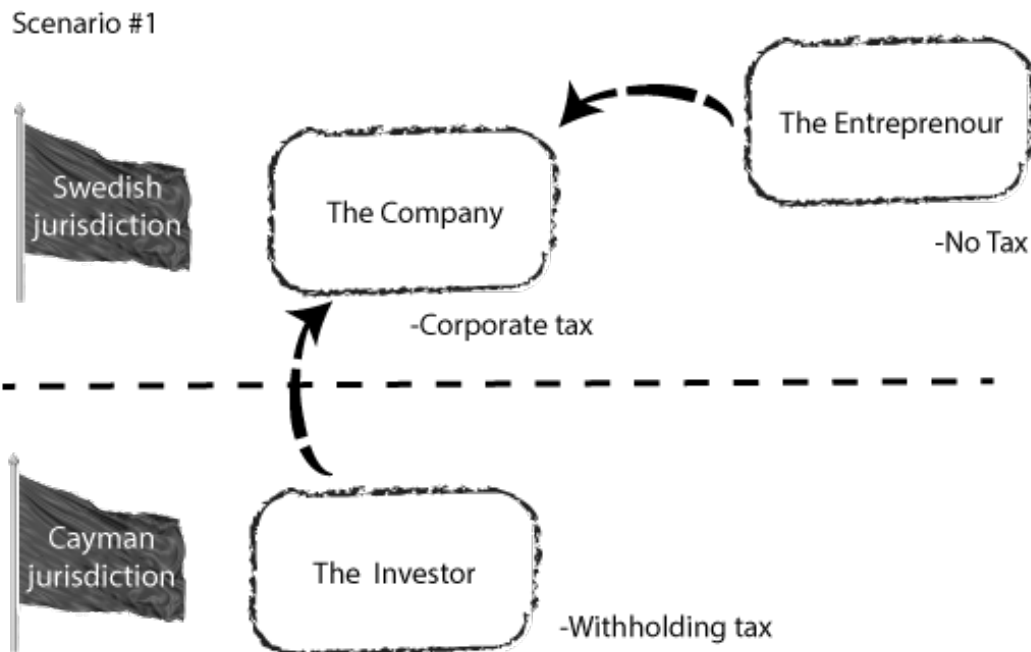
I will here compare the tax and ROI affects of five different scenarios building upon this basic premise. You can find all the numbers in Appendix A. The five Scenarios:

1. The company is based in Sweden; the entrepreneur is based in Sweden and the investor is based in Cayman.
2. The company is based in Sweden but is owned by a Cayman holding company which is owned in equal parts by the investor and the entrepreneur. The entrepreneur is based in Sweden and the investor in Cayman.
3. The company is based in the US; the entrepreneur is based in the US and the investor in is based Cayman.
4. The company is based in the US but owned by a Cayman holding company that is owned in equal parts by the investor and the entrepreneur. The entrepreneur is based in the US and the investor in Cayman.
5. The last scenario is the same as the fourth except that the Entrepreneur does not repatriate his earnings to the US.

This is the computed results of the scenarios.

Scenario #1.

The company's profit is taxed at 26.3% each year. When profits grow the amount of taxes grows as well. The accumulated corporate taxes are \$424.000, paid in Sweden. The investor pays 30% in withholding taxes on both the accumulated dividends (\$89.000) and the sales of the stock (\$867.000). The entrepreneur does not pay any other taxes since he owns more than 10% of the company is thereby exempt from corporation capital gains tax in Sweden. The ROI over 5 years is for the entrepreneur is 2774% and for the investor it is 131%.

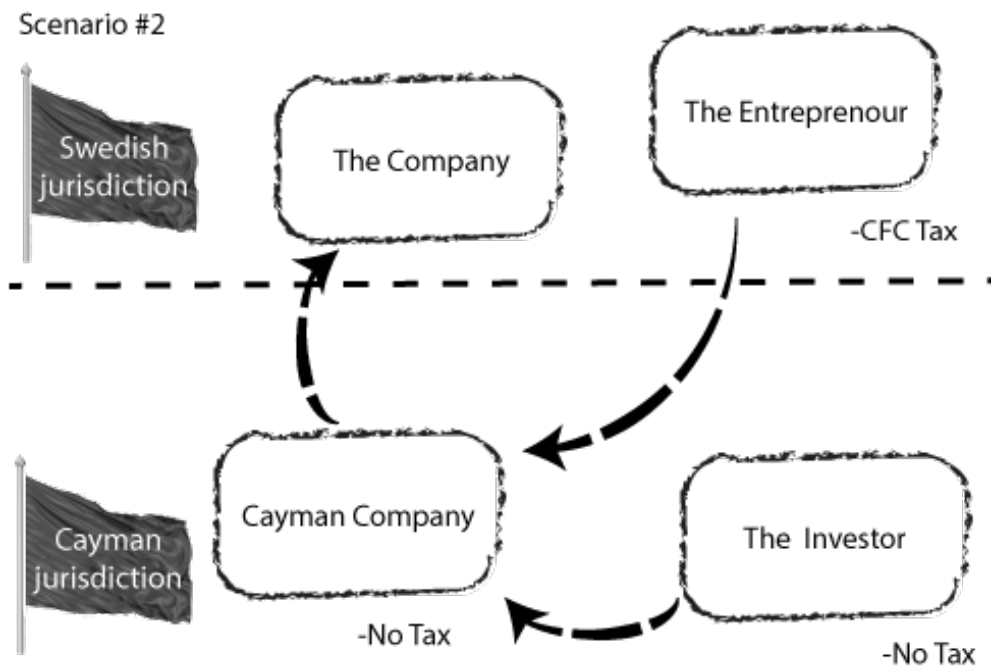


The scenario is really interesting for the entrepreneur who only gets affected by the corporate tax the company pays. This is due to that the entrepreneur falls under the exemption that there are no capital gains in the case that the Swedish company owns 10% or more of a subsidiary in the EU.

Scenario #2.

In option number two the investor and the entrepreneur start a company on the Cayman Islands ("Cayman Company"). All the intellectual property is allocated to the Cayman Company and it licenses/rents/leases it out to the company at a cost that match the profit of the company. Every year the Cayman Company gives out half of its yearly profits in dividends and the Cayman Company is sold after five years. In this scenario the investor does not pay any taxes. There are no corporate tax, capital gains tax or withholding taxes in the Caymans. The entrepreneur pays CFC taxes on their dividends and sales of the Cayman Company. The CFC tax will in this case be the Swedish corporate tax of 26.3% (\$1.014.000).

The ROIs over 5 years are for the entrepreneur is 2365% and for the investor it is 245%. That's a little bit worse for the entrepreneur but a lot better for the investor.

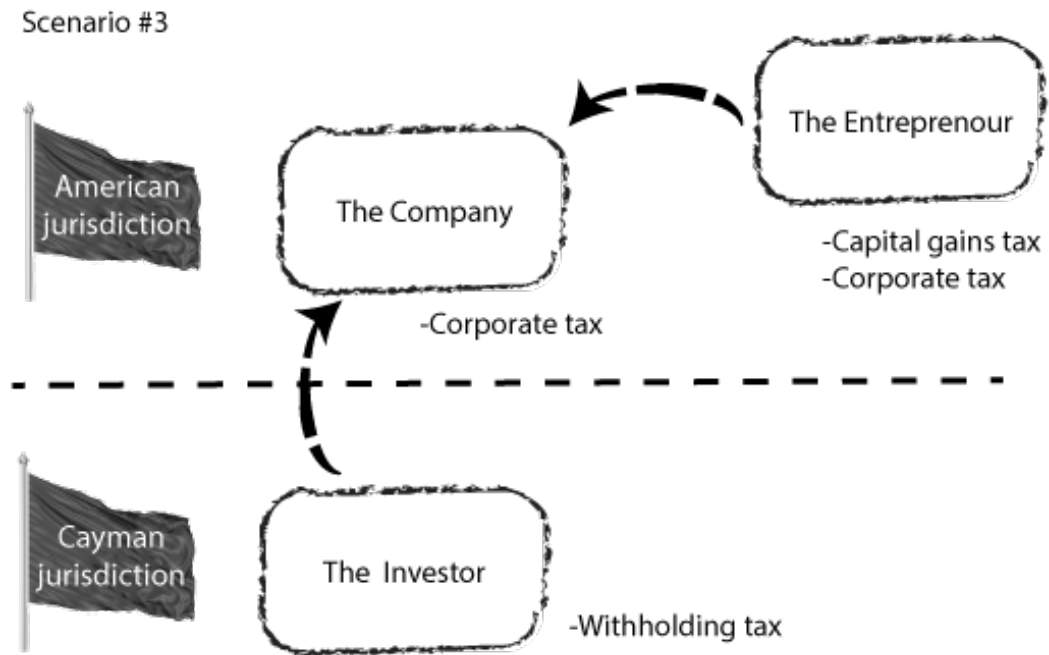


The investor does not have to pay withholding taxes in this case since the Cayman Company does not operate or do business in Sweden.

The entrepreneur gets a higher tax rate in this setup since they no longer fall under the exemption for owning other companies within the ECC area. For a company where the owners are Swedish it's more or less impossible to legally go around profit taxes.

Scenario #3

In scenario number three the company and the entrepreneur is located in the US. The entrepreneur has a c-corp (the corporate tax rate applies, as opposed to pass-through rules for LLCs). The entrepreneur and the investor own stock directly in the company. The company pays corporate taxes on the profit on an annual basis (\$527.000). The effective rate is 32.6%. The Investor pays a 30% withholding tax on both the dividends (\$81.000) and the sale of the stock (\$810.000). The Entrepreneur pays capital gains taxes on the dividends and sales of stock (\$380.000) and then they also pay corporate tax (\$707.000) on what's left.

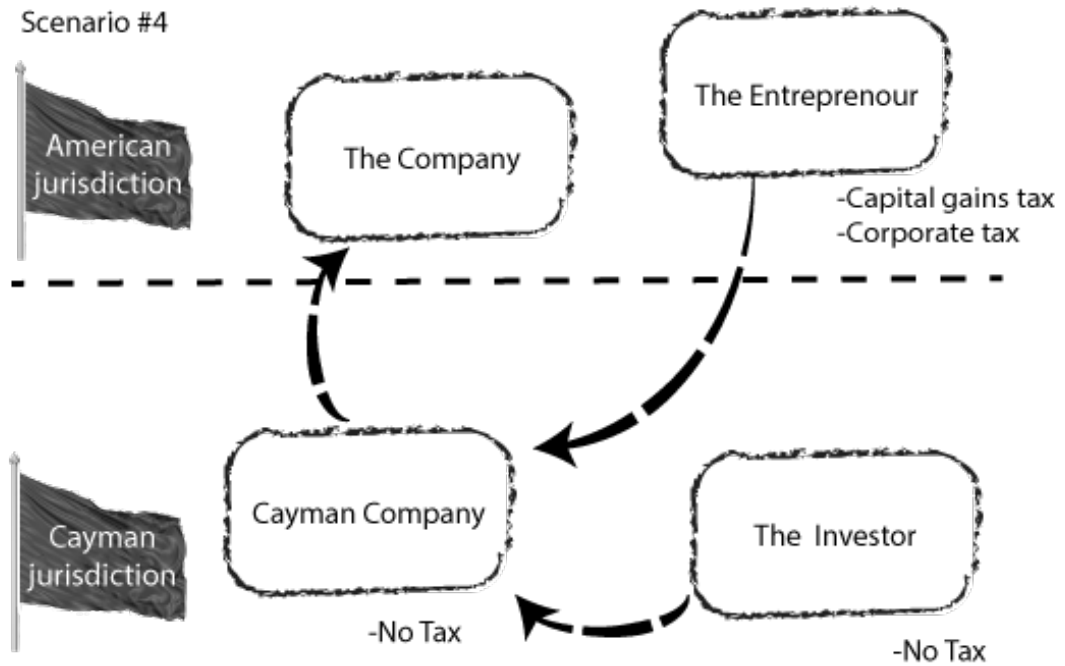


The ROI over 5 years are for the entrepreneur is 985% and for the investor it is 115%.

In this scenario I have not taken into account the deductions that might be possible for the company as well for the entrepreneur. They pay effective rates over 30% when the US average is well below 20%. If I would have these facts its likely that the investor would have been better off then it where in Sweden (131%) but the difference for the entrepreneur would not have been as big. The tax-exemption in Sweden is a real good incentive to keep money working in the company.

Scenario #4

In the fourth scenario the investor and the entrepreneur start a company on the Cayman Islands ("Cayman Company"). All the intellectual property is allocated to the Cayman Company and it licenses it out to the company, which is based in the U.S., at a cost that's the same as the profit of the company. Every year the Cayman Company gives out all profits in dividends and the Cayman Company gets sold after five years.



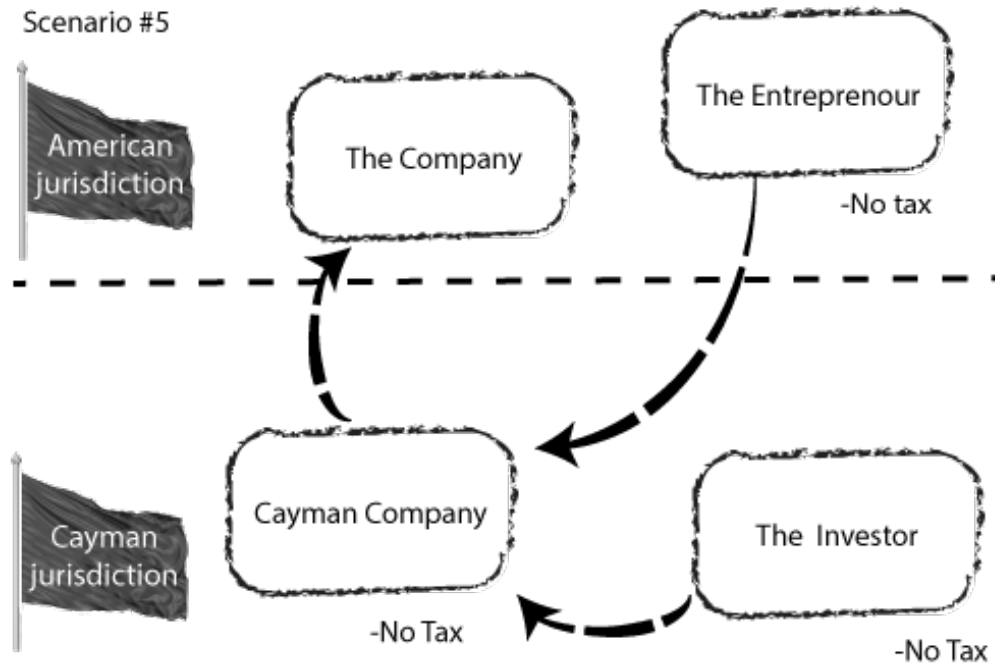
In this case the investor does not pay any taxes. There are no corporate tax, capital gains tax or withholding taxes on Cayman.

The entrepreneur, who repatriates the dividends and profits from sales to the US, pays capital gains taxes on their dividends and sales of the Cayman company (\$563.000) and also corporate tax at the end of the year (\$1.061.000).

In this case the yearly ROI over a five-year period for the entrepreneur is 2131% and for the investor it is 245%. This scenario is pretty similar to the Swedish equivalent (scenario #2). The biggest reason for this is that the CFC tax comes into play.

Scenario #5

In the last case the entrepreneur chooses not to repatriate his profits. The result for the investor is the same as in scenario #4 but the entrepreneur gets 3756% in ROI over the five-year period.



When comparing the scenarios and asking the question: is Sweden competitive, the answer is yes for the global investor, but no for the Swedish/American entrepreneur. This is mostly due to the repatriation policy of the US.

For the Swedish entrepreneur the best scenario own shares in the a startup with another Swedish holding company. This is due to that the money is exempt from taxation due to that they control more then 10% of the company. But, if the most important is to get an global investor, then the Swedish entrepreneur should consider starting a company in a low-tax jurisdiction. The returns for the investor are more or less double (under the right circumstances).

Upcoming changes.

The current political situation in Sweden is rather stable and 2013 the corporate tax rate will be lowered to 22%. In the US the political situation is very much more unstable, though both major parties agree that its time to slash corporate tax-rates and to close loopholes. The loophole mostly mentioned in this report is not showing up very much in those discussions. GOP even declares that they want to keep them and also do a tax-holiday. During spring 2013 the some of the "Bush tax cuts" will expire. So capital gains will be raised from 15% to 20% for income over \$400.000 and income from dividends will experience drastic raises where the top level will raise from 15% to 39.6%. However, the loophole of repatriation of money will most likely not be closed within a next coming future, especially not when GOP directly mentions in their platform that they don't want it to happen. They prefer instituting a temporary tax holiday.

On top of this countries like Germany, Spain and France has together with the OECD has managed to put pressure on the EU to make new laws in regards to VAT. They want VAT to be paid in the country where business takes place, no matter where the people are located. This would redraw the map and affect some jurisdictions like Ireland a lot.

If you are an entrepreneur and you are planning to keep your money in your company,

then Sweden is a competitive place to be based. If you want investment or want more money in your pocket, then moving abroad is a very attractive option.

In Summary

What I have found possible is to set up holding or owner companies in jurisdictions that are more tax favorable. When doing so I can see that the two main factors are the regulations in regards to owning FJEs and regulations governing transactions.

Assuming that the goal is to have an effective tax rate of zero, (excluding sales tax and social security), the first thing a company must do is to allocate corporate profits to a jurisdiction where there are neither corporate taxes nor withholding taxes paid. This means profits needs to be shifted to a low tax jurisdiction or there need to be exemptions such as the US one where corporate tax does not have to be paid if profits are not repatriated. In the use of low-tax jurisdictions, the way seems to be to allocate assets such as tangibles, intellectual properties and capital in the low-tax jurisdictions and then offer these resources to operating companies in high-tax jurisdictions. As learned in the literature studied ways of doing this is by lending out these assets in different ways and getting paid either by interests or payments of licenses or other costs. This together with the authorities difficulties with estimating the pricing (transfer pricing) of these services makes it seem like a fully legal and feasible way to go. If profits are shifted pro-tax then it also solves the problem with withholding taxes.

6. Conclusion

My questions for this theses where:

- What options are there for a Swedish startup company with global investors to structure themselves to optimize owners' ROI?
- How do the options available to a company starting in Sweden differ from starting in the U.S.?

The conclusion I reached is that the best options for a Swedish startup company with global investors to structure themselves to optimize owners' ROI are to two-fold. The best one for the global investor is to set up a holding company in a low-tax jurisdiction. And the best one for the entrepreneur (through LLC) is to own stock directly in the startup company.

The difference between starting in Sweden and the US are for the entrepreneur. In Sweden they are tax-exempt if they own more then 10% of the company (through LLC), and then they only have to pay corporate taxes for the company. In the US the entrepreneur has a legal way of keeping the money away from any taxation by funneling profits to an offshore company and then not repatriating the profits.

Overall, the Swedish model is competitive, but there are now wonder that investors are based out of tax havens.

There are many factors and things I have not looked at, like social security, purchasing power and societal effects of the development. These things and many others can effect my conclusions.

7. Reference List

Altig, D. and Carlstrom, C., 1999. 'Marginal tax rates and income inequality in a life-cycle model.' *The American Economic Review*. 89 (5): 1206, 9. [Accessed from JSTOR 8 October 2012.]

Berk, DeMarzo 2011. *Corporate Finance*. 2nd ed., Pearson Education, Upper Saddle River, New Jersey.

Butler, J., 2009. 'Illojal Skattekonkurrens OECDs arbete gentemot skatteparadis.' Final thesis for Lund University's Law Program. Available at: <<http://lup.lub.lu.se/luur/download?func=downloadFile&recordOid=1556577&fileOid=1564035>>. [Accessed 25 November 2012].

Carlsson, M., 2012. 'Gömda förmögenheter flödar tillbaka.' *Dagens Nyheter*. Available at: <<http://www.dn.se/ekonomi/gomda-formogenheter-flodar-tillbaka>>. [Accessed 8 October 2012].

Cayman Islands Monetary Authority, 2008. 'Regulatory Framework: Statistics.' Available at: <http://www.cimoney.com.ky/regulatory_framework/default.aspx?id=358>. [Accessed 15 September 2012].

Central Intelligence Agency, 2012. 'United States.' *The World Factbook*. Available at: <<https://www.cia.gov/library/publications/the-world-factbook/geos/us.html>>. [Accessed 15 September 2012].

Citizens for Tax Justice, 2012(a). 'The U.S. has a low corporate tax rate.' Available at: <<http://www.ctj.org/pdf/businessroundtable.pdf>>. [Accessed 6 October 2012].

Citizens for Tax Justice, 2012(b). 'General Electric's Ten-Year Tax Rate only Two Percent.' Available at: <http://www.ctj.org/taxjusticedigest/archive/2012/02/press_release_general_electric.php>. [Accessed 9 November 2012].

Citizens for Tax Justice, 2012(c). 'Obama Promoting Tax Cuts at Boeing, a Company that Paid Nothing in Net Federal Taxes Over Past Decade.' Available at: <<http://www.ctj.org/pdf/boeing2012.pdf>>. [Accessed 18 December 2012].

Citizens for Tax Justice, 2011. 'Corporate Taxpayers & Corporate Tax Dodgers, 2008-2010.' Available at: <<http://ctj.org/corporatetaxdodgers>>. [Accessed 12 January 2013].

Columbia University, 1995. *Educating America for the 21st century: developing a strategic plan for educational leadership*. Available at: <http://ariel.adgrp.com/~ghb/trips/940717_ICT/policy/ILT/EdPlan.html>. [Accessed 18 October 2012].

Davis, N., 2009. 'Tax spotlight worries Caymans.' *BBC News*. Available at: <<http://news.bbc.co.uk/2/hi/americas/7972695.stm>>. [Accessed 5 November 2012].

Deloitte, 2012. 'International Tax: Sweden Highlights.' Available at: <http://www.deloitte.com/assets/Dcom-Global/Local%20Assets/Documents/Tax/Taxation%20and%20Investment%20Guides/2012/dttl_tax_highlight_2012_Sweden.pdf>. [Accessed 13 December 2012].

Democrats, 2012. '2012 Democratic National Platform.' Available at: <<http://www.democrats.org/democratic-national-platform>>. [Accessed 7 February 2013].

Drucker, J., 2012. 'Google Revenues Sheltered in No-Tax Bermuda Soar to \$10 Billion.' Bloomberg News. Available at: <<http://www.bloomberg.com/news/2012-12-10/google-revenues-sheltered-in-no-tax-bermuda-soar-to-10-billion.html>> [Accessed 12 December 2012].

Edwards, C. and Mitchell D., 2008. *Global Tax Revolution: The rise of tax competition and the Battle to defend it*. Washington, D.C.: Cato Institute.

Economist, The, 2012. *Pocket World in Figures 2012*. Profile Books, Ltd.: London.

Economist, The, 2007. 'Places in the Sun.' Available at: <<http://www.economist.com/node/8695139>>. [Accessed 3 December 2012].

Ekonomifakta, 2012. 'Bolagskatt.' Available at: <<http://www.ekonomifakta.se/sv/Fakta/Skatter/Skatt-pa-foretagande-och-kapital/Bolagsskatt/>>. [Accessed 3 November 2012].

Ernst and Young, 2013. *Managing Capital: The Essential Guide for Fast-Growth Companies*. Available at: <<http://www.ey.com/GL/en/Services/Strategic-Growth-Markets/Managing-capital--the-essential-guide-for-fast-growth-companies>>. [Accessed 5 February 2013].

FactCheck, 2012. 'Warren: GE Pays No Taxes.' Available at: <<http://www.factcheck.org/2012/04/warren-ge-pays-no-taxes/>>. [Accessed 4 February 2013].

FaktaBank, 2001. 'Näringsbetingade aktier skattefria.' Available at: <<http://node.blinfo.se/fakta.gml?nummer=03:118>>. [Accessed 17 September 2012].

Flexer, R.W., Baer, R.M., Luft, P. and Simmons, T.J., 2008. *Transition planning for secondary students with disabilities*. 3rd ed. Upper Saddle River, New Jersey: Pearson.

Gardner, M.; Phillips, R.; McIntyre, R.; and Wilkins, R.; 2011. "Corporate Tax Payers and Corporate Tax Dodgers." Joint project of Citizens for Tax Justice and the Institute on Taxation and Economic Policy. Available at: <<http://www.ctj.org/corporatetaxdodgers/CorporateTaxDodgersReport.pdf>> [Accessed 24 February 2013].

GOP, 2012. '2012 Republican Platform.' Available at: <<http://www.gop.com/2012->

[republican-platform_home/](#)>. [Accessed 7 February 2013].

Gravelle, Jane, 2010. 'Tax Havens: International Tax Avoidance and Evasion.' *Congressional Research Service, Report for Members and Committees of Congress*. Available at: <www.crs.gov>. [Accessed 5 December 2012].

Groves, P.J. and King, K., 1997. *Intellectual property rights and their valuation: A handbook for bankers, companies, and their advisors*. Abington, England: Gresham Books.

Hendy, R.F.E. and Warburton, A.O., 2006. 'International Comparison of Australia's Taxes.' Written for the Australian Treasurer. Available at: <http://comparativetaxation.treasury.gov.au/content/report/downloads/CTR_full.pdf>. [Accessed on 30 November 2012].

Horan, S., 2009, *Private Wealth: Wealth Management in Practice*. Hoboken, New Jersey: CFA Institute.

Higgs & Johnson, 2011. 'Guide to formation of Cayman islands exempted companies' Available at: <<http://www.higgsjohnson.com/legalGuides/cayman%20guide%20to%20formation%20of%20cayman%20islands%20exempted%20companies.pdf>>. [Accessed 3 March 2013].

Jorgenson, Dale, 1996. *Investment: Capital Theory and Investment Behavior*. Cambridge, Massachusetts: MIT Press.

Kocieniewski, D., 2011. 'U.S. Business Has High Tax Rates but Pays Less.' *The New York Times*. Available at: <http://www.nytimes.com/2011/05/03/business/economy/03rates.html?_r=0>. [Accessed 8 October 2012].

KPMG, 2011. 'Corporate and Indirect Tax Survey 2010.' Available at: <<http://www.kpmg.com/BB/en/IssuesAndInsights/ArticlesPublications/Documents/Corp-and-Indirect-Tax-Oct12-2010.pdf>>. [Accessed 26 November 2012].

KPMG, 2009. 'Corporate and Indirect Tax Survey 2008.' Available at: <<http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Documents/tax-survey-2008-O-0808.pdf>>. [Accessed 26 November 2012].

KPMG, 2008. 'Corporate and Indirect Tax Survey 2007.' Available at: <http://www.kpmg.com/Ca/fr/IssuesAndInsights/ArticlesPublications/Documents/KPMG_CorporateIndirectTaxRateSurvey_Accessible5final.pdf>. [Accessed 26 November 2012].

Lowtaxnet, 2013. 'Cayman Islands, Double taxation treaties' Available at: <<http://www.lowtax.net/lowtax/html/jca2tax.html>>. [Accessed 25 February 2013].

Löwdell, H., 2004. 'Den nya CFC lagstiftningens utformning och funktion samt dess förenlighet med EG-rätten.' Master's thesis for Gothenburg University's School of Business, Economics and Law. Available at: <<http://hdl.handle.net/2077/1970>>. [Accessed 25 November 2012].

Office of Tax Policy, 2007. 'Approaches to improve the competitiveness of the US business tax system for the 21st century.' U.S. Department of the Treasury. Available at: <<http://www.treasury.gov/resource-center/tax-policy/Documents/Approaches-to-Improve-Business-Tax-Competitiveness-12-20-2007.pdf>>. [Accessed on 2 February 2013].

Organization of Economically Developed Countries, 2010. *Model Tax Convention: On Income and on Capital*. Available at: <http://fiscus.fgov.be/interfzfznl/fr/downloads/ocde_en.pdf>. [Accessed 18 October 2012].

Organization of Economically Developed Countries, 2010. 'Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.' Available at: <http://www.oecd.org/document/34/0,3746,en_2649_37427_1915490_1_1_1_37427,00.html>. [Accessed 2 February 2013].

Organization of Economically Developed Countries, 2011. 'Corporate Loss Utilisation through Aggressive Tax Planning.' Available at: <http://www.uscib.org/docs/Corporate_Loss_Utilisation_through_Aggressive_Tax_Planning.pdf>. [Accessed 22 December].

Palan, R., Murphy, R., and Chavagneux C., 2010. *Tax Havens: How Globalization Really Works*. Ithaca, New York: Cornell University Press.

PKF International Ltd., 2010. 'Cayman Islands Tax Guide 2010.' Available at: <<http://www.pkf.com/media/135155/cayman%20islands%20pkf%20tax%20guide%202010.pdf>>. [Accessed 8 February 2013].

Reforming America's Taxes Equitably Coalition, 2012. 'Democratic and Republican Platforms Agree: Corporate tax rate is too high, needs reform.' Available at: <<http://www.ratecoalition.com/index.php/media-center/press-releases/393-democratic-and-republican-platforms-agree-corporate-tax-rate-is-too-high-needs-reform>> [Accessed 6 October 2012].

Senate Republican Policy Committee, 2012. 'Territorial vs. Worldwide Taxation.'

Available at: <<http://www.rpc.senate.gov/policy-papers/territorial-vs-worldwide-taxation>>. [Accessed 20 October 2012].

Skatteverket, 2010. 'CFC Beskattning.' Available at: <http://www.skatteverket.se/download/18.6efe6285127ab4f1d25800010714/CFC_beskattning.pdf>. [Accessed 18 December 2012].

Skatteverket, 2011(a). *Skatter i Sverige: Skattestatistisk årsbok*. Rapport, Elanders Sverige 2011. Available at: <<http://www.skatteverket.se/download/18.5fc8c94513259a4ba1d800065200/15214.pdf>> [Accessed 17 January 2013].

Skatteverket, 2011(b). 'Handledning för internationell beskattning 2011.' Available at: <<http://www.skatteverket.se/rattsinformation/handledningarhandbocker/internationellbeskattningskv352/internationellbeskattning/201135215.4.70ac421612e2a997f85800044689.html>>. [Accessed 24 September 2012].

Skatteverket, 2012(a). '25,12 eller 6 procents moms?' Available at: <<http://www.skatteverket.se/foretagorganisationer/moms/vadarmoms/2512eller6procentsmoms.4.7459477810df5bccdd480005156.html>>. [Accessed 2 December 2012].

Skatteverket, 2012(b). *Skatter i Sverige: Skattestatistisk årsbok*. Available at: <<http://www.skatteverket.se/download/18.5fc8c94513259a4ba1d800065200/15214.pdf>>. [Accessed 2 December 2012].

Skatteverket, 2012(c). *Personal interview with civil servant*. Conducted 4 April 2012.

Skatteverket, 2013. *Handledning för beskattning av inkomst år 2012*. Available at: <<http://www.skatteverket.se/rattsinformation/handledningarhandbocker/beskattningavinkomstskv399/beskattningavinkomst/2012.4.71004e4c133e23bf6db800061613.html>>. [Accessed 2 December 2012].

Swedish Government, 2012. 'Jobb och tillväxtsatsningar: Sänkt bolagsskatt, investeraravdrag och stärkt rättsäkerhet.' Available at: <<http://www.regeringen.se/content/1/c6/19/89/76/f7cc5d60.pdf>>. [Accessed 18 November 2012].

Statistiska centralbyrån, 2012. 'Homepage.' Available at: <<http://www.scb.se>>. [Accessed 23 September 2012].

Tax Policy Center, 2010. 'Corporate Income Tax as a Share of GDP, 1946-2006.' Available at: <<http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=263&Topic2id=70>>. [Accessed 12 January 2013].

Tax Policy Center, 2011. 'Corporate Income Tax Returns: Balance Sheet, Income Statement, and Tax Items for Specified Income Years, 1980-2008..' Available at: <<http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=66&Topic2id=70>>. [Accessed 12 January 2013].

Tax Rate Guide and Tax Help Website, 2012(a). 'Cayman Islands Tax Rates.' Available at: <<http://www.taxrates.cc/html/cayman-islands-tax-rates.html>>. [Accessed 6 February 2013].

Tax Rate Guide and Tax Help Website, 2012(b). 'Sweden Tax Rates.' Available at: <<http://www.taxrates.cc/html/sweden-tax-rates.html>>. [Accessed 18 January 2013].

Tax Reform Act of 1986. Public Law 99-514, 100 Stat. 2085, enacted October 22, 1986. Washington, D.C.: U.S. Library of Congress.

Transparency International, 2010. 'Corruption Perception Index 2010.' Available at: <<http://www.transparency.org/cpi2010/results>>. [Accessed 10 October 2012].

U.S. Census, 2012. 'US & World population Clocks.' Available at: <<http://www.census.gov/main/www/popclock.html>>. [Accessed 6 October 2012].

U.S. Congressional Budget Office, 2005. 'Corporate Income Tax Rates: International Comparisons.' Available at: <<http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/69xx/doc6902/11-28-corporatetax.pdf>>. [Accessed 6 October 2012].

U.S. Government Accountability Office, 2008(a). 'Statement of Michael Brostek: Cayman Islands: Business Advantages and Tax Minimization Attract U.S. Persons and Enforcement Challenges Exist.' *Testimony Before the Committee on U.S. Finance, U.S. Senate.* ” GAO Report 08 779T.

U.S. Government Accountability Office, 2008(b). 'Cayman Islands: Business Advantages and Tax Minimization Attract U.S. Persons and Enforcement Challenges Exist.' *GAO Report to the Chairman and Ranking Member, Committee on Finance, U.S. Senate.* ” GAO Report 08 778.

U.S. Internal Revenue Service, 2012. 'Instructions for Form 1120.' U.S. Department of the Treasury. Available at: <<http://www.irs.gov/pub/irs-pdf/i1120.pdf>>. [Accessed 23 January 2013].

U.S. Internal Revenue Service, 2012. 'Tax Treaty Overview.' U.S. Department of the Treasury. Available at: <<http://www.irs.gov/Individuals/International-Taxpayers/Tax->

[Treaty-Overview](#)>. [Accessed 15 September 2012].

U.S. Internal Revenue Service, 2008. 'U.S. Tax Withholding on Payment to Foreign Persons.' Available at: <<http://www.irs.gov/Businesses/U.S.-Tax-Withholding-on-Payments-to-Foreign-Persons>>. [Accessed 18 January 2013].

U.S. Department of State, 2012. 'U.S. Relations with Cayman Islands.' Available at: <<http://www.state.gov/r/pa/ei/bgn/5286.htm>>. [Accessed 15 October 2012].

U.S. Senate Committee on Finance, 2008. 'The Cayman Islands and Offshore Tax Issues.' *Hearing Before the Committee on Finance*. Available at: <[http://permanent.access.gpo.gov/gpo2714/58198\[1\].pdf](http://permanent.access.gpo.gov/gpo2714/58198[1].pdf)>. [Accessed 10 January 2013].

Wikipedia, 2012. 'Cayman Islands.' Available at: <http://en.wikipedia.org/wiki/Cayman_Islands>. [Accessed 18 September 2012].

Wikipedia, 2013. 'Förvaltningsdomstol.' Available at: <<http://sv.wikipedia.org/wiki/F%C3%B6rvaltningsdomstol>>. [Accessed 4 February 2013].

Wikipedia, 2013. 'Ikea.' Available at: <<http://en.wikipedia.org/wiki/IKEA>>. [Accessed 5 February 2013].

Wikipedia, 2013. 'Tenth Amendment to the United States Constitution.' Available at: <http://en.wikipedia.org/wiki/Tenth_Amendment_to_the_United_States_Constitution>. [Accessed 5 February 2013].

Wikipedia, 2012. 'Commerce Clause.' Available at: <http://en.wikipedia.org/wiki/Commerce_Clause>. [Accessed 6 October 2012].
Wikipedia, 2013. 'Separation of Powers under the United States Constitution.' Available at: <http://en.wikipedia.org/wiki/Separation_of_powers_under_the_United_States_Constitution>. [Accessed 6 October 2012].

Wikipedia, 2013. 'Internal Revenue Service.' Available at: <http://en.wikipedia.org/wiki/Internal_Revenue_Service>. [Accessed 6 October 2012].

8. Appendices