

Intra-Industry Diffusion of Profit Shifting Strategies

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Abstract: Does tax knowledge spread across firms? This paper provides systematic evidence along these lines using data on US-listed firms' presence in tax havens and an event study. An enterprise is more likely to own a subsidiary in a specific tax haven once another enterprise operating in the same sector enters this tax haven. The inclusion of three-way fixed effects, the absence of pre-trends, and several robustness checks consolidate the results. Moreover, profit shifting spillovers vary over time, across sectors, and by tax haven. The findings suggest that firms replicate the tax avoidance schemes of their peers and carry policy implications.

Keywords: Multinational enterprises, profit shifting, tax havens, foreign direct investments, spillovers.

JEL codes: F14, F23, H26, L25, M21.

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1 Introduction

In the aftermath of the recent tax scandals, multinational enterprises (MNEs) have frequently been accused of large-scale tax avoidance. Some of them artificially shift profits from affiliates in high-tax countries toward affiliates in low-tax countries to decrease their average effective tax rate. The techniques designed to this end are now relatively well-identified and documented in the literature ([Beer, de Mooij, and Liu, 2020](#)). They notably involve a tax-efficient use of transfer prices, intercompany debt, and a relocation of intellectual property rights in tax havens. However, less is known about the factors prompting MNEs to engage in profit shifting activities. Tax rate differentials between jurisdictions naturally play a key role in profit shifting. A perhaps more challenging question is whether an MNE influences the income shifting behavior of other MNEs. The literature points in this direction. An old body of research establishes the existence of technology spillovers. Research and development, innovation, exports, and foreign direct investments (FDIs) activities implemented by some firms generate positive externalities and foster the performance of other firms, for instance through labor mobility. More recently and more closely related to this paper, [Cen, Maydew, Zhang, and Zuo \(2017\)](#), [Lim, Shevlin, Wang, and Xu \(2018\)](#), [Barrios and Gallemore \(2019\)](#), [Gallemore, Gipper, and Maydew \(2019\)](#), and [Bauckloh, Hardeck, Wittenstein, and Zwergel \(2021\)](#) suggest that the same could apply to tax planning technology. [Cen et al. \(2017\)](#), [Lim et al. \(2018\)](#), [Barrios and Gallemore \(2019\)](#), and [Gallemore et al. \(2019\)](#) show that firms connected to low-tax firms via the supply chain and auditor, employee, and bank ties have lower effective tax rates. [Bauckloh et al. \(2021\)](#) observe that news about tax avoidance practices of an MNE entails a negative stock price reaction among its peers. This response, according to the authors, stems from the fact that investors expect similar firms to employ similar practices.

The present paper delves into the latter assertion and focuses on intra-industry spillovers, profit shifting, and tax haven FDIs. In the first part of the paper, I build a database on the worldwide network of US-listed firms' subsidiaries between 1993 and 2013. I capitalize on the fact that the Securities and Exchange Commission (SEC) requires these companies to disclose every year a list of their subsidiaries. On this basis, I compile a unique database disaggregated at the firm-country-year level indicating the number of subsidiaries each US-listed enterprise declares in each tax haven and each year. The analysis then improves on the previous ones, often performed at the firm-year level and limited to (cash) effective tax rates, whose variations can be independent of tax avoidance. The second part proceeds with an event study. I scrutinize the evolution of the probability to report a physical presence in a given tax haven when at least one other company operating in the same 4-digit

SIC sector also does. The effect of peer entry is quantified while controlling for numerous confounding factors. The fine level of the database allows inserting three-way fixed effects, thereby mitigating endogeneity concerns and fine-tuning the identification strategy. The firm-year, country-year, and firm-country fixed effects neutralize, among others, the impact of all firm-, sector-, and country-year-specific causes of tax haven FDIs such as firm productivity and corporate tax rates.

The benchmark results reveal that, all other things being equal, the average probability to report a subsidiary in a specific tax haven is 10 percent higher when a peer is present in this tax haven. The spillover effect progresses over time and grows four fold five years post peer entry. This finding is corroborated by diverse sensitivity checks. First, it is driven neither by the estimation methodology (linear probability model versus binary model) nor by the industry classification. Second, the conclusion is robust across classifications of tax havens. The baseline equation uses the lists of tax havens elaborated by [Hines and Rice \(1994\)](#) and [Dyreng and Lindsey \(2009\)](#), standard in the literature. Nonetheless, adopting one list, the intersection of the two lists, or omitting one tax haven at a time delivers the same results. On the same note, I find consistent results after excluding the largest tax havens. Workhorse international trade theories predict that FDIs should be directed toward large and central countries ([Brainard, 1993](#); [Head and Mayer, 2004](#); [Helpman, Melitz, and Yeaple, 2004](#)). As a consequence, FDIs in large and well-connected tax havens like Ireland might have nothing to do with aggressive tax planning in the first place. Yet, small and remote tax havens concentrate a disproportionately high number of US-listed firms. It is therefore reasonable to consider that FDIs in small and isolated jurisdictions like the Marshall Islands have no or little economic substance and are purely attributable to profit shifting. Furthermore, the results are validated by falsification tests. I randomly assign each 4-digit SIC industry to another 4-digit SIC industry and examine whether profit shifting activities in the randomly drawn industry affects firms' physical presence in tax havens. This is not the case. In the same vein, there is no pre-existing trend, i.e., the presence of firms in tax havens does not depend on future peer entry in tax havens. This rules out the possibility that the treatment variable picks the effect of past and unobserved firm- and sector-country-year shocks, lends credence to the parallel trend assumption, and more generally supports a causal interpretation of the results.

Lastly, I provide stylized facts about profit shifting spillovers and investigate the existence of heterogeneous effects along three dimensions: over time, across sectors, and by tax haven. Profit shifting has amplified in the last decades ([Grubert, 2012](#); [Klassen and Laplante, 2012](#)) and has been found to be more prevalent in finance and services ([Gumpert, Hines,](#)

and Schnitzer, 2016; Merz and Overesch, 2016). Hence, I posit that spillovers are more pronounced (i) in the 2004-2013 period than in the 1993-2003 period and (ii) in services and financial sectors than in manufacturing. The regression results substantiate both assumptions. In addition, profit shifting spillovers differ by tax haven. They are stronger for the most tax aggressive jurisdictions, like Barbados, Luxembourg, and Switzerland, where corporate tax rates are at very low levels.

The findings are new in the literature as they are to the best of my knowledge the first to uncover the existence of (intra-industry) spillovers of profit shifting. In a sense, they partly explain the rapid development of profit shifting activities witnessed in the 1990s-2000s and contribute to the literature on the determinants of corporate tax avoidance and profit shifting (Alm, 2019; Beer et al., 2020; Wang, Xu, Sun, and Cullinan, 2020). They also have policy implications. Corporate tax avoidance has become an important issue in a decade of economic and political turmoil. The multiple tax scandals, the rise of within-country income inequalities, lasting budget deficits in Europe and the US, and the covid-19 pandemic have pushed governments to implement anti profit shifting measures. Against this background, the results emphasize that firms tend to reproduce the tax schemes of their peers. They indicate that when a firm is found undertaking tax dodging activities in some tax havens, public authorities could pay particular attention to other corporations operating in the same sector because they are more likely to carry out operations with these tax havens. In this regard, the fact that intra-industry spillovers are more salient in services and financial sectors as well as for very aggressive tax havens suggests that policy makers might want to devote more efforts to these industries and jurisdictions.

The remainder of the paper is structured as follows. First, section 2 introduces the data used to conduct the analysis and presents descriptive statistics. Section 3 then lays out the econometric exercise, the results, and the robustness checks. Section 4 briefly concludes and discusses avenues for subsequent research.

2 Data

The data originate from two complementary sources: Compustat and Exhibit 21 filings. Compustat is a database containing extensive information on balance sheets, income statements, and cash flows of all publicly listed firms in North America since 1950. These firms, despite being few in number, amass a significant share of overall sales, profits, and employment (Asker, Farre-Mensa, and Ljungqvist, 2014). It is worth noting that they are the most likely to engage in tax haven FDIs and profit shifting. Earlier work ack-

nowledges the existence of fixed and sunk costs for FDIs. Besides establishing facilities overseas, FDIs generally require completing market research *ex ante*, creating new distribution networks, etc. Merely the largest and most productive firms can afford and find profitable to pay these costs (Helpman et al., 2004). The same logic applies to profit shifting (Bilicka, Devereux, and Guceri, 2020). Avoiding taxes necessitates an excellent knowledge of the tax code. Firms must recruit expensive tax experts to exploit loopholes and other legal technicalities to book their income in tax-friendly jurisdictions (Jones, Te-mouri, and Cobham, 2018). For example, PricewaterhouseCoopers received nearly \$55 million from Caterpillar for developing its tax dodging strategy (US Senate Permanent Subcommittee on Investigations, 2014). For these reasons, not having a representative sample of the universe of firms is not a problem for this paper.¹

The Compustat data are merged with data extracted from Exhibit 21 filings. The SEC requires US-listed firms to disclose, each year, a list of their significant subsidiaries in Exhibit 21 of Form 10-K.² A subsidiary is qualified as significant if its assets (or revenues) represent at least 10 percent of consolidated assets (or revenues). Moreover, any subsidiary is treated as significant if by combining all undisclosed subsidiaries into one fictive subsidiary, the composite accounts for at least 10 percent of global assets (or revenues). Therefore, Exhibit 21 filings reflect where more than 90 percent of US-listed firms' assets and revenues are recorded. They allow observing where most of the subsidiaries of US-listed firms are incorporated and how these networks evolve over time. An interesting feature of Exhibit 21 filings is that they are electronically filed since 1993 and publicly available on the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) platform. Figure 1 gives an example. It displays (a part of) the list of subsidiaries reported by the firm Johnson & Johnson in 2012 in the US and abroad. One potential caveat is that firms might have incentives to under-estimate the number of subsidiaries in tax havens. Dyreng, Hoopes, Langetieg, and Wilde (2020) argue however that most disclosures are accurate, even when it comes to tax havens. In this study, I exploit an updated version of the database constructed by Dyreng and Lindsey (2009) covering the 1993-2013 period.

The final sample consists of 14,070 firms active in 436 4-digit SIC sectors, all of which reported one or several subsidiaries at some point inside or outside the US. The database

1. Small and medium enterprises (SMEs) do not generally have enough financial resources to engage in profit shifting. They are less internationally-oriented and more prone to *evade* taxes. Tax evasion is undoubtedly illegal, while tax avoidance is closer to the sharp line between legality and illegality. Hence, the strategies used are not the same in the two cases. For example, SMEs tend to turn to informality because they have a lower probability to be audited.

2. Note that companies are not obliged to convey financial information concerning each of these subsidiaries.

FIGURE 1 – Non-exhaustive list of the significant subsidiaries reported by Johnson & Johnson in Exhibit 21 filings in 2012

EX-21 5 ex21-subsidariesxform10xk.htm SUBSIDIARIES

EXHIBIT 21

Johnson & Johnson, a New Jersey corporation, had the domestic and international subsidiaries shown below as of December 30, 2012. Certain U.S. subsidiaries and international subsidiaries are not named because they were not significant in the aggregate. Johnson & Johnson has no parent.

Name of Subsidiary	Jurisdiction of Organization
U.S. Subsidiaries:	
Acclarent, Inc.	Delaware
ALZA Corporation	Delaware
Animas Corporation	Delaware
Biosense Webster, Inc.	California
CNA Development LLC	Delaware
Codman & Shurtleff, Inc.	New Jersey
Cordis Corporation	Florida
Cordis International Corporation	Delaware
Cordis LLC	Delaware
DePuy Mitek Holding Corporation	Delaware
DePuy Mitek, LLC	Massachusetts
DePuy Orthopaedics, Inc.	Indiana
Rutan Realty LLC	New Jersey
Scios Inc.	Delaware
SterilMed, Inc.	Minnesota
Synthes USA Products, LLC	Delaware
Synthes USA, LLC	Delaware
Synthes, Inc.	Delaware
The Anspach Effort, LLC	Florida
Wellness & Prevention, Inc.	Michigan
International Subsidiaries:	
Almaco Holding AG	Switzerland
Apsis	France
Apsis Germany GmbH	Germany
Beijing Dabao Cosmetics Co., Ltd.	China
Berna Biotech Korea Corporation	Korea, Republic of
Berna Rhein B.V.	Netherlands
Biosense Webster (Israel) Ltd.	Israel
Cilag Advanced Technologies GmbH	Switzerland
Cilag AG	Switzerland
Cilag GmbH International	Switzerland

Notes: See <https://www.sec.gov/Archives/edgar/data/200406/000020040613000038/ex21-subsidariesxform10xk.htm>.

TABLE 1 – List of tax havens

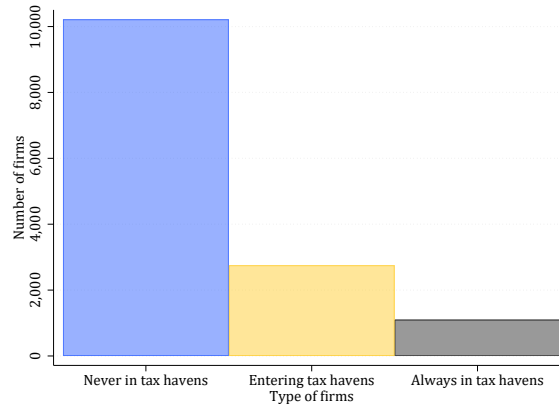
Andorra, Anguilla, Antigua and Barbuda, Aruba, Bahamas, Bahrain, Barbados, Belize, Bermuda, British Virgin Islands, Cayman Islands, Cook Islands, Costa Rica, Cyprus, Dominica, Gibraltar, Grenada, Guernsey, Hong Kong, Ireland, Isle of Man, Jersey, Jordan, Lebanon, Liberia, Liechtenstein, Luxembourg, Macau, Malaysia, Maldives, Malta, Marshall Islands, Mauritius, Monaco, Montserrat, Nauru, Netherlands Antilles, Niue, Panama, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Saint Martin, Samoa, San Marino, Seychelles, Singapore, Switzerland, Turks and Caicos Islands, and Vanuatu.

is assembled at the firm-tax haven-year level. The list of tax havens draws on the lists of [Hines and Rice \(1994\)](#) and [Dyreng and Lindsey \(2009\)](#), both typical in the corporate tax avoidance literature. A country is assumed to be a tax haven if it figures in at least one of the two lists. In total, 50 foreign countries are viewed as tax havens (see table 1).

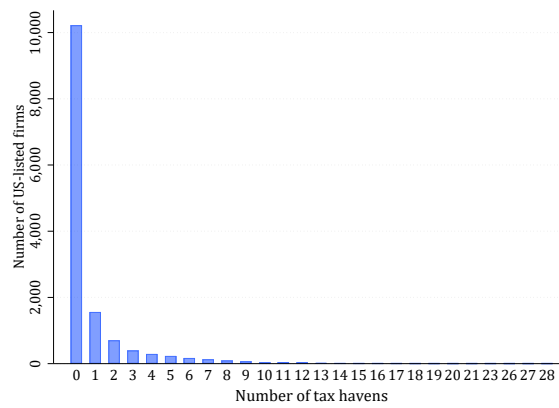
Among these 14,070 companies, 10,220 companies (73 percent) never declared a subsidiary in a tax haven, while 2,753 companies (19 percent) entered at least one tax haven

FIGURE 2 – Summary statistics

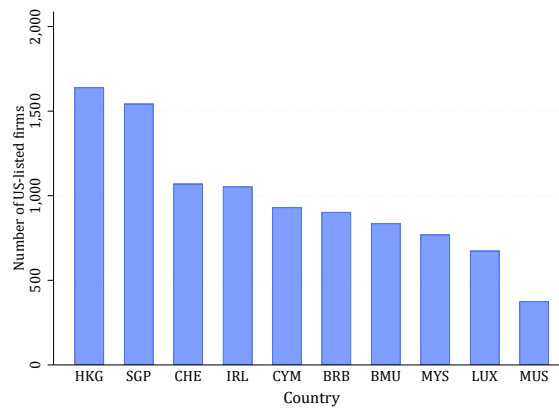
(a) Presence of US-listed firms in tax havens
(extensive margin)



(b) Presence of US-listed firms in tax havens
(intensive margin)



(c) Top 10 tax havens



for the first time between 1993 and 2013 (see figure 2a). The 1,097 remaining firms (8 percent) always reported at least one subsidiary in a tax haven. It means that beyond data availability, 1993-2013 is ideal for the analysis since the number of firms operating in tax havens has soared during this period. On average, the firms present in tax havens were located in three distinct tax havens. 40 (18) percent of these companies were implanted in one (two) tax haven(s), so the average is driven by a very few companies having subsidiaries in multiple tax havens (see figure 2b). According to figure 2c, Hong Kong was the most common tax haven of US-listed firms. 11.66 percent of the firms disclosed at least one subsidiary in this jurisdiction. Singapore (10.97 percent), Switzerland (7.60 percent), Ireland (7.49 percent), and the Cayman Islands (6.62 percent) join the top 5. There are also sizable disparities across sectors. Several sectors stand out when exploring the presence of firms in tax havens at the extensive and intensive margins (presence or not, total number of subsidiaries, average number of subsidiaries): business services, chemicals, computers, construction, electronics, insurance, and water transportation.³

3 Econometric analysis

3.1 Identification strategy

Armed with this database, I run the following linear probability model (LPM) with ordinary least squares to see whether tax dodging schemes propagate within sectors:

$$FDI_{i,c,t} = \alpha TREAT_{i,c,t} + \mu_{i,t} + v_{c,t} + \gamma_{i,c} + \epsilon_{i,c,t} \quad (1)$$

The dependent variable $FDI_{i,c,t}$ is a dummy variable equal to 1 if firm i has at least one subsidiary in tax haven c in year t . On the right-hand side, $TREAT_{i,c,t}$ is a dichotomous variable equal to 1 if another firm operating in the same 4-digit SIC sector discloses in year t a subsidiary in tax haven c . To reduce endogeneity and purge the treatment effect of confounding factors, I introduce a battery of three-way fixed effects: firm-year fixed effects $\mu_{i,t}$, country-year fixed effects $v_{c,t}$, and firm-country fixed effects $\gamma_{i,c}$. The first set of fixed effects absorb sector- and firm-year determinants of FDIs and aggressive tax planning. They incorporate, among other things, determinants already highlighted in the literature such as productivity and intangible assets. The country-year fixed effects encompass country-year factors influencing inward FDIs from US-listed firms. These factors include (but are not limited to) corporate tax rates and opacity. The third and last set

3. More details are available upon request.

TABLE 2 – Baseline results

Dependent variable	$FDI_{i,c,t}$
$TREAT_{i,c,t}$	1.35e-3 ^a (2.74e-4)
Firm-year FEs	Yes
Country-year FEs	Yes
Firm-country FEs	Yes
R ²	0.69
No. of obs.	5,514,400

Notes: This table reports the baseline regression results of equation (1). The standard error, in parentheses, is clustered at the firm-year level. ^b $p < 0.05$, ^a $p < 0.01$. See section 3 for more details.

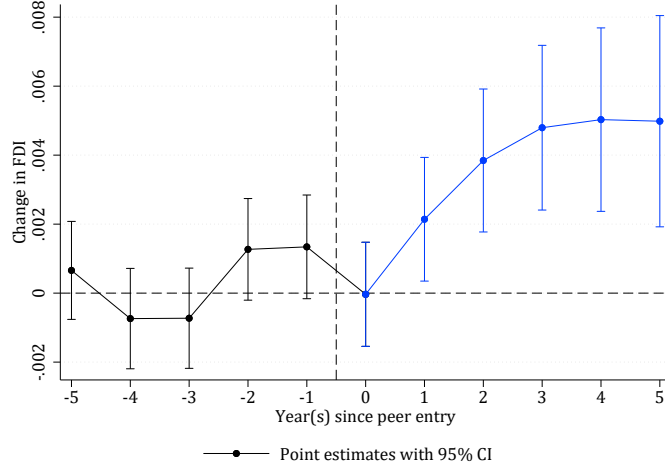
of fixed effects, firm-country specific, captures firm-country time-invariant causes of FDIs like distance between the headquarter and the tax haven as well as firm-country specific knowledge.

In simple words, the coefficient of interest α translates the average effect of peer presence in a tax haven (at the extensive margin) on the firm's probability to own subsidiaries in this tax haven. Take two firms A and B, active in two different sectors S_A and S_B , and assume that they have comparable global trends in tax haven FDIs, i.e., $\mu_{A,t} - \mu_{A,t-1} \approx \mu_{B,t} - \mu_{B,t-1}$. Further assume that at least one firm in S_A is present in country c while no company in S_B is implanted in country c . The identification of α relies on the hypothesis that FDIs of both enterprises in jurisdiction c would have evolved similarly if no firm in S_A were established in tax haven c .

3.2 Main results

The benchmark result is outlined in table 2. The coefficient of interest $\hat{\alpha}$ is equal to 1.35e-3 and statistically significant at the 1 percent level. Given that the average predicted value of $FDI_{i,c,t}$ is equal to 1.33 percent, the regression result indicates that, other things held constant, the average probability to own a subsidiary in a given tax haven increases by 10 percent if another firm in the same sector also does.

FIGURE 3 – Sensitivity analysis: dynamics



Notes: This figure outlines how $FDI_{i,c,t}$ varies before and after the treatment. The black coefficients correspond to $\hat{\beta}_k$, i.e., what happens before the treatment. For instance, the coefficient for “-3” is given by $\hat{\beta}_3$. The blue coefficients correspond to $\hat{\alpha} + \sum_k \hat{\zeta}_k$, i.e., what happens after the treatment. For instance, the coefficient for “3” is given by $\hat{\alpha} + \sum_{k=1}^3 \hat{\zeta}_k$. Standard errors are clustered at the firm-year level. See equation (2) and section 3 for more details, and Appendix table A2 for a full table.

3.3 Robustness

Binary model A series of tests now evaluate the robustness of this finding. Table 3 panel A proves that it is not ascribable to the estimation technique. There is no consensus in the econometrics literature on the estimator one should use when the dependent variable is binary (Horrace and Oaxaca, 2006; Angrist and Pischke, 2009; Battay, Cox, and Jackson, 2019; Gomila, 2020). LPMs and binary models have their own advantages and drawbacks. On the one hand, LPMs are easier to interpret and more transparent but they might deliver inconsistent estimates under some conditions. On the other hand, binary models guarantee that the predicted probabilities lie on the unit interval but they may suffer from the incidental parameters problem. An important point, indeed, is that estimating binary models with high-dimensional fixed effects is not trivial. Groups for which the dependent variable does not vary should be excluded. This omission leads to the so-called incidental parameters problem and the estimates, biased, need to be corrected accordingly. I estimate a logit model building on Hinz, Stammann, and Wanner (2020). They design a correction procedure for binary models with three-way fixed effects akin to equation (1). Reassuringly, $\hat{\alpha}$ remains positive and statistically significant at standard levels.

TABLE 3 – Sensitivity analysis: main tests

Dependent variable	$FDI_{i,c,t}$
Panel A: Binary model	
$TREAT_{i,c,t}$	0.14 ^b
Panel B: Treatment variable	
$TREAT_{i,c,t}^C$	1.95e-3 ^a
$SHARE_{i,c,t}$	0.11 ^a
Panel C: Classification of tax havens	
$TREAT_{i,c,t}^{HR}$	9.33e-4 ^a
$TREAT_{i,c,t}^{DL}$	1.32e-3 ^a
$TREAT_{i,c,t}^{DL \cap HR}$	8.95e-4 ^a
$TREAT_{i,c,t}^{EX6}$	1.53e-3 ^a
Panel D: Industry definition	
$TREAT_{i,c,t}^{>15}$	6.77e-4 ^a
$TREAT_{i,c,t}^{3-digit}$	1.23e-3 ^a
Panel E: Falsification test	
$TREAT_{i,c,t}^{random}$	-2.80e-4
Firm-year FEs	Yes
Country-year FEs	Yes
Firm-country FEs	Yes

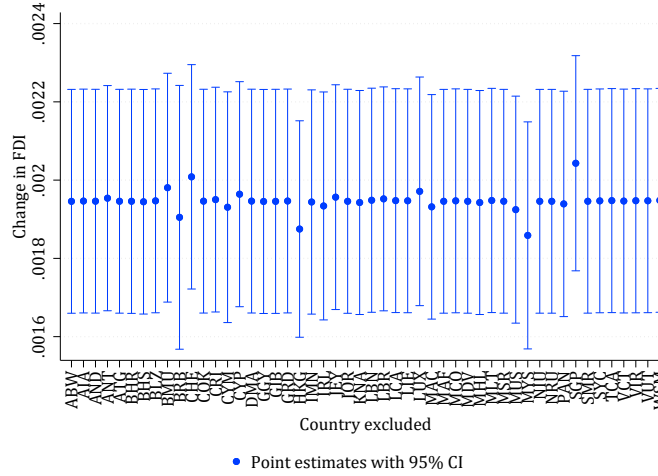
Notes: This table gauges the robustness of the results for equation (1) outlined in table 2. Standard errors are clustered at the firm-year level and not reported for space. ^b $p < 0.05$, ^a $p < 0.01$. See section 3 for more details and Appendix table A1 for a full table.

Dynamics Next, I enrich equation (1) with lagged and leading values of $TREAT_{i,c,t}$, denoted $TREAT_{i,c,t}^{t-k}$ and $TREAT_{i,c,t}^{t+k}$ respectively. They allow examining how the probability of a firm to disclose a subsidiary in a tax haven fluctuates before and after peer entry in this specific tax haven. Without loss of generality, I select a 10-year window around the treatment and estimate equation (2) below:

$$FDI_{i,c,t} = \alpha TREAT_{i,c,t} + \sum_{k=1}^5 \beta_k TREAT_{i,c,t}^{t+k} + \sum_{k=1}^5 \zeta_k TREAT_{i,c,t}^{t-k} + \mu_{i,t} + v_{c,t} + \gamma_{i,c} + \epsilon_{i,c,t} \quad (2)$$

The results can be visualized in figure 3. Two comments are in order. First, the effect is progressive and persistent. It amounts to +38 percent after three years and stabilizes. Second, there is little evidence of pre-existing trends. The probability to report a subsidiary in a given tax haven does not significantly vary before the treatment at the 5 percent level,

FIGURE 4 – Sensitivity analysis: eliminating one tax haven at a time



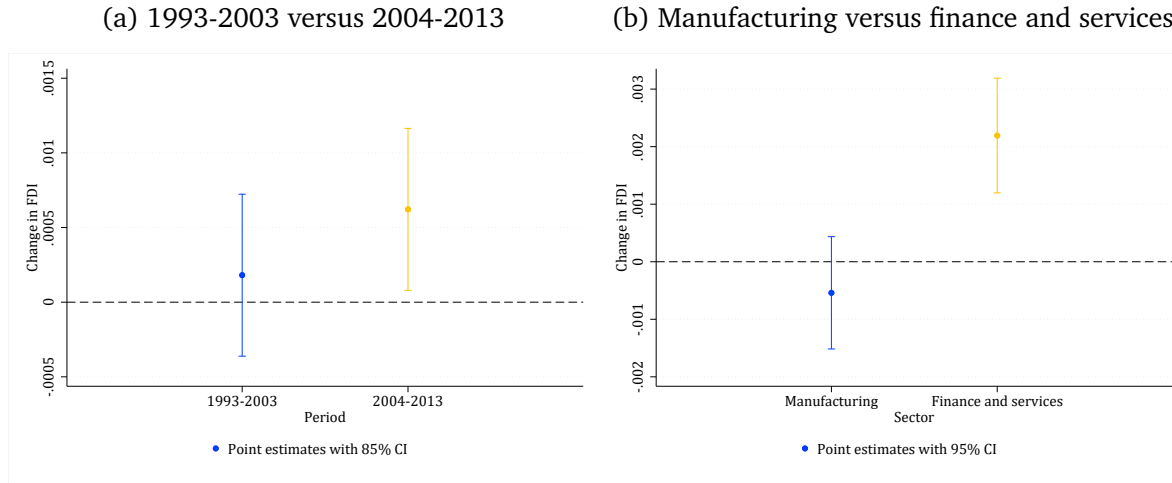
Notes: This figure shows how $\hat{\alpha}$ varies after excluding one tax haven at a time from regression (1). Standard errors are clustered at the firm-year level. See section 3 for more details.

thereby corroborating the common trend assumption. Note that parallel trends imply that the treatment variable is unlikely to be correlated with past unobserved firm- and sector-country-year shocks and greatly alleviate reverse causality concerns.

Treatment variable Table 3 panel B replaces $TREAT_{i,c,t}$ by $TREAT_{i,c,t}^C$, counting the number of firms in the same sector reporting at least one subsidiary in tax haven c and year t , or by $SHARE_{i,c,t}$, measuring the share of firms in the same sector reporting at least one subsidiary in tax haven c and year t . These alternative variables include information on both the extensive and intensive margins of peer presence in tax havens. Again, the two regressions yield a positive and significant coefficient consistent with the benchmark estimate.

Classification of tax havens In table 3 panel C, I modify this time the set of tax havens. Different classifications coexist because a low statutory corporate income tax rate is not a sufficient condition to be seen as a tax haven. Other criteria are determinant: lack of effective exchange of information, lack of transparency in legislative, legal or administrative provisions, etc. Insofar as they are difficult to assess, characterizing a country as a tax haven is somewhat vague and arbitrary. That is why I rerun the regression by using the classifications of Hines and Rice (1994) and Dyreng and Lindsey (2009) separately ($TREAT_{i,c,t}^{HR}$ and $TREAT_{i,c,t}^{DL}$) or by forming a more restricted list composed of the countries

FIGURE 5 – Heterogeneous effects: over time and across sectors



Notes: These graphs compare the intensity of spillovers over time and across sectors. Standard errors are clustered at the firm-year level. See section 3 for more details and Appendix table A3 for a full table.

found in the two lists ($TREAT_{i,c,t}^{DL \cap HR}$).⁴ A fourth regression puts six tax havens aside: Hong-Kong, Ireland, Luxembourg, Malaysia, Singapore, and Switzerland ($TREAT_{i,c,t}^{EX6}$). Because these countries are relatively large and well-connected with the rest of the world, FDIs of US-listed firms in these countries could be unrelated to tax avoidance. Notice in this regard that all six countries are in figure 2b. FDIs in remote and small jurisdictions like Jersey and Mauritius, for their part, more certainly fall within the scope of profit shifting. Appendix figure A1 illustrates that many tax havens, despite their size and isolation, attract a high number of US-listed firms that is disproportionate with what international trade theories would posit. Along similar lines, figure 4 reproduces the results after omitting one tax haven at a time. On the whole, the results are stable and coincide with the baseline estimate in all five cases, so they should hold for a large range of classifications.

Industry definition Table 3 panel D removes the smallest sectors. Firms operating in concentrated sectors may be more connected, for instance through strategic alliances. Hence, we may expect the results to be driven by such sectors. To verify that it is not the case, I reproduce the results by keeping only 4-digit SIC sectors with more than 15 enterprises ($TREAT_{i,c,t}^{>15}$) or by extending sectors at the 3-digit SIC level ($TREAT_{i,c,t}^{3-digit}$). Unsurprisingly, the point estimates are of lower magnitude. They are still coherent with

4. The two lists share 37 tax havens. Nonetheless, the classification of Dyreng and Lindsey (2009) is the only one to enumerate Aruba, Costa Rica, Malaysia, Mauritius, Nauru, Niue, Samoa, San Marino, and Seychelles. On the other hand, Hines and Rice (1994), unlike Dyreng and Lindsey (2009), retain the British Virgin Islands, Jordan, Maldives, and Saint Martin.

TABLE 4 – Heterogeneous effects: the role of tax havens' characteristics

Column	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Dependent variable	α_c	α_c	α_c	α_c	α_c	α_c	α_c
THS_c	0.29 ^b (0.14)						
$LACIT_c$		0.46 ^b (0.21)					0.42 ^b (0.18)
LG_c			0.24 (0.17)				-0.19 (0.53)
$TRSP_c$				-0.19 (0.14)			-0.20 (0.16)
AA_c					-6.46e-4 (0.10)		-0.04 (0.12)
$DTTA_c$						0.25 ^b (0.12)	0.34 (0.50)
R^2	0.12	0.30	0.08	0.05	0.00	0.09	0.38
No. of obs.	27	27	27	27	27	27	27

Notes: This table reports the regression results of equation (4) with different specifications. All variables are standardized. Standard errors, in parentheses, are heteroskedasticity-robust. The missing values stem from the fact that the tax haven score is not defined for all 50 tax havens. ^b $p < 0.05$, ^a $p < 0.01$. See section 3 for more details.

the reference one and validate that profit shifting spillovers are quite pervasive.

Falsification test In table 3 panel E, I mix all firms together and form 436 sectors in a random way as a placebo test. If the estimates exposed thus far truly reflect intra-industry spillovers, then we should observe no change in FDIs when another company from a random sector enters a tax haven. The result substantiates this claim. All in all, the aforementioned exercises attest to the existence of intra-industry profit shifting spillovers.

3.4 Heterogeneous effects

Before concluding, I explore the existence of heterogeneous effects over time, across industries, and between tax havens.

Disparities over time and across sectors Equation (1) estimates an average profit shifting spillover effect, but there are reasons to expect disparities over time and across sectors. Gumpert et al. (2016) and Merz and Overesch (2016) find that profit shifting of US MNEs has escalated in recent years, notably thanks to the implementation of the “check-

the-box” rules in 1997. In parallel, another stream of research emphasizes considerable industry-specific heterogeneity in profit shifting. Gumpert et al. (2016) and Merz and Overesch (2016) show that profit shifting is more intense in services and financial sectors compared to manufacturing, in line with the view that intangible assets facilitate tax dodging practices. Accordingly, I conjecture that spillover effects are larger (i) between 2004 and 2013 and (ii) in services and financial sectors (SIC 60-67, SIC 70-88) than in manufacturing (SIC 20-39). To confront these hypotheses with data, regression (1) is run on the four corresponding subsamples. Figures 5a and 5b graphically depict the regression results and support both hypotheses. As expected and thus not surprisingly, spillovers effects are stronger in the second subperiod (figure 5a) and in services and financial industries (figure 5b).

Country-specific spillovers Spillover effects could differ by tax haven, too. Appendix figure A2 confirms this and, in fact, reveals sizable disparities across jurisdictions. The figure plots the results obtained after adding a series of variables that interact the treatment term $TREAT_{i,c,t}$ with tax haven dummies $\mathbb{1}_c$:

$$FDI_{i,c,t} = \sum_c \alpha_c TREAT_{i,c,t} \times \mathbb{1}_c + \mu_{i,t} + \nu_{c,t} + \gamma_{i,c} + \epsilon_{i,c,t} \quad (3)$$

Well-known tax havens such as Barbados, Luxembourg, and Switzerland, already in figure 2c, stand out and feature in the top 10. A natural question emerges: What explains these differentials? One possibility is that spillovers depend on tax havens’ aggressiveness:

$$\hat{\alpha}_c = \eta + THS_c + \zeta_c \quad (4)$$

THS_c denotes the tax haven score computed by the Tax Justice Network.⁵ $\hat{\alpha}_c$ and THS_j are standardized for the ease of interpretation. The regression results of equation (4), provided in table 4 column (1), uncover a positive correlation between profit shifting spillovers and tax havens’ aggressiveness. A one standard deviation increase in the tax haven score is associated with a 0.29 standard deviation increase in income shifting spillovers. Columns (2)-(6) supplement column (1) and focus on each of the five components of the index, namely: lowest available corporate income tax rate (LACIT), loopholes and gaps (LG), transparency (TRSP), anti-avoidance (AA), and double tax treaty aggressiveness (DTTA). They demonstrate the prominent role of corporate income tax rates applicable in tax havens.

5. Due to data limitations, the data correspond to 2019. Given that tax havens’ characteristics do not significantly change over time, this should not constitute a major problem for this paper.

4 Conclusion

Using information on subsidiaries of US-listed companies in tax havens and an event study, I unveil in this paper the existence of intra-industry spillovers of profit shifting. A firm is more likely to own a subsidiary in a specific tax haven once another firm in the same industry establishes a physical presence in this tax haven. The results pass several robustness checks and suggest that firms tend to duplicate the tax dodging schemes of their peers. More work is now needed in this direction. Although US-listed firms are for many of them multinational and thus likely to appear in alternative databases, it would be interesting to ascertain the external validity of the findings through triangulation of data sources. Identifying the exact channels whereby profit shifting knowledge disseminates across multinational firms is another promising and challenging task for future research.

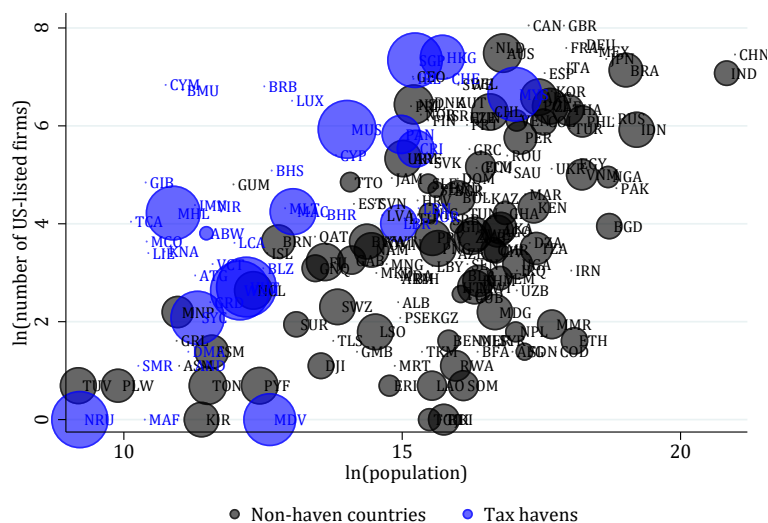
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Appendix

FIGURE A1 – Presence of US-listed firms in foreign countries



Notes: This figure represents on the y-axis the number of US-listed firms disclosing at least one subsidiary in each foreign country at some point between 1993 and 2013 and on the x-axis the total population of each country. The population size data are from 2003 and come from the World Bank. Bubble size for country c is proportional to $\sum_j dist_{jc} \times GDP_{j,2003}$ after standardization (data retrieved from the Geodist database of CEPII).

TABLE A1 – Sensitivity analysis: main tests (full table)

Panel	A	B	B	C	C	C	D	D	E
Dependent variable	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$
$TREAT_{i,c,t}$	0.14 ^b (0.07)								
$TREAT^C_{i,c,t}$		1.95e-3 ^a (1.45e-4)							
$SHARE_{i,c,t}$			0.11 ^a (5.69e-3)						
$TREAT^{HR}_{i,c,t}$				9.33e-4 ^a (3.07e-4)					
$TREAT^{DL}_{i,c,t}$					1.32e-3 ^a (2.85e-4)				
$TREAT^{HR\cap DL}_{i,c,t}$					8.95e-4 ^a (3.22e-4)				
$TREAT^{EX6}_{i,c,t}$						1.53e-3 ^a (2.45e-4)			
$TREAT^{>15}_{i,c,t}$							6.77e-4 ^a (2.47e-4)		
$TREAT^{3-digit}_{i,c,t}$								1.23e-3 ^a (7.43e-5)	
$TREAT^{random}_{i,c,t}$									-2.80e-4 (3.31e-4)
Firm-year FEs	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country-year FEs	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm-country FEs	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R ² (for LPMs only)		0.69	0.69	0.69	0.69	0.64	0.70	0.69	0.69
No. of obs.	82,736	5,514,400	5,514,400	4,301,232	5,073,248	4,852,672	3,646,650	5,514,400	5,514,400

Notes: This table evaluates the robustness of the benchmark estimate in table 2. Standard errors, in parentheses, are clustered at the firm-year level.
^b $p < 0.05$, ^a $p < 0.01$. See section 3 for more details.

TABLE A2 – Heterogeneous effects: dynamics (full table)

Dependent variable	$FDI_{i,c,t}$
$TREAT_{i,c,t}^{t+5}$	6.59e-4 (7.17e-4)
$TREAT_{i,c,t}^{t+4}$	-7.38e-4 (7.35e-4)
$TREAT_{i,c,t}^{t+3}$	-7.28e-4 (7.34e-4)
$TREAT_{i,c,t}^{t+2}$	1.27e-3 (7.44e-4)
$TREAT_{i,c,t}^{t+1}$	1.34e-3 (7.59e-4)
$TREAT_{i,c,t}$	-0.34e-4 (7.62e-4)
$TREAT_{i,c,t}^{t-1}$	2.18e-3 ^a (7.35e-4)
$TREAT_{i,c,t}^{t-2}$	1.70e-3 ^b (7.20e-4)
$TREAT_{i,c,t}^{t-3}$	9.51e-4 (7.24e-4)
$TREAT_{i,c,t}^{t-4}$	2.34e-4 (7.29e-4)
$TREAT_{i,c,t}^{t-5}$	-4.58e-5 (7.40e-4)
Firm-year FEs	Yes
Country-year FEs	Yes
Firm-country FEs	Yes
R ²	0.81
No. of obs.	1,238,800

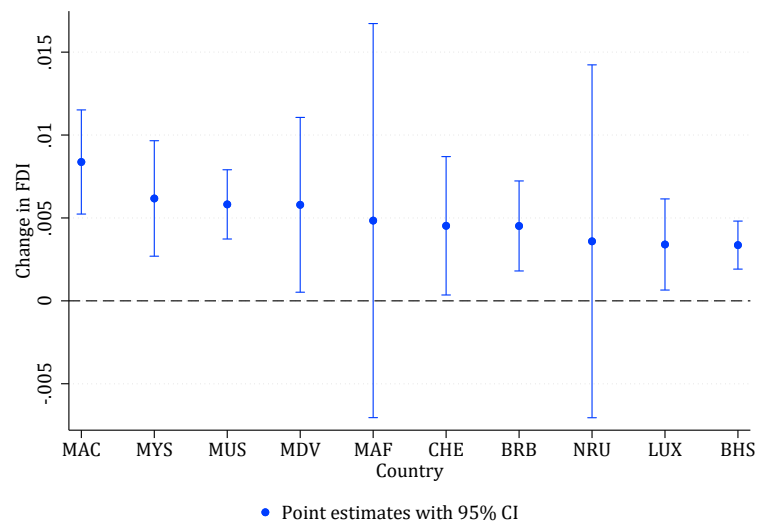
Notes: This table reports the baseline regression results of equation (2). Standard errors, in parentheses, are clustered at the firm-year level. ^b $p < 0.05$, ^a $p < 0.01$. See section 3 for more details.

TABLE A3 – Sensitivity analysis: over time and across sectors (full table)

Subsample	1993-2003	2004-2013	Manufacturing	Finance and services
Dependent variable	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$	$FDI_{i,c,t}$
$TREAT_{i,c,t}$	1.81e-4 (3.74e-4)	6.21e-4 (3.74e-4)	-0.54e-3 (4.23e-4)	2.19e-3 ^a (5.03e-4)
Firm-year FEs	Yes	Yes	Yes	Yes
Country-year FEs	Yes	Yes	Yes	Yes
Firm-country FEs	Yes	Yes	Yes	Yes
R ²	0.74	0.81	0.70	0.70
No. of obs.	3,002,700	2,480,050	2,535,450	1,346,900

Notes: This table reports the baseline regression results of equation (1) for different subsamples. Standard errors, in parentheses, are clustered at the firm-year level. ^b $p < 0.05$, ^a $p < 0.01$. See section 3 for more details.

FIGURE A2 – Regression results of equation (3)



Notes: This figure represents the regression results for equation (3) and highlights the top 10 tax havens. They correspond to the tax havens with the highest $\hat{\alpha}_j$. Standard errors are clustered at the firm-year level. See section 3 for more details.