THE AMAZON METHOD

HOW TO TAKE ADVANTAGE OF THE INTERNATIONAL STATE SYSTEM TO AVOID PAYING TAX

Richard Phillips - Jenaline Pyle - Ronen Palan

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The Amazon method:

How to take advantage
of the international state system
to avoid paying tax

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PREFACE

With the onset of the coronavirus pandemic in the spring of 2020, the international association of Amazon workers called for all warehouses to be closed, so that they would not have to continue risking their health for the company. But their call fell on deaf ears. Despite continued protests over the lack of health protections, operations continued and Amazon's coffers rang like never before. In 2020, Amazon's revenues increased by a record US$ 106 billion to a whopping US$ 386 billion. Amazon's founder Jeff Bezos, the richest person in the world, reportedly pocketed over US$ 70 billion in additional wealth.

The Amazon case shows the downside of globalization. Through the market power of multinational corporations, social wealth is concentrated in the hands of a few. This, however, is at the expense of the public. We know the stories of unfair competitive practices and exploitative working conditions: through predatory pricing, Amazon is driving competitors like Diapers.com out of business. Warehouse workers report feeling "like robots", only lucky to have escaped the multitude of accidents, or struggling with Orwellian surveillance practices and union busting.

Multinationals like Amazon now control about 50% of world trade. The Fortunes Global 500, the 500 largest corporations in the world, collect over US$ 30 trillion in revenues annually - almost twice the gross domestic product of the entire European Union. However, a substantial part of global trade is intra-company trading. These transactions and financial flows between affiliates of the same corporation are the building blocks of the tax avoidance schemes that enable the immense concentration of wealth in the hands of owners like Jeff Bezos.

To this end, the strategists of aggressive tax planning exploit the loopholes that originate from the differences between jurisdiction and their various inadequate tax regulations. In other words, they create a kind of arbitrage profit through the planned interaction of the multinational group of companies in the international sate system.

The damage to society is huge. Every year, multinational corporations shift over US$ 1.38 trillion in profits to tax havens. Worldwide, US$ 245 billion in direct tax revenues are lost in this way. However, it is difficult to make precise statements about the tax dodges of individual companies like Amazon. The lack of information and the opacity in reporting by these companies makes it almost impossible for the public to see how much tax they ultimately pay. Yet, multinationals benefit hugely from the public infrastructure provided by taxpaying citizens and businesses. The logical conclusion is that this obfuscation is intentional. In the following, this is referred to as reporting arbitrage: a deliberate method of concealing aggressive tax planning strategies.

This study on the "Amazon method" sheds light on the obscure international tax planning of the Amazon group. Its originality lies in the newly developed research technique, called Equity Mapping (EM). While existing studies are limited to the domestic dimension of Amazon's financial activities, the authors use the EM technique to examine the international interrelationships. The tax planning strategy of the global player is thus examined in detail and comprehensively.

Amazon's method is referred to by the authors as a Tax Credit Arbitrage Scheme (TCA scheme). The coordinating centre is the tax haven Luxembourg. In the small European Grand Duchy, Amazon subsidiaries book massive operating losses from international business, i.e., the business outside the USA. The generation of these losses is systematic and largely takes place in the global south, especially in India. In this manner, Amazon collects loss carryforwards, which are then turned into tax credits

in the USA. Consequently, Amazon is most likely paying little or no tax at all and will not do so in the near future.

However, this is only the first strike. Paradoxically, Amazon is not only accumulating losses but also untaxed profits in Luxembourgish companies. These are supposed to be taxed in the USA according to US regulations. However, at the end of the day, they are not repatriated and thus remain untaxed in foreign subsidiaries. Instead, these profits are to be permanently re-invested in international business. In other words, they provide a growth engine and an unfair competitive advantage for Amazon's expansion.

In short, the report illustrates that, by using the TCA scheme and opacity in reporting, Amazon's aggressive global tax planning aims to push its own tax burden as close to zero as possible. Amazon will certainly not be the only multinational to use these methods. The study therefore provides us with valuable insights into tax planning strategies of large corporations in general, and Big Tech in particular. Now, political consequences must be drawn from these new insights.

The European Commission had already launched an investigation into Amazon in 2015 on its illicit profit shifting. However, as we can now see, the narrow focus on profit shifting is leading us down the wrong track. The secret of Amazon's method is not to be found in the handling of profits but in the systematic production of losses. The demand that arises from this is clear. A renewed investigation of Amazon by the European Commission and competent authorities must follow.

The creation of a fair tax system is long overdue, and in view of skyrocketing public debts in the wake of the Covid-19 crisis, we can no longer afford the tax abuse of large corporations. Instead of austerity policies, we need tax justice. The absurd concentration of power and wealth must be combated with redistribution. In this way, we can cover the costs of the crisis and pave the way for a social-ecological and digital transition.

Tax justice goes hand in hand with tax transparency and therefore with mandatory public country-by-country reporting for all large corporations, enabling the public to hold them accountable. It requires an effective global corporate minimum tax of 25% to curb international tax competition. It means enforcing the principle of unitary taxation for multinationals, so that no country is played off by networks of subsidiaries and tax havens. It requires the definition of a "significant digital presence" to be anchored in tax law, so that tech companies with digital business models can be made to pay tax, even if they have no physical establishment in a jurisdiction. Today, the call for tax justice is moreover a call for an excess profit tax in order to have crisis profiteers like Amazon contribute to the resolution of the crisis.

Tax Amazon Now!
Martin Schirdewan

MEP, Co-President of
The Left in the European Parliament

SUMMARY OF FINDINGS

A small minority of businesses in the world are multinational enterprises (MNEs). These organizations have become key vehicles for innovation, wealth creation, but also wealth concentration in the modern world. Many countries have introduced systems of corporate taxation as instruments for the redistribution of power and wealth, ensuring that businesses contribute to the cost of maintaining the state-of-the-art infrastructure provided by the societies from which they benefit. MNEs employ some of the sharpest legal and accounting brains to exploit the system of rules, regulations and taxation created by states, especially gaps and loopholes arising between different jurisdictions, to avoid paying taxes. Cross-subsidies is the direct impact of international corporate tax mitigation strategies; the less MNEs pay in taxation, the more someone else has to pay, typically sections in society that are unable to employ those professional services.

In this report we look at the way Amazon has organized its domestic and international business to minimize taxation worldwide. This study complements existing studies, which rely on information contained in Amazon Form 10-K annual filings in the United States and company accounts of various European and UK subsidiaries. We employ, in addition, a new technique, which we call **"equity mapping"** (EM), to cross-examine Amazon's international activities over the last decade against subsidiary level records to study Amazon's integrated tax planning strategies. The equity mapping technique was developed out of an ongoing CORPLINK study funded by the European Research Council Advanced Grant. As a result, this report highlights select parts of Amazon's financial reporting that have generally been ignored by other analysts.

Existing studies reached the conclusion that Amazon pays either very little tax or no tax at all in the US. However, due to reporting opacity, the precise numbers are disputed and Amazon's activities outside the US are neglected. We identify certain gaps in the currently available data as presented by Amazon that raise important questions about the role played by Luxembourg and Amazon's non-EU subsidiaries in Amazon's tax planning. Losses generated outside of the EU appear to have been converted by Amazon into tax credits in the U.S, thus ensuring that Amazon pays little or no taxation. Our analysis leads to the conclusion that Amazon operates with a specific **tax credit arbitrage scheme** coordinated through subsidiaries located in Luxembourg.

Over the last decade, Amazon has generated greater untaxed profits than the total amount of taxes it has ever owed. Much of this has taken the form of "loss carryforwards"—an accounting term that describes qualifying net operating losses that are used to reduce future tax liabilities. Amazon's **net total operating loss carryforwards reached US$ 13.4 billion by 2020**. This figure was higher than the total taxes payable by the group for the entirety of the group's history to date (US$11.71 billion). Much of those losses originated from Amazon's non-European subsidiaries. Unfortunately, Amazon's reporting of its international affairs is perplexing and raises doubts about its tax affairs. Subsidiary data reveals that loss-making has been a common and recurring feature distributed across many members of the corporate group. For instance, one of Amazon's Indian subsidiaries alone generated over US$3.46 billion in cumulative operating losses over the last decade. Its operating expenses averaged 220 percent greater than the level of operating revenues reported by the company.

Despite accumulating heavy losses internationally, **Amazon also accumulated US$ 17.2 billion of unrepatriated profits in its international segment**. It remains a mystery as to how Amazon posted such heavy losses while simultaneously accumulating unrepatriated profits. Based on US rules for Controlled Foreign Subsidiaries (CFCs) these profits accumulated abroad are supposed to be taxed in the US. However, the profits are never formally repatriated, but re-invested in international activities in perpetuity so that they remain untaxed. The accumulation of tax deferrals, the single largest of which has typically been the losses generated in foreign markets, has been used to dramatically limit the level of income taxes reportedly paid out from Amazon's cash flow.

The conclusion of this study is that **Luxembourg is at the centre of Amazon's system** of globally coordinated losses that simultaneously generate also unrepatriated profits. This is supported by observation that Luxembourgish set of entities account for the inexplicable ~75% of all Amazon's international sales. The European Commission conducted an investigation of Amazon in 2015. From this investigation, it is plausible to infer that the unrepatriated profits are the result of **illicit profit shifting**. However, the EC's investigation focused narrowly on only two Luxembourgish subsidiaries. More importantly, it did not focus on the actual strategy of tax planning, which is the accumulation of losses generated primarily by non-EU subsidiaries to create tax credits (instead of producing profits).

Financial reporting can be likened to a script with highlighted entries wherein in the final report only the highlighted entries are left visible. The analyst relies on data provided by the MNEs in order reconstruct the full script from those entries. Amazon present financial data in a confusing manner, thus making it more difficult to identify and quantify tax mitigation strategies. This report presents reasonable interpretation of the data available but further analysis of Amazon's reports would necessitate additional discussion following this report. The report suggests therefore that further investigation is necessary by the EC or another public authority. Specifically, such investigation should concentrate on the simultaneous rise in international losses and unrepatriated profits coordinated through Luxembourg. Such investigation by public authorities has become even more significant considering that Amazon's method of tax avoidance includes also reporting arbitrage. That is to say, Amazon appears to create opacity in reporting on purpose and presents data in a confusing manner in order to conceal potential its aggressive tax planning strategy.

Amazon Web Services (AWS) present another puzzle. Although rising in importance and accounting by now more than 10% of Amazon's global sales, it is unclear how much taxes AWS pays or even if it pays any taxes at all. Further investigation is required here as well.

Amazon is unlikely to be alone in pursuing tax credit arbitrage. The authors of this report found evidence that other large American firms may be pursuing a similar strategy and possibly with the encouragement of US government policy. More importantly, political divisions and sovereign spaces enable constructive opacity in accounting, taxation and corporate governance. As a result, it is impossible to identify the precise amount of tax that is paid or avoided not only by Amazon, but by other MNEs as well. Tax and reporting arbitrage are enabled not only by a specific set of jurisdictions, typically branded offshore financial centres, but may be arise either accidentally or indeed intentionally in geopolitical competitive markets.

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GLOSSARY

AWS	Amazon Web Services
CFC	Controlled Foreign Company
CJEU	Court of Justice of the European Union
EC	European Commission
EM	Equity Mapping
ETR	Effective Tax Rate
GAAP	Generally Accepted Accounting Principles
IFRS	International financial reporting standards
IRS	Internal Revenue Service
ITEP	The Institute on Taxation and Economic Policy
10-K	Annual report required by the U.S. SEC
MNE	Multinational Enterprise
OFC	Offshore Financial Centre
ROW	Rest of World
SEC	Securities and Exchange Commission
TCJA	Tax Cuts and Jobs Act
TJN	Tax Justice Network

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PURPOSE OF STUDY

Multinational enterprises (MNEs) can be defined as organisations that make use 'of productive resources for the purpose of supplying goods and services to the economy in accordance with plans developed and put into effect within the firm' (Penrose, 2009, 15). Although only a small minority of businesses in the world are multinationals, these organizations have become key vehicles for innovation and wealth creation in modern capitalist societies. Jean-Phillipe Robé, a legal scholar and political economist, shows that by historical quirk, multinational enterprises grew into the giants of the modern world by exploiting rules that were set up originally for the protection of individual's rights to property, autonomy, justice and free will, to create, in effect, transnational privatized spaces in control of vast societal resources. The MNE had become, he writes, are a device 'for the concentration of property rights over productive assets' (Robé, 2020, 7). So much so, that by now eight individuals have managed to harness this system of concentrated privatized transnational space to the point of 'owning' assets at above US$ 100 billion. An individual with 100 billion wealth who invests in a modest 5% wealth yielding financial instrument would make US$ 570,000 every hour, 24 hours day, every day of a year. It takes such individuals only 2.6 minutes to 'earn' enough money to buy the most expensive dish ever made (the Grand Velas Tacos at $25,000), slightly more than a full day to purchase the most expensive car ever made, the Pagani Zonda $17.5, or a month to buy the most expensive home available. To think that such concentration of property rights is deployed merely to allocate resources as efficiently as possible is naïve.

Another absurdity of the modern world is how these individuals manage to harness the services of the entire modern state system as a protection racket for their wealth. They do not have to maintain an army to protect their wealth. The state system does. Such concentration of power and wealth in hands of the very few was never intended to take place, nor is it believed to be of use to anyone, including these individuals or their inheritors. On the contrary, states set up rules, regulations and taxation, decried by some as 'red tape,' to ensure that the great potential for innovation and efficiency in a system of private ownership is distributed fairly and widely, both in term of access to the potential benefits as producers and consumers.

Taxation is a key dimension of the system of redistribution of power and wealth. Taxation is used to ensure that the state-of-the-art infrastructure is made available to society; that the education system that provides the quality researchers, engineers and technicians and managers needed by the MNEs, that the stable political and legal system protects future investment. The health system, roads, bridges, tunnels, ports, airports, the internet, and all other infrastructure is needed by the concentrated private wealth, which also helps – or should help, in principle - finance the infrastructure. Economists are fond of saying that there is no such thing as free lunch. They are correct. If the MNE does not pay, say, for polluting the river, the river is still left polluted and someone else has to pay the price. If the MNE does not pay corporate tax, then someone else, typically the weaker members of society pay. Corporate taxation as a system was introduced, in other words, not only to finance costly infrastructures, but also to ensure that the MNEs, or rather, their shareholders, are not using the corporate vehicle as a system of subsidy by which the poor are paying for the rich to become even richer. Is that too much to ask for?

MNEs that somehow manage to reduce their taxation do not only not pay their fair share. They are using their power and wealth so that someone else pays for them, and by implication, they use their power and wealth to earn a subsidy from society.[1] Yet, we find that some MNEs are able to use the very system of rules, regulations and taxation enacted by states as a vehicle for further concentration of power. They take advantage of the inevitable gaps, loopholes, omissions in law, particularly those that exist between countries, to arbitrage the rules of one country against another, forging a path of least resistance through the maze of rules.

1 For discussion see: (Nesvetailova and Palan, 2020; Robé, 2020).

Amazon has been singled out in a number of studies among multinationals as a notorious offender that pays little or no tax at all. We know that when Amazon enters a market, it is not long before it starts to dominate the market sending local businesses into bankruptcy. But if Amazon is then able to minimize or pay no taxation at all, then it robs those markets of potential income from those bankrupt businesses and ensures that as countries enter its system of cross-subsidies, their markets serve in effect as a tool for further concentration of power and wealth in the hands of few. The results are clear to all to see, Amazon's main shareholder, Jeff Bezos is 'worth' now nearly US$ 200 billion, and is ex-wife US$ 60 billion. But how did this level of concentration of power came about? The system of corporate taxation, often reaching 30% or more in the core countries in which Amazon operates should have ensured that a)Amazon competes on a more equal footing with others, preventing such level of concentration or power and wealth, and b) that the benefits of Amazon's success would have been distributed more widely. This study uses Amazon's own financial reports to try to disentangle the complex and sophisticated techniques used by Amazon to create such concentration of wealth in the hands of so few.

The amount Amazon pays in the U.S. or in other countries is disputed. Moreover, the clever technique used to ensure that Amazon is cross-subsidised by the societies in which it operates is not entirely clear. The Institute on Taxation and Economic Policy (ITEP) estimates that despite rising pre-tax income, from $5.6 billion in 2017 to $11.1 billion in 2018 and $13.2 billion in 2019 in the U.S. alone, Amazon's total federal tax was negative – a rebate of 102 million dollars.[2]

The ITEP reports argues that:

> *"The mechanisms the company [Amazon] is using to drop its effective tax rate are mostly unchanged: the company saved $1.8 billion using tax breaks for stock options, and it saved $639 million using various tax credits… The effects of depreciation breaks are complex. Part of the effect is to move tax payments further into the future, even though the net effect in the long run reduces the company's tax liability. This makes it important to look at a company like Amazon over several years.[3]"*

A report by the Fairtax Mark concurs with ITEP on Amazon's overall tax strategy but estimates, in contrast, that Amazon has paid $3.4 billion in income taxes this decade.[4] A Uniglobal study reached the conclusion that "During the last six years, Amazon paid only $7.8 billion in income taxes… whereas in the last two years Amazon Europe received tax credits for more than half a billion euros"[5]. Recently President Biden named Amazon specifically among large American MNEs that that "use various loopholes where they pay not a single solitary penny in federal income tax".[6] Amazon's own position is that ETR is not a particularly useful method to assess its performance, given the myriad reasons this value can change dramatically from year to year.

2 https://itep.org/the-price-we-pay-for-amazon-in-its-prime/
3 https://itep.org/amazon-has-record-breaking-profits-in-2020-avoids-2-3-billion-in-federal-income-taxes
4 "The Silicon Six" The Fairtax Mark, 2019 [online] Available at: https://fairtaxmark.net/wp-content/uploads/2019/12/Silicon-Six-Report-5-12-19.pdf [Last accessed 1 April 2021].
5 "Amazon and the Covid-19 Crisis" Uniglobal Union, 2020, page 7. [online]
Available at: https://www.uniglobalunion.org/sites/default/files/public_shared/amazoncovid_en_pages.pdf [Last accessed 1 April 2021].
6 https://www.reuters.com/article/us-usa-biden-amazon-taxes-idUKKBN2BN3LL

Still, much of Amazon's tax affairs remain a puzzle. Much has been made about how Amazon pays little or no federal taxation; yet few question Amazon's activities outside the U.S. For instance, from Amazon's accounts it is unclear whether Amazon's fastest growing source of income, Amazon Web Services, has any income attributed to foreign states where they are generated, or solely to the U.S. market, and whether AWS paid any tax in Europe or abroad. In addition, foreign subsidiaries are sometimes treated as domestic for tax purposes, whereas in other sets of data they are classified as foreign. Fairfax study began to outline Amazon's international tax strategy, noting an extensive use of U.S. tax credits and deferrals, and anecdotally presenting snapshots from a small handful of European subsidiaries. Yet Amazon's foreign subsidiaries number in the hundreds, their structure and mode of operation remains unknown.

This report builds on existing studies but uses a new method of investigation we call 'equity mapping', a technique that relies on data derived from subsidiaries to cross-examine consolidated reporting. Whereas existing research on Amazon's tax paying has been limited by a domestic focus (as European agencies have focused on Amazon's activities in Europe), we adopt an integrated approach which seeks to understand how the US, International, and AWS components are organized as part of an integrated strategy for managing its tax affairs.

We should be clear that there are limits to this approach. First, the data we analyse is produced either by Amazon or by Amazon's subsidiaries and collated by data providers Bureau van Dijk in their Orbis data service, and was not independently verified. Secondly, not all of Amazon's subsidiaries are likely to be contained in the Orbis data (for instance, there are no Japanese subsidiaries reported in the Orbis database, one of the larger foreign markets Amazon singles out in its reporting). In addition, many of Amazon's subsidiaries are located in jurisdictions that either do not require annual filings by subsidiaries, or are not required to present those accounts to the public (like its subsidiaries in the U.S., the largest cohort of the corporate group). Nonetheless, in comparing consolidated against subsidiary filings, the international aspect of Amazon's operation appears to be relatively representative of many of the values and trends reported in its annual accounts.

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WHO IS AMAZON?

The question of who is Amazon is far more complicated than commonly assumed, not least because multinational enterprises (MNEs) are not unified legal persons. Strictly speaking, they consist of group of companies held together through equity ownership, whereby each unit in the group may be considered by law to be an independent corporation. The complexity of laws surrounding the very existence of MNEs as economic actors and the diverging rules governing how their activities are reported can present opportunities for tax and reporting arbitrage. Tax arbitrage includes techniques that take advantage of gaps, loopholes and other omissions in the laws of different countries to minimize corporate and other forms of taxation (such as capital gains tax and the like). Reporting arbitrage include techniques that take advantage of gaps, loopholes or other omissions in reporting rules in different countries in order to create opacity of the groups' accounts, including its rate of taxation, to the outside world. Understanding the different reporting systems, purposes, methodologies, and requirements demonstrates the challenges of defining the boundaries of corporate groups and understanding their tax affairs.

Large, public corporations in the United States generally keep many different sets of records to provide a complete picture of the company's financial position, not all of which are publicly available. For instance, the group maintains an internal document showing its capacity to pay bills, the extent to which it can withstand downturns in revenues and unexpected expenses. This is an internal document that is not publicly made available. Similarly, the group budget, which sets revenue targets and spending limits, is not made publicly available. The Internal Revenue Service (IRS), state tax authorities as well as many foreign jurisdictions, in which the group holds subsidiaries, require financial reports. This third category of reports are not publicly available, which is why it is impossible to have a complete picture of what taxes a company like Amazon does regarding tax.

To complicate matters, the group consists of separate and independent legal persons, 'corporation' (or 'company' in English jurisprudence or 'societé' in French law), and only those own assets and partake in contracts in markets.[7] So while consolidated accounts (like 10-K SEC filings) present a story "as if" an MNE is a singular operating unit, each member of the group is a distinct legal person and within the group that commonly interact with each other in complex ways that shape the way corporate finance works. Only those legal persons, subsidiaries, actually own things or partake in contracts in the marketplace that generate value. Those values are aggregated and consolidated into one narrative associated with an entity called "Amazon".

This legal basis to the corporate group subjects each of its members to their own reporting requirements spread across a multitude of jurisdictions around the world. This is often ignored, especially by analysts of US corporations, because the legal statues of the (American) states in which entities are incorporated frequently allow those persons to present little or no information, particularly financial information, to the public. Consequently, there is often little choice other than the official consolidated accounts from which to use for assessing many US corporations. The fact is that the US is the world's largest 'secrecy jurisdiction' (TJN, 2020). Outside of the US, a number of jurisdictions commonly known as Offshore Financial Centres (OFCs), like the Caymans Islands, present different arbitrage opportunities for multinational enterprises to help minimize corporate taxes or obfuscate reporting, following the U.S. example to some extent. The extent to which corporations use these jurisdictions complicates attempts to independently verify behaviours at the level of discrete subsidiaries.

7 For discussion see: (Robé, 2011).

While many important accounts of what a corporate does are private, some are for public consumption. The most commonly used are the consolidated annual accounts, referred to as the 10-K filings in the US. These financial reports required by the Securities and Exchange Commission (SEC) and are intended to provide transparency and information about the company's business practices to investors. The SEC and IRS both use actuarial accounting and help shape the industry standard referred to as Generally Accepted Accounting Principles (GAAP), though they sometimes differ in specific rules. Because the IRS has to collect taxes in accordance with tax laws, there can be some divergence between SEC and IRS accounting approaches. Furthermore, accrual accounting standards calculate costs over time, rather than from a cash-flow basis and thus may not be paid in that fiscal period covered. This contributes to possibilities for disconnections between the time period of the report, and the time periods of many things described in accounts, such as taxation and the use of deferrals.[8]

Amazon also takes advantage of different reporting requirements to present data in a confusing manner. For instance, although Amazon refers to its International division as a separate segment, there is a tendency to blur geographical categories when it comes to describing income and taxes. Some European sales of AWS may not be classified as "foreign" so that value from the international retail segment can be captured as a domestic investment (such as the historical use of a partnership structure to organise transfer pricing between Luxembourg entities investigated by the EC). In addition, Amazon's 10-K accounts do not distinguish between the EU and the rest of the world (ROW), except in some years when attributions were given as to the source of operating profits and losses. Rather, Amazon's accounts only single out two EU jurisdictions and lump all other European markets under ROW.

Existing studies of Amazon tend to rely primarily on the 10-K reporting. According to the latest 10-K (FY 2020), Amazon.com, Incorporated is an American business based in Seattle, Washington, incorporated in Delaware, and has income originating from operations into three distinct areas: North America, International, and AWS (Amazon Web Services). In 2020, its overall sales were US$386 billion. The majority (61%) of this was from its North American retail division with US $236 billion in sales, while the

Table 1 – Information on reportable segments and reconciliation to consolidated net sales is as follows (in millions $US)

Row	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2010 2020	
1	18,707	26,705	34,813	44,517	50,834	63,708	79,785	106,110	141,366	170,773	236,282	973,100	North America
2	15,497	21,372	26,280	29,934	33,510	35,418	43,983	54,297	65,866	74,723	104,412	505,292	International
3	-	-	-	-	4,644	7,880	12,219	17,459	25,655	35,026	45,370	148,253	AWS
4	34,204	48,077	61,093	74,452	88,988	107,006	135,987	177,866	232,887	280,522	386,064	1,626,645	Consolidated

Source: Amazon 10-K various years

8 https://sccinsight.com/2020/02/09/understanding-amazons-income-tax-bill/

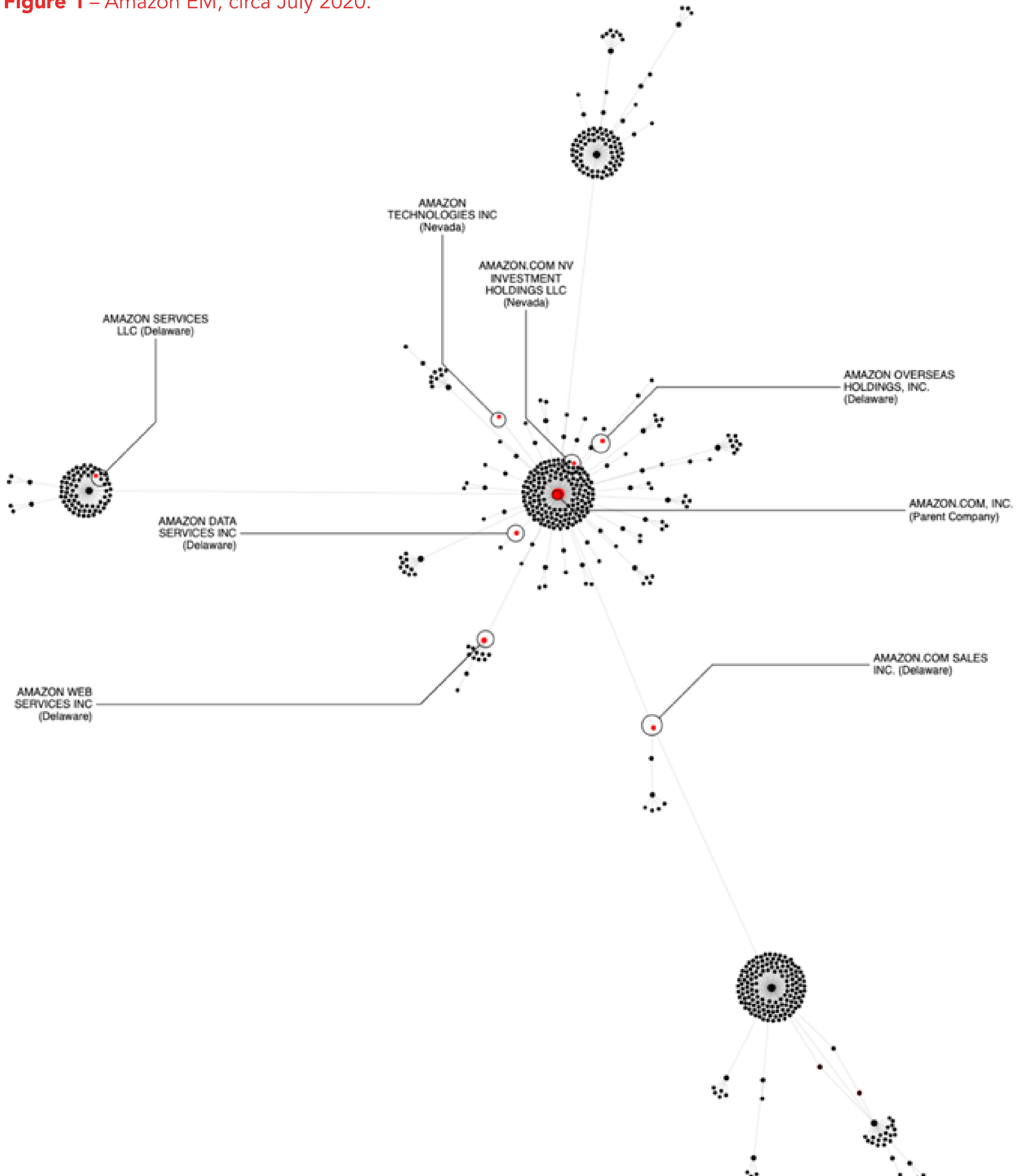
international retail segment reported US $104 billion (27%) and AWS reported US $45 billion (11.5%). Sales in its North American division come primarily from retail sales of consumer products (including from other retail sellers) and subscriptions (including digital streaming) through North-American based online and physical stores for consumers in Canada, the US, and Mexico. It also includes export sales from these online stores. The International division consists of retail sales of consumer products and subscriptions through online stores outside the US division, but also includes export sales from these online stores to customers in Canada, the US, and Mexico.

Yet as highlighted earlier, Amazon is not simply the sum total of the numbers used to describe its accounts. It is a set of accounts generated by the distinct legal persons that make up the group itself. For the purpose of this study, we include considerations of subsidiary reporting data to gain insights into the legal organisation and change over time, as well as to be able to construct, to the extent that is possible, an alternative set of financial accounts describing its international activities as they exist is their own respective legal personality. The underlying techniques for doing so were developed through on ongoing "CORPLINK" research project funded by a European Research Council Advanced Grant in which the authors of this report have participated. Using the Orbis database, CORPLINK developed a set of powerful analytical methods that help map the inner legal structure of firms and allow for a more thorough examination of the historical and managerial behaviour of each entity. The data is 'cleaned' and then displayed with the help of an algorithm in a visual map we call equity mapping (EM). Our techniques allow us to track corporate patterns and analyse potential weaknesses in the system of governance that may affect that ability of stakeholders to monitor effectively. To learn more about the approach see: Nesvetailova et al., 2020; Phillips, et al., 2020.

Figure 1 shows the legal structure of Amazon, mapping the relationship between various subsidiaries, their registered name and location. From this perspective, it is evident that Amazon is organized not simply through Delaware and Nevada (the only jurisdictions mentioned in Amazon's latest list of 'significant subsidiaries') but also, critically, Luxembourg. Indeed, all of these jurisdictions are known for lower levels of taxation precisely because of the way in which complex international regulations and treaties allow different forms of arbitrage opportunities to be used.

It is apparent from Amazon's EM that Amazon's legal structure is not reducible to the description of itself as three independently managed segments. For example, Amazon Overseas Holding Inc. (Delaware) is a standalone subsidiary with no further sub-holdings, whereas the majority of Amazon's non-American subsidiaries are held via a branch headed by Amazon.com Sales Inc. (Delaware). AWS may be described as its own "segment" yet various Amazon "web service" entities are distributed throughout different parts of the structure. For instance, while there is a separate branch controlled by Amazon Web Services Inc. (Delaware), Amazon Data Services Inc. (Delaware) resides in a separate branch not linked through equity control to AWS. Other European "Web Service" companies, in turn appear to reside in the same cluster of ownership as entities involved in the retail segment. Yet legal structure gives us two important handles to cross-examine public accounts. Firstly, it gives us an ability to clarify subsidiary control so that we can interrogate the history of their ownership, governance, and financial reporting, for example. It also gives us clues as to where entities may be relocated to and moments of key restructuring that can add important historical context to understanding who, how and when arrangements are changed and what discernible impact that may have on reporting behaviours.

Figure 1 – Amazon EM, circa July 2020.

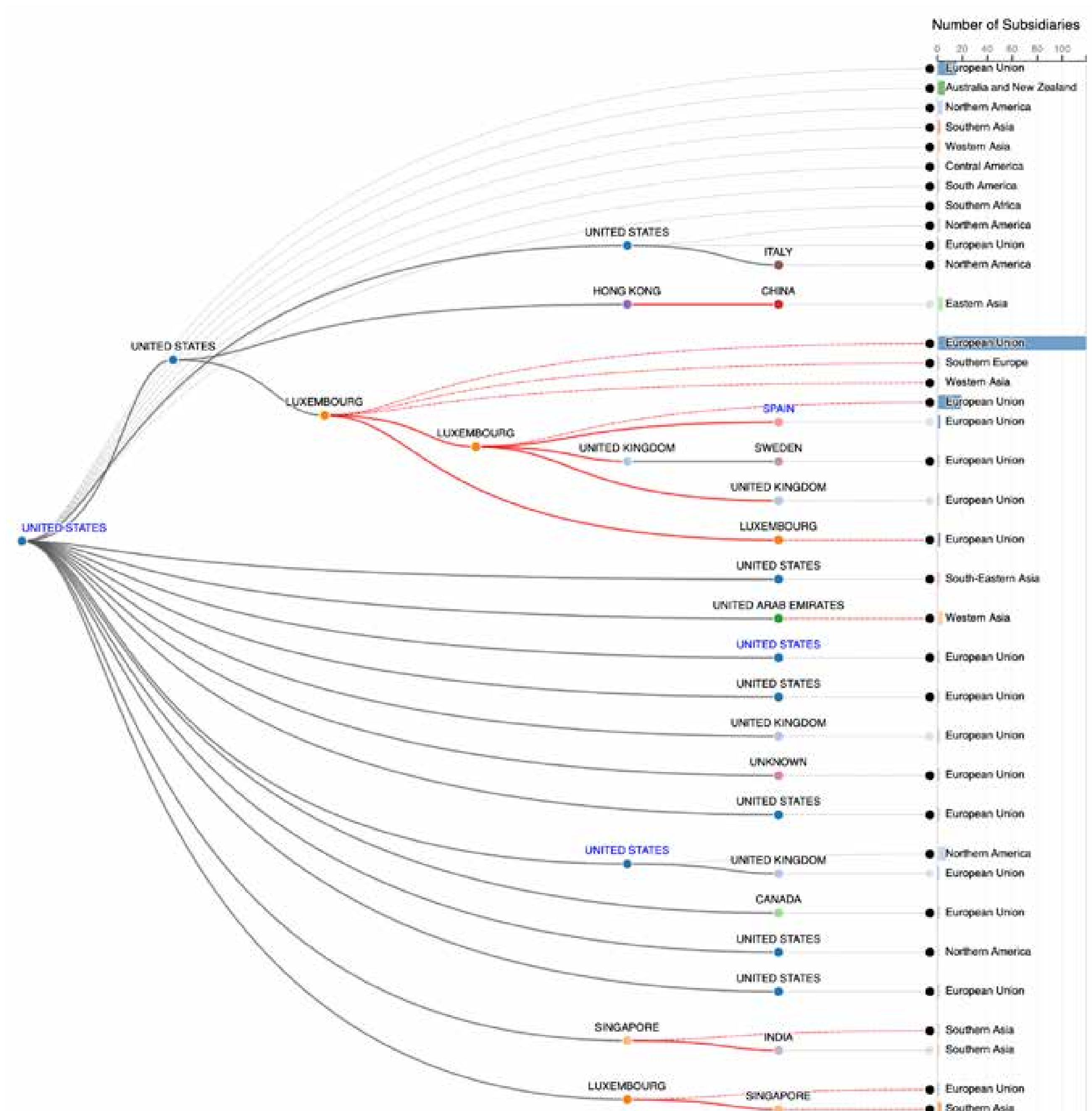


Legend:

EM	=	Equity mapping of subsidiary holding
Red Dot	=	Important subsidiary named in Amazon's 10-K
Black Dot	=	private subsidiary not mentioned in the latest report
Cluster	=	large groupings of subsidiaries held important intermediate holding companies and generate a spatial clustering effect
Conduits	=	subsidiaries that own only one or even a few other subsidiaries, yet these holdings are themselves major shareholdings in a large set of subsidiaries, are visually distinguished as being 'in-between' the main parent company and the disparate sub-clusters of the group

Another way of displaying Amazon's EM is presented in Figure 2, which uses the data from Figure 1 to display more clearly the central role of different intermediate holding group subsidiaries from a variety of domestic and international jurisdictions and the volume of subsidiaries they hold from different regions around the world.

Figure 2 – Core Intermediary Subsidiary Holdings of Amazon



02

THE THEORY BEHIND AMAZON'S GLOBAL TAX STRATEGY

The current international regime of business taxation is predicated on the differences between active and passive income. Active business income is generally taxed wherever the activity occurs, in 'source' jurisdiction, while passive income (or investment income) is assigned to the jurisdiction where the investors reside. Over time and for a variety of reasons, passive income taxation, also known as resident taxation, has been abandoned by most countries (for discussion see: Matheson et al., 2013.). By now, among OECD countries only the US and the Netherlands have maintained the principle of resident taxation—although even that is in some doubt (Avi-Yonah, 2019). This has created a situation where US investors are taxed twice on foreign investments: first at the source, then on repatriation to the US.

To resolve this situation, the US tax credit system invoked a doctrinal position known as capital export neutrality (CEN) (Graetz, 2016). Under this position, an international tax regime should promote neutrality about a resident's choice between domestic and foreign investments. In the early 1960s, the US introduced the concept of the controlled foreign company (CFC) whereby certain foreign affiliates are considered as part of the U.S parent for tax purposes, thus hoping to eliminate the advantages of setting up intermediary subsidiaries in low-tax offshore financial centres (OFCs). Tax rules in the US also differentiate between conduit (or pass-through) enterprises and corporations. "Income earned through certain domestic business entities—'corporations' for tax purposes—is subject to taxation once at the entity level and again when distributed to the entity's owners. By contrast, income earned through other business entities—'conduits' for tax purposes—is taxable directly to the entity's owners and not taxable at the entity level" (Speck, 2015). In 1996, Congress introduced the 'tick the box' rules for CFCs. This required a US parent company to choose how the CFC would be treated for tax purposes. Known as 'electivity', this gives companies a choice between being treated as a conduit or a corporation, irrespective of their actual function. A CFC could be considered an independent corporation in its country of residence, but a mere 'conduit' for American tax purpose. If the CFC happened to register losses, those losses accrue to the parent and are subject to tax deferrals. Unsurprisingly, tax advisors have taken what one tax scholar calls 'an instrumental approach' (Speck, 2015), to the distinction between a corporation and a conduit and applied this distinction to their CFCs, thus seeking their preferred tax status while limiting adverse non-tax consequences. As a result of these policies, many US CFCs do not pay tax directly but instead allocate their net profits or, as we will see in the case of Amazon, apparent losses, to the parent.

For Amazon, like other companies employing this strategy, a set of foreign subsidiaries are treated as domestic entities for US tax purposes. Amazon does not specify which foreign entities are treated as being US domestic tax resident or which among them generate operating profits or losses. Yet because of the amount of losses Amazon generates internationally, and the correlation between foreign operating losses from its international segment with the early growth in foreign loss carryfowards, at least until FY2016/17, we can reasonably infer the likely treatment of Amazon's Luxembourgish CFCs within the clustering of where losses were generated. Indeed, the EC investigation into Amazon uncovered that the main European operations, all headquartered in Luxembourg, were held via a partnership structure. The implications are that the Luxembourgish 'partnership' were logged in the U.S. as conduits for tax purposes rendering the profits of that partnership a US domestic concern. While Amazon would restructure these entities following the EC investigation (discussed below), the continuity between foreign losses and unrepatriated profits that have accrued and tax deferrals created in the US from these, strongly suggests a continued use of CFC rules in the management of its international activities. This is particularly significant because it appears that the high level of loss-making foreign entities is being used to generate a vast amount of tax credits and deferrals.

This baseline system has been altered by recent tax reform in three ways. First, one of the effects of Tax Cuts and Jobs Act (or Trump tax reforms) was to exempt from US tax any profits of US CFCs that are less than 10 percent of a company's net value of foreign tangible assets (such as equipment, machinery, and structures). We speculate that the changes may be one of the reasons that Luxembourg is no longer classified as 'significant subsidiaries' in Amazon's recent annual reports. Second, the new tax law allows CFCs to deduct 50 percent of profits greater than 10 percent of net asset value so defined, which, at the 21 percent corporate rate, makes the effective rate on this income (called global intangible low-tax income) equal to 10.5 percent. Firms may claim credits for 80 percent of foreign taxes attributable to global intangible low-tax income, which means that US corporations pay a residual tax on any foreign profits taxed at rates of 13.125 percent (10.5 divided by 0.8) or less." (Sammartino and Toder, 2019, 3). In addition to lowering the statutory tax rate from 35% to 21%, the 2017 Tax Cuts and Jobs Act included a grandfather clause for companies that have managed to defer or postpone tax liability from prior years, like Amazon. As ITEP researchers explain, "Instead of paying these deferred taxes at the previous 35 percent rate, Amazon now gets an extra reward for postponing the taxation of this income: a 40 percent discount from 35 to 21 percent. This is the source of Amazon's US $789 million windfall."[9]

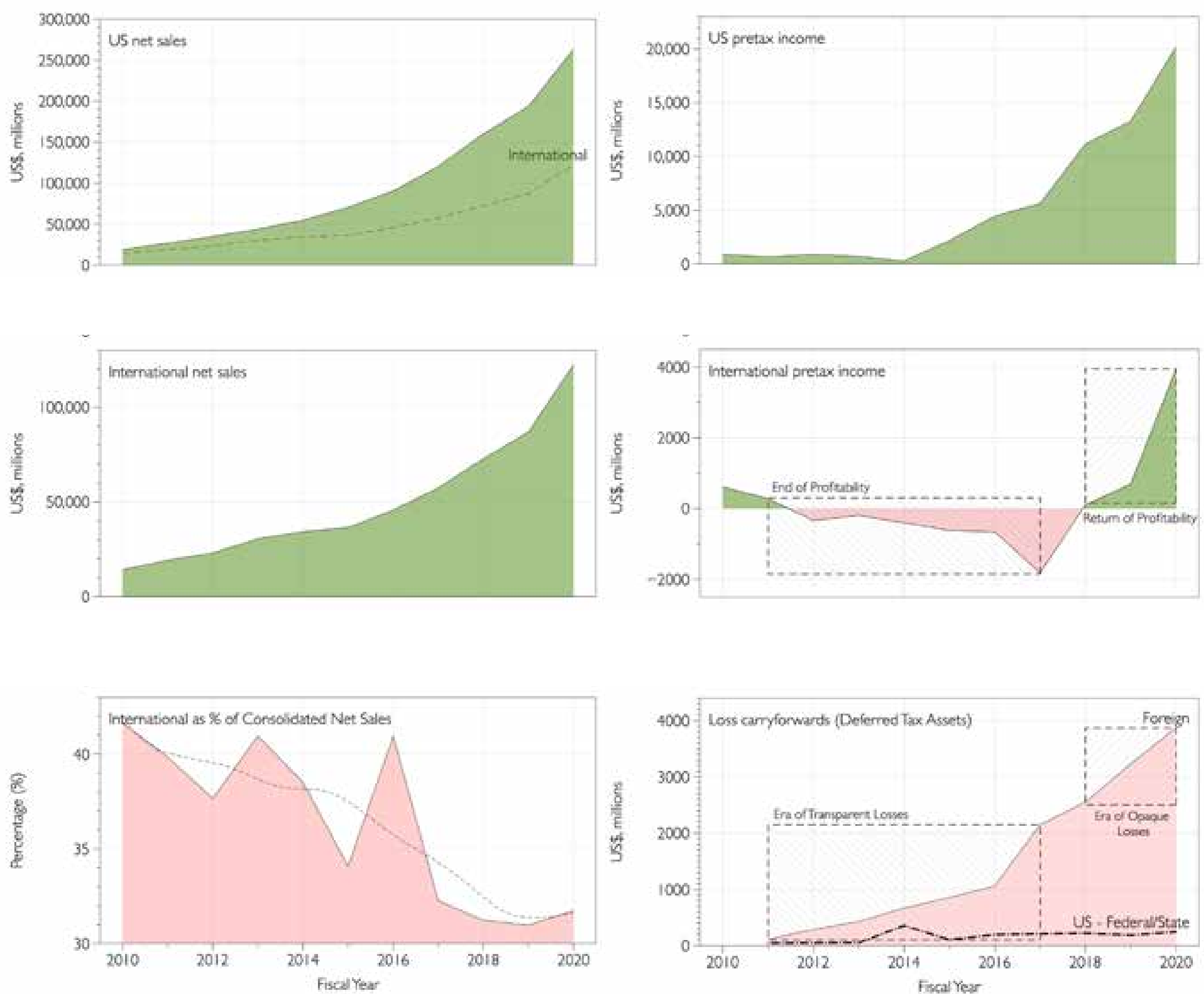
9 https://itep.org/amazon-inc-paid-zero-in-federal-taxes-in-2017-gets-789-million-windfall-from-new-tax-law

03

PROFIT, LOSSES AND TAX CREDITS

The baseline analysis of Amazon's tax affairs begins with data from their most recent 10-K filing (fig. 3) which reveals several important trends (fig. 4 and 5).

Figure 3 – Amazon's US and International net sales, pre-tax income and Loss carryforwards, 2010-2020



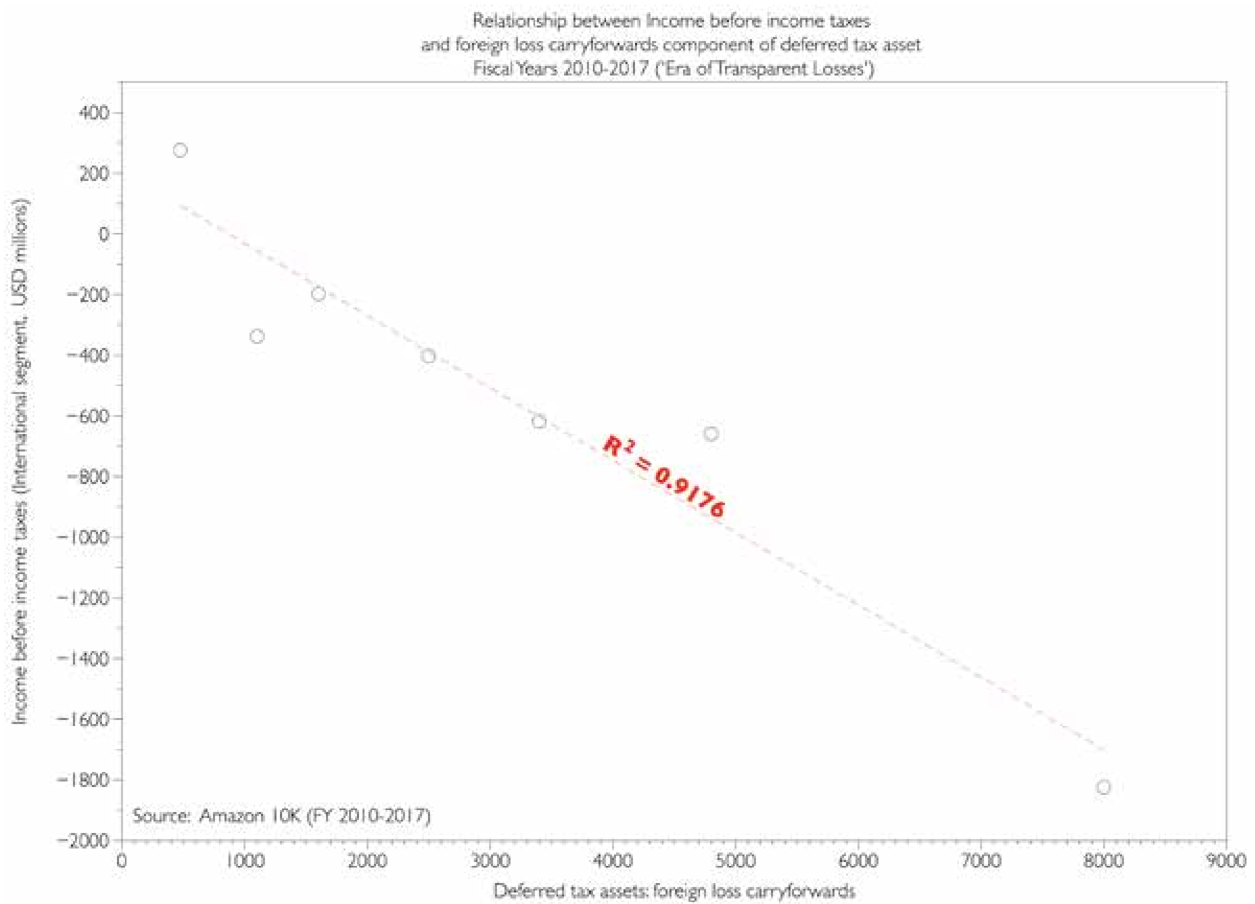
Source: Amazon 10-K various years

During this period from 2010-2020, Amazon's international sales (by geography, not by segment) as a portion of Amazon's consolidated net sales ranged declined from a period high of 42 percent to a low of roughly 31 percent in 2019. However, as mentioned above, the category of domestic (US) sales is likely to contain sales from AWS. What is clear is that in the period from 2010 to 2020, pre-tax income rose quickly and consistently while the international segment began to diverge significantly from FY 2011 onwards. In that year, international pre-tax income entered a period of losses, which would persist for most of the period examined, until FY 2018.

During this early period (FY 2011-2017), the majority of foreign losses turned into deferred tax assets. The movement of both values were strongly correlated (see figure 4). We refer to this era as the 'era of transparent losses'. However, it should be recognised that in theory, any qualifying loss from any subsidiary could be converted into a deferral in this manner, and the presence of losses manifest as deferred tax assets need not be related at all to the aggregate value of all profit and losses posted by international subsidiaries. It just happens to be so during this period. Losses can be equally hidden from view in consolidated accounts, and that is precisely what appears to have taken place from FY2018 onwards, when, in spite of an overall return to profitability internationally, there were nonetheless large increases in foreign losses converted into tax assets that is otherwise invisible from looking at pre-tax income alone. This is precisely why a consideration of subsidiary level accounts is critical to understanding where these losses are coming from and why they persist with such regularity over time. We refer to this era as the 'era of opaque losses.'

Distinguishing between the FY 2011-2017 (era of transparent losses) and 2018 onwards (era of opaque losses) is a useful way to navigate both changes in Amazon's reporting style as well as coordinating with external events (like the EVC case). Amazon's 10-K reports suggest that the group has accumulated net foreign operation losses, which were used for income tax purposes (tax deferrals are only one form loss carryforwards take) above what can be accounted from subsidiary data. The manner by which deferrals were accumulated is clearer from subsidiary filings from the era of transparent losses.

Figure 4 – The 'Transparent Period' Accounting for Lost Carryforwards, 2010-2017



Source: Amazon 10-K various years

Table 3 – The components of the provision for income taxes, net are as follows (in millions)

Row	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	accumulated
1	311	103	562	144	-	-	-	-	-	-	-	US and state current
2	-	-	-	-	214	215	1136	-137	-129	162	1835	US federal, current
3	-	-	-	-	65	237	208	211	322	276	626	US state, current
4	311	103	562	144	279	452	1344	74	193	438	2461	US current
5	37	52	131	173	204	417	327	724	563	1140	956	International, current
6	348	155	693	317	483	869	1671	798	756	1578	3417	total current
7	1	157	-156	-133	-	-	-	-	-	-	-	US and state, deferred
8	-	-	-	-	-125	473	116	-202	565	914	-151	US federal, deferred
9	-	-	-	-	-11	-171	-31	-26	5	8	-190	US state, deferred
10	1	157	-156	-133	-136	302	85	-228	570	922	-341	US, deferred
11	3	-21	-109	-23	-180	-221	-331	199	-129	-126	-213	International, deferred
12	4	136	-265	-156	-316	81	-246	-29	441	796	-554	total deferred
13	352	291	428	161	167	950	1425	769	1197	2374	2863	10,977 provision, net

Source: Amazon 10-K various years

Table 4 – Cash taxes paid, net of refunds (in millions)

Row	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Accumulated	
1	75	33	112	169	177	273	412	957	1184	881	1713	5,986	Cash taxes paid, (net of refunds)

Source: Amazon 10-K various years

The figure for cash tax is likely to include the €250 million fine from the EC (~US $300 million) but as the fine is contested, the payment is in escrow and may ultimately be cash outgoing. Similarly, it should be noted that in recent years, Amazon has recognize significant "settlements with tax authorities", such as the undisclosed sum in 2018 after France sought a €200 million settlement.[10] Similarly, Amazon reportedly paid €100 million to settle a tax dispute in 2017 with the Italian government.[11] Officially, tax settlements by 2020 reached U$1.45 billion, a value approximately 25 percent the value of income taxes paid for the whole of the 2010-2020 period. In other words, without these challenges from tax authorities, the gap between income tax provisions and taxes paid is likely to have been closer to 40% of reported net tax provisions on average for the period.

Table 5 – Deferred income tax assets are as follows (in millions)

Row	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	
1	43	47	53	357	107	198	211	222	188	245	Loss carryforwards U.S. - Federal/States
2	113	289	427	669	856	1062	2149	2551	3232	3876	Loss carryforwards - Foreign
3	412	482	590	780	854	968	901	1064	1373	2457	Accrued liabilities, reserves, and other expenses
4	178	281	396	534	727	1073	1026	1293	1585	2033	Stock-based compensation
5	41	129	249	156	189	330	349	321	-	-	Deferred revenue
6	64	129	164	154	148	66	-	-	-	-	Assets held for investment
7	-	-	-	117	222	179	35	69	2385	1886	Depreciation and amortization
8	-	-	-	-	-	-	279	2386	6648	10183	Operating lease liabilities
9	98	133	177	125	268	171	167	94	728	559	Other items
10	7	12	107	116	41	39	381	734	772	207	Tax credits
11	956	1502	2163	3008	3412	4086	5498	8734	16911	21446	Total Gross Deferred Assets
12	-227	-415	-698	-901	-1069	-1012	-2538	-4950	-5754	-5803	Less valuation allowances
13	729	1087	1465	2107	2343	3074	2960	3784	11157	15643	Deferred Tax Assets, net
14	-95	86	227	271	62	454	-157	-544	-1321	-866	Net Deferred Tax assets (liabilities), net of valuation allowances

Source: Amazon 10-K various years

10 https://www.ft.com/content/8237140e-0a67-11e8-8eb7-42f857ea9f09
11 https://www.reuters.com/article/us-amazon-italy-tax-idUSKBN1E91KM

Table 6 – Net Operating Loss Carryforwards for Income Tax Purposes vs Cash, Cash Equivalent and Marketable Securities held by foreign subsidiaries (in millions)

Row	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	
1		474	1100	1600	2500	3400	4800	8000	7800	8600	13400	Foreign
2		384	89	275	1900	1100	76	226	627			Federal
3		585	606	880	1100	2000	1000	858	919			State
4	1600	3600	4300	4600	4600	5800	8600	9600	12000	13400	17200	Cash held by foreign subsidiaries as cash, cash equivalent and marketable securities

Source: Amazon 10-K various years

Table 6 shows that net total operating loss carryforwards reached US$ 13.4 billion by 2020. In addition, table 6 shows US$ 17.2 billion of unrepatriated profits in the form of cash, cash equivalent, and marketable securities being accumulated by 2020. Both of these figures are far higher than the cash payment paid (table 7). Indeed, they are higher than the total taxes payable by the group not just for the period in question, but for the entirety of the group's history to date (US$11.71 billion). The data suggest the accumulation of foreign profits and the accumulation of operating losses are not caused by random, idiosyncratic events, but occur in a stable, linear and highly predictable manner. Both are correlated (fig 5) and, significantly, equally correlated to the growth of net sales for the group as a whole.

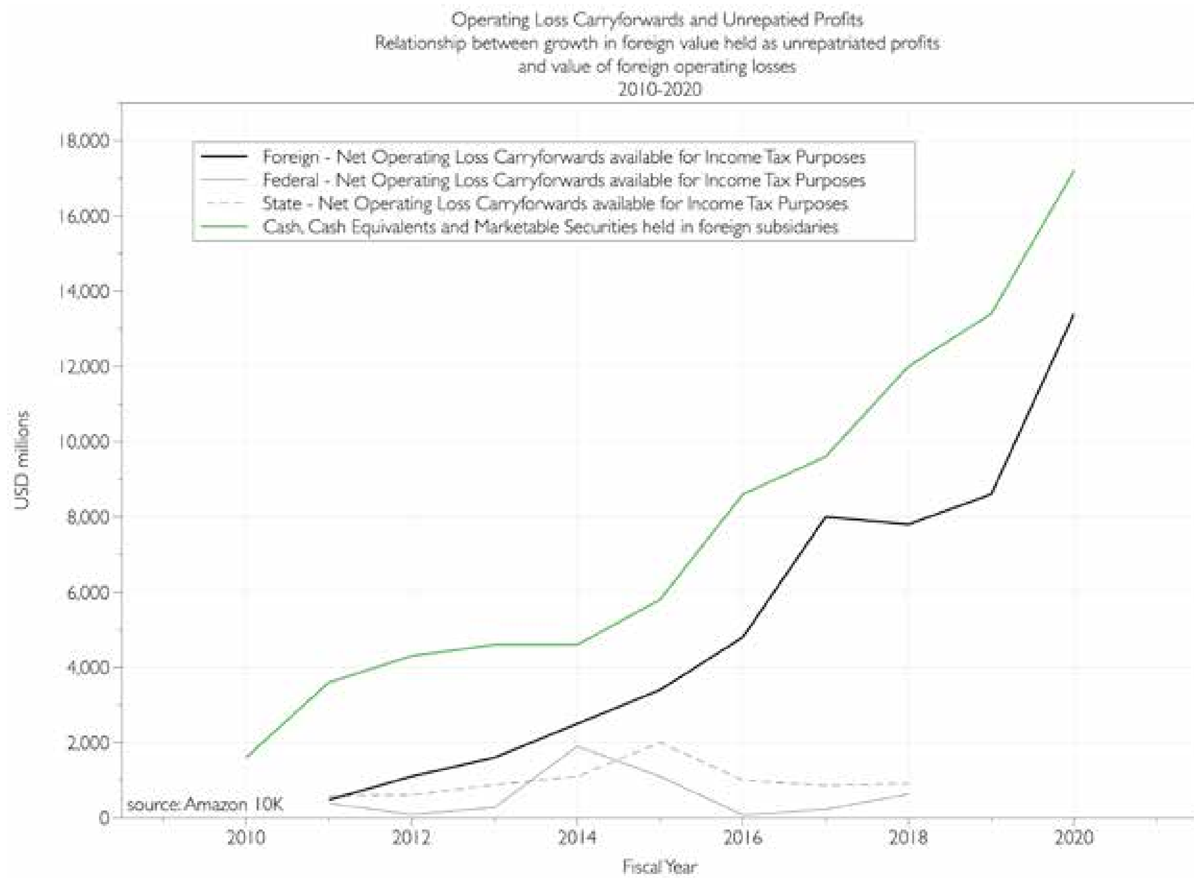
Amazon's public filings provide no credible explanation for why these losses emerged from FY 2011 onwards, why the international segment differs so dramatically from the domestic retail segment, nor why they can produce losses as well as untaxed profits with such regularity se Annex A). Accordingly, to gain deeper insights into this phenomenon, we must resort to the public accounts of Amazon's foreign subsidiaries.

Table 7 – Cash taxes paid, net of refunds (in millions)

Row	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	
1	75	33	112	169	177	273	412	957	1184	881	1713	Cash taxes paid, (net of refunds)

Source: Amazon 10-K various years

Figure 5 – Close Correlations between Loss Carryforwards and Unrepatriated Profits



Source: Amazon 10-K various years

04

USING ORBIS TO UNDERSTAND THE INTERNATIONAL DYNAMICS OF AMAZON'S TAX AFFAIRS

The divergence in performance between Amazon's domestic and international retail segments which have generated a high growth of net operating loss carryforwards (table 6 above), begs the question of how such losses were built up. While the predictability of loss-making may suggest some level of managed artificiality, to get a better handle on this requires a more direct and systematic review of its foreign reporting behaviours over time.

Using the Orbis database to compare against Amazon's 10-K gives greater clarity regarding these developments over time. Amazon distinguishes between two sets of categories of sales on its 10-K reports. One category, 'international sales mix' is represented on figure 5 below by a solid black line, and a category of 'net sales from international markets' represented with a red line in the same figure. Included in this category are key markets for Amazon, including Germany, UK, Japan, Canada and Mexico, as Amazon defines, "Net sales generated from internationally-focused online stores". Data for Canada and Mexico are otherwise classified in North American markets and difficult to identify. This renders the comparison of international sales and net sales more difficult.

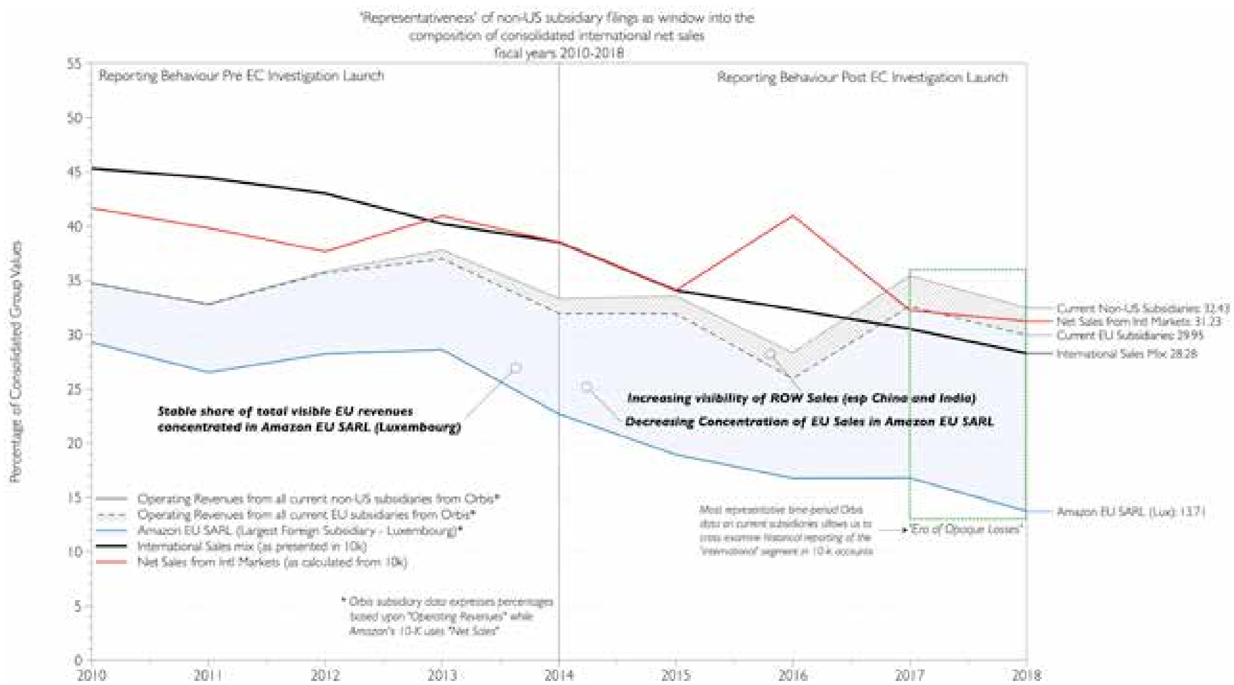
Table 8 provides a country-by-country breakdown of how the international sales mix and net sales from international markets were calculated.

Table 8 – Net sales attributed to countries that represent a significant portion of consolidated net sales are as follows (in millions)

Row	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	
1	18,707	26,705	34,813	43,959	54,717	70,537	90,349	120,486	160,146	193,636	263,520	United States
2	5,296	7,230	8,732	10,535	11,919	11,816	14,148	16,951	19,881	22,232	29,565	Germany
3	3,929	5,348	6,478	7,291	8,341	9,033	9,547	11,372	14,524	17,527	26,483	United Kingdom
4	5,025	6,576	7,800	7,639	7,912	8,264	10,797	11,907	13,829	16,002	20,461	Japan
5	-	-	-	5,028	6,099	7,356	11,146	17,150	24,507	31,125	46,035	Rest of world
6	34,204	48,077	61,093	74,452	88,988	107,006	135,987	177,866	232,887	280,522	386,064	Consolidated

Source: Amazon 10-K various years

Figure 6 – Consolidation of Amazon's Non-US Subsidiary filings



Source: Amazon 10-K various years & Orbis

The distinction of 'international' net sales employed in Amazon's 10-K filing is difficult to parse. While there were periods where international sales (as tabulated from the geographical breakdown of sales) equated the sales generated by the 'international' retail segment, there are also periods where it differs. For instance, during the period of 2010-2012, the international sales mix figure stood above 'net sales' from international markets and it is possible to calculate independently (Figure 6). This is to be expected, as Amazon was not reporting figures for the rest of the world then. Yet over time, with the growth in AWS in recent years, the extent to which AWS income has been recognized in the US has contributed to the divergence in defining how much income is international.

In so far as data from foreign subsidiaries mixes the two segments, it is best to compare Orbis estimates against the derived total sales from the international market (the black line in figure 6). The Orbis data suggests that the EU retail segment has long made up the majority of Amazon's foreign income. Furthermore, Orbis data reflects the general decline in group income originating in foreign markets. For instance, the portion of operating revenues of currently active EU incorporated subsidiaries declined from roughly 35 percent of group revenues in 2010 to about 30 percent in 2018 (black dashed lines). Indeed, the single largest EU subsidiary, Amazon EU SARL (referred to as LuxOpCo in the EC investigation) in particular has seen a proportionate decline in operating revenues it reports from FY2015 onwards. In part, these developments point to an widening distribution of where operating revenues are being reported in Europe, as well as the growing importance of territories outside the EU that have steadily 'filled in the gap' left by the declining share of income reported in Europe.

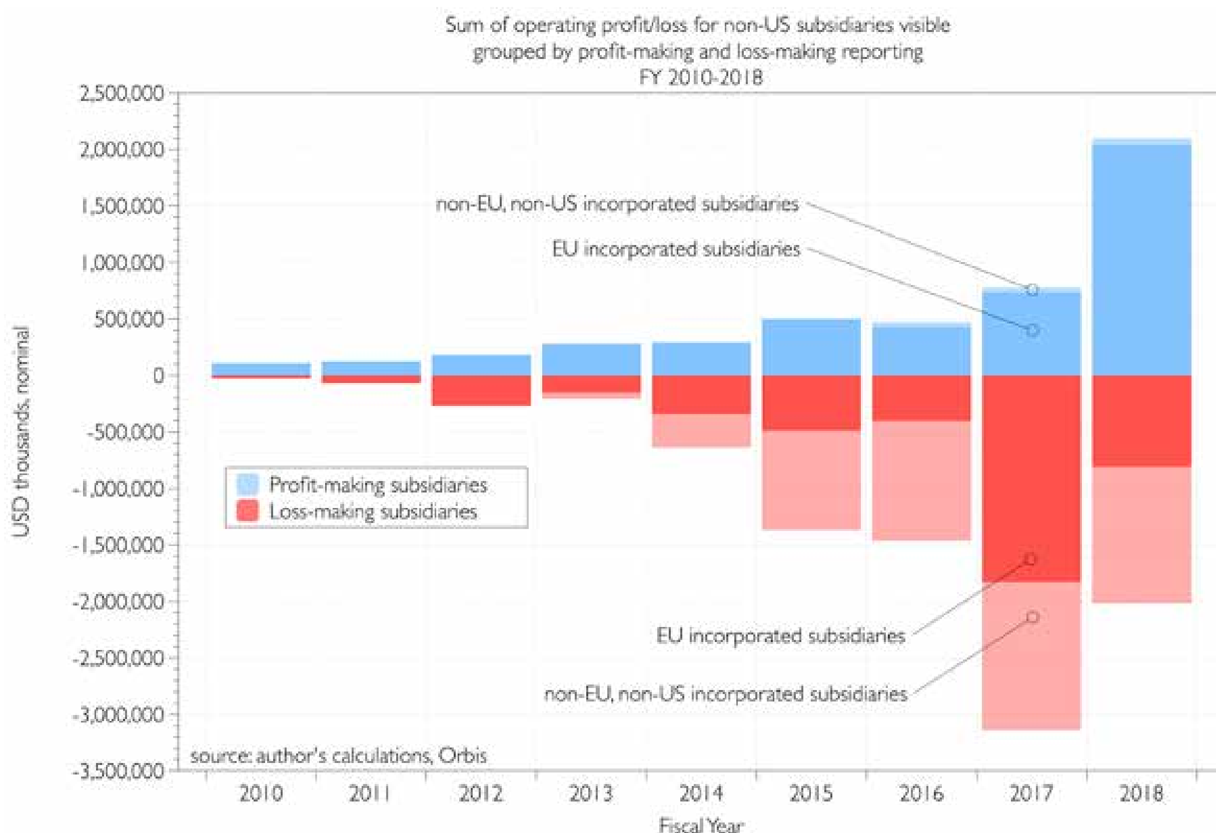
Yet the values visible from Orbis also are beginning to actually exceed the values in the consolidated reports, even though we know there is some degree of incompleteness and unidentifiable Amazon subsidiaries (such as those from Japan). While these can be artefacts of intra-group transfers (which we cannot gain insight to), the behaviour of data suggests it offers a good level of representativeness in explaining historical trends, with its greatest representativeness being in the most recent comparable fiscal years.

05

DISAGGREGATION OF AMAZON'S INTERNATIONAL OPERATING PROFIT AND LOSS

Disaggregating the accounts further allows us to better understand what is being reported in Amazon's official reports. The groups' international business has consistently declared operating losses and, until recently, those losses outstripped operating income in the aggregate. Using the Orbis database allows us to shed additional light on where and when this is happening. Figure 6 shows the operating profit/loss categories based on subsidiary data from the Orbis database.

Figure 7 – Operating profit/loss for Non-US Subsidiaries, 2010-18



Source: Orbis Database

According to this data, and consistent with early acknowledgements in the annual reports, the generation of operating profits is almost the exclusive preserve of European subsidiaries. Similarly consistent with 10-K accounts is the 'oversupply' of operating losses that, in the aggregate, confirms a recurring state of net operations losses being generated internationally. Finally, and also consistent with early depictions in the 10-K, operating losses are most common in foreign subsidiaries outside of Europe. This sheds further light on the fact that while the ROW losses are significant in value and highly skewed in terms of the likelihood of occurrence, there are nonetheless significant losses involving European subsidiaries as well (in value terms, this is largely accounted for by Amazon's subsidiaries in Luxembourg). In 2017, Amazon reported uncharacteristically high losses in Europe, primarily in two of their largest Luxembourg entities. The following year's records, in turn, show EU losses, occurring in part because of the impact of tax settlements being made and charged against one of Amazon's Italian subsidiaries, for instance.

Orbis data is, therefore, highly consistent with the behaviour described earlier regarding the "era of transparent losses"—namely the fact that the majority of the total net operating losses posted by the international segment appear to have been converted into loss carryforwards used to defer income tax payments. Similarly, one can observe that the sum total of operating losses accountable from foreign subsidiaries is closely correlated with, as well as comparable in value to, the value of deferred tax assets generated by loss carryovers (figure 8 and figure 9 respectively). This not only reinforces the representativeness of subsidiary level data to explain consolidated accounts but also helps explain why losses can occur alongside the accumulation of profits.

In another instance, figure 6 differentiates the subsidiaries producing operating losses, from the subsidiaries producing operating profits. In the consolidated accounts, the losses outstrip the operating profits in the international segment. The fact that only the subset of the visible losses we see at the subsidiary level are sufficient to explain the majority of the overall net operating losses reported in the 10-K filings, as indeed, the subsequent conversion into deferred tax assets means that much of what we can see as the EU subsidiaries generating operating profits in figure 7 may simply not have been converted into taxable income, but instead, preserved as an untaxed, unrepatriated profit held in 'foreign subsidiaries'.

Figure 8 – Losses among non-US subsidiaries and Foreign Losses Carryforwards

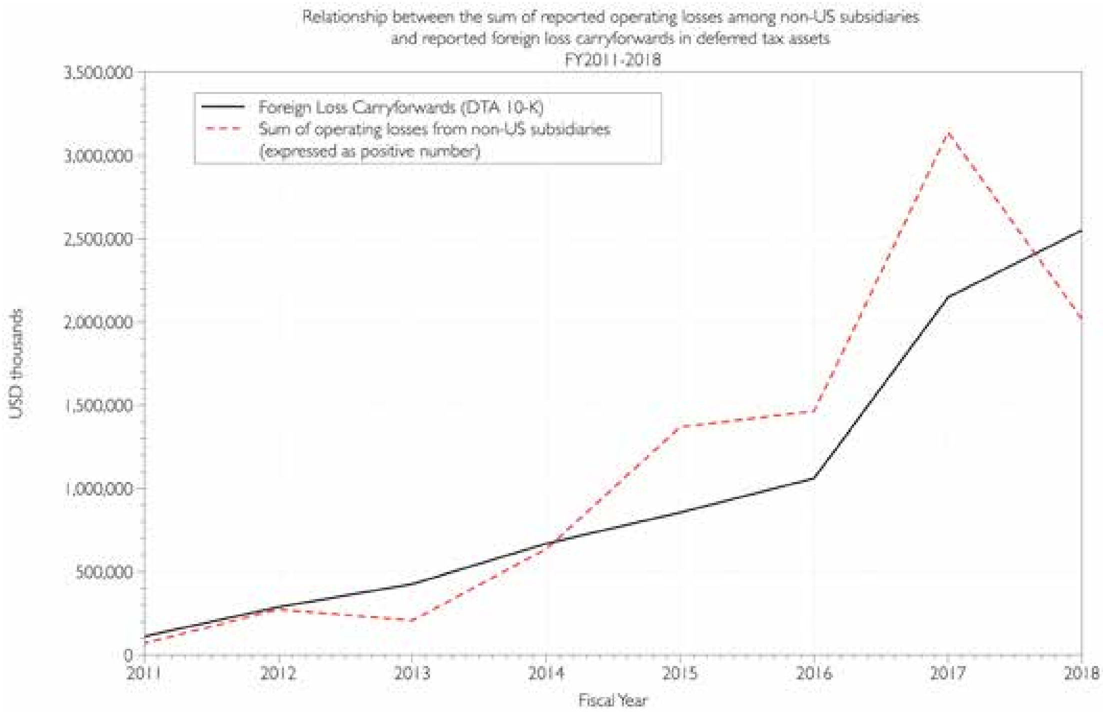
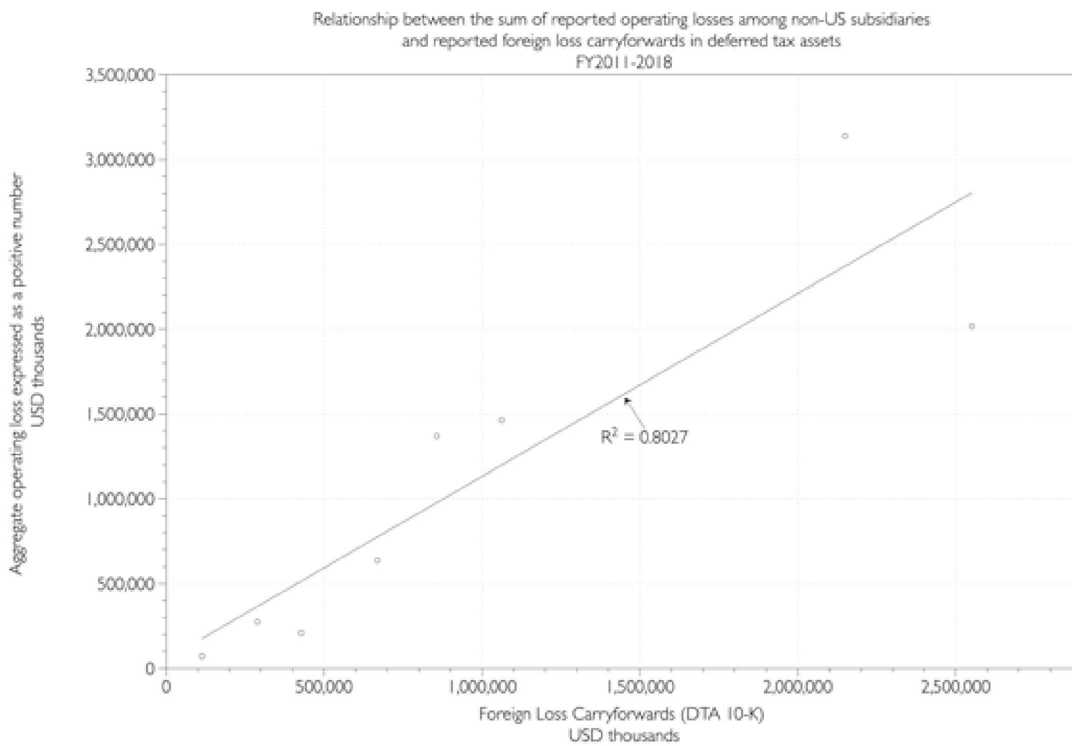


Figure 9 – Linear relation over time between these two sets of numbers



Source: Amazon 10-K various years

06

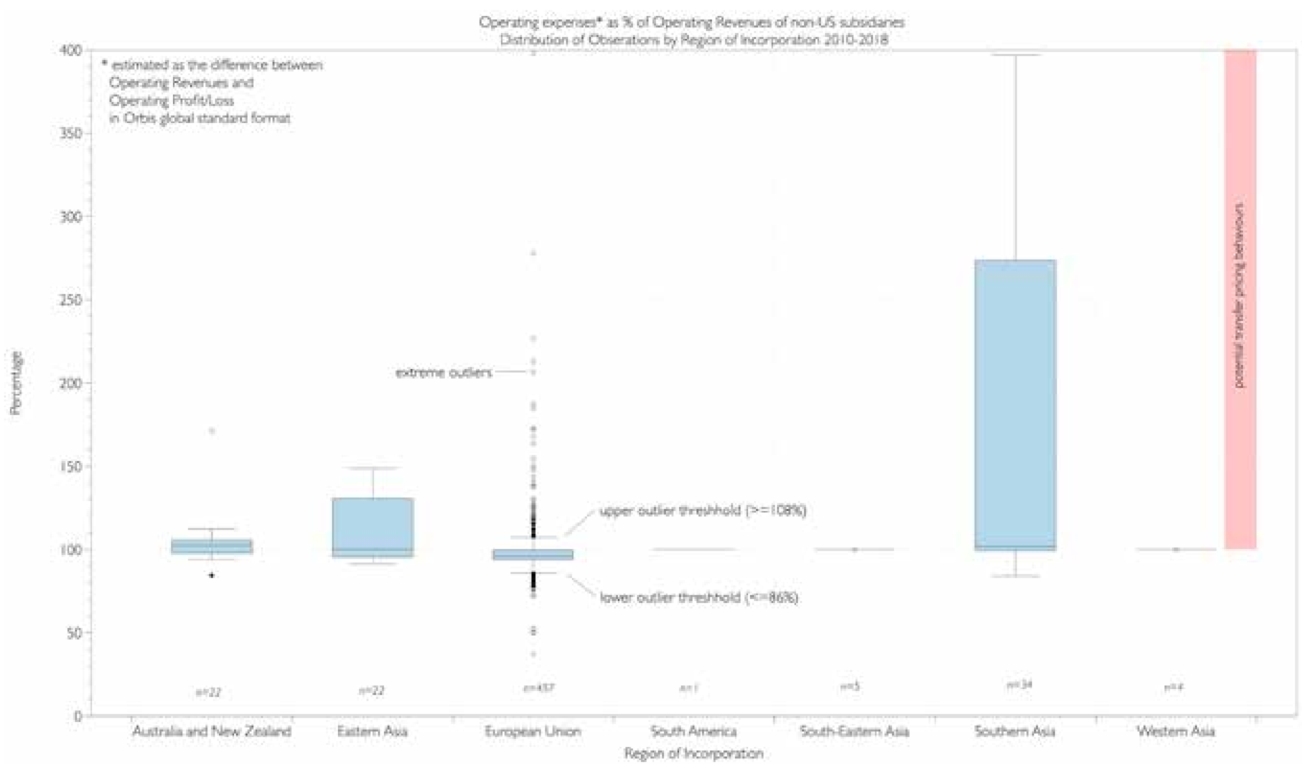
UNUSUAL BEHAVIOUR AMONG INDIAN SUBSIDIARIES

Subsidiary level data also allows us to better understand how losses are being produced with such regularity. As figure 9 shows, outside of the EU, the majority of observable subsidiaries registered in the Orbis database are running operating losses (because operating expenses are above 100 percent of operating revenues). Yearly reports from Australia and New Zealand subsidiaries, for instance, have a median observation of operating expenses at 102.6 percent of revenues. For Eastern Asia (i.e. China), while median level of operating expenses is 100 percent of revenues, the extent of the losses produced also exhibits a larger range (with operating expenses up to 150 percent of revenues observed). Excessive loss-making seems to occur in Southern Asia (i.e. India) where median levels of 101.95 percent are overshadowed by a high number of incidents with reports well over 200 percent and indeed more extreme ends of the distribution reaching nearly 400 percent.

While loss-making appears to be 'built in' to the expensing structure exhibited for ROW subsidiaries, some losses have accrued in Europe as well. The difference is that in Europe, the production of operating losses (as well as some operating profits) is less of a 'normal' event, but, statistically speaking, an extreme event—an 'outlier' (identified by the spread of white and black dots in figure 10). Perhaps surprisingly, these 'outlier reports' tend to originate from specific places—they concentrate in various subsidiaries long at the centre of Amazon's European activities, headquarted in Luxembourg and subject to earlier EC investigations (see figure 10). Figure 11 shows that cases where the level of operating losses are more extreme are all concentrated in subsidiaries with less than U$1 billion in operating revenue. In other words, what these subsidiaries lack in operating revenues, they make up for in operating expenses and the volume of cases observed. This is how ROW losses, in the aggregate, have come to outstrip EU losses over time.

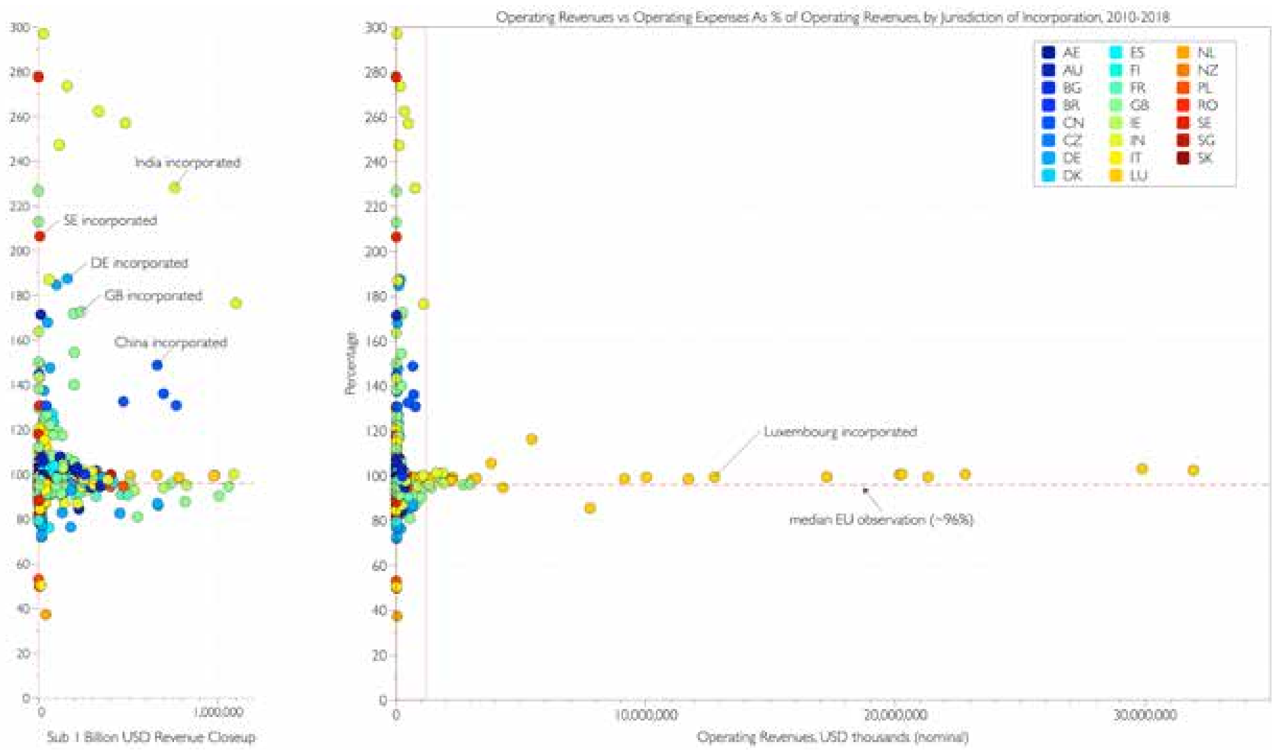
Subsidiary data also reveals that loss-making has been a permanent attribute among Amazon's Indian subsidiaries for its observable history. In some of Amazon's Indian subsidiaries for instance, loss-making has been a permanent attribute in their accounts for the entirety of the history observable. For instance, one of the single largest cases of consistent loss-making occurs in an Indian entity. The subsidiary in question is named Amazon Seller Services Private Limited. The reason this single subsidiary, like many others of a similar size, has consistently report losses is because its operating expenses are over twice as high as its revenues. This entity has been loss-making for the whole period of observable information (2012-2018) and started posting consistently high levels of losses between after FY2014-2017 (operating expenses were relatively pegged at about 250 percent of turnover for this 4 year period). Over its visible history (visible in Orbis data), operating expenses were, on average, 220 percent greater than operating revenue, resulting in 3.46 billion USD in operating loss. The magnitude of these losses alone dwarfs all recorded settlements with tax authorities reported in Amazon's K-10 2020. By FY2018, this single entity had accumulated operating losses comparable to 44 percent of the accumulated net foreign operating loss carryovers reported that year.

Figure 10 – Operating losses outside of North America



Source: Orbis Database

Figure 11 – Loss Making Subsidiaries, International



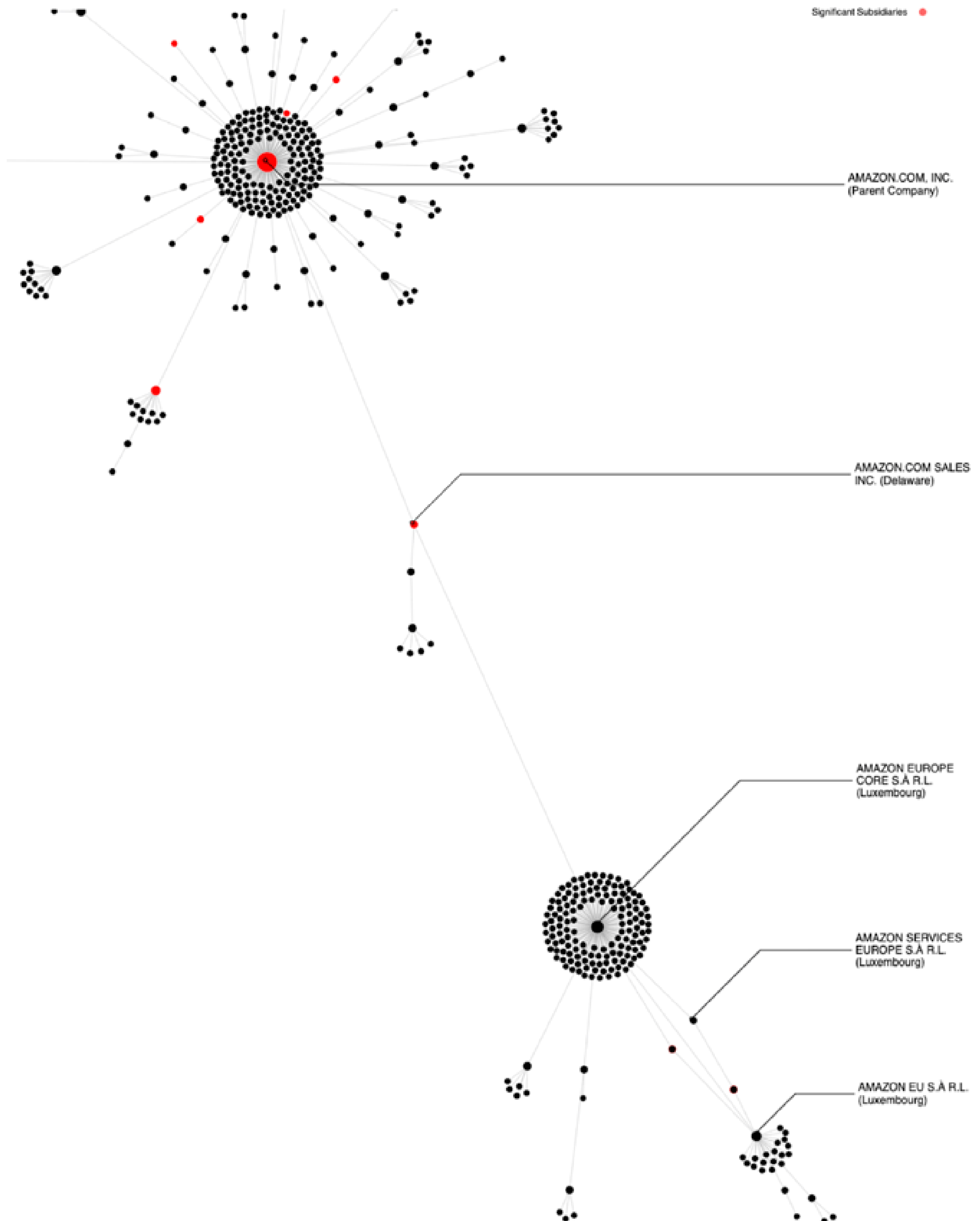
Source: Orbis Database

07

LUXEMBOURG AND AMAZON’S TAX PLANNING

The available evidence suggests that Luxembourg subsidiaries are used as vehicles for accumulating losses internationally and recording those losses in a way that generates tax credits in the US. The puzzle is the source of those losses recorded by Amazon’s Luxembourg entities; losses that, as we saw above, take place both outside, but also inside of the EU. While losses in India are occurring in a different branch of the group (yet one with a Luxembourg entity nonetheless in a conduit intermediation position), the losses occurring in the EU occur in the branch which shows two basic clusters of activity owned by Amazon.com Sales incorporated (Delaware) (figure 12.) One is in a small, seemingly insignificant little branch where notable Chinese losses are occurring, but with the main European holdings and the Luxembourg subsidiaries acting as a gateway.

Figure 12 – EM of Amazon's holding through Luxembourg gateway



Source: Orbis Database

The Luxembourg branch illustrated on this EM controls approximately 69% of all international subsidiaries for which we can account (fig. 12). The three most critical Luxembourg entities highlighted are Amazon Europe Core Sarl (the successor to the "Lux SCS" shell company targeted by the EC investigation), Amazon Services Europe Sarl, and Amazon EU Sarl (referred to as LuxOpCo in the EC investigation). These are the largest entities visible according to revenues. Two of them ("Core" and "EU" SARL) are where the largest loss-making events occur in Europe. In our estimation, all three also account the unrepatriated profits of the Amazon global store.

Private subsidiary accounts are very different from those of a highly regulated and highly scrutinised public corporation. The accounting categories available are dramatically reduced, and at a higher level of aggregation. Nonetheless, one balance sheet category in particular, what Orbis classifies as 'other current assets' in their globally standardised reporting, is remarkably close to the figures cited in Amazon's 10-K regarding the accumulation of cash, cash-equivalent and marketable securities (itself a form of "current asset"). The growth in official values is highly correlated to the growth in comparable values reported by these subsidiaries, and indeed, in the most recent year available for comparison, FY 2018, the values are essentially identical as they were at several other earlier periods (figure 13). This suggests that Luxembourg continues to play a dominant, dual role as the global manager for the group's untaxed profits, and as an originator or transferor of losses from unknown foreign jurisdictions into tax credits and deferrals usable within the US tax system.

As we discuss in the penultimate section below, this cluster of activities and the role of Luxembourg and its arbitrage opportunities have historically meant that the group could locate profits in an untaxable form—such as a liquid asset subject to US taxation given CFC rules, yet not actually taxed because the value is not formally 'repatriated' (meaning it is turned into a taxable income on Amazon's consolidate profit and loss account). Amazon itself explicitly states that it does not intend to repatriate these funds, and instead intends to re-invest them into its international activities, in perpetuity. We cannot prove this through Orbis data alone, yet there is not only a continuity over time in the behaviour of the numbers we track, the location of where they occur, and a clear track record of making the structure of its Luxembourg subsidiaries allow it to access US CFC rules. This historical evidence was established by the EC investigation in 2014.

Figure 13 – Luxembourg at the centre of a system of globally coordinated losses that simultaneously generates unrepatriated profits

08

EC CASE AGAINST AMAZON AND LUXEMBOURG

The EC investigation into transfer pricing violations as constituting illegal state aid, ultimately focussed on two of Amazon's subsidiaries, "LuxOpCO" or Amazon EU Sarl and Amazon Europe Technologies Holding SCS or "Lux SCS" (see figure 14).

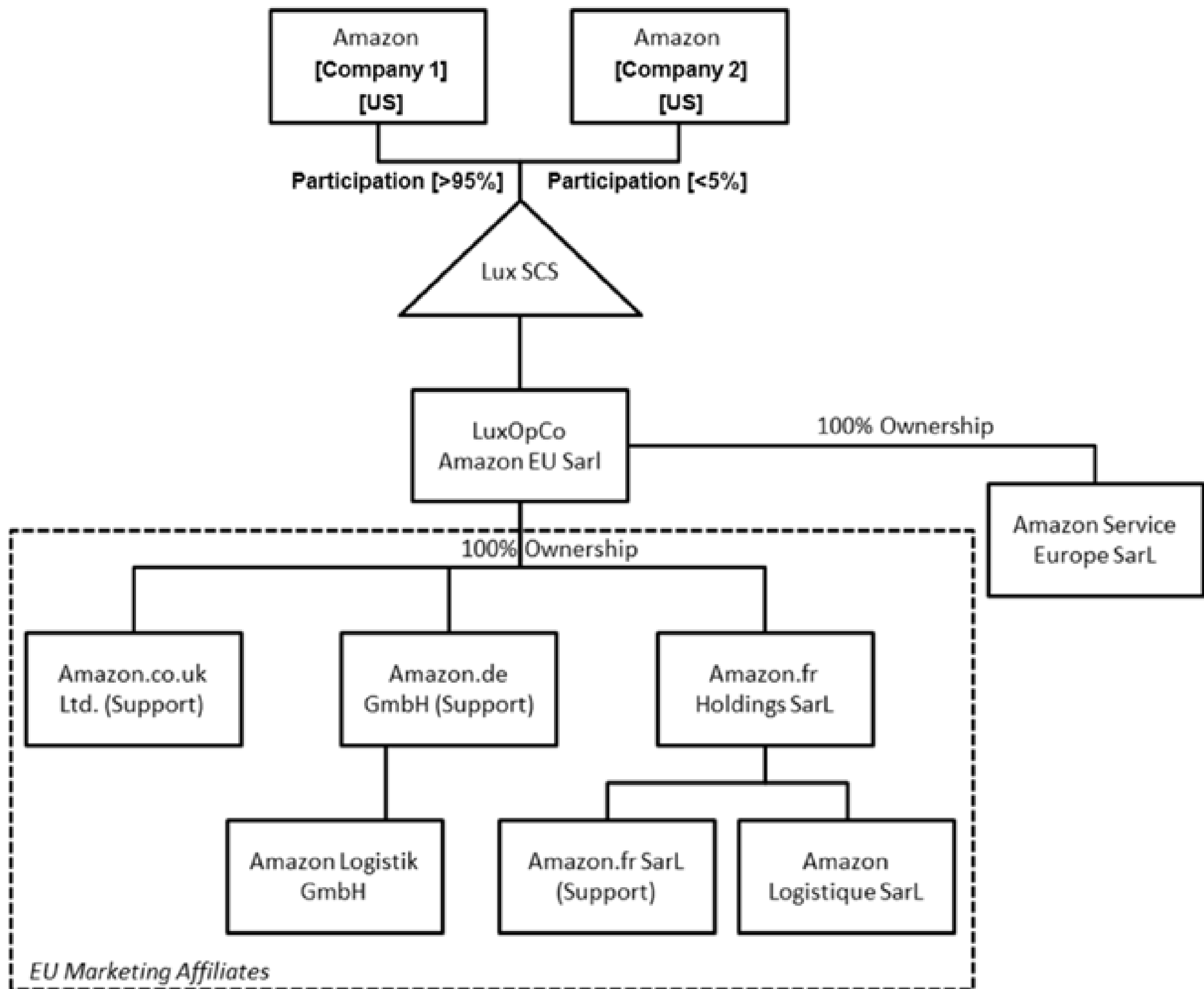
One of the key findings unearthed by the investigation (discussed further below) was what Amazon's European operations were grouped together as a single consolidated tax group (a 'vertical' fiscal unity as it was over the period concerned by the EC inquiry). The extraction of profits from that group occurred through transfer pricing based upon intangible intellectual property 'owned' by Lux SCS. Yet because Lux SCS was itself not a "corporate entity" for tax purposes, it was, instead set up as a partnership (see figure 15). This arrangement allowed the jurisdictional status of the partners themselves to be used to define where the profits from this activity were subject to tax (in this case, the US). Part of the magic behind this arrangement was the fact that, as a partnership, its members were not considered as subsidiaries producing revenues, profits and losses factored into the consolidated accounts described in Amazon's revenue segments and tax breakdowns. Rather, they were treated as an equity investment in unconsolidated subsidiaries. In so far as these equity investments, and any gains from it, were not repatriated, it would thus also remain untaxed.

Yet the EC was more concerned with how some of the profits reached Lux SCS in the first place. Focusing on mechanisms already being reported about publicly in various "Lux Leaks", the EC investigation not only relied upon Amazon to reveal information about itself that could be used by investigators (which took years for this Q&A exchange to complete), but the case became very narrow in its focus on the relationship between the two Amazon entities. Such narrow focus may have deflected attention from the role played by these entities in the wider context discussed above. In addition, the case focused on 'profit shifting' in a company that does not actually focus on producing profits. Consequently, the investigation seems to have missed the core strategy of widespread 'production' of losses that could be turned into useful assets for mitigating income taxes, a technique that ultimately proved more valuable to Amazon's cash flow strategy. In the end, the EC case concluded with a €250 million fine for a decade's worth of conduct the investigation looked into.

Looking back at the case, early in into the investigation, Amazon had already initiated a major restructuring that was outside of the remit of the EC's investment. Comparing the structure as it was depicted then (and visible in the historical shareholding records collected as part of the production of EMs), with current Orbis data, we observed that the structure at the centre of EC investigations, Lux SCS was removed, and the current Amazon Europe Core SARL was instituted in its place. Amazon EU Sarl, still the single largest foreign entity with the single largest share of visible economic activity in its financial reporting, continues to play the same role today. In the years that followed the investigation, this entity was 'hollowed out', both in terms of the subsidiaries it held (once larger than it is today), but equally in the proportion of revenues it directly manages.

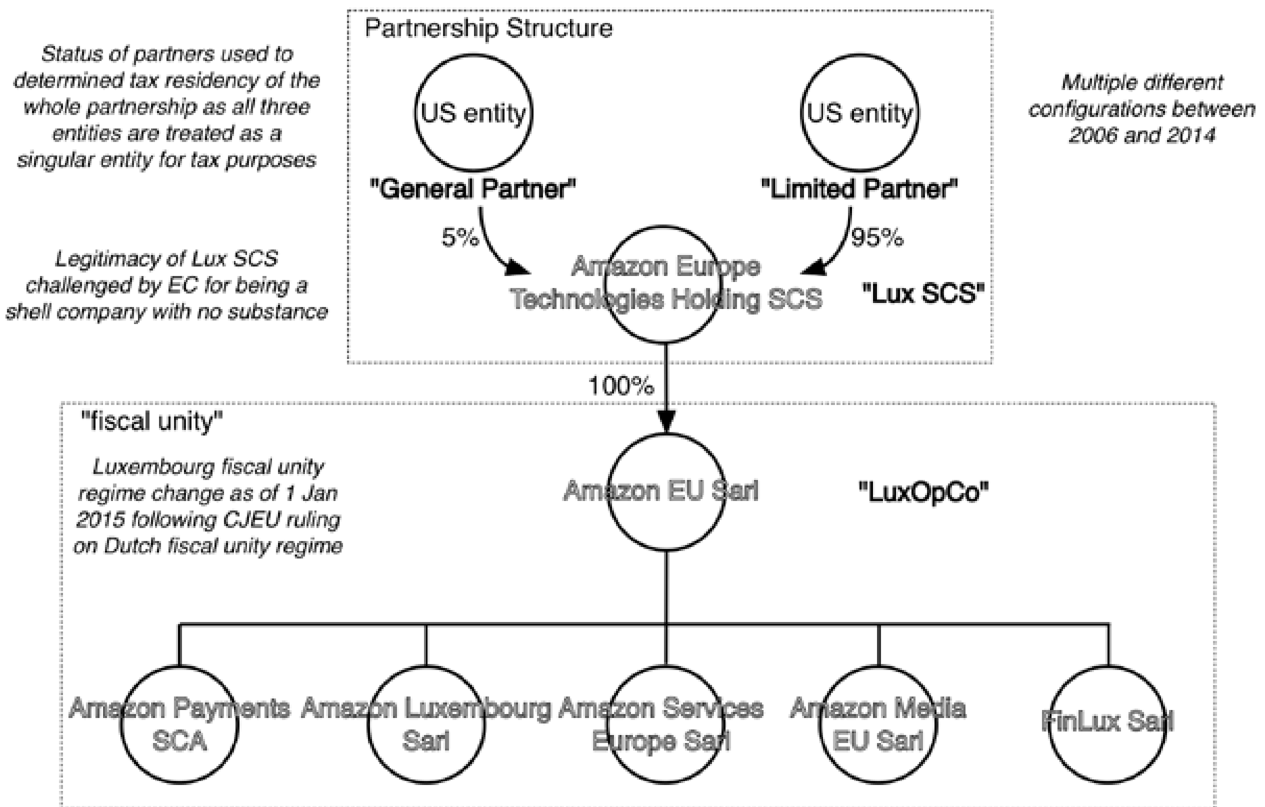
To our knowledge, no one has explained the changes that took place since the EC investigation. Accordingly, we have tried our best to provide an educated guess based upon available evidence as to the reasons for some of the changes started in 2015. We distinguish between the 'old model' at the centre of the EC investigatory period, and the new model as it has evolved.

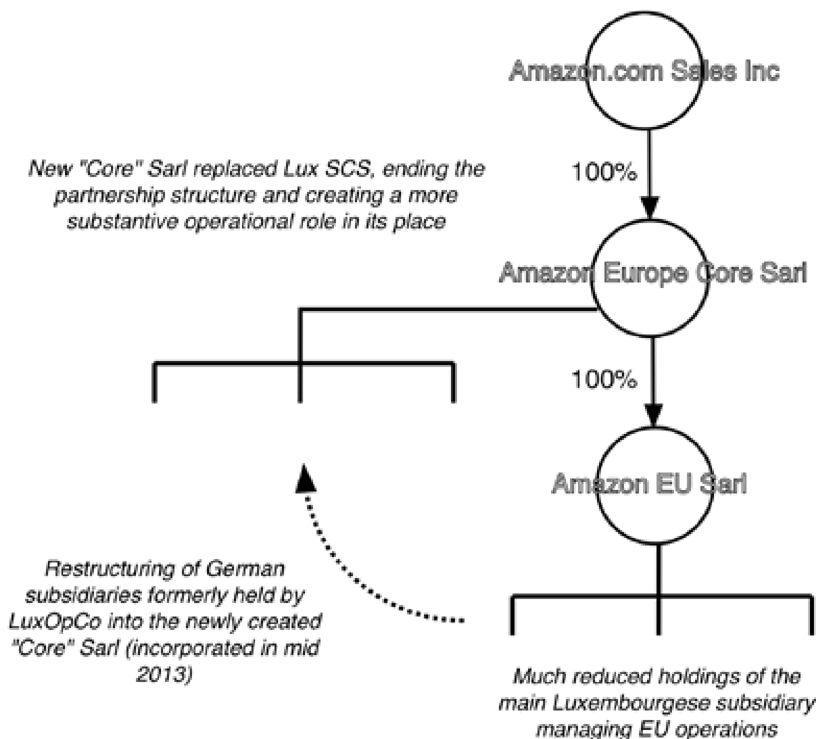
Figure 14 – Amazon's Luxembourgish structure as presented in the EC case



Source: https://ec.europa.eu/competition/state_aid/cases/254685/254685_1614265_70_2.pdf, p 10.

Figure 15 – EM analysis of Amazon's Luxembourgish arrangement pre and post EC case





AMAZON'S OLD MODEL

In the old model, Amazon's investment through its key Luxembourgish entities adopted a split ownership pattern known as general partner and limited partner. Both the general partner and limited partner are Amazon's U.S. subsidiaries, but one, the general partner controls only 5% of Amazon Europe Holding Technologies SCS. In such arrangement, the general partner tends to be the entity that active controls activities of its subsidiary, in this case, Amazon Europe Technologies Holding SCS. The limited partner, which owns 95%, is construed as a passive investor in Amazon Europe Technologies Holdings SCS. The passive partner is likely to have been a CFC of the US entity, and through electivity, its profits could be deferred indefinitely until such a time as profits are repatriated. As this Luxembourgish set of entities accounted for ~75% of all Amazon's international sales, this arrangement was key to Amazon's international strategy.

During that time, Luxembourg allowed the different Luxembourgish entities to be treated in a consolidated manner. At that time rules of 'fiscal unity regime', which would change in 2015, allowed consolidation for directly held entities ("vertical fiscal unity"). This rule may explain why the two key Luxembourgish entities are tightly grouped together in the double structure. In this grouping, the top held Luxembourg subsidiary, Amazon Europe Technologies Holding SCS (described in the EC case as Lux SCS') is the final repository of profits, whereas the entity it controls, Amazon Eu Sarl (described in the EC case as LuxOpCo') is the controller of the rest of Amazon's subsidiaries benefitting from fiscal unity which allows consolidation of profits and losses of the rest as one single entity.

For several years, Amazon repatriated profits to the U.S., and the figure of repatriation appears to be the one that has contributed to the €250 million fine imposed by the EC.

AMAZON'S NEW MODEL

The Court of Justice of the European Union (CJEU) ruling in 2015 changed Amazon's old calculations. The CJEU ruling on EU rights of establishment created the option of what might be called "horizontal fiscal unity", so that all entities in a chain or entities themselves could be consolidated so long as they were located in Luxembourg or the EU, including many new German subsidiaries created by Amazon. The CJEU ruling effectively created new opportunities for creative consolidation of accounts. The switch from a vertical to a horizontal fiscal unity created an either/or situation which probably nullified the old model, requiring, we believe, those changes observed after 2015.

Either way, in our estimation those changes have not affected Amazon's core strategy of employing its Luxembourgish entities to consolidate both losses that accrue in the U.S as tax deferrals and as repositories of Amazon's international unrepatriated profits. The persistence of loss-making but also in the likely residence of the group's untaxed profits, suggests that there may also be continuity in the ability of have these entities subject to US CFC rules. *Speculation aside, only an investigation by government regulatory body, or by the EC, can get to the bottom of the structure employed by Amazon in Luxembourg and explain rising international losses in the context of rising unrepatriated cash or near cash holdings in these Luxembourg subsidiaries.*

09

AMAZON WEB SERVICES. WHERE DOES IT FIT IN?

Amazon Web Services is a cluster of entities registered in the state of Delaware. Its sales (primarily renting of the group's computation infrastructure as a service to third parties) accounts for nearly1/8 of Amazon's revenues and nearly 2/3 of Amazon's overall profits according to its 2019 10-K filing. It does not appear to have tax residency outside of the US and while its sales are subject to sales tax abroad, it does not appear to pay corporate tax abroad.

AWS has also benefitted from changing to new lease accounting standards published by the Financial Accounting Standards Board (FASB), which public companies were required to adopt in 2019, known as ASC 840. Following the Enron collapse, the accounting standards were shifted to track and disclose all leased assets. It appears likely that under the new accounting guidelines, Amazon's operating leases may include its fulfilment centres, logistical businesses that support Amazon, etc. This is significant for AWS given its ability to write off capital investments in both hardware and software facilitating AWS business. This change in accounting may result in a greater impact on Amazon's business structure and tax burden than previously understood. To put this into perspective, in 2004, Amazon had a depreciation cost equivalent to slightly over 1% of its total revenue. However, from 2011 depreciation began to grow, reaching 5.5% by 2020. It does appear that this may have accelerated under the Tax Cuts and Jobs Act, which in addition to lowering the corporate tax rate from 35% to 21%, increased the bonus depreciation.[12] Depreciation rules allow Amazon to retain between 1-5% of their total revenues as tax-free profit, which they can only get in the US. This underscores the importance of keeping income and assets in the US going forward. Ultimately, the tax consequences of doing so appear to be mitigated by the extreme divergence between how the international dimensions are split between those that generate losses that qualify for tax benefits, and those that generate profits, which qualify for being held as untaxed, unrepatriated profits that can be used to repeat the groups cash flow managements needs in a sustained and predictable manner.

12 https://www.irs.gov/newsroom/tax-law-offers-100-percent-first-year-bonus-depreciation

10

CONCLUSIONS

Effective tax rates (ETRs) are a common metric used to compare and rank public corporations on the amount of taxes they pay. In Amazon's case, ETRs have been used to argue that Amazon effectively pays no federal income tax. Amazon painstaking details a multitude of reasons why ETRs are a problematic metric. Over the last decade, however, Amazon has generated greater untaxed profits than the total amount of taxes it has ever owed. Much of this has taken the form of "loss carryforwards"—an accounting technique where qualifying net operating losses are used to reduce future tax liabilities and much of those were generated from its international operations. Taken at face value, Amazon's international business has steadily declined over the past decade from a high of 48 percent of group net sales in 2009 to 27 percent in 2020. Yet, Amazon's reporting of its international affairs is perplexing and raise doubts about its tax affairs.

In disconnected ways, existing studies have identified two strategic aspects of Amazon's fiscal and financial strategy. The first is Amazon's overriding financial focus is on revenue growth and cash flow.[13] Amazon relies on its cash liquidity, rather than profitability, to pay for maintenance and expansion. The group has sustainably generated operating cash flows at roughly 10 percent of its revenues.[14] In our view, cash-flow management is far more central to Amazon's tax planning strategy than is normally assumed. Indeed, focusing on Amazon's management of its cash flow, this report highlights select parts of Amazon's financial reporting that have generally been ignored by other analysts.

Second, Amazon has made extensive use of US allowances for accelerated depreciation to write-down the value of its fixed assets (such as all the hardware and computing infrastructure that goes into its highest growth segment, Amazon Web Services) thus reducing profitable income subject to taxation. The accumulation of tax deferrals, the single largest of which has typically been the losses generated in foreign markets, has been used to dramatically limit the level of income taxes reportedly paid out from its cash flow.

Existing studies have also neglected a third and crucial dimension of Amazon's strategy, its loss-making international operations. Amazon's international businesses have been largely ignored because its 10-K reporting in this area is minimal, to the point of being incomprehensible. Consequently, this study has had to make use of a different source of public information, the filings produced by hundreds of Amazon's foreign subsidiaries as part of their statutory requirements. This report cross-examines Amazon's international activities over the last decade—fiscal years 2010-2020—against subsidiary level records of "currently" identifiable subsidiaries (as of circa mid-2020) available in the Orbis database from Bureau Van Dijk. This approach has developed out of an ongoing CORPLINK study funded by the European Research Council looking into innovative comparative forensic approach we call 'equity mapping (EM).[15]

13 Fox, J., 2014. "At Amazon, It's All About Cash Flow." Harvard Business Review, [online] pp.2-5. Available at: https://hbr.org/2014/10/at-amazon-its-all-about-cash-flow [Accessed 1 April 2021].
14 Dunbar, N. 2018. 'Watching over Amazon's cash flow machine' EuroFinance [online]. Available at: https://www.eurofinance.com/news/watching-over-amazons-cash-flow-machine/ [accessed 1 April 2021]
15 CORPLINK has been funded by the ERC Advanced Study grant no. 694943. See https://cordis .europa.eu/project/id/694943

Ambiguous reporting terminology and changing data categories or missing data, prevent us from reaching a categorical conclusion. Our analysis of Amazon's reported earnings and tax statements over time reveal not just a changing strategy but suggest deliberate obfuscation. Based on the available data and information, we can conclude that Amazon's claims about international losses merit further investigation, as it appears to be artificially created. This report provides considerable evidence to question a superficial acceptance of Amazon's numbers. Moreover, and more importantly, treating Amazon International (which is most likely European) separately from the US market and AWS appears to reduce Amazon's ETR.

This report presents reasonable interpretation of the data available but further analysis of Amazon's reports would necessitate additional discussion following this report. Key to such approach would be a global approach focusing on the role of Amazon International's subsidiaries in Luxembourg and not just Luxembourg's role vis-à-vis other European entities. This would require formal investigation by the EC. This is important not only to understand Amazon's taxes, but also because Amazon is unlikely to be alone in pursuing tax credit arbitrage. The authors of this report found evidence that other large American firms may be pursuing a similar strategy and possibly with the encouragement of US government policy.

ANNEX A: AMAZON'S STATEMENT ON THE CONCEPT OF ETR

"Our effective tax rates could be affected by numerous factors, such as changes in our business operations, acquisitions, investments, entry into new businesses and geographies, intercompany transactions, the relative amount of our foreign earnings, including earnings being lower than anticipated in jurisdictions where we have lower statutory rates and higher than anticipated in jurisdictions where we have higher statutory rates, losses incurred in jurisdictions for which we are not able to realize related tax benefits, the applicability of special tax regimes, changes in foreign currency exchange rates, changes in our stock price, changes to our forecasts of income and loss and the mix of jurisdictions to which they relate, changes in our deferred tax assets and liabilities and their valuation, changes in the laws, regulations, administrative practices, principles, and interpretations related to tax, including changes to the global tax framework, competition, and other laws and accounting rules in various jurisdictions. In addition, a number of countries have enacted or are actively pursuing changes to their tax laws applicable to corporate multinationals."

Explaining losses in their international segments

"Our international activities are significant to our revenues and profits, and we plan to further expand internationally. In certain international market segments, we have relatively little operating experience and may not benefit from any first-to-market advantages or otherwise succeed. It is costly to establish, develop, maintain international operations and stores, and promote our brand internationally. Our international operations may not become profitable on a sustained basis.

Source: K-10, 2020

ANNEX B: AMAZON'S ETR ACCORDING TO ITEP STUDY

	U.S. Pre-tax Income, $ Billions (excluding state)	Current Federal Income Tax, $ Billions	Effective Federal Income Tax Rate	Statutory tax rate
2020	$20.2	$1.8	9.4%	21%
2019	$13.3	$0.162	1.2%	21%
2018	$11.2/			
$10.8	$-0.129/ $-0.13	-1.2%	21%	
2017	$5.4	-$0.14	-2.5%	35%
2016	$4.5	$0.45	10%	35%
2015	$2	$0.12	5.9%	35%
2014	$0.2	$0.21	91.7%	35%
2013	$0.7	$0.03	5.1%	35%
2012	$0.9	$0.13	15.1%	35%
2011	$0.6	$0.03	4.7%	35%
2010	$0.9	$0.05	5.9%	35%
2009	$0.5	$0.04	8.1%	35%

· Source: Institute on Taxation and Economic Policy (ITEP) analysis of 10-K annual financial reports and SEC filings (https://itep.org/amazon-in-its-prime-doubles-profits-pays-0-in-federal-income-taxes/; https://itep.org/amazon-has-record-breaking-profits-in-2020-avoids-2-3-billion-in-federal-income-taxes/)

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