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Ending Corporate Inversions: Past Failures, Continued Controversy, and Proposals for Reform

Shane Zahrt

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# ENDING CORPORATE INVERSIONS:
PAST FAILURES, CONTINUED CONTROVERSY, 
AND PROPOSALS FOR REFORM

Shane Zahrt†

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I. INTRODUCTION

In 1949, Earl Bakken and his brother-in-law founded the company Medtronic in a garage in northeast Minneapolis.\(^1\) From those humble beginnings, Medtronic grew to become the largest medical technology company in the world.\(^2\) The company remained based in Minneapolis until mid-2014 when Medtronic announced plans to acquire a competitor, Covidien, and become an Ireland-based corporation.\(^3\) To be clear, the company would not be run from Ireland—its CEO and corporate headquarters would stay put in Minnesota.\(^4\) Instead, Medtronic would simply be changing its place of incorporation to an overseas address to avoid certain features of the U.S. tax system through a process known as "inversion."\(^5\)

An inversion is typically defined as “a transaction in which a U.S. corporation’s stock or assets are transferred to a foreign corporation to reduce tax and regulatory costs.”\(^6\) As with Medtronic, however, while inverting corporations might change their address on paper, “the actual headquarters of inverted firms typically remain in the United States.”\(^7\) One estimate by researchers at the non-partisan Joint Commission on Taxation predicted that the U.S. Treasury stands to lose up to $20 billion in tax revenues over the next decade if Congress does not act soon to prevent

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4. Id.
5. Id.
inversions. Moreover, the practice is exceedingly unpopular with the American public.

This is not the first time that a rash of corporate inversions has drawn the ire of policymakers and the American public. As recently as 2004, Congress made major changes to the tax code designed to discourage inversions. This Article seeks to summarize previous efforts at major reform and address what caused those efforts to fail. It begins with a brief summary of the history and origins of corporate inversions, followed by an explanation of the unique features of the U.S. tax code that make inversions attractive to corporations. Then, this Article examines current proposals to curb inversions and looks to other possible responses to the issue. This Article concludes that in order for regulatory or legislative efforts to prevent inversions from succeeding, they must be accompanied by broader corporate tax reform.

II. BACKGROUND

A. Corporate Inversions: Definition and Origins

Policymakers generally do not seek to inhibit the ability of domestic corporations to merge with foreign entities. But,” as Treasury Secretary Jack Lew put it, “these activities should be based on economic efficiency, not tax savings.” One such example is the acquisition of beer-maker Anheuser-Busch by the Belgian

8. Joseph Walker, The Fuzzy Math of Calculating Lost Tax Dollars, WALL ST. J., July 15, 2014, at A2, available at LEXIS. It should be noted, however, that an accurate cost estimate is extremely difficult due to the multitude of variables that must be taken into account. See id.


11. See infra Part II.C.

12. See infra Part II.A.

13. See infra Part II.B.

14. See infra Part IV.

15. See infra Part VI.

16. Jacob J. Lew, Close the Tax Loophole on Inversions, WASH. POST (July 27, 2014), http://www.washingtonpost.com/opinions/jacob-lew-close-the-tax-loophole-on-inversions/2014/07/27/2ea50966-141d-11e4-98ee-da9a85133bc9_story.html. Lew points out that recent inversions have not only been motivated by tax savings, but also “expressly justified by” tax considerations. Id.
corporation Inbev. Although Anheuser-Busch is no longer based in the United States, this is not the type of transaction lawmakers seek to prevent because “the company is Belgian, not just as a tax matter but in terms of the physical location of its corporate headquarters in Leuven.” Instead, the types of inversions that most concern policymakers are those in which a U.S. corporation moves its place of incorporation to a low-tax or no-tax jurisdiction where it otherwise has relatively little activity or presence. Congress largely succeeded in eliminating this type of inversion, often dubbed a “naked inversion,” by way of 2004 legislation. However, the 2004 law left open significant loopholes that make possible the inversions seen today.

Currently, “[c]orporate inversions occur through three different paths: the substantial activity test, merger with a larger foreign firm, and merger with a smaller foreign firm.” In a “substantial business activity” inversion, a U.S. parent corporation that does substantial overseas business creates a foreign subsidiary in the overseas jurisdiction. The U.S. corporation and foreign subsidiary then engage in a stock exchange, after which “the new entity is a foreign corporation with a U.S. subsidiary.” The majority of today’s inversions, however, typically take place by way of a merger with a smaller foreign corporation.

In general, “merger” simply refers to the practice of two corporations combining into a single entity. Following a merger,
“only one of the two companies will survive. But the survivor will have succeeded by operation of law to all of the assets, liabilities, rights, and obligations of the two constituent corporations.”27 In a merger that results in an inversion, the “effective control of the new company stay[s] with the shareholders of the U.S. corporation[,]” 28 despite the fact that the corporation is now headquartered overseas. 29

How widespread is the issue? In a 2014 report to Congress, the Congressional Research Service estimated that forty-seven companies have undertaken inversions in the past decade, 30 with over two-dozen companies making the move overseas since 2008. 31 Inversions have recently come under increased scrutiny, with opponents of the practice—including President Obama—arguing that inversions amount to “gaming the system.” 32 The Treasury Department asserts the following: “There is no policy reason to permit a domestic entity to engage in an inversion transaction when its owners retain a controlling interest in the resulting entity, only minimal operational changes are expected, and there is significant potential for substantial erosions of the U.S. tax base.” 33

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own name and identity and acquires the assets and liabilities of the former.” BLACK’S LAW DICTIONARY 1138 (10th ed. 2014).

27. BAINBRIDGE, supra note 26, at 51.

28. CRS REPORT 2, supra note 20, at 4.

29. As an illustration, the Congressional Research Service points to the details of a recent merger between a U.S. corporation and an Irish competitor. Id. at 4–5. Upon completion of the merger, shareholders of the U.S. company were expected to “control 73% of the combined company, with the shareholders of the Irish company controlling the remaining 27%. The press release notes expected tax benefits from the merger at $165 million in 2016, out of $535 million of total cost savings.” Id. at 5.


32. Kevin McCoy, Obama Steps Up Criticism of Tax Inversions, USA TODAY (July 24, 2014, 7:18 PM), http://www.usatoday.com/story/money/business/2014/07/24/obama-tax-inversions-criticism/13120369/. To illustrate his point, President Obama likened the practice of corporate inversions to “simply changing your mailing address to avoid paying taxes.” Id.

The practice has also proven unpopular with the American people. One public policy poll found that around fifty-nine percent of registered voters nationwide believe that Congress should act to “penalize and discourage companies” from engaging in inversions. 34 Inversions are even less popular with registered voters in Medtronic’s home state of Minnesota. A September 2014 poll found that sixty-eight percent of Minnesota voters disfavored inversions. 35

B. Why Do United States Corporations Invert?

1. The United States Has the Highest Corporate Tax Rate in the Developed World

Corporations that choose to engage in inversions point to a number of reasons for doing so. These often include “increased operational flexibility, better cash management, and access to international capital markets.” 36 In general, U.S.-based multinational corporations seek to reincorporate abroad in order to recognize the significant tax savings that accompany avoiding certain features the U.S. tax code. 37

In the time since the U.S. tax code received its last major makeover in 1986, many other countries have lowered their tax
rates. According to Treasury Secretary Jack Lew, this has left "the United States with the highest corporate tax rate in the developed world." There is bipartisan agreement that the tax code is in need of reform. Both President Obama and Republicans in the House of Representatives proposed reductions in the corporate tax rate during the 2013–2014 session of Congress. Despite some common ground, however, there is "disagreement over why the corporate tax system needs to be reformed, and what specific policy measures should be included in a reform." Many observers of the current political environment rightly predicted that broad reform to the corporate tax structure was unlikely to proceed due to partisan gridlock. Even after Congress reached a previously unachievable permanent solution for setting Medicare reimbursement rates, observers were pessimistic about the prospects for other reforms.

As a result of the United States' high statutory corporate tax rate, low-tax or no-tax jurisdictions like Bermuda and the Cayman

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38. Lew, supra note 16.
39. Id.
40. See Michael J. Graetz, The Bipartisan 'Inversion' Evasion, WALL ST. J., Sept. 25, 2014, at A13, available at LEXIS ("President Obama, Mr. Lew and just about everyone in Congress agree that the laws governing corporate taxation need rewriting.").
42. See COMM. ON WAYS AND MEANS, CHAIRMAN DAVE CAMP, TAX REFORM ACT OF 2014 DISCUSSION DRAFT SECTION-BY-SECTION SUMMARY 49 (2014).
45. Mike DeBonis, Congress Congratulates Itself for the 'Doc Fix' Deal, but Can It Happen Again?, WASH. POST, (Mar. 31, 2015), http://www.washingtonpost.com/politics/congress-congratulating-itself-for-the-doc-fix-deal-but-can-it-happen-again/2015/03/31/cf69c1c-d75f-11e4-8103-6a84725d9f9d_story.html ("Republicans and Democrats happen to agree that the yearly "doc fix" charade is a problem in need of fixing. Issues like government spending and corporate taxation tend not to generate similar accord.")
Islands were among the most popular destinations for corporate inversions prior to the American Jobs Creation Act of 2004. In recent years, corporations have more frequently sought out new homes in the United Kingdom or Europe. Ireland, with a 12.5% corporate tax rate—more than twenty percent lower than the U.S. statutory rate—has been a particularly popular destination. A 2014 report issued by Ireland’s Department of Finance estimated the country’s effective tax rate—the tax rate actually paid by corporations in its jurisdiction—at 10.9% over the decade spanning 2002-12, and 8.4% in the year 2012.

Thus, the relatively heavy burden of the U.S. corporate tax rate is a major reason that companies choose to invert. While an attractive solution to this burden might be to simply lower tax rates, Treasury Secretary Jack Lew has argued that more is required. In a 2014 editorial, Lew wrote, “[E]ven if we cut our tax rates . . . we would still need to enact anti-inversion provisions because companies always would find countries with near-zero rates to which they could relocate.”

2. Corporate Tax on Worldwide Earnings

Another feature of the tax code that makes inversions attractive to multinational corporations is the fact that the United States taxes corporate income on a worldwide basis. “Under the

46. See CRS REPORT 2, supra note 20, at 6.
48. Id. Of the eleven pending or completed inversions identified by Bloomberg News in late 2014, Ireland was the reincorporation destination for five. Id.
49. IRISH DEP’T OF FIN., EFFECTIVE RATES OF CORPORATION TAX IN IRELAND: TECHNICAL PAPER 18–19 (2014). Even outside the realm of inversions, Ireland has become a popular destination for corporations seeking to lower international tax bills. It was revealed through U.S. Senate hearings that U.S.-based firm Apple Computers took advantage of Ireland’s lax tax code to lower its effective tax rate “on international earnings to just under 2%.” John Walsh, Effective Corporate Tax Rate ‘Under 11%’, IRISH EXAMINER (Apr. 8, 2014), http://www.irishexaminer.com/business/effective-corporate-tax-rate-under-11-264661.html.
50. See Lew, supra note 16.
51. Id.
worldwide approach, all income of domestically-headquartered companies is subject to tax, including income earned abroad. 53 This makes the United States distinct from most other countries that "only tax the profits of domestic and foreign firms earned within their territories." 54 To avoid double-taxing corporations that have already paid taxes in the country in which those profits were earned, "the United States allows the domestic corporation to claim a foreign tax credit . . . ." 55 The more common approach internationally—taxing only profits earned within a nation’s borders—is referred to as the "territorial" approach. 56

The major exception to the U.S. practice of taxing worldwide income is the repatriation rule. 57 This rule is also frequently referred to as a "deferral." 58 The repatriation rule functions by "allow[ing] U.S. corporations to defer the payment of tax on foreign income earned by a separate foreign subsidiary corporation until the funds are repatriated, or remitted to the United States as dividends or other income." 59 Put another way, if a multinational corporation based in the United States never transfers foreign earnings back to the U.S. parent company, it will never pay U.S. taxes on those earnings. 60

The result of this policy is that a corporation’s cash often ends up "trapped" overseas. 61 That is, the corporation avoids investing that foreign income in the United States to avoid the high tax penalty that would accompany doing so. 62 For many of the largest multinational corporations in the United States, this amounts to tens of billions of dollars in overseas cash assets that cannot be used to reinvest within the United States without paying the country’s

53. Id.
54. Simpson, supra note 6, at 679; see also Dittmer, supra note 52, at 2.
56. Dittmer, supra note 52, at 2.
57. See Simpson, supra note 6, at 680.
59. Simpson, supra note 6, at 680.
60. See id.
61. See, e.g., Kate Linebaugh, Top U.S. Firms Are Cash-Rich Abroad, Cash-Poor at Home, WALL ST. J., Dec. 4, 2012, at B1, available at LEXIS.
62. Id.
thirty-five percent corporate tax rate. Presently, General Electric leads the way with an estimated $110 billion in cash assets “trapped” in foreign jurisdictions. At the time its inversion was announced, Minnesota-based Medtronic had just over $20 billion in cash assets overseas.

Thus, the incentive to invert arises from the fact that “[w]hen the parent corporation is moved out of the United States and into a low-tax or no-tax jurisdiction, U.S. tax rules cease to apply to the group as a whole.” From a policy standpoint, “[f]or good reason, almost no one likes or defends deferral as such.” In fact, both advocates of a move to territorial taxation as well as those who defend the worldwide system cite deferral as a justification of their position. “U.S. companies would no longer be tax deterred from repatriating their overseas earnings if the repatriations were tax free, either under dividend exemption or because the earnings had already been taxed here.”

C. History of Inversions and Attempts at Reform

1. Early Inversions

As defined by the U.S. Treasury Department in 2002, “[a]n inversion is a transaction through which the corporate structure of a U.S.-based multinational group is altered so that a new foreign corporation, typically located in a low-tax or no-tax country, replaces the existing U.S. parent corporation . . . .” While

64. Id. (“GE’s $110 billion leads U.S. companies, followed by Microsoft’s $76.4 billion, Pfizer’s $69 billion, Merck & Co.’s $57.1 billion and Apple’s $54.4 billion.”).
67. SHAVIRO, supra note 58, at 169.
68. Id.
69. Id.
inversions have taken different forms over the years, the origins of the maneuver are traced back to the early 1980s.\footnote{71}{See id. at 3 n.1; Kun, supra note 6, at 315–16 ("The 1983 McDermott transaction was the first major restructuring to attract significant attention from the IRS.").}

In 1983, a U.S. corporation called McDermott International exploited a loophole in "the Internal Revenue Code to remove non-taxed passive income from the United States' taxing jurisdiction."\footnote{72}{Kun, supra note 6, at 316.} Shortly after the McDermott transaction, Congress took action to prevent similar incidents. It amended the Internal Revenue Code to impose tax consequences on a domestic corporation that would offset the benefits of the corporation's decision to move overseas.\footnote{73}{Id.}

Initially, it seemed as if Congress had fixed the problem. But inversion activity only ceased until 1994 when the Helen of Troy Corporation, a Texas-based hair care appliance manufacturer, "proposed that its shareholders exchange their shares [in the United States based corporation] for shares of a new Bermuda corporation."\footnote{74}{Willard B. Taylor, Corporate Expatriations—Why Not?, 78 TAXES 146, 146 (2000).} The regulations in place at the time "did not require the recognition of gain on the exchange of stock of a U.S. corporation for stock of a foreign corporation by less than five percent shareholders."\footnote{75}{Id. at 147.} Put more succinctly, publicly held United States corporations could freely reincorporate overseas without causing their shareholders to suffer any adverse tax consequences.\footnote{76}{Id.}

In response to this transaction, the IRS announced new regulations that would require shareholders in companies that inverted after April 18, 1994, to recognize a gain on the transfer of those shares.\footnote{77}{Id. at 147.} "The IRS assumed that the 'toll-charge' imposed on shareholders would defer future [corporate] inversions."\footnote{78}{Id.} While these regulations had temporary success, by 1998 corporations were again seeking to expatriate with increasing frequency.\footnote{79}{Id. at 316.}

In response to the flurry of inversion activity from 1998 to 2002, Congress passed the American Jobs Creation Act of 2004—
one of the most drastic revisions of the U.S. tax code since 1986.\textsuperscript{80} The details of this legislation, and its shortcomings in light of the recent resurgence in inversions, will be discussed in a forthcoming section.\textsuperscript{81}

2. 1996 IRS Regulations

As stated above, following the Helen of Troy inversion in the early 1990s, the IRS aimed to discourage inversions by enacting new regulations.\textsuperscript{82} The new regulations imposed four tests that were required to be met before a foreign corporation could acquire shares of a U.S. corporation tax free:

(a) In the transaction, U.S. shareholders of the U.S. corporation cannot acquire more than 50 percent in the voting power or value of the stock of the foreign corporation . . . . (b) There cannot otherwise be a U.S. “control” group—that is, not more than 50 percent in the voting power or value of the stock of the foreign corporation can be owned by U.S. persons who are officers or directors of the U.S. corporation or five percent or greater shareholders of the foreign corporation . . . . (c) The foreign corporation must have a value at the closing . . . that is at least equal to the value of the U.S. target . . . . (d) The foreign corporation, directly or through qualified subsidiaries or partnerships, must have been engaged in the active conduct of a trade or business outside of the United States for the 36 months before the closing date, and there can be no intention at the closing date to dispose of that business.\textsuperscript{83}

Had these same regulations been in place at the time of the Helen of Troy inversion, the transfer of shares to the new Bermuda shell corporation would have been fully taxable.\textsuperscript{84} It is important to note, however, that it is the corporation’s shareholders, not the

\textsuperscript{80} Kim, supra note 36, at 163.
\textsuperscript{81} See infra Part II.C.3.
\textsuperscript{82} Taylor, supra note 74, at 147.
\textsuperscript{83} Id.
corporation itself, who are forced to face this tax. This is why a New York Times columnist recently asked readers to “pause and reflect [on the fact] that Medtronic is pushing a transaction that from Day 1 may cost some of its shareholders as much as 33 cents on the dollar.” In fact, some Medtronic shareholders brought suit against its board of directors to enjoin them from forcing shareholders to face this tax while reimbursing top executives. Similarly, Fortune magazine called this “[a]nother reason that Main Street shouldn’t trust Wall Street.” The conclusion that might be drawn here is that while these early measures likely succeeded in dissuading some companies from attempting inversions, they fell far short of a permanent solution.

3. The American Jobs Creation Act of 2004

Signed into law by President George W. Bush on October 22, 2004, the American Jobs Creation Act of 2004 amended nearly 600 code sections, including provisions designed to discourage the use of corporate inversions. Most significantly, the Jobs Creation Act imposed a two-step regime on the recognition of a corporate inversion, based on continuity-of-ownership thresholds. First, the Jobs Creation Act “provides that when a new foreign parent is at least 80% owned by the former parent’s stockholders, the new law treats the foreign parent as a domestic corporation, thus generally denying to the firm the tax benefits of the inversion.” Second, if “at least 60 percent but less than 80 percent” of the new foreign corporation is owned by the former parent’s stockholders, “the foreign status of the acquiring corporation is respected but certain other adverse tax consequences apply, including the inability to

86. Id.
89. Kim, supra note 36, at 163–64.
90. CRS REPORT 1, supra note 7, at 11.
91. Id.
use tax attributes to reduce certain corporate-level income or gain...recognized by the expatriated entity.\textsuperscript{92}

By imposing these continuity-of-ownership requirements, Congress successfully took away the ability of multinational corporations to complete an inversion by “buy[ing] a P.O. box in the Cayman Islands and call[ing] it a day.”\textsuperscript{93} However, rather than eliminate inversions, the continuity-of-ownership rules set the stage for the inversions that would become prevalent nearly a decade later. Inverting is no longer as simple as setting up a P.O. box, but it may still be accomplished by merging with an existing foreign corporation.\textsuperscript{94}

The Jobs Creation Act also implemented a temporary “tax holiday” intended to incentivize “multinational corporations...to repatriate [some of the] billions in overseas profits” that were trapped outside of the United States.\textsuperscript{95} The tax holiday temporarily allowed U.S. corporations to repatriate income “at an effective tax of 5.25% instead of the top 35% rate.”\textsuperscript{96} A 2011 U.S. Senate report found that multinational corporations responded by repatriating $312 billion to the United States, avoiding around $3.3 billion in U.S. taxes in the process.\textsuperscript{97}

The primary congressional objective in passing the tax holiday was to incentivize multinational corporations to invest cash in the United States in the form of creating U.S. jobs.\textsuperscript{98} The 2011 Senate

\textsuperscript{92. GENERAL EXPLANATIONS, supra note 33, at 64; see also DEP’T OF THE TREASURY, REPORT TO THE CONGRESS ON EARNINGS STRIPPING, TRANSFER PRICING AND U.S. INCOME TAX TREATIES 10 (2007).}
\textsuperscript{93. Adams, supra note 44 (explaining that prior to the act, a company could invert simply by changing its address).}
\textsuperscript{94. Id. (explaining that an inversion by merger is possible if less than eighty percent of the new company’s shares are owned by the U.S. entity).}
\textsuperscript{97. PERMANENT SUBCOMM. ON INVESTIGATIONS OF THE COMM. ON HOMELAND SEC. AND GOVERNMENTAL AFFAIRS, supra note 96.}
\textsuperscript{98. See id. at 6.}
report found that around two-thirds of the top repatriating corporations had actually cut U.S. jobs after bringing the cash to the United States, resulting in net job losses of 20,931 in the three years following the enactment of the tax holiday.\textsuperscript{99} Moreover, a mere five corporations realized over one-quarter of the benefits of the repatriation holiday.\textsuperscript{100}

Finally, the Jobs Creation Act sought to limit inversions by imposing an excise tax on the shares of an inverting corporation held by its executives, when those shares were received as compensation.\textsuperscript{101} This measure was specifically targeted at dissuading those individuals who sit in a position to carry out a corporate inversion from doing so by imposing significant personal financial cost on those executives.\textsuperscript{102} However, some corporations that have initiated inversions in recent years have softened the effect of this provision by agreeing to pay significant sums to shield their executives from these tax bills.\textsuperscript{103} Medtronic, for example, "estimates that it will give $63 million of nondeductible payments to its top executives and directors to cover their excise taxes and the taxes they will owe on their excise tax subsidy."\textsuperscript{104}

Thus, while the 2004 legislation largely succeeded in doing away with "naked" inversions, it also left open mechanisms by which U.S. corporations could invert.\textsuperscript{105} Moreover, as will be discussed below, the bill failed to address tax avoidance mechanisms employed by inverted corporations, such as "earnings stripping."\textsuperscript{106}

\textsuperscript{99} Id. at 10–11.
\textsuperscript{101} See \textit{26 U.S.C. § 4985(a)} (2012). This excise tax applies to "the value . . . of the specified stock compensation held (directly or indirectly) by or for the benefit of such individual or a member of such individual’s family . . . at any time during the 12-month period beginning on the date which is 6 months before the expatriation date." \textit{Id.} § 4985(a)(2).
\textsuperscript{102} Hayes, \textit{supra} note 84.
\textsuperscript{103} \textit{Id.}
\textsuperscript{104} Allan Sloan, \textit{Corporate Inversion: Another Reason Main Street Shouldn’t Trust Wall Street}, WASH. POST, Sept. 12, 2014, at A18, \textit{available at 2014 WLNR 25263756}.
\textsuperscript{105} CRS REPORT 2, \textit{supra} note 20, at 6.
\textsuperscript{106} See \textit{infra} Part III.A.
III. CURRENT CONTROVERSY: CORPORATE INVERSIONS FROM 2004–2014

A. Recent Increase in Inversions

As discussed in the previous section, the Jobs Creation Act largely did away with so-called “naked inversions,” but left the door open for two primary types of inversions to continue.107 According to the Congressional Research Service, these are “the naked inversion via the business activity exemption, and merger with a smaller company.”108

Recall that in a “substantial business activity” inversion, a U.S. parent corporation that does substantial overseas business creates a foreign subsidiary in the overseas jurisdiction.109 The U.S. corporation and foreign subsidiary then engage in a stock exchange, after which the new entity is a foreign corporation with a U.S. subsidiary.110 “Using the business activity route would require significant economic operations in the target country.”111 This is one reason that the United Kingdom has become a popular destination for inverting companies—many U.S. corporations already do substantial business there, while very little substantive economic activity occurs in formerly popular tax havens such as Bermuda or the Cayman islands.112

Finally, it should be noted that there is another likely reason that the United Kingdom has been a popular destination of late: companies would like to maintain the option of a future inversion. “Because of freedom of movement rules in the European Union, the UK cannot have anti-inversion laws . . . .”113

B. Treasury Department Announces New Regulations

In the absence of congressional action to address inversions, the Department of Treasury announced in the fall of 2014 that it would take regulatory measures to curb inversions.114 Because the

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107. CRS REPORT 2, supra note 20, at 6.
108. Id.
109. Id. at 4.
110. Id.
111. Id. at 6.
112. Id.
113. Id.
114. See Press Release, U.S. Dep’t of the Treasury, Treasury Announces First
Treasury Department's options are somewhat limited due to questions about the extent of its authority, its announced regulations seek to use current laws to "eliminate[] certain techniques inverted companies currently use to access the overseas earnings of foreign subsidiaries of the U.S. company that inverts without paying U.S. tax." Substantively, the regulations seek to limit the ability of inverted corporations to access overseas cash through the creative use of loans. Corporations would no longer be able to make "hopscotch" loans, in which a foreign subsidiary loans cash to the new foreign parent company as opposed to the U.S. entity repatriating the cash and being taxed on it at U.S. rates. The new regulations would treat these loans as "U.S. property" for the purposes of taxation, and treat the loan as a taxable dividend. The new regulations also seek to reinforce the existing continuity-of-ownership rules put in place by the Jobs Creation Act. Specifically, the Treasury Department seeks to eliminate some of the creative ways that corporations have manipulated the eighty percent threshold. Recall that if more than eighty percent of the ownership of the new foreign corporation is identical to that of the inverting U.S. corporation, the entity is treated as a U.S. corporation for tax purposes. A corporation might engage in a number of maneuvers prior to inversion to make itself appear smaller on paper in order to avoid this threshold.

Steps to Reduce Tax Benefits of Corporate Inversions (Sept. 22, 2014).
115. Treasury Secretary Jacob Lew was quoted in July of 2014 as saying, "We do not believe we have the authority to address this inversion question through administrative action." Richard Rubin, Lew Explores U.S. Inversion Limits He Dismissed in July, BLOOMBERG, Aug. 6, 2014, available at http://www.bloomberg.com/news/2014-08-06/lew-explores-u-s-inversion-limits-he-dismissed-in-july.html. By early August of the same year, however, Secretary Lew had reversed his position and announced that Treasury was "reviewing a broad range of authorities" to address inversions through administrative action. Id.
117. Id.
118. Id.
119. Id.
120. Id.
122. Treasury Actions, supra note 116.
First, the "cash box" method refers to a practice where the foreign corporation makes itself appear larger using assets that "are not used by the entity for daily business functions," thus making it appear as if the foreign corporation makes up more than twenty percent of the new entity.\(^{123}\) The Treasury Department’s regulations aim to end this practice by disregarding these assets where at least fifty percent of the foreign corporation’s assets are passive.\(^{124}\)

Next, the Treasury Department seeks to "[p]revent U.S. companies from reducing their size pre-inversion by making extraordinary dividends."\(^{125}\) These are referred to as "skinny-down" dividends and are designed to allow the inverting corporation to reduce its size below the eighty-percent threshold.\(^ {126}\) The Treasury Department’s new rules would disregard these pre-inversion dividends for the purpose of calculating ownership percentages.\(^ {127}\)

Finally, the new Treasury Department regulations aim to prevent the use of "spinversions." A "spinversion" occurs when a corporation transfers some of its operations to a new foreign corporation and then spins off that corporation to its public shareholders.\(^ {128}\) This allows "[s]hareholders [to] get the benefits of lower tax bills for that separated unit . . . ."\(^ {129}\) The Treasury Department seeks to end this practice.\(^ {130}\)

The new regulations appear to have had at least some immediate impact, including possibly playing a role in the decisions of pharmaceutical company AbbVie and banana producer Chiquita to abandon their planned inversions.\(^ {131}\) In the

\(^{123}\) Id.
\(^{124}\) Id.
\(^{125}\) Id.
\(^{126}\) Id.
\(^{127}\) Id.
\(^{128}\) Id.
\(^{130}\) Treasury Actions, supra note 116.
\(^{131}\) Just weeks after the Treasury Department announced the new regulations, pharmaceutical company AbbVie announced that it would not be moving forward with its planned inversion. David Gelles, After Tax Inversion Rules Change, AbbVie and Shire Agree to Terminate Their Deal, N.Y. TIMES, (Oct. 20, 2014, 6:05 PM), http://dealbook.nytimes.com/2014/10/20/abbvie-and-shire-agree-to-terminate-their-deal/. AbbVie executives specifically cited these regulations as the reason for the collapse of the deal. Id. The company was quoted as saying, "The
case of Medtronic, the new regulations reportedly led Moody’s Investor Financial Services and Standard & Poor’s Financial Services, two of the largest credit rating firms in the nation, to consider downgrading their ratings of Medtronic’s corporate debt. The new regulations will significantly alter the way Medtronic will finance the deal, but the company has decided to proceed nonetheless. While these results are promising for policymakers who seek to put a permanent end to inversions, such results are likely temporary. The impact of these regulations seems unlikely to extend beyond those inversions that were already in progress at the time of the Treasury Department’s announcement.

IV. LEGISLATIVE PROPOSALS TO END INVERSIONS

Both Democrats and Republicans in Congress agree that corporate inversions must be addressed by legislative action. That is where the agreement ends. Whereas many Republicans insist that inversions are an “inevitable consequence of a flawed tax system” and seek broad tax reform, Democrats tend to favor action targeted specifically at the practice of inversions. To that end, Democrats

notice [of the regulations] introduced an unacceptable level of risk and uncertainty given the magnitude of the proposed changes and the stated intention of the Department of Treasury to continue to revise tax principles to further impact such transactions . . . . “ Id. Banana producer Chiquita also announced that it was canceling its planned acquisition of an Irish company. David Gelles, Chiquita Will Not Buy Irish Banana Producer, Clearing Way for Move to Brazil, N.Y. TIMES (Oct. 24, 2014, 9:51 AM), http://dealbook.nytimes.com/2014/10/24/chiquita-shareholders-reject-inversion-deal-clearing-way-for-rival-bid/. However, although the Treasury Department regulations would have impacted its deal, it is unclear if the regulations or other factors are what caused Chiquita to reconsider. Id.


133. Id. Following the announcement of the Treasury Department’s proposed regulations, Medtronic officials reportedly met twice to discuss whether to proceed with the Covidien merger and inversion. Id. at D2. Because Medtronic was planning to employ a “hopscotch” loan in order to make use of its overseas cash to fund the merger, and the new regulations limit that practice, Medtronic will now be forced to borrow $16.3 billion to fund the inversion rather than the $2.8 billion it had originally planned to borrow. Id. Even after carefully weighing these new considerations, Medtronic’s management decided to proceed with the merger. Id.

134. Mider, supra note 47.

135. Id.
proposed numerous bills in the 2013–2014 session of Congress to
discourage inversions.136

Before discussing specific reform proposals, it is important to
note that a primary reason legislative remedies are preferable to
administrative ones is the ability for them to apply retroactively. As
a general principle, federal law places constraints on the retroactive
application of "temporary, proposed, or final regulation[s]."137
Such regulations may not be applied to a date prior to when the
regulations are entered in the Federal Register.138 Or—as is the case
here—prior to the date "on which any notice substantially
descrying the expected contents of any temporary, proposed, or
final regulation is issued to the public."139

This general rule is particularly significant because it means
that any regulatory action taken by the Treasury Department may
only apply to inversions that are completed after Secretary Lew’s
September 22, 2014, notice.140 As a result, inversions already
completed in 2014, before the announcement—the same
inversions that sparked controversy in the first place—would not be
affected by these regulations at all. If policymakers wish to
retroactively thwart inversions that are already completed or in
progress, an act of Congress is required.141

The upcoming sections analyze those proposals, before
moving on to consider alternative proposals.

138. Id. § 7805(b)(1)(A).
139. Id. § 7805(b)(1)(C).
140. Treasury Actions, supra note 116.
141. 26 U.S.C. § 7805(b)(6) allows the general prohibition on retroactive
regulations to be “superseded by a legislative grant from Congress authorizing the
Secretary to prescribe the effective date with respect to any regulation.” It should
be noted that some observers opine that retroactive tax legislation may be in
conflict with the Due Process Clause of the Fifth Amendment. U.S. CONST. amend.
V; ERIKA K. LUNDER, ROBERT MELTZ & KENNETH R. THOMAS, CONG. RESEARCH SERV.,
R42791, CONSTITUTIONALITY OF RETROACTIVE TAX LEGISLATION 1, 1–4 (2012).
However, the Supreme Court has recognized that the enactment of retroactive tax
laws is “sometimes required by ‘the practicalities of producing national
legislation.’” Id. at 1 (quoting United States v. Carlton, 512 U.S. 26, 33 (1994)).
A. Lowering the Continuity-of-Ownership Threshold

As noted above, the Jobs Creation Act created a two-tiered regime based on continuity-of-ownership. Alteration to further restrict these requirements would be an attempt to directly limit the ability of companies to complete an inversion by way of merging it with a smaller company. A pair of proposals from 2014 would lower the threshold to fifty percent. That is, the U.S. government would continue to recognize and tax the post-merger company as a domestic corporation if “more than 50 percent of the stock . . . of the entity is held . . . by former shareholders of the domestic corporation.”

Supporters sought to make this measure retroactive to May 8, 2014. Doing so would not only discourage future inversions, but may have thwarted some inversions that are already completed or in progress. Given the lengths corporations have been willing to go to manipulate existing continuity-of-ownership rules, this proposal seems unlikely to put a permanent end to inversions. At best, it may delay inversions by making large enough foreign merger targets harder for U.S. corporations to find.

B. Barring Inverted Companies from Receiving Government Contracts

Another proposal was introduced simultaneously in the U.S. Senate and House of Representatives on July 30, 2014. The intended impact of the bill was evident from the title given to it by its sponsors: No Federal Contracts for Corporate Deserters Act of 2014. The bill would prevent inverted corporations from being able to obtain contracts from the federal government. Consistent with other recent proposals, the law would define an inverted

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142. See supra Part II.C.3.
143. CRS REPORT 2, supra note 20, at 6.
144. H.R. 4679, 113th Cong. (2014); S. 2360, 113th Cong. (2014). This is also in line with an anti-inversion proposal contained in President Obama’s budget proposal for fiscal year 2015, released in March of 2014. See GENERAL EXPLANATIONS, supra note 33, at 64–65.
146. CRS REPORT 2, supra note 20, at 13.
147. See supra Part III.3.B.
149. S. 2704; H.R. 5278.
150. S. 2704; H.R. 5278.
corporation as one with over fifty percent continuity-of-ownership between the former domestic corporation and the new foreign parent.  

Similar laws have been on the books each year since 2002, but their scope is limited to certain contracts from certain agencies. The proposal would also have closed what is viewed as a loophole in the current law by requiring the agency issuing the contract to include a clause preventing companies from obtaining subcontracts.

Had this proposal passed, it would likely have been a victory of political symbolism rather than a substantial deterrent for companies considering inversion. The bill's sponsors estimate that roughly $1 billion in federal contracts have gone to inverted corporations in the past five years. While $1 billion over five years is by no means an insubstantial amount, sacrificing certain government contracts seems likely to be a price worth paying for companies seeking to access many billions more in cash reserves stored overseas. It might be successfully argued that this proposal is an appropriate piece of a larger anti-inversion legislation scheme, or even a punitive measure to symbolically punish those companies who use tax planning techniques to avoid U.S. taxes. On its own, however, the proposal does not seem likely to have a serious effect as a deterrent on corporations.

C. Imposing an "Exit Tax" on Unrepatriated Earnings

Another bill was put forward in the U.S. Senate in September of 2014 with another almost comically on-the-nose title: the Pay What You Owe Before You Go Act. To understand this proposal, 


152. KATE M. MANUAL & ERIKA K. LUNDER, CONG. RESEARCH SERV., R43780, CONTRACTING WITH INVERTED DOMESTIC CORPORATIONS: ANSWERS TO FREQUENTLY ASKED QUESTIONS 1 (2014).

153. *Id.* at 9; see also S. 2704 § 4713(a)(2); H.R. 5278 § 4713(a)(2).


155. See Rubin, supra note 63.

it is helpful to look at the way the United States treats wealthy individual taxpayers who renounce their U.S. citizenship. As it does with corporate income, the United States taxes the income of its individual citizens on a worldwide basis—a practice that has been upheld by the Supreme Court. As a result, some individuals choose to expatriate in order to avoid certain U.S. taxes. When they do so, however, the United States imposes a tax on certain of their assets. "The theory of the [individual] exit tax is that [it] is the last chance the U.S. has of taxing you. It is a capital gain tax as if you sold your property when you left." The proposed corporate exit tax would work in a similar fashion. If enacted, the proposal would impose a tax on all of a corporation’s unrepatriated earnings before the corporation renounces its U.S. residence. Because this is a novel proposal, there is very little reliable data available to predict whether it would

157. Cook v. Tait, 265 U.S. 47, 55–56 (1924). The Court held that "the basis of the power to tax was not and cannot be made dependent upon . . . the domicile of the citizen, that being in or out of the United States, but upon his relation as citizen to the United States and the relation of the latter to him as citizen." Id. at 56.


159. See 26 U.S.C. §§ 877, 877A (2012). The Internal Revenue Code requires that certain individuals with a net worth of over $2 million or an average annual net income tax for the five years preceding expatriation of greater than a certain inflation-indexed amount pay a tax on all property as if it were sold for fair market value on the date of expatriation. Id. §§ 877, 877A. A prominent recent example of this practice gained headlines when Eduardo Saverin, a billionaire and co-founder of the website Facebook, expatriated to Singapore. Susanna Kim, Facebook IPO: Eduardo Saverin Defends Citizenship Move, ABC NEWS (May 17, 2012, 4:16 PM), http://abcnews.go.com/blogs/business/2012/05/facebook-ipo-eduardo-saverin-defends-citizenship-move/.


succeed in dissuading corporations from inverting.\footnote{162} At the very least, passage of a tax on unrepatriated earnings would likely add to the complexity of the cost-benefit analysis that a company must perform before making the decision to invert.\footnote{163}

V. OTHER POSSIBLE REFORMS

A. Lowering or Eliminating the Corporate Income Tax

Some commentators have implored policymakers to lower the corporate tax rate.\footnote{164} Others, including Treasury Secretary Lew counter that, “even if we cut our tax rates and broaden the tax base, we would still need to enact anti-inversion provisions because companies always would find countries with near-zero rates to which they could relocate.”\footnote{165} A recent Congressional Research

\footnote{162}{It should be noted that some European nations have adopted similar exit tax provisions into law, which are designed to impose taxes on companies seeking to expatriate for tax reasons. See Mitchell A. Kane & Edward B. Rock, \textit{Corporate Taxation and International Charter Competition}, 106 MICH. L. REV. 1229, 1275 (2008). For two reasons, however, these laws do not provide helpful comparisons with which to evaluate the proposed U.S. exit tax. First, the European Court of Justice has heard a number of challenges to exit taxes, but the grounds on which they have been decided have no parallels in U.S. law. See, e.g., Case C-371/10, Nat’l Grid Indus. BV v. Inspecteur van de Belastingdienst Rijnmond, 2011 E.C.R. I-12273. Second, in general, the motivations behind a particular nation’s tax policy are highly specific to that nation, and it is therefore difficult to make effective comparisons to the U.S. system. See Omri Y. Marian, \textit{Meaningless Comparisons: Corporate Tax Reform Discourse in the United States}, 32 VA. TAX REV. 133, 203 (2012) ("Tax writers have much to learn from the experience of other taxing jurisdictions. However, as much as a comparative approach is desirable, it is also dangerous if ill executed. Bad comparisons produce inaccurate guidance that may not bring about the desired results of tax reform.").}

\footnote{163}{It is further difficult to estimate the effect of this proposal because the individual expatriation tax itself is an imperfect comparison. Individuals who expatriate must consider a broad range of non-monetary benefits that arise from U.S. citizenship, including the right to vote in U.S. presidential elections. See Kirsch, \textit{supra} note 158, at 875 n.45.}


\footnote{165}{Lew, \textit{supra} note 16. In the extreme, there are even some who have argued that the United States could permanently solve the inversion issue by becoming a no-tax jurisdiction itself. See James Mann, \textit{Note, Corporate Inversions: A Symptom of a Larger Problem, the Corporate Income Tax}, 78 S. CAL. L. REV. 521, 522}
Service report injected a dose of political reality into this analysis, concluding that "[a]lthough a lower rate would reduce the incentives to invert, it would be difficult to reduce the rate to the level needed to stop inversions, especially given the effect of the revenue loss on the budget."\textsuperscript{166}

It is unlikely that cutting corporate tax rates will be the stand-alone solution that some hope it to be. Moreover, there is very little consensus over how to precisely measure the effective tax rate that is actually paid by corporations in the first place.\textsuperscript{167} Some argue that although the U.S. statutory rate of 35\% is high when compared to many other countries, the effective rate paid by U.S. corporations is only 27.7\%.\textsuperscript{168} This is roughly equal to the effective rate paid by corporations in other economically developed nations.\textsuperscript{169}

That said, some reduction in the corporate tax rate seems likely to occur in the relatively near future, as both President

\textsuperscript{\textsuperscript{166}} CRS REPORT 2, \textit{supra} note 20.
\textsuperscript{\textsuperscript{167}} For an explanation of the difference between the statutory and effective corporate tax rates, see generally Eric Toder, \textit{Business Taxation: What Are the Statutory and Effective Corporate Tax Rates?}, TAX POL’Y CENTER, http://www.taxpolicycenter.org/briefing-book/key-elements/business/statutory.cfm (last updated July 9, 2008) ("The statutory corporate tax rate is the rate that is imposed on taxable income of corporations, which is equal to corporate receipts less deductions for labor costs, materials, and depreciation of capital assets. In contrast, the effective corporate tax rate (ETR) measures the taxes a corporation pays as a percentage of its economic profit.").
\textsuperscript{\textsuperscript{169}} Id. The Economic Policy Institute points to estimates by PriceWaterhouseCoopers, an international corporate consulting firm, which found that the U.S. effective corporate tax rate for the period between 2006 and 2009 was 27.7\%, as compared to a weighted average effective tax rate among other developed nations of 27.2\%. \textit{Id.} The nations comprising that average include "Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Ireland, Israel, Italy, Japan, Korea, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, and United Kingdom." \textit{Id.} at 7 n.2.
Obama and Republicans in the House of Representatives have proposed reductions in the corporate tax rate. As summed up in a proposal by the President, the United States "essentially trades off greater tax expenditures, loopholes, and tax planning for a higher statutory corporate tax rate relative to other countries." In addition to providing incentives not to invert, there are numerous compelling reasons for reducing the statutory rate, including international competitiveness and the heavier burden it places on small businesses relative to large ones.

At the end of the day, the cuts proposed by President Obama or congressional Republicans will likely be insufficient to entirely deter corporations from inverting. As Secretary Lew pointed out, lowering rates to the extent required to deter inversions would be incredibly difficult given revenue concerns. However, given the benefits that lower rates would have on the international competitiveness of the U.S. tax code, as well as the decreased burden on small businesses, Congress should act soon to lower rates even if stopping inversions is only a small part of the underlying motivation.

B. Taxing Corporate Income on a Territorial Basis

Inversions do not change how the U.S. operations of a company are taxed. Whether it is earned by a foreign corporation or a domestic one, "[a]ll income earned within U.S. borders is taxed the same—in the year earned and at statutory tax rates up to thirty-five percent." Recall that one of the reasons inversions are attractive to U.S. multinational corporations is because the United

170. PRESIDENT'S FRAMEWORK, supra note 41, at 2.
171. COMM. ON WAYS & MEANS, supra note 42, at 49.
172. PRESIDENT'S FRAMEWORK, supra note 41, at 2.
173. See Small Bus. Admin., Office of Advocacy, Effective Federal Income Tax Rates Faced by Small Businesses in the United States, in SMALL BUSINESS TAX ISSUES AND BENEFITS 1, 6 (Alton E. Kastenberg ed., 2010) [hereinafter Small Business Tax Rates]. Small businesses face a set of challenges in the federal tax system as compared to large businesses. Id. ("Small businesses often . . . lack the economies of scale that large business have, and they have less access to the capital markets.").
174. See Lew, supra note 16.
176. CRS REPORT 2, supra note 20, at 2.
States employs a system of “worldwide” taxation.\textsuperscript{177} Today, as a result of patchwork legislation and variable treatment of different types of income based on the source, it might be fairer to say, as one observer has, that “the U.S. rules, for almost a century, have been suspended in the middle between the worldwide and territorial poles . . . \textsuperscript{178}"

In recent years, countries across the globe have engaged in “a substantial movement . . . toward territoriality.”\textsuperscript{179} This includes the United Kingdom, which made the move to territoriality for similar reasons as the United States might consider doing so—repeated threats that domestic United Kingdom companies would reincorporate outside the United Kingdom for tax reasons.\textsuperscript{180} Naturally, then, it is worth considering whether the United States should follow the trend of becoming a territorial jurisdiction to remain competitive with other international tax systems.

From a partisan perspective, moving the United States to a territorial system of taxation has long been a Republican goal.\textsuperscript{181} Opponents of the move point to estimates that a move to a territorial system “might reduce U.S. revenues by $130 billion over ten years.”\textsuperscript{182} The major roadblock that remains in the way of the United States making the switch to a territorial system is the idea—justified or not—that if foreign-source income were not subject to U.S. taxes, U.S. corporations would find ways to shift earnings overseas.\textsuperscript{183} That is, corporations would attempt to make it appear as if larger portions of their earnings are coming from overseas than is the reality, in order to lessen the U.S. tax burden.

Ultimately, the impact of such a move is extremely difficult to predict because it depends on a variety of factors. “Whether a worldwide or territorial tax will create more U.S. jobs, more fairly distribute U.S. taxes, or accomplish a host of other beneficial results, depends on the responses of people and nations reacting dynamically to each others’ choices.”\textsuperscript{184} For that reason, the debate

\begin{itemize}
  \item \textsuperscript{177} See supra Part II.B.2.
  \item \textsuperscript{178} SHAVIRO, supra note 58, at 2.
  \item \textsuperscript{179} Id. at 135.
  \item \textsuperscript{180} Id.
  \item \textsuperscript{181} Id. at 3.
  \item \textsuperscript{182} Id.
  \item \textsuperscript{183} Id. at 4.
  \item \textsuperscript{184} Timothy Hisao Shapiro, Tax First, Ask Questions Later: Problems Predicting the Effect of President Obama’s International Tax Reforms, 16 STAN. J.L. BUS. & FIN. 141, 2015.
\end{itemize}
over whether the United States should move toward a territorial system of taxation should encompass much more than corporate inversions. From the standpoint of economic efficiency and global competitiveness, the move might be a beneficial one because it would bring the United States into line with the global trend toward territorial taxation. However, the move may also create a new set of perverse incentives for multinational corporations to invest abroad where they will incur the lowest tax bill, rather than at home in the U.S. economy.

The conclusion of this discussion, at least for the time being, is that a move to territorial taxation is an attractive option not only to stem corporate inversions, but also to modernize the U.S. international corporate tax system in general. Although it is possible that the United States will follow the trend toward this system in the future, political realities of the day would suggest that this will not be soon.

C. Changing the Way the United States Defines Corporate Tax Residence

Central to the inversion debate is the concept that a corporation has a “residence” for tax purposes. Countries define corporate residence in different ways, but there are two primary tests for locating a corporation: “a legal system can adopt either the ‘place of incorporation’ (‘POI’) rule or some version of the ‘real seat’ (‘RS’) rule.” Under POI, a corporation’s residence is dependent solely on one formalistic consideration: its place of incorporation. Under RS, more factors are taken into account.

178 (2010).
185. Id.
186. Id. (“[Territorial taxation] shrinks the tax base, however, by ignoring foreign-source income and arguably treats corporations invested heavily in tax havens more favorably than similarly wealthy corporations invested solely in the United States.”).
187. See Shaviro, supra note 58, at 3 (discussing the partisan divide on support for the move to territorial taxation during the 2008 presidential campaign).
188. Omri Marian, Jurisdiction to Tax Corporations, 54 B.C. L. Rev. 1613, 1613–14 (2013) (“Determining a corporation’s tax residence . . . is necessary to calculate the tax liabilities of the corporation and its affiliates, and sometimes, its shareholders.” (footnotes omitted)).
189. Kane & Rock, supra note 162, at 1235.
190. Id. The primary benefits of a POI system are its efficiency and its cost-effective administration. Marian, supra note 188, at 1622. This efficiency arises from the legal certainty that is provided by the POI system—the entity is taxed at
consideration, including the location of the corporation’s administrative headquarters, or where most of the corporation’s employees or assets are located.191

The fact that inversions by U.S. corporations are even possible is due to the country’s adherence to a POI system.192 That said, RS systems are also subject to abuse, although those abuses may require greater creativity on the part of corporate officers.193 One possible solution to this problem is

[f]or the U.S. to adopt a test under which a corporation that is (i) managed and controlled from the United States; or (ii) the securities of which are listed on an exchange in the United States . . . will be treated as a “domestic” corporation for federal income tax purposes.194

Thus, adoption of such a system may come at the cost of some level of efficiency that is achieved by the POI system. The benefit, however, is that such a system would make the process of incorporating overseas to avoid U.S. taxes more burdensome on a corporation, likely dissuading many from doing so.

Those considerations aside, revisiting the definition of corporate residence is not the most urgent or effective area of reform. To be sure, “[b]oth U.S. individuals, and those from outside who want to be economically active here or to access our capital markets, still frequently choose U.S. incorporation due to nontax advantages that they associate with it.”195 If the United States does proceed on this front, it should tread lightly, keeping in mind that international tax policy is not made in a vacuum. Expansion of the definition of what makes a corporation a U.S. corporation might attach U.S. resident status to multinational corporations in a

191. Kane & Rock, supra note 162, at 1235.
192. Marian, supra note 188, at 1629 (“POI residence tests can easily be avoided by incorporating in a foreign jurisdiction.”).
193. Id. RS tests that consider the place of management in determining tax residence can be manipulated by a corporation conducting all board meetings and other important management proceedings in a foreign country. Id. Tax practitioners reportedly speculate that this practice gave rise to a travel feature that most are familiar with today—the airport hotel. Id.
194. Id. at 1664.
195. Shaviro, supra note 58, at 194.
way that other countries deem overly aggressive, potentially inviting retaliation.\textsuperscript{196}

VI. CONCLUSION

The U.S. corporate tax system at times can feel like a hopeless patchwork of statutes and regulations. The deeply political nature of proposed reforms often make the prospects for broad, meaningful reforms seem hopeless. For those reasons, it would not be unreasonable to conclude that "[a]lmost no one likes the existing U.S. international tax system, and no one should like it. It is at once too burdensome and too flexible . . . ."\textsuperscript{197} Corporate inversions are merely one symptom of more significant problems with the tax code.

The United States has the highest statutory corporate rate in the developed world,\textsuperscript{198} but also "raises far too little revenue relative to its tax planning, compliance, and administrative costs."\textsuperscript{199} While the regulatory actions recently announced by the Treasury Department may be effective in temporarily stalling the current wave of inversions, they will likely do no better than to serve as stopgap measures. Without action by Congress, the inversion problem will persist and possibly accelerate in years to come.

While there is great value in the measures proposed by President Obama and congressional Democrats to directly discourage inversions, the long-term competitiveness of the U.S. international tax code would benefit greatly from the broad reform that others have proposed. There will not be one solution that cures all of the system's ills. But a combination of the solutions outlined above may not only discourage future inversions, but they may also modernize the corporate tax code in larger ways. Lowering corporate tax rates, moving from a world-wide to a territorial system of taxation, altering or eliminating the repatriation rule, and other options outlined in this Article are all creative and perhaps desirable solutions to the problem.

As for Medtronic, the company continues to be controlled from its corporate campus in a suburb just outside of Minneapolis, not far from the garage where the company began in 1949. On

\begin{flushleft}
\textsuperscript{196} \textit{Id.} at 195.  \\
\textsuperscript{197} \textit{Id.} at 199.  \\
\textsuperscript{198} \textit{See} \textit{Lew, supra} note 16.  \\
\textsuperscript{199} \textit{Shaviro, supra} note 58, at 199.  \\
\end{flushleft}
paper, however, Medtronic’s residence may soon be over 3,500 miles and an ocean away. If the United States does not act soon, many others may follow.