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MORE U.S. CORPORATIONS PREPARE TO RENOUNCE THEIR AMERICAN 'CITIZENSHIP' TO DODGE TAXES

Please Join Other Newspapers Editorializing Against Corporate Inversions

"Corporate inversions" are national news. Hundreds of stories have appeared in major papers, on radio and on television exposing recent efforts by Burger King, Walgreens and other corporations to dodge U.S. taxes by becoming a foreign company on paper. Scores of editorials and columns have condemned corporations for these actions and have criticized the legal loophole that makes it possible. (See a partial list of editorials and columns here.)

The fact that an American corporation can renounce its U.S. "citizenship" by purchasing a smaller foreign firm, and then become a subsidiary of that firm usually with a corporate address in a tax haven, has caught the attention and raised the ire of the American public. When Walgreens announced earlier this year that it might declare itself Swiss, the move raised questions about what it means to be an American company. President Obama said in speeches and interviews that inverting companies are "corporate deserters." Many commentators called them "unpatriotic."A recent nationwide poll found that over two-thirds of likely voters disapprove of corporate inversions, including 86% of Democrats, 80% of Independents and 69% of Republicans.

Although Walgreens announced later that it had decided not to become a Swiss company, the corporate inversion story isn't over. In fact, it's just heating up. Burger King is buying the Canadian restaurant chain Tim Hortons, and it is using the corporate inversion loophole to become a Canadian company. The corporation has denied that it is making the move to avoid paying its fair share in U.S. taxes, but tax and investment experts are highly skeptical.

Senator Ron Wyden (D-OR), chairman of the Senate Finance Committee, said industry sources told him that there could be 25 more corporate defections before the end of the year. "The inversion virus now seems to be multiplying every few days," Wyden said. "The time for action is now."

In the 31 years from 1983 through 2014, 75 U.S. corporations have undergone corporate inversions – 29 from 1983 to 2004, 47 from 2004 to 2013, and 14 pending in 2014. [See table below for 14 companies that have completed or have pending inversions so far this year.] But until Walgreens, most Americans had never heard of corporations abandoning the United States to avoid paying taxes. Nor did they know that a corporation can declare itself a foreign firm while keeping its headquarters and operations here at home.

President Obama and key members of Congress have called for legislation to make it more difficult for corporations to invert. The Obama administration is also exploring issuing an executive order, which would remove some of the tax incentives to invert but not block them. Achieving either goal will require continued pressure from opinion leaders and the public in sharply divided Washington. For this reason, *it is critical that your publication inform Americans about what is happening right now by editorializing on this matter, or else it is likely that nothing will change*.

Status of Corporate Inversions in 2014

Status	U.S. Company	U.S. HQ Location	Foreign Acquisition Target	Foreign HQ	New Tax Domicile	Deal Value $ Millions
Pending	AbbVie Inc.	Illinois	Shire	Ireland	Jersey, U.K.	54,000
Completed	Actavis PLC	New Jersey	Forest Laboratories	New York	Ireland	28,000
Pending	Applied Materials Inc.	California	Tokyo Electron Ltd	Japan	Netherlands	7,060
Pending	Auxilium Pharmaceuticals Inc.	Pennsylvania	QLT	Canada	Canada	345
Pending	Burger King	Florida	Tim Hortons, Inc.	Canada	Canada	11,200
Pending	C&J Energy Services Inc.	Texas	Nabors Industries (completion/production businesses)	Bermuda	Bermuda	2,860
Pending	Chiquita Brands International	North Carolina	Fyffes	Ireland	Ireland	526
Completed	Endo Health Solutions	Pennsylvania	Paladin Labs	Canada	Ireland	1,600
Pending	Horizon Pharma Inc.	Illinois	Vidara Therapeutics	Ireland	Ireland	660
Pending	Hospira Inc.	Illinois	Danone	France	NA	5,000
Pending	Medtronic Inc.	Minnesota	Covidien PLC	Ireland	Ireland	42,900
Pending	Mylan Inc.	Pennsylvania	Abbott Laboratories generic drug unit	Illinois	Netherlands	5,300
Withdrawn	Pfizer Inc.	New York	AstraZeneca PLC	U.K.	N.A.	122,000
Pending	Salix Pharmaceuticals	North Carolina	Cosmo Technologies/Cosmo Pharmaceuticals	Italy	Ireland	2,700
						284,151

Sources: news reports

The flood of corporate inversions is due to several reasons. First, the prospect of federal corporate tax reform in the near-term is dead, so companies are going in search of tax haven addresses to reduce their tax rates. Second, many firms have billions in profits offshore that go untaxed until they are brought back to the U.S. Rather than repatriate those profits, companies can use a tax inversion to keep them offshore permanently, and avoid paying the U.S. taxes they owe. Finally, Wall Street investment banks "are estimated to have collected, or will soon collect, nearly $1 billion in fees over the last three years advising and persuading American companies to move the address of their headquarters abroad (without actually moving)," according to *The New York Times.*

HOW CORPORATE INVERSIONS WORK AND WHY THEY ARE UNFAIR TO OTHER TAXPAYERS

Corporate inversions are made possible by a loophole in U.S. law that allows a corporation to become foreign when it buys a foreign company and then becomes a subsidiary of that new entity – even if the foreign company is much smaller than the American firm. The foreign company is typically incorporated in a tax haven. To qualify for an inversion, more than 20% of the stock of the newly merged company must be owned by foreigners, or 25 percent of company operations must take place abroad. These are very low hurdles that make inversions relatively easy.

For more about how corporate inversions work and for additional information, see the ATF fact sheet "Corporate Tax Inversions."

The U.S. corporation doesn't actually move its operations overseas – the change takes place mostly on paper. An inverted corporation continues to take advantage of an educated American workforce; relies on our legal system to protect its investments and patents; uses our transportation system to get its products to market; and has ready access to more than 300 million American consumers. In addition, some inverting corporations benefit directly or indirectly from federally-funded research, and will continue to sell their products and services to the federal government. But they will slash what they pay for those services, leaving American taxpayers to pick up the tab.

In an August 6 press conference, President Obama bemoaned the fact that inversions allow corporations to continue to enjoy the benefits of operating in America without fully sharing in the cost:

> "It's not fair. It's not right. The lost revenue to Treasury means it's got to be made up somewhere, and that typically is going to be a bunch of hardworking Americans who either pay through higher taxes themselves or through reduced services. And in the meantime, the company is still using all the services and all the benefits of effectively being a U.S. corporation; they just decided that they'd go through this paper exercise."

Corporations don't invert because they have decided that a tax haven is a better place to do business than the United States. They invert because they can dodge millions if not billions of dollars a year in taxes while continuing to enjoy the immense advantages of remaining headquartered here.

The U.S. Treasury will lose at least $19.5 billion over the next 10 years from corporate inversions, according to the Joint Committee on Taxation. But the figure is likely much higher given that estimates were made before the growing wave of inversions. For instance, if Pfizer succeeds in inverting (it is about to try for a second time this year with AstraZeneca) it could save up to $1.4 billion a year.

If Walgreens had completed an inversion it would have cost the U.S. Treasury $4 billion over five years, according to equities research firms' estimates analyzed in a widely-cited report by Americans for Tax Fairness and Change to Win Retail Initiatives. Walgreens ultimately decided not to invert in part because of fear of a potential "consumer backlash." However, it would be wrong to assume that other corporations will also back down. Most of the companies currently planning to invert, with the exception of Burger King, are much less visible than Walgreens. These companies won't be as concerned about a consumer backlash because most consumers have never heard of them.

Only if the press remains focused on the inversion story and its potential costs to U.S. taxpayers will Americans even know that the wave of inversions is growing.

THE PROSPECTS FOR CHANGE

Congress is scheduled to be back for just two weeks (Sept. 8 – 19) before breaking for the election campaign. That leaves very little time to come up with a bipartisan deal on this issue. Many lawmakers prefer to not deal with what some consider a controversial issue before the election. Instead, they say the inversion crisis should be addressed through comprehensive corporate tax reform – but Congress has shown little appetite for such an ambitious effort anytime soon.

The best we can hope for is that over the next two months the stage gets set for Congress to act on corporate inversions in the lame duck session after the November election; President Obama issues an executive order that will take away much of the financial incentive for corporations to invert; and candidates get pressed to say how they will address corporate inversions and other more significant tax reform issues as they run for office in coming weeks. *We urge you to raise these issues as you meet with candidates this election season.*

There are several possible approaches to slow or halt the flood of corporate inversions. Our preference is Option 1, passage of the Levin bills. *We urge you to strongly support this option*.

Option 1: Pass the Levin bills to make it more difficult for corporations to invert

Congress could pass stand-alone legislation to restrict inversions. The Stop Corporate Inversions Act of 2014 (S. 2360) by Sen. Carl Levin (D-MI) already has 22 cosponsors. The Levin bill would make it more difficult for corporations to invert disallowing an inversion if 50% (instead of the current level of 20%) or more of the merged corporation is owned by shareholders of the original American corporation. The Senate bill is temporary – a two-year limit to give Congress time to reform the corporate tax system.

Rep. Sander Levin (D-MI), Ranking Member of the House Ways and Means Committee, has introduced a companion bill in the House (H.R. 4679), which would be permanent; it would raise $19.5 billion over 10 years. The Obama administration strongly supports both bills. Senate Majority Leader Harry Reid (D-NV) could bring the legislation to the floor at any time. However, House Republican leaders are much less likely to do so. For either bill to progress, there must be significant outside pressure, both from the public and from opinion leaders.

Option 2: Adopt proposals to make inversions less attractive financially

Sen. Chuck Schumer (D-NY), a member of the Senate leadership, proposes reducing financial incentives for U.S. corporations to invert. He would restrict "earnings stripping," a legal loophole used to make it appear that a U.S. subsidiary of an inverted foreign corporation earns less in profits than it actually does. The corporation achieves this by having the profitable U.S. subsidiary borrow large sums of money from the foreign parent company. A U.S. subsidiary can deduct 50% of the cost of this loan, lowering what it appears to make in profits and effectively shifting the profit to the foreign parent company, located in a tax haven. The Schumer proposal would allow the U.S. subsidiary to deduct only 25% of its interest payment. It also includes other provisions to make inversions less attractive, including a requirement to get IRS pre-approval for certain transactions between the inverted foreign corporation and the U.S. subsidiary for a period of 10 years. Schumer doesn't claim that his bill (not yet introduced) will solve the inversions problem, but he says that it is "one piece of the puzzle."

Option 3: Take executive action to curb financial incentives to invert

Whether Congress acts or not, President Obama could take action using his executive power, and the Treasury Department is busy examining his options. This alone should make corporate CEOs think twice about inverting.

Stephen Shay, a professor at Harvard Law School and a former international tax official at the Department of the Treasury, recently published an article in Tax Notes outlining the executive branch's power to significantly reduce incentives to invert absent new legislation. First, he argues that Treasury can block the current practice by inverted corporations to load the new U.S. subsidiary with debt so it appears to lose money, and thus reduce its tax bill. Shay says that current law permits reclassifying this debt as equity, so it cannot be used to make a profitable corporation appear less profitable for tax purposes. Second, he argues that the executive branch can prevent inverted corporations from using profits that are currently offshore and untaxed by the United States to finance foreign acquisitions or to do stock buy-backs without paying U.S. taxes on the profits.

Neither action would block corporate inversions, but they would make inversions significantly less profitable. If the Obama administration acts, it likely will come under fire by Republicans who already argue that the president has overstepped his authority on a number of issues. Even though President Obama has spoken out strongly against corporate inversions, increased pressure from opinion leaders is needed to ensure that he takes action.

Option 4: Adopt the yet to be announced Wyden-Hatch proposal

Senate Finance Committee Chairman Ron Wyden (D-OR) has said that he is working with Ranking Member Orrin Hatch (R-UT) on a bipartisan solution to the corporate inversion problem. Wyden has expressed support for approaches that raise the requirements for corporate inversions and that lower incentives to invert. He has also stated that he favors short-term legislation to deal with the issue while Congress prepares to undertake major tax reform. Hatch has focused on what he says is the true cause of the inversion problem – U.S. corporate tax rates, which in his opinion are too high, forcing American corporations to invert. No details about a Wyden-Hatch proposal have yet been revealed.

THE ARGUMENT THAT INVERSIONS ARE CAUSED BY HIGH CORPORATE TAX RATES IS MISLEADING

Corporations argue that inversions are justified because the U.S.'s top corporate tax rate on profits – 35% – is the highest in the world, which puts American companies at a disadvantage. They claim that if Congress would lower corporate tax rates to 25% the incentive to invert would be removed.

But a recent, influential paper by Edward Kleinbard, University of Southern California law professor and former staff director of Congress's Joint Tax Committee, asserts that the "competitiveness narrative is largely fact-free." Kleinbard states that "whether one measures effective marginal or overall tax rates, sophisticated U.S. multinational firms are burdened by tax rates that are the envy of their international peers."

The key is to focus on *effective* tax rates – what corporations actually pay – rather than the top *statutory* rates – what they are legally supposed to pay. Many U.S. large corporations don't pay anything close to the 35% statutory rate, in part due to fact that they use various loopholes and accounting tricks to make it appear that their profits were earned in offshore tax havens.

For example:

- The U.S.'s average effective corporate tax rate is 27.1% compared with 27.7% for the other 30 OECD countries, according to the Congressional Research Service.
- Profitable U.S. corporations paid income taxes amounting to just 12.6% of worldwide income in 2010, according to the Government Accountability Office.

- Citizens for Tax Justice's survey of 288 corporations, which included most of the Fortune 500 corporations that were profitable each year from 2008 through 2012, found that they paid an average effective federal tax rate of just 19.4% over that period.
- Twenty-six profitable Fortune 500 firms paid no federal income taxes from 2008-2012, according to Citizens for Tax Justice. General Electric, one of the most notorious corporate tax dodgers, claimed $3.1 billion in refunds on $27.5 billion in profits during that period. The entire company paid less in federal taxes in five years than a single American family pays in one year.

It is critical to note that companies doing inversions already pay an effective tax rate lower than 25%. For instance, AbbVie's inversion with Shire, an Irish firm, will cut AbbVie's global tax rate from 22.6% in 2013 to 13% in 2016. Generic drugmaker Mylan, which is pursuing an inversion in the Netherlands by buying the offshore assets of Abbott Labs, paid a an effective global corporate income tax rate of just 16.2% in 2013.

*An ATF fact sheet on "Corporate Tax Rates" is available here***.**

CONCLUSION

The example of Walgreens' aborted inversion shows the power of the media and of consumers to affect this debate. Reporters and opinion writers brought the story to the attention of millions of Americans, who found the idea outrageous that corporations would renounce their U.S. "citizenship" to avoid paying their fair share of taxes. Many of them agreed with President Obama and others that these actions are "unpatriotic," and that the companies are "corporate deserters." Others were outraged to learn that these corporations would pay less for the same services that they pay for now and make everyone else pick up the tab.

Currently, at least 14 corporations are planning to invert – some believe the number could be 25 or more. With the exception of Burger King and Chiquita, these companies – Medtronic, Mylan, AbbVie and others – are not household names. It will be easier for these companies to escape public scrutiny.

But if corporate inversions are not stopped, the U.S. government will take on more debt, American families will end up paying more in taxes, or they will get fewer services for their tax dollars. Only if there is continued media attention and public outcry will policymakers feel compelled to act strongly to restrict corporate inversions.

Americans for Tax Fairness *is a diverse coalition of 425 national and state organizations that collectively represent tens of millions of members. The organization was formed on the belief that the country needs comprehensive, progressive tax reform that results in greater revenue to meet our growing needs. ATF is playing a central role in Washington and in the states on federal tax-reform issues.*