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If You Can't Beat Them, Join Them: The U.S. Solution to the Issue of Corporate Inversions

Scott DeAngelis

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Notes

If You Can't Beat Them, Join Them: The U.S. Solution to the Issue of Corporate Inversions

ABSTRACT

There is an old proverb, "If you can't beat them, join them," that suggests that those who cannot win against some group should stop fighting and instead band together with them. It seems clear that when it comes to corporate inversions, the United States cannot win. Instead, countries overseas have taken advantage of tax break schemes to lure multinational companies away from the United States. This Note suggests that to prevent further foreign inversions, the United States should join these foreign countries in two ways. First, the United States should put its support behind the OECD's plan of a multilateral instrument that would eliminate some of the unfair tax practices that facilitate controversial inversions. Second, the United States should implement its own patent box policy immediately, as there is no guarantee that the OECD's multilateral instrument will come to fruition.

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I. INTRODUCTION

Corporate inversions have once again gained the attention of both the media and politicians. This is not surprising, as there have been a surge of inversions in the past decade.¹ Not only has the quantity of inversions warranted notice, but the size of these transactions and the highly recognizable companies that have either inverted recently or plan to invert in the coming years have also been noteworthy.² Among some of the more well known corporations to invert are those in the technology and pharmaceutical industries that hold large amounts of intellectual property.³ Presumably this is in part due to favorable tax incentive policies, such as the patent box,

1. *New CRS Data: 47 Corporate Inversions in the Last Decade*, WAYS & MEANS COMM. DEMOCRATS (July 7, 2014), <http://democrats.waysandmeans.house.gov/press-release/new-crs-data-47-corporate-inversions-last-decade-2> [<http://perma.cc/Q24Z-HM6Z>] (archived Oct. 1, 2015) (“Forty-seven U.S. corporations have reincorporated overseas through corporate inversion in the last 10 years.”).

2. See DONALD J. MARPLES & JANE G. GRAVELLE, CONG. RESEARCH SERV., R43568, CORPORATE EXPATRIATION, INVERSIONS, AND MERGERS: TAX ISSUES 1 (2014) [hereinafter CRS REPORT] (noting the interest of many high-profile companies in merging with non-U.S. firms).

3. See *id.* at 2 (explaining that many of the announced mergers involve firms from the pharmaceutical industry).

that have become popular in recent years. Among some of the popular destinations for these multinational companies are Ireland, Luxembourg, the Netherlands, and the United Kingdom—all of which have developed patent box devices within the last eight years in their own efforts to forestall companies from inverting in foreign locations.⁴

Corporate inversions have not been accomplished without criticism. Both the United States and the Organization for Economic Cooperation and Development (OECD)⁵ have been critical of such policies.⁶ The United States has proposed legislation to counter these corporate inversions; however, as in the past, these provisions are reactive in nature and are destined to fail again.⁷ On the other hand, the OECD has proposed a seemingly promising plan that deals with some of the most concerning tax issues.⁸

This Note focuses on corporate inversions from the perspective of the United States, with special attention given to inversions involving technology and pharmaceutical firms since the most recent wave of inversions has been motivated by tax incentives concerning intellectual property. Part II provides background on corporate taxation and the inversion process. Part III explores the recent wave of inversions and why certain countries have benefited more than others. Ireland, Luxembourg, the Netherlands, and the United Kingdom are examined specifically because the United States can borrow the tax strategies of these countries when developing a plan to address corporate inversions. Part IV discusses current responses to corporate inversions. Part V suggests that to begin benefitting from corporate inversions, the United States should join forces with countries to support the OECD plan and also follow the movement of certain European countries that have already implemented a patent box regime.

4. Jason M. Brown, *Patent Box Taxation: A Comparison of Four Recent European Patent Box Tax Regimes and an Analytical Consideration of If and How the United States Should Implement Its Own Patent Box*, 46 INT'L L. 913, 915–16 (2012) (listing the countries that have patent box tax regimes).

5. The OECD is an international organization whose mission is to promote policies to better the economic and social well-being of people around the world. *See What We Do and How*, ORG. FOR ECON. COOPERATION & DEV. [OECD] (2015), <http://www.oecd.org/about/whatwedoandhow/> [<http://perma.cc/L9AR-UMVN>] (archived Oct. 1, 2015).

6. *See infra* Part IV (examining various reactions to corporate inversions).

7. *See infra* Part IV.A.2.

8. *See generally* ORG. FOR ECON. COOPERATION & DEV. [OECD], DEVELOPING A MULTILATERAL INSTRUMENT TO MODIFY BILATERAL TAX TREATIES (2014) [hereinafter MULTILATERAL INSTRUMENT], <http://dx.doi.org/10.1787/9789264219250-en> [<http://perma.cc/V3LW-MDGH>] (archived Oct. 1, 2015).

II. CORPORATE TAXATION AND CORPORATE INVERSIONS

Before delving into a discussion on corporate inversions, it is useful to briefly examine the background of corporate taxation. The tax system in the United States differs from tax systems found throughout the rest of the world. These differences illustrate some of the motivations behind the corporate inversion movement. Corporate inversions can be accomplished in a variety of ways, each with the goal of escaping the reach of U.S. taxation. While the most recent wave of global corporate inversions has gained much attention, this trend is certainly not the first of its kind.

A. Worldwide Versus Territorial Tax Regimes

One of the biggest differences between the tax systems of the United States and those of other countries is worldwide taxation versus territorial taxation. A worldwide tax regime taxes a domestic corporation on all of its income, whether the income is generated domestically or abroad.⁹ This tax system, though not the most common, is used by the United States.¹⁰ This means that income earned by a U.S. corporation from foreign transactions is subject to taxation both in the United States, the residence country, and in the source country where the transaction took place.¹¹ Usually corporations are not taxed on income earned abroad in foreign subsidiaries until it is paid, or repatriated, to the U.S. parent company—usually done in the form of dividends.¹² Foreign tax credits are usually allowed to offset some of the U.S. tax that a corporation would otherwise have to pay when a corporation chooses to repatriate earnings.¹³ Many multinational corporations defer this income indefinitely by leaving their profits abroad, allowing them to escape U.S. taxation.¹⁴ In a country with a worldwide tax system, foreign corporations are taxed only to the extent they earn income that originated in that country.

9. CRS REPORT, *supra* note 2, at 2 (describing the U.S. international tax system).

10. *See id.*

11. *See id.* (explaining how U.S. corporate income is taxed).

12. *Id.* at 2–3 (explaining how foreign income can be deferred until it is repatriated).

13. Orsolya Kun, *Corporate Inversions: The Interplay of Tax, Corporate, and Economic Implications*, 29 DEL. J. CORP. L. 313, 335–36 (2004) (“The United States provides a credit against U.S. income taxes for foreign income taxes paid or accrued.”).

14. Sarah Stodola, *10 Big Corporate Tax Breaks, and Who Benefits*, THE FISCAL TIMES (Feb. 9, 2011), <http://www.thefiscaltimes.com/Articles/2011/02/09/10-Big-Corporate-Tax-Breaks?page=0%2C0> [<http://perma.cc/4JZ7-BQJG>] (archived Sept. 20, 2015) (explaining that many companies leave their profits overseas indefinitely).

A more popular tax regime used by foreign countries is a territorial tax regime that imposes tax only on income derived within the geographical boundaries of that country. This system usually exempts income that is generated from outside of the home country's geographical boundaries from being taxed.¹⁵ Although many foreign countries operate under a territorial tax regime, these systems have strong provisions designed to prevent the shifting of income out of the country to evade being taxed domestically.¹⁶ Such provisions make territorial tax systems less appealing to corporations than they otherwise would be, though this is not to say that they are less appealing than a worldwide tax system.

B. Corporate Taxation in the United States

As previously noted, the United States uses a worldwide tax system.¹⁷ The current statutory corporate tax rate in the United States is 35 percent, among the highest in the world.¹⁸ Although the U.S. statutory corporate tax rate of 35 percent is quite high when compared to other companies, the effective rate is well below 35 percent—sometimes as low as 13 to 17 percent due to certain available tax breaks.¹⁹ For instance, research and experimentation tax credits are highly beneficial to technology and pharmaceutical companies.²⁰

Being subject to a worldwide taxation scheme may be extremely disadvantageous to corporations competing globally. The United States has chosen to provide foreign tax credits as a way to alleviate some of the competitive disadvantage that companies incorporated in the United States may experience—foreign income taxes paid or accrued are credited against U.S. income taxes.²¹ This credit

15. See Tyler M. Dumler, *Charging Less to Make More: The Causes and Effects of the Corporate Inversion Trend in the U.S. and the Implications of Lowering the Corporate Tax Rate*, 13 U.C. DAVIS BUS. L.J. 88, 91 (2012) (explaining that a territorial tax system does not tax income generated from foreign sources).

16. Alexandra Thornton, *The Skinny on Corporate Inversions*, CTR. FOR AM. PROGRESS (Sept. 25, 2014), <https://www.americanprogress.org/issues/tax-reform/report/2014/09/25/97827/the-skinny-on-corporate-inversions/> [<http://perma.cc/4TUW-KG5V>] (archived Sept. 20, 2015) (“[T]hese systems have strong provisions to prevent domestic companies from shifting income.”).

17. See CRS REPORT, *supra* note 2, at 2.

18. See Kyle Pomerleau, *Corporate Income Tax Rates Around the World, 2014*, TAX FOUND. (Aug. 20, 2014), <http://taxfoundation.org/article/corporate-income-tax-rates-around-world-2014> [<http://perma.cc/4D4X-RUY4>] (archived Oct. 3, 2015) (listing the highest corporate tax rates in the world).

19. Thornton, *supra* note 16 (noting the United States' effective tax rate).

20. Stodola, *supra* note 14 (listing pharmaceutical and high tech companies as being among those that benefit from research and experimentation tax credits).

21. Derek E. Anderson, *Turning the Corporate Inversion Transaction Right Side Up: Proposed Legislation in the 108th Congress Aims to Stamp Out Any Economic*

alleviates the double taxation of foreign-source income without eliminating the tax on domestic-source income.²² This foreign tax credit is limited to the amount of U.S. tax liability on foreign-source income, which is determined by U.S. tax law.²³ Although these tax credits prevent double taxation, the overall tax paid on foreign investments may still be higher for U.S. corporations when compared to that of their competitors.²⁴

To illustrate, let us assume that there is a multinational corporation, A-Corp, incorporated in the United States, that generates \$100 million from its operations in Ireland. Under the worldwide tax regime, A-Corp will be subject to Irish taxation (12.5 percent) as well as U.S. corporate taxation (35 percent) minus any foreign credits received for the initial Irish taxation for any income derived in Ireland. Therefore, A-Corp would owe \$12.5 million (12.5 percent \times \$100 million) in taxes to the Irish government. The U.S. government would then credit A-Corp for this amount and collect the difference between the taxable amount under the U.S. tax rate of 35 percent and the amount credited. Thus, A-Corp would owe the U.S. government \$22.5 million ((35 percent \times \$100 million) – \$12.5 million) in taxes. This does not include the corporate tax that this corporation would owe the state in which it is incorporated. Assuming the average state corporate tax rate in the United States of 4.1 percent, another \$4.1 million (4.1 percent \times \$100 million) in state corporate tax would be owed. This results in a grand total of \$39.1 million in taxes from the A-Corp's \$100 million worth of operations in Ireland.

Now let us assume there is another multinational corporation, B-Corp, incorporated in a territorial tax jurisdiction that also generates \$100 million from its operations in Ireland. B-Corp would only have to pay 12.5 percent of the \$100 million of income, resulting in a total amount of tax paid of \$12.5 million. Through this simplified example, it is easy to recognize the advantage that B-Corp has over A-Corp for being subject to a territorial tax system instead of a worldwide tax system.

C. The Corporate Inversion Transaction

A corporate inversion is the process of a U.S.-based multinational corporation reincorporating in a foreign jurisdiction,

Vitality of the Corporate Inversion Transaction, 16 FLA. J. INT'L L. 267, 281 (2004) ("Foreign credits are one way that the U.S. government has chosen to deal with this competitive disadvantage."); Kun, *supra* note 13, at 335 (explaining the foreign tax credit).

22. Kun, *supra* note 13, at 335–36 ("The foreign tax credit mitigates the double taxation of foreign-source income without offsetting the tax on U.S.-source income.")

23. *Id.* at 336 (describing the constraints of the tax credit).

24. Anderson, *supra* note 21, at 281 ("[T]he U.S. corporations are still paying a full amount of tax on their foreign investments, and foreign corporations are not.")

often doing so to reduce its tax burden.²⁵ The core element of the transaction is the establishment of the original U.S. corporation as a subsidiary of a foreign parent corporation.²⁶ Although corporations renounce their U.S. citizenship by executing a corporate inversion, they are not required to relocate their business operations.²⁷ On the contrary, the business operations of these corporations remain in the United States while benefiting from lower foreign tax systems.²⁸

After a corporation inverts, it is no longer subject to the U.S. worldwide taxation regime.²⁹ The corporation saves money because any income earned in a foreign country by the new foreign corporation is taxed according to that country's tax code rather than the U.S. worldwide tax regime.³⁰ Additionally, the corporation retains its U.S. corporate status and the benefits such status provides.³¹ On the other hand, the switch in jurisdiction changes the laws governing the fiduciary duties of corporate officers and directors.³²

The corporate inversion transaction takes three main forms: (1) a share inversion, (2) an asset inversion, or (3) a combined inversion.³³ "[A]n inversion transaction can be costly because of legal, accounting, and banking fees."³⁴ Inversions may also be costly to shareholders, as realizing any capital gains would trigger tax liabilities for the shareholders.³⁵ Shareholders are usually compensated for these taxes in the form of higher stock prices, as evidenced in studies showing a significant increase in stock prices for companies announcing inversions.³⁶

A share transaction is one in which the foreign corporation acquires all of the stock of the domestic inverting corporation, making

25. *Corporate Inversion*, INVESTOPEDIA, <http://www.investopedia.com/terms/c/corporateinversion.asp> [<http://perma.cc/348Q-82DT>] (archived Sept. 20, 2015) (defining corporate inversion).

26. See Kun, *supra* note 13, at 319 (describing the form of the corporate inversion transaction).

27. Anderson, *supra* note 21, at 269 (explaining how corporate inversions abuse the purpose of treaties).

28. *Id.* ("[T]heir business operations remain in the United States while they take advantage of more friendly foreign tax regimes.").

29. Kun, *supra* note 13, at 313 (explaining the consequences of a corporate inversion).

30. Anderson, *supra* note 21, at 280 (explaining how corporate inversions lead to savings).

31. Kun, *supra* note 13, at 313 (describing the basics of a corporate inversion transaction).

32. *Id.* (noting some of the consequences of corporate inversion transactions).

33. *Id.* at 319 (explaining the different forms a corporate inversion can take).

34. Eloine Kim, *Corporate Inversion: Will the American Jobs Creation Act of 2004 Reduce the Incentive to Re-Incorporate?*, 4 J. INT'L BUS. & L. 152, 158 (2005) (listing some expenses associated with a corporate inversion transaction).

35. See *id.* (explaining that shareholders may be subjected to tax liabilities).

36. See *id.* (noting how stock prices generally increase after the announcing an inversion).

the domestic corporation a subsidiary of the new foreign parent corporation.³⁷ The shareholders are then given stock of the new foreign parent corporation as compensation for their stock of the domestic corporation.³⁸ This does not require any relocation of the business operations and is often viewed as a transaction that occurs only on paper.³⁹ Triangular mergers, for example, are often used to execute share inversions.⁴⁰

An asset transaction is one in which the inverting corporation exchanges its assets for stock in the new foreign parent corporation.⁴¹ An asset inversion is a “complete corporate restructuring that replaces the former U.S. parent [corporation],” through liquidation, with the new foreign parent corporation.⁴² The U.S. Corporation becomes a subsidiary of the foreign corporation, resulting in the shareholders owning stock in the foreign corporation.⁴³

A drop-down transaction, sometimes called a combined inversion, uses a mixture of both asset and stock transactions.⁴⁴ In this scenario, assets are transferred to the new foreign parent in exchange for stock, with the foreign parent transferring some of those assets back to a domestic subsidiary.⁴⁵ As a result, the original U.S. corporation no longer exists, and shareholders end up holding the same amount of stock in the new foreign corporation as they held in the former U.S. corporation.⁴⁶ Regardless of the method used, the goal is to create a new foreign parent so that the domestic corporation is subject to a foreign tax regime, rather than to the U.S. worldwide tax regime.⁴⁷

D. Reasons for Inverting

Corporations that choose to invert may provide a wide variety of justifications, such as “increased operational flexibility, better cash management, and access to international capital markets.”⁴⁸ However, the U.S. Treasury Department considers these rationales to

37. Harvard Law Review Ass'n, VI. *Drawing Lines Around Corporate Inversion*, 118 HARV. L. REV. 2270, 2273 (2005) (discussing share transactions).

38. *Id.* (explaining how a share transaction works).

39. Anderson, *supra* note 21, at 278 (discussing the stock exchange transaction).

40. *See* Kun, *supra* note 13, at 320 (noting the use of triangular mergers).

41. Harvard Law Review Ass'n, *supra* note 37, at 2273.

42. *See* Kun, *supra* note 13, at 322 (explaining asset inversions).

43. Kim, *supra* note 34, at 161.

44. *See* Harvard Law Review Ass'n, *supra* note 37, at 2273.

45. CRS REPORT *supra* note 2, at 3 n.16 (describing drop-down inversions).

46. Kim, *supra* note 34, at 161.

47. Anderson, *supra* note 21, at 280 (noting the purpose of corporate inversion transactions).

48. Kim, *supra* note 34, at 153 (listing reasons corporations claim to invert).

be superficial, finding that the true motivation is to escape tax liability.⁴⁹ Whatever the true motivation for inverting may be, it cannot be denied that corporations can significantly reduce their tax liability by inverting.

The United States is a desirable place to incorporate due to its large consumption market and corporate protections.⁵⁰ At one time, these qualities allowed the United States to charge multinational corporations higher corporate tax rates than other countries without the worry of companies incorporating elsewhere.⁵¹ While these incentives may still exist, the appeal to incorporate in the United States has faded. While many OECD countries have lowered their corporate tax rates over the past few decades, the United States has maintained a corporate tax rate of 35 percent.⁵² Although competing multinational corporations face similar taxation on income generated within the United States, the income generated in foreign countries is not taxed equally.⁵³ This may place U.S. corporations at a competitive disadvantage with respect to tax burdens, motivating U.S. corporations to use corporate inversion transactions to escape the burden of the United States' worldwide tax regime.⁵⁴ This is also why many of the corporations that choose to invert often have large foreign profits, as these corporations have the most to gain from escaping a worldwide tax system.

While politicians in the United States may describe companies that invert as unpatriotic or deserters,⁵⁵ corporate officers and boards of directors have a duty to the shareholders, which is independent of national loyalty.⁵⁶ According to a study conducted by the University of Chicago, corporate inversions occurring "between 1993 and 2013 outperformed the market average in the years following the transactions."⁵⁷ With respect to shareholders, directors may have a

49. See *id.* (noting that the U.S. Treasury Department sees these reasons as pretext).

50. Dumler, *supra* note 15, at 96–97 (noting the United States' enormous consumption market).

51. *Id.* (explaining that the United States can arguably charge multinational corporations higher taxes than other countries).

52. See *id.* at 90–91, 96–97 (comparing corporate tax rates).

53. *Id.* at 98 (noting the taxes faced by multinational corporations).

54. See Anderson, *supra* note 21, at 269–70 (explaining why corporations may choose to invert).

55. Brian Faler, *Obama Blasts 'Corporate Deserters'*, POLITICO (July 24, 2014, 6:29 PM), <http://www.politico.com/story/2014/07/obama-corporate-deserters-taxes-109357.html> [<http://perma.cc/6LBW-YWMS>] (archived Sept. 20, 2015) (reporting that President Obama and other lawmakers consider those companies who invert to be "deserters").

56. See Harvard Law Review Ass'n, *supra* note 37, at 2279 (noting that a director's responsibilities lie with his or her shareholders).

57. Brooke Sutherland, *Investors Cheer, U.S. Jeers at Tax-Driven Deals: Real M&A*, BLOOMBERG BUS. (June 17, 2014, 3:42 PM), <http://www.bloomberg.com/>

hard time justifying a decision to remain incorporated in the United States when they could invert and potentially save millions of dollars in taxes that could then be passed along to shareholders.

Many of the tax benefits from inversions are a result of post-inversion techniques such as income shifting.⁵⁸ Income shifting refers to any technique by which a multinational corporation is able to have income generated in one jurisdiction reported in another jurisdiction offering lower corporate taxation.⁵⁹ The income is shifted through inter-company payments often taking the form of management fees, licensing fees or royalties.⁶⁰ Income shifting has gained the attention of both lawmakers in the United States and the OECD.⁶¹

Earnings stripping, a common income shifting technique, occurs when a corporation pays excessive interest amounts to related third parties as a way to reduce its taxable income.⁶² In one earnings stripping technique, the U.S. corporation makes a payment on a loan created by its foreign parent, creating interest that is fully deductible as a business expense.⁶³ The U.S. corporation could also make royalty, management or administrative expense payments to the foreign parent corporation, which would be considered deductible payments.⁶⁴

E. Prior Waves of Inversions

1. The McDermott Transaction

The McDermott, Inc. corporate inversion transaction was one of the first corporate inversions to gain much attention from the Internal Revenue Service (IRS).⁶⁵ McDermott, Inc. performed a stock exchange with McDermott International, a Panamanian corporation.⁶⁶ The McDermott inversion was motivated by the substantial tax savings the company believed it would achieve by

news/articles/2014-06-16/investors-cheer-u-s-jeers-at-tax-driven-deals-real-m-a [http://perma.cc/SQ6E-LA52] (archived Sept. 20, 2015) (describing the positive returns for corporations that have inverted).

58. See Kim, *supra* note 34, at 162.

59. Omri Marian, *The Function of Corporate Tax-Residence in Territorial Systems*, 18 CHAP. L. REV. 157, 177 (2014) (discussing income shifting).

60. See Kun, *supra* note 13, at 338 (explaining how income shifting works).

61. See Marian, *supra* note 59, at 178 (noting the criticism that income shifting has drawn).

62. *Earnings Stripping Law and Legal Definition*, USLEGAL.COM (2015), <http://definitions.uslegal.com/e/earnings-stripping/> [http://perma.cc/2JDE-6Q9S] (archived Oct. 5, 2015).

63. Anderson, *supra* note 21, at 281 (discussing earnings stripping techniques).

64. *Id.* at 281–82.

65. Anderson, *supra* note 21, at 275 (discussing the McDermott transaction).

66. *Id.* (explaining the McDermott merger).

removing its foreign earnings from the reach of the U.S. corporate tax system.⁶⁷

The inversion provoked Congress to enact § 1248(i) of the Internal Revenue Code, which requires shareholders of U.S. corporations to recognize gains from these stock exchanges on their individual income taxes.⁶⁸ Under § 1248(i), the receipt of a foreign subsidiary's stock in such a transaction is treated like a taxable distribution.⁶⁹ However, one can avoid this gain recognition by "exchanging the U.S. corporation's stock for stock in a newly formed foreign subsidiary with no earnings and profits."⁷⁰

By enacting I.R.C. § 163(j), Congress attempted to "prevent earnings stripping through foreign related-party debt."⁷¹ This section prohibits deductions of inter-company interest payments made to entities that are not under U.S. taxation if the deductions exceed 50 percent of the company's adjusted taxable income.⁷² This section functions to prevent U.S. corporations from leveraging a corporation for the purposes of reducing its taxable income.⁷³ However, corporations with a debt-to-equity ratio of less than 1.5 to 1 are not subject to this rule.⁷⁴

2. The Helen of Troy Transaction

The second cycle of corporate inversions began when Helen of Troy⁷⁵ inverted into a Bermuda corporation in 1994 with the desire to be subjected to a lower effective tax rate and enhance stockholder value.⁷⁶ This was the first "pure" inversion, meaning the corporation inverted to a foreign nation in which it had no previous relationship.⁷⁷ The IRS responded to this inversion by issuing new regulations under § 367(a) of the Internal Revenue Code to make "the transfer of stock or securities of a domestic corporation by a U.S. person to a foreign corporation" taxable if the transferors own, in the

67. Joseph A. Tootle, Note, *The Regulation of Corporate Inversions and "Substantial Business Activities"*, 33 VA. TAX REV. 353, 364 (2013) (explaining the motivation behind the McDermott inversion).

68. See 26 U.S.C. § 1248(i) (2015).

69. See *id.*

70. Tootle, *supra* note 67, at 365 (describing how to get around § 1248(i)).

71. Harvard Law Review Ass'n, *supra* note 37, at 2282 (explaining Congress's motivation); see also 26 U.S.C. § 163(j) (2015).

72. See 26 U.S.C. § 163(j).

73. Kim, *supra* note 34, at 163 (explaining the effect of § 163(j)).

74. See 26 U.S.C. § 163(j).

75. Helen of Troy is a publicly traded corporation founded in El Paso, Texas, operating primarily in the personal care products industry.

76. Kun, *supra* note 13, at 316 (discussing the Helen of Troy inversion).

77. Tootle, *supra* note 67, at 366 (noting the uniqueness of the Helen of Troy inversion).

aggregate, a majority of the corporation.⁷⁸ Under these regulations, shareholders of inverting corporations were required to recognize gain (but not loss) on the inversion transaction.⁷⁹ The gain was valued as the difference between the fair market value of their shares and the adjusted bases in those shares.⁸⁰

3. Late 1990s and Early 2000s Wave

Corporate inversions gained notoriety in the late 1990s and 2000s as a wave of corporations sought to reduce their tax burdens.⁸¹ Bermuda and the Cayman Islands were popular destinations for parent corporations involved in corporate inversions, likely because these countries have no corporate income tax and yet are still believed to have “highly developed legal, institutional, and communications infrastructures.”⁸² This wave of inversions, unlike the McDermott and Helen of Troy transactions, attracted attention from the popular press, drawing strong public criticism.⁸³

In May 2002, the Department of Treasury published a report identifying three main concerns about corporate inversions: (1) erosion of the U.S. tax base, (2) a cost advantage for foreign-controlled firms, and (3) a reduction in perceived fairness of the system.⁸⁴ These concerns, coupled with the growing attention that corporate inversions were receiving, led to the American Jobs Creation Act of 2004, which intended to limit inversions to those that are legitimate and not enacted solely for tax purposes.⁸⁵ The American Jobs Creation Act of 2004 was promulgated in § 7874 of the Internal Revenue Code and applies to transactions taking place after March 4, 2003.⁸⁶

The American Jobs Creation Act contains two alternative tax regimes applicable to inversions.⁸⁷ The first tax regime applies when the new foreign parent company is owned by at least 80 percent of the former parent’s stockholders.⁸⁸ In this case, the inverted foreign parent company is treated as if it were a domestic corporation,

78. 26 C.F.R. § 1.367(a)–3(c)(1) (2014); Kun, *supra* note 13, at 316 (citing 26 U.S.C. § 367(a) (2015)).

79. Tootle, *supra* note 67, at 366 (explaining the impact of the statute).

80. *See id.* (describing the effect of the statute).

81. CRS REPORT, *supra* note 2, at 5 (explaining the media attention with this wave of inversions).

82. *See id.* (noting popular destinations).

83. Tootle, *supra* note 67, at 367 (noting the media attention).

84. CRS REPORT, *supra* note 2, at 6.

85. *See id.* (detailing the impetus for the new Act).

86. 26 U.S.C. § 7874 (2015).

87. *Id.*

88. *Id.*

basically as if the inversion had never happened.⁸⁹ The second regime applies when the continuity of ownership is less than 80 percent but at least 60 percent.⁹⁰ These types of inversions are referred to as limited inversions and are subject to more lenient sanctions than those accompanying the first type of inversions discussed.⁹¹ Under this second regime, the new foreign parent is not treated like a domestic corporation, but the corporation cannot use foreign tax credits or net operating losses to offset any U.S. taxes on gains (i.e., “toll taxes”) that apply to transfers of assets to the new entity.⁹² The American Jobs Creation Act also created an exemption for corporations with substantial business activity in a foreign country when compared to their total business activities.⁹³

Congress did not define “substantial” and instead opted to defer to the Treasury Department to interpret the meaning of substantial business activities.⁹⁴ To help clarify this issue, the Treasury Department issued temporary regulations in 2006.⁹⁵ Two tests were established to determine whether a company qualified for the substantial business activities exception: (1) a facts and circumstances test and (2) a bright-line safe harbor test.⁹⁶ The facts and circumstances test determines whether an inverted corporation has substantial business activities in a foreign nation by considering all the facts and circumstances of each case.⁹⁷ For further guidance, the regulations provided a nonexclusive list of factors to be considered and examples of activities that would satisfy the test.⁹⁸ The safe harbor test stated that, generally, if at least 10 percent of a corporation’s employees, assets, and sales were located in a foreign country, it would be considered to have substantial business activities in that country.⁹⁹ The bright-line safe harbor test was eventually dismantled by regulations in 2009, and “the examples that illustrated the application of the facts and circumstances test were also removed.”¹⁰⁰ A new set of regulations was implemented in 2012, which replaced the former facts and circumstances test with a new bright-line test.¹⁰¹ A corporation did not satisfy the new bright-line test unless “at least 25 % of its group employees [(both in terms of the

89. *Id.*

90. *Id.*

91. Kim, *supra* note 34, at 164 (describing limited inversions).

92. *See id.*

93. *See id.* (noting the substantial business activity exemption).

94. Tootle, *supra* note 67, at 371.

95. *Id.* at 378–79 (discussing the 2006 temporary regulations).

96. *Id.*

97. *Id.*

98. *Id.* at 379.

99. *Id.*

100. *Id.* at 379–80 (discussing the 2009 temporary regulations).

101. *Id.* at 384 (discussing the 2012 temporary regulations).

number of employees and their compensation)], group assets, and group income are located or derived in that country."¹⁰²

III. THE RECENT WAVE OF INVERSIONS AND PATENT BOXES AS A TOOL FOR COMPETITION

Following the enactment of the American Jobs Creation Act of 2004, companies desiring to invert for tax benefits and retain control of the business had two options: (1) qualify for the business activity exemption or (2) merge with a smaller company.¹⁰³ The business activity exemption required the corporation to have significant economic activity in the target country. This led to a trend in inversions away from countries like Bermuda and the Cayman Islands, to larger countries with substantial economic activity like Ireland, Luxembourg, the Netherlands, and the United Kingdom.¹⁰⁴

These countries also have favorable tax treaties with the United States with respect to intellectual property. The extensive bilateral tax-treaty networks of these countries eliminate any worry of double taxation.¹⁰⁵ Luxembourg, the Netherlands, and Ireland all have treaties with the United States that are favorable for companies owning large values of intellectual property. This stems from three common characteristics of their treaty agreements: (1) zero percent withholding tax, (2) low corporate tax rate on royalties, and (3) less restrictive limitation on benefits (LOB) provisions than newer treaties.¹⁰⁶ These features demonstrate the advantageous tax treatment of income derived from intellectual property in these countries. This treatment has allowed these countries to attract companies, especially those in the technology and pharmaceutical industries, using tax incentive schemes such as patent boxes.

Therefore, an examination into the tax strategies of these countries is valuable, as the United States could emulate similar tactics to curb more inversions to foreign countries or even attract foreign companies to re-incorporate in the United States.

102. *See id.*

103. *See Kim, supra* note 34, at 164 (explaining the substantial business exemption).

104. CRS REPORT, *supra* note 2, at 6 (discussing post-2004 inversions).

105. *See* GRANT THORNTON INT'L LTD., A GUIDE TO BUSINESS RELOCATION IN EUROPE 4 (2011) [hereinafter GUIDE TO RELOCATION], <http://www.grant-thornton.ch/files/gti%20business%20relocation%20a5%20f.pdf> [<http://perma.cc/NM7G-BBF4>] (archived Oct. 5, 2015) (noting the number of double tax treaties in various countries).

106. *See id.* at 5 (describing various IP regimes).

A. Overview of Patent Boxes

A very large portion of the recent wave of corporate inversions has involved companies in the technology and pharmaceutical industries, which hold large amounts of intellectual property. One reason for this is the development of the patent box, a tax incentive tied to intellectual property that has been developed by certain European countries over the last eight years. Though patent boxes have attracted some criticism, they are legal under EU law as long as they do not amount to illegal state aid.¹⁰⁷

In general, a patent box is a tax incentive that grants a lower tax rate to income earned from intellectual property; however, its specific definition may vary by jurisdiction.¹⁰⁸ Patent boxes are also known as “innovation boxes,” a term that better expresses the broad scope of the intellectual property covered under the tax incentive.¹⁰⁹ Not only does the scope of what qualifies as intellectual property differ from country to country, but the incentives also offered differ.¹¹⁰ For example, the patent box tax rate is 5 percent in the Netherlands, 10 percent in the United Kingdom, and 15 percent in France and Spain.¹¹¹ Specific details of this tax incentive scheme are discussed in the remainder of this Part.

B. Ireland

Ireland introduced corporate taxes in 1976.¹¹² The distinguishing characteristic of the current Irish corporate tax system is the relatively low rate of 12.5 percent, first applied on January 1, 2003.¹¹³ One aim of the low tax rate was to attract inward investment to Ireland.¹¹⁴ Ireland’s transition from one of the poorest countries in Western Europe to one of the wealthiest, earning itself the nickname

107. Suzanne Lynch, *Controversy Over ‘Double Irish’ Raises Issue of EU’s Power Over Tax Regimes*, THE IRISH TIMES (Oct. 17, 2014), <http://www.irishtimes.com/business/economy/controversy-over-double-irish-raises-issue-of-eu-s-power-over-tax-regimes-1.1966394> [<http://perma.cc/B3SW-T2TC>] (archived Oct. 5, 2015) (discussing the legality of patent boxes).

108. W. Wesley Hill, *The Patent Box as the New Innovation Incentive for the Several States: Lessons from Intellectual Property–Tax Competition*, 42 AIPLA Q.J. 13, 16 (2014).

109. See Brown, *supra* note 4, at 921–22 (describing the Dutch Innovation Box).

110. See *id.* (noting the wide range of patent boxes).

111. *Id.* (listing examples of patent box tax rates).

112. AIDAN WALSH & CHRIS SANGER, THE HISTORICAL DEVELOPMENT AND INTERNATIONAL CONTEXT OF THE IRISH CORPORATE TAX SYSTEM 2, 5 (2014), http://www.budget.gov.ie/Budgets/2015/Documents/EY_Historical_Dev_International_Context_Irish_%20Corporation_Tax.pdf [<http://perma.cc/Q388-8NEB>] (archived Oct. 5, 2015).

113. *Id.*

114. *Id.* at 2 (explaining the motivation behind Ireland’s tax policy).

of the “Celtic Tiger,” is evidence that its low tax rate has been lucrative.¹¹⁵ The investments in Ireland produced by inversions have arguably helped to soften the blow of the property and banking crash that struck in 2008.¹¹⁶

Ireland is a popular destination for many pharmaceutical companies; nine out of the top ten largest global pharmaceutical companies, as well as many leading technology companies, have opened operations in Ireland.¹¹⁷ Ireland is attractive to the pharmaceutical industry for several reasons: a low corporate tax, a strong industry presence, a legal infrastructure similar to that of the United States, and an increasingly competent workforce.¹¹⁸ The income-shifting technique discussed in Part II is easy to use in the technology or pharmaceutical industries, where patents are often used and valuable to corporations.¹¹⁹ While a patent could be developed in the labs of a corporation residing in a high-tax jurisdiction, it is easy for the patent to then be legally owned by an affiliate corporation residing in a jurisdiction that is considered a tax haven.¹²⁰ Technology goliaths like “Microsoft, Hewlett Packard, Dell, Intel, Oracle, and Google,” all of which have organized subsidiaries in Ireland, commonly use this practice.¹²¹

Ireland technically uses a worldwide tax system, although the system can sometimes operate like a territorial system due to the country’s unique interpretation of the term “resident.”¹²² Corporations that are residents of Ireland are taxed on their income wherever in the world it derives—like a worldwide tax system.¹²³ Similar to the United States, foreign tax credits are given for any foreign tax paid on profits before they arrived in Ireland.¹²⁴ Non-Irish

115. See Yoram Margalioth, *Taxing Multinationals: Policy Analysis with a Focus on Technology*, 1 BRIT. TAX REV. 97, 107 (2011) (explaining Ireland’s rise out of poverty).

116. Tom Fairless, *EU to Investigate Corporate Tax Codes in Ireland, Luxembourg, Netherlands*, WALL STREET J. (June 10, 2014), <http://www.wsj.com/articles/eu-to-investigate-corporate-tax-codes-in-ireland-luxembourg-netherlands-1402441870> [<http://perma.cc/6YWS-WVLV>] (archived Oct. 5, 2015) (explaining Ireland’s struggle to recover from the crash of 2008).

117. Vanessa Houlder et al., *Tax Avoidance: The Irish Inversion*, FIN. TIMES (April 29, 2014, 5:47 PM), <http://www.ft.com/intl/cms/s/2/d9b4fd34-ca3f-11e3-8a31-00144feabdc0.html#axzz3NnaCKIWO> [<http://perma.cc/TJ3L-8LQT>] (archived Sept. 20, 2015) (noting the large number of pharmaceutical companies that have inverted to Ireland).

118. See *id.* (explaining what is attractive about Ireland).

119. See *supra* Part II.

120. Marian, *supra* note 59, at 177–78 (discussing the ease with which intellectual property can be used to avoid taxation).

121. See Hill, *supra* note 108, at 21 (listing some of the companies that have inverted to Ireland).

122. See WALSH & SANGER, *supra* note 112, at 8, 18.

123. *Id.*

124. See *id.* at 8.

resident corporations are taxed only on Irish-source income—like a territorial tax system.¹²⁵ Under Irish law, a corporation is a resident if it is managed and controlled in Ireland or, in certain circumstances, if it is incorporated in Ireland.¹²⁶ This definition, which differs from the United States, has allowed corporations to use certain tactics to reduce taxation, such as the “double Irish,” discussed in further detail below. This is because residents are taxed on worldwide profits while nonresidents are taxed only on Irish-source income.¹²⁷

One popular scheme that had been used by corporations to reduce their tax burden was the double Irish structure.¹²⁸ This strategy was used to move profits from Ireland to countries like Bermuda that have no corporate tax by taking advantage of the different definitions of residence in the U.S. and Irish tax codes.¹²⁹ Ireland taxes companies based on where they operate out of, while the United States taxes companies based on where they are registered.¹³⁰ Corporations with operations in Ireland could make royalty payments for intellectual property to a separate Irish-registered subsidiary that is physically located in a country like Bermuda, where the corporate income tax is zero.¹³¹ Through this technique, corporations are able to cut their effective tax rate below the already low 12.5 percent corporate tax rate, sometimes down to as low as 2 percent.¹³² Technology and pharmaceutical companies were the main actors using this technique because they could shift, with relative ease, large portions of their income by assigning intellectual property rights abroad. One company that has taken advantage of the double Irish is Google, which holds “intellectual property in an Irish company that is tax-resident in Bermuda.”¹³³ Google reportedly saved over \$3 billion in 2010 through the use of the double Irish.¹³⁴ Facebook has also taken advantage of this structure, moving more than \$700 million to the Cayman Islands through the double Irish

125. *Id.* at 3.

126. See Irish Tax and Customs, REVENUE (Sept. 2012) <http://www.revenue.ie/en/tax/ct/basis-charge.html> [<http://perma.cc/PY6H-EZ99>] (archived Nov. 13, 2015).

127. See WALSH & SANGER, *supra* note 112, at 3.

128. See Houlder et al., *supra* note 117 (discussing the double Irish).

129. *Id.*

130. Marlene Y. Satter, *Closing Irish Tax Loophole May Spook Corporations but Not Economy*, THINKADVISOR (Nov. 6, 2014), http://www.thinkadvisor.com/2014/11/06/closing-irish-tax-loophole-may-spook-corporations?page_all=1 [<http://perma.cc/7R6F-Z5A2>] (archived Sept. 20, 2015) (explaining taxation in Ireland).

131. See *Death of the Double Irish*, ECONOMIST (Oct. 18, 2014), <http://www.economist.com/news/finance-and-economics/21625876-irish-government-plans-alter-one-its-more-controversial-tax> [<http://perma.cc/UH6J-AJ52>] (archived Sept. 20, 2015) (explaining the effect of the double Irish).

132. *Id.*

133. Houlder et al., *supra* note 117.

134. Hill, *supra* note 108, at 17–18.

structure.¹³⁵ Industries with large intellectual property portfolios stood to benefit the most from this strategy, which was one reason why many of these companies chose to invest in Ireland.¹³⁶

On October 14, 2014, Irish Finance Minister Michael Noonan announced that Ireland would be closing the double Irish loophole.¹³⁷ Though Ireland's 12.5 percent corporate tax rate will remain in place, as of January 1, 2015, companies incorporated in Ireland will be considered tax residents in Ireland.¹³⁸ The closing of the double Irish loophole is reported to be the result of pressure from the European Union and the U.S. government to discontinue the practice.¹³⁹ Notably, the closing of the double Irish also contains a grandfather provision, which allows existing corporations using the double Irish strategy to keep those arrangements for six more years.¹⁴⁰ This could potentially impact a great number of companies, considering at least 249 companies used the double Irish provision in 2012.¹⁴¹

With the closing of the double Irish loophole, the government also announced it would introduce its own patent box, formally known as a "knowledge development box."¹⁴² This tax benefit allows firms to pay a lower tax rate on profits from intellectual property booked¹⁴³ in Ireland.¹⁴⁴ Therefore, although technology and pharmaceutical companies may be losing benefits with the closing of the double Irish, Ireland hopes to retain these companies using

135. Robert W. Wood, *Ireland Corks Double Irish Tax Deal, Closing Time for Apple, Google, Twitter, Facebook*, FORBES (Oct. 14, 2014, 2:37 AM), <http://www.forbes.com/sites/robertwood/2014/10/14/ireland-corks-double-irish-tax-deal-closing-time-for-apple-google-twitter-facebook/print/> [http://perma.cc/9H8X-QPU6] (archived Sept. 20, 2015).

136. See Joe Harpaz, *Will Irish Tax Law Change Stop Corporate Inversions?*, FORBES (Oct. 15, 2014, 3:44 PM), <http://www.forbes.com/sites/joeharpaz/2014/10/15/will-irish-tax-law-change-stop-corporate-inversions/> [http://perma.cc/6EM4-TF2G] (archived Sept. 20, 2015) (explaining why intellectual property holding companies benefited most from the double Irish).

137. Sam Schechner, *Ireland to Close 'Double Irish' Tax Loophole*, WALL STREET J. (Oct. 14, 2014), <http://www.wsj.com/articles/ireland-to-close-double-irish-tax-loophole-1413295755> [http://perma.cc/5VM9-99RH] (archived Sept. 20, 2015).

138. *Id.*

139. See Cory Hester, *Irish Tax Loophole Used by Some U.S. Companies to Be Phased Out*, WESTLAW MERGERS & ACQUISITIONS DAILY BRIEFING, 2014 WL 5285823 (Oct. 17, 2014).

140. Schechner, *supra* note 137 (discussing the window of compliance).

141. Caelainn Barr & Theo Francis, *Ireland Moves to Close One Tax Break and Opens Another*, WALL STREET J. (Nov. 4, 2014), <http://www.wsj.com/articles/ireland-closes-one-tax-break-and-opens-another-1415149644> [http://perma.cc/NP29-JAEU] (archived Sept. 20, 2015).

142. *Death of the Double Irish*, *supra* note 131.

143. "Booking profits" is a term used to describe when and where profits are declared for accounting purposes.

144. *Death of the Double Irish*, *supra* note 131 (explaining the knowledge development box).

attractive incentives such as the newly announced “knowledge development box.”

C. Luxembourg

Luxembourg is also a popular destination for companies contemplating inversion. The country has a very stable economy and political environment with a pro-business government.¹⁴⁵ Like Ireland, it is also home to a large pool of highly skilled, multilingual employees.¹⁴⁶ Another enticing factor is Luxembourg’s central location within the European Union, which facilitates mobility.¹⁴⁷

Luxembourg introduced its patent box in December 2007.¹⁴⁸ Its scheme allows any Luxembourg taxpaying entity to exclude 80 percent of net income derived from intellectual property from its taxes.¹⁴⁹ This exclusion results in an effective patent box tax rate of 5.76 percent, making it among one of the lowest rates in the world.¹⁵⁰ The patent box (also known as the IP box) applies to a wide range of intellectual property, including patents, trademarks, designs, domains names, models, and software copyrights.¹⁵¹ The patent box also applies to both self-developed intellectual property and acquired intellectual property rights, absent a requirement of any additional development.¹⁵² Additionally, the patent box applies to a broad range of intellectual property income, including ordinary intellectual property income, embedded income, and capital gains income from the sale of intellectual property rights.¹⁵³

D. The Netherlands

The Netherlands has a rich history of international trade,¹⁵⁴ evidenced by its extensive networks of treaties, which eliminates concerns of double taxation.¹⁵⁵ Additionally, the Netherlands has

145. See GUIDE TO RELOCATION, *supra* note 105, at 33.

146. See *id.*

147. See *id.*

148. Brown, *supra* note 4, at 918 (discussing Luxembourg’s patent box).

149. *Id.*

150. See *id.* at 918–19.

151. *Id.* at 919.

152. *Id.*

153. *Id.* at 919–20.

154. PWC, DOING BUSINESS IN THE NETHERLANDS 14 (2014), http://www.pwc.nl/nl_NL/nl/assets/documents/pwc-rapport-doing-business-in-the-netherlands.pdf [<http://perma.cc/4G73-CFBK>] (archived Sept. 20, 2015) (noting the Netherlands’ history of being a trading nation).

155. See GUIDE TO RELOCATION, *supra* note 105, at 4 (showing the number of bilateral treaties that various countries have).

favorable rules on corporate governance and board structure, making it a desirable destination for corporate inversions.¹⁵⁶

The Netherlands originally enacted a patent box in 2007 but later revised it in 2010.¹⁵⁷ One purpose of the revision was to lower the effective patent box tax rate to 5 percent, making it the lowest patent box tax rate in the world.¹⁵⁸ At the same time, the Dutch government removed the maximum applicable amount of the regime and changed the name of the patent box to the Dutch Innovation Box.¹⁵⁹ The innovation box applies to patents and all innovations and activities to which R&D declaration is issued.¹⁶⁰ The box does not apply to trade names, brands or logos.¹⁶¹ Unlike the scheme in Luxembourg, the Dutch Innovation Box generally only applies to self-developed intellectual property, with an exception for certain acquired intellectual property that is further developed.¹⁶² The scheme applies to all income and economic benefits derived from the innovative asset; however, for patented intellectual property, "more than 30 percent of the income must be attributable to the patent right."¹⁶³

E. The United Kingdom

Recognizing the departure of many high-tech companies from the United Kingdom, the country recently dramatically overhauled its corporate tax code.¹⁶⁴ It reduced its corporate tax rate to 21 percent in 2014, down from 28 percent in 2010.¹⁶⁵ The United Kingdom also lowered its tax on income from intellectual property, creating a patent box device.¹⁶⁶ The patent box effective tax rate in the United Kingdom, which was adopted in April 2013, is 10 percent.¹⁶⁷ The scheme is more of a true "patent box" regime because it only applies to companies filing patents or supplementary protection certificates

156. *See id.* at 41.

157. Brown, *supra* note 4, at 921.

158. *See id.*

159. *See id.*

160. *Id.* at 921–22.

161. *Id.* at 922.

162. *See id.*

163. *Id.* at 923.

164. Tom Fairless & Shayndi Raice, *In Inversion Tax Deals, U.K. Is a Winner*, WALL STREET J. (July 28, 2014), <http://www.wsj.com/articles/in-inversion-tax-deals-u-k-is-a-winner-1406551914> [<http://perma.cc/CQQ6-G7AZ>] (archived Sept. 20, 2015) (noting the country's dramatic overhaul of its tax code).

165. WALSH & SANGER, *supra* note 112, at 6; Fairless & Raice, *supra* note 164.

166. *See* Fairless & Raice, *supra* note 164 (discussing the United Kingdom's patent box).

167. Hill, *supra* note 108, at 16.

in the United Kingdom and does not include other popular forms of intellectual property such as trademarks or copyrights.¹⁶⁸

There is little doubt that the United Kingdom has become a large beneficiary of the patent box device regime.¹⁶⁹ However, this may be just one reason for its recent popularity as a place for companies to invert. The location, language, and lifestyle are also enticing to American executives.¹⁷⁰ The United Kingdom's proximity to Europe and London's role as a center for international finance are also important considerations.¹⁷¹

IV. RESPONSES TO INVERSIONS

The quantity of corporations that have recently inverted and their notoriety have gained the attention of multiple governments and international associations.¹⁷² This Part examines the reactions to the companies that have inverted and the countries in which they have reincorporated. This Part also discusses attempts by governments and international entities to cease further inversions.

A. Political Pressures from the United States

1. Concerns from the U.S. Perspective

One of the main complaints about corporate inversions is that they erode the U.S. tax base.¹⁷³ With fewer corporations paying U.S. taxes, remaining taxpayers, other businesses, and individuals are left to pick up the slack. Corporate inversions may also have an impact on state tax revenues, as many states base their corporate taxes on federal taxable income. The U.S. Treasury Department claims that corporate inversions, which diminish the tax revenue base, cost the United States billions of dollars each year.¹⁷⁴ In fact, it is estimated that plans to end corporate inversions could raise \$17 billion over the

168. *Id.*

169. *See* Fairless & Raice, *supra* note 164.

170. *Id.*

171. *Id.*

172. *See* CRS REPORT, *supra* note 2, at 5 (discussing the attention surrounding the current wave of inversions).

173. *Treasury Secretary Calls on Congress to Address Corporate Inversions*, 7/24/2014 FED. TAXES WEEKLY ALERT, art. 3 (July 24, 2014), WESTLAW [hereinafter *Treasury Secretary*] (noting that Secretary of the Treasury, Jacob Lew, has described corporate inversions as "hollow[ing] out the U.S. corporate income tax base").

174. Dumler, *supra* note 15, at 89 (explaining the costs of a diminished tax base).

next decade.¹⁷⁵ Federal revenue from corporate income tax has decreased dramatically—going from nearly one-third of total revenues in the 1950s to less than 10 percent in 2012.¹⁷⁶

Legislative bodies often refer to U.S. corporations that use corporate inversion as deserters or claim that they are being unpatriotic; however, these classifications have not completely thwarted the corporate inversion movement.¹⁷⁷ The fact that companies are continuing to invert may further reduce the stigma attached to inverting, which could lead to even more corporate inversions. Notwithstanding the stigma, companies that wish to remain competitive may feel their only option is to invert. Companies that choose to invert in the face of possible reputational losses likely feel that the tax benefits far outweigh any potential losses, reputational or otherwise.

2. Proposed U.S. Legislation

While both political parties have argued in favor of reducing the corporate tax rate, no legislation reducing the statutory rate has been passed. The corporate statutory tax rate in the United States is higher than both the average rates of the other OECD countries and of the fifteen largest economies in the world.¹⁷⁸ Critics argue that the United States must lower its own tax rate if it truly wants to prevent inversions.¹⁷⁹ There may be some legitimacy to this argument as the high U.S. corporate tax rate of 35 percent only generates about half as much revenue as the OECD countries that apply a corporate tax rate averaging about 29 percent.¹⁸⁰ While reducing the tax rate in the United States may reduce the incentive to invert, some worry that this would lead to a “race to the bottom” scenario in which countries eventually cut their tax rates down to zero in order to attract corporations.¹⁸¹

175. Richard Rubin, *U.S. Seeks Legislation to Curb Offshore Tax Deals*, BLOOMBERG BUS. (July 16, 2014, 4:10 PM), <http://www.bloomberg.com/news/articles/2014-07-16/obama-administration-seeks-curbs-on-offshore-tax-deals> [<http://perma.cc/FM8V-6LDN>] (archived Sept. 20, 2015) (discussing proposed plans for corporate inversion legislation).

176. See Thornton, *supra* note 16 (explaining the trend in corporate tax share).

177. See Anderson, *supra* note 21, at 274 (noting criticisms of those companies that choose to invert).

178. CRS REPORT, *supra* note 2, at 11 (comparing the U.S. corporate tax rate to other countries).

179. See *id.* (explaining the possibility of lowering the corporate tax rate in the United States).

180. Dumler, *supra* note 15, at 103.

181. See James S. Henry & Nicole Tichon, *Corporate Taxation—The Next Race to the Bottom*, TAX JUSTICE NETWORK (Mar. 30, 2012), <http://taxjustice.blogspot.com/2012/03/corporate-taxationb-next-race-to-bottom.html> [<http://perma.cc/SZB5-C8B2>]

The Secretary of the Treasury has urged Congress to immediately enact legislation to “shut down this abuse of our tax system,” referring to corporate inversions as a pressing matter.¹⁸² One suggestion that the Secretary of the Treasury has provided is to change the cutoffs used in the American Jobs Creation Act of 2004.¹⁸³ The Secretary’s plan would reduce the 60 percent test altogether, while replacing the 80 percent test with a greater-than-50 percent test.¹⁸⁴ This, in turn, would cause many of the companies considering inversion to re-evaluate their decision, as many of them would still be considered domestic under the 50 percent standard.¹⁸⁵

In May of 2014, an anti-corporate inversions bill was proposed, titled the Stop Corporate Inversions Act of 2014.¹⁸⁶ As demonstrated in the American Jobs Creation Act of 2004, a company is considered inverted if U.S. shareholders own at least 80 percent of its stock after it reincorporates abroad.¹⁸⁷ The Stop Corporate Inversions Act would decrease, from 80 percent to 50 percent, the proportion of U.S. shareholders needed to be in control of the new corporations stock for the corporation to still be treated as domestic.¹⁸⁸ The act would also continue to treat the surviving company as domestic for tax purposes if management and control of the company remained in the United States and “either 25 percent of its employees, sales or assets are located in the United States.”¹⁸⁹

On July 29, 2014, a second anti-corporate inversion bill was proposed, titled the No Federal Contracts for Corporate Deserters Act.¹⁹⁰ U.S. Senators Dick Durbin (D-Ill.) and Carl Levin (D-Mich.), along with U.S. Representatives Rosa DeLauro (D-Conn.) and Lloyd Doggett (D-Tex.), introduced the bill.¹⁹¹ According to a description on Senator Durbin’s website, if enacted, the proposed “legislation would bar contracts from going to businesses that incorporate overseas, are majority-owned by shareholders of the old U.S. corporation, and do not have substantial business opportunities in the foreign country in which they are incorporating.”¹⁹² The legislation, like the proposed

(archived Sept. 20, 2015) (warning of a possible race to the bottom of corporate taxation).

182. *Treasury Secretary, supra* note 173.

183. *See id.*

184. *Id.*

185. *See id.*

186. Cory Hester, *Pending Legislation Could Thwart Corporate Inversions*, WESTLAW CAP. MKTS. DAILY BRIEFING, 2014 WL 2932692 (July 1, 2014) [hereinafter *Pending Legislation*].

187. 26 U.S.C. § 7874 (2015).

188. *See Pending Legislation, supra* note 190.

189. *Id.*

190. Cory Hester, *Second Anti-Corporate Inversion Bill Proposed in Congress*, 28 NO. 8 WESTLAW J. GOV’T CONTRACT 10 (2014) [hereinafter *Bill Proposed*].

191. *Id.*

192. *Durbin & Leading Congressional Democrats Introduce the No Federal Contracts for Corporate Deserters Act*, DICK DURBIN: UNITED STATES SENATOR (July 29,

Stop Corporate Inversions Act, would apply to all inversions that were not finalized by May 8, 2014.¹⁹³ The proposed legislation would also allow federal agencies to prohibit businesses from holding federal contracts if they subcontract with inverted corporations, which, in turn, would curtail subcontracting to inverted corporations.¹⁹⁴

While this proposed legislation has made certain companies, such as AbbVie, reconsider their inversion plans, the threat of legislation has been largely unsuccessful.¹⁹⁵ In August of 2014, Mallinckrodt PLC, an Ireland-based corporation, completed its acquisition of Questcor Pharmaceuticals, Inc., a U.S.-based corporation, in a \$5.8 billion transaction.¹⁹⁶ The residence of the new company is now Ireland.¹⁹⁷ Horizon Pharma, an Illinois-based corporation, finalized a merger with Vidara International Therapeutics Ltd., an Ireland-based corporation, in September of 2014.¹⁹⁸ This merger created a new company, Horizon Pharma PLC, incorporated in Ireland.¹⁹⁹ This merger was finalized despite Horizon Pharma's expressed concerns over the Stop Corporate Inversions Act or other proposed legislation.²⁰⁰ Medtronic Inc., a Minneapolis-based corporation, acquired Covidien in a \$49.9 million deal earlier this year.²⁰¹ Medtronic and Covidien became wholly owned subsidiaries of a new Irish-based parent corporation.²⁰² Furthermore, there are a number of inversions currently in progress. Chiquita Brands International Inc., a Charlotte-based corporation, will combine with

2014), <http://www.durbin.senate.gov/public/index.cfm/pressreleases?ID=9c531ebf-12c0-4996-9e97-02e27cf14543> [<https://perma.cc/YXP3-CHT2?type=source>] (archived Sept. 20, 2015).

193. *Bill Proposed*, *supra* note 190.

194. *Id.* (explaining the details of the proposed legislation).

195. *AbbVie Reconsidering \$54bn Tax Inversion Takeover of Dublin-Headquartered Shire*, FINFACTS IRELAND (Oct. 15, 2014), http://www.finfacts.ie/irishfinancenews/article_1028314.shtml [<https://perma.cc/7YCG-R35X?>] (archived Sept. 20, 2015) (explaining that AbbVie's board is considering the impact of the U.S. Treasury's proposed changes).

196. *Mallinckrodt Pharmaceuticals (MNK) Completes Acquisition of Questcor Pharmaceuticals, Inc. (QCOR)*, BIOSPACE (Aug. 15, 2014), <http://www.biospace.com/News/mallinckrodt-pharmaceuticals-completes-acquisition/343541> [<http://perma.cc/PB86-TXRQ>] (archived Sept. 20, 2015).

197. Martin A. Sullivan, *Lessons from the Last War on Inversions*, TAX ANALYSTS, May 26, 2014, at 866, <http://taxprof.typepad.com/files/sullivan-1.pdf> [<http://perma.cc/B2CL-7HMX>] (archived Sept. 20, 2015).

198. *Horizon Pharma Completes Acquisition of Vidara Therapeutics International plc*, HORIZON PHARMA (Sept. 19, 2014), <http://ir.horizon-pharma.com/releasedetail.cfm?releaseid=871747> [<http://perma.cc/A66L-52VZ>] (archived October 20, 2015).

199. *Id.*

200. *See Pending Legislation*, *supra* note 186 (explaining the Horizon Pharma merger).

201. David Crow, *Medtronic: The Tax Inversion That Got Away*, FIN. TIMES (Jan. 27, 2015), <http://www.ft.com/intl/cms/s/0/ddcd9ad6-a5cf-11e4-ad35-00144feab7de.html#axzz3SoBoixBe> [<http://perma.cc/K39W-KKFM>] (archived Oct. 6, 2015).

202. *Id.*

Fyffes PLC, a Dublin-based corporation.²⁰³ This deal, premised on a stock-for-stock transaction worth \$1.07 billion, will make both Chiquita and Fyffes wholly owned subsidiaries of Chiquita Fyffes PLC, which will be incorporated in Ireland.²⁰⁴

B. European Investigations Into Illegal State Aid

The United States is not alone in its criticism of tax haven countries and their controversial techniques. Germany's finance minister Wolfgang Schaeuble, for example, has called for a ban on patent box tax breaks.²⁰⁵ Schaeuble argues that patent box regimes run counter to EU rules designed to deter discriminatory tax rules.²⁰⁶ While creative tax incentive regimes such as patent boxes have attracted some criticism, they are legal under EU law as long as they do not amount to illegal state aid.²⁰⁷ Under EU law, offering special deals to certain companies without offering other companies similar deals is considered illegal state aid.²⁰⁸ Several countries have been suspected of making such deals.

On June 11, 2014, EU regulators opened a formal investigation into corporate tax regimes in Ireland, Luxembourg, and the Netherlands.²⁰⁹ This investigation was prompted by concerns that several major multinational corporations—Apple, Amazon, Google, and Starbucks—were receiving beneficial tax deals greater than what is allowed under EU law.²¹⁰ This came after a U.S. investigation into Apple in May 2013 found no evidence that Apple had done anything illegal, despite paying little or no corporate tax on at least \$74 billion in revenue over the previous four years due to exploiting the double Irish loophole.²¹¹ The UK Parliament has also held hearings on

203. Michael Glasser, *Companies Look to Corporate Inversions to Reduce Tax Burdens*, WESTLAW MERGERS & ACQUISITIONS DAILY BRIEFING (June 19, 2014), 2014 WL 2748364 (discussing the Chiquita Brands merger).

204. *Id.*

205. Annika Breidhardt, *Germany Calls on EU to Ban "Patent Box" Tax Breaks*, REUTERS (July 9, 2013), <http://uk.reuters.com/article/2013/07/09/uk-europe-taxes-idUKBRE9680KY20130709> [<http://perma.cc/9GBQ-U5SH>] (archived Sept. 20, 2015).

206. *Id.*

207. *See* Lynch, *supra* note 107 (explaining the legality of patent boxes).

208. James Kanter & Mark Scott, *Amazon's Tax Deal with Luxembourg May Break Rules, E.U. Regulator Says*, N.Y. TIMES (Jan. 16, 2015), <http://www.nytimes.com/2015/01/17/business/amazon-luxembourg-european-commission.html> [<https://perma.cc/K7FB-AK5F>] (archived Sept. 20, 2015).

209. Fairless, *supra* note 116.

210. *Id.*

211. *Id.*

corporate tax dodging, investigating Google, Amazon, and Starbucks.²¹²

The investigations by the European Union led to a series of preliminary findings. In November 2014, EU authorities issued a report accusing the Netherlands of making a special deal with Starbucks.²¹³ Among other concerns, the European Commission was doubtful that the royalty paid by Starbucks to a British partner for the use of its intellectual property rights (a recipe for coffee roasting) adhered to international guidelines.²¹⁴ In January 2015, the European Union's antitrust office preliminarily found that Amazon had entered into a tax deal with the Luxembourg government that amounted to unfair state aid.²¹⁵

C. The OECD's Proposed Plan

The OECD and the Group of Twenty countries (G20) have adopted a fifteen-point Action Plan aimed at addressing base erosion and profit shifting, known as the Base Erosion and Profit Shifting (BEPS) Project.²¹⁶ One important goal of the plan is to eliminate the "artificial shifting of profit to no or low tax environment jurisdictions."²¹⁷ In other words, the OECD hopes "to prevent corporations from gaming the international tax system."²¹⁸ This plan would update the current international tax system by implementing a multinational instrument.²¹⁹ The multilateral instrument proposed

212. Jesse Drucker & Rainer Buerger, *OECD Proposes Plan for Crackdown on Companies' Tax Avoidance*, BLOOMBERG BUS. (July 19, 2013), <http://www.bloomberg.com/news/articles/2013-07-19/oecd-proposes-plan-for-crackdown-on-companies-tax-avoidance> [<https://perma.cc/6S9U-F2GG>] (archived Sept. 20, 2015) (noting UK Parliament's three hearings on corporate tax dodging).

213. James Kanter, *E.U. Accuses Starbucks and Netherlands of Making Unfair Tax Deal*, N.Y. TIMES (Nov. 14, 2014), <http://www.nytimes.com/2014/11/15/business/international/starbucks-eu-tax-deal.html> [<https://perma.cc/RMB7-77V5>] (archived Sept. 20, 2015) (discussing the European Union's investigation into the Netherlands' tax practices).

214. *See id.*

215. Kanter & Scott, *supra* note 208 (discussing the EU's preliminary finding of its investigation into Amazon and Luxembourg).

216. ORG. FOR ECON. COOPERATION & DEV. [OECD], OECD/G20 BASE EROSION AND PROFIT SHIFTING PROJECT EXPLANATORY STATEMENT 3 (2014), [hereinafter EXPLANATORY STATEMENT] www.oecd.org/tax/beps-2014-deliverables-explanatory-statement.pdf [<https://perma.cc/BC48-DRM5>] (archived Sept. 20, 2015) (explaining the OECD's plan).

217. *Id.* at 7.

218. David Jolly, *O.E.C.D. Calls for Coordinated Fight Against Corporate Tax Avoidance*, N.Y. TIMES (Sept. 16, 2014), <http://www.nytimes.com/2014/09/17/business/international/oecd-fights-corporate-tax-avoidance.html> [<http://perma.cc/EZV5-FF6B>] (archived Sept. 20, 2015) (explaining the OECD's goal of combating corporate tax avoidance).

219. *See generally* MULTILATERAL INSTRUMENT, *supra* note 8.

by the OECD would not wholly supersede the current bilateral treaties but would modify and coexist with the bilateral treaties.²²⁰ A revised draft of the plan was released on May 22, 2015, asking for comments to be submitted by June 17, 2015.²²¹ The OECD hopes to conclude drafting by the end of the 2016 calendar year.²²²

There is ostensibly strong political support for adapting the current international tax system to complement the globalized and sophisticated world that we live in today.²²³ Such adaptation is long overdue as the current network of bilateral tax treaties was developed in the 1920s for the purposes of eliminating double taxation.²²⁴ Instead of double taxation, the most recent problem is double non-taxation.²²⁵ It is hoped that such a multilateral tax instrument would reduce tax avoidance abuses in cases of dual residence, a source of the double non-taxation problem.²²⁶

The specific benefits of the agreement are multiple. Nations would benefit from a more detailed picture of companies' operations due to a requirement that companies report their revenue, profit, and taxes paid in each jurisdiction.²²⁷ The proposal also hopes to neutralize hybrid mismatch arrangements that allow corporations to escape taxes by setting up entities or transfers in two or more countries for no other productive purpose.²²⁸ The OECD also hopes to address the transparency of transfer pricing and how intangible assets, like intellectual property, are reported.²²⁹ Technology and pharmaceutical firms, which hold large amounts of intellectual property, stand to lose the most from such provisions.

220. *Id.* at 17–18.

221. *OECD Releases New BEPS Draft Dealing with Tax Treaty Abuse*, MNE TAX (May 22, 2015), <http://mnetax.com/oecd-releases-new-beps-draft-dealing-tax-treaty-abuse-8780> [<http://perma.cc/NBQ4-QP44>] (archived Sept. 20, 2015).

222. *First Steps Towards Implementation of OECD/G20 Efforts Against Tax Avoidance by Multinationals*, ORG. FOR ECON. COOPERATION & DEV. [OECD] (June 2, 2015), <http://www.oecd.org/tax/first-steps-towards-implementation-of-oecd-g20-efforts-against-tax-avoidance-by-multinationals.htm> [<http://perma.cc/2Y6N-K44B>] (archived Sept. 20, 2015).

223. *See id.*

224. *See id.*

225. *See* EXPLANATORY STATEMENT, *supra* note 216, at 3.

226. *See* Michael Xu, *Road Forward to a Multilateral Tax Treaty Regime?*, DLA PIPER (Oct. 29, 2014), <https://www.dlapiper.com/en/us/insights/publications/2014/10/international-tax-news-oct-2014/road-forward-to-a-multilateral-tax-treaty/> [<https://perma.cc/NTM7-GCG3>] (archived Sept. 20, 2015) (listing some of the goals of the OECD's proposed multilateral agreement).

227. Jolly, *supra* note 218 (describing some of the benefits of the OECD's proposed plan).

228. *Id.*

229. *Id.*

V. THE U.S. SOLUTION TO CORPORATE INVERSIONS

The United States should learn from prior experience and abandon its protectionist approach to preventing corporate inversions by joining many of the countries that have taken a more proactive approach. The best course of action for the United States would be to join the member countries of the OECD and G20 and adopt the OECD's proposed multilateral instrument. If the agreement is not sufficiently structured or fails to be implemented, the United States should immediately implement its own patent box.

A. Support the Multilateral Instrument Proposed by the OECD

Ideally, pressure from the United States and other interested countries would be sufficient to make the OECD's proposed multilateral instrument a reality. Such an agreement would be optimal for the United States because it would address a large array of issues currently leading major corporations to invert. It would also reduce pressure on Congress to quickly overhaul the U.S. tax code, an idea that has support but appears politically infeasible. The United States should not support such agreement unconditionally but should instead only support the proposal if it contains certain conditions.

One condition should be full participation by all OECD and G20 countries. If certain countries—such as the ones benefiting the most from corporate inversions—do not join the agreement, the instrument will lose one of its primary purposes. Additionally, the provisions in the OECD's proposed agreement that were designed to make it harder for companies to shift profits by assigning intellectual property to offshore entities must be maintained for the United States to join in the agreement. Under current treaty agreements, it is possible for offshore subsidiaries to take credit for profits arising from patents developed in the United States.²³⁰ For example, Mountain View, the California-based Google affiliate corporation, “has avoided as much as \$2 billion in worldwide income taxes annually” by attributing foreign profits to an intellectual property holding company in Bermuda.²³¹ This proposed agreement should also include the outlawing of patent boxes, a proposal that might be met with some resistance. However, the United Kingdom, a country that has very recently implemented a patent box, has noted that it would support the OECD plan.²³²

230. Drucker & Buerger, *supra* note 212 (explaining how intellectual property companies currently avoid taxation).

231. *Id.*

232. *See id.* (providing a statement made by the UK Prime Minister, David Cameron, who declared he would “call on fellow leaders to get behind this action plan”).

If the United States wants to ensure the effectiveness of such provisions in the OECD plan, it should also urge the OECD to reconsider the supplementary nature of its multilateral treaty. As previously explained, the OECD views the proposed agreement as not wholly superseding the current bilateral treaties but instead coexisting with the bilateral treaties. The United States should insist that the proposed agreement be preemptive and take precedence over any conflicting terms in existing bilateral treaties. Failure to do so may allow countries to continue using methods that the OECD plan seeks to eliminate.

Despite the support for this proposal, there are several reasons to doubt that the multilateral instrument will be passed in a form that the United States would find satisfactory. The EU Treaty gives member states full autonomy in the area of taxation, including corporate income taxation.²³³ It is unlikely that the proposed multilateral instrument could take this power away, making the removal of patent boxes entirely up to the countries that are implementing them. There is reason to doubt that countries will voluntarily remove their patent box regimes, as evidenced by the past reluctance of member states to give up some of their sovereignty regarding corporate taxation.²³⁴ If the countries currently using patent boxes oppose the OECD plan, it may never materialize.²³⁵ It is difficult to imagine why these countries would be willing to adopt such a plan when the OECD has no power to compel them to do so.²³⁶

Another concern is that the current proposal fails to consider the lack of participation of developing countries that are not members of the OECD.²³⁷ Without full participation, countries not party to the treaty may develop unfair tax strategies in an effort to attract multinational corporations. This clearly does not resolve the issue of corporations gaming the international tax system but only changes where they settle. This concern might be minimal, however, as many of the countries left out of the agreement are too politically and economically unstable for corporations to ever consider establishing residence there, despite the potential massive tax breaks. On the other hand, some believe that the current proposed multilateral tax

233. See Lynch, *supra* note 107 (“Under EU law, member states have the right to set their own tax rates.”).

234. Michael P. Devereux & Clemens Fuest, *Corporate Income Tax Coordination in the European Union*, OXFORD UNIV. CTR. FOR BUS. TAXATION (Oct. 2009), at 3 (“[M]ember States were very reluctant to give up some of their sovereignty in the field of corporate taxation . . .”).

235. See Drucker & Buergin, *supra* note 212 (“Achieving the plan’s objectives may be hamstrung by the role that several European countries—including Ireland, the Netherlands and Luxembourg—play in enabling the avoidance.”) (quoting Sol Picciotto, an emeritus professor of law at Lancaster University in the United Kingdom).

236. See *id.*

237. See *id.*

treaty might be unrealistically broad and include too many countries.²³⁸ Though multilateral tax treaties have existed in the past, they have typically occurred between regional countries with similar legislative structures.²³⁹ As there is no guarantee that the OECD instrument will be implemented in a satisfactory matter, it is important for the United States to act promptly by creating a U.S. patent box regime.

B. Create a U.S. Patent Box

Countries often view corporations heavily linked with intellectual property, such as technology and pharmaceutical companies, as desirable residents due to their potential to spur innovation domestically.²⁴⁰ Countries have attracted such firms using various tactics, one of which being tax incentives that favor the creation, development, and commercialization of intellectual property.²⁴¹ One such tax incentive strategy that has been implemented by several countries is the adoption of a patent box.

This proactive strategy is different from those typically employed by the United States, which instead has sought to enact protectionist tax laws. The United States could learn from the recent movement by the United Kingdom and initiate a competitive approach by enacting patent box legislation. Such legislation would serve as an incentive to companies with large amounts of intellectual property to choose the United States as their destination. One of the strongest reasons to adopt a proactive approach, rather than a reactive approach, is that it simply is not possible for legislation to keep pace with evolving corporate practices. In the past, the United States has tried to combat corporate inversions by making the law stricter, but each time corporations have found new ways to take advantage of gaps in the tax code. Even if Congress effectively closes these gaps, it is still likely that some companies will slip through the cracks. In fact, in a recent example, changes to U.S. Treasury rules initially halted Minnesota-based Medtronic's inversion plans because it could not access its overseas cash pile to finance the takeover of Covidiean, an Ireland-based company.²⁴² However, the company eventually used the bond market to finance part of the \$49.9 billion deal.²⁴³

238. See Xu, *supra* note 226 (noting the difficulty in implementing a broad multilateral tax treaty).

239. See *id.* (listing several examples of regional multilateral tax treaties that have been successful).

240. See Hill, *supra* note 108, at 13 (explaining that governments have turned to tax incentives to attract companies and spur innovation).

241. See *id.* at 13–14.

242. See Crow, *supra* note 201 (discussing Medtronic's inversion).

243. *Id.*

When developing a patent box, there are numerous aspects to consider regarding the nature of the regime. At what rate should the patent tax be set? Which types of intellectual property should qualify? Should the patent box apply only to self-developed intellectual property or also to acquired intellectual property? In answering these questions, the overarching goal should be to encourage the expansion of domestic innovation, commercialization, and production.

In order to meaningfully compete with recent patent boxes, the United States should set the patent tax rate somewhere in the range of 10 to 15 percent. While this range represents the upper range of recent patent tax rates, this is still much lower than the current U.S. corporate income tax rate of 35 percent. The U.S. patent box tax rate does not need to be lower than this because other benefits to incorporating in America may place the United States on equal footing with other countries that have slightly lower rates. This rate will hopefully discourage corporate inversions that occur solely for tax purposes while still allowing those inversions enacted for purely legitimate reasons to occur free of stigma.

The United States should follow the United Kingdom's lead and focus its patent box specifically on patents, as patents are highly valuable in the technology and pharmaceutical industries, whose companies comprise the majority of the current corporate inversions. Whether to include more types of intellectual property is not as important a consideration because there are pros and cons to both.

The U.S. patent box should only apply to self-developed intellectual property or acquired intellectual property that has been additionally developed. In addition, the United States should include a requirement that a significant portion of the production of the patented item must take place within the United States for the patent box to apply. Such a requirement has the potential to create U.S. jobs and capture other tangible benefits. This feature would be unique to the United States—as tying benefits to performance is not allowed under the EC Treaty due to its emphasis on the free movement of workers and capital.²⁴⁴

Given that protectionist legislation to stop corporate inversions has failed to be implemented, one could argue that any proposal to implement a patent box would also fail to be approved by Congress. In fact, there have already been two proposals to implement a U.S. patent box tax regime—both of which have failed.²⁴⁵ With the wave of

244. See *The Lisbon Treaty and Tax Legislation in the EU*, EUR. COMM'N TAXATION & CUSTOMS UNION (2015), http://ec.europa.eu/taxation_customs/taxation/gen_info/tax_policy/article_6759_en.htm [<http://perma.cc/2UR8-NYQZ>] (archived Sept. 20, 2015) (discussing the EU's emphasis on mobility).

245. Bernard J. Knight, Jr. & Goud Maragani, *As Part of Any New Patent Legislation, the New Congress Should Enact a Patent Box Regime to Bolster America's Competitiveness for New Innovation and Increase Job Opportunities for the Middle*

inversions continuing, hopefully support for this type of legislation will increase. Even if such legislation ultimately fails to pass, serious consideration of a patent box by Congress could act as leverage and convince other countries to (1) amend their treaties with the United States and eliminate many of the provisions that are disadvantageous to the United States and (2) support the implementation of OECD's proposed multilateral instrument, which should be the ultimate goal of the United States.

VI. CONCLUSION

Corporate inversions have become a hot-button issue recently, garnering attention from both mass media and policymakers across the globe. The main motivation for these inversions is the difference in tax systems between the United States and other countries. Corporate inversions allow corporations to escape the obligation of U.S. taxation, thereby costing the United States government billions of dollars every year.

Ireland, Luxembourg, the Netherlands, and the United Kingdom have become a popular destination for inversions. This is especially true for corporations holding large amounts of intellectual property, due to the patent box regimes established by these countries. These countries and companies have been the subject of a great deal of criticism from the United States, the European Union, and the OECD. Despite this criticism, no formal legislation or agreement has been implemented.

The United States should take a proactive approach to dealing with the issue of corporate inversions. Ideally, this would involve the adoption of a new multilateral treaty proposed by the OECD that resolves all of the tax concerns of the United States. However, the United States should not rely solely on the OECD proposal. It should instead abandon its usual protectionist approach, which ignores important business considerations, and try to attract businesses through the adoption of a patent box. A U.S. patent box regime would put pressure on other countries to cooperate in a multilateral tax treaty and attract desirable companies that would spur innovation domestically.

*Scott DeAngelis**

Class, BLOOMBERG BNA (Jan. 9, 2015), <http://www.mwe.com/files/Publication/eedf51be-c04c-445b-9ee2-c0b51be532d0/Presentation/PublicationAttachment/e36b3c40-9ecd-4df4-953f-c8a46205eae7/PDFArtic.pdf> [<http://perma.cc/AM7A-4BB3>] (archived Sept. 20, 2015).

* J.D. Candidate/Ph.D. Student in Law and Economics