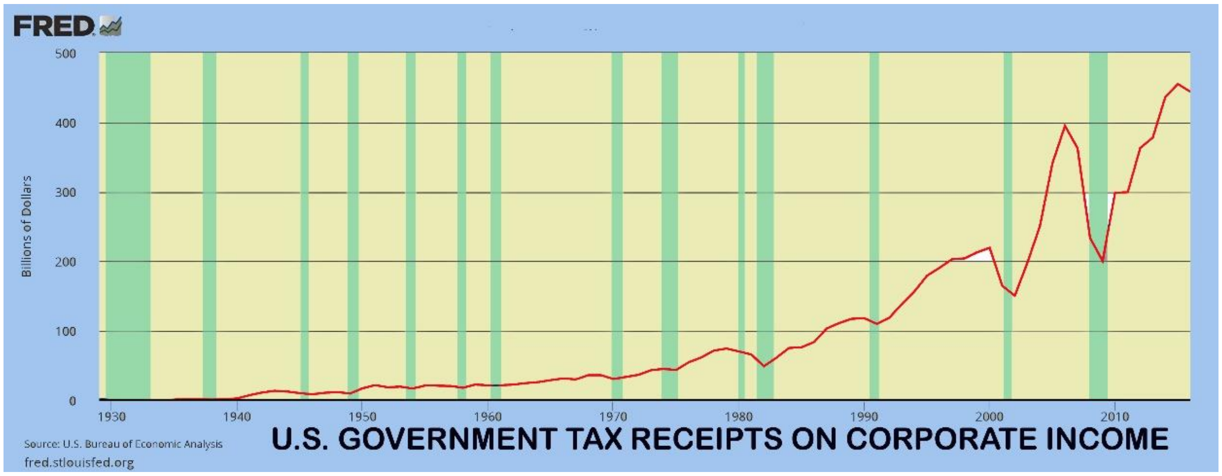
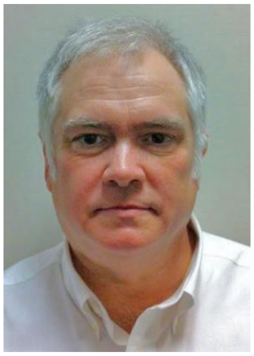



***"American companies looking to avoid paying domestic tax rates are holding about $2.6 trillion in overseas earnings, a number that has been rising steadily for years, according to new research from Capital Economics". -- CNBC," April 28, 2017***

# TAX INVERSIONS: THE GOOD THE BAD AND THE UGLY

Peer Reviewed

By Phillip Fuller and Henry Thomas



Fuller

Thomas

Phillip Fuller, DBA Phillip.R.Fuller@sums.edu is a Professor of Finance, Department of Economics, Finance, and General Business, Jackson State University and Henry Thomas, CPA is an Instructor of Accounting, College of Business, Jackson State University.

## Abstract

Tax inversions are a popular topic of discussion among politicians, consultants, news outlets, and academics. Tax inversions are not a new topic; they were discussed in the early 1990s and in the previous decade. Tax inversion is a tax strategy in which a company reincorporates in another country for tax purposes. Several U.S. firms have merged with foreign firms in order to move their headquarters out of the U.S. Firms have defended their tax inversions by saying that inversions enhanced shareholders' wealth by increasing the firms' efficiencies and/or reducing their corporate taxes.

The federal government has attempted to reduce and/or eliminate tax inversions. The government is concerned that tax inversions will reduce the tax base at a time when the federal government is experiencing budget deficits and the national debt is at an all-time high. Furthermore, individuals are increasingly aware of the huge financial disparity between the wealthiest members of our society and everybody else, and they believe tax inversions exacerbate this disparity in wealth.

This paper discusses the history of tax inversions along with tax inversion research, and addresses current status of inversions and possible solutions. The purpose of this paper is to help individuals better understand tax inversions.

# Introduction

Virtually all developed countries require firms to pay taxes on income earned domestically. However, the U.S. requires its domestic firms to pay taxes on income that is earned domestically and internationally. Firms incorporated in the U.S. pay taxes on foreign income when the income is repatriated back to the U.S. or paid back as dividends. U.S. taxes owed on foreign income that has not been repatriated back to the U.S. are referred to as deferred income taxes.

Since the U.S. top statutory tax rate is 35% for income earned domestically and internationally, and is one of the highest among developed countries, U.S. firms have used tax inversions to avoid paying taxes on foreign earnings. (However, their effective rate is usually lower since corporations take advantage of various loopholes, exemptions, and tax credits.) Tax inversion is a tax strategy in which a company reincorporates in another country for tax purposes. Table 1 below presents completed inversions from 2014 through 2016.

Reducing tax liabilities of corporations is not illegal, and in the eyes of shareholders, inversions may be viewed as a good thing. Corporations and individuals are not required to pay more than the required amount of taxes owed, based on the prevailing tax laws. One of management's main responsibilities is to enhance shareholders' wealth. Enhancing shareholders' wealth is frequently cited by textbooks, e.g., Brigham and Daves (2016) and Ross, Westerfield, and Jordan (2017) as a primary goal of management. Moreover, management may believe that a legal implemental tax strategy that helps to minimize overall tax expense fulfills their responsibility to shareholders and expectations of shareholders. The Institute of Taxation and Economic Policy (ITEP) (2017) reported that approximately $2.6 trillion has not been repatriated back to the U.S. The ITEP believes that the Fortune 500 companies are avoiding up to $767 billion in federal income taxes.

Table 1: List of Inversions Completed from 2014 through 2016

| Company Name | Previous U.S. Location | New "Headquarters" | Year Completed | Top Executives Based in U.S. |
|---|---|---|---|---|
| Arris International PLC | Georgia | England | 2016 | Yes |
| Card Tronics | Texas | England | 2016 | No |
| IHS Markit Ltd. | Colorado | England | 2916 | Yes |
| Johnson Control International Plc | Wisconsin | Ireland | 2016 | Yes |
| Waste Connections Inc. | Texas | Canada | 2016 | Yes |
| Civeo Corp. | Texas | Canada | 2015 | Yes |
| Energy Fuels Inc. | Wyoming | Canada | 2015 | Yes |
| Livanova | Texas | England | 2015 | No |
| Medtronic Plc | Minnesota | Ireland | 2015 | Yes |
| Mylan NV | Pennsylvania | Netherlands | 2015 | Yes |
| Steris Plc | Ohio | England | 2015 | Yes |
| Wright Medical Group NV | Tennessee | Netherlands | 2015 | Yes |
| Endo International Plc | Pennsylvania | Ireland | 2014 | Yes |
| Horizon Pharma Plc | Illinois | Ireland | 2014 | Yes |
| Restaurant Brands Int. Inc. | Florida | Canada | 2014 | No |
| Theravance Biopharma Inc. | California | Cayman | 2014 | Yes |

Source: https://www.bloomberg.com/graphics/tax-inversion-tracker/

Some individuals, firms, and government officials are concerned that tax inversions are bad because of their negative impact on the U.S. As Table 2 below indicates, the federal government has been running a budget deficit almost every year this century, and the national debt has more than tripled. Individuals may wonder to what extent inversions contribute to the federal deficit and national debt by reducing the U.S. tax base and collected income taxes. Taxpayers may also wonder if their taxes will increase or if the federal government will provide less funding to the military, education, health care, infrastructure, and other desirable projects and programs. In addition, citizens who rely on services that are financed and/or subsidized by the federal government are concerned that the federal government will reduce the funding of these services. Moreover, Brodwin (2014) noted that small business owners and consumers wondered if they might have to pay higher taxes because of inversions.

Table 2: 2000-2015 Summary of the Federal Government's Receipts, Outlays, Budget Surplus and Deficits, and the National Debt (in Billions)

| Year | Receipts[1] | Outlays[1] | Budget Surpluses or Deficits (-)[1] | National Debt[2] |
|---|---|---|---|---|
| 2000 | 2,025.2 | 1,789.0 | 236.2 | 5,674.2 |
| 2001 | 1,991.1 | 1,862.8 | 128.2 | 5,807.5 |
| 2002 | 1,853.1 | 2,010.9 | -157.8 | 6,228.2 |
| 2003 | 1,782.3 | 2,159.9 | -377.6 | 6,783.2 |
| 2004 | 1,880.1 | 2,292.8 | -412.7 | 7,379.1 |
| 2005 | 2,153.6 | 2,472.0 | -318.3 | 7,932.7 |
| 2006 | 2,406.9 | 2,655.1 | -248.2 | 8,507.0 |
| 2007 | 2,568.0 | 2,728.7 | -160.7 | 9,007.7 |
| 2008 | 2,524.0 | 2,982.5 | -458.6 | 10,024.7 |
| 2009 | 2,105.0 | 3,517.7 | -1,412.7 | 11,909.8 |
| 2010 | 2,162.7 | 3,457.1 | -1,294.4 | 13,561.6 |
| 2011 | 2,303.5 | 3,603.1 | -1,300.0 | 14,790.3 |
| 2012 | 2,450.0 | 3,537.0 | -1,087.0 | 16,066.2 |
| 2013 | 2,775.1 | 3,454.6 | -679.5 | 16,738.2 |
| 2014 | 3,021.5 | 3,506.1 | -484.6 | 17,824.1 |
| 2015 | 3,249.9 | 3,688.3 | -438.6 | 18,150.6 |

Sources: [1] Office of Management and Budget. Table 1.1—Summary of Receipts, Outlays, and Surpluses or Deficits (–): 1789–2021. http://www.whitehouse.gov/omb/budget/Historicals/
[2]U.S. Department of the Treasury. Historical Debt Outstanding - Annual 2000 - 2015. http://www.treasurydirect.gov/govt/reports/pd/histdebt/histdebt_histo5.htm

People are also concerned about the fairness of tax inversions, since shareholders appear to be the main beneficiaries. The fairness of the tax code is a relevant issue. Frequently, news outlets discuss the disparity in income and ownership of assets between the wealthiest Americans and everyone else. Shah (2014) reported that the wealth gap between America's rich and its middle class could partially be attributed to the increase in stock prices since 2009. Shah noted that stocks are disproportionately owned by the affluent. Consequently, affluent Americans are more apt than others to benefit from inversions. The New York State Bar (2003) believed that the lawful use of inversions could undermine the public's confidence in the integrity of the U.S. tax system.

## Impact of Inversions

Desai and Hines (2002) found that inverting firms tend to be larger, have sizable foreign assets and extensive debt, and face lower foreign tax rates than non-inverting firms. Their event study found that inverted companies' market value increased by 1.7% within a five-day window (two days before and after the announcement date).

However, only 10 of the 19 companies analyzed had abnormal gains during the five-day window.

Seida and Wempe (2003) concluded that the typical inverted firm's effective tax rate decreased by 8% and that firms experienced abnormal returns on the date shareholders approved the inversion. They found that inverted companies deferred their U.S. taxable income to post-inversion periods, and inverted firms' non-U.S. income increased.

Cloyd, Mills, and Weaver (2003) conducted an event study and did not find statistical evidence that inversions increased shareholder wealth. They found that the average return in the announcement period was negative, but the negative returns were insignificant. They examined post-inversion price changes up to six months after the announcement and still did not find signs of statistically significant price changes. They believed their findings were attributed to the taxation of either shareholders and/or the firm when inversion occurred and/or nontax costs, such as being labeled unpatriotic. They also found that inverted firms were significantly larger and had higher effective tax rates than their industrial counterparts.

Seida and Wempe (2004) claimed that firms did not perform tax inversions to avoid paying taxes on income earned abroad, but rather to lower the amount of taxes that they paid on income earned in the U.S. They found that post-inversion revenues did not increase substantially from pre-inversion revenues. However, they found that the mean foreign pretax income nearly doubled from 11% to 21% while pre-inversion tax profit margin decreased from 9% to a post-inversion tax profit margin of -6.5%. They assumed that the changes were due to earning stripping, i.e., the newly formed U.S. subsidiary paying internal interest and other fees to the non–U.S. parent or its subsidiaries.

Dowling (2014) presented a philosophical discussion on tax avoidance. The ethical and social responsibility issues that related to tax avoidance from several viewpoints were discussed. For example, he claimed that U.S. multinational firms should pay taxes in the U.S. for the use and protection of its security laws, and that the same firms should also pay taxes in other countries to compensate for the use of their public facilities. He discussed the costs of tax avoidance to the firm, government, and society. He pointed out that some individuals considered taxes as legalized theft by the government, while other individuals considered taxes as a rightful appropriation of funds to run an elected government.

Chorvat (2015) performed the first event study in recent years focusing on tax inversions. She re-examined the impact of inversion announcements for 1993-2013 on stock prices. She found no discernible price change around the announcement date. However, she found economically and statistically significant excess returns five years after the inversions. She believed that management used asymmetrical information to determine whether it was beneficial to shareholders to invert.

Badkin, Glover, and Levine (2015) found that inversions lowered a firm's corporate tax rate but benefited shareholders disproportionately. Shareholders benefited disproportionately from inversions due to their investments' tax basis. Some medium and long-term taxable shareholders did not benefit from inversions, since U.S tax code requires taxable shareholders to recognize their capital gains at the time of the inversions. They also found that CEOs and short-term, foreign, and tax exempt shareholders benefitted disproportionately from inversions. Moreover, the net impact of an inversion on shareholders depended on each shareholder's specific circumstances.

Gjörup and Nilsson (2016) provided evidence that inversions increased shareholder wealth. They examined specific factors to identify which of those factors were associated with a firm's decision to invert. They found that U.S. corporations with a high degree of foreign board members were more apt to invert. They also found a negative relationship between insider ownerships and firms' propensity to invert. They did not find any statistical evidence that Corporate Social Responsibility or institutional ownership impacted a firm's decision to invert.

## History

The first known inversion from the U.S. occurred in 1983 when McDermont International relocated to Panama, which prompted the enactment of tax code Section 1248 (i) (Avi-Yonah, 2002). Section 1248 (i) requires gains from certain sales or exchanges of stock in certain foreign corporations to be taxed. Section 1248 (i) was one of the first attempts to discourage corporate tax inversions.

In the late 90s and beginning of the new millennium, U.S. corporations used "naked inversions" to legally reorganize. In a naked inversion, a corporation moves its tax address to a tax haven such as Bermuda or the Cayman Islands by establishing a new holding company that is owned by shareholders of the founding corporation. The founding corporation becomes a subsidiary and continues to operate as it had done before the inversion, but without being required to pay U.S. taxes on income earned abroad.

Firms also reduced their taxes by engaging in post-inversion earning stripping. In earning stripping, the newly formed holding company receives payments from its "newly formed U.S. subsidiary." These payments lower the U.S. taxes. Some of the payments may include commissions and royalties. The subsidiary can incur unreimbursed expenses from its holding company and/or other affiliated subsidiaries. Profitable projects can also be shifted to affiliated foreign subsidiaries, and transfer pricing can reduce taxable income of the founding corporation (New York Bar, 2003).

In many cases, firms transferred intellectual properties to their foreign holding company. For example, Rubin (2015) reported that Gilead shifted income from the U.S. to reduce U.S. taxes by transferring ownership of its intellectual properties to Ireland. In 2014, Gilead reported $8.2 billion in foreign income before taxes, which was an amount higher than its non-U.S. sales.

Webber (2011) noted that Senators Baucus (Democrat from Montana) and Grassley (Republican from Iowa) spearheaded a bipartisan legislative effort to prevent naked inversions. The Senators considered tax inverters to be unpatriotic since the corporations in effect gave up their "American Citizenship." Congress passed the American Jobs Creation Act of 2004, which included IRC Section 7874. Section 7874 was enacted to discourage tax inversions.

Under Section 7874, if 80% or more of the owners (by vote or value) of the newly inverted company were owners of the former domestic firm, the foreign firm is taxed as if it were still a U.S. corporation. If the former owners of the firm own 60% but less than 80% of the foreign corporation, the foreign corporation loses its ability to use net operating losses and other tax attributes for up to ten years after the inversion.

Section 7874 did not apply if the former owners owned less than 60% of the foreign corporation. Section 7874 also did not apply if the Expanded Affiliated Group (EAG) had substantial business activities in the foreign firm's country of incorporation. EAG included the foreign corporation, along with all the companies it was connected to by a claim of greater than 50%. If a company followed Section 7874, the inverted company was treated as a foreign corporation, i.e., only paid taxes on income earned in the U.S., i.e. the inversion was viewed as a "safe harbor."

Section 7874 inversions were allowable if the inverted firm had "substantial business activity" in the new foreign parent company's country of incorporation. The term "substantial business activity" was not defined in 2004. Marples and Graville (2014) noted that since Section 7874 did not define substantial business activity, the Treasury Department could. Marple and Graville speculated that the lack of specificity was intentional to discourage inversions since corporations would be concerned about the consequences of an inversion that did not satisfy the substantial business activity requirement. Section 7874 ended most naked inversions (Kontrimas and Whit, 2010 and Hungerford, 2014).

Regulations governing section 7874's substantial business activity were introduced in 2006 but expired in 2009. In 2006, an EAG was considered to have substantial business activities if at least 10% of the EAG's employees, assets, and sales were from the foreign corporation's country of incorporation. In 2009, the 2006 regulation was replaced by another regulation that eliminated the safe harbor provision.

The 2009 regulations retained the pure facts-and-circumstance test which was used to evaluate firm's substantial business activities, i.e., the business conducted, property ownership, services performed, managerial activity, and the importance of the business activity within the foreign country (Kontrimas and Whit, 2010.)

After the 2008 U.S. election, some inverted corporations were afraid that a Democratic Congress and President Obama would amend U.S. laws regarding tax havens such as Bermuda and the Cayman Islands. Thus, some corporations that inverted in Bermuda and the Cayman Islands reincorporated in countries that had tax treaties with the U.S., such as Switzerland and Ireland. For example, Accenture had incorporated in Bermuda in 2001, then reincorporated in Ireland in 2009; Noble had incorporated in the Cayman Islands in 2002, then reincorporated in Switzerland in 2009.

Corporations reincorporated in countries that had tax treaties with the U.S. made it more problematic for Congress to pass new tax legislation aimed at inverted corporations (Hungerford, 2014). By reincorporating in European countries, inverted firms avoided the stigma associated with inverting in a tax haven, such as Bermuda and the Cayman Islands, while having access to a highly skilled workforce in countries that offered favorable business climates (Gelles, 2013).

The U.S. Treasury has used its authority to reduce the tax benefit of – and when possible, stop – tax inversions for some companies merging with a foreign company to eliminate or at least minimize the incentives to invert (The White House and Department of Treasury, 2016).

In 2012, the U.S. Treasury Department issued a temporary regulation, T.D. 9592. This regulation changed the threshold for EAG to meet the substantial business activity requirement of Section 7874. It required that the EAG have at least 25% of the group's employees, assets, and income to be located or derived in the relevant foreign country, rather than 10%. Some believed that T.D. 9592 effectively eliminated the substantial business activities exception to Section 7874, since most multinational corporate activities are relatively far-flung and not very concentrated, making it difficult for multinationals to satisfy the 25% threshold (IRS, 2012).

Gelles (2013) believed that changing the threshold requirements would cause firms to use acquisitions and mergers to meet the significant business requirements. In a merger, a U.S. firm can acquire a foreign firm and then renounce its U.S. citizenship and declare another country with a more favorable tax environment as its domicile (Patton, 2014).

The U.S. Treasury Department (2014) issued Tax Notice 2014-52 that targeted companies engaged in or contemplating tax inversions. The notice was designed to discourage U.S. firms from engaging in inversions and post-inversion activities which would reduce their U.S. taxes. The tax notice prevented inverted companies from:

- Accessing a foreign subsidiary's earnings while deferring U.S. tax using hopscotch loans.
- Restructuring a foreign subsidiary to access the subsidiary's earnings tax-free.
- Transferring cash or property from CFC to avoid U.S. taxes.
- Reducing their pre-inversion size by paying extraordinary dividends to meet the 80% threshold.
- Transferring assets to a newly formed foreign corporation that is spun off to shareholders, thereby avoiding the associated tax liabilities.

The U.S. Treasury Department (2015) issued Tax Notice 2015-79. The tax notice was issued after the announcement of a proposed $159 billion merger of Pfizer, Inc. and Allergen PLC. The purpose of this tax notice was to further tighten the anti-inversion rules of section 7874 and to reduce the tax benefits of inversion transactions. Notice 2015-79 limits:

- The ability of the inverting firms to "cherry pick" their tax residency. To satisfy the 25% business activities exception, the new foreign parent must be a tax resident in the foreign country in which it is created or organized.
- The ability of U.S. companies to inflate the new foreign parent corporation's size and therefore avoid the 80% rule by disregarding any assets acquired with a principal purpose of avoiding the 80% rule, regardless of whether the assets are passive assets.

Moreover, the White House and the U.S. Treasury (2016) stated that by using the U.S. Treasury's existing tax authority, the U.S. Treasury has been able to:

- Prevent inverted companies from accessing a foreign subsidiary's earnings while deferring U.S. tax using creative loans, which are known as "hopscotch" loans, and from restructuring a foreign subsidiary to access the subsidiary's earnings tax-free.
- Close a loophole to prevent inverted companies from transferring cash or property from a foreign subsidiary to the new parent to completely avoid U.S. tax.
- Make it more difficult for U.S. entities to invert by strengthening the requirement that the former owners of the U.S. entity own less than 80% of the new combined entity.
- Block a particularly blatant form of inversion known as a "third country" inversion, where a U.S. firm merges with a firm based in one foreign country, but then locates its tax residence in a third country—essentially cherry-picking the tax rules under which they operate.
- Address "serial inverters" by ensuring that firms cannot avoid the existing anti-inversion rules by acquiring foreign-owned corporate groups that themselves have grown larger through inversions or acquisitions of U.S. firms.
- Limit the ability of firms to strip earnings out of the U. S. by treating certain payments between related parties as non-deductible dividends instead of deductible interest payments and otherwise strengthening the rules characterizing financial instruments as debt or equity for tax purposes.

## Current Status of Inversions

The Obama administration made it more difficult for firms to benefit from inversions. In the past, U.S. firms could merge with smaller foreign firms and move their tax address out of the U.S. For example, if U.S. Corp merged with Half-Pint Shamrock, a small firm incorporated in say, Ireland, and then incorporated to form Half-Pint

Shamrock U.S. in Ireland, the newly incorporated parent firm would be outside the tax jurisdiction of the U.S. and pay taxes only on income earned in the U.S.

Now, U.S. firms must merge with a larger foreign firm,to the extent that U.S. shareholders no longer own 80% or more, by vote or value, of the newly formed foreign parent company. Otherwise, the newly formed foreign parent company is still treated as a domestic U.S. company for tax purposes and must pay taxes on income earned in the U.S. and repatriated income earned abroad. To benefit from an inversion, U.S. Corp must merge with a large corporation, say, Big Shamrock, so that after the merger, the former shareholders of U.S. Corp own less than 80%, by vote or value, of the new parent corporation, Big Shamrock U.S.

Some loopholes have been closed to make it more difficult for firms, say, U.S. Corp and Big Shamrock, to successfully merge and take advantage of tax inversions. In the past, U.S. Corp could intentionally reduce its value by paying extraordinary dividends and/or transferring assets to a subsidiary that is subsequently spun off to shareholders. Now, firms cannot pay extraordinary dividends and/or spinoff assets to downsize to ultimately reduce their value so that shareholders of U.S. Corp will own less than 80% of Big Shamrock U.S.

In the past, a firm like Half-Pint Shamrock could grow by merging with other corporations and with each merger increase its value and shareholder base. In fact, Half-Pint Shamrock could grow to be as large as, or larger than, Big Shamrock and later merge with U.S. Corp so that after the merger, the shareholders of U.S. Corp will own less than 80% of the newly merged company, Half-Pint Shamrock U.S. Afterwards, Half-Pint Shamrock U.S. would comply with tax inversions guidelines and no longer have to pay U.S. taxes on income earned abroad.

Now, firms cannot avoid anti-inversion rules by acquiring firms that themselves have grown larger through inversions or by acquiring U.S. firms. In other words, Half-Pint Shamrock cannot increase its size and value by acquiring U.S. firms and other inverted firms and then merge with U.S. Corp and comply with tax inversions guidelines.

In the past, firms could take advantage of third country inversions. For example, U.S. Corp and Big Shamrock could merge to form Big Shamrock U.S., but Big Shamrock U.S.'s tax residence could be in a third country other than the country where Big Shamrock U.S. was created or organized. Now, to be in compliance with inversion guidelines, Big Shamrock U.S. must be under the tax jurisdiction of the country where it was created or organized. In addition, at least 25% of the business activity of Big Shamrock U.S. must be in the country where it was created or organized.

As in the past, if U.S. Corp merges with Big Shamrock and the original owners of U.S. Corp own less than 60% of the newly merged company, no penalties are triggered, and it is viewed as perfectly acceptable. Afterwards, Big Shamrock U.S. must pay U.S. taxes on income earned only in the U.S. If the merger results in the former owners of U.S. Corp owning between 60% and less than 80% of Big Shamrock U.S., some adverse tax consequences could follow. (Presumably to discourage tax inversions, the U.S. Treasury Department did not state what the adverse tax consequences would be.)

## Future of Inversions

By using Tax Notices, the Treasury Department has made it more difficult and less beneficial for corporations to invert. In the Tax Notices, the Treasury Department has encouraged Congress to pass legislation that focuses on inversions. Hopefully, the federal government will address this issue. Both Democrats and Republicans in Congress believe that inversions are bad for the U.S.

Two proposals are being discussed that some believe will discourage future inversions. One proposal focuses on a border tax. In the border tax proposal, goods imported will be taxed, while income from exports will not be taxed. The border tax proposal assumes a tax on imports may reduce firms' willingness to establish cross-border manufacturing facilities. For example, Avery Corporation recently moved its machinery from Meridian, MS to a plant in Mexico to be more competitive. If imports are taxed, firms like Avery Corporation will be less willing to move their current manufacturing facilities or to build new facilities in other countries such as Mexico. Furthermore, since the income from exports is not taxed, more firms may ramp up their U.S. production. Firms that provide products or services for both domestic and foreign consumption will be tempted to shift costs to the domestic side of the company while shifting earnings to the export side of the company to lower their taxes. It seems reasonable that a border tax may discourage firms from shifting production to another country, but it is not clear that it will discourage firms from inverting if they can take advantage of lower tax rates abroad

Another proposal is to lower corporate tax rates on income earned in the U.S. and abroad. Some believe lowering corporate tax rates will reduce the benefits of inverting and will discourage inversions and make American firms more competitive. Moss (2017) reported that Chinese executives are worried that if the U.S. lowers its tax rates, American corporations would become more competitive.

The Institute of Taxation and Economic Policy (ITEP) (2017) reported that approximately $2.6 trillion has not been repatriated back to the U.S. Table 3 below presents the eleven firms with the most unrepatriated income. Except for General Electric, the firms have increased their unrepatriated income each year. ITEP believes that the Fortune 500 companies are avoiding up to $767 billion in federal income taxes.

Table 3: Unrepatriated Income of Eleven Major Corporations, 2014-2016

| Company | Total as of 2016 (in millions) | Total as of 2015 (in millions) | Total as of 2014 (in millions) |
|---|---|---|---|
| Apple | 230,200 | 200,100 | 137,100 |
| Pfizer | 197,096 | 193,587 | 175,798 |
| Microsoft | 124,000 | 108,300 | 92,900 |
| General Electric | 82,000 | 104,000 | 119,000 |
| IBM | 71,400 | 68,100 | 61,400 |
| Johnson & Johnson | 66,200 | 58,000 | 53,400 |
| Cisco | 65,600 | 58,000 | 52,700 |
| Merck | 63,100 | 59,200 | 60,000 |
| Google | 60,700 | 58,300 | 47,400 |
| Exxon Mobil | 54,000 | 51,000 | 51,000 |
| Proctor & Gamble | 49,000 | 45,000 | 44,000 |
| **TOTAL** | **1,014,296** | **958,587** | **850,698** |

Source: Institute of Taxation and Economic Policy http://www.itep.org/pdf/pre0327.pdf

Although firms have a significant amount of unrepatriated income abroad, they may not repatriate all the funds, especially if the lowered tax rates are still not competitive. Furthermore, some firms may need to use the funds to finance foreign operations. But to the extent income is repatriated, tax revenues will increase as firms pay taxes on the repatriated income. If firms increase their dividends, tax revenues will also increase to the extent shareholders pay taxes on dividends. For example, in 2017, Apple has more than $256 billion dollars in cash of which a significant portion is overseas. Apple recently increased its dividends and share buyback plan. Repatriation may also stimulate economic growth if firms use the funds to modernize and enlarge their current facilities and/or to build new factories, offices, distribution centers, etc.

If corporate taxes continue to be higher in the U.S. than in most countries, firms will be tempted to invert and shift income abroad. But as Congress and the executive branch work together in the coming months and years, the number of inversions will decrease as firms are forced to comply with stricter inversion requirements and have a more favorable tax environment in the U.S.

# REFERENCES

Avi-Yonah, Reuven S. (2002) "For Haven's Sake: Reflections on Inversion Transactions." *Tax Notes* 95 (12), 1793-9. http://repository.law.umich.edu/cgi/viewcontent.cgi?article=1813&context=articles

Badkin, Anton, Brent Glover and Oliver Levine. (2016) “Are Corporate Inversions Good for Shareholders?” http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2700987

Brigham, Eugene F. and Phillip R. Daves. (2016) *Intermediate Financial Management,* 12th edition. Cengage Learning. Boston.

Babkin, Anton, Brent Glover, and Oliver Levine. (2016) “Are Corporate Inversions Good for Stakeholders?” *Journal of Financial Economics*, Forthcoming. http://ssrn.com/abstract=2700987.

Brodwin, David. (2014, Aug 1) “Corporate Tax Inversion Leave You with the Bill.” *U.S. News and World Report*. http://www.usnews.com/opinion/economic-intelligence/2014/08/01/corporate-inversion-tax-avoidance-hurts-small-businesses-and-consumers

Chovart, Elizabeth. (2016) Expectations and Expatriation: A Long-run Event Study. University of Chicago, Public Law Working Paper No.445. https://ssrn.com/abstract=2309915.

Clemente, Frank, Hunter Blair and Nick Trokel. (2016) “Corporate Tax Chartbook: How Corporations Rig the Rules to Dodge the Taxes They Owe.” Economic Policy Institute http://www.epi.org/files/pdf/107544.pdf

Cloyd, Bryan C., Lillian F. Mills, and Connie D. Weaver. (2003) “Firm Valuation Effects of the Expatriation of U.S. Corporations to Tax-Haven Countries.” *The Journal of the American Taxation Association: Supplement* 25 (1), 87-109.

Desai, Mihir A. and James R. Hines Jr. (2002) “Expectations and Expatriations: Tracing the Causes and Consequences of Corporate Inversions.” *National Bureau of Economics Research*: http://www.nber.org/papers/w9057.pdf

Dowling, Grahame R. (2014) “Curious Case of Corporate Tax Avoidance: Is it Socially Irresponsible?” *Journal of Business Ethics.* 124 (1), 173-184.

Gelles, David. (2013, Oct. 8) “New Corporate Tax Shelter: A Merger Abroad.” *The New York Times. http://www.cnbc.com/2013/10/09/new-corporate-tax-shelter-a-merger-abroad.html*

Gjörup, Alexander and Gustav Nilsson. (2016) Corporate Tax Inversions and Reputational Costs- A Study on Board-Level Patriotism and the Decision to Expatriate. http://lup.lub.lu.se/student-papers/record/8883160

Hungerford, Thomas L. (2014) "Policy Responses to Corporate Inversions: Close the Barn Door before the Horse Bolts." Economic Policy Institute, Issue Brief #386, http://www.epi.org/publication/policy-responses-corporate-inversions/

Institue of Taxation and Economic Policy (2017) “Fortune 500 Companies Hold a Record $2.6 Trillion Offshore.” http://www.itep.org/pdf/pre0327.pdf

Kontrimas, Andrius R. and Walt Whit. (2010) “Corporate Tax Inversions - Location of the Multinational Parent Company, Anti-Inversion Legislation and Competitiveness of US-Based Multinationals.” Presented at the 13th Annual Tax Symposium, sponsored by the State Bar of Texas at Plano Texas. http://www.texastaxsection.org/LinkClick.aspx?fileticket=t2ZqNOMHQA0%3D&tabid=59

New York Bar Association Tax Section. (2002, May 24) “Report on Out-bound Inversion Transactions,” Report No. 1014. http://old.nysba.org/Content/ContentFolders20/TaxLawSection/TaxReports/1014report.pdf

Office of Management and Budget. (2016) Table 1.1—Summary of Receipts, Outlays, and Surpluses or Deficits (–): 1789–2021. https://www.govinfo.gov/content/pkg/BUDGET-2017-TAB/pdf/BUDGET-2017-TAB.pdf

Marples, Donald J. and Jane G. Graville. (2014) “Corporate Expatriation, Inversions, and Mergers: Tax Issues.” *Congressional Research Services*. http://democrats.waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/CRS%20report%20on%20inversions.pdf

Moss, Trefor. (2017, May 2) “China Keeps a Wary Eye on Trump’s Tax-Cut Plan.” *Wall Street Journal.* https://www.wsj.com/articles/why-china-fears-trump-tax-cuts-1493725300

Patton, David. (2014. Aug. 12) "Will Tax Inversions Sink the U.S. Economy?" http://www.forbes.com/sites/mikepatton/2014/08/12/will-tax-inversions-sink-the-u-s-economy/

U.S. Department of the Treasury. (2016) Historical Debt Outstanding - Annual 2000-2015. http://www.treasurydirect.gov/govt/reports/pd/histdebt/histdebt_histo5.htm

Ross, Stephan A., Randolph W. Westerfield and Bradford D. Jordan. (2017) *Essential of Corporate Finance* 9ed McGraw Education New York.

Rubin, Richard. (2015, Feb. 26) “Gilead Avoids Billions in U.S. Taxes on its $1,000–a-Pill Drug.” *Bloomberg*. http://www.bloomberg.com/news/articles/2015-02-26/gilead-avoids-billions-in-u-s-taxes-on-its-1-000-a-pill-drug

Seida, Jim A. and William F. Wempe. (2003) “Investors and Managers’ Reactions to Corporate Inversion Transactions.” http://papers.ssrn.com/sol3/papers.cfm?abstract_id=359820

Seida, Jim A. and William F. Wempe. (2004) “Effective Tax Rate Changes and Earnings Stripping Following Corporate Inversion” *National Tax Journal*. 57 (4), 805-28.: http://www.ntanet.org/NTJ/57/4/ntj-v57n04p805-28-effective-tax-rate-changes.pdf

Shah, Neil. (2014, Dec. 17) “Wealth Gap between America’s Rich and Middle Class-Families Widest on Record*.” Wall Street Journal* http://blogs.wsj.com/economics/2014/12/17/wealth-gap-between-americas-rich-and-middle-class-families-widest-on-record/?mod=ST1

The White House and U.S. Department of Treasury. (2016) *The Presidents’ Framework for Business Tax Reform: An Update*. https://www.treasury.gov/resource-center/tax-policy/Documents/The-Presidents-Framework-for-Business-Tax-Reform-An-Update-04-04-2016.pdf

U.S. Department of the Treasury. (2012) *Internal Revenue Bulletin: 2012-28*. Internal Revenue Service T.D. 9592. https://www.irs.gov/irb/2012-28_IRB/ar10.html

U.S. Department of the Treasury. (2014, Sept. 22) *Fact Sheet: Treasury Actions to Rein in Corporate Tax Inversions* http://www.treasury.gov/press-center/press-releases/Pages/jl2645.aspx

U.S. Department of the Treasury. (2015, Nov 19) *Fact Sheet: Additional Treasury Actions to Rein in Corporate Tax Inversions* https://www.treasury.gov/press-center/press-releases/Pages/jl0281.aspx

U.S. Department of the Treasury. (2016) Historical Debt Outstanding - Annual 2000-2015. http://www.treasurydirect.gov/govt/reports/pd/histdebt/histdebt_histo5.htm

Webber, Stuart. (2011) "Escaping the U.S. Tax System: From Corporate Inversions to Re-Domiciling." *Tax Notes International*. 63 (4), 273-295. http://corit-academic.org/wp-content/uploads/2011/12/Escaping-the-U.S.-Tax-System-Webber.pdf

Wells, Ken, Jonathan Allen and Richard Rubin. (2015, Jan. 14) "How an Obscure Tax Loophole Brought Down Obama's Treasury Nominee," *Bloomberg* http://www.msn.com/en-us/news/money/how-an-obscure-tax-loophole-brought-down-obama's-treasury-nominee