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Immoral Legislation and Tax Benefits for Expat Corporations Notes

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Note

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JENNIFER KARR

Corporate tax inversions are a growing tax avoidance trend. In a corporate tax inversion, an American corporation changes residence from the United States to a foreign jurisdiction, generally without much or any change in its business operations, in order to avoid paying U.S. taxes. Many industrialized countries, such as the U.K. and Ireland, now offer much lower corporate tax rates than the U.S., and have become popular destinations.

Traditionally, spectators have attempted to evaluate the morality of corporate decisions. In some ways, this makes sense, given recent Supreme Court cases such as Hobby Lobby and Citizens United, which have pushed corporations further toward personhood. At the same time, corporations are supposed to act in the best interest of shareholders, whether or not their actions are moral. For this reason, this Note ignores the moral nature of a corporation's decision to invert, and instead assesses the U.S. laws which permit such inversions. Laws are analyzed through the lens of the three main theories of morality—deontology, utilitarianism, and Aristotelean virtue—as well as corporate social responsibility.

In determining that corporate tax inversions not only have a negative impact on U.S. small businesses and general taxpayers, but often host countries as well, this Note offers four workable solutions. First, Congress should pass the Stop Corporate Inversions Act, which buffs the already active Internal Revenue Code § 7874. Second, the Internal Revenue Service should issue regulations in the spirit of Internal Revenue Code § 367 that will provide better guidelines for corporations that wish to move abroad. Third, the definition of “corporate residence” should be altered to include corporations with U.S. management. Fourth, intellectual property should be included in Subpart F. Finally, when passing legislation regarding corporate inversions, Congress must ask certain questions based in the three theories of morality in order to pass more moral laws. A moral body of laws will help to lessen the tax burden shifted to small businesses and general taxpayers by corporate tax avoidance. At the same time, a moral body of laws should provide benefits to corporations which are truly changing their place of residence for business purposes.

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Immoral Legislation and Tax Benefits for Expat Corporations

JENNIFER KARR*

I. INTRODUCTION

Public opinion tends not to favor corporations.¹ The IRS has not garnered high public opinion either, with only a fifty-eight percent approval rating, according to a Gallup poll.² In both cases, an essential unfairness lies at the heart of individual taxpayers' dissatisfaction.³ That's not surprising when, "in 1953 families and individuals paid 59 per cent of federal revenues and corporations 41 per cent . . . this ratio has now shifted to approximately 80:20 in favour of corporations."⁴

According to recent estimates, "the US federal authorities lose some \$170 billion annually to corporate tax avoidance."⁵ Senator Bernie Sanders compiled a list of the top ten most egregious corporate tax avoiders, with some corporations' tax rates being in the negative.⁶ Corporate inversions

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¹ See, e.g., Julia Battilana, *Multinational Corporations Under Fire From Public Opinion Campaigns*, <http://people.hbs.edu/jbattilana/ENGMay16.pdf> (2011) [<https://perma.cc/SJT6-UZXA>] (discussing protest movements against multinational corporations); Frank Newport, *Americans Similarly Dissatisfied with Corporations, Government*, GALLUP (Jan. 17, 2013), <http://www.gallup.com/poll/159875/americans-similarly-dissatisfied-corporations-gov.aspx> (last visited Feb. 21, 2016) [<https://perma.cc/JG6B-2TVD>] (discussing Americans' dissatisfaction with the influence of large corporations on the government).

² Jeffrey M. Jones & Lydia Saad, *Americans Sour on IRS, Rate CDC and FBI Most Positively*, GALLUP (May 23, 2013), <http://www.gallup.com/poll/162764/americans-views-irs-sharply-negative-2009.aspx> (last visited Feb. 21, 2016) [<https://perma.cc/JSE4-6LY8>].

³ See, e.g., Robert W. Wood, *Hate the IRS? You'll Love These Laws*, FORBES (Aug. 3, 2013), <http://www.forbes.com/sites/robertwood/2013/08/03/hate-the-irs-youll-love-these-laws/> (last visited Feb. 21, 2016) [<https://perma.cc/NQ9W-N5TT>] (detailing several scandals involving the IRS, including Lois Lerner's targeting of one political group over others and IRS seizures not complying with the law).

⁴ John Christensen & Richard Murphy, *The Social Irresponsibility of Corporate Tax Avoidance: Taking CSR to the Bottom Line*, 47 DEVELOPMENT 37, 38–39 (2004) [hereinafter *Social Irresponsibility*].

⁵ *Id.* at 38.

⁶ Bernie Sanders, *Top 10 Corporate Tax Avoiders*, BERNIE SANDERS: UNITED STATES SENATOR FOR VERMONT, <http://www.sanders.senate.gov/top-10-corporate-tax-avoiders> (last visited Apr. 12, 2016) [<https://perma.cc/M4RQ-M38M>].

are an increasingly popular form of corporate tax avoidance.⁷ In possibly its simplest description, a corporate inversion is a “transaction[] in which a U.S.-based company changes its place of incorporation from the United States to a foreign jurisdiction, often without an accompanying change in its business operations . . . primarily to reduce U.S. taxation of foreign and even domestic income.”⁸

Frequent criticisms of corporate inversions tend to involve assessing the morality (or lack thereof) of corporations engaging in the practice.⁹ They have been described by opponents as:

immoral, wrong, contemptible, the most blatant example of abusive corporate tax shelters that increasingly plague our country, outrageous, an unpatriotic tax dodge, a pure tax avoidance mechanism that is very bad public policy, a stealth weapon used by management to evade corporate accountability, disgusting, rotten, reprehensible behavior, awful, one of the ugliest issues that anybody has seen for a while, a crisis that is reaching epidemic proportions, troubling from a policy viewpoint, and a bad example of corporate tax cheating.¹⁰

Even President Obama has used the term “unpatriotic tax loophole” when referring to the allowance for inversions.¹¹ While many debate the morality of corporations taking advantage of legal tax “loopholes,” this Note, rather, looks inward at the domestic laws which both create the, at least perceived, need for inversions, and the ability for corporations to engage in them. Assessing the morality of corporations essentially is fruitless, as corporations are meant to act in the best interest of shareholders.¹² But democratic governments should act in ways that benefit

⁷ DONALD J. MARPLES & JANE G. GRAVELLE, CONG. RESEARCH SERV., R43568, CORPORATE EXPATRIATION, INVERSIONS, AND MERGERS: TAX ISSUES (2015) 1–2 (discussing a “second wave” of inversions).

⁸ Joseph A. Tootle, *The Regulation of Corporate Inversions and “Substantial Business Activities”*, 33 VA. TAX REV. 353, 354 (2013).

⁹ See, e.g., *Social Irresponsibility*, *supra* note 4, at 39 (arguing that various types of corporate tax avoidance are unethical); Susan H. Godar, Patricia J. O’Connor, & Virginia Anne Taylor, *Evaluating the Ethics of Inversion*, 61 J. BUS. ETHICS 1 (2005) (finding corporate inversions to be unethical under deontology and possibly utilitarianism as well) [hereinafter *Ethics of Inversion*].

¹⁰ Hale E. Sheppard, *Fight or Flight of U.S.-Based Multinational Businesses: Analyzing the Causes for, Effects of, and Solutions to the Corporate Inversion Trend*, 23 NW. J. INT’L L. & BUS. 551, 558 (2003) (internal quotation marks omitted) [hereinafter *Fight or Flight*].

¹¹ Damian Paletta & Dana Mattioli, *Double Punch for Inversion Deals*, WALL ST. J. (Aug. 5, 2014 7:03 PM), <http://www.wsj.com/articles/u-s-treasury-exploring-ways-to-deter-tax-inversions-without-congress-1407265800> [https://perma.cc/5LBY-RYPK].

¹² See, e.g., August Jackson, *Does a Corporation Owe Fiduciary Duty to Shareholders?*, CHRON, <http://smallbusiness.chron.com/corporation-owe-fiduciary-duty-shareholders-70243.html> [https://per

the people.¹³ For this reason, it is the legislation that permits corporations to avoid taxes which should be assessed, rather than the corporations themselves.

Understanding the moral nature of corporate inversion legislation requires an analysis of the effects of said laws as well as the process by which they come to fruition. Such analysis will shed light on the problematic nature of the status quo and provide insight as to how legislators can write more effective and beneficial laws.

Part II of this Note examines theories of morality and the history of corporate inversions. The major theories—utilitarianism, deontology, and Aristotlean Virtue—are used as explorative tools for breaking apart corporate inversion regulation over the past twenty-five years. It is important to note that, as it is the laws themselves which will be under a microscope, a brief analysis of whether state actors can have a moral component will be necessary; this question, for the most part, is answered in the affirmative. These theories provide a way to better understand the persisting problems with inversion legislation and provide guidance in creating a more moral body of laws.

Part III discusses the problems in the current system. A large part of why present legislation falls short is its piecemeal nature. One might picture it as a sinking ship with a growing number of holes. Instead of focusing on the big picture, legislators are focusing on slowly patching each individual hole, as more and more come into being. Further, Congress seems reluctant to fully commit to any specific type of regulation. This lack of focus and commitment have led to large companies continuing to move abroad, which is a loss in tax revenue for the U.S.

Part IV offers solutions for both creating more moral laws, and for altering the current laws in ways that will best benefit the country. In a theoretical sense, it would be beneficial for politicians to examine the moral nature of legislation passed. Perhaps more pragmatically (and realistically), however, there are several more concrete, workable solutions which should help to lessen the rush to invert. Current corporate inversion law should be buffed by the passage of legislation which was proposed in 2014. That legislation would strengthen § 7874. Congress should also alter the definition of corporate residence and offer clear regulations for corporations which truly want to move abroad. Finally, intellectual property (IP) should no longer be excluded from Subpart F.

On one hand, these changes would make it more difficult for U.S.

ma.cc/57E6-UCHB] (discussing a corporation's fiduciary duties to shareholders) (last visited Feb. 21, 2016).

¹³ What is Democracy?, LECTURE AT HILLA UNIVERSITY FOR HUMANISTIC STUDIES (2004), <https://web.stanford.edu/~ldiamond/iraq/whaisdemocracy012004.htm> (last visited Feb 14, 2016) [<https://perma.cc/67PM-5VRX>].

corporations to invert. On the other hand, they would make it easier for truly international corporations to change their place of corporate residence. As will be explored further in this Note, some proposed solutions are simply not workable—for example lowering the corporate tax rate in order to compete with European countries would likely lead to an unsustainable burden on small businesses and individual taxpayers. There must be clear guidelines for corporations wishing to change their corporate residence, and these residency changes ought to be evaluated on a case-by-case basis.

Finally, Part V concludes this Note.

II. THE CORPORATION, THE INVERSION, AND MORALITY

A. *Evolution of the Modern Corporation*

Summarizing the evolution of the modern corporation can lend some insight as to why our laws exist as they do today. While modern corporations are seen as for-profit businesses, prior to the nineteenth century they were actually “formed chiefly for political or charitable purposes.”¹⁴ At the beginning of United States history, state legislatures chose participants and terms for corporations, which were established by the state issuing special acts.¹⁵ These state-created corporations formed “in order to address public needs, such as transportation or infrastructure.”¹⁶ Because of public displeasure and the burden placed on the legislative system, incorporation became available to everyone in the early nineteenth century—though each state government had to create its own incorporation statutes.¹⁷

In the twentieth century, incorporation statutes moved further and further away from government regulation.¹⁸ New Jersey was the first state to allow corporations to hold stock in other corporations, making many modern corporate structures possible.¹⁹ The states also permitted corporations to: exist perpetually, organize for any (lawful) purpose except banking, amend certificates of incorporation, own stock in other corporations, own unlimited land, and merge with other corporations.²⁰ Beginning in the late nineteenth century, states “race[d]” to deregulate.²¹ Deregulation meant attracting more corporations to the state, bringing

¹⁴ WILLIAM T. ALLEN ET AL., COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION 90 (4th ed. 2012).

¹⁵ *Id.* at 90.

¹⁶ *Id.* at 91.

¹⁷ *Id.*

¹⁸ *Id.* 92.

¹⁹ *Id.*

²⁰ *Id.* at 92–93.

²¹ *Id.* 93.

business as well as corporation franchise fees to the state.²² In more recent history, however, the judiciary and federal securities laws have imposed some regulations on public corporations, in the “flavor of early corporation law.”²³ Yet, with Delaware as the most popular state for incorporation, the Delaware General Corporation Law (DGCL) is a “nonregulatory, enabling statute with few mandatory features.”²⁴

Notably, since corporations now have a history of being designed by the states, with federal commissions playing a regulatory part, a tension between federal and state governments may reduce the ability of the federal government to act morally when lawmakers feel they must defer to the states.

B. *The United States’ System*

While some countries employ a territorial system of taxation,²⁵ the United States imposes a worldwide system.²⁶ In some cases, this results in double taxation because corporations are taxed on: (1) domestic income and (2) foreign income.²⁷ To avoid double taxation, the United States issues limited foreign tax credits equal to the amount of taxes the corporation paid on their foreign income.²⁸

Further, the U.S. is a liberal market economy, which emphasizes “arm’s length relationships and public trading.”²⁹ A feature of the liberal market economy is its flexible regulatory structure, which “benefits industries targeting low costs and those operating in sectors characterized by radical innovation.”³⁰ Liberal market economies best fit within the

²² *Id.*

²³ *Id.* at 94.

²⁴ *Id.* at 93 (internal quotation marks omitted).

²⁵ See Tootle, *supra* note 8, at 357 (“Under a territorial system, a nation taxes only income from sources within its boundaries.”).

²⁶ See *id.* at 356 (describing the United States’ worldwide system of taxation).

²⁷ See *id.* (“Under a worldwide system, a nation taxes both the domestic income of its citizens and residents, and the income of its citizens and residents that is earned in foreign nations.”); *Fight or Flight*, *supra* note 10, at 552–53 (“U.S. tax applies to income earned by the foreign corporation that is ‘effectively connected’ with the ‘conduct of a trade or business’ within the United States. In addition, a foreign corporation is generally subject to a thirty percent tax when it receives certain passive income derived from sources within the United States.”).

²⁸ See Tootle, *supra* note 8, at 356 (“[T]he United States uses a system of foreign tax credits [which] . . . reduces a citizen’s or resident’s U.S. income tax liability by the amount of foreign income taxes paid on foreign source income.”).

²⁹ Reuven S. Avi-Yonah, *Corporate Taxation and Corporate Social Responsibility*, 11 N.Y.U. J. LAW & BUS. 1, 17 (2009) [hereinafter *Taxation*]. Other nations can be corporatist, like Germany and Japan, relying on “tightly integrated private and networked associations to resolve significant dilemmas of economic integration,” or statist, like France, “depend[ing] on hierarchical solutions in resolving coordination problems.” *Id.* at 16.

³⁰ Reuven S. Avi-Yonah, *Corporate Social Responsibility and Strategic Tax Behavior*, 6 (John M. Olin Ctr. for Law & Econ., Working Paper No. 69, 2006) at 10 [hereinafter *Strategic Tax Behavior*].

aggregate or “nexus of contracts” view of the corporation.³¹ Proponents of the aggregate view argue that the corporation is “an aggregate of its members or shareholders” (as opposed to a “creature of the state” under the artificial entity theory, or a “separate entity controlled by its managers” under the real entity theory).³² The implications of subscribing to the aggregate view will be discussed, *infra*.

C. *From the First Corporate Tax Inversion to the Modern Inversion*

While there are several different models of corporate inversions,³³ the first known inversion occurred in 1983 by McDermott, Inc.³⁴ McDermott had a wholly-owned Panamanian subsidiary.³⁵ That subsidiary issued to McDermott shareholders an amount of common stock equal to ninety percent of its voting power.³⁶ In exchange, the Panamanian subsidiary received about sixty-eight percent of the stock of its parent company.³⁷ In effect, McDermott became an international corporation through its Panamanian subsidiary, but the American shareholders held most of the power over the company.

After the Internal Revenue Service (IRS) unsuccessfully challenged the McDermott inversion, Congress enacted Section 1248(i)³⁸ of the Internal Revenue Code (“IRC” or “the Code”).³⁹ Essentially, Section 1248(i) treats an exchange of stock between domestic shareholders of a foreign corporation and the foreign corporation as a dividend.⁴⁰ So, in an exchange like McDermott’s, the shares should be treated as though they had first

³¹ See *Taxation*, *supra* note 29, at 12, 17 (“The liberal model . . . best fits the aggregate theory of the firm.”).

³² *Id.* at 12, 15.

³³ In stock transactions, “the shareholders of a U.S. corporation exchange their shares for stock in a foreign corporation.” Tootle, *supra* note 8, at 363. Reincorporations, or asset transactions, involve a U.S. corporation merging with its foreign parent, and the foreign parent surviving. *Id.* In a drop-down transaction, “the U.S. corporation transfers its assets to the foreign parent through a reincorporation and the foreign parent immediately contributes some of those assets to a newly formed U.S. subsidiary.” *Id.* A spin-off involves a multinational creating a foreign subsidiary “to which is contributes the business it desires to divest.” *Id.* at 364.

³⁴ See *id.* at 364 (discussing the McDermott transaction). This first corporate inversion was structured as a stock transaction. *Id.* at 364–65. Notably, the McDermott inversion has lagged the S&P eighty-five percent since their inversion was completed. Kevin Drawbaugh, “*Inversions*” *Don’t Always Benefit Investors*, WASH. POST., Aug. 19, 2014, at A09.

³⁵ See Peter Canellos, *Acquisition of Issuer Securities by a Controlled Entity: Peter Pan Seafoods, May Department Stores, and McDermott*, 45 TAX LAWYER 1, 10 (1991) (discussing McDermott’s transaction with its Panamanian subsidiary).

³⁶ *Id.* at 10.

³⁷ *Id.*

³⁸ 26 U.S.C. § 1248(i) (2012).

³⁹ See Tootle, *supra* note 8, at 365 (“Although the Service was unsuccessful in its challenge [against McDermott], the transaction prompted Congress to enact Section 1248(i) of the Code.”).

⁴⁰ 26 U.S.C. § 1248(i) (2012).

been issued to the domestic McDermott corporation, and then distributed to shareholders as dividends.⁴¹ The result would be taxation on the dividends.

Following the enactment of Section 1248(i), in 1989, Congress enacted Section 163(j),⁴² which was “designed to deter interest stripping transactions.”⁴³ However, since it only applies to corporations with debt to equity ratios of 1.5 to 1 or more, “it is generally accepted that the provision does not deter interest stripping transactions.”⁴⁴

After a second corporation inverted in 1994, the IRS “issued new regulations under Section 367(a)⁴⁵ of the Code that made transfers of stock of domestic corporations to foreign corporations taxable if, in the aggregate, all U.S. transferors owned 50% or more of the stock of the foreign parent by vote or by value immediately after the exchange.”⁴⁶ Under Section 367(a), transfers of stock from a U.S. corporation to a foreign corporation are taxable.⁴⁷

Inversions resurfaced with gusto in the late 1990s and early 2000s.⁴⁸ Within the American Jobs Creation Act of 2004⁴⁹ lies Section 7874⁵⁰ of the IRC. Section 7874 applies to “corporate inversions after which a certain percentage of former shareholders of the U.S. company own stock in the foreign parent company, or the ‘surrogate foreign corporation’ in the statute’s language.”⁵¹

There are two main provisions in Section 7874.⁵² First, if shareholders who originally held stock in the domestic corporation, or former corporate partners who owned capital or profit interest in the domestic corporation,

⁴¹ Canellos, *supra* note 35, at 10–11 (explaining how Section 1248(i) would apply to an inversion like McDermott’s).

⁴² 26 U.S.C. § 163j (2012).

⁴³ Tootle, *supra* note 8, at 365. In an interest stripping transaction, either the new foreign parent or another related party extends a loan to the U.S. operating company. The U.S. operating company then pays what is nominal “interest” to its parent and deducts the amount paid from its U.S. source taxable income. Ordinarily, the foreign parent is obligated to pay the 30% U.S. withholding tax on the interest it receives from the U.S. operating company. Through careful use of international tax treaties, however, the U.S. tax liability on the interest paid to the foreign parent may be greatly reduced or altogether avoided. Further, it is possible that under the foreign nation’s laws, the foreign parent corporation will not be taxed on the interest received. *Id.* at 361–62.

⁴⁴ *Id.* at 366.

⁴⁵ 26 U.S.C. § 367(a).

⁴⁶ Tootle, *supra* note 8, at 366.

⁴⁷ 26 U.S.C. § 367(a).

⁴⁸ Tootle, *supra* note 8, at 366–67 (“Despite [the regulations’] effect, more large corporations inverted during the latter half of the 1990s, including Triton Energy, Tyco, Fruit of the Loom, Gold Reserve Corporation, Transocean, and White Mountain Insurance Group. The economic downturn of the early 2000s reduced the impact of the section 367(a) regulations . . . which may have prompted more inversions.”).

⁴⁹ American Jobs Creation Act of 2004, Pub. L. No. 108-357, 118 Stat. 1418.

⁵⁰ 26 U.S.C. § 7874 (2012).

⁵¹ Tootle, *supra* note 8, at 368.

⁵² 26 U.S.C. § 7874(a)(2) (2012).

own sixty percent of the stock in the foreign corporation, the foreign corporation is considered a surrogate foreign corporation.⁵³ Second, if either of the same groups of people own eighty percent of the foreign company's stock, then the foreign company is treated as a domestic corporation.⁵⁴ However, there is an exception. In both of these cases, the foreign corporations are not considered foreign surrogates or domestic corporations if they have "substantial business activity" in the foreign country.⁵⁵ Because of the "substantial business activity" rule, and because previously popular inversion countries (like the Cayman Islands and Bermuda) do not have a lot of economic activity, countries like Ireland, Switzerland, and the UK are now popular destinations.⁵⁶

In a sixty-percent inversion, the yearly taxable gain cannot be less than the inversion gain.⁵⁷ "Inversion gains include any gain on property or stock transferred to the foreign parent, and any licensing income on that property, without offset for losses or credits other than the foreign tax credit."⁵⁸ Otherwise, these inversions are not "pure" inversions and are treated "leniently."⁵⁹

Section 7874 hasn't been entirely prohibitive, as corporations can simply keep their corporate structure as is while reinvesting revenue overseas, which allows for indefinite deferral on tax payments.⁶⁰ Further, multinational corporations have shifted about seventy-five billion dollars out of the country by "investing in active sectors like Ireland manufacturing."⁶¹

Finally, according to Tyler Dumler, Section 7874 may only have diverted some possible inversions to other tax avoidance tactics:

[Multi-national corporations] are now eroding the U.S. tax revenue base through alternative methods. Such methods include: income trapping using indefinite deferrals of active income in foreign countries; repatriation of excessive foreign tax credits; avoidance of taxation on holding companies in low-tax jurisdictions using "check the box" regulations and hybrid entities; continuing to increase debt shares in high-tax

⁵³ 26 U.S.C. § 7874(a)(2)(B)(ii)(I).

⁵⁴ 26 U.S.C. § 7874(b).

⁵⁵ 26 U.S.C. § 7874(a)(2)(B)(iii).

⁵⁶ MARPLES & GRAVELLE, *supra* note 7, at 6 (discussing how the business activity exemption has caused some corporations to invert in European countries).

⁵⁷ 26 U.S.C. § 7874(a)(1).

⁵⁸ Tootle, *supra* note 8, at 369.

⁵⁹ *Id.* at 369–70.

⁶⁰ 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. 89, 89 (2012).

⁶¹ *Id.* at 89–90.

jurisdictions to take advantage of applicable interest credits; and related tax planning behavior.⁶²

Current Congressional considerations will be discussed, *infra*. Now that the current status of inversions and corporate inversion law has been discussed, an exploration of moral theories will show how our laws should be evaluated.

D. Basics of Morality

For the purposes of this note, I focus the discussion mainly on utilitarianism and Kant's deontological theory, while also touching on Aristotelian virtue.⁶³ A discussion of whether or not these theories of morality and ethics are truly applicable to state actors will be reserved for later in the Note.⁶⁴

1. Utilitarianism

Utilitarianism describes a set of consequentialist theories; consequentialism describes moral theories where normative properties depend only on consequences, whereas utilitarian theories focus on aggregate welfare.⁶⁵ Under utilitarianism, "[o]ur basic ethical concern is to bring it about, so far as we can, that there is more welfare or utility in the world rather than less, and, in the simplest version of utilitarianism, we should simply act in the most efficient way to bring that about."⁶⁶ Because utilitarianism is a type of consequentialism,⁶⁷ the moral goodness of an act depends not on the actor's motives or intentions, but on the outcome, or consequence, of her action.⁶⁸ So, for example, if an actor knew that killing one person would save one hundred other people, under a utilitarian moral theory that killing would likely be considered morally just.

To be clear, though utilitarianism is a form of consequentialism, the two are not synonymous. Consequentialists believe that, by any means, an

⁶² *Id.* at 94–95.

⁶³ These are the three theories that generally influence public policy debates. STEPHEN UTZ, TAX POLICY: AN INTRODUCTION AND SURVEY OF THE PRINCIPAL DEBATES 35 (1993) [hereinafter TAX POLICY]. For a more in depth discussion of these theories, see, for example, Stephen Utz, *Chapter Three: How Taxes Affect People's Welfare*, in TAX POLICY: AN INTRODUCTION AND SURVEY OF THE PRINCIPAL DEBATES (1993); Bernard Williams, *Chapter Three: Foundations: Well-Being*, in ETHICS AND THE LIMITS OF PHILOSOPHY; Bernard Williams, *Chapter Five: Styles of Ethical Theory*, in ETHICS AND THE LIMITS OF PHILOSOPHY (1985).

⁶⁴ See *infra* Part II.E.

⁶⁵ See WILLIAMS, *supra* note 64, at 75 ("All the variants [of utilitarians] agree on aggregating welfare, that is to say, adding together in some way the welfare of all the individuals involved.")

⁶⁶ *Id.* at 77.

⁶⁷ *Id.* at 35–36 (referring to utilitarianism as a type of "welfarist consequentialism").

⁶⁸ See TAX POLICY, *supra* note 63, at 35 ("Consequentialism is the view that in evaluating alternative courses of conduct as good or bad, not with respect to other goals but as such, we need only consider the consequences of the available choices.")

end that produces good is morally good (but there is disagreement about how to determine which consequences are “good” and which are “bad”).⁶⁹ Utilitarians care about producing the greatest amount of pleasure (mental pleasure, specifically, according to John Stuart Mill) for the greatest amount of people.⁷⁰

Mill emphasized mental pleasure as utility, and therefore mental pleasures as uniquely valuable.⁷¹ In his *Principles of Political Economy*, he argues that, in matters of taxation, “whatever sacrifices [the government] requires from [persons or classes] should be made to bear as nearly as possible with the same pressure upon all, which, it must be observed, is the mode by which least sacrifice is occasioned on the whole.”⁷² Further, he argued, “[e]quality of taxation . . . means equality of sacrifice.”⁷³ This, however, poses further questions. What exactly does “equality of sacrifice” entail? Surely a middle class person paying a fifteen percent marginal tax rate still bears more of a relative burden than a billionaire paying a tax rate as high as even ninety percent. A much more in depth discussion of this particular point is beyond the scope of this note, but the question should be considered when discussing possible legislative changes.

A problem with evaluating actions from a utilitarian moral theory is that the ultimate consequences of an action may not be clear for some time.⁷⁴ As an extreme example, consider a person with a time machine. She utilizes the time machine to return to early twentieth century Germany and kills Hitler. By doing this, she saves the lives of more than six million people. While it seems like the death of one has clearly produced the greatest amount of happiness by saving the lives of so many others, what if, as a result of the Holocaust not happening, an even more expansive genocide takes place in the future? This very problem is more than evident in recent anti-inversion legislation. While lawmakers may (or may not) believe they are creating laws that will benefit the greatest amount of people, they may actually be harming more than they are helping. For example, consider a raise in the corporate tax for the purpose of funding more social programs. Suppose that, at first, the extra revenue does, in fact, fulfill this purpose. But suppose then, that corporations find ways to shelter

⁶⁹ See Corey A. Ciochetti, *Tricky Business: A Decision-Making Framework for Legally Sound, Ethically Suspect Business Tactics*, 12 CARDOZO PUB. L. POL’Y & ETHICS J. 1, 9 (2013) (“[T]he means . . . to obtain [an] end are morally irrelevant as long as good is produced.”).

⁷⁰ See *id.* at 11 (“To Mill, good actions were those that produce the greatest mental pleasure (happiness or well-being) and bad actions are those that tend to produce mental pain (unhappiness).”).

⁷¹ See JOHN STUART MILL, *PRINCIPLES OF POLITICAL ECONOMY* 42, 445 (1848) (discussing value, nature, and scarcity).

⁷² *Id.* at 804.

⁷³ *Id.*

⁷⁴ See Ciochetti, *supra* note 69, at 12 (“[T]he consequences of an action are not always clear and it is exceptionally difficult to understand how these uncertain consequences will help or harm other people.”).

their money, resulting in an actual reduction of overall revenue collected, and new social programs that can no longer be sustained. Though the lawmakers might have had pure intentions, their action resulting in a negative consequence cannot be considered moral from a utilitarian viewpoint.

Notably, business ethics professor Corey A. Ciochetti writes, “evaluating the greatest good for the greatest number of people is a time consuming process. Many moral decisions require a much faster answer.”⁷⁵ Time is an interesting factor when applied to state actors who have much greater resources than the average person and who act at a different pace entirely than the average person.

2. Deontology

Conversely, while deontology does take consequences into account, the real focus of an act’s moral nature lies in the actor’s intention or motivation.⁷⁶ According to Kant, “[n]othing in the world—indeed nothing even beyond the world—can possibly be conceived which could be called good without qualification except a *good will*.”⁷⁷ So, if an actor’s intent in killing someone is nothing other than to take their life, then the act would most likely not be considered moral under a deontological view, even if the unintended consequence is to save the lives of others. Think of deontology as choosing the “right” thing to do instead of the “good” thing to do.⁷⁸ That’s all fine when applied to individuals, but questions arise when applying deontology to governments (especially democratic governments).

Under Kant’s theory of deontology, an action is only moral if both the action and the reason for the action “can be willed as universal law.”⁷⁹ Ciochetti identifies three steps in determining whether an action is moral under Kantian theory: (1) “define a . . . statement[] that states your reason for acting as you propose;” (2) ask “can this decision be universalized?”; (3) ask “would you want to live in such a world?”⁸⁰ So, under a Kantian view of morality, it would be imperative to know the reason for the government’s action, to consider whether such laws can be universalized, and to determine whether such a world would be beneficial. The high probability that corporate inversions are deontologically immoral is

⁷⁵ *Id.*

⁷⁶ TAX POLICY, *supra* note 63, at 37 (“The essential feature of deontological ethical theories is their insistence on the role of intention or motivation in giving value to actions and, derivatively, to the consequences of action.”).

⁷⁷ IMMANUEL KANT, FOUNDATIONS IN THE METAPHYSICS OF MORALS 393 (1785).

⁷⁸ Ciochetti, *supra* note 69, at 13 (“[E]mphasis is on the ‘right thing to do’ rather than the ‘good thing to do.’”).

⁷⁹ *Ethics of Inversion*, *supra* note 9, at 3.

⁸⁰ Ciochetti, *supra* note 69, at 15–16.

obvious.⁸¹ But, with the (arguably optimistic) understanding that corporations govern themselves to benefit shareholders and the U.S. government exists only by and for the people, surely corporations and governments ought to have different, even competing, motivations.

“Kant argued that people have the capacity to act out of [a] sense of duty because people have the ability to reason.”⁸² Can governments reason? Certainly, governments are made up of people, who presumably have the ability to reason. And each legislator in a democratic government is elected by a majority of her constituents, who also have the ability to reason. But laws are not made by single representatives, which leaves us with the question: can a large group of lawmakers be considered in the same light as an individual? This question will be discussed *infra*.

3. *Virtue*

To evaluate one’s morality from Aristotle’s virtue-based perspective, one must evaluate the actor as a whole. The consequences of an actor’s actions and the intentions of any one given act are less important than an individual’s whole moral past.⁸³ So, if an actor who has generally acted with bad will and to negative consequences commits a good act, that act will not be considered *as good* as if an actor who has generally acted with good will and to positive consequences commits the same act.⁸⁴ Put more eloquently, “[f]or Aristotle . . . practical reason required the dispositions of action and feeling to be harmonized; if any disposition was properly to count as a virtue, it had to be part of a rational structure that included all the virtues.”⁸⁵

Unlike utilitarianism and deontology, Aristotelean virtue does not base itself on any given act. Put succinctly, while a utilitarian might ask, “What was the outcome of his action?” and a deontologist might ask, “What was the motivation for her action?,” under the virtue-based theory, one might ask, “Is he living his life with the goal of being a good person?”⁸⁶ A virtuous person is one with good character.⁸⁷

But applying virtue to states is problematic when one considers this definition of virtue: “an acquired human quality the possession and exercise of which tends to enable us to achieve those goods which are

⁸¹ *Ethics of Inversion*, *supra* note 9, at 3 (claiming that under Kantian deontology, corporate inversions are immoral).

⁸² Ciochetti, *supra* note 69, at 14.

⁸³ UTZ, *supra* note 63, at 38.

⁸⁴ *See id.* (“Not only the moral habits of the agent, but the opportunities for forming them are important in assessing how good the individual acts of this person are, and how good the person as a whole is.”).

⁸⁵ WILLIAMS, *supra* note 63, at 36.

⁸⁶ Ciochetti, *supra* note 70, at 18–19.

⁸⁷ *See id.* at 19 (“The key to [v]irtue [e]thics is the development of . . . a good character.”).

internal to practices and the lack of which effectively prevents us from achieving any such goods.”⁸⁸ States are obviously, by definition, not human. Suppose “human” was left out of the definition. Can states “acquire” qualities? Certainly over time governments have changed—some for the better and some for the worse. Given the advances in social justice made since the inception of our nation, it would be easy to argue that the United States has evolved for the better.

Yet, Aristotlean virtue is even harder to apply to states when one considers that “for Aristotle virtue was an internalized disposition of action, desire, and feeling . . . It involves the agent’s exercise of judgment . . . [and] favorable and unfavorable reactions to other people, their characters and actions.”⁸⁹ Although Aristotle referred to the individual, it is worth considering the implications of applying his theory to governmental bodies. In any case, applying Aristotlean virtue to state actors is challenging, in the least.

4. Corporate Social Responsibility

Worthy of note, though perhaps not incredibly helpful, is a critical theory specific to corporations called Corporate Social Responsibility (“CSR”). CSR theorists examine “the obligations and inclinations, if any, of corporations organized for profit, voluntarily to pursue social ends that conflict with the presumptive shareholder desire to maximize profit.”⁹⁰ For instance, in one CSR article, the writers reject the idea that there should be no distinction between the legality and morality of corporate tax avoidance.⁹¹ Interestingly, the writers of that same article conclude that, in order to curb tax avoidance and other harmful tax practices, global initiatives (not corporations themselves) must be utilized to create a framework to “balance the need [of] sovereign states to protect their tax revenues from aggressive tax avoidance, with a respect for the right of democratic governments to determine a tax rate appropriate to their circumstances.”⁹² Finally, the writers advocate for a worldwide, rather than

⁸⁸ ALASDAIR MACINTYRE, *AFTER VIRTUE: A STUDY IN MORAL THEORY* 190–91 (2d ed., 1984). Virtue ethics focus on a definition of character which is based upon a determined list of twelve good attributes that fall into a golden mean between two vices (e.g., bravery is a virtue between the vices of cowardice and foolhardiness). This list is not determined in any principled or analytical way. This poses further questions when determining what values would comprise the character of a virtuous state. *Aristotle’s Ethics Table of Virtue and Vices*, CENTRAL WASH. UNIV., http://www.cwu.edu/~warren/unit1/aristotles_virtues_and_vices.htm (last visited Mar. 31, 2016) [<https://perma.cc/Q5AX-X6HR>].

⁸⁹ WILLIAMS, *supra* note 63, at 35–36.

⁹⁰ David L. Engel, *An Approach to Corporate Social Responsibility*, 32 *STAN. L. REV.* 1, 5–6 (1979).

⁹¹ See *Social Irresponsibility*, *supra* note 4, at 39 (“It is not possible to be ethical in one area of business conduct and to act otherwise in another area.”).

⁹² *Id.* at 42.

a territorial system.⁹³

But, while CSR theorists comment on the ethics and morality of corporate actions and on possible solutions to problems, they stop short of examining the morality and ethics of the laws themselves. Rather, it seems that they view laws as tools, instead of things with innately measurable morality. In fact, this is one of the criticisms in international tax expert Reuven Avi-Yonah's working paper, *Corporate Social Responsibility and Strategic Tax Behavior*. Avi-Yonah points out the "illegitima[cy]" of CSR under the aggregate view of the corporation.⁹⁴ Continuing under the aggregate view, he further argues, "if corporations are not permitted to engage in CSR, then all social responsibility functions devolve on the state . . . But if corporate managers are required to minimize tax payments as much as possible, that could mean that the state is left without adequate resources to fulfill its governmental function."⁹⁵ Notably, most European Union governments utilize CSR programs.⁹⁶

Given Avi-Yonah's argument, if, as in a liberal market economy, the United States adopts an aggregate view of the corporation, this creates a catch-22. If the moral responsibility to perform all socially conscious functions falls on the state, then it would follow that it is the state's responsibility to collect as much revenue as possible in order to fund social programs. Yet, according to Avi-Yonah, the aggregate view leaves the corporation with no moral responsibility to pay taxes not required by the state.⁹⁷ So, either CSR *is* illegitimate as a critical theory, or one-hundred percent of the moral responsibility falls on the state. Avi-Yonah gives the following example of an instance where it is only the state's obligation to remedy a crisis. In the event of a health crisis, corporations owe no obligation to address it.⁹⁸ However, the resources the state needs are funded by taxes—many of which are collected from corporations.⁹⁹ While Avi-Yonah argues that, despite the aggregate view, the state "can expect the corporation to contribute its fair share to the ability of the state to fulfill its obligations,"¹⁰⁰ what exactly "fair share" means or how to go about adequately collecting it is much less obvious.

Perhaps the failings of CSR theories are highlighted most here. While

⁹³ *Id.*

⁹⁴ *Strategic Tax Behavior*, *supra* note 30, at 3–4, 19, 23.

⁹⁵ *Id.* at 5.

⁹⁶ *See id.* at 11 ("Practically every EU government (including even the UK) has programs designed to foster CSR."). *See generally* European Commission, Corporate Social Responsibility: National Public Policy in the European Union (2004), <http://www.ec.europa.eu/social/BlobServlet?docId=2036&langId=en> (last visited Feb. 16, 2016) [<https://perma.cc/Y6ZJ-LV2Q>].

⁹⁷ *See Strategic Tax Behavior*, *supra* note 30, at 3–5.

⁹⁸ *Id.* at 14–15.

⁹⁹ *Id.* at 15.

¹⁰⁰ *Id.*

the artificial entity and real entity views place responsibility on corporations to act morally (or, at least, in a socially responsible way), the aggregate view requires that corporations pay their fair share.¹⁰¹ Furthermore, despite any of the CSR theories imposing moral obligation on corporations, Learned Hand famously stated in *Helvering v. Gregory*,¹⁰² that there is “not even a patriotic duty” to pay more taxes than the minimum required.¹⁰³ Notably, in *Gregory*, Hand assessed a tax deficiency against corporate tax evaders.¹⁰⁴

However, Avi-Yonah provides this particularly illuminating point: “[e]ven if from the perspective of management CSR is an illegitimate tax on shareholders, the government could still legitimately try to encourage corporations to engage in CSR by giving tax incentives.”¹⁰⁵ In the next subsection, this Note addresses the questions previously raised in the utilitarian, deontology, and virtue sections: that is, whether a state can be a moral actor.

E. *Can States Act Morally?*

Since the theories of morality introduced in this Note have mainly concerned individuals, the question of whether *states* can act morally is really a question of the legitimacy of applying said theories to states. If determined that one in good conscious cannot apply any of the most explored theories of morality to states, it begs the question: does any responsibility on the state exist?

Let’s begin by considering one theory of what makes an actor moral: “[w]hat gives the capacity to make decisions a moral cast is the ability of the individual and external observers to evaluate the decision and its consequences from a distinctly moral perspective.”¹⁰⁶ There are really two points to this inquiry. First, can the “individual” (the state in our case) evaluate its own decisions and consequences from a moral perspective? Second, can external observers evaluate the state’s decisions from a moral perspective?

In response to the first pointed question, the U.S. government evaluates its own laws in multiple ways. A law can be upheld or overturned by a Supreme Court ruling.¹⁰⁷ The president can make an executive order.¹⁰⁸

¹⁰¹ *Id.* at 23.

¹⁰² 69 F.2d 809 (2d Cir. 1934).

¹⁰³ *Id.* at 810.

¹⁰⁴ *Id.* at 811.

¹⁰⁵ *Strategic Tax Behavior*, *supra* note 30, at 5.

¹⁰⁶ DAVID C. THOMASMA & DAVID N. WEISSTUB, *THE VARIABLES OF MORAL CAPACITY* 10 (2004).

¹⁰⁷ *See, e.g.*, *Marbury v. Madison*, 5 U.S. 137, 177 (1803) (establishing judicial review).

¹⁰⁸ U.S. CONST. art. 2, §§ 1, 3.

And Congress can create new laws to replace old ones that it feels are no longer appropriate or just.¹⁰⁹ But when the Supreme Court, Congress, or the president make and overturn laws, are they doing so from a moral perspective? In other words, when the Supreme Court chooses to uphold a law, are they basing their decision in any part on utilitarianism, deontology, Aristotlean virtue, or any other moral perspective?

Comments from justices post-decision could help determine whether or not morality comes into play. For instance, after the famous *Citizens United*¹¹⁰ ruling, Justice Ginsburg said that it is the one ruling she would overturn if she could choose one, and that it “pave[s] the way for more unfettered campaign spending by corporations.”¹¹¹ In this comment, Justice Ginsburg takes a utilitarian stance by considering the effects the decision could have on future elections. In fact, given our standard of *stare decisis*, perhaps all court decisions are utilitarian because each decision must look to future effects. Conversely, *stare decisis* almost requires that justices only evaluate and alter past decisions in the most extreme circumstances. So its evaluation of laws can, most likely, be evaluated from a moral perspective. At the same time, the moral determination of the Supreme Court’s ability (or willingness, perhaps) to evaluate its own past decisions is hazier.

As to the question of external observers, given the wealth of articles written about many of our laws, executive orders, and Supreme Court decisions, this second prong appears to be much more easily met.

The idea of states acting morally (or immorally) is not a new one. Machiavelli viewed states as potential moral actors.¹¹² He even recognized that states are made up of human leaders. For instance, in *Discourses* he wrote, “[h]appy is that state which produces a man prudent enough to provide it with laws and institutions by which it may live securely without any need to alter them.”¹¹³ Machiavelli continued, “least happy of all is the one whose institutions are entirely off the path that leads to a right and perfect end.”¹¹⁴ He discusses government’s regard for civil rights.¹¹⁵ Further, he posited that “laws make men good.”¹¹⁶ Laws accomplish this

¹⁰⁹ U.S. CONST. art. I, § 8.

¹¹⁰ *Citizens United v. Fed. Election Comm’n*, 558 U.S. 310 (2010).

¹¹¹ Charlotte Alter, *Ginsburg Says Citizens United Was Supreme Court’s Worst Ruling*, TIME (Sept. 29, 2014), <http://time.com/3445010/ruth-bader-ginsburg-citizens-united/> (last visited Feb. 21, 2016) [<https://perma.cc/FLJ6-F8E9>].

¹¹² See *infra*, notes 114–19 and accompanying text.

¹¹³ Niccolò Machiavelli, *Discourses upon the First Ten Books of Titus Livy*, in THE PRINCE 91 (Daniel Donno ed., Daniel Donno trans., Bantam Books 1981) (1513).

¹¹⁴ *Id.*

¹¹⁵ See *id.* at 93 (discussing a government ruled by aristocracy, which, he argues had no regard for civic right.)

¹¹⁶ See *id.* at 96.

feat by imposing morality on men.¹¹⁷ Particularly relevant to the discussion of whether corporate inversion laws are moral or not is his assertion that “all laws enacted to increase liberty derive from the conflict between [the common people and the aristocrats].”¹¹⁸ In fact, Machiavelli’s *The Prince*, while directed towards a “prince” or other national leader, is really directed towards a state government.¹¹⁹ Like a nation governed by royalty, a democratic nation is ruled by modern-day royals—of which are people who can act morally or immorally.

Another argument for regarding states as moral actors is that, in the contemporary global world, states can even assess and affect the morality of other states. For example, “a state actor can draw attention to a violation of a moral norm [and] make it a focus of international discussion and action.”¹²⁰

But what of Aristotlean virtue? While utilitarianism and deontology are more easily applicable to states, is it possible to apply a virtue theory to a state? To do so, one could look at a nation’s history and body of laws. By doing this with the U.S., one could argue that the nation is not necessarily moral because it has not always acted morally;¹²¹ yet it arguably has become more moral over time.¹²² But a problem still exists. This note contends that part of the reason nations can be moral (or immoral) is because they are governed by humans.¹²³ But, while the nation has its own body of laws stretching back to its founding, the people who govern have changed many times over. Although one can evaluate long-term outcomes and even legislators’ intentions from a moral standpoint, perhaps it is impossible to apply Aristotlean virtue when the human actors in charge constantly change.

Overall, while some theorists might disagree, it does seem possible to apply morality to states, at least in the sense of deontology, and certainly utilitarianism. In the next section, having accepted states as moral actors under the theories of utilitarianism and deontology, this Note applies these theories to our body of corporate tax inversion laws.

¹¹⁷ *Id.* (“Whoever organizes a state and establishes its laws must assume that all men are wicked and will act wickedly whenever they have the chance to do so.”).

¹¹⁸ *Id.*

¹¹⁹ See generally NICCOLO MACHIAVELLI, *THE PRINCE* (Daniel Donno ed., Daniel Donno trans., Bantam Books 1981) (1513).

¹²⁰ ROBERT W. MCELROY, *MORALITY AND AMERICAN FOREIGN POLICY: THE ROLE OF ETHICS IN INTERNATIONAL AFFAIRS* 52 (1992).

¹²¹ For example, the legality of slavery and oppression of women, minorities, and LGBT individuals, Jim Crow laws, McCarthyism, etc.

¹²² For example, the outlawing of slavery, gradual gains of civil rights for women, minorities, and LGBT individuals, etc.

¹²³ See *infra* Part II.D.2.

III. THE IMMORAL STATE

Having discussed the leading theories of morality, let us return to modern corporate tax inversions, to see how our inversion laws fare. Corporate inversions affect both the U.S. and their host country. A 2002 Treasury report “identified three main concerns about corporate inversions: erosion of the U.S. tax base, a cost advantage for foreign-controlled firms, and a reduction in perceived fairness of the tax system.”¹²⁴ In this section, these and other concerns will be discussed.

A. *Financial Cost*

Corporate inversions cost the U.S. billions of dollars annually.¹²⁵ As Tyler Dumler points out, even though the U.S. Treasury has lost billions of dollars to inversions, it is “still responsible for generating adequate revenue to fund the government budget.”¹²⁶ According to Dumler, this amalgam of loss and persisting need results in a greater tax burden for individuals and domestic businesses.¹²⁷ Hale E. Sheppard agrees, writing “the number of corporations that are paying taxes in the United States decreases as the frequency of inversions increases, thereby making the remaining U.S. taxpayers responsible for a larger portion of the government budget.”¹²⁸ According to the U.S. Treasury, President Obama’s plan to eliminate inversions will raise \$17 billion over the next ten years.¹²⁹

And what if U.S. corporations choose not to ever repatriate foreign income? Many never do, and current estimates are that about \$1.7 trillion in foreign earnings of U.S. corporations remain abroad.¹³⁰ That is \$1.7 trillion untaxed in the U.S. and not used in the U.S. market. Or, think of it

¹²⁴ MARPLES & GRAVELLE, *supra* note 7, at 1–2.

¹²⁵ See, e.g., *House Democrats Introduce Legislation to Tighten Restrictions on Corporate Tax Inversions*, DEMOCRATS WAYS AND MEANS COMM. (May 20, 2014), <http://democrats.waysandmeans.house.gov/press-release/house-democrats-introduce-legislation-tighten-restrictions-corporate-tax-inversions> [<http://web.archive.org/web/20160610180552/http://democrats.waysandmeans.house.gov/press-release/house-democrats-introduce-legislation-tighten-restrictions-corporate-tax-inversions>] (last visited Feb. 21, 2016) (“There have been more than 40 corporate inversions in the last decade, costing the U.S. tax base billions of dollars.”) [hereinafter *House Democrats*]; Dumler, *supra* note 60, at 89.

¹²⁶ Dumler, *supra* note 60, at 92.

¹²⁷ *Id.*

¹²⁸ *Fight or Flight*, *supra* note 10, at 563.

¹²⁹ See Vanessa Houlder, Vincent Boland, & James Politi, *Tax Avoidance: The Irish Inversion*, FIN. TIMES (Apr. 29, 2014), <http://www.ft.com/intl/cms/s/2/d9b4fd34-ca3f-11e3-8a31-00144feabdc0.html#axzz3O6XUIRrj> [<https://perma.cc/3HZ4-CJNX>] (“In March, President Obama announced plans to slam the door on inversions by the end of this year, a move the U.S Treasury said would raise \$17 billion over the coming decade.”).

¹³⁰ See Joshua Simpson, *Analyzing Corporate Inversions and Proposed Changes to the Repatriation Rule*, 68 N.Y.U. ANN. SURV. AM. L. 673, 680–81 (2013) (discussing how the repatriation rule has failed and possible legislative solutions).

as a \$1.7 trillion tax deficit that must be made up by someone.

B. *Effects on Host Countries*

Ireland, in particular, does not want to be perceived as a tax haven.¹³¹ With an already low corporate tax rate of 12.5 percent, Ireland offered a zero percent tax rate for transfers of intellectual property from one Irish-registered subsidiary to another.¹³² As of October 2014, Ireland is attempting to close that loophole by requiring all Irish-registered companies to become tax *residents* in Ireland within the next six years.¹³³ While this will require a corporation to do more than just register in Ireland, it still leaves open a huge opportunity for tax benefit for U.S. intellectual property companies that invert. In fact, it seems that Ireland has benefitted from U.S. corporations inverting:

[Pharma] employs less than two percent of Ireland's workforce, yet data published by the U.S. Commerce Department suggests that Ireland generated profits in 2011 of \$21.8 billion for U.S. chemical and pharma companies. That is third of all foreign profits for U.S. companies in the sector, and about forty percent of all Irish corporate profits. U.S. pharma companies paid a tax rate of less than six percent on over \$100 billion of Irish profits over the last decade, according to an FT analysis. It showed that the Irish subsidiaries of U.S. chemical companies have cut their tax rates far below the statutory rate, from an average of eight percent in the seven years to 2004 to 4.5 percent in the following seven years.¹³⁴

However, consider that the EU recently found fault with Irish tax policy with regard to at least one large company: Apple. The corporation has a long history with Ireland.¹³⁵ In 1990, an Apple tax adviser said that Apple was the "largest employer in the Cork area with 1,000 employees and 500 persons engaged on a sub-contract basis."¹³⁶ The European

¹³¹ See Houlder, Boland, & Politi, *supra* note 129 (stating that Ireland insists it is not a tax haven).

¹³² Joe Harpaz, *Will Irish Tax Law Change Stop Corporate Inversions?*, FORBES (Oct. 15, 2014), <http://www.forbes.com/sites/joeharpaz/2014/10/15/will-irish-tax-law-change-stop-corporate-inversions/> (last visited Feb. 21, 2016) [<https://perma.cc/6L9K-PZCR>].

¹³³ See *id.* (discussing the closing of the "Double Irish" tax loophole).

¹³⁴ Houlder, Boland, & Politi, *supra* note 129.

¹³⁵ See Poornima Gupta & Padraic Halpan, *Apple Has Been Dodging Taxes in Ireland for More Than 32 Years*, BUS. INSIDER (May 26, 2013), <http://www.businessinsider.com/apple-avoiding-taxes-in-ireland-2013-5> [<https://perma.cc/LHM4-5XBM>] ("Apple has operated almost tax-free in Ireland since 1980, welcomed by a government keen to bring jobs to what was then one of Europe's poorest countries, former company executives and Irish officials have said.")

¹³⁶ *European Commission Says Apple's Irish Tax Deals Constituted State Aid*, RTE NEWS (Oct. 1, 2014), <http://www.rte.ie/news/2014/0930/648865-ireland-tax-apple/> [<https://perma.cc/S7J2-ZAU7>].

Commission accused Irish officials of “giving Apple unlawful state aid masquerad[ing] as tax breaks.”¹³⁷ The U.S. Senate seemed to agree, given that a Senate investigative panel used Apple’s relationship with Ireland as a “case study” when looking into “how American companies dodged taxes by shifting profits offshore.”¹³⁸ Senators Levin and McCain claimed that Apple’s tax planning helped the corporation to avoid \$44 billion over the course of four years.¹³⁹

According to the European Commission, “aggressive tax planning . . . erodes the tax base of Member States, which are already financially constrained.”¹⁴⁰ Professor Kleinbard, of the University of Southern California’s Gould School of Law, writes, “The light bulb has gone off that trade wars by another name and conducted through the tax system are just as ruinous.”¹⁴¹

C. *Other Costs*

Avi-Yonah claims, “when a corporation engages in aggressive tax planning . . . it is breaching an implicit bargain with the state that created it, gave it legal rights, and created the conditions for it to make those same profits it is attempting to shield from tax.”¹⁴² Building on his argument that corporate inversions force a shifting of the tax burden onto domestic businesses, Dumler argues that such a burden could cause domestic corporations to hire less workers or pay lower wages.¹⁴³ Shifting the burden onto individuals could have entirely different sorts of consequences. “Respected bar associations have . . . argu[ed] that corporate inversions not only impair the integrity of the voluntary compliance system, but also violate the spirit, if not the letter of the law.”¹⁴⁴

The IRS depends on voluntary compliance to raise revenue. The U.S. has a voluntary compliance rate of over eighty percent.¹⁴⁵ But what if individuals and small-business owners were to witness large corporations with rich CEOs paying less in taxes, while their own tax burdens increase?

¹³⁷ Patricia Cohen & James Kanter, *Europeans Accuse Ireland of Giving Apple Illegal Tax Break*, N.Y. TIMES, Oct. 1, 2014, at B01.

¹³⁸ *Id.*

¹³⁹ Robert W. Wood, *Forget Inversions, These 20 Huge, Profitable Companies, Already Pay Zero Tax*, FORBES (Aug. 15, 2014), <http://www.forbes.com/sites/robertwood/2014/08/15/forget-inversions-these-20-huge-profitable-companies-already-pay-zero-tax/> [<https://perma.cc/3K3G-J33V>].

¹⁴⁰ Press Release, Eur. Comm’n, *State Aid: Comm’n Investigates Transfer Pricing Arrangements on Corp. Taxation of Apple (Ireland) Starbucks (Netherlands) and Fiat Finance and Trade (Luxembourg)* (June 11, 2014).

¹⁴¹ Patricia Cohen & James Kanter, *supra* note 137.

¹⁴² *Taxation*, *supra* note 29, at 20.

¹⁴³ Dumler, *supra* note 60, at 99.

¹⁴⁴ *Fight or Flight*, *supra* note 10, at 565.

¹⁴⁵ IRS, IRS STRATEGIC PLAN, 2009–2013 (2008), http://www.irs.gov/pub/newsroom/long_term_measures.pdf [<https://perma.cc/5F4H-ZSBV>].

According to Dumler, the allowance of corporate inversions causes the public to “perceive[] the U.S. tax system as operating unfairly by allowing corporations to escape taxation, while requiring individuals to pick up the slack, thereby corroding the legitimacy of the governmental tax system.”¹⁴⁶ Less voluntary compliance will only magnify the problem.

In one article, the writers claim other likely costs: employees seeing jobs shifted to foreign countries, increased fear of job loss, negative company image, barriers to long term survival of the company, difficulty for the U.S. government to provide necessary services, and political stresses in the new host country.¹⁴⁷ These predictions don’t seem too far off when taking into account that, “many U.S. multinationals have shifted research, manufacturing, and regional headquarters overseas, resulting in 600 U.S. companies employing 100,000 people in Ireland alone.”¹⁴⁸ The most recent data shows that unemployment in the U.S. is at about 4.9 percent.¹⁴⁹

D. Utilitarian Evaluation

Have corporate inversion laws—particularly Section 7874—affected the overall level of happiness? Inversions have cost the U.S. billions of dollars, leaving an extra burden on individual taxpayers and small business owners.¹⁵⁰ While this may have conferred some benefit on the Irish economy, inversions have hurt the U.S.¹⁵¹ And while corporations often claim their reason for inverting relates to their fiduciary duty owed to shareholders, sometimes shareholders end up losing money in the transaction.¹⁵² For example, “the inversion forces the U.S. stockholders to ‘recognize’ gain . . . based on the difference between the fair market value of the shares of the new foreign parent that they receive and the adjusted basis that they had in the stock of the former domestic parent . . . that they surrendered in the exchange.”¹⁵³

Shareholders may end up with more concerns than the immediate gain or loss of stock value. “[O]nce the parent of the multinational corporate

¹⁴⁶ Dumler, *supra* note 60, at 92.

¹⁴⁷ See *Ethics of Inversion*, *supra* note 9, at 4–5 (discussing potential consequences).

¹⁴⁸ Simpson, *supra* note 130, at 683.

¹⁴⁹ *Databases, Tables & Calculators by Subject*, BUREAU OF LABOR STATISTICS, U.S. DEP’T. OF LABOR (Feb. 19, 2016), <http://data.bls.gov/timeseries/LNS14000000> [<https://perma.cc/GPS2-GL8U>].

¹⁵⁰ See *Fight or Flight*, *supra* note 10, at 563 (“[T]he number of corporations that are paying taxes in the United States decreases as the frequency of inversions increases, thereby making the remaining U.S. taxpayers responsible for a larger portion of the government budget. . . . [T]he U.S. Treasury estimates that these transactions are costing the country ‘billions’ of dollars annually.”).

¹⁵¹ See *supra* Part III.

¹⁵² See Laura Saunders, *How to Ease the Tax Hit from an “Inversion”*, WALL ST. J., Aug. 2, 2014, at B1 (discussing ways that shareholders lose out in inversions).

¹⁵³ *Fight or Flight*, *supra* note 10, at 557.

group is established in a tax-haven country . . . the laws of that jurisdiction then govern the rights and obligations of the corporation.”¹⁵⁴ This means that shareholders are *not* protected by U.S. law. Further, “unsophisticated or naïve shareholders” might not realize that an inversion is more than just a “technical maneuver with only tax implications.”¹⁵⁵ Given these facts, it would be difficult to determine that Section 7874 passes muster under a utilitarian measure of morality.

E. *Deontological Evaluation*

Lawmakers’ motivations seem to be good in theory—fairness, equality, and protecting the tax base are all admirable goals. But stating one thing and then doing another raises questions about true motivations. For instance, lobbyists can influence lawmakers’ decisions.¹⁵⁶ And, since the McDermott inversion in 1983, only a handful of piecemeal laws against inversions have come about.¹⁵⁷ As discussed, *supra*, at least Section 163(j) does not even do what it was intended to do.¹⁵⁸ Such a lofty goal as “fairness” is reminiscent of the “War on Drugs” or the “War on Terror,” which may sound admirable, but can never truly be won.¹⁵⁹ Perhaps goals such as “fairness” or “equality” are merely politicians’ smoke and mirrors way of attempting to keep a tax base, which already disapproves of the IRS,¹⁶⁰ relatively compliant with the tax law.

However, our laws appear to pass more easily under a deontological theory than under a utilitarian one. According to the literature accompanying laws and proposed laws, the motivation is moral. Although the outcomes have not been nearly as positive as the intentions, possibly, legislators’ intentions are good, even if their actions are not.

¹⁵⁴ *Id.* at 566

¹⁵⁵ *Id.*

¹⁵⁶ See Annie Linskey, *Lott Joins Lobbying Push to Keep Up Corporate Inversions*, BLOOMBERG (Aug. 9, 2014), <http://www.bloomberg.com/news/2014-08-08/companies-bulk-lobbying-as-obama-seeks-to-curb-inversions.html> [<https://perma.cc/GUV9-KZSL>] (discussing “lobbying effort by companies that want to preserve the option of reducing their corporate taxes by moving their legal addresses overseas.”).

¹⁵⁷ See *supra* Part II.C.

¹⁵⁸ *Id.*

¹⁵⁹ For example, some have argued that the “War on Terror” is a way for politicians to make sure our country is always at war, gaining patriotism, soldiers, oil, and access to our privacy. See, e.g., Seth C. Lewis & Stephen D. Reese, *What is the War on Terror? Framing Through the Eyes of Journalists*, 86 J&MC QUARTERLY 85, 86 (2009), <https://journalism.utexas.edu/sites/journalism.utexas.edu/files/attachments/reese/what-is-war-terror-framing-lewis-reese.pdf> [<https://perma.cc/3BY9-4U9Y>] (discussing the longevity of the “War on Terror,” and the fact that such a war has no “delineated . . . clear enemy nor battlefield”); Anup Shah, *War on Terror*, GLOBAL ISSUES (Oct. 7, 2013), <http://www.globalissues.org/issue/245/war-on-terror> [<https://perma.cc/33Z8-PG3N>] (discussing the loose definition of “terror” in the “war on terror” and social costs that have come with the war).

¹⁶⁰ See Jones & Saad, *supra* note 2 (describing the public’s low approval rating of the IRS).

IV. MORAL LAWS WILL AID IN FIXING THE CORPORATE TAX AVOIDANCE ACHIEVED THROUGH INVERSIONS

What is the importance of an inquisition into the morality of laws? Well, focusing on utilitarianism and deontology forces legislators to evaluate their decisions both from a personal standpoint and from a more objective and future-looking standpoint. Legislators seem to agree, at least, that something needs to be done about corporate inversions. Their motivations for change inform the direction corporate inversion laws should go.

A. Motivations

Motivation for proposed changes to corporate inversion law appears to center around equality. According to Representative Danny Davis, the Stop Corporate Inversions Act of 2014 is “about fairness.”¹⁶¹ Representative Davis said, “At its heart, it says that America should not have two sets of rules: one for ordinary folks and one for those with armies of lawyers who can skirt and bend the law to avoid paying their fair share of taxes. This is a notion so fundamental to our democracy it seems it should be self-evident.”¹⁶² Representative Davis’s comments echo the familiar notions of equality so fundamental to our nation, which have been spoken and written about since Thomas Jefferson wrote, in the Declaration of Independence, “We hold these truths to be self-evident, that all men are created equal”¹⁶³ Admirable in theory, sure, but despite our oft-quoted core belief in equality, our nation’s history contains numerous examples of the constant struggle between those who would like equal rights, and those who seek to deny them.¹⁶⁴

Representative Davis isn’t the only politician spouting fairness and equality rhetoric. Representative Jan Schakowsky pointed out that corporations reap the benefits of “tax-payer funded research, our transportation infrastructure, our top-rate education system and productive employees it produces, and our world-leading economy.”¹⁶⁵ She claims that these same corporations “have used inversions to avoid their fair share of U.S. taxes—taxes that pay for the investments that have helped them profit and thrive.”¹⁶⁶ Representative Rosa DeLauro’s sentiments resemble Representative Schakowsky’s: “[w]e can’t continue to stand by idly while

¹⁶¹ *House Democrats*, *supra* note 125.

¹⁶² *Id.*

¹⁶³ THE DECLARATION OF INDEPENDENCE para 2. (1776).

¹⁶⁴ For example, civil rights for women, minorities, and homosexuals have only come after long battles (many of which are ongoing).

¹⁶⁵ *House Democrats*, *supra* note 125.

¹⁶⁶ *Id.*

companies avoid taxes at the expense of everyone else.”¹⁶⁷

Lawmakers say they want to stop corporate inversions in order to lessen unfairness, or inequality toward other taxpayers. But according to the Department of the Treasury, fairness to individual and small business taxpayers isn’t the only concern. The Treasury Department’s explanations of revenue proposals contains two other motivations for change. First, “[i]nversion transactions raise significant policy concerns because they facilitate the erosion of the U.S. tax base through deductible payments by the remaining U.S. members of the multinational group to the non-U.S. members and through aggressive transfer pricing for transactions between such U.S. and non-U.S. members.”¹⁶⁸ Again, the erosion of the U.S. tax base plays a forefront role in motivating change. Second, “[t]here is no policy reason to permit a domestic entity to engage in an inversion transaction when its owners retain a controlling interest in the resulting entity, only minimal operational changes are expected, and there is significant potential for substantial erosion of the U.S. tax base.”¹⁶⁹ That leaves a positive and a negative reason: (1) allowing inversions erodes the U.S. tax base and (2) there is no policy reason to allow them.

While there exists ample commentary from lawmakers on *why* corporate inversion law needs to be changed, little exists on why they have chosen certain solutions over others. U.S. lawmakers must change the way they look at consequences and motivations in order to create a moral body of laws.

B. Current Proposals for Change

The following are proposed changes to corporate inversion law. Note the piecemeal nature of these proposals, and how none truly address the problem.

1. *Stop Corporate Inversions Act of 2015 (S. 198 and H.R. 415)*

Boasting projected estimated savings of \$34 billion in tax revenue,¹⁷⁰ the Stop Corporate Inversions Act¹⁷¹ (SCIA) would amend section 7874. There are three main provisions of the act: (1) SCIA would require shareholders of the foreign corporation to own at least fifty percent of the

¹⁶⁷ *Id.*

¹⁶⁸ DEP’T OF THE TREASURY, GEN. EXPLANATIONS OF THE ADMIN.’S FISCAL YEAR 2015 REVENUE PROPOSALS 64 (2014), <http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2015.pdf> (last visited Feb. 21, 2016) [<https://perma.cc/NR8V-K54B>].

¹⁶⁹ *Id.* at 64–65.

¹⁷⁰ DEMOCRATS WAYS AND MEANS COMMITTEE, *H.R. 415: Stop Corporate Inversions Act of 2015*, <http://democrats.waysandmeans.house.gov/bill/hr-415-stop-corporate-inversions-act-2015> [<http://web.archive.org/web/20150420022119/http://democrats.waysandmeans.house.gov/bill/hr-415-stop-corporate-inversions-act-2015>].

¹⁷¹ H.R. Res. 415, 114th Cong. (2015); S. Res. 198, 114th Cong. (2015).

new, combined corporation (up from twenty percent previously);¹⁷² (2) even if fifty percent is owned by shareholders of the foreign corporation, inversion is still prohibited “if the affiliated group that includes the combined foreign corporation is managed and controlled in the United States and engages in significant domestic business activities in the United States;”¹⁷³ and (3) SCIA would repeal the sixty to eighty percent ownership test.¹⁷⁴ The bill was originally introduced on May 8, 2014, and would therefore apply to all inversions completed after that date.¹⁷⁵

SCIA comes after an administrative proposal to curb corporate inversions, since more than forty inversions have occurred since Section 7874 was enacted in 2004.¹⁷⁶

2. *No Federal Contracts for Corporate Deserters Act of 2015 (H.R. 1809)*

Simply put, the No Federal Contracts for Corporate Deserters Act (NFCCD) would deny federal contracts to corporations that have inverted.¹⁷⁷ Detractors argue that the NFCCD would deter competition and put U.S. jobs at risk.¹⁷⁸ These same detractors, however, argue that legislators must incentivize corporations to stay in the U.S. by lowering the corporate tax rate.¹⁷⁹ But competing with tax rates as low as 12.5 percent (as in Ireland) is unreasonable because it would require cutting the current U.S. tax rate by nearly two thirds.¹⁸⁰

3. *Proposed and Failed*

In 2014, aside from SCIA and NFCCD, Congress also proposed the Corporate Inverters Earnings Stripping Reform Act (CIESRA, S. 2786)¹⁸¹ and the Pay What You Owe Before You Go Act (PWOBGA, S. 2895 and

¹⁷² *Sens. Durbin and Reed, Reps. Levin and Doggett Introduce Legislation to Curb Corporate Tax Inversions*, DEMOCRATS WAYS AND MEANS COMMITTEE, <http://democrats.waysandmeans.house.gov/press-release/sens-durbin-and-reed-reps-levin-and-doggett-introduce-legislation-curb-corporate-tax#> [<http://web.archive.org/web/20151128104814/http://democrats.waysandmeans.house.gov/press-release/sens-durbin-and-reed-reps-levin-and-doggett-introduce-legislation-curb-corporate-tax>].

¹⁷³ *Id.*

¹⁷⁴ *Id.*

¹⁷⁵ *Id.*

¹⁷⁶ *Id.*

¹⁷⁷ H.R. 1809, 114th Cong. (2015).

¹⁷⁸ Letter in Opposition to “No Federal Contracts for Corporate Deserters Act” to the Members of the United States Congress, (Sept. 8, 2014) (<https://www.uschamber.com/letter/letter-opposition-no-federal-contracts-corporate-deserters-act>) [<https://perma.cc/4RC2-XWPL>].

¹⁷⁹ *Id.*

¹⁸⁰ Chad Stone, *Reality Check on Corporate Taxes*, U.S. NEWS & WORLD REP., (Nov. 13, 2015, 12:00 PM), <http://www.usnews.com/opinion/economic-intelligence/2015/11/13/reality-check-on-corporate-income-tax-rates> [<https://perma.cc/6RD6-M3U2>] (noting that, although the U.S. corporate tax rate is thirty-five percent, with other factors included, it is actually closer to forty percent).

¹⁸¹ S. Res. 2786, 113th Cong. (2014).

H.R. 5549).¹⁸² Unlike SCIA and NFCCD, neither of these were renewed in 2015.

CIESRA contains two main provisions: (1) it “[a]mends the Internal Revenue Code to impose limitations on the tax deduction for interest paid by corporations which are designated as applicable entities (i.e., members of an expanded affiliated group which includes a surrogate foreign corporation which is not treated as a domestic corporation)” and (2) it “[p]rohibits such an entity from claiming a tax deduction for interest that exceeds 25% of its adjusted taxable income and from carrying forward interest which is paid or accrued during the first year in which such entity becomes an applicable entity.”¹⁸³ The goal of CIESRA was to curb interest stripping transactions.¹⁸⁴

PWOGBA “[a]mends the [IRC] to require the recapture in subpart F income . . . the accumulated deferred foreign income of such corporation . . . for its last taxable year.”¹⁸⁵ In other words, the U.S. would recapture foreign undistributed earnings over U.S. undistributed earnings which were not tax deferred.¹⁸⁶ The purpose was “to include in income the unrepatriated earnings of groups that include an inverted corporation.”¹⁸⁷

C. Moral Proposals

According to a 2002 Treasury Report, fairness, equality, and protection of the U.S. tax base are the three most important goals.¹⁸⁸ Lawmakers should apply major theories of morality in order to write moral laws with greater ease. They should ask four questions in determining whether a law is morally sound: (1) Will this law create the greatest amount of happiness for the greatest amount of people?; (2) Will that happiness be sustainable?; (3) Are our motivations themselves moral?; and (4) Will this law contribute to a greater body of moral laws? In the following subsections, I will evaluate proposals for change while keeping these questions in mind.

1. *Incentivize Corporations to Remain in the U.S.*

Most of the enacted and proposed legislation has worked (or proposed

¹⁸² S. Res. 2895, 113th Cong. (2014); H. Res. 5549, 113th Cong. (2014).

¹⁸³ *Corporate Inverters Earnings Stripping Reform Act of 2014*, CONGRESS.GOV, <https://www.congress.gov/bill/113th-congress/senate-bill/2786> [<https://www.congress.gov/bill/113th-congress/senate-bill/2786>] (last visited Feb. 21, 2016).

¹⁸⁴ *Id.*

¹⁸⁵ *Pay What You Owe Before You Go Act*, CONGRESS.GOV, <https://www.congress.gov/bill/113th-congress/senate-bill/2895> (last visited Feb. 21, 2016) [<https://perma.cc/ARS2-JQ9D>].

¹⁸⁶ *Id.*

¹⁸⁷ *S. 2895 (113th): Pay What You Owe Before You Go Act*, GOVTRACK.US, <https://www.govtrack.us/congress/bills/113/s2895> (last visited Feb. 21, 2016) [<https://perma.cc/6YLG-FUXN>].

¹⁸⁸ See *supra* note 124 and accompanying text.

to work) to penalize corporations that try to invert. It is worth considering, however, the possibility that offering corporations incentives not to invert might contribute to greater productivity and efficiency. Passing legislation that reduces the burden of individual taxpayers and small businesses while also providing incentives to corporations, if effective, would further utilitarian ends.

Lawmakers should first look at “underlying conditions [that] lead[] to expatriation.”¹⁸⁹ Such a goal might begin with revising and restructuring the piecemeal laws currently in place. Piecemeal laws, like trying to put out a large fire with cups of water, lack effectiveness. As soon as one of these laws is passed, multi-national corporations find work-arounds. For example, despite Section 7874, these corporations continue eroding the U.S. tax revenue base through methods such as: “income trapping using indefinite deferrals of active income in foreign countries; repatriation of excessive foreign tax credits; [and] avoidance of taxation on holding companies”¹⁹⁰ Right now, corporate inversion law looks much like a game of “Whack-a-Mole.” When one mole is bopped, another pops its head up. This system’s inherent inadequacy won’t be fixed with more piecemeal laws.

One of the most often suggested incentives, naturally, is to lower the corporate tax rate.¹⁹¹ To be sure, the U.S. does have a high corporate tax rate compared to other industrialized nations.¹⁹² But lowering the corporate tax rate to be competitive with popular inversion nations would create a slew of other problems. Most importantly, it would lead to greater after-tax income inequality.¹⁹³ Further, in 2013 corporate taxes brought in \$275 billion in revenue.¹⁹⁴ Cutting or severely reducing the corporate tax rate would leave a huge deficit to be made up by *someone*. This is to say that a small corporate tax rate decrease would necessarily hurt individuals and small businesses. While an in depth study of the exact reduction in the corporate tax rate that could be beneficial is beyond the scope of this note, see Figure 1¹⁹⁵ for a measure of other industrialized nations’ current rates

¹⁸⁹ Dumler, *supra* note 60, at 89.

¹⁹⁰ *Id.* at 95.

¹⁹¹ See, e.g., Charles Krauthammer, *Lower Corporate Tax Rates. Now.*, WASH. POST (Aug. 29, 2014), https://www.washingtonpost.com/opinions/charles-krauthammer-obama-should-take-the-lead-in-lowering-corporate-tax-rates/2014/08/28/19319dba-2ee9-11e4-bb9b-997ae96fad33_story.html?utm_term=.9c1d9db84bb8 [<https://perma.cc/CF8R-J7UN>] (arguing that liberals and conservatives should agree that lowering the corporate tax rate will solve the problem).

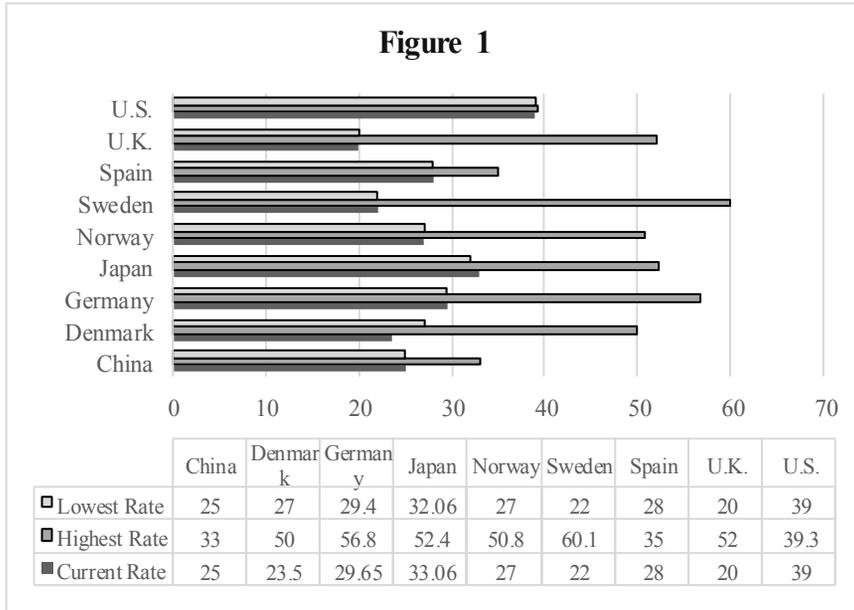
¹⁹² See *infra* Figure 1.

¹⁹³ Jared Bernstein, *Cutting the Corporate Tax Would Make Other Problems Grow*, N.Y. TIMES (Aug. 25, 2014), <http://www.nytimes.com/2014/08/26/upshot/cutting-the-corporate-tax-would-grow-other-problems.html> [<https://perma.cc/2C73-KGM9>].

¹⁹⁴ *Id.*

¹⁹⁵ The data used in this graph can be found at TRADING ECONOMICS, <http://www.tradingeconomics.com>, by searching for each particular country.

and past high and low rates (in percentages). Note that many of these countries are currently at or near their lowest rates ever. In fact, the United States is the only country shown on the graph that has remained at about the same rate over time.



2. Enact the Stop Corporate Inversions Act

Though part of the ongoing piecemeal legislative acts, enacting SCIA will make corporate inversions much more difficult than they currently are. The combination of lowering the corporate tax rate to lessen the motivation to invert and making inversions more difficult (and possibly more expensive for the corporation) should minimize the number of companies that invert. SCIA works to beef up the important, but only semi-effective, Section 7874 and should not (yet) be abandoned.

The IRS continues to utilize Section 7874 as a tool to increase restrictions on inversions. In December of 2015, the IRS issued a notice (the Notice) laying out additional regulations to cut down on inversions structured to avoid the governance of Section 7874.¹⁹⁶ There are a couple of updates provided in this notice, two of which I will outline, as they are the main substantive updates to the 7874 regulations. It will be helpful to lay these out in order to show how the IRS tries to catch up with inversion schemes.

First, the Notice addresses inversion schemes that take advantage of

¹⁹⁶ IRS Notice 2015-79, 2015-49 I.R.B. 775.

the substantial business activity exception by utilizing third countries, generally tax havens, to avoid taxes.¹⁹⁷ In other words, a foreign corporation will acquire the U.S. corporation (together called the “expanded affiliated group,” or “EAG”) and the EAG will have substantial business activity in the foreign country, but the foreign acquiring corporation will have achieved tax residency in a tax haven country. Under the new regulations, the EAG “cannot have substantial business activities in the relevant foreign country when compared to the EAG’s total business activities unless the foreign acquiring corporation is subject to tax as a resident of the relevant foreign country.”¹⁹⁸

Second, the Notice further addresses third country schemes describing such transactions as ones in which, “the stock or assets of the existing foreign corporation are acquired by the new third-country parent, and the shareholders of the existing foreign corporation receive more than 20 percent of the stock of the new third-country parent.”¹⁹⁹ Such set ups “erode the U.S. tax base.”²⁰⁰ Further, the IRS and Department of the Treasury have discovered that, in these scenarios, “the likelihood that there is a sufficient non-tax business purpose for replacing the U.S. parent with a foreign parent is significantly lower than Congress assumed when it established the 80-percent threshold.”²⁰¹ The regulations will now disregard such stock when determining whether the eighty percent threshold has been met.²⁰²

The Notice clarifies the definitions of important topics such as avoidance property and inversion gain income.²⁰³ The effectiveness of these changes remains to be seen, but the very BandAid-like nature sparks doubt. In any event, 7874 remains the IRS’s greatest tool against inversions, so SCIA should be enacted to give 7874 more power.

3. Regulations that Provide Guidance for Corporations Wishing to Move Abroad

IRC § 367²⁰⁴ provides an example of how we might structure laws in the best interest of the greatest number of people. Section 367 governs the transfers of property from the United States to a foreign corporation.²⁰⁵ Under this section, the IRS can stop a transfer from receiving

¹⁹⁷ *Id.*

¹⁹⁸ *Id.* at 776.

¹⁹⁹ *Id.*

²⁰⁰ *Id.* at 777.

²⁰¹ *Id.*

²⁰² *Id.* The Notice dictates four requirements for the regulation to apply. *Id.*

²⁰³ *Id.* at 778–80.

²⁰⁴ 26 U.S.C. § 367 (2012).

²⁰⁵ 26 U.S.C. § 367(a)1.

nonrecognition status under IRC § 351.²⁰⁶ The regulations provide guidance on which transfers Section 367 should apply to.²⁰⁷ A similar system could work well for corporate inversions.

Some corporations have important, non-tax-related reasons for moving to a different country. For example, some corporations are owned primarily by U.S. shareholders, but do the majority of their business in another country. These transfers should be evaluated on a case-by-case basis. Regulations could provide further guidance on what constitutes residency. A discretionary law like this would be more workable than a large change, such as lowering or getting rid of the corporate tax, or changing the U.S. to a territorial system of taxation. Rather than hurting small businesses and individuals by lowering the corporate tax rate, we could simply evaluate each corporation's status based on its own situation. And changing the U.S. to a territorial rather than a worldwide system of taxation would not work as well as my proposal for two reasons: nations with territorial systems still face a corporate inversion problem and the U.S. already gives foreign tax credits to corporations.

4. *Change the Definition of Corporate Residence*

Another workable solution would be to change how corporate residence is defined. This solution would supplement the previously proposed solution. If corporate residents included corporations with U.S. management, only corporations that are truly foreign corporations would benefit. This would also complement current corporate tax inversion statutes like 7874. Again, the regulations could be left to provide precise guidelines.

5. *Include IP in Subpart F*

Finally, Subpart F should be broadened to include income from CFCs holding U.S.-generated patents or other intellectual property. This would help to counteract the benefit of Ireland offering a zero percent tax rate on IP transfers,²⁰⁸ and other exploitation that has followed.²⁰⁹

Limiting the IP benefits of inverting, re-defining corporate residence, and allowing exceptions on a case-by-case basis would make it much more difficult for corporations to invert, while allowing for genuine foreign corporations to operate in their country of business. As it is, corporations take advantage of allowances in the IRC. By definition they cannot be held

²⁰⁶ 26 U.S.C. § 351 (2012); 26 U.S.C. § 367(a)1.

²⁰⁷ 26 C.F.R. § 1.367(a)-(b).

²⁰⁸ Harpaz, *supra* note 132.

²⁰⁹ Simpson, *supra* note 130, at 683 (“Corporations may also use agreements that share the cost of intellectual property research and development between the foreign parent and the U.S. subsidiary, and that provide the foreign parent with rights to exploit the intellectual property abroad and the U.S. subsidiary with rights to use the intellectual property in the United States.”).

accountable for moral decisions, as they exist solely for the benefit of shareholders. It is only natural (and good business) to take advantage of legal tax loopholes. In order to take the burden of corporate tax avoidance off small businesses and individual taxpayers, we must change the fundamentals of inversion laws.

V. CONCLUSION

Numerous commentators have remarked upon the measure of a corporation's morality when it inverts. In light of cases such as *Hobby Lobby*²¹⁰ and *Citizen's United*,²¹¹ it is not surprising that some attribute morality to corporations. But this note argues that assessing a corporation's morality and admonishing it for acting in a perceived immoral way is fruitless because corporations are meant to act for their shareholders—not for the greater good. Instead, we should examine the laws that permit corporations to act against the best interest of the nation, as these laws are passed by representatives elected by the people to act in their interest. Though the question of whether state actors can act morally may not be resolved, I argue that we must assume that they can. Certainly a better case can be made for measuring the morality of state actors than corporations. The State holds the power to set strict rules by which corporations must abide.

When writing new laws, legislators should keep four main questions in mind, with the goal of answering each in the affirmative: (1) Will this law create the greatest amount of happiness for the greatest amount of people?; (2) Will that happiness be sustainable?; (3) Are our motivations themselves moral?; and (4) Will this law contribute to a greater body of moral laws?

I believe that, in answering these questions in the affirmative, there are five ways in which we can lessen the occurrence of corporate tax inversions. First, we should examine incentives for corporations to remain in the States while keeping the interests of small businesses and individual taxpayers at the forefront. Second, in order to buff up current anti-inversion legislation, SCIA should be passed. Third, issue regulations in the spirit of Section 367 that will provide better guidelines for corporations that wish to move abroad. Fourth, change the definition of corporate residence to include corporations with U.S. management. Finally, include IP in Subpart F.

These are workable solutions that mostly avoid the traditional piecemeal laws. Instead of always being one step behind corporations,

²¹⁰ See *Burwell v. Hobby Lobby Stores, Inc.*, 134 S.Ct. 2751, 2775 (2014) (finding that for-profit corporations have the right to religious freedom).

²¹¹ See *Citizens United v. Federal Elections Comm'n*, 558 U.S. 310, 349 (2010) (finding that corporations' political speech is protected under the First Amendment).

legislators should rework the very definitions that permit corporations to invert. Legislators must also understand that the moral impetus to lessen the tax burden on small businesses and individuals is theirs alone. We cannot rely on corporations to do anything other than what is in the best interest of shareholders. For this reason, legislators must take on the responsibility.