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Burgers, Doughnuts, and Expatriations: An Analysis of the Tax Inversion Epidemic and a Solution Presented Through the Lens of the Burger King-Tim Hortons Merger

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BURGERS, DOUGHNUTS, AND EXPATRIATIONS: AN ANALYSIS OF THE TAX INVERSION EPIDEMIC AND A SOLUTION PRESENTED THROUGH THE LENS OF THE BURGER KING-TIM HORTONS MERGER

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ABSTRACT

Currently, the concept of tax inversion is a major corporate phenomenon. In the United States, companies pay taxes on all earnings, whether or not they were accumulated here. With one of the highest corporate tax rates in the world, this is a major expense for U.S. corporations competing in the world market. While most companies simply deal with the tax burden, some U.S. corporations buy foreign companies and relocate the company headquarters to the acquisition's home country. This corporate expatriation allows companies to avoid U.S. taxes on earnings in a number of ways. This Note will examine tax inversion through the lens of the 2014 Burger King-Tim Hortons merger and the resulting expatriation of the American burger purveyor from Florida to Canada. In particular, this Note will (1) examine why tax inversions have come about, (2) look at how politicians and academics have reacted to the phenomenon, (3) analyze the intricacies of the Burger King-Tim Hortons merger, and (4) propose a new solution that would actually curtail tax inversions and corporate expatriations within the United States.

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TABLE OF CONTENTS

INTRODUCTION

You are the head of a major international corporation, and you have just secured a deal that will expand your revenue four-fold and nearly double your market cap.[1] You have funding locked up, and your investors are thrilled at the growth prospects for the company. In addition to all of these benefits, you discover that you can save substantially on your tax bill by merely relocating your corporate headquarters. Would you let that benefit sit idle? With a duty to maximize shareholder wealth, is it not your duty to take advantage of the opportunity?

On August 26, 2014, Burger King Worldwide Inc. announced to the world its plans to purchase Tim Hortons Inc. and, in turn, become the third-largest fast-food company.[2] It is not the formation of this fast-food giant, however, that drew the ire of members of the U.S. government[3] and the Department of the Treasury.[4] That, instead, resulted from the decision to form a new parent organization for the two merged companies that is headquartered

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[1] Market capitalization is the total market value of a company's outstanding shares, and is calculated by multiplying a company's current outstanding shares by the current market price for the company's stock. *See Market Capitalization*, INVESTOPEDIA, http://www.investopedia.com/terms/m/marketcapitalization.asp [https://perma.cc/7FSK-6XMN].

[2] Leslie Patton & Craig Giammona, *Burger King to Buy Tim Hortons for About $11 Billion*, BLOOMBERG (Aug. 26, 2014, 4:38 PM), http://www.bloomberg.com/news/2014-08-26/burger-king-agrees-to-buy-tim-hortons-in-move-to-lower-taxes.html [https://perma.cc/E8G8-JKSE]. The deal was finalized on December 12, 2014. *See* Press Release, 3G Capital, Restaurant Brands International (Dec. 12, 2014), http://www.3g-capital.com/rbi.html [https://perma.cc/6EDC-ENSN].

[3] *See* Ramsey Cox, *Levin: Public disapproval could cost Burger King*, THE HILL (Aug. 26, 2014, 10:33 AM), http://thehill.com/blogs/floor-action/senate/215960-levin-public-disapproval-could-cost-burger-king [https://perma.cc/MB8V-UWVT]; Press Release, Senator Sherrod Brown, With Burger King in talks to Buy Tim Horton's, Brown Urges Congressional Action to Address Inversion; Calls for Creation of Global Minimum Tax, (Aug. 25, 2014), http://www.brown.senate.gov/newsroom/press/release/-with-burger-king-in-talks-to-buy-tim-hortons-brown-urges-congressional-action-to-address-inversions-calls-for-creation-of-global-minimum-tax [https://perma.cc/Y7MK-G9SM].

[4] *Tim Hortons, Burger King reaction: U.S. down on tax inversions*, CBC NEWS (Sept. 23, 2014, 5:41 AM), http://www.cbc.ca/news/business/tim-hortons-burger-king-reaction-u-s-cracks-down-on-tax-inversions-1.2774913 [https://perma.cc/T77F-HM5H].

in Canada.[5] While Burger King is steadfast in maintaining that the deal was purely a strategic initiative,[6] critics cried foul that the move was primarily a tax inversion.[7] Either way, nearly $500 million of foreign taxable income is escaping the grasp of the Internal Revenue Service.[8]

Tax inversions are transactions typically employed by U.S. corporations, whereby the corporation becomes a subsidiary of a new parent company that is domiciled outside the United States.[9] The purpose of such a move, primarily, is to gain the benefit that foreign companies enjoy under the U.S. Tax Code.[10] The primary basis for the tax benefit is that the average worldwide corporate tax rate is 25 percent, while the U.S. corporate tax rate is over 39 percent.[11] When a company expatriates to a foreign country, that company only has to pay U.S. taxes on U.S. earnings, as opposed to paying tax on the basis of all earnings (as it would in the United States).[12]

Solutions have been proposed in the past to help curtail the number of expatriations amongst U.S. corporations, but they have obviously either not been put into effect or have been unsuccessful.[13] There are few—President Barack Obama included—who would

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[5] Press Release, Burger King Worldwide Inc., World's Third Largest Quick Service Restaurant Company Launched With Two Iconic And Independent Brands: Tim Hortons And Burger King (Aug. 26, 2014), http://investor.bk.com/burgerking/web/conteudo_en.asp?idioma=1&tipo=43682&conta=44&id=166086 [https://perma.cc/9FYL-3ED7].

[6] Patton & Giammona, *supra* note 2.

[7] *See* Cox, *supra* note 3; CBC NEWS, *supra* note 4.

[8] *See* Andrew Flowers, *Burger King Might Save $8.1 Million by Moving to Canada. What's The Whopper Equivalent?*, FIVETHIRTYEIGHT (Aug. 28, 2014, 12:03 PM), http://fivethirtyeight.com/datalab/burger-king-might-save-8-1-million-by-moving-to-canada-whats-the-whopper-equivalent/ [https://perma.cc/3KPU-2C8K].

[9] *Definition of tax inversion*, FIN. TIMES, http://lexicon.ft.com/Term?term=tax-inversion [https://perma.cc/HU7C-TVVU].

[10] *See id.*

[11] *See* Amy Fontinelle, *Do U.S. High Corporate Tax Rates Hurt Americans?*, INVESTOPEDIA, http://www.investopedia.com/articles/investing/051614/do-us-high-corporate-tax-rates-hurt-americans.asp [https://perma.cc/8GRR-NYBS].

[12] CBC NEWS, *supra* note 4.

[13] *See infra* Part II.

challenge inversions based on their legality.[14] Their argument, instead, is that such moves are "gaming the system," and that these companies are "corporate deserters."[15] If the tax code allows for corporate expatriation to occur, those who seek to prevent inversions need to find a solution that succeeds in a way that prior suggestions have not.

Part I of this Note will discuss what allows tax inversion to be such a useful strategy and how previous companies have fared using it. Part II will introduce the previously proposed solutions to expatriation and how they were supposed to effect change. Part III will explain the deal between Burger King and Tim Hortons, highlighting the finances involved and the reactions elicited. Finally, Part IV will propose a multi-level solution that would cure the expatriation problem and keep inversions like the Burger King-Tim Hortons merger from occurring, provided they were executed solely for tax reasons.

I. TAX INVERSION AND CORPORATE EXPATRIATION: EXPLANATION AND HISTORY

Though the Burger King-Tim Hortons situation has brought tax inversion to the forefront of national news, it is not a new concept. One of the first tax inversions involved a company called McDermott International, Inc. and its corporate move to Panama in 1983.[16] Thus, the reasons a corporation might elect for a tax inversion have been in place for over thirty years. But what are those reasons? What is it in the U.S. Tax Code that lays the framework for a beneficial corporate expatriation?

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[14] *See* Katherine Rushton & Denise Roland, *New US tax inversion rules usher in era of forced 'economic patriotism'*, TELEGRAPH (Sept. 27, 2014, 1:25 PM), http://www.telegraph.co.uk/finance/personalfinance/tax/11125557/New-US-tax-inversion-rules-usher-in-era-of-forced-economic-patriotism.html [https://perma.cc/P4CR-4EBL].

[15] *Id.*

[16] Kevin Drawbaugh, *INSIGHT—When companies flee US tax system, investors often don't reap big returns*, THOMSON REUTERS (Aug. 18, 2014, 1:00 AM), http://www.reuters.com/article/2014/08/18/usa-tax-inversion-idUSL2N0PW16620140818 [https://perma.cc/J9LU-SNAM].

A. The U.S. Tax Code

The United States has a corporate taxation policy for foreign income that is different from most leading economic nations.[17] Other members of the G-7 have adopted at least a modified form of the taxation system known as "territorial taxation."[18] In this system, income earned outside of the corporate domicile is taxed by the nation in which that income is earned.[19] The United States instead makes use of the "worldwide" taxation system.[20] Under this method, all income—regardless of where it is earned—is taxed by the domicile country, though the tax on foreign income can be offset by deductions for already paying a foreign tax on that income.[21]

This difference in tax systems is the framework that makes tax inversion an attractive option for U.S. corporations. Corporate taxation is based on certain income brackets, much like the personal income tax. The statutory tax rate can range anywhere from 15 percent (on annual income below $50,000) to 35 percent (on annual income exceeding $10,000,000).[22] However, the tax rate can actually exceed 35 percent in two instances: when a corporation earns more than $100,000 annually (the lesser of either a 4 percent premium or $11,750) and when a corporation has taxable income of over $15,000,000 annually (the lesser of either a 3 percent premium or $100,000).[23]

Opponents of excess corporate taxation claim that these tax rates—which can be as high as 39 percent—are the highest in the world and that, ultimately, U.S. corporations pay more in taxes than foreign corporations.[24] Looking at these statutory rates and

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[17] Thornton Matheson, Victoria Perry & Chandra Veung, *Territorial vs. Worldwide Corporate Taxation: Implications for Developing Countries* 3 (Int'l Monetary Fund, Working Paper No. 13/205), http://www.imf.org/external/pubs/ft/wp/2013/wp13205.pdf [https://perma.cc/N3KC-835U].

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] *Id.*

[22] I.R.C. § 11 (2012).

[23] *Id.*

[24] *U.S. Corporate Tax Rates Are the Highest in the Developed World*, HERITAGE FOUND., http://www.heritage.org/federalbudget/corporate-tax-rate [https://perma.cc/42T2-6RGS].

applying them as gospel is simply not correct.[25] Certain methods of tax savings within the Internal Revenue Code allow for the statutory rate to actually be lower.[26] This lower rate is referred to as the effective marginal tax rate.[27] These methods include certain tax benefits (deductions, credits, and exemptions)[28] and the benefits of using tax shields, whereby companies use debt to deduct interest payments from taxable income.[29] According to a 2010 study, the average effective marginal corporate tax rate in the United States is actually 12.6 percent.[30] So why invert? Companies that are paying their tax bills must be acutely aware of the percentage of income that is being taken out. If that is the case, the answer is that the 12.6 percent figure is merely an average and that every company is different.

B. The Benefits of Inversion

There are advantages outside of the lower statutory tax rate that can make an inversion worthwhile for the newly domiciled company. The following sections will address the major advantages inherent in a tax inversion.

1. U.S. Tax Savings on Foreign Income

As mentioned previously, the United States uses a worldwide taxation system instead of a territorial system.[31] Many countries around the world, like the United Kingdom, Germany, and—notably for Burger King's situation—Canada, use the territorial system.[32]

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[25] *See* MARK P. KEIGHTLEY & MOLLY F. SHERLOCK, CONG. RESEARCH SERV., R42726, THE CORPORATE INCOME TAX SYSTEM: OVERVIEW AND OPTIONS FOR REFORM 3 (2014), http://fas.org/sgp/crs/misc/R42726.pdf [https://perma.cc/HN6W-NHJN].

[26] *Id.*

[27] *Id.* at 9.

[28] *Id.*

[29] *Definition of Tax Shield*, INVESTOPEDIA, http://www.investopedia.com/terms/t/taxshield.asp [https://perma.cc/DY2W-XNNJ].

[30] Andrew Ross Sorkin, *Tax Burden in U.S. Not as Heavy as It Looks, Report Says*, N.Y. TIMES (Aug. 18, 2014, 9:20 PM), http://dealbook.nytimes.com/2014/08/18/tax-burden-in-u-s-not-as-heavy-as-it-looks-study-finds/?_php=true&_type=blogs&_r=0 [https://perma.cc/UWH7-9R4W].

[31] Matheson, Perry & Veung, *supra* note 17.

[32] *Id.* at 4.

Multinational corporations can derive income from several different countries. Burger King alone does business in over ninety-five countries.[33] If any of those countries have an effective tax rate lower than that of the United States, the United States will be able to claim anything above that up to the applicable U.S. tax rate (after deductions and other tax benefits have been taken into account).[34]

Through a tax inversion, the new parent of the merged companies will likely have been formed in a country that either (1) employs the territorial tax system or (2) has a lower effective tax rate than the United States.[35] In the first instance, the United States will no longer get the excess over previously paid taxes on foreign income because the parent is not domiciled in the United States.[36] In the second instance, the new domicile country has a smaller difference between its tax rate and that of foreign countries, so the excess tax bill would be smaller than it would be in the United States. In either case, tax savings are realized as a result of tax inversion.

2. Earnings Stripping

Earnings stripping is a more "creative" way of extracting savings out of a tax inversion move. Most often, this process involves lending from the now-foreign parent company to its U.S. subsidiary.[37] In this specific instance, the parent will make loans to the U.S. subsidiary.[38] These loans are subject to interest payments by the subsidiary to the parent, and these interest payments are tax deductible for the subsidiary.[39] Thus, the U.S. subsidiary is essentially sending its earnings out of the country as interest to its parent.[40]

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[33] BURGER KING WORLDWIDE INC., 2013 ANNUAL REPORT 66 (2014).

[34] *See* Matheson, Perry & Veung, *supra* note 17, at 3–4.

[35] DONALD J. MARPLES, CONG. RESEARCH SERV., RL31444, FIRMS THAT INCORPORATE ABROAD FOR TAX PURPOSES: CORPORATE "INVERSIONS" AND "EXPATRIATION" 4, 5 (2008), http://wikileaks.org/wiki/CRS-RL31444 [https://perma.cc/NQ57-XAUE].

[36] *Id.* at 6.

[37] *Id.*

[38] *Id.*

[39] *Id.*

[40] *Id.*

Let us use a hypothetical situation based on the Burger King-Tim Hortons merger. In 2013, Burger King earned $436.7 million of income for the U.S. and Canada market segment, but nearly $743.1 million worldwide.[41] Also in 2013, Burger King paid an effective tax rate of roughly 27.5 percent on all income.[42] By comparison, Tim Hortons paid an effective tax rate of 26.8 percent in Canada in 2013.[43] Assuming there has been no tax inversion, the income earned worldwide will be taxed for the amount owed in the United States that was not already paid abroad if it is repatriated within the United States.[44] When Burger King forms the new parent corporation in Canada, the new corporation will pay taxes according to Canada's territorial taxation system.[45]

Now, let us say Burger King wants to get that money back into the United States. In the non-tax inversion situation, that money will essentially be taxed at the U.S. rate as soon as it enters the country.[46] However, after the tax inversion, the parent could make a loan to the subsidiary that is subject to interest. That money would still be taxed according to the Canadian tax rate—which is lower than the U.S. rate—causing a substantial tax savings.[47] Further, as an added bonus, the subsidiary would then be able to deduct the interest payments it makes to the parent from its U.S. taxable income.[48]

As a means of trying to curb this practice, the United States has a withholding tax rate of 30 percent for U.S.-sourced interest that is being held abroad (that is, interest earned by a foreign corporation from a U.S. corporation).[49] However, certain countries have treaties with the United States that either reduce or eliminate that withholding tax.[50] Conveniently, Canada and the

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[41] BURGER KING WORLDWIDE INC., 2013 ANNUAL REPORT 39 (2014).

[42] *See id.* at 38 ($88.5 million of income taxes divided by $322.2 million of earnings before taxes equals 27.5 percent).

[43] TIM HORTONS INC., 2013 ANNUAL REPORT 38 (2014).

[44] *See supra* text accompanying notes 20–21.

[45] *See* Matheson, Perry & Veung, *supra* note 17.

[46] *See supra* text accompanying notes 20–21.

[47] *See supra* notes 41–43.

[48] Ilan Benshalom, *The Quest to Tax Interest Income in a Global Economy: Stages in the development of International Income Taxation*, 27 VA. TAX REV. 631, 677 (2008).

[49] MARPLES, *supra* note 35, at 6.

[50] *Id.*

United States have such a treaty that eliminates the withholding tax completely.[51] Thus, the parent would only have to pay taxes on interest income in Canada and the money loaned to Burger King in the United States would be untouched.

3. "Hopscotch" Loans

When a company inverts, it almost certainly has money housed abroad that it has yet to repatriate.[52] When a company decides to invert and creates a foreign parent company, the new foreign parent now has the option of receiving "hopscotch" loans.[53] These are loans of the previously offshore earnings from a foreign subsidiary to the new parent company, which completely bypass the former U.S. parent.[54] From there, the parent can then give the money back to the U.S. subsidiary through either another loan or a capital contribution.[55] This transfer allows the company to avoid many of the taxes that would have been imposed on the income had the money merely been repatriated.[56]

While the process bears a similarity to earnings stripping, there is a notable difference in the flow of the earnings. A "hopscotch" loan is made from foreign earnings in order to get the money back to the U.S. subsidiary relatively tax-free.[57] Earnings stripping, on the other hand, can be used both ways.[58] The initial

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[51] *Treaty Changes—Fifth Protocol Highlights*, SERBINSKI ACCOUNTING FIRMS, http://www.serbinski.com/whats-new/fifth-protocol.shtml [https://perma.cc/86C3-Z3E6].

[52] *See generally* Michael Hiltzik, *Solving the inversion crisis: How the U.S. can keep companies at home*, L.A. TIMES (Dec. 4, 2015), http://www.latimes.com/business/hiltzik/la-fi-hiltzik-20151204-column.html [https://perma.cc/3ESZ-PPZV].

[53] Keith Martin, *Corporate Inversions—section 7874, section 385, section 163(j), section 956, hopscotch loans, earnings stripping, Levin, Schumer, Wyden, Treasury, government contract*, CHADBOURNE (Sept. 2014), http://www.chadbourne.com/corporate_inversions_0914_projectfinance/ [https://perma.cc/U359-35G4].

[54] *Id.*

[55] *Id.*

[56] *See id.*

[57] *Id.*

[58] Jeanne Sahadi, *Treasury acts to stop overseas tax 'inversions'*, CNN MONEY (Sept. 22, 2014, 10:08 PM), http://money.cnn.com/2014/09/22/news/economy/treasury-inversions/ [https://perma.cc/5F3W-8WKE].

loan is a way to get foreign earnings back into the United States, while the interest payments are a way to get U.S. earnings out of the country.[59]

C. Previous Instances of Tax Inversion by U.S. Companies

Tax inversions were first spotted amongst U.S. corporations in the early 1980s.[60] In 1983, McDermott International Inc. became the first American company to leave these shores for greener tax pastures, which happened to be in Panama.[61] This specific inversion tactic was accomplished through a loophole in the Internal Revenue Code, which was shortly thereafter closed by Congress.[62] Following that action, inversions laid relatively dormant until 1990, when Flextronics International Ltd. made the move from California to Singapore.[63] The true decade of inversions took place shortly thereafter, from 1994–2003, when twenty-nine separate companies uprooted their corporate headquarters.[64] Notable among these companies were Tyco (New Hampshire to Switzerland), Fruit of the Loom (Kentucky to the Cayman Islands), Ingersoll-Rand (New Jersey to Ireland), and Michael Kors (New York to Hong Kong).[65]

In 2004, Congress decided to take action to curb inversions by passing the American Jobs Creation Act of 2004.[66] In short, the Act aimed to effectively end inversions to countries where no substantial business operations took place by denying the tax advantages of an inversion if the previously American corporation's stockholders held 80 percent or more of the new foreign

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[59] *Id.*

[60] *See* Jesse Drucker & Zachary R. Mider, *Tax Inversion: How U.S. Companies Buy Tax Breaks*, BLOOMBERG QUICKTAKE (May 27, 2014) (revised Nov. 23, 2015), http://www.bloombergview.com/quicktake/tax-inversion [https://perma.cc/U85X-LJPV].

[61] *Tracking Tax Runaways*, BLOOMBERG (Oct. 14, 2014), http://www.bloomberg.com/infographics/2014-09-18/tax-runaways-tracking-inversions.html [https://perma.cc/QHP4-UWWZ].

[62] Orsolya Kun, *Corporate Inversions: The Interplay of Tax, Corporate, and Economic Implications*, 29 DEL. J. CORP. L. 313, 315–16 (2004).

[63] *Tracking Tax Runaways*, *supra* note 61.

[64] *Id.*

[65] *Id.*

[66] *See infra* notes 74–87.

firm.[67] This new law stemmed the tide of inversions, but only those to locations where no substantial business operations took place.[68] From 2005 to 2014, forty more companies expatriated out of the United States.[69] In 2015, six inversions took place, with another four currently pending.[70] The eleven completed or pending mergers do not include the potential inversions of notable companies, such as AbbVie.[71]

II. PREVIOUS "SOLUTIONS" TO THE TAX INVERSION PROBLEM AND THEIR EFFECTS ON INVERSIONS

It is clear that the number of expatriations of U.S. companies has been on the rise over the last twenty years.[72] This is despite the passage of what was supposed to be an effective solution in 2004.[73] The government continues to try to curb tax inversions through legislation and agency directives, while academics and critics have proposed their own fixes to the problem.

A. Solutions Enacted by the Federal Government

The U.S. government has been proactive over the last twelve years in trying to prevent inversions. The following Sections will address the major steps that the government has taken since 2004.

1. The American Jobs Creation Act of 2004

Just two weeks before his re-election, President George W. Bush signed the American Jobs Creation Act of 2004 into effect.[74] The

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[67] *See* DONALD J. MARPLES & JANE G. GRAVELLE, CONG. RESEARCH SERV., R43568, CORPORATE EXPATRIATION, INVERSIONS, AND MERGERS: TAX ISSUES 1 (2014), http://fas.org/sgp/crs/misc/R43568.pdf [https://perma.cc/8RAZ-KBUJ].

[68] *See id.*

[69] *Tracking Tax Runaways*, *supra* note 61.

[70] Drucker & Mider, *supra* note 60.

[71] Catherine Boyle, *Lew's tax inversion move: The deals which might suffer*, CNBC (Sept. 23, 2014 8:46 AM), http://www.cnbc.com/id/102024229# [https://perma.cc/4P4Y-WQ3Z].

[72] *See supra* notes 63–70.

[73] *See supra* notes 66–68.

[74] American Jobs Creation Act of 2004, Pub. L. No. 108-356, 118 Stat. 1418 (2004). *See also* Charles H. Purcell, Robert D. Starin, Eric E. Freedman & Andrew H. Zuccotti, *American Jobs Creation Act of 2004—Summary of Major*

Act was the first major restructuring of business taxes since the 1986 Tax Reform Act.[75] Among the many tax reforms contained within the American Jobs Creation Act of 2004 were specific rules regarding the eligibility of inverted companies to avoid U.S. taxation.[76] The legislation separated inverted companies into two distinct categories.[77]

The first category treats an inverted corporation as a U.S.-domiciled company for tax purposes if the newly formed entity satisfies three distinct elements. First, the foreign entity must have acquired a company previously incorporated in the United States.[78] Second, the former owners of the U.S. corporation must own 80 percent or more of the new foreign company.[79] Third, the newly formed entity must not have any substantial business activities in the domicile of the foreign entity.[80]

A company has "substantial business activities" in a foreign domicile when (1) at least 25 percent of the company's employees are employed there and at least 25 percent of the overall payroll is housed there, (2) at least 25 percent of the company's assets are located there, and (3) at least 25 percent of the company's income is derived from there.[81]

The second category, "limited inversions," utilizes the same elements as the first category, with one significant difference: the former owners of the U.S. company must own from 60 to 80 percent of the new entity.[82]

Energy Legislation, K&L GATES (Nov. 11, 2004), http://www.klgates.com/american-jobs-creation-act-of-2004---summary-of-major-energy-legislation-11-10-2004/ [https://perma.cc/Y6R4-E4LA].

[75] Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2085 (1986). *See also The American Jobs Creation Act of 2004: Overview of Domestic & International Provisions* 4, DELOITTE (2004), http://benefitslink.com/articles/deloitteETI041008.pdf [https://perma.cc/73VZ-HZTJ].

[76] *Id.*

[77] Eloine Kim, *Corporate Inversion: Will the American Jobs Creation Act of 2004 Reduce the Incentive to Re-Incorporate?*, 4 J. INT'L BUS. & L. 152, 160, 164 (2005), http://scholarlycommons.law.hofstra.edu/cgi/viewcontent.cgi?article=1130&context=jibl [https://perma.cc/2RG-DHC3].

[78] *Id.* at 164.

[79] *Id.*

[80] *Id.*

[81] I.R.S. Bulletin T.D. 9592 (July 9, 2012), http://www.irs.gov/irb/2012-28_IRB/ar10.html#d0e2458 [https://perma.cc/32PK-GQ7X].

[82] Kim, *supra* note 77, at 164.

Companies that fall within the first category are still classified under the Internal Revenue Code as domestic corporations and are, as such, ineligible for the benefits associated with expatriation.[83] Companies classified as "limited inversions" within the second category are deemed foreign entities by the Internal Revenue Code, but not without restrictions.[84] The foreign entity would be subject to U.S. taxation on any gain made in the actual inversion, along with any gain or income recognized within ten years following the inversion on the transfer of stock or the licensing of certain property.[85]

The new classifications might have helped to avoid the specific types of inversions mentioned, but they still did not address the real reason behind tax inversions. A company using an inversion does not typically do so merely to relocate, but instead to try to avoid the worldwide taxation system and to partake in earnings stripping.[86] With the incentive to invert still alive, companies will look for new ways to escape U.S. taxation by either finding new and creative ways to expatriate or even choosing to incorporate outside of the United States.[87]

2. New Department of the Treasury Regulations

On August 5, 2014, the Obama Administration stated that it was looking very seriously into taking executive action to put a halt to tax inversion deals.[88] The threat of action on the matter apparently did nothing to deter Burger King from going ahead with its plans. Some news outlets saw the move as a direct challenge to the White House and the executive branch in general.[89]

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[83] DELOITTE, *supra* note 75, at 24.

[84] Kim, *supra* note 77, at 164.

[85] *Id.*

[86] *See supra* notes 37–51.

[87] Kim, *supra* note 77, at 166.

[88] Myles Udlund & Brett Logiurato, *Obama Is Considering Bypassing Congress To Try To Stop Companies From Leaving America To Save On Taxes*, BUS. INSIDER (Aug. 5, 2014, 7:28 PM), http://www.businessinsider.com/obama-executive-action-on-inversions-warren-2014-8 [https://perma.cc/WE8A-Y92C].

[89] *See* Joe Weisenthal, *Burger King Just Issued A Direct Challenge To The White House*, BUS. INSIDER (Aug. 25, 2014, 6:58 AM), http://www.businessinsider.com/the-politics-of-burger-king-possible-purchase-of-tim-hortons-2014-8 [https://perma.cc/ER6J-CQ36].

In response, just about a month later, the Treasury Department issued new guidelines that President Obama said would "discourage companies from taking advantage of corporate inversions—moving their tax residence overseas on paper to avoid paying their fair share in taxes here at home."[90]

The new Treasury Department regulations are aimed at targeting several major facets of inversion deals.[91] Among the regulations are two very important changes to the inversion landscape relevant to the Burger King-Tim Hortons merger. First, "hopscotch" loans have been rendered useless.[92] Now, when a U.S. foreign subsidiary makes a loan to the new foreign parent, that loan is considered to be U.S. property for tax purposes and, thus, treats the loan as if it had been made before the inversion had taken place.[93]

Second, staying beneath the ever-important 80 percent ownership threshold to avoid being labeled a U.S.-domiciled company[94] has become more difficult.[95] It is not uncommon for a company involved in an inversion transaction to be below the 80 percent threshold. Some companies, in order to get below the threshold, have taken to giving out a large dividend just prior to the inversion that essentially shrinks the size of the U.S. corporation.[96] This smaller subsidiary then accounts for less than 80 percent ownership of the newly formed company.[97] The new Treasury requirements have made those types of dividends inconsequential because such dividends will not be counted for the purposes of determining ownership.[98]

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[90] Kevin Drawbaugh & Jason Lange, *U.S. Treasury moves against tax-avoidance 'inversion' deals*, REUTERS (Sept. 23, 2014, 11:09 AM), http://www.reuters.com/article/2014/09/23/us-tax-inversion-treasury-idUSKCN0HH2TM20140923 [https://perma.cc/9JUM-VBCZ].

[91] Press Release, U.S. Department of the Treasury, Fact Sheet: Treasury Actions to Rein in Corporate Tax Inversions (Sept. 22, 2014), http://www.treasury.gov/press-center/press-releases/Pages/jl2645.aspx [https://perma.cc/4WN3-R2YP].

[92] *Id.*

[93] *Id.*

[94] *See supra* notes 78–80.

[95] Sahadi, *supra* note 58.

[96] *Id.*

[97] *Id.*

[98] *Id.*

These regulations are merely the first salvo in the government's fight to stop inversions, and they are relatively weak in firepower. The provisions do not even mention earnings stripping, let alone a way to punish the practice.[99] However, the Department of the Treasury has said that it plans on implementing more guidelines in the future.[100]

Before discussing the application of purely academic solutions, it needs to be made clear that Burger King already satisfies the elements of both the American Jobs Creation Act of 2004 and the new Treasury Department regulations. Under the final deal structure, the previous owners of Burger King own roughly 76 percent of the new parent company.[101] This structure allows the new parent to be recognized as a "limited inversion," which makes Burger King a foreign entity for tax purposes.[102]

B. Solutions Proposed by Academics

While the U.S. government has produced more practical solutions within the context of current law, academics and scholars have been apt to propose more drastic and wide-ranging methods to curb inversions. The following Sections will address the most common of these proposals.

1. Shift to a Territorial Tax System

A territorial tax system seems to be the most obvious solution to the inversion problem as a whole, considering it is the default basis for the procedure. If the United States were to switch from its current worldwide system, the incentive to keep foreign earnings from being repatriated would no longer exist, as

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[99] Howard Gleckman, *Treasury's New Rules May Slow, But Won't Stop Corporate Tax Inversions*, FORBES (Sept. 23, 2014, 6:41 PM), http://www.forbes.com/sites/beltway/2014/09/23/treasurys-new-rules-may-slow-but-wont-stop-corporate-tax-inversions/.

[100] *Id.*

[101] New Red Can. P'ship, Registration Statement 11 (Form S-4) (Sept. 16, 2014) [hereinafter New Red Can. P'ship]. The New Red Canada Partnership was later named Restaurant Brands once the merger was completed. *See* Rest. Brands Int'l Ltd. P'ship, Form 8-K (Dec. 12, 2014).

[102] *See supra* notes 77–80.

there would be no additional U.S. tax levied as a sort of toxic "cherry on top."

Some argue that such a change would not make a difference in deterring companies from expatriation. Professor Reuven S. Avi-Yonah of the University of Michigan Law School writes that U.S. multinationals would still elect to invert "even if the U.S. adopted territoriality."[103] One of the main reasons Professor Avi-Yonah cites is that earnings stripping can lower the U.S. tax bill with no condition upon which tax system the United States employs.[104] Others argue that a territorial tax system would have done absolutely nothing to stop another fundamental reason for inversions: "hopscotch" loans.[105]

Yet, despite the criticism, there are those who believe that the switch could do nothing but help to get earnings from U.S. companies abroad back into the United States. As of July of 2014, U.S. companies have nearly $2 trillion in offshore accounts that are free from U.S. taxation.[106] Further, the tax bill of a company in a territorial tax system can be considerably less than the tax bill of a company subject to the worldwide tax system.[107] For example, a U.S. company has a subsidiary operating in Switzerland. That foreign affiliate would be forced to pay the full 35 percent U.S. tax rate on earnings there (a combination of both Swiss and U.S. taxes, with deductions applied).[108] The U.S. company would not actually be able to take advantage of the 8.5 percent Swiss corporate tax rate.[109]

For Burger King, the shift to a territorial tax system would have been unlikely to deter the company from reforming in Canada.

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[103] Reuven S. Avi-Yonah, *For Haven's Sake: Reflections on Inversion Transactions*, TAX NOTES 1793 (June 17, 2002), http://repository.law.umich.edu/cgi/viewcontent.cgi?article=1813&context=articles [https://perma.cc/5HU3-SUVW].

[104] *See generally id.*

[105] *See* Martin Sullivan, *Don't Count on Tax Reform to Stop Inversions*, FORBES (Aug. 5, 2014, 11:20 AM), http://www.forbes.com/sites/taxanalysts/2014/08/05/dont-count-on-tax-reform-to-stop-inversions/.

[106] *How to stop the inversion perversion*, ECONOMIST (July 26, 2014), http://www.economist.com/news/leaders/21608751-restricting-companies-moving-abroad-no-substitute-corporate-tax-reform-how-stop [https://perma.cc/KB59-6NUA].

[107] Diana Furchtgott-Roth & Yevgeniy Feyman, *The Merits of a Territorial System*, 29 MANN. INST. POL'Y RES. 1, 3 (2012), http://www.manhattan-institute.org/pdf/ir_29.pdf [https://perma.cc/W5XB-YJ23].

[108] *Id.*

[109] *Id.*

Though the switch might make it attractive for most companies to repatriate foreign income, Canada has special provisions that allow for repatriated income to be tax-free, provided it is "derived from active business income."[110] Because the effective rates of taxation between Canada and the United States are not substantially different, the allure of repatriating foreign profit would likely be attractive enough to cause Burger King to leave.[111]

2. Enact Strict Limits on Earnings Stripping

As was explained earlier, another one of the primary factors driving U.S. companies to invert is earnings stripping.[112] There are a couple of theoretical measures the United States could take to eliminate a foreign company's earnings stripping power.

First, there could be an outright ban or severe limits on earnings stripping by foreign companies. The problem with this specific measure is that not all foreign companies are inverted U.S. companies.[113] The United States is an attractive investment opportunity for foreign companies because there is the potential for an excellent return.[114] With earnings stripping available, companies can then send a significant portion of that return out of the United States and back to the foreign parent—the same way an inverted company would.[115] If that power were to be taken away and foreign companies were forced to pay the U.S. tax rate on U.S. earnings, some would be less apt to invest resources here.[116]

Second, Congress and the Department of the Treasury could specifically target inverted companies in the passage of earnings stripping restrictions.[117] In fact, such options are already being

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[110] John Carney, *Burger King's Move Should Spare It Some Tax*, WALL ST. J. (Aug. 26, 2014, 6:07 PM), http://www.wsj.com/articles/burger-kings-move-should-spare-it-some-tax-heard-on-the-street-1409090819?autologin=y [https://perma.cc/8J5W-8UGA] (internal quote removed).

[111] *See supra* notes 52–56.

[112] *See supra* Part I.B.2.

[113] *See* Martin Sullivan, *Can Congress Pass Tax Reform That Would Stop Inversions?*, FORBES (Sept. 30, 2014, 8:40 AM), http://www.forbes.com/sites/taxanalysts/2014/09/30/can-congress-pass-tax-reform-that-would-stop-inversions/.

[114] *Id.*

[115] *Id.*

[116] *Id.*

[117] *Id.*

discussed. Senator Charles Schumer of New York recently proposed his own method of limiting earnings stripping, which centers on limiting the amount of interest expense paid to the foreign parent that the U.S. subsidiary could deduct.[118]

Such a move, on its face, would seem to limit the amount of earnings that a company could strip. However, there is a major flaw. The reason a company pays the interest is to get U.S. earnings out of the country in the form of interest, not to deduct the interest payments on the company's tax return;[119] that is just an added bonus. Putting a cap on what is deductible will not keep a company from stripping earnings if it is still advantageous to do so.

Criticism also rests on whether earnings stripping is actually a big enough problem for the United States to make it a worthwhile fight. In terms of the interest deduction argument, the IRS has data showing that foreign companies, including subsidiaries and inverted companies, actually deduct less than domestic corporations.[120]

3. Lower the Corporate Income Tax Rate

For those seeking a simple option that is politically easy to explain, decreasing the corporate income tax is ideal. On the surface, the United States has the highest statutory corporate income tax rate in the world.[121] Though lowering the corporate income tax would seem to be merely a "quick fix," it does have some definite benefits for business in the United States.

Consider even a 5 percent decrease in the statutory tax rate across all income levels: such a move would bring several advantages to U.S. businesses.[122] First, the U.S. tax rate would become more in line with the tax rates of its major trading partners.[123]

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[118] Siobhan Hughes, *Q&A: Schumer's Proposal to Strip Benefits of Corporate Earnings Stripping*, WALL ST. J. (Aug. 14, 2014, 4:50 PM), http://blogs.wsj.com/washwire/2014/08/14/qa-schumers-proposal-to-strip-benefits-of-corporate-earnings-stripping/ [https://perma.cc/5KKJ-LCPF].

[119] MARPLES, *supra* note 35.

[120] *See* Kyle Pomerleau, *New Earnings Stripping Bill is Fundamentally Unserious*, TAX FOUND. (Sept. 9, 2014), http://taxfoundation.org/blog/new-earnings-stripping-bill-fundamentally-unserious [https://perma.cc/C9NG-8RJR].

[121] HERITAGE FOUND., *supra* note 24.

[122] *See* 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, 571 (2003).

[123] *Id.*

Second, it would reduce domestic costs to U.S. exporters.[124] As these costs are often factored into prices, U.S. exports would become more attractive to foreign buyers. Third, multinationals (both foreign and domestic) would be more apt to repatriate their foreign-source income for use in the United States.[125] Finally, a lower tax rate might serve as an incentive for investment by foreign corporations in the United States.[126]

The benefits of a lower corporate income tax rate do not stop at the corporate level. According to the Heritage Foundation, a decrease to a 25 percent federal corporate income tax rate would result in (1) an annual rise in GDP of nearly $132 billion per year, (2) an increase of nearly 581,000 available jobs annually, and (3) a $2,484 annual increase in after-tax income for a typical family of four.[127]

So, if there are so many benefits to be had, why hasn't anything been done to lower the statutory corporate income tax rate? It is certainly not for a lack of effort. President Obama proposed to lower the rate in both 2012[128] and 2013.[129] There was a bipartisan plan born out of the House Ways and Means Committee in early 2014 that still has yet to be acted upon.[130] Ultimately, and unsurprisingly, it comes down to the partisan divide and the apparent inability to compromise. Republicans want comprehensive tax reform that would also include tax cuts for the wealthiest Americans,

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[124] *Id.*

[125] *Id.*

[126] *Id.*

[127] Dr. Karen Campbell & John L. Ligon, *The Economic Impact of a 25 Percent Corporate Income Tax Rate*, HERITAGE FOUND. (Dec. 2, 2010), http://www.heritage.org/research/reports/2010/12/the-economic-impact-of-a-25-percent-corporate-income-tax-rate [https://perma.cc/2U8W-RZLV].

[128] Zachary A. Goldfarb, *Obama proposes lowering corporate tax rate to 28 percent*, WASH. POST (Feb. 22, 2012), http://www.washingtonpost.com/business/economy/obama-to-propose-lowering-corporate-tax-rate-to-28-percent/2012/02/22/gIQA1sjdSR_story.html [https://perma.cc/L2WM-NFW3].

[129] John D. McKinnon & Colleen McCain Nelson, *Obama Offers New Deal on Corporate Taxes, Jobs*, WALL ST. J. (July 31, 2013, 6:36 AM), http://online.wsj.com/news/articles/SB10001424127887323854904578636903853862978?mod=ITP_pageone_0&mg=reno64-wsj [https://perma.cc/AV4U-CZBG].

[130] Howard Gleckman, *What Dave Camp's Tax Reform Plan Would Really Mean*, FORBES (July 8, 2014, 3:28 PM), http://www.forbes.com/sites/beltway/2014/07/08/what-dave-camps-tax-reform-plan-would-really-mean/.

which is something that Democrats are firmly against. Corporate tax reform would be the best option to keep companies from inverting, but it seems to be far more polarizing than it should be.

4. Ban Inversions

If curbing corporate inversions is the aim of Congress, why not target the inversions themselves rather than the ancillary benefits? The answer is that it is far too complicated to declare an outright ban on inversions. It all rests upon what the definition of an inversion is. If it is defined as a company that engages in a sort of "sham" merger with a small foreign corporation so that it might reincorporate elsewhere, then the "ban" was already put in effect by the American Jobs Creation Act of 2004.[131] The threshold is already quite high for a domestic company to be able to claim the benefits of an inversion without still being subjected wholly to the U.S. tax system.[132]

The amount of inversions out of the United States is considerably smaller than the amount of inbound M&A activity.[133] In 2013, there were five completed inversions of U.S. corporations.[134] That same year, there were 1,278 transactions worth about $60 billion involving the purchase of U.S. assets by foreign companies.[135] The ban on full-fledged inversions seems to be effective on that front, and anything more—based on the current thresholds—would seem to be a hindrance to genuine business interests.

III. BURGER KING AND TIM HORTONS: A NEW QUAGMIRE

The Burger King-Tim Hortons merger is a multi-faceted deal that is based on several different environmental and internal factors for each company. Section A will examine Burger King's

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[131] *See supra* notes 74–87.
[132] *Id.*
[133] *See* Scott A. Hodge, *IRS Data Contradicts Kleinbard's Warnings of Earnings Stripping from Inversions*, TAX FOUND. (Sept. 2, 2014), http://taxfoundation.org/blog/irs-data-contradicts-kleinbard-s-warnings-earnings-stripping-inversions [https://perma.cc/3MGP-VXLA].
[134] *Id.*
[135] *Id.*

relative market position at the time of the deal. Section B will analyze the key details of the merger agreement. Section C will take a look at the general reaction to the deal, in both the federal government and the community.

A. Faltering Business

It has been a rough start to the decade for Burger King. In 2012, it was unseated as the second-largest burger chain in the United States for the first time, by Wendy's.[136] This is troubling for a few reasons. First, Wendy's has fewer stores nationwide than Burger King, which points to lesser sales per store.[137] Second, in 2006, Burger King and Wendy's placed two and three, respectively, in the overall restaurant rankings.[138] Since then, Subway and Starbucks have passed them both, even though McDonald's has been able to maintain the number one spot.[139]

Why has Burger King been in a steady decline? One reason is poor strategic vision. When the Great Recession hit in 2008 and forced many to look for cheaper alternatives for their eating pleasure, McDonald's expanded its menu to include the McCafe line and various salads and wraps.[140] Meanwhile, Burger King stood firm and continued to cater only to "young males with an appetite for burgers."[141] Marketing failures have not helped either. The company just recently ended its poor experiment with "Satisfries," dubbed the "saddest fries" by detractors.[142] The company even

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[136] Candice Choi, *Wendy's, not Burger King, is No. 2 in sales*, USA TODAY (Mar. 19, 2012, 7:28 PM), http://usatoday30.usatoday.com/money/industries/food/story/2012-03-19/wendys-not-burger-king-number-2/53650010/1 [https://perma.cc/PK7Y-ZCUQ].

[137] *Id.*

[138] *Id.*

[139] *Id.*

[140] Jordan Melnick, *Long Live the King*, QSR MAGAZINE (Aug. 2012), http://www.qsrmagazine.com/reports/long-live-king [https://perma.cc/DZT2-C454].

[141] *Id.*

[142] Leo Sun, *Why Burger King's 'Satisfries' Failed to Satisfy Hungry Americans*, THE MOTLEY FOOL (Aug. 17, 2014), http://www.fool.com/investing/general/2014/08/17/why-burger-kings-satisfries-failed-to-satisfy-hung.aspx [https://perma.cc/4FDA-QV53].

thought it was somehow a good idea to offer a Facebook promotion whereby if users "defriended" ten friends, they could get a coupon for a free Whopper.[143]

A second reason is the growing popularity of more health-conscious and better quality fast-food options. Restaurants like Panera Bread Co., Chipotle Mexican Grill, and Five Guys Burgers and Fries all grew considerably according to the same survey that dropped Burger King so precipitously in the rankings.[144] Social awareness and the use of non-genetically modified ingredients have become a major selling point for consumers.[145]

In 2010, major global investment firm 3G Capital purchased Burger King.[146] In announcing the acquisition to the world, 3G Capital made it clear that it saw exciting opportunities for Burger King in both its product offerings and in international expansion.[147] 3G Capital has a reputation within the industry for being a profit maximization enabler in the form of cost-cutting measures.[148] Three key goals in place—new products, international expansion, and cost-cutting—and, suddenly, the acquisition of a "Canadian icon"[149] does not sound like a bad idea.

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[143] Jenna Wortham, *'Whopper Sacrifice' De-Friended on Facebook*, N.Y. TIMES (Jan. 15, 2009, 6:51 PM), http://bits.blogs.nytimes.com/2009/01/15/whopper-sacrifice-de-friended-on-facebook/ [https://perma.cc/LX2K-XX6J].

[144] Tiffany Hsu, *Wendy's dethrones Burger King as second-biggest burger chain*, L.A. TIMES (Mar. 20, 2012), http://articles.latimes.com/2012/mar/20/business/la-fi-wendys-20120320 [https://perma.cc/CL6X-3Y8S].

[145] Chris Nichols, *At McDonald's despair, at Chipotle arrogance*, YAHOO! FIN. (Oct. 22, 2014, 3:55 PM), http://finance.yahoo.com/news/at-mcdonald-s-despair--at-chipotle-arrogance-165813219.html [https://perma.cc/PW6R-94B7].

[146] Press Release, Burger King Worldwide Inc., 3G Capital Acquisition of Burger King Holdings, Inc. (Oct. 19, 2010), http://investor.rbi.com/~/media/Files/B/BurgerKing-IR/documents/lf/pdfs/press-release-20101019.pdf [https://perma.cc/4LLM-BUQK].

[147] *Id.*

[148] Sital S. Patel, *Why 3G Capital won't flip its Burger King-Tim Horton's deal*, MARKETWATCH (Aug. 26, 2014, 1:36 PM), http://blogs.marketwatch.com/thetell/2014/08/26/why-3g-capital-wont-flip-its-burger-king-tim-hortons-deal/ [https://perma.cc/CLP3-8EJC].

[149] Sonya Bell, *Tim Hortons: a Canadian icon that belongs to us all*, THE GUARDIAN (Aug. 26, 2014), http://www.theguardian.com/world/2014/aug/26/tim-hortons-canadian-icon-burger-king [https://perma.cc/PN54-CCXZ].

B. The Anatomy of a Deal

The merger is a deal between national treasures. Burger King has been a U.S. institution since 1954[150] and is the second-largest hamburger chain in the world.[151] Tim Hortons has been a source of pride for Canada since 1964, when Toronto Maple Leaf and future Hockey Hall of Fame member Tim Horton decided to open a single coffee and doughnut shop in Hamilton, Ontario.[152] That single shop has grown into the largest quick service restaurant in Canada.[153] Interestingly, this is not Tim Hortons's first go-around as a merger candidate with a major American fast-food restaurant.[154] In 1995, Wendy's purchased Tim Hortons, but spun it off ten years later[155] so that the company could evaluate the value of the two restaurant chains separately.[156]

Altogether, Burger King acquired Tim Hortons for roughly $11.4 billion (CA$12.5 billion).[157] Debt accounted for $3 billion of the total, all of which was provided solely by Warren Buffett's Berkshire Hathaway.[158] The debt ultimately came out to a 9

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[150] *About Us*, BURGER KING, http://www.bk.com/about-bk [https://perma.cc/M76K-4VJC].

[151] Burger King is still the second-largest hamburger chain internationally, despite being passed domestically by Wendy's. *Id.*

[152] *About Us*, TIM HORTON'S, http://www.timhortons.com/us/en/about/the-story-of-tim-hortons.php [https://perma.cc/7C9F-JQR4].

[153] *Corporate Profile*, TIM HORTON'S, http://www.timhortons.com/us/en/corporate/profile.php [https://perma.cc/9Q6X-8ZFS].

[154] *See 1995: U.S. burger giant buys Tim Hortons doughnut chain*, CBC, http://www.cbc.ca/archives/categories/economy-business/consumer-goods/tim-hortons-coffee-crullers-and-canadiana/us-burger-giant-buys-tim-hortons-doughnut-chain.html [https://perma.cc/NK5V-FFHH].

[155] The idea of spinning off Tim Hortons from Wendy's was proposed by activist investor William Ackman. Mr. Ackman now, coincidentally, owns 11 percent of Burger King. *See* Rob Cox, *Burger King Wins Support Where Wendy's Didn't in Tim Hortons Deal*, N.Y. TIMES (Aug. 26, 2014, 2:20 PM), http://dealbook.nytimes.com/2014/08/26/burger-king-wins-support-where-wendys-didn't-in-tim-hortons-deal/ [https://perma.cc/YD3S-V74J].

[156] *Id.*

[157] Patton & Giammona, *supra* note 2.

[158] Noah Buhayar, *Berkshire to Hold Common Stake in Burger King Parent*, BLOOMBERG (Dec. 17, 2014, 2:35 PM), http://www.bloomberg.com/news/articles/2014-12-15/berkshire-to-hold-larger-stake-in-burger-king-tim-hortons-parent [https://perma.cc/D3KL-MEDZ].

percent preferred equity stake in the newly formed company.[159] Overall, Tim Hortons's shareholders received CA$65.50 in cash and .8025 a share of the new entity for each share of Tim Hortons they owned.[160]

C. Reaction to the Deal

Certain members of Congress voiced an almost immediate dissatisfaction with the deal.[161] Former Congressman Dave Camp (R-Michigan) placed the blame with the White House, saying that the United States had "been down this rabbit hole before," and that if the White House does not get "serious" about inversions, more good companies will leave the country.[162] House Speaker Paul Ryan (R-Wisconsin) sees inversions as a "dangerous trend," but wants them fixed as part of an overall tax reform.[163] Former Senator Carl Levin (D-Michigan), a long-time opponent of inversions, chastised Burger King for "renouncing its U.S. citizenship" and warned that Congress cannot "wait any longer" to address corporate inversions.[164] Senator Sherrod Brown (D-Ohio) went so far as to call for a boycott of Burger King in the United States.[165]

The executive branch was quick to try and curtail inversion activity from happening in the near future. Within a month of the merger announcement, the Treasury Department proposed its new

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[159] *Id.*

[160] New Red Can. P'ship, *supra* note 101, at 4.

[161] *See* Brett Logiurato, *Here's Why Legislation Aimed At Tax Inversions Might Not Have Any Effect On Burger King*, BUS. INSIDER (Aug. 25, 2014, 3:36 PM), http://www.businessinsider.com/burger-king-tim-hortons-merger-inversion-law-2014-8 [https://perma.cc/B9Z7-7E7W].

[162] Richard Rubin & Ian Katz, *Crackdown Targets Inversions Designed to Limit U.S. Taxes*, BLOOMBERG (Sept. 22, 2014, 8:13 PM), http://www.bloomberg.com/news/2014-09-22/treasury-unveils-anti-inversion-rules-against-tax-deals.html [https://perma.cc/94K6-EJKN].

[163] Logiurato, *supra* note 161.

[164] Ramsey Cox, *Levin: Public disapproval could cost Burger King*, THE HILL (Aug. 26, 2014, 10:33 AM), http://thehill.com/blogs/floor-action/senate/215960-levin-public-disapproval-could-cost-burger-king [https://perma.cc/87FM-YJ4S].

[165] Vauhini Vara, *Is the Burger King-Tim Hortons Deal About More Than Taxes?*, NEW YORKER (Aug. 26, 2014), http://www.newyorker.com/business/currency/burger-king-wants-deal-tim-hortons [https://perma.cc/EME5-TUL3].

regulations for curbing corporate inversions.[166] President Obama recognized the Treasury Department's efforts to keep companies from seeking to "exploit this loophole" in the tax system.[167]

While the merger was met with near-unanimous scorn from the U.S. government, investors greeted the news with a great deal of optimism. On Monday, August 26th, 2014—the day that the merger was officially announced—Burger King closed up 19.5 percent from Friday's close.[168] Likewise, Tim Hortons closed 19 percent higher.[169] To further illustrate that excitement, daily volume trading was up considerably for both companies.[170]

In announcing the merger, Burger King understood the skepticism of its motives by saying that the deal was "not a tax-driven deal."[171] For the new company, Canada actually represents the largest share of revenue.[172] Something to note is that all of the skepticism about the deal is aimed at Burger King's intentions, but none of these criticisms examine the deal from Tim Hortons's perspective.[173] In terms of locations, Tim Hortons makes up roughly 25 percent of the new parent's operations.[174] However, Tim Hortons contributes more than 70 percent of the revenues.[175] The hope, according to Burger King senior management, is that the newly formed company can leverage Burger King's worldwide experience to expand Tim Hortons's massively profitable operations across the globe.[176]

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[166] *See supra* notes 88–102 and accompanying text.

[167] CBC NEWS, *supra* note 4.

[168] Adam Jones, *Burger King and Tim Hortons investors react to acquisition news*, MKT. REALIST (Aug. 28, 2014, 3:01 PM), http://marketrealist.com/2014/08/must-know-burger-king-tim-hortons-investors-react-news/ [https://perma.cc/692R-FTDG].

[169] *Id.*

[170] The average number of shares traded daily for Burger King and Tim Hortons are 600,000 and 300,000 shares, respectively. On August 26th, 21.5 million Burger King shares and 12 million Tim Hortons shares were traded on the New York Stock Exchange. *Id.*

[171] Vara, *supra* note 165.

[172] *Id.*

[173] *See supra* notes 161–65 and accompanying text.

[174] Venessa Wong, *What You Don't Know About How Tim Hortons Makes Money*, BLOOMBERG BUSINESSWEEK (Aug. 27, 2014), http://www.businessweek.com/articles/2014-08-27/tim-hortons-has-higher-revenue-than-burger-king [https://perma.cc/L73S-HAVV].

[175] *Id.*

[176] Vara, *supra* note 165.

IV. A Solution to the Inversion Problem and How It Would Keep Mergers Like the Burger King-Tim Hortons Deal from Occurring

Burger King's explanation for the merger makes sense, as far as saying that the move is not solely about taxes. However, that explanation does not quite explain why Burger King is moving to Canada, nor does it answer the question as to why the owners of a target company with more revenue than the acquiring company are only getting a 22 percent stake. The possibility of repatriating profits, as well as getting a slight tax break, are definitely incentive enough to make a move that Burger King has every right under current U.S. law to make. If Congress and the President want to keep deals like this from happening, they need to change the way the laws work. The best way to do that is not simply to choose one of the solutions listed earlier, but rather to choose from among those solutions to create a comprehensive block against non-meaningful corporate expatriations.

A. Change the Inversion Thresholds (Again)

With the new Treasury Department regulations, it has become more difficult for companies to get below the 80 percent threshold.[177] Still, it is only an 80 percent threshold. Further, the two sides have the power to dictate the terms of the stock swap. In Burger King's case, they negotiated the .8025 per share exchange with Tim Hortons.[178] It would be an unlikely coincidence if they arrived at the 76 percent ownership stake for Burger King owners randomly.[179]

Congress could amend the American Jobs Creation Act of 2004 so that it requires at most 60 percent ownership of the foreign company in order to qualify as a foreign entity. In this instance, the Burger King-Tim Hortons parent would not be considered a foreign entity as a result of its merger. Keep in mind, Burger King certainly could still pursue the merger deal if its true aims were actually operational synergies. However, it would not be

[177] Sahadi, *supra* note 58.
[178] Buhayar, *supra* note 158.
[179] *See supra* note 101.

able to invert unless it gave up a great deal of ownership, which would probably not be a preferable outcome for Burger King.

In addition, a change in the thresholds would likely render a costly and time-consuming switch to a territorial taxation system less useful.[180] By moving the threshold, many of the inversions designed simply to take advantage of a territorial tax system elsewhere would not occur because of the limits on ownership. If, after the threshold is set at 60 percent, the acquiring company still wants to acquire the target, then it is likely due to reasons other than a slight tax break on worldwide profits.

B. Put Limits on Earnings Stripping by Inverted Companies

The new Treasury Department regulations have eliminated hopscotch loans, one of the major benefits of inversions.[181] Earnings stripping, however, is still eligible to be used with full force.[182] An outright ban on earnings stripping is impractical.[183] At the same time, putting a limit on deductions really would not accomplish much, because tax deductions are not the ultimate goal of earnings stripping.[184]

The better option is to tax interest paid from a U.S. subsidiary to a foreign parent as domestic earnings would be taxed. This type of retroactive treatment of distributed earnings has already been mentioned in the new Treasury Department regulations.[185] If dividends can be counted as earnings, there is no reason why interest payments to a parent company cannot receive similar treatment.

The problem with this solution is that the United States already has a withholding tax of 30 percent that they have eliminated with other countries through various treaties.[186] The elimination of the withholding tax means that the United States cannot tax

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[180] *See* Chye-Ching Huang, Chuck Marr & Joel Friedman, *The Fiscal and Economic Risks of Territorial Taxation*, CTR. ON BUDGET AND POLICY PRIORITIES (Jan. 31, 2013), http://www.cbpp.org/cms/?fa=view&id=3895 [https://perma.cc/2JZJ-C249].

[181] Fact Sheet, *supra* note 91.

[182] *See* Gleckman, *supra* note 99.

[183] *See supra* notes 113–16 and accompanying text.

[184] *See supra* notes 117–19 and accompanying text.

[185] *See supra* notes 96–98 and accompanying text.

[186] MARPLES, *supra* note 35.

that interest income that is being held in the foreign country.[187] However, this solution proposes treating that interest income retroactively as U.S. earnings, as opposed to foreign interest income. It is a difference in language only, but it is enough of a change that it does not violate those treaties.

Another counter to this solution is that the United States wants to keep an incentive for foreign companies to invest their resources here.[188] The response is that this is true. Foreign companies want to continue to strip earnings out of the United States, and the United States would like to keep allowing truly foreign companies to do it because they are bringing resources into the country. In order to allow foreign companies to strip while keeping inverted companies from stripping, the United States could impose restrictions on the eligibility of foreign companies to partake in earnings stripping. The most obvious choice would be a restriction based on time abroad. The new regulations could state that an inverted company will be subject to retroactive earnings taxation for a period of five years. This would give companies thinking about inverting another reason to take a second look at their plans to decide whether they are looking to invert merely for short-term advantages or long-term synergies.

CONCLUSION

This Note has proposed a hybrid solution in order to deter corporate expatriations, but not necessarily the merger deals themselves. If a merger between Burger King and Tim Hortons makes operational sense, there is no reason for the U.S. government to stand in the way. The concern has never been that this merger is the sort of "sham" merger that the American Jobs Creation Act of 2004 was initially designed to block. Instead, the concern is why Burger King finds it necessary to create a Canadian—as opposed to a U.S.—parent. If the solution that this Note has proposed were implemented, Burger King would need and want a better reason than merely the benefits that would now be rendered moot. In the end, the U.S. government wants to solve the problem of getting what it feels it deserves from operations carried out within its borders. This solution is the answer.

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[187] *Id.*

[188] *See supra* notes 113–16 and accompanying text.