Congress of the United States
JOINT COMMITTEE ON TAXATION
Washington, DC 20515–6453

JUL 1 4 2015

**MEMORANDUM**

**TO:** [redacted]

**FROM:** Thomas A. Barthold T.A.B.

**SUBJECT:** Revenue Estimate Request

This memorandum is in response to your request for revenue estimates of H.R. 415, the "Stop Corporate Inversions Act of 2015," which would limit the ability of U.S. domestic entities to invert.

Under present law, the U.S. tax treatment of a multinational corporate group depends significantly on whether the parent corporation of the group is domestic or foreign. For purposes of U.S. tax law, a corporation is treated as domestic if it is incorporated under the laws of the United States or of any State.[1] All other corporations (that is, those incorporated under the laws of foreign countries) are treated as foreign.[2] Thus, place of incorporation determines whether a corporation is treated as domestic or foreign for purposes of U.S. tax law, irrespective of other factors that might be thought to bear on a corporation's "nationality," such as the location of the corporation's management activities, employees, business assets, operations, revenue sources, the exchanges on which the corporation's stock is traded, or the residence of the corporation's shareholders. Only domestic corporations are subject to U.S. tax on a worldwide basis. Foreign corporations are taxed only on income that has a sufficient connection with the United States.

Until enactment of the American Jobs Creation Act of 2004 ("AJCA"),[3] a U.S. parent corporation could reincorporate in a foreign country, potentially without any exit tax to compensate the United States for the loss of future tax revenue from the departing company.[4] It

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[1] Sec. 7701(a)(4).

[2] Sec. 7701(a)(5).

[3] Pub. L. No. 108-357.

[4] For a description of the possible tax consequences of a reincorporation transaction before AJCA, see Joint Committee on Taxation, *Background and Description of Present-Law Rules and Proposals Relating to Corporate Inversion Transactions* (JCX-52-02), June 5, 2002, p. 4.

was not always clear, however, whether the re-incorporations had a significant non-tax purpose or effect, or whether the corporate group had a significant business presence in the new country of incorporation. These transactions were commonly referred to as inversions. Under prior law, inversion transactions could produce a variety of tax benefits, including the removal of a group's foreign operations from U.S. tax jurisdiction and the potential for reduction of U.S. tax on U.S.-source income through, for example, large payments of deductible interest or royalties from a U.S. subsidiary to the new foreign parent (subject to certain deduction restrictions such as the section 163(j) earnings stripping rules for some related party interest payments).

AJCA included provisions designed to curtail inversion transactions. In particular, AJCA section 801 added to the Code the anti-inversion rules of section 7874. These anti-inversion rules deny certain tax benefits of a typical inversion transaction by deeming the new top-tier foreign corporation to be a domestic corporation for all Federal tax purposes. This sanction generally applies to a transaction in which, pursuant to a plan or a series of related transactions: (1) a U.S. corporation becomes a subsidiary of a foreign-incorporated entity or otherwise transfers substantially all of its properties to such an entity in a transaction completed after March 4, 2003; (2) the former shareholders of the U.S. corporation hold (by reason of the stock they had held in the U.S. corporation) 80 percent or more (by vote or value) of the stock of the foreign-incorporated entity after the transaction; and (3) the foreign-incorporated entity, considered together with all companies connected to it by a chain of greater than 50 percent ownership (that is, the "expanded affiliated group"), does not have substantial business activities in the entity's country of incorporation, compared to the total worldwide business activities of the expanded affiliated group.[5]

Similar rules apply if a foreign corporation acquires substantially all of the properties constituting a trade or business of a domestic partnership.[6]

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[5] AJCA also provides a lesser set of sanctions (the "toll charge rules") with respect to a transaction that would meet the definition of an inversion transaction described above, except that the 80 percent ownership threshold is not met. In such a case, if at least a 60-percent ownership threshold is met, a second set of rules applies to the inversion. Under these rules, the inversion transaction is respected (that is, the foreign corporation is treated as foreign), but any applicable corporate-level inversion gain (defined in section 7874(d)(2)) generally may not be offset by tax attributes such as net operating losses or foreign tax credits.

[6] Sec. 7874(a)(2)(B)(i).

**TO:** [redacted] 
**SUBJECT:** Revenue Estimate Request

Your proposal eliminates the toll charge rules for transactions in which historic shareholders of the expatriated entity own at least 60 percent, but less than 80 percent, of the stock of the new foreign-incorporated entity.

The proposal reduces the historic stock ownership threshold at which the new foreign-incorporated entity is treated for purposes of the Code as a domestic corporation from 80-percent historic ownership to more than 50-percent historic ownership.

Consequently, if, in a transaction that otherwise satisfies the present law requirements for applicability of the anti-inversion rules, the historic shareholders of the former domestic corporation own more than 50 percent of the stock (by vote or value) of the new foreign-incorporated entity, the new foreign-incorporated entity is considered a domestic corporation for all purposes of the Code.

The proposal provides that, if a transaction satisfies requirements for applicability of the anti-inversion rules except for the 50-percent historic ownership test, the new foreign-incorporated entity is treated as a domestic corporation for all purposes of the Code if the expanded affiliated group that includes the new foreign corporation has significant business activities in the United States and the management and control of the expanded affiliated group occurs, directly or indirectly, primarily within the United States.

The proposal is effective for taxable years ending after May 8, 2014 and for acquisitions occurring after May 8, 2014. For purposes of estimating your proposals, we have assumed that it would be enacted August 1, 2015.

We estimate that your proposal would have the following effects on Federal fiscal year liabilities.

**Fiscal Years**
**[Billions of Dollars]**

| 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2015-20 | 2015-25 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 0.2 | 2.4 | 2.2 | 2.7 | 3.2 | 3.6 | 4.1 | 4.6 | 5.2 | 5.9 | 6.9 | 14.3 | 41.0 |