CNBC

June 7, 2016

Tax Crackdown is Turning American Companies Into Prey

By Brad Anderson, former CEO of Best Buy

New U.S. Treasury regulations aimed at curbing tax inversions, where U.S. companies acquire foreign counterparts and headquarter abroad, seem to be working. But their broader goal — to keep American corporate capital at home — has failed.

Consider the recent mergers-and-acquisitions activity. Chicago-based CF Industrial Holdings and Netherlands-based OCI called off their $8 billion planned inversion, citing new U.S. tax rules. Meanwhile, German-based Bayer launched a $62 billion takeover bid for St. Louis-based Monsanto. American companies are still leaving — just as prey, not predators.

Monsanto is just the latest in a slew of recent high-profile takeovers of U.S. companies. Recently, Winton-Salem-based Krispy Kreme was taken over by Keurig owner JAB Beech, which is based in Luxembourg. And earlier this year, Chicago-based Baxalta was taken over by Ireland-based Shire for $32 billion. Also earlier this year, Chinese firm Dalian Wanda acquired Hollywood's Legendary Entertainment, and Tianjin Tianhai acquired nearby Ingram Micro for $6 billion.

Raleigh-based Salix Pharmaceuticals tried to pursue an inversion in 2014 with the Irish arm of Italian drug maker Cosmo but was blocked by Treasury regulations. But months later, Salix still went abroad after being taken over by Canada's Valeant Pharmaceuticals, which itself left the U.S. for Canada in 2010.

Last year saw the most U.S.-targeted foreign acquisitions in history, with a total value of more than $400 billion. "If you make inversions more difficult, more U.S. companies may simply be acquired," said international tax lawyer Robert Scarborough prophetically last year.

Whether American companies arrive at their new foreign addresses through inversions or being taken over, they still escape the uncompetitive and unique American corporate tax code that requires them to pay tax twice on their worldwide income, once where it was earned and then again in the U.S. (No matter where a company is headquartered, it always has to pay U.S. tax on its U.S. earnings.)

Escaping double taxation allows the consolidated company to direct more resources to its employees, customers, and shareholders, many of whom are pensioners and retirees. Krispy Kreme's planned international expansion, for instance, can accelerate with its tax savings from going abroad. Monsanto would have more money to invest in developing new, more productive seeds. The bad news? These jobs, investments, and opportunities are often created abroad instead of at home.

Ironically, it's the double taxation that American companies are trying to escape that that has made them such vulnerable takeover targets in the first place. A company's value is a multiple of its earnings. To the extent that double taxation eliminates American companies' earnings, it causes them to be artificially undervalued and takeover targets for foreign firms looking to unlock their true worth.

Treasury regulations have also not stopped American companies from increasingly stranding foreign profits overseas in order to prevent the double taxation that would occur if they were brought back home. According to one analysis, Fortune 500 companies have $2.4 trillion held offshore, where it is being reinvested to create jobs and economic activity in other countries.

A better solution to stop the outflow of American corporate capital that doesn't involve more regulations is reforming the country's uncompetitive tax code that puts its companies at an unfair disadvantage with their foreign competitors. Chiefly, this means ending double taxation by moving to a territorial tax system that only taxes profits once, where they are earned. It also means dramatically lowering the 35 percent corporate tax rate to bring it in line with international norms.

Such reform would take away the incentive for American companies to keep profits overseas and seek — now seemingly futile — inversions. It would also increase the value of American companies and level the international playing field so they wouldn't be such valuable takeover targets. It may even return the U.S. to its rightful place where companies come to, not leave from.

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