Once a U.S. Corporation, Always a U.S. Corporation…

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Date : November 25, 2013

Omri Marian, Jurisdiction to Tax Corporations, 54 **B.C. L. Rev.** 1613 (2013).

Imagine a 19 year old college student in Texas stumbles upon a new business idea to sell built-to-order computers shipped directly to customers out of his dorm room. The idea proves revolutionary, and the student is inundated with orders. To grow the business the student forms a corporation, naturally in Texas. Eventually the corporation grows into the largest personal computer maker in the world, with over 90% of its sales outside the United States.

Absent some significant tax planning, however, the company would pay US tax on all of its worldwide income, including the income from foreign sales. This is because the United States taxes the worldwide income of all U.S. taxpayers regardless of the source of the income. On the other hand, an identical "foreign" company with identical sales would only be subject to U.S. tax on the income from sales made inside the United States.. The reason for this disparity is that, under U.S. law, a corporation is treated as a U.S. taxpayer if it is legally organized under the laws of the United States, any State thereof or the District of Columbia and foreign if it is not, regardless of business model or source of income.

The solution, therefore, seems obvious – simply move the corporation's place of legal organization from the United States to some other country (preferably a country with a low or zero corporate income tax). Unfortunately under so-called "anti-inversion" rules if a U.S. company changes its place of legal incorporation and, among other things, is not being bought by a foreign competitor or moving its primary place of business, it remains treated as a U.S. taxpayer, and pays U.S. tax, notwithstanding the move.

Taken together, this could be thought of as a "once a U.S. corporation, always a U.S. corporation" rule. But this seems troubling. After all, the company formed by the 19 year old kid in his dorm room is significantly different from the multinational behemoth of today. Yet the strict, bright-line, all-or-nothing U.S. definition of corporate residence means the decision of the 19 year old kid to incorporate in Texas effectively locks all of the company's profits into the U.S. tax net (or, at a minimum, requires significant U.S. tax planning) for perpetuity. This arises not out of any affirmative policy choice of the United States but rather from the interaction of a set of ossified, confusing and convoluted corporate residency rules.

Omri Marian tackles this problem in his article *Jurisdiction to Tax Corporations*. In this article, Prof. Marian rejects the bright-line, all-or-nothing rules leading to the "once a U.S. corporation always a U.S. corporation" result. Instead, he proposes replacing the regime with an instrumentalist one. This involves a two-step approach: (1) determine the underlying normative goal of the corporate tax, and (2) implement whatever residency rule accomplishes that underlying goal.

For those unfamiliar with international tax scholarship, it may seem odd that such a proposal could come across as shocking to some. Yet it could, precisely because, for the most part, the tax literature has tended to bounce between two definitions of corporate residence: (1) place of legal incorporation and (2) primary place of business and management. Every time a problem arises with one test, someone proposes replacing it with the other, ad infinitum. Prof. Marian rejects this paradigm. To do so, he must make the controversial, yet ultimately correct, move of declaring that corporate "residency" in a globalized world is meaningless. Rather, multinational corporations can establish residency under any of these rules without changing their ultimate business model at all. So if corporate residency is utterly and completely meaningless from an economic standpoint, debating which method of corporate residency best

reflects the true economics of the firm proves a losing battle. Prof. Marian hammers home precisely this point.

There is much to like in this article. A number of scholars have recently begun to argue that many, if not most, international tax rules have no independent underlying economic rationale and thus should be purely instrumental in their goals. Prof. Marian demonstrates how this can apply to corporate residency. In doing so, this article provides one of the first modern realistic avenues out of a perennial problem in the international tax literature. Even if it is not the first do so, challenging long-held assumptions and recasting them in a way to move the debate forward provides a significant contribution to any field. Prof. Marian accomplishes precisely this.

Having said that, I remain skeptical of the proposals made in the article. At times this may be because I do not share the same underlying normative goals as Prof. Marian, at others because I do not believe the instruments he uses will actually achieve his goals. For example, as one alternative Prof. Marian considers the normative goal of the corporate income tax to be a proxy tax on access to liquid capital. Assuming this normative goal, the article proposes using the place of public listing as the jurisdiction of residence of the corporation. True, this would permit countries that provide sophisticated capital markets to tax the income of such corporations. But it would not act to tax the pool of underlying capital itself. Unless there were strong rents available in a particular jurisdiction, there is no reason to believe that companies could not raise the exact same capital from somewhere else, such as the Luxembourg Stock Exchange, solely for tax purposes.

Even worse, there is no reason to think that Luxembourg would not offer low rates of tax for companies to list on the Luxembourg Stock Exchange as a form of tax competition. Since Luxembourg (among other countries) already offers low tax rates to entice companies to relocate there, it does not seem absurd to think it could do so for a place of listing rule as well. In fact, the world witnessed such a “race to the bottom” in the form of taxing interest on publicly-traded debt instruments in the 1980s, although at that time it was the United States leading the way by exempting foreign investors from U.S. tax on so-called “portfolio interest” specifically to attract foreign capital into the United States.

A purist approach, even if ultimately wrong, may well avoid such implementation questions, but an instrumentalist one could well fall prey to them. Perhaps this is less an indictment of the article and more a complaint of international tax more broadly.

Ultimately, however, this is a theoretical article and on that front it succeeds. I am in agreement with the conclusion, which states “Obviously, the model developed is not exhaustive, in the sense that it cannot possibly consider all possible purposes for which different countries choose to tax corporations. But its strength is in its flexibility to consider new purposes and interactions of various purposes in the specific contexts of each jurisdiction. As such, the model can provide guidance even with respect to purposes of corporate taxation not explicitly considered herein.”

This article establishes itself as part of a promising trend in international tax scholarship, one I hope more scholars pursue going forward.

Cite as: Adam Rosenzweig, *Once a U.S. Corporation, Always a U.S. Corporation…*, JOTWELL (November 25, 2013) (reviewing Omri Marian, *Jurisdiction to Tax Corporations*, 54 **B.C. L. Rev.** 1613 (2013)), http://tax.jotwell.com/once-a-u-s-corporation-always-a-u-s-corporation/.