legal rules. He proposes the following strategies to curb shareholder-creditor agency costs: (1) covenants in debt contracts and pricing; (2) executive compensation to mirror the debt-equity capital structure of the company through deferred compensation and pension benefits; and (3) the presence of an institutional lender that would alter corporate governance. He concludes that while “shareholder value maximization” can be used to promote corporate governance, it can be overused.12

The articles by Rock and Adler and Kahan demonstrate the complicated legal trade-offs that must be struck to channel stakeholders’ reward-seeking and risk-averse behavior responsibly and cost effectively.


Professor Stout applauds the authors for considering the effect on corporate creditors of company managers being more aligned with shareholders. But she suggests they expand their analyses to include shareholder primacy’s negative consequences. Stout addresses two of those negative consequences: shareholders fixating on the company’s short-term instead of long-term future, and shareholders focusing on specific investments of creditors but also of other stakeholders such as employees, customers, and suppliers. However, she concludes that the cure for shareholder primacy has proven debilitating for public companies, prompting fewer private companies to go public, and for those that do, resulting in shorter life expectancies for their duration. If the benefits of the shareholder-centric model outweigh its costs, Stout responds to Rock’s and Adler’s and Kahan’s articles by retaining the shareholder primacy but smoothing its edges through changes in creditors’ rights and shareholders’ obligation. Stout recommends corporate law experts stop lobbying for shareholder primacy, and instead embrace the new shareholder-centric reality despite its problems for creditors as noted by Rock, Adler and Kahan.

A Brief Review of Corporate Tax Articles of 2013

By Jordan M. Barry, Karen C. Burke, and Monica Gianni

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In this article, the authors provide a survey of corporate tax articles published in 2013.

This article provides a short survey of corporate tax articles published in 2013, with the goal of bringing readers’ attention to articles that may be of interest but might have escaped their notice. Therefore its scope is limited in two major ways.

First, this article focuses on “pure” corporate tax articles. So, for example, it does not include articles primarily devoted to international tax, even though many of those articles have significant implications for corporate tax. That line was often challenging to draw, and some of the excluded articles are referenced in the footnotes.

Second, there are no articles that were published in Tax Analysts publications, under the premise that regular Tax Notes readers generally would have noticed them already. The article focuses mostly on law reviews and specialized tax journals, but not exclusively. Apologies to anyone whose excellent article may have been missed; please know that it was not intentional.

To help readers with particular areas of interest, the articles are organized into rough subject matter categories. Those categories are Corporate Tax Burden; Acquisitions and Reorganizations; General Utilities Repeal and Sections 336 and 338; International Aspects of the Corporate Income Tax; Taxation of Big and Small Business; Corporate Governance and Executive Compensation; and Relationship Between the Corporate Income Tax and Consumption Taxes.

A. Corporate Tax Burden

As a legal matter, the corporate income tax is imposed on corporations. However, in an economic sense, corporations are collections of people — shareholders, managers, employees, and other stakeholders — organized in a particular way. Therefore, the corporate income tax is actually a tax

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on those different groups. How the economic burden of the corporate income tax falls on each of them remains a matter of great importance — and ongoing debate. Those debates have taken on an additional dimension with the increasing globalization of corporations and as other developed nations have cut their statutory corporate tax rates.

1. Kimberly A. Clausing, “The Future of the Corporate Tax,” 66 Tax L. Rev. 419 (2013). Clausing argues that the U.S. corporate tax, although badly in need of reform, has a vital role to play in the U.S. economy. She begins by discussing the role of capital taxation in general and then turns to the specific challenges of the U.S. corporate tax. Although some argue that taxing capital is inefficient, recent theoretical literature suggests an important role for a positive tax on capital income at levels consistent with current practices. Indeed, pragmatic reasons militate against abolishing the taxation of capital income: A zero or low tax on capital income poses a risk of eviscerating the labor income tax base through income shifting, particularly among high-income individuals who have discretion over the form in which they receive compensation. Because capital income skews to the upper end of the income spectrum, under plausible assumptions about corporate tax incidence, the corporate tax continues to play a vital role in enhancing progressivity while raising revenue and protecting the individual income tax base. Clausing concludes by considering several reforms that would reduce existing distortions in the U.S. corporate tax, alleviate biases in favor of particular organizational forms, and improve international business taxation.

2. Kimberly A. Clausing, “Who Pays the Corporate Tax in a Global Economy?” 66 Nat’l Tax J. 151 (2013). Clausing considers the discrepancy between theoretical predictions and empirical evidence concerning the incidence of the corporate tax burden in an increasingly integrated global economy. Although theory suggests that labor should bear a substantial portion of the corporate tax burden, the empirical evidence does not show a robust linkage between corporate taxes and wages. Indeed, globalization may undermine some of the open-economy assumptions concerning the shifting of corporate taxes onto labor. The silver lining of international tax avoidance is that the ability to shift profits to low-tax jurisdictions without altering the underlying real investments partially insulates workers in high-tax countries, such as the United States, from adverse wage effects. The article has policy implications concerning the role of the corporate tax in enhancing progressivity as well as the need to design international tax reform carefully to avoid generating real responses to differences in corporate tax rates.

3. Julie A. Cronin et al., “Distributing the Corporate Income Tax: Revised U.S. Treasury Methodology,” 66 Nat’l Tax J. 239 (2013). This article discusses the Treasury Department’s revised method for estimating the distribution of the corporate income tax burden. Before 2008, Treasury assumed that the corporate tax was borne entirely by capital. Under the revised method, corporate tax revenue has three components, consisting of (1) the share of corporate tax attributable to supernormal or “excess” returns, borne by capital; (2) the share of corporate tax attributable to cash flow returns, which imposes no burden in the long run; and (3) the remainder of the corporate tax, borne equally by labor and positive normal capital income. Overall, the revised method assigns 82 percent of the burden of the corporate tax to supernormal or normal capital and 18 percent to labor. Because some of the changes are offsetting and corporate taxes are only a small portion of the total federal tax base, the revised method does not significantly affect the current law baseline distribution relative to Treasury’s pre-2008 approach. Importantly, the new method makes it possible to differentiate among reform proposals that affect supernormal and normal returns differently, such as cutting rates or altering cost recovery allowances.

4. Jennifer Gravelle, “Corporate Tax Incidence: A Review of General Equilibrium Estimates and Analysis,” 66 Nat’l Tax J. 185 (2013). Gravelle reviews the literature on corporate tax incidence under open-economy general equilibrium models. She considers four recent studies with widely divergent estimates of the relative shares of the corporate tax burden borne by labor and capital and identifies key assumptions that may account for those differences. Features of real-world corporate tax systems — such as the many U.S. tax provisions that mitigate a high statutory tax rate and subsidize debt — may affect incidence but are not reflected in stylized open-economy models. Those models also assume that only a single country changes its corporate tax rate at any time, while in reality countries may adjust their corporate tax rates in tandem. Even in an open-economy scenario, under plausible assumptions, capital may continue to bear virtually the entire corporate tax burden. That conclusion is supported by an alternative approach to allocating the corporate tax burden based on the “new view” of property tax, which considers the impact of local taxes from a national perspective.

relative industry concentration ratios as a proxy for competitiveness and find that an increasing amount of the corporate tax is shifted to labor in the form of reduced wages as industry concentration increases. Consistent with several recent studies focusing on variations in corporate tax rates across countries, the article concludes that a significant portion of the corporate tax burden is shifted from capital to labor under conditions of imperfect competition. In the aggregate, a one dollar increase in corporate tax revenues translates to a roughly 60-cent reduction in wages. An important caveat is that the potential dynamic effects of corporate tax shifting are not modeled. Therefore, the study is indicative of the short-run incidence; the adjustment process may operate differently over longer periods.

6. Staff of the Joint Committee on Taxation, “Modeling the Distribution of Taxes on Business Income,” JCX-14-13 (2013). Until recently, because of data limitations and methodological difficulties, the JCT did not estimate the distributional effects of changes affecting the taxation of corporate income or passthrough business income. Reflecting the demand for more information on the distributional consequences of tax changes and reduced uncertainty concerning the incidence of business taxes, the JCT will now distribute changes in business taxes among income groups using an “expanded income” concept. Under its revised approach, the JCT assumes that 25 percent of the burden of the corporate tax is borne by labor in the long run. Because changes to corporate tax laws must be scored over a 10-year budget window, the JCT assumes pragmatically that capital income bears 100 percent of the changed tax burden in year 1 (the short term) and 75 percent in year 10 (the long run). Because passthrough businesses are less internationally mobile, however, the JCT allocates only 5 percent of the long-run burden of passthrough business taxes to labor. Two examples of hypothetical reform proposals — one increasing taxes on corporate income and the other increasing taxes on passthrough income — suggest that redistributing the tax burden from corporations to passthroughs would increase the overall progressivity of the tax system. That result reflects (1) labor’s smaller share of the tax burden on passthrough income and (2) the skewing of passthrough owners at the upper end of the income distribution.

B. Acquisitions and Reorganizations

The taxation of corporate acquisitions and reorganizations remained a topic of great interest in 2013. The following articles helped illuminate the complicated rules that pervade those areas and also suggested ways in which the rules might be improved to promote greater efficiency and certainty.

1. Herbert Beller and William R. Pauls, “The Aftermath of a Section 355 Transaction (Part I),” 40 Corp. Tax. 3 (2013). Beller and Pauls’s article is the first of two that examine situations in which events occurring after a completed spinoff can jeopardize that spinoff’s tax-free treatment. The article begins with a review of the statutory and nonstatutory requirements that a spinoff must satisfy to qualify for nonrecognition treatment. The authors then move to a discussion of post-spin actions that can adversely affect a tax-free section 355 spinoff. Those post-spin actions include transactions that affect the business purpose requirement, transactions involving dispositions of assets by the distributing or the distributed corporation, reorganizations, and asset drop-downs.

2. Deborah L. Paul, “Spin-offs, Leverage and Value Extraction — A Spin by Any Other Name . . .” 91 Taxes 99 (2013). Paul’s article addresses the tax consequences that can result from differently structured spinoffs. The IRS has generally allowed taxpayers to obtain favorable tax results if the form the taxpayer has chosen is more tax-advantageous than another form that ultimately produces the same (nontax) result. Paul considers whether it is possible to develop a spinoff tax regime that does away with formal distinctions. Even though deals continue to get done under the current system, many proposed deals must first go through the IRS ruling process, which is costly, uncertain, and produces idiosyncratic results. Accordingly, the IRS should publish rulings confirming standards set forth in private rulings and providing consistent rules for economically equivalent transactions. The author notes at the end of the article that the IRS recently announced that it will limit its ruling policy on spinoffs. That policy will apply until specific issues are resolved through the issuance of IRS guidance. Given that new no-ruling
policy in some spinoff areas, it is imperative that the IRS issue published guidance expeditiously.

3. Jeffrey T. Sheffield, “Spin-offs, Corporate Capital Structure and Disguised Sales,” 91 Taxes 119 (2013). A corporation can spin off the stock of a subsidiary to the corporation’s shareholders tax free under section 355 if it meets specific requirements. Sheffield discusses the circumstances under which pre-spinoff internal restructurings and external dispositions conducted in connection with a spinoff should result in taxation. Internal restructurings involve transferring necessary operations, including assets and liabilities, to the subsidiary before the spinoff. External dispositions are methods to extract value from the subsidiary, such as having the controlling corporation receive cash from outside the corporate group in exchange for some of the controlling corporation’s pre-spinoff interest in the subsidiary. Sheffield proposes that internal restructurings should not trigger gain, even when the subsidiary assumes liabilities that exceed the bases turings should not trigger gain, even when the subsidiary assumes liabilities that exceed the bases.

4 External subsidiaries that receive a deemed loss to the extent of deemed gains. The disallowance rules for deemed asset sales and allow deemed losses to the extent of deemed gains. The final regulations should facilitate deemed asset sales of subsidiaries and S corporations.

2. Don Leatherman, “The Scope of the General Utilities Repeal,” 91 Taxes 235 (2013). The General Utilities doctrine was “repealed” through judicial and legislative changes from 1969 through 1987, and more recent complementary changes address a variety of concerns with the scope of the General Utilities repeal. Leatherman recommends that the scope of the General Utilities repeal be further developed and refined, with the IRS and Treasury adopting regulations under section 337(d) to provide an overarching general rule. More specific actions are needed to implement the General Utilities repeal, including simplifying the uniform loss rules of reg. section 1.1502-36 and revising section 362(e)(2) to prevent loss duplication in connection with section 368(a)(1)(B) reorganizations. Regarding prop. reg. section 1.337(d)-3, the article recommends eliminating the rule addressing a partnership’s disposition of a partner’s stock, while retaining and modifying the deemed-redemption rule for a partnership’s ownership of a partner’s stock.

3. W. Eugene Seago and Edward J. Schnee, “Section 338 Transactions: Why ADSP and AGUB Can Differ,” 119 J. Tax. 158 (2013). In some circumstances, a corporate purchaser of stock can elect to have the purchase treated as an asset purchase instead of a stock purchase under section 338. In a deemed asset sale, one would generally assume that the aggregate deemed selling price (ADSP) of the target’s assets would be the same as the adjusted grossed-up basis (AGUB) of the assets to the purchaser. Seago and Schnee discuss why differences in the ADSP and AGUB arise, and the significance of those differences, using the analytical framework of a section 338(h)(10) election for sale of a subsidiary’s stock. Disparities between ADSP and AGUB can occur when (1) the purchaser uses contingent consideration, producing a difference in timing; (2) the purchaser has stock that was not recently purchased, resulting in a lower basis for the purchaser in the target’s assets; or (3) the target has contingent or other liabilities that are taken into account differently for ADSP and AGUB under tax accounting rules, which can lead to permanent differences in some cases.

D. International Corporate Income Tax Issues

Proposals to reform the U.S. international tax system, particularly regarding U.S. corporations,

\[ \text{Section 338(h)(10) election for sale of a subsidiary’s stock.} \]

5\[ \text{The conclusions in the article would apply equally to a deemed asset sale in the case of a section 338(g) election, a section 338(h)(10) election for an S corporation, and a section 336(e) election.} \]
featured prominently in tax policy debates in 2013. Much of that discussion focused on how the increasingly global scale of corporate operations should affect U.S. corporate tax policy and policymaking.

1. Reuven S. Avi-Yonah, “Corporate and International Tax Reform: Proposals for the Second Obama Administration (and Beyond),” 40 Pepp. L. Rev. 1365 (2013). Avi-Yonah offers corporate and international tax reform proposals for consideration over various time horizons. For the long term, the author proposes enacting a VAT and simplifying the corporate tax by allowing the expensing of all capital expenditures. For the medium term, he advocates using formulary apportionment to allocate U.S. multinationals’ income across jurisdictions. Avi-Yonah also comments favorably on President Obama’s proposed minimum tax on the foreign-source income of U.S. multinationals and suggests several near-term measures, including (1) basing U.S. corporate residence on the location of management and control instead of the place of incorporation; (2) allowing full cross-crediting of foreign income taxes, disregarding the activity that generated the credit; (3) abolishing the branch profits tax, as well as most regular withholding tax on dividends, interest, and royalties; (4) tightening and extending the earnings stripping rules of section 7874; and (5) repealing the 1980 Foreign Investment in Real Property Tax Act.

2. Steven A. Bank, “The Globalization of Corporate Tax Reform,” 40 Pepp. L. Rev. 1307 (2013). Bank describes several ways in which international organizations and international tax competition has affected corporate tax policy in the last decade. In particular, he argues that those institutions and forces have caused corporate tax systems and rates to converge and that those forces will become even more powerful over time. Those dynamics, combined with the increasingly global scale on which corporations do business, suggest that any viable corporate tax reform must be multinational rather than purely domestic in nature — and that policymakers should adjust their thinking accordingly.  

3. Malcolm Gammie, “Taxing Corporate Profits in a Global Economy,” 42 British Tax Rev. (2013). Even though most economists view the design of the corporate tax system as deeply flawed, governments and tax administrators remain committed, for pragmatic reasons, to taxing domestic production in a competitive international environment. Corporate tax systems are generally designed to mesh with a country’s personal income tax system and function largely as a withholding tax on income that otherwise will not be taxed to the shareholder until she sells her stock or the corporation distributes its profits. Because corporations represent a “big box of savings” for their owners, corporate profits need to be taxed as they accrue in the corporation’s hands if a tax on personal income (rather than consumption) is deemed desirable. As long as countries seek to tax individuals on their income and levy a source-based tax on corporate profits, they have an incentive to maintain some version of a corporate profits tax.  

4. Susan C. Morse, “A Corporate Offshore Profits Transition Tax,” 91 N.C. L. Rev. 549 (2013). Many commentators have argued that the United States should move from its worldwide tax system, which taxes U.S. citizens, residents, and corporations on their worldwide income, to a territorial tax system, which would only impose tax on income earned within the United States. The non-U.S. subsidiaries of U.S. corporations hold between $1 trillion and $2 trillion of offshore earnings that have not been subjected to U.S. tax. If the United States transitioned from a worldwide tax system to a territorial one, it is unclear how those earnings should be treated. Morse proposes a transition tax at a rate of 5 to 10 percent, with no offset for foreign tax credits, and considers the efficiency, administrability, and equity of that transition tax. She also suggests that focusing on financial accounting measures of unremitting earnings may help resolve administrative problems with the transition tax, as well as curb tax avoidance.

E. Taxation of Big and Small Business

Several articles in 2013 considered the ways in which our corporate income tax laws treat large and small corporations differently. They also examined whether those disparities make sense and how the law affects new companies’ decisions on their organizational form.

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8While the continued fall in corporate tax rates has fueled concerns about a race to the bottom, evidence concerning the nature and extent of corporate tax competition remains elusive. See Michael P. Devereux and Simon Loretz, “What Do We Know About Corporate Tax Competition?” 66 Nat’l Tax J. 745 (2013).
1. Steven A. Bank, “Taxing Bigness,” 66 Tax L. Rev. 379 (2013). Bank reviews the origins of the graduated corporate income tax rate structure that was first enacted in 1935. The change from a flat tax to one with graduated rates was promoted based on a need for a tax on “bigness.” Perhaps more important than the structure itself, the move to graduated income tax rates set the stage for a corporate tax policy that treats large and small corporations differently. Over time, the government’s justification for graduated rates changed from a tax on bigness to a subsidy for small businesses. The author questions whether it is still essential today for small businesses to have that sort of subsidy, especially since small businesses can use alternative forms of entities to reduce taxes, such as S corporations and limited liability companies. Changing the rate structure to a flat tax could increase efficiencies by reducing the tax incentive for small corporations to use the corporate form and could also raise a nontrivial amount of revenue.

2. Susan C. Morse, “Startup Ltd.: Tax Planning and Initial Incorporation Location,” 14 Fla. Tax Rev. 319 (2013). Morse analyzes how tax planning considerations affect the place-of-incorporation decisions of recently founded U.S.-based private business enterprises with global ambitions. In many instances, non-U.S.-parented multinational corporations may have tax advantages over U.S.-parented multinationals. Yet, in most industries, even globally oriented U.S.-based start-ups typically incorporate in the United States. The article hypothesizes and considers several possible explanations. First, the proposed tax advantages to having a non-U.S. parent corporation may be smaller than they appear. Second, U.S. incorporation may have fewer upfront costs, which could be important for resource-constrained start-up companies. Third, investors may prefer to invest in U.S. corporations for reasons of substance or familiarity. Finally, founders and investors may worry that U.S. tax laws may change in ways that are adverse to U.S.-based companies with non-U.S. parent corporations. The article also discusses the industries in which non-U.S. parent corporations are common and considers what characteristics distinguish those industries.

F. Corporate Governance and Executive Pay

Several articles in 2013 focused on using corporate income taxes as a tool for achieving nontax policy goals or to correct behavioral distortions inadvertently created by our existing corporate tax system.

1. Richard M. Hynes, “Taxing Control,” 38 J. Corp. L. 567 (2013). Takeover defenses are generally believed to reduce the value of public companies by making it more difficult to remove or discipline ineffective or unfaithful managers. When a company goes public, the existing owners have strong incentives to structure the firm in a way that maximizes its value. Why, then, do so many firms go public with takeover defenses? Hynes argues that the tax system encourages public corporations to overuse takeover defenses at the time of their initial public offerings. All else being equal, a corporation that goes public with a lower level of takeover defenses will generally receive a higher price for its stock. However, the pecuniary gains from the sale of stock are subject to tax, while the non-pecuniary benefits that come from having control over the corporation are not. Thus, the tax system distorts the choice of takeover defense levels and encourages founders and managers to keep more control than they would otherwise. The article considers several possible policy responses, including imposing tax based on the IPO value that the firm would have had without anti-takeover devices, taxing anti-takeover devices, and banning them outright.

2. David I. Walker, “A Tax Response to the Executive Pay Problem,” 93 B.U. L. Rev. 325 (2013). Some commentators have argued that there is a market failure regarding high-ranking executives at public firms and that it has fueled the well-documented growth in executive compensation. Walker assumes the correctness of that argument as a starting point. He then proposes a two-pronged tax response: a surtax on executive compensation above a specific threshold, coupled with corporate-level tax relief intended to help investors. Walker argues that those measures would reduce the unfairness stemming from excessive executive compensation while improving the lot of investors, who presumably bear the burden of the purported market failure.

G. Corporate Income and Consumption Taxes

These articles explored the relationship between the corporate income tax and consumption taxes, considering both federal and state-level perspectives.

9See also Karen C. Burke, “Passthrough Entities: The Missing Element in Business Tax Reform,” 40 Marq. L. Rev. 1329 (2013) (arguing that policymakers must consider the interactions between corporations and the passthrough sector when evaluating corporate tax reforms).
1. Noël B. Cunningham and Mitchell L. Engler, "Prescription for Corporate Income Tax Reform: A Corporate Consumption Tax," 66 Tax L. Rev. 445 (2013). Cunningham and Mitchell derive policy prescriptions based on two premises. First, there is a "widely shared bipartisan view that the corporate income tax is a 'bad' tax that is desperately in need of reform or repeal." Second, there is also "a growing consensus" that the United States should adopt a federal consumption tax to help address our long-term deficit problem. The article argues that both of those issues can be addressed simultaneously by turning the corporate income tax into a consumption tax. It discusses several ways in which that transition might be accomplished. In particular, it analyzes and compares two recent reform proposals — the "Growth and Investment Tax Plan" and the "Modern Corporate Tax" (both of which the authors find promising).

2. Darien Shanske, "A New Theory of the State Corporate Income Tax: The State Corporate Income Tax as Retail Sales Complement," 66 Tax L. Rev. 305 (2013). Shanske notes that, in the abstract, many commentators oppose state-level corporate income taxes for a variety of reasons. However, he contends that the case for state-level corporate income taxes is strongest when considered in the context of existing state and local tax systems, which he describes as "an embarrassment wrapped in inertia inside thoughtlessness." State-level corporate income taxes have proved to be more flexible tools than property taxes, VATs, and individual sales or income taxes, all of which are significantly constrained by legal and political barriers. In effect, corporate income taxes expand the inefficiently narrow bases of state sales taxes, offering a second-best solution in a world where broadening the sales tax base directly is not feasible. Nevertheless, broadening state sales taxes in that way is both underinclusive — goods purchased from noncorporate entities are not taxed — and overinclusive — goods purchased from corporate entities are subject to sales tax and the corporate entity pays corporate income tax.

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11See President’s Advisory Panel on Federal Tax Reform, “Simple, Fair, and Pro-Growth: Proposals to Fix America’s Tax System” (Nov. 1, 2005).