

PENNSYLVANIA STATE LAW

CENTER FOR THE STUDY OF MERGERS AND ACQUISITIONS

SLIDES ILLUSTRATING (1) A PROTOTYPICAL INVERSION TRANSACTION, AND (2) THE IMPACT OF TREASURY'S 2016 INVERSION AND SECTION 385 REGULATIONS

Accompanying Thompson, *A Basic Guide to the Treasury's April 2016 Regulations in Inversions and Inter-
Company Debt*

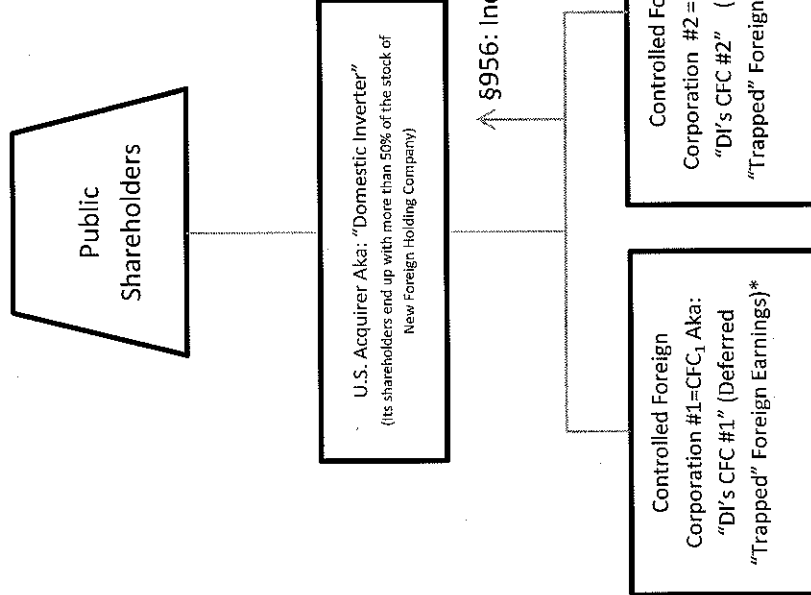
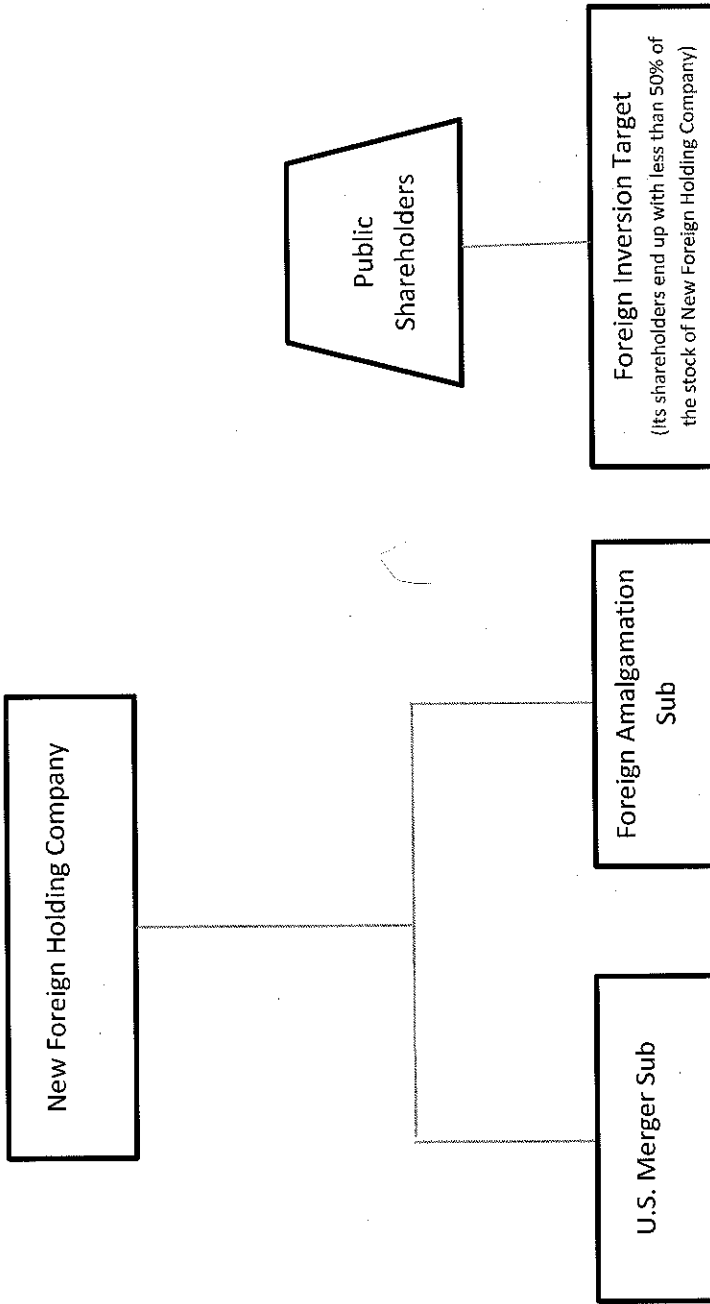
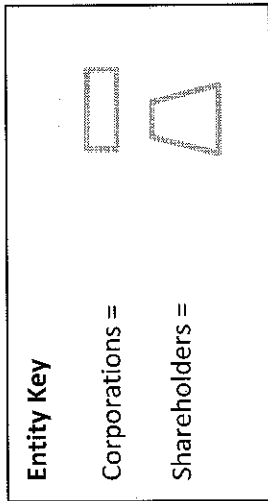
Professor Samuel C. Thompson, Jr.

Draft April 26, 2016

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PROTOTYPICAL INVERSION TRANSACTION

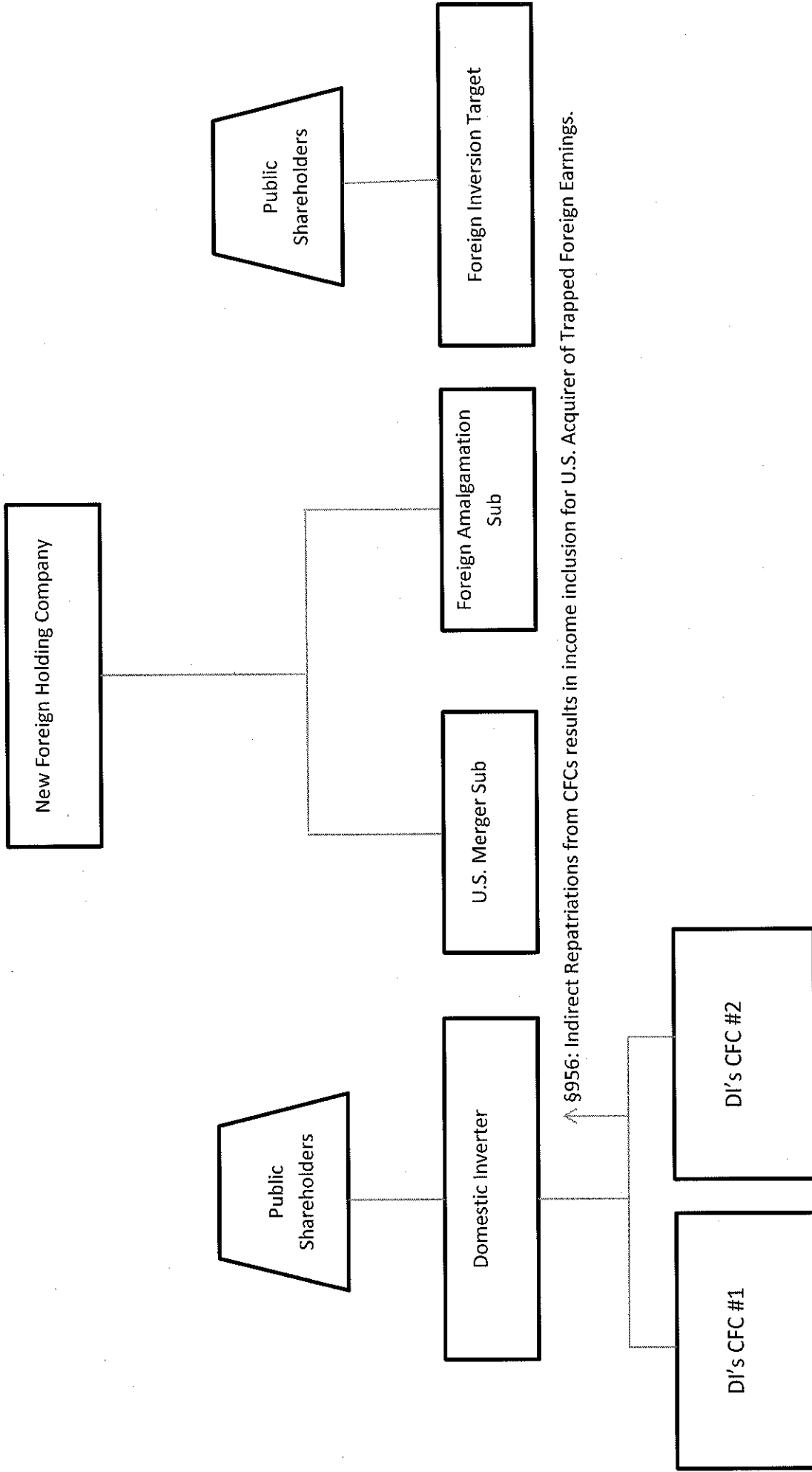
SLIDE #1 PRE-INVERSION STRUCTURE



*Total Deferred "Trapped" Foreign Earnings of all CFCs = \$2 trillion (\$1 trillion in cash)

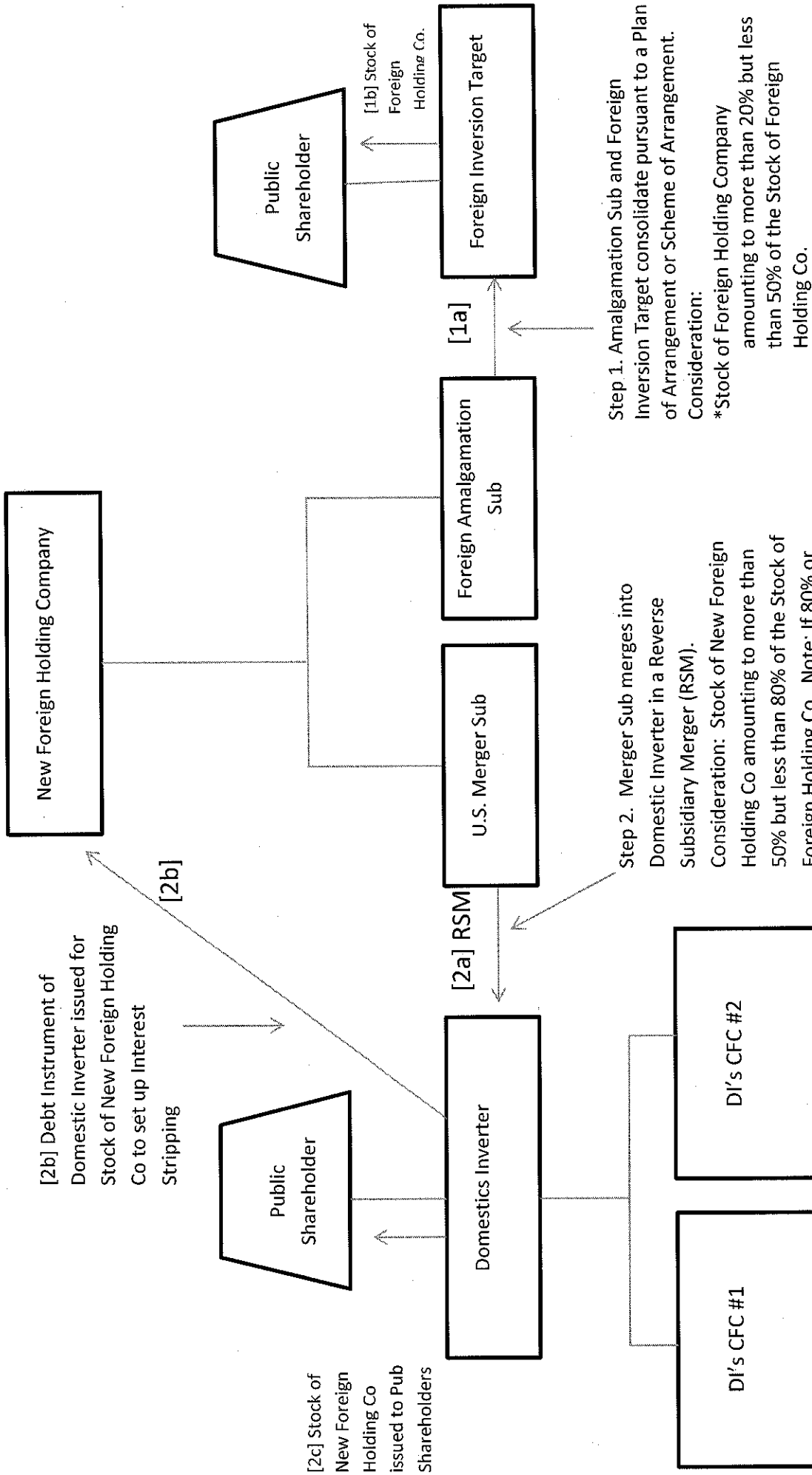
PROTOTYPICAL INVERSION TRANSACTION

SLIDE #2 SUMMARY OF THE PRE-INVERSION STRUCTURE



PROTOTYPICAL INVERSION TRANSACTION

SLIDE #3 THE INVERSION TRANSACTION



Step 1. Amalgamation Sub and Foreign Inversion Target consolidate pursuant to a Plan of Arrangement or Scheme of Arrangement. Consideration:

- *Stock of Foreign Holding Company amounting to more than 20% but less than 50% of the Stock of Foreign Holding Co.

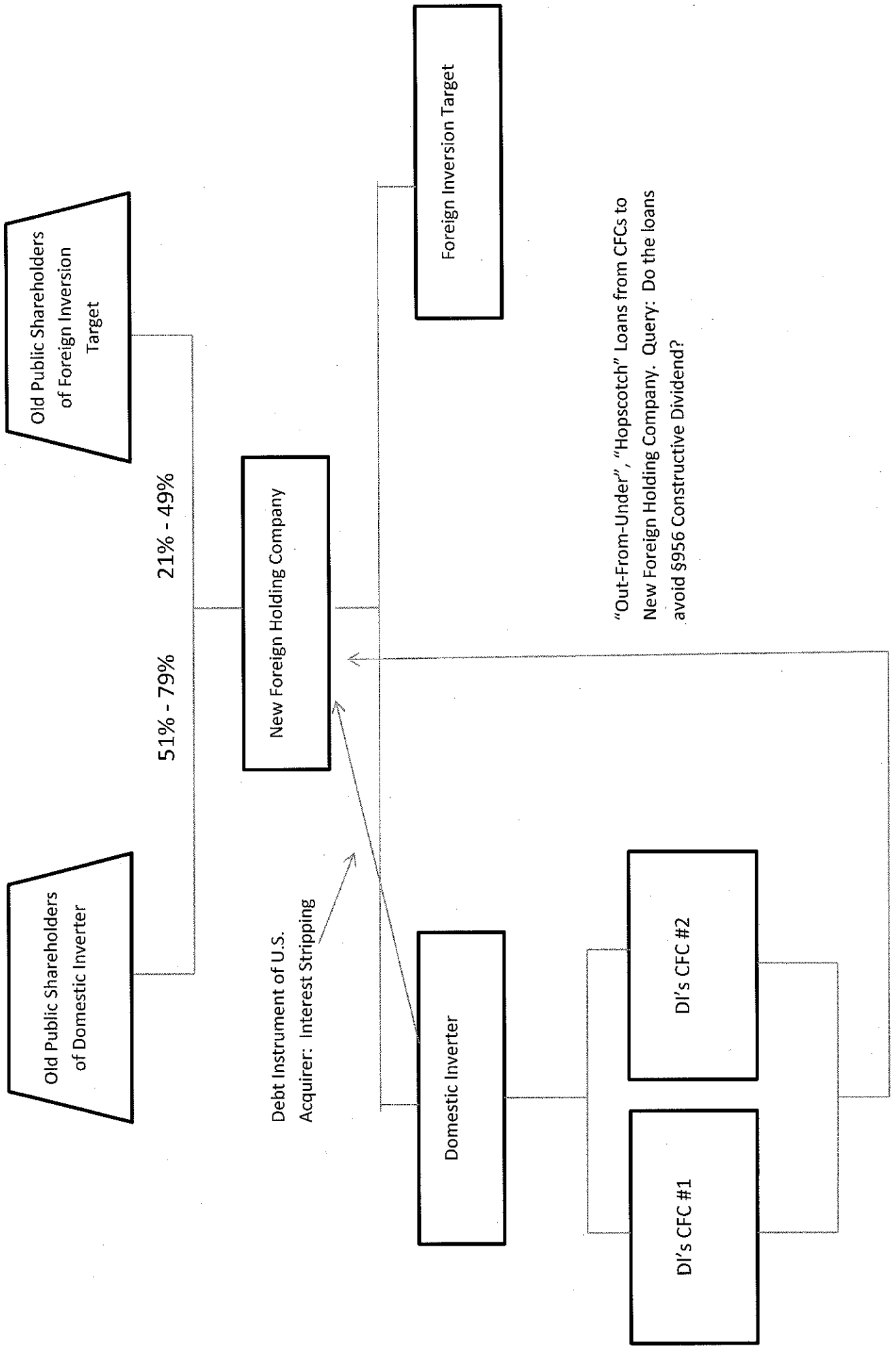
- *Possibly some cash to satisfy the more than 20% but less than 50% requirement.

Step 2. Merger Sub merges into Domestic Inverter in a Reverse Subsidiary Merger (RSM).

Consideration: Stock of New Foreign Holding Co amounting to more than 50% but less than 80% of the Stock of Foreign Holding Co. Note: If 80% or more, then under § 7874, New Foreign Holding Company is treated as a U.S. corporation.

PROTOTYPICAL INVERSION TRANSACTION

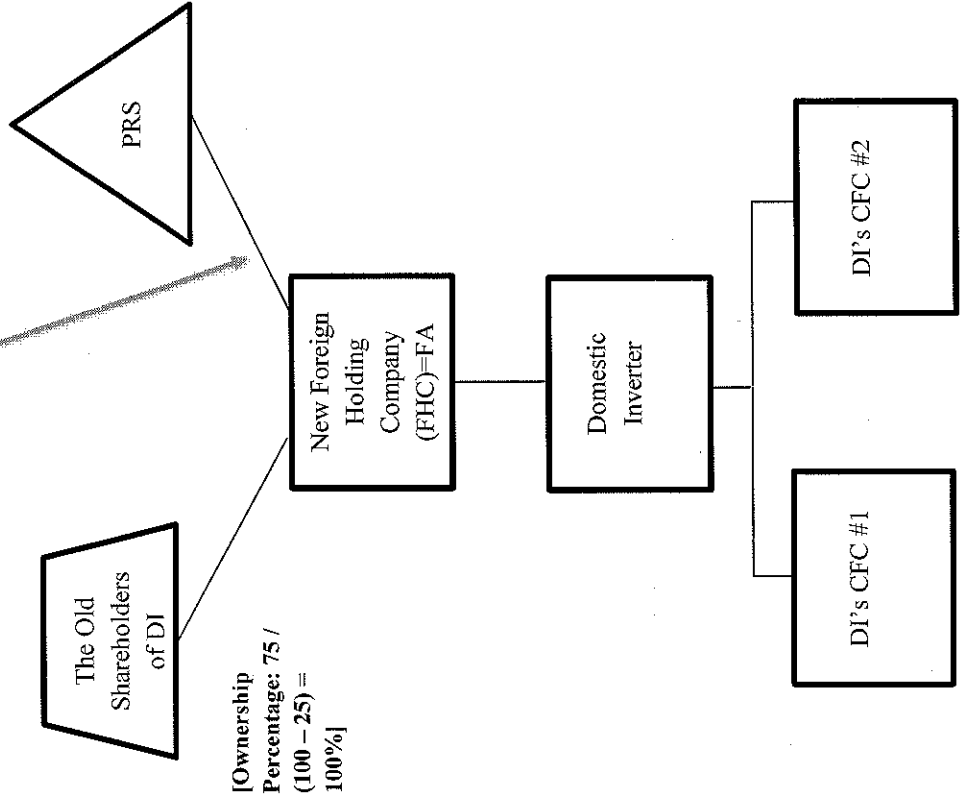
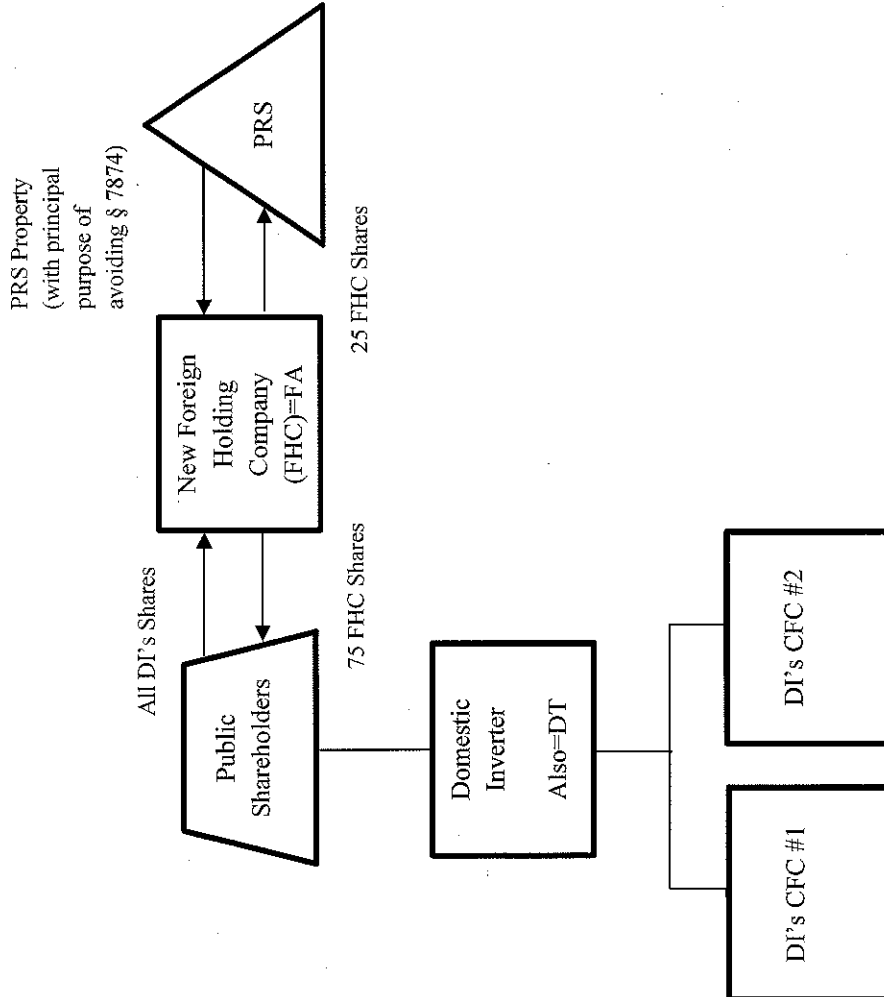
SLIDE #4 POST INVERSION STRUCTURE



2016 TREASURY INVERSION REGS: IMPACT ON INVERSION STRUCTURE

SLIDE # 5 ANTI-STUFFING RULES REG. §1.7874-4T, EXAMPLE 3

Reg. §1.7874-4T disregards stock of FHC issued for PRS business assets in a transaction related to the DI acquisition with the "principal purpose of avoiding the purposes of section 7874." PRS's shares in FHC are disregarded. FHC is domestic.

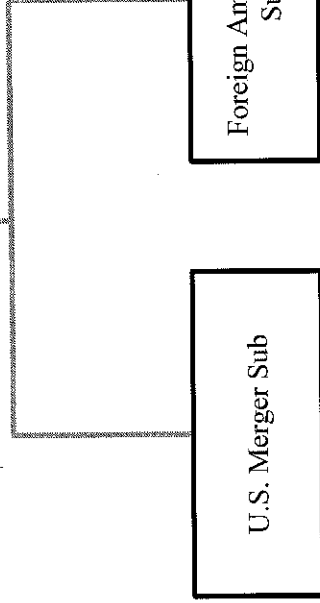
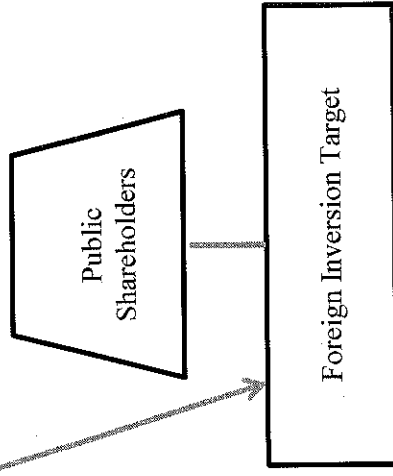


2016 TREASURY INVERSION REGS: IMPACT ON INVERSION STRUCTURE

SLIDE #6 THE ANTI-CASH BOX RULE, REG § 1.7874-7I

§ 1.7874-7I will disregard certain stock of Foreign Inversion Target (FIT) attributable to passive assets, effectively ensuring that FIT's net active assets must have a value of at least 21% of the stock of FHC. A similar rule applies for the § 367 substantiality test.

New Foreign Holding Company (FHC)



Public Shareholders

Domestic Inverter

DI's CFC #2

DI's CFC #1



U.S. Merger Sub

Foreign Amalgamation Sub

Foreign Inversion Target

2016 TREASURY INVERSION REGS: IMPACT ON INVERSION STRUCTURE
SLIDE # 7 THIRD-COUNTRY TRANSACTION, REG § 1.7874-9T

§ 1.7874-9T disregards stock of the New Foreign Holding Company that is issued to the shareholders of the Foreign Inversion Target for the purpose of determining whether the 80% threshold is met.

[Ownership Percentage Calculation:
 $65 / (100 - 35) = 100\%$]

The Old Shareholders of Domestic Inverter

[65 FHC shares]

The Old Shareholders of Foreign Inversion Target

[35 FHC shares to be disregarded]

[In the transaction, FHC acquired all the stock of DI with 65 shares of the newly issued FHC stock.]

Domestic Inverter (DI)

[In the transaction, FHC acquired all the stock of FIT with the remaining 35 shares of the newly issued FHC stock.]

New Foreign Holding Company (FHC) = a Domestic Corp (A tax resident of Country Y)

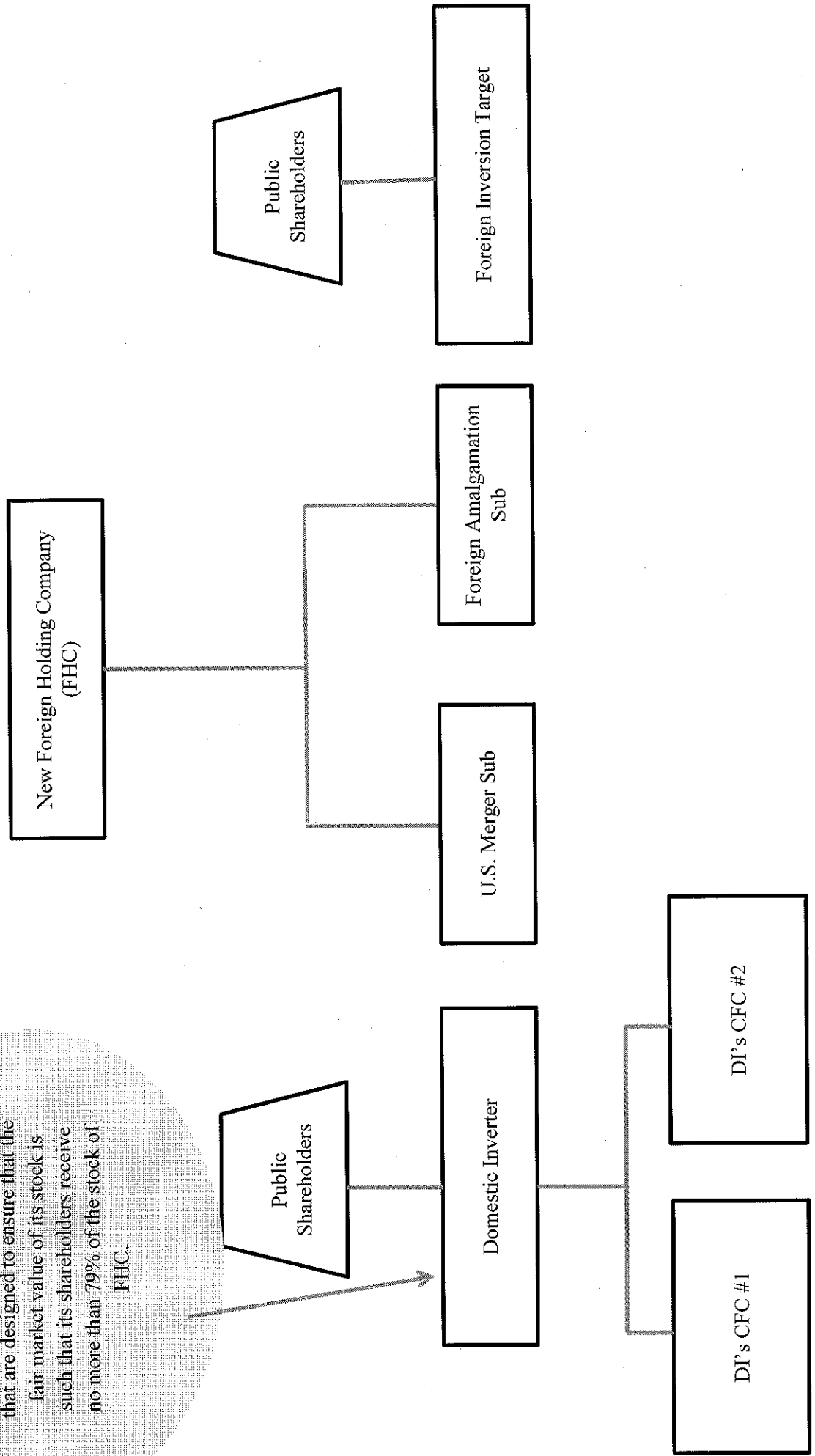
Foreign Inversion Target (FIT) (A tax resident of Country X)*

* Note: FIT is a resident of a Country X, and FHC is a resident of Country Y, a third country. See the Example in § 1.7874-9T(f).

2016 TREASURY INVERSION REGULATIONS: IMPACT ON INVERSION STRUCTURE

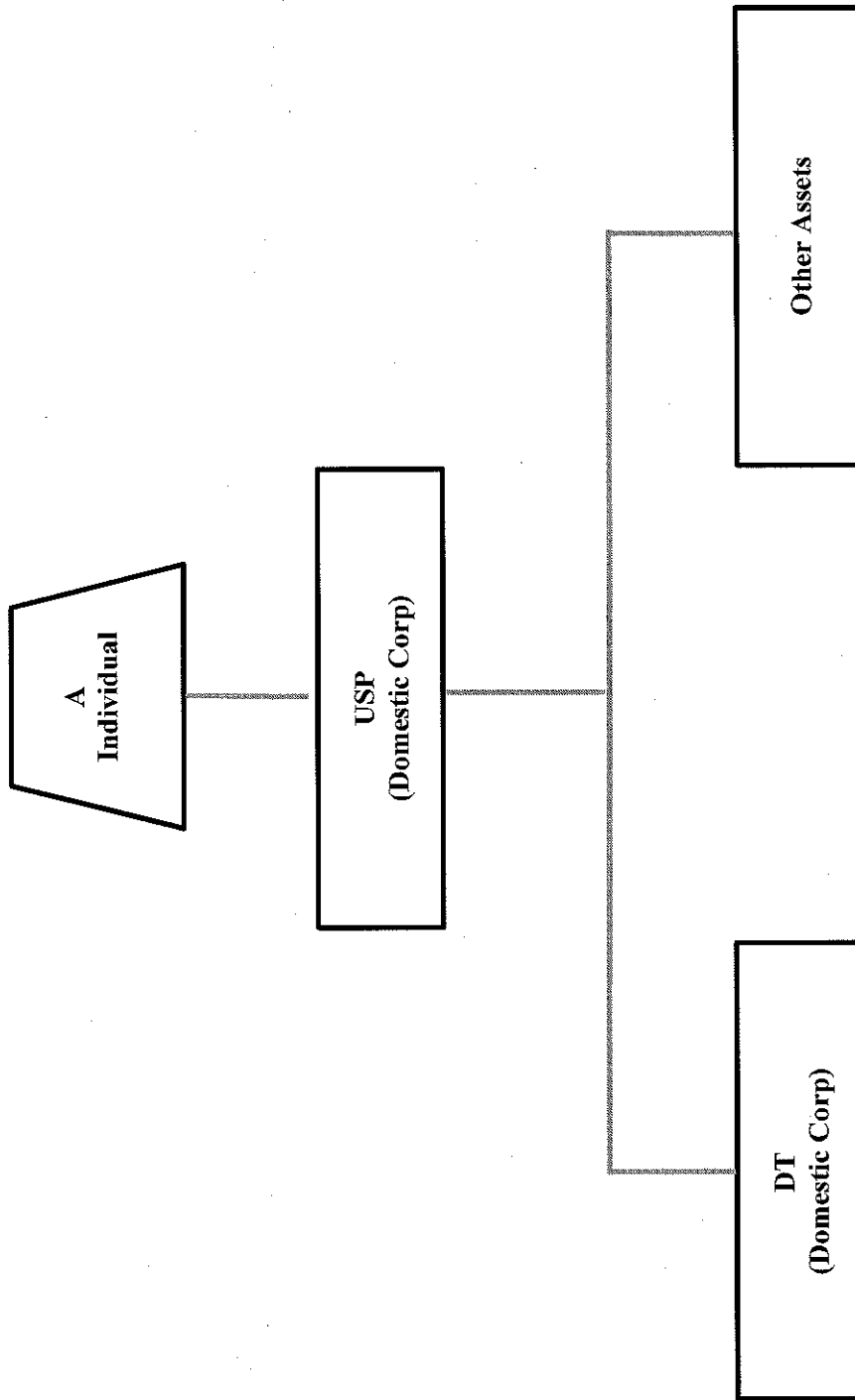
SLIDE #8 SLIMMING DOWN NOCDS, REG § 1.7874-10T

Section 1.7874-10T will disregard certain "slimming down" distributions by Domestic Inverter that are designed to ensure that the fair market value of its stock is such that its shareholders receive no more than 79% of the stock of FHC.



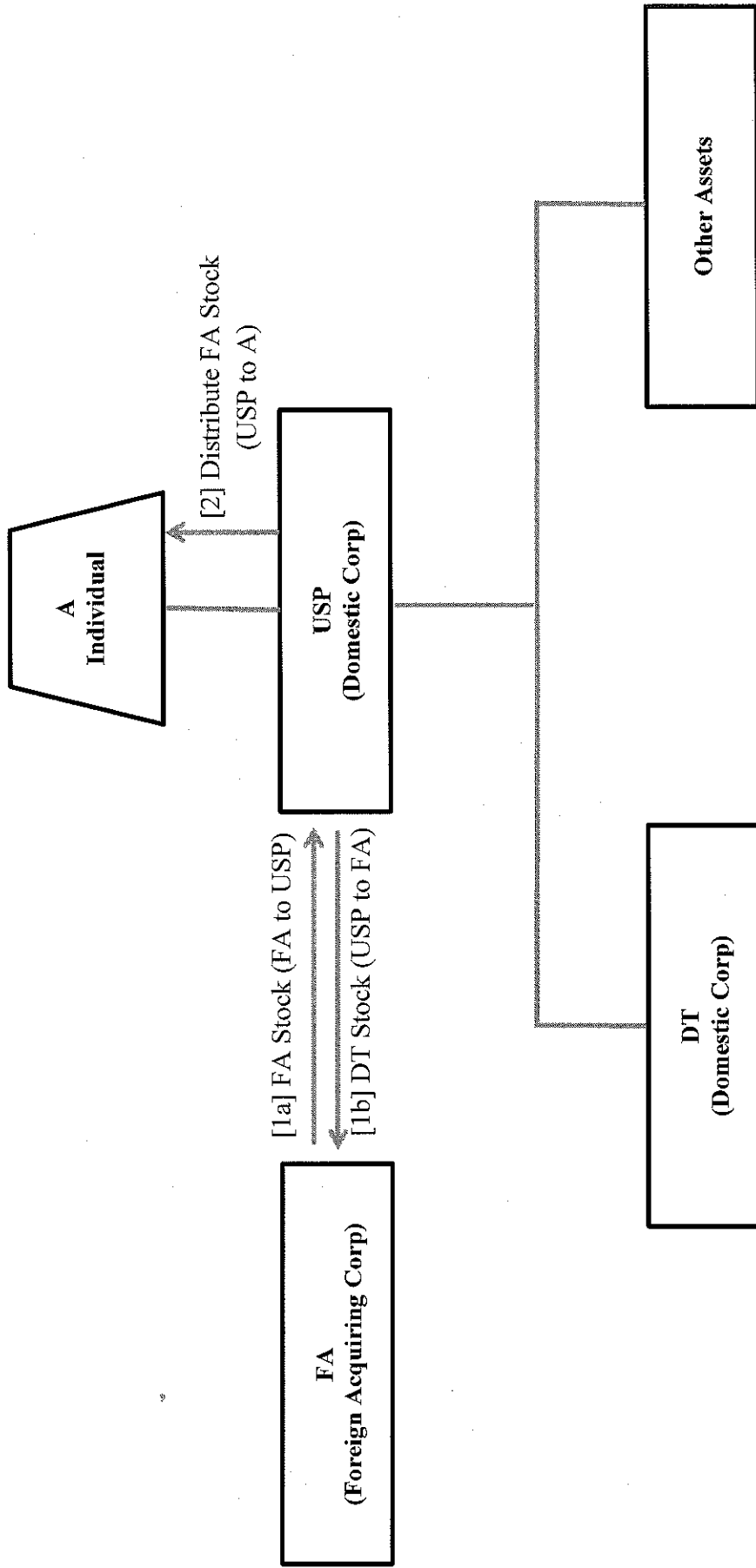
2016 TREASURY INVERSION REGULATIONS: IMPACT ON INVERSION STRUCTURE

SLIDE #9 SPINVERSION, BEFORE, REG § 1.7874-6T(g), EXAMPLE 1



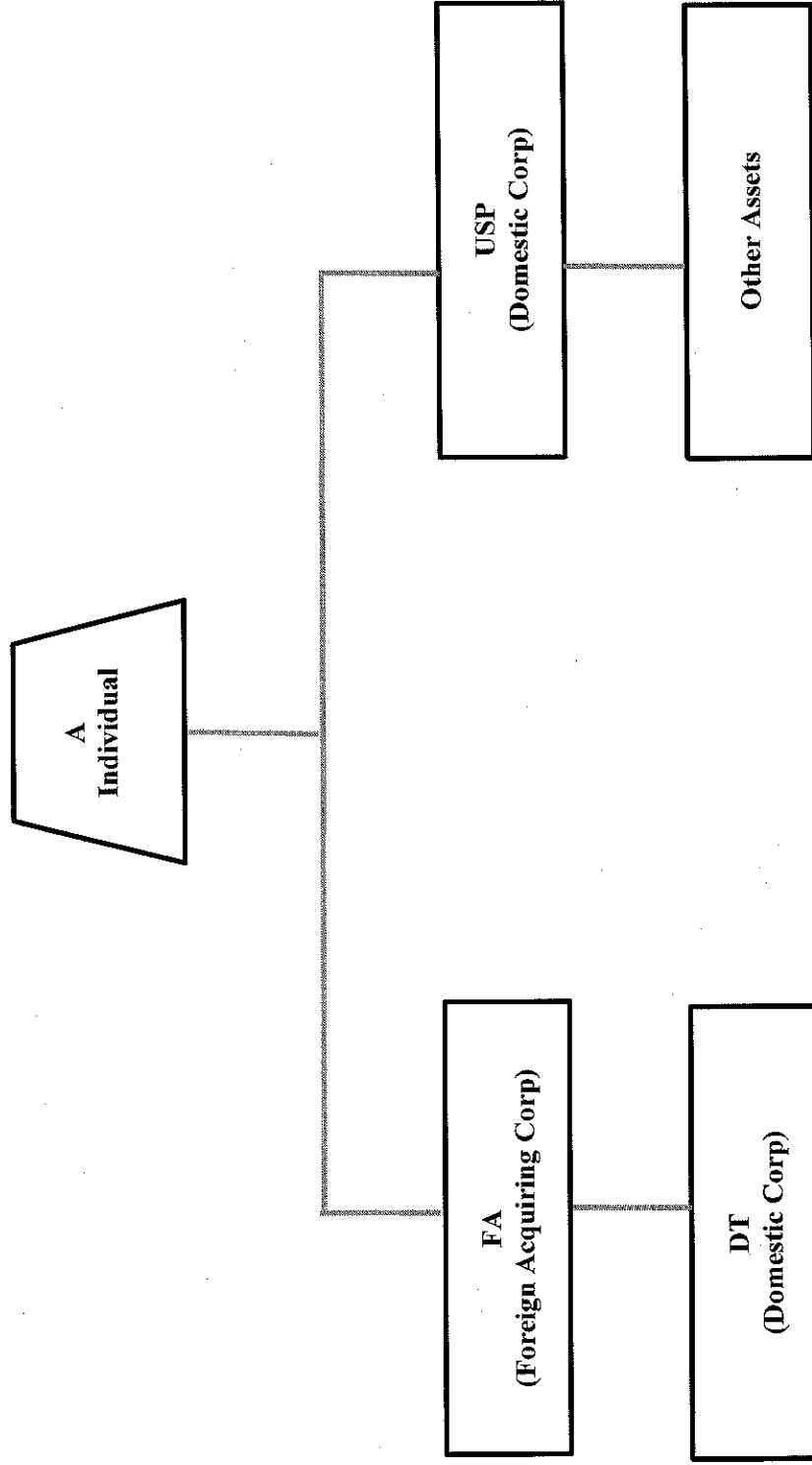
2016 TREASURY INVERSION REGULATIONS: IMPACT ON INVERSION STRUCTURE

SLIDE #10 SPINVERSION, THE SPIN, REG § 1.7874-6T(g), EXP 1, USP SPINS OFF DT TO FA

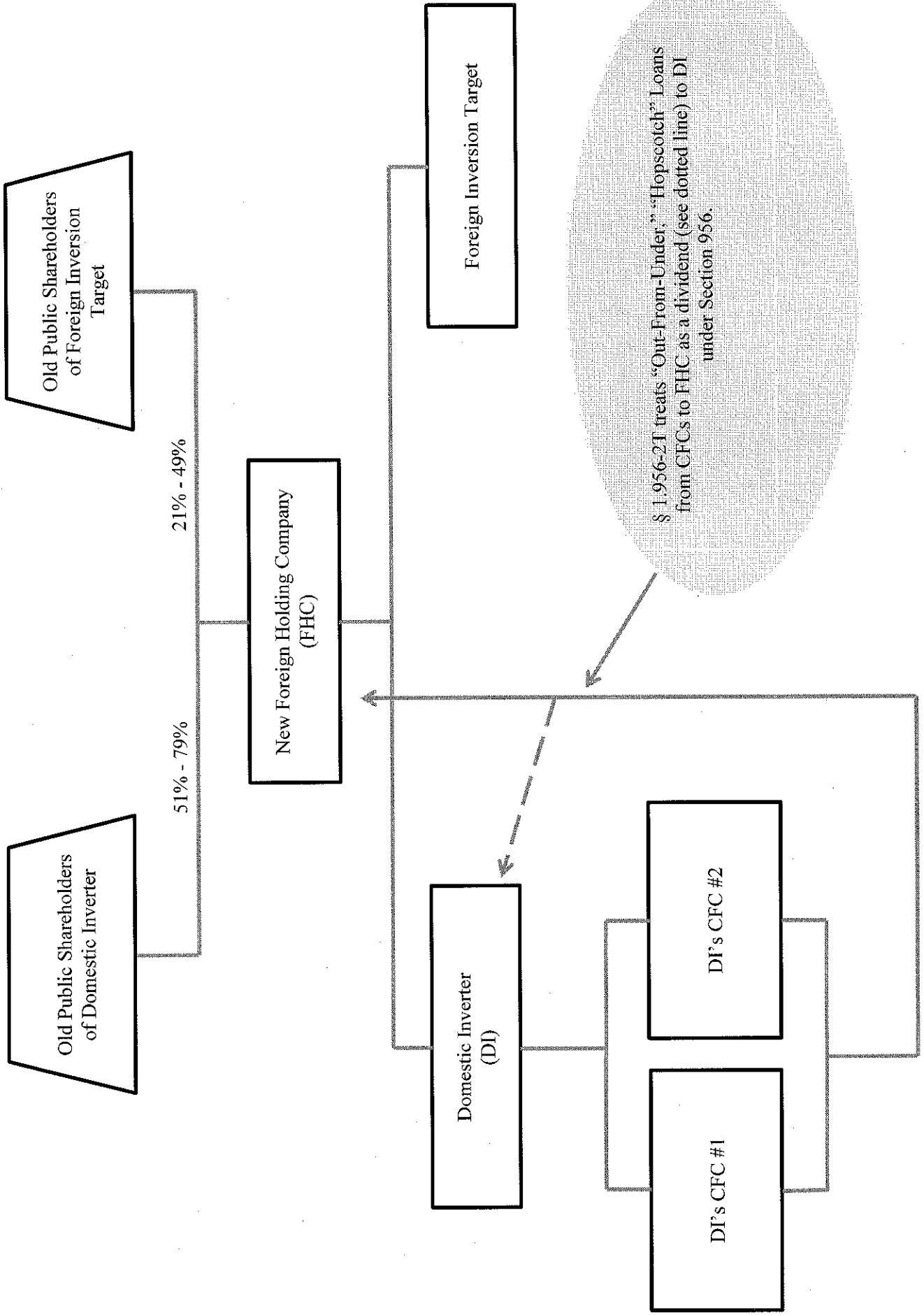


2016 TREASURY INVERSION REGULATIONS: IMPACT ON INVERSION STRUCTURE

SLIDE #11 SPINVERSION, AFTER, REG § 1.7874-6T(g), EXP 1: DT HAS INVERTED AS SUB OF FA

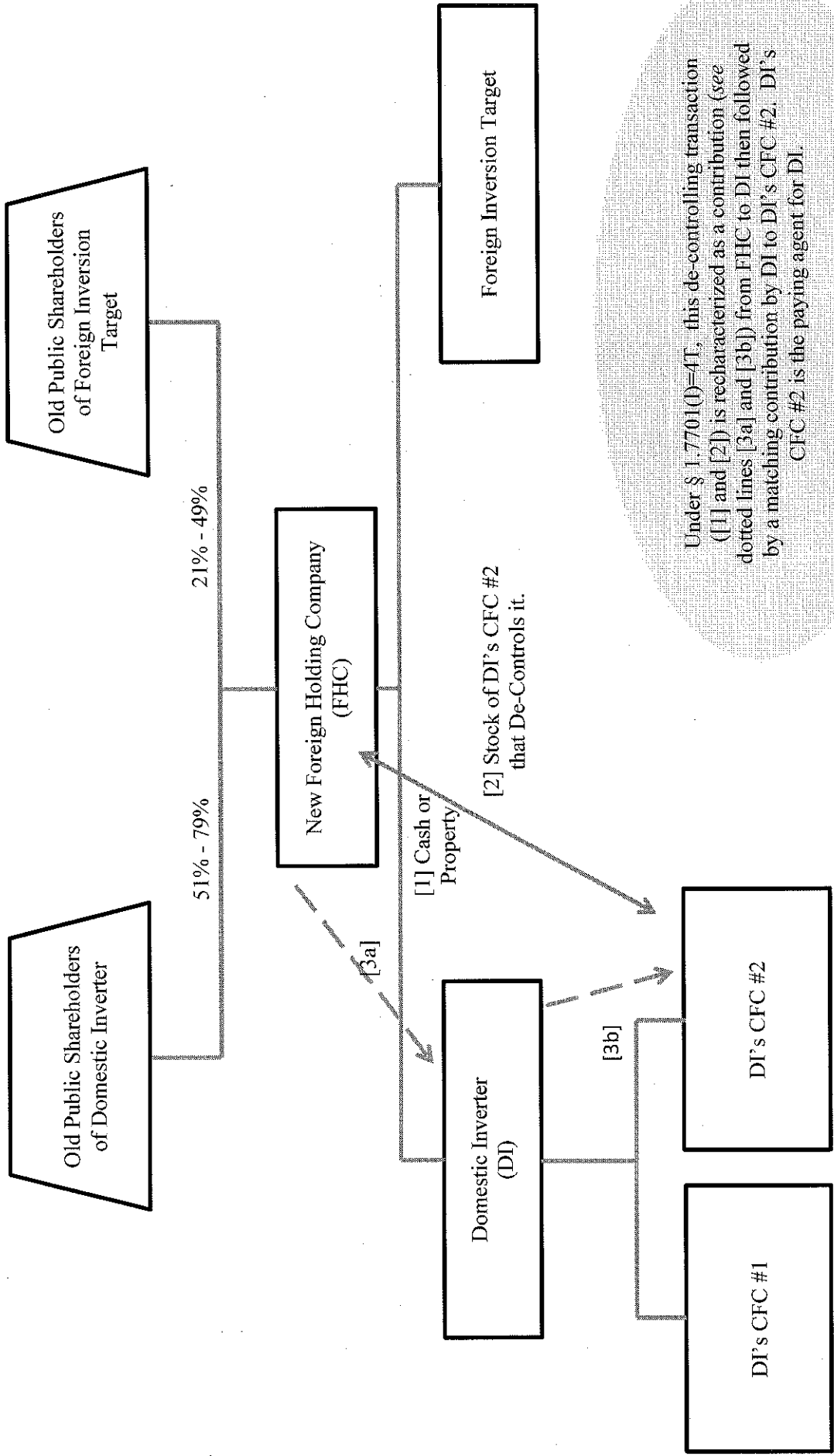


2016 TREASURY INVERSION REGULATION: POST-INVERSION TAX AVOIDANCE
SLIDE #12 ANTI-HOPSCOTCH LOAN RULE, REG § 1.956-2T(a)(4)



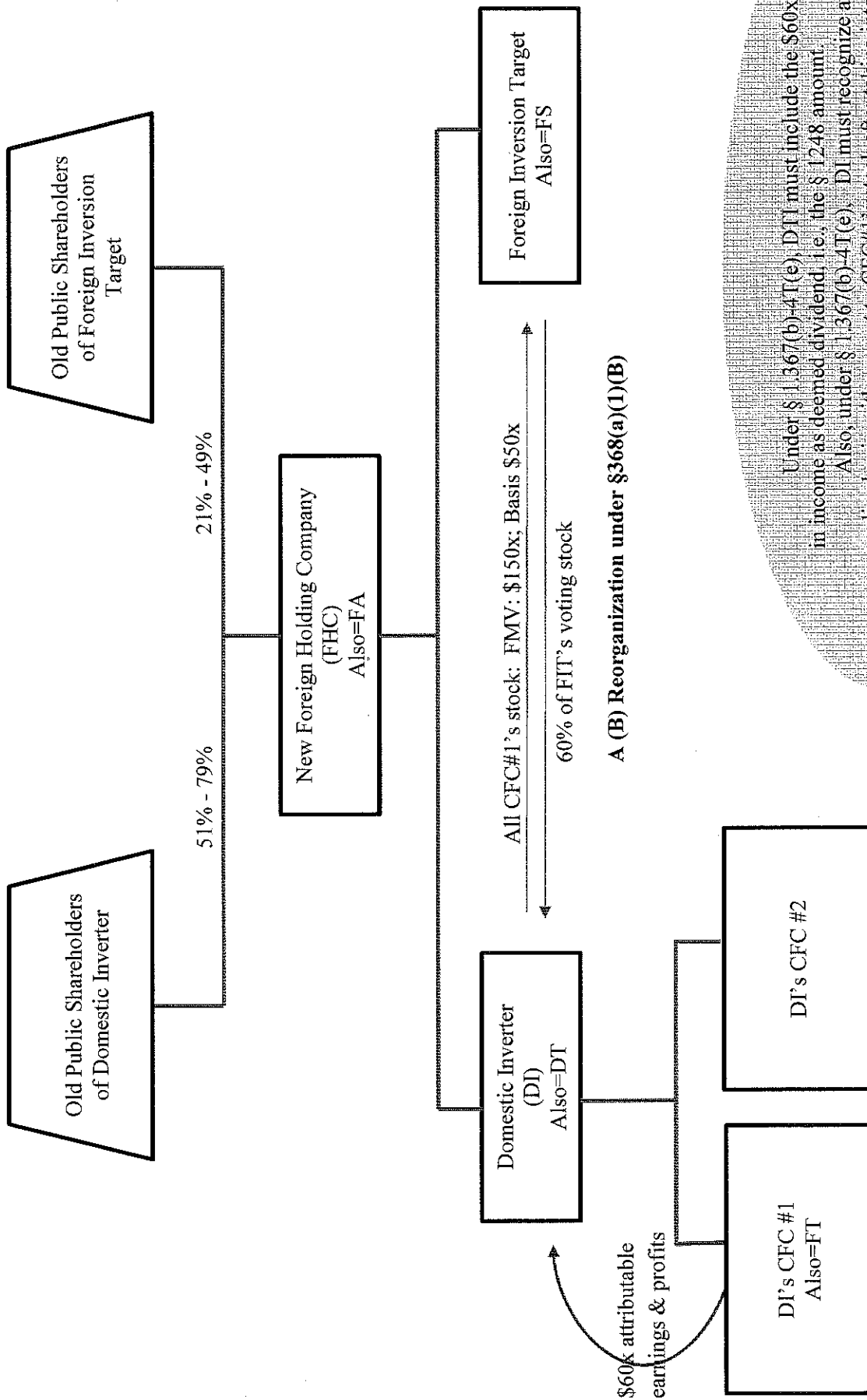
2016 TREASURY INVERSION REGULATION: POST-INVERSION TAX AVOIDANCE

SLIDE #13 ANTI-DECONTROL OF CFC RULE, REG § 1.7701-1(d)



Under § 1.7701(d)=4T, this de-controlling transaction ([1] and [2]) is recharacterized as a contribution (see dotted lines [3a] and [3b]) from FHC to DI then followed by a matching contribution by DI to DI's CFC #2. DI's CFC #2 is the paying agent for DI.

TREASURY INVERSION REGULATION: POST-INVERSION TAX AVOIDANCE
SLIDE # 14 CFC STOCK DILUTION RULE, REG. § 1.367(b)-4T(e)



\$60x attributable earnings & profits

Domestic Inverter (DI) Also=DT

All CFC#1's stock: FMV: \$150x; Basis \$50x

Foreign Inversion Target Also=FS

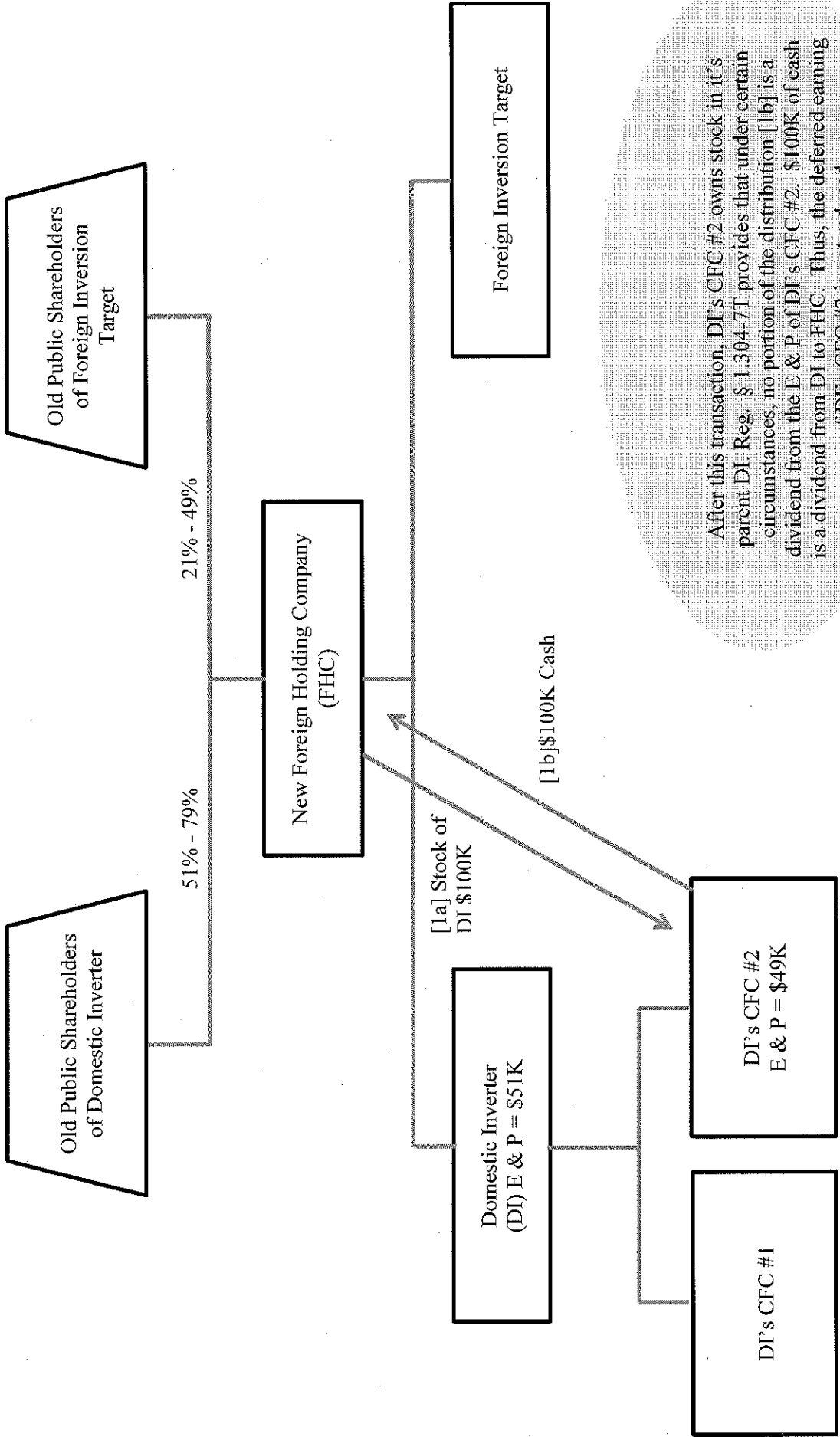
DI's CFC #1 Also=FT

DI's CFC #2

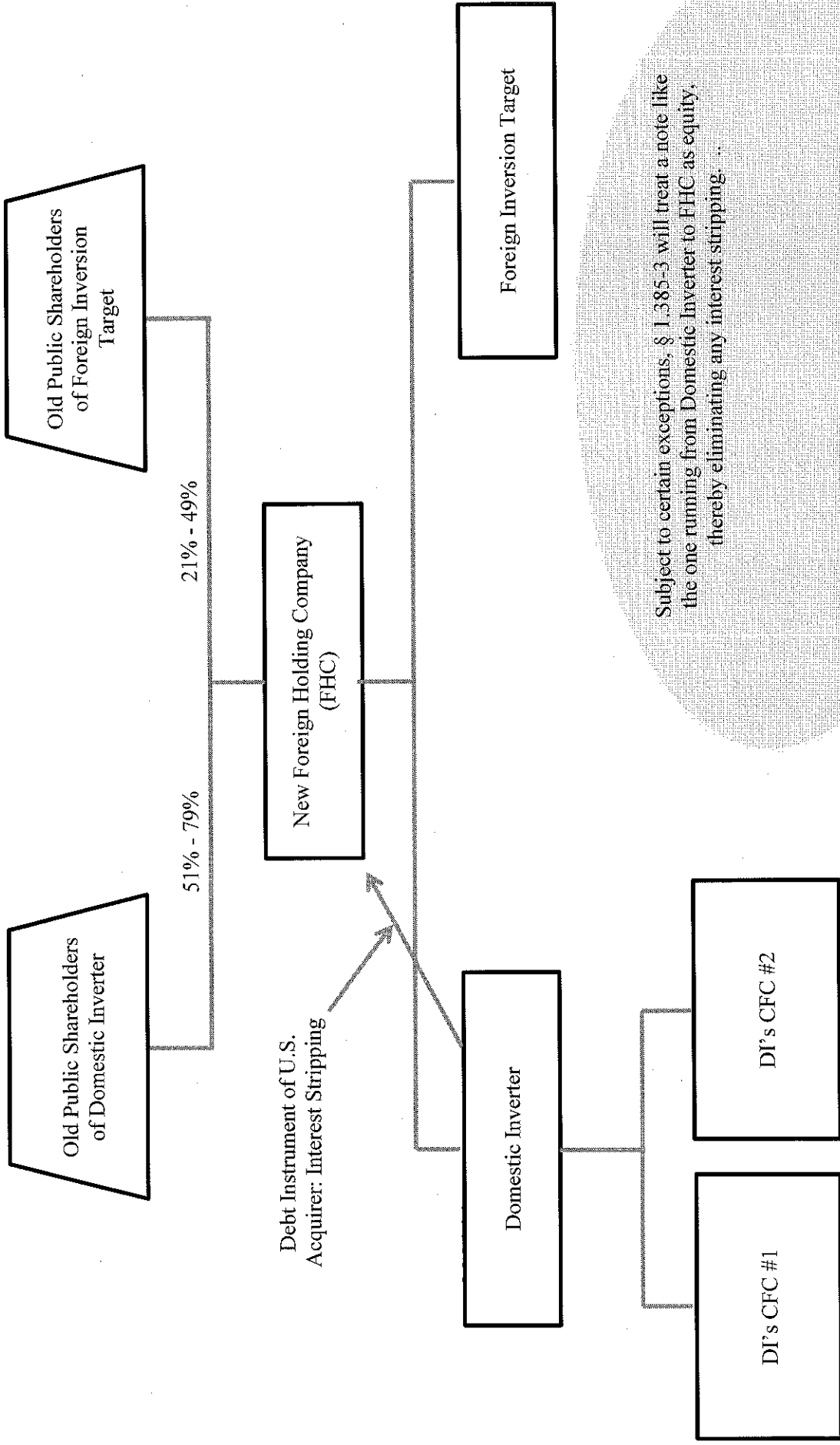
A (B) Reorganization under §368(a)(1)(B)

Under § 1.367(b)-4T(e), DI must include the \$60x in income as deemed dividend, i.e., the § 1248 amount. Also, under § 1.367(b)-4T(e), DI must recognize all realized gain with respect to CFC#1's stock after taking into account any increase in basis resulting from the deemed dividend. In this example, DI must recognize: \$150x - (\$50x + \$60x) = \$40x. If CFC#1 had no E&P, DI would recognize \$100x of realized gain.

TREASURY INVERSION REGULATIONS: POST-INVERSION TAX AVOIDANCE
SLIDE #15 ANTI-SECTION 304 AVOIDANCE RULE, REG. § 1.304-7I



TREASURY SECTION 385 REGULATIONS: POST-INVERSION TAX AVOIDANCE
SLIDE #16 POTENTIAL POST INVERSION INTEREST STRIPPING



Subject to certain exceptions, § 1.385-3 will treat a note like the one running from Domestic Inverter to FHC as equity, thereby eliminating any interest stripping.