Corporate Inversion
Reconciling Global Competitiveness, Fiduciary Duty, & Ethics

Some Management and Ethics Perspectives of Corporate Inversion

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Addressing Corporate Inversions

3 Perspectives to Consider

• US Tax Policy
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• Corporate Governance & Responsibility
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• Ethics
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Corporate collapses and scandals

have:

* increased the level of distrust between the public and the business community*

* increased the expectation for transparency of corporate actions*
Because of reduced trust,

the public has characterized corporate actions involving corporate inversion as falling along a continuum of “bad decisions” from unpatriotic to criminal, even though corporate inversions are legal.
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**A Matter of Interest . . .**

Criticism regarding whether corporate inversion is good or bad depends upon whose *interests* are being served . . .

- Shareholders
- Corporate management & directors
- Society as a whole
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Legislative Action – Federal & State

In October 2002 Congress passed and President Bush signed into law the *Sarbanes-Oxley Act* establishing new governance rules for corporations and accountants (reporting requirements, certification of financial reports, employee “whistleblower” protections).

Various states (e.g., Connecticut, Minnesota, Maine, and West Virginia) have considered or passed legislation addressing corporate responsibility.
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A Change in the Paradigm

Questions regarding Interests require ---

Policy perspectives other than Tax Benefits ---

Consideration regarding decisions based upon corporate best interest versus impact on the interests of the community.

all clearly suggest . . .

A Change in the overall paradigm of corporate behavior is underway . . .
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**Fiduciary Duty to Shareholders**

Under American corporate law, officer and director fiduciary duty requires actions that maximize ROI for company Shareholders.

Current tax law permits corporate inversion.

Keeping taxes as low as possible is a business variable that may enhance a company’s ROI.

Therefore, corporate management arguably must consider inversion if so doing would be in the shareholder’s best interest.
Corporate scandals and subsequent legislative response have called into question the standards by which corporate officers and directors are seeking to “maximize shareholder value.”

If following the spirit of the law promotes actions geared at realizing maximum monetary results, then arguably, following the letter of the law should require adherence to rules geared at promoting and maintaining consumer confidence in the system.
Corporate Governance . . .

*Corporate Governance* is a concept whereby a company sets forth the rules by which officers, directors, and employees will conduct business.

Distribution of Rights and Responsibilities for the Board and for managers, shareholders, and stakeholders

Rules and Procedures for Decision-Making

*To provide a structure through which company objectives are set and the means of attaining such objectives and monitoring performance.*
Currently, U.S. Companies are not statutorily subject to a universal, common code of conduct.

There have been numerous initiatives inviting voluntary participation . . .

In July 2002, the President announced an initiative entitled “A New Ethic of Corporate Responsibility.”

This initiative challenged CEOs to comply with the existing disclosure rules, proposed provisions to strengthen SEC rules, and established a Corporate Fraud Task Force.
Shinn (2001) suggests an organization’s governance system has 4 features:

1. *Information Institutions* (accounting rules, audit procedures, standards settings, 3rd-party analysis)

2. *Oversight Institutions* (boards/directors, rules addressing fiduciary responsibilities)

3. *Control Institutions* (degree of voice of minority SH’s in case of contested control and the rules that govern such contests)

4. *Managerial Institutions* (hiring, compensating, and firing of senior managers)
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Impact of Legislative Action on Corporate Governance

According to a PricewaterhouseCoopers survey in March 2003 . . .

85% of US multinational companies have altered their control and compliance practices

Only 1/3 believe Sarbanes-Oxley will restore investor confidence

More than half said the law merely formalized what they were already doing
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Code of Conduct and Governance

Regardless of the governance structure that an organization has -- one thing is consistent throughout . . .

Effective corporate governance must begin with and have the full support of the Board of Directors.
Traditional Corporate law requires officers and directors to act in the best interests of their corporation, not the public at large.

Commentators are increasingly calling for an expansion of corporate law requiring officers and directors to limit corporate actions that would have an adverse effect on the community at large.
Corporate Responsibility versus Fiduciary Duty

According to a recent *Business Week* poll,

95% of 1000 adults surveyed agreed:

*U.S. corporations should have more than one purpose. They also owe something to their workers and the communities in which they operate, and they should sometimes sacrifice some profit for the sake of making things better for their workers and communities.*

Only 4% agreed with the statement that

*U.S. corporations should have only one purpose – to make the most profit for their shareholders.*
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Corporate Responsibility versus Fiduciary Duty

As a result of corporate missteps, public distrust, and changing public expectations - - and notwithstanding recent legislative mandates for change . . .

When faced with issues such as whether to engage in corporate inversion transactions, the Treasury Department’s suggested policy approach to inversions may ultimately require consideration of a company’s corporate conscience . . .
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Corporate Ethics

“Ethics, like democracy, is a lot easier in theory than in practice.”
Entine, ‘96

Corporate ethics shares many of the tenets of the Corporate Responsibility movement, but the focus is primarily on behavior, from top management on down throughout the corporation.
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Corporate Ethics

2003 *Ethics Resource Center* survey (1500 workers)

82% expressed a perception that “top management keeps promises and commitments to the employees.”

21% of managers under 30 feel pressure to compromise on company ethics standards, compared to 9% of managers overall.

The clear message is that leaders and managers “set the target, the climate, the ethos, the expectations that fuel behavior.”

Thomas Donaldson, Wharton
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Corporate Ethics

When exploring corporate ethics, two key areas are prevalent in today’s environment:

**Patriotism**
According to one commentator, current tax law addressing corporate inversions there is a disparity between what is good for the country and what is good for the company. After 9-11, a number of legislators introduced or co-sponsored bills to stem the practice of corporate inversions.

**Fairness**
Small and mid-size companies are arguably at a competitive disadvantage as they are ineligible for a 10% effective reduction in tax rates because they cannot engage in corporate inversion.
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Summary

Corporate inversion is a creature of U.S. laws.

Public debate is likely to continue into this election year regarding corporate governance, ethics, and their relation to traditional corporate practices, including fiduciary duty of corporate officers and directors.

In an environment of heightened public scrutiny, opportunities exist to evaluate the issue of changing U.S. tax policy from multiple perspectives, including not just tax policy, but also

Corporate governance, and

Corporate behavior (ethics)