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Corporate Inversions: Stanley Works and the Lure of Tax Havens

Just after being promoted to head of tax planning at American HandyWorks, Inc., Roger Meyerson found himself buried in research on the practice of moving companies to tax havens. His company's largest competitor, Stanley Works, had announced on February 8, 2002, that it was moving the legal domicile of the company to Bermuda for strategic and tax reasons. HandyWork's Chief Financial Officer Jonathan Stern wanted Meyerson to stay on top of the issue and provide a detailed report on how Stanley planned to lower its effective tax rate by seven to nine percentage points as it had claimed it could in a press release. Stanley's market value had jumped $200 million dollars—a gain of over 5%—the day after they announced the deal; Stern wanted to know where these gains were coming from and whether HandyWorks could capitalize on the structure as well. As it had turned out, Stanley's announcement marked the beginning of a prolonged appreciation in Stanley's stock price that was also driven by several key alliances and positive results (see **Exhibit 1** for stock price history and recent events). Three months later, on May 10, Stanley's shareholders had very narrowly approved the inversion transaction, but Stanley announced that it would need to hold a second vote because the first had shown "irregularities." Stanley lost $250 million of market value on May 10.

Meyerson reviewed these figures. First he wanted to understand what was driving Stanley to do this. Then he wanted to gauge the market's reaction to determine what opportunities this mechanism might offer HandyWorks—in particular, did HandyWorks have to follow suit in order to stay competitive? In order to do this, Meyerson knew that he had to understand the link between Stanley's motivations and the large swings in market value that the move to Bermuda had prompted.

Stanley Works

Founded in 1843 by Frederick T. Stanley, The Stanley Works had grown to nearly 15,000 employees, was a member of the Standard & Poor's (S&P) 500 Index, and was the leading toolmaker in the United States with sales of $2.6 billion. It divided its operations into two groups, Tools (77% of sales) and Doors (23% of sales). The Tools division manufactured hand tools for consumer and

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Professor Mihir A. Desai of the Harvard Business School and Professor James R. Hines Jr. of the University of Michigan prepared this case with Research Associate Mark F. Veblen. American Handyworks and its executives are fictional. The material regarding Stanley Works has been drawn from published sources. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

professional use, and mechanics' tools as well as pneumatic and hydraulic tools for industrial uses. The hand tools were distributed directly to retailers such as home centers and indirectly to end users through third-party distributors. Ultimately the products were used for everything from simple around-the-home fix-it jobs to major construction projects ranging from buildings to utilities to railroads. The more sophisticated products found their way onto assembly line equipment at major vehicle makers. The Doors division manufactured a full range of door systems, from ordinary doors for use in residential homes to reinforced commercial systems such as automatic and revolving doors. Door products were sold under a variety of brand names through both direct and indirect sales channels. Much of Stanley's sales were concentrated in a few mass market home centers—Home Depot, Sears, and Wal-Mart, for example—with Home Depot accounting for approximately 18% of 2001 revenues. Nonetheless, Stanley operated in over thirty countries, with foreign operations accounting for 30% of total sales. Meyerson glanced over the consolidated financial statement data he had retrieved from Stanley's most recent annual report to the Securities and Exchange Commission (see **Exhibit 2**). He also noted Stanley's equity beta of 0.89 and the 30-year Treasury Bond yield of 3.41%, as reported by Bloomberg.

Planned Reincorporation in Bermuda

A February 8th press release provided a general outline of Stanley's intentions—to "modify [its] corporate structure so that the company's place of incorporation will be changed from Connecticut to Bermuda." Chairman and Chief Executive John Trani cited increased operational flexibility, better access to international capital markets, and improved tax efficiency as strategic motivations for implementing the restructuring.

> This strategic initiative will strengthen our company over the long-term. An important portion of our revenues and earnings are derived from outside the United States, where nearly 50% of our people reside. Moreover, an increasing proportion of our materials are being purchased from global sources. This change will create greater operational flexibility, better position us to manage international cash flows and help us to deal with our complex international tax structure. . . . In addition to operational flexibility, improved worldwide cash management and competitive advantages, the new corporate structure will enhance our ability to access international capital markets, which is favorable for organic growth, future strategic alliances and acquisitions. Finally, enhanced flexibility to manage worldwide tax liabilities should reduce our global effective tax rate from its current 32% to within the range of 23%–25%.

At the same time, Trani assured investors (a) that the transaction would "be seamless and transparent for all stakeholders—employees, customers and vendors—around the world" and (b) that "corporate operations [would] continue to be managed from our current headquarters in New Britain, Connecticut, and these changes will not affect day-to-day operations."

The journalistic and editorial ranks of the business press, however, were decidedly less enthusiastic about the transaction—as were politicians in Washington. Already several teams of Congressmen and Senators were making plans to introduce legislation banning such transactions.[1] A *New York Times* editorial quipped in a piece entitled "The Bermuda Tax Triangle":

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[1] The Reversing the Expatriation of Profits Offshore Act (the REPO Bill), proposed in the Senate, would have required that an inverting company continue to be taxed as a domestic corporation if (1) the foreign entity held substantially all of the assets of the inverting domestic company, and (2) former shareholders of the domestic corporation owned at least 80% of the foreign company's stock. It also provided that if U.S. shareholders owned more than 50% but less than 80% of the foreign company,

> Stanley Works ought to change its name to Stanley Flees. The maker of distinctive black-and-yellow tools that for 159 years has made its home in New Britain, Conn., is planning to reincorporate in Bermuda in order to stiff Uncle Sam. Stanley is only the latest in an alarming exodus of greedy companies, but the prospect of the venerable firm taking off for a tax haven caused one local congressman to note that Benedict Arnold, too, left Connecticut and sailed off to Bermuda.[2]

The reaction to Stanley's decision, and Stanley's willingness to withstand it, only sharpened Meyerson's interest in understanding what made Stanley anxious to expatriate.

Primer on International Taxation

In order to figure out Stanley's motivation, Meyerson realized that he needed to revisit some of the foundations of how tax rules affect U.S. multinational firms. In particular, he wanted to understand how the income from foreign operations is taxed and what effects foreign operations have on a firm's overall tax position.

Concept of Residence of Domicile

The U.S. government taxes all companies that do business in the United States on their U.S. income. In addition, it taxes American firms on their foreign income. Accordingly, the United States is said to use a **worldwide income tax system**. This, naturally, makes the definition of what constitutes a domestic company crucially important. From a legal perspective, an American firm is any firm incorporated in the United States. A firm is free to choose its jurisdiction of incorporation, and (under U.S. law) is not required to produce or sell anything in the country that serves as its tax home. Many other countries, including Germany, the Netherlands, Canada, and France—not to mention tax havens—tax only income generated inside their borders. Because they tax their residents (regardless of "citizenship") only on domestic income, such countries are said to use a **territorial income tax system**.

Foreign Tax Credits

While the United States taxes the worldwide incomes of its corporations on top of taxes they pay to foreign governments, American firms are permitted to claim tax credits for foreign taxes paid (to avoid "double taxation"—levels of taxation that could erode the economic viability of business). Here, Meyerson struggled to get his hands around a complex set of rules and regulations. Since the foreign tax credit is intended to alleviate international double taxation, and not to reduce U.S. tax liabilities on profits earned *within* the United States, the foreign tax credit is limited to U.S. tax liability on foreign-source income. For example, an American firm with $200 of foreign income that faces a U.S. tax rate of 35% has a foreign tax credit limit of $70 (35% of $200). If the firm pays foreign income taxes of less than $70, then the firm would be entitled to claim foreign tax credits for all of its foreign taxes paid. If, however, the firm pays $90 of foreign taxes, then it would be permitted to claim no more than $70 of foreign tax credits.

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the IRS would scrutinize the transaction and the company's financials for the subsequent 10 years and would disallow various deductions. Several other proposals with similar features were also submitted in Congress.

[2] "The Bermuda Tax Triangle," *The New York Times*, May 13, 2002.

Deferral of Taxes Due on Foreign Earnings

Meyerson also knew that American companies were permitted to defer any U.S. tax liabilities on certain unrepatriated foreign profits until they actually receive such profits in the form of dividends.[3] To illustrate deferral, Meyerson considered the case of a subsidiary of an American company that earned $500 in a foreign country with a 20% tax rate. This subsidiary paid taxes of $100 to the foreign country (20% of $500), and might have remitted $100 in dividends to its parent U.S. company, using the remaining $300 ($500 minus $100 of taxes minus $100 of dividends) to reinvest in its own (foreign) operations. The American parent firm then had to pay U.S. taxes on the $100 of dividends it received (and was eligible to claim a foreign tax credit of $20 for the foreign income taxes its subsidiary paid on the $100). But the American firm was not required to pay U.S. taxes on any part of the $300 that the subsidiary earned abroad and did not remit to its parent company. If, however, the subsidiary were to pay a dividend of $300 the following year, the firm would then be required to pay U.S. tax (after proper allowance for foreign tax credits) on that amount.

Limitations on Deferral and Anti-abuse Rules

While Meyerson saw a great opportunity in deferral, he quickly discovered the Controlled Foreign Corporations (CFC) rules and so-called Subpart F income classification. U.S. tax law contains these provisions to prevent American firms from delaying the repatriation of lightly taxed foreign earnings. These tax provisions apply to all CFCs, which are foreign corporations owned at least 50% by American individuals or corporations who hold stakes of at least 10% each. Under the Subpart F provisions of U.S. law, some foreign income of controlled foreign corporations is "deemed distributed" whether or not remittance actually (or ever) occurs, and therefore is immediately taxable by the United States.[4] Subpart F income includes passive income derived either through (a) insuring risks outside the CFC's home country or (b) so-called "foreign base company income." This latter category includes holding company income such as dividends, interest, and royalties as well as sales, service, shipping, and oil and gas related income. In general, these rules prevent U.S. corporations from setting up affiliates in tax havens to hold investments (and therefore earn either deferred or tax-free returns on the investments).

Excess Credit or Deficit Credit Positions

Taxpayers whose foreign tax payments are larger (smaller) than the foreign tax credit limit are said to have "excess (deficit) foreign tax credits." American law permits taxpayers to use excess foreign tax credits in one year to reduce their U.S. tax obligations on foreign source income in either of the two previous years (carry-backs) or in any of the following five years (carry-forwards).[5] In

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[3] This deferral is available only on the active business profits of American-owned foreign affiliates that are separately incorporated as subsidiaries in foreign countries.

[4] Subpart F income consists of income from passive investments (such as interest and dividends received from investments in securities), foreign base company income (that arises from using a foreign affiliate as a conduit for certain types of international transactions), income that is invested in United States property, money used offshore to insure risks in the United States, and money used to pay bribes to foreign government officials. American firms with foreign subsidiaries that earn profits through most types of active business operations, and that subsequently reinvest those profits in active lines of business, are not subject to the Subpart F rules, and are therefore able to defer U.S. tax liability on their foreign profits until they choose to remit dividends at a later date.

[5] Foreign tax credits are not adjusted for inflation. Barring unusual circumstances, firms generally apply their foreign tax credits against future years only when unable to apply them against either of the previous two years. The most common

practice, the calculation of the foreign tax credit limit relies on "worldwide averaging"—that is, all repatriated earnings, and their associated foreign tax credits, would be considered jointly.

Expense Allocations under the FTC System

In addition to the rules governing the taxation of repatriated earnings, Meyerson knew that multinational firms such as Stanley also faced expense allocation rules. Firms with certain types of tax-deductible expenses, particularly interest charges, expenditures on research and development, and some general administrative and overhead expenses, are required to allocate fractions of these expenses between domestic and foreign source—even if the expenses were incurred entirely in the United States. The logic behind these rules appeared to be that raising investment capital, producing innovations, and managing firm operations all contribute to the worldwide income of the firm. The intention of the U.S. allocation rules is to retain the tax benefits of the deductibility of such expenses against domestic income only for the portion of expenses that contribute to producing domestic income.

U.S. tax rules implement this principle by allocating a certain portion (usually foreign assets as a% of total assets[6]) of particular expense items against foreign source income. These expenses reduce the amount of foreign income for the purpose of calculating the foreign tax credit limit, which is costly for firms with excess foreign tax credits (but not costly for firms with deficit foreign tax credits). Because interest expense is typically a firm's largest allocable expense, in practice, firms with lightly-taxed foreign income and considerable U.S. interest expenses are likely to incur significant costs associated with the inability to receive the full benefits of interest expense deductions.

Inversion Transactions

Mechanics of Inversions

Meyerson consulted with Alison Lee, HandyWork's Vice President and General Counsel. After carefully defining an inversion transaction as a restructuring by a company of its corporate form such that it became a foreign company (with the same dispersed U.S. shareholders), she talked Meyerson through two slides she had prepared.

Lee proposed that the tax purpose of an expatriation was to avoid U.S. tax liabilities associated with foreign income (see **Exhibit 3**). The way this was accomplished was by removing foreign assets and foreign business activity from ownership by an American corporation, thereby effectively eliminating U.S. taxes on any income it generated. Prior to inverting, dividends from foreign operations were received by the American parent company, while subsequent to the inversion, dividends from foreign operations (as well as those from American operations) were received by the Bermuda (in this example) parent company.

Lee's second slide reflected the general requirement under U.S. law that foreign inversions be "recognition events" for capital gains tax purposes, meaning that taxpayers would incur capital gains

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reason why firms do not apply excess foreign tax credits against either of the previous two years is that they already have excess foreign tax credits in those years.

[6] While there is a long history to shifting definitions for these ratios, interest expenses were usually allocated between domestic and foreign source based on the fraction of assets located inside and outside the United States.

tax liabilities for any previously unrecognized gains.[7] The nature of the capital gains taxes triggered by inversions depended on the way in which the inversion was structured; there were several possibilities, falling into two general categories (see **Exhibit 4**). In a taxable stock transfer, the new foreign parent company effectively exchanged its own shares for shares of the American company, a transaction that required individual and other shareholders to recognize capital gains equal to the difference between fair market values of the shares and tax basis. At the conclusion of such a transfer, shareholders owned shares in the new foreign parent company, and the American operations were typically organized as a subsidiary of the new foreign parent. In an asset transaction, the new foreign parent company acquired an American firm's assets, thereby triggering taxes on capital gains at the corporate level equal to the difference between fair market value and basis.[8]

Lee also pointed out a peculiarity of such transactions. In the Stanley case, as in several others, the inversion to Bermuda (i.e., reincorporation in Bermuda) was accompanied by structuring the deal so the new parent company would be registered as an external company in Barbados. This permitted Stanley to take advantage of favorable withholding tax treatment of dividends and interest remitted from the United States to the foreign parent company.[9] Stanley and other companies are subject to rules requiring that tax-deductible interest payments from an American subsidiary to its foreign parent company not exceed interest payments that unrelated parties would require for the same loans. Furthermore, Stanley—or any other foreign-owned American subsidiary with a debt/equity ratio that exceeds 1.5—is not permitted to deduct interest payments to a foreign parent in excess of 50% of the subsidiary's adjusted gross income. Lee also mentioned in passing that the deals also presented an interesting twist with respect to the incentive to engage in tax planning overseas—companies reducing their foreign taxes would no longer face higher U.S. taxes as a consequence.

The History of Inversions

Lee also provided details on selected corporate expatriations over the last 20 years (see **Exhibit 5**). Meyerson noticed that expatriating companies were historically dominated by the oil and gas and reinsurance businesses, but recent expatriates appeared to be drawn from a more general distribution of American industrial companies. Indeed, seven of the firms were members of the S&P 500.[10] Since the middle of 2001, firms with an aggregate market capitalization of over $25 billion had announced inversions. Meyerson also noticed the variety of transaction structures that were used to accomplish inversions and noted that a number were the consequence of normal M&A (merger and acquisition) activity.[11]

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[7] This applied to gains only. Losses were not realized, but instead shareholders received carryover basis in the newly issued stock.

[8] There were variants, including drop-down transactions, that entailed a combination of these two transactions, and associated capital gains tax liabilities at both the individual shareholder and U.S. corporate level. Other structures allowed U.S. shareholders to elect to be treated differently from non-U.S. shareholders.

[9] The United States imposes withholding taxes of 30% on cross-border dividend and interest payments from foreign-owned American subsidiaries to their parent companies unless local tax rates are sufficiently high or a bilateral tax treaty specifies otherwise. Barbados and the United States have a tax treaty that eliminates the U.S. withholding tax on interest paid by an American subsidiary to its Barbados parent company, and reduces the corresponding withholding tax rate on dividend payments to 5%.

[10] These S&P 500 firms are Cooper, Ingersoll Rand, Nabors, Noble, Stanley, Transocean, and Tyco.

[11] Accenture and Seagate represented the initial capitalization of companies abroad and, as such, constitute non-inversion expatriations.

Meyerson pressed Lee for a bit of color on the stories behind the past inversions. She explained that there had been a trickle of such transactions in the 1980s and 1990s. The first occurred in 1983, when McDermott, a U.S. corporation, set up a Panamanian subsidiary, McDermott International, to acquire the American entity. Though the IRS challenged the transaction, McDermott's tax-favored treatment prevailed, and Congress subsequently adopted a rule making such transactions taxable to U.S. shareholders. In 1994, Helen of Troy announced an inversion designed to qualify as a tax-free share exchange to its shareholders, despite the new rules. In order to prevent this sort of transaction from becoming commonplace among American companies, new rules were again issued. The new rules made acquisitions of U.S. companies taxable to U.S. shareholders if the acquiring (foreign) company was not larger than the U.S. entity. Holding companies created to acquire U.S. operations (as in Helen of Troy) would therefore trigger taxes to U.S. shareholders. With such broad scope, this had the potential to complicate legitimate cross-border merger and acquisition transactions.[12]

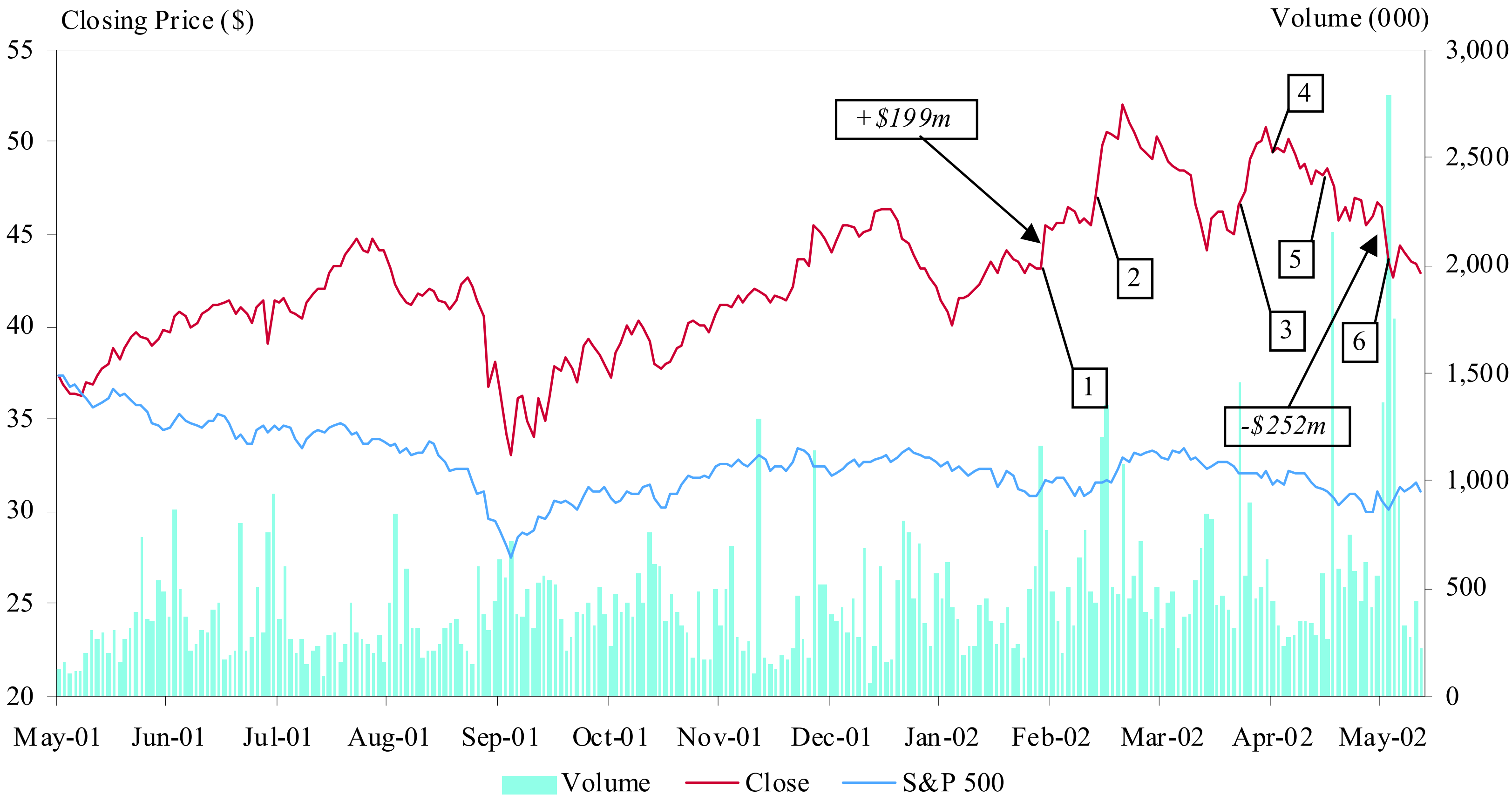
Ferreting Out the Market's Assessment

Meyerson puzzled over Stanley's recent stock price history—in particular, he stared at the $200 million jump in market value the day after the inversion was announced and the slightly larger drop in value the day the revote was announced. He realized that he was going to need much more detail on Stanley's international operations and capital structure, which he found in the footnotes to consolidated financial statements in Stanley's Form 10-K. First, Meyerson wanted a sense of the base in interest expense Stanley was using for its expense allocation calculations (see Note H in **Exhibit 6**). Then, he wanted to understand just how integral a part of Stanley's overall operations foreign divisions were (see Note O in **Exhibit 7**). Meyerson's harbored the hope, however, that he could find extensive information on Stanley's tax situation in its income tax disclosure (see Note P in **Exhibit 8**). Estimating the average tax rate Stanley faced in foreign countries would allow him to make a more accurate determination of how large the repatriation tax savings might be.

Seeing how much shareholder value was at stake, Meyerson wanted to isolate how an inversion could generate such large market value swings. Looking over the numbers, Meyerson's biggest concern was that he might not be able to account for all of the market value change Stanley had experienced after announcing its inversion. Meyerson considered the possibility that these market value gains could represent tax savings or other economic consequences not proposed by Lee. Finally, Meyerson considered the tax consequences to Stanley shareholders and wondered if these consequences should figure into his calculations. With this understanding, Meyerson, Stern, and Lee could then decide if an inversion would be the right thing for American HandyWorks to undertake as well.

[12] In the case of large-scale transactions such as the formation of DaimlerChrysler, the merging parties requested private-letter rulings from the IRS prior to executing the merger stating that the transaction would not face scrutiny under these rules.

Exhibit 1 Stanley Works One-Year Annotated Price History



1	2/8/02	Stanley Works announces intention to execute inversion transaction to Bermuda.
2	2/25/02	Announces strategic alliance with Home Depot.
3	4/3/02	Increases analyst guidance figures based on strong retail sales; this and all other earnings estimates exclude the possible impact of re-incorporation in Bermuda.
4	4/11/02	Senate to draft legislation eliminating and reversing inversion transactions.
5	4/26/02	First quarter earnings rose due to cost-cutting measures; results reflected "continuing weak markets."
6	5/10/02	Stanley Works agrees to hold a revote by shareholders after the initial vote only approved the inversion transaction by a very narrow margin above the required two-thirds majority and the Connecticut Attorney General declared the meeting "rife with voting irregularities."

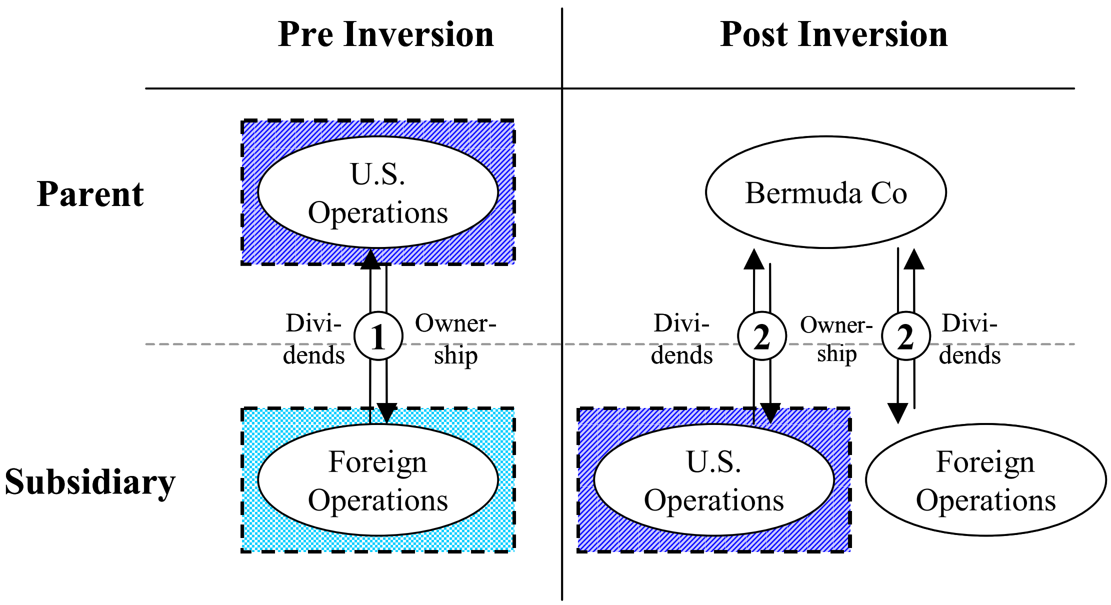
Source: Casewriter.

Exhibit 2 Financial Highlights, The Stanley Works

(Millions of dollars, except per share data)	2001	2000	1999
INCOME STATEMENT			
Net sales	**2,624.4**	**2,748.9**	**2,751.8**
Cost of sales	1,701.3	1,751.5	1,813.9
Selling, general and administrative	593.7	656.6	703.0
Interest-net	25.6	27.1	27.9
Other-net	(5.3)	20.0	(2.5)
Restructuring charges and asset	72.4	-	(21.3)
Total Costs & Expenses	2,387.7	2,455.2	2,521.0
Earnings before income taxes	**236.7**	**293.7**	**230.8**
Income taxes	78.4	99.3	80.8
Net earnings	**158.3**	**194.4**	**150.0**
Net earnings per share of common	1.85	2.22	1.67
SUMMARY STATEMENT OF CASH FLOW			
Depreciation and amortization	82.9	83.3	85.6
Changes in operating assets and liabilities:	(109.3)	(83.7)	(49.7)
Capital expenditures	(73.1)	(64.4)	(102.9)
Asset sales and business acquisitions	(69.5)	14.1	35.1
Proceeds from (payments on) total debt	43.3	27.0	(96.5)
Equity issuance (repurchase)	14.4	(99.7)	(11.4)
Cash dividends on common stock	(80.5)	(78.3)	(77.5)
Effect of exchange rate changes on cash	(7.4)	(9.6)	(5.0)
Increase (decrease) in cash and equivalents	21.6	5.6	(22.1)
BALANCE SHEET			
Cash and cash equivalents	115.2	93.6	
Accounts and notes receivable	551.3	531.9	
Inventories	410.1	398.1	
Property, plant and equipment	494.3	503.7	
Goodwill and other intangibles	236.1	175.9	
Other assets	248.7	181.6	
Total assets	**2,055.7**	**1,884.8**	
Short-term borrowings	177.3	207.6	
Accrued expenses	528.1	493.6	
Long-term debt	316.9	254.8	
Other liabilities	201.1	192.3	
Shareowners' equity	832.3	736.5	
Total liabilities and shareowners' equity	**2,055.7**	**1,884.8**	

Source: Stanley Works Form 10-K.

Exhibit 3 Transaction Schematics—Entities in Affiliated Group Subject to U.S. Taxation



Transaction Summary

1. U.S. parent owns all worldwide operations
2. Bermuda parents owns U.S. and foreign operations separately

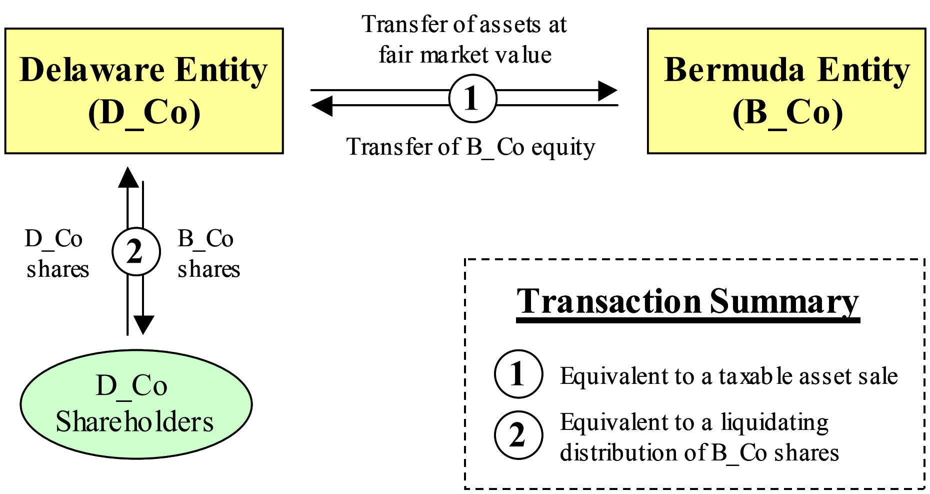
Subject to direct U.S. taxation

Subject to adjusted U.S. taxation (repatriations, foreign tax credits)

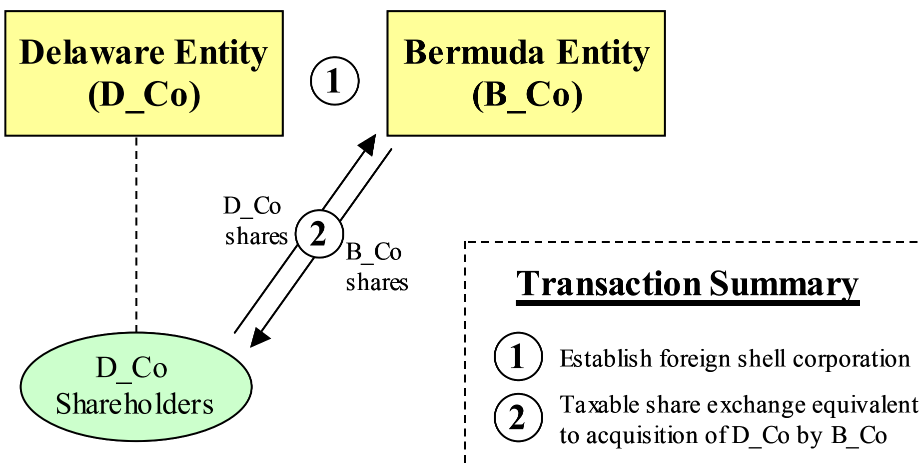
Source: Casewriter.

Exhibit 4 Transaction Schematics—Asset Inversions and Stock Inversions

Asset Inversion



Stock Inversion (aka Taxable Stock Transfer)



Source: Casewriter.

Exhibit 5 Selected Historical Inversion Transactions

Company (Ticker)	Announced	Destination	Transaction Detail	Market Value	Company Description
Mcdermott (MDR)	2/10/1983	Panama	Taxable Stock Transfer	727	Deepwater and subsea oil and gas production facilities
Helen Of Troy (HELE)	12/30/1993	Bermuda	Taxable Stock Transfer	104	Personal care products and accessories
Triton Energy (OIL)	2/8/1996	Cayman	Taxable Stock Transfer	1,945	International oil and gas exploration and production
Chicago Bridge & Iron (CBI)	12/18/1996	Netherlands	Subsidiary IPO	na	Storage tanks, natural gas processing plants
Tyco (TYC)	3/17/1997	Bermuda	Taxable Stock Transfer (M&A related)	9,713	Diversified manufacturer
Santa Fe International (GSF)	6/1/1997	Cayman		na	Offshore drilling
Fruit Of The Loom (FTL)	2/11/1998	Cayman	Taxable Stock Transfer	1,823	Basic and casual apparel
Playstar	5/5/1998	Antigua	F-Reorg.	na	Internet gaming and gambling
Gold Reserve (GLDR)	11/24/1998	Canada	Taxable Stock Transfer	27	Gold mining
Xoma (XOMA)	11/24/1998	Bermuda	Asset	160	Drug developer
Transocean (RIG)	3/15/1999	Cayman	Taxable Stock Transfer [a]	2,539	Offshore drilling
PXRE (PXT)	7/7/1999	Bermuda	Taxable Stock Transfer	223	Re/insurance
Everest Reinsurance (RE)	9/17/1999	Bermuda	Taxable Stock Transfer	1,311	Re/insurance
White Mountain Insurance (WTM)	9/23/1999	Bermuda	Asset	675	Re/insurance
Trenwick (TWK)	12/19/1999	Bermuda	Asset (M&A related)	279	Re/insurance
Applied Power	3/10/2000	Bermuda	Subsidiary Spin-off	na	Enclosures for electronic systems
R&B Falcon (FLC)	8/21/2000	Cayman	Acquired by Foreign Entity	4,906	Offshore drilling
Foster Wheeler (FWC)	11/29/2000	Bermuda	Taxable Stock Transfer [a]	183	Engineering & energy equipment
Cooper Industries (CBE)	6/11/2001	Bermuda	Taxable Stock Transfer	3,551	Electrical products
Global Marine (GLM)	9/4/2001	Cayman	Taxable Stock Transfer (M&A related)	2,667	Offshore drilling
Ingersoll Rand (IR)	10/16/2001	Bermuda	Taxable Stock Transfer	6,719	Tools & machinery
Nabors Industries (NBR)	1/2/2002	Bermuda	Taxable Stock Transfer	4,657	Offshore drilling
Noble Drilling (NE)	1/31/2002	Cayman	Taxable Stock Transfer	4,223	Offshore drilling
Stanley Tools (SWK)	2/8/2002	Bermuda	Taxable Stock Transfer	3,688	Hand- and industrial tools
NON-INVERSION EXPATRIATIONS					
Seagate Technology	4/20/2001	Cayman	"Ab Initio"	na	Hard disk drives
Accenture	7/19/2001	Bermuda	"Ab Initio"	na	Consulting

Source: Compiled by casewriter from Compustat, CRSP, Hoovers, New York State Bar Association, and SEC Documents.

[a] F- or C-Reorganization with drop down.

Exhibit 6 The Stanley Works Notes to Consolidated Financial Statements

Note H: Long-Term Debt and Financing Arrangements

(Millions of dollars)	**Interest Rate**	**2001**	**2000**
Notes payable in 2002	7.40%	100.0	100.0
Notes payable in 2004	5.80%	120.0	120.0
Notes payable in 2007	4.50%	75.0	-
Industrial revenue bonds due in varying amounts to 2010	5.8–6.8%	19.6	19.6
ESOP loan guarantees, payable in varying monthly installments through 2009	6.10%	22.5	27.9
Other, including net swap receivables		(20.2)	(12.7)
Total long-term debt		**316.9**	**254.8**
Less: current maturities		120.1	6.1
Long-term debt		**196.8**	**248.7**

Aggregate annual maturities of long-term debt for the years 2003 to 2006 are $7.1 million, $101.0 million, $2.8 million, and $0.6 million, respectively, and $85.3 million thereafter. Interest paid during 2001, 2000, and 1999 amounted to $33.4 million, $36.1 million, and $30.8 million, respectively.

Source: Stanley Works Form 10-K.

Exhibit 7 The Stanley Works Notes to Consolidated Financial Statements

Note O: Geographic Area

(Millions of dollars)	2001	2000	1999
Net sales			
United States	1,885.2	1,984.0	1,962.5
Other Americas	185.4	203.3	199.0
Europe	456.7	459.3	493.2
Asia	97.1	102.3	97.1
Consolidated	**2,624.4**	**2,748.9**	**2,751.8**
Long-lived assets			
United States	593.5	458.3	442.1
Other Americas	28.5	31.3	28.1
Europe	254.1	266.7	286.3
Asia	38.2	34.2	36.7
Other	-	-	6.4
Consolidated	**914.3**	**790.5**	**799.6**

Source: Stanley Works Form 10-K.

Exhibit 8 The Stanley Works Notes to Consolidated Financial Statements

Note P: Income Taxes

Significant components of the company's deferred tax liabilities and assets as of the end of each fiscal year were as follows:

(Millions of dollars)	2001	2000
Deferred tax liabilities:		
Depreciation	78.0	82.4
Other	5.8	16.4
Total deferred tax liabilities	**83.8**	**98.8**
Deferred tax assets:		
Employee benefit plans	16.5	26.4
Doubtful accounts	10.8	16.1
Inventories	7.7	13.8
Amortization of intangibles	14.7	16.4
Accruals	12.8	13.9
Restructuring charges	14.9	20.7
Foreign and state operating loss carryforwards	21.0	16.1
Valuation allowance	(21.0)	(16.1)
Other	0.8	6.9
Total deferred tax assets	**78.2**	**114.2**
Net deferred tax (liabilities) asset	**(5.6)**	**15.4**

Valuation allowances reduced the deferred tax asset attributable to foreign and state loss carryforwards to the amount that, based upon all available evidence, is more likely than not to be realized. Reversal of the valuation allowance is contingent upon the recognition of future taxable income and capital gains in specific foreign countries and specific states, or changes in circumstances which cause the recognition of the benefits to become more likely than not.

Income tax expense consisted of the following:

(Millions of dollars)	2001	2000	1999
Current:			
Federal	24.1	40.1	25.3
Foreign	19.6	16.7	13.7
State	5.9	7.0	5.6
Total current	**49.6**	**63.8**	**44.6**
Deferred (benefit):			
Federal	33.4	34.7	32.1
Foreign	(7.0)	(2.9)	0.8
State	2.4	3.7	3.3
Total deferred (benefit)	**28.8**	**35.5**	**36.2**
Total	**78.4**	**99.3**	**80.8**

Income taxes paid during 2001, 2000, and 1999, were $41.4 million, $59.7 million, and $22.4 million, respectively.

Exhibit 8 (continued) The Stanley Works Notes to Consolidated Financial Statements

Note P: Income Taxes (continued)

The reconciliation of federal income tax at the statutory federal rate to income tax at the effective rate was as follows:

(Millions of dollars)	2001	2000	1999
Tax at statutory rate	82.8	102.8	80.8
State income taxes, net of federal benefits	5.4	6.7	5.8
Difference between foreign and federal income tax	(15.9)	(7.0)	(4.5)
Other-net	6.1	(3.2)	(1.3)
Income taxes	**78.4**	**99.3**	**80.8**

The components earnings before income taxes consisted of the following:

(Millions of dollars)	2001	2000	1999
United States	212.9	267.5	201.0
Foreign	23.8	26.2	29.8
Total pretax earnings	**236.7**	**293.7**	**230.8**

Undistributed foreign earnings of $62.2 million at December 29, 2001 are considered to be invested indefinitely or will be remitted substantially free of additional tax. Accordingly, no provision has been made for taxes that might be payable upon remittance of such earnings, nor is it practicable to determine the amount of this liability.

Source: Stanley Works Form 10-K.