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Burger King Buys Out Tim Hortons

By Laurence Cromp-Lapierre and Gabrielle Dorais, LL.M Candidates, 2015 | October 10, 2014

On August 26, Burger King Worldwide, Inc. ("Burger King") and Tim Hortons Inc. ("Tim Hortons"), a Canadian-based multinational fast casual restaurant, announced that an agreement was reached under which the two companies would create a new global entity in the quick-service restaurant sector.

Tim Hortons, founded in Ontario in 1964, is best known for its coffee and donuts and is currently Canada's largest fast-food company. Tim Hortons generated more than $3.25 billion in revenues in 2013, so one could argue that it was strategic for both entities to consolidate their strong franchisee networks.

The anticipated transaction, a $12.5-billion merger, will generate combined sales of $23-billion, with more than 18,000 restaurants in 100 countries. It will create the world's third-largest fast-food company. The deal has been unanimously approved by both boards of directors, but remains subject to the ratification of Tim Hortons' shareholders.

The transaction's structure provides that Burger King and Tim Hortons will both be owned by a new entity, an unnamed Ontario-based parent company. The new company will be led by Burger King's current chief executive, Daniel Schwartz, while maintaining each entity's respective headquarters in Miami and Oakville in Ontario. 3G Capital Inc., a Brazilian private equity group that currently owns more than 70% of Burger King, will preserve majority ownership of the resulting entity with a 51% stake. According to the terms of the deal, Tim Hortons' shareholders will receive, for each share, C$65.50 in cash and 0.8025 common shares of the new entity. They could also choose an option to receive either an all-cash payment of C$88.50 or 3.0879 shares in the new company. Shares owned by Burger King's shareholders will be converted into shares comprising 99% of one new entity share and 1% of a unit of an Ontario limited partnership owned by the new parent company created by the transaction.

This cross-border transaction is viewed as a tax or corporate inversion. Because the U.S. government imposes taxes on American companies' revenues generated abroad, tax inversion transactions can be key to avoid double taxation. The mechanics behind a tax inversion is fairly simple: an American company relocates its headquarters to a country where its business is taxed at a lower rate while still conducting its operations from the United States.

Numerous politicians have condemned the rising popularity of tax inversions. On September 22, 2014, the U.S. Department of Treasury released an action plan to rein in corporate tax inversions and is pressing Congress to pass legislation. Such legislation would prevent former owners of a U.S. entity from owning more than 80% of the merged entity and prevent inverted companies from accessing a foreign subsidiary's earnings while deferring U.S. taxes through the use of creative loans.

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These new measures are unlikely to endanger the Burger King/Tim Hortons merger. In fact, given 3G Capital's 51% ownership in the novel entity, the 80% threshold would not impede the deal. Further, Tim Hortons has sufficient cash flow to fund the transaction, which may render the new rules on cross-boarder inter-company loans inapplicable.

In addition, characterizing this deal as a 'tax dodge' is too restrictive. In the current financial context, in order to grow and acquire a predominant place in a global market, companies must be strategic and flexible, and willing to expand in foreign countries. Although the Burger King/Tim Hortons merger is advantageous from a tax perspective, one of the main purposes of this deal is for these two companies to position themselves as global leaders in the food industry. As Alex Behring, Executive Chairman of Burger King and Managing Partner of 3G Capital, mentioned, "By bringing together our two iconic companies under common ownership, we are creating a global QSR [quick-service restaurant] powerhouse. Our combined size, international footprint and industry-leading growth trajectory will deliver superb value and opportunity for both Burger King and Tim Hortons shareholders, our dedicated employees, strong franchisees, and partners."

Despite the fact that the transaction is still subject to approval by Tim Hortons' shareholders as well as Canadian and American regulatory authorities, the parties expect the deal to close by the end of year or in early 2015. It will be interesting to see whether, in the upcoming months, governmental officials will attempt to prevent the closing of this specific deal and/or future similar transactions.