

Experts expect corporate tax inversions to survive new rules

6 April 2016, by Tom Murphy

President Obama scored a victory this week when Pfizer scrapped a \$160-billion overseas deal that would have kept a chunk of the drugmaker's profits beyond the U.S. tax man's reach.

But recent, aggressive federal actions that discouraged Pfizer Inc.'s combination with another drugmaker, Allergan PLC, won't stop all so-called inversions, or deals that end with a company relocating to another country—at least on paper—and trimming its U.S. tax bill in the process.

Tax and legal experts say these deals, which have come under growing criticism from politicians, will remain attractive to some companies until the U.S. pursues a massive tax law overhaul.

"There may be a temporary respite from inversions, but the large financial benefits ... are still there," said Bret Wells, a tax lawyer and law professor at the University of Houston.

Even the Obama administration, which has taken several steps to discourage inversions in recent years, says Congress ultimately must step into this fight.

In an inversion, a U.S. corporation and a foreign company combine into a parent company based in the foreign country. For tax purposes, the U.S. company becomes foreign-owned, even if all the executives and operations stay in the U.S.

Inversions have become particularly popular in health care. They allow companies to avoid paying additional taxes that the U.S. government would impose on money earned overseas and then transferred back to the parent. They can reduce corporate tax liability in other ways, and they provide some relief from the U.S. corporate tax rate of 35 percent, which is the highest in the industrialized world.

But Obama and others have said these deals

shortchange the country because corporations fail to pay their fair share of taxes.

Earlier this week, the Treasury Department announced a third round of regulations designed to limit the practice and make it less lucrative for companies. The new regulations seek, among other things, to limit inversion benefits like tax deductions that can stem from internal corporate borrowings.

Pfizer cited the new regulations in scuttling its deal.

These rules will make it harder for U.S. companies to find a foreign deal partner, said Donald Goldman, a professor at Arizona State University's W.P. Carey School of Business. He added that the regulations "will definitely have a chilling effect on inversions."

They actually will come close to killing the practice, according to Robert Willens, president of a New York-based tax and accounting service and a former Lehman Brothers managing director.

But he said some narrowly tailored deals that have the right balance of U.S. and foreign ownership should survive. He cited as an example the pending \$14.6 billion combination of Milwaukee-based Johnson Controls Inc. and Ireland's Tyco International, companies that make security and other building control systems.

Johnson Controls spokesman Fraser Engerman said the company was reviewing the new Treasury regulations and wouldn't speculate on what impact they might have on the Tyco deal.

At least one company that has already completed an inversion isn't having second thoughts. Medical device maker Medtronic PLC, which completed a nearly \$43 billion combination with Ireland's Covidien last year, said Wednesday that it has done a preliminary review of the Treasury rules and

concluded that they do not have a material financial impact on the company.

Treasury Secretary Jacob Lew has said the new rules are designed to make inversions less economically beneficial for companies, but only anti-inversion legislation from Congress can stop the transactions.

Leaders in the Republican-controlled Congress say the issue underscores the need for comprehensive tax reform, but such a massive undertaking is unlikely in an election year that also is the last year of Obama's presidency.

"We really need to scrub the whole code," Senate Majority Leader Mitch McConnell, R-Ky., told reporters on Tuesday. "The chances of doing a [tax](#) reform this year are pretty slim."

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APA citation: Experts expect corporate tax inversions to survive new rules (2016, April 6) retrieved 29 September 2022 from <https://phys.org/news/2016-04-experts-corporate-tax-inversions-survive.html>

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