Medtronic Adds to Inversion Fears

By Robert W. Wood • Wood LLP • San Francisco

Medtronic has agreed to buy Covidien for $42.9 billion in cash and stock. Medtronic is the world's largest stand-alone medical device maker, selling pacemakers, defibrillators and stents. Covidien makes devices used in surgical procedures, such as surgical staples, feeding pumps and ventilators. Medtronic is going out of its way to downplay the inversion deal, an astute move after Pfizer's failed attempt to merge with AstraZeneca.

Medtronic said operational headquarters would remain in Minneapolis. It even pledged $10 billion in U.S. technology investments over 10 years. Still, it's clear executive offices will be in Ireland, saving taxes.

Medtronic Chief Executive Omar Ishrak said Medtronic's corporate tax rate will remain around 18 percent. However, Medtronic is holding more than $14 billion in cash, most of it outside the U.S. since it does not pay taxes until it brings profits back. That and other facts make the tax aspects of this deal huge.

Two recent inversion attempts failed. One was Pfizer's bid for Britain's AstraZeneca, and the other was Omnicom Group's grab for France's Publicis Groupe. Inversions do not cut taxes on pure U.S. earnings, but can shield income around the world from the high 35-percent U.S. corporate tax rate.

U.S. tax law started cracking down on inversions a decade ago, yet a foreign partner can be alluring. It may not be hard to ensure that more than 20 percent of the post marriage combination is owned by foreigners. Code Sec. 7874 already covers these deals, but is complex and has failed to work.

Now, Congress could change the 20-percent rule to a whopping 50 percent. That would make sure a foreign company would have to really and truly be the controlling buyer. Ron Wyden, chairman of the Senate Finance Committee, said the Medtronic deal underscores the urgent need to pursue corporate tax reform. But so far legislative efforts to deter inversions have not gained much traction.

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