

BENEFITS-RELATED TAX STRATEGY PATENTS

Commentary on the Patent Reform Act of 2007

Issued Patents and Patent Applications

Editor's Note: This section is a regular feature of the Compensation Planning Journal and was first included in the May 4, 2007 issue (Vol. 35, No. 5) along with a lead article entitled "Tax Strategy Patents — Policy and Practical Considerations," by Charles F. Wieland III, Esq. and Richard S. Marshall, Esq. (both with Buchanan Ingersoll & Rooney PC) as an introduction to this topic. In this issue, this section includes a list of both the patents issued and the patent applications pending that appear to involve benefits-related tax strategies. Please note that the lists in this issue include only a brief description of the patents and patent applications. For a more detailed summary of the patents issued, please see the May 4, 2007 issue, and for the patent applications pending, please see the June 1, 2007 issue. (See the August 3, 2007 issue for patent application 20070055605, and the September 7, 2007 issue for patent applications 20070185799, 20070185800, 20070185801, 20070185802 and 20070185803.) This section will also periodically include a more detailed analysis of a patent that has been issued or that is currently pending with the U.S. Patent and Trademark Office.

As of April 3, 2007, the U.S. Patent and Trademark Office had classified 53 patents and 84 published patent applications that deal with tax strategies. The number of actual tax strategy applications may, however, significantly exceed these published for several reasons. Many applications may not have been published and are being maintained in confidence because they were filed before publication of patent applications became part of the patent law in 1999. In addition, applications that have been filed in the last 18 months would not yet have been published. Furthermore, applicants may elect not to have their applications published in the U.S. if they do not file applications outside the U.S., which predictably would be the case with respect to tax strategies involving U.S. laws. Finally, the U.S. Patent and Trademark Office's classification covers, in essence, only computer-implemented tax strategies, and therefore, it is unclear whether there are other patent applications directed to non-computer-implemented tax strategy-based processes.

The tax strategy patents and patent applications summarized below include only those that have been granted to date and published by the U.S. Patent and Trademark Office and that appear to be benefits related. Readers who wish to review the entire list of tax strategy patents can do so at the following U.S. Patent and Trademark Office website: http://www.uspto.gov/patft/class705_sub36r.html.

Commentary on the Patent Reform Act of 2007

On September 7, 2007, the U.S. House of Representatives passed the Patent Reform Act of 2007 (H.R. 1908), which includes a provision that would prohibit the granting of tax strategy patents. Patent reform legislation is currently stalled in the U.S. Senate for reasons other than the tax strategy patent issues. Provided below is commentary by Marcia S. Wagner, Esq., of The Wagner Law Group, on the House version of the bill.

The House Tax Patent Provision is Naked

by Marcia S. Wagner, Esq.¹

In the classic story, "The Emperor Has No Clothes," all agree that the clothes made for the emperor by two frauds are beautiful until a small child states that the emperor is naked. Reporters have posted stories about the current patent provision in the House-passed bill stating its approval by the AICPA, the Texas Bar Association and a senior official in the Treasury Department. This article will show that, despite such reported approval, this provision is either extremely sloppy, disingenuous or both.

The current definition of "tax planning method" in the House-passed patent bill would result in undercutting all patents, even those that have nothing to do with tax planning. This is because the definition of "tax planning

¹ Marcia S. Wagner is the principal of The Wagner Law Group, an ERISA/employee benefits boutique law firm in Boston, MA. Ms. Wagner has practiced law for 20 years and specializes in ERISA/employee benefits.

BENEFITS-RELATED TAX STRATEGY PATENTS

method" includes "a plan, strategy, technique, or scheme that . . . has, when implemented, the effect of reducing, minimizing, or deferring, a taxpayer's tax liability." If this provision is read literally (as many courts do read federal law) this would encompass virtually all commercially successful patents, as each of them has such an effect.

Any commercially successful product or technique that provides a competitive advantage would result in lower sales, profits and taxes for competitors. For example, any more efficient means of selling or producing goods or services would lower sales tax receipts and would presumably not be patentable if this legislation passed. Another example is a more efficient automobile which would result in lower taxes for fuel and could not be patented under the House bill provision.

Even if this provision were read more narrowly to require that a tax provision specifically address or be related to the technique, it would still be problematic. This is because, after a patent application is required to be disclosed and while it is still pending, a competitor of the inventor (e.g., a generic drug manufacturer) could hire a lobbyist to urge that Congress enact a minimal tax credit (e.g., one cent for every 1,000,000 pills) for manufacturers using the techniques disclosed in the patent application. If the lobbyist were successful, under the provision as drafted, a patent could then not be obtained for the new drug, as utilization of the technique would reduce a taxpayer's liability.

Therefore, the effect of any provision attempting to ban "tax patents" should be limited to tax planning methods which have as their primary purpose the reduction, minimization or deferral of taxes. This would prevent its application to inventions that could affect tax liability if such effect is not the primary purpose of the invention such as, for example, a new technique for manufacture qualifying for a tax credit for research and development. Revising the definition so that only "tax planning methods" that meet a common sense meaning of that definition (i.e., those that have as their primary purpose the reduction, minimization or deferral of taxes) are affected would avoid this result.

Also, it is important to address use of tax legislation to game the system utilizing tax provisions passed well after a patent application has been filed. A bill banning tax patents should provide that tax legislation enacted after a patent application is required to be published cannot affect such an application, or, at the least, that tax legislation that has not been favorably referred by at least one committee of jurisdiction (currently Ways and Means in the House and Finance in the Senate) by the time a patent application is published can not affect that patent. This would preclude attempts to game the system by defeating competitors' innovations through lobbying tax committees after the specifics of the invention have been publicly disclosed.

We have assumed that the intent is to limit the prohibition to those affecting federal taxes. Extending it to all taxes would present severe practical problems due to the number of sources of taxing systems (e.g., local and foreign). If extended, it should be limited to the state level and only in conjunction with limiting the definition of "tax planning method" as discussed above. Further, the limitation should only be applicable in cases in which the law or legislation has been placed in an easily searchable data base, so that the problem of searching for tax patents now faced by tax practitioners is not simply transferred to inventors.

Finally, the problems with this provision support a conclusion that the House bill addressing patents was rushed through without appropriate consideration. This is particularly the case given the importance assigned to laws addressing intellectual property by notables such as Alan Greenspan. If this provision is indicative of the care taken with respect to the remainder of the bill, the House leadership should be embarrassed.

Issued Benefits-Related Tax Strategy Patents

- **United States Patent:** 6,963,852
Granted: November 8, 2005
Inventor: Koresko, V; John J.
— System and method for creating a defined benefit pension plan funded with a variable life insurance policy and/or a variable annuity policy.

- **United States Patent:** 6,766,303
Granted: July 20, 2004
Inventor: Marshall
— Method for hedging one or more liabilities associated with a deferred compensation plan.