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Comment

*53 A LICENSE TO DONATE: PATENTS, TAX LAW, AND THE AIDS EPIDEMIC

Robert M. Kane, Jr. [FNa1]

I. Introduction

In 2007, 2.3 million adults became infected with the Human Immunodeficiency Virus ("HIV"), bringing the total number of people infected with HIV worldwide to 33 million. [FN1] Annually, millions of HIV victims die from AIDS. [FN2] Twenty-five million people have died of AIDS since the beginning of the epidemic. [FN3] National security experts note the AIDS epidemic has the potential to create numerous failed states. [FN4] The United States government has made combating the AIDS epidemic a priority goal, with its moral imperative to help people and its desire to prevent the creation of failed states. [FN5] However, Congress is not doing everything that it can in ***54** order to successfully combat the AIDS epidemic.

United States tax law concerning patent donations hamstrings the government's ability to combat the AIDS epidemic. Pharmaceutical companies have developed AIDS-treatment drugs that will extend the life of AIDS victims. [FN6] However, AIDS victims in poor countries cannot afford these drugs. [FN7] In order to combat the AIDS epidemic in these countries, it is necessary to change our tax laws to encourage corporations to donate medical and pharmaceutical patents [FN8] and licenses to use patents. [FN9]

When a corporation donates money to a non-profit organization, section 170 of the Internal Revenue Code ("the Code") allows a tax deduction equal to the amount of the money donated. [FN10] If a company donates a laptop, furniture, or uniforms, it is permitted to take a tax deduction equal to the fair market value of the property contributed. [FN11] However, if a pharmaceutical company donates a patent for an AIDS-treatment drug, it is only allowed to take a tax deduction equal to the lesser of the fair market value of the patent or its tax basis in the patent. [FN12] As the tax basis in a patent is usually zero, [FN13] this often results in a patent donor receiving no tax deduction for the donation. [FN14] While a deduction is possible for patent donations, the Internal Revenue Service ("the Service") prohibits any tax deduction for the donation of a license to use a patent. [FN15] Thus, if a pharmaceutical company donates a license to use a patent of an AIDS-treatment drug, it will not receive a tax deduction. [FN16]

***55** Prior to 2004, section 170 of the Code allowed a fair market value tax deduction for the donation of a patent. [FN17] However, a belief that corporations were abusing the tax deduction for patent donations prompted Congress to pass the American Jobs Creation Act of 2004 ("AJCA") to remove the fair market value tax deduction. [FN18] The loss of the fair market value deduction removes an essential incentive to encourage corporations to donate patents to non-profit organizations. [FN19] Without an immediate economic incentive, corporations will not donate patents or licenses to use patents. [FN20] Thus, this change in United States tax law

hampers the government's ability to combat the AIDS epidemic.

In order to help combat the AIDS epidemic that is plaguing the world, [FN21] this comment proposes amending the Code to allow a corporation to receive a fair market value tax deduction for donations of patents and licenses to use patents. The fair market value tax deduction will encourage pharmaceutical companies to donate patents and licenses to non-profit organizations. [FN22] Donations of licenses to use patents will ensure that AIDS victims in countries that cannot afford drug treatment are able to receive vital, life-extending drugs. [FN23] The fair market value tax deduction for patent donations will encourage companies to donate medical patents, for which they do not have a profitable use, to non-profit organizations and universities who might be able to utilize the patent to develop drugs and medical technologies. [FN24]

This comment also proposes that Congress create a Science Advisory Council charged with determining which patent and license donations are entitled to receive the fair market value tax deduction. Donors would only receive a deduction for licenses or patents that are in the public's best interest. The Science Advisory Council will focus on patents and licenses that can be used to help save lives, reduce ***56** incapacitated workforces due to illness, and develop medical technologies. [FN25] The Science Advisory Council will ensure that the abusive donations that occurred prior to the AJCA's enactment are not repeated.

Prior case law should be utilized to create a framework to determine the fair market value of a patent or license. This comment will use the handful of cases that have decided the value of patents to establish common factors that the courts have relied on in valuing patents. [FN26] These common factors will be the framework with which donors can value their patents and licenses. Until Congress or the Service provide more guidance regarding valuation, prior case law affords the best opportunity to value patents and licenses.

Section II of this comment provides an overview of the history of patent donations, including a discussion of the cases relating to patent valuation. Section III discusses the three proposals of this comment: (1) the creation of a fair market value tax deduction for donations of patents and licenses to use patents; (2) the creation of the Science Advisory Council; and (3) the development of a framework to determine the value of patents and licenses.

II. Overview

A. Tax Law for Patent Donations

1. History of Patent Donations

Section 170 of the Internal Revenue Code (“the Code”) allows an individual or corporation to take a tax deduction when it donates property to a qualified non-profit organization. [FN27] The amount of the tax deduction may be as much as the fair market value of the property. [FN28] In 1958, the Internal Revenue Service (“the Service”) issued Revenue Ruling 58-260, which stated that a donation of an undivided interest in a patent is allowed a tax deduction equal to the fair market value of the patent. [FN29]

In 1992, Arthur Andersen published a study that promoted patent donations as a new way to financially benefit corporations. [FN30] Corporations and their consultants realized the tax benefits they could reap by donating “orphan patents.” [FN31] “Orphan ***57** patents” are generally considered patents which are not consistent

with a corporation's core technologies or mission, are not appropriate for licensing to third parties, and have no value for "defensive purposes" [FN32] in competitive markets. [FN33] Andersen's report led to a dramatic increase in the number of patents donated by corporations. [FN34] Universities were the primary recipients of corporate patent donations. [FN35]

However, some companies abused the donation policy by excessively inflating the values of their patents prior to donation in order to claim a larger tax deduction. [FN36] SBC Communications was accused of claiming a $7.3 million tax deduction for donating a worthless patent to the University of Texas. [FN37] One industry expert claimed that this "patent stinks like a dead cow in the Houston shipping channel on a hot summer day." [FN38] Some companies abused the system by claiming millions of dollars in tax deductions for donating patents to universities that did not have the equipment to utilize the patent. [FN39] AlliedSignal donated a patent to the University of Virginia for specialty aluminum alloys, valued at more than $7 million. [FN40] However, the university lacked the equipment to produce the alloys and subsequently forfeited the patent to avoid paying thousands of dollars in maintenance fees. [FN41]

2. The Service Responds to Overvaluation of Patents

By the end of 2003, the Department of Treasury ("the Treasury") and the Service came to believe that companies were taking deductions for donated patents that "significantly exceeded the actual value of such donations." [FN42] Service officials ***58** declared that "hundreds of millions of dollars of deductions for potentially overvalued patent donations" would be reviewed. [FN43] In one example, the Service challenged the valuation of a patent where the donor claimed a tax deduction of $22.4 million. [FN44] The company accepted the Service's determination that the value of the patent was approximately $15 million. [FN45] The company overvalued its patent, which would have resulted in an additional $7 million of tax deductions for the company at the Treasury's expense.

The Service believed one cause of the overinflated valuations was that corporations did not take into account the existence of other similar innovations or restrictions placed on the donee's use of the patent when they calculated the patent's fair market value. [FN46] The existence of a patent for a similar innovation creates product competition and patent validity issues that may decrease the value of a patent. [FN47] Additionally, restrictions placed on a donated patent reduce the value of the patent because the donee is not allowed to use the patent as it wishes. [FN48]

In response to these valuation concerns, the Service issued Revenue Ruling 2003-28, which requires patent donors to factor any restrictions on the donee's use of the patent into the fair market value of the donated patent. [FN49] In 2004, the Service issued Notice 2004-7, which lists only three factors that must be taken into account when determining the fair market value of a patent. [FN50] These factors include "(1) whether the patented technology has been made obsolete by other technology; (2) any restrictions on the donee's use of, or ability to transfer, the patented technology . . . and (3) the length of time remaining before the patent's expiration." [FN51]

Commentators criticized Notice 2004-7 as providing "little guidance on the proper method of computing a patent's fair market value." [FN52] The factors listed in Notice 2004-7 were "negative factors," which only provided instances in which the value of a patent should be reduced. [FN53] Notice 2004-7 did not provide any guidance ***59** on how a company could determine the fair market value of their donated patent. [FN54] Many commentators claimed the Service's failure to create a standard framework within which to determine the fair market value of a patent was a cause of the abusive overvaluations. [FN55] The lack of an articulated framework

for valuing a patent, however, became moot with the passage of the American Jobs Creation Act ("AJCA"). [FN56]

3. Congress Responds to Abusive Deductions for Patent Donations

By 2003, Congress became concerned with corporations taking abusive and excessive tax deductions for donated patents. [FN57] Senator Chuck Grassley, former Chairman of the Senate Finance Committee, commented that corporations have reduced "their tax bills by hundreds of millions of dollars each year" by donating intellectual property of "little or no value" to charities. [FN58] Legislative responses were proposed to help combat abusive tax deductions taken on donated patents. [FN59] These proposals would have created safeguards to stop abusive valuations of patents, while still allowing a fair market value deduction. [FN60] For instance, House Resolution 3837 would have required the donor to obtain a qualified appraisal of the fair market value of the patent and disclosure of the contribution on the donor's income tax return. [FN61] The resolution also would have allowed the Treasury to prescribe valuation methodologies for valuing patents. [FN62]

Ultimately, Congress passed the AJCA. [FN63] Section 882 of the AJCA amended section 170 of the Code to limit the amount of the immediate tax deduction for the ***60** donation of a patent to the lesser of the fair market value of the patent or the taxpayer's basis in the patent. [FN64] Section 882 of the AJCA permits the patent donor to take additional tax deductions in future taxable years. [FN65] The additional tax deductions are based on the net income earned by the donee that is allocable to the donated patent. [FN66] The net income for the taxable year is reduced by a decreasing-sliding scale over the legal life of the patent. [FN67] The scale limits the additional deduction to 100% of the net income allocable to the patent in year one decreasing down to 10% of the income in year twelve. [FN68] The additional increases are deductible only to the extent that the aggregate amount of the increases exceeds the amount of the original tax deduction taken for the donation. [FN69] To be permitted to take the additional deductions, the donor and donee must comply with certain reporting requirements. [FN70]

4. Problems with Post-AJCA Tax Law Concerning Patent Donations

Many commentators argued the AJCA will cause corporations to stop donating patents. [FN71] A taxpayer's basis in internally-developed patents is usually close to zero since expenditures used to create patents are often deducted as incurred. [FN72] Commentators have noted that since the AJCA limits the immediate deduction to the lesser of the fair market value of the patent or the taxpayer's basis in the patent, the ***61** immediate tax deduction will almost always be zero, or very close to it. [FN73]

Commentators viewed the "income deduction approach" utilized by the AJCA as an inadequate incentive. [FN74] Potential future deductions will not be substantial, as it may take a non-profit organization years to derive any income from the patent. [FN75] At that point, the decreasing sliding-scale will further reduce the amount of the deduction the donor can take based on the income earned by the donee. [FN76] Furthermore, the "income deduction approach" imposes heavy record-keeping burdens on the donor and donee. [FN77]

Finally, because the "income deduction approach" does not "properly" value patents, it does not create an incentive for corporations to donate patents. [FN78] This approach bases the value of the deduction on the amount of income earned by the donee, not the fair market value of the patent. [FN79] However, a non-profit organization that receives a patent for an AIDS-treatment drug will not want to sell the drug to AIDS victims for a profit. [FN80] The non-profit organization will want to donate the drugs to AIDS victims. Since the donee will not receive income from donating the drugs, the donor will not receive a tax deduction. [FN81] Therefore, the

"income deduction approach" does not encourage corporations to donate patents. [FN82]

Prior to the AJCA, section 170 of the Code "provided a means that encouraged donation and promoted progress" through the fair market value tax deduction. [FN83] The common reaction among corporations is that no patent donations will be made ***62** without an "immediate economic incentive." [FN84] The loss of the fair market value tax deduction was compared to changes made to the tax law in 1969 that "removed all incentives for artists and authors to contribute their works to charity, and as a result, charitable donations by artists and authors have disappeared." [FN85] Commentators also noted the fair market value tax deduction minimized the need for direct government subsidies to those organizations benefiting from patent donations. [FN86]

Society is the "ultimate benefactor" of patent donations. [FN87] The AJCA amended section 170 of the Code to replace the immediate fair market value tax deduction for patent donations with gradually decreasing deductions over a twelve year period based on the income of the donee attributable to the patent. [FN88] The reduced tax deduction will discourage pharmaceutical companies from donating patents that could potentially lead to a medical break-through. [FN89]

B. Disallowance of Deduction for Donation of Licenses to Use Patents

While Congress permits a minimal tax deduction for patent donations, Congress does not allow tax deductions for donations of licenses to use patents. [FN90] The Service issued Revenue Ruling 2003-28, which states that no tax deduction is allowed for the donation of a license to use a patent. [FN91] Withholding a tax deduction for the donation of a license to use a patent removes a vital incentive for corporations to donate licenses to use patents that serve the "public good." [FN92] Thus, the tax law discourages pharmaceutical companies from donating licenses to use their AIDS-treatment drug patents to non-profit organizations.

If a pharmaceutical corporation believes a patent might have a profitable application in the future, then the corporation will donate only a license to use the patent, not its entire interest in the patent. [FN93] Corporations will be loath to donate ***63** their full rights in a patent only to end up being sued for patent infringement by the donee if the company later finds a profitable use for the patent. [FN94] Corporations might conclude that it is not in their best interest to donate a patent, and thus consider donating only licenses to use patents. However, corporations might further conclude that without a tax deduction they do not have any incentive to donate licenses to use patents.

A hypothetical example is useful to illustrate the effect Revenue Ruling 2003-28 has on the donation of licenses to use patents. Assume Company A is a pharmaceutical company that has developed an AIDS-treatment drug that will help to prolong the lives of AIDS victims. [FN95] Swaziland is a country in southern Africa with an adult population that has an AIDS infection rate of 38.8%. [FN96] Since the gross domestic product per capita is $4,800, [FN97] Company A might decide they cannot profitably sell the drug to Swaziland consumers at a price that the consumers would be able to afford. [FN98] As an AIDS drug is potentially very profitable, [FN99] Company A would not be willing to donate its patent, and thus forgo the revenue to recoup its expenditures to develop the drug. [FN100] However, Company A might be willing to donate a license to use its patent, licensing a non-profit organization to distribute its AIDS-treatment drug solely to citizens of Swaziland. Currently, under Revenue Ruling 2003-28, Company A would not be entitled to receive any tax deduction for its donation of a license to use a patent. [FN101]

It is unlikely that a pharmaceutical company will donate a patent on a profitable drug because it needs to sell

the drug to recover the expenses it incurred to develop the patent. [FN102] Donations of drug patents are most likely to lead to drug designs or technologies that may one day in the future create a medical break-through. [FN103] ***64** However, the AIDS epidemic is devastating the world now. [FN104] In order to help combat the current AIDS crisis, Congress needs to provide an incentive to encourage corporations to help now. By not allowing a fair market value tax deduction for the donation of a license to use a patent, the government is missing an opportunity to create an incentive for pharmaceutical companies to take the one plausible action they can: donating licenses to use their AIDS-treatment drugs. [FN105] Thus, the key for transferring corporations' AIDS-treatment drugs to AIDS victims [FN106] is through donations of licenses to use patents.

C. Prior Case Law Concerning Patent Valuation

"Patent valuation is tough." [FN107] Congress and the Service have given little guidance on patent valuation. [FN108] Until Congress or the Service provides a framework for valuing patents and licenses, [FN109] prior case law is the best authority for donors to rely on to value their patents. [FN110]

There are three methods commonly used to value patents: the market method, cost method, and income method. [FN111] The market method values patents based on the prices at which comparable patents were sold around the valuation date. [FN112] The cost method bases valuation on the "costs necessary to re-create" the patent. [FN113] The income method values a patent based on the present value of the future income that the patent will produce. [FN114] Commentators have noted the income method is the superior method for valuing patents because, unlike the market method, it does not need to compare the patent to other similar patents. [FN115] Furthermore, it values patents ***65** based on future earnings while the cost method focuses on historical costs. [FN116] Courts most commonly use the income method in determining patent valuations. [FN117]

Only one case has specifically addressed the valuation of a donated patent. [FN118] In Smith v. Comm'r, the petitioner donated four patents to Santa Clara University. [FN119] The petitioner claimed a tax deduction of $208,642 for the patents. [FN120] The Service disallowed the deduction, arguing the patents had a fair market value of zero on the date contributed. [FN121] Both parties submitted valuation appraisals to the court. [FN122] The appraisal submitted by the Service included such factors as: (1) the potential market of products attributable to the patent, (2) anticipated market penetration, (3) unit cost of the products, (4) a reasonable royalty rate, (5) patent validity, and (6) technological feasibility of developing products from the patent. [FN123]

The court endorsed the factors used by the Service's appraiser to value the patent, as well as noted any "factor which affects what a willing purchaser will pay is relevant for determining fair market value." [FN124] The court also noted that "difficulty of enforcement and potential litigation" are relevant factors. [FN125] The court held the value of the patents was $4,500, thus the petitioner could only take a tax deduction for that amount. [FN126] In Podd v. Comm'r, the Tax Court endorsed the factors listed in Smith v. Comm'r to determine the fair market value a purchaser would pay for a license to use a patent. [FN127]

While Smith is the only case to rule on the valuation of a donated patent, other cases have determined the fair market value of a patent. [FN128] While the courts have used various factors to determine the value of a patent under the income method, there is a common core of factors utilized by the courts. The common factors articulated by the courts include: potential market for products produced from the patent, [FN129] anticipated market penetration of the products, [FN130] net profit from expected ***66** sales of products created by the patent, [FN131] patent validity, [FN132] royalty rates paid by other users of the product, [FN133] and any other "factor which affects what a willing purchaser will pay" for the patent. [FN134] These cases provide taxpayers with ju-

dicial precedents for factors to use to value patents.

III. Discussion

This comment proposes changes to the current tax law in order to encourage companies to donate patents and licenses to non-profit organizations. Part A proposes amending the Internal Revenue Code ("the Code") to allow a fair market value tax deduction for patent donations that are approved by the Science Advisory Council. Part B proposes amending the Code to allow a fair market value tax deduction to donors of licenses to use patents that are approved by the Science Advisory Council. Part C develops a framework for valuing patents and licenses for purposes of the tax deduction that is based on prior judicial decisions.

A. Fair Market Value Tax Deduction for Donations of Patents & Science Advisory Council

Section 170 of the Code should be amended to allow a donor of a patent to receive a tax deduction equal to the fair market value of the patent if the donation is approved by the Science Advisory Council (discussed infra). [FN135] Amending the Code to allow a fair market value tax deduction for a patent donation approved by the Science Advisory Council will give corporations an immediate economic incentive ***67** to donate patents. [FN136] Increasing patent donations will allow non-profit organizations to utilize patents in order to develop products that will promote medical progress.

Along with the public goodwill generated by a donation, the tax benefits of a fair market value deduction might make patent donation a more attractive option than selling the patent. [FN137] A pharmaceutical company may not have a profitable use for one of its patents, but perhaps a non-profit organization will be able to use the patent to develop products to help treat AIDs victims. [FN138] Without a fair market value tax deduction, however, corporations will not donate patents. [FN139]

Congress should give the Secretary of the Treasury and Secretary of the Department of Health & Human Services the authority to create the Science Advisory Council, and to appoint members to it. [FN140] The primary purpose of the Science Advisory Council will be to help fight the AIDS epidemic and other health issues. The Science Advisory Council will use the Art Advisory Panel as a model. [FN141] Like the Art Advisory Panel, the Science Advisory Council will consist of twenty-five members and be composed of experts in the field. [FN142] The members will be doctors, hospital administrators, pharmaceutical companies, non-profit organizations, and patent experts.

The Science Advisory Council will determine if the patent or license donation to a particular non-profit organization is in the public's best interest. The Science Advisory Council will use the following factors to determine if a patent donation is in the public's best interest: (1) the cost of the tax revenue forgone by the Treasury, (2) the likelihood the patent will lead to products that fight diseases and improve ***68** public health, (3) the donee's capability to successfully develop the patent to create medicines or medical products, (4) the donee's intent to donate the products of the patent to those in need, and (5) the patent's potential to lead to products that will protect America's national interests. If the Science Advisory Council determines it is in the public's best interest for the patent to be donated, then it will approve the donation, and the donor will receive a tax deduction in the amount of the fair market value of the patent. [FN143]

The Science Advisory Council will address and mitigate the risks that led to abusive patent donations. One

critique of the fair market value tax deduction prior to the American Jobs Creation Act ("AJCA") is that companies abusively inflated the value of their patents to claim a higher tax deduction. [FN144] However, requiring companies to obtain approval from the Science Advisory Council in order to receive a tax deduction will act as a form of deterrence. [FN145] This will allow the Internal Revenue Service ("the Service") to be aware of the deductions claimed by companies and which patents each company specifically claimed for the deduction. [FN146] This disclosure will discourage companies from claiming abusive tax deductions as they know the Service will be aware of the specific patent they donated. [FN147]

Another critique of the pre-AJCA fair market value tax deduction is that a patent might have value, but without the proper equipment and technology to develop the patent, the patent will be worthless in the donee's hands. [FN148] The Science Advisory Council will mitigate this risk by determining that the donee has the proper technology to successfully utilize the patent. [FN149] A donee without the equipment to utilize the patent diminishes the public's value in having the patent donated, and thus ***69** the donor should not receive a fair market value deduction. [FN150]

Commentators have criticized the fair market value tax deduction, noting that corporations only donate patents that are "incapable of being immediately used or licensed." [FN151] Therefore, it would be unnecessary to give a fair market value deduction because a deduction that covers the transaction cost of the donation is sufficient to motivate corporations to donate patents. [FN152] However, the fact that a patent is "incapable of being immediately used" by a corporation does not necessarily mean the patent is valueless. [FN153] Although a patent might not be capable of being used today, it might lead to a medical break-through tomorrow. Since the patent will be donated to a non-profit organization, the public will benefit from any technologies unlocked by the patent.

B. Fair Market Value Tax Deduction for Donations of Licenses to Use Patents

Section 170 of the Code should be amended to allow a donor of a license to use a patent to receive a tax deduction equal to the fair market value of the license if the donation is approved by the Science Advisory Council. However, any restriction on the use of the license will affect the fair market value of the license, and thus affect the amount of the tax deduction. [FN154]

Amending the Code to allow a fair market value tax deduction for the donation of a license to use a patent will result in more licenses being donated to non-profit organizations. [FN155] It is against the nature of a corporation to donate their entire interest in a patent that is or has the potential to be profitable. [FN156] Even if a patent was deemed to be unprofitable, a corporation may want to retain it in case they later find a profitable use for the patent. [FN157] However, a pharmaceutical company might be willing to donate to a non-profit organization a license to use their patent that is ***70** geographically restricted to countries in which they do not plan to sell their drugs. [FN158] Allowing a deduction for donations of licenses to use patents will be the main driver of getting AIDS-treatment drug patents in the hands of non-profit organizations that will be able to use the license for the public's benefit.

Currently, a corporation that donates a license to use a patent receives no tax benefit [FN159] and must continue to pay patent maintenance fees. [FN160] Therefore, it is necessary to allow a fair market value tax deduction for a donation of a license to use a patent in order to give a financial incentive for corporations to donate licenses. A tax deduction, along with public goodwill, might be enough incentive to pharmaceutical companies to donate licenses to use their drug patents to non-profit organizations.

Valuation of licenses to use patents raises the same abuse concerns as valuations of patents. [FN161] However, the Science Advisory Council will be able to mitigate the risks of abusive donations for licenses to use patents in the same manner that it does for patent donations. The Science Advisory Council will ensure that companies do not receive a fair market value tax deduction for valueless licenses or for licenses donated to donees incapable of utilizing the license. [FN162]

Allowing a tax deduction for the donation of a license to use a patent creates a win-win-win situation. Pharmaceutical companies will "win" by receiving a tax benefit that will increase their after-tax income. [FN163] AIDS victims who receive treatment from non-profit organizations licensed to distribute drugs will "win" by receiving potentially life-saving drugs they otherwise could not afford. [FN164] Although the government will forgo some tax receipts, in the end, even the government will ***71** "win" by not having to spend as much money combating the AIDS epidemic. [FN165] Thus, this proposal is a solution that will benefit all parties at the table.

C. Prior Case Law as Framework for Valuing Patents

In light of the lack of valuation guidance given by Congress and the Service, taxpayers are often unsure if the Service will accept their patent's value. [FN166] Until Congress or the Service provides a framework for valuing patents and licenses to use patents, donors should apply prior case law when valuing patents. [FN167] Donors should use the core set of common factors articulated by the courts [FN168] under the income method analysis to determine the fair market value of their patent.

This framework will provide donors with some certainty as to the courts' acceptance of their valuation if the Service decides to litigate the patent's value. [FN169] The Tax Court has commonly accepted the income method in determining the value of a patent. [FN170] Furthermore, the Tax Court has approved the common core of factors in multiple cases involving patent valuation. [FN171] This framework will focus the valuation on determining the value of the patent or license from which the corporations are forgoing benefits. [FN172] Until Congress or the Service provides valuation guidance, [FN173] this framework will be the best alternative for donors to apply when valuing their patents.

Alternatively, Congress could require the Science Advisory Council to determine the fair market value of the patents and licenses they decide are entitled to a fair ***72** market value tax deduction. [FN174] Congress can look to the Art Advisory Panel as a model. The Service created the Art Advisory Panel in 1968 after highly-publicized cases of artwork valuation abuse. [FN175] The Art Advisory Panel has been tasked with reviewing donated artworks to determine their fair market value. [FN176] The Panel's recommendation of the artwork's value is accepted by the Service. [FN177] The Art Advisory Panel has been considered an overall success. [FN178] Similarly, Congress could require that the Science Advisory Council determine the value of all donated patents, and that the Service would accept the Science Advisory Council's determination of value. This would settle patent valuation issues definitively. [FN179]

IV. Conclusion

The AIDS epidemic is devastating the world. [FN180] Millions of victims die each year from AIDS, and millions more become infected with HIV. [FN181] Current projections show that under the current response to AIDS, the epidemic will continue to get worse. [FN182] Although the United States has made it a priority to

combat the AIDS epidemic, our tax law hinders the government's fight against AIDS.

Congress needs to change our tax law to encourage companies to donate patents and licenses to non-profit organizations. The fair market value tax deduction for donations of patents and licenses will provide an incentive for corporations to make such donations. [FN183] Through donations of licenses to use AIDS-treatment drugs, vital anti-retroviral drugs will be distributed to AIDS victims. Donations of patents to non-profit organizations and universities may lead these organizations to develop products the donor could not or would not want to develop. The Science Advisory Council will ensure that the abusive patent donations that occurred before the AJCA ***73** do not happen again. For a small reduction in tax receipts, [FN184] the government will be able to more effectively fight the AIDS pandemic, to the relief of millions of AIDS victims worldwide.

[FNa1]. J.D. Candidate, May 2011, Temple University James E. Beasley School of Law; Certified Public Accountant, Pennsylvania; Master of Science, Professional Accounting, Seton Hall University; Bachelor of Science, Accounting, Seton Hall University. I would like to thank Professor Andrea Monroe for her assistance and advice throughout the writing process. For Mom and Dad, thanks for everything.

[FN1]. Robert Hecht et al., Critical Choices in Financing the Response to the Global HIV/AIDS Pandemic, 28 Health Aff. 1591, 1591 (2009). An estimated 9.5 million people currently require antiretroviral treatment and an estimated 23 million more will eventually need such treatment. Anil Soni & Rajat Gupta, Bridging the Resource Gap: Improving Value for Money in HIV/AIDS Treatment, 28 Health Aff. 1617, 1618 (2009).

[FN2]. See UNAIDS, 2008 Report on the Global AIDS Epidemic 15 (2008) (noting 2.2 million people died from AIDS in 2005 and 2 million people died from AIDS in 2007).

[FN3]. Id.

[FN4]. See Sheryl Gay Stolberg, In Global Battle on AIDS, Bush Creates Legacy, N.Y. Times, Jan. 5, 2008, at A1 (noting Colin Powell, then Secretary of State, believed AIDS ‘threatened to wipe out the entire child-bearing population‘ of some African states). Powell noted this would create “a climate ripe for terrorism[,]” thus making AIDS a “national security matter.” Id. Joshua Bolten, then chief of staff to the President, noted that the AIDS epidemic was “headed to destroy a whole continent.” Id.

[FN5]. See generally President George W. Bush, State of the Union, (Jan. 29, 2003), in N.Y. Times, Jan. 29, 2003, at A12 [hereinafter State of the Union] (stating that America can lead the world in sparing innocent people from the plague of the AIDS epidemic). President Bush noted that in regards to the AIDS epidemic, “seldom has history offered a greater opportunity to do so much for so many.” Id.

[FN6]. See John Carreyrou, New Regimen: Inside Abbott's Tactics to Protect AIDS Drug; Older Pill's Price Hike Helps Sales of Flagship; A Probe in Illinois, Wall St. J., Jan. 3, 2007 at A1 (noting Abbott Laboratories and Bristol-Myers Squibb Co. are two companies that have developed AIDS-treatment drugs).

[FN7]. Countries like Kenya, Nigeria, and Zambia, are heavily infected with HIV, but only have annual per capita spending on healthcare of $100. UNAIDS, supra note 2, at 156. Thus, “many medications are deemed too expensive for routine use.” Id. at 157.

[FN8]. A patent is the government's grant to the patentee of the exclusive right to make, use, and sell his or her

invention throughout the country. 35 U.S.C. § 154(a)(1) (2006). The term of the patent can last for twenty years from the date of the filing of the patent application. Id. § 154(a)(2).

[FN9]. "Licenses are considered as nothing more than a promise by the licensor not to sue the licensee ...." Jim Arnold Corp. v. Hydrotech Sys., Inc., 109 F.3d 1567, 1577 (Fed. Cir. 1997) (citing Spindelfabrik Suessen-Schurr v. Schubert & Salzer, 829 F.2d 1075, 1081 (Fed. Cir. 1987), cert. denied, 484 U.S. 1063 (1988)). In the granting of a license, title to the patent remains with the licensor (patentee), not the licensee. Id.

[FN10]. I.R.C. § 170(a) (2006).

[FN11]. Id. § 170(e).

[FN12]. Id. § 170(e)(1)(B).

[FN13]. See Nicholas C. Tomlinson, Tax Abuse Halting Progress? An Inside Look at Patent Donations and Their Tax Deductibility, 35 Sw. U. L. Rev. 183, 192 (2006) (noting corporate patents developed internally have a tax basis of zero). If a corporation purchases a patent, its basis in the patent will be equal to the amount paid to purchase the patent. I.R.C. § 1012 (2006).

[FN14]. See Xuan-Thao Nguyen & Jeffrey A. Maine, Giving Intellectual Property, 39 U.C. Davis L. Rev. 1721, 1747 (2006) ("[Current tax law] eliminate [s] an immediate tax deduction for gifts of intellectual property.").

[FN15]. Rev. Rul. 2003-28, 2003-1 C.B. 594. If a company purchased a license to use a patent, and has a tax basis in the patent, it would still receive no tax deduction if it donated the license. Id.

[FN16]. Id. Currently, drug treatment represents a quarter of the costs of AIDS funding. Hecht et al., supra note 1, at 1596. Thus, lowering drug treatment costs would result in substantially more AIDS victims being able to receive treatment.

[FN17]. I.R.C. § 170(e) (2006).

[FN18]. Don Macbean, Abstract, Better to Give Than to Receive: Evaluating Recent IP Donation Tax Policy Changes, 2005 Duke L. & Tech. Rev. 19, PP 1-2 (2005), available at http://www.law.duke.edu/journals/dltr/articles/pdf/2005dltr0019.pdf. The AJCA amended section 170 to limit the deduction to the lesser of the fair market value or the taxpayer's basis in the patent. American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 882(a), 118 Stat. 1418, 1627 (codified as amended at I.R.C. § 170(e)(1)(B) (2006)).

[FN19]. See Nguyen & Maine, supra note 14, at 1758 ("The [AJCA] is inconsistent with the government's historical approach of encouraging economic and socially desirable behavior through immediate tax benefits."); Tomlinson, supra note 13, at 192 (noting the AJCA will make patent donations "undesirable").

[FN20]. Nguyen & Maine, supra note 14, at 1724.

[FN21]. In 2003, President Bush called the AIDS epidemic a "plague of nature" in his State of the Union address. State of the Union, supra note 5.

[FN22]. See generally Nancy J. Knauer, The Paradox of Corporate Giving: Tax Expenditures, the Nature of the

Corporation, and the Social Construction of Charity, 44 DePaul L. Rev. 1, 32 (1994) ("Charitable giving is fueled and encouraged by the federal income tax charitable contribution deduction ... [which] reduces the cost of giving, thereby increasing the amount that a donor can transfer to a qualified charity.").

[FN23]. In Cameroon, for example, funding for antiretroviral drugs represents the majority of the funding gap between needed and actual expenditures. See Soni & Gupta, supra note 1, at 1620 (explaining that in Cameroon "funding for antiretrovirals still represents the majority of the unmet need").

[FN24]. See President & Fellows of Harvard Coll., Recent Development: Tax Treatment of Patent Donations in a Post-JOBS Act World, 18 Harv. J. L. & Tech. 295, 304 (2004) [hereinafter Tax Treatment of Patent Donations] ("Orphan drugs--drugs whose potential sales are not worth the cost of development to their owners--represent some of the best successes attributable to patent donation.").

[FN25]. While the Science Advisory Council's focus will be on medical patents, it will also review non-medical related patents for eligibility for a fair market value tax deduction. A discussion on how the Science Advisory Council works in non-medical related context is beyond the scope of this comment.

[FN26]. See Terri W. Cammarano & Richard F. Riley, Jr., Valuation Remains the Toughest Issue When Donating Patents, Valuation Strategies, Nov.-Dec. 2003, at 18, 24 ("Only a few published cases provide substantial guidance on [ ] methods to value donated patents.").

[FN27]. See generally I.R.C. § 170 (2006). Corporations may deduct charitable contributions up to ten percent of their taxable income. Id. § 170(b)(2)(A).

[FN28]. See Treas. Reg. § 1.170A-1(c)(1) (2008) (stating that with few exceptions, value of contribution made in property, other than money, is the fair market value of the property at date of contribution). Fair market value is defined as "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts." Id. § 1.170A-1(c)(2).

[FN29]. Rev. Rul. 58-260, 1958-1 C.B. 126.

[FN30]. Tomlinson, supra note 13, at 190.

[FN31]. See Macbean, supra note 18, P 5 (noting company executives "realized that prudent cost management required donating" orphan patents to reduce maintenance fee payments and to receive tax benefits).

[FN32]. For example, if Microsoft developed a new operating system but decided the operating system was not profitable for sale, the company could obtain a "defensive" patent to ensure that no competitors could create the system and compete with Microsoft's other products.

[FN33]. Ron Layton & Peter Bloch, IP Donations: A Policy Review 5 (Int'l Intellectual Prop. Inst. 2004), available at http://www.iipi.org/reports/IP_ Donations_Policy_Review.pdf.

[FN34]. See Tomlinson, supra note 13, at 190 ("After Andersen's report, the patent donation gained prominence in the corporate world ...."). For example, in 1996, Dow Chemical Company made the first major corporate patent donation to a non-profit organization. Id. By 2001, a Dow representative stated "the donation of unused intellectual property has resulted in millions of dollars of tax credits over the past six years." Layton & Bloch,

supra note 33, at 6.

[FN35]. See Layton & Bloch, supra note 33, at Appendix IV (reviewing publicly-announced patent donations and indicating universities are prime recipients).

[FN36]. See Macbean, supra note 18, P 1 ("[T]he recent proliferation of IP donations has been accompanied with abuse as some donors have overstated the value of their donations in an effort to claim inflated tax deductions.").

[FN37]. See Teresa Riordan, Patents; Some Corporations Take Generous Tax Write-offs for Donated Patents, An Industry Gadfly Says, N.Y. Times, Mar. 17, 2003, at C2 (stating SBC's failure to conduct a thorough search resulted in the donation of a patent that was "probably worthless" because similar computer software had already been developed by other companies).

[FN38]. Id.

[FN39]. Barnaby J. Feder, Patent Donations Are Novel Corporate Gift, N.Y. Times, Nov. 17, 2002, at BU5.

[FN40]. Stephanie Strom, I.R.S. Focuses on Noncash Donations to Charities, N.Y. Times, Dec. 24, 2003, at A18.

[FN41]. Id. "Not all donated patents turn out to be as valuable to the nonprofit organizations that receive them as the donors claim[.]" Id. One university professor noted the "bottom line" of the patent was that it "cost us money with no benefit." Feder, supra note 39, at BU5.

[FN42]. Katherine M. Stimmel, Tax Simplification Treasury to Seek Appraisals For Donations of Patents, Cars, 08 Daily Tax Rep. GG-3 (Jan. 14, 2004) (quoting Pam Olson, Assistant Secretary of the Treasury for Tax Policy); see Strom, supra note 40, at A18 (noting Internal Revenue Commissioner Mark Everson stated the Service is "seeing an increasing number of donations that don't pass the smell test").

[FN43]. Cassell Bryan-Low, Deductions for Patent Donations Draw Deeper Scrutiny From IRS, Wall St. J., Oct. 7, 2003, at A2.

[FN44]. Tomlinson, supra note 13, at 200.

[FN45]. See Bryan-Low, supra note 43, at A2 (noting the IRS determined the value of the patent to be two-thirds of $22.4 million and Lubrizol accepted that decision).

[FN46]. Id.

[FN47]. See Smith v. Comm'r, 41 T.C.M. (CCH) 1427, 1429 (1981), aff'd, 691 F.2d 508 (9th Cir. 1982) (noting potential purchasers of patents will consider patent validity when determining what they will pay for the patent). SBC's valuation of a donated patent did not include a search for examples of other similar software, the existence of which might have made the patent worthless. Riordan, supra note 37, at C2.

[FN48]. Rev. Rul. 2003-28, 2003-1 C.B. 594, 595; see also Mary Varson Cromer, Don't Give Me That!: Tax Valuation of Gifts to Art Museums, 63 Wash. & Lee L. Rev. 777, 785 (2006) ("[R]estricted gifts should be given a lower value than unrestricted gifts ....").

[FN49]. Rev. Rul. 2003-28, 2003-1 C.B. 594, 595. For example, if the patent donor prohibits the donee from selling any products created from the patent for a period of five years, then Revenue Ruling 2003-28 requires the donor to reduce the fair market value of the patent to take into account the restriction they imposed on the donee's use of the patent. Id.

[FN50]. I.R.S. Notice 2004-7, 2004-3 I.R.B. 310.

[FN51]. Id.

[FN52]. E.g., Nguyen & Maine, supra note 14, at 1753.

[FN53]. I.R.S. Notice 2004-7, 2004-3 I.R.B. 310.

[FN54]. Nguyen & Maine, supra note 14, at 1753.

[FN55]. See id. at 1749 (noting the growing valuation conflict between companies and the Service is a result of the Service never fully articulating "a standard or approach for determining the fair market value of donated intellectual property"); Macbean, supra note 18, P 6 (noting "inadequacy of IRS guidance with respect to valuation methods of IP" has facilitated abuse); Tax Treatment of Patent Donations, supra note 24, at 300 (noting the Service's failure to articulate methodology for determining a patent's value has made patent valuations "subject to abuse and inaccuracy"). The lack of guidance for patent valuation is in stark contrast to donations of art, in which the Service will issue a Statement of Value for the art, upon request by the taxpayer, which the taxpayer may rely upon for purposes of their tax return. Rev. Proc. 96-15, 1996-1 C.B. 627.

[FN56]. See generally Nguyen & Maine, supra note 14, at 1753 (noting the Service's enforcement campaign became moot after passage of the AJCA).

[FN57]. See William A. Drennan, Charitable Donations of Intellectual Property: The Case for Retaining the Fair Market Value Tax Deduction, 2004 Utah L. Rev. 1045, 1077 (2004) (noting Senator Charles Grassley stated Congress has "learned that there is widespread abuse involving donations of patents").

[FN58]. 150 Cong. Rec. S11019, 11021 (daily ed. Oct. 10, 2004) (statement of Sen. Grassley). See generally Paul R. Kitch, Patent Donations: Big Money. Big Trouble?, Intellectual Property Today, Mar. 2004, at 33 (providing sample of companies that have donated patents along with the value of the patents donated: SAIC (over $100 million), DuPont ($64 million), Shell Oil ($83.5 million), and Ford ($22 million)).

[FN59]. H.R. 3837, 108th Cong. § 1 (2004); S. 2103, 108th Cong. § 1 (2004).

[FN60]. H.R. 3837; S. 2103. The Intellectual Property Owners Association urged enactment of these bills, and strongly opposed bills that would have eliminated the tax deductions for IP donations. BNA, Legislation: Industry Group Backs Measures to Preserve Deduction for Intellectual Property Donations, Patent, Trademark & Copyright Law Daily, Mar. 26, 2004.

[FN61]. H.R. 3837.

[FN62]. Id.

[FN63]. American Jobs Creation Act of 2004, Pub. L. No. 108-357, 118 Stat. 1418 (codified as amended in

scattered titles and sections of the U.S.C.).

[FN64]. Id. § 882(a); I.R.C. § 170(e)(1)(B) (2006). The Congressional Budget Office estimated that the reduced tax deductions of the AJCA would save $307 million in 2005 and $3.65 billion from 2005-2014. Tomlinson, supra note 13, at 203.

[FN65]. See American Jobs Creation Act § 882(b) (allowing additional deductions in future years); I.R.C. § 170(m)(1) (same).

[FN66]. See American Jobs Creation Act § 882(b) (deduction allowed based on the "qualified donee income with respect to such contribution"); I.R.C. § 170(m)(1) (same).

[FN67]. See American Jobs Creation Act § 882(b) (income is not treated as allocable to the patent if the income is accrued after the legal life of the patent); I.R.C. § 170(m)(6)-(7) (same).

[FN68]. American Jobs Creation Act § 882(b); I.R.C. § 170(m)(7). No deductions are permitted after the twelfth year of the donation. See American Jobs Creation Act § 882(b) (table ending at twelfth year after date of contribution); I.R.C. § 170(m)(7) (same).

[FN69]. American Jobs Creation Act § 882(b); I.R.C. § 170(m)(1)-(2). For example, suppose a company donates a patent that has a fair market value of $200,000 and a basis of zero. The donee earns $10,000 of income attributable to the patent in year one and $50,000 in year twelve. Section 170(m)(7) of the Code limits the amount of the additional deductions. I.R.C. § 170(m)(7). In year one, 100% of the $10,000 of income will be an increase used to calculate additional tax deductions. Id. However, in year twelve, only 10% of the $50,000 ($5,000) of income will be deductible. Id. Thus, the post-AJCA section 170 limits the tax deduction to $15,000 over a period of twelve years. Prior to the AJCA, the patent donor would have been entitled to an immediate tax deduction of $200,000. I.R.C. § 170(e) (2000) (current version at I.R.C. § 170(e) (2006)).

[FN70]. The patent donee must file a return every taxable year which includes the amount of net income of the donee that is allocable to the donated patent. I.R.C. § 6050L(b)(1)(D) (2006).

[FN71]. See Nguyen & Maine, supra note 14, at 1724 ("[A]bsent immediate economic incentives, no donations will be made."). But see Tax Treatment of Patent Donations, supra note 24, at 303 (noting AJCA's deductions "provide more than enough incentive to motivate socially useful university patent donations").

[FN72]. Nguyen & Maine, supra note 14, at 1746-47. The low basis in internally-developed patents is primarily attributable to § 174 of the Code, which allows taxpayers to immediately deduct, rather than capitalize, "research and experimental expenditures." See I.R.C. § 174(a)(1) (2006). Research and experimental expenditures include all costs incident to the development of a product, and include the costs of obtaining a patent. Treas. Reg. § 1.174-2(a)(1) (1994).

[FN73]. See, e.g., Nguyen & Maine, supra note 14, at 1746-47 (noting the AJCA "reduced or, in many cases, eliminated an immediate tax deduction for gifts of intellectual property").

[FN74]. Id. at 1762 (noting society will suffer "because the tax system fails to encourage the dissemination of orphan intellectual property").

[FN75]. Id. at 1756-57.

[FN76]. Id. at 1747-48, 1757. For example, in year four after the donation, the income earned from the patent will be reduced by 80% to determine the donor's deduction. I.R.C. § 170(m)(7) (2006). By year ten, only 20% of the income earned from the patent will be deductible by the donor. Id. After year twelve, no deductions are permitted for the donor. Id.

[FN77]. Nguyen & Maine, supra note 14, at 1762-63. Each donee of a patent donation must file a return every taxable year that includes the amount of net income of the donee which is allocable to the donated patent. I.R.C. § 6050L(b)(1)(D) (2006). Never before in the Code has an entity's tax deduction been based on the ability of another entity to derive income from the donated asset. See generally Nguyen & Maine, supra note 14, at 1757 ("The 2004 Act is inconsistent with the government's historical approach of encouraging economic and socially desirable behavior through immediate tax benefits.").

[FN78]. See Nguyen & Maine, supra note 14, at 1754-55 (arguing immediate fair market value deduction for donors of intellectual property would be the most effective incentive).

[FN79]. I.R.C. § 170(m).

[FN80]. In fact, selling products to charity recipients for a profit is contrary to the reason for allowing a tax deduction. See S. Rep. No. 91-552, at 16 (1969), reprinted in 1969 U.S.C.C.A.N. 2027, 2052 (noting the basis for tax deductions for amounts given to non-profit organizations is the funds "would be used for educational, charitable, religion, etc., purposes"); Vada Waters Lindsey, The Charitable Contribution Deduction: A Historical Review and a Look to the Future, 81 Neb. L. Rev. 1056, 1057 (2003) (noting charitable deductions are allowed for donations to those organizations which "are thought to enhance the betterment of society").

[FN81]. See I.R.C. § 170(m)(1) (stating deduction may only be taken from "the applicable percentage of qualified donee income with respect to such contribution").

[FN82]. See Tomlinson, supra note 13, at 205 (noting the AJCA "reduces tax incentives" for patent donations).

[FN83]. Id. at 206; see also Knauer, supra note 22, at 32 ("Charitable giving is fueled by and encouraged by the federal income tax charitable contribution deduction ....").

[FN84]. Nguyen & Maine, supra note 14, at 1724; see also Shelby D. Green, Corporate Philanthropy and the Business Benefit: The Need for Clarity, 20 Golden Gate U. L. Rev. 239, 240 (1990) (noting many corporations make charitable contributions to realize tax benefits).

[FN85]. Drennan, supra note 57, at 1152.

[FN86]. Nguyen & Maine, supra note 14, at 1743.

[FN87]. Id. at 1771.

[FN88]. American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 882(b), 118 Stat. 1418, 1628 (2004).

[FN89]. See Tomlinson, supra note 13, at 205 (noting AJCA "reduces tax incentives" for patent donations). Furthermore, until recently, a corporation that owned orphan patents was limited to two methods of disposing of the patent to avoid payment of maintenance fees: donation or abandonment. See Tax Treatment of Patent Donations, supra note 24, at 296 (noting prior to the AJCA, corporations saw donations as "an attractive alternative to aban-

donment"). However, patents are "fast becoming a sought-after financial" asset. Trolls Demanding Tolls, Economist, Sep. 12, 2009, at 84. Over $4 billion of patents related to "telecoms, medical equipment, biotechnology, and the internet" were bought and sold last year, and the market is estimated to grow by 20% to 30% a year. Id. As a result, corporations now have a market in which they can sell their orphan patents. Id. Without a fair market value tax deduction, patent donations will be financially unattractive to corporations that can sell their patents and recover some of their research expenditures. See id. (noting well-timed patent sales are a way for corporations to meet quarterly profit targets).

[FN90]. I.R.C. § 170(e)(1)(B)(iii) (2006); Rev. Rul. 2003-28, 2003-1 C.B. 594.

[FN91]. Rev. Rul. 2003-28, 2003-1 C.B. 594. To be entitled to a tax deduction a company must donate their entire interest in the patent. Id.

[FN92]. Cf. Knauer, supra note 22, at 56 ("[T]he ultimate goal of corporate giving ... remains that of profit maximization.").

[FN93]. A good analogy can be made between lawyers and corporations that own patents. After spending a tremendous amount of time and money to graduate law school and pass the bar, a practicing lawyer would never consider "donating" her law degree to charity. However, a lawyer would consider "donating" a Saturday of her time to help provide legal services to people who would otherwise be unable to afford her legal services.

[FN94]. Kitch, supra note 58, at 34. Patent holders have the legal right to prohibit other companies from using their patent. 35 U.S.C. § 154(d) (2006); see also Zenith Radio Corp. v. Radio Corp. of America, 121 F. Supp. 803, 805 (1954) (noting that inherent in a property element of a patented invention is "the monopoly--the right effectively to prohibit others from practicing the invention or profiting therefrom without owner's consent").

[FN95]. Abbott Laboratories and Bristol-Myers Squibb Co. are two of the companies that have developed AIDS-treatment drugs. See generally Carreyrou, supra note 6, at A1 (discussing AIDS-treatment drugs and their makers).

[FN96]. Cent. Intelligence Agency, The World Factbook 2008, at 554 (2008).

[FN97]. Id. at 555.

[FN98]. See Carreyrou, supra note 6, at A1 (noting, for example, in 2003-2004 an AIDS-treatment drug sold by Abbott Laboratories cost about $7,000 per year).

[FN99]. The gross profit margin of Abbott Laboratories was 57.3% in 2008. Abbott Labs., Annual Report (Form 10-k), at 33 (Feb. 20, 2009). The gross profit margin of Bristol-Myers Squibb was 76% in 2008. Bristol Myers Squibb Co., Annual Report (Form 10-k), at 82 (Feb. 20, 2009).

[FN100]. See Jeffrey D. Bauman et al., Corporations Law and Policy 88 (6th ed. 2007) (noting commentators have long argued "the only social responsibility of a corporation is to maximize profits").

[FN101]. See Rev. Rul. 2003-28, 2003-1 C.B. 594 (stating 'a license to use a patent is not deductible if the taxpayer retains any substantial right in the patent').

[FN102]. See Tax Treatment of Patent Donations, supra note 24, at 304 (noting firms will only donate patents

that lack ready commercial applications).

[FN103]. Thus it is important to provide a fair market value tax deduction for donations of both patents and licenses to use patents.

[FN104]. See Hecht et al., supra note 1, at 1591 (noting thirty-three million people are infected with HIV worldwide).

[FN105]. Allowing a fair market value tax deduction will result in declines in the cost of antiretroviral drug treatment, which is desperately needed to ensure that more AIDS victims receive treatment. UNAIDS, supra note 2, at 15.

[FN106]. Currently, 9.5 million people require antiretroviral drug treatment, and it is estimated that 23 million more people will need such treatment in the future. Soni & Gupta, supra note 1, at 1618.

[FN107]. Tomlinson, supra note 13, at 199; see Cammarano & Riley, supra note 26, at 20 (“[T]he most interesting question regarding charitable donations of patents is how to value the darn things.”); see also Kitch, supra note 58, at 34 (“To understate matters, the fair market value of a patent is generally not easily determinable.”).

[FN108]. See, e.g., Nguyen & Maine, supra note 14, at 1749 (noting the Service never fully articulated “a standard or approach for determining the fair market value of donated intellectual property.”). Congress defined fair market value, in terms of charitable contributions, as “the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.” Treas. Reg. § 1.170A-1(c)(2) (2008).

[FN109]. Unlike patents, the Service will provide a valuation of artwork upon request by the taxpayer. Rev. Proc. 96-15, 1996-1 C.B. 627. The Service could also provide such a service for patent donations.

[FN110]. The following cases have decided on the valuation of patents: Estate of Gribauskas v. Comm'r, 116 T.C. 142 (2001), rev'd on other grounds, 342 F.3d 85 (2d Cir. 2003); Podd v. Comm'r, 75 T.C.M. (CCH) 2575 (1998); Nestle Holdings, Inc. v. Comm'r, 70 T.C.M. (CCH) 682 (1995); Sandvik, Inc. v. Comm'r, 52 T.C.M. (CCH) 1181 (1986); Estate of Paxton v. Comm'r, 44 T.C.M. (CCH) 771 (1982); Smith v. Comm'r, 41 T.C.M. (CCH) 1427, 1428 (1981), aff'd, 691 F.2d 508 (9th Cir. 1982).

[FN111]. Cammarano & Riley, supra note 26, at 23.

[FN112]. Id. at 24.

[FN113]. Id. (citing Smith and Parr, Valuation of Intellectual Property and Intangible Assets 318-19 (John Wiley & Sons, 2000)).

[FN114]. Tomlinson, supra note 13, at 197.

[FN115]. Id.; see also Cammarano & Riley, supra note 26, at 24 (noting income method is well suited to patents, which are unique by their very nature).

[FN116]. Tomlinson, supra note 13, at 197; see also Cammarano & Riley, supra note 26, at 24 (noting cost method fails to consider a patent's “profits from commercializing, investment risk, and earnings growth poten-

tial").

[FN117]. See Cammarano & Riley, supra note 26, at 24-27, 47-48 (reviewing judicial cases involving patent valuation, noting income approach is most commonly used by courts in determining patent valuation).

[FN118]. Tomlinson, supra note 13, at 198 (citing Smith v. Comm'r, 41 T.C.M. (CCH) 1427 (1981), aff'd, 691 F.2d 508 (9th Cir. 1982)).

[FN119]. 41 T.C.M. (CCH) at 1427.

[FN120]. Id. at 1428.

[FN121]. Id.

[FN122]. Id.

[FN123]. Id. The Service's appraiser utilized an income-based analysis to value the patents. Cammarano & Riley, supra note 26, at 24.

[FN124]. Smith, 41 T.C.M. (CCH) at 1428-29.

[FN125]. Id. at 1429.

[FN126]. Id. At the time of the decision, Revenue Ruling 58-260 was in effect, which permitted a tax deduction equal to the fair market value of the patent. Rev. Rul. 58-260, 1958-1 C.B. 126.

[FN127]. Podd v. Comm'r, 75 T.C.M. (CCH) 2575, 2589 (1998) (citing Smith, 41 T.C.M. (CCH) at 1429).

[FN128]. See Tomlinson, supra note 13, at 198 (noting Smith v. Comm'r was the only case to specifically address valuation for patent donations); Sandvik, Inc. v. Comm'r, 52 T.C.M. (CCH) 1181 (1986) (determining whether fair market value allocation assigned to patent was reasonable); Estate of Paxton v. Comm'r, 44 T.C.M. (CCH) 771 (1982) (determining whether sales price of patent reasonably reflected fair market value).

[FN129]. Smith, 41 T.C.M. (CCH) at 1428; Sandvik, Inc., 52 T.C.M. (CCH) at 1186. In Sandvik, a company sold a subsidiary that owned patents. 52 T.C.M. (CCH) at 1182-83. The price paid by the purchasers was then ratably applied to the subsidiary's assets to form the company's basis in its assets. Id. at 1185. Based on the valuation appraisal of the assets, the company assigned a basis of $14.7 million to the patents. Id. After the sale of the subsidiary, the Court of Appeals for the Seventh Circuit ruled the patents were invalid. Id. As a result, the company wrote off its basis in the patents and claimed a tax loss in the amount of the remaining basis. Id. The Service claimed the loss should be disallowed because the amounts the company already deducted from the patents for amortization purposes exceeded the fair market value of the patents. Sandvik, Inc., 52 T.C.M. (CCH) at 1186. In determining the fair market value at the time of the purchase, the Tax Court reviewed the valuation appraisals submitted by the parties. Id. at 1186-89. The Tax Court noted the following factors were determinative of the fair market value of the patents: (1) total market for the product, (2) the company's market share, (3) the amount of net income attributable to the patents, (4) royalty income to be received by other manufacturers of the product, (5) risk of competition from similar products, and (6) remaining legal life of the patents. Id. at 1186-87, 1191.

[FN130]. Smith, 41 T.C.M. (CCH) at 1428; Sandvik, Inc., 52 T.C.M. (CCH) at 1186.

[FN131]. Sandvik, Inc., 52 T.C.M. (CCH) at 1186; Paxton, 44 T.C.M. (CCH) at 821. In Paxton, a patent owner sold his patents for $2 million. 44 T.C.M. (CCH) at 817. The Service believed the value of the patents was substantially less than $2 million, thus the excess of the sales price over the value of the patents should be treated as income, not capital gain. Id. The Tax Court used the following factors to determine the fair market value of the patents: (1) market for the product, (2) the company's market share, (3) sales of the product, (4) net profit from sales, (5) expected preeminent market position at the end of the patent protection period, (6) and value attributable to profits derived from sales of related products. Id. at 820-21.

[FN132]. Smith, 41 T.C.M. (CCH) at 1428; Podd, 75 T.C.M. (CCH) at 2589.

[FN133]. Sandvik, Inc., 52 T.C.M. (CCH) at 1187; Smith, 41 T.C.M. (CCH) at 1428.

[FN134]. Smith, 41 T.C.M. (CCH) at 1429.

[FN135]. Currently, section 170(e)(1) of the Code limits the amount of the tax deduction for a donation of a patent to the lesser of the fair market value of the patent or the taxpayer's basis in the patent. I.R.C. § 170(e)(1)(B) (2006).

[FN136]. See Tomlinson, supra note 13, at 206 (noting the fair market value tax deduction "provided a means that encouraged donation and promoted progress"); Kitch, supra note 58, at 33 (noting significant benefit of patent donation for corporations is tax deduction); cf. Nguyen & Maine, supra note 14, at 1771 (noting best way to encourage donations is through economic incentives).

[FN137]. See Knauer, supra note 22, at 57 (noting corporate giving relies on the corporation's desire to capitalize on the goodwill associated with the charitable contribution).

[FN138]. See Tax Treatment of Patent Donations, supra note 24, at 300 ("Orphan drugs--drugs whose potential sales are not worth the cost of development to their owners--represent some of the best successes attributable to patent donation.").

[FN139]. See Nguyen & Maine, supra note 14, at 1757 ("[W]hat incentivizes behavior is a system of immediate economic benefits ...."); Jeremy Bond, Leveraging Patent Donations to Grow Technology-Based Business 3 (Economic Development Now) (May 21, 2007), available at http://www.thecati.com/news/IEDC_ EDNow_052107.pdf (noting patent donations have largely dried up since passage of AJCA). No study has compared the number of patent donations pre- and post-AJCA. Information on post-AJCA donations is difficult to obtain as industry group and patent-valuation companies are no longer reporting on patent donation issues. See generally International Intellectual Property Institute, Newsroom, http://www.iipi.org/nav_newsroom/Press_Releases.asp (last visited Feb. 1, 2010) (providing press releases for industry groups and patent-valuation companies); M Cam, Inc., News and Events, http://www.m-cam.com/news?year=2005 (last visited Feb. 1, 2010) (same). Due to the lack of reporting on patent donation issues, as well as the development of a financial market for patents, the most reasonable inference to be drawn is that patent donations have largely decreased since the AJCA. Trolls Demanding Tolls, supra note 89, at 84.

[FN140]. See generally Drennan, supra note 57, at 1106 (suggesting creation of "Patent Advisory Panel" to re-

view valuations of donated patents).

[FN141]. The Art Advisory Panel has been tasked to review donated artworks to determine the fair market value of the artwork. Nguyen & Maine, supra note 14, at 1765. The Art Advisory Panel's recommendation of the artwork's value is accepted by the Service for tax return purposes. Nancy A. McLaughlin, Increasing the Tax Incentives for Conservation Easement Donations--A Responsible Approach, 31 Ecology L.Q. 1, 89 (2004).

[FN142]. See Drennan, supra note 57, at 1091 (noting Art Advisory Panel consists of twenty-five experts).

[FN143]. Without approval from the Science Advisory Council, patent donors will only be able to deduct the lesser of the fair market value of the patent or their basis in the patent in accordance with section 170. See I.R.C. § 170(e)(1)(B) (2006) (limiting charitable contribution deduction for donations of patents to lower of fair market value or donor's basis in the patent).

[FN144]. See, e.g., Tax Treatment of Patent Donations, supra note 24, at 298 (noting corporations abused patent donations “as a means of lightening their tax liabilities”). One of Congress's concerns in removing the fair market value tax deduction was companies were taking “hundreds of millions of dollars” in tax deductions for donating valueless patents. 150 Cong. Rec. S. 11019-21 (daily ed. Oct. 10, 2004).

[FN145]. Patent donations were subject to abuse because little disclosure was required by companies in the forms they filed with the Service in claiming a tax deduction for a patent donation. Bryan-Low, supra note 43, at A2.

[FN146]. In contrast, for tax return purposes, most companies list the total value of all patents donated, as opposed to individually listing the value claimed for each donated patent. Id. Prior to the AJCA, the Service hired patent valuation firms to help review the value of donated patents. Id. However, the creation of the Science Advisory Council will allow the Service to concentrate its patent valuation experts on those companies that have been approved by the Science Advisory Council to receive fair market value tax deductions for donated patents.

[FN147]. See generally Ronald A. Pearlman, Demystifying Disclosures: First Steps, 55 Tax L. Rev. 289 (2002) (noting enhanced disclosure contributes to improved tax enforcement and increases voluntary compliance).

[FN148]. See Tax Treatment of Patent Donations, supra note 24, at 298 (noting corporations claimed deductions for patents that “were of little practical use to the recipient university”); Strom, supra note 40, at A18 (noting AlliedSignal donated patent valued at $7 million to University of Virginia, which subsequently forfeited the patent because it lacked the equipment to utilize it.).

[FN149]. This mitigation will be one of many factors in determining whether the patent donation should be entitled to a fair market value tax deduction. See supra text accompanying notes 142-43, for a discussion of the factors.

[FN150]. The net result of the AlliedSignal patent donation seems to be a loss of $7 million of income that the Treasury could tax. See generally Strom, supra note 40, at A18 (noting university forfeited patent due to lack of equipment to develop the patent). The Science Advisory Council's review of the donation will ensure donees are able to utilize the patent. See supra text accompanying notes 142-43.

[FN151]. See Tax Treatment of Patent Donations, supra note 24, at 304 (noting tax deductions only provide incentive for corporations to donate patents that they would otherwise abandon).

[FN152]. See id. (noting fair market value tax deduction provides “an unneeded windfall to donors”).

[FN153]. See id. (“Orphan drugs--drugs whose potential sales are not worth the cost of development to their owners--represent some of the best successes attributable to patent donation.”).

[FN154]. In essence, restrictions on the license to use a patent would affect the fair market value of the license in the same way that restrictions on property affect the fair market value of the property. Thus, under Revenue Ruling 85-99, the fair market value tax deduction would be reduced in light of the restriction. Rev. Rul. 85-99, 1985-2 C.B. 83. In donations of property other than patents, the Tax Court has held that restrictions placed on the donee's property reduces the fair market value of the property and must be reflected in the tax deduction. Cromer, supra note 48, at 787 (citing Silverman v. Comm'r, 27 T.C.M. (CCH) 1066 (1968); Murphy v. Comm'r, 61 T.C.M. (CCH) 2935 (1991), rev'd on other grounds, 8 F.3d 28 (9th Cir. 1993)).

[FN155]. Cf. Tomlinson, supra note 13, at 206 (noting pre-AJCA fair market value tax deduction encouraged patent donation). But cf. Nguyen & Maine, supra note 14, at 1734-43 (describing why non-profit organizations prefer outright ownership of patents to licenses).

[FN156]. See generally Tax Treatment of Patent Donations, supra note 24, at 304-05 (noting firms will only donate patents that lack ready commercial applications). However, patents that are not profitable today may hold the key to unlocking medical technologies tomorrow. Thus, it is important to allow a fair market value tax deduction for donations of patents.

[FN157]. Cf. Kitch, supra note 58, at 34 (noting corporations do not want to be sued for infringement of the very patent they donated).

[FN158]. Sub-Saharan Africa is the “worst-affected area” of people infected with AIDS. Almost Halfway There, Economist, Oct. 3, 2009, at 100. The gross domestic product per capita for sub-Saharan countries is very low; for example, it is $900 for Mozambique and $500 for Zimbabwe. Cent. Intelligence Agency, supra note 96, at 404, 647. While sub-Saharan Africa is one of the areas hit worst by the AIDS epidemic, its citizens cannot afford AIDS drugs. See Carreyrou, supra note 6, at A1 (noting the cost of AIDS-treatment drugs sold by Abbott Laboratories is $7,000 per year). Therefore, since pharmaceutical companies cannot profitably sell their AIDS drugs to sub-Saharan Africa, it will be in their financial interest to receive a tax deduction for donating a license to use a patent to non-profit organizations that can distribute the drugs to sub-Saharan Africa countries.

[FN159]. Rev. Rul. 2003-28, 2003-1 C.B. 594.

[FN160]. The title of the patent remains with the patent donor, and does not transfer to the licensee. Jim Arnold Corp. v. Hydrotech Sys., Inc., 109 F.3d 1567, 1577 (Fed. Cir. 1997). “Patent holders are required to pay maintenance fees to keep their patents active.” Tax Treatment of Patent Donations, supra note 24, at 296-97. Maintenance fees range between $490 and $4,110, depending on the life of the patent. 37 C.F.R. § 1.20(e)-(g) (2009).

[FN161]. See supra Part III.A, for a discussion of potential patent valuation abuses.

[FN162]. Furthermore, the Science Advisory Council will determine the percentage of the value of the patent that the donated license represents. The Science Advisory Council will look at the amount of potential revenue of the license compared to total revenue that could be earned by the patent. Of particular importance for AIDS-treatment drug patents will be determining the amount of income the pharmaceutical company could have

earned had it sold the drug to the particular country in which it licensed the donee to distribute the drug. This amount will then be divided by estimated total revenue from the patent to determine the percentage of the value of the patent that the license represents.

[FN163]. See Tomlinson, supra note 13, at 189 (noting a major corporate benefit of patent donations is tax deduction).

[FN164]. More than five million people in poor and middle-income countries might benefit from AIDS-treatment drugs, but currently do not have access to the drugs. Almost Halfway There, supra note 158, at 100. Thus, there would be at least five million "winners" from this policy change.

[FN165]. See Nguyen & Maine, supra note 14, at 1743 ("[T]he charitable deduction minimizes the need for direct government subsidies ....").

[FN166]. See id. at 1749 (noting the Service never fully articulated "a standard or approach for determining the fair market value of donated intellectual property").

[FN167]. See Estate of Gribauskas v. Comm'r, 116 T.C. 142, 153 (2001), rev'd on other grounds, 342 F.3d 85 (2d Cir. 2003) ("[A] patent is valued by quantifying a variety of factors ... includ[ing] the age of the patent, its economic and legal life, the income it generates, the products with which the underlying item competes, the risks of the relevant industry, and the status of the economy."). Another approach is to multiply a list of factors including the "potential market," the "anticipated market penetration," the "unit cost," "patent validity," and "technological feasibility." Smith v. Comm'r, 41 T.C.M. (CCH) 1427, 1428 (1981), aff'd, 691 F.2d 508 (9th Cir. 1982).

[FN168]. The common factors articulated by the courts are: (1) potential market for products produced from the patent, (2) anticipated market penetration of the products, (3) net profit from expected sales of products created by the patent, (4) patent validity, (5) royalty rates paid by other users of the product, and (6) any other "factor which affects what a willing purchaser will pay" for the patent. See supra notes 123-34 and accompanying text.

[FN169]. See Tomlinson, supra note 13, at 205 (noting "companies need more certainty about valuation standards"). The donor will be able to take comfort in the fact that the factors used by their valuation appraisal have prior judicial acceptance.

[FN170]. See Cammarano & Riley, supra note 26, at 24-27, 47-48 (finding the income approach is most commonly used by courts in determining patent valuation) (citing Smith, 41 T.C.M. (CCH) at 1427; Nestle Holdings, Inc. v. Comm'r, 70 T.C.M. (CCH) 682 (1995); Sandvik, Inc. v. Comm'r, 52 T.C.M. (CCH) 1181 (1986)).

[FN171]. See supra notes 123-34 and accompanying text.

[FN172]. In essence, the value of the benefits the corporation is foregoing by donating the patent or license should be the same amount that an independent buyer would pay to purchase the patent or license. Thus, this framework would satisfy the fair market value as defined in the Code. Treas. Reg. § 1.170A-1(c)(2) (as amended in 2008).

[FN173]. Unlike patents, the Service will provide a valuation of artwork upon request by the taxpayer. Rev. Proc. 96-15, 1996-1 C.B. 627, 628. The Service could also provide such a service for patent donations.

[FN174]. See generally Drennan, supra note 57, at 1106 (recommending the Service create a “Patent Advisory Panel” to review patent valuations in cases that involve charitable contributions valued at over $20,000).

[FN175]. See McLaughlin, supra note 141, at 87-88 (describing development of the Art Advisory Panel). Due to art valuation abuses, Congress considered repealing the charitable deduction for donations of “tangible property.” Id. at 88-89.

[FN176]. See Nguyen & Maine, supra note 14, at 1765 (describing Art Advisory Panel as twenty-five members, including art dealers and museum curators, who review and evaluate art appraisals for tax purposes); see also Anne-Marie E. Rhodes, Big Picture, Fine Print: The Intersection of Art and Tax, 26 Colum. J.L. & Arts 179, 197 (2003) (noting how in 2000, the Art Advisory Panel reviewed 2,546 items of art valued at $267 million by taxpayers).

[FN177]. McLaughlin, supra note 141, at 89.

[FN178]. See Douglas J. Bell, Changing I.R.C. § 170(e)(1)(A): For Art's Sake, 37 Case W. Res. L. Rev. 536, 545 (1986-87) (describing increasing success of Art Advisory Panel); see also 73 Fed. Reg. 4308 (Jan. 24, 2008) (noting existence of Art Advisory Panel is in the public interest).

[FN179]. In addition to providing certainty to taxpayers who no longer have to worry about the Service challenging their patent's valuation, this would also prevent abusive overvaluations of patents.

[FN180]. In 2003, President Bush called the AIDS epidemic a “plague of nature” in his State of the Union address. State of the Union, supra note 5.

[FN181]. See UNAIDS, supra note 2, at 15 (noting 2.2 million people died from AIDS in 2005 and 2 million people died from AIDS in 2007); Hecht et al., supra note 1, at 1591 (noting 2.3 million adults were infected with HIV in 2007).

[FN182]. See Hecht et al., supra note 1, at 1591 (“Without a change in approach, a major epidemic will still be with us in 2031.”).

[FN183]. See, e.g., Tomlinson, supra note 13, at 206 (noting the fair market value tax deduction “provided a means that encouraged donation and promoted progress”).

[FN184]. Prior to the AJCA, it was estimated that companies claimed around $300 million dollars worth of tax deductions each year. See id. at 203 (estimating passage of the AJCA would recapture $307 million in tax deductions in 2005). Since the Science Advisory Council will only approve patent or license donations that are in the best interests of the public to be donated, the amount of the deductions claimed for patent donations will be substantially less than it was prior to the AJCA.
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