

## TAX PATENTS

### Present Law

Patents have increasingly been sought and issued for various tax-related inventions, including strategies for reducing a taxpayer's taxes.

In a 1998 case, *State Street Bank*,<sup>1</sup> the U.S. Court of Appeals for the Federal Circuit ("Federal Circuit Court") held that a method of doing business could be patented. The case involved a data processing system for a partnership structure of mutual funds that had advantageous tax consequences. The case has been considered a key decision allowing the patenting of business methods of all types.<sup>2</sup> Since 1998, numerous tax-related patents have been issued or applied for, in some cases involving tax strategies less related to computer or other mechanical data processing systems. More recently, the Federal Circuit Court has indicated that some business methods are unpatentable.<sup>3</sup>

The patents that have been granted or applied for have involved many aspects of the tax law, including financial products, charitable giving, estate planning, and tax deferred exchanges.<sup>4</sup>

### Reasons for Change

Tax-related patents, if valid, remove from the public domain particular ways to satisfy a taxpayer's legal obligations. Tax-related inventions that have been patented cannot be practiced without the permission of the patent holder. Thus, a tax-related patent may have the effect of forcing or encouraging taxpayers to pay more tax than they would otherwise lawfully owe, either because taxpayers are not able to engage in a particular transaction or financial structure without the permission of the patent holder or because, if permission is granted, such permission requires payment of an undesirable charge. Taxpayers might seek other, more questionable alternatives to the patented invention in an attempt to avoid the scope of the patent. Unauthorized use of patented inventions may have adverse consequences for taxpayers or their advisers, who may face patent infringement suits for using, or suggesting use, of patented tax-related inventions. This could undermine uniform application of the tax laws, decrease public confidence in the nation's tax laws, and increase public dissatisfaction with tax laws if compliance must be accompanied by patent searches and licensing.

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<sup>1</sup> *State St. Bank & Trust Co. v. Signature Fin. Group, Inc.*, 149 F.3d 1368 (Fed. Cir. 1998), *cert. denied*, 525 U.S. 1093 (1999).

<sup>2</sup> See Statement of Nicholas Godici, Commissioner for Patents, U.S. Patent and Trademark Office, before the Senate Committee on Finance Hearing on "Bridging the Tax Gap" (July 21, 2004).

<sup>3</sup> *In re Comiskey*, No. 2006-1286 (Fed. Cir. Sept. 20, 2007).

<sup>4</sup> In September 2007, the Department of the Treasury issued proposed regulations identifying transactions involving certain types of tax-related patents as reportable transactions under section 6011 of the Internal Revenue Code of 1986. 72 Fed. Reg. 54,615 (Sept. 26, 2007).

The availability of patent protection also could encourage, in a variety of ways, the further development of aggressive tax shelter transactions or of transactions that do not achieve the expected tax results. For example, tax-related inventions do not necessarily have to deliver their claimed tax benefits to be eligible for a patent; yet strategies or methods that do not achieve the intended tax result might be marketed as “legitimate” based on the existence of a patent.<sup>5</sup>

Finally, the creativity and ingenuity reflected in many tax planning techniques developed over the years without patent protection suggests that even without such protection there are sufficient incentives for tax planning innovation.

### **Explanation of Provision**

Under the provision, a patent may not be obtained for a tax planning invention.

A tax planning invention means a plan, strategy, technique, scheme, process, or system that is designed to reduce, minimize, avoid, or defer, or has, when implemented, the effect of reducing, minimizing, avoiding, or deferring, a taxpayer’s tax liability, or is designed to facilitate compliance with tax laws, but does not include tax preparation software and other tools or systems used solely to prepare tax or information returns.

The term “taxpayer” is defined as an individual, entity, or other person (as defined in section 7701 of the Internal Revenue Code of 1986).

The terms “tax,” “tax laws,” “tax liability,” and “taxation” refer to any Federal, State, county, city, municipality, foreign, or other governmental levy, assessment, or imposition, whether measured by income, value, or otherwise.

The term “State” means each of the several States, the District of Columbia, and any commonwealth, territory, or possession of the United States.

No inference is intended as to whether any business method, including any tax-related invention, is otherwise patentable under present law, or as to whether any software is entitled under present law to patent protection as distinct from copyright protection.

### **Effective Date**

The provision takes effect on the date of enactment.

The provision shall apply to any application for a patent or application for a reissue patent that is (a) filed on or after such date of enactment; or (b) filed before such date if a patent or reissue patent has not been issued pursuant to the application as of that date.

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<sup>5</sup> The Department of the Treasury expressed similar concerns in the preamble to the proposed regulations it issued in September 2007.

The provision shall not be construed as validating any patent issued before the date of enactment for an invention described in section 101(b) of title 35, United States Code, as amended by this section.