

DELAWARE, INTELLECTUAL PROPERTY AND CORPORATE IRRESPONSIBILITY

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The Intellectual Property Holding Company

Tax Use and Abuse from Victoria's Secret to Apple

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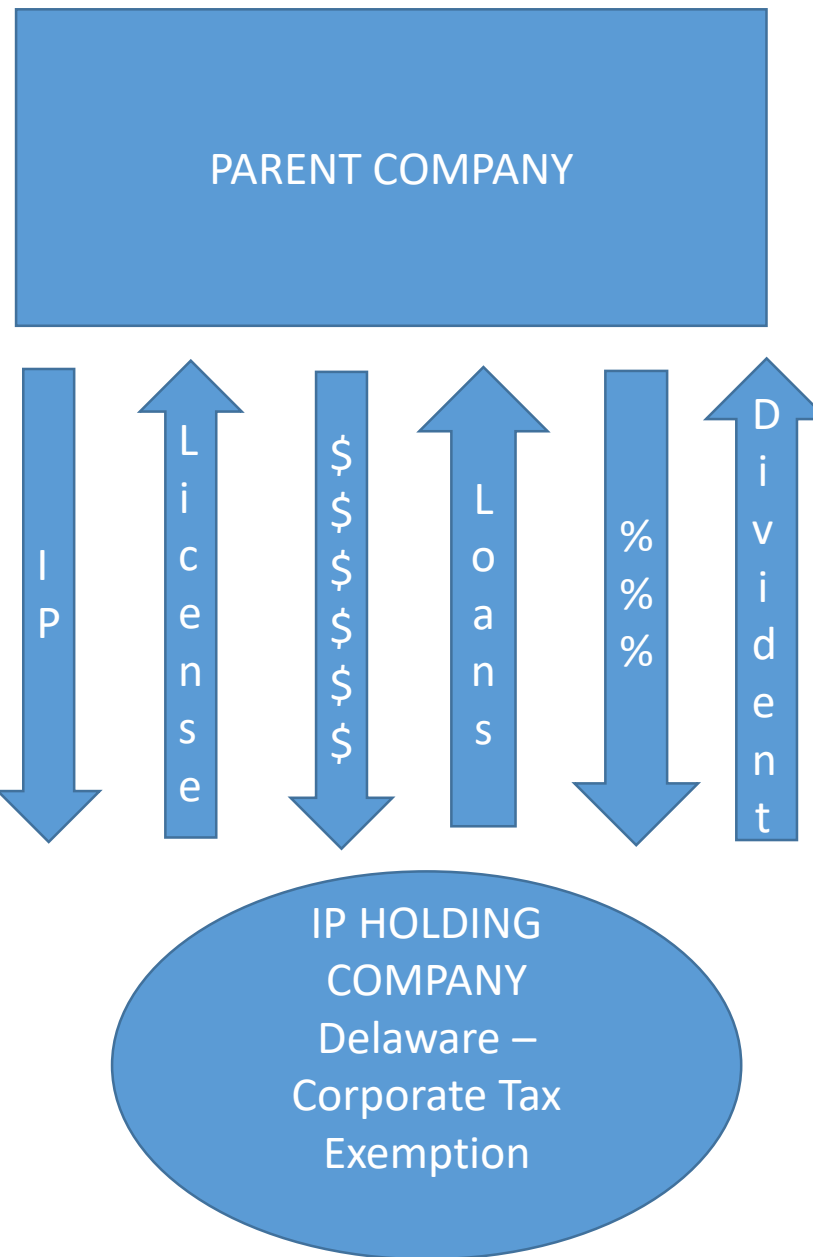


CAMBRIDGE



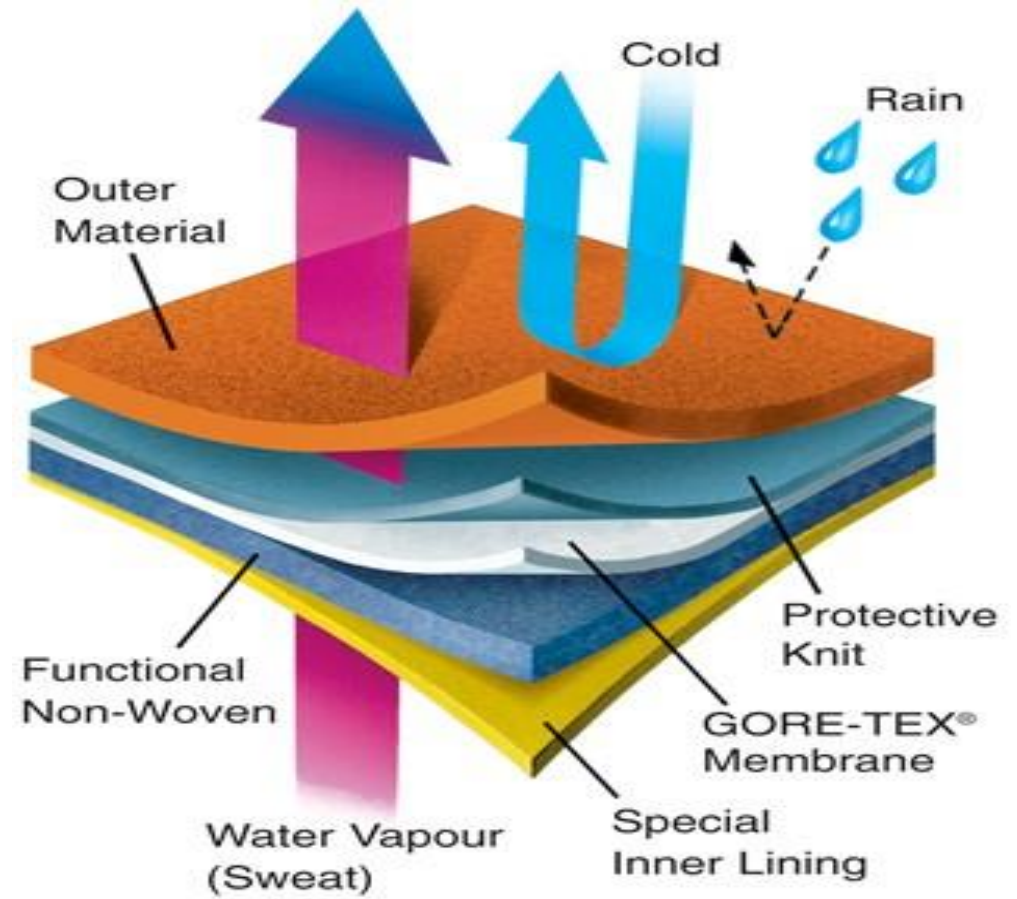
Delaware Legislations: The IP Gift to Corporations

- In 1958: 30 Del. C. §1902(b)(1)-(14) – corporate income tax exemptions
 - Fourteen different groups (fraternities, religious, education, animal cruelty preventions, not-for-profit leagues, etc.)
 - Group 8th – 30 Del. C. §1902(b)(8) - corporations confined to the maintenance and management of their intangible investments (stocks, bonds, notes)
- In 1984:
 - Added in 30 Del. C. §1902(b)(8): (stocks, bonds, notes, ... **patents, patent applications, trademarks, trade names and similar types of intangible assets**).



Sherwin-Williams





Uber

Gore-Tex Case Study

- Annual Sales: \$3 Billion
- 3,500 Patents worldwide in electronics, medical devices, polymer processing, etc.
- Parent Company: \$\$\$ R & D, Inventions, Patents from USPTO; Assigns to Delaware IP Holding Company and Licenses Back
- **Gore Enterprise Holdings, Inc./Delaware IP Holding Company**
 - Zero expense for salary; \$1,583 for rent
 - \$231,000,000 (7.5% royalty rate on the \$3.08 Billion sales)
 - Enjoys Delaware Corporate Tax Exemption
 - Pays No State Tax to Any Other States

EVERYWHERE

- Nordstrom:
 - Paid its Delaware/IP Holding Company \$212,284,273 to use its own Trademark in 2003.
 - Received “loans” from the Delaware/IP Holding Company for slightly lesser amounts during the same period.
 - Deducted royalty payments and interest payments as ordinary and necessary expenses!
 - Delaware/IP Holding Company paid no state tax on \$212,284,273 royalty income in 2003

Surtees v. VFJ Ventures (Ala. Civ. App. 2008)

- VJF
- Lee/Wrangler Jeans:
 - Facilities in Alabama.
 - Sold \$2.1 Billion clothing products in 2001.
 - Paid \$102,000,000 to Delaware/IP Holding Companies for royalties to use the Trademarks Lee and Wrangler.
 - Deducted all \$102,000,000 as ordinary and necessary expenses!

Uber? Lyft?

- 1.45% of \$\$Billions Delaware IP Holding Company Scheme



Delaware and Corporate Irresponsibility

- *Intangible Property* Holding Company Scheme and State Tax Avoidance
- Corporations, Employees and Locality
- Schools, Roads, Infrastructure

ACME Royalty v. Director of Revenue (Missouri 2002)

- Gore-Tex IP Assignment/License Back Scheme Between Parent and Subsidiary Corporations
- **Gore Enterprise Holdings, Inc./Delaware** (royalties from patent licensing)
- Missouri wanted to tax the royalty income generated within the state.
- Court held that the Delaware/IP Holding Company does not have property, payroll, sales in Missouri. It is outside the reach of Missouri taxation.

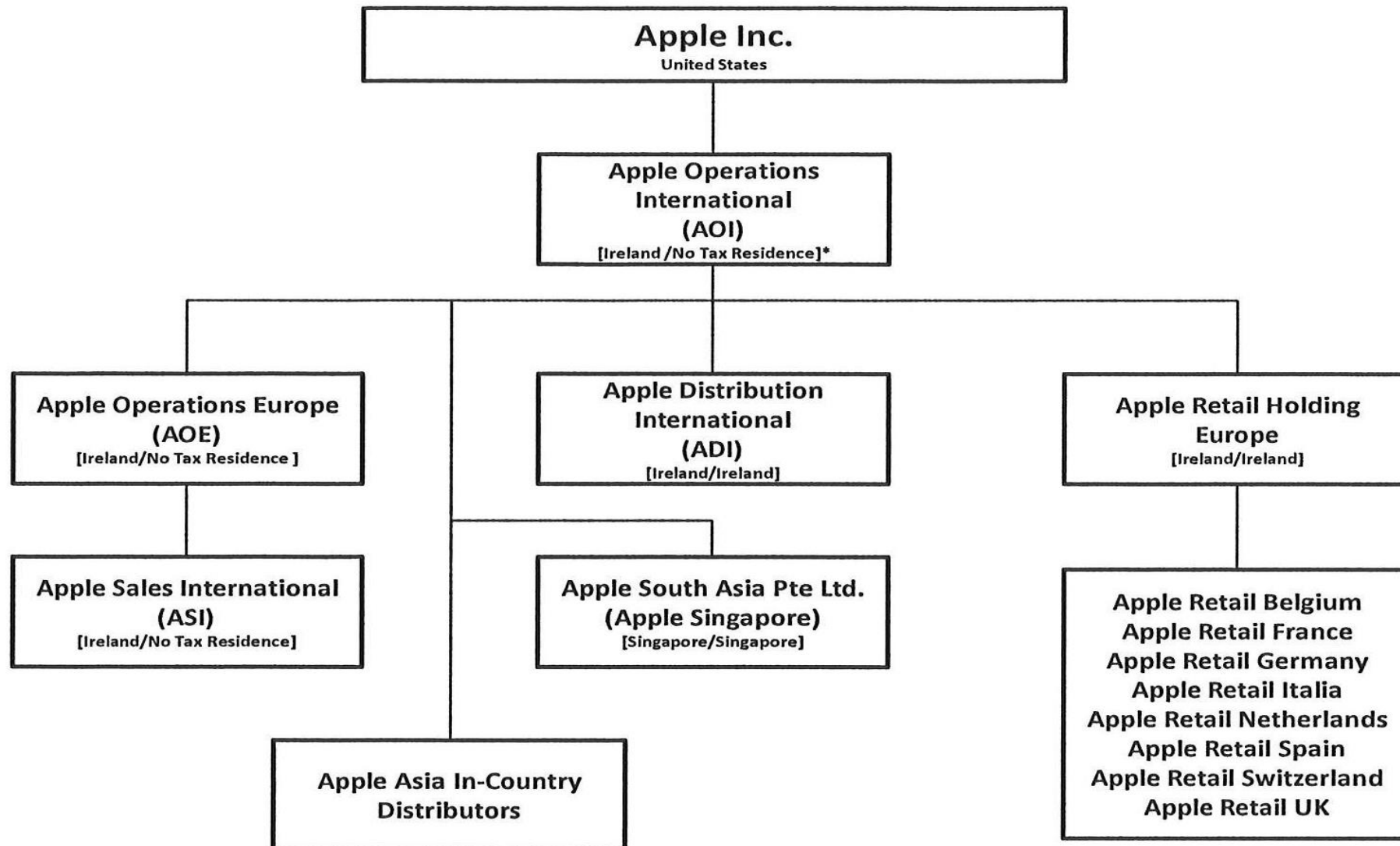
Maryland Court Responded to Gore-Tex & Other IP Holding Companies

- *Gore-Tex v. Comptroller of the Treasury* (87 A.3d 1263 (Md. 2014))
- *Staples, Inc. v. Comptroller of the Treasury* (the Delaware Corporation has no any employee or owns no any real or tangible property in Maryland)
- *Staples the Office Superstore, Inc. v. Comptroller of the Treasury* (the Delaware Corporation has no any employee or owns no any real or tangible property in Maryland)
- Court: Staples and Superstore lacked economic substance as separate business entities. They were part of a unitary business enterprise that included Staples C&C and Staples East.
- Court: Staples and Superstore had nexus with Maryland and were subject to Maryland tax.

Closing the Loophole: State Responses

- Asserting Nexus Over the Out-of-State IP Holding Company
- Disallowing the Parent Company's Deduction of Royalty Payments
- Enacting "Add-Back" Statutes
- Adopting "Combined Reporting"

Apple's Offshore Organizational Structure



*Listed countries indicate country of incorporation and country of tax residence, respectively.

Apple

- In 2011: ASI paid only \$10 million in global taxes despite having \$22 Billion in foreign income (effective tax rate of .05 percent)
- AOI: 0 percent rate.
- Ireland: tax corporations that are managed and controlled in Ireland. (ASI, AOE, AOI are NOT managed and controlled in Ireland. They are not subject to tax in Ireland. They are not subject to U.S. tax because they were incorporated in Ireland)

Microsoft

- Microsoft's main foreign subsidiary is Round Island One (RIO) which is incorporated in Ireland but headquartered in Bermuda.
- Ireland: tax corporations that are managed and controlled in Ireland. (RIO is NOT managed and controlled in Ireland. It is not subject to tax in Ireland. Bermuda tax is 0. It is NOT subject to U.S. tax because it is incorporated in Ireland)
- Microsoft (tier 1) owns Microsoft Singapore Holdings (first-tier sub) which owns Microsoft Asia Island Ltd (MAIL- second-tier sub), a Bermuda IP Holding Company with no employee:
- IP? Cost-sharing arrangement

Uber

- 10 Dutch subsidiaries; 7 out of 10 have no employees
- The Netherlands: effective tax rate of 5%.
- Uber International C.V. (first-tier subsidiary) incorporated in the Netherlands, with headquarters in Bermuda.
- Netherlands: tax corporations that are managed and controlled in the Netherlands (Uber International C.V. is managed and controlled in Bermuda. It is not subject to tax in the Netherlands. Bermuda tax is 0. It is NOT subject to U.S. tax because it is incorporated in the Netherlands).
- Uber and Uber International C.V. entered into a cost-sharing arrangement: Uber International C.V. paid \$1 million for the right to use Uber's IP/tech!