

BF&R Docket No. 2224811  
Petition Filed: 2/17/2023  
Box No. [REDACTED]  
IN RE: GILEAD SCIENCES INC  
PETITION FOR Review of Refund for Corporate Net Income Tax  
PERIOD(S) 2019

AND NOW, July 13, 2023, pursuant to the Fiscal Code, the Act of 1929, April 9, P.L. 343, as amended, (72 P.S. § 1 et seq), the Board of Finance and Revenue of the Commonwealth of Pennsylvania, based upon the reasons set forth herein, hereby ORDERS the following:

### **Jurisdiction**

This matter is before the Board of Finance and Revenue pursuant to Section 2704 of The Tax Reform Code of 1971, 72 P.S. § 9704.

### **Issues**

1. Whether Petitioner included in its sales factor numerator certain receipts from sales of tangible personal property not ultimately destined for and consumed in Pennsylvania?
2. Whether Petitioner is entitled to special apportionment for calculating its corporate net income tax by using an equally weighted three-factor apportionment method?
3. Whether Petitioner is entitled to exclude its royalty, management fee and research and development cost share income from its Pennsylvania taxable income and sales factor as multiform or unrelated income?

### **Statement of the Case**

Petitioner, Gilead Sciences, Inc., a Delaware corporation, developer, producer and seller of pharmaceuticals, requests a refund of 2019 Pennsylvania corporate net income tax based on sales factor and taxable income reductions requested in the above-listed issues.

Petitioner has its headquarters, principal place of business and commercial domicile in Foster City, California. Petitioner is a biopharmaceutical company that discovers, develops and sells commercial pharmaceutical drugs. Petitioner sells and distributes drugs

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internationally and in the United States exclusively through wholesale sales and specialty pharmacies.

Petitioner's mission is to discover and develop transformational therapies in areas of unmet medical need in areas such as viral diseases, inflammatory diseases and oncology. Scientists pursue molecules and technologies leading to the approval of innovative medicines and therapies advancing the current standard of care. Research and development (R&D) costs range from less than \$ [REDACTED] to more than \$ [REDACTED] per drug making up a substantial share of the average total cost of developing a new drug. This development process often takes a decade or more during which Petitioner does not receive financial return on its investment. R&D involves a variety of activities such as invention, clinical testing, applications to the Food and Drug Administration (FDA), incremental innovation and development of dosages, clinical testing of a new drug against an old drug, and safety monitoring or clinical trials to detect side effects. The steps of bringing a drug to market are as follows: discovery and development; pre-clinical research; clinical research; FDA review; and FDA post-market safety monitoring.

Petitioner received royalty income for licensing pharmaceuticals to foreign manufacturers outside the United States such as companies in India, Japan, and Ireland. This is done to enhance distribution and sales in the international market.

Petitioner received management fee income for performing management services for foreign manufacturers outside the United States (Australia and Ireland). Services included R&D sales and marketing.

Petitioner entered cost sharing arrangements with foreign affiliates. Participants share intangible development costs related to Petitioner's R&D outside the United States. Development costs include direct costs, indirect costs, routine costs of intellectual property (IP) protection and other R&D service costs. This arrangement ensures all future IP developed by the foreign affiliates is used in those affiliates' territories and not in the United States.

Petitioner primarily sells products through three large distributors: Cardinal Health, Inc.; McKesson Corp.; and AmerisourceBergen Corp. There is a nationwide sales force of Petitioner's pharmaceutical representatives who meet with healthcare providers prescribing Petitioner's products. These representatives establish a market and create demand for Petitioner's products. Petitioner also markets by television, radio and print advertising campaigns. Petitioner adds that its distributors do not advertise, market or otherwise create demand for Petitioner's products but merely render inventory management and logistics services.

Petitioner filed its 2019 corporate report with the Pennsylvania Department of Revenue claiming a \$ [REDACTED] corporate net income tax liability. This tax was calculated with an \$ [REDACTED] adjusted income apportioned by a factor of [REDACTED] less a net loss deduction of \$ [REDACTED]. The apportionment factor was the product of a sole sales factor, [REDACTED].

Petitioner filed a refund claim based on the above-listed issues at the Board of Appeals (BOA), but the BOA denied relief. Petitioner requested use of equally weighted three apportionment factors because it was a manufacturer relying extensively on capital and labor for which the single sales factor did not adequately reflect Petitioner's business activity in Pennsylvania. Petitioner requested exclusion of its royalties, management fees and research and development cost share income from taxable income and sales factor as wholly unrelated to its activity in Pennsylvania. Petitioner requested reduction of the sales factor numerator to the amount of receipts from product consumed in Pennsylvania and cited as support the case of Com. v. Gilmour Manufacturing Co., 822 A.2d 676 (Pa. 2003) (holding "dock sales" delivered in Pennsylvania to an out-of-state buyer retrieving and transporting these goods out-of-state were not Pennsylvania sales). Three-factor apportionment was denied because the BOA found Petitioner had not clearly shown how the single apportionment factor method did not fairly represent the extent of Petitioner's business activity in Pennsylvania as required by 72 P.S. § 7401(3)2.(a)(18) of the Tax Reform Code. The BOA denied Petitioner's multiform/unrelated income claim because it did not accept Petitioner's interpretation of "ultimate destination" and did not agree Petitioner submitted sufficient evidence proving this claim. The taxable income at issue was "part of Petitioner's unitary business subject to apportionment under the United States Constitution" and "properly included in Petitioner's taxable income." The BOA distinguished Petitioner's case as involving sales to customers' distribution centers in Pennsylvania and found that these facts were outside the parameters of the Gilmour decision.

Petitioner files the instant review of refund at the Board of Finance and Revenue (BF&R) requesting a refund of 2019 corporate net income tax based on the above-listed issues.

Petitioner emphasizes that its products cannot be used when located in a distributor's warehouse, therefore, Petitioner's distributors cannot be the ultimate destinations of Petitioner's products because these distributors are not consumers. The ultimate destination of Petitioner's products are the pharmacies or hospitals where Petitioner's products can be used. Petitioner cites the Gilmour decision arguing that the ultimate destination of the goods, and not the place where the goods are physically delivered to the purchaser, is the controlling factor in determining where a sale is attributed. Petitioner argues that receipts from its sales to distributors were for products consumed throughout the United States and not only in Pennsylvania.

Petitioner describes its business as capital and labor intensive and concludes that a three-factor apportionment method with payroll and property factors should be included in apportionment to properly reflect its business activities in Pennsylvania. Considering shipments to wholesalers as the ultimate destination with a sole sales factor results in a disproportionate apportionment factor.

Petitioner requests multiform/unrelated income treatment for its royalty income, management fee income and research and development cost sharing arrangements income claiming that these incomes are distinctly different from and wholly unrelated to Petitioner's business in Pennsylvania. In 2019, Petitioner claims it received royalty income for licensing its

pharmaceuticals to foreign manufacturers outside the United States. In 2019, Petitioner claims it received income for performing management services for foreign manufacturers outside the United States (in Australia and Ireland). These services were research and development, sales and marketing services. In 2019, Petitioner claims it received income from research and development cost sharing agreements under which participants shared intangible development costs related to Petitioner's research and development outside the United States. There were direct costs, indirect costs, routine costs of intellectual property protection and other research and development service costs. Cost-sharing agreements were to ensure that intellectual property developed by foreign affiliates was used in the foreign affiliates' territories.

### **Conclusion**

Petitioner's refund request is denied because Petitioner is not entitled to the requested sales factor numerator reduction, multiform/unrelated income treatment, or special apportionment.

Petitioner's request to decrease its sales factor numerator is denied because sales with Pennsylvania destinations were correctly included in the sales numerator. Sales of tangible personal property are in Pennsylvania if the property is delivered or shipped to a purchaser, within Pennsylvania, regardless of the f.o.b. point or other conditions of the sale. See 72 P.S. § 7401(3)2.(a)(16); see also Gilmour Mfg. Co. v. Com., 750 A.2d 948 (Pa. Commw. 2000), aff'd, 822 A.2d 676 (Pa. 2003) (Department of Revenue interpretation incorrect for allowing sales to out-of-state purchasers who received products in Pennsylvania and subsequently resold the products outside Pennsylvania to be included as Pennsylvania sales in the sales factor).

Product delivered to distributors in Pennsylvania were Pennsylvania sales. Petitioner provided the distributors' Pennsylvania delivery locations supporting its proposed sales factor numerator, but it was not clear whether those sales were second sales, or whether sales to the distributors in Pennsylvania were the initial Pennsylvania sales; Petitioner did not adequately describe its relationship with the distributors. The reported receipts were correctly included in the sales factor numerator.

The transaction in Gilmour was a dock sale, that is, a sale to an out-of-state purchaser delivered to a Pennsylvania location for pick-up by the purchaser and transportation to the purchaser's out-of-state location. Petitioner effectively argues that sales must be traced through the distribution chain to determine the ultimate destination of sold goods for sales factor purposes, but Gilmour does not support such a method. In this case, Petitioner sold its goods to distributor customers in Pennsylvania and delivered these goods in Pennsylvania; therefore, receipts from these Pennsylvania distributor sales are correctly included in Petitioner's sales factor.

Petitioner's request for multiform income treatment is denied for lack of sufficient evidence proving entitlement to such treatment. See Container Corp. v. Franchise Tax Board of California, 463 U.S. 159 (1983) (assigning burden of proof to taxpayer and requiring taxpayer to clearly show unrelated nature of assets it seeks to exclude); see also Com. v. ACF

Industries, 441 Pa. 129, 142, 271 A.2d 273, 280 (1970) (proposing “a truly divisionalized business conducting disparate activities with each division internally integrated” as the standard for multiform/unrelated assets treatment). Where the Board does not accept Petitioner’s interpretation of “ultimate destination” and does not agree Petitioner submitted sufficient evidence proving its claim, receipts will not be removed from income or from the sales factor.

Petitioner’s request for special apportionment is denied because Petitioner has not shown that the standard apportionment methods did not fairly represent the extent of its business activity within Pennsylvania. See 72 P.S. § 7401(3)2.(a)(18). Petitioner has not provided sufficient evidence on its arrangements with its distributors and product sales and, thus, has not satisfied the condition precedent to special apportionment.

As to Petitioner’s challenge to the validity and/or constitutionality of the statutes at issue, the Board of Finance and Revenue cannot decide whether a Pennsylvania statute is unconstitutional. See Parsowith v. Commonwealth of Pennsylvania Department of Revenue, 555 Pa. 200, 723 A.2d 659 (1999); Land Holding Corp. v. Board of Finance and Revenue, 388 Pa. 61, 130 A.2d 700 (1957). Petitioner has not presented sufficient details or evidence supporting claims that the Department’s application of Pennsylvania law to this case violated the United States or Pennsylvania Constitutions. See 72 P.S. § 9705.

Accordingly, this Board enters the following:

**ORDER**

This petition is denied.

**By Order Of The Board Of Finance And Revenue**

**Jacqueline A. Cook, Chair**  
**Designee for Stacy Garrity, State Treasurer**

**David R. Kraus, Board Member**

**Paul J. Gitnik, Board Member**

