

1 **H. B. 2993**

2  
3 (By Delegates White and T. Campbell)

4 (By Request of the State Tax Division)

5 [Introduced February 2, 2011; referred to the  
6 Committee on Finance.]

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9  
10 A BILL to amend and reenact §11-13AA-3, §11-13AA-4, §11-13AA-5,  
11 §11-13AA-7, §11-13AA-11 and §11-13AA-12 of the Code of West  
12 Virginia, 1931, as amended, all relating to the West Virginia  
13 Commercial Patents Incentives Tax Act, defining terms;  
14 clarifying carryover provisions; specifying when credit  
15 accrues; disallowing credit based on related party  
16 transactions; disallowing application of credit in addition to  
17 specified other tax credits; making technical corrections to  
18 use appropriate terminology; and retroactively adjusting the  
19 effective date language.

20 *Be it enacted by the Legislature of West Virginia:*

21 That §11-13AA-3, §11-13AA-4, §11-13AA-5, §11-13AA-7,  
22 §11-13AA-11 and §11-13AA-12 of the Code of West Virginia, 1931, as  
23 amended, be amended and reenacted, all to read as follows:

24 **ARTICLE 13AA. COMMERCIAL PATENT INCENTIVES TAX ACT.**

1 **§11-13AA-3. Definitions.**

2 (a) *General.* -- When used in this article, or in the  
3 administration of this article, terms defined in subsection (b) of  
4 this section have the meanings ascribed to them by this section,  
5 unless a different meaning is clearly required by either the  
6 context in which the term is used, or by specific definition, in  
7 this article.

8 (b) *Terms defined.* --

9 (1) "Agreement" means any agreement or contractual  
10 relationship entered into after the effective date of this section  
11 between Marshall University or West Virginia University and a  
12 person developing patents in this state ~~and~~ that is either:

13 (A) A corporation established under the laws of this state  
14 that meet the requirements of section three, article twelve,  
15 chapter eighteen-b of this code; or

16 (B) A center for economic development and technological  
17 advancement created pursuant to section three, article twelve-a,  
18 chapter eighteen-b of this code.

19 (2) "Business activity" means all activities engaged in or  
20 caused to be engaged in by a person with the object of gain or  
21 economic benefit, direct or indirect. For purposes of this  
22 definition, the term "gain or economic benefit, direct or indirect"  
23 does not include income realized by any person in the form of  
24 wages, salary or income that is reported on federal form W-2.

1           (3) "Commercial use" means selling, licensing, leasing or  
2 otherwise making patents available to a third party for a price,  
3 fee, royalty, commission or other consideration called by whatever  
4 name. "Commercial use" also means, in the case of patents  
5 developed by the developer for the developer's own commercial use,  
6 the first use of the patents in a manufacturing or other business  
7 activity of the developer. "Commercial use" does not include any  
8 selling, licensing, leasing or otherwise making patents available  
9 to a third party when done by a broker or by any person who does  
10 not own the patent sold, licensed, leased or otherwise made  
11 available.

12           (4) "Commissioner" and "Tax Commissioner" are used  
13 interchangeably herein and mean the Tax Commissioner of the State  
14 of West Virginia or his or her designee.

15           (5) "Copyright" means a copyright that is registered with the  
16 United States Copyright Office or with a similar office of a  
17 foreign country when the foreign copyright is recognized under  
18 federal law.

19           ~~(6) "Credit year" means the taxable year in which the person~~  
20 ~~realizes the net profit attributable to a patent. In the case of~~  
21 ~~a license or lease to use patents, "credit year" means each taxable~~  
22 ~~year during the term of the license or lease to use patents.~~

23           ~~(7)~~ (6) "Delegate" in the phrase "or his or her delegate",  
24 when used in reference to the Tax Commissioner, means any officer

1 or employee of the Tax Department of the Department of Revenue duly  
2 authorized by the Tax Commissioner directly, or indirectly, by one  
3 or more redelegations of authority to perform the functions  
4 mentioned or described in this article.

5 (7) "Development of a patent," "developing patents" or  
6 "development" means the act of fostering, causing or accelerating  
7 the progress of a process, or a machine, or the manufacturing of  
8 product, or a composition of matter, or improvement thereto through  
9 significant investment of money, performance of research, or  
10 application of design or engineering expertise, which culminates in  
11 the issuance of a patent, as defined in this article, for that  
12 process, machine, manufacturing of a product, composition of  
13 matter, or improvement.

14 (8) "Developer" means a person engaged in this state in  
15 developing patents for direct use in a manufacturing process or  
16 product and who has an agreement, as defined in this section, with  
17 Marshall University or West Virginia University.

18 (9) "Directly used in manufacturing process or product, "and  
19 "direct use in manufacturing process or product" with reference to  
20 patents ~~mean the use of patents directly in those activities or~~  
21 ~~operations which constitute an integral and essential part of the~~  
22 ~~manufacturing processes and products, as contrasted with and~~  
23 ~~distinguished from those activities or operations which are simply~~  
24 ~~incidental, convenient or remote to the manufacturing activity such~~

1 ~~as those activities that are incidental. Those activities that are~~  
2 ~~incidental to business activities such as bills, marketing,~~  
3 ~~inventory control, order fulfillment, shipping and tracking are not~~  
4 ~~considered an integral and essential part of the manufacturing~~  
5 process or product means application or incorporation of a patented  
6 process, machine, manufactured article or composition of matter, in  
7 manufacturing operations or processes, or in manufactured products,  
8 in circumstances where United States or foreign patent laws require  
9 that the specific patent for the process, machine, manufactured  
10 article or composition of matter be owned by the manufacturer, or  
11 purchased, leased, licensed or authorized by contract to be applied  
12 or incorporated in the manufacturing operation, processes or  
13 product, and where such lawful ownership, purchase, lease,  
14 licensure or contractual authorization is in effect.

15 (10) "Manufacturing" means any business activity classified as  
16 having a sector identifier, consisting of the first two digits of  
17 the six-digit North American Industry Classification System code  
18 number of thirty-one, thirty-two or thirty-three.

19 (11) "Mask work" means a series of related images, however  
20 fixed or encoded:

21 (A) Having or representing the predetermined, three-  
22 dimensional pattern of metallic, insulating or semiconductor  
23 material present or removed from the layers of a semiconductor chip  
24 product; and

1 (B) In which series the relation of the images to one another  
2 is that each image has the pattern of the surface of one form of  
3 the semiconductor chip product.

4 (12) "Owner", when used in reference to a pass-through entity,  
5 means a person who owns an equity interest in the pass-through  
6 entity.

7 (13) "Partnership" includes a syndicate, group, pool, joint  
8 venture or other unincorporated organization through or by means of  
9 which any business, financial operation or venture is carried on,  
10 which is not a sole proprietorship, trust or estate, and which is  
11 treated as a partnership for federal income tax purposes for the  
12 taxable year.

13 (14) "Pass-through entity" means a partnership, limited  
14 liability company, small business corporation (S corporation) or  
15 other entity treated as a partnership for federal income tax  
16 purposes for the taxable year.

17 (15) "Patent" means a United States or foreign national patent  
18 grant or United States certificate of invention or certificate of  
19 protection under the Plant Variety Protection Office of the United  
20 States Department of Agriculture and is limited to patents  
21 developed in this state for direct use in a manufacturing process  
22 or product, or both developed for use and directly used in a  
23 manufacturing process or product in this state. For purposes of  
24 this article, patents do not include copyrights, trademarks, mask

1 works, trade secrets or any intellectual property that is not a  
2 patent.

3       (16) "Person" includes a natural person, corporation, limited  
4 liability company or partnership. A single member liability  
5 company that is treated as a disregarded entity for federal income  
6 tax purposes is be treated as a disregarded entity for purposes of  
7 this article.

8       (17) "Purchase" means a transaction under which title to an  
9 item is transferred for consideration, or a license or lease  
10 contract for at least three years is executed, regardless of  
11 whether title to the item is transferred at the end of the lease or  
12 license period.

13       (18) "Taxpayer" means any person subject to the tax imposed by  
14 article twenty-three or twenty-four of this chapter or to both  
15 taxes. In the case of a sole proprietorship that is not subject to  
16 either the tax imposed by article twenty-three or twenty-four of  
17 this chapter, the term "taxpayer" means a natural person who owns  
18 a disregarded entity and who is subject to the tax imposed by  
19 article twenty-one of this chapter on his or her income from  
20 business activity in this state, or any sole proprietor who is  
21 subject to the tax imposed by article twenty-one of this chapter.

22       (19) "Trademark" means any trademark, trade name, service mark  
23 or other identifying symbol or name that is registered with the  
24 United States Patent and Trademark Office or with a similar office

1 of a foreign country when the foreign registration is recognized  
2 under federal law.

3 (20) "Trade secret" means information, including a formula,  
4 pattern, compilation, program device, method, technique or process,  
5 that:

6 (A) Derives independent economic value, actual or potential,  
7 from not being generally known to, and not being readily  
8 ascertainable by proper means, by other persons who can obtain  
9 economic value from its disclosure or use; and

10 (B) Is the subject of efforts that are reasonable under the  
11 circumstances to maintain its secrecy.

12 **§11-13AA-4. Tax incentive for developing patents in this state.**

13 (a) *Allowance of credit.* -- A person engaging in this state in  
14 developing patents for direct use in a manufacturing process or  
15 product and who has an agreement, as defined in section three of  
16 this article, with Marshall University or West Virginia University  
17 is allowed a credit, when computing the person's liability for  
18 business franchise tax imposed by article twenty-three of this  
19 chapter and corporation net income tax imposed by article twenty-  
20 four of this chapter, in the amount allowed under subsection (b) of  
21 this section. When the developer is a sole proprietor or a pass-  
22 through entity, that amount of the credit remaining after first  
23 applying it against the tax liability under article twenty-three of  
24 this chapter for the taxable year is allowed when computing the tax



1 imposed by article twenty-one of this chapter on income from the  
2 person's business activity. No credit is allowed under this  
3 article for any activity, investment, assets, or expenditures for  
4 which any of the tax credits authorized under articles thirteen-d,  
5 thirteen-e, thirteen-q, thirteen-r, thirteen-s, or thirteen-x of  
6 this chapter, has been authorized, taken or allowed. No credit is  
7 allowed under this article for any activity, investment, assets, or  
8 expenditures for which the tax credits authorized under article  
9 thirteen, chapter eighteen-b, has been, authorized, taken or  
10 allowed.

11 (b) *Amount of credit.* -- The amount of credit allowed under  
12 this section is equal to twenty percent of the royalties, license  
13 fees or other consideration received by the developer during the  
14 taxable year from the sale, lease or licensing of a patent  
15 developed in this state for direct use in a manufacturing process  
16 or product by the person in taxable years beginning on or after  
17 January 1, 2011: *Provided,* That the amount of credit allowed under  
18 this section is thirty percent, rather than twenty percent, when  
19 the person reinvests at least eighty percent of the amount of the  
20 credit claimed for the taxable year in depreciable property  
21 purchased for purposes of developing additional patents in this  
22 state in taxable years beginning on or after January 1, 2011, or  
23 improving upon a patent developed in this state or contributing to  
24 a stipend to retain a graduate or post-doctoral student in this

1 state integral to the development of the patents or related  
2 technology in taxable years beginning on or after January 1, 2011,  
3 during the next taxable year of the person, and the person has an  
4 agreement, as defined in section three of this article, for the  
5 development of a patent.

6 (c) *Rules for application of credit.* -- The amount of credit  
7 computed under this section is allowed in accordance with the  
8 following rules and applied as provided in subsection (d) of this  
9 section:

10 (1) No credit is allowed under this section for royalties,  
11 rents, license fees or other consideration received by the  
12 developer of the patent for a patent developed outside this state,  
13 except as provided in subdivision (2) of this subsection;

14 (2) When the person developed the patent for direct use in a  
15 manufacturing process or product through that person's activity in  
16 this state and through that person's activity in one or more other  
17 states, the consideration received by the developer during the  
18 taxable year from the sale, lease or license of the patent  
19 developed through multistate activity of the developer is  
20 multiplied by a fraction, the numerator of which is the direct  
21 costs of developing the patent in this state and the denominator of  
22 which is the total direct costs of developing the patent. The  
23 product of this computation establishes the consideration to be  
24 used in subsection (b) of this section;

1           (3) If a person receives a portion of a royalty that would be  
2 eligible for a tax credit under this section because of a business  
3 association, licensing agreement or otherwise, the person may  
4 receive the tax credit allowable to the portion of royalties that  
5 person receives provided the person has an agreement, as defined in  
6 section three of this article, with Marshall University or West  
7 Virginia University and otherwise meets the requirements for  
8 entitlement to this credit, as set forth in subsection (a) of this  
9 section;

10           (4) Unused credit may be carried forward until the earlier of  
11 the tax year when the credit is used up or ~~used for a period of~~  
12 ~~nine~~ the ninth consecutive tax year after ~~the taxable year in~~  
13 ~~which the credit allowed by this section accrues to the person~~ the  
14 first tax year in which the taxpayer is eligible to claim the  
15 credit. When the person is an owner of a pass-through entity,  
16 credit ~~accrues to~~ may be taken by the owner beginning in the tax  
17 year when ~~it accrues to~~ credit may be taken by the pass-through  
18 entity or when the pass through entity gains entitlement to the  
19 credit;

20           (5) No credit is allowed under this section for consideration  
21 received by the developer for patents developed for direct use in  
22 a manufacturing process or product before the taxable year  
23 beginning January 1, 2011. For purposes of this subdivision, a  
24 patent was developed for direct use in a manufacturing process or

1 product before January 1, 2011, if ~~before that date~~ it was sold,  
2 leased or licensed to a third party prior to January 1, 2011, or  
3 before that day it was reduced to practice for purely commercial  
4 purposes by the developer or a person related to the developer, as  
5 defined in subsection (b), Section 267 of the Internal Revenue Code  
6 of 1986, as amended; ~~and as defined in section nine, article~~  
7 ~~twenty-one of this chapter or section three, article twenty-four of~~  
8 ~~this chapter; and~~

9       (6) No credit is allowed under this section for consideration  
10 received by the developer from a person related to the developer,  
11 as defined in subsection (b), Section 267 of the Internal Revenue  
12 Code of 1986, as amended for patents developed for direct use in a  
13 manufacturing process or product; and

14       ~~(6)~~ (7) No credit is allowed under this section beginning with  
15 the eleventh taxable year after the patent was first directly used  
16 in a manufacturing process or product.

17       (d) *Application of credit.* -- The amount of the credit  
18 computed under this section is allowed as a credit against tax as  
19 provided in this subsection, but the credit may not reduce the tax  
20 below zero.

21       (1) *Business franchise tax.*-- The amount of the allowable  
22 credit shall first be taken as a credit against the tax liability  
23 of the developer for the taxable year under article twenty-three of  
24 this chapter.

1           (2) *Corporation net income tax.* -- The amount of the allowable  
2 credit remaining, if any, after first applying the credit against  
3 the tax imposed by article twenty-three of this chapter shall then  
4 be taken as a credit when computing the liability of the developer  
5 for the taxable year under article twenty-four of this chapter.

6           (3) *Personal income tax on business income.* --

7           (A) When the developer is a sole proprietor, the amount of the  
8 allowable credit is taken as a credit when computing the liability  
9 of the developer for the taxable year on business income under  
10 article twenty-one of this chapter.

11           (B) When the developer is a pass-through entity, the amount of  
12 allowable credit remaining, if any, after first applying the credit  
13 against the tax imposed by article twenty-three of this chapter for  
14 the taxable year is allowed as a credit against the tax imposed for  
15 the taxable year on the West Virginia source income of the pass-  
16 through entity under article twenty-one of this chapter and the  
17 amount of the credit is distributed to the owners of the pass-  
18 through entity in the same manner as items of partnership income,  
19 gain loss or deduction are distributed or allocated for the taxable  
20 year.

21 **§11-13AA-5. Tax credit for use of a patent in a manufacturing**  
22 **process or product in this state that was developed**  
23 **in this state.**

1           (a) *Allowance of credit.* -- A person directly using a patent  
2 developed in this state in a manufacturing process or product in  
3 this state is allowed a credit against the person's liability for  
4 business franchise tax imposed by article twenty-three of this  
5 chapter and corporation net income tax imposed by article twenty-  
6 four of this chapter, the amount computed under subsection (b) of  
7 this section. When the user of a patent is a sole proprietor or a  
8 pass-through entity, that amount of credit allowed against income  
9 taxes shall be against the tax imposed by article twenty-one of  
10 this chapter.

11           (b) *Amount of credit.* -- The amount of credit allowed under  
12 this section is equal to twenty percent of the net profit  
13 attributable to the patent: *Provided,* That the amount of credit  
14 allowed under this section is equal to thirty percent of the net  
15 profit attributable to the patent when the person claiming the  
16 credit reinvests in capital improvements to add product lines to or  
17 increase productivity in this state during the next taxable year an  
18 amount equal to at least eighty percent of the tax credit amount  
19 used for the taxable year. For purposes of this article, the term  
20 "net profits" means West Virginia taxable income as determined for  
21 purposes of article twenty four of this chapter, before application  
22 of this credit and after application of all credits allowable under  
23 this chapter except this credit. In the case of taxpayers that are  
24 not subject to the tax imposed by article twenty-four, "net

1 profits" means West Virginia taxable income as determined for  
2 purposes of article twenty-one of this chapter, before application  
3 of this credit and after application of all credits allowable under  
4 this chapter except this credit. In circumstances where net profit  
5 is not solely attributable to and the exclusive result of the  
6 direct use of a patent in a manufacturing process or product in  
7 this state, the taxpayer shall determine net profit solely  
8 attributable to and the exclusive result of the direct use of a  
9 patent in a manufacturing process or product in this state, and net  
10 profit for purposes of determining the amount of credit allowable  
11 under this article shall be the net profit solely attributable to  
12 and the exclusive result of the direct use of a patent in a  
13 manufacturing process or product in this state.

14 (c) *Rules for application of credit.* -- The amount of credit  
15 computed under this section is allowed in accordance with the  
16 following rules and applied as provided in subsection (d) of this  
17 section:

18 (1) The credit allowed by this section is applied after all  
19 other credits allowed by this chapter have been applied against the  
20 person's business franchise tax and West Virginia income tax  
21 liabilities for the taxable year under this chapter;

22 (2) Unused credit may be carried forward until the earlier of  
23 the tax year when the credit is used up or used for a period of  
24 nine the ninth consecutive tax year after the taxable year in which

1 ~~the credit allowed by this section accrues to the person~~ the first  
2 tax year in which the taxpayer is eligible to claim the credit.  
3 When the person is an owner of a pass-through entity, credit  
4 ~~accrues to~~ may be taken by the owner beginning in the tax year when  
5 ~~it accrues to~~ credit may be taken by the pass-through entity or  
6 when the pass through entity gains entitlement to the credit;

7 (3) Any credit not used within the ten-year period described  
8 in subdivision (2) of this subsection is forfeited beginning with  
9 the eleventh taxable year after the ~~taxable year in which the~~  
10 ~~credit accrued to the person~~ first tax year in which the taxpayer  
11 is eligible to claim the credit;

12 (4) No credit is allowed under this section for using a patent  
13 in this state when the person began using the patent before January  
14 1, 2011;

15 (5) No credit is allowed under this section for using a patent  
16 in this state for which the taxpayer is allowed credit under  
17 another article of this chapter.

18 (6) No credit is allowed under this section for any patent  
19 acquired from, by or between, leased from, by or between, licensed  
20 from, by or between, or otherwise authorized to be used from, by or  
21 between related persons, as defined in subsection (b), Section 267  
22 of the Internal Revenue Code of 1986, as amended.

23 (7) Amounts received from, by or between related persons, as  
24 defined in subsection (b), Section 267 of the Internal Revenue Code



1 of 1986, as amended, are disallowed when calculating net profit  
2 attributable to a patent.

3 (d) *Application of credit.* -- The amount of the credit  
4 computed under this section is allowed as a credit against tax as  
5 provided in this subsection, but the credit may not reduce the tax  
6 below zero.

7 (1) *Business franchise tax.* -- The amount of the allowable  
8 credit shall first be taken as a credit against the tax liability  
9 of the person allowed the credit for the taxable year under article  
10 twenty-three of this chapter.

11 (2) *Corporation net income tax.* -- The amount of the allowable  
12 credit remaining, if any, after first applying the credit against  
13 the tax imposed by article twenty-three of this chapter shall then  
14 be taken as a credit when computing the liability of the  
15 corporation for the taxable year under article twenty-four of this  
16 chapter.

17 (3) *Personal income tax on business income.* --

18 (A) When the person allowed the credit is a sole proprietor,  
19 the amount of the allowable credit is taken as a credit when  
20 computing the liability of the person allowed the credit for the  
21 taxable year on business income under article twenty-one of this  
22 chapter.

23 (B) When the person allowed the credit is a pass-through  
24 entity, the amount of allowable credit remaining, if any, after

1 first applying the credit against the tax imposed by article  
2 twenty-three of this chapter for the taxable year is allowed as a  
3 credit against the tax imposed for the taxable year on the West  
4 Virginia source income of the pass-through entity under article  
5 twenty-one of this chapter and the amount of the credit is  
6 distributed to the owners of the pass-through entity in the same  
7 manner as items of partnership income, gain loss or deduction are  
8 distributed or allocated for the taxable year.

9 **§11-13AA-7. Identification of a patent and required records.**

10 (a) *Required records.* -- Every developer of a patent in this  
11 state for direct use in a manufacturing process or product and  
12 every person who uses a patent directly in a manufacturing process  
13 or product in this state who claims a credit under this article  
14 shall maintain sufficient records to establish the following facts  
15 for each item of a patent for which a credit is allowed under this  
16 article:

17 (1) Its identity;

18 (2) The amount of net profit attributable to the patent;

19 (3) The month and taxable year in which the patent was first  
20 used, placed in service or directly used in the person's  
21 manufacturing process or product in this state;

22 (4) The amount of credit taken; and

1           (5) The date the patent was disposed of or otherwise ceased to  
2 be directly used in the person's manufacturing process or product  
3 in this state.

4           (b) *Enhanced ~~deduction of credit.~~* -- Any person who claims the  
5 enhanced credit under section four or five of this article shall  
6 maintain sufficient records to clearly establish entitlement to  
7 claim the amount of the enhanced credit. At a minimum those  
8 records shall identify:

9           (1) Each and every item of depreciable property purchased for  
10 purposes of claiming the enhanced credit;

11           (2) The date the depreciable property identified in  
12 subdivision (1) of this subsection was purchased, its cost and its  
13 estimated useful life determined using ~~strait~~ straight-line method  
14 of depreciation;

15           (3) The date the depreciable property identified in  
16 subdivision (1) of this subsection was placed in service or used in  
17 the person's business activity in this state;

18           (4) The date the depreciable property identified in  
19 subdivision (1) of this subsection was taken out of service or use  
20 in the person's business activity in this state and the reason why  
21 the property was taken out of service or use; and

22           (5) Other information that the Tax Commissioner may reasonably  
23 require by rule promulgated as provided in section eleven of this  
24 article.

1 (c) *New jobs.* -- Every person who claims a credit under this  
2 article shall also maintain sufficient records to establish the  
3 number and types of new jobs, if any created, the wages and  
4 benefits paid to employees filling the new jobs and the duration of  
5 each job.

6 (d) *Exception.* -- This section does not apply to an owner of  
7 a pass-through entity that develops or uses a patent for which a  
8 credit is allowed under this article.

9 **§11-13AA-11. Interpretation and construction.**

10 (a) No inference, implication or presumption of legislative  
11 construction or intent may be drawn or made by reason of the  
12 location or grouping of any particular section, provision or  
13 portion of this article; and no legal effect may be given to any  
14 descriptive matter or heading relating to any section, subsection  
15 or paragraph of this article.

16 (b) The provisions of this article shall be ~~reasonably~~  
17 strictly construed in order to effectuate the legislative intent  
18 recited in section two of this article.

19 **§11-13AA-12. Effective date.**

20 The provisions of this article retroactively become effective  
21 on ~~July~~ January 1, 2011, and apply only to a patent developed in  
22 this state ~~after the taxable years~~ in tax years beginning on or  
23 after January 1, 2011, and to a patent purchased, leased or

1 licensed for use on or after that date for direct use in the  
2 taxpayer's manufacturing process or product in this state.

NOTE: The purpose of this bill is to make technical changes to correct some infirmities related to incorrect terminology, unworkable effective dates, and to disallow some related transactions within the Commercial Patent Incentives Tax Act.

Strike-throughs indicate language that would be stricken from the present law, and underscoring indicates new language that would be added.