

MANUFACTURING PROPERTY TAX ADJUSTMENT CREDIT

REPORT TO THE JOINT COMMITTEE ON GOVERNMENT AND FINANCE

July 1, 2021

Submitted by:

West Virginia State Tax Department
Matthew R. Irby
State Tax Commissioner

MANUFACTURING PROPERTY TAX ADJUSTMENT CREDIT

This report is submitted to the Joint Committee on Government and Finance pursuant to the provisions of West Virginia Code §11-13Y-8(a), which requires in pertinent part:

“The Tax Commissioner shall provide to the Joint Committee on Government and Finance by the first day of July, two thousand eleven, and on the first day of July of each year thereafter, a report detailing the amount of credit claimed pursuant to this article. The report is to include the amount of credit claimed against the business franchise tax and the amount of credit claimed against the corporate net income tax.”

In conformity with the above requirement, the following report provides details on the Manufacturing Property Tax Adjustment Credit (Inventory Tax Credit) from Corporation Net Income Tax (CNIT) and Business Franchise Tax (BFT) returns in State Tax Department databases as of May 28, 2021.¹

Description of the Inventory Tax Credit

As with all other businesses, manufacturers are subject to both State and local taxes. State and local taxes may include tangible personal property taxes on manufacturing inventory, other than finished goods inventory destined for export outside the State. Several tax reform studies have recommended repeal of manufacturing inventory property taxes. However, the tax on inventory is provided for in the West Virginia Constitution and generally benefits local governments. Thus, any change in the tax on inventory would require a Constitutional Amendment to be ratified by the State’s electorate. The Manufacturing Property Tax Adjustment Credit enacted by Chapter 215, Acts of the Legislature, Regular Session, 2008 provides some tax relief to manufacturers without directly reducing revenue for local governments.

As codified in West Virginia Code §11-13Y-1 *et seq.*, eligible Taxpayers are allowed a tax credit in an amount equal to the West Virginia Property Tax paid by the Taxpayer on the value of manufacturing inventory of the eligible Taxpayer during the Corporation Net Income Tax or Business Franchise Tax year. The credit was effective for tax years beginning on or after January 1, 2009. Pertinent definitions related to the Manufacturing Property Tax Adjustment Credit included in the Statute are as follows:

"Eligible taxpayer" means any manufacturing business that is subject to the tax imposed under article twenty-three [§§11-23-1 *et seq.*] or twenty-four [§§11-24-1 *et seq.*] of this chapter, or both: *Provided*, That taxpayers owning property assessed by the Board of Public Works are not eligible taxpayers for purposes of this article. "Eligible taxpayer" also means and includes those members of an affiliated group of taxpayers engaged in a unitary business, in which one or more members of the affiliated group is a person subject to the tax imposed under article twenty-three or article twenty-four of this chapter, or both. Affiliates not engaged in the unitary business do not qualify as eligible taxpayers.

¹ The Business Franchise Tax was eliminated for taxable years beginning on and after January 1, 2015. For this reason, Inventory Tax Credit claims beyond calendar year 2014 are restricted to claims against the Corporation Net Income Tax.

"Manufacturing business" means any business primarily engaged in business activity classified as having a sector identifier, consisting of the first two digits of the six-digit North American Industry Classification System code number, of thirty-one, thirty-two or thirty-three that also paid ad valorem property tax on manufacturing inventory to one or more West Virginia counties during the taxable year.

"Manufacturing inventory" means and is limited to raw materials, goods in process and finished goods of a business primarily engaged in business activity classified as having a sector identifier, consisting of the first two digits of the six-digit North American Industry Classification System code number, of thirty-one, thirty-two or thirty-three.

"Pass-Through Entities" include Sub-Chapter S-corporations, partnerships and other business types treated in a similar manner.

"Tax year" or "taxable year" means the tax year of the taxpayer for federal income tax purposes.

"Taxpayer" means any person subject to the tax imposed under article twenty-three [§§11-23-1 et seq.] or twenty-four [§§11-24-1 et seq.] of this chapter, or both.

Data Notes

Taxpayers use a variety of taxable periods for purposes of filing income tax returns. For consistency, the Tax Years reported in this document reflect the year in which a Taxpayer's taxable year begins. For example, some Taxpayers are calendar year filers (*i.e.*, Tax Year 2020 began on January 1, 2020) while others are fiscal year filers² (*e.g.*, Tax Year 2020 began on July 1, 2020). Although the statutory due dates³ of tax returns for calendar year Taxpayers occurred before the analysis date (*i.e.*, May 28, 2021) of this report, many Taxpayers use an automatic six-month extension of time before filing final returns with credit claims. Most returns of fiscal year taxpayers would not be due until after the analysis date. Given that the majority of both calendar year and fiscal year 2020 returns had not yet been filed or fully processed by the Tax Department at the time of this analysis, Tax Year 2020 credit claims are omitted from this report. In addition, due to the complex nature of some tax returns, many Tax Year 2019 returns have yet to be fully processed.

To not misrepresent State Inventory Tax Credit claims, statistical results for all taxable periods—particularly more recent Tax Years—may not include certain returns which are not finalized and thus do not represent complete records of manufacturing inventory tax credit claims. Additionally, tax returns can generally be amended through the third year following the original due date of the return. It is important to note that credit claims for Tax Years 2017, 2018, and 2019 as provided

² Statutory due dates for fiscal year Taxpayers are on or before the 15th day of the third month following the close of the taxable year for Pass-Through Entities and Partnerships or the 15th day of the fourth month following the close of the taxable year for C-Corporations.

³ Tax Year 2020 due dates are March 15, 2021 for Pass-Through Entities treated as a partnership for federal and state income tax purpose and April 15, 2021 for C-Corporations and limited liability companies that elect to be treated as a corporation for federal and state income tax purposes.

in the tables and figures of this report may be subject to revision by the Taxpayer or upon audit by the Tax Department.

Manufacturing Property Tax Adjustment Credit Claimed

Table 1 and Figure A provide data collected from Inventory Tax Credit claims by tax and business type as reported on Corporation Net Income Tax and Business Franchise Tax returns for Tax Years 2009 through 2019. Business Franchise Tax returns are separated into those for Pass-Through Entities (PTEs) and C-Corporations (C-Corp). Appendix A provides changes in the claims of this credit between the July 1, 2020 report and current reports for the most recent five taxable periods.

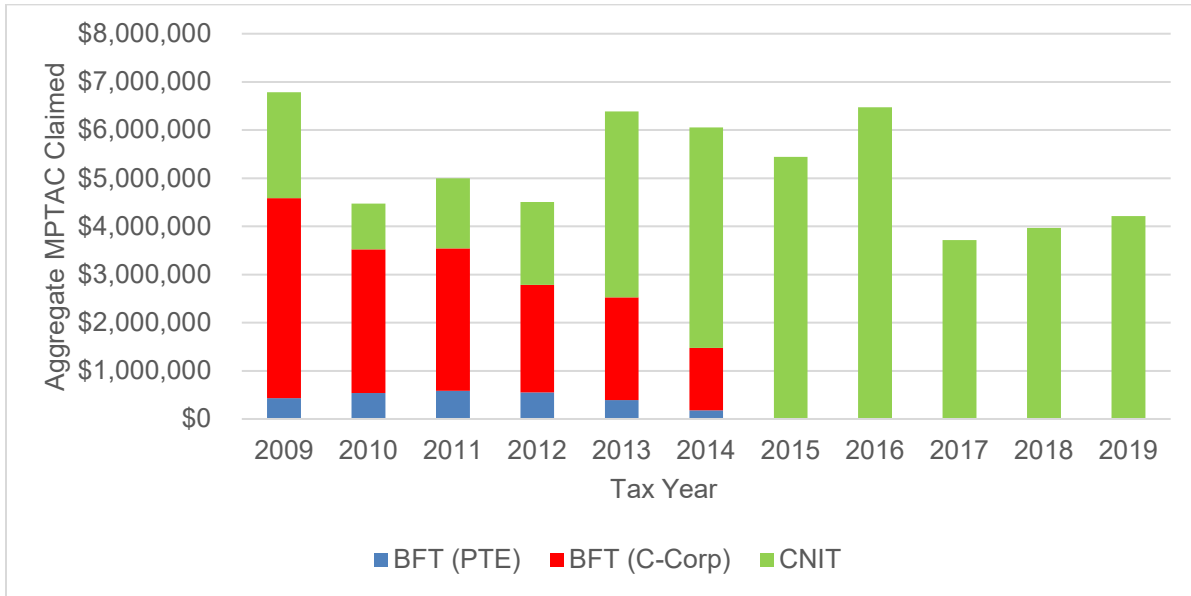
**Table 1
State Inventory Tax Credit Claims by Tax and Business Type**

Tax Year	BFT (PTE)	BFT (C-Corp)	CNIT	Total
2009	\$ 432,473	\$ 4,154,918	\$ 2,196,430	\$ 6,783,821
2010	\$ 536,322	\$ 2,983,392	\$ 950,770	\$ 4,470,484
2011	\$ 588,395	\$ 2,951,417	\$ 1,458,096	\$ 4,997,908
2012	\$ 549,663	\$ 2,232,806	\$ 1,722,414	\$ 4,504,883
2013	\$ 394,511	\$ 2,133,700	\$ 3,859,477	\$ 6,387,688
2014	\$ 181,249	\$ 1,296,725	\$ 4,576,216	\$ 6,054,190
2015	\$ (*)	\$ (*)	\$ 5,442,592	\$ 5,442,592
2016	\$ (*)	\$ (*)	\$ 6,472,356	\$ 6,472,356
2017	\$ (*)	\$ (*)	\$ 3,713,930	\$ 3,713,930
2018	\$ (*)	\$ (*)	\$ 3,967,699	\$ 3,967,699
2019	\$ (*)	\$ (*)	\$ 4,212,590	\$ 4,212,590
Total	\$ 2,682,613	\$ 15,752,958	\$ 38,572,570	\$ 57,008,141

(*) No inventory tax credit claims against BFT Liabilities effective with BFT termination on January 1, 2015.

From Tax Year 2009 through Tax Year 2014, roughly 90 taxpayers per year benefited from the State Inventory Tax Credit program. Corporate taxpayers accounted for more than 70 percent of the claims from Tax Year 2009 through Tax year 2014. The total number of inventory tax credit claimants declined by more than 50 percent between 2014 and 2015 largely due to the termination of the Business Franchise Tax on January 1, 2015. Between 2015 and 2018, the number of inventory tax credit claimants declined by a further 20 percent. The decline may be attributable to the use of other tax credits, such as the Manufacturing Investment Tax Credit, changes in federal tax laws, additional investment and related bonus depreciation, and other actions which would tend to reduce the income tax liability of manufacturers.

Figure A
State Manufacturing Inventory Tax Credit Claims by Tax and Business Type



Comparison of Manufacturing Inventory Taxes Paid with State Tax Credit Claims

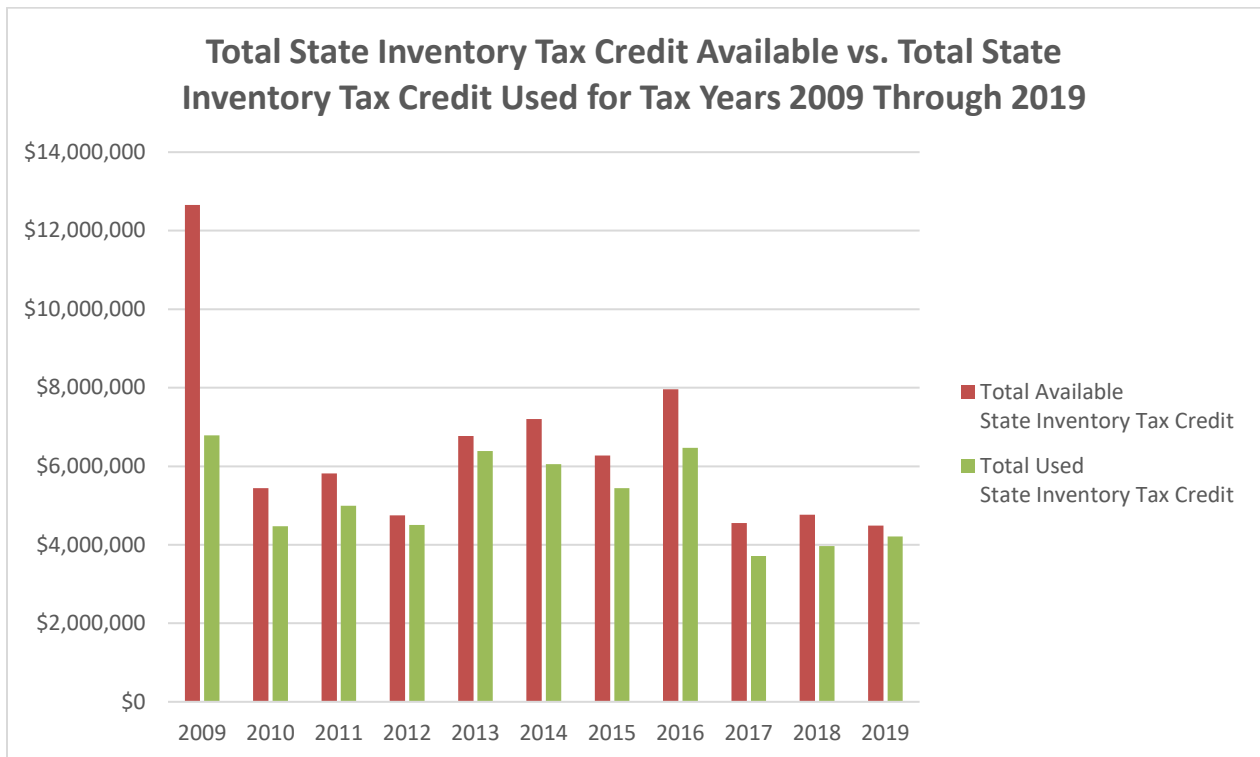
The Inventory Tax Credit allows manufacturers an offset of up to 100 percent of local manufacturing inventory taxes paid against their combined pre-credit tax liability for State Corporation Net Income Tax and Business Franchise Tax. Statistical feedback from property tax assessment data for the ten-year period between Property Tax Year 2009 and Property Tax Year 2018 indicate an average of \$34 million per year in local inventory property taxes assessed to the manufacturing sector. By comparison, State tax credits based on inventory taxes paid, averaged roughly \$5.5 million per year between 2009 and 2014 and slightly more than \$4.7 million per year between 2015 and 2019. The State tax credit effectively offset roughly 16 percent of the total local inventory tax paid in years when the State imposed both a Business Franchise Tax and a Corporation Net Income Tax on manufacturers. Following the elimination of the Business Franchise Tax, the tax credit offset amount declined to 14 percent of the local inventory tax paid by the manufacturing sector.

The lower level of actual tax credit claims is due to the fact that local property taxes imposed on manufacturing inventory tend to be greater in magnitude than State income taxes for many in the manufacturing sector. Based on statistical data published by the Internal Revenue Service’s Statistics of Income Division, more than 40 percent of all U.S. manufacturing firms filing annual income tax returns report no net taxable income on their tax returns in any given year⁴. Federal taxable income is the starting point for the determination of the West Virginia Income Tax. These businesses would pay no West Virginia income taxes and therefore would not be able to claim any inventory tax credits. Businesses with taxable income would be able to claim the inventory

⁴ Internal Revenue Service SOI Tax Stats-Historical Table 14b.

tax credit. However, some of these Taxpayers would pay more in local inventory property taxes than in State income taxes and therefore be limited in the use of the Inventory Tax Credit. West Virginia also offers manufacturing investment tax credits against income tax with the result of less tax liability remaining for offset by the Inventory Tax Credit. The following sections examine statistical use of the Inventory Tax Credit for the subgroup of manufacturers with net taxable income and pre-credit State Corporation Net Income Tax liability.

Based on State Inventory Tax Credit schedules filed for Tax Years 2015 to 2019 for companies with a pre-credit state tax liability, roughly 95 percent of reported available credit funds were claimed by Taxpayers. For comparison, the average ratio of claimed credit to available credit was approximately 84 percent for Tax Years 2009 to 2012. The following graph compares the amount of credit available and amount of credit used by the subset of taxpayers with a pre-credit State tax liability between Tax Years 2009 through 2019. The total reported Inventory Tax Credit available decreased from \$7.2 million in Tax Year 2014 to \$4.5 million in Tax Year 2019. Credit usage rates may appear lower in tax year 2019 because many Corporation Net Income Tax returns have not been fully processed yet.



Manufacturing Inventory Personal Property Tax for Tax Year 2020

The basis for the credit is the West Virginia Property Tax paid by manufacturers on the value of manufacturing inventory. Manufacturing inventory is essentially raw materials, goods in process, and finished goods of a manufacturer. Based upon information from the West Virginia State Tax Department Property Tax Division, the total potential manufacturing inventory Personal Property Tax would range between \$34 million to \$40 million after application of the exemption provided by the Freeport Amendment (see Appendix B for the formal description of the exemption).⁵

Table 2

Manufacturing Inventory Personal Property Tax for Tax Year 2020

Item	Value	Percentage of Appraised Value
Supplemental - Raw Materials	\$ 1,129,671,112	44.1%
Supplemental - Finished Goods	\$ 172,287,480	6.7%
Supplemental - Goods in Process	\$ 469,420,805	18.3%
Supplemental - Machine in Process of Installation	\$ 320,710,476	12.5%
Supplemental - Parts Held for Owner's Use	\$ 139,248,788	5.4%
Supplemental - Supplies Held for Owner's Liability	\$ 135,501,890	5.3%
Inventory	\$ 56,765,576	2.2%
Supplemental - Incomplete Construction	\$ 23,994,250	0.9%
Supplemental - Inventory	\$ 92,538,997	3.6%
Supplies Held for Owner's Use	\$ 3,486,272	0.1%
Supplemental - Tool in Process of Installation	\$ 13,911,455	0.8%
Supplemental - Consigned Goods	\$ 2,730,785	0.1%
Raw Materials	N/A	-
Finished Goods	\$ -	0.0%
Consigned Goods	\$ 24,695	0.0%
Parts Held for Owner's Use	\$ 15,807	0.0%
Goods in Process	N/A	-
Total Appraised Value of Inventory	\$ 2,560,308,388	
Assessed Value of Inventory	\$ 1,536,185,033	
Tax Rate		0.024
Estimated Property Taxes on Manufacturing Inventory	\$ 36,868,441	

⁵ These data are provided for illustration of Tax Year 2020 tax rates related to inventory property taxes in West Virginia. Rates of levy vary from year to year; rates of levy for other taxable periods are available online at <https://www.wvsao.gov/localgovernment/reports>.

Formal definitions of all Property Tax classes are presented in Appendix B. Class III tax rates would apply to manufacturing inventory located outside municipal borders, while Class IV tax rates would apply to manufacturing inventory located inside municipal borders. In Table 2, the estimated property taxes on manufacturing inventory were calculated by taking the weighted average of the Class III and Class IV rates and applying this rate of 2.4% to the assessed value of the manufacturing inventory, as it is often difficult to determine whether certain manufacturing inventory items fall outside or inside municipal boundaries. Manufacturing property tends to be more heavily concentrated in jurisdictions with higher than average property tax rates.

As shown in Table 3, five industries account for 65 percent of the total taxable inventory value. Detail on all manufacturing classifications is presented in Appendix C.

Table 3

Manufacturing Inventory Appraised Value for Tax Year 2019 (Largest Industries)

NAICS	Description	Appraised Value	% of Total
324	Petroleum and Coal Product Manufacturing	\$ 449,392,303	17.6%
325	Chemical Manufacturing	\$ 433,756,771	16.9%
336	Transportation Equipment Manufacturing	\$ 302,458,702	11.8%
327	Nonmetallic Mineral Product Manufacturing	\$ 272,118,694	10.6%
332	Fabricated Metal Product Manufacturing	\$ 208,383,282	8.1%

Since the number of Inventory Tax Credit claimants is small, summaries of the credit by manufacturing classification have been withheld to avoid the possible disclosure of tax information for individual taxpayers. The amount of tax credit is constrained by the Taxpayer's Corporation Net Income Tax liability. For Taxpayers who take advantage of this credit, approximately 82 percent of available credit is used on average. The average amount of credit claimed per year from 2011 to 2014 was roughly \$5.5 million. The elimination of the Business Franchise Tax in January 2015 reduced the average credit claimed between 2015 and 2019 to \$4.7 million per year, as the tax credit currently only offsets the Corporation Net Income Tax. When all returns are finalized for the 2017 to 2019 period, the average annual credit claimed since 2015 is expected to range between \$5.0 million and \$5.6 million per year.

Appendix A
Manufacturing Property Tax Adjustment Credit Claims by Tax and Business Type

Table A-1
Claims from Current Report

	2013	2014	2015	2016	2017	2018	2019	Total
BFT (PTE)	\$ 394,511	\$ 181,249	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	575,760
BFT (C-Corp)	2,133,700	1,296,725	0	0	0	0	0	3,430,425
CNIT	3,859,477	4,576,216	5,442,592	6,472,356	3,713,930	3,967,699	4,212,590	32,244,860
Total	\$ 6,387,688	\$ 6,054,190	\$ 5,442,592	\$ 6,472,356	\$ 3,713,930	\$ 3,967,699	\$ 4,212,590	36,251,045

Table A-2
Claims from July 1, 2020 Report

	2013	2014	2015	2016	2017	2018	2019	Total
BFT (PTE)	\$ 394,511	\$ 181,249	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	575,760
BFT (C-Corp)	2,133,700	1,006,891	0	0	0	0	0	3,140,591
CNIT	3,859,477	4,576,216	5,442,592	3,481,413	2,431,865	286,448	0	20,078,011
Total	\$ 6,387,688	\$ 5,764,356	\$ 5,442,592	\$ 3,481,413	\$ 2,431,865	\$ 286,448	\$ 0	23,794,362

Table A-3
Changes in Claims from July 1, 2020 Report to Current Report

	2013	2014	2015	2016	2017	2018	2019	Total
BFT (PTE)	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	0
BFT (C-Corp)	0	289,834	0	0	0	0	0	289,834
CNIT	0	0	0	2,990,943	1,282,065	3,681,251	4,212,590	12,166,849
Total	\$ 0	\$ 289,834	\$ 0	\$ 2,990,943	\$ 1,282,065	\$ 3,681,251	\$ 4,212,590	12,456,683

Appendix B

Property Tax Classes and the Freeport Amendment

Property Tax Classes:

Class I – All tangible personal property employed exclusively in agriculture, including horticulture and grazing; all products of agriculture, including livestock, while owned by the producer; all notes, bonds, bills and accounts receivable, stocks and any other intangible personal property.⁶

Class II – All property owned, used, and occupied by the owner exclusively for residential purposes; all farms, including land used for horticulture and grazing, occupied, and cultivated by their owners or bonafide tenants.

Class III – All real and personal property situated outside municipalities, exclusive of Classes I and II.

Class IV – All real and personal property situated inside municipalities, exclusive of Classes I and II.

Freeport Amendment:

West Virginia Constitution §10-1c. Exemption from ad valorem taxation of certain personal property of inventory and warehouse goods, with phase into full exemption over five-year period.

Notwithstanding any other provisions of this Constitution, tangible personal property which is moving in interstate commerce through or over the territory of the State of West Virginia, or which was consigned from a point of origin outside the State to a warehouse, public or private, within the State for storage in transit to a final destination outside the State, whether specified when transportation begins or afterward, but in any case specified timely for exempt status determination purposes, shall not be deemed to have acquired a tax situs in West Virginia for purposes of ad valorem taxation and shall be exempt from such taxation, except as otherwise provided in this section. Such property shall not be deprived of such exemption because while in the warehouse the personal property is assembled, bound, joined, processed, disassembled, divided, cut, broken in bulk, relabeled, or repackaged for delivery out of state, unless such activity results in a new or different product, article, substance or commodity, or one of different utility. Personal property of inventories of natural resources shall not be exempt from ad valorem taxation unless required by paramount federal law.

The exemption allowed by the preceding paragraph shall be phased in over a period of five consecutive assessment years, at the rate of one fifth of the assessed value of the property per assessment year, beginning the first day of July, one thousand nine hundred eighty-seven.

⁶ Class I property has been exempt from the Property Tax since Tax Year 2008.

Appendix C

Manufacturing Inventory Property Tax by North American Industry Classification System (NAICS) Codes for Tax Year 2020

NAICS	Description	Appraised Value of Inventory	Assessed Value of Inventory	Estimated Property Taxes On Manufacturing Inventory	Share of Total Appraised Value
324	Petroleum and Coal Product Manufacturing	\$449,392,303	\$269,635,382	\$6,471,249	17.6%
325	Chemical Manufacturing	\$433,756,771	\$260,254,063	\$6,246,098	16.9%
336	Transportation Equipment Manufacturing	\$302,458,702	\$181,475,221	\$4,355,405	11.8%
327	Nonmetallic Mineral Product Manufacturing	\$272,118,694	\$163,271,216	\$3,918,509	10.6%
332	Fabricated Metal Product Manufacturing	\$208,383,282	\$125,029,969	\$3,000,719	8.1%
331	Primary Metal Manufacturing	\$194,718,673	\$116,831,204	\$2,803,949	7.6%
323	Printing and Related Support Activities	\$167,322,615	\$100,393,569	\$2,409,446	6.5%
339	Miscellaneous Manufacturing	\$145,031,434	\$87,018,860	\$2,088,453	5.7%
321	Wood Product Manufacturing	\$95,863,528	\$57,518,117	\$1,380,435	3.7%
333	Machinery Manufacturing	\$64,990,516	\$38,994,310	\$935,863	2.5%
335	Appliance and Component Manufacturing	\$60,890,018	\$36,534,011	\$876,816	2.4%
316	Leather and Allied Product Manufacturing	\$51,196,716	\$30,718,030	\$737,233	2.0%
326	Plastics and Rubber Product Manufacturing	\$47,045,965	\$28,227,579	\$677,462	1.8%
312	Beverage and Tobacco Manufacturing	\$23,379,952	\$14,027,971	\$336,671	0.9%
311	Food Manufacturing	\$18,977,336	\$11,386,402	\$273,274	0.7%
337	Furniture and Related Product Manufacturing	\$9,747,091	\$5,848,255	\$140,358	0.4%
322	Paper Manufacturing	\$7,688,672	\$4,613,203	\$110,717	0.3%
334	Computer and Electronic Product Manufacturing	\$5,499,482	\$3,299,689	\$79,193	0.2%
314	Textile Product Mills	\$1,072,321	\$643,393	\$15,441	0.0%
313	Textile Mills	\$509,334	\$305,600	\$7,334	0.0%
315	Apparel Manufacturing	\$264,983	\$158,990	\$3,816	0.0%
Totals		\$2,560,308,388	\$1,536,185,033	\$36,868,441	100.0%