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OFFICE WEST VIRGINIA
SECRETARY OF STATE

WEST VIRGINIA LEGISLATURE
SEVENTY-NINTH LEGISLATURE
REGULAR SESSION, 2010

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ENROLLED

COMMITTEE SUBSTITUTE

FOR

Senate Bill No. 185

(SENATORS McCABE AND FOSTER, *original sponsors*)

[Passed March 11, 2010; in effect ninety days from passage.]

SB 185

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AN ACT to amend the Code of West Virginia, 1931, as amended, by adding thereto a new article, designated §11-13AA-1, §11-13AA-2, §11-13AA-3, §11-13AA-4, §11-13AA-5, §11-13AA-6, §11-13AA-7, §11-13AA-8, §11-13AA-9, §11-13AA-10, §11-13AA-11, §11-13AA-12 and §11-13AA-13, all relating generally to allowing tax incentives when computing business franchise and West Virginia income tax liabilities, corporate or personal, as the case may be, for profits attributed to the use of patents directly used in a manufacturing process or product developed in this state or for royalties generated from patents directly used in a manufacturing process or product developed in this state; providing short title, legislative findings and purpose; defining certain terms; specifying terms, conditions and rules for taking of tax credits; providing for forfeiture of unused credit after period of years; allowing Tax Commissioner to prescribe rules; requiring periodic reports by Tax Commissioner on cost and effect of tax incentives; providing rule of construction; providing effective date; and specifying termination date.

Be it enacted by the Legislature of West Virginia:

That the Code of West Virginia, 1931, as amended, be amended by adding thereto a new article, designated §11-13AA-1, §11-13AA-2, §11-13AA-3, §11-13AA-4, §11-13AA-5, §11-13AA-6, §11-13AA-7, §11-13AA-8, §11-13AA-9, §11-13AA-10, §11-13AA-11, §11-13AA-12 and §11-13AA-13, all to read as follows:

ARTICLE 13AA. COMMERCIAL PATENT INCENTIVES TAX ACT.

§11-13AA-1. Short title.

1 This article may be cited as the “West Virginia Commer-
2 cial Patent Incentives Tax Act.”

§11-13AA-2. Legislative findings and purpose.

1 The Legislature finds that encouraging the development
2 and use of commercial intellectual properties in this state
3 is in the public interest and promotes the general welfare
4 of the people of this state. In order to encourage greater
5 development and use in this state of commercial intellec-
6 tual properties by West Virginia businesses and thereby
7 increase economic opportunity in this state, there are
8 hereby enacted tax incentives for developing and using
9 patents in this state.

§11-13AA-3. Definitions.

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

7 (b) *Terms defined.* –

8 (1) “Agreement” means any agreement or contractual
9 relationship entered into after the effective date of this

10 section between a person developing patents in this state
11 and either:

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

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

18 (2) “Business activity” means all activities engaged in or
19 caused to be engaged in by a person with the object of gain
20 or economic benefit, direct or indirect.

21 (3) “Commercial use” means selling, licensing, leasing or
22 otherwise making patents available to a third party for a
23 price, fee, royalty, commission or other consideration
24 called by whatever name. “Commercial use” also means,
25 in the case of patents developed by the developer for the
26 developer’s own commercial use, the first use of the
27 patents in a manufacturing or other business activity of
28 the developer.

29 (4) “Commissioner” and “Tax Commissioner” are used
30 interchangeably herein and mean the Tax Commissioner
31 of the State of West Virginia or his or her designee.

32 (5) “Copyright” means a copyright that is registered
33 with the United States Copyright Office or with a similar
34 office of a foreign country when the foreign copyright is
35 recognized under federal law.

36 (6) “Credit year” means the taxable year in which the
37 person realizes the net profit attributable to a patent. In
38 the case of a license or lease to use patents, “credit year”
39 means each taxable year during the term of the license or
40 lease to use patents.

41 (7) “Delegate” in the phrase “or his or her delegate”,
42 when used in reference to the Tax Commissioner, means

43 any officer or employee of the Tax Department of the
44 Department of Revenue duly authorized by the Tax
45 Commissioner directly, or indirectly, by one or more
46 redelegations of authority to perform the functions
47 mentioned or described in this article.

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

53 (9) "Directly used in manufacturing process or product"
54 and "direct use in manufacturing process or product"
55 mean the use of patents directly in those activities or
56 operations which constitute an integral and essential part
57 of the manufacturing processes and products, as con-
58 trasted with and distinguished from those activities or
59 operations which are simply incidental, convenient or
60 remote to the manufacturing activity such as those
61 activities that are incidental. Those activities that are
62 incidental to business activities such as bills, marketing,
63 inventory control, order fulfillment, shipping and tracking
64 are not considered an integral and essential part of the
65 manufacturing process or product.

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

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

73 (A) Having or representing the predetermined, three-
74 dimensional pattern of metallic, insulating or semiconduc-
75 tor material present or removed from the layers of a
76 semiconductor chip product; and

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

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

83 (13) "Partnership" includes a syndicate, group, pool,
84 joint venture or other unincorporated organization
85 through or by means of which any business, financial
86 operation or venture is carried on, which is not a sole
87 proprietorship, trust or estate, and which is treated as a
88 partnership for federal income tax purposes for the
89 taxable year.

90 (14) "Pass-through entity" means a partnership, limited
91 liability company, small business corporation (S corpora-
92 tion) or other entity treated as a partnership for federal
93 income tax purposes for the taxable year.

94 (15) "Patent" means a United States or foreign national
95 patent grant or United States certificate of invention or
96 certificate of protection under the Plant Variety Protection
97 Office of the United States Department of Agriculture and
98 is limited to patents developed in this state for direct use
99 in a manufacturing process or product, or both developed
100 for use and directly used in a manufacturing process or
101 product in this state. For purposes of this article, patents
102 do not include copyrights, trademarks, mask works, trade
103 secrets or any intellectual property that is not a patent.

104 (16) "Person" includes a natural person, corporation,
105 limited liability company or partnership. A single member
106 liability company that is treated as a disregarded entity
107 for federal income tax purposes is be treated as a disre-
108 garded entity for purposes of this article.

109 (17) "Purchase" means a transaction under which title to
110 an item is transferred for consideration, or a license or

111 lease contract for at least three years is executed, regard-
112 less of whether title to the item is transferred at the end of
113 the lease or license period.

114 (18) "Taxpayer" means any person subject to the tax
115 imposed by article twenty-three or twenty-four of this
116 chapter or to both taxes. In the case of a sole proprietor-
117 ship that is not subject to either the tax imposed by article
118 twenty-three or twenty-four of this chapter, the term
119 "taxpayer" means a natural person who owns a disre-
120 garded entity and who is subject to the tax imposed by
121 article twenty-one of this chapter on his or her income
122 from business activity in this state, or any sole proprietor
123 who is subject to the tax imposed by article twenty-one of
124 this chapter.

125 (19) "Trademark" means any trademark, trade name,
126 service mark or other identifying symbol or name that is
127 registered with the United States Patent and Trademark
128 Office or with a similar office of a foreign country when
129 the foreign registration is recognized under federal law.

130 (20) "Trade secret" means information, including a
131 formula, pattern, compilation, program device, method,
132 technique or process, that:

133 (A) Derives independent economic value, actual or
134 potential, from not being generally known to, and not
135 being readily ascertainable by proper means, by other
136 persons who can obtain economic value from its disclosure
137 or use; and

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

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

1 (a) *Allowance of credit.* – A person engaging in this state
2 in developing patents for direct use in a manufacturing
3 process or product and who has an agreement, as defined

4 in section three of this article, with Marshall University or
5 West Virginia University is allowed a credit, when com-
6 puting the person's liability for business franchise tax
7 imposed by article twenty-three of this chapter and
8 corporation net income tax imposed by article twenty-four
9 of this chapter, in the amount allowed under subsection (b)
10 of this section. When the developer is a sole proprietor or
11 a pass-through entity, that amount of the credit remaining
12 after first applying it against the tax liability under article
13 twenty-three of this chapter for the taxable year is
14 allowed when computing the tax imposed by article
15 twenty-one of this chapter on income from the person's
16 business activity.

17 (b) *Amount of credit.* – The amount of credit allowed
18 under this section is equal to twenty percent of the roy-
19 ties, license fees or other consideration received by the
20 developer during the taxable year from the sale, lease or
21 licensing of a patent developed in this state for direct use
22 in a manufacturing process or product by the person in
23 taxable years beginning on or after January 1, 2011:
24 *Provided,* That the amount of credit allowed under this
25 section is thirty percent, rather than twenty percent, when
26 the person reinvests at least eighty percent of the amount
27 of the credit claimed for the taxable year in depreciable
28 property purchased for purposes of developing additional
29 patents in this state in taxable years beginning on or after
30 January 1, 2011, or improving upon a patent developed in
31 this state or contributing to a stipend to retain a graduate
32 or post-doctoral student in this state integral to the
33 development of the patents or related technology in
34 taxable years beginning on or after January 1, 2011,
35 during the next taxable year of the person, and the person
36 has an agreement, as defined in section three of this
37 article, for the development of a patent.

38 (c) *Rules for application of credit.* – The amount of credit
39 computed under this section is allowed in accordance with

40 the following rules and applied as provided in subsection
41 (d) of this section:

42 (1) No credit is allowed under this section for royalties,
43 rents, license fees or other consideration received by the
44 developer of the patent for a patent developed outside this
45 state, except as provided in subdivision (2) of this subsec-
46 tion;

47 (2) When the person developed the patent for direct use
48 in a manufacturing process or product through that
49 person's activity in this state and through that person's
50 activity in one or more other states, the consideration
51 received by the developer during the taxable year from the
52 sale, lease or license of the patent developed through
53 multistate activity of the developer is multiplied by a
54 fraction, the numerator of which is the direct costs of
55 developing the patent in this state and the denominator of
56 which is the total direct costs of developing the patent.
57 The product of this computation establishes the consider-
58 ation to be used in subsection (b) of this section;

59 (3) If a person receives a portion of a royalty that would
60 be eligible for a tax credit under this section because of a
61 business association, licensing agreement or otherwise, the
62 person may receive the tax credit allowable to the portion
63 of royalties that person receives;

64 (4) Unused credit may be carried forward until used for
65 a period of nine consecutive years after the taxable year in
66 which the credit allowed by this section accrues to the
67 person. When the person is an owner of a pass-through
68 entity, credit accrues to the owner when it accrues to the
69 pass-through entity;

70 (5) No credit is allowed under this section for consider-
71 ation received by the developer for patents developed for
72 direct use in a manufacturing process or product before
73 the taxable year beginning January 1, 2011. For purposes

74 of this subdivision, a patent was developed for direct use
75 in a manufacturing process or product before January 1,
76 2011, if before that date it was sold, leased or licensed to
77 a third party prior to January 1, 2011, or before that day
78 it was reduced to practice for purely commercial purposes
79 by the developer or a person related to the developer, as
80 defined in subsection (b), Section 267 of the Internal
81 Revenue Code of 1986, as amended, and as defined in
82 section nine, article twenty-one of this chapter or section
83 three, article twenty-four of this chapter; and

84 (6) No credit is allowed under this section beginning
85 with the eleventh taxable year after the patent was first
86 directly used in a manufacturing process or product.

87 (d) *Application of credit.* – The amount of the credit
88 computed under this section is allowed as a credit against
89 tax as provided in this subsection, but the credit may not
90 reduce the tax below zero.

91 (1) *Business franchise tax.* – The amount of the allowable
92 credit shall first be taken as a credit against the tax
93 liability of the developer for the taxable year under article
94 twenty-three of this chapter.

95 (2) *Corporation net income tax.* – The amount of the
96 allowable credit remaining, if any, after first applying the
97 credit against the tax imposed by article twenty-three of
98 this chapter shall then be taken as a credit when comput-
99 ing the liability of the developer for the taxable year under
100 article twenty-four of this chapter.

101 (3) *Personal income tax on business income.* –

102 (A) When the developer is a sole proprietor, the amount
103 of the allowable credit is taken as a credit when comput-
104 ing the liability of the developer for the taxable year on
105 business income under article twenty-one of this chapter.

106 (B) When the developer is a pass-through entity, the
107 amount of allowable credit remaining, if any, after first
108 applying the credit against the tax imposed by article
109 twenty-three of this chapter for the taxable year is
110 allowed as a credit against the tax imposed for the taxable
111 year on the West Virginia source income of the pass-
112 through entity under article twenty-one of this chapter
113 and the amount of the credit is distributed to the owners
114 of the pass-through entity in the same manner as items of
115 partnership income, gain loss or deduction are distributed
116 or allocated for the taxable year.

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

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

12 (b) *Amount of credit.* – The amount of credit allowed
13 under this section is equal to twenty percent of the net
14 profit attributable to the patent: *Provided*, That the
15 amount of credit allowed under this section is equal to
16 thirty percent of the net profit attributable to the patent
17 when the person claiming the credit reinvests in capital
18 improvements to add product lines to or increase produc-
19 tivity in this state during the next taxable year an amount
20 equal to at least eighty percent of the tax credit amount
21 used for the taxable year.

22 (c) *Rules for application of credit.* – The amount of credit
23 computed under this section is allowed in accordance with
24 the following rules and applied as provided in subsection
25 (d) of this section:

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

31 (2) Unused credit may be carried forward until used for
32 a period of nine consecutive years after the taxable year in
33 which the credit allowed by this section accrues to the
34 person. When the person is an owner of a pass-through
35 entity, credit accrues to the owner when it accrues to the
36 pass-through entity;

37 (3) Any credit not used within the ten-year period
38 described in subdivision (2) of this subsection is forfeited
39 beginning with the eleventh taxable year after the taxable
40 year in which the credit accrued to the person;

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

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

47 (d) *Application of credit.* – The amount of the credit
48 computed under this section is allowed as a credit against
49 tax as provided in this subsection, but the credit may not
50 reduce the tax below zero.

51 (1) *Business franchise tax.* – The amount of the allowable
52 credit shall first be taken as a credit against the tax
53 liability of the person allowed the credit for the taxable
54 year under article twenty-three of this chapter.

55 (2) *Corporation net income tax.* – The amount of the
56 allowable credit remaining, if any, after first applying the
57 credit against the tax imposed by article twenty-three of
58 this chapter shall then be taken as a credit when comput-
59 ing the liability of the corporation for the taxable year
60 under article twenty-four of this chapter.

61 (3) *Personal income tax on business income.* –

62 (A) When the person allowed the credit is a sole propri-
63 etor, the amount of the allowable credit is taken as a credit
64 when computing the liability of the person allowed the
65 credit for the taxable year on business income under
66 article twenty-one of this chapter.

67 (B) When the person allowed the credit is a pass-through
68 entity, the amount of allowable credit remaining, if any,
69 after first applying the credit against the tax imposed by
70 article twenty-three of this chapter for the taxable year is
71 allowed as a credit against the tax imposed for the taxable
72 year on the West Virginia source income of the pass-
73 through entity under article twenty-one of this chapter
74 and the amount of the credit is distributed to the owners
75 of the pass-through entity in the same manner as items of
76 partnership income, gain loss or deduction are distributed
77 or allocated for the taxable year.

§11-13AA-6. Transfer of credit to successors.

1 (a) *Mere change in form of business.* – A patent may not
2 be treated as disposed of by reason of a mere change in the
3 form of conducting the business as long as the patent is
4 retained and directly used in a manufacturing process or
5 product in this state and the person that developed the
6 patent retains a controlling interest in the successor
7 business. In this event, the successor business is allowed
8 to claim the amount of credit still available with respect
9 to the patent transferred to a successor.

10 (b) *Transfer or sale to successor.* – A patent may not be
11 treated as disposed of under this article by reason of any
12 transfer or sale to a successor business which continues to
13 directly use the patent in a manufacturing process or
14 product in this state. Upon transfer or sale, the successor
15 acquires the amount of credit or deduction that remains
16 available under this article for each subsequent taxable
17 year.

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

1 (a) *Required records.* – Every developer of a patent in
2 this state for direct use in a manufacturing process or
3 product and every person who uses a patent directly in a
4 manufacturing process or product in this state who claims
5 a credit under this article shall maintain sufficient records
6 to establish the following facts for each item of a patent
7 for which a credit is allowed under this article:

8 (1) Its identity;

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

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

13 (4) The amount of credit taken; and

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

17 (b) *Enhanced deduction of credit.* – Any person who
18 claims the enhanced credit under section four or five of
19 this article shall maintain sufficient records to clearly
20 establish entitlement to claim the amount of the enhanced
21 credit. At a minimum those records shall identify:

22 (1) Each and every item of depreciable property pur-
23 chased for purposes of claiming the enhanced credit;

24 (2) The date the depreciable property identified in
25 subdivision (1) of this subsection was purchased, its cost
26 and its estimated useful life determined using strait-line
27 method of depreciation;

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

31 (4) The date the depreciable property identified in
32 subdivision (1) of this subsection was taken out of service
33 or use in the person's business activity in this state and the
34 reason why the property was taken out of service or use;
35 and

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

39 (c) *New jobs.* – Every person who claims a credit under
40 this article shall also maintain sufficient records to
41 establish the number and types of new jobs, if any created,
42 the wages and benefits paid to employees filling the new
43 jobs and the duration of each job.

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

**§11-13AA-8. Failure to keep records of a patent for which
credit allowed.**

1 A person who does not keep the records required for
2 identification of a patent for which a credit would be
3 allowable under this article is subject to the following
4 rules:

5 (1) A person is treated as having disposed of, during the
6 taxable year, any patent for which a credit was allowed
7 under this article which the taxpayer cannot establish is

8 still being directly used in the person's manufacturing
9 process or product in this state at the end of that year.

10 (2) If a person cannot establish when a patent was placed
11 in service in direct use in the person's manufacturing
12 process or product in this state, no credit is allowed under
13 this article.

§11-13AA-9. Tax credit review and accountability.

1 (a) Beginning on February 1, 2013, and continuing
2 annually on February 1, the Tax Commissioner shall
3 submit to the Governor, the President of the Senate and
4 the Speaker of the House of Delegates a tax credit review
5 and accountability report evaluating the cost effectiveness
6 of the credits allowed under this article during the most
7 recent year for which information is available. The criteria
8 to be evaluated include, but are not limited to, for each
9 year:

10 (1) The number of taxpayers claiming the credit;

11 (2) The net number, type and duration of new jobs
12 created by all taxpayers claiming the credit and the wages
13 and benefits paid;

14 (3) The cost of the credit;

15 (4) The cost of the credit per new job created; and

16 (5) A comparison of employment trends for the industry
17 and for taxpayers within the industry that claim the credit
18 or deduction; and

19 (b) Taxpayers claiming the credit shall provide informa-
20 tion that the Tax Commissioner requires to prepare the
21 report required by this section. The information is subject
22 to the confidentiality and disclosure provisions of sections
23 five-d and five-s, article ten of this chapter.

§11-13AA-10. Promulgation of rules.

1 The Tax Commissioner shall adopt procedural and
2 interpretive rules or propose legislative rules for legisla-
3 tive approval, as appropriate, in the manner prescribed in
4 article three, chapter twenty-nine-a of this code, that the
5 Tax Commissioner considers necessary to administer this
6 article.

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

1 (a) No inference, implication or presumption of legisla-
2 tive construction or intent may be drawn or made by
3 reason of the location or grouping of any particular
4 section, provision or portion of this article; and no legal
5 effect may be given to any descriptive matter or heading
6 relating to any section, subsection or paragraph of this
7 article.

8 (b) The provisions of this article shall be reasonably
9 construed in order to effectuate the legislative intent
10 recited in section two of this article.

§11-13AA-12. Effective date.

1 The provisions of this article become effective on July 1,
2 2011, and apply only to a patent developed in this state
3 after the taxable years beginning on or after January 1,
4 2011, and to a patent purchased, leased or licensed for use
5 after that date for direct use in the taxpayer's manufactur-
6 ing process or product in this state.

§11-13AA-13. Termination of credit.

1 The Tax Commissioner may not allow any credit for a
2 patent developed or purchased leased or licensed after
3 December 31, 2016, unless this credit is sooner terminated
4 or continued by the Legislature. Termination of the credit
5 allowed by this article, as provided in this section, does
6 not adversely affect the ability of a taxpayer to claim the

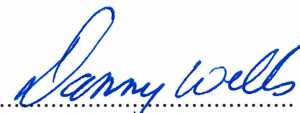
17 [Enr. Com. Sub. for S. B. No. 185

7 benefit of any credit accruing under this article prior to
8 January 1, 2016.

A handwritten signature in black ink, appearing to be "D. J. [unclear]", located at the bottom center of the page.

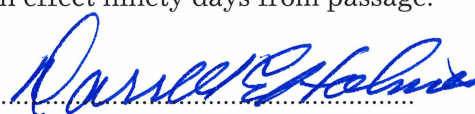
The Joint Committee on Enrolled Bills hereby certifies that the foregoing bill is correctly enrolled.



.....
Chairman Senate Committee


.....
Chairman House Committee

Originated in the Senate.

In effect ninety days from passage.


.....
Clerk of the Senate


.....
Clerk of the House of Delegates


.....
President of the Senate


.....
Speaker House of Delegates

The within *is approved* this the *25th*
Day of *March*, 2010.


.....
Governor

PRESENTED TO THE
GOVERNOR

MAR 19 2010

Time 5:00 pm