

1 **ENROLLED**

2 **H. B. 2993**

3
4 (By Delegates White and T. Campbell)

5 (By Request of the State Tax Division)

6
7 [Passed March 12, 2011; in effect ninety days from passage.]

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9
10 AN ACT 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 modifying the
13 provisions of the West Virginia Commercial Patents Incentives
14 Tax Act generally; defining terms; providing for tax credit
15 carryover and accrual; restricting eligibility for tax credit;
16 providing for disallowance of tax credit; providing for strict
17 construction; and retroactively adjusting the effective date
18 of the provisions of the Act.

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

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

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

24 **§11-13AA-3. Definitions.**

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

7 (b) *Terms defined.* --

8 (1) "Agreement" means any agreement or contractual
9 relationship entered into after the effective date of this section
10 between a person developing patents in this state and either:

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

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

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

23 (3) "Commercial use" means selling, licensing, leasing or
24 otherwise making patents available to a third party for a price,

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

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

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

17 (6) "Delegate" in the phrase "or his or her delegate", when
18 used in reference to the Tax Commissioner, means any officer or
19 employee of the Tax Department of the Department of Revenue duly
20 authorized by the Tax Commissioner directly, or indirectly, by one
21 or more redelegations of authority to perform the functions
22 mentioned or described in this article.

23 (7) "Development of a patent," "developing patents" or
24 "development" means the act of inventing or discovering any new and

1 useful process, machine, article of manufacture, or composition of
2 matter, or any new and useful improvement thereto through
3 significant investment of money, performance of research, or
4 application of design or engineering expertise, which culminates in
5 the issuance of a patent, as defined in this article.

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

10 (9) "Directly used in manufacturing process or product, "and
11 "direct use in manufacturing process or product" with reference to
12 patents means application or incorporation of a patented process,
13 machine, article of manufacture or composition of matter, in
14 manufacturing operations or processes, or in manufactured products,
15 in circumstances where United States or foreign patent laws require
16 that the specific patent for the process, machine, article of
17 manufacture or composition of matter be owned by the manufacturer,
18 or purchased, leased, licensed or authorized by contract to be
19 applied or incorporated in the manufacturing operation, processes
20 or product, and where such lawful ownership, purchase, lease,
21 licensure or contractual authorization is in effect.

22 (10) "Manufacturing" means any business activity classified as
23 having a sector identifier, consisting of the first two digits of

1 the six-digit North American Industry Classification System code
2 number of thirty-one, thirty-two or thirty-three.

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

5 (A) Having or representing the predetermined, three-
6 dimensional pattern of metallic, insulating or semiconductor
7 material present or removed from the layers of a semiconductor chip
8 product; and

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

12 (12) "Net profits" means West Virginia taxable income as
13 determined for purposes of article twenty four of this chapter,
14 before application of this credit and after application of all
15 credits allowable under this chapter except this credit. In the
16 case of taxpayers that are not subject to the tax imposed by
17 article twenty-four, "net profits" means West Virginia taxable
18 income as determined for purposes of article twenty-one of this
19 chapter, before application of this credit and after application of
20 all credits allowable under this chapter except this credit. In
21 circumstances where net profit is not solely attributable to and
22 the exclusive result of the direct use of a patent in a
23 manufacturing process or product in this state, the taxpayer shall
24 determine net profit solely attributable to and the exclusive

1 result of the direct use of a patent in a manufacturing process or
2 product in this state, and net profit for purposes of determining
3 the amount of credit allowable under this article shall be the net
4 profit solely attributable to and the exclusive result of the
5 direct use of a patent in a manufacturing process or product in
6 this state.

7 (13) "Owner", when used in reference to a pass-through entity,
8 means a person who owns an equity interest in the pass-through
9 entity.

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

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

20 (16) "Patent" means a United States patent issued pursuant to
21 35 U.S.C. §101, et seq. or the Patent Cooperation Treaty done at
22 Washington, on June 19, 1970 and is limited to plant patents,
23 design patents and patents developed in this state for direct use
24 in a manufacturing process or product, or both developed for use

1 and directly used in a manufacturing process or product in this
2 state. For purposes of this article, patents do not include
3 copyrights, trademarks, mask works, trade secrets or any
4 intellectual property that is not a patent.

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

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

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

1 (20) "Trademark" means any trademark, trade name, service mark
2 or other identifying symbol or name that is registered with the
3 United States Patent and Trademark Office or with a similar office
4 of a foreign country when the foreign registration is recognized
5 under federal law.

6 (21) "Trade secret" means information, including a formula,
7 pattern, compilation, program device, method, technique or process,
8 that:

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

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

15 **§11-13AA-4. Tax incentive for developing patents in this state.**

16 (a) *Allowance of credit.* -- A person engaging in this state in
17 developing plant patent, design patent or patents for direct use in
18 a manufacturing process or product and who has an agreement, as
19 defined in section three of this article, is allowed a credit, when
20 computing the person's liability for business franchise tax imposed
21 by article twenty-three of this chapter and corporation net income
22 tax imposed by article twenty-four of this chapter, in the amount
23 allowed under subsection (b) of this section. When the developer
24 is a sole proprietor or a pass-through entity, that amount of the

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

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

1 improving upon a patent developed in this state or contributing to
2 a stipend to retain a graduate or post-doctoral student in this
3 state integral to the development of the patents or related
4 technology in taxable years beginning on or after January 1, 2011,
5 during the next taxable year of the person, and the person has an
6 agreement, as defined in section three of this article, for the
7 development of a patent.

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

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

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

1 product of this computation establishes the consideration to be
2 used in subsection (b) of this section;

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

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

18 (5) No credit is allowed under this section for consideration
19 received by the developer for patents developed for direct use in
20 a manufacturing process or product before the taxable year
21 beginning January 1, 2011. For purposes of this subdivision, a
22 patent was developed for direct use in a manufacturing process or
23 product before January 1, 2011, if it was sold, leased or licensed
24 to a third party prior to January 1, 2011, or before that day it

1 was reduced to practice for purely commercial purposes by the
2 developer or a person related to the developer, as defined in
3 subsection (b), Section 267 of the Internal Revenue Code of 1986,
4 as amended;

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

10 (7) No credit is allowed under this section beginning with the
11 eleventh taxable year after the patent was first directly used in
12 a manufacturing process or product.

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

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

21 (2) *Corporation net income tax.* -- The amount of the allowable
22 credit remaining, if any, after first applying the credit against
23 the tax imposed by article twenty-three of this chapter shall then

1 be taken as a credit when computing the liability of the developer
2 for the taxable year under article twenty-four of this chapter.

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

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

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

18 **§11-13AA-5. Tax credit for use of a patent in a manufacturing**
19 **process or product in this state that was developed**
20 **in this state.**

21 (a) *Allowance of credit.* -- A person directly using a plant
22 patent, design patent or patent developed in this state in a
23 manufacturing process or product in this state is allowed a credit
24 against the person's liability for business franchise tax imposed

1 by article twenty-three of this chapter and corporation net income
2 tax imposed by article twenty-four of this chapter, the amount
3 computed under subsection (b) of this section. When the user of a
4 patent is a sole proprietor or a pass-through entity, that amount
5 of credit allowed against income taxes shall be against the tax
6 imposed by article twenty-one of this chapter.

7 (b) *Amount of credit.* -- The amount of credit allowed under
8 this section is equal to twenty percent of the net profit
9 attributable to the patent: *Provided,* That the amount of credit
10 allowed under this section is equal to thirty percent of the net
11 profit attributable to the patent when the person claiming the
12 credit reinvests in capital improvements to add product lines to or
13 increase productivity in this state during the next taxable year an
14 amount equal to at least eighty percent of the tax credit amount
15 used for the taxable year.

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

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

1 (2) Unused credit may be carried forward until the earlier of
2 the tax year when the credit is used up or the ninth consecutive
3 tax year after the first tax year in which the taxpayer is eligible
4 to claim the credit. When the person is an owner of a pass-through
5 entity, credit may be taken by the owner beginning in the tax year
6 when credit may be taken by the pass-through entity or when the
7 pass through entity gains entitlement to the credit;

8 (3) Any credit not used within the ten-year period described
9 in subdivision (2) of this subsection is forfeited beginning with
10 the eleventh taxable year after the first tax year in which the
11 taxpayer 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 credit.* -- Any person who claims the enhanced
5 credit under section four or five of this article shall maintain
6 sufficient records to clearly establish entitlement to claim the
7 amount of the enhanced credit. At a minimum those records shall
8 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 straight-line method of
14 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 strictly construed
17 in order to effectuate the legislative intent recited in section
18 two of this article.

19 **§11-13AA-12. Effective date.**

20 The provisions of this article retroactively become effective
21 on January 1, 2011, and apply only to a patent developed in this
22 state in tax years beginning on or after January 1, 2011, and to a
23 patent purchased, leased or licensed for use on or after that date

1 for direct use in the taxpayer's manufacturing process or product
2 in this state.