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WEST VIRGINIA CHAMBER OF COMMERCE MANUFACTURERS ISSUES FORUM

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UPDATE ON WEST VIRGINIA TAX ISSUES

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Concerns About Stability

The reported news from last week's West Virginia Economic Outlook Conference is not good. Revenue collections are projected to be \$100 million under estimate for the current fiscal year. So where are collections?

Revenue Source	Estimated Collection Collections FY 2010	Estimated Collections through October	Actual Collections through October	To Date % Collected
Personal income tax	\$1,522,000,000	\$491,150,000	\$454,757,000	93%
Consumes sales/use taxes	\$1,144,000,000	\$387,700,000	\$371,582,000	96%
Severance Tax	\$ 288,500,000	\$ 73,400,000	\$ 98,332,000	134%
WVCNIT/BFT	\$ 230,800,000	\$ 64,300,000	\$ 80,631,000	125%
B&O Taxes	\$ 136,500,000	\$ 38,400,000	\$ 37,517,000	98%
Total General Revenue Fund				
Fund	\$3,788,000,000	\$ 1,177,410,000	\$ 1,161,368,000	98%

Source of revenue numbers: West Virginia State Budget Office's website

Observation: Total State revenues collected during the first four months are approximately \$16 million under estimate. The revenue picture will need to get much worse for collections to be \$100 million under estimate.

West Virginia Tax Modernization Project

1. On November 20, 2009, the West Virginia Tax Modernization Project will meet at the Charleston Marriott. Preliminary proposals developed by committees of the Tax Modernization Project will be discussed.

2. The public will have an opportunity to comment on the proposals and to submit their oral or written tax modernization ideas and proposals during the meeting, or by emailing proposals to wvtmp@wv.gov.

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Business Franchise Tax

1. The rate of the business franchise tax, which is imposed on the taxable capital of business entities, is being reduced annually and is scheduled to be zero for tax years beginning after December 31, 2014. While nobody has suggested extending this phase-out period to generate additional revenue, so long as the recession continues in West Virginia this possibility exists.

2. Rate Reduction Schedule:

For taxable years beginning after:	The rate of tax is:
December 31, 2008	0.48%
December 31, 2009	0.41%
December 31, 2010	0.34%
December 31, 2011	0.27%
December 31, 2012	0.21%
December 31, 2013	0.10%
December 31, 2014	0% and no minimum tax

Corporation Net Income Tax

1. The rate of the corporation net income tax is being reduced over a period of years to 6.5%. For 2009, the tax rate is 8.5%. However, future rate reductions are tied to the health of the State's Rainy Day Fund. Consequently, if on any June 30th the balance in the Rainy Day Fund drops below 10% of the general revenue fund budget for the next fiscal year of the State, the rate reduction scheduled for the next first day of January is deferred. The rate reduction schedule is as follows:

For taxable years beginning after:	The rate of tax is:
December 31, 2008	8.5%
December 31, 2011	7.75%
December 31, 2012	7.0%
December 31, 2013	6.5%

While the tax rate is 8.5% for tax years beginning on and after January 1, 2009, the rate reductions scheduled for 2012, 2013 and 2014 may be deferred depending on West Virginia's economy and whether the State needs to dip into the Rainy Day Fund in a meaningful way.

2. Four other changes that took effect for the current tax year are:

- Mandatory combined reporting by commonly owned corporations engaged in unitary business;
- Add-back to federal taxable income of intangible and interest expenses paid to related persons (broadly defined); and
- Change in treatment of partnership distributive share; and
- Captive real estate investment trusts and captive regulated investment companies.

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Consumers Sales and Use Taxes

1. In 2007, the sales tax law was amended so that manufacturers and other businesses that have a West Virginia direct pay permit (because they are exempt under Section 11-15-9(b)(2)) can avoid paying imbedded sales tax on work done by construction contractors. *See* W. Va. Code § 11-15-8d.

2. In 2009, this provision was amended so that it also applies to construction work for high technology businesses and internet advertising businesses. *See* W. Va. Code §§ 11-15-8d and 11-15-9h.

“High-technology business” means and is limited to businesses primarily engaged in the following activities:

- Computer hardware design and development;
- Computer software design, development, customization and upgrade;
- Computer systems design and development;
- Website design and development;
- Network design and development;
- Design and development of new manufactured products which incorporate computer hardware and software;
- Electronic data processing;
- Network management, maintenance, engineering, administration and security services;
- Website management, maintenance, engineering, administration and security services; and
- Computer systems management, maintenance, engineering, administration and security services.

“High-technology business” as so defined is intended to include businesses which engage in the activities enumerated above as their primary business activity, and not as a secondary or incidental activity and not as an activity in support of or incidental to business activity not specifically enumerated above. W. Va. Code § 11-15-9h(b)(2).

No regulations or publications have been issued by the State Tax Department explaining Section 11-15-9h or providing guidance on its application.

Property Taxes

1. Tangible personal property of a high technology business, as defined in the preceding section, is also eligible for special property tax treatment beginning July 1, 2009.

- Servers directly used in a high-technology business or in an internet advertising business, and other tangible personal property directly used in a high-technology business or an internet advertising business are valued at their salvage value.
- Salvage value is 5% of original cost and the assessed value of the property is 60% thereof.

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- The determination of whether tangible personal property is eligible for this treatment is initially made by the county assessor.
- Any time after the property is returned for taxation but prior to January 1st of the tax year, any taxpayer may apply to the county assessor for information on whether any particular item of property qualified for this treatment.
- If the taxpayer and county assessor do not agree, the issue may be submitted to the Tax Commissioner as provided in W. Va. Code § 11-6J-5.

2. *Property Inventory Taxes.* -- For tax years beginning after December 31, 2008, a manufacturer that pays West Virginia property taxes on manufacturing inventory may claim the amount of taxes paid against its business franchise tax liability. Unused credit may then be applied against its corporation net income tax liability. This credit is applied after all other credits are applied. Unused credit is forfeited. *See W. Va. Code § 11-13Y-1 et seq.*

- “Manufacturing business” means one engaged in a business activity classified as having a North American Industry Classification System Code that begins with 31, 32 or 33.
- Manufacturing inventory is limited to raw materials, goods in process and finished goods.

3. *Assessment Appeals Burden of Proof.* -- The Supreme Court of Appeals has clarified that when a taxpayer contests the assessed value of his property, the burden of proof is on the taxpayer to show by clear and convincing evidence that the assessed value is wrong and what the correct value should be. This burden is much higher than the typical burden in civil litigation.

4. *Exoneration Burden of Proof.* -- Clear and convincing evidence is also the burden of proof when taxpayer applies to a county commission for an exoneration of property taxes due to a clerical error or a mistake occasioned by an unintentional or inadvertent act, as distinguished from a mistake growing out of negligence or the exercise of poor judgment.

- The “duty of care” element of negligence found in tort cases is used to distinguish an intentional or inadvertent act from that of a negligent act or the exercise of poor judgment, *e.g.*, what would the reasonable hypothetical person do?
- “Negligent act” and “poor judgment” are interchangeable terms.
- “Unintentional” and “inadvertent” are interchangeable terms.

5. *Appeals Reform.* -- For the last two legislative sessions, the Chamber of Commerce has been working to reform the property tax appeals process to provide greater due process for all taxpayers. The Chamber’s Taxation Committee is working with legislators, county commissioners, county assessors, the State Tax Department and other interested groups to develop an acceptable bill for consideration by the Legislature in January.