CHAPTER 1
CORPORATION NET INCOME TAX[1]

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Table of Contents

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¶ 101 Introduction

Law: W. Va. Code § 11-24-1 *et seq*., *as amended.*

History: The West Virginia Corporation Net Income Tax Act first became effective on July 1, 1967. However, during the first 20 years of the corporation net income tax's existence, the principal business tax in West Virginia was the business and occupation tax, a gross receipts based tax levied on various categories of gross receipts at different rates for each category. As the corporation net income tax rates were relatively low (6% until 1983, and 6% and 7% until July 1, 1987), and a credit was allowed against the corporation net income tax for business and occupation and carrier income taxes, the corporation net income tax was not a primary business tax in the State. Effective July 1, 1987, the carrier income tax was repealed, the business and occupation tax on most businesses was repealed, and the corporation net income tax rate was increased to 9.75%. Consequently, the corporation net income tax and, to a lesser extent, the business franchise tax discussed in chapter 2 of this Guidebook became the principal business taxes on corporations doing business in West Virginia.

The tax rate in effect on July 1, 1987 was reduced 0.15% each July 1 for the next five years as follows: 9.60% for 1988, 9.45% for 1989, 9.30% for 1990, and 9.15% for 1991 until July 1, 1992 when the rate became 9%. This statutory rate remained in place until January 1, 2007, when the rate was reduced to 8.75% for taxable periods beginning after December 31, 2006. The rate was then reduced to 8.5% for taxable periods beginning after December 31, 2008 through 2011 and the rates phased down to 7.75% in 2012, 7.0% in 2013 and 6.5% in taxable periods 2014 and thereafter. A table presenting the corporation net income tax rate history is presented at ¶ 111 below.

Conformity with federal statute: For simplicity and to aid in interpretation and enforcement, the West Virginia statute adopts federal definitions wherever possible. Since the corporation net income tax is a conformity statute, the meaning of "federal taxable income" has generally been amended annually in order to incorporate applicable federal changes through December 31st of the calendar year preceding the due date of the annual return. (*See* ¶ 104 below.)

Many provisions are in common with the business franchise tax: (*Senate Bill 680, enacted by the West Virginia Legislature during its 2008 Regular Session, provided for a scale-back of the rate of business franchise tax imposed under Chapter 11, Article 23 of the West Virginia Code. Effective for taxable years beginning on or after January 1, 2015, there is no tax due under this article. However, the conformity of concepts and provisions between the corporation net income tax and the business franchise tax retain historic relevance.)* The corporation net income tax statute has many provisions essentially the same as those included in the business franchise tax statute (*see* chapter 2 of this Guidebook). Specifically, the three-factor formula used by most corporations to apportion income within and without this State is the same three-factor formula used to apportion capital within and without this State for purposes of the business franchise tax. Banks and other financial organizations used a special gross receipts factor to apportion their business income for income tax purposes as well as for purposes of the business franchise tax. Therefore, a corporation doing business in

West Virginia would usually apportion its income and capital to determine that which is taxable by West Virginia in the same manner. The exception is interstate motor carriers. They may apportion their trucking company income using a mileage factor but they apportioned their capital for purposes of the business franchise tax using the three-factor formula. Additionally, a corporation reduces its federal taxable income and its capital for certain state and local obligations and obligations secured by residential real estate in the same manner to determine capital subject to the business franchise tax and income subject to the corporation net income tax.

Combined reporting: The West Virginia Corporation Net Income Tax statute was amended on March 20, 2007 (SB 749) and March 8, 2008 (SB 680) to repeal consolidated filings and require two or more corporations (including owned partnerships and limited liability companies) engaging in a unitary business to file a combined report for taxable years beginning on or after January 1, 2009. Additionally, taxable members of a unitary business may elect to file a combined return rather than separate returns. (*See* ¶ 117 below.)

¶ 102 Taxable Corporations

Law: W. Va. Code § 11-24-3a, *as amended.*

Definition of corporation: "Corporation" means "any corporation" as defined by the laws of this State or organization of any kind treated as a corporation for tax purposes under the laws of this State, wherever located, which if it were doing business in this State would be a "taxpayer." The business conducted by a partnership which is directly or indirectly held by a corporation shall be considered the business of the corporation to the extent of the corporation's distributive share of the partnership income, inclusive of guaranteed payments to the extent prescribed by regulation. The term "corporation" includes a joint-stock company and any association or other organization which is taxable as a corporation under the federal income tax law. Banks, banking associations, trust companies, building and loan associations, savings and loan associations and other financial organization are also subject to the corporation net income tax (*see* ¶ 110 below).

Definition of engaging in business: For purposes of the corporation net income tax, "doing business" or "engaging in business" is generally defined to mean any corporation which enjoys the benefits and protection of government and laws in the State. (W. Va. Code § 11-24-3a(11).) However, West Virginia's jurisdiction to impose the corporation net income tax is limited by federal law (15 USC § 381(a)(1)). The federal statute provides that when a foreign corporation's in-state activities do not exceed the following activities in a state, that state may not impose a net income tax on the corporation:

(1) Activity in the state by employees soliciting orders for the sale of tangible personal property where the employees soliciting orders have no authority to accept the orders;

(2) Activities by employees displaying or promoting goods in the state without soliciting or taking orders for the sale of tangible personal property;

(3) Solicitation activities by nonemployee representatives conducted through an office or other business location in the state not owned, leased or operated

by the foreign corporation; and

(4) Mere delivery of goods in the state by company-operated vehicles.

These activities are protected regardless of how frequently they occur.

Although not set forth in the regulations, the following activities within this State will be looked at to determine whether a corporation is doing business in this State:

(1) The maintenance of an office;

(2) The maintenance of merchandise for sale;

(3) The sale or distribution of merchandise from a vehicle to purchasers within this State;

(4) The regular performance of a service for a resident of this State; or

(5) The operation of income-producing property or other business property (whether real or personal) located in this State.

West Virginia, like many states, has been much more aggressive in recent years in attempting to assert nexus over foreign corporations considering even minimal connections to the State (that is not excluded by 15 USC § 381(a)(1) discussed above) as a basis for asserting jurisdiction to tax the foreign corporation's net income. This effort includes contacting taxpayers who simply have registered to do business in the State through the West Virginia Secretary of State's office. The State's nexus questionnaire (Form WV/Nexus) calls for a significant amount of information regarding a corporation's activities in the State in an attempt to establish some causal link to assert nexus.

West Virginia has adopted a rebuttable economic nexus threshold for out-of-state financial organizations doing business in West Virginia. In general, there is a presumption of nexus when the bank or other financial organization during any year solicits business from 20 or more persons in this State and its gross receipts attributable to sources in this State equals or exceeds $100,000 subject to certain exceptions. (W. Va. Code § 11-24-7b(d).) This threshold was discussed and approved in the MBNA case discussed at ¶ 110 below.

Further evidence of the State's aggressive position on nexus for out-of-state corporations is the 2012 West Virginia Supreme Court decision in *Craig A. Griffith, West Virginia State Tax Commissioner v. ConAgra Brands, Inc.*, 229 W. Va. 190, 728 S.E.2d 74 (2012).

The ConAgra decision involved the receipt of royalties from the licensing of intangible trademarks and trade names. Through the execution of licensing agreements, ConAgra Brands had been collecting royalty payments for the use of its trademarks and trade names by various unrelated, third party licensees and ConAgra Foods affiliated licensees. The royalties were collected by ConAgra Brands from the sale by the licensees of food products bearing the trademarks and trade names to clients and customers throughout the United States, including West Virginia.

ConAgra Brands did not own or rent any offices, warehouses or other facilities in West Virginia and did not maintain any inventory or sell or distribute merchandise in this State. ConAgra Brands had no employees or agents in West Virginia. Various licensees sold or distributed products bearing the trademarks and trade names to wholesalers and retailers located in West Virginia, and the licensees provided services in West Virginia to those clients and customers. ConAgra Brands provided no services in that regard and, *as stipulated,* did not direct or dictate how the licensees distributed the products bearing the trademarks and trade names. Nevertheless, ConAgra Brands paid all expenses in defending its trademarks and trade names against infringement and in overseeing national marketing by developing marketing strategies and purchasing advertisements with national media outlets.

The State's assessment of Con Agra (which was actually a Multistate Tax Commission Audit) stated that ConAgra Brands failed to pay corporation net income tax on income from royalties from the licensing of trademarks and trade names.

The WV Supreme Court of Appeals in ruling in favor of the taxpayer stated that:

- (Syllabus point 2). "A state tax on interstate commerce will not be sustained unless it: '(1) has a substantial nexus with the State; (2) is fairly apportioned; (3) does not discriminate; and (4) is fairly related to the services provided by the State.' *Maryland v. Louisiana*, 451 U.S. 725, 754, 101 S.Ct. 2114, 2133, 68 L.Ed.2d 576, 600 (1981)." Syl. pt. 1, *Western Maryland Railway Co. v. Goodwin, Comm'r*, 167 W. Va. 804, 282 S.E.2d 240 (1981).
- (Syllabus point 3). "Assessments against a foreign licensor for West Virginia corporation net income and business franchise tax, on royalties earned from the nation-wide licensing of food industry trademarks and trade names, satisfied neither "purposeful direction" under the Due Process Clause nor "significant economic presence" under the Commerce Clause, where the foreign licensor, with no physical presence in this State, did not sell or distribute food-related products or provide services in West Virginia and where: (1) all products bearing the trademarks and trade names were manufactured solely by unrelated or affiliated licensees of the foreign licensor outside of West Virginia, (2) the foreign licensor did not direct or dictate how its licensees distributed the products and (3) the licensees, operating no retail stores in West Virginia, sold the products only to wholesalers and retailers in this State."

Multi-state nexus issues

Many states are moving away from a physical presence nexus standard for corporate income tax purposes and instead adopting an economic nexus standard, which includes nexus created by in-state use of intangibles, as well as a factor presence, or a bright-line standard under which a taxpayer will have nexus if the amount of its property, payroll or sales in a state meets a predetermined threshold The following states have been identified as formally adopting (via statute, regulation or court determination) an economic nexus standard: Alabama, Arizona, Arkansas, California, Connecticut, Colorado, Florida, Idaho, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, New Hampshire, New Jersey, New Mexico, New York State, New York City (limited to certain credit card transactions), North Carolina, Ohio, Oklahoma, Oregon, South Carolina, Tennessee, Utah, Washington (for certain B&O taxpayers), West Virginia (financial institutions) and Wisconsin.

States adopting a factor presence nexus standard similarly reflect the application of an economic nexus standard. Under the Multi–State Tax Commission's "Factor Presence Nexus Standard," an out-of-state taxpayer doing business in a state will have substantial nexus with the state and be subject to the state's franchise and income tax if any of the following thresholds are exceeded in the state during the tax period:

(1) $50,000 or 25% of the total property;
(2) $50,000 or 25% of the total payroll; or
(3) $500,000 or 25% of the total sales.

On June 21, 2018 the US Supreme Court ruled in Wayfair v. South Dakota, overturning both *Quill* and *National Bellas Hess*, finding that the physical presence nexus standard articulated in the two earlier opinions "is unsound and incorrect". Although Wayfair is a sales tax case, those states that retained a physical presence standard for income taxes may, in light of the *Wayfair* decision, expand their income tax nexus provisions to include bright line/factor presence nexus standards.

¶ 103 Exempt Corporations

Law: W. Va. Code §§ 11-24-1 *et seq*. and 11-24-5
Comparable Federal: IRC §§ 501, 1362.

The following corporations are exempt from the West Virginia corporation net income tax (WVCSR § 110-24-5):

Corporations: Corporations that are exempt from federal income tax are exempt from the corporation net income tax. However, certain regulated investment companies and real estate investment trusts are subject to the tax as specified in W. Va. Code § 11-24-4b.

Exempt organizations: A limited exemption is provided to entities that are exempt from federal income tax under the provisions of IRC § 501. If a tax-exempt entity is engaged in activities generating unrelated business income, the entity is subject to tax on this income. Thus, the filing of a Federal Form 990-T to report unrelated business income makes the entity subject to filing a West Virginia corporation income tax return. (WVCSR § 110-24-5.1.a.1.)

Insurance companies: Insurance companies that pay the West Virginia tax on premium income and insurance companies that pay the surcharge imposed by W. Va. Code § 23-2C-3(f)((1) or (3) or that would be subject to those taxes if their business were transacted in this state are exempt. *See* W. Va. Code § 11-24-3a (17) and §11-24-5(b). In addition, "farmers mutual fire insurance companies" are exempt, as provided in W. Va. Code § 33-22-16, and "fraternal benefit societies" are exempt, as provided in W. Va. Code § 33-23-29. (WVCSR § 110-24-5.1.a.2 and 3.)

Farm credit associations: Production credit associations organized under the provisions of the federal "Farm Credit Act of 1933" are exempt. It should be noted, however, that this exemption is not applicable if the production credit association or credit union is a cooperative association organized under the provisions of W. Va. Code § 19-4-2 *et seq*.

Certain trusts for employees: Certain trusts established under § 186 of the Labor Relations Act of 1947 for employees are exempt.

S corporations: Corporations which elect under IRC § 1362 to be taxed as pass-through entities (called "S corporations") are exempt from the West Virginia corporation net income tax and, unlike the federal income tax, there is no capital gain or built-in gains tax. However, S corporations are required to file an information return on Form WV/SPF-100. Nevertheless, just like a federal S corporation, the income, loss, and specially allocated items are passed through to the S corporation shareholders for reporting on their respective income tax returns. (W. Va. Code § 11-24-5(d).) *See* ¶ 119 below regarding nonresident withholding requirements.

Other exempt corporations: Racing associations (W. Va. Code § 19-23-12), credit unions (W. Va. Code § 31C-2-8), and hospital service corporations (W. Va. Code § 33-24-4), including Blue Cross/Blue Shield type corporations (W. Va. Code § 33-24-1) are also exempt.

¶ 104 Definition of "Taxable Income"

Law: W. Va. Code § 11-24-3a(44).

"West Virginia taxable income" means the taxable income of a corporation as defined by the laws of the United States for federal income tax purposes, adjusted, as provided in the corporation net income tax law, except that in the case of a corporation having income from business activity which is taxable without this State, its "West Virginia taxable income" is the portion of its taxable income as so defined and adjusted as is allocated or apportioned to this State under the provisions of the corporation net income tax law. (W. Va. Code § 11-24-3a.)

Annually, the West Virginia Legislature amends and reenacts WV Code § 11-24-3 (definitions) by updating the meaning of "federal taxable income" and certain other terms used in the West Virginia Corporation Net Income Tax Act to conform with their definitions for federal income tax purposes. The most recent update bill passed the Legislature February 9, 2018 and took effect upon its passage. The bill was retroactive to the extent that it incorporated changes in federal law made after December 31, 2016 but before January 1, 2018, and made those changes effective for tax years beginning on or after January 1, 2017, to the extent those changes were effective for federal income tax purposes.

Federal tax reform: On December 22, 2017 President Trump signed the Tax Cuts and Jobs Act which made the most significant changes to the federal tax code since 1986. The Act lowered corporate tax rates, expanded the tax base and provided for a revised system of taxation on multinational corporations. Some of the key provisions of the Act include:

- Permanently reducing the corporate tax rate from 35% to 21%; repealing the corporate alternative minimum tax (AMT)
- Limiting deductions for net interest expense to 30% of EBITDA through 2021
- Allowing businesses to expense 100% of the cost of certain qualified property placed in service after 9/17/2017 and before 2023
- Imposing a one-time transition tax on post-1986 tax-deferred foreign earnings of 15.5% for liquid assets and 8% for illiquid assets
- Providing for a 20% deduction from federal taxable income for qualified business income of pass-through entities (PTE)
- 100% bonus depreciation on "qualified property"
- 80% limitation on net operating losses (NOLs) with no carryback

*New international system provisions***:**

- Moving from a worldwide taxation system to a territorial system that provides a deduction for repatriated foreign earnings
- Creating a new category of foreign income – Global Intangible Low-Taxed Income (GILTI) – with an effective rate of 10.5%
- New effective lower rate, 13.125%, on certain directly earned foreign income – Foreign Derived Intangible Income (FDII)
- New minimum tax – Base Erosion Anti-Abuse Tax (BEAT) – meant to prevent certain deductions of specified payments to a foreign related person

West Virginia, along with most other States, will be affected by these changes. Most state income tax systems use federal taxable income or adjusted gross income as a starting point for state income tax computations, but they do not automatically conform to federal tax rate changes. Thus, state income taxes would generally be expected to rise (immediately or in the near term) as the federal tax base expands, unless states align their tax rates with federal tax rate reductions. States that do not adjust their rates could significantly increase their tax revenues (and taxpayers would pay more in state taxes) without the states taking any action at all.

States generally conform to the Internal Revenue Code in one of several ways: (1) they automatically tie to the federal tax law as it changes (known as "rolling" conformity states); (2) they tie to the federal tax law as of a specific date (known as "fixed" conformity states – including West Virginia); or (3) they pick and choose different federal tax law provisions and dates to which they will conform (known as "selective" conformity states).

To date, West Virginia has adopted all of the changes to federal tax law made effective with the Tax Cuts and Jobs Act through the end of 2017. It remains to be seen if the State Legislature will make any changes to de-couple from any of the federal provisions during upcoming legislative sessions.

¶ 105 Increasing Adjustments to Federal Taxable Income

Law: W. Va. Code §§ 11-24-6(b), 11-24-6a.
Comparable Federal: IRC §§ 103, 172, 199, 312.

The following increases are made to federal taxable income to arrive at unapportioned West Virginia taxable income:

Income from state and local obligations: Interest or dividends from any state or local bonds or securities (exempt for federal income tax purposes under IRC § 103) are added to income. This includes income from securities issued by West Virginia and its political subdivisions.

Income from federal securities not exempt from state taxes but exempt from federal taxes: Interest or dividends (less related expenses to the extent not deducted in determining federal taxable income) on obligations or securities of any authority, commission or instrumentality of the United States, which the laws of the United States exempt from federal income tax, but not from state income taxes, are added to income.

Income-type taxes deducted for federal purposes: Income taxes and other taxes, including franchise and excise taxes, which are based on, measured by, or computed with reference to net income and imposed by this State or any other taxing jurisdiction, are added to income to the extent deducted in determining federal taxable income.

Federal depreciation/amortization for West Virginia water/air pollution control facilities previously expensed for West Virginia income tax purposes: Depreciation/amortization of water/air pollution control facilities is not allowed as a deduction, if such costs have previously been fully deducted for West Virginia corporate net income tax purposes, and is added to income.

Unrelated business income of exempt corporations: The amount of unrelated business taxable income, as defined by IRC § 512 of a corporation which by reason of its purposes is exempt from federal income taxes, is added to income.

Net operating losses deducted for federal income tax purposes: The amount of any net operating loss deduction taken for federal income tax purposes under IRC § 172 is added to income.

Federal deduction for charitable contributions to Neighborhood Investment Programs (NIP), if claiming the West Virginia NIP Tax Credit: If the West Virginia NIP credit is claimed for corporate net income tax purposes, the amount of the West Virginia charitable contribution is added to income.

Net operating loss from sources outside the United States: Taxpayers with foreign source income must adjust their federal taxable income by the amount of their taxable income or loss from sources outside the United States.

Foreign taxes deducted for Federal income tax purposes: Foreign taxes are not allowed as a deduction and must be added to income.

Qualified production activity deduction taken under IRC § 199: The qualified production activity deduction is not allowed as a deduction and must be added to income.

Intangible and interest expense for related parties: Taxpayers must add back otherwise deductible intangible and interest expenses paid, accrued or incurred in connection with a related member, unless an exception applies. (W. Va. Code §§ 11-24-4b(c)(1) and 11-24-4b(d)(1).) As used here, "related member" is broadly defined in W. Va. Code § 11-24-3a(32) and includes a "related entity," which is broadly defined in W. Va. Code § 11-24-3a(31). If the related member was subject to tax in West Virginia, another state, or a foreign nation on a tax base that included the intangible or interest expense, then the taxpayer will receive a credit against West Virginia tax. However, if the expense is a unitary business expense of the taxpayer and unitary business income of the related member, the expense and income will wash when unitary business income of the group is determined and add back is not required.

Dividends paid deduction for certain captive real estate investment trusts: A captive real estate investment trust must add back the dividend paid deduction otherwise allowed by federal law. A captive real estate investment trust is defined as shares or beneficial interest which: (1) are not regularly traded on an established securities market and (2) are more than 50 percent of the voting power or value of the beneficial interests or shares which are owned or controlled by a single entity that is (a) treated as an association taxable as a corporation under federal law and (b) not exempt from federal income tax under IRC § 501(a). (W. Va. Code § 11-24-4b(a) and § 11-24-3a(3) (defining "captive real estate investment trust").)

Dividends paid deduction for certain regulated investment companies: Certain regulated investment companies must add back the dividend paid deduction otherwise allowed by federal law unless the company is a qualified regulated investment company. Shares that are held in a segregated asset account of a life insurance corporation are considered a qualified regulated investment company, thus not subject to the add back requirement. (W. Va. Code § 11-24-4b(b) and § 11-24-3a(28)(c) (defining "qualified real estate investment trust").)

¶ 106 Decreasing Adjustments to Federal Taxable Income

Law: W. Va. Code §§ 11-24-6(c), 11-24-6(f).
Comparable Federal: IRC §§ 51, 78, 169(d), 172, 861-863, 951.

Old Law - Adjustment to certain gains: This adjustment has been eliminated for tax years beginning on and after January 1, 2009. (*See* W. Va. Code § 11-24-6(c)(1).) For prior years, any gain from the sale of property which had a higher fair market value on July 1, 1967, than the adjusted basis at said date for federal income tax purposes is recomputed using a stepped-up basis equal to its fair market value at said date for purposes of computing gain taxable by this State. However, gain for State corporation net income tax purposes cannot exceed the sales price so as to create a loss. The purpose of this adjustment is to prevent the taxation of a property's appreciation prior to the implementation of the corporation net income tax. The adjustment for capital gains is made on an asset-by-asset basis. While not formally accepted by the Department, the State has been known to accept a proration of value before and after July 1, 1967, where the fair market value as of July 1, 1967, cannot be determined.

Current law provides for the following decreases to federal taxable income:

Refund or credit for taxes included in federal income: The amount of any refund or credit for overpayment of income and other taxes (including franchise and excise taxes) which are based on, measured by, or computed with reference to net income, imposed by West Virginia or any other taxing jurisdiction, is subtracted from income to the extent properly included in gross income for federal income tax purposes.

Interest to carry state and local obligations disallowed for federal income tax purposes: The full amount of interest expense actually disallowed in determining federal taxable income which was incurred to purchase or carry securities of any state or of any political subdivision thereof is subtracted from income.

Salary expenses disallowed by reason of federal jobs credit: The amount of salary expenses disallowed as a deduction for federal income tax purposes due to claiming the federal jobs credit under IRC § 51 is subtracted from income.

Federal adjustment for certain foreign dividends: The amount required to be added to federal taxable income as a dividend received from a non-United States corporation under IRC § 78 by a corporation electing to take the foreign tax credit for federal income tax purposes is subtracted from income.

Income of controlled foreign corporations: The amount of income of controlled foreign corporations included in federal adjusted gross income of United States corporations by the operation of IRC § 951 (foreign source income) is subtracted from income.

Certain foreign source income: Any amount included in federal adjusted gross income which is foreign source income under IRC §§ 861-863 is subtracted from income.

Disallowed depreciation for federal income tax purposes of pollution facilities: State law allows taxpayers an election to expense the cost of certain air and water pollution control facilities, located in this State, in the year in which the cost of acquisition, construction or development was paid or incurred. If this election is made, the total amount of any federal deduction for depreciation or amortization of such cost is disallowed. The election is made in the return for the year in which the cost was paid or incurred. Once made, the election is irrevocable. Eligible air and water pollution control facilities are those facilities, located in this State, that are “certified pollution control facilities” as defined in IRC § 169(d) for federal income tax purposes.

Employer contributions to medical savings accounts included in federal taxable income less amounts withdrawn for non-medical purposes: The amount included in federal taxable income for employer contributions to a medical savings account under W. Va. Code § 33-16-15, less withdrawals for nonmedical expenses is subtracted from income.

Interest on Resort Area District Bonds: Effective July 12, 2013, any income or interest on Resort Area District bonds are exempt from taxation pursuant to W.Va. Code § 7-25-19(c).

Allowance for certain state and local obligations and obligations secured by residential real estate: Certain income that is exempt from the West Virginia corporation net income tax is not subtracted to arrive at unapportioned taxable income. Instead, the percentage of the total assets which are exempt from West Virginia tax is determined and the result is then multiplied by unapportioned taxable income to give the amount deducted as tax exempt income. Specifically, a corporation is allowed to reduce its unapportioned taxable income by the proportion that the value of its total assets bears to:

(1) obligations and securities of the United States or any agency, authority, commission or instrumentality of the United States;

(2) obligations of the State of West Virginia or any political subdivision of the State;

(3) investments or loans primarily secured by mortgages or deeds of trust or liens or security agreements on residential property (including “mobile homes”) *located in West Virginia* and occupied by non-transients.

The definition of federal obligations qualifying for a reduction to the tax base is rather broad and includes not only direct obligations of the federal government, but also direct obligations and securities of “any other corporation or entity created under the authority of the United States Congress for the purpose of implementing or furthering an objective of national policy.” (W. Va. Code § 11-24-6(f)(1)(a).) However, the Business Franchise Tax Regulations indicated that instruments issued by another taxpayer that have a federal government guarantee, as opposed to a direct obligation, will not qualify for adjustment of the tax base. (WVCSR § 110-23-3.4.6.1.a.2.) For discussion and listing of certain investment vehicles that are either exempt or taxable, *see* TAA 93-002.

In order to determine the proportion of income from these sources to be included in the tax base, it will be necessary for taxpayers to determine the *monthly* averages of the obligations noted above as well as the *monthly* averages of the taxpayer's total assets. Monthly averages are determined by computing an average for each month of the taxable year and dividing the sum of the monthly averages by the number of months in the taxable year. Once monthly averages have been determined, the taxable proportion of income can be computed by the following formula:

$$\text{Unapportioned taxable income} \times \left(1 - \frac{\text{Average monthly balance of excluded obligations}}{\text{Average monthly total assets}}\right) = \text{Taxable income after allowance}$$

For purposes of determining average monthly balances, the Regulations state that the balances should be determined at "cost" in the same manner as the obligations, investments, and loans are reported on Schedule L of the taxpayer's federal income tax return. Presumably, "cost" can be either the book or tax basis of the obligation. According to the Business Franchise Tax Regulations, "when a taxpayer does not maintain records sufficient to clearly establish the monthly beginning and ending account balances, the average of the monthly beginning and ending account balances shall be deemed to be zero unless the taxpayer can otherwise affirmatively establish to the satisfaction of the Tax Commissioner the amount of the average monthly beginning and ending account balances." (WVCSR § 110-23-3.4.6.3.a.) An example of the foregoing computation is as follows:

Assume a corporate taxpayer has unapportioned taxable income of $200,000 for 2017. Assume further that asset balances are as follows:

United States securities owned and total assets as of:

				Monthly Averages	
Date	**U.S. Securities**	**Total Assets**		**U.S. Securities**	**Total Assets**
01/01/17	$ 300,000	$ 2,000,000		$ 312,500	$ 2,100,000
02/01/17	325,000	2,200,000		337,500	2,250,000
03/01/17	350,000	2,300,000		300,000	2,275,000
04/01/17	250,000	2,250,000		175,000	2,275,000
05/01/17	100,000	2,300,000		75,000	2,325,000
06/01/17	50,000	2,350,000		25,000	2,325,000
07/01/17	0	2,300,000		0	2,300,000
08/01/17	0	2,300,000		0	2,350,000
09/01/17	0	2,400,000		0	2,425,000
10/01/17	0	2,450,000		25,000	2,425,000
11/01/17	50,000	2,400,000		55,000	2,425,000
12/01/17	60,000	2,450,000		70,000	2,455,000
12/31/17	80,000	2,460,000			
			TOTAL	**$ 1,375,000**	**$ 27,930,000**

Based upon the above, the corporation's adjusted taxable income is determined to be $190,154 as follows:

$$\$200{,}000 \times \left(1 - \left(\frac{\underline{1{,}375{,}000} \div 12}{(27{,}930{,}000 \div 12)}\right)\right) = \$190{,}154$$

Adjusted federal taxable income: Federal taxable income plus increasing adjustments less decreasing adjustments produces adjusted Federal taxable income, which becomes West Virginia net taxable income for wholly West Virginia corporations, after deducting the West Virginia net operating loss deduction carryforward. West Virginia corporations are those that have their commercial domicile in West Virginia and are not taxable in another state.

Multi-state corporations are required to allocate and apportion their income. Multi-state corporations are corporations that are taxable in this State and in one or more other states. To illustrate these computations, here is the applicable portion of pages 1 and 2 from 2017 Form WV/CNF-120 (the 2018 version of this form was not available at the time of writing):

Line	
5. Total nonbusiness income allocated everywhere – Form WV/CNF-120APT, Sch. A1, Line 8, Column 3	________
6. Total income subject to apportionment – Subtract Line 5 from line 4	________
7. West Virginia apportionment factor – Form WV/CNF-120APT, Sch. B, Part 1, Line 8; Part 2 or Part 3, Col. 3	________
8. West Virginia apportioned income – Line 6 multiplied by Line 7	________
9. Nonbusiness income allocated to West Virginia – Form WV/CNF-120APT, Sch. A2, Line 12	________
10. West Virginia taxable income – Multistate corporations add lines 8 and 9, wholly West Virginia enter line 4	________
11. West Virginia net operating loss carryforward – Schedule NOL, Column 6 total	________
12. Subtotal (line 10 less line 11)	________
13. REIT Inclusion and Other Taxable Income	________
14. WV Net Taxable Income – Add Lines 12 and 13	________

West Virginia net operating loss deduction: West Virginia net operating loss carryover and carrybacks are subtracted from federal taxable income. In other words, the federal net operating loss is an increasing adjustment to federal taxable income; whereas the specifically computed West Virginia net operating loss deduction is allowed as a decreasing adjustment. Furthermore, if a corporation is required to allocate and apportion its income, the net operating loss deduction is taken after such allocation and apportionment. The loss carryback period and the loss carryforward period are just like the federal rules. However, not more than $300,000 of net operating losses from any taxable year may be carried back. In addition, since the West Virginia net operating loss deduction is determined in accordance with IRC § 172, taxpayers now have available an election to not carryback a net operating loss deduction which is not tied to the treatment of their federal net operating loss deduction. (W. Va. Code § 11-24-6(d).)

In the context of group return filers under W. Va. Code § 11-24-13e, as a general rule, NOLs can only be carried forward (or backwards) to be applied against West-Virginia source income of the combined group member to which it is attributable. NOLs <u>cannot</u> be used by other members of the combined group. There is, however, an exception for NOLs earned when the Taxpayer was filing on a consolidated basis for

West Virginia corporation net income tax purposes for a taxable year that began before January 1, 2009. Those NOLs can be carried over and applied against the income of any former member of the consolidated (controlled) group. (W. Va. Code § 11-24-13c(b)(G).)

Schedule NOL is designed to support claiming of a West Virginia net operating loss carryforward deduction by providing information on the year of the loss and how the loss was/is being used.

For federal income tax purposes, IRC § 444 does not permit the carryback of fiscal year net operating losses for fiscal year personal service corporations. However, since IRC § 172 (not § 444) controls for West Virginia corporation net income tax purposes, fiscal year personal service corporations should be permitted net operating loss carrybacks even though this is not allowed for federal income tax purposes.

¶ 107 Direct Allocation of Certain Items of Nonbusiness Income

Law: W. Va. Code §§ 11-24-7(b), 11-24-7(d)
Comparable Federal: IRC § 631.

A corporation having business income which is taxable both in this State *and* in another state must allocate and apportion its adjusted federal taxable income. A corporation is taxable in another state if:

(1) The corporation is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporation stock tax in another state, or

(2) Another state has jurisdiction to subject the corporation to a net income tax, regardless of whether, in fact, that state does or does not subject the taxpayer to such tax. (WVCSR § 110-24-7.)

The definition of "business income" was amended and now means income arising from transactions and activity in the regular course of taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property or the rendering of the services in connection therewith constitute integral parts of the taxpayer's regular trade or business operations and includes all income which is apportionable under the Constitution of the United States. (W. Va. Code § 11-24-3a(2).) Essentially, all income that may be apportioned without violating the U.S. Constitution is now business income. "Nonbusiness income" means all income other than business income.

The matter of whether business income is apportionable to a State or is considered allocable non-business income is an issue that both taxpayers and the states have continually grappled with. Over the past few years many states, including West Virginia, have expanded their definitions of business income to require more income be subject to apportionment. The broad nature of the definition of business income in West Virginia to include "…all income apportionable under the Constitution of the United States" adds more uncertainty to the issue and seems to provide a great deal of latitude to state tax administrators in determining a taxpayer's business income apportionable to the State.

If a taxpayer is taxable in another state, rents and royalties from real or tangible personal property, capital gains, interest, dividends or patent or copyright royalties (to the extent that they constitute nonbusiness income of the taxpayer) are allocated directly as provided below, but only to the extent they constitute nonbusiness income. (W. Va. Code § 11-24-7(d).)

Rents and royalties from real property: If net income or loss from rents and royalties from real estate located in West Virginia is nonbusiness income, it is allocated to this State. Rent from real property constitutes business income, which is subject to apportionment rather than direct allocation, when the rental of the property is the principal business or the income serves an operational rather than an investment function of the corporation.

Rents and royalties from tangible personal property: Net income or loss from rentals and royalties from tangible personal property are allocated to this State to the extent that the property is utilized in this State and the property generates nonbusiness income. The extent of utilization is determined by the number of days the property is physically located within and without this State. If the corporation was not organized or taxable in another state, all the net rentals and royalties from tangible personal property are allocated to this State. The operational versus functional test discussed above also applies here.

Capital gains: If capital gains and losses from sales of *real property* located in this State are nonbusiness income, they are allocable to this State. This is also true of *tangible personal property if* the property had a situs in this State at the time of the sale, *or* the taxpayer's commercial domicile is in this State and the taxpayer is *not* taxable in another state in which the property had situs. In addition, capital gains and losses from sales of *intangible personal property* are allocable to this State if the taxpayer's commercial domicile is in this State and the income is nonbusiness income. Moreover, the statute provides that gains under IRC § 631(a) and (b) from the sale of natural resources severed in the state are allocated to this State if they are *nonbusiness* income. The operational versus functional test discussed above also applies here.

Interest and dividends: Interest and dividend income is allocated to the state if the corporation's commercial domicile is in this State and the income is nonbusiness income. Interest income is business income which is not subject to direct allocation if it arises out of the business activity of the corporation. The operational versus functional test discussed above also applies here.

Patent and copyright royalties: If patent and copyright royalties are nonbusiness income, they are allocated to this State if the patent or copyright is used by the corporation in this State. If the patent or copyright is used by a corporation which has its commercial domicile in this State, and which is not taxable in another state, the royalties are allocated to West Virginia if they are nonbusiness income. The operational versus functional test discussed above also applies here.

Corporate partner's distributive share-history: For taxable years beginning before January 1, 2009, a corporate partner's distributive share of partnership income, gain, loss, deduction or credit is allocated to this State to the extent it is derived from partnership activity in this State, whether such income is business or nonbusiness income *in the hands of the partnership*. The partnership needs to allocate its distributive share that is nonbusiness income. The partnership also needs to apportion its distributive share that is business income using the partnership's apportionment factors. Nonbusiness income distributive share that is allocated to this State is then divided among the partners in the same manner as partnership income is distributed. Business income distributive share apportioned to this State is then divided among the partners in the same manner as partnership income is distributed. Each member of the partnership must report its proportionate share of nonbusiness income allocated to this State plus its proportionate share of business income apportioned to this State as income allocated to this State. (W.Va. Code § 11-24-7(d)(5).) The purpose of this methodology is to avoid having the business income of the partnership being subject to double apportionment, first using the apportionment factors of the partnership and then apportioned using the apportionment factors of the corporation.

Corporate partner's distributive share-current law: For taxable years beginning after December 31, 2008, a corporation's distributive share from a partnership is nonbusiness income only if the corporation's interest in the partnership generates nonbusiness investment income. If the interest generates business income, then the items of distributive share are treated just like other similar items of the corporation when determining its adjusted West Virginia taxable income. Additionally, the corporation's proportionate share of partnership's property, payroll and sales factors are included when computing the corporation's property, payroll and sales factors. If the partnership's business is unitary with one or more members of corporate owner's combined or unitary group, then the corporation's portion of distributive share is included when determining the business income of the combined group and the corporation's proportionate share of the partnership factors are included when apportioning the business income of the combined or unitary group. (W. Va. Code § 11-24-13c(c).)

¶ 108 Apportionment by Three-Factor Formula (With Double-Weighted Sales)

Law: W. Va. Code § 11-24-7.

For taxpayers other than motor carriers and financial organizations, after the direct allocation of certain nonbusiness income, the remaining adjusted federal taxable income is apportioned by multiplying by a fraction, the numerator of which is the sum of the property factor plus the payroll factor plus two times the sales factor, and the denominator of the fraction is four. Where any fraction has a numerator of zero and a denominator of other than zero, the factor is deemed to be zero, *i.e.*, 0/100 = 0. (WVCSR § 110-24-7.3.a.) In cases where a factor has a denominator of zero, the denominator of the apportionment formula fraction is decreased by the number of factors having zero. If the sales factor denominator is zero, then the apportionment fraction denominator is decreased by two. The following formula is applicable:

$$\text{Taxable income subject to apportionment} \times \frac{\text{Property factor + payroll factor + (2 x sales factor)}}{4} = \text{Apportioned taxable income}$$

Property factor: The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used by the taxpayer within West Virginia during the taxable year, and the denominator is the average value of all real and tangible personal property owned or rented and used by the taxpayer during the taxable year. The formula is as follows:

$$\text{Property factor} = \frac{\text{Average value of real and tangible personal property in W.Va.}}{\text{Average value of all real and tangible personal property}}$$

The average value of all real and tangible personal property is taken from the taxpayer's federal income tax return, Schedule L. The average value of property is determined by averaging the values at the beginning and end of the taxable year. However, in cases where there are substantial fluctuations during the year, the Tax Commissioner may require the taxpayer to average monthly values. For purposes of determining the average value of property, original cost is to be used. Property that is not owned, but rented by the taxpayer, is valued at eight times the net annual rental rate. Rent includes all amounts payable under the lease arrangement in situations where a rental agreement obligates the lessee to pay for such items as interest, taxes, insurance, repairs, etc., as is typically found in a triple net lease. Leasehold improvements are considered property for purposes of apportionment, even if the improvements revert to the lessor upon termination of the lease.

For purposes of determining the property factor as it relates to moveable tangible personal property used within and without West Virginia, the value of the moveable property is determined by multiplying the original cost of such property by a fraction, the numerator of which is the number of days the moveable property has a physical presence in West Virginia and the denominator of which is the number of days of physical presence everywhere during the taxable year. Days of physical location can be determined by statistical methods or any other reasonable basis acceptable to the Tax Commissioner. The following formula is appropriate:

$$\text{Value of moveable property} = \text{Cost of moveable property in W.Va. during any part of year} \times \frac{\text{Days within W.Va.}}{\text{Days everywhere}}$$

Payroll factor: The payroll factor is a fraction, the numerator of which is the total compensation paid in West Virginia during the taxable year, and the denominator of which is the total compensation paid by the taxpayer to all employees regardless of domicile as reflected on the taxpayer's federal income tax return. The formula follows:

$$\text{Payroll Factor} = \frac{\text{Payroll in W.Va.}}{\text{Total payroll}}$$

For purposes of the payroll factor, compensation typically means all wages and other forms of remuneration paid to employees for personal services that are reportable on federal Forms W-2. Payments made to independent contractors or to individuals who are not deemed employees for federal income tax purposes are not considered compensation for purposes of the payroll factor.

Compensation is deemed paid in West Virginia and is considered as a part of the numerator in the payroll factor if the employee's services are either:

(1) performed entirely within West Virginia; or

(2) performed both within and without this State, but the services performed without West Virginia are incidental to the employee's services within this State; or

(3) performed both within and without West Virginia and one of the following elements is present:

   (a) the employee's base of operations is located within West Virginia; or

   (b) the employee has no base of operations but the employee is directed or controlled from a location within West Virginia; or

   (c) there is no base of operations in any state in which some of the employee's services are performed and the employee's residence is located within West Virginia.

Sales factor: The sales factor is a fraction, the numerator of which is the gross receipts of the taxpayer derived from normal business transactions and activities within West Virginia, net of any returns and allowances. The denominator of the fraction is the total gross receipts derived by the taxpayer from its normal business activities and reflected as gross income on its federal income tax return. Below is the applicable formula:

$$\text{Sales Factor} = \frac{\text{Gross receipts from activities within W.Va.}}{\text{Total gross receipts}}$$

The West Virginia corporation net income tax includes a throwout rule, with respect to the sales factor. A throwout rule eliminates from the denominator of the sales factor (i) all destination sales to those states in which the taxpayer transacts no business, (ii) sales to those states where no business is subject to a corporation income tax, franchise tax, or corporation stock tax, or (iii) where the destination state lacks jurisdiction to impose a corporation net income tax, irrespective of whether such state imposes such tax. (WVCSR § 110-24-7.7.g.)

Gross receipts typically means gross income and not gross profit or net income, and it includes all interest income, service charges, carrying charges, federal and state excise taxes (including sales taxes) passed on to the buyer. (WVCSR § 110-24-7.7.a.2.A.) Accordingly, no reduction for cost of goods sold or other expenses (except returns and allowances) shall be subtracted in arriving at gross receipts. If business income includes interest from governmental obligations exempt from taxation by West Virginia, such amounts shall be excluded from the numerator and denominator.

If a taxpayer departs from or modifies the basis for excluding or including gross receipts in the sales factor used in returns for prior years, it must disclose such information by attaching a statement to the West Virginia corporation income tax return, setting forth the nature and effect of the change. (WVCSR § 110-24-7.7.b.)

Sale of tangible personal property: Sales of tangible personal property are deemed attributable to West Virginia under either of the following conditions:

(1) The property is delivered or shipped to a purchaser other than the United States government, who is located within the State of West Virginia. The f.o.b. point, or other conditions of sale, are irrelevant for this purpose. West Virginia sales include delivery to a third party located in West Virginia, if the seller is so directed by an out-of-state purchaser.

(2) The tangible property is shipped from a West Virginia location and the purchaser is the United States government.

In situations where a taxpayer sells tangible personal property to a purchaser located within a state in which the taxpayer is not taxed, then such sales shall be excluded from the denominator of the sales factor.

As discussed in ¶ 101 above, for taxable years beginning after December 31, 2008, all members of a unitary group engaging in business activity in West Virginia must be included in a combined report. The business income of the unitary group is then apportioned using the numerator of each group member’s property, payroll and sales factors and the unitary group’s aggregate denominators, when no member is a motor carrier or financial organization subject to a special apportionment rule.

Sales of other than tangible property: In cases where the taxpayer's business activities consist of sales other than sales of tangible personal property, the sales are considered West Virginia transactions if either:

(1) the income-producing activity is performed within West Virginia;

(2) the income-producing activity is performed both within and without West Virginia and a greater proportion of the income-producing activity is performed within West Virginia as compared to any other state based on the cost of the performance of the service or sale (WVCSR § 110-24-7.7.h.1.); or

(3) if the sale constitutes business income to the taxpayer, or the taxpayer is a financial organization subject to special apportionment rules.

Alternative apportionment methods: In situations where either the taxpayer or the Tax Commissioner believes the statutory allocation and apportionment provisions do not fairly represent the extent of a taxpayer's business activities in West Virginia, the taxpayer may petition or the Tax Commissioner may require, with respect to all or part of the taxpayer's business activities: (1) separate accounting; (2) the exclusion of one of the factors; (3) the inclusion of one or more additional factors; or (4) the use of any other method, including a unitary basis in order to equitable allocate or apportion the taxpayer's income. Taxpayers (including public utilities) desiring approval to use an alternative method of allocation must file a petition with the Tax Commissioner no later than the *original* due date (without regard to any extension) of the annual West Virginia corporation income tax return. (W. Va. Code § 11-24-7(h)(1).)

Unitary method: For tax years beginning on or after January 1, 2009, mandatory combined reporting is required of unitary groups of corporations that have one or more members that do business in West Virginia and in one or more other states and/or nations. Thus, for purposes of determining the business income of combined or unitary group, the law disregards the fact that members of such groups are separate legal entities if they, together, engage in unitary business activity. (W. Va. Senate Bill 749, 2007 Regular Session.) Unless the unitary group elects to report on a worldwide combine basis, the combined group will include domestic corporations formed under the various state laws and certain other corporations, as provided in W. Va. Code § 11-24-13f(a).

Essentially, the federal taxable income of all members of the unitary group is adjusted as provided in West Virginia law and business income is apportioned to West Virginia using the West Virginia numerator of each taxable member and the unitary group's denominator for each of the factors.

A corporation may have different streams of income. The streams may include, for example nonbusiness income (*e.g.*, investment income not serving an operational function), business income from one or more different unitary groups and business income from business activity that is not unitary business income. Each stream of income may be subject to a different apportionment rule. The business income of the combined or unitary group includes only that portion of the corporation's adjusted federal taxable income that is attributable to the group's unitary business activity. The corporation will need to keep appropriate records to properly report these different streams of income.

Schedules UB are utilized to enable a unitary business group to determine the amount of its unitary business income that is attributable to West Virginia. Schedule UB-4CR is a Microsoft Excel spreadsheet on which to report the unitary business income of the combined group engaged in unitary business activity. A combined report that includes all members of the combined group engaged in unitary business activity is required by W. Va. Code § 11-24-13a(j). If the taxable members of the combined group file separate returns, a copy of UB-4CR must be filed with each return. If an election is made by the taxable members to file a combined return for the taxable members, the UB-4CR is filed with the combined return. The schedule UB-4CR is located on the Tax Department's website at www.wvtax.gov and is formatted to the Tax Department's specifications in common Microsoft Excel 97-2003 format for consistency.

Once a taxable member's share of the unitary group's West Virginia adjusted federal taxable income is determined, that member's West Virginia taxable income is determined as provided in W. Va. Code § 11-24-13c.

Prior law: For tax years beginning before January 1, 2009, a taxpayer could request to file on a unitary basis (WVCSR § 110-24-7a). An affiliated group of corporations that filed a consolidated federal income tax return could elect to file a consolidated West Virginia return in which the adjusted federal taxable income of the entire federal combined group was apportioned using the group's property, payroll and sales factors.

¶ 109 Special Apportionment for Motor Carriers

Law: W. Va. Code § 11-24-7a *et seq*.

The special rules for apportioning business income of motor carriers replaced the general apportionment formula of the corporation net income tax. A "motor carrier" is any corporation engaging in the transportation of passengers or property for compensation by motor vehicle over roads in this State, whether traveling on a scheduled route or otherwise. This definition encompasses not only trucks but also taxi cabs, and is broader than the definition of motor carrier found in the motor carrier tax.

The special apportionment formula for motor carriers is:

$$\frac{\text{Miles traveled in state}}{\text{Total miles traveled}}$$

If the total mileage of a motor carrier in this State is 5% or less of its total mileage nationwide during a year and if the motor carrier either (i) travels less than 50,000 miles in this State or (ii) makes no more than 12 trips in this State, the apportionment formula of subsection 7a(b) for motor carriers does not apply. Note that miles means gross miles, not revenue miles.

¶ 110 Special Apportionment for Financial Organizations

Law: W. Va. Code § 11-24-7b

History: The Legislature found during the 1991 Regular Session that the general formula set forth in W. Va. Code § 11-24-3 for apportioning the taxable income of corporations taxable in this State as well as in another state is inappropriate for use by "financial organizations" due to the particular characteristics of those organizations and the manner in which their business is conducted. Accordingly, any organization meeting the statutory definition of a financial organization must use a special apportionment formula to determine its taxable income.

Financial Organization Defined: The definition of a "financial organization" includes all bank holding companies, regulated financial corporations, and any other entity (credit unions are exempt) so long as more than half of the entity's gross business income is derived from loans, the extension of credit, leasing and related activities, the operation of a credit card business, estate and trust services, and the acceptance of deposits.

Generally, in accordance with a rebuttable nexus presumption provided in the statute, financial organizations are deemed to have sufficient contact with West Virginia to be subject to the business franchise and corporation net income taxes if, during a tax year, they solicit business with 20 or more persons or entities located within West Virginia or if the out-of-state organization generates gross receipts of $100,000 or more from West Virginia customers. (W. Va. Code § 11-24-7b(d).)

For purposes of determining whether sufficient contact with the state exists to be subject to the corporation net income tax, gross receipts from certain types of secondary market assets are not considered. (Secondary market assets are obligations that were not originally solicited or contracted by the present owner.) Specifically, gross receipts from the following ownership interests (and certain related activities) will not be considered in determining whether a financial organization is subject to taxation:

(1) An interest in a real estate mortgage investment which is a conduit, such as a real estate investment trust or a regulated investment company;

(2) An interest in a security representing ownership or participation in a pool of promissory notes or certificates or interest that provide for payments in relation to payments or reasonable projections of payments on the notes or certificates;

(3) An interest in a loan from which the interest is attributed to a consumer loan, a commercial loan or a secured commercial loan in which the payment obligations were solicited and entered into by a person that was independent and was not acting on behalf of the owner; or an interest in the right to service or collect income from such a loan; or

(4) An amount held in an escrow or trust account with respect to the above interests.

If a financial organization is subject to taxation when gross receipts from the foregoing interests are not considered, such receipts must, however, be included when apportioning its income.

Financial organizations that are taxable in West Virginia and in one or more other states are required to use a special single factor formula to apportion their income to West Virginia for corporation net income tax purposes. This single factor is based upon the ratio of the financial organizations gross receipts derived from West Virginia as compared to total gross receipts everywhere and may be stated as follows:

$$\frac{\text{(Total Gross Receipts from WV)}}{\text{(Total Gross Receipts)}} \quad \times \quad \text{Adjusted Federal Taxable Income}$$

Excluded from both the numerator and the denominator of the gross receipts factor are interest or fees earned on obligations and securities of the United States, West Virginia, or its political subdivisions and certain investments or loans secured by real property or mobile homes located in West Virginia and occupied by non-transients.

The following types of receipts (income, not principal) are to be included in both the numerator and the denominator:

- lease or rental of tangible property;
- loans secured by real or tangible property;
- consumer loans;
- commercial loans and installment obligations;
- syndication and participation loans;
- credit card service charges and fees;
- credit card merchant discount fees;
- performance of specified financial and fiduciary services;
- fees from travelers checks and money orders; and

All other types of receipts not allocable to another state where the financial organization is taxable are attributable to West Virginia or any other state based on the laws of the taxpayer’s domicile.

The validity of the West Virginia statue was upheld in a court challenge. In this case, MBNA (*see* ¶ 102 above) argued that it did not have taxable nexus with West Virginia because it did not have any real or tangible personal property nor any employees located in West Virginia. The State argued that physical presence is not required to show a substantial nexus for purposes of the State's taxation of financial institutions domiciled outside the State. Rather, the State argued, MBNA's significant business in this State was sufficient to meet the substantial nexus standard of the Commerce Clause of the U.S. Constitution. The West Virginia Supreme Court of Appeals agreed with the State and ruled that the imposition of West Virginia's business franchise tax and corporation net income tax on MBNA for the years 1998 and 1999 did not violate the Commerce Clause. The U.S. Supreme Court rejected an appeal of the case.

Method of filing: For taxable years beginning before January 1, 2009, out-of-state financial organizations generally filed on a separate return basis. This is because the elective filing option was to file a West Virginia consolidated return that included all corporations included in the federal consolidated return. For taxable years beginning on or after January 1, 2009, financial organizations that are part of a unitary group doing business in West Virginia must file a combined report of the group's business income. Each member of the group having taxable nexus with West Virginia will then file its separate West Virginia return. (*See* ¶ 101 above.) Only those members of a combined group that use the same apportionment method may be included in a combined report. Therefore, when a combined or unitary group includes both financial institutions and other corporations and both types of corporations have one or more members with taxable nexus, two combined reports will needed to be prepared, one for the financial organizations and one for the other corporations.

Financial Organization Transition Credit: Financial organizations were eligible for a transition tax credit equal to the net increase in Corporation Net Income Tax liability multiplied by 80% in 2009, 60% in 2010, 40% in 2011, 20% in 2012, 10% in 2013, and 0% in 2014 and thereafter. This transition tax credit was not permitted to reduce the annual Corporation Net Income liability below $1 million. (W. Va. Code § 11-24-9b.)

Multistate apportionment issues

Over the last decade states are slowly but steadily (on average one to three states a year) moving away from an equally weighted three factor (property, payroll and sales) apportionment formula and adopting a heavier weighted sales factor formula or a single sales factor formula. These states also tend to trade the cost of performance method of sourcing sales of non-tangible personal property and services for the market-based sourcing approach.

¶ 111 Rate of Tax

Law: W. Va. Code §§ 11-24-4, 11-24-4a.

For taxable years beginning on or after:	**The rate of tax is:**
January 1, 2012	7.75%
January 1, 2013	7.00%
January 1, 2014	6.50%*

* *See* ¶ 101 above.

For the period July 1, 1967 through December 31, 1982, the tax rate was 6% of West Virginia taxable income. A graduated rate structure was added on January 1, 1983, which continued through June 30, 1987. For this period the tax rate was 6% on the first $50,000, with the rate of 7% on the excess above $50,000 of taxable income.

For taxable periods beginning after June 30, 1987 and ending before January 1, 2012, the tax rates were as follows. Each of these rate changes took effect on July 1 the year, except for the rate changes that took effect on or after January 1, 2007:

1987	9.75%	1991	9.15%
1988	9.60%	1992 thru 2006	9.00%
1989	9.45%	2007 thru 2008	8.75%
1990	9.30%	2009 thru 2011	8.50%

¶ 112 Accounting Periods and Methods

Law: W. Va. Code § 11-24-8 *et seq*.
Comparable Federal: IRC § 441 and following.

Accounting period: The accounting period (taxable year) for West Virginia tax purposes is the same as the taxpayer's federal accounting period. If a taxpayer's federal taxable period or year changes, the West Virginia taxable year also changes.

Accounting method: A taxpayer's method of accounting for West Virginia income tax purposes is the same as the taxpayer's method for federal income tax purposes. This rule also applies when the taxpayer changes its method of accounting for federal income tax purposes. In order to prevent amounts from being duplicated or omitted, the regulations simply state that adjustments are to be taken into account. (WVCSR § 110-24-8.4.a.)

Change in accounting method: If a taxpayer's method of accounting is changed, other than from an accrual to an installment method, any additional tax which results from adjustments determined to be necessary solely by reason of the change shall not be greater than if such adjustments were ratably allocated and included for the taxable year of the change and the preceding taxable years, not in excess of two, during which the taxpayer used the method of accounting from which the change is made. There is also a limitation of any additional tax resulting in a change from the accrual to the installment method. The tax forms and instructions have not provided for this tax break.

Although the tax forms and instructions have not provided for this adjustment, WVCSR 110-24-8.5.a.2 contains the following procedure for using this special tax computation:

(1) Compute tax for current year, regular method, including determination of effective tax rate.

(2) Multiply the dollar amount of the income adjustments, included in the West Virginia taxable income, by the current year effective tax rate.

(3) Pro-rate the adjustments over the current year and no more than two preceding years.

(4) Multiply the dollar amount of the adjustments allocated to each of the years, to the extent included in West Virginia taxable income by the effective tax rate applicable to each of the years.

If the total tax on the adjustments for the three year period is less than the tax on the adjustments as determined for the current year, the differences may be used to reduce the current year's tax liability.

Accounting adjustments: Since the starting point for West Virginia taxable income is federal taxable income, any accounting adjustments made for federal income tax purposes are also required.

If no method of accounting has been regularly used by the taxpayer, or if the method used does not clearly reflect income, then the computation of taxable income is made under such a method that, in the opinion of the Tax Commissioner, clearly reflects income.

¶ 113 Credits Against Tax

Law: W. Va. Code §§ 11-24-9, 11-24-9a *et seq*.

The following credits are currently available, subject to appropriate limitations:

(1) Economic Opportunity Tax Credit – Schedule WV/EOTC-1;
(W. Va. Code § 11-13Q-1 *et seq*.);

(2) Manufacturing Investment Tax Credit – Schedule WV/MITC-1;
(W. Va. Code § 11-13S-1 *et seq*.);

(3) Historic Rehabilitated Buildings Investment Credit – Schedule RBIC;
(W. Va. Code § 11-24-23a);

(4) West Virginia Neighborhood Investment Program Credit – Form WV/NIPA-2;
(W. Va. Code § 11-13J–1 *et seq*.);

(5) Environmental Agricultural Equipment Tax Credit – Form WV/AG-1;
(W.Va. Code § 11-13K-1 *et seq*.);

(6) Electric, Natural Gas and Water Utilities Rate Reduction Credit – Schedule L; (W.Va. Code § 11-24-11);

(7) Telephone Utilities Rate Reduction Credit – Schedule K; (W.Va. Code § 11-24-11a);

(8) West Virginia Military Incentives Credit – Schedule J; (W.Va. Code § 11-24-12);

(9) Credit for utility taxpayers with net operating loss carryovers – Schedule WV/UNOLC-1; (W.Va. Code §11-24-11b);

(10) Apprentice Training Tax Credit – Schedule WV/ATTC-1; (W. Va. Code § 11-13W-1 *et seq*.);

(11) Film Industry Investment Tax Credit – Schedule WV/FIIA-TCS; (W. Va. Code § 11-13X-1 *et seq*.);

(12) Manufacturing Property Tax Adjustment Credit – Schedule WV/MPTAC-1; (W. Va. Code § 11-13Y-1 *et seq*.);

(13) Alternative Fuel Tax Credit – scheduled to expire December 31, 2017 - Schedule AFTC-1; (W. Va. Code §11-6D-1 et seq.);

(14) Commercial Patent Incentives Tax Credits – scheduled to expire December 31, 2016 - Schedule CPITC-1; (W. Va. Code §11-13AA-1 *et seq*.);

(15) Innovative Mine Safety Technology Tax Credit – scheduled to expire December 31, 2018 - Schedule IMSTTC-1 (W. Va. Code § 11-13BB-3).

(16) Farm-to-Food Bank Tax Credit – (W. Va. Code § 11-13DD-1 *et seq*.)

The following credits are allowable if accrued prior to the expiration date, subject to appropriate limitations:

(1) Business Investment & Job Expansion Credit - Form WV/BCS-A, and WV/BCS-1 or WV/BCS-Small; [December 31, 2002];

(2) Aerospace Industrial Facility Investment Credit – Form WV/AIF-1; (W. Va. Code § 11-13D-3f) [not allowed for taxable years beginning after December 31, 2002];

(3) Strategic Research and Development Tax Credit – Schedule WV/SRDTC-) 1; (W. Va. Code § 11-13R-1 *et seq*.) [applicable with respect to

expenditures and investments in service from January 1, 2003 through December 31, 2013].

Also see Form WV/CNF-120TC (Summary of Corporation Net Income Tax Credits) and Chapter 3 of the Guidebook for a comprehensive list of available tax credits.

In general, tax credits earned by one member of a combined or unitary group may not be applied against the West Virginia tax liabilities of any other member of that group, even if the taxable members of the group elect to file a single return under W. Va. Code § 11-24-13e. However, a special rule applies to economic development credits that were earned during a tax year for which the taxpayer participated in the filing of a consolidated West Virginia corporation net income tax return.[2] *See* W. Va. Code § 11- 24-13c(b)(2).

¶ 114 Returns and Payment of Tax

Law: W. Va. Code §§ 11-24-13, 11-24-20.

Annual returns: An annual income tax return is required to be filed by any West Virginia corporation, including S corporations. West Virginia Corporation Net Income Tax Return Form WV/CNF-120 is to be used by all corporations, except S corporations, which must use West Virginia Income Tax for S Corporation and Partnership Form WV/SPF-100. (W. Va. Code §§ 11- 24-13, 11-24-13a, and 11-24-13b.)

Attachments and Statements Required: West Virginia requires that certain additional information and statements from the federal income tax return be attached to the West Virginia return when filed. For example, corporate taxpayers should expect to attach a copy of pages 1 through 5 of the signed federal income tax return, and Schedule M-3 if applicable. For taxpayers that attach a proforma federal income tax return, additional federal consolidated return data is also required, if applicable. These attachments should include a copy of pages 1 through 5 of the consolidated federal income tax return, plus federal Form 851 (Affiliation Schedule), along with spreadsheets showing the consolidation of income and expense, and balance sheet entries for every corporation included in the consolidated federal return.

Beginning in 2016, West Virginia requires a checkbox response regarding whether disregarded entities are included within the corporation net income tax return. If there are disregarded entities, a Tax Return Questionnaire must be completed and attached to the filed return.

[2] Consolidated returns may not be filed for a tax year that begins on or after January 1, 2009. W. Va. Code § 11-24-13a(a)(2).

Due dates: The annual return is due on or before the 15th day of the fourth month after the close of the taxable year (April 15 for calendar-year corporations) for taxable corporations.[3] For S Corporations, the annual return is due on or before the 15th day of the third month after the close of the taxable year (March 15). Federal income tax returns are due at the same time. (W. Va. Code § 11-24-13.) Since the federal Form 990-T for unrelated business income of exempt organizations is due within four and one-half months (instead of three and one-half months) after the close of the taxable year, the Tax Department has informally stated that the West Virginia Corporation Net Income Tax Return will be considered due on the same date. In addition, federal extensions for exempt organizations filing Form 990-T will be recognized.

Payment of tax: Any balance of tax as shown on the return is due on the original due date of the return. An extension of time for filing does not extend the time for payment of the tax. In order to avoid interest and late payment penalties, the balance of the tax due must be paid by the original due date of the return. (W. Va. Code § 11- 24-14.) If the tax due is not paid with the original return, the tax due should be paid by filing a tentative return, using Form WV/CNF-120T.

Extension of time to file: The attachment of a copy of the federal Application for Automatic Extension of Time to File Corporation Income Tax Return (Form 7004) to the annual West Virginia return will automatically extend the time for filing the West Virginia return. The Tax Commissioner has authority to grant and has granted extensions for reasonable cause for up to six months beyond the federal limit of six months. (W. Va. Code § 11-24-18.)

Penalty for late filing and failure to include correct information: Additions to tax are imposed for failure to file a return on or before the due date (determined with regard to an extension to file). Additions to tax are also imposed for failure to pay all tax shown to be due on a return on or before the due date (determined without regard to and extension of time to file). Further discussion of additions to tax is provided in chapter 9 of this Guidebook.

Any S corporation or partnership that fails to file and/or include all the correct information on Form WV/SPF100 and Form WV/NRW-2 or Form WV/NRW-4 when applicable, by the required filing date is subject to a penalty of $50.00 for each information return that they failed to file or include correct information on, not to exceed $100,000.

Report of change in federal taxable income: If the amount of a taxpayer's federal taxable income reported on its federal income tax return for any taxable year is changed or corrected by the Internal Revenue Service, the taxpayer must report such change or correction in federal taxable income within 90 days after the final determination[4] of such change. (W. Va. Code § 11-24-20; WVCSR § 110-24-20.)The

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[3] For tax years that began before January 1, 2016, the due date of the annual return was the fifteenth day of the third month following the close of the taxable year.

[4] Neither the statute nor the legislative rule defined the term "final determination" and there is no reported case law on the subject.

regular form marked “Amended” must be used for this purpose. When making such report, the taxpayer must disclose to the Tax Commissioner the full particulars of such federal tax change or correction. Similar rules apply for S corporations.[5]

This rule clearly applies when a taxable member of a combined or unitary group files a separate West Virginia return or elects under W. Va. Code § 11-24-13e to file a combined return with the other taxable members of the group. It is not clear, however, the extent to which this rule applies when there is a change in the federal taxable income of a member of a combined or unitary group and that member is not taxable in West Virginia, but the federal change affects the business income of the combined or unitary group.

Amended returns: If a federal amended return is required, then generally a West Virginia amended return is required unless there is no change in federal taxable income. In other words, a change in federal credits should not require an amended West Virginia return. An amended state return is filed on Form WV/CNF-120 marked “Amended” and is due within 90 days after filing an amended federal return. (W. Va. Code § 11-24-20.) This applies when the taxpayer files its annual return on a separate company basis. However, for a taxable year beginning after December 31, 2008, if the taxpayer is a member of a combined group engaged in unitary business in this state, the taxpayer shall file with the amended return an amended combined report for the combined group.

For any taxable year beginning after December 31, 2008, a taxpayer engaged in unitary business activity in the State that filed an amended federal return, which filed a group return under W. Va. Code § 11-24-13e, may not file a separate amended West Virginia return. The member that filed the group return shall file an amended corporation net income tax return for the group for the tax year. The member shall attach to the amended group return an amended combined report for the combined group engaged in unitary business in the state. (WVCSR § 110-24-20.)

Consistency in Reporting: In completing the West Virginia Corporation Net Income Return, if a taxpayer departs from or modify past procedures for classifying business income and nonbusiness income, for valuing property or including or excluding property in the property factor, for treating compensation paid in the payroll factor, for including or excluding gross receipts in the sales factor, then the taxpayer must disclose by separate attached schedule the nature and extent of the variance or modification. If the corporation makes sales of tangible personal property which are shipped into a state in which the corporation is not taxable, the corporation must identify the state to which the property is shipped and report the total amount of sales assigned to such state. These sales are excluded from both the numerator and denominator of the sales factor. (*See* ¶ 108 above.)

Tentative carrybacks: West Virginia law permits the filing of a tentative loss carryback similar to federal law as the result of a net operating loss and/or capital loss

[5] Failure to advise the Tax Commissioner of the final determination of federal income tax liability, as required by W. Va. Code § 11-24-20, prevents the running of the three-year statute of limitations on issuance of an assessment. (See W. Va. Code § 11-10-15(a) and (c)(2)).

carryback. Form WV/CNF-139 is used for this purpose. Unless there is a federal Form 1139 filed, the carryback will probably be challenged by the Department. (*See* ¶ 106 above.)

¶ 115 Business Activities Report

Law: W. Va. Code § 11-23-28

Introduction: Unless specifically exempted, every corporation or partnership that carries on any business activity or owns or maintains property in West Virginia must file an annual Business Activities Report (Form BAR-0) with the Tax Commissioner. This report must be filed on or before the 15th day of the 4th month after the end of a corporation's or partnership's taxable year. There are no taxes or fees associated with the filing of this report.

While the filing of a Business Activities Report is not to be used in considering whether or not a corporation or partnership is subject to taxation by West Virginia, there are adverse consequences to taxpayers that do not file the report. The statute specifically prohibits, until such a Business Activity Report is filed, any taxpayer from utilizing the West Virginia court system to pursue any claim not related to a tax liability. For example, a taxpayer will be prevented, until such time as current and past due Business Activity Reports have been filed, from pursuing in a West Virginia court a contractual dispute that is governed by West Virginia law.

Exemptions from Filing: A corporation or partnership will be exempt from filing a Business Activities Report if any of the following conditions are satisfied:

(1) During the taxable year for which a report is due, the corporation or partnership is registered to engage in business in West Virginia (*see* ¶ 1001, chapter 10 of this Guidebook).

(2) A tax return was filed for the taxable year in question covering any of the taxes subject to the provisions of the West Virginia Tax Procedures and Administration Act (*see* ¶ 902, Chapter 9 of this Guidebook).

(3) The corporation or partnership is an organization expressly exempted from taxation by West Virginia or Federal statute or regulation; or its activities are similarly exempted.

Business Activity: Unless exempted as noted above, all taxpayers that engage in any business activity or own or maintain property in West Virginia are required to file an annual Business Activities Report. The following activities, unless specifically exempted, will require the filing of a Business Activities Report:

(1) Maintaining an office or other place of business in West Virginia.

(2) The presence of employees, agents, representatives, or independent contractors within this State if they are conducting business on behalf of the corporation or partnership, regardless of whether the individual or person is residing or regularly stationed in West Virginia.

(3) Owning or maintaining any real, tangible or intangible property within West Virginia.

(4) Any activity carried on by a financial organization that would be includible in the numerator of the special apportionment formula to be used by financial organizations (*see* ¶ 206, Chapter 2 of this Guidebook).

¶ 116 Estimated Tax

Law: W. Va. Code §§ 11-10-18a, 11-24-16 *et seq*.

A taxable corporation is required to file a Declaration of Estimated Corporation Net Income Tax (Form WV/CNF-120ES) and make estimated tax payments if its West Virginia taxable income can reasonably be expected to exceed $10,000. Estimated tax is defined as a corporation's expected income tax liability minus its credits. A corporation is generally required to pay in equal installments at least 90% of the tax due for the filing period. Installment payments are usually due in four equal installments. Returns and payments are due on or before the 15th day of the fourth, sixth, ninth, and twelfth months of the corporation's taxable year. These dates match the federal estimated tax payment dates.

Exceptions to the 90% estimated payment rule: There are two exceptions to the 90% general rule:

Exception 1, Prior Year's Tax: This exception applies if the corporation paid an amount equal to or more than the tax shown on its return for the preceding year. A return showing tax liability must have been filed for the preceding year and the preceding year must have been a period of twelve months.

Exception 2, Tax On Annualized Income: An amount equal to 90% of the tax determined by placing on an annual basis the taxable income for: (A) the first three months of the taxable year, in the case of the installment required to be paid in the 4th month, (B) either the first three months or the first five months of the taxable year in the case of the installment required to be paid in the 6th month, (C) either the first six months or the first eight months of the taxable year in the case of the installment required to be paid in the 9th month, and (D) either the first nine months or the first eleven months of the taxable year in the case of the installment required to be paid in the 12th month.

To annualize income, multiply taxable income for the period by 12 and divide the result by the number of months in the period (3, 5, 6, 8, 9, or 11, as the case may be).

Form WV/CNF-120U is used to compute the penalty and/or the exceptions to the penalty. The rate is subject to adjustment twice a year-on April 15 for the succeeding July 1 through December 31, and on October 15 for the succeeding January 1 through June 30. The current penalty rate is 9.5% per annum.

¶ 117 Combined Reporting

Law: W. Va. Code §§ 11-24-13a, 11-24-13c - 11-24-13f.

Combined reporting is a tax reporting method where all of the members of a unitary group are required to determine their net income based on the activities of the unitary group as a whole. Unitary group members that have nexus with West Virginia apportion the total group income to West Virginia through an apportionment formula.

Combined reporting treats each filer as a part of one business – part of the unitary group. If the income reported to West Virginia is the income of all of the unitary businesses apportioned to West Virginia, then the related corporations are afforded less flexibility when considering structuring and reporting transactional activity among affiliates.

More specifically, the regulations provide that the terms “combined group” and “unitary group” are used interchangeably and mean the group of all taxpayers whose income and apportionment factors are required to be taken into account in determining the taxpayer’s share of the net business income or loss apportionable to West Virginia. (WVCSR § 110-24-3.2.1.)

It is important to note that combined reporting in West Virginia refers to a “combined report” of the income and apportionment factors of all members of the unitary group, and does not mean that the group is required to file a combined tax return for West Virginia. The use of a combined report does not disregard the separate identities of the members of the combined group. Each taxpayer member of the combined group is responsible for West Virginia Corporate Income Tax based on its taxable income or loss apportioned or allocated to the state, which includes, in addition to other types of income, the taxpayer member’s apportioned share of business income of the combined group, where business income of the combined group is computed as a summation of the individual net business incomes of all members of the combined group. (W. Va. Code § 11-24-13c). A member’s net business income from the unitary business is determined by removing all but unitary business income, expense and loss from that member’s total federal taxable income.

“Combined Report” refers to a Schedule UB series of forms which are to be attached to a taxpayer’s annual corporation net income tax return and which report the income and apportionment information of all corporations that are members of the taxpayer’s “commonly owned” combined group. (WVCSR § 110-24-3.2.2.) (*See* ¶ 108 below.)

“Commonly Owned” or “Common Ownership” mean, in general, that more than 50% of the voting control of one or more corporations or other entities is directly or indirectly owned by one or more common owners, whether corporate or non-corporate, subject to comprehensive specific rules and examples in the regulations. (WVCSR § 110-24-3.2.3.) (*See* ¶ 108 below.)

"Stapled Entities" is a recent definition in the regulations "where, by reason of their form of ownership, or restrictions on transfer of ownership, or other terms or conditions, whether existing by operation of law, by written contract, or otherwise, in the case of a transfer of one or more ownership interests, require more than 50% of the voting control of each entity to be transferred." Thus, "two or more corporations that are stapled entities are treated as commonly owned or under common ownership, and subject to inclusion in a combined group." (WVCSR § 110-24-3.2.3.c.)

Careful study of the "Commonly Owned" or "Common Ownership" definition is necessary in order to discern its applicability. Specific rules and examples include: direct and indirect voting control, tiered ownership, and related versus unrelated owners. (WVCSR § 110-24-3.2.3.)

"Unitary business" means "a single economic enterprise that is made up either of separate parts of a single business entity or of a commonly controlled group of business entities that are sufficiently interdependent, integrated and interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts. For purposes of the corporation net income and business franchise taxes, any business conducted by a partnership shall be treated as conducted by its partners, whether directly held or indirectly held through a series of partnerships, to the extent of the partner's distributive share of the partnership's income, regardless of the percentage of the partner's ownership interest or the percentage of its distributive or any other share of partnership income. A business conducted directly or indirectly by one corporation through its direct or indirect interest in a partnership is unitary with that portion of a business conducted by one or more other corporations through their direct or indirect interest in a partnership if there is a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts and the corporations are members of the same commonly controlled group." (*See* W. Va. Code § 11-24-3a(43).)

The statute was again amended in 2009 (SB 540). Those changes are retroactive to taxable years beginning after December 31, 2008.

The primary changes for taxable years beginning after December 31, 2008 included:

(1) Distributive share from an interest in a partnership or other entity taxed like a partnership for federal income tax purposes will no longer be treated as allocable business income. Such income will be treated like any other income of the corporation, and the corporation's property, payroll and sales factors will include the corporation's proportionate share of the partnership's factors. A business conducted directly or indirectly by one corporation through its direct or indirect interest in a partnership will be unitary with that portion of a business conducted by one or more other corporations if there is a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts and the corporations are members of the same commonly controlled group. (WVCSR § 110-24-13a.2.a.) A partnership interest that is not part of a

unitary business will be treated as a discrete separate business;

(2) The federal deduction for interest expenses and intangible expenses paid to a related person must be added back to federal taxable income, unless an exception to add-back applies. When the expense is paid to a related person who is a member of a controlled group and the expense is a unitary business expense, both the expense and the income are disregarded when unitary business income is computed and there is no add-back. However, an interest expense or intangible expense may be paid to a related person who is not part of the controlled group engaged in a unitary business. In this situation, add-back is required unless an exception applies. Also, if the expense is not a unitary business expense, add-back is required even though the expense is paid to a member of the combined group, unless an exception applies;

(3) The dividends paid deduction allowed by federal law must be added back to federal taxable income when the dividends are paid by a captive real estate investment trust (REIT) or captive regulated investment company (RIC);

(4) Special rules apply to charitable contributions paid from unitary business income or of unitary business property;

(5) Combined reporting rules also apply to parent subsidiary groups even though no corporation is taxable outside of West Virginia, when the group is engaged in a unitary business; Combined reports must be prepared on a water's-edge basis, unless the combined group elects to prepare the report on a world-wide combination basis, which is irrevocable for 10 tax years; and

6) "Special Apportionment Members" continue to include motor carriers and financial organizations.

Note: SB 386 amended and reenacted W.Va. Code §11-24-13f with respect to water's-edge corporations to exempt from taxation certain income exempt from taxation under certain Federal tax treaties; clarifies the entities that must be included in a water's-edge group combined report; provides the Tax Commissioner with authority to require reports or make adjustments regarding combined reports; and authorizes the Tax Commissioner to promulgate legislative, procedural or emergency rules, as necessary. This bill passed the Legislature March 8, 2012, and took effect June 6, 2012.

Combined report: The members of a combined or unitary group may annually elect to designate one taxpayer member of the group to file a single annual return for the taxable members of the group in lieu of the filing of separate annual returns. An election to file a single annual return is made by an electing key corporation by completing an Election to File Unitary Taxpayers' Group Return, filed in conjunction with its West Virginia Corporation Net Income Tax return, setting forth the information prescribed by the Tax Commissioner. This election is made with an original, timely filed return, determined by including any authorized extensions for filing the return.

Once made, the election to file a group return for all matters for the taxable year of the election will remain in effect until 30 days following the receipt by the Tax Commissioner of a written notice of termination of the election by any of the taxpayer members. The taxpayer member that is terminating the election shall also notify the previously designated key corporation that the election is being terminated. The termination shall only be applied prospectively.

The designation of a key corporation for purposes of filing the single annual return has many other procedural implications that should be considered concurrent with considering the annual election. (W. Va. Code § 11-24-13e.)

Multi-state issues with combined reporting: Currently 28 states and the District of Columbia and New York City require combined reporting by corporations that are members of a unitary group: Alaska, Arizona, California, Colorado, Connecticut (2016), Hawaii, Idaho, Illinois, Kansas, Kentucky (2019), Maine, Massachusetts, Michigan, Minnesota, Montana, Nebraska, New Hampshire, New Jersey (2019), New York State and City, North Dakota, Ohio (for the Commercial Activity Tax and only if consolidated filing is not elected), Oregon, Rhode Island (2015), Texas, Utah, Vermont, West Virginia and Wisconsin. New Mexico also has combined reporting provisions, but it is only mandatory for certain big-box retailers. Further, the Multistate Tax Commission has adopted a model combined reporting statute, which has been used by a handful of jurisdictions, including Connecticut, District of Columbia, and West Virginia.

A growing trend in states recently adopting combined reporting provisions is the inclusion of tax haven laws. Under tax haven laws adopted by certain states, including Alaska, Connecticut, District of Columbia, Kentucky, Montana, Rhode Island and West Virginia, corporate taxpayers generally must include in their water's-edge returns the income and apportionment factors of unitary corporate affiliates formed or engaged in business in "tax havens." The intent of such laws is to prevent multinational corporations from avoiding state income taxation by shifting domestically earned income to tax haven affiliates. There is no single, agreed-upon definition of a tax haven, but a tax haven can be thought of simply as a country with a low or zero tax rate in which a company reports a significant amount of income but has insignificant actual operations.

States generally use one of the following two approaches to tax havens: the "blacklist" approach (e.g., a list of jurisdictions) and the "factor" or "criteria" approach. Under the factor or criteria approach, a "tax haven" is statutorily defined so taxpayers generally must look to specific qualitative criteria to determine if a jurisdiction qualifies as a tax haven. For example, jurisdiction's tax rate is lower than the state's or has created a tax regime favorable for tax avoidance, etc. Of the states that have adopted tax haven provisions, Montana has adopted the blacklist approach, while the remaining states have adopted the factor/criteria approach. It's worth mentioning that in response to international tax law changes contained in the federal Tax Cuts and Jobs Act (P.L. 115-97), Oregon in 2018 retroactively repealed its tax haven laws, effective for tax years beginning on or after January 1, 2017.

Combined reporting provisions generally are unique to each state. This lack of uniformity creates a whole host of issues for taxpayers – from how terms are defined to which entities are included in the combined group, to the treatment of entities located in a "tax haven" jurisdiction. The following is a small sample of some of the issues facing multistate and multination companies subject to states' combined reporting laws.

- What is a unitary business? Does the state adopt the three unities test (i.e., unity of ownership, unity of operation, unity of centralized management) or does it follow the Multistate Tax Commission's model definition[6] or does it adopt its own, unique definition?[7]

- Are pass-through entities included in the combined group? If not automatically included, can they be included at the tax commissioner's discretion?

- Can different lines of business be included in the same combined report (e.g., can general corporation be part of the same combined group with financial organizations or insurance companies)?

- Does the state require the combined group include income from affiliated entities organized in a tax haven jurisdiction? If so, how does the state define tax haven? Does the state adopt a list of jurisdictions it deems to be tax havens or does the state define "tax haven"?[8]

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[6] The Multistate Tax Commission defines unitary business as "a single economic enterprise that is made up of either separate parts of a single business entity or of a commonly controlled group of business entities that are sufficiently interdependent, integrated and interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts."

[7] West Virginia's definition of "unitary business" appears on page 1-4, above.

[8] The term "tax haven" is defined in W. Va. Code § 11-24-3a(a)(38) and means a jurisdiction that, for a particular tax year in question: (A) is identified by the Organization for Economic Cooperation and Development as a tax haven or as having a harmful preferential tax regime; or (B) has no, or nominal, effective tax on the relevant income and: (i) has laws or practices that prevent effective exchange of information for tax purposes with other governments regarding taxpayers subject to, or benefitting from, the tax regime; (ii) lacks transparency. For purposes of this definition, a tax regime lacks transparency if the details of legislative, legal or administrative provisions are not open to public scrutiny and apparent or are not consistently applied among similarly situated taxpayers; (iii) facilitates the establishment of foreign-owned entities without the need for a local substantive presence or prohibits these entities from having any commercial impact on the local economy; (iv) explicitly or implicitly excludes the jurisdiction's resident taxpayers from taking advantage of the tax regime's benefits or prohibits enterprises that benefit from the regime from operating in the jurisdiction's domestic market; or (v) has created a tax regime which is favorable for tax avoidance, based upon an overall assessment of relevant factors, including whether the jurisdiction has a significant untaxed offshore financial or other services sector relative to its overall economy. For purposes of this definition, the phrase "tax regime" means a set or system of rules, laws, regulations or practices by which taxes are imposed on any person, corporation or entity, or on any income, property, incident, indicia or activity pursuant to governmental authority.

- In states that have recently enacted combined reporting, how are net operating losses (NOLs) and tax credits treated pre- and post- combined reporting adoption? Can NOLs and credits generated pre-combination be shared by members of the group? What about entities new to the group? Can an entity share NOLs and credits that were generated before it joined the group?

- For compliance ease are taxpayers over-including entities in the combined group?

- In states that have not adopted mandatory combined reporting provisions, can taxpayers be forced to file on a combined basis to more accurately reflect the business's activities in the state? If so, how is the combined report calculated?

- In states that enact new combined reporting provisions, or amend current combined reporting provisions, how and when will the taxpayer account for these changes for financial reporting purposes?

Another trend is that more states are adopting market based sourcing rules to determine when gross receipts from furnishing services and intangibles should be included in the numerator of a state's sales factor in its apportionment formula.[9] Under market based sourcing rules, sales from services are assigned to a state to the extent the customer of the taxpayer receives the benefit of the service in the taxing state; and sales from intangible property are assigned to the taxing state to the extent the property is used in the taxing state. Under traditional sourcing rules, West Virginia and a number of other states, source sales, other than sales of tangible personal property, to the taxing state if the income-producing activity is performed in the taxing state; or if the income-producing activity is performed both in and outside the taxing state a greater proportion of the income-producing activity is performed in the taxing state than in any other state, based on costs of performance.[10]

The issues identified above offer only a partial list of some of the challenges that state tax administrators and taxpayers face in administering combined reporting for multi-state corporations.

¶ 118 Consolidated Returns

Law: W. Va. Code § 11-24-13a.

Consolidated returns are not allowed for any taxable year beginning after December 31, 2008. For taxable years beginning before January 1, 2009, the following rules applied.

The prior regulations provided that a corporation that elected to file a consolidated federal income tax return as part of an affiliated group of corporations must file a

[9] States that have adopted market based sourcing for services and intangibles include Alabama, Arizona, California, Georgia, Illinois, Iowa, Maryland, Massachusetts, Michigan, Minnesota, Nebraska, New York, Ohio (CAT), Oklahoma, Pennsylvania, Utah and Wisconsin.

[10] See, e.g., W. Va. Code § 11-24-7(e)(12)

separate West Virginia income tax return unless all members of the affiliated group elected to file a consolidated West Virginia income tax return. The filing of a consolidated West Virginia return was considered to be consent by the group. If a consolidated West Virginia return was filed for any taxable year ending after June 30, 1987, the members of the affiliated group must thereafter continue to file a consolidated return unless the Tax Commissioner consented to revocation of the election. (W. Va. Code § 11-24-13a(a) and (b)(1), prior WVCSR § 110-24-43a.) The filing method was also controlling for West Virginia business franchise taxes. However, there was a statutory change for taxable years ending after March 8, 1990, to remove this controlling filing method for severance and telecommunications taxes. (W. Va. Code § 11-24-13a(i).)

Prior regulations were not detailed except for computing taxable income applicable to financial institutions where a taxable year includes a time period prior to July 1, 1987. (W. Va. Code § 11-24-13a(c), prior WVCSR § 110-24-13a.5.) The filing of West Virginia consolidated returns were not permitted unless all members of the consolidated group had their commercial domicile in West Virginia. (WVCSR § 110-24-7.3.a.1.)

For taxable years beginning prior to January 1, 2009, the Tax Commissioner also had authority to require corporations to file consolidated returns to clearly reflect taxable income, if the Tax Commissioner determined that intercompany pricing or transactions have artificially shifted taxable income to, between, or among affiliated groups. However, under S. B. 749, a consolidated return may not be filed, or required by the Tax Commissioner, for taxable years beginning after December 31, 2008. (*See* ¶ 101 above.)

¶ 119 Nonresident Shareholder Withholding

Law: W. Va. Code § 11-21-71a

S corporations are required to withhold West Virginia income tax from each nonresident shareholder that has not given to the S corporation a West Virginia Nonresident Income Tax Agreement, Form WV/NRW-4. The amount to be withheld for years beginning after December 31, 2007 is 6.5% of the nonresident shareholder's share of the S corporation's Federal Taxable Income or portion thereof that is derived from or attributable to West Virginia sources, whether such amount is actually distributed or is deemed to have been distributed for Federal Income Tax purposes.

TAA 92-005 provides the following guidance regarding nonresident shareholders:

> Income from intangible personal property, including annuities, dividends, interest, and gains from the disposition of intangible personal property constitute income from West Virginia sources only
>
> to the extent that such income is from property employed in a business, trade, profession, or occupation carried on in West Virginia. (W. Va. Code § 11-21-32(b)(2)).
>
> Accordingly, income of nonresident individuals from rents or royalties for the use of, or for the privilege of using in West Virginia, patents, copyrights, secret processes and formulas, goodwill, trade-

> marks, trade brands, franchises, and other like property is taxable if such property has a business situs in West Virginia. Income of nonresidents from other intangible personal property such as shares of stock in C corporations, bonds, notes, bank deposits and other indebtedness is taxable if such property has a business situs in West Virginia.
>
> Intangible personal property has a business situs in West Virginia if it is employed as capital in West Virginia, or the possession and control of the property has been localized in connection with a business, trade, profession, or occupation carried on in West Virginia so that its substance and value attach to and become an asset of the business, trade, profession, or occupation carried on in West Virginia.

The individual nonresident shareholders may claim the amount withheld as a credit against their West Virginia Personal Income Tax liability by attaching a copy of the information statement provided by the S corporation to their West Virginia (Nonresident) Income Tax Return, Form IT-140.

Payment of Tax Withheld: The entire tax withheld from the nonresident shareholder is required to be paid on or before the 15th day of the 3rd month following the close of the taxable year and must accompany the corporation's West Virginia S corporation return. An extension of time to file does not extend the date for payment of tax.

Information Statement of Tax Withheld: Every S corporation required to deduct and withhold tax on nonresident shareholders must provide an information statement to each nonresident shareholder. The information statement provided by the S corporation is not required to be attached to the nonresident shareholder's West Virginia (Nonresident) Income Tax Return, Form IT-140. (For years prior to 2007, Form IT-140NR should be filed.) The S corporation may satisfy this requirement by indicating this information on Form WV/NRW-2, Statement of West Virginia Income Tax Withheld for Nonresident Individual or Organization or in the supplemental information area of the nonresident shareholder's copy of Federal Schedule K-1 or by an attachment to the Federal Schedule K-1 listing the same information. The nonresident shareholders must complete and attach Form IT-140W (West Virginia Withholding Tax Schedule) to their West Virginia Nonresident Income Tax Return to claim credit for the tax withheld.

¶ 120 Composite Nonresident Personal Income Tax Return

Law: W. Va. Code § 11-21-51a

An S Corporation, instead of withholding tax on distributions of West Virginia source income to its nonresident shareholders, may elect to satisfy the nonresident withholding requirements by filing a West Virginia Nonresident COMPOSITE Income Tax Return (Form IT-140NRC) for one or more of its nonresident shareholders. A composite return is a return filed on a group basis as though there was only one taxpayer. A list setting forth the name, address, taxpayer identification number, and percent of ownership of each nonresident shareholder included in the return must be maintained. The list should NOT be submitted with the composite return, but should be made available to the State Tax Department upon request. The return does not have to be signed by each nonresident shareholder provided it is signed by a corporate officer. When filing a composite return, no personal exemptions may be utilized and the rate of tax is 6.5% of the taxable income. The S corporation is responsible for collecting and remitting all income tax due at the time the return is filed. The due date for a composite return is the 15th day of the 4th month following the close of the taxable year. A $50.00 processing fee must also accompany the composite return.

Any nonresident shareholder included in a composite return that has income from any other West Virginia source, must file a separate Nonresident Personal Income Tax Return for the taxable year to report and pay Personal Income Tax on all of his West Virginia source income. The nonresident may claim credit for his or her share of West Virginia income tax remitted with the composite return.

¶ 121 Recordkeeping Requirements

Law: W. Va. Code § 11-24-19.

Every corporation subject to tax under the West Virginia Corporation Net Income Tax Act, and any corporation required to file a return of information with respect to income, must keep such permanent books of account or records as are sufficient to establish the amount of income, deductions, credits or other matters required to be shown by such corporation in any return of such tax or information. The Tax Commissioner is authorized to prescribe the content and form of returns and statements and may require the inclusion in a return, document, or statement of any information he deems necessary for the proper enforcement of the West Virginia Corporation Net Income Tax Act.

Bookkeeping entries of themselves are not conclusive of the amount of income. The actual facts rather than the book entries control. Also, entries on another individual's books are not conclusive against a taxpayer. The books or records required by this regulation must be kept at all times available for inspection by authorized representatives of the Tax Commissioner. The records required in this regulation must be kept accurately, but no particular form is required for keeping the records. Such methods of accounting must be used as will enable the Tax Commissioner to ascertain whether liability for tax has been incurred, and if so, the correctness of the amounts required to be reported in any return of tax or information.

¶ 122 Procedure and Administration

Law: W. Va. Code § 11-24-41

The West Virginia Tax Procedure and Administration Act discussed in Chapter 9 of this Guidebook applies to the corporation net income tax.

¶ 123 Corporation Net Income Tax Return Forms and Schedules

Forms discussed in this chapter are available at the Department's website: http://www.tax.wv.gov.First choose the **Business** icon located along the top of the webpage, and then choose **Corporate Income Tax** from the list along the left column of the page. . The next page that appears will include some of the following forms and schedules, which are available to print or download:

Forms:

BAR-0	Business Activity Report
CNF-120	West Virginia Corporation Net Income Tax Return
CNF-120 APT	Allocation and Apportionment for Multistate Businesses
CNF-120 ES	Estimated Corporate Income/Business Franchise Tax Payment
CNF-120-EXT	Extension Corporation Net Income Tax
CNF-120 TC	Summary of Corporation Net Income Tax Credits
CNF-120 OPT	Election to Report Based on Worldwide Unitary Combined Basis
CNF-120 U	Underpayment of Estimated Tax Penalty
CNF-120 W	Withholding Tax Schedule
CNF-139	Corporation Application for Refund from Carryback of Net Operating Loss
SPF-100	Income/Business Franchise Tax Return for S Corporation and Partnership
SPF-100 APT	Allocation and Apportionment for Multistate Businesses
SPF-100-T	Extension of Time to File Information Returns
WV-100V	Income Tax for S Corporations and Partnerships Electronic Payment Voucher and Instructions
WV-120V	Corporation Net Income Tax Electronic Payment Voucher and Instructions

Schedules:

SP	Shareholder/Partner Information and Nonresident Withholding
UB-1	List of Members in Unitary Combined Group
UB-2	Calculation of WV Taxable Capital of Combined Group
UB-3	Calculation of WV Taxable Income for Combined Group
UB-4-APT	Allocation and Apportionment for Multistate Businesses
UB-4APTSUM	Allocation and Apportionment Summary for Unitary Group
UB-4-CR	Combined Reporting Spreadsheet

Index – Chapter 1 – Corporation Net Income Tax