

MANUFACTURING PROPERTY TAX ADJUSTMENT CREDIT

REPORT TO THE JOINT COMMITTEE ON GOVERNMENT AND FINANCE

July 1, 2023

Submitted by:

West Virginia State Tax Department
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MANUFACTURING PROPERTY TAX ADJUSTMENT CREDIT

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

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

In conformity with the above requirement, the following report provides details on the Manufacturing Property Tax Adjustment Credit (Inventory Tax Credit) from Corporation Net Income Tax (CNIT) and Business Franchise Tax (BFT) returns in State Tax Department databases as of May 22, 2023.¹

Description of the Inventory Tax Credit

As with all other businesses, manufacturers are subject to both State and local taxes. State and local taxes may include tangible personal property taxes on manufacturing inventory, other than finished goods inventory destined for export outside the State. Several tax reform studies have recommended repeal of manufacturing inventory property taxes. However, the tax on inventory is provided for in the West Virginia Constitution and generally benefits local governments. Thus, any change in the tax on inventory would require a Constitutional Amendment to be ratified by the State's electorate. Such an Amendment was submitted to voters for approval in November 2022 and not approved. The Manufacturing Property Tax Adjustment Credit provides some tax relief to manufacturers without directly reducing revenue for local governments.

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

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

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

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

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

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

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

Data Notes

Taxpayers use a variety of taxable periods for the purpose of filing income tax returns. For consistency, the Tax Years reported in this document reflect the year in which a Taxpayer's taxable year begins. For example, some Taxpayers are calendar year filers (*i.e.*, Tax Year 2022 began on January 1, 2022) while others are fiscal year filers² (*e.g.*, Tax Year 2022 began on July 1, 2022). Although the statutory due dates³ of tax returns for calendar year 2022 Taxpayers occurred before the analysis date (*i.e.*, May 22, 2023) of this report, many Taxpayers use an automatic six-month extension of time before filing final returns with credit claims. Most returns of fiscal year taxpayers would not be due until after the analysis date. Given that most calendar year and fiscal year 2022 returns had not yet been filed or fully processed by the Tax Department at the time of this analysis, Tax Year 2022 credit claims are omitted from this report. In addition, due to the complex nature of some tax returns, many Tax Year 2021 returns have yet to be fully processed.

To not misrepresent State Inventory Tax Credit claims, statistical results for all taxable periods—particularly more recent Tax Years—may not include certain returns which are not finalized and thus do not represent complete records of manufacturing inventory tax credit claims. Additionally, tax returns can generally be amended through the third year following the original due date of the return. It is important to note that credit claims for Tax Years 2019, 2020, and 2021 as provided in the tables and figures of this report may be subject to revision by the Taxpayer or upon audit by the Tax Department.

² Statutory due dates for fiscal year Taxpayers are on or before the 15th day of the third month following the close of the taxable year for Pass-Through Entities or the 15th day of the fourth month following the close of the taxable year for C-Corporations. "Pass-Through Entities" include Sub-Chapter S-corporations, partnerships and other business types treated in a similar manner.

³ Tax Year 2022 due dates are March 15, 2023, for Pass-Through Entities treated as a partnership for federal and state income tax purpose and April 18, 2023, for C-Corporations and limited liability companies that elect to be treated as a corporation for federal and state income tax purposes.

Inventory Tax Credit Claimed

Table 1 and Figure A provide data collected from Inventory Tax Credit claims by tax and business type as reported on Corporation Net Income Tax and Business Franchise Tax returns for Tax Years 2009 through 2021. Business Franchise Tax returns are separated into those for Pass-Through Entities (PTEs) and C-Corporations (C-Corp). Appendix A provides changes in the claims of this credit between the July 2022 report and the current report for Tax Years 2014 through 2020.

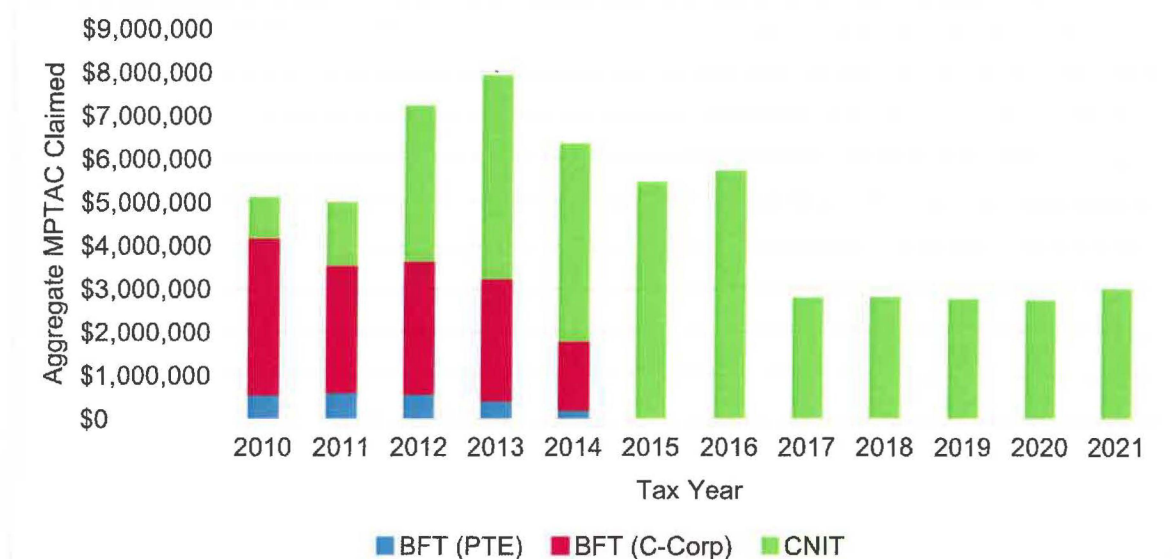
Table 1
State Inventory Tax Credit Claims by Tax and Business Type*

Tax Year	BFT (PTE)	BFT (C-Corp)	CNIT	Total
2009	\$432,473	\$4,746,959	\$2,196,430	\$7,375,862
2010	\$536,322	\$3,633,213	\$950,770	\$5,120,305
2011	\$588,395	\$2,951,417	\$1,458,096	\$4,997,908
2012	\$549,663	\$3,087,753	\$3,604,231	\$7,241,647
2013	\$394,511	\$2,832,347	\$4,707,003	\$7,933,861
2014	\$181,249	\$1,599,903	\$4,576,216	\$6,357,368
2015	\$0	\$0	\$5,469,086	\$5,469,086
2016	\$0	\$0	\$5,731,639	\$5,731,639
2017	\$0	\$0	\$2,805,905	\$2,805,905
2018	\$0	\$0	\$2,823,412	\$2,823,412
2019	\$0	\$0	\$2,780,572	\$2,827,509
2020	\$0	\$0	\$2,756,480	\$2,756,480
2021	\$0	\$0	\$3,013,187	\$3,013,187
Total	\$2,682,613	\$18,851,592	\$42,873,027	\$64,407,232

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

Between 2016 and 2021, the number of inventory tax credit claimants declined by 21 percent. The decline may be attributable to the use of other tax credits, such as the Manufacturing Investment Tax Credit, changes in federal tax laws, additional investment and related bonus depreciation, and other actions which would tend to reduce the income tax liability of manufacturers.

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



Comparison of Manufacturing Inventory Taxes Paid with State Tax Credit Claims

The Inventory Tax Credit allows manufacturers an offset of up to 100 percent of local manufacturing inventory taxes paid against their combined pre-credit tax liability for State Corporation Net Income Tax and Business Franchise Tax. Statistical feedback from property tax assessment data for the ten-year period between Property Tax Year 2010 and Property Tax Year 2019 indicates an average of \$32 million per year in local inventory property taxes assessed to the manufacturing sector. By comparison, State tax credits based on inventory taxes paid averaged roughly \$5.5 million per year between 2009 and 2014 and slightly more than \$3.6 million per year between 2015 and 2021. The State tax credit effectively offset roughly 16 percent of the total local inventory tax paid in years when the State imposed both a Business Franchise Tax and a Corporation Net Income Tax on manufacturers. Following the elimination of the Business Franchise Tax, the tax credit offset amount declined to 14 percent of the local inventory tax paid by the manufacturing sector.

Local property taxes paid on inventory are often greater in magnitude than the amount of corporate net income taxes paid by manufacturing entities. Based on statistical data published by the Internal Revenue Service's Statistics of Income Division, more than 40 percent of all U.S. manufacturing firms filing annual income tax returns, report no net taxable income on their tax returns in any given year⁴. Federal taxable income is the starting point for the determination of the West Virginia Income Tax. These businesses would pay no West Virginia income taxes and therefore would not be able to claim any inventory tax credits. Businesses with taxable income would be able to claim the inventory tax credit. However, some of these Taxpayers would pay more in local inventory property taxes than in State income taxes and therefore be limited in the use of the Inventory Tax Credit. West Virginia also offers manufacturing investment tax credits

⁴ Internal Revenue Service SOI Tax Stats-Historical Table 14b <https://www.irs.gov/statistics/soi-tax-stats-historical-table-14b>

against income tax with the result of less tax liability remaining for offset by the Inventory Tax Credit.

Based on State Inventory Tax Credit schedules filed for Tax Years 2016 to 2021 for companies with a pre-credit state tax liability, roughly 83 percent of reported available credit funds were claimed by Taxpayers. For comparison, the average ratio of claimed credit to available credit was approximately 84 percent for Tax Years 2009 to 2012. Figure B compares the amount of credit available, and amount of credit used by the subset of taxpayers with a pre-credit State tax liability between Tax Years 2016 and 2021. The total reported Inventory Tax Credit available increased from \$5.7 million in Tax Year 2016 to \$5.8 million in Tax Year 2021.

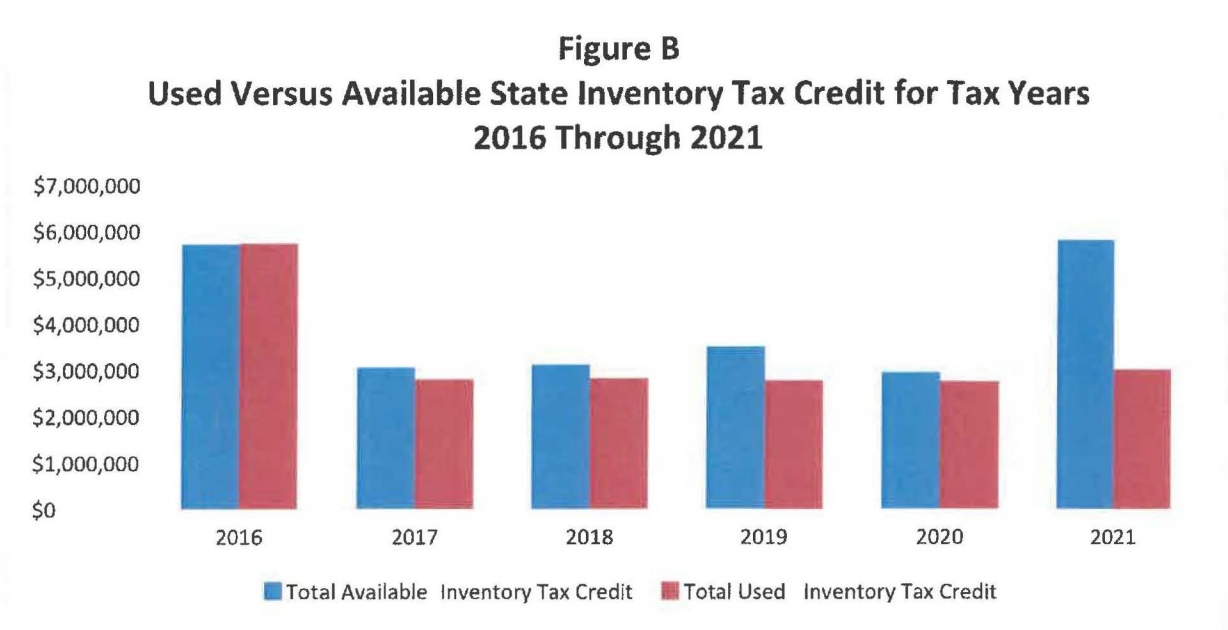


Table 2 contains data on the number of tax credit claims and the share of total credit attributable to the top 5 claims by years since 2015.

Table 2
Inventory Tax Credit Claims

Tax Year	Number of Claims	Share of Credit – Top 5 Claims
2016	38	50.3%
2017	30	58.9%
2018	31	61.5%
2019	31	58.2%
2020	26	54.4%
2021	30	49.5%

The value of the tax credit tends to be concentrated among a small group of Taxpayers with significant year-to-year variance heavily dependent on the profits and tax liability of this small group of participants. On average, the top five taxpayers account for nearly 56 percent of total tax credit claimed each year.

Manufacturing Inventory Personal Property Tax for Tax Year 2022

The basis for the credit is the West Virginia Property Tax paid by manufacturers on the value of manufacturing inventory. Manufacturing inventory is essentially raw materials, goods in process, and finished goods of a manufacturer. Based upon information from the West Virginia State Tax Department Property Tax Division, the total potential manufacturing inventory Personal Property Tax would range between \$34 million to \$38 million after application of the exemption provided by the Freeport Amendment (see Appendix B for the formal description of the exemption).⁵

⁵ These data are provided for illustration of Tax Year 2022 tax rates related to inventory property taxes in West Virginia. Rates of levy vary from year to year; rates of levy for other taxable periods are available online at <https://www.wvsao.gov/localgovernment/reports>.

Table 3
Manufacturing Inventory Personal Property Tax for Tax Year 2022

Item	Value	Percentage of Appraised Value
Supplemental - Raw Materials	\$973,919,638	38.6%
Supplemental - Finished Goods	\$185,850,547	7.4%
Supplemental - Goods in Process	\$458,473,472	18.2%
Supplemental - Machine in Process of Installation	\$299,381,960	11.9%
Supplemental - Parts Held for Owner's Use	\$157,532,472	6.2%
Supplemental - Supplies Held for Owner's Liability	\$151,747,102	6.0%
Inventory	\$54,536,780	2.2%
Supplemental - Incomplete Construction	\$139,593,752	5.5%
Supplemental - Inventory	\$77,471,573	3.1%
Supplies Held for Owner's Use	\$516,190	0.0%
Supplemental - Tool in Process of Installation	\$22,311,778	0.9%
Supplemental - Consigned Goods	\$724,222	0.0%
Parts Held for Owner's Use	\$11,569	0.0%
Total Appraised Value of Inventory	\$2,522,071,055	100.0%
Assessed Value of Inventory	\$1,513,242,633	
Tax Rate	2.40%	
Estimated Property Taxes on Manufacturing Inventory	\$36,317,823	

Formal definitions of all Property Tax classes are presented in Appendix B. Class III tax rates would apply to manufacturing inventory located outside municipal borders, while Class IV tax rates would apply to manufacturing inventory located inside municipal borders. In Table 3, the estimated property taxes on manufacturing inventory were calculated by taking the weighted average of the Class III and Class IV rates and applying this rate of 2.4% to the assessed value of the manufacturing inventory, as it is often difficult to determine whether certain manufacturing inventory items fall outside or inside municipal boundaries. Manufacturing property tends to be more heavily concentrated in jurisdictions with higher property tax rates.

As shown in Table 4, five industries account for 69 percent of the total taxable inventory value. Details on all manufacturing classifications are presented in Appendix C.

Table 4
Manufacturing Inventory Appraised Value for Tax Year 2022 (Largest Industries)

NAICS CODE	Description	Appraised Value of Inventory	% of Total
325	Chemical Manufacturing	\$641,669,466	25.4%
331	Primary Metal Manufacturing	\$465,284,554	18.5%
336	Transportation Equipment Manufacturing	\$237,058,104	9.4%
332	Fabricated Metal Product Manufacturing	\$203,431,154	8.1%
321	Wood Product Manufacturing	\$197,657,618	7.8%

Since the number of Inventory Tax Credit claimants is small, summaries of the credit by manufacturing classification have been withheld to avoid the possible disclosure of tax information for individual taxpayers. The amount of tax credit is constrained by the Taxpayer's Corporation Net Income Tax liability. For Taxpayers who take advantage of this credit, approximately 89 percent of available credit is used on average. The average amount of credit claimed per year from 2011 to 2014 was roughly \$5.5 million. When all returns are finalized for the 2019 to 2021 period, the average annual credit claimed since 2015 is expected to range between \$3.4 million and \$3.8 million per year.

Appendix A
Inventory Tax Credit Claims by Tax and Business Type

Table A-1
Claims from Current Report

	2014	2015	2016	2017	2018	2019	2020	Total
BFT (PTE)	\$181,249	\$0	\$0	\$0	\$0	\$0	\$0	\$181,249
BFT (C-Corp)	\$1,599,903	\$0	\$0	\$0	\$0	\$0	\$0	\$1,599,903
CNIT	\$4,576,216	\$5,469,086	\$5,731,639	\$2,805,905	\$2,823,412	\$2,780,572	\$2,756,480	\$26,943,310
Total	\$6,357,368	\$5,469,086	\$5,731,639	\$2,805,905	\$2,823,412	\$2,780,572	\$2,756,480	\$28,724,462

Table A-2
Claims from July 1, 2022 Report

	2014	2015	2016	2017	2018	2019	2020	Total
BFT (PTE)	\$181,249	\$0	\$0	\$0	\$0	\$0	\$0	\$181,249
BFT (C-Corp)	\$1,296,725	\$0	\$0	\$0	\$0	\$0	\$0	\$1,296,725
CNIT	\$4,576,216	\$5,469,086	\$6,472,356	\$3,708,201	\$2,953,670	\$3,274,802	\$2,980,613	\$29,434,944
Total	\$6,054,190	\$5,469,086	\$6,472,356	\$3,708,201	\$2,953,670	\$3,274,802	\$2,980,613	\$30,912,918

Table A-3
Changes in Claims from July 1, 2022 to Current Report

	2014	2015	2016	2017	2018	2019	2020	Total
BFT (PTE)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
BFT (C-Corp)	\$303,178	\$0	\$0	\$0	\$0	\$0	\$0	\$303,178
CNIT	\$0	\$0	(\$740,717)	(\$902,296)	(\$130,258)	(\$494,230)	(\$224,133)	(\$2,491,634)
Total	\$303,178	\$0	(\$740,717)	(\$902,296)	(\$130,258)	(\$494,230)	(\$224,133)	(\$2,188,456)

Appendix B

Property Tax Classes and the Freeport Amendment

Property Tax Classes:

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

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

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

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

Freeport Amendment:

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

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

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

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

Appendix C

Manufacturing Inventory Tax Allocated by North American Industry Classification System (NAICS) Codes for Tax Year 2022

NAICS CODE	Description	Appraised Value of Inventory	Assessed Value of Inventory	Estimated Property Taxes On Manufacturing Inventory	Share of Total Appraised Value
325	Chemical Manufacturing	\$641,669,466	\$385,001,680	\$9,240,040	25.4%
331	Primary Metal Manufacturing	\$465,284,554	\$279,170,732	\$6,700,097	18.5%
336	Transportation Equipment Manufacturing	\$237,058,104	\$142,234,862	\$3,413,637	9.4%
332	Fabricated Metal Product Manufacturing	\$203,431,154	\$122,058,692	\$2,929,409	8.1%
321	Wood Product Manufacturing	\$197,657,618	\$118,594,571	\$2,846,270	7.8%
339	Miscellaneous Manufacturing	\$183,095,600	\$109,857,360	\$2,636,577	7.3%
324	Petroleum and Coal Product Manufacturing	\$143,037,076	\$85,822,246	\$2,059,734	5.7%
326	Plastics and Rubber Product Manufacturing	\$123,996,026	\$74,397,616	\$1,785,543	4.9%
327	Nonmetallic Mineral Product Manufacturing	\$100,069,415	\$60,041,649	\$1,440,999	4.0%
333	Machinery Manufacturing	\$77,202,767	\$46,321,660	\$1,111,720	3.1%
335	Electrical equipment, Appliance and Component Manufacturing	\$54,988,847	\$32,993,308	\$791,839	2.2%
322	Paper Manufacturing	\$25,642,121	\$15,385,273	\$369,246	1.0%
312	Beverage and Tobacco Manufacturing	\$24,718,514	\$14,831,108	\$355,947	1.0%
311	Food Manufacturing	\$21,203,004	\$12,721,802	\$305,323	0.8%
337	Furniture and Related Product Manufacturing	\$10,494,156	\$6,296,494	\$151,116	0.4%
323	Printing and Related Support Activities	\$6,254,788	\$3,752,873	\$90,069	0.2%
334	Computer and Electronic Product Manufacturing	\$3,652,139	\$2,191,283	\$52,591	0.1%
314	Textile Product Mills	\$1,258,191	\$754,915	\$18,118	0.1%
315	Apparel Manufacturing	\$915,426	\$549,256	\$13,182	0.0%
313	Textile Mills	\$434,757	\$260,854	\$6,260	0.0%
316	Leather and Allied Product Manufacturing	\$7,332	\$4,399	\$106	0.0%
Total		\$2,522,071,055	\$1,513,242,633	\$36,317,823	100.0%