



## WEST VIRGINIA CORPORATION NET INCOME TAX NONBUSINESS INCOME

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The West Virginia Corporation Net Income Tax is a tax imposed upon the West Virginia taxable income of every domestic and foreign corporation which engages in business in West Virginia or which derives income from property, activity, or other sources in West Virginia. The West Virginia Corporation Net Income Tax is a federal conformity tax in that the starting point in computing West Virginia taxable income is the federal taxable income of the corporation. Certain increasing and decreasing adjustments, as required by State law, must be made to federal taxable income to arrive at West Virginia taxable income. Multi-state corporations must take one further step to determine West Virginia taxable income. They are required to allocate certain items of nonbusiness income and apportion their remaining income based on a four factor formula consisting of payroll, property, and double weighted sales factors.

The purpose of this publication is to provide multi-state corporate taxpayers with information regarding what is nonbusiness income and how it is allocated for West Virginia Corporation Net Income Tax purposes. This publication is meant to be a source of general information and is not a substitute for tax laws or regulations.

### SUMMARY

Nonbusiness income - All income that is not business income is nonbusiness income. Essentially nonbusiness income is income that is not earned from transactions and activity in the regular course of the taxpayer's trade or business.

Allocation - The direct assignment for tax purposes of certain types of income to specific states. Usually, the state where the property is located or if the taxpayer is not taxable in that state, the taxpayer's state of commercial domicile.

Thus, income that is not earned in the course of the taxpayer's trade or business will normally be allocated to and taxable in the state where the property generating the income is located or in the state of commercial domicile.

### BUSINESS INCOME

Perhaps the best way to understand nonbusiness income is to first understand how the law defines business income.

"Business income" is defined as income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's trade or business operations. In essence, all income which arises from the conduct of trade or business operations is business income unless it is clearly classifiable as nonbusiness income.

Business income is apportioned to West Virginia by use of a four factor apportionment formula. This apportionment formula consists of a property factor, a payroll factor, and a double weighted sales factor.

## NONBUSINESS INCOME

“Nonbusiness income” is defined as all income that is not business income. Essentially, all income that is not earned from transactions and activity in the regular course of a taxpayer’s trade or business is considered nonbusiness income.

If a taxpayer’s business activities take place both in and out of West Virginia and they are subject to a net income or franchise tax in another state, certain items of income, to the extent that they constitute nonbusiness income may be allocated. That is, the income is taxable in the state where it arose. All other net income must be apportioned.

However, if a taxpayer’s business is conducted entirely within West Virginia, all of their net income, after adjustments, is subject to the West Virginia Corporation Net Income Tax regardless of whether it is business or nonbusiness income.

Under West Virginia Code § 11-24-7 (d) only certain types of income can be classified as nonbusiness income. The types of income that can be classified as nonbusiness income include the following:

rents and royalties from real and tangible personal property  
capital gains  
interest  
dividends  
patent or copyright royalties  
corporate partner’s distributive share of partnership income

What follows is a discussion of these classes of nonbusiness income that can be allocated.

### RENTS AND ROYALTIES FROM REAL PROPERTY

Rents and royalties from real property are nonbusiness income if the property is not used in the taxpayer’s trade or business.

Net rents and royalties from real property located in West Virginia are allocated West Virginia.

### RENTS AND ROYALTIES FROM TANGIBLE PERSONAL PROPERTY

Rents and royalties from tangible personal property are nonbusiness income if the property is not used in the taxpayer’s normal trade or business activity.

Net rents and royalties from tangible personal property are allocated to West Virginia as nonbusiness income:

- (1) by the ratio of the properties use in West Virginia as compared to other states, or
- (2) totally, if the taxpayer’s commercial domicile is in West Virginia and the taxpayer is not organized under the laws of or taxable in the state in which the property is used.

It is important to understand that “commercial domicile” means the principal place from which the trade or business of the taxpayer is directed or managed.

The measure of use of tangible personal property in this state as compared to other states is determined by multiplying the rent and royalties by a fraction. The numerator of this fraction is the number of days of physical location of the property in West Virginia during the period. The denominator is the number of days of physical location of the property everywhere during all rental and royalty periods in the taxable year. If the physical location of the property during the rental or royalty period is unknown or unascertainable by the taxpayer, then it is presumed that the taxpayer used the tangible personal property in the state in which the property was located at the time the rental or royalty payer obtained possession.

## CAPITAL GAINS/LOSSES

A capital gain arises when a capital asset is sold for a gain. A capital loss occurs when the capital asset is sold for a loss. Broadly speaking, all assets are capital assets except those excluded from the definition of a capital asset by the Internal Revenue Code.

What is a capital asset? Each item of property that the corporation held (whether or not connected with its trade or business) is a capital asset, except:

- Assets that can be inventoried or property held mainly for sale to customers.
- Depreciable or real property used in the trade or business.
- Certain copyrights; literary, musical, or artistic compositions; letters or memorandums; or similar property.
- Accounts or notes receivable acquired in the ordinary course of trade or business for services rendered or from the sale of property described in 1 above.
- A U.S. Government publication received from the Government or any of its agencies in a manner other than buying it at the price offered for public sale, which is held by a taxpayer who received the publication or by a second taxpayer in whose hands the basis of the publication is determined, for purposes of determining gain from a sale or exchange, by referring to its basis in the hands of the first taxpayer.

## CAPITAL GAINS/LOSSES FROM REAL PROPERTY

Capital gains and losses from sales of real property located in West Virginia are allocable to West Virginia if the gain/loss is nonbusiness income.

## CAPITAL GAINS/LOSSES FROM TANGIBLE PERSONAL PROPERTY

Capital gains and losses from sales of tangible personal property are allocable to West Virginia if the gain/loss is nonbusiness income and (1) the property was located in West Virginia at the time of the sale, or (2) the taxpayer's commercial domicile is in West Virginia and the taxpayer is not taxable in the state in which the property was located.

## CAPITAL GAINS/LOSSES FROM INTANGIBLE PERSONAL PROPERTY

Capital gains and losses from the sales of intangible personal property, e.g. stocks, bonds, etc., are allocable to West Virginia if the taxpayer's commercial domicile is in West Virginia and the gain/loss is nonbusiness income.

## GAINS FROM THE SALE OF NATURAL RESOURCES

Gains pursuant to section 631 (a) and (b) of the Internal Revenue Code of 1986, as amended, from the sale of natural resources severed in West Virginia are allocable to West Virginia if they are nonbusiness income. Section 631 (a) of the Internal Revenue Code establishes an election for the taxpayer to consider cutting of timber as a sale or exchange and Section 631 (b) deals with gains or losses from the disposal of timber when the owner retains an economic interest in the timber.

## ORDINARY GAINS AND LOSSES

Ordinary gains and losses are considered to be business income and cannot be allocated; only capital gains/losses can be allocated as nonbusiness income.

## INTEREST AND DIVIDEND INCOME

Dividend income is presumed to be nonbusiness income unless a taxpayer is primarily engaged in the business of making investments.

Interest income is nonbusiness income when it is earned from intangible property that was not created in the regular course of the taxpayer's trade or business operations. Interest income is also nonbusiness income where the reason for acquiring and holding the intangible property is not related to or incidental to the taxpayer's trade or business operations.

Interest and dividend income, if they are nonbusiness income, are allocated to West Virginia if the taxpayer's commercial domicile is in West Virginia.

## PATENT AND COPYRIGHT ROYALTIES

Patent and copyright royalties are nonbusiness income if the patent or copyright did not arise out of or was not created in the regular course of the taxpayer's trade or business operations where the purpose for acquiring and holding the patent or copyright is not related to or incidental to such trade or business operations.

Patent and copyright royalties are allocated to West Virginia (1) if the patent or copyright is used by the taxpayer in West Virginia or (2) if the patent or copyright is used by the taxpayer in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in West Virginia.

A *patent* is used in a state to the extent that it is employed in production, fabrication, manufacturing, or other processing in that state or to the extent that a patented product is produced in that state. If the basis of receipts from patent royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilizations, the patent is utilized in the state in which the taxpayer's commercial domicile is located.

A *copyright* is used in a state to the extent that printing or other publication originates in that state. If the basis of receipts from copyright royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the copyright is utilized in the state in which the taxpayer's domicile is located.

## CORPORATE PARTNER'S DISTRIBUTIVE SHARE

A corporate partner's distributive share of partnership income, gain, loss, deduction or credit is allocated to West Virginia to the extent it is derived from partnership activity in West Virginia, whether such income is business or nonbusiness income in the hands of the partnership. State law presumes that a corporate partner's distributive share of partnership income is nonbusiness income.

Questions about the classification of specific items of income should be addressed to the:

West Virginia Department of Tax and Revenue  
Taxpayer Services Division  
P. O. Box 3784  
Charleston, WV 25337-3784

Telephone: (304) 558-3333 or  
Toll free within West Virginia 1-800-WVTAXS (1-800-982-8297) or  
TDD service for the hearing impaired 1-800-2TAXTDD (1-800-282-9833)

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