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Annual Survey of Virginia Law: Taxation

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TAXATION

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This article covers legislative changes and judicial decisions affecting Virginia taxation from July, 1991 to July, 1992. Its purpose is to alert Virginia's tax and general practitioners to these developments.

In its 1992 session, the General Assembly of Virginia passed many bills amending Title 58.1 of the Code of Virginia (Code). These enactments affect a broad range of areas, including individual and corporate income tax, retail sales and use tax, miscellaneous taxes administered by agencies other than the Department of Taxation and miscellaneous local taxes. Unless noted otherwise, legislation during the 1992 session is effective July 1, 1992.

The Supreme Court of Virginia decided several cases, including one case granted certiorari by the Supreme Court of the United States concerning state taxation of federal retirement benefits. The court also rendered decisions concerning miscellaneous local taxation issues, including transient occupancy taxes, business license taxes, and utility taxes. The Virginia Department of Taxation did not finalize any significant regulations this year.

I. LEGISLATIVE ACTIVITY

A. *Taxes Administered by the Department of Taxation*

1. General Provisions

Section 58.1-3 of the Code, relating to secrecy of information, was amended to authorize the Department of Taxation to make

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certain tax information available to the Department of Treasury in order to help locate owners of unclaimed property.¹

The Assembly enacted omnibus legislation amending eight sections of the Code related to taxes administered by the Department of Taxation.² This legislation makes the following changes:

(1) It eliminates the requirement that a taxpayer be notified by certified or registered mail that a check for payment of taxes has been returned by the bank;³

(2) It amends the definition of "income and deductions from Virginia sources" to include prizes paid by the Virginia Lottery Department and gambling winnings from wagers placed or paid at a location in Virginia;⁴

(3) It requires taxpayers to file an amended state return if (i) the reported amount of federal taxable income on a federal tax return is changed by the Internal Revenue Service or (ii) if additional estate tax is due as a result of a determination of a federal estate tax deficiency, unless the Department has sufficient information from which to compute the additional tax and the taxpayer has paid such tax;⁵

(4) It amends the definition of Virginia taxable income for individuals and corporations to include items subject to accumulation distributions;⁶

(5) It changes the time period for filing an amended return to (i) within three years from the last day prescribed by law for the timely filing of the return, or (ii) within ninety days from the final determination of any change or correction in the taxpayer's liability for any federal tax upon which the state tax is based, whichever is later, provided that the refund due does not exceed the decrease in Virginia tax attributable to the federal change, or (iii) within one year of filing an amended Virginia return resulting in the payment of additional tax, provided that the amended return raises no

1. Act of Mar. 20, 1992, ch. 386, 1992 Va. Acts 497 (codified as amended at VA. CODE ANN. § 58.1-3(C)(viii) (Cum. Supp. 1992)).

2. Act of April 13, 1992, ch. 678, 1992 Va. Acts 993 (codified as amended at VA. CODE ANN. §§ 58.1-12, -302, -311, -402, -906, -1823, and -2508 (Cum. Supp. 1992)).

3. VA. CODE ANN. § 58.1-12(B) (Cum. Supp. 1992).

4. *Id.* § 58.1-302 (Cum. Supp. 1992).

5. *Id.* §§ 58.1-311, -906(B) (Cum. Supp. 1992).

6. *Id.* §§ 58.1-322(B), -402(B) (Cum. Supp. 1992).

new issues and the refund does not exceed the amount of the payment with the prior amended return;⁷ and,

(6) It clarifies that the exemption from license fees or income taxes applicable to insurance companies does not apply to the retail sales and use tax.⁸

2. Income Tax

The General Assembly repealed sections 58.1-339.1 and 58.1-437 of the Code relating to the income tax credit for television and radio broadcasters who broadcast public service messages concerning substance abuse. The amendment applies to taxable years beginning on and after January 1, 1992.⁹

New legislation extends the sunset for the tax credit for machinery and equipment used for processing recyclable materials from January 1, 1993 to January 1, 1995.¹⁰

The Assembly amended the methodology for determining whether a landlord is eligible for a tax credit for rent reductions provided to low income elderly and disabled tenants.¹¹ Effective January 1, 1992, a landlord may use comparable units in the same market area if there are no comparable units in the same property to determine compliance with the fifteen percent threshold.¹²

The Assembly revised the provisions of section 58.1-332 of the Code relating to credits for income taxes paid to other states.¹³ Formerly, the credit was limited to the proportion of the taxpayer's Virginia income tax obligation represented by the relationship of his taxable income in the other state to his Virginia taxable income.¹⁴ The new legislation addresses situations where the income taxed by another state is less than that taxed by Virginia.

7. *Id.* § 58.1-1823 (Cum. Supp. 1992). The time period in the current statute is the later of three years from the last day prescribed by law for the timely filing of the return or within sixty days from the final determination of any change or correction in the taxpayer's liability for any federal tax upon which a state tax is based. *Id.* (Repl. Vol. 1991).

8. *Id.* § 58.1-2508 (Cum. Supp. 1992).

9. Act of Mar. 20, 1992, ch. 394, 1992 Va. Acts 506.

10. Act of Mar. 17, 1992, ch. 313, 1992 Va. Acts 391. The tax credit to which this act applies can be found in VA. CODE ANN. § 58.1-338 (Repl. Vol. 1991).

11. Act of Mar. 19, 1992, ch. 369, 1992 Va. Acts 469 (codified as amended at VA. CODE ANN. § 58.1-339 (Cum. Supp. 1992)).

12. VA. CODE ANN. § 58.1-339(iii) (Cum. Supp. 1992).

13. Act of Mar. 17, 1992, ch. 317, 1992 Va. Acts 402 (codified as amended at VA. CODE ANN. § 58.1-332(A) (Cum. Supp. 1992)).

14. VA. CODE ANN. § 58.1-332 (Repl. Vol. 1991).

The amended section limits the credit to the amount of income tax otherwise payable under Virginia law if all taxable income earned outside of Virginia is earned from a single state contiguous to Virginia.¹⁵ The provisions of this act are effective for taxable years beginning on or after January 1, 1992.¹⁶

During the 1992 session the General Assembly deferred the effective dates of several previous enactments. Practitioners should note that the effective date of additional withholding allowances found in sections 58.1-461, 58.1-462, and 58.1-470 of the Code has been deferred from January 1, 1993 to January 1, 1995.¹⁷ Similarly, two separate enactments defer the effective date for low-income housing credits, set forth in three sections of the Code, from January 1, 1992 until January 1, 1994. This legislation is effective for taxable years on or after January 1, 1992.¹⁸

The Assembly amended section 58.1-322 of the Code relating to the computation of Virginia taxable income.¹⁹ Effective for taxable years beginning on or after January 1, 1992 and until January 1, 1994, in determining Virginia taxable income an individual must add back any self-employment tax deduction to the extent excluded from federal adjusted gross income.²⁰ In addition, this legislation defers the subtraction, to the extent included in federal adjusted gross income, of self-employment tax for taxable years beginning on or after January 1, 1994 through January 1, 1997.²¹

The Code was also amended²² to exempt from income taxation the first \$250 of interest income earned from a financial institution with at least one office in the Commonwealth²³ and to phase in a new Virginia business activity investment tax credit of \$3,750 in

15. *Id.* § 58.1-332(A)(ii) (Cum. Supp. 1992).

16. Act of Mar. 17, 1992, ch. 317, 1992 Va. Acts 402.

17. Act of Mar. 20, 1992, ch. 385, 1992 Va. Acts 497 and Act of Mar. 20, 1992, ch. 401, 1992 Va. Acts 508.

18. Act of Mar. 17, 1992, ch. 325, 1992 Va. Acts 410 and Act of Mar. 17, 1992, ch. 347, 1992 Va. Acts 428 (codified as amended at VA. CODE ANN. §§ 36-55.63, 58.1-336, and 58.1-435 (Cum. Supp. 1992)).

19. Act of Apr. 3, 1992, ch. 665, 1992 Va. Acts 979 and Act of Apr. 4, 1992, ch. 691, 1992 Va. Acts 1014 (codified as amended at VA. CODE ANN. § 58.1-322 (Cum. Supp. 1992)).

20. VA. CODE ANN. § 58.1-322(B)(8) (Cum. Supp. 1992).

21. *Id.* § 58.1-322(C)(16) (Cum. Supp. 1992).

22. Act of Apr. 3, 1992, ch. 686, 1992 Va. Acts 1008 (codified as amended at VA. CODE ANN. §§ 58.1-322, -438 (Cum. Supp. 1992)).

23. VA. CODE ANN. § 58.1-322(C)(17) (Cum. Supp. 1992).

1992, \$7,500 in 1993, \$15,000 in 1994 and \$30,000 in 1995.²⁴ These provisions are effective for taxable years beginning on or after January 1, 1994 if reenacted by the 1993 session of the General Assembly. This act expires for taxable years beginning on or after January 1, 1999.²⁵

An amendment to section 58.1-460 of the Code relating to income tax withholding²⁶ now excludes from withholding amounts paid pursuant to individual retirement plans (IRA) and simplified employee pension plans (SEPP), or to their beneficial owners, or to a financial institution, corporation, partnership or other person or entity with respect to benefits paid as custodian, trustee, or depository for an IRA or SEPP. The amendments are made by revising the definitions of "wages," "employees," and "employer"²⁷ and are effective for all taxable years beginning on or after January 1, 1992.²⁸

3. Retail Sales and Use Tax

The provisions of the Code relating to exemptions from sales and use tax embodied in section 58.1-608 have been amended by four separate enactments.

The exemption for controlled drugs purchased for use by a licensed physician in his professional practice has been broadened to apply regardless of whether the practice is organized as a sole proprietorship, partnership or professional corporation.²⁹

The previous exemption for alcoholic beverages sold in Virginia ABC stores has been deleted and such beverages are now subject to the sales and use tax.³⁰

24. *Id.* § 58.1-438 (Cum. Supp. 1992). Any tax credit which is not usable for the tax year in which the investment is made may be carried over for a maximum of five years until the full credit is utilized. *Id.* § 58.1-438(C).

25. Act of Apr. 3, 1992, ch. 686, 1992 Va. Acts 1008.

26. Act of Mar. 30, 1992, ch. 519, 1992 Va. Acts 663 (codified as amended at VA. CODE ANN. § 58.1-460 (Cum Supp. 1992)).

27. VA. CODE ANN. § 58.1-460 (Cum. Supp. 1992).

28. Act of Mar. 30, 1992, ch. 519, 1992 Va. Acts 663.

29. Act of Mar. 27, 1992, ch. 494, 1992 Va. Acts 627 (codified as amended at VA. CODE ANN. § 58.1-608(A)(7)(a) (Cum. Supp. 1992)).

30. Act of Mar. 17, 1992, ch. 314, 1992 Va. Acts 392 (former provision at VA. CODE ANN. § 58.1-608(A)(1)(d) (Repl. Vol. 1991)).

Section 58.1-608 of the Code, relating to exemptions from the retail sales and use tax, was amended this session.³¹ The amendments clarify the effective dates for certain governmental and commodities exemptions, nonprofit civic and community service exemptions, and nonprofit cultural organization exemptions.³² Nonprofit historical societies maintaining research libraries are no longer required to provide free admission to the public in order to qualify for the exemption.³³ One of the amendments changes the effective date for the exemption for nonprescription drugs from July 1, 1992 to July 1, 1994.³⁴

Similarly, legislation amended section 58.1-610 of the Code to classify any person furnishing and installing locks and locking devices as a retailer, rather than a contractor, under the sales and use tax provisions.³⁵

4. Miscellaneous Taxes

a. Criminal Penalties for Certain State Tax Offenses

Legislation enacted this year amended eight sections in title 58.1 of the Code and added a section to each of titles 18.2 and 58.1 relating to criminal penalties for certain state tax offenses.³⁶ The new section in title 18.2 makes the knowing issuance of a bad check for the payment of taxes a Class 1 misdemeanor.³⁷ The new section in title 58.1 creates a Class 6 felony for converting or diverting collection of sales, use or withholding taxes and includes a five-year statute of limitations.³⁸ Finally, the Code now allows a summons to any witness or a summons to produce any document

31. Act of Mar. 23, 1992, ch. 437, 1992 Va. Acts 559 and Act of Apr. 1, 1992, ch. 601, 1992 Va. Acts 857 (codified as amended at VA. CODE ANN. § 58.1-608(A) (Cum. Supp. 1992)).

32. VA. CODE ANN. § 58.1-608(A) (Cum. Supp. 1992).

33. *Id.* § 58.1-608(A)(9)(a) (Cum. Supp. 1992).

34. *Id.* § 58.1-608(A)(7)(o) (Cum. Supp. 1992).

35. Act of Mar. 23, 1992, ch. 404, 1992 Va. Acts 510 (codified as amended at VA. CODE ANN. § 58.1-610 (Cum. Supp. 1992)).

36. Act of Apr. 5, 1992, ch. 763, 1992 Va. Acts 1184 (codified as amended at VA. CODE ANN. §§ 18.2-182.1, 58.1-216, -486, -637, -1005, -1008, -1017, -1614, -1618, and -1816 (Cum. Supp. 1992)).

37. VA. CODE ANN. § 18.2-182.1 (Cum. Supp. 1992). This new section now defines the violations referred to in amended VA. CODE ANN. §§ 58.1-486, -637. *Id.* § 18.2-182.1.

38. *Id.* § 58.1-1816 (Cum. Supp. 1992).

to be personally served by an employee of the Department of Taxation or in the manner provided in section 58.1-217.³⁹

b. Disposition of Tax Revenues

Under legislation amending section 58.1-1724, revenues collected from the two percent regional gas tax may now be applied to the capital as well as the operating deficit and debt service of the mass transit system.⁴⁰

B. Taxes Administered by Other Agencies

1. Motor Fuel and Special Fuel Tax

The Assembly amended sections 58.1-2704, 58.1-2706, and 58.1-2707 of the Code.⁴¹ Added to section 58.1-2704 is a new formula, effective October 1, 1992, for calculating the amount of fuel used in the operations of any motor carrier in the Commonwealth.⁴² The amendment to section 58.1-2706 shortens the refund period from 180 days to 90 days when the amount of credit to which any motor carrier is entitled exceeds the amount of its tax liability. In addition, this section now grants the State Corporation Commission discretion to require an audit when refunds of motor fuel tax are requested.⁴³ The prior statute required the Commission to perform an audit for refunds of \$100 or more.⁴⁴

2. Virginia Motor Vehicle Sales and Use Tax

The tax rate on daily rental passenger cars called for in section 58.1-2402 has been increased from two and one-half percent to four percent.⁴⁵

39. *Id.* § 58.1-216 (Cum. Supp. 1992). VA. CODE ANN. § 58.1-217 (Repl. Vol. 1991) directs service of writs, processes and orders by the sheriff or constable of the county or city.

40. Act of Mar. 30, 1992, ch. 579, 1992 Va. Acts 775 (codified as amended at VA. CODE ANN. § 58.1-1724 (Cum. Supp. 1992)).

41. Act of Mar. 17, 1992, ch. 309, 1992 Va. Acts 389 (codified as amended at VA. CODE ANN. §§ 58.1-2704, -2706, -2707 (Cum. Supp. 1992)).

42. VA. CODE ANN. § 58.1-2704 (Cum. Supp. 1992).

43. *Id.* § 58.1-2706 (Cum. Supp. 1992).

44. *Id.* § 58.1-2706(C) (Repl. Vol. 1991).

45. Act of Mar. 20, 1992, ch. 384, 1992 Va. Acts 496 (codified as amended in VA. CODE ANN. § 58.1-2402(A)(4) (Cum. Supp. 1992)).

C. *Local Taxes*

1. General Provisions

As of July 1, 1992, in addition to local taxes and other fees, charges generated by the sale of utility services may be paid by credit card.⁴⁶

2. Real Property Tax

The General Assembly amended section 58.1-3211 of the Code,⁴⁷ relating to income and net worth limitations for property tax relief for the elderly and handicapped, to add Henrico and Fauquier to the list of counties that may raise the income and financial worth limitations for any exemption or deferral program.⁴⁸

3. Tangible Personal Property, Machinery and Tools

The General Assembly amended section 58.1-3506 of the Code, relating to taxation of tangible personal property, to create a separate classification for forest harvesting equipment so that a locality may tax such equipment at a lower rate.⁴⁹

Sections 58.1-3506 and -3507 were also amended to classify and assess taxes against energy conversion and cogeneration equipment.⁵⁰ The amendment to section 58.1-3506 expands the separate classification for generating or cogeneration equipment to include, without limitation, equipment purchased by firms engaged in the business of generating electricity, steam or both.⁵¹

46. Act of Mar. 16, 1992, ch. 292, 1992 Va. Acts 363 (codified as amended at VA. CODE ANN. § 58.1-3013 (Cum. Supp. 1992)).

47. Act of Mar. 17, 1992, ch. 346, 1992 Va. Acts 427 (codified as amended at VA. CODE ANN. § 58.1-3211 (Cum. Supp. 1992)).

48. *Id.* § 58.1-3211(3). A separate enactment added only Henrico County to the list of counties that can raise the income and financial worth limitations for any exemption and deferral program. Act of Mar. 20, 1992, ch. 383, 1992 Va. Acts 495 (codified as amended at VA. CODE ANN. § 58.1-3211 (Cum. Supp. 1992)). Both acts were signed into law by the Governor.

49. Act of Apr. 3, 1992, ch. 642, 1992 Va. Acts 945 (codified as amended at VA. CODE ANN. § 58.1-3506 (Cum. Supp. 1992)).

50. Act of Apr. 3, 1992, ch. 680, 1992 Va. Acts 1000 (codified as amended at VA. CODE ANN. §§ 58.1-3506, -3507 (Cum. Supp. 1992)).

51. VA. CODE ANN. § 58.1-3506 (Cum. Supp. 1992).

4. License Taxes

During the 1992 session, the Assembly amended sections 58.1-3706 and 58.1-3732 of the Code relating to limitations on the rate of local license taxes. These provisions become effective July 1, 1993.⁵² They limit the license tax rate on any person, firm or corporation designated as the principal or prime contractor receiving federal appropriations for research and development services. Documentation must be provided confirming the applicability of this section to the local commissioner of revenue or finance officer.⁵³ This legislation also excludes from gross receipts for license tax purposes the original cost of computer software and hardware sold to a United States federal or state government entity. The property must have been purchased within two years of the sale to the government entity by the original purchaser and the purchaser must have been contractually obligated at the time of the purchase to resell to a state or federal government entity.⁵⁴

The Assembly also extended from July 1, 1992 until July 1, 1995 the authority of any city or county to impose a license tax on businesses that sever oil from the earth.⁵⁵

5. Miscellaneous Taxes

a. Transient Occupancy Tax and Food and Beverage Tax

Sections 58.1-3819 and -3833 of the Code have been amended to provide that all collections of transient occupancy, food, beverage and meals taxes are deemed to be held in trust for the county, city or town imposing the tax.⁵⁶

b. Local Utility Tax

The Assembly amended section 58.1-3814 of the Code, relating to local utility tax, to eliminate the possibility of double taxation

52. Act of Apr. 3, 1992, ch. 632, 1992 Va. Acts 925 (codified as amended at VA. CODE ANN. §§ 58.1-3706, -3732 (Cum. Supp. 1992)).

53. VA. CODE ANN. § 58.1-3706 (Cum. Supp. 1992).

54. *Id.* § 58.1-3732 (Cum. Supp. 1992).

55. Act of Mar. 20, 1992, ch. 397, 1992 Va. Acts 397. The code section describing this tax can be found in VA. CODE ANN. § 58.1-3712.1 (Repl. Vol. 1991).

56. Act of Mar. 13, 1992, ch. 263, 1992 Va. Acts 322 (codified as amended at VA. CODE ANN. §§ 58.1-3819, -3833 (Cum. Supp. 1992)).

of compressed natural gas sales by making the section inapplicable to utility sales of products used as motor vehicle fuels.⁵⁷

6. Enforcement, Collection, Refunds, Remedies and Review of Local Taxes

The Assembly amended several provisions of the Code relating to local tax collection and administration.⁵⁸ Section 58.1-3149 now specifically permits the common practice of local treasurers to allow the payment of taxes and other fees at bank branches.⁵⁹ In addition, the Code now authorizes all local treasurers to employ private collectors to collect local taxes, other than real estate taxes, that remain delinquent for a period of *six* months or more.⁶⁰ Previously, this section authorized the use of private collectors only by treasurers of counties under the county manager plan of government for taxes delinquent for a period of *two* months.⁶¹ This legislation also requires a governing body to obtain the treasurer's approval before employing a collector or attorney to collect any local taxes, other than real estate taxes, that have been delinquent for six months or more.⁶²

Sections 58.1-3980 and 58.1-3984 of the Code, relating to applications for correction of local taxes, have been amended to permit a taxpayer to apply for a correction of an assessment within three years from the last day of the tax year for which such assessment is made, or within one year from the date of the assessment, whichever is later.⁶³

57. Act of Mar. 20, 1992, ch. 399, 1992 Va. Acts 507 (codified as amended at VA. CODE ANN. § 58.1-3814 (Cum. Supp. 1992)).

58. Act of Apr. 3, 1992, ch. 683, 1992 Va. Acts 1006 (codified as amended at VA. CODE ANN. §§ 58.1-3149, -3919.1, -3934 (Cum. Supp. 1992)).

59. VA. CODE ANN. § 58.1-3149 (Cum. Supp. 1992).

60. *Id.* § 58.1-3119.1 (Cum. Supp. 1992).

61. *Id.* § 58.1-3919.1 (Repl. Vol. 1991).

62. *Id.* § 58.1-3934. (Cum. Supp. 1992). A separate enactment incorporated the same amendments to VA. CODE ANN. §§ 58.1-3919.1 and -3934 relating to the collection of delinquent local taxes. Act of Apr. 3, 1992, ch. 625, 1992 Va. Acts 906 (codified as amended at VA. CODE ANN. §§ 58.1-3919.1, -3934 (Cum. Supp. 1992)).

63. Act of Mar. 20, 1992, ch. 382, 1992 Va. Acts 495 (codified as amended at VA. CODE ANN. §§ 58.1-3980, -3984 (Cum. Supp. 1992)).

II. JUDICIAL DECISIONS

A. *State Taxation of Federal Retirement Benefits*

The 1989 U.S. Supreme Court decision *Davis v. Michigan Department of Treasury*⁶⁴ established that a state which taxes federal government pensions while exempting state government pensions from taxation violates the doctrine of intergovernmental tax immunity embodied in the Supremacy Clause of the Constitution of the United States.⁶⁵ Unfortunately, in *Davis* the State of Michigan conceded that refunds were due if the tax was invalid; therefore, the Supreme Court did not decide whether the decision had retroactive application.⁶⁶

Retroactive application of the *Davis* decision was the issue in *Harper v. Virginia Department of Taxation (Harper I)*.⁶⁷ Initially, the Supreme Court of Virginia affirmed the trial court's ruling that the *Davis* decision should be applied only prospectively. Following the three-pronged test announced in *Chevron Oil Co. v. Huson*,⁶⁸ the court found (i) that the *Davis* decision established a new principle of law, (ii) that retroactive application would do nothing to retard or develop the doctrine of intergovernmental tax immunity, and (iii) that the equities favored the Commonwealth.⁶⁹ The Supreme Court of the United States vacated this decision and remanded⁷⁰ the case for further consideration based on their holding in *James B. Beam Distilling Co. v. Georgia*.⁷¹ On remand (*Harper II*),⁷² the Supreme Court of Virginia reaffirmed its earlier decision and its use of the *Chevron Oil* test, holding that the grounds for the *Beam* decision were narrowly confined to an issue of choice of law and that *Beam* did not reject the *Chevron Oil* test. Furthermore, the court held that because the U.S. Supreme Court did not

64. 489 U.S. 803 (1989).

65. U.S. CONST. art. VI, cl. 2; see, e.g., *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819).

66. *Davis*, 489 U.S. at 817.

67. 241 Va. 232, 401 S.E.2d 868, *vacated*, 111 S. Ct. 2883, *reaff'd*, 242 Va. 322, 410 S.E.2d 629 (1991), *cert. granted*, 112 S. Ct. 1934 (1992), *and order granting cert. modified*, 112 S. Ct. 2298 (1992).

68. 404 U.S. 97 (1971).

69. *Harper I*, 241 Va. at 237-40, 401 S.E.2d at 871-73.

70. 111 S. Ct. 2883 (1991).

71. 111 S. Ct. 2439 (1991).

72. *Harper v. Virginia Dept. of Taxation (Harper II)*, 242 Va. 322, 410 S.E.2d 629 (1991).

rule on the retroactive application of its decision in *Davis*, the use of the *Chevron Oil* test was not foreclosed by precedent.⁷³

In May, 1992, the Supreme Court of the United States granted a writ of certiorari for *Harper II*.⁷⁴ If the taxpayer ultimately prevails on this issue, the potential tax refund liability, inclusive of interest, could reportedly exceed \$440,000,000.⁷⁵

B. Local Tax Ordinances

1. Transient Occupancy Tax Ordinance

In *Delta Air Lines, Inc. v. County Board of Arlington*,⁷⁶ the Supreme Court of Virginia affirmed the validity of Arlington County's transient occupancy tax. The Code enables cities, counties and towns to enact ordinances that levy taxes on hotels, motels, boarding houses and travel campgrounds.⁷⁷ Arlington's ordinance imposed a five percent tax on "each and every transient."⁷⁸ Both the enabling legislation and the local ordinance contain an exemption from the tax for continuous occupancy by the same individual or group for thirty or more days,⁷⁹ which the hotels claimed applied in this case.

Under its ordinance, the County assessed two hotels for taxes, penalties and interest for lodging secured by Delta Air Lines for use by its employees. Delta and the hotels sought a declaration that the County's ordinance was invalid and that the taxes were incorrectly assessed because the thirty-day exemption applied.⁸⁰ The trial court ruled that the County's ordinance was valid and that the thirty-day exemption did not apply to Delta because Delta was not a "person" within the ordinance's definition of a transient or an individual or group under the language of the enabling statute.⁸¹

73. *Id.* at 326, 410 S.E.2d at 631-32.

74. 112 S. Ct. 1934. The order granting certiorari has been modified to limit argument to the issue of retroactive application of the *Davis* decision. 112 S. Ct. 2298 (1992).

75. *Harper I*, 241 Va. at 239, 401 S.E.2d at 873.

76. 242 Va. 209, 409 S.E.2d 130 (1991).

77. VA. CODE ANN. §§ 58.1-3819, -3820 (Repl. Vol. 1991).

78. *Delta Air Lines*, 242 Va. at 212, 409 S.E.2d at 132, (quoting § 40-2 of the Code of the County of Arlington).

79. *Delta Air Lines*, 242 Va. at 213, 409 S.E.2d at 133. Compare VA. CODE ANN. § 58.1-3819 (Cum. Supp. 1992) with Arlington County Code § 40-1(e).

80. *Delta Air Lines*, 242 Va. at 210-11, 409 S.E.2d at 131.

81. *Id.* at 214, 409 S.E.2d at 133.

Delta and the hotels argued that the County's ordinance was invalid because it levied the tax on "each and every transient," rather than on "hotels, motels, boarding houses and travel campgrounds" as allowed under the enabling statute.⁸² The Supreme Court of Virginia affirmed the trial court's holding that the ordinance was valid, finding that specific references in section 58.1-3819⁸³ to taxes levied on "hotels" and to language enabling localities to allow businesses a commission for collection of such taxes "imposed on the consumer" authorized the county to enact a transient occupancy tax ordinance holding either the consumer, the hotel, or both, liable for the payment of the tax.⁸⁴ However, the supreme court reversed the trial court's entry of summary judgment in favor of the County, holding that the trial court erred in determining that a corporation was not a person for purposes of defining transient. The case was remanded to resolve factual matters surrounding the application of the thirty-day exemption to Delta.⁸⁵

Justices Hassell and Whiting dissented on the basis that the County's ordinance was invalid, believing that the enabling statute does not give the County the authority to levy a tax on each and every transient. Their separate opinion states that ordinances levying taxes upon citizens are construed most strongly against the government and provisions in ordinances are not to be extended beyond the clear import of the language used.⁸⁶

2. Business License Taxes

In *Monument Associates v. Arlington County Board*,⁸⁷ the County of Arlington assessed additional business license taxes against the taxpayer contending that the taxpayer should have used the accrual method of accounting, rather than the cash method, for reporting gross receipts for purposes of the business license taxes.⁸⁸

At issue in this case was a county ordinance providing that:

82. *Id.* at 212, 409 S.E.2d at 132.

83. VA. CODE ANN. § 58.1-3819 (Repl. Vol. 1991).

84. 242 Va. at 212-13, 409 S.E.2d at 132.

85. *Id.* at 214, 409 S.E.2d at 133.

86. *Id.* at 217-18, 409 S.E.2d at 134-35 (Hassell and Whiting, JJ., dissenting).

87. 242 Va. 145, 408 S.E.2d 889 (1991).

88. *Id.* at 147, 408 S.E.2d at 890.

The calculation of gross receipts for license tax purposes shall be on either a cash or actual basis, provided, however, that the basis used must coincide with the system of accounts used by the taxpayer and the method employed by the taxpayer for federal and state income tax purposes.⁸⁹

The taxpayer used the accrual method for federal and state income tax purposes, but used the cash method for reporting gross receipts for county business license taxes.⁹⁰

A rebuttable presumption exists in favor of the validity of a tax assessment and the taxpayer must establish that the assessments were invalid or illegal to be entitled to relief.⁹¹ The trial court ruled that the taxpayer failed to carry its burden and denied the relief sought. The Supreme Court of Virginia affirmed the trial court's decision.⁹²

The taxpayer argued that the obvious intent of the ordinance was to require taxpayers to report actual, cash receipts during the applicable tax period and contended that the proper role of the proviso was not to create requirements beyond the language, but instead to limit the language that precedes it.⁹³ The Supreme Court of Virginia disagreed, holding that the proviso was the controlling clause and clearly required that the method used to calculate gross receipts for business license purposes must coincide with the system and method used to report federal and state income taxes.⁹⁴

In making its ruling, the court cited several rules of statutory construction. First, an enactment should be interpreted, if possible, in a manner which gives meaning to every word. However, if words found in an enactment appear to have been inserted by inadvertence or mistake, are incapable of any sensible meaning, or are repugnant to the remainder of the enactment and tend to nullify it, the words will be treated as surplusage.⁹⁵ The court determined that the legislative intent of the ordinance was clearly

89. *Id.* at 147, 408 S.E.2d at 890 (quoting § 11-1(f) of the Code of Arlington County).

90. *Monument Assocs.*, 242 Va. at 147, 408 S.E.2d at 890.

91. *Id.* at 148, 408 S.E.2d at 891.

92. *Id.* at 151, 408 S.E.2d at 892.

93. *Id.* at 148-49, 408 S.E.2d at 891.

94. *Id.* at 149, 408 S.E.2d at 891.

95. *Id.* at 149-50, 408 S.E.2d at 891-92 (citations omitted).

stated in the proviso and rejected the use of the words "cash or actual" in the ordinance as surplusage.⁹⁶

An exemption from business, professional, and occupation license (BPOL) tax was the issue in *Board of Supervisors of Fairfax County v. Group Health Ass'n, Inc.*⁹⁷ The Fairfax County Code grants an exemption from BPOL tax which encompasses non-profit organizations operating a facility for the welfare of the residents of the area.⁹⁸ Tax exemption provisions must be strictly construed against the taxpayer and it is the burden of the taxpayer to prove that it qualifies for the exemption.⁹⁹ Although the trial court ruled that the taxpayer qualified for the exemption, the Supreme Court of Virginia held that the taxpayer failed to meet its burden and entered final judgment in favor of the County.¹⁰⁰

3. Utility Taxes on Cable Television Service

In *Cox Cable Hampton Roads, Inc. v. City of Norfolk*,¹⁰¹ the Supreme Court of Virginia struck down a local cable television company's First Amendment challenge of a Norfolk ordinance enacted to permit the city to impose a utility tax on cable television service.¹⁰² The court, citing similar types of cases, held that the Norfolk City Charter conferred the general power of taxation, which includes a power to impose the tax on cable television service.¹⁰³ In answering the First Amendment challenge, the court held that the tax at issue did not violate the cable company's First Amendment rights because the tax applies to all cable companies that might operate in the city, does not target a small group of First Amendment speakers, and is not content based.¹⁰⁴ The taxpayer contended the justification for the tax required a compelling government interest because it applies only to one company.¹⁰⁵ But the court responded that such a view would eliminate the ability of local governments to raise operating revenues through general tax-

96. *Id.* at 150, 408 S.E.2d at 892.

97. 243 Va. 296, 414 S.E.2d 602 (1992).

98. FAIRFAX COUNTY CODE § 4-7-1(a)(3).

99. *Group Health*, 243 Va. at 298-99, 414 S.E.2d at 603 (citing *Commonwealth v. Manzer*, 207 Va. 996, 1000, 154 S.E.2d 185, 189 (1967)).

100. *Group Health*, 243 Va. at 229, 414 S.E.2d at 604.

101. 242 Va. 394, 410 S.E.2d 652 (1991).

102. *Id.* at 396, 410 S.E.2d at 652.

103. *Id.* at 398, 410 S.E.2d at 654.

104. *Id.* at 401, 410 S.E.2d at 655.

105. *Id.* at 400-01, 410 S.E.2d at 655.

ation ordinances whenever there happened to be a single or only a few enterprises engaging in First Amendment activities.¹⁰⁶

The cable company also alleged that the tax infringed on its Equal Protection rights because the tax imposed by the ordinance applied to the cable company and their subscribers, but not to satellite operators and their users.¹⁰⁷ The City of Norfolk filed a demurrer, which the trial court granted, on the basis that satellites are a form of cable television service and the ordinance imposes a tax on both.¹⁰⁸ The Supreme Court of Virginia reversed the judgment of the trial court and remanded the Equal Protection claim for a trial on the merits.¹⁰⁹

106. *Id.* at 400-01, 410 S.E.2d at 655.

107. *Id.* at 401-02, 410 S.E.2d at 656.

108. *Id.* at 402, 410 S.E.2d at 656.

109. *Id.* at 402-403, 410 S.E.2d at 656.