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Taxation

Craig D. Bell
McGuireWoods, LLP, Richmond, Virginia

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TAXATION

Craig D. Bell *

I. INTRODUCTION

This article reviews significant recent developments in the law affecting Virginia taxation. Each section covers legislative changes, judicial decisions, and selected opinions or pronouncements from the Virginia Department of Taxation and the Attorney General of Virginia over the past year. Part One of this article discusses legal developments regarding taxes imposed and administered by the State. Section II addresses changes made to Virginia corporate and individual income tax law, and Section III covers legal changes pertaining to retail sales and use taxes. Part Two of this article documents legal developments of local government taxes. Sections IV and V address changes to the law regarding Virginia real and personal property taxes, respectively. Section VI discusses a judicial decision regarding Virginia's business professional occupation license tax.

The overall purpose of this article is to provide Virginia tax and general practitioners with a concise overview of the recent developments in Virginia taxation that will most likely impact their practices. This article does not, however, discuss many of the numerous technical legislative changes to title 58.1 of the Virginia Code, which covers taxation.


Mr. Bell practices primarily in the areas of state and local taxation, and civil and criminal tax litigation. He is a Fellow of the American College of Tax Counsel, a member of the J. Edgar Murdock Inn of Court (U.S. Tax Court), an adjunct professor of tax law at the College of William and Mary School of Law, and a past chair of both the Tax and Military Law Sections of the Virginia State Bar, as well as the Tax Section of the Virginia Bar Association.
II. INCOME TAX

A. Recent Significant Legislative Activity

1. Fixed Date of Conformity

The 2008 General Assembly amended Virginia Code section 58.1-301, which mandates conformity of terms to the Internal Revenue Code, to advance Virginia's fixed date of conformity from December 31, 2006 to December 31, 2007.1 Virginia continues, however, to disallow the federal bonus depreciation deduction and the five-year net operating loss carry-back period for state income tax purposes.2 The new date of conformity enables the state to adopt provisions from three federal tax acts. The first set of provisions is from the Small Business and Work Opportunity Tax Act of 2007, which increases and extends United States Code section 179 expensing and several other tax breaks for small businesses.3 The second set is from the act to assist Virginia Tech victims, which excludes income received from Virginia Tech out of amounts transferred from the Hokie Spirit Memorial Fund if those amounts are paid on account of the tragic events on April 16, 2007.4 Finally, the new conforming date enables the state to adopt provisions of the Mortgage Forgiveness Debt Relief Act of 2007, which provides an exemption so certain homeowners do not have to pay taxes for debt forgiveness on their troubled home loans.5 This latter federal tax law also extends a provision allow-
ing homeowners to deduct mortgage insurance payments from their taxable income and provides other forms of tax relief.6

2. Subtractions from Income for Space Launch Services and Payload Delivery

The 2008 General Assembly enacted two subtractions from Virginia personal and corporate income tax laws to allow gains from the sale of launch services and gains resulting from the delivery of payload to be subtracted from taxable income.7 The first subtraction is available for gains from the sale of actual launch services to space flight participants or launch services used for training.8 The launch services must be performed in Virginia or originate from a Virginia airport or spaceport to qualify.9

The second subtraction may be used for gains recognized "as a result of resupply services contracts for delivering payload . . . entered into with the Commercial Orbital Transportation Services division of the National Aeronautics and Space Administration or other space flight entity."10 To exclude gains from resupply services contracts, the launches must take place at an airport or spaceport located in Virginia.11

Both subtractions apply to tax years beginning on or after January 1, 2009.12

3. Biodiesel Fuel Credit

The 2008 General Assembly enacted Virginia Code section 58.1-439.12:02 to create a nonrefundable income tax credit against personal and corporate income tax for producers of biodiesel and green diesel fuel.13 The credit is in an amount equal to

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6. Id. sec. 3, 26 U.S.C. § 163 note C.
9. Id.
11. Id.
$0.01 per gallon of biodiesel or green diesel fuel produced. The credit is available for taxable years beginning on or after January 1, 2008. The amount of the credit may not exceed $5000 annually. Taxpayers may earn the credit during the first three years of production of biodiesel or green diesel fuels. Unused, but otherwise available, credits may be transferred to another producer for use on a Virginia income tax return. Such a credit transfer must be reported to the Virginia Department of Taxation. Any credit not used during the taxable year may be carried over to the next three taxable years.

The new statute defines biodiesel fuel to mean "a fuel composed of mono-alkyl esters of long-chain fatty acids derived from vegetable oils or animal fats, designated B100, and meeting the requirements of ASTM D6751." Green diesel fuel is defined as "a fuel produced from nonfossil renewable resources including agricultural or silvicultural plants, animal fats, residue and waste generated from the production, processing, and marketing of agricultural products, silvicultural products, and other renewable resources, and meeting applicable ASTM specifications."

4. Riparian Forest Buffer Protection for Waterways Tax Credit

Virginia Code section 58.1-339.10 allows a tax credit to certain taxpayers who own land abutting a waterway and who forbear harvesting timber on certain portions of that land. The credit is equal to twenty-five percent of the value of the timber on the portion of the land retained as a buffer, but it may not exceed the lesser of $17,500 or the total amount of tax due for the taxable year.

15. Id.
16. Id.
17. Id.
18. Id.
19. Id.
22. Id.
In 2007, the Virginia Tax Commissioner ruled that trusts, including grantor trusts, did not qualify for this credit because the language in the statute specified that the credit was only available to individuals and corporations. The Commissioner ruled that a trust was neither an individual nor a corporation and, thus, not entitled to the credit. The 2008 General Assembly amended the statute to allow an individual's grantor trust to claim the Riparian Forest Buffer Protection for Waterways tax credit for taxable years beginning January 1, 2008.

5. Automatic Tax Return Filing Extensions for Deployed Service Members

The 2008 General Assembly adopted several automatic filing extensions for certain state and local tax returns for members of the armed forces who are deployed outside the United States. The General Assembly amended Virginia Code section 58.1-341(A) to provide an automatic extension to file an income tax return to every member of the armed services of the United States deployed outside of the United States. The extension expires ninety days following the completion of the service member's deployment. The amended statute defines the armed services of the United States to include "active duty service with the regular Armed Forces of the United States or the National Guard or other reserve component."

At the local level, the new legislation calls for the automatic extension of the filing dates on (1) real property taxes imposed on a primary residence and (2) personal property taxes imposed on a qualifying vehicle; a qualifying vehicle is defined by Virginia Code section 58.1-3523 and owned by members of the armed services of

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26. Id.
31. Id.
the United States deployed outside of the United States.\textsuperscript{32} The same definition of the armed services of the United States as set out for the state income tax filing extension applies to these local tax filing extensions.\textsuperscript{33}

6. Administration of the Land Preservation Tax Credit

The 2008 General Assembly adopted a number of changes to simplify the administration of the land preservation tax credit. First, the legislature amended Virginia Code section 58.1-3 to include as a confidential tax document any document required to be filed with the Virginia Department of Conservation and Recreation under the land preservation tax credit program.\textsuperscript{34} Currently, any donor who has made an easement that will generate a land preservation tax credit of one million dollars or more must file certain forms and documents with the Virginia Department of Conservation and Recreation and the Virginia Department of Taxation to qualify for the tax credits.\textsuperscript{35}

The General Assembly also enacted legislation to permit the disclosure of information regarding transferred land preservation tax credits and related assessments to the transferor and transferee of those credits.\textsuperscript{36} As the legislation relates to the transfer of the land preservation tax credits, the transferor is deemed to consent to disclosing any confidential tax information relevant to eligibility and value of the credit or other tax attribute transferred to the transferee.\textsuperscript{37} The transferee is also deemed to consent to the disclosure by the Virginia Department of Taxation to the transferor of the "amount of the transferred credit or other tax attribute used or absorbed on the transferee’s tax return when such disclosure is necessary in the administration of" the land preservation tax credit program.\textsuperscript{38}

\textsuperscript{32} Id. § 58.1-3916 (Cum. Supp. 2008).
\textsuperscript{33} Id.
\textsuperscript{38} Id. § 58.1-3.3(2) (Cum. Supp. 2008).
The legislation also included Virginia Code section 58.1-394.3, to provide for a simplified audit and assessment of the land preservation tax credit where the credit is attributable to any pass-through entity item. The statute of limitations for assessing a tax due to an adjustment to the land preservation tax credit attributable to a pass-through entity item with respect to an owner of the pass-through entity is “three years after the later of (i) the last day for filing the pass-through entity return for the taxable year of the pass-through entity, as extended, or (ii) the date on which the pass-through entity return for such taxable year was filed.” The new statute also permits the owner who signed the pass-through entity return, or any other owner or person authorized to sign the pass-through entity return, to enter into an agreement with the Virginia Department of Taxation to extend the period for assessing any tax.

Under the new law, the Virginia Tax Commissioner must mail to each owner of the pass-through entity notice of the beginning of an audit or administrative proceeding at the pass-through entity level regarding a pass-through entity item, and notice of the final administrative adjustment resulting from any such proceeding. The Commissioner need not mail notices to any owner with less than a one percent interest in the profits of the pass-through entity if the entity has more than one hundred owners.

The new statute also allows the department to consolidate administrative appeals or protests of an assessment filed with the Commissioner pursuant to Virginia Code section 58.1-1821 in which taxation of the same pass-through entity items is at issue. In any such proceeding regarding a pass-through entity item, the pass-through entity may participate in the proceeding. The new consolidation provisions apply to “any tax attributable to items of income, gain, loss, deduction, credit, or other tax attribute that is recognized or reportable by the pass-through entity” and that the owner of the pass-through entity must report

41. Id. § 58.1-394.3(B) (Cum. Supp. 2008).
42. Id. § 58.1-394.3(C) (Cum. Supp. 2008).
43. Id.
44. Id. § 58.1-394.3(D) (Cum. Supp. 2008).
45. Id.
pursuant to Virginia Code section 58.1-391 or similar Code provisions.\footnote{Id. § 58.1-394.3(E) (Cum. Supp. 2008).}

The legislation amended the statute authorizing applications to the Commissioner pursuant to section 58.1-1821. Specifically, any person aggrieved by department action regarding a transferred credit or other tax attribute may apply for relief under section 58.1-1821 or "request to join an application already filed by another person assessed with tax or similarly aggrieved . . . with respect to the same credit or tax attribute."\footnote{Id. § 58.1-1821 (Cum. Supp. 2008).} The Commissioner has the discretion to permit joinder or consolidate proceedings in these administrative appeals where the adjustments to credits or other tax attributes arise from the same transaction or occurrence, "provided that no interests are prejudiced and the joinder or consolidation advances administrative economy."\footnote{Id.}

B. Recent Judicial Decision: No Virginia Tax When Nonresident Lacks Minimum Contacts

The Circuit Court for the City of Richmond held that income passed through to a nonresident taxpayer from an out-of-state limited liability company operating in Virginia is not subject to the individual income tax if the taxpayer does not have the requisite minimum contacts with Virginia.\footnote{DiBelardino v. Commonwealth, No. CL06-5696, slip op. at 4 (Va. Cir. Ct. June 22, 2007) (Richmond City) (unpublished decision).}

Daniel Dutton and the DiBelardinos were nonresident members of a Delaware LLC (the "LLC") qualified to do business in Virginia.\footnote{Id., slip op. at 2.} The ownership of the LLC was divided into "investor" units and "management" units.\footnote{Id.} Only an owner of a management unit could control the management of the LLC.\footnote{Id.} Dutton and the DiBelardinos owned investor units.\footnote{Id.} Dutton had no other contact with Virginia.\footnote{Id.} The DiBelardinos' connections to Vir-
Virginia were the LLC investor unit and ownership of two bed and breakfast facilities in Norfolk.55

In 2002, the LLC received settlement proceeds for pending litigation over the development and sale of a fire escape ladder.56 The DiBelardinos did not report the settlement proceeds on their 2002 Virginia nonresident income tax return.57 Dutton did not file a return with Virginia in 2002.58 Neither Dutton nor the DiBelardinos believed that the proceeds were subject to tax in Virginia.59 Both taxpayers were assessed with individual income tax on their respective receipts of the proceeds.60 They appealed their assessments to the Virginia Tax Commissioner, who upheld the assessments.61 The taxpayers filed suit, arguing that the income was investment income, not income from property or business in Virginia.62

The Virginia Department of Taxation argued that because federal income tax law treats the taxpayers as partners for income tax purposes, Virginia treats them as partners for state income tax purposes.63 The settlement proceeds were distributed to all partners based on their membership interests.64 Moreover, because the LLC owned property and conducted business in Virginia, the department argued that the income was Virginia source income.65

Income passed through a partnership to partners retains its character.66 Despite the lack of clarity in the record, the circuit court held that the proceeds were Virginia source income.67

Even though the settlement proceeds were Virginia source income, the court stated that before a state can reach an individual for tax purposes, the individual must have minimum contacts

55. Id.
56. Id.
57. Id.
58. Id.
59. Id.
60. Id.
61. Id.
62. Id.
63. Id., slip op. at 3.
64. Id.
65. Id.
66. Id.
67. Id.
with the state. The court noted that the record contained little to demonstrate the connections between the taxpayers and Virginia. The department's argument was that Virginia could apply the tax based on the LLC's authority to do business in Virginia. The court, however, looked at the connections the DiBelardinos and Mr. Dutton had with Virginia. The court found that the DiBelardinos had minimum contacts with Virginia through their bed and breakfast property interests located in Norfolk. However, nothing in the record indicated that Mr. Dutton had any contact with Virginia other than his ownership of an investor unit in the LLC. Thus, the court upheld the assessment with respect to the DiBelardinos, but found the assessment on Mr. Dutton to be improper for lack of minimum contacts.

The circuit court correctly examined the steps necessary to tax nonresident individuals. Before Virginia can tax a nonresident's income, it must have jurisdiction (i.e., minimum contacts) over the nonresident. It is apparent from the court's opinion that the department's sole argument for jurisdiction was that the nonresident received Virginia source income. There was no dispute that the pass-through entity income was Virginia source income (assuming the proceeds from the patent dispute involving the LLC's development of a fire escape ladder constituted trade or business income). The mere receipt of Virginia source income, however, does not create a sufficient contact with Virginia to establish the requisite jurisdiction to tax the nonresident. The court recognized this lack of jurisdiction and, based on the record, held that Virginia did not have sufficient minimum contacts with Mr. Dutton. However, because the DiBelardinos managed other business interests in Virginia, they had sufficient contacts with Virginia and were subject to taxation.

68. Id., slip op. at 4.
69. Id.
70. Id.
71. Id.
72. Id.
73. Id.
74. See id., slip op. at 3.
75. See id., slip op. at 2-4.
76. See id., slip op. at 4.
77. Id.
78. Id.
C. Ruling of the Virginia Tax Commissioner: First Intangible Holding Company Add-Back Ruling

The Virginia Tax Commissioner issued her first ruling addressing the add-back requirement for intangible expenses paid to an entity affiliated with the taxpayer. The add-back requirement, effective for taxable years 2004 and thereafter, forces a taxpayer to report intangible expenses paid to an affiliated entity and to add back the intangible royalty expenses (the "royalties") that do not qualify for one of the "safe harbor" provisions.

At issue in this ruling was the proper application of the "subject to tax" safe harbor. The "subject to tax" safe harbor states that the add back shall not be required for any portion of the intangible expenses and costs if one of the following applies:

1. The corresponding item of income received by the related member is subject to a tax based on or measured by net income or capital imposed by Virginia, another state, or a foreign government that has entered into a comprehensive tax treaty with the United States government.

The taxpayer in this ruling did not add back certain intangible expenses subject to tax in another state. The Virginia Department of Taxation's auditor adjusted the taxpayer's return by adding back 97.547% of the royalties. The auditor determined that only 2.453% of the royalties were subject to tax in another state after they were apportioned to that state. The taxpayer appealed and argued that all of the royalties qualified for the "subject to tax" safe harbor and that the auditor's adjustment violated the Due Process and Commerce Clauses of the Constitution of the


82. TAX RULING, supra note 79.

83. Id.

84. Id.
United States because it taxed the royalty recipient, an entity that did not have a substantial nexus with Virginia.85

The Commissioner denied the taxpayer's appeal.86 The Commissioner relied upon the limiting words "portion" and "corresponding item" used in the add-back statute.87 With regard to the use of these words, the Commissioner noted:

[T]he "subject to tax" test must be satisfied for each item of the Parent's income that corresponds to each portion of the Taxpayer's royalty payments for which an exception is claimed. Thus, the exception is not automatically allowed for all of the royalty payments if one of the conditions is satisfied, but is allowed only with respect to the portion of royalty payments for which a condition is satisfied. One portion of the Taxpayer's royalty payments may be excluded from the add-back to the extent it satisfies one of the conditions; while another portion may be excluded to the extent it satisfies another condition. The remainder is added back.88

The Commissioner determined that the fact that the gross amount of royalties appears on the affiliate's return in another state does not permit the taxpayer to exclude the entire amount of royalties from the add-back requirement.89 The safe harbor is limited to that portion of the taxpayer's royalties paid to the affiliate that corresponds to the portion of the affiliate's income subject to tax in other states, as evidenced by the apportionment percentages shown in the affiliate's tax returns in other states.90

The Commissioner held that the add-back statute does not violate either the Due Process Clause or the Commerce Clause of the Constitution.91 Although the Due Process Clause was not addressed in the ruling, the Commissioner noted that deductions are a matter of legislative grace and the Commerce Clause does not require states to allow taxpayers to deduct items at will.92 Furthermore, the Commissioner noted that the corporate income

85. *Id.*
86. *Id.*
87. *Id.*
88. *Id.*
89. *Id.*
90. *Id.*
91. *Id.*
92. *Id.*
tax with the add-back statute is fairly apportioned and does not discriminate against interstate commerce.\textsuperscript{93}

The real issues in this case were interpreting the add-back statute and deriving the General Assembly's intentions when it adopted the "subject to tax" safe harbor. More succinctly, did the word "portion" refer to a portion of a single expense or to a single expense as a whole in relation to all of the corporation's intangible expenses? While the Commissioner decided that the former interpretation is correct, the latter interpretation might have a more practical meaning.\textsuperscript{94} Corporations that own intangible property usually license more than one piece of intangible property to their affiliates. This fact gives credence to the interpretation that a "portion" refers to an expense as a whole in relation to all of the corporation's intangible expenses.

With this ruling, the Commissioner has made her position on the meaning of the "subject to tax" safe harbor clear. It is highly unlikely that the exact meaning of this safe harbor will be addressed by the General Assembly in the future. Therefore, litigation will be necessary to obtain a different application of this provision. For that to happen, however, a corporation must decide that it makes economic sense to bear the expense of challenging this interpretation in court as opposed to abandoning this tax planning technique and using other methods to reduce its Virginia corporate income tax liability.

\section*{III. RETAIL SALES AND USE TAX}

\textbf{A. Recent Significant Legislative Activity}

1. Exemption for Certain Data Center Computer Equipment

The 2008 General Assembly adopted a new exemption from Virginia sales and use tax when it enacted Virginia Code section 58.1-609.3(17).\textsuperscript{95} The statute is narrowly drafted and applies only

\begin{flushleft}
\textsuperscript{93} Id.  \\
\textsuperscript{94} See id.  \\
\end{flushleft}
to certain computer equipment purchased or leased for use by data centers located in a Virginia locality that has an unemployment rate above 4.9% for the calendar quarter ending in November 2007. The exemption is further restricted to apply only to equipment used for the processing, storage, retrieval, or communication of data, including but not limited to servers, routers, connections, and other enabling hardware when part of a new investment of at least $75 million in such exempt property, when such investment results in the creation of at least 100 new jobs paying at least twice the prevailing average wage in that locality.

The exemption also applies to computer equipment purchased or leased to “upgrade, add to, or replace computer equipment purchased or leased in the initial investment.” The exemption does not apply to computer software sold separately from the equipment or to general building improvements or fixtures.

Prior to this new exemption, only computer equipment used directly in manufacturing or by Internet service providers would qualify for an exemption from Virginia’s sales and use tax.

2. Exemption for Textbook Sales

Under current law, a sales tax exemption is available for purchasing school textbooks from a local school board or its authorized agency, and for textbooks used by students attending nonprofit colleges and other nonprofit institutions of learning. Effective July 1, 2010, this exemption will broaden to apply to textbook sales made by for-profit institutions.

3. Sunset Date for Several Media-Related Exemptions

The 2008 General Assembly extended the sunset date for two media-related sales and use tax exemptions. The legislature extended the sunset date for the audiovisual works sales and use

97. Id.
98. Id.
99. Id.
100. Id. § 58.1-609.3(2), -609.6(2) (Cum. Supp. 2007).
tax exemption from July 1, 2009 to July 1, 2019.103 This exemption applies to the lease, rental, license, sale, other transfer, or use of any audio or video tape, film, or other audiovisual work when acquired for licensing, distributing, broadcasting, commercially exhibiting, or reproducing the work, or using or incorporating the work in another work.104 The exemption also applies to the provision of production services or fabrication related to the production of any portion of a qualifying audiovisual work.105

The legislature also extended the sunset date for the sales and use tax exemption for printing materials purchased by advertising businesses that ship the materials out of Virginia.106 The exemption was set to expire on July 1, 2008, but will now expire on July 1, 2012.107

B. Recent Judicial Decision: Gifts Delivered to Other States Exempt from Sales Tax

Virginia’s Circuit Court for the City of Richmond held that the sales tax does not apply to sales of tangible personal property at a Virginia retail store if the retailer immediately ships the property to a location outside of Virginia.108 The taxpayer, Bloomingdale’s, Inc., applied for the correction of an assessment of sales tax on sales made at its McLean, Virginia store.109 The Virginia Department of Taxation assessed sales tax on numerous transactions which can be summarized in five examples set forth below.110

1. The merchandise was purchased with cash at the McLean store and shipped from a warehouse outside of Virginia to a loca-
tion in the District of Columbia.111 The risk of loss remained with Bloomingdale’s until delivery in the District of Columbia.112 Bloomingdale’s collected and remitted sales tax to the District of Columbia.113

2. The merchandise was purchased by credit card from the McLean store by a person who was not present at the store but had a Virginia telephone number.114 The merchandise was shipped from Virginia to New York, and the risk of loss remained with Bloomingdale’s until delivery in New York.115 Bloomingdale’s collected and remitted sales tax to New York.116

3. The merchandise was purchased by credit card from the McLean store by a person who was not present at the store but had a Virginia telephone number.117 The merchandise was shipped from Virginia to North Carolina, and the risk of loss remained with Bloomingdale’s until delivery in North Carolina.118 Bloomingdale’s did not collect or remit sales tax because it is not registered to collect sales tax in North Carolina.119

4. The merchandise was purchased by credit card from the McLean store by a person who was not present at the store but had a Virginia telephone number.120 The merchandise was shipped from Virginia to Florida, and the risk of loss remained with Bloomingdale’s until delivery in Florida.121 Bloomingdale’s collected and remitted sales tax to Florida.122

5. The merchandise was purchased by credit card from the McLean store by a person who was present at the store.123 The merchandise was shipped from Virginia to Massachusetts and the

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111. Id. at 1.
112. Id.
113. Id.
114. Id. at 2.
115. Id.
116. Id.
117. Id.
118. Id.
119. Id.
120. Id.
121. Id.
122. Id.
123. Id.
risk of loss remained with Bloomingdale's until delivery in Massachusetts. The department assessed sales tax on these transactions based on Title 23 of the Virginia Administrative Code section 10-210-680. This section requires sales tax to be collected and remitted when a person buys a gift in Virginia and directs the seller to deliver the gift to another person. Furthermore, title 23 of the Virginia Administrative Code section 10-210-780 interprets the interstate commerce exemption. This regulation applies the exemption only in cases where the tangible personal property is delivered outside of Virginia to the purchaser of the property.

The circuit court examined the statute that imposes the sales tax, Virginia Code section 58.1-603, to determine whether the tax applied to these transactions. Section 58.1-603 imposes the sales tax “upon every person who engages in the business of selling at retail or distributing tangible personal property in this Commonwealth . . . [on] the gross sales price of each item or article of tangible personal property when sold at retail or distributed in this Commonwealth.” To be a “sale” under Virginia Code section 58.1-602, there must be a transfer of title or possession.

To support its position that the transactions were subject to Virginia sales tax, the department argued that the parties to each sale were the property purchaser and Bloomingdale's, not the person who actually received the property and Bloomingdale's. The department asserted that when the customer paid for the items at the time of the sale and instructed Bloomingdale's to ship the item by common carrier to another party, the sale was

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124. Id.
125. Id.
129. Id.
130. Bloomingdale's, slip op. at 2–3.
133. Bloomingdale's, slip op. at 2.
complete and the customer had constructive possession of the item at that time. According to the department, a taxable event—the sale—occurred. The circuit court disagreed.

In each of the five example transactions, the circuit court ruled that there was no transfer of title or possession of the merchandise in Virginia. The court observed that under Virginia Code section 8.2-401(2), title to the merchandise does not pass until delivery is complete. In addition, the court noted that Bloomingdale's retained the risk of loss on the merchandise during delivery. As title to the merchandise did not pass in Virginia, and in one example the merchandise was never present in Virginia, the court held that sales tax did not apply to the disputed transactions. The court also ruled that sections 10-210-680 and 10-210-730 of Title 23 of the Virginia Administrative Code are not in conformity with the Code of Virginia.

The department's position that the purchaser in each of the five transactions had constructive possession of the merchandise is very questionable. The fragile nature of this position is best illustrated with the facts in the first example, where the tangible personal property sold was never present in Virginia. For Virginia to tax the sale of tangible personal property that is never present in Virginia is violative of the Commerce Clause of the United States Constitution.

134. Id., slip op. at 2–3.
135. Id., slip op. at 3.
136. Id.
137. Id.
138. Id. (citing VA. CODE ANN. § 8.2-401(2) (Cum. Supp. 2008)).
139. Id.
140. Id., slip op. at 2–3.
141. Id., slip op. at 3.
PART TWO: TAXES ADMINISTERED BY LOCALITIES

IV. REAL PROPERTY TAX

A. Recent Significant Legislative Activity


The 2008 General Assembly amended Virginia Code section 58.1-3221.2 to add other performance guidelines and standards that energy-efficient buildings could meet or exceed to be classified as a separate class of real property.142 Prior to the amendment, only buildings that exceeded the energy-efficiency standards prescribed in the Virginia Uniform Statewide Building Code by at least thirty percent were deemed energy-efficient buildings, and where the certification of energy efficiency was performed by an engineer or contractor bearing no relation to the taxpayer.143

The new legislation expands the criteria an energy-efficient building may meet to obtain this property classification. Effective July 1, 2008, any building that meets or exceeds performance standards of the Green Globes Building Rating System of the Green Building Initiative, Leadership in Energy and Environmental Design (LEED) Green Building Rating System, EarthCraft House program, or Energy Star System will also qualify as an energy-efficient building.144 Certification of energy efficiency will be issued under any of the four programs or upon determination by an engineer designated by the locality that the building meets or exceeds the performance guidelines or standards under any of the programs.145

144. Id. § 58.1-3221.2(C) (Cum. Supp. 2008).
145. Id.
2. New Appraisal Certification Program for Local Government Appraisers

The 2008 General Assembly adopted legislation that requires the Virginia Department of Taxation to establish a certification program for all supervisors, assessors, and appraisers contracted by any county or city to perform Virginia real property tax assessments or reassessments. Prior to adoption of this legislation, the department needed to certify at least one full-time real estate appraiser or assessor in each city and county. Under the new law, the department must establish certification requirements that include minimum education, training, and experience; and standards of conduct and practice. The new law also requires the certification to occur before any supervisor, assessor, or appraiser may be contracted by a city or county to perform an assessment or reassessment. The amendments also empower the department to “suspend, revoke, or deny renewal of an existing certificate, or refuse to issue a certificate” and to require remedial education.

B. Recent Judicial Decision: Designation for Property Tax Exemption Revoked for New Property

The Circuit Court of Botetourt County held that Virginia Baptist Homes, Inc. (“VBH”), a nonprofit religious organization that had a property tax exemption pursuant to Virginia Code section 58.1-3650.33(A), was not entitled to the benefits of this exemption for the “Glebe,” a continuing care facility that required its residents to pay one hundred percent of the cost of their care.

In 1976, the Virginia legislature designated VBH as a benevolent entity. VBH operated continuing care retirement facilities

152. Id., slip op. at 4.
in Culpeper and Newport News. At the time VBH received its property tax exemption, the stated purpose of VBH was: "To solicit sufficient funds, establish and maintain an institution where aged, indigent and infirm men and women may be provided with a comfortable home gratuitously or upon such other conditions as may be prescribed by the management from time to time."154

VBH’s Culpeper and Newport News facilities both subsidized the cost of their residents’ care. Some years later, VBH amended its articles of incorporation to remove all references to maintaining an institution that provides a comfortable home to the aged, indigent, and infirm. In 1998, VBH acquired the Glebe, and VBH conceded at trial that it was not entitled to a property tax exemption for this property until the Glebe began operations.157

The designation property tax exemption VBH received in 1976 is defined by Virginia Code sections 58.1-3650 and 58.1-3650.33. In relevant part, the exemption states as follows:

The real and personal property of an organization designated (emphasis added) within this article and used by such organization exclusively for religious, charitable, patriotic, historical, benevolent or public park and playground purpose... shall be exempt from taxation so long as such organization is operated not for profit and the property so exempt is used in accordance with the purpose for which the organization is classified.159

Section 58.1-3650.33 designates VBH as such an organization and states that VBH is classified and designated as a religious and benevolent organization. The circuit court noted that subsection B of section 58.1-3650.33 provides that “[p]roperty owned by [VBH] and used by it exclusively for religious or benevolent purposes on a nonprofit basis, as set for in subsection A of this
section, is hereby determined to be exempt from taxation, state and local, including inheritance tax."\textsuperscript{161}

The court concluded that the statutory language of these two subsections required VBH to establish that the Glebe property met certain requirements.\textsuperscript{162} These requirements were that the Glebe be used on a nonprofit basis and exclusively for religious or benevolent purposes.\textsuperscript{163}

The court noted that the evidence at trial showed the Glebe was open to all potential residents regardless of their religious beliefs or lack thereof.\textsuperscript{164} Similarly, the Glebe did not require its staff to practice or adhere to any specific religion or belief.\textsuperscript{165} Although there was a chapel located on the grounds of the Glebe, it was not used for specific religious services, but rather for independent meditation, prayer, and occasionally by visiting clergy of various religious backgrounds for services.\textsuperscript{166} Therefore, the court held that although VBH certainly operated the Glebe with much good will, a tenuous connection existed between religion and the care provided at the Glebe, and VBH's operations were not exclusively for a religious purpose.\textsuperscript{167}

The court also took issue with the fact that residents at the Glebe had to pay one hundred percent of their costs, suggesting a lack of benevolence.\textsuperscript{168} VBH argued that it would eventually provide care to the financially needy residing at the Glebe, but that it had not done so as of the time the lawsuit was initiated.\textsuperscript{169} The court noted that residents at VBH's other continuing care facilities were subsidized.\textsuperscript{170} Thus, the court concluded that these facts prevented it from finding that VBH operated the Glebe immediately and directly to promote the religious and benevolent pur-

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\item \textsuperscript{161} Botetourt County, slip op. at 2.
\item \textsuperscript{162} Id.
\item \textsuperscript{163} Id., slip op. at 2–3.
\item \textsuperscript{164} Id., slip op. at 3.
\item \textsuperscript{165} Id.
\item \textsuperscript{166} Id.
\item \textsuperscript{167} Id.
\item \textsuperscript{168} Id., slip op. at 4.
\item \textsuperscript{169} Id.
\item \textsuperscript{170} Id.
\end{itemize}
poses for which VBH was created and for which it received its property tax exemption.\footnote{Id.}

When VBH argued that it would provide financial assistance to its residents at the Glebe in the future, the court responded that the Glebe potentially would not be in a position to do so given that the facility had millions of dollars in debt and had only recently established a small benevolence fund from contributions made by supporters.\footnote{Id.} The circuit court held that VBH and its operations of the Glebe in Botetourt County did not satisfy the requirements necessary to be exempt from property taxes pursuant to Virginia Code sections 58.1-3650 and 58.1-3650.33.\footnote{Id., slip op. at 5. The Supreme Court of Virginia granted VBH's petition for appeal on February 28, 2008. Supreme Court of Virginia Record No. 072042, \textit{available at} http://www.courts.state.va.us/scv/appeals/072042.html (last visited Oct. 10, 2008). All briefs have been filed for the appeal and oral argument was held during the September court session. \textit{See} Supreme Court of Virginia, September Argument Docket, http://www.courts.state.va.us/docket.htm (last visited Oct. 10, 2008).}

\section*{V. Tangible Personal Property Tax}

\subsection*{A. Recent Significant Legislative Activity: Sunset Date for Certain Satellite Equipment}

section 15.2-4607 before June 30, 2019, then this classification statute will expire on the same date the special improvements tax expires.177

B. Recent Judicial Decision: Standard of Review for State Tax Commissioner Decisions on Appeals of Local Tax Determinations

1. Factual and Procedural Background

The Circuit Court for Chesterfield County held in Chesterfield County v. Palace Laundry, Inc., that a business that provides linens to customers did not qualify for the exemption from the local business tangible personal property tax available to a laundry or processing business.178

Linens of the Week ("LOW") provides linens to customers in a laundered and finished condition.179 LOW owns all of the linens.180 LOW was assessed with unpaid business tangible personal property tax by Chesterfield County.181 LOW argued that it was a laundry business under Virginia Code section 58.1-1101(A) or 58.1-3507 and exempt from the business tangible personal property tax.182 In the alternative, LOW argued that it was an exempt processing business under Virginia Code section 58.1-3507.183 LOW appealed the assessment to the Virginia Tax Commissioner, who found that LOW was not a laundry business, but was a processing business.184 In the ruling, the Commissioner determined that linen supply companies are industrial processors for purposes of the sales and use tax and that there was no

181. Agreed Stipulation of Facts ¶ 32.
182. Palace Laundry, slip op. at 2.
183. Id.
184. Id.
reason to classify such companies differently for purposes of the tangible personal property tax.\textsuperscript{185}

Chesterfield County filed suit, seeking to overturn the Commissioner's ruling with respect to the position that LOW was a processing business.\textsuperscript{186} LOW counterclaimed, seeking to overturn the Commissioner's ruling with respect to the position that LOW was not a laundry business.\textsuperscript{187} The circuit court found that LOW was neither a laundry business nor a processing business and reinstated Chesterfield County's assessment for unpaid business tangible personal property tax.\textsuperscript{188}

2. Appropriate Standard of Review

Prior to examining the substantive issues in this case, the circuit court addressed the appropriate standard of review applicable to decisions of the Virginia Tax Commissioner (the "State Commissioner") and the Chesterfield County Tax Commissioner (the "County Commissioner").\textsuperscript{189} The court concluded that LOW had the burden of showing that the State Commissioner erroneously determined that LOW was not a laundry business.\textsuperscript{190} Further, the court concluded that the county bore the burden of showing that the State Commissioner erroneously determined that LOW was a processing business.\textsuperscript{191}

The circuit court also addressed the deference that it should give to the State Commissioner's ruling and to the county's decision.\textsuperscript{192} The court noted that the State Commissioner must presume the assessment of the County Commissioner to be "prima facie correct," and that there is a presumption of validity attached to the decision of the State Commissioner.\textsuperscript{193} The court did not

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\item[185.] VA. DEP'T OF TAXATION, PUB. DOC. 05-142 (Aug. 26, 2005), available at http://www.policylibrary.tax.virginia.gov/OTP/policy.nsf (follow "Rulings of the Tax Commissioner" hyperlink; then follow "2005" hyperlink; then follow "PD 05-142" hyperlink).
\item[186.] Palace Laundry, slip op. at 2.
\item[187.] Id.
\item[188.] Id., slip op. at 1.
\item[189.] Id., slip op. at 2–3.
\item[190.] Id., slip op. at 2.
\item[191.] Id.
\item[192.] Id., slip op. at 2–3.
\item[193.] Id. (quoting VA. CODE ANN. § 58.1-3983.1 (B)(4) (Cum. Supp. 2008)).
\end{itemize}
acknowledge, however, that the State Commissioner had determined that the conclusion of the County Commissioner was in error.

3. Definitions of a Laundry Business and a Processing Business

When the circuit court looked to the substance of this case, it first examined whether LOW was a laundry business. The court noted that the Virginia Code does not define a laundry business and stated that when a term is not defined in the Code, the term is given its plain meaning. The court also noted that the State Commissioner looked to the North American Industrial Classification System ("NAICS") for a definition of a laundry business in her ruling on the County Commissioner's decision. In its opinion, the court concluded that the NAICS specifically excluded linen services as a laundry business and defined linen services separately. The court found this definition persuasive. In addition, the court noted that LOW is not required to launder its linens by agreement with its customers. Rather, it is only required to provide clean linens to its customers. LOW also does not launder linens owned by others. For these reasons, the court concluded that LOW is a "linen supply business," not a laundry business.

Next, the circuit court examined whether LOW was a processing business. A processing business is not defined for business tangible personal property tax purposes, but it is defined for sales and use tax purposes. The Supreme Court of Virginia has defined processing as taking a raw material and treating it,
"rendering [a] product more marketable or useful." The circuit court held that when LOW buys new linens, the linens are not rendered more useful or marketable than when they were originally acquired. For this reason, the court found that LOW is not a processing business. This holding is also curious as soiled linens are clearly not useful or marketable.

LOW filed a petition for appeal with the Supreme Court of Virginia, which the court subsequently granted. On September 12, 2008, the court affirmed the judgment of the circuit court and stated, "Cleaning and maintaining its rental property does not transform a rental business into a processing business." The court held that LOW is a linen supply business and that cleaning and maintaining the linens is ancillary to the service that the company provides.

VI. BUSINESS PROFESSIONAL OCCUPATION LICENSE TAX

The Circuit Court for the City of Lynchburg held that the city could not include in its measure of taxable gross receipts a taxpayer's gross receipts generated, but not taxed, by other Virginia localities. English Construction Company, Inc. and W. C. English, Inc. (collectively referred to as "English") are contractors that have their principal place of business in Lynchburg. English also maintains definite places of business in other localities. In *English Construction Co. v. City of Lynchburg*, the city maintained that it could assess gross receipts under Virginia Code section 58.1-3715(A) that were not taxed by the other locali-

205. *Id.*, slip op. at 5 (citing Commonwealth v. Orange-Madison Cooper. Farm Serv., 220 Va. 655, 658, 261 S.E.2d 532, 534 (1980)).
206. *Id.*
207. *Id.*
209. *Id.* at *7.*
210. *Id.*
212. *Id.*, slip op. at 2.
213. *Id.*, slip op. at 1.
ties because English had its principal place of business in Lynch-
burg. Accordingly, the city assessed English with its Business,
Professional, and Occupation License ("BPOL") tax on all of the
gross receipts English received from projects in other localities
that were not subject to a BPOL tax in those localities. English
initiated its lawsuit challenging the city's assessment on its
BPOL receipts received, but not taxed, in these other localities.
English maintained that the city had no authority to tax such re-
ceipts.

The circuit court, after noting that English had the burden to
show that the city's assessments were invalid, held that English
met its burden. The court stated that the city had no express
statutory authority to support the challenged assessments.
The court principally relied on Virginia Code sections 58.1-
3703.1(A)(3) and 58.1-3715 to reach its decision. Section 58.1-
3703.1(A)(3)(a) provides:

The gross receipts for a contractor shall be attributed to the definite
place of business at which his services are performed, or if his servic-
es are not performed at any definite place of business, then the defi-
gnite place of business from which his services are directed or con-
trolled, unless the contractor is subject to the provisions of § 58.1-
3715.

Section 58.1-3715 provides that although a contractor is obli-
gated to procure a license in the jurisdiction where its principal
offices are located, it may also be required to obtain a license in
another jurisdiction if its business in that jurisdiction exceeds
$25,000. In that situation, the other

county, city or town may require of such contractor a local license,
and the amount of business done in such other county, city or town
in which a license tax is paid may be deducted by the contractor from

214. Id., slip op. at 1–2.
215. Id.
216. Id., slip op. at 1.
217. Id., slip op. at 2.
218. Id.
219. Id.
220. See id.
the gross revenue reported to the county, city or town in which the principal office or any branch office of the contractor is located.\textsuperscript{223}

Therefore, the circuit court held that there is no express authority for the city to tax the gross receipts that English earned in other localities, and that the city's assessments for such taxes were invalid and abated.\textsuperscript{224}

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\textsuperscript{223} Id.
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\textsuperscript{224} English Constr. Co., slip op. at 2.
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