§ 58.1-609.3. Commercial and industrial exemptions.

The tax imposed by this chapter or pursuant to the authority granted in §§ 58.1-605 and 58.1-606 shall not apply to the following:

1. Personal property purchased by a contractor which is used solely in another state or in a foreign country, which could be purchased by such contractor for such use free from sales tax in such other state or foreign country, and which is stored temporarily in Virginia pending shipment to such state or country.

2. (i) Industrial materials for future processing, manufacturing, refining, or conversion into articles of tangible personal property for resale where such industrial materials either enter into the production of or become a component part of the finished product; (ii) industrial materials that are coated upon or impregnated into the product at any stage of its being processed, manufactured, refined, or converted for resale; (iii) machinery or tools or repair parts therefor or replacements thereof, fuel, power, energy, or supplies, used directly in processing, manufacturing, refining, mining or converting products for sale or resale; (iv) materials, containers, labels, sacks, cans, boxes, drums or bags for future use for packaging tangible personal property for shipment or sale; or (v) equipment, printing or supplies used directly to produce a publication described in subdivision 3 of § 58.1-609.6 whether it is ultimately sold at retail or for resale or distribution at no cost. Machinery, tools and equipment, or repair parts therefor or replacements thereof, shall be exempt if the preponderance of their use is directly in processing, manufacturing, refining, mining or converting products for sale or resale. The provisions of this subsection do not apply to the drilling or extraction of oil, gas, natural gas and coalbed methane gas. In addition, the exemption provided herein shall not be applicable to any machinery, tools, and equipment, or any other tangible personal property used by a public service corporation in the generation of electric power, except for raw materials that are inputs to production of electricity, including fuel.

3. Tangible personal property sold or leased to a public service corporation engaged in business as a common carrier of property or passengers by railway, for use or consumption by such common carrier directly in the rendition of its public service.

4. Ships or vessels, or repairs and alterations thereof, used or to be used exclusively or principally in interstate or foreign commerce; fuel and supplies for use or consumption aboard ships or vessels plying the high seas, either in intercoastal trade between ports in the Commonwealth and ports in other states of the United States or its territories or possessions, or in foreign commerce between ports in the Commonwealth and ports in foreign countries, when delivered directly to such ships or vessels; or tangible personal property used directly in the building, conversion or repair of the ships or vessels covered by this subdivision. This exemption shall include dredges, their supporting equipment, attendant vessels, and fuel and supplies for use or consumption aboard such vessels, provided the dredges are used exclusively or principally in interstate or foreign commerce.

5. Tangible personal property purchased for use or consumption directly and exclusively in basic research or research and development in the experimental or laboratory sense.

6. Tangible personal property sold or leased to an airline operating in intrastate, interstate or foreign commerce as a common carrier providing scheduled air service on a

continuing basis to one or more Virginia airports at least one day per week, for use or consumption by such airline directly in the rendition of its common carrier service.
7. Meals furnished by restaurants or food service operators to employees as a part of wages.
8. Tangible personal property including machinery and tools, repair parts or replacements thereof, and supplies and materials used directly in maintaining and preparing textile products for rental or leasing by an industrial processor engaged in the commercial leasing or renting of laundered textile products.
9. (i) Certified pollution control equipment and facilities as defined in § 58.1-3660, except for any equipment that has not been certified to the Department of Taxation by a state certifying authority pursuant to such section and (ii) effective retroactive to July 1, 1994, and ending July 1, 2006, certified pollution control equipment and facilities as defined in § 58.1-3660 and which, in accordance with such section, have been certified by the Department of Mines, Minerals and Energy for coal, oil and gas production, including gas, natural gas, and coalbed methane gas.
10. Parts, tires, meters and dispatch radios sold or leased to taxicab operators for use or consumption directly in the rendition of their services.
11. High speed electrostatic duplicators or any other duplicators which have a printing capacity of 4,000 impressions or more per hour purchased or leased by persons engaged primarily in the printing or photocopying of products for sale or resale.
12. From July 1, 1994, and ending July 1, 2011, raw materials, fuel, power, energy, supplies, machinery or tools or repair parts therefor or replacements thereof, used directly in the drilling, extraction, or processing of natural gas or oil and the reclamation of the well area. For the purposes of this section, the term "natural gas" shall mean "gas," "natural gas," and "coalbed methane gas" as defined in § 45.1-361.1. For the purposes of this section, "drilling," "extraction," and "processing" shall include production, inspection, testing, dewatering, dehydration, or distillation of raw natural gas into a usable condition consistent with commercial practices, and the gathering and transportation of raw natural gas to a facility wherein the gas is converted into such a usable condition. Machinery, tools and equipment, or repair parts therefor or replacements thereof, shall be exempt if the preponderance of their use is directly in the drilling, extraction, refining, or processing of natural gas or oil for sale or resale, or in well area reclamation activities required by state or federal law.
13. Beginning July 1, 1997, and ending July 1, 2011, (i) the sale, lease, use, storage, consumption, or distribution of an orbital or suborbital space facility, space propulsion system, space vehicle, satellite, or space station of any kind possessing space flight capability, including the components thereof, irrespective of whether such facility, system, vehicle, satellite, or station is returned to this Commonwealth for subsequent use, storage or consumption in any manner when used to conduct spaceport activities; (ii) the sale, lease, use, storage, consumption or distribution of tangible personal property placed on or used aboard any orbital or suborbital space facility, space propulsion system, space vehicle, satellite or space station of any kind, irrespective of whether such tangible personal property is returned to this Commonwealth for subsequent use, storage or consumption in any manner when used to conduct spaceport activities; (iii) fuels of such quality not adapted for use in ordinary vehicles, being produced for, sold and exclusively used for space flight when used to conduct spaceport activities; (iv) the sale, lease, use,

storage, consumption or distribution of machinery and equipment purchased, sold, leased, rented or used exclusively for spaceport activities and the sale of goods and services provided to operate and maintain launch facilities, launch equipment, payload processing facilities and payload processing equipment used to conduct spaceport activities.

For purposes of this subdivision, "spaceport activities" means activities directed or sponsored at a facility owned, leased, or operated by or on behalf of the Virginia Commercial Space Flight Authority.

The exemptions provided by this subdivision shall not be denied by reason of a failure, postponement or cancellation of a launch of any orbital or suborbital space facility, space propulsion system, space vehicle, satellite or space station of any kind or the destruction of any launch vehicle or any components thereof.

14. Semiconductor cleanrooms or equipment, fuel, power, energy, supplies, or other tangible personal property used primarily in the integrated process of designing, developing, manufacturing, or testing a semiconductor product, a semiconductor manufacturing process or subprocess, or semiconductor equipment without regard to whether the property is actually contained in or used in a cleanroom environment, touches the product, is used before or after production, or is affixed to or incorporated into real estate.

15. Semiconductor wafers for use or consumption by a semiconductor manufacturer.

(1993, c. 310; 1994, cc. 365, 381; 1995, cc. 101, 204, 719; 1996, c. 816; 1997, c. 834; 2001, cc. 429, 468, 769; 2003, c. 859; 2004, Sp. Sess. I, c. 3; 2006, cc. 385, 519, 524, 541, 618.)

Editor's note. - Acts 2004, Sp. Sess. I, c. 3, cl. 3, provides: "That the Tax Commissioner shall develop and publish guidelines for purposes of implementing the amendments to the Commonwealth's retail sales and use taxes pursuant to the provisions of this act. Such guidelines shall include, but shall not be limited to, a bracket system for the collection of retail sales and use taxes in the Commonwealth on transactions of $5 or less. The development of such guidelines shall be exempt from the provisions of the Administrative Process Act (§ 2.2-4000 et seq.) of the Code of Virginia."

Acts 2004, Sp. Sess. I, c. 3, cl. 4, provides: "That the amendments to § 58.1-609.3 of the Code of Virginia pursuant to the provisions of this act shall not result in sales or use tax liability for any tangible personal property purchased or leased pursuant to a bona fide contract for the sale or lease of tangible personal property that was entered into on or before March 1, 2004, and provided that such tangible personal property was placed in service on or before August 1, 2004."

Acts 2004, Sp. Sess. I, c. 3, cl. 5, provides: "That notwithstanding any provision of law to the contrary, including § 56-582 of the Code of Virginia, any public utility that is, as a result of the provisions of this act, subject to a sales and use tax on tangible personal property purchased or leased for use or consumption by such utility in the rendition of its public service is hereby authorized to recover from each customer that customer's pro rata share of the public utility's actual expense therefor by means of a sales and use tax surcharge. The surcharge shall be subject to annual review and verification by the State Corporation Commission in the year subsequent to the surcharge, based on data provided in an annual information filing or other information provided to the State Corporation Commission by such utility; however, such review and verification shall neither constitute a rate case nor be the subject of a rate case. If the State Corporation Commission determines that the amount of the surcharge differed from the actual sales and use tax incurred as a result of the provisions of this act, a surcharge adjustment shall be applied in the following year. Any excess in the surcharge shall be refunded to ratepayers as a

deduction against the surcharge to be imposed in that subsequent year. Any shortfall in the surcharge shall be recovered through an increase in the surcharge to be imposed in that subsequent year. A surcharge that is allocated on a proportionate basis or according to the allocation factors in the utility's most recent State Corporation Commission-approved cost allocation study shall be presumed valid."
Acts 2004, Sp. Sess. I, c. 3, cl. 10, provides: "That the provisions of this act shall not become effective unless the Commonwealth's reimbursements to certain local governments for tangible personal property tax relief on qualifying vehicles, as such term is defined in § 58.1-3523 of the Code of Virginia, are set at $950 million per year for tax year 2006 and each succeeding tax year, payable over the 12-month period that corresponds with the Commonwealth's fiscal year, beginning July 2006, under legislation passed by the 2004 Special Session I of the General Assembly that becomes law."
Acts 2004, Sp. Sess. I, c. 1, set the reimbursement rate at $950 million for tax years beginning in 2006.
Acts 2006, c. 524, cl. 2, provides: "That the provisions of this act are declaratory of existing law."

The 2001 amendments. - The 2001 amendments by cc. 429 and 468 are identical, and substituted "Beginning July 1, 1997, and ending July 1, 2011" for "July 1, 1997, through June 30, 2001" at the beginning of subdivision 13.
The 2001 amendment by c. 769 substituted "ending July 1, 2006" for "through June 30, 2001" in clause (i) of paragraph 9; and substituted "and ending July 1, 2006" for "June 30, 2001" near the beginning of paragraph 12.

The 2003 amendments. - The 2003 amendment by c. 859 inserted "except for any equipment that has not been certified to the Department of Taxation by a state certifying authority pursuant to such section" in subdivision 9.

The 2004 amendments. - The 2004 amendment by Sp. Sess. I, c. 3, effective September 1, 2004, added the last sentence in subdivision 2; and in subdivision 3, deleted the clause (i) designation, the language "subject to a state franchise or license tax ... and tangible personal property sold or leased to a public service corporation" preceding "engaged in business" and "motor vehicle or" following "passengers by."

The 2006 amendments. - The 2006 amendments by cc. 385 and 618 are identical, and in the third sentence of subdivision 2, substituted "drilling or extraction of oil" for " drilling, extraction, refining, or processing of oil"; and in subdivision 12, substituted "2011" for "2006" and deleted "refining" following "extraction" in the first and third sentences.
The 2006 amendments by cc. 519 and 541 are identical, and added subdivision 14.
The 2006 amendment by c. 524 added present subdivision 15.

Law review. - For survey article on developments in the law affecting Virginia taxation, see 38 U. Rich. L. Rev. 267 (2003).
For 2006 survey article, "Taxation," see 41 U. Rich. L. Rev. 283 (2006).

Editor's note. - The cases annotated below were decided under prior law corresponding to repealed § 58.1-608.

CASE NOTES

Former paragraph 1 provides industrial exemption. The former first paragraph is intended to provide exemption for machinery and tools used in processing, manufacturing, refining, mining, or conversion of products for sale or resale only in the industrial sense. Golden Skillet Corp. v. Commonwealth, 214 Va. 276, 199 S.E.2d 511 (1973).

Methanometers and first-aid supplies furnished to employees of a coal company were protective materials and, therefore, were exempt from the sales tax. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

Processing and manufacturing are not synonymous. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

The definition of processing is considerably less stringent than the definition of manufacturing. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

While all manufacturing is a type of processing, not all processing constitutes manufacturing. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

Definitions of "processing" and "manufacturing" compared. - The definition of processing, unlike the definition of manufacturing, does not require transformation of a raw material into an article of substantially different character. It merely requires that the product undergo a treatment rendering the product more marketable or useful. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

Only industrial processing equipment exempt. - Not all processing qualifies for the exemption set forth in this section. The exemption applies only to machinery and tools used in processing only in the industrial sense. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

In determining whether a particular type of processing constitutes industrial processing within the meaning of this section, it is necessary to focus upon the nature of the processing itself, rather than the nature of the processor's sale of the products. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

A company may be both a retailer and an industrial processor. The retail nature of a taxpayer's operations is not dispositive of the question of whether the taxpayer may enjoy the benefit of the exemption for industrial processing. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980) (decided prior to 1979 amendment adding subdivision (37) (now subdivision 5) of § 58.1-609.2)

Sale at wholesale level not required for processing exemption. - This section provides an exemption for machinery used in processing articles "for sale or resale" and in no fashion indicates that the processed products must be sold at the wholesale level in order for the processor to be entitled to the exemption. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

Production of feed and fertilizer was industrial processing. - The mixing together of grains and additives in the production of feed and the mixing together of the chemicals in the production of fertilizer by a farm cooperative satisfied all the requisites of industrial processing. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980) (decided prior to 1979 amendment).

Thus, machinery, etc., used was exempt. - The machinery, fuel and equipment used in its feed and fertilizer operation by a farm cooperative were exempt under this section from sales and use taxes, since the operation constituted industrial processing within the meaning of this section. The fact that the cooperative sold the feed and fertilizer to farmers at retail did not disqualify the cooperative from the benefit of the exemption. Commonwealth, Dep't of Taxation v. Orange-Madison Coop. Farm Serv., 220 Va. 655, 261 S.E.2d 532 (1980).

Process of preparing and frying chicken for sale at retail is not industrial. - The process of preparing and frying chicken for sale at retail, notwithstanding the novelty of the patented method and cookers used by the franchisees, is not an industrial operation within intent of this section. Golden Skillet Corp. v. Commonwealth, 214 Va. 276, 199 S.E.2d 511 (1973).

Processing does not include the growth of laboratory animals for sale under a strictly prescribed protected environment. State Tax Comm'r v. Flow Research Animals, Inc., 221 Va. 817, 273 S.E.2d 811 (1981).

Meaning of "packaging." - Although "packaging" has not been defined in this section, it is reasonable to infer a legislative intent that the word, as used in the introductory paragraph of this section, means placing in a package or container. Webster Brick Co. v. Department of Taxation, 219 Va. 81, 245 S.E.2d 252 (1978).

"Packaging" and "packing" distinguished. - The packaging exemption at the end of the introductory paragraph of this section was not applicable to dunnage bags used to "pack" cubes of brick in railway cars rather than to "package" bricks in containers. Webster Brick Co. v. Department of Taxation, 219 Va. 81, 245 S.E.2d 252 (1978).

Tangible personal property used in mining industry, in order to be exempt from taxation, must meet three requirements. First, it must be a machine, tool, or other industrial device. Second, the item, whether it remains personalty or is ultimately incorporated into realty, must be used directly in processing, manufacturing, refining, mining or conversion. Third, the purpose of the specified activity must be to provide a product for sale or resale. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

The structure itself of a coal tipple, which contained, inter alia, a foundation, windows, floors, walls, work areas for employees and a roof, was not exempt from taxation as machinery used to process coal. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

Repair parts and supplies for trucks used to haul coal between mines and the tipple are exempt from taxation. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

Truck scales located at a coal tipple and used to weigh the coal transported from mines before it was unloaded and for the "blending of coal" which was necessary to meet customer specification for the marketable product, were used directly in processing within the meaning of § 58.1-602. Thus, the scales were exempt from sales taxation. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

Materials used to build and maintain haul roads from coal mines to public highways enroute to the coal tipple are used directly in the process of mining and are tax-exempt. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

Materials used in reclamation of strip-mined lands are taxable. When reclamation occurs, mining and processing have ended. The mere fact that materials are essential to an activity mandated by law does not in and of itself render the materials subject to exempt status. Commonwealth, Dep't of Taxation v. Wellmore Coal Corp., 228 Va. 149, 320 S.E.2d 509 (1984).

The legislature intended former subdivision 19 to be a restrictive provision exempting only that tangible personal property purchased or leased and used in scientific or traditional physical science research and development which generates new tangible products or new processes or the improvement of existing products or processes, not mere management studies, reports or surveys. Commonwealth v. Research Analysis Corp., 214 Va. 161, 198 S.E.2d 622 (1973).

Airline's baggage handling equipment. - Since transporting and handling passenger baggage is an integral part of an airline's common carrier service, the equipment necessary for loading or unloading and the handling of baggage is used directly by airline in the rendition of its common carrier service and is thus exempt from taxation under this section. Commonwealth v. United Airlines, 219 Va. 374, 248 S.E.2d 124 (1978).

Anti-hijacking equipment. - The fact that anti-hijacking surveillance equipment is required under federal law does not in and of itself render the equipment subject to exempt status under this section, but since anti-hijacking equipment is used directly by an airline in the rendition of its common carrier service, it is therefore exempt from taxation under the provisions of this section. Commonwealth v. United Airlines, 219 Va. 374, 248 S.E.2d 124 (1978).

Airline's reservations and ticketing equipment. - Reservations and ticketing equipment is used directly in the rendition of an airline's common carrier service and, therefore, is exempt from taxation under this section. Commonwealth v. United Airlines, 219 Va. 374, 248 S.E.2d 124 (1978).

Airport facilities used in preparation of food for aircraft. - Facilities at an airport used in the preparation of food served to passengers when the aircraft is airborne are not used directly by airline in the rendition of its common carrier service under the provisions of this section; hence, assessments on the facilities used for the preparation of food would not be erroneous. Commonwealth v. United Airlines, 219 Va. 374, 248 S.E.2d 124 (1978).

Food and related items used by airline. - Food and related items used by an airline which served meals to passengers only when the time of flight occurred around regular meal hours and which charged the same fare on flights whether or not food was served were not "used directly" in the rendition of its common carrier service so as to exempt an airline from payment of sales and use taxes on the food and related items. Commonwealth v. United Airlines, 219 Va. 374, 248 S.E.2d 124 (1978).
Department of Taxation regulations which provide that the furnishing of meals by an airline to passengers or others is not use or consumption of tangible personal property by the airline directly in the rendition of its common carrier service, and that the sales and use tax applies to meals delivered to carriers in this State to be furnished without a specific charge therefor to passengers, are not inconsistent with former subdivision 26. Commonwealth v. United Airlines, 219 Va. 374, 248 S.E.2d 124 (1978).

This chapter does not define the key word "directly" as used in this section. Commonwealth v. Community Motor Bus Co., 214 Va. 155, 198 S.E.2d 619 (1973).

Legislative intent in using phrase "directly in the rendition of its public service." - The legislature, in using the phrase "directly in the rendition of its public service" in former subdivision 10 (see now subdivision 3), intended to narrow the scope of the exemption and exempted only such essential tangible personal property used immediately and principally by a common carrier to keep its motor vehicles on the road in performance of its public service. Commonwealth v. Community Motor Bus Co., 214 Va. 155, 198 S.E.2d 619 (1973).