

Income/Franchise:

Virginia: Manufacturer Allowed to Exclude Unused Stored Raw Materials from Property Factor

Case No. 201263, Va. (2/10/22). The Virginia Supreme Court (Court) affirmed that an out-of-state-based tobacco manufacturer with an in-state storage warehouse may exclude the value of raw materials (i.e., leaf tobacco) that aged while being stored in Virginia from its property factor for Virginia corporation income tax apportionment purposes when those materials are ultimately processed and used in manufacturing outside of Virginia, because the materials are *not* being “used” during the in-state aging process under state law. In doing so, the Court deferred to the lower court’s finding of fact that the storage of the leaf tobacco in Virginia is not necessary for the aging process; the leaf tobacco will age regardless of where it is kept; and the manufacturer does “absolutely nothing” to the in-state stored leaf tobacco (that is, it “just sits there”). The Court also agreed that allowing raw materials to sit does not constitute “processing” because processing under state law requires that these materials undergo treatment that will result in a product that is more marketable or useful. Because the manufacturer does not introduce any treatment to the leaf tobacco, nor does it perform any affirmative act or activity to prompt or aid the aging process, the Court reasoned that it does not “use” the leaf tobacco under state law by storing it in its in-state warehouse. Accordingly, the Court agreed with the lower court that the Virginia Department of Taxation’s underlying corporation income tax assessments for the years at issue were erroneous and ordered it to refund the amount of the manufacturer’s overpayments on such assessments. Please contact us with any questions.

URL: <https://www.vacourts.gov/opinions/opnscvwp/1201263.pdf>

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