

Procurement Guidance - (10/2016)

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T3.4.2 - Taxes

A Taxes

1 General

a. This section provides general information on a range of taxation issues including:

- (1) Using tax clauses in contracts (including foreign contracts);
- (2) Asserting immunity or exemption from taxes; or
- (3) Obtaining tax refunds.

b. This section does not present the full scope of the tax laws and regulations. Therefore, contracting officers (CO) should work closely with legal counsel when tax questions arise.

c. COs must consult legal counsel before negotiating with any taxing authority for the purpose of:

- (1) Determining whether or not a tax is valid or applicable; or
- (2) Obtaining an exemption from, or refund of, a tax.

d. When the FAA's constitutional immunity from State or local taxation may be at issue, contractors should be discouraged from negotiating independently with taxing authorities if the contract involved is either:

- (1) A cost-reimbursement contract, or
- (2) A fixed-price contract containing a tax escalation clause.

e. The CO should consult legal counsel for the following before purchasing goods or services from a foreign source:

- (1) Information on foreign tax treaties and agreements in force and on the implementation of any foreign-tax-relief programs and
- (2) Resolution of other tax questions affecting the prospective contract.

2 Federal Excise Taxes

a. Federal excise taxes are levied on the sale or use of particular supplies or services. Subtitle D of the Internal Revenue Code of 1954, Miscellaneous Excise Taxes, 26 U.S.C. 4041, et seq., and its implementing regulations, 26 CFR 40 through 299, cover miscellaneous federal excise tax requirements. Questions arising in this area should be directed to legal counsel. The most

common excise taxes are--

(1) Manufacturers' excise taxes imposed on certain motor-vehicle articles, tires and inner tubes, gasoline, lubricating oils, coal, fishing equipment, firearms, shells, and cartridges sold by manufacturers, producers, or importers; and

(2) Special-fuels excise taxes imposed at the retail level on diesel fuel and special motor fuels.

b. Sometimes the law exempts the Federal Government from these taxes. COs should solicit prices on a tax-exclusive basis when the Government is exempt from these taxes, and on a tax-inclusive basis when no exemption exists.

c. COs should take maximum advantage of available Federal excise tax exemptions.

3 General Exemptions

a. No Federal manufacturers' or special-fuels excise taxes are imposed in many contracting situations as, for example, when the supplies are for any of the following:

(1) The exclusive use of any State or political subdivision, including the District of Columbia (26 U.S.C. 4041 and 4221);

(2) Shipment to a United States possession or Puerto Rico, or for export. Shipment or export must occur within 6 months of the time title passes to the Government. When the exemption is claimed, the words "for export or shipment to a possession" must appear on the contract or purchase document, and the contracting officer must furnish the seller proof of export (see 26 CFR 48.4221-3);

(3) Further manufacture, or resale for further manufacture (this exemption does not include tires and inner tubes) (26 CFR 48.4221-2);

(4) Use as fuel supplies, ships or sea stores, or legitimate equipment on vessels of war, including

(a) Aircraft owned by the United States and constituting a part of the armed forces; and

(b) Guided missiles and pilotless aircraft owned or chartered by the United States. When this exemption is to be claimed, the purchase should be made on a tax-exclusive basis. The CO shall furnish the seller an exemption certificate for Supplies for Vessels of War (an example is given in 26 CFR 48.4221-4(d)(2); the IRS will accept one certificate covering all orders under a single contract for a specified period of up to 12 calendar quarters) (26 U.S.C. 4041 and 4221);

(5) A nonprofit educational organization (26 U.S.C. 4041 and 4221); (6) Emergency vehicles (26 U.S.C. 4053 and 4064(b)(1)(c)).

b. Other Federal Tax Exemptions.

(1) Pursuant to 26 U.S.C. 4293, the Secretary of the Treasury has exempted the United States from the communications excise tax imposed in 26 U.S.C. 4251, when the supplies and services are for the exclusive use of the United States. (Secretarial Authorization, June 20, 1947, Internal Revenue Cumulative Bulletin, 1947-1, 205.)

(2) Pursuant to 26 U.S.C. 4483(b), the Secretary of the Treasury has exempted the United States from the federal highway vehicle users tax imposed in 26 U.S.C. 4481. The exemption applies whether the vehicle is owned or leased by the United States. (Secretarial Authorization, Internal Revenue Cumulative Bulletin, 1956-2, 1369.)

4 State and Local Taxes

a. *Definition.* "State and local taxes" means taxes levied by the States, the District of Columbia, Puerto Rico, possessions of the United States, or their political subdivisions.

b. Application of State and Local Taxes to the FAA.

(1) Generally, purchases and leases made by the Federal Government are immune from State and local taxation. Whether any specific purchase or lease is immune, however, is a legal question requiring advice and assistance of legal counsel.

(2) When it is economically feasible to do so, the FAA should take maximum advantage of all exemptions from State and local taxation that may be available. If appropriate, the CO should provide a Standard Form 1094, U.S. Tax Exemption Form, or other evidence to establish that the purchase is being made by the FAA.

c. Application of State and Local Taxes to FAA Contractors and Subcontractors.

(1) Prime contractors and subcontractors must not normally be designated as agents of the Government for the purpose of claiming immunity from State or local sales or use taxes. Before any such determination is made the CO shall consult with legal counsel.

(2) When a prime contractor or a subcontractor under a prime contract makes a purchase instead of the FAA, the right to an exemption of the transaction from a sales or use tax may not rest on the Government's immunity from direct taxation by States and localities. It may rest instead on provisions of the

particular State or local law involved, or, in some cases, the transaction may not in fact be expressly exempt from the tax.

(3) Frequently, property (including property acquired under the progress payments clause of fixed-price contracts or the Government property clause of cost-reimbursement contracts) owned by the Government is in the possession of a contractor or subcontractor. Situations may arise in which States or localities assert the right to tax Government property directly or to tax the contractor's or subcontractor's possession of, interest in, or use of that property. In such cases, the CO shall seek review and advice from legal counsel on the appropriate course of action.

d. Matters Requiring Special Consideration.

(1) The imposition of State and local taxes may result in special contract considerations including the following:

(a) With coordination of legal counsel, a contract may -

(i) State that the contract price includes or excludes a specified tax or

(ii) Require that the contractor take certain actions with regard to payment, nonpayment, refund, protest, or other treatment of a specified tax. Such special treatment may be appropriate when there is doubt as to the applicability or allocability of the tax, or when the applicability of the tax is being litigated.

(b) The applicability of State and local taxes to purchases by the FAA may depend on the place and terms of delivery. When the contract price will be substantial, alternative places and terms of delivery should be considered in light of possible tax consequences.

(c) Indefinite-delivery contracts for equipment rental may require the contractor to furnish equipment in any of the States. Since leased equipment remains the contractor's property, States and local governments impose a wide variety of property, use, or other taxes on equipment leased to the Government. The amount of these taxes can vary considerably from jurisdiction to jurisdiction.

(d) *The North Carolina State and Local Sales and Use Tax.*

(i) The North Carolina Sales and Use Tax Act authorizes counties and incorporated cities and towns to obtain each year from the Commissioner

of Revenue of the State of North Carolina a refund of sales and use taxes indirectly paid on building materials, supplies, fixtures, and equipment that become a part of or are annexed to any building or structure erected, altered, or repaired for such counties and incorporated cities and towns in North Carolina. In *United States v. Clayton*, 250 F. Supp.

827 (1965), it was held that the United States is entitled to the benefit of the refund, but must follow the refund procedure of the Act and the regulations to recover what it is due.

(ii) The Act provides that, to receive the refund, claimants must file, within 6 months after the claimant's fiscal year closes, a written request substantiated by such records, receipts, and information as the Commissioner of Revenue may require. No refund will be made on an application not filed within the time allowed and in such manner as the Commissioner may require. The requirements of the Commissioner are set forth in regulations that provide that, to substantiate a refund claim for sales or use taxes paid on purchases of building materials, supplies, fixtures, or equipment by a contractor, the Government must secure from the contractor certified statements setting forth the cost of the property purchased from each vendor and the amount of sales or use taxes paid. In the event the contractor makes several purchases from the same vendor, the certified statement must indicate the invoice numbers, the inclusive dates of the invoices, the total amount of the invoices, and the sales and use taxes paid. The statement must also include the cost of any tangible personal property withdrawn from the contractor's warehouse stock and the amount of sales or use tax paid by the contractor. Similar certified statements by subcontractors must be obtained by the general contractor and furnished to the claimant. Any local sales or use taxes included in the contractor's statement must be shown separately from the State sales or use taxes.

(iii) The clause prescribed at 3.4.2-9 requires contractors to submit to COs by November 30 of each year a statement disclosing North

Carolina State and local sales and use taxes paid during the 12-month period that ended the preceding September 30. The CO should ensure that contractors comply with this requirement and shall obtain the annual refund to which the Government may be entitled. The application for refund must be filed each year before March 31 and in the manner and form required by the Commissioner of Revenue. Copies of the form may be obtained from the State of North Carolina Department of Revenue, PO Box 25000, Raleigh, North Carolina 27640.

5 State and Local Tax Exemptions

a. Evidence needed to establish exemption from State or local taxes depends on the grounds for the exemption claimed, the parties to the transaction, and the requirements of the taxing jurisdiction. Such evidence may include the following:

- (1) A copy of the contract or relevant portion;
- (2) Copies of purchase orders, shipping documents, credit-card-imprinted sales slips, paid or acknowledged invoices, or similar documents that identify an agency or instrumentality of the United States as the buyer;
- (3) A U.S. Tax Exemption Form (SF 1094);
- (4) A State or local form indicating that the supplies or services are for the exclusive use of the United States;
- (5) Any other State or locally required document for establishing general or specific exemption;
- (6) Shipping documents indicating that shipments are in interstate or foreign commerce.

b. If a reasonable basis to sustain a claimed exemption exists, the seller will be furnished evidence of exemption, as follows:

- (1) Under a contract containing the clause at 3.4.2-8, Federal, State, and Local Taxes, Competitive Contracts, or at 3.4.2-7, Federal, State, and Local Taxes (Noncompetitive Contract), in accordance with the terms of those clauses;
- (2) Under a cost-reimbursement contract, if requested by the contractor and approved by the CO or at the discretion of the CO;

(3) Under a contract or purchase order that contains no tax provision,

if—

(i) Requested by the contractor and approved by the CO or at the discretion of the CO; and

(ii) Either the contract price does not include the tax or, if the transaction or property is tax exempt, the contractor consents to a reduction in the contract price.

B Clauses

[view contract clauses](#)

C Forms

[view procurement forms](#)