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DEPARTMENT OF STATE REVENUERevenue Ruling #2017-10ST  
May 14, 2018

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**ISSUES**

Sales and Use Tax - Applicability of Indiana Sales & Use Tax to Purchases Made by Contractor Exclusively Operating on Behalf of the Federal Government

Authority: IC § 6-2.5-1-14.7; IC § 6-2.5-1-14.9; IC § 6-2.5-1-27.7; IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-4-9; IC § 6-2.5-5-24; [45 IAC 2.2-3-14](#); [45 IAC 2.2-5-25](#); [45 IAC 2.2-5-49](#); Sales Tax Information Bulletin #4 (June 2016); Sales Tax Information Bulletin #60 (November 2017); 4 U.S.C. § 107; McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819); U. S. v. New Mexico, 455 U.S. 720, 733 (1982); U.S. v. Metro. Gov't of Nashville & Davidson County, 808 F.2d 1205, 1208 (6th Cir. 1987).

A company ("Company") is seeking a determination as to whether it is subject to the Indiana gross retail and use tax on the purchase, storage, use or consumption of tangible personal property to fulfill lump sum, cost reimbursement and time and material contracts on behalf of the federal government.

**STATEMENT OF FACTS**

Company is a Kentucky limited liability company. Company is a construction contractor that performs contracts exclusively for the United States federal government. Company provides the following information regarding its business:

The Company offers design-build and design-bid-build general contracting and construction management services to various agencies of the federal government. The Company does not purchase and improve property only to sell it in an arms' length transaction with the United States. Rather, work is undertaken at an existing government facility, often which is actively operating.

Because of the Company's eligibility to participate in special federal programs, the Company provides construction services exclusively to the United States federal government. Many of the Company's projects involve the Department of Veterans Affairs ("VA"). Program contracts include Multiple Award Task Order Contracts and Indefinite Delivery Indefinite Quantity contracts. Many of its projects are awarded following submission of Request for Proposal responses. While the Company provides services in states other than Indiana, approximately thirty percent (30%) of the Company's federal contracts in 2016 involve government properties located within Indiana. The remainder of the Company's federal contracts are in states surrounding Indiana.

The federal government maintains extensive control over the Company during the execution and fulfillment of the contracts. With respect to contracts with the VA, all work is performed under the direction of the Contracting Officer. Regular conferences are often required between the parties. At any time, however, the government's Contracting Officer can make changes in the work within the general scope of the contract. Furthermore, in some cases these adjustments can be made without any equitable adjustments benefiting the Company. The government must also order and approve contract changes, and may be involved in conflict resolution involving the Company. While the Company is encouraged to develop cost savings plans, any such plans must ultimately be approved by the government.

The Company is also subject to many reporting requirements. For example, payroll must be reported to the federal government on a weekly basis. The Company must also submit executive compensation information to the government. When the Company's contract is with the VA, daily reporting on the Company's activities is required.

The federal government also dictates employee relations and wages within the Company. All Company employees and employees of any subcontractors classified as tradesmen or craftsmen must be paid

predetermined amounts based upon tasks performed, rather than merely complying with federal minimum wage and overtime requirements. Special anti-discrimination flyers must also be displayed and made available for employees. Many wage requirements and other employee related provisions must be incorporated into the contracts of any subcontractors hired by the Company as well.

Certain activities of the Company are also limited or subject to government control. For example, the government places limits on what the Company may do with respect to existing vegetation, structures, equipment, utilities and improvements at a job site. The contract dictates when work must begin under the contract and when it must cease, both in terms of a commencement and completion date and a daily work schedule, which must be coordinated with federal facility management. The government must approve the work schedule and can require the Company to increase the number of shifts, overtime operations, days of work, and/or the amount of construction plant.

Under the standard agreement with the federal government, the government maintains the right to take possession of or use any completed or partially completed part of the work, including materials and supplies. The Company receives incremental payments throughout its work on the project based on the work completed on a monthly basis.

For purposes of these federal contracts, "work" specifically includes the ordering of job specific materials and supplies, which are often shipped directly to the federal facility. In addition, when supplies are provided under the contract, it is the government that inspects and accepts the supplies. In the case of VA contracts, the materials and supplies are inspected by VA resident engineers. Additionally, title to property acquired by the Company for use in fulfilling its federal contracts typically passes upon the vendor's delivery of the property. If the contract is cancelled before completion, the title to any work, complete or incomplete, passes to the government if title had not previously passed.

It is also contemplated that pursuant to FAR 52.229-3, which is incorporated by reference into the contracts, the federal government is responsible for all federal, state, and local taxes. Further, the contracts provide that the government will provide evidence to establish exemption from any federal, state or local tax imposed on the transactions or property covered by the contract. As a result, the Company has previously received, and expects to continue to receive, an executed Form ST-105 General Sales Tax Exemption Certificate with respect to federal construction projects in Indiana.

## DISCUSSION

The Supremacy Clause of the United States Constitution generally prevents states from imposing a tax on the United States government. It provides that "[t]his Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." Various United States Supreme Court decisions have expounded on this principle. See *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819); *U. S. v. New Mexico*, 455 U.S. 720, 733 (1982); *U.S. v. Metro. Gov't of Nashville & Davidson County*, 808 F.2d 1205, 1208 (6th Cir. 1987).

4 U.S.C. § 107 further states the following:

- (a) The provisions of sections 105 and 106 of this title shall not be deemed to authorize the levy or collection of any tax on or from the United States or any instrumentality thereof, or the levy or collection of any tax with respect to sale, purchase, storage, or use of tangible personal property sold by the United States or any instrumentality thereof to any authorized purchaser.
- (b) A person shall be deemed to be an authorized purchaser under this section only with respect to purchases which he is permitted to make from commissaries, ship's stores, or voluntary unincorporated organizations of personnel of any branch of the Armed Forces of the United States, under regulations promulgated by the departmental Secretary having jurisdiction over such branch.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires tangible personal property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). Additionally, the purchaser "shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state." *Id.*

Indiana also imposes a complimentary use tax on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). Under [45 IAC 2.2-3-14](#)(2), exemptions that apply to the sales tax also apply to use tax.

IC § 6-2.5-5-24 provides an exemption for sales to the United States government, in relevant part:

- (a) Transactions are exempt from the state gross retail tax to the extent that the gross retail income from those transactions is derived from gross receipts that are:
  - (1) derived from sales to the United States government, to the extent the state is prohibited by the Constitution of the United States from taxing that gross income . . .

The Department's regulations at [45 IAC 2.2-5-25](#) expands on the exemption, stating the following:

- (a) There is not a blanket exemption from the sales tax for purchases by governmental agencies and units. It provides that **only the purchase of tangible personal property used by the governmental agency in connection with a governmental function may be purchased exempt from sales tax.**
- (b) Purchases by a governmental agency or subdivision to be used in connection with or for a proprietary activity are subject to the sales tax.
- (c) Proprietary activities by governmental agencies and subdivisions include:
  - (1) Activities in connection with the sale of tangible personal property, such as college book stores, food services, concessions, etc.
  - (2) Activities in connection with the rental of tangible personal property made to the general public.
- (d) In every case in which a governmental agency engages in a proprietary type activity as defined above, the agency must pay sales tax on the purchase of all tangible personal property used in connection therewith.
- (e) The construction of buildings and structures for use in proprietary activities such as concession stands, is subject to sales tax on the tangible personal property incorporated therein.
- (f) Governmental agencies should refer to the gross income tax regulations and instructions for other examples of proprietary type activities.

**(Emphasis added).**

[45 IAC 2.2-5-49](#) further states the following:

- (a) The gross retail tax shall not apply to such part of the gross income from transactions constituting selling at retail as is exempt from the gross income tax under the provisions of [IC 6-2.1-3-2](#).
- (b) The state gross retail tax shall not apply to so much of the gross receipts of any transaction from sales to the United States Government, **but only to the extent to which the state of Indiana is prohibited from taxing such gross receipts by the Constitution of the United States.**

**(Emphasis added).**

The Department has interpreted 4 U.S.C. § 107 as follows in Sales Tax Information Bulletin #4 (June 2016):

Under federal law (4 U.S.C. 107), state and local governments may not levy or collect any type of sales or use tax on transactions in which the U.S. government sells personal property to others. Therefore, federal agencies are not required to register as retail merchants with the department and will not have a Retail Merchants Certificate number to use on an exemption certificate (Form ST-105 or SSTGB Form F0003).

Regarding the tax collection responsibilities of a contractor, IC § 6-2.5-4-9(b) provides that a contractor is a retail merchant making a retail transaction when the contractor disposes of tangible personal property or converts tangible personal property into real property under a time and material contract. However, the transaction is not a retail transaction, and thus not subject to tax, "if the ultimate purchaser or recipient of the property to be added to a structure or facility would be exempt from the state gross retail and use taxes if that purchaser or recipient had directly purchased the property from the supplier for addition to the structure or facility." IC § 6-2.5-4-9(c).

IC § 6-2.5-1-14.9 provides a definition of "contractor," stating that the term means "any person engaged in converting construction material into real property on behalf of another person. The term includes, but is not limited to, general or prime contractors, subcontractors, and specialty contractors." "Construction materials" are any tangible personal property to be converted into real property. IC § 6-2.5-1-14.7. A "time and material contract" is "a contract in which the cost of construction material and the cost of labor or other charges are stated

separately." IC § 6-2.5-1-27.7.

With respect to the use tax, this tax is imposed on a contractor's conversion of construction material into real property if that construction material was purchased by the contractor. However, the use tax does not apply to conversions of construction material if "the person for whom the construction material is being converted could have purchased the material exempt from the state gross retail and use taxes, as evidenced by a properly issued exemption certificate, if that person had directly purchased the construction material from a retail merchant in a retail transaction" or "the conversion of the construction material into real property is governed by a time and material contract as described in [IC 6-2.5-4-9\(b\)](#)." IC § 6-2.5-3-2(c).

Finally, Sales Tax Information Bulletin #60 (November 2017) provides the following guidance regarding the use of General Sales Tax Exemption Certificate (Form ST-105):

**1. Exemptions** - Notwithstanding the general rule, a contractor's purchase of construction material is not subject to tax - i.e., tax does not need to be paid by the contractor at the time of purchase - if the contractor's customer would be exempt from the sales and use taxes if the customer purchased the construction material directly from the supplier. A customer's ability to purchase construction material exempt from tax is evidenced by the customer's properly completed Form ST-105 General Sales Tax Exemption Certificate.

**a.** A contractor making exempt purchases as described above should do so only after obtaining and retaining a copy of the customer's properly completed Form ST-105 General Sales Tax Exemption Certificate.

**b.** To purchase construction material exempt from tax, the contractor purchasing the construction material must submit its own properly completed Form ST-105 General Sales Tax Exemption Certificate to the supplier at the time the material is purchased. A contractor's subsequent, non-exempt use or disposition of construction material that the contractor purchased or otherwise acquired exempt from tax will subject the contractor's use of that construction material to tax. See *SUBSECTION B - APPLICATION OF USE TAX*.

**Note:** When a contractor purchases or otherwise acquires construction material without paying sales tax, the contractor has the burden of proof with respect to establishing that its purchase or use of that construction material was exempt from tax and that the disposition of that construction material was not subject to the sales or use tax.

Regarding its evaluation of the relevant law cited herein (as well as other relevant court cases, statutes, and regulations to which you cited, but which are not included in this Revenue Ruling), Company states the following:

The Company performs construction services exclusively for the federal government and its agencies under written contracts. The federal government and its agencies are exempt from the gross retail and use taxes. The Company's contracts contemplate that the federal government will be the party ultimately responsible for any gross retail and use taxes imposed upon the Company as a result of its fulfillment of the contracts. As such, the Company has previously been provided and expects to continue to receive an executed Indiana General Sales Tax Exemption Certificate Form ST-105 with respect to federal projects in Indiana. Thus, assuming the Company is properly registered as a retail merchant in Indiana, the Company may issue its own Form ST-105 for its purchase of construction materials to be incorporated into real property under contracts with the federal government.

This interpretation is correct. The Company may issue its own ST-105 to its vendors to purchase construction materials exempt from Indiana sales tax in order to fulfill its contracted obligations to the federal government clients.

The Company's vendors may accept the Company's properly completed ST-105, which will relieve the vendors of responsibilities related to sales tax collection. As such, unless the Company's vendors have some other reason to reject the properly completed ST-105 provided by the Company, a properly completed ST-105 should be presumed to be correct and the vendor should not request proof that the Company is in fact working on behalf of a federal agency. In any subsequent audit where a vendor has accepted a properly completed ST-105, the Company, not the vendor, has the burden of proof with respect to establishing that its purchase or use of that construction material was exempt from tax and that the disposition of that construction material was not subject to the sales or use tax, and the liability will fall on Company for the payment of any tax.

## **RULING**

Company may issue its own ST-105 to its vendors to purchase construction materials exempt from Indiana sales tax in order to fulfill its contracted obligations to the federal government clients.

### CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances as stated herein are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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