MOTOR VEHICLES: Gas tax to be paid on gas sold to manufacturers under cost-plus contracts to U. S.
TAXATION: Government.

September 23, 1940

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Honorable Roy H. Cherry
State Inspector of Oils
Jefferson City, Missouri

Dear Sir:

This will acknowledge receipt of your letter of September 13, 1940, which is as follows:

"The Missouri Petroleum Industries Committee has requested an opinion from this department as to the taxability under state laws of sales of motor vehicle fuels to contractors for use in connection with the national defense work under cost-plus contracts with the federal government. I regard this question of such importance that I hesitate to issue a ruling without an opinion from the legal department of the state of Missouri.

"In their request to this department, the following questions were asked:

Question No. 1

Will the supplier of motor fuels to the purchasing contractor be justified in accepting, in lieu of your state gasoline tax, U. S. Form 1094 executed by the designated contracting officer of the U. S. Government named in each contract?

Note: The fuels are being sold to the contractor by the supplier for use by the contractor in the performance of work in accordance with the terms of the contract entered into by the contractor with the U. S. Government. It is understood the supplier will bill the contractor for the fuel and show on his bill for purposes of identification the 'government number' applied to each contract.

Question No. 2.

Since the contractor purchases the motor fuels for use in performance of the work specified in the contracts for which he bills the U. S. Government in accordance with the terms thereof, would not the transaction be tax exempt as a sale for the use of the United States, inasmuch as the fuel is actually used by the contractor in his performance of the terms of the contract?

"I am enclosing a copy of a ruling by the Bureau of Internal Revenue regarding the application of federal excise taxes to sales to contractors engaged in similar work."

In reaching a conclusion on these questions it is not necessary to set out the various acts of Congress authorizing the Navy and Army departments to purchase equipment and supplies on a cost-plus basis. It suffices to say that there are several acts designed to promote and provide for our national defense and all that we have consulted contain provisions for the letting of contracts on a cost-plus basis.

The nature of such a contract, as we understand it, is that the United States Government contracts with a private industry to manufacture needed materials agreeing to pay the

manufacturer thereof the actual cost of manufacture plus a fixed percentage of the actual cost as a profit. (Words & Phrases Perm. Ed. Vol. 9 p. 794).

Numerous manufacturers in Missouri who hold these contracts will, of course, use gasoline in completing their contracts and we are informed that in some instances the contracts require transportation of the manufactured products to a place of acceptance. This in some instances will be by motor vehicle. These items, if required, are considered as part of the cost to the manufacturer in completing his contract.

The question for determination appears to be: Are sales of gasoline to a manufacturer under contract to the United States on a cost-plus basis, sales for the exclusive use of the United States? (We assume the gasoline so purchased is used exclusively in completion of the government contracts.) If so, such sales are exempt from the two cents a gallon tax imposed on the sale of gasoline in this state.

The immunity of the United States Government from taxation by the state exists, in this case, not by reason of any act of Congress, but rather, due to the implied immunity resulting from the dual sovereignty of state and Nation. Allen v. Regents of University of Georgia 58 S. Ct. 980, 304 U. S. 439. We point this out because of the ruling of the United States Treasury Department attached to your opinion request. The Internal Revenue Code does not operate to create a tax exemption from state taxes. The act provides that "no tax under this chapter shall be imposed with respect to the sale of any article - (1) for use by the vendee as material in the manufacture or production of, or as a component part of, an article enumerated in this chapter; (2) for resale by the vendee for such use by his vendee, if such article is in due course so resold; (3) for the exclusive use of the United States, * * *." (26 USCA 3442). As will be noted this act only affects taxes imposed "under this chapter." (Chap. 29 Internal Revenue Code).

Thus, as above stated, the tax exemption of these manufacturers, if it exists at all, must arise from the "immunity implied from the dual sovereignty recognized by the Constitution," on the theory that sales of gasoline thus made are sales to the United States and cannot be taxed. In an opinion to you, dated March 8, 1939, we considered this im-

munity of the United States from the gasoline tax imposed under the laws of Missouri and concluded that such sales (those made to the United States for its exclusive use) were not subject to this tax and therefore we will not now re-examine that question. Neither is it necessary to do so because in our opinion the facts here do not bring these manufacturers into the immune class.

In the instant case the sales of gasoline are not made to the United States (or its instrumentality) for its exclusive use. The sales are made to a private manufacturer who is under contract to the United States Government to produce certain material. The only burden laid upon the United States is that the price it must pay for the manufactured product will be greater if the manufacturer must pay the tax on the gasoline he uses in compliance with his government contract.

In Helvering v. Gerhardt 58 S. Ct. 969, 304 U. S. 375, the whole question of implied immunity due to dual sovereignty was reexamined. The court in the course of that opinion said, l. c. S. Ct. 976:

> "The fact that the expenses of the state government might be lessened if all those who deal with it were tax exempt was not thought to be an adequate basis for tax immunity in Metcalf & Eddy v. Mitchell, * *."

In the footnote reference appended to this statement it is stated: "Upon full consideration, the same principle was recently applied in James v. Dravo Contracting Co., 302 U.S. 134, 58 S.Ct. 208, 82 L.Ed. 155, 114 A.L.R. 318, although the limitation there was upon the immunity of the federal government."

In the Dravo Contracting Company case the court was considering whether or not a gross receipt tax on the contracting company was valid as against the contention that a burden was imposed on the United States Government. The gross receipts of the company arose from a contract the company had with the government to build a levee. (It does not appear if it was under a cost-plus contract). The court held said tax not to be a burden on the government saying at l. c. S. Ct. 219, 220:

"The case differs toto coelo from that wherein the government enters into a contract with an individual or corporation to perform services necessary for carrying on the functions of government--as for carrying the mails, or troops, or supplies, or for building ships or works for government use. In those cases the government has no further concern with the contractor than in his contract and its execution. It has no concern with his property or his faculties independent of that. How much he may be taxed by, or what duties he may be obliged to perform towards, his State is of no consequence to the government, so long as his contract and its execution are not interfered with. In that case the contract is the means employed for carrying into execution the powers of the government, and the contract alone, and not the contractor, is exempt from taxation or other interference by the State government.

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"The contention ultimately rests upon the point that the tax increases the cost to the government of the service rendered by the taxpayer. But this is not necessarily so. The contractor, taking into consideration the state of the competitive market for the service, may be willing to bear the tax and absorb it in his estimated profit rather than lose the contract. In the present case, it is stipulated that respondent's estimated costs of the respective works, and the bids based thereon, did not include, and there was not included in the contract price paid to respondent, any specified item to cover the gross receipts tax, although respondent knew of the West Virginia act imposing it, and respondent's estimates of cost did include 'compensation and liability insurance, construction bond and property taxes.'

"But if it be assumed that the gross receipts tax may increase the cost to the government, that fact would not invalidate the tax. * * * * *"

The case of Trinity Farm Construction Co. v. Grosjean, 291 U.S. 466, 78 L. Ed. 919, seems to be in complete analogy with the instant case, except it does not appear whether there was a cost-plus contract involved. In that case the construction company had contracted to build a levee for the United States. In the construction of the levee gasoline was used and a tax was demanded of the company. The company sought to escape the tax on the theory it placed a burden on the United States. The court ruled against this contention saying at l. c. 921:

> "If the payment of state taxes imposed on the property and operation of appellant affects the federal government at all, it at most gives rise to a burden which is consequential and remote and not to one that is necessary, immediate or direct."

Thus we see that before such a contention will be sustained it must be made to appear that the burden upon the United States is substantial and direct. As pointed out it has been ruled that the mere fact the expenses of the government might be lessened if these manufacturers were tax exempt is not an adequate basis for applying the immunity due to dual sovereignty.

While none of the cases considered here make it clear what kind of contract the builders of these levees were working under, we do not think that the mere fact a cost-plus contract is involved can have any bearing on the law. This is just one of many methods that might have been used to determine what price the government would pay and what profit the manufacturer would receive. There could be nothing about such a contract that would warrant the construction that the manufacturer is an instrumentality of the government or that the government is the actual manufacturer of the material.

CONCLUSION

Therefore it is our opinion that sales of gasoline made to manufacturers who are producing materials for the United States government under cost-plus contracts are not exempt from the tax on said gasoline imposed by the laws of Missouri. We observe in this connection that the tax on all gasoline so sold, that is not used to propel motor vehicles on our highways, will be refunded anyway if proper claims are filed by the purchasers of said gasoline.

Respectfully submitted,

LAWRENCE L. BRADLEY
Assistant Attorney General

Approved:

COVELL R. HEWITT
(Acting) Attorney General

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