

SENATE JOINT RESOLUTION NO. 150

Directing the Commission to Study Virginia's State and Local Tax Structure for the 21st Century to study the impact of the Virginia sales and use tax, and more particularly the "true object" test, on federal government contractors.

Agreed to by the Senate, February 11, 2000
Agreed to by the House of Delegates, March 8, 2000

WHEREAS, the Commonwealth enacted its sales and use tax in 1966 and since that time has enacted very few changes to that tax except for a one-half cent increase; and

WHEREAS, a contractor doing business with the federal government is not entitled to claim the governmental exemption from the Virginia sales and use tax on his purchases of tangible personal property that are delivered to the federal government unless the contractor has been deemed a "purchasing agent" for the federal government or the purchases are made pursuant to an actual federal government purchase order issued by the contractor; and

WHEREAS, the federal government rarely designates its contractors as purchasing agents or permits its contractors to issue government purchase orders; and

WHEREAS, without the protection of the governmental exemption from the Virginia sales and use tax, federal government contractors are required to pay the tax on purchases of tangible personal property delivered to the federal government unless another exemption applies; and

WHEREAS, if its contract is deemed to be a "contract for the purchase and sale of tangible personal property" rather than a "contract for services" a contractor may purchase items deliverable to the federal government and such purchases will be exempt from the Virginia sales and use tax as "purchases made for resale"; and

WHEREAS, if, instead, the contract is deemed to be a "contract for services," the law treats all items purchased by the contractor pursuant to that contract as items for use by the contractor in performing its services, and the contractor is required to pay the Virginia sales and use tax on such items notwithstanding that the purchased items are delivered directly to the government and are not used by the contractor; and

WHEREAS, the "true object" test set forth in 23 VAC 10-210-4040 is used to determine whether a contract is a contract for the purchase and sale of tangible personal property or a contract for services; and

WHEREAS, under certain federal government contracts, the federal government has the discretion to order either tangible personal property or services or both during the term of the contract, and because the contract does not have a single purpose or "object" at its inception, the contractor is unable to apply the "true object" test to determine whether its contract is for services or for the purchase and sale of tangible personal property and whether its purchases are or are not subject to the Virginia sales and use tax until the contract actually has been performed; and

WHEREAS, the duration of such multipurpose contracts can be for up to five years, and the application of the "true object" test to such long-term multipurpose contracts unfairly burdens a contractor who reasonably believes that the contract is for the purchase and sale of tangibles and therefore treats its purchases as exempt from the Virginia sales and use tax, only to have the Department of Taxation, years later, review the contract in retrospect, deem the contract to be a contract for services and treat the contractor's purchases as taxable; and

WHEREAS, federal contract regulations require that any federal contract for the procurement of property rather than services must incorporate Federal Acquisition Regulation 52.222-20 (Part 52.222-20 of Title 48 of the Code of Federal Regulations) promulgated under the Walsh-Healey Act, 41 U.S.C. § 35 et seq., and that federal contracts for services must contain references incorporating federal acquisition regulations promulgated under the Service Contract Act of 1965, 41 U.S.C. §§ 351-358; and

WHEREAS, the inclusion of the Walsh-Healey Act federal acquisition regulations or the Service Contract Act federal acquisition regulations in a federal government contract provides a convenient test for classifying the contract as either a property procurement contract or a services contract; and

WHEREAS, the Commonwealth's current sales and use tax structure, the lack of flexibility in the "true object" test, and the difficulty experienced by federal government contractors in determining the taxability of purchases of tangible personal property under multipurpose contracts places unfair economic burdens on government contractors who face potential tax assessments on purchases years after the applicable contract was bid; and

WHEREAS, since the adoption of the sales and use tax in the Commonwealth, the federal government has greatly expanded its use of multipurpose contracts, and the negative economic impact of

the "true object" test on federal government contractors in Virginia has increased significantly; and

WHEREAS, these additional economic burdens on Virginia contractors places them at a competitive disadvantage relative to contractors from other states; and

WHEREAS, the current application of the Virginia sales and use tax to federal government contractors impedes economic development in the Commonwealth because the uncertainty of the tax effect of purchases of tangible personal property, the difficulty of application of the tax, and the severe economic impact of non-compliance discourages federal government contractors from establishing businesses in or relocating to Virginia; and

WHEREAS, the unique aspects of federal government contracting need to be acknowledged, the uncertainty over the applicability of the Virginia sales and use tax needs to be reduced, and a fair and equitable means by which contractors can determine how the tax will be applied to their purchases of tangibles needs to be provided; now, therefore, be it

RESOLVED by the Senate, the House of Delegates concurring, That the Commission to Study Virginia's State and Local Tax Structure for the 21st Century, established by House Joint Resolution No. 578 (1999), shall study, among its other charges, the impact of the Virginia sales and use tax, and more particularly the "true object" test, on federal government contractors. The Commission shall (1) examine all aspects of the sales and use tax structure to ensure its viability, fairness, and appropriateness as applied to federal government contractors; (2) analyze the Department of Taxation's implementation of the "true object" test to multipurpose contracts; (3) evaluate the feasibility of creating a presumption regarding the purpose of a federal government contract based upon the incorporation therein by the contracting federal government agency of either the Walsh-Healey Act federal acquisition regulations or the Service Contract Act federal acquisition regulations; and (4) evaluate whether it is advisable to require that the true object of a federal government contract be determined by and be consistent with the true object of the overall procurement to which the contract relates rather than on a contract-by-contract basis.

The Commission shall complete its work in time to submit its findings and recommendations to the Governor and the 2001 Session of the General Assembly as provided in the procedures of the Division of Legislative Automated Systems for the processing of legislative documents.