Michigan Law Review

Volume 40 | Issue 3

1942

CONSTITUTIONAL LAW - CONSTITUTIONALITY OF STATE SALES TAX ON DEFENSE MATERIALS PURCHASED UNDER A COST-PLUS-A-FIXED-FEE CONTRACT WITH THE FEDERAL GOVERNMENT

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CONSTITUTIONAL LAW — CONSTITUTIONALITY OF STATE SALES TAX ON DEFENSE MATERIALS PURCHASED UNDER A COST-PLUS-A-FIXED-FEE CONTRACT WITH THE FEDERAL GOVERNMENT — X had a cost-plus-a-fixed-fee contract with the federal government, under which the government reserved the right to pay directly for purchases made by *X* pursuant to contract to give prior authorization for each purchase over $500, to inspect and acquire title to materials delivered under such contract, and to furnish materials itself. *X* ordered lumber from plaintiff, who contested the constitutionality of an Alabama sales tax levied on this sale, contending that the tax was levied on a transaction by which the United States secured goods for governmental purposes. *Held*, the tax should be sustained, since *X*, and not the government, was legally obligated to pay for the materials, and since *X* was an independent contractor.[1] Such a tax

[1] The Alabama court found it unnecessary to decide whether *X* was an independent contractor as to such purchases, but it states strong arguments for the conclusion that he was not, in view of government control over the purchases. King & Boozer v. State, (Ala. 1941) 3 So. (2d) 572.

is not invalid merely because the tax burden is passed on to the government. *Alabama v. King & Boozer*, (U. S. 1941) 62 S. Ct. 43.

This decision is remarkable in holding immaterial the fact that the burden of the tax was passed immediately and entirely to the government, simply because the tax was paid by an independent contractor. The cases cited by the Court do not support this conclusion but rather support the converse position.[2] In these cases the decisions upholding the tax were primarily based on the speculative nature of the tax burden upon the government, whereas in the principal case the tax burden is certain to be borne exclusively by the government. The interposition of an independent contractor between the government and the taxing authority has never been regarded as controlling when the burden of the tax falls directly and immediately upon the federal government,[3] although his presence has been used to circumscribe immunity where the tax burden on the government is doubtful. One reason for this distinction is the fact that in so far as the burden of a given tax does not fall upon the government, the finding of immunity deprives the state of its revenue without affording a commensurate protection to the federal government and in addition confers an unwarranted personal immunity on the contractor.[4] The result of the principal case, as distinguished from its logic, does not seem startling when viewed in the light of the economic, political, and historical background of the immunity doctrine. The necessity of preventing the imposition of destructive and regulatory taxes on one government by the other underlies the implied constitutional immunity. The scope of the doctrine was probably limited by two factors: First, justice required that the states should be reimbursed for the services rendered federal

[2] Metcalf & Eddy v. Mitchell, 269 U. S. 514, 46 S. Ct. 172 (1926), involved an income tax on the consulting engineer of a public works project, which was held valid because it imposed only a speculative burden on the government. Trinityfarm Construction Co. v. Grosjean, 291 U. S. 466, 54 S. Ct. 469 (1934), involved an excise tax on gasoline used by a contractor in constructing levees for the federal government, wherein there was no indication that the economic burden was shifted to the government. In James v. Dravo Contracting Co., 302 U. S. 134 at 154, 58 S. Ct. 208 (1937), it was said that a gross receipts tax on a contractor would not be invalid because of the mere possibility that it might enter into the contractor's estimate. It was in fact stipulated that the contract price included no item to cover such tax, although the contractor was fully aware of the tax. The other two cases cited involved income taxes on employees of governmental agencies which were upheld because the burden upon the governmental function was not actual and substantial, but conjectural. Helvering v. Gerhardt, 304 U. S. 405, 58 S. Ct. 969 (1938); Graves v. New York ex rel. O'Keefe, 306 U. S. 466, 59 S. Ct. 595 (1939).

[3] James v. Dravo Contracting Co., 302 U. S. 134 at 164, 58 S. Ct. 208 (1937). Two state cases of similar facts should be noted. Although each reached the same result as the principal case, neither based the decision on the independent contractor concept. Standard Oil v. Lee, 145 Fla. 385, 199 So. 325 (1940); Boeing Airplane Co. v. State Commission of Revenue, 153 Kan. 712, 113 P. (2d) 110 (1941).

[4] For example, if a state tax of $1 on sales to a contractor resulted in an actual increase in cost to the government of $.25, $.75 being absorbed by the contractor, the finding of immunity would deprive the state of $1 revenue, protect the federal government only to extent of a $.25 burden, and confer upon the contractor a windfall of $.75.

instrumentalities which indirectly benefit the people of every state. Secondly, if immunity were extended too far back in the series of events leading to the transaction by which a part of the tax burden might be passed on to the government, the limitation on states' power to tax would be extended, although the need of protecting the federal government is diminished. The Supreme Court in the first instance might have held that the constitutional immunity extended only to discriminatory and regulatory taxation of governmental instrumentalities, leaving to Congress, in the exercise of powers conferred by the necessary and proper clause,[5] the function of providing further immunity. Instead, the early cases extended the doctrine to give complete protection without Congressional intervention.[6] Today, many factors, absent during the early development of the doctrine, are present to support a narrower construction of implied constitutional immunity. The proposition that "the power to tax is the power to destroy" is no longer tenable,[7] and the due process clause has been developed in a substantive sense to prohibit discriminatory, arbitrary, and confiscatory taxation.[8] Differences as to the severity of the burden may now be the basis for reaching opposite results under the immunity doctrine.[9] The expansion of governmental activities has seriously increased the burden of tax immunity on the states, and calls for a closer examination of its limitations. The existence of Congressional power to provide immunity beyond that implied in the Constitution has been at least impliedly recognized,[10] and there is a growing belief that Congress is in a better position than the courts to judge whether a nondiscriminatory, nonregulatory tax unreasonably interferes with the functions of the federal government. Since the present court is willing to disregard precedent which it feels is unsound and is shifting the resolution of traditionally judicial questions to Congress, there is little to obstruct a radical restriction of the immunity doctrine.[11] In view of the above considerations, it is submitted that the tax in the principal case would have been upheld even if the government had

[5] U. S. Const., Art. I, § 8.

[6] See cases cited in Panhandle Oil Co. v. Mississippi ex rel. Knox, 277 U. S. 218, 48 S. Ct. 451 (1928).

[7] Id., 277 U. S. at 223 (dissenting opinion); Graves v. New York ex rel. O'Keefe, 306 U. S. 466 at 487-492, 59 S. Ct. 595 (1939).

[8] 16 C. J. S. 1338-1347 (1939).

[9] Panhandle Oil Co. v. Mississippi ex rel. Knox, 277 U. S. 218 at 223, 48 S. Ct. 451 (1928).

[10] 38 MICH. L. REV. 738 (1940). A case showing the extent of this power was decided on the same day as the principal case, the court holding a sales tax on lumber purchased to recondition houses acquired by the Federal Land Bank of St. Paul through mortgage foreclosures invalid, since Congress had stipulated immunity from taxation. Federal Land Bank of St. Paul v. Bismarck Lumber Co., (U. S. 1941) 62 S. Ct. 1.

[11] That this process has been initiated is apparent from a reading of the Gerhardt and Graves cases holding income taxation of government employees valid. Helvering v. Gerhardt, 304 U. S. 405, 58 S. Ct. 969 (1938); Graves v. New York ex rel. O'Keefe, 306 U. S. 466, 59 S. Ct. 595 (1939). See also James v. Dravo Contracting Co., 302 U. S. 134, 58 S. Ct. 208 (1937).

been treated as the purchaser. Although the *Panhandle Oil* case [12] held such a tax invalid, Justice Holmes, speaking for the minority, asserted that when the federal government is a purchaser it does not stand differently with respect to a sales tax from any other purchaser.[13] This view [14] is undoubtedly shared by the majority of the court today.[15]

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[12] This was a case involving a sales tax on gasoline purchased by the United States Coast Guard. Panhandle Oil Co. v. Mississippi ex rel. Knox, 277 U. S. 218, 48 S. Ct. 451 (1928).

[13] Id., 277 U. S. 218 at 224.

[14] All of the justices who participated in the majority opinion of the Panhandle case have now left the Court.

[15] An opinion of the attorney general of Michigan based upon the principal case will prompt Michigan to levy several million dollars in sales taxes upon contractors with the federal government whom state officials had thought to be immune from the sales tax. See DETROIT FREE PRESS 17:8 (Dec. 4, 1941). This news item states that federal officials expect to spend $50,000,000 in reimbursing contractors who have been subjected to sales taxes since the decision in the principal case.