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STATE OF MINNESOTA
DEPARTMENT OF REVENUE

In the Matter of the Proposed Adoption of
an Amended Rule of the Minnesota
Department of Revenue Governing
Constitutional Exemptions from Sales
and Use Tax

STATEMENT OF NEED
AND REASONABLENESS

GENERAL STATEMENT

This document has been prepared as a verbatim affirmative presentation of the facts necessary to establish the statutory authority, need for, and reasonableness of the proposed rule. It is submitted pursuant to Minnesota Statutes, section 14.23 (1990) and Minnesota Rules Part 1400.0500 (1989) requiring a Statement of Need and Reasonableness.

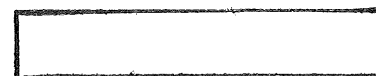
A Notice of Solicitation of Outside Information or Opinions regarding the Constitutional Exemptions from Sales and Use Tax was published in the State Register on June 22, 1992. The notice specifically mentioned this rule and invited interested persons to submit comments or suggestions in writing to the Department by July 22, 1992. No written comments were submitted.

This rulemaking proceeding proposes to amend the rules relating to Constitutional Exemptions from Sales and Use Tax. The existing rule needs to be expanded to clarify how this exemption applies in certain situations.

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The changes being proposed for this rule are of several types. (1) Some of the changes involve grammatical and form changes. (2) Some of the changes clarify special situations that arise in sales to federal and foreign governments and sales and purchases by federal and foreign governments. (3) Some of the changes are to clarify issues that are often misunderstood by taxpayers as evidenced by taxpayer inquiries and audit issues.

IMPACT ON SMALL BUSINESSES

The impact of this rule on small businesses has been considered. The proposed rule does not impose new filing, or payment requirements on small businesses and therefore is not expected to place any additional financial or administrative burden on small businesses.

SPECIAL NOTICE OF RULEMAKING

Pursuant to Minnesota Statutes, section 14.11 (1990), the proposed rule will not require the expenditure of public monies by local units of government and will not have any direct adverse effects on agricultural lands in this state.

AUTHORITY TO ADOPT RULES

Minnesota Statutes, section 270.06 (1990) grants the Commissioner of Revenue authority to promulgate rules concerning administration and enforcement of the sales and use tax laws.

RULE ANALYSIS

Through this rule, the commissioner seeks to clarify the constitutional exemptions from sales and use tax. Changes in statutory language are incorporated. Examples are given. Procedural requirements are clarified.

Subpart 1. This subpart gives the statutory citation and the exemption granted by Minnesota Statutes, section 297A.25, subdivision 4. The subpart headnote was changed to more accurately describe the contents of the subpart.

Subpart 2. This subpart is generally the same as subpart 2 in the existing rule. Grammatical and form changes were made to improve clarity. The additional information in items A through D was added to address and clarify common areas of misunderstanding in the application of this subpart.

Item A. This is a new item. Examples of entities whose purchases are recognized as being exempt under the doctrine of intergovernmental immunity were added.

Item B. This is a new item. It clarifies that federally chartered banks and savings and loans association are not considered exempt under the

doctrine of intergovernmental immunity. This issue is dealt with in greater detail in subpart 6 of this rule.

Item C. This item is new. It explains that purchases must be billed to and paid for directly by the federal government in order to be exempt. This is reasonable because the constitution only prohibits states, without the consent of Congress, from levying a tax directly against the federal government. It also ensures that only official purchases of the federal government are exempted from sales tax and that those purchases that are not official are subject to sales tax.

Item D. This item is new and is generally procedural. It explains the types of documentation the seller may accept from the federal government to authorize an exempt purchase. This subpart is necessary to inform those who make sales to the federal government of the types of documentation they may accept that will relieve them of the duty of collecting and remitting the tax otherwise due. It is reasonable because the seller is relieved of their duty to collect the tax by accepting any document that clearly shows that the purchaser is the federal government.

Subpart 3. The last phrase in this subpart was amended. The existing rule provides that sales and use tax cannot be imposed if the sale is an integral part of interstate commerce. This is incorrect. Under the constitution, the state is only prohibited from imposing a sales or use tax if the imposition of the tax will unduly burden interstate commerce.

Subpart 4. This subpart is generally the same as subpart 4 in the existing rule. A nonsubstantive grammatical change was made to improve clarity.

Subpart 5. This is a new subpart. It explains how sales to foreign consuls should be treated and the procedures that must be followed. It is reasonable because the exemption from Minnesota sales and use tax is based on sales tax exemption cards that are issued by the United States Department of State, Office of Foreign Missions. The extent of the exemption granted by these cards is determined by the exemption the consular official's country provides to U.S. personnel stationed there.

Subpart 6. This is a new subpart. It explains the differences in taxability of sales to and purchases by: (1) federal credit unions, (2) federally chartered banks and savings and loans, and (3) state chartered credit unions, banks, and savings and loans. It is necessary because it is an area that is often misunderstood by those who sell to these entities and by the entities themselves, as demonstrated by inquiries and compliance problems. It is reasonable because it incorporates the court decision in Midwest Federal Savings and Loan Association v. Commissioner of Revenue, 259 N.W.2d 596 (1977). Item B, which explains the applicability of sales and use tax to sales to and purchases by state chartered credit unions, banks, and savings and loans, was added for clarification purposes as many taxpayers that sell to federal credit unions, banks, etc. will also sell to those that are state chartered.

Subpart 7. This is a new subpart. It clarifies that while purchases by the federal government are exempt from sales and use taxes, sales by the federal government are subject to tax, except as provided by Congress. It also clarifies

that if the federal government does not collect the sales tax the purchaser is liable for the use tax on taxable items. This is necessary because there is a common misunderstanding among taxpayers that items that are purchased from the federal government are not subject to sales and use tax simply because the federal government is the seller.