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TAX EXEMPTIONS FOR SPECIAL SERVICES DISTRICTS

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You asked whether a special services district is exempt from (1) state sales and use taxes on items and services it buys and (2) federal excise taxes, especially the 3% federal tax on telecommunications services.

The Office of Legislative Research is not authorized to give legal opinions and this report should not be considered one.

SUMMARY

Municipal special services districts authorized under state law are exempt from paying state sales and use tax on items and services they buy. They are also exempt from the 3% federal tax on communications services and from any other federal excise tax that exempts political subdivisions of local governments.

The federal government imposes many excise taxes other than the communications tax, including taxes on various types of fuel, air transportation services, and ship passengers. This report addresses only exemptions from the communications tax, since this seems to be the federal excise tax service a special service district is most likely to pay. If you would like us to determine exemptions for any other federal excise tax, please let us know.

SPECIAL SERVICES DISTRICTS

State law allows municipalities to create special services districts (SSDs) on behalf of the property owners of an area, such as a downtown shopping district. The districts are created by municipal ordinance. The law specifies that the districts "constitute a body politic and corporate" (CGS § 7-339n). The district has the power to impose additional property taxes on property owners in the district in order to provide them with additional services.

STATE SALES AND USE TAXES

State law exempts sales of tangible personal property and services to the state, any of its political subdivisions, or any of “its or their respective agencies” from the sales and use taxes (CGS §12-412(1)). According to Michael Galliher of the Department of Revenue Services’ (DRS) research division, an SSD would be considered an agency of a municipality, and would thus be considered exempt. DRS has not issued any written ruling on this exact question.

FEDERAL COMMUNICATIONS TAX

The federal government imposes a 3% tax on amounts paid for local and long distance telephone and teletype service. The tax does not apply to any state or political subdivision of a state.

Federal tax law does not define “political subdivision,” but federal income tax regulations do. Those regulations state that the term covers any local governmental unit that either (1) is a municipal corporation or (2) has been delegated any of the government's sovereign powers, such as the power to tax (Income Tax Regulations, §1.103(b)). Both of these criteria apply to a Connecticut SSD.

Although the regulation defining “political subdivision” applies only to the federal income tax, IRS revenue rulings have applied the definition for all federal tax purposes (IRS ruling #200238001, 9/20/2002, p. 2, copy enclosed).

Thus, it appears that an SSD is exempt from the federal communications tax, as well as from any other federal excise tax that exempts political subdivisions of state and local governments. The IRS requires exempt entities to have an exemption certificate. The certificate

can be in any form that includes the information the IRS Code and regulations require and must be filed with the communications services provider (IRS Publication 510, Excise Taxes for 2003, p.5).

JL:ro