OCT 8 1997 199904037

Index No.: 4081.01-00
Control No.: TAM-112305-97

INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM

District Director

"This document may not be used or cited as precedent. Section 6110 (j) (3) of the Internal Revenue Code."

Taxpayer Name:

Taxpayer Address:

Taxpayer Identification No.:

Periods Involved:

Conference Held:

Issues

Is tax imposed by § 4081(a) of the Internal Revenue Code on the total number of gallons of undyed diesel fuel removed from the taxpayer's refinery, including previously-taxed gallons, and, if so, must the full amount of the liability be reported on the taxpayer's Form 720?

Is a credit allowed on Form 720 for tax paid with respect to previously-taxed diesel fuel that is removed from the taxpayer's refinery? If not, is a claim for a refund of the second tax paid with respect to diesel fuel available?

Facts

The taxpayer operates a refinery.

the taxpayer purchased diesel fuel to mix with its diesel fuel. The purchased diesel fuel was removed from the bulk transfer/terminal system and delivered to the taxpayer's refinery by truck and trailer. Therefore, tax was imposed with respect to the diesel fuel that was purchased by the taxpayer.

The taxpayer contacted the district office to express its concern that a second tax would be imposed with respect to the purchased diesel fuel removed from its refinery at the rack. The taxpayer asked the district office if it could take a credit for off-highway business use, under § 6427(l)(1), on Form 720 in an

amount equal to the second tax that would be imposed upon removal. The district office advised the taxpayer that it could not take a credit. The district office instructed the taxpayer to report, and pay tax on, the total number of gallons of undyed diesel fuel removed from its refinery at the rack and to file a claim for a refund of the second tax as provided under § 4081(e).

For the tax periods 9412, 9503, and 9506, the taxpayer took "blind credits," that is, the taxpayer reported on Part I of Form 720 the difference between the number of gallons removed from its refinery at the rack and the number of gallons of previously-taxed diesel fuel included in the removal. The blind credits were not disclosed on Form 720. The taxpayer did not make any adjustments or claims on Part III of Form 720.

Law

Section 4081(a)(1)(A) imposes a tax on the removal of diesel fuel from any refinery or terminal. Section 4082 provides that the tax under § 4081 does not apply to diesel fuel that is indelibly dyed in accordance with Treasury regulations and destined for a nontaxable use.

Section 40.6011(a)-1(a)(1) of the Excise Tax Procedural Regulations provides that the return of any tax to which 26 C.F.R. part 40 applies, including the § 4081 tax, must be made on Form 720, Quarterly Federal Excise Tax Return, according to the instructions applicable to the form. Under § 40.6011(a)-1(a)(2), a return must be filed reporting tax liability incurred during each calendar quarter.

Section 4081(e) provides that if any person that paid the tax imposed by § 4081 with respect to any diesel fuel establishes to the satisfaction of the Secretary that a prior tax was paid (and not credited or refunded) with respect to such diesel fuel, then an amount equal to the tax paid by such person shall be allowed as a refund (without interest) to such person in the same manner as if it were an overpayment of tax imposed by § 4081.

Under § 6416(d), a person entitled to a refund under § 4081(e) may not take a credit on Form 720 instead of claiming a refund.

Section 6511(b) provides that a claim for credit or refund of any overpayment of tax must be filed by the taxpayer within three years from the time the return was filed or two years from the time the tax was paid, whichever period expires later.

Section 6427(l)(1) provides that, if any diesel fuel on which tax has been imposed under § 4081 is used by any person in a nontaxable use, such as an off-highway business use, the Secretary shall pay to the ultimate purchaser an amount equal to

the amount of tax imposed. Section 6421(e)(2) defines "off-highway business use" as use by any person in a trade or business other than as a fuel in a highway vehicle that is registered, or required to be registered, for highway use.

Section 6427(i)(1) provides that no claim filed under § 6427(l) shall be allowed unless filed by the purchaser not later than the time prescribed for filing a claim for credit or refund of overpayment of income tax for that taxable year.

Rationale

The taxpayer asserts that the law allows it to claim blind credits on Part I of Form 720 to avoid duplicate tax payments and minimize administrative burdens. We disagree.

Section 4081(a) imposes a tax on all nonbulk removals of diesel fuel from a refinery at the rack with the exception of properly dyed diesel fuel destined for nontaxable use. Tax is imposed on the total number of gallons of diesel fuel removed and that liability must be reported on Form 720 in accordance with § 40.6011(a)-1(a). Blind credits are not permitted. The stringent statutory requirements related to diesel fuel taxation were enacted by Congress, in part, to address substantial levels of diesel fuel tax evasion. Congress anticipated that tax would be imposed twice under certain circumstances, such as removal from the refinery of previously-taxed diesel fuel, and enacted § 4081(e) to provide a mechanism for refund of the second tax. Section 4081(e) provides that, if a second tax is paid with respect to diesel fuel, the amount of that tax may be refunded, upon the satisfaction of certain conditions. Sections 4081(e) and 6416(d) expressly provide for payment of a refund under § 4081(e), not allowance of a credit. In order to claim a refund of a second tax paid under § 4081(a), the taxpayer would need to have paid a second tax with respect to previously-taxed diesel fuel and filed a claim for refund in accordance with § 6511(b).

In this case, the taxpayer did not pay the tax and did not file a refund claim. By claiming blind credits, the taxpayer assumed that a credit against its tax liability was available in the amount of the second tax with respect to that fuel. However, under § 6416(d), a credit under § 4081(e) is prohibited.

Alternatively, the taxpayer asserts that it is eligible for a credit under § 6427(l)(1) in the amount of the prior tax because the previously-taxed diesel fuel was used in an off-highway business use. We disagree.

The legislative history to the Highway Revenue Act of 1956, 1956-2 C.B. 1150, indicates that Congress enacted the exemption for fuel used in an off-highway business use to address fuel used by the ultimate purchaser in nonhighway vehicles and in motorized

equipment. See generally Highway Revenue Act, 1956: Hearings on H.R. 10660 Before the Senate Committee on Finance, 84th Cong., 2nd Sess. (1956). The use contemplated by Congress is the ultimate use of diesel fuel in a motor, not the use of diesel fuel in a mixture that produces other diesel fuel. An illustration of Congressional intent to ensure that diesel fuel used in the manufacture of diesel fuel is not exempt from tax is found in § 6416(b)(3)(B), which provides that there is no overpayment of tax where previously-taxed fuel is used for fuel purposes, for example as an additive, in the manufacture of another product, such as diesel fuel.

The taxpayer's use of previously-taxed diesel fuel in the production of its diesel fuel is not an off-highway business use of previously-taxed diesel fuel. Thus, a credit or refund is not available under § 6427(l)(1) for the amount of tax imposed on the diesel fuel used to produce diesel fuel. Furthermore, even if a claim was allowable under § 6427(l), the taxpayer would have to report, on Part I of Form 720, the total number of gallons of diesel fuel removed from its refinery and make a claim, as required by § 6427(i)(1), on Part III of Form 720 . The taxpayer did not make a claim for diesel fuel used in an off-highway business use on its Form 720.

Conclusions

Tax is imposed by § 4081(a) on the total number of gallons of undyed diesel fuel removed from the taxpayer's refinery, including any previously-taxed gallons, and liability for this total number of gallons must be reported on the taxpayer's Form 720.

A credit is not allowed on Form 720 for any tax paid with respect to previously-taxed diesel fuel that is removed from the taxpayer's refinery. However, the taxpayer may file a claim for refund of the second tax paid with respect to diesel fuel under § 4081(e).

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(j)(3) provides that it may not be used or cited as precedent. In accordance with § 6110(c), names, addresses, and taxpayer identifying numbers have been deleted.

- END -