

Office of Chief Counsel
Internal Revenue Service
Memorandum

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to: W. Ricky Stiff
Chief, Excise Tax Program

from: William P. O'Shea
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subject: Request for non-taxpayer specific legal advice; auxiliary power units (APU)

This memorandum responds to your request for guidance on an issue affecting multiple taxpayers in the commercial airline industry. Specifically, this memorandum provides legal advice regarding the rules for a payment or credit related to kerosene used in a commercial aircraft's auxiliary power unit (APU) that draws its fuel from the same tank that supplies fuel to the propulsion system of an aircraft.

This memorandum may not be used or cited as precedent. It is intended only for use by the office that requested it.

ISSUE

Whether kerosene used in a commercial aircraft's APU is fuel "used in commercial aviation" for purposes of § 6427(l)(4)(A) of the Internal Revenue Code?

CONCLUSION

Kerosene used in a commercial aircraft's APU is not fuel used in commercial aviation for purposes of § 6427(l)(4)(A) because the kerosene is not used in the propulsion system of an aircraft. When that kerosene is drawn from the same tank that supplies fuel to the propulsion system of an aircraft, a reasonable determination of the quantity of fuel used

by the APU is acceptable for purposes of computing the payment or credit, in accordance with the rules provided in § 48.6427-1(d) of the Manufacturers and Retailers Excise Tax Regulations.

FACTS

Numerous commercial airlines have filed substantial refund claims for the amount of excise tax imposed on the kerosene used to operate the APU on their aircrafts. You have requested advice to determine whether to allow these claims.

The APU is a small generator that is usually located in the tail section of a jet aircraft. The device provides power for an aircraft's electrical and air conditioning systems and for starting the propulsion engines of the aircraft (or restarting them in case of a shutdown during flight). The APU does not propel the aircraft. The APU does, however, operate on kerosene that it draws from the fuel tank of the aircraft that also supplies the aircraft's propulsion engines.

LAW AND ANALYSIS

Section 4081(a) imposes a tax on certain removals, entries, and sales of taxable fuel, including kerosene.

Under § 4081(a)(2)(A), the rate of tax on kerosene is \$.244 per gallon. However, § 4081(a)(2)(C) provides that the rate of tax on kerosene removed from any refinery or terminal directly into the fuel tank of an aircraft is \$.219 per gallon if the kerosene is for use in general aviation, and \$.044 per gallon if the kerosene is for use in commercial aviation.

Section 4041(a)(1) imposes a tax on any liquid other than gasoline sold for use or used in a diesel-powered highway vehicle or a diesel-powered train for use as a fuel in such vehicle or train. An exception to the tax imposed by § 4041(a)(1) exists for any liquid taxed under § 4081 (other than at the Leaking Underground Storage Tank trust fund rate) that is not credited or refunded.

Section 4083(b) provides that commercial aviation means any use of an aircraft in a business of transporting persons or property for compensation or hire by air, unless properly allocable to transportation exempt from taxes imposed by §§ 4261 and 4271 by reason of § 4281 or § 4282 or by reason of § 4261(h) or (i).

Section 6427(l)(1) generally provides that if any kerosene on which tax is imposed is used by any person in a nontaxable use, the Secretary shall pay (without interest) to the ultimate purchaser of such fuel an amount equal to the tax imposed under § 4041 or 4081, reduced by any payment to the ultimate vendor. Nontaxable use means any use that is exempt from the tax imposed by § 4041(a)(1) other than by reason of a prior imposition of tax.

Section 6427(l)(4)(A) limits the amount of credit or payment under § 6427(l)(1) for kerosene used in commercial aviation. If tax was imposed at the rate of \$.244, the credit or payment amount is \$.20; if tax was imposed at the rate of \$.219, the credit or payment is \$.175; and if tax was imposed at the rate of \$.044, the credit or payment amount is zero.

Section 48.4041-7 provides rules for dual use of taxable liquid fuel under § 4041. The rules provide, in pertinent part, that while tax applies to all taxable liquid fuel sold for use or used as a fuel in the motor that is used to propel a motor vehicle, motorboat, or aircraft, tax does not apply to liquid fuel sold for use or used in a separate motor to operate special equipment (whether or not the equipment is mounted on the vehicle).

Section 48.6427-1(d) indicates that the principles set forth in § 48.4041-7 are equally applicable in determining whether a credit or payment is to be allowed under § 6427. Thus, if diesel fuel or special motor fuel used in a separate motor is drawn from the same tank as the one that supplies fuel for the propulsion system of a vehicle, a reasonable determination of the quantity of the fuel used in the separate motor will be acceptable for purposes of computing the payment or credit. The determination must be based, however, on the operating experience of the person using the fuel, and a statement, signed by the person, evidencing the operating experience must be maintained as part of the records of the person claiming the payment or credit.

Fuel is “used in commercial aviation” only if, among other conditions, it is also “used in an aircraft.” The principles of § 48.4041-7 relating to dual use of taxable liquid fuel used in a separate motor apply to the kerosene used in an aircraft's APU. The kerosene used to operate the APU is not used in the propulsion system of the aircraft; rather, it is used in a separate motor operating the APU. The APU is special equipment that provides power for an aircraft's electrical and air conditioning systems and for starting the propulsion engines of the aircraft (or restarting them in case of a shutdown during flight). Because the kerosene is not used in the propulsion system of the aircraft, the kerosene is not “used in an aircraft” and thus not “used in commercial aviation.”

Accordingly, only kerosene used in the propulsion system of the aircraft is considered to be used in commercial aviation. The kerosene used in the APU is used in a nontaxable use under § 6427(l)(2), without the limitation of § 6427(l)(4).

This analysis also applies to: (1) kerosene used in an APU in an aircraft that is not engaged in commercial aviation; and (2) aviation gasoline used in an APU in an aircraft, whether or not the aircraft is engaged in commercial aviation.

Please call Deborah Karet at (202) 622-3130 if you have any further questions.

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