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Internal Revenue Service (I.R.S.)

Technical Advice Memorandum

Issue: March 30, 1990

October 11, 1989

Section 9999

9999.00-00

9999.98-00 Not Able to Identify Under Present List

TR-32-127-89

Taxpayer's Name: * * *

Taxpayer's Address: * * *

Taxpayer's Identification No.: * * *

Years Involved: 8604, 8704, 8804, 8806, 8809, 8812, 8903, 8906

No Conference Held.

LEGEND:

X = * * *

Y = * * *

A = * * *

B = * * *

C = * * *

D = * * *

E = * * *

F = * * *

G = * * *

H = * * *

I = * * *

J = * * *

ISSUES

1. Whether X may purchase gasoline and/or diesel fuel tax free for resale through its service stations to members of its tribe and the general public.
2. Whether, after October 13, 1987, X's tribal economic subsidiaries are considered to be engaged in 'essential governmental functions' and are permitted to purchase gasoline and/or diesel fuel tax free for use in their operations.

FACTS

X is an Indian tribe that is listed in [Revenue Procedure 83-87, 1983-2 Cumulative Bulletin 606](#), as an entity that is treated as a state for certain tax purposes. Y is the tribe's governing body.

X has several economic subsidiaries known as A, B, C, D, E, F, G, H, I, and J. None of the subsidiaries is separately incorporated and all their property is held in the name of X. Y is responsible for the overall management of the subsidiaries. The subsidiaries provide employment and job training for tribal members. The income from the subsidiaries finances tribal government programs including general government administration, education, health, welfare and housing.

A manages the commercial enterprises of the tribe. It employs and trains members of the tribe and operates commercial entities including grocery stores, service stations and various other stores and shops. A majority of the fuel it purchases is for sale to tribal members through retail outlets. Other fuel is sold to the general public through its service stations.

B manages the operation of two sawmills that are operated by tribal members. Essentially all of the fuel it purchases is for use in the operation of the mill and its equipment.

C manages and operates the agricultural activities of the tribe including the growing of crops for sale. The fuel it purchases is used in the operation of the equipment needed to run the venture.

D is responsible for any major building activity taking place on the reservation including construction of all commercial buildings, HUD housing, pipeline construction, etc. The fuel it purchases is used in the operation of the construction equipment.

E is responsible for the operation of a major ski resort. It employs and trains tribal members in its operation. The fuel it purchases is used in the operation of the equipment needed to run the ski resort.

F manages, operates and maintains camp locations with recreational facilities for fishing, hunting, backpacking, and other sports activities. F's mission is to (1) protect, conserve, and control the wildlife, recreational, and natural resources of the reservation, (2) manage and develop fish and wildlife habitat, (3) furnish information to Y for use in establishing seasons and bag limits, and (4) coordinate fish, wildlife, and recreation development with other activities on the reservation. The fuel it purchases is used in the operation of vehicles and equipment.

G manages the cattle operation owned by the tribe. The fuel it purchases is used in the operation of equipment.

H operates commercial enterprises including a motel, restaurant, supermarket, variety store, movie theater and service station. The fuel it purchases is used in the operation of equipment and is also sold through the service station primarily to tribal members residing in the area and also to the general public.

I operates commercial enterprises owned by the tribe including a grocery store and service station. The fuel it purchases is used in the operation of equipment and is also offered for sale by the service station to tribal members and to the general public.

J operates as a public utility overseeing the providing of utility services to the reservation. It also serves as a liaison with public utility providers off the reservation. The fuel it purchases is used in the operation of equipment.

Neither X nor its subsidiaries have retained any documents or records that would indicate the quantities of fuel used in nonhighway applications.

On April 10, 1985, X was issued a private letter ruling that held that, under [section 7871\(a\)\(2\) of the Internal Revenue Code](#), purchases and uses made by X's subsidiaries A thru F were exempt from federal excise taxes to the same extent that states were also exempt.

APPLICABLE LAW

Effective for gasoline removed after 1987, section 4081(a)(1) of the Code imposes a tax at the rate specified in section 4081(a)(2), on the earlier of the removal or sale of gasoline by the refiner or importer thereof or the terminal operator.

Effective for the years in question prior to 1988, section 4081(a)(1) generally provided for the imposition of a tax on gasoline sold by the producer or importer thereof, or by any producer of gasoline.

Section 4091 of the Code (effective after March 31, 1988) imposes an excise tax on the sale of any taxable fuel (the definition of which includes diesel fuel) by the producer or importer thereof or by any producer of a taxable fuel.

Section 4041(a) of the Code imposes a tax on the sale or use of diesel fuel where no tax was imposed under section 4091.

There is currently no tax-free sale provision for the sale of gasoline to a state or local government, but a credit or refund is available under section 6416(b)(2) or section 6421 of the Code on gasoline which is purchased by a state or local government for its exclusive use. For the tax years in question prior to January 1, 1988, under section 4221(a)(4), gasoline could be purchased from producers tax free by state or local governments for the exclusive use of the state or local government. Under sections 4041(g) and 4093(c)(1) (effective after March 31, 1988) of the Code, state or local governments may make tax-free purchases of diesel fuel for their exclusive use.

[Section 7871\(a\)\(2\)](#) of the Code provides that, subject to [section 7871\(b\)](#), an Indian tribal government shall be treated as a state for purposes of an exemption from, credit or refund of, or payment with respect to, an excise tax imposed by, (A) chapter 31 (relating to tax on special fuels), (B) chapter 32 (relating to manufacturers excise taxes), subchapter B of chapter 83 (relating to communications excise tax), or (D) subchapter D of chapter 36 (relating to tax on use of certain highway vehicles).

Section 7701(a)(40)(A) of the Code provides that the term 'Indian tribal government' means the governing body of any tribe, band, community, village or group of Indians, or (if applicable) Alaska Natives, which is determined by the Secretary of the Treasury, after consultation with the Secretary of the Interior, to exercise governmental functions. See [Rev. Proc. 83-87](#) for the Secretary's determination.

[Section 7871\(b\)](#) of the Code provides that [section 7871\(a\)\(2\)](#) shall apply with respect to any transaction only if, in addition to any other requirement of this title applicable to similar transactions involving a state or political subdivision thereof, the transaction involves the exercise of an essential governmental function of the Indian tribal government.

[Section 7871\(e\)](#) of the Code, effective after October 13, 1987, provides that for purposes of [section 7871](#), the term 'essential governmental function' shall not include any function which is not customarily performed by state and local governments with general taxing powers.

For periods on and before October 13, 1987, section 305.7871-1(d) of the Temporary Procedural and Administrative Tax Regulations provides that an 'essential governmental function' of an Indian tribal government (or portion thereof) is described as a function of a type which is (1) eligible for funding under [25 U.S.C. 13](#) and the regulations thereunder; (2) eligible for grants and contracts under [25 U.S.C. 450\(f\), \(g\), and \(h\)](#) and the regulations thereunder; or (3) an essential governmental function under section 115 and the regulations thereunder when conducted by a state or political subdivision thereof. The April 10, 1985, letter ruling to X indicated that the activities of X's subsidiaries A thru F were of the type that were eligible for funding under [25 U.S.C. 13](#) and, thus, the activities were considered to be essential governmental functions.

RATIONALE

ISSUE 1

In [Rev. Proc. 83-87](#) the Secretary has designated X as an Indian tribal government that is to be treated similarly to a state for purposes of [section 7871](#) of the Code. Under [section 7871\(b\)](#), the exemption from excise taxes accorded tribal governments by virtue of their similar treatment to states is not applicable unless X can demonstrate that the underlying transaction involves the exercise of an essential governmental function of X's tribal government. For periods on and before October 13, 1987, section 305.7871-1(d) of the temporary regulations is determinative as to what constitutes an essential governmental function. Subsequent to October 13, 1987, [section 7871\(e\)](#) provides that an essential governmental function does not include any function which is not customarily performed by state or local governments with general taxing powers. Activities that are customarily performed by such governments include, but are not limited to, functions related to law enforcement, public safety, street building and maintenance, maintenance

of public parks, public education, and public health.

In the Conference Committee Report on [P.L. 97-473](#) (which granted the exemption), it is also stated that 'the tax-exempt articles must be for the Indian Tribal government's EXCLUSIVE (emphasis added) use in carrying out the essential governmental function'. See [H.R. Conf. Rep. No. 984, 97th Cong., 2d Sess. 11 1983](#), [1983-1 C.B. 522, 524](#). The exclusive use requirement is one that has also been traditionally and statutorily applied to tax-free sales to state or local governments. In those instances, a sale for the 'exclusive use' of a state or local government has been identified as a sale of an article that is not for resale by the state or local government. Thus, should a state resell an article to a state resident or a state employee for his or her private use, the state would not be entitled to purchase the article tax free. (But see [Rev. Rul. 73-542, 1973-2 C.B. 541](#), which allows tax free sales to bus owner-operators that operate the buses under employment contracts with a county school board). If, prior to January 1, 1988, gasoline was purchased tax free, and thereafter sold or used (prior to use by the state) under circumstances that did not amount to an exclusive use, the state must inform the manufacturer, producer, or importer from whom the gasoline was purchased that the gasoline was disposed of in a manner that did not amount to an exclusive use by the state. See sec. 48.4221-5(d) of the Manufacturers and Retailers Excise Tax Regulations. If diesel fuel was purchased tax free and thereafter similarly sold or used, the state would be liable for tax under section 4041(a)(1) of the Code.

ISSUE 2

As indicated previously herein, for purposes of defining 'essential governmental purposes' after October 13, 1987, [section 7871\(e\)](#) of the Code controls. Such definition is more restrictive than the regulatory definition that controls for periods on and before such date. Although in many instances X's economic subsidiaries provide funding to tribal government programs that in turn provide essential governmental functions, i.e., government administration, health and welfare, etc., the facts indicate that, in most cases, it is the subsidiaries that are involved in the purchases of fuels and not any organizations administering the tribal programs. The activities of most of the subsidiaries, such as logging, agricultural and general retail operations, are obviously not to be considered essential governmental functions. The exception is the activities carried on by F. The activities of F are comparable to those activities of a state agency that manages and develops parklands, including the natural and physical resources thereof. Such activities have traditionally been provided by state and local governments and are considered to be associated with the exercise of an essential state governmental function. Inasmuch as the issue is not presented, nor has any documentation been retained, relating to any farm, off-highway or nontaxable uses as those terms are used in sections 6420, 6421, and 6427 of the Code, this memorandum does not address the taxability of fuels utilized by X or its subsidiaries in such operations.

CONCLUSION

1. For those tax periods where tax-free sales of gasoline or diesel fuel to state or local governments are permitted, X may not purchase gasoline or diesel fuel tax free for resale through its service stations to members of its tribe or to the general public.
2. After October 13, 1987, X's tribal subsidiaries, except in the case of F, are not considered to be engaged in 'essential governmental functions'. Accordingly, after such date, where tax-free sales of gasoline or diesel fuel to state or local governments are permitted, X's tribal subsidiaries (except F) would not be permitted to purchase gasoline or diesel fuel tax free for use in their operations.

The April 10, 1985, letter ruling to X is revoked effective October 14, 1987.

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(j)(3) of the Code provides that it shall not be used or cited as precedent.

Temporary or final regulations pertaining to one or more of the issues addressed in this

memorandum have not been adopted. Therefore, this memorandum will be modified or revoked by the adoption of temporary or final regulations to the extent that the regulations are inconsistent with any conclusions in the memorandum. See section 11.03 of [Rev. Proc. 89-2, 1989-1 I.R.B. 21, 28](#). A technical advice memorandum concerning a continuing transaction however, is generally not revoked or modified retroactively if the taxpayer can demonstrate that the criteria in section 11.04 of [Rev. Proc. 89-2](#) are satisfied.

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

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