

INTERNAL REVENUE SERVICE
NUMBER: **INFO 2000-0004**
Release Date: 3/31/2000

Index Number: 4261.00-00

03-14-2000

Dear [REDACTED]

This letter responds to your inquiry dated February 2, 2000, to the Commissioner of Internal Revenue, which forwards correspondence from your constituent, [REDACTED]. [REDACTED] is concerned with a notification he received from his telephone service provider informing him that he would be subject to federal excise tax on frequent flyer mileage he earned as a result of his usage of the provider's long distance services.

The Congress passed a law concerning this tax in 1997, but its effects are somewhat different from that described by the service provider. As part of the Taxpayer Relief Act of 1997, section 4261(e)(3) was added to the Internal Revenue Code. Under that section, any amount paid for the right to award frequent flyer miles is subject to an excise tax.

Thus, when a telephone service provider purchases the right to award frequent flyer miles to a customer, it pays the tax to the air carrier selling the miles. The air carrier then pays the tax over to the United States. Because the customer is not paying any amount for the right to award frequent flyer miles, this tax does not apply to the transaction between the customer and its telephone service provider. The telephone company may be showing on its invoice to the customer an amount representing the tax that was paid on its purchase of the frequent flyer miles from the air carrier, but the tax, as enacted by the Congress, does not apply to the customer's receipt of the miles as a consequence of its purchase of telephone services.

This tax, as well as several other federal excise taxes relating to air transportation, is paid into the Airport and Airway Trust Fund (the Trust Fund). Amounts in the Trust Fund are used to plan, construct, develop, operate, and maintain air traffic control, air navigation, and communications for the airway system. In addition, certain portions of the budget of the Department of Transportation concerned with air transportation and air safety, including over half of the expenditures of the Federal Aviation Administration, come from the Trust Fund.

I hope this information is helpful to you in responding to your constituent. If you have any questions, please contact [REDACTED]

Sincerely,

Assistant Chief Counsel
(Passthroughs and Special Industries)

By:

Richard A. Kocak
Chief, Branch 8

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