



COLORADO
Department of Revenue

Taxation Division

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GIL-15-014

May 28, 2015

XXXXXXXXXXXXXXXXXX
ATTN: XXXXXXXXXXXX
XXXXXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXX

Re: Sales Taxability of Federal Excise Tax on Aviation Fuel Later Refunded to Customers

Dear XXXXXXXXXXXX,

You submitted on behalf of XXXXXXXXXXXX ("Company") a request for guidance to determine whether an airline who received a refund of federal excise tax is entitled to a refund of state sales tax paid on the amount of federal excise tax refunded.

The Colorado Department of Revenue ("Department") issues general information letters and private letter rulings. A general information letter provides a general overview of the relevant tax issues but is not binding on the Department. A private letter ruling provides a specific determination for a specific set of facts, is binding on the Department but not on the taxpayer, and requires payment of a fee. For more information about general information letters and private letter rulings, please see Department Regulation 24-35-103.5 at www.colorado.gov/revenue/tax > Tax Library > Rulings.

The Department treats this request as one for a general information letter. It is important to remember that general information letters, such as this one, are general discussions of tax law and are not binding on the Department. If a retailer would like the Department to issue a private letter ruling on the issue raised here, the retailer can resubmit a request and fee in compliance with Department Regulation 24-35-103.5.

Issue

1. An airline receives a refund of federal excise tax paid on an earlier purchase of aviation fuel. Would the airline be entitled to a refund of state sales tax paid on the amount of federal excise tax refunded?
2. If so, should the aviation fuel supplier refund the state sales tax to the airline directly or should the airline seek the refund from the Department?

Background

Company is a supplier of aviation fuel and services. Company charges its customers both federal excise tax and Colorado state sales tax on its sales of aviation fuel. One of its customers is an commercial airline ("Airline") which requests a refund of state sales tax paid on refunded federal excise tax for aviation fuel it purchased.

Company purchases aviation fuel from a supplier. The Internal Revenue Service ("IRS") levied a federal excise tax ("FET") of \$.244/gal on this sale. Company passed on the full cost of the FET on the aviation fuel to Airline. Company also charged Airline state sales tax on the full purchase price of the sale, including the FET. Airline is registered with the IRS as a "commercial airline." Aviation fuel used in commercial aviation is subject to a \$.044/gal FET. Airline is eligible for a \$.20/gal refund from the IRS. Airline is requesting that Company credit them for state sales tax paid on this exempted amount ("Refundable Amount").

Discussion

1. *Taxability of the Refundable Amount*

Company's sales of aviation fuel to Airline are subject to Colorado sales tax.¹

Generally, the United States levies by default a \$.244/gal FET on the sale, removal, or entry of kerosene, including special kerosene blends used as aviation fuel.² The incidence of taxation is the removal of the kerosene from either a refinery or terminal rack (distribution facility).³ The aviation fuel supplier removes the kerosene from the refinery or terminal rack and is, thus, directly liable for the FET. The supplier can sell aviation fuel directly to the aircraft operator or it can act as a wholesaler and sell the aviation fuel to a retailer who in turn sells the fuel to an aircraft operator. Nonetheless, the incidence of the FET is always on the party that removes the fuel from the refinery or terminal rack regardless of the many parties the aviation fuel passes through before reaching the ultimate purchaser. In contrast, the incidence of state sales tax always falls on the last step in the transaction - the retail sale of the aviation fuel from the retail supplier to the aircraft operator.⁴

In some instances, the aircraft operator itself can be the direct payor of the FET. If an aircraft operator is registered with the IRS as a "commercial airline"⁵ and the aviation fuel is directly removed from the terminal rack into the fuel tank of the aircraft operator's aircraft, an FET of only \$.044/gal for commercial aviation is levied on the sale and the aircraft operator is directly liable for the FET. However, this situation is not the general rule. It applies only to certain "secure" airports where the aviation fuel supply chain is tightly controlled to limit diversion of aviation fuel to non-aviation uses.⁶

If the aviation fuel is *not* directly removed into the aircraft operator's aircraft, the default FET of \$.244/gal is initially levied on aviation fuel supplier. If the aircraft operator is registered as a commercial airline and it used the aviation fuel for commercial aviation purposes, the \$.044/gal commercial aviation rate is achieved through a refund of \$.20/gal to either the aviation fuel vendor or the aircraft operator. If the aviation fuel vendor passes on the cost of the full \$.244/gal default FET to the aircraft operator, the aircraft operator may seek a

¹ § 39-26-715(1)(a)(I) C.R.S.

² See IRS Publication 510 (Rev. July 2013), pg. 7; I.R.C. § 4081(a)(2)(A)(iii)

³ See IRS Publication 510 (Rev. July 2013), pg. 8; I.R.C. § 4081(a)(1)(A)(ii)

⁴ See § 39-26-104(1)(a), C.R.S.; 1 CCR 201-4, Reg. 26-102.9

⁵ | RS Notice 2005-4, 2005-1 CB 289

⁶ See IRS Publication 510 (Rev. July 2013), pg. 10-11; I.R.C. § 4081(a)(2)(C)(i). As of 2015, this particular scenario only applies to two airports in Colorado. See IRS Notice 2005-4, 2005-1 CB 289. For the treatment of state sales tax in this situation, consult General Information Letter, GIL 14-004 available at www.Colorado.gov/pacific/tax/letter-rulings.

\$.20/gal refund from the IRS.⁷ Company follows this practice. If the vendor passes on only \$.044/gal of the full \$.244/gal FET to the aircraft operator, the aircraft operator would waive its right to a refund and assign that right to the aviation fuel vendor.⁸ In either case, the aircraft operator effectively pays an FET rate of \$.044/gal. In both cases, the \$.044/gal FET is subject to state sales tax. However, in the first case the aircraft operator would, at least initially, pay a higher state sales tax because the full default \$.244 FET is included in the purchase price.

We start with the general rule that sales tax is a transactional tax. This means the tax is assessed based on the facts that existed at the time of the transaction is entered into. Any events that occur after the transaction generally do not affect the taxability of the transaction.⁹ The initial purchase price, including any indirect costs such as excise taxes paid by the retailer or manufacturer,¹⁰ determines the amount of sales tax paid by the purchaser. The parties cannot retroactively adjust this price in light of subsequent events.¹¹ This principle is usually applied when a retailer retroactively lowers the initial purchase price as compensation for damages or provides a discount as an inducement to accelerate payments on an installment plan.

However, this situation is somewhat different from the general rule. It is not a price adjustment based on a subsequent, unanticipated contingency or a later discretionary act by the buyer or seller. Instead, it is based on a non-contingent price adjustment. It is more like an exemption than a subsequent price adjustment.

The Airline's initial purchase of the aviation fuel and the subsequent FET refund can be thought of as one transaction: the purchase of aviation-grade kerosene for its use as fuel for commercial aircraft. Airline was registered with the IRS as a "commercial airline" when it initially purchased the aviation fuel from Company. At the time of the transaction, Airline purchased the kerosene for its value as fuel for commercial aviation use. As long as the aviation fuel was actually used for commercial aviation purposes, Airline was always entitled to a partial refund of the FET from the time of the purchase. The default FET rate was levied on the initial sale of the aviation fuel as an administrative measure to prevent diversion of the aviation fuel to non-aviation uses. Therefore, the Refundable Amount is more like bond or refundable security deposit than an actual part of the purchase price. The IRS only withholds the Refundable Amount until it receives proof that the aviation fuel was actually used for commercial aviation. It is not part of the purchase price of the transaction. A refund of the state sales tax paid on the Refundable Amount would reflect this reality.

As a way of illustrating this principle, suppose that Airline had waived its right to the FET refund and assigned it to Company. Company would have paid the default \$.244/gal rate upon removal from the terminal rack but assessed Airline only \$.044/gal of the FET cost but *not* including the other \$.20/gal FET cost in the purchase price. Therefore, Airline would

⁷ See I.R.C. § 6427(l)(1), (4); Joint Committee on Taxation, *Technical Explanation of H.R. 6408, The "Tax Relief and Health Care Act of 2006," as Introduced in the House on December 7, 2006* (JCX-50-06), Dec. 7, 2006.

⁸ See IRS Publication 510 (Rev. July 2013), pg. 16; I.R.C. § 6427(l)(1), (4).

⁹ See generally *S. Cal Edison v. State Bd. of Equalization*, 7 Cal. 3d 652, 102 Cal. Rptr. 766, 498 P.2d 1014 (1972) (retailer not entitled to sales tax relief for price adjustment subsequently made after sale and based on damages paid by retailer to purchaser).

¹⁰ 1 CCR 201-4, Reg. 39-26-102.7(a)(1), (7).

¹¹ See §§ 39-26-102(7)(a) and 39-26-104(1)(a), C.R.S.

never have paid state sales tax on the Refundable Amount because it was never included in the purchase price to begin with. Instead, Company would have been entitled to the FET refund. By contrast, in the transaction in question, Airline would pay the same sales tax only if it received a refund of the state sales tax on the Refundable Amount. Without this refund, Airline would be in effect paying a higher state sales tax on a functionally equivalent transaction.

Our guidance here is similar to that given in GIL-07-033. There, a beer manufacturer sold product to a beverage wholesaler who would either resell the product to beverage retailers or would agree to provide the product as samples to consumers. The beer manufacturer charged a lower price for product used as samples and would subsequently credit distributor the price difference for the portion of product used for sample purposes. We advised distributor that it could use the final discounted purchase price for samples originally recorded at the higher price and that such a post-sale price adjustment was not a change based on subsequent events but, rather, a correction of what was intended as the original price. We think the same result applies here with respect to the aviation fuel price adjustment.

2 Either the Airline or Company may apply for the Refund of sales tax.

Section 39-26-703, C.R.S. authorizes either the buyer to claim a refund or the retailer to claim a credit on its sales tax return if it refunds the sales tax to the buyer. Thus, in this case, either the Airline or Company may effectuate the refund, at the Company's election.

Miscellaneous

This letter represents the good faith opinion of Department personnel who are knowledgeable on state taxes issues. However, the Department does not make a specific determination here on any of the issues raised and the Department is not bound by this general information letter.

The Department administers state and state-administered local sales and use taxes. This letter does not address sales and use taxes administered by home-rule cities and home-rule counties. You may wish to consult with local governments, which administer their own sales or use taxes about the applicability of those taxes. Visit our web site at www.colorado.gov/revenue/tax for more information about state and local sales taxes.

Enclosed is a redacted version of this letter. Pursuant to statute and regulation, this redacted letter will be made public within 60 days of the date of this letter. Please let me know in writing within that 60-day period whether you have any suggestions or concerns about this redacted letter.

Sincerely,

Neil L. Tillquist
Colorado Department of Revenue