eOffice of Chief Counsel
Internal Revenue Service
memorandum

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to: Air Transportation Industry Counsel
Office of Division Counsel
(Large Business and International)

from: Curt Wilson
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(Passthroughs & Special Industries)

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subject: Section 4271 - Tax on Transportation of Property by Air

This Chief Counsel Advice responds to your request for assistance dated July 6, 2010. This advice may not be used or cited as precedent.

LEGEND

Parent =

Organizer =

Carrier =

Retailer =

ISSUE

Who is the taxpayer and who is the collector for purposes of § 4271 of the Internal Revenue Code (the Code) in the facts described below?

CONCLUSION

The related party Organizer is the taxpayer and Carrier is the collector for purposes of § 4271 of the Code in the facts described below.

FACTS

Parent is a corporation in the business of transporting property. Among other subsidiaries that it owns, Parent wholly owns Carrier and Organizer, and Organizer wholly owns Retailer (collectively, "Subsidiaries"). Parent and each of its Subsidiaries are separate legal entities.

Retailer receives property from unrelated third-party customers (Customers), delivers property scheduled for air transportation to the airport by truck, loads and unloads aircraft operated by Carrier, sorts the property at different stages of transportation in facilities operated by Parent or its Subsidiaries, and delivers the property by truck to its ultimate destination.

Carrier provides transportation of property by air, including flying and maintaining the aircraft and providing qualified pilots, crew, and maintenance staff. Carrier owns and leases a large number of aircraft for transporting property by air. Carrier receives most of the property it transports from Organizer.

Organizer does not physically transport any property; rather, it coordinates all aspects of the movement of the property from origin to destination, including scheduling (such as holiday or expedited delivery) and volume management. To that end, Organizer has entered into agreements with Carrier, Retailer, and various unrelated air carriers. The unrelated air carriers account for a minimal amount of Carrier's costs for transportation by air. The remainder of Organizer's costs for transportation by air is attributable to services provided by Retailer.

Under the agreements, Carrier employs qualified pilots and crew; Carrier also is responsible for aircraft maintenance, flight document preparation, aircraft fuel and oil, and pays all airport landing, parking, ramp, and servicing fees. Organizer also engages in a wide variety of activities related to transportation by air, such as air network planning and production flow, airport slots, and aircraft acquisition.

Customer pays Retailer a fee that is based on how quickly Customer wants its property delivered to its ultimate destination. The fee paid by Customer to Retailer includes the cost of both ground and air transportation (if air transportation is required to meet the delivery deadline). If the delivery plan for Customer's property includes the use of aircraft, Retailer allocates the entire fee it collected to Organizer. Retailer then charges Organizer for its costs associated with ground transportation of the property. Under its

contracts with Carrier, Organizer reimburses Carrier for its cost to carry property by air, plus a percentage markup.

When Customer delivers property to Retailer, Customer will generally not know that the Subsidiaries are different legal entities because they operate as one delivery business that is identified by a single brand name. For example, the published fees for the services do not inform Customers shipping property by air that Carrier and Organizer are legal entities separate from Parent.

LAW AND ANALYSIS

Section 4271(a) of the Code imposes upon the amount paid for taxable transportation of property by air a tax equal to 6.25 percent of the amount so paid. The tax applies only "to amounts paid to a person engaged in the business of transporting property by air for hire." The rule of the previous sentence is restated in § 49.4271-1(b)(1) of the Facilities and Services Excise Tax Regulations. These regulations provide that the tax applies, for example, to amounts paid to an air carrier by a freight forwarder or express company for the transportation of property by air, but does not apply to amounts paid by a shipper to a freight forwarder or express company. Thus, the tax does not apply to amounts paid to a person to facilitate or otherwise arrange the transportation of property by air unless that person is directly engaged in the business of transporting property by air.

Section 4271(b)(1) generally provides that the tax imposed by subsection (a) shall be paid by the person making the payment subject to tax (the taxpayer) and § 4291 generally provides that every person receiving any payment for transportation of property by air shall collect the amount of the tax from the person making such payment (the collector). Section 49.4271-1(f) of the regulations further provides that the tax is collected by the person engaged in the business of transporting property by air for hire who receives such payment (with a limited exception relating to the U.S. Postal Service).

Section 4272 provides that the term "taxable transportation" generally includes transportation by air which begins and ends in the United States.

The facts presented raise two questions: (1) who is the person engaged in the business of transporting property by air for hire under § 4271(a), and therefore the collector, and (2) who is the person making the payment subject to tax under § 4271(b), and therefore the taxpayer?

Parent holds itself out as in the business of providing transportation of property, including by air, for hire. Parent has organized its business in such a way, however, that each component of its delivery system (that is, Carrier, Organizer, and Retailer), is a separate legal entity under local law. You have also indicated that Parent and Subsidiaries are recognized as separate legal entities for federal tax purposes. See § 301.7701-2 of the Procedure and Administration Regulations.

The average shipping customer generally does not know that Parent and its subsidiaries are separate legal entities because they operate as one delivery business identified by a single brand name. Similarly, Parent files a consolidated income tax return for itself and its subsidiaries. For purposes of administering the federal excise tax on the transportation of property by air, however, neither the Code nor the applicable regulations allow a consolidated excise tax return. Neither the customer's perception nor the fact that Parent and its subsidiaries are related entities in a controlled group that is generally identified by a single name are factors in determining the statutory taxpayer and collector for excise tax purposes under § 4271. Therefore, the affiliated nature of the relationship between the entities and the customer's perception are not material to this analysis.

Generally, in the Chapter 33 excise taxes, including § 4271, the term "person" refers to each separate legal entity recognized for federal tax purposes. For example, the proposed regulations under § 40.0-1(d) of the Excise Tax Procedural Regulations (73 FR 43890) provide that business units (for example, a parent corporation and a subsidiary corporation, a proprietorship and a related partnership, or the various members of a consolidated group) are separate persons. This interpretation reflects a plain reading of § 7701(a)(1) (defining the term "person" for purposes of Title 26) and §§ 301.7701-1 and 301.7701-2. This interpretation is also supported by a long line of judicial precedent including the Supreme Court's holding in Moline Properties, Inc. v. Comm'r, 319 U.S. 436 (1943) (recognizing the "doctrine of corporate entity" and a corporation's status as a separate taxable entity for federal tax purposes). Parent, Carrier, Organizer, and Retailer are separate corporate entities and, for purposes of this analysis, it is not relevant that Carrier, Organizer, and Retailer are "brother-sister" subsidiaries of Parent. Thus, Parent, Carrier, Organizer, and Retailer are separate persons for purposes of applying § 4271.

Who is the collector?

To determine who is the collector in this case, we consider two elements of § 4271(a). Section 4271(a) applies to (i) amounts paid for taxable transportation of property by air that are (ii) paid to a person engaged in the business of providing transportation of property by air for hire. Although the calculation of the tax base is not under consideration in this case, generally, for purposes of the first element of § 4271(a), the "amount paid" for taxable transportation of property by air must relate to a payment for air transportation. In this case, there is no dispute that payment for air transportation occurs. To meet the first element of § 4271(a), however, the amount paid must be paid for "taxable transportation."

Who provides the taxable transportation of property by air?

Taxable transportation, as defined in § 4272, includes domestic transportation by air. Section 4261 (taxable transportation of persons by air), like § 4271, provides that an

amount paid is taxable only if it is paid for taxable transportation. Thus, guidance under § 4261 on this issue is relevant for determining whether an amount paid is for taxable transportation of property by air for purposes of § 4271. To determine whether a person provides taxable transportation for purposes of the excise taxes imposed on transportation by air, the person must retain "possession, command, and control" of the aircraft. Thus, Rev. Rul. 60-311, 1960-2 C.B. 341, holds that where the owner of an aircraft leases it to others for the transportation of persons by air but retains possession, command, and control of the aircraft, the owner is furnishing a taxable transportation service under § 4261, but where the owner transfers the complete possession, command, and control of the aircraft to a lessee, either by a charter-party or by actual practice, the owner is not engaging in a taxable transportation service but is merely leasing the aircraft. In Rev. Rul. 60-311, a helicopter rental company made available to the lessees helicopters that met the specifications of the lessees, pilots, experienced mechanics and maintenance. The lessees made decisions as to the time and place for operations, but the rental companies controlled load limits, decisions on whether to fly in given weather conditions, etc. The revenue ruling reasoned that because the helicopter rental company maintained possession, command and control of the helicopters and performed all services in connection with their operation, the rental companies were furnishing taxable transportation to the lessees, not merely leasing the helicopter.

In this case, Carrier provides aircraft, pilots, mechanics and maintenance, like the helicopter rental company in Rev. Rul. 60-311. You have asked, however, whether Organizer is the person that actually retains possession, command, and control of the aircraft because Organizer has far more indicia of control than the lessees in Rev. Rul. 60-311. Control over what cargo Carrier transports, control over the aircrafts' destinations, control over loading and unloading of cargo, and control over the timing of departures, and other scheduling decisions is not determinative of possession, command, and control for purposes of this issue, however.

In this regard, we think Rev. Rul. 76-394, 1976-2 C.B. 355, provides relevant guidance. In Rev. Rul. 76-394, X company provided air transportation services for a number of entities whose controlling shareholders also owned the stock of X. X company owned the aircraft and the pilot and crew were employed by X. Hiring of the pilot and crew was subject to the concurrence of the other entities, however. While the overall disposition of the aircraft was under the control of X company, the aircraft was operated at the direction of the related entity using the aircraft for any particular flight, subject to the discretion of the X company pilot as to safety requirements. All the other entities shared in the annual operating expenses of the company based on their percentage of use, and paid their share to X. Citing to Rev. Rul. 60-311 and Rev. Rul. 68-343, 1968-1 C.B. 491 (which involved similar facts), Rev. Rul. 76-394 concludes that X company has the essential elements of possession, command, and control of the aircraft at all times because X company owns the aircraft, employs the pilot and crew, and provides their services with the aircraft, irrespective of the fact that the other entities direct the pilot as to destination and other details concerning actual flights when using the aircraft.

In this case, Carrier owns (or leases) the aircraft at issue, employs the pilot and crew, and provides the services of the pilot and crew with the aircraft under the terms of the agreements with Organizer. As in Rev. Rul. 76-394 and Rev. Rul. 60-311, a person other than the owner and operator of the aircraft, in this case Organizer, directs the pilot as to destination and other details concerning actual flights. Nevertheless, Carrier retains the essential elements of possession, command, and control and is the person that provides taxable air transportation under the rationale of Rev. Rul. 76-394, irrespective of the fact that Organizer directs other details concerning actual flights when using the aircraft. Therefore, we conclude that Carrier is the person that provides taxable transportation of property by air.

You have asked us to consider whether Rev. Rul. 75-296, 1975-2 C.B. 440, supports a different conclusion. Rev. Rul. 75-296 compares the situation of two travel agencies for purposes of § 4261 and § 4291. The first travel agency is an independent broker that sells tours in aircraft it charters from airlines. The first travel agency is not under the supervision or control of any airline, and prescribes the time of departures, the origin, and the destination of the chartered flights. The revenue ruling concludes that the first travel agency is required to collect the transportation tax, file returns, and pay over the tax to the government, because the first travel agency is acting as a principal, and thus is a person receiving payment under § 4291. This is consistent with § 49.4261-7(h)(2) of the Facilities and Services Excise Tax regulations, which provides that the charterer of a conveyance that sells taxable transportation to other persons must collect and account for the tax with respect to all amounts paid to it for transportation.

In contrast, Rev. Rul. 75-296 concludes that the second travel agency is an agent of an airline because it is under the supervision and control of the airline, and therefore must collect the tax and remit it to the airline for the filing of returns and payment of the tax. Thus, under the rationale of the revenue ruling, the airline is the person responsible for filing the returns and paying the tax to the government in the second situation, even though the second travel agency must collect the tax on behalf of the airline.

We do not think that the holding in Rev. Rul. 75-296 governs this case. The regulations relating to chartered conveyances in § 49.4261-7(h) specifically apply to the transportation of persons; there is no similar provision in the regulations under § 4271 relating to chartered conveyances applicable to the transportation of property. We attribute that difference in the regulatory structure between the regulations under § 4261 and § 4271 to the difference in the statutory provisions--§ 4271, unlike § 4261, limits its application to amounts paid to a person engaged in the business of transportation by air, as discussed below. Because § 4261 does not have a similar requirement (unlike the identical statutory provisions relating to “taxable transportation”), the travel agency in Rev. Rul. 75-296 did not have to be engaged in the business of taxable transportation by air in order to expose itself to responsibility to collect the tax under § 4261 as a person who received payment for air transportation services within the meaning of § 4291. Further, unlike the travel agencies in Rev. Rul. 75-296, Organizer is not an agent under the supervision and control of Carrier. Instead, Organizer and Carrier are

related parties. Carrier owns aircraft and Carrier's employees actually fly and maintain the planes. Under Rev. Rul. 76-394, that is enough to treat Carrier as the person that provides taxable transportation, regardless of the level of control exercised by Organizer over Carrier. Additionally, Organizer is not under the supervision and control of Carrier and therefore is not considered the agent of Carrier under Rev. Rul. 76-394. Therefore, we conclude that the holding of Rev. Rul. 76-394 (relating to related entities) is more relevant than the holding of Rev. Rul. 75-296 (related to principals and agents) in the present case, for purposes of determining who is providing the taxable transportation. Thus, for purposes of the first element of § 4271(a) (amounts paid for taxable transportation of property by air), Carrier is the person providing taxable transportation of property by air.

The analysis does not end here, however, because we must also determine who is engaged in the business of transporting property by air for hire under the second element of § 4271(a).

Who is engaged in the business of transporting property by air for hire?

For purposes of indentifying the collector, we also apply the second element of § 4271(a), to determine who is engaged in the business of transporting property by air for hire. As noted above, identifying the taxpayer and collector under § 4271 (transportation of property by air) is different than identifying their counterparts under § 4261 (transportation of persons by air) because the second element of § 4271(a) (unlike § 4261) provides that the tax applies only to amounts paid to a person engaged in the business of transporting property by air for hire. The statute is designed to make the person actually engaged in the business of transporting property by air the person responsible for collecting the tax. This is evidenced by, among other things, the example in § 49.4271-1(b)(3) of the regulations, providing that the tax applies to amounts paid to an air carrier by a freight forwarder or express company for the transportation of property by air, but not to amounts paid by a shipper to a freight forwarder or express company. Because the affiliated nature of the relationship between the entities is not material to this analysis, as discussed above, the amounts paid by Organizer to Carrier, like the amounts paid by the freight forwarder to the air carrier in the regulations, are for transportation of property by air. Thus, Organizer is not the collector.

Carrier is a person engaged in the business of transporting property by air for hire both with respect to property transported for Organizer and property transported for other shippers. This is so even though a customer may not be aware that Carrier, not Parent, is the person that provides the service (because of the integrated nature of the provision of the service); even though a minimal amount of cargo space is actually sold to the public; and even though Organizer exercises a great deal of control over the timing, destination, and other aspects of Carrier's services. Consequently, Carrier is engaged in the business of transporting property by air for hire. Carrier meets both elements of § 4271(a) because Carrier provides taxable transportation and is engaged in the

business of transporting property by air for hire. Thus, Carrier is the collector under § 4291 and § 49.4271-1(f) of the regulations and is required to collect the tax from the taxpayer.

Who is the taxpayer?

To determine who is the taxpayer, § 4271(b)(1) provides that the § 4271 tax shall be paid by the person making the payment subject to the tax; that is, the person making the payment to the person engaged in the business of transporting property by air for hire. Organizer has entered into agreements with Carrier to pay for transportation of property by air. Carrier bills Organizer for its services and Organizer effectuates the transfer of funds for the services. Organizer is a "person" within the meaning of § 4271(b)(1). Organizer is the person making the payment subject to the tax. Thus, Organizer is the taxpayer under § 4271(b)(1).

This memorandum does not address the tax base on which the 6.25% tax is to be applied.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

We hope this memorandum has addressed the questions you raised concerning the excise tax under § 4271. Please call (202) 622-3130 if you have any further questions regarding this matter.