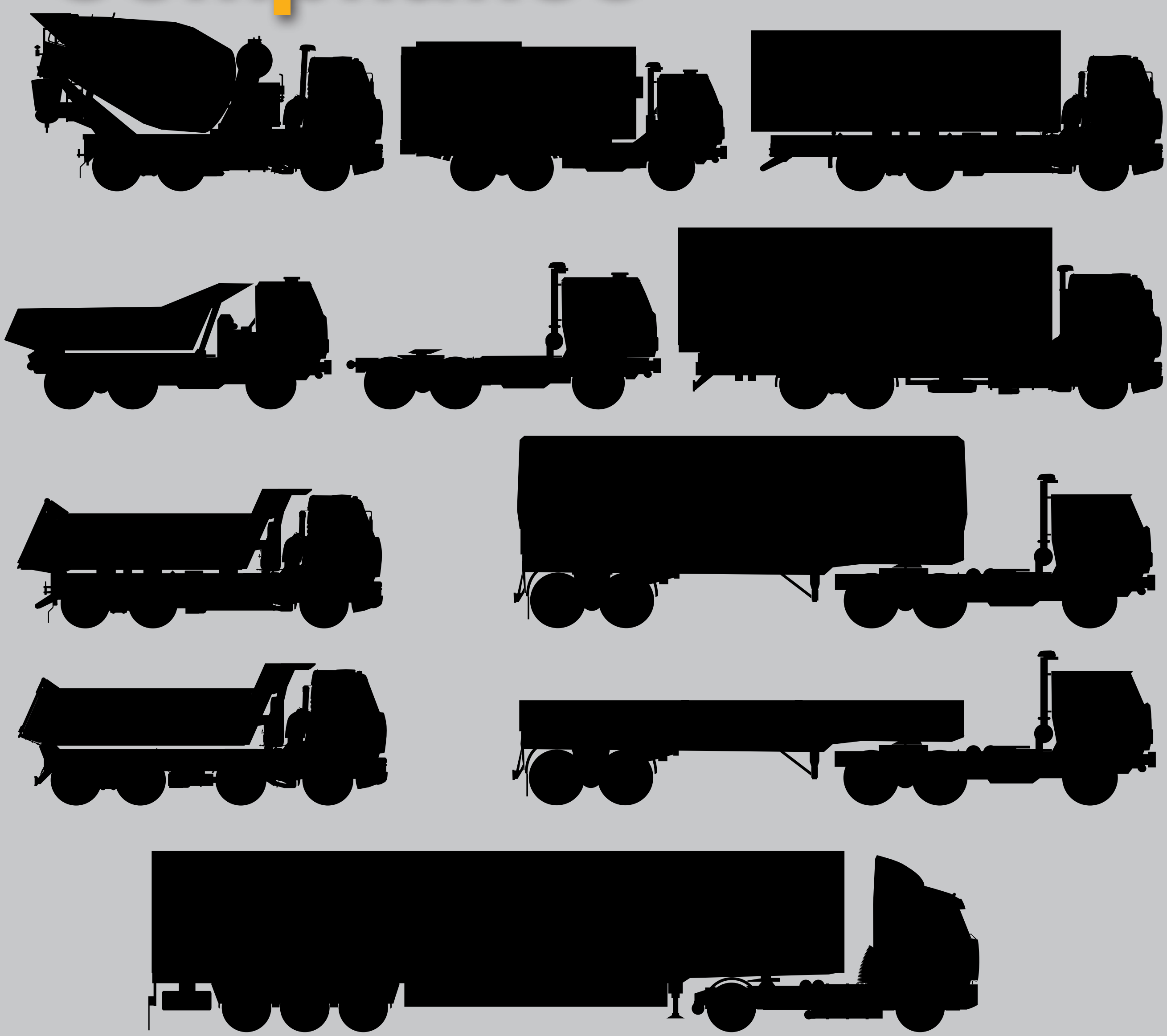
Driven

NADA MANAGEMENT SERIES

A DEALER GUIDE TO

Federal Excise Tax Compliance



NADA-ATD Resource Toolbox

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A DEALER GUIDE TO

Driven Federal Excise Tax Compliance

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A DEALER GUIDE TO
Federal Excise Tax Compliance

I. EXECUTIVE SUMMARY: OVERVIEW OF FET—THE BIG PICTURE

“Excise—A hateful tax levied upon commodities, and adjudged not by the common judges of property, but wretches hired by those to whom excise is paid.”

—Samuel Johnson
A Dictionary of the English Language (1755)

A. Introduction

The United States imposes excise taxes on a variety of commodities and services. The list of items subject to excise tax runs the gamut from the ridiculous (artificial fishing lures) to the sublime (reinsurance premiums). Unfortunately for sellers of commercial and vocational vehicles (or “work trucks”), truck, trailer, and semitrailer bodies and chassis and truck tractors have been subject to federal excise tax (FET) for more than a half-century.

The current version of FET, which is contained in the Internal Revenue Code (IRC), provides for a punishing 12 percent tax on the “first retail sale” of a taxable body, chassis, or tractor. This substantial tax can not only depress potential sales of new work trucks, it is also confusing and difficult to apply because it applies to some bodies, chassis, and tractors but not others. This can lead to disparities when some sellers make aggressive tax determinations (*i.e.*, that an article is non-taxable) and thereby enjoy a 12 percent price advantage over their more conservative competitors who deem an item as subject to the tax because they are unwilling to risk an IRS audit. The subjective nature of the tax can create “gray areas” which are highly problematic for truck dealers and others who routinely buy or sell potentially taxable work trucks, trailers, and truck tractors.

The FET provisions are contained, for the most part, in just three sections of the Internal Revenue Code: IRC §§ 4051-53. At first glance, these relatively short code sections do not look particularly complicated. However, in practical application, the tax is quite complex and unclear in some crucial respects. The goal of this guide is to provide information to retail sellers of work trucks to enable them to apply the tax correctly in instances in which the rules are clear, and to make reasonable risk assessments regarding the tax in instances in which the rules are unclear.

B. The Fundamentals

Basic application of the FET involves a three-part analysis:

1. Is the article being sold the *type of article* that is subject to the tax?
2. If so, is the sale of the article in question the *type of sale* that triggers the tax?
3. If so, what *portion of the price* charged in the transaction in question is subject to the 12 percent tax?

As discussed in detail in the sections that follow, each of these inquiries has its own set of complexities. For example, the first part of the analysis—whether an article is the type of article subject to the FET raises issues such as:

- The gross vehicle weight rating of a truck body
- The "primary design" of a vehicle that is used to some significant extent for off-highway use
- Whether a vehicle is designed "solely" for use as a mobile mount for machinery if it also has the incidental capability of carrying small tools or other such items
- Whether a remanufactured article has been altered to the extent that the IRS will treat it as a "new" article for tax purposes

The second question—whether a particular sale of a taxable item is a taxable "first retail sale"—likewise presents challenges, such as:

- Determining if the article was involved in a prior, potentially taxable sale
- Whether the purchaser of the article is eligible to purchase on a tax-free basis and, if so, whether the purchaser has complied with any necessary registration and certification requirements
- Whether the installation of a part or accessory on a used vehicle triggers the so-called "Six-Month Rule"
- Whether a particular use of an article prior to its "first retail sale" (such as use as a demonstrator vehicle) triggers tax

Once it is determined that the article being sold is taxable, and that the sale (or use) of the article is one that triggers tax, the taxpayer must then compute the taxable price that is subject to the 12 percent tax. This third question, like the others, can be quite complicated. It can involve:

- Determining the amount, if any, of installation charges and delivery charges that can be deducted from the taxable price
- Computing "constructive sales prices" for sales of taxable articles to affiliated companies
- Computing "presumed markup percentages" for certain retail sales by manufacturers or importers

As discussed in Section IX, the computation of the tax due on a taxable sale often will be more complicated than simply multiplying the retail sale price of an article by 12 percent.

This guide presents a discussion of the crucial FET issues faced by retailers of truck, trailer, and semi-trailer bodies and chassis and truck tractors, and is based on the law as of December 2010.[1] Please be aware that in every case, the application of the FET depends on the particular facts of the article being sold and the transaction in which it is sold. Often, the FET is difficult to apply and does not yield an obvious answer as to whether a retail seller should charge tax or not in a particular transaction. In many cases, the best available guidance is found in informal guidance from the IRS called "Letter Rulings," and "Technical Advice Memoranda" (TAMs).[2] Such guidance is issued by the IRS but generally cannot be relied upon by any taxpayer other than the taxpayer who requested or is the subject of such a ruling. As a result, truck dealers must consult periodically with their tax advisors to seek guidance on what articles and sales are subject to the FET. Also, due to the fact-specific nature of the FET, retailers should not treat the information in this guide as advice in any particular transaction.

II. HOW FET WORKS— THE BASIC CONCEPTS

In order to understand when and how to apply the Federal Excise Tax (FET), the taxpayer first needs to be familiar with some basic concepts regarding how the tax works. The six important concepts that will be discussed in this section are:

1. The types of items that may be subject to FET
2. The calculation of a vehicle's gross vehicle weight
3. An item's "suitability for use" with vehicles below the taxable gross vehicle weight level
4. The determination of whether a part or accessory is taxable
5. The person or entity that is responsible to pay the tax
6. The effect a prior taxable sale has on the taxability of an item

A. Items that are Subject to FET

1. Certain Trucks, Trailers, Semitrailers, Tractors, and Parts and Accessories

There are four basic categories of items that may be subject to FET (under IRC § 4051):

- **Automobile truck chassis and bodies** that are not *suitable for use* with a vehicle that has a gross vehicle weight rating of *33,000 pounds or less;*[3]
- **Truck trailer and semitrailer chassis and bodies** that are not *suitable for use* with a vehicle that has a gross vehicle weight rating of *26,000 pounds or less;*
- **Tractors**[4] that are "chiefly used for highway transportation in combination with a trailer or semitrailer," and that have a gross vehicle weight rating of *more than 19,500 pounds* and a gross combined weight (tractor, plus trailer or semitrailer) of *more than 33,000 pounds.* (The "suitable for use" concept does not apply to tractors.);
- **Parts or accessories** sold on or in connection with a taxable chassis, body, or tractor, or subsequently installed on a vehicle in a manner that triggers the so-called "Six-Month Rule." (For more discussion on parts/accessories, see **Truck versus Tractor** below.)

Determination of a vehicle's gross vehicle weight (a misnomer in light of the fact that a truck body, of itself, is not a "vehicle") and suitability for use with a vehicle below the taxable gross vehicle weight level, are discussed below in B and C. Parts and accessories are discussed in greater detail in D.

In addition, a chassis, body, or tractor will potentially be subject to FET only if it is a component part of a highway vehicle. A highway vehicle is generally defined as "any self-propelled vehicle, or any trailer or semitrailer, designed to perform a function of transporting a load over public highways, whether or not also designed to perform other functions."[5]

If the sale is subject to FET, the tax will be 12 percent of the taxable sales price of the body, chassis, or tractor. Some items and charges may be excluded from the taxable sales price, as discussed below in D and in Section IX.

2. Separate Tax For Separate Items

It is important to keep in mind that chassis, bodies, and parts or accessories are each taxed as separate items under FET; the tax is not applied on a vehicle-by-vehicle basis. In other words, for a single vehicle, the chassis may be taxable, but not the body, the body may be taxable, but not the chassis; or both the chassis and body may be taxable. Similarly, even if the chassis (or body) is taxable, some chassis (or body) parts or accessories may not be subject to tax.

3. Truck versus Tractor

There are many vehicles that have the ability both to carry cargo and tow a trailer or semitrailer. Because the gross vehicle weight threshold for taxable trucks is different from that for taxable tractors, the taxability of an item may depend on whether the IRS treats the item as a truck or a tractor.[6]

The Treasury Regulations define "Tractor[7]" as "a highway vehicle *primarily* designed to tow a vehicle, such as a trailer or semitrailer, *but (sic) does not carry cargo on the same chassis as the engine*."

A vehicle equipped with air brakes and/or a towing package will be *presumed*[8] to be primarily designed as a tractor.

The Treasury Regulations define "Truck[9]" as "a highway vehicle that is *primarily* designed to transport its load on the same chassis as the engine even if it is also equipped to tow a vehicle, such as a trailer or semitrailer."

Simply because a vehicle can carry *any* cargo on the same chassis as the engine does not mean that it is automatically considered a "truck" (and not a tractor). The IRS has expressly rejected this interpretation.[10]

Instead, if a vehicle can both carry cargo on its chassis and tow a trailer or semitrailer, the determination of whether the vehicle is a tractor or truck depends on "which function is of greater importance."[11] In determining which function is most important (*i.e.*, the towing function or the cargo-carrying function), the IRS focuses on the vehicle's physical characteristics, such as its towing capacity, its cargo-carrying capacity and its ability to operate and brake safely when it tows or carries cargo. For example, the IRS has determined that a vehicle was a tractor where its physical characteristics "maximize[d] towing capacity at the expense of carrying capacity."[12]

An incomplete chassis cab may also be treated as a truck or a tractor for FET purposes. An incomplete chassis cab will be treated as a tractor if it is equipped with one or more of these items:

- "A device for supplying pressure from the chassis cab to the brake system (air or hydraulic) of the towed vehicle"
- "A mechanism for protecting the chassis cab brake system from the effects of a loss of pressure in the brake system of the towed vehicle"
- "A control linking the brake system of the chassis to the brake system of the towed vehicle"
- "A control in the cab for operating the towed vehicle's brakes independently of the chassis cab's brakes"
- "Any other equipment designed to make it suitable for use as a tractor"[13]

On the other hand, an incomplete chassis cab will be treated as a truck if:

- It is not equipped with any such items *and*
- The purchaser provides a certificate that the cab "will not be equipped for use as a tractor"[14]

It is unclear whether an incomplete chassis cab is a tractor or a truck if it does not have any of the identified equipment indicative of a tractor, but the seller also does not receive the certificate required for the cab to be treated as a truck. At least one court has concluded that even if the incomplete chassis cab were not equipped with any of the "tractor" items identified in the Treasury Regulations, the cab still would be treated as a tractor, unless the purchaser provided the required certification.[15]

B. Gross Vehicle Weight (GVW) Rating

In order to determine whether chassis, bodies, and tractors are taxable, a taxpayer needs to have a basic understanding of how a vehicle's gross vehicle weight (GVW) is determined. GVW is defined as the "maximum total weight of a loaded vehicle."[16] The seller must establish the GVW of a chassis, body, or vehicle "if such article requires no additional manufacture other than (a) the addition of readily attachable articles, such as tire or rim assemblies or minor accessories (b) the performance of minor finishing operations, such as painting or (c) in the case of a chassis, the addition of a body."[17]

With respect to chassis, most dealers or distributors will simply rely on the GVW rating established by the manufacturer. However, as discussed below, if a dealer or distributor modifies the chassis, such reliance may not be possible. With respect to bodies, GVW ratings are not routinely assigned by the manufacturer.[18] Instead, the GVW rating for a body is determined by applying the "suitable for use" standard, which is discussed below in C.

1. Calculation of GVW

The IRS has provided some guidance on which factors should be included and excluded in calculating the GVW rating of a chassis. The IRS has ruled that in determining the GVW, the manufacturer/seller cannot consider readily attachable components (*i.e.*, springs, brakes, rims and tires), but only the strength of the chassis frame, and the capacity and placement of axles.[19] However, it is not entirely clear if factors other than frame strength and axle capacity and placement may be considered in the calculation of gross vehicle weight, so long as the calculation does not factor in readily attachable components.[20]

In calculating the GVW of a semitrailer, the full weight of the vehicle is not solely supported by the axles, but also by the towing vehicle. Accordingly, the IRS has stated that the weight the towing vehicle supports must be factored into the calculation of GVW.[21] One method for calculating the GVW of a semitrailer is set forth in Revenue Procedure 76-21.[22]

2. Reasonableness Standard and Conflicting GVW Designations

The GVW established by the manufacturer/seller under the guidelines noted above will generally be accepted by the IRS unless it determines that such a weight rating is "unreasonable in light of the facts and circumstances in a particular case."[23] In one example, the IRS determined that a taxpayer's GVW rating for a chassis was unreasonable because the rating did not reflect the subsequent addition of a tag axle.[24]

As noted above, a seller may generally rely on a manufacturer's determination of a vehicle's GVW. However, it is unlikely the seller will be able to rely on that determination if it subsequently modifies the chassis or body in a manner that affects the GVW calculation.[25] A seller also likely will not be able to rely on a manufacturer's GVW if the seller provides a higher rating in its advertisements, invoices, or other documents. The Treasury Regulations expressly state that if the GVW rating on a label or identifying device attached to a chassis, body, or tractor is different from the GVW rating represented in an advertisement, a sales invoice or a warranty agreement, then the IRS will use the highest GVW rating in determining whether FET applies.[26] Although this provision refers only to labels/identifying devices, advertisements, invoices, and warranties, the IRS has indicated that the seller's representation of a higher GVW rating *in any type of document* could be considered the seller's established GVW for tax purposes.[27]

C. What Does "Suitable for Use" Mean?

As noted above, a truck, trailer, or semitrailer chassis or body will be subject to FET only if it is not "suitable for use" with a vehicle that has a GVW rating below a certain GVW level (33,000 pounds for trucks and 26,000 pounds for trailers and semitrailers). "Suitability for use" is defined as *practical and commercial fitness*.[28] That means whether an item is "suitable for use" with a particular weight vehicle is measured by whether such use is reasonable from an engineering perspective and a price perspective.[29] This test is applied separately to the body and chassis of the vehicle.[30]

1. Chassis

In order to determine the suitability for use of a chassis, the IRS generally will look simply to the GVW rating of the particular chassis at issue.[31] As noted above, a dealer generally may rely on the GVW supplied by the manufacturer for an unmodified chassis. If that rating is below the taxable weight threshold (33,000 pounds or less for trucks and 26,000 pounds or less for trailers and semitrailers), then the chassis is suitable for use with such lighter-duty vehicles, and therefore the chassis is not taxable.

2. Bodies

A "suitability for use" determination for a body is more difficult, because "sellers do not routinely ascribe GVW ratings to the bodies they sell."[32] In addition, most truck bodies can be installed on many different chassis that cover a range of GVWs. For example, a 22-foot platform body is commonly installed on single-axle trucks rated 28,000 pounds GVW and on tandem-axle trucks rated 38,000 pounds GVW. Therefore, in order to determine if a body may reasonably be used with a vehicle that weighs less than the taxable weight threshold, the taxpayer does *not* look at the GVW of the chassis on which a particular body is installed in a particular sale. Instead, it looks at all the different types of chassis on which that body model is generally installed.[33] In other words, if the taxpayer installs a truck body on a chassis with a 34,000-pound GVW rating, but that same truck body also is typically installed on chassis with a 32,900-pound GVW rating, that body likely will *not* be taxable. That is because, if a particular body model is determined to be suitable for use with vehicles rated below the taxable GVW level, then *all* sales of that body will be nontaxable, *even when* such body is mounted on a chassis exceeding that weight level in any particular sale.

Unfortunately, the IRS has provided taxpayers with little guidance in determining how much use a body must have with a chassis rated below the taxable weight level in order to satisfy the "suitable for use" test and be nontaxable. In one letter ruling[34] the IRS considered 244 sales of a particular model refuse packer body over a three-year period. Just over 15 percent of these bodies were installed on chassis with GVW ratings of 33,000 pounds or less, and the IRS determined that this particular body was "suitable for use" with vehicles rated 33,000 pounds GVW or below and, therefore, was not taxable in *all* of its sales. However, *the IRS did not adopt any bright line rule*. In other words, the IRS may decide a particular model body that is installed on a chassis rated below the taxable weight level 20 percent of the time is nevertheless taxable, or that a particular body model installed on a chassis rated below the taxable weight level only 10 percent of the time still is not taxable.

This lack of general guidance means that a taxpayer must be prepared to defend its position that a particular body model is suitable for use with a chassis rated below the applicable taxable thresholds (*i.e.*, 33,000 pounds GVW or less for trucks and 26,000 pounds GVW or less for trailers and semitrailers). A taxpayer's best evidence with respect to the "suitable for use" test is its own sales data. However, sales data from manufacturers and other retailers also may be persuasive, *so long as* that sales data concerns the same body model or substantially similar body models. In general, the best way to demonstrate that a particular body model at issue is suitable for use with a vehicle rated below the applicable taxable level is to show (1) a high number of sales of this body model and (2) in a significant percentage of these sales, the body model is installed on vehicles rated below the taxable level. A taxpayer should not simply rely on the percentage. For example, if a taxpayer can demonstrate that a particular trailer body model was installed on a chassis rated 26,000 pounds GVW or less in *35 percent of 250 sales*, that evidence likely will be more persuasive than evidence that a particular trailer body was installed on such a chassis in *40 percent of 10 sales*.

Retail sellers of bodies need to review their sales data periodically and make determinations as to the taxability of those bodies. In addition to the sales data discussed above, retail sellers should consider whether the use of a particular body with a taxable chassis could be characterized as an aberration, based on the existence of special circumstances. Because there is no bright line test for a percentage of sales on nontaxable chassis that will justify tax-free treatment of a particular model body, retail sellers of bodies should work with their tax advisors to determine which bodies should be treated as taxable. Keep in mind that, without clear guidance on this issue, the decision to treat a body as taxable or not simply may depend on the level of risk a retail seller is willing to assume in the event the IRS disagrees with the seller's "suitable for use" analysis.

3. Safe Harbors

For four specific types of bodies, the IRS has eliminated a taxpayer's need to prove suitability for use with vehicles rated below the taxable weight level. In 2005, the IRS issued a Revenue Procedure establishing four safe harbors for certain types of bodies.[35] If a body falls into one of these safe harbors, the IRS "will not challenge [a taxpayer's] determination that [such body] meet[s] the 'suitable for use standard' and sales thereof are excluded from" FET. In other words, if a body satisfies one of the four safe harbors, it should not be taxable under IRC § 4051. These four safe harbors are:

- "Dump truck bodies with load capacities of 8 cubic yards or less"
- "Dry freight and refrigerated truck van bodies 24 feet or less in length"
- "Refuse packer truck bodies with load capacities of 20 cubic yards or less"
- "Platform truck bodies 21 feet or less in length"

NOTE: A body may be nontaxable based on the "suitable for use" test, even if it does not fall into one of these safe harbors. For example, many 24-foot platform bodies likely would be nontaxable under the "suitable for use" test; however, because this body does not fall within the safe harbor, a taxpayer must be prepared to defend this position with sales data, as described above.

D. Parts and Accessories

1. "Sold on or in Connection With"

A part or accessory (defined below) is taxable if it (1) is sold on or in connection with a taxable body, chassis, or tractor, and (2) "contributes toward the highway transportation function" of the taxable body, chassis, or tractor.[36] If a part or accessory is taxable, it is taxed at the same rate as a taxable chassis, body, or tractor—12 percent. Examples of parts or accessories that do contribute to the transportation function (and thus are subject to FET) are:

- Loading and unloading equipment
- Towing winches, and
- All other machinery and equipment contributing to either
  - The maintenance or safety of the vehicle,
  - The preservation of the cargo (other than refrigeration units), or
  - The comfort or convenience of the driver or passengers[37]

If machinery or equipment does not contribute to the transportation function and the taxpayer has sufficient records to support it, FET will not apply to the portion of the sale price that relates to such machinery or equipment, so long as "the reasonableness of the charge…is supportable by adequate records."[38] Some examples of machinery/equipment that do not contribute to the transportation function of a taxable chassis, body, or tractor (and thus are not subject to FET) are:

- Equipment designed to spread materials on the highway[39]
- Car crushing equipment mounted on the chassis of a mobile car crusher[40]
- Lead shields between the body walls of a mobile medical facility[41]
- Certain components of vacuum loaders and sewer cleaners[42]
- Certain components of vehicles that grind traffic lines off the pavement and of vehicles that mark lanes in pavement[43]

It is important to note that the parts and accessories sold on or in connection with a chassis, body, or tractor are taxable only if that chassis, body, or tractor is also taxable. For example, if the sale of a chassis is not subject to tax, the lift gate sold on or in connection with such chassis similarly should not be taxable.

2. Installed Within Six Months

If a part or accessory is installed on a vehicle containing a taxable chassis, body, or tractor within six months after the date the owner actually takes possession of the vehicle, then, *subject to certain exceptions*, a 12 percent tax applies to the price of the part or accessory, including the cost of installation. The application of this rule, known as the Six-Month Rule, is discussed in detail in Section V. In determining if an item is a taxable part or accessory for purposes of the Six-Month Rule, the Treasury Regulations under section 4051 expressly state parts or accessories that were treated as nontaxable under the now-repealed section 4061(b)(1) and (2) similarly will be treated as nontaxable under section 4051.[44] *However, this principle appears to apply only to parts or accessories falling within the Six-Month Rule.*[45]

The terms "part" and "accessory," with respect to the Sixth-Month Rule, are defined as:

- Any article the primary use of which is to improve, repair, replace, or serve as a component part of [a taxable chassis, body, or tractor]
- Any article designed to be attached to or used in connection with such chassis, body, or tractor to add to its utility or ornamentation
- Any article the primary use of which is in connection with such chassis, body, or tractor, whether or not essential to its operations or use

However, this regulation also provides that an item is not considered a taxable part or accessory if it constitutes the "load" of the truck and its primary purpose is unrelated to the vehicle, such as performing a job site function unrelated to the transporting, loading, or unloading of the vehicle. For example, a construction derrick would not be considered a taxable part or accessory.

3. Over the Counter Sales

If you sell a part or accessory by itself—*i.e.*, not on or in connection with a taxable chassis, body, or tractor, and not installed on a vehicle in a manner that triggers the Six-Month Rule—then the sale of that part or accessory will not be taxable.[46] There is no tax on spare or replacement parts or accessories.[47]

However, even if the part or accessory is not sold or shipped at the same time as a taxable chassis, body, or tractor, the IRS may still treat the part or accessory as being sold in connection with the taxable item, in which case the sale of the part or accessory would be taxable. For instance, the Treasury Regulations provide the following examples where a part or accessory will be treated as taxable even though it may not be billed or shipped with the taxable chassis, body, or tractor:

- Where the part or accessory has been ordered at the time the taxable chassis, body, or tractor is sold
- The chassis, body, or tractor is sold without essential parts or accessories

unless the taxpayer can show that the sale of such parts or accessories is not in connection with such chassis, body, or tractor.[48]

Note however, that if a chassis part or accessory is sold at the same time as a taxable body and a non-taxable chassis (or no chassis), then the chassis part or accessory would not be taxable based on the fact that the body itself is taxable.[49] The same reasoning would apply to the sale of a body part or accessory at the same time as a taxable chassis and a nontaxable body (or no body).

In general, if your customer (1) buys a taxable chassis, body, or tractor and (2) at or around the same time, buys or orders a part or accessory for use with such chassis, body, or tractor, and (3) such part or accessory contributes to the highway transportation function of the chassis, body, or tractor, *then* you should treat the part or accessory as taxable, *unless* the customer can provide you with sufficient documentation that the part or accessory is being purchased as a spare or replacement item.

4. 25-Foot Crane Presumption

The IRS has adopted a specific rule, often referred to as the "25-Foot Rule," to determine whether a crane is a taxable part or accessory.[50] Under this rule, a crane that (1) has "an extended horizontal reach, from the center line of the mast, of 25 feet or less," and (2) is installed on trucks to load and unload those trucks, is presumed to be "designed and primarily used for loading and unloading" those trucks. Such a crane is a taxable part or accessory, *unless the presumption is rebutted*.

On the other hand, if a crane had an extended horizontal reach (excluding easily removed extensions) greater than 25 feet, the crane is presumed "not to be designed or primarily used for loading and unloading trucks upon which they are mounted." Such a crane is not a taxable part or accessory, *unless the presumption is rebutted*.[51]

It is important to understand that the length of a crane will not necessarily determine its taxability,; this "rule" simply creates a presumption. If a crane is more than 25 feet long, but its design or primary use is loading and unloading the truck on which it is installed, that crane likely would be taxable, despite the presumption of nontaxability. Similarly, if a crane is 25 feet or shorter, but its design and primary use is *not* for loading and unloading the truck to which it is attached, that crane likely would be nontaxable, despite the presumption of taxability. However, retail sellers that treat cranes 25 feet or shorter as nontaxable should be prepared to defend that position if their tax returns are audited.[52]

This rule was issued with respect to cranes, but the rationale arguably should apply to other equipment used in a similar manner, such as certain aerial devices[53] and conveyors.

E. The Person Who Pays the Tax

1. The "First Retail Sale"

In general, the person or entity that makes the "first retail sale" of a taxable chassis, body, or tractor is responsible for paying the FET. This will often be a dealer or distributor that sells the taxable item to an end-user. However, a "first retail sale" for purposes of triggering FET is not necessarily a retail sale, as that term is commonly understood. Under certain circumstances FET may be triggered by (1) a sale to a dealer or distributor, (2) a lease, and/or (3) use by a manufacturer, dealer or distributor. (The concept of "first retail sale" is discussed in greater detail in Section III.)

2. Further Manufacturing

Often, customers may request certain modifications to a chassis, body, or tractor the customer owns. Such modifications, if material enough, may result in that chassis, body, or tractor being deemed a new taxable article. In such a case, where the customer retains title to the item throughout the modification process, the person or entity responsible for the tax may be the customer rather than the modifier.[54] However, if during the modification process, the modifier discards the chassis, body, or tractor (or the major components thereof) to which the customer holds title and replaces it with a new one, the modifier of the new components, not the customer, likely will be liable for the FET.[55] Details about this so-called "Further Manufacturing" are discussed in Section V.

3. Six-Month Rule

As discussed in Section V, when an installer installs a taxable part or accessory on a vehicle under the Six-Month Rule, the owner of the vehicle is primarily liable to pay the FET. However, the installer retains *secondary* responsibility for the tax.

F. Prior Taxable Sale

1. General Rule: Articles Subject to FET Only Once

If a body, chassis, or tractor has been the subject of a prior taxable sale, that same item will generally not be subject to FET again on a later sale.[56] This is true even if tax was not actually paid on the first sale (e.g., the sale of the taxable article qualified as a tax-free sale under section 4221).[57] Of course, if an item has been modified to the extent it is treated as a new taxable item (*i.e.*, further manufacturing), the "first retail sale" of the modified item will be taxable even if, prior to modification, the item previously had been involved in a taxable sale. For more discussion of prior taxable sales, see Section III.

2. Trailer and Semitrailer Exception

Although an item generally is taxable only once under IRC § 4051, an exception to this principle exists for trailers and semitrailers. If a trailer or semitrailer chassis or body is sold within six months after a prior taxable sale, the second sale also will be taxable.[58] However, the seller in the second sale may qualify to claim a tax credit in the amount equal to the tax paid on the *first taxable sale*. In order to qualify for the available credit, the second seller would need to submit to the IRS, along with the form claiming the credit, a signed statement that complies with the IRS requirements.[59] The claimed credit cannot be more than the amount of the tax triggered by the second taxable sale.

G. Question & Answers

1. True or False

If a new truck is rated 35,000 pounds GVW, both the body and chassis of the vehicle are subject to FET.

Answer: False

When a completed vehicle is sold, an FET analysis must be done separately for the body and for the chassis. In such case, the question is whether the article in question is suitable for use with a vehicle rated 33,000 pounds GVW or less. In all likelihood, a chassis rated 35,000 pounds GVW will be subject to FET. However, it does not necessarily follow that the body is also taxable. In many cases, a body that is suitable for use with vehicles rated 33,000 pounds GVW or less—and is thus nontaxable—is installed on a chassis rated above the taxable threshold.

2. True or False

All platform bodies longer than 21 feet are subject to FET.

Answer: False

Under the safe harbors established in Rev. Proc. 2005-19, platform bodies 21 feet or less in length are treated as nontaxable. However, platform bodies in excess of 21 feet will still be treated as nontaxable if the seller can show that such a body is suitable for use with vehicles rated 33,000 pounds GVW or less. Many platform bodies longer than 21 feet have commercial and practical fitness for use in vehicles below the taxable threshold and those bodies will be nontaxable.

3. True or False:

Some cranes that have an extended horizontal reach from the center line of the mast of less than 25 feet are not subject to FET.

Answer: True

A crane that is not designed or primarily used to load or unload the truck on which it is mounted is not subject to tax. This is the case without regard to the length of the extended reach of the crane. Although cranes with an extended reach greater than 25 feet are *presumed* to be nontaxable, it does not follow that all shorter-reach cranes are taxable.

4. True or False

If a dealer takes a trade-in of a three-month-old truck rated more than 33,000 pounds GVW, and the dealer sells the used truck without modification the following week, the sale is taxable under the Six-Month Rule.

Answer: False

The Six-Month Rule applies only to installation of parts/accessories on a taxable body or chassis that has been in service less than six months. In this case, the dump truck is just a used dump truck. Since that truck previously was in a "first retail sale"—even if the transaction was a tax-free sale made, for example, to a local government—it would not be subject to FET upon its resale.

5. Multiple Choice

When determining the GVW rating of a chassis for FET purposes, a retail seller can consider the following types of readily attachable components:

a. tires and brakes
b. rims and springs
c. any component that affects weight-carrying capacity
d. none of the above

Answer: d

Under Rev. Rul. 85-196, clarified by Rev. Rul. 86-142 and 86-113, the calculation of GVW cannot take into account any readily attachable components.

6. Multiple Choice

In order for a truck body to be considered "suitable for use" with vehicles rated 33,000 pounds GVW or less, the retail seller must be able to show that the body in question is installed:

a. 51 percent or more of the time on vehicles rated 33,000 pounds GVW or less
b. 10 percent or more of the time on vehicles rated 33,000 pounds GVW or less
c. 100 percent of the time on vehicles rated 33,000 pounds GVW or less
d. none of the above

Answer: d

There is no bright-line percentage of use of a body on vehicles rated 33,000 pounds GVW or less that establishes that the body in question is nontaxable. The IRS, in a Technical Advice Memorandum and in informal comments at seminars, has made clear that sellers need not show 100 percent or even 51 percent use of a body with vehicles rated below the threshold in order to treat the body as nontaxable in all sales. In general, the larger the population of sales a retailer can show (of its own sales and/or sales of others), the lower percentage of use on vehicles rated 33,000 pounds GVW or less is needed to support a determination that the body in question is always taxable.

III. SALE OF A NEW ARTICLE

This section discusses situations in which FET is triggered by the *sale* (as opposed to the use or lease) of *new* (as opposed to used) chassis, bodies, or tractors. "New" articles are those that were not previously involved in a taxable sale. Generally, the subsequent sale or use of *used* articles will not trigger FET. However, there are exceptions. Some of these exceptions are discussed in Section II (trailer and semitrailer exception), Section IV (foreign-manufactured articles used in a foreign country prior to importation), and Section V (further manufacturing).

A. Overview

1. Must be "New"

FET applies only to "first retail sales." A sale of an article that has either been (a) in a prior transaction to which FET applied or, (b) in a transaction that qualified for tax-free treatment[60] will generally not be treated as a "first retail sale" and therefore will not be taxable. That is because such articles are not considered to be "new" for purposes of this section. (In addition, any sales of tax-exempt articles are not subject to FET, even if they are sold in "first retail sales.")[61]

2. What is the "First Retail Sale?"

The general rule is that unless the article is being sold on a tax-free or tax-exempt basis, the "first retail sale" of a body, chassis, or tractor will trigger FET (so long as the other requirements for a taxable body, chassis or tractor are satisfied).[62] Therefore, understanding the concept of a "first retail sale" is essential to understanding how FET applies to sales of new articles.

Because FET applies only to "first retail sales," it is known as a "retail sales tax." However, that label can be very misleading because the IRS has defined a "first retail sale" so broadly that it can, under certain circumstances, apply to traditional wholesale transactions.

The IRS has defined a "first retail sale" as any sale that does not satisfy one of three exceptions:

- There has been a prior taxable sale of the body, chassis, or tractor
- The sale qualifies for tax-free treatment (as discussed in Section VI)
- The sale is for resale *and* the sale for resale satisfies the requirements for tax-free treatment (as discussed below in this section)[63]

If a sale does not satisfy one of these three exceptions (and the sold item is not otherwise exempt under IRC § 4053), the sale is treated as a "first retail sale" *even* if the sale is not to a traditional retail customer (*i.e.*, end-user). As a result, a "first retail sale" can, under certain circumstances, apply to traditional wholesale transactions. Indeed it may not even be a sale at all; instead, merely *using* an article prior to its sale or *leasing* an article may be deemed a "first retail sale" and trigger FET. (For a discussion of when the use or lease of an article triggers tax, see Section VIII.)

B. Transactions Involving New Articles

There are three basic types of sales transactions that involve a new body, chassis, or tractor:
Sale by a manufacturer directly to a retail end-user; sale by a manufacturer to a dealer or distributor; and sale by a dealer or distributor to a retail end-user.
In each case, the sales transaction will be deemed a "first retail sale" unless it falls within an exception:

1. Sale by a manufacturer directly to a retail end-user
2. Sale by a manufacturer to a dealer or distributor
3. Sale by a dealer or distributor to a retail end-user

In each case, the sales transaction will be deemed a "first retail sale" unless it falls within an exception.

1. A sale of a new, taxable body, chassis, or tractor by its manufacturer directly to a retail end-user will be a "first retail sale" that triggers FET, *unless* (a) the sale is to a purchaser or for a use that qualifies for tax-free treatment (e.g., a non-profit educational organization), or (b) the sale is of the type of article that is exempt from FET (e.g., an ambulance or hearse). (These tax-free sales and tax-exempt sales are discussed in greater detail in Sections VII and VI, respectively.)

2. A first sale of a new, taxable body, chassis, or tractor by its manufacturer to a dealer or distributor will be a "first retail sale" that triggers FET, *unless* (a) the sale satisfies the requirements for a tax-free sale for resale (described below), (b) the sale is to a purchaser or for a use that qualifies as a tax-free sale (e.g., a non-profit educational organization), or (c) is of the type of article that is exempt from FET (*e.g.*, an ambulance or hearse).

3. A sale of a new, taxable body, chassis, or tractor by a dealer or distributor to a retail end-user will be a "first retail sale" that triggers FET, *unless* (a) the prior sale between the manufacturer and the dealer was a taxable sale (*i.e.*, the sale did *not* satisfy the requirements for a tax-free sale for resale (as described below), (b) the sale is to a purchaser or for a use that qualifies as a tax-free sale (*e.g.*, a non-profit educational organization), or (c) the sale is of the type of item being sold is exempt from FET (*e.g.*, an ambulance or hearse).

Essentially, if you are selling a new, taxable body, chassis, or tractor that has never been placed in service by an end-user, you must assume your sale of that article is subject to FET. You then should go through a checklist to determine if there is a basis to make the sale without FET.

- *First*, determine if the article is one of the tax-exempt items identified in IRC § 4053 (see Section VII).
- *Second*, determine if your purchaser has provided you with a valid resale certificate (see below).
- *Third*, determine if the sale is to a purchaser or for a use that qualifies as a tax-free sale under IRC § 4221 (see Section VI).

C. Tax-Free Sales for Resale

If the sale of an article is to an entity that is not purchasing the article to use, but is instead purchasing it to re-sell to another end user (a dealer's purchase from a manufacturer for resale, for example) then that initial "sale for resale" (from the manufacturer to the dealer) is not subject to FET, if certain requirements are satisfied.

In order to apply the FET correctly to a sale, you will need to understand three basic concepts concerning sales for resale:

1. A tax-free sale for resale does not exempt all subsequent sales of that article from FET, only the sale to the reseller. For example, a body sold by a manufacturer to its distributor tax-free in a sale for resale will be taxable when subsequently sold by the distributor to an end-user (unless the sale or item otherwise qualifies for tax-free treatment under IRC § 4221 or is exempt under IRC § 4053). In other words, a tax-free sale for resale by a manufacturer to a distributor simply *shifts* the responsibility to pay the FET from the manufacturer to the distributor.[64]

2. The buyer must provide the seller with a valid resale certificate. A sale for resale may be conducted tax-free (*i.e.*, shifting the tax liability from the seller to the buyer) *only* if the buyer provides the seller with a valid resale certificate and the sale satisfies other requirements, as discussed in 3, below.

3. If the sale for resale is taxable, any subsequent sale of that article is not taxable. If a sale for resale does *not* satisfy the requirements for a tax-free sale that sale for resale triggers tax and any subsequent sale of that article is not taxable, even when the subsequent sale is a traditional retail sale (*e.g.*, a sale from a distributor to an end-user). This is because a "prior taxable sale" would already have occurred, so the subsequent sale is not a "first retail sale, as defined by the IRS. For example, if a body sold for resale by its manufacturer to a distributor does not satisfy the requirements for a tax-free sale, that sale triggers FET and the manufacturer is responsible for paying the tax to the IRS. Then, when the distributor subsequently sells the same body to an end-user, that sale does *not* trigger FET (because the body has been in a previous taxable sale).

D. Replacement Bodies and Chassis

A new body or chassis that is purchased as a replacement is subject to FET. There are no exceptions or special rules for bodies or chassis that are purchased as replacements. For example, a new body that is purchased for the purpose of replacing a damaged body that is mounted on a used chassis is treated exactly the same, for FET purposes, as a new body that is purchased together with a new chassis. (Similarly, the FET rules with respect to the purchase of used bodies do not differ depending on whether the body is purchased as a replacement body.)

The belief that replacement articles are not taxable is a common mistake. Some of the confusion probably comes from an FET exception concerning the installation of replacement *parts or accessories*.[65] In order to avoid this trap, just keep in mind that a chassis, body, or tractor is *never* considered to be a "part or accessory," as those terms are used by the IRS.

E. Specifics

As noted above, the tax treatment of sales for resale can be confusing because "first retail sales" include certain sales that simply are not retail sales in the ordinary sense of that term. In other words, the current IRS definition of a "first retail sale" can include "sales for resale" if they do not satisfy the requirements for tax-free treatment.

NOTE: When looking at older IRS rulings on "sales for resale": Prior to October 1, 1987, the definition of a "first retail sale" expressly excluded most sales for resale.[66] This bit of history remains relevant today to the extent you are looking at older IRS rulings for guidance. Older rulings may state, in general, that a sale for resale is not taxable or is not a "first retail sale." These decisions may lead you to believe that sales for resales are categorically exempt from FET, but this is not true.[67] All sales for resale (*e.g.*, a sale by a manufacturer to its dealer) now are subject to FET *if* the requirements for tax-free treatment are not satisfied.

1. Requirements for a Tax-Free Sale for Resale

In order for a manufacturer and dealer to conduct a sale as a tax-free sale for resale, all of the following requirements must be satisfied:[68]

- The buyer must provide the seller with a certificate[69] in which the buyer certifies that it is purchasing the article for resale. This certificate, known as an "exemption certificate" or a "resale certificate" must be in a particular form.[70] We have provided a form resale certificate below.
- The resale certificate must be signed by the buyer and the signing must occur by the time of the sale.
- The buyer must sign the certificate in good faith.
- The seller must accept the certificate in good faith.

A sample of what such a certificate could look like is shown on the following page.

SAMPLE EXEMPTION/RESALE CERTIFICATE

Exemption Certificate

I hereby certify under penalties of perjury that I am ____ (Title) of ____________________________________ (Name of purchaser), that I am authorized to execute this certificate, and that:

(Check appropriate line)

_____ the article or articles specified in the accompanying order, or on the reverse side hereof, (or)

_____ all orders placed by the purchaser for the period commencing _______________________________ (Date) (period not to exceed 12 calendar quarters), are purchased either for resale or for lease on a long-term basis.

I understand that the fraudulent use of this certificate to secure exemption will subject me and all parties making such fraudulent use to a fine of not more than $10,000, or to imprisonment for not more than five (5) years, or both, together with costs of prosecution.

____

(Signature)

____

(Address)

2. How the Requirements have Changed

Taxpayers need to be aware that in 1998, the requirements for a resale certificate changed—but the form certificate the IRS provides in its regulations[71] was not updated to reflect those changes.

The *first change* is that a purchaser now must sign the certificate "under penalties of perjury." It is not entirely clear whether this requirement was intended to be in lieu of or in addition to the previously required statement of liability for fraudulent use of the certificate. However, until the IRS clarifies this issue, the authors recommend that the perjury language be in addition to the fraudulent use language.

The *second change* is that the purchaser is no longer required to be registered (or to provide its registration number on the resale certificate) in order for the sale to be treated as a tax-free sale for resale. However, it is important to note that the elimination of the registration requirement was limited only to tax-free sales for resale. Registration is still required for certain tax-free sales under IRC § 4221.

3. No Requirement that a Sale for Resale be Conducted on a Tax-Free Basis

The parties to a sale of a taxable article for resale—such as a body manufacturer and its distributor—may, *but are not required to*, conduct that sale as a tax-free sale for resale. In order for the manufacturer to make its sale on a tax-free basis to the distributor, the parties must comply with the requirements discussed above. If this is done, the manufacturer's sale of the taxable item will not trigger FET. The distributor will be the party that must pay the tax due on its resale of the item to an end-user, unless the distributor's resale to the end-user otherwise qualifies for tax free treatment under section 4221 or is tax-exempt under section 4053.

However, the manufacturer and the distributor are free to choose to treat the manufacturer's sale to the distributor as the taxable sale. They can do so simply by having the distributor *not* provide a resale certificate to the manufacturer. In addition, the resale certificate can be completed to apply to a particular sale or to cover all sales for a given period of time. If a resale certificate is not limited to one specific transaction, but instead covers all the transactions between the distributor and a particular seller during a specified period of time (e.g., a three-year period), then the distributor may revoke a previously provided resale certificate, with respect to future sales between the two parties, at any time by sending the seller a written notice of revocation.[72]

Therefore, the manufacturer and reseller have several options. By providing a resale certificate or not, by providing a resale certificate that covers a single sale or up to three years' worth of sales, or by revoking an existing resale certificate,the manufacturer and reseller can determine whether to treat all, some or none of their sales as tax-free sales for resale.

If a sale were conducted as a tax-free sale for resale, then the reseller would become responsible for payment of FET to the IRS upon the article's "first retail sale" (which likely will be the sale by the reseller to a retail customer). On the other hand, if a sale were *not* conducted as a tax-free sale for resale, then the initial seller would be responsible for paying the FET to the IRS (but the initial seller likely will pass through the cost of the FET to the reseller).

There are several practical results that flow from the use or non-use of a resale certificate. In the absence of a certificate, a manufacturer, rather than a dealer or a distributor, will be the taxpayer in most cases. Typically, manufacturers are bigger companies that have the accounting personnel to deal efficiently with FET issues and returns.

Without a resale certificate, the 12 percent tax is imposed on the wholesale price (which generally must be marked up by the presumed markup percentage, see Section IX) instead of the higher retail price. Depending on the difference between the wholesale and retail prices, imposing the tax at the wholesale level may result in a lower amount of tax, even when the presumed markup percentage is taken into account.

On the other hand, if the article will be resold by a dealer or distributor to an entity (*e.g.*, a state or local government) or for a use (*e.g.* for export) that could be conducted on a tax-free basis (see Section VI), use of a resale certificate may be advantageous. If a resale certificate is used, and the dealer/distributor complies with the requirements for a tax-free sale, then neither the manufacturer nor the dealer/distributor would pay FET. But if no resale certificate is used, the manufacturer would be responsible to pay FET (although, under certain circumstances, he might be able to seek a refund or credit of the article is ultimately sold in a tax-free sale see *e.g.*, 26 U.S.C. 6416(b)(2), (6)).

4. Strict Compliance Required for Tax-Free Sales for Resale

Note that at least one federal court has held that strict compliance with the applicable requirements is required to conduct a sale for resale on a tax-free basis.[73] In that case, the court held that as a result of the lack of full compliance with the certificate requirements, no tax-free sale for resale had occurred and therefore, the manufacturer was responsible for the FET on its sales to the dealers. The court rejected arguments based on good faith compliance with the regulatory requirements, and on the fact that the dealers had already paid the tax. The bottom line is that you should strictly comply with the IRS's regulatory requirements in order to sell an article tax-free in a sale for resale, even where (1) the evidence suggests that buyer and seller both intended to conduct the sale tax-free, and (2) the parties substantially complied with the regulatory requirements.

5. Timing of Certificates

The IRS regulations state that the buyer must provide the resale certificate to the seller, and the seller must accept the resale certificate, *by the time* of the sale to the buyer. At least one court has addressed this issue,[74] holding that delivery of the resale certificates two years after the sale did not meet the requirements for a tax -free sale, noting that resale certificates were required at or prior to the sale, not after the fact. Two years later is one thing, but what if the initial seller obtained the resale certificate just a day or two after the sale? What if the certificate were given after payment but before the delivery of the title to the buyer? There is no direct guidance on these questions, but given the plain language of the regulations and the ruling in the Volvo case (see 4, above), if the parties want a sale for resale to be treated as a tax-free sale, they would be well-advised to strictly comply with all applicable requirements – and ensure that the certificate is delivered and accepted before the sale.

6. Confusion Among Taxpayers and IRS Agents

As this section demonstrates, the issue of "first retail sales" as applied to sales for resale can be very confusing, not only to taxpayers but also to local IRS agents. Despite the IRS's broad definition of a "first retail sale" to include certain sales for resale, the assumption often will be that a sale by a manufacturer to a dealer/distributor is tax-free (and a sale by the dealer/distributor to an end-user is taxable). If you are a reseller and involved in an audit, you need to determine, as a threshold issue, whether you are the entity responsible for any FET that may be due.

7. Not Inconsistent with Statutory Mandate

It is interesting to note that Congress's definition of a "first retail sale," as set forth in IRC § 4051, is much more traditional than the expansive definition in the IRS's Treasury Regulations. The definition in the statute states: "The term "first retail sale" means the first sale, for a purpose *other than for resale* or leasing in a long-term lease, after production, manufacture, or importation."

Therefore, it initially appears that the IRS exceeded its authority from Congress by issuing regulations that define a "first retail sale" so broadly. On the one hand, Congress expressly states that a sale for resale is not a "first retail sale," and on the other hand, the IRS issues regulations defining a "first retail sale" to include certain sales for resale (*i.e.*, those sales that do not comply with the applicable certification requirements.) However, at least two courts have addressed this argument and determined that the IRS acted within its scope of authority.

In *Volvo* (see 4, above), the court determined that the IRS did not overstep its bounds with respect to its broad definition of a "first retail sale" because section 4052(d) of the Code provided the IRS with the necessary authority.[75] Likewise, in *Freightliner* (see 5, above), the court referred to section 4052(d) in rejecting a taxpayer's claim that the IRS's definition of a first retail sale was inconsistent with the authority Congress has granted it.

However, in 1998, section 4052(d) was modified and section 4052(g) was added to the Code. The relevant language with respect to this issue is now in section 4052(g), and the new language reflects the changes Congress made to the certification requirements in 1998 (as discussed above). Section 4052(g) states: "The Secretary shall prescribe regulations which permit, in lieu of any other certification, persons who are purchasing articles taxable under this subchapter for resale…to execute a statement (made under penalties of perjury) on the sale invoice that such sale is for resale" and directs that the regulations "shall not impose any registration requirement as a condition of using such procedure."

C. Questions and Answers

1. Taxability of Replacement Bodies

A customer wants to buy a new, taxable body from our dealership and have us install it on a chassis the customer already owns. The customer is buying the new body to replace a body that was recently wrecked. The customer claims that the new body is not taxable because it is simply a replacement part for a vehicle on which he already paid FET. Is he correct?

Answer: No

There is no tax exemption for a "replacement" body. Perhaps your customer is confusing the concept of a replacement body with the concept of a replacement *part or accessory*. Under the so-called "Six-Month Rule," the installation of a replacement part or accessory will not trigger FET. However, a body is *not* a part or accessory. *See* Letter Ruling 8626068 (March 31, 1986) (noting that "[t]he 6-month rule… has no significance with respect to articles (chassis and bodies) taxable under section [4051 [FET]]."

A body is a distinct taxable article, not a "part" of a completed vehicle. FET applies separately to each truck chassis and truck body. A taxable truck body can be installed on a nontaxable truck chassis and vice versa. The tax is not applied to truck "vehicles" as a whole. When a new body is purchased to replace a discarded body, the tax history of the discarded body (or the chassis on which the new body will be installed) is immaterial.

2. Resale Certificates

Several manufacturers of taxable truck bodies have advised us that their sales of the bodies to us will be a taxable sale, subject to FET unless we provide them with some kind of certificate. We thought only retail sales were subject to FET. Are the manufacturers correct and if so, what type of certificate should we provide?

Answer: The manufacturers are correct.

Although FET is commonly referred to as a "retailer's tax," the IRS treats a sale of a taxable body from a manufacturer to a dealer for resale as *taxable unless* certain conditions are satisfied.

A manufacturer's sale of a taxable truck body to you will be subject to FET unless you and the manufacturer meet certain certification requirements. In general, in order for a sale for resale to be nontaxable, the buyer must provide the seller with a certificate in which the buyer certifies that it is purchasing the subject article for resale. However, Treas. Reg. § 48.4052-1 requires that this so-called resale certificate be in a particular form. In addition, the resale certificate, by the time of the sale, must be signed by the buyer (or an authorized officer or employee of the buyer) in good faith and be accepted by the seller in good faith. *See* Treas. Reg. § 48.4052-1 and Treas. Reg. § 145.4052-1(a)(6).

If any of the conditions described above are not satisfied (and the sale does not qualify for tax-free treatment or a tax exemption), then the IRS will treat the sale of a taxable body by a manufacturer to a dealer for resale as a taxable sale subject to FET, even though, technically, the sale is not a retail sale. Although the manufacturer, and not you, will be liable for the FET, the amount of the tax likely will be passed on to you. If the sale for resale by the manufacturer to you is a taxable sale, then the subsequent sale of the truck body by you to your customer generally will not be taxable, *even though* it is a retail sale. *See* Treas. Reg. § 145.4052-1(a)(2)(iii) providing that, except for certain sales of trailers, a sale is not taxable if "[t]here has been a prior taxable sale of the article."

D. Putting You to the Test

1. True or False

A replacement body, *i.e.*, a new body mounted on a used chassis, is treated the same for FET purposes as a new body that is mounted on a new chassis.

Answer: True

A new replacement body will be subject to tax unless it is suitable for use with a vehicle rated 33,000 lbs or less (or otherwise qualifies for tax-free treatment or a tax exemption).

2. True or False

The FET applies both to retail sales and to sales by manufacturers to distributors.

Answer: True

Although the FET is referred to as a "retail" sales tax, any sale will be taxable unless the sale satisfies one of three exceptions (*i.e.*, the sale is tax-free under IRC § 4221, the sale satisfies the requirements for a sale for resale or long-term lease, or the chassis, body, or tractor was previously sold in a taxable sale.) *See* Temp. Treas. Reg. § 145.4052-1(a)(2).

3. True or False

A manufacturer does not have to charge FET on the sale of a taxable body to one of its dealers, so long as the dealer is going to re-sell the body and charge tax.

Answer: False

In order for a manufacturer to sell an otherwise taxable body on a tax-free basis to one of its dealers, the dealer must provide the manufacturer with a resale certificate (which is executed and accepted in good faith) in the form set forth in the IRS regulations. *See* Treas. Reg. §§ 145.4052-1(a)(6) *and* 48.4052-1.

4. True or False

A distributor has one month after it purchases a taxable body from the manufacturer to provide the manufacturer with a valid resale certificate or statement.

Answer: False

In order for a sale to be tax-free based on the fact that it is a sale for resale, the resale certificate or statement must be accepted by the manufacturer by the time of the sale to the distributor. *See* Treas. Reg. §48.4052-1.

5. True or False

In order to conduct a sale for resale on a tax-free basis, the purchaser must be registered with the IRS.

Answer: False

Although this was a requirement several years ago, neither the purchaser nor the seller needs to be registered with the IRS to participate in a tax-free sale for resale, but the resale certificate or statement now must be signed under penalties of perjury. *See* Treas. Reg. §48.4052-1. (Registration of purchaser and/or seller may still be required for tax-free treatment under IRC § 4221. *See* Section VI.)

6. Fill in the Blank

A resale certificate or statement cannot cover a period greater than ___ calendar quarters.

Answer: 12 calendar quarters (three years).

7. True or False

If a new, taxable truck chassis is sold in the United States on a tax-free basis to a municipality, and the used vehicle is subsequently sold into Mexico where it is used, the used vehicle would be subject to FET if it is imported back into the United States and sold.

Answer: False

Only the "first retail sale" of a taxable article is potentially subject to tax. In this case, the chassis in question, when new, is sold in a first retail sale to a municipality. The fact that the municipality was able to purchase it on a tax-free basis under IRC § 4221(a)(4) does not change the fact that the chassis was involved in a "first retail sale." Thus, the chassis would not be subject to FET if it is exported into Mexico and then imported back into the United States.

8. True or False

An end-user seeking to purchase a chassis rated 45,000 pounds GVW cannot avoid FET by buying a used chassis that is manufactured in a foreign country and importing that chassis into the United States.

Answer: True

The FET applies to new and used chassis that are manufactured abroad and imported into the United States (so long as the chassis in question has not previously been in a "first retail sale" in the United States). The first use of the chassis following its importation is treated as the "first retail sale" of the chassis, and the end-user will be responsible to file a Form 720 with the IRS and pay the applicable tax.

IV. EXPORTS AND IMPORTS TO FOREIGN COUNTRIES

This section discusses how federal excise tax under IRC § 4051 is applied to imports and exports of vehicles[76] to foreign countries, such as Canada or Mexico. In this section, the exporting of a vehicle refers to a vehicle that is manufactured in the United States by a U.S. manufacturer and is then sold to a foreign dealer or a foreign end-user. Additionally, the importation of a vehicle refers to a vehicle that is *either* (a) manufactured in a foreign country by a foreign manufacturer and then is sold to a U.S. dealer or a U.S. end-user, or (b) manufactured in the United States by a U.S. manufacturer, exported to a foreign country and subsequently re-sold to a U.S. dealer or a U.S. end-user.

A. Overview

When determining if a sale of a vehicle for export or import triggers FET, the question is the same as for all other sales: Is the sale a "first retail sale," as defined by the IRS? (A "first retail sale" is discussed in detail in Section III.) If the answer is yes, then the sale is taxable; if the answer is no, then it is not.

Once a "first retail sale" of a vehicle has occurred, then any *subsequent* sale of that vehicle generally would not be taxable. When determining if FET applies to exports and imports, it is important to keep in mind that even if a sale of a vehicle is conducted on a tax-free basis pursuant to the export exemption, it is still considered a "first retail sale," which means any subsequent sale of that vehicle generally will not be subject to FET. (For a discussion on the requirements to conduct a sale for export on a tax-free basis, see Section VI.)

Tax Treatment of Basic Transactions Involving Exports and Imports

There are six different basic scenarios involving sales transactions that involve exporting or importing a vehicle:

1. Sale by a U.S. manufacturer of its chassis, body, or tractor to a foreign end-user
2. Sale by a U.S. manufacturer of its chassis, body, or tractor to a foreign dealer or distributor
3. Sale by a U.S. dealer of a U.S.-manufactured chassis, body, or tractor to a foreign end-user, dealer, or distributor
4. Purchase by a U.S. end-user of a foreign-manufactured chassis, body or tractor that the purchaser imports to the United States and uses
5. Purchase by a U.S. dealer or distributor of a foreign-manufactured chassis, body or tractor, that the purchaser imports to the United States and sells
6. Purchase by a U.S. dealer, distributor, or end-user of a *U.S.-manufactured* chassis, body or tractor from a foreign dealer or end-user that the purchaser imports to the United States and uses or sells

Below is a summary of how FET generally would apply to each of these transactions.

1. FET Applied to Export Sales

a. Sale by a U.S. Manufacturer of its Chassis, Body, or Tractor to a Foreign End-User (e.g., a Canadian Retail User).

A sale by a U.S. manufacturer of its chassis, body, or tractor to a foreign end-user is subject to FET, unless the U.S. manufacturer complies with the requirements for tax-free sales for exports under IRC § 4221(a)(2). (See discussion at Section VI.)

b. Sale by a U.S. Manufacturer of its Chassis, Body, or Tractor to a Foreign Dealer or Distributor

A sale by a U.S. manufacturer of its chassis, body, or tractor to a foreign dealer or distributor is subject to FET unless the U.S. manufacturer complies with the requirements for tax-free sales for resales. (See Section III). *Note that the IRS has determined (in a 2000 letter ruling) that a U.S. manufacturer may not use an export exemption for its sale to a Canadian dealer.* (This determination is discussed below in B.).

c. **Sale by a U.S. Dealer of a U.S.-Manufactured Chassis, Body, or Tractor to a Foreign End-User, Dealer or Distributor**

A sale by a U.S. dealer or distributor to a foreign end-user, dealer or distributor may be subject to FET, depending on how the initial sale between the U.S. manufacturer and the U.S. dealer/distributor was structured.

If the initial sale by the manufacturer to the dealer/distributor were not conducted as a tax-free sale for resale, then that sale is considered the "first retail sale."[77] Therefore, the subsequent sale by the dealer/distributor to the foreign purchaser generally would not be subject to FET.

On the other hand, if the initial sale by the manufacturer to the dealer/distributor were conducted as a tax-free sale for resale, then the subsequent sale by the dealer/distributor to the foreign purchaser would be subject to FET, *unless* the foreign purchaser were (a) a dealer/distributor, and the sale to the foreign purchaser complied with the requirements for a tax-free sale for resale,[78] or (b) an end-user *and* the sale to the foreign purchaser complied with the requirements for a tax-free sale for export under IRC § 4221(a)(2) (discussed below).

2. **When FET Applies to Import Sales**

a. **Purchase by a U.S. End-User of a Foreign-Manufactured Chassis, Body, or Tractor, which Purchaser then Imports to the U.S. and Uses**

If a U.S. end-user imports to the U.S. a *new or used* foreign-made chassis, body, or tractor (*i.e.*, an article that has never before been in the U.S.), then the first use of the article by the end-user after importation will trigger FET. This is because the "first retail sale" (which, as discussed in Section VIII, includes the first use) after importation is subject to FET. It is important to keep in mind that for FET purposes, a "first retail sale" means a first retail sale in the United States,[79] so it does not matter if, for example, prior to importation to the United States, a Canadian manufacturer previously sold the article in a retail sale.

b. **Purchase by a U.S. Dealer or Distributor of a Foreign-Manufactured Chassis, Body, or Tractor, which Purchaser then Imports to the U.S. and Sells**

If a U.S. dealer or distributor imports to the U.S. a new or used foreign-made chassis, body, or tractor (*i.e.*, an article that has never before been in the U.S.), and sells it to a U.S. end-user, then the sale to the end-user is the "first retail sale" after importation, and the sale is subject to FET. If the U.S. dealer or distributor imports the same article and sells it for resale to another U.S. dealer or distributor, then such sale would not trigger FET, *if* the sale satisfied the requirements for a tax-free sale for resale.

c. **Purchase by a U.S. Dealer, Distributor or End-User from a Foreign Dealer or End-User of a U.S.-Manufactured Chassis, Body, or Tractor, Which Purchaser then Imports to the U.S. and Uses or Sells**

If any U.S. purchaser imports a *U.S.-manufactured* chassis, body, or tractor from a foreign country, the taxability of the subsequent sale by the importer in the U.S. depends on the sales history of the article. If, prior to exportation to the foreign country, the article had been involved in a taxable transaction – that is, subject to a "first retail sale" in the U.S, then the sale or use by the importer generally would not be taxable. On the other hand, if, prior to exportation, the article had not been subject to a "first retail sale" in the U.S., then the sale or use by the importer would trigger FET, unless, in the case of a sale, the importer's sale was a tax-free sale for resale.

B. Specifics

1. **The Importer's Dilemma**

As noted above, the taxability of an imported article that was originally manufactured in the U.S. will depend largely on events that occurred prior to the article's initial exportation. Most importers will be able to determine that a given chassis, body, or tractor was manufactured in the U.S., but they will not have access to other information that is necessary for a tax determination.

There are four general FET scenarios that could occur when a U.S.-manufactured article is exported to a foreign country:

1. The U.S. manufacturer, or a U.S. dealer that purchased the article from the manufacturer, paid the FET
2. The U.S. manufacturer, or a U.S. dealer that purchased the article from the manufacturer, did not pay FET, but sold the article in a "first retail sale" and was responsible for the payment of FET
3. The U.S. manufacturer, or a U.S. dealer that purchased the article from the manufacturer, properly sold the article to a foreign end-user as a tax-free sale for export
4. The U.S. manufacturer, or U.S. dealer that purchased the article from the manufacturer, properly sold the item to a foreign dealer or distributor tax-free as a sale for resale

In the first three scenarios, a taxable sale occurred, and therefore any subsequent sale of the article typically would not trigger FET. Accordingly, any sale by the importer would not be taxable. (With respect to scenario 3, a tax-free sale for export generally is treated the same way as a tax-paid sale. In other words, a taxable sale includes a sale that qualifies for tax-free treatment, and once a taxable sale occurs, the IRS cannot tax any subsequent sale of the article.[80])

However, if the fourth scenario occurred, then the first sale or use following importation likely would trigger FET. This is because a tax-free sale for resale merely *shifts* the responsibility to pay the tax from the initial seller to a subsequent seller. (See Section III B.3.)

What all this means is that the importer will often be put in the impossible situation of determining tax liability without access to the information necessary to make such a determination. In such a situation, the conservative approach is for the importer to charge FET on its sale of the article. This reflects the fact that, in an audit situation, the taxpayer has the burden of proof with respect to the tax position it has taken. When the sale history of an imported vehicle is unknown, the importer should contact its tax adviser to discuss the best way to proceed.

The Export Exemption

Cannot Use the Export Exemption for Sales for Resales? In at least one letter ruling[81] the IRS concluded that a taxpayer could *not* treat its sale of certain vehicles to a Canadian dealer as a tax-free sale for export. The rationale used by the IRS was that a tax-free sale for export applies only to a taxable sale, and a sale for resale is not a taxable sale. Accordingly, the IRS concluded that in order for the taxpayer to sell vehicles to a Canadian dealer tax-free, the taxpayer would need to satisfy the requirements for a tax-free sale for resale.[82] To avoid an IRS assessment in an audit, you should comply with the requirements for a tax-free sale for resale for sales to foreign dealers, and not use an export exemption.*

Unused and Undamaged Exception. As noted above, typically, if a sale of a U.S.-manufactured chassis, body, or tractor to a foreign end user qualifies as a tax-free sale for export, the subsequent sale in the U.S. by an importer generally is not taxable. The principle is that the IRS generally may only assess the tax on the first taxable sale of an article (which includes a sale that qualifies for tax-free treatment—*i.e.*, a tax-free sale for export), and not on any subsequent sales of that

* "The issue of whether a sale to a foreign dealer may be conducted as a tax-free sale for export (as opposed to a tax-free sale for resale) is further discussed in Scenario 3 of a Chief Counsel Advisory, issued May 13, 2011, as clarified in a Chief Counsel Advisory, issued May 27, 2011. Although Scenario 3 indicates that a sale in the US to a foreign dealer may be conducted as a tax-free sale for export, the subsequent Chief Counsel Advisory appears to both confirm the conclusion it reached in Scenario 3 and confirm the principle that a sale for resale is not a taxable retail sale (which was the rationale used in Letter Ruling 200036038 for determining that the sale to a foreign dealer could not qualify for a tax-free sale for export). In addition, it should be noted that the ruling in Rev. Rul. 85-95 (which is discussed in Letter Ruling 200036038 and in the second Chief Counsel Advisory) predates an amendment to the IRS's definition of a "first retail sale." See Chapter 3, Item 8, entitled "A Little Bit of History". Given the confusion surrounding this issue, the most conservative approach for sales to foreign dealers continues to be to comply with the requirements for a tax-free sale for resale, rather than a tax-free sale for export. However, if you are involved in an audit based on your use of an export exemption for sales to foreign dealers, we strongly recommend you contact your tax counsel on this issue to discuss the best way to proceed."

same article (*i.e.*, a sale in the United States by an importer). In other words, if a sale is done on a tax-free basis, the IRS generally loses its only opportunity to assess the tax. However, this principle does not apply if, following exportation to a foreign country and prior to importation back to the United States, the article is neither used nor damaged (*i.e.*, if the foreign purchaser ships the article back to the U.S. in an unused and undamaged condition. Under such circumstances, the first retail sale of the article in the United States by the importer would trigger FET, even though the article previously was involved in a tax-free sale for export.[83]

C. Questions and Answers

1. Import of Canadian-Manufactured Trucks

Our company will be purchasing several new truck chassis manufactured in Canada, and then importing the chassis in to the U.S.. Each of these chassis has a GVW in excess of 33,000 pounds. We plan to sell the trucks in retail sales. Will we need to pay FET on these chassis? Would it matter if the chassis had been used in Canada prior to being imported in to the U.S.?

Answer: Yes

The first retail sale of the chassis following importation in to the U.S. would trigger FET. NO, the tax treatment does not change if the chassis were used in Canada prior to importation.

FET is triggered upon the "first retail sale" of the chassis. In prior Revenue Rulings, the IRS has not treated a sale in a foreign country as a "first retail sale." *See* Rev. Rul. 83-40 (stating that "[a] truck chassis manufactured outside the United States, imported into the United States, and sold or used is subject to the manufacturer's excise tax [which is the predecessor to the retailer's excise tax under IRC § 4051] whether or not it was used outside the United States prior to importation"); *see also* Rev. Rul. 85-95 (stating that a dealer in a foreign country sold the truck at retail in that country and ruling that the retail sale of the used truck in the United States following importation was the first retail sale of the truck).

Therefore, if the chassis is manufactured in Canada and imported by your company, then your sale of the chassis to end-users would be the "first retail sale" of the chassis for FET purposes, and your company would be responsible for the tax. Your responsibility for the tax does not change depending on whether the chassis were sold or used in Canada prior to your purchase.

Although there have been certain regulatory and/or statutory changes since the transactions that were the subject of those decisions occurred, the rationale in these decisions, as it relates to your question, should still apply.

2. Tax Liability of Customers Buying Canadian-Manufactured Trucks Directly from Canada

We are a retail truck dealership. We have been losing business because retail customers think they can avoid paying FET by purchasing taxable Canadian-manufactured truck chassis directly from the Canadian dealership. Is that true?

Answer: No

In fact, customers will create extra tax burdens for themselves by buying directly from the Canadian dealers.

The first retail sale or *use* of a taxable truck chassis in the U.S. that was manufactured in Canada is subject to FET. *See* IRC § 4052(a)(3). This rule applies regardless of the identity of the user (*i.e.*, there is no exception for retail customers). Accordingly, if a customer purchases a taxable truck chassis manufactured in Canada, and then imports it into the U.S., that customer's first use of the chassis will trigger FET (assuming the customer uses it prior to selling it).

Rather than avoiding FET, the customer is *increasing* its tax burdens and liabilities by purchasing the truck chassis directly from a Canadian dealer. If the retail customer purchases the Canadian truck chassis from a dealership in the U.S., then the *dealership* is the taxpayer for FET purposes. But if the retail customer purchases the truck chassis directly from the Canadian dealer, then the *customer* will be the taxpayer for FET purposes (assuming the customer uses it or sells it in a taxable sale). This means that the customer is responsible to pay the tax and has the obligation to file an excise tax return (Form 720) with the IRS.

This could be a significant burden for a retail customer who otherwise would not need to file a Form 720. Rather than avoiding the tax, the retail customer not only has to pay the tax, but also must incur the administrative burdens of doing so. And, if the customer fails to file a Form 720, the customer risks an IRS audit and the payment of penalties and interest.

In addition, if the customer is not familiar with the calculation of FET, the customer will not be aware that, in calculating the tax it owes, it likely will have to add the presumed mark up percentage to the taxable price. *See* Treas. Reg. § 145.4052-1(d)(2) (noting that where an importer is liable for the FET, the presumed mark-up percentage applies). Thus, even when a customer files a Form 720 with respect to its use of the Canadian truck chassis, the customer risks underreporting its tax liability and potentially accruing interest and penalty charges.

3. Tax Liability for Export to Canada?

We are a dealership that generally sells trucks at retail. Recently, a Canadian dealer has expressed an interest in purchasing several of our trucks. Would the IRS treat such sales as subject to FET?

Answer: It depends.

First, FET generally would not apply if the trucks previously had been involved in a taxable sale (and the trucks had not been further manufactured since that sale). For example, if you are a U.S. dealership, and purchased the trucks directly from the manufacturer and, at the time of the sale, did not provide the manufacturer with a valid resale certificate, then the sale by the manufacturer would trigger tax and the manufacturer would be responsible for paying the FET. Under such circumstances, any subsequent sale of the same trucks (*e.g.*, the sale by you to the Canadian dealer) would not trigger FET.

However, assume you did provide the manufacturer with a valid resale certificate, and that the sale otherwise complied with the requirements for a tax-free sale for resale. In that case, the IRS would treat the subsequent sale from you to the Canadian dealer as taxable, unless the sale was conducted on a tax-free basis.

In Letter Ruling 200036038, the IRS ruled that sales for resale (*e.g.* your sale to the Canadian dealer) did not qualify as a tax-free sale for export. Instead, the IRS determined that in order to conduct a sale to a Canadian dealer on a tax-free basis, the sale needed to comply with the requirements for a tax-free sale for resale.

V. THE MODIFICATION OF AN ARTICLE

Generally, the subsequent sale or use of a previously used article will not trigger FET because FET applies only to the "first retail sale," and a used article typically will already have been the subject of a "first retail sale." However, this general rule does not necessarily apply when a previously used article is subsequently modified.

This section discusses the circumstances in which federal excise tax applies to the act of *modifying* a *used* article. For purposes of this section, the term "modification" includes repairs. Triggering FET by modifying a previously-used article generally will occur in one of two ways:

1. the modification will fall under the so-called Six-Month Rule, or
2. the modification will constitute "further manufacturing" and fall under the so-called "Further Manufacturing Rule"

However, if you are only the modifier of the article, and not its owner, you may not be liable for any FET triggered by your modification.

A. Overview

The general rule is that once an article has been involved in a prior transaction that either triggered FET or was exempt from FET under IRC § 4221, any subsequent sale or use of that article will not trigger tax. *However*, as with most general rules, there are exceptions.

With respect to modified or repaired articles, there are two big exceptions to the general rule that an article previously involved in a taxable sale will no longer be taxable. These two exceptions are: (1) the Six-Month Rule and, (2) the Further Manufacturing Rule.

1. The Six-Month Rule

Summary of the Rule: Under the Six-Month Rule,[84] FET may be triggered by the *installation* (not the "first retail sale") of certain parts or accessories on a vehicle that contains a taxable chassis, body, or tractor. More specifically, FET will be triggered when the installation occurs within six months after the vehicle is first placed in service (*i.e.*, the date the vehicle's owner actually took possession of the vehicle),[85] unless (1) the part or accessory is a replacement part or accessory, or (2) the aggregate price of *all* parts or accessories (including the price of installation) that are installed on the article within this six-month period is not more than $1,000.

This rule is intended to prevent customers from avoiding FET by buying stripped down vehicles and subsequently adding desired parts and accessories. The amount of FET due under the Six-Month Rule is 12 percent of the price of the part or accessory, including the price of the installation.

Who Pays the Tax: Under the Six-Month Rule, the owner of the vehicle (or its lessee or operator)[86] is primarily responsible for the FET, but the installer remains *secondarily* liable for the tax.

The authors are not aware of any IRS rulings or court decisions that include a detailed discussion of the concept of secondary liability; however, the term suggests that the IRS can pursue the installer for the FET if it does not receive payment from the customer.[87] This rule presents several problems for the installer. *First*, in many cases, the installer will have no way of ascertaining the date when the article was first placed in service or the aggregate price of installations of parts or accessories on the article during the relevant six-month period. *Second*, the installer will have no way to ascertain whether or not the customer files an FET return and pays the tax due. In light of these limitations, a conservative approach would be for the installer to charge the customer the FET on the installation and include the FET on the installer's next quarterly return. This way, the installer can avoid possible secondary liability in the future.

B. Further Manufacturing Rule

1. Summary of the Rule

The concept of "further manufacturing" is that, when significant modifications or repairs are made to an item, the improved or changed item is treated as "new" for FET purposes. The new item is once again subject to tax upon its "first retail sale" (Of course, the modified article is only taxable if, as modified, it satisfies the requirements of a taxable article.)

In determining whether an article has been further manufactured, you first need to answer three general questions:

1. Did the modifications to a chassis, body, or tractor change the transportation function of a vehicle?
2. Did the modifications restore a wrecked vehicle into a usable vehicle?
3. Did the modifications extend a vehicle's useful life?

If the answer to all three of these questions is "No," then further manufacturing has not occurred.[88] If the answer to any of these three questions is "Yes," then you need to determine whether the article, prior to the modification, was a taxable article.

In general, if the article were a taxable article prior to the modification, then the so-called "75 Percent Rule" would apply.[89] If it were *not* a taxable article prior to the modification, then the 75 Percent Rule would not apply.

C. 75 Percent Rule

Under the 75 Percent Rule, if the cost of the modifications (including repairs to the used article (*i.e.*, chassis, body, or tractor) exceeds 75 percent of the retail price of a new article that is comparable to the now-modified article, then that article has been "further manufactured." As discussed below, the IRS has not defined the term "cost" with respect to the 75 Percent Rule. However, at a minimum, the term "costs" likely would include labor, parts, and all other expenses incurred as a direct result of the modification process.

For example:

Used Body	$10,000
Repairs/Modifications	$80,000
Current Retail Price of Comparable New Body	$100,000
Sales Price of Modified Body	$95,000

Because the repairs are > 75 percent of the $100,000 retail price, the article is deemed to have been "further manufactured," and therefore FET is due on $95,000.

As noted above, if an article is further manufactured, any subsequent "first retail sale" of that article (including use) will trigger FET. The good news is that when the 75 Percent Rule applies, extremely few modifications, as a practical matter, will exceed the 75 percent cost threshold.

When the 75 Percent Rule does not Apply — Modified Article May Still be Subject to FET: The 75 Percent Rule does not apply if the item, as modified, would be taxable if new, *and* the item was *not* taxable prior to the modifications.[90] If the modifications convert a previously non-taxable article into a taxable one, that article likely will be treated as being further manufactured—even if the modification does not exceed the 75 percent threshold. (For practical purposes, the types of changes necessary to convert a non-taxable article into a taxable one generally will always fall into one of the three categories of further manufacturing discussed above.)

For example, if a chassis has a gross vehicle weight (GVW) rating of 32,000 pounds, it would not be a taxable article (see Section II). However, if the chassis were modified by the addition of a lift axle, and the added lift axle increased the GVW rating of the chassis to more than 33,000 pounds,[91] then it would be a taxable chassis (assuming the other requirements for a taxable chassis were satisfied). Under these circumstances, the chassis would have been further manufactured and its "first retail sale" would trigger

FET. This is the case *even though* the cost of the lift axle would never exceed the 75 percent threshold.

The Tax and Who Pays it: The FET due on the modified chassis, body, or tractor is 12 percent of the sale price of the modified item. (See Section IX for a discussion on how to determine the correct taxable sale price to which the 12 percent FET applies.) The FET is *not* calculated based on the cost of the modifications. (However, in situations in which an end-user has its used article modified into a taxable article, the taxable price may be limited to the cost of the modification. (See Section IX discussing the deduction of certain used components under IRC § 4052(b)(1)(B)(iii).)

When the *customer* furnishes the chassis, body or tractor to be further manufactured and retains title to the item throughout the modification process, the *customer*, not the modifier, may be responsible for paying FET to the IRS.[92] However, if the modifier discards the chassis, body, or tractor to which the customer holds title, the IRS likely will determine that the modifier, not the customer, is liable for the FET.[93]

Of course, further manufacturing does not occur only at a customer's request. A modifier may purchase a used article and then modify it for the modifier's own use or for resale. If that were the case, then the modifier would be liable for the FET, assuming the modifications constituted further manufacturing. In addition, because the modifier would be treated as the manufacturer of the modified vehicle, a taxable sale by the modifier generally would be subject to the presumed markup percentage. (See Section IX for a discussion on the presumed markup percentage.)

1. The Mere Combination Rule

The so-called "Mere Combination Rule"[94] is an exception to the Further Manufacturing Rules. The Mere Combination Rule provides that the installation of certain specified items on a chassis, body or tractor will not constitute further manufacturing the chassis, body or tractor. Therefore, under the Mere Combination Rule, the otherwise applicable further manufacturing rules do not apply to the addition[95] of the following articles:

- "Any coupling device (including any fifth wheel)
- Wrecker crane
- Loading and unloading equipment (including any crane, hoist, winch, or power liftgate)
- Aerial ladder or tower
- Snow and ice control equipment
- Earth moving excavation and construction equipment
- Spreader, sleeper cab, cab shield
- Wood or metal floor"[96]

D. The Interrelationship Among the Rules

If the installation of a part or accessory is not taxable under the Further Manufacturing Rules, it may still trigger FET under the Six-Month Rule. For example, the addition of a tag axle to a chassis with a GVW rating of 34,000 pounds likely will not be considered further manufacturing under the 75 Percent Rule (because the cost of the tag axle would rarely, if ever, exceed 75 percent of a comparable new chassis). However, if the tag axle were installed within six months after the date the vehicle were first placed in service, the installation might trigger FET under the Six-Month Rule.

You also need to keep in mind that the Mere Combination Rule only provides an exception to the Further Manufacturing Rules, not the Six-Month Rule. For example, because a fifth wheel is one of the items identified in the Mere Combination Rule, its installation on a tractor would not constitute further manufacturing. However, the Six-Month Rule provides no similar exception for fifth wheels. Therefore, if the fifth wheel were installed on the tractor within the applicable six-month period, the installation might trigger FET. Likewise, an item identified in the Mere Combination Rule still might be treated as a taxable part/accessory when sold on or in connection with the *sale* of a *new* taxable chassis, body or tractor. (See Section II.)

Similarly, a modification may not trigger FET under the Six-Month Rule, but may constitute further manufacturing. For example, if modifications were made to a non-taxable chassis or if modifications were made to a chassis after the applicable six-month period had expired, then the Six-Month Rule would not apply. However, those same modifications still might trigger FET if they converted the nontaxable chassis into a taxable one or if the modifications exceeded the 75 percent cost threshold.

E. The Six-Month Rule—A Closer Look

1. Purpose of the Six-Month Rule

When a new item is sold, the parts/accessories installed on that new item generally would be subject to FET.[97] Therefore, the purpose of the Six-Month Rule is to prevent a purchaser from lowering the FET due on a sale by buying a stripped-down chassis, body or tractor, and then, soon after the purchase, installing all the bells and whistles on the item tax-free

2. The Dollar Threshold

As noted above, the installation of parts or accessories are not taxable under the Six-Month Rule if the total price of such parts and accessories (including the cost of installation) is not more than $1,000. Congress increased this dollar threshold from $200 to $1,000, effective August 6, 2007.[98]

3. How the Tax Works

In determining whether the dollar threshold is exceeded, a taxpayer must consider the *aggregate price of all* the parts/accessories installed within the applicable six-month period. For example, if a vehicle were first placed in service in July, and parts/accessories (including installation) were installed on August 5 at a cost of $300, on October 20 at a cost of $400 and on November 14 at a cost of $500, then FET would be due on $1,200 *even though* the price of no single installation exceeded $1,000—and even if the work were done by three different installers.

It also is important to understand, as indicated in the above example, that once the dollar threshold under the Six-Month Rule is exceeded, the FET applies *to the entire price of all the parts and accessories (including installation) installed on the vehicle during the six-month period*, and not only that portion of the amount that exceeds the dollar threshold. In other words, using the example above, if the total price of the parts or accessories installed on a vehicle during the applicable six-month period equals $1,200, then FET is due on the entire $1,200 amount, and not only on $200 (*i.e.*, the amount in excess of the $1000 threshold).

In addition to multiple installers, the Six-Month arguably applies to multiple articles. As a general rule, separate articles in a single vehicle (e.g., a chassis and a body) are treated as entirely separate items for FET purposes. (See Section II.) However, an exception to this rule appears to occur in the application of the Six-Month Rule, which refers to installations on a "vehicle" that contains a taxable article. Thus, in theory, at least, it appears that, in determining whether the $1,000 threshold has been exceeded, the IRS could aggregate installations on both the chassis and the body of a given vehicle. However, we are aware of no IRS rulings addressing this issue.

F. The Difficulty with Secondary Liability

As noted above, installers are only *secondarily* liable for FET under the Six-Month Rule. Typically it is a good thing when you are not the first party the IRS will look to for tax liability; however, secondary liability can place installers in a difficult position because they have little control over managing this potential liability.

First, even if an installer knows how to calculate correctly whether the dollar threshold has been exceeded, the installer still may not have access to the information needed to do so. This is because the Six-Month Rule is not installer-specific, but refers to any and all installers that may have installed a part or accessory on a particular vehicle.

An installer likely would be aware only of the installations to the vehicle that the installer personally installed; the installer likely would not know whether prior or subsequent installations of parts and accessories occurred or the total cost of those installations. (Although the installer can ask the customer about previous installations, there is no guarantee that the contact person has the relevant information or is willing to give it to the installer.) The authors are aware of no rulings discussing how the IRS would assess tax against an installer under the Six-Month Rule, where installations by more than one installer occurred during the applicable six-month period.

In addition, as noted above, because the customer will be primarily responsible for the FET, and not the installer, the installer has no way of knowing, at the time of installation, whether the tax will be properly paid. Therefore, it is extremely difficult for the installer to manage its exposure to tax liability.

One way to manage its potential liability is for installers to simply pay the FET, and pass the cost on to the customers. Although it might not be technically correct for the secondarily liable installer to pay the tax in the first instance, the IRS is unlikely to object when it has received the full amount of tax due on a transaction. The authors are aware of many installers that use this approach and have not heard of any instance in which the IRS has questioned this practice. If the IRS were to object, then presumably the installer would seek a refund and pay it to the customer, who would then file a return.

Another option is to advise the customer that he or she is primarily responsible for the tax. This has two primary advantages: (1) a customer who is aware of his or her tax responsibility will be more likely to pay the tax (thereby relieving the installer of its secondary liability), and (2) an installer's relationship with its customer may sour if a customer is blindsided by a tax liability he or she did not know existed.

Accordingly, installers may want to consider letting their customers know when they have (or potentially could have) tax liability under the Six-Month Rule. For example, installers could stamp a legend on invoices for modifications of customer-owned bodies and chassis that states:

> *NOTICE: Modifications to customer-owned truck, trailer, and semitrailer bodies and chassis and tractors within six months after the vehicle is placed in service may trigger a federal excise tax under section 4051(a) of the Internal Revenue Code. In such cases, the customer may be primarily responsible for filing a tax return (IRS Form 720) and paying the applicable tax directly to the IRS. Consult with your tax adviser for more details.*

1. **Further Manufacturing Rules: A Closer Look**

a. History—In General

In the early days of the FET, a modification to a body, chassis, or tractor was "further manufacturing" if it "result[ed] in the production of a different article." *See* Rev. Rul. 82-157, 1982-2 C.B. 288 (September 7, 1982). However, the IRS did not provide taxpayers with clear guidance as to what types of modifications would constitute further manufacturing. Instead, further manufacturing decisions were made by the IRS on an ad hoc basis. *See id.* (noting "[w]hether or not an improvement is significant will be determined on a case-by-case basis").

A few years later, the IRS provided taxpayers with some clear guidance in Rev. Rul. 87-85, 1987-2 C.B. 251 (September 8, 1987). That ruling provided a list of 30 Revenue Rulings addressing the scope of manufacturing and further manufacturing. Although those 30 rulings were decided under the old manufacturer's excise tax, the IRS stated that those rulings continued to apply under the current retailer's excise tax "to the extent that they determine whether a particular operation is, or is not, an act of manufacture or further manufacture."

The IRS then provided additional guidance on the question of further manufacturing in a revenue ruling that identified three categories of modifications that constituted further manufacturing.[99] These three categories were: (1) modifications to a chassis, body, or tractor that change the transportation function of a vehicle, (2) modifications that restore a wrecked vehicle into a usable vehicle, and (3) modifications that extend a vehicle's useful life.

Although the IRS did not expressly adopt these three categories of manufacturing described above, subsequent letter rulings indicate that the IRS looks to those three categories in determining whether further manufacturing has occurred.[100] As a result, in determining whether a modification constitutes further manufacturing, the modifier first must determine if a modification falls into one of those three categories. (This determination can be aided by reference to the list of 30 Revenue Rulings identified in Rev. Rul. 87-85, 1987-2 C.B. 251 (September 8, 1987).)[101]

The IRS has not clarified the exact nature of the relationship between the three categories of further manufacturing and the 75 Percent Rule. However, it appears that (1) if a modification does not fall into one of these three further manufacturing categories, then no further manufacturing has occurred, and (2) if the modification does fall into one of these categories, then the modifier must determine whether the 75 Percent Rule applies (*i.e.*, whether the item was taxable prior to the modifications and whether the modified item, if *new*, would be taxable). However, because the 75 percent threshold is rarely exceeded, the modifier can short-cut this analysis by first using the 75 Percent Rule calculation (assuming the 75 Percent Rule applies). If the 75 percent threshold is not exceeded, then no further manufacturing has occurred. If the 75 Percent Rule does not apply or if the 75 percent threshold is exceeded, then the modifier must determine if the modification was of the type that satisfies one of the three categories identified above. However, as a practical matter, if the 75 percent threshold is exceeded, it is very likely that the modification will also fall into one of the three categories that constitute further manufacturing.

NOTE: It is important to keep in mind, especially when reviewing older IRS rulings that the 75 Percent Rule has been in effect only since January 1, 1998. From November 9, 1988 through the year 1997, a narrower version of the 75 Percent Rule applied.[102]

One of the major differences between the prior, narrower rule and the current rule is that the 75 percent threshold in the prior rule applied only to modifications or *repairs that extended the useful life of the vehicle*. In other words, whereas the current 75 Percent Rule applies to all three categories of modifications (including repairs) that otherwise would constitute further manufacturing, the narrower rule adopted by the IRS in Rev. Rul. 91-27, 1991-1 C.B. 192 (April 15, 1991) did *not* apply to the first two categories of such modifications (*i.e.,* modifications that change the transportation function of the vehicle and modifications that restore a wrecked vehicle into a useable vehicle).

b. Application of the 75 Percent Rule

75 Percent Rule Applied Separate to Each Article, Not "Vehicle": In the only substantive ruling to date discussing the application of the 75 Percent Rule, the IRS confirmed that the 75 Percent Rule should be applied separately to each article (*i.e.*, a tractor or a truck, trailer, or semitrailer body or a truck, trailer, or semitrailer chassis) as opposed to applying the rule to the complete vehicle comprised of both a body and a chassis.[103]

For example, assume a modifier is asked to repair a vehicle, and the vehicle's body will need extensive repairs, but the vehicle's chassis will need only minor repairs. In determining if the 75 percent threshold has been exceeded, the modifier may *not* compare the cost of the modifications to the *vehicle* (*e.g.*, the chassis *and* the body) to the retail price of a comparable new *vehicle* (*e.g.*, a new chassis and body). Instead, the modifier separately must determine if the modifications to the *chassis* exceed 75 percent of the retail price of an equivalent new chassis, and if the modifications to the *body* exceed 75 percent of the retail price of an equivalent new body.

c. Ambiguities in the 75 Percent Rule

The calculation of "cost." The 75 Percent Rule is based on the "cost" of the modifications performed on a chassis, body, or tractor. However, the IRS has not provided any guidance as to how to calculate such costs. For example, if the chassis, body, or tractor were owned by the customer, the cost of the modification likely would be the full cost charged by the modifier to the customer.

However, when the modifier owns the chassis, body, or tractor being modified, it is unclear how the IRS would determine the "cost." For example, the IRS could define cost to include those charges that would have been part of an arm's-length transaction (*e.g.*, a profit percentage), or the IRS could permit a modifier to define cost based purely on its internal cost, including a percentage of overhead costs.

In other words, it is unclear if the term "cost" refers to the cost to the modifier or the cost to a retail customer. For example, assume a modifier buys for $20,000 a 1-year-old used chassis, body or tractor that was previously subject to tax. The modifier's internal costs (parts, labor, overhead, etc.) incurred in performing the modifications are $75,000. The modifier then sells the chassis, body or tractor for $100,000. Assume further that the retail price of a comparable, new chassis, body, or tractor is $105,000.

In this example, the modifier would make a profit of $5,000 ($100,000 minus $20,000 and minus $75,000) upon its sale of the modified article. However, the determination of whether the 75 percent threshold would be exceeded differs depending on whether the $5,000 profit is included as a "cost" of the modification, because $75,000 in "costs" does not exceed 75 percent of $105,000, but $80,000 in "costs" does.

While it may seem odd to deem the profit margin as part of the dealer's "cost"—the IRS may take the position that the dealer's "cost" should be the same as a customer's cost and therefore, it should include the amount the dealer would have charged the customer for the same modification. Until the IRS provides additional guidance on this issue, the conservative approach for determining the "cost" of modifications for purposes of the 75 Percent Rule is for a modifier to use the amount it would have charged a customer for the same modifications (*i.e.*, the "cost" amount should include the modifier's profit).

G. What is "Retail Price"?

Similarly, the actual wording of the 75 Percent Rule requires the modifier to compare the cost of the modifications to the *retail price of* a comparable new tractor, chassis or body. However, the retail price is not necessarily the same amount as the *taxable price*. For example, the equipment on a tractor, chassis, or body that does not contribute to the transportation function of that tractor, chassis, or body generally is not subject to FET,[104] but may account for a significant portion of the price of the tractor, chassis or body. Accordingly, whether further manufacturing has occurred may depend on whether the 75 percent calculation considers the price of nontaxable parts of the modified tractor, chassis or body. The IRS has not yet addressed this issue. In the authors' view, however, the IRS likely would apply the 75 Percent Rule by determining whether the cost to modify the *taxable* parts of the tractor, body, or chassis exceeds 75 percent of the *taxable price* of a comparable, new tractor, body or chassis.

H. Use After Further Manufacture

Even if a modifier were to modify a tractor, chassis, or body for its own use, the modifier still would be liable for FET if such modifications constitute further manufacturing. This makes sense if the modifier considers that further manufacturing a used tractor, chassis or body is treated as creating an entirely new taxable tractor, chassis or body. Like any new taxable tractor, chassis or body, FET will be triggered upon that item's "first retail sale," which may include its first use.

For example, consider again the situation in which the addition of a lift axle further manufactures a chassis by converting a nontaxable chassis into a taxable one. If, prior to selling that chassis, a modifier uses the chassis in its business for a few months, then the modifier would be responsible for the FET, upon its first use of the chassis. This is true even if the modifier subsequently sells the chassis in what would otherwise have been a tax-free sale (*e.g.*, a sale to a state or local government). Of course, once the modifier's first use of the chassis triggers FET, then *any* subsequent sale of the modified article would not be subject to FET, unless that article is one again further manufactured.) For a more detailed discussion about how use can trigger FET, see Section VIII.

I. Keep In Mind

1. Exemption for Further Manufacturing

Under IRC § 4221, there is a tax exemption that, in general, applies to certain sales whereby the purchaser buys a chassis, body or tractor for the purpose of further manufacturing it. This exemption permits the *seller to* sell an otherwise taxable chassis, body or tractor tax-free for the purchaser to use to further manufacture the chassis, body or tractor. It does *not* permit the modifier/new owner to further manufacture the chassis, body or tractor without triggering FET. Upon the further manufacturing of a chassis, body or tractor, the modifier/owner still would be responsible for FET upon its "first retail sale." (For more details on this exemption and the necessary requirements, see Section VI.)

2. Sales of Parts or Accessories

The Six-Month Rule refers to the *installation* of a part or accessory on a *used* tractor, chassis, or body, and the Further Manufacturing Rules refer to the *first retail sale* of a *modified* tractor, chassis, or body. Neither rule is relevant with respect to (1) the sale of parts or accessories in connection with the *first retail sale* of a *new* tractor, chassis, or body, or (2) the sale of *uninstalled* parts or accessories without a related sale of a tractor, chassis, or body. These two types of sales of parts and accessories are discussed in Section II.

3. Deduction of Used Components

Under IRC § 4052(b)(1)(B)(iii), a user might be able to exclude the value of used components from the taxable price of the "first retail sale" of a further manufactured chassis, body, or tractor. However, there are certain requirements that must be satisfied in order to qualify for this exclusion. For a discussion of these requirements, see Section IX.

J. Further Manufacturing Flow Chart

The questions and answers in the following six steps may help a modifier determine whether or not FET applies to a particular modification.

“FURTHER MANUFACTURING” FLOW CHART

1.

Is the modified tractor, chassis or body suitable for use with a vehicle that satisfies the GVW (and, if a tractor, the GCW) requirements for a taxable tractor, chassis or body?

If NO → FET does not apply

If YES → **Proceed to Step 2**

2.

Do the modifications constitute “mere combination”? [See IRC § 4052(c) for a list of items that fall into the category of “mere combination”]

If NO → Proceed to Step 3

If YES → **Determine whether the Six-Month Rule applies***

* [See IRC § 4051(b) for the factors that must be present in order for the Six-Month Rule to apply. If these factors are not present, then FET will not apply. If these factors are present, then customer is primarily liable and the modifier is secondarily liable for tax on parts and installation.]

3.

Were the modifications of the type considered to be further manufacturing? [Do modifications fall into one of the three categories identified by Rev. Rul. 91-27? See also Rev. Rul. 87-85 for list of 30 rulings regarding particular modifications.]

If NO → FET does not apply (unless the 6-Month Rule applies)

If YES → **Proceed to Step 4**

4.

Does the cost of modifications/repairs exceed 75 percent of the retail price of a comparable new article?

If NO → Proceed to Step 5

If YES → **Proceed to Step 6**

5.

Would the tractor, body, or chassis, prior to modification, be taxable if it were new? [IRC § 4052(f)(2)]

If NO → FET will apply* Proceed to Step 6

If YES → then FET will not apply (unless the 6-Month Rule applies)

6.

Is title to the tractor, body, or chassis that was modified held by the modifier or an end-user?

If held by the MODIFIER → the modifier will be the taxpayer upon first retail sale or use after modification

If held by an END-USER → the end-user may be the taxpayer upon first retail sale or use after modification

K. Questions and Answers

1. Calculation of Tax Under the 75 Percent Rule

We are considering purchasing a 3-year-old, taxable body at an auction for $2,000 and performing extensive repairs on it. We estimate that the cost to refurbish the body would be about $17,000 and that a comparable, new body would sell for $22,000 at retail. We would then add a lift axle to a one-year old, taxable truck chassis, and install the repaired body on the chassis. The cost of adding the lift axle would be about $5,000. A similar, new chassis would sell for about $40,000. When we sell the vehicle at retail to the customer, is it taxable under the 75 Percent Rule? If yes, then how should the tax be calculated?

Answer: First, you must determine separately whether the modifications you make to the body trigger FET under the 75 Percent Rule, and whether the modifications you make to the chassis trigger FET under that rule.

Based on the information provided in your question, the cost of the modifications to the used body ($17,000) exceeds 75 percent of the retail price of a new body comparable to the repaired body ($22,000). Accordingly, under the 75 Percent Rule, you have further manufactured the body. This means that the "first retail sale" of the modified body will trigger FET.

You then do the same calculation for the chassis. Under your facts, the addition of the lift axle to the chassis ($5,000) does not exceed 75 percent of the retail price of a new chassis comparable to the modified chassis ($40,000). Therefore, you have not further manufactured the chassis and the "first retail sale" of the modified chassis would not be subject to tax.

Please note that the 75 Percent Rule applies to both the chassis and body in your situation because both the chassis and body were taxable prior to your modifications.The 75 Percent Rule would not apply to the body if the used body previously had not been taxable, and would not apply to the chassis if the used chassis previously had not been taxable.

Once you determine that the repaired body would be further manufactured (and therefore subject to tax), the cost of the repairs is no longer relevant. The tax due on the further manufactured body is 12 percent of the retail price of the repaired body.

2. Nontaxable Article Modified Into Taxable Article

Recently a customer brought us a three-year old used chassis that was rated 32,900 pounds GVW and asked us to install a lift-axle that would cause the chassis' GVW to exceed 33,000 pounds. (We will re-rate the chassis' GVW to 35,000 pounds.) Does this modification trigger FET?

Answer: The installation of the lift-axle constitutes further manufacturing, which means that the "first retail sale" of the modified chassis will trigger FET. However, it is the customer, not you, who will be responsible to pay the FET.

Under the circumstances you describe, the addition of the lift-axle would be an act of "further manufacture." *See* Rev. Rul. 87-85, 1987-2 C.B. 251 (September 8, 1987) and; Rev. Rul. 75-129, 1975-1 C.B. 336 (1975).) The 75 Percent Rule, which excludes certain modifications and repairs from constituting further manufacturing, does not apply in this case. This is because the 75 Percent Rule is not applicable where both (1) the article (in this case, the 32,900-pound GVW chassis) was not previously taxable and (2) the article, as modified or repaired (in this case, a chassis having a GVW in excess of 33,000 pounds), would be taxable if it were sold new.

Prior to the installation of the lift-axle, the chassis you describe was nontaxable because it was rated below the taxable threshold (*i.e.*, 33,000 pounds GVW or below). You indicate that you will re-rate the GVW of the chassis to 35,000 pounds.[105] Accordingly, the installation of the lift-axle will cause the chassis to exceed 33,000 pounds GVW. Under these facts then, the 75 Percent Rule provides no tax relief. Accordingly, the modified chassis would be taxable, because it would be treated as a new chassis rated above 33,000 pounds GVW.

Although the installation of the lift-axle makes the chassis taxable, the good news is that the *customer*, not you, may be the party liable for the tax. Generally, where the customer furnishes the article to be further manufactured and retains title thereto and to the subsequently modified article, the customer bears any resulting tax liability. *See* Treas. Reg. § 48.0-2(a)(4)(ii). However, there are exceptions, and modifiers who modify customer-owned articles should confirm with their tax counsel that their particular modifications do not subject them to tax liability. *See e.g.*, Private Letter Rulings 9245003 (July 23, 1992) and 9713009 (December 12, 1996).

The customer will need to file a tax return and pay the tax due even if he never sells the modified chassis. Federal excise tax is triggered not only by the retail sale of a taxable article, but also by the use of a taxable article, where that use is prior to the first retail sale of the article. *See* IRC § 4052(a)(3). However, the tax for which the customer is responsible may be based on a price that is considerably less than the value of the entire chassis. *See* I.R.C § 4052(b)(1)(B)(iv).

3. Who Pays the Tax When a Used Vehicle is Rebuilt?
We are sometimes asked to rebuild badly damaged customer-owned semitrailers (which consist of a semitrailer chassis and a semitrailer body). During the rebuilding process, we remove all the body parts and fabricate a new body from all new parts and materials, which parts and materials are supplied from our inventory. The rebuilt body is greater than 26,000 pounds GVW. If the customer retains title to the semitrailer throughout the rebuilding process, can we still be liable for any resulting tax on the rebuilt body under IRC § 4051?

Answer: Yes
You can be (and likely would be) liable for FET on the rebuilt body even though your customer retains title to the semitrailer throughout the rebuilding process.

In order to determine who is liable for the tax on the new body, it is necessary to determine who the "manufacturer" of the body is for excise tax purposes. Generally, if a third party manufactures a taxable article for a customer who provides materials, and it is agreed that the *customer retains title to such materials and to the finished article*, the customer (and not the third party actually manufacturing the article) will be treated as the "manufacturer" for excise tax purposes. *See* Treas. Reg. 48.0-2(a)(4)(ii). *See* also Rev. Rul. 83-149, 1983-2 C.B. 186 (October 3, 1983), Situation 3; Letter Ruling 8638002 (June 5, 1986).

However, under facts similar to yours—*i.e.*, when a body is discarded in its entirety—the IRS has concluded that the customer's retention of title to the vehicle is not persuasive in determining who is the "manufacturer." In Letter Rulings 9713009 (December 12, 1996), TAMs, 9245003 (July 23, 1992) and 9144003 (July 22, 1991), the IRS ruled that the fabricator of the new body, rather than the customer, was liable for FET. In Letter Ruling 9713009 (December 12, 1996), the IRS explained "although it may be unclear as to who has ownership of the completed body, [the fabricator has] contributed all the parts and materials for the fabrication of such body and [is] considered the manufacturer of the newly-fabricated semi-trailer body." *See also* Revenue Rulings 69-437, 1969-2 C.B. 208 (stating that if the owner of the finished article is unclear at the time of manufacturing, a primary factor in the determination of the manufacturer of such article "is the relative values of material furnished by each of the parties to the transaction").

Based on the information you provided in your question (*i.e.*, that you discard the furnished body and that all of the parts and materials for the new body are supplied from your inventory), you would likely be treated as the "manufacturer" of the new body and would be liable for FET upon your sale of the new body to the customer.

However, the identity of the manufacturer of an article is fact-specific. Accordingly, you should provide your tax advisor with a detailed account of the operations you perform in the rebuilding process, including an account of which parts and materials you supply and which are supplied by your customer. In addition, you should advise your tax counsel with respect to any agreements or understandings you have with the customer regarding ownership, production or sale of the finished article.

L. Putting You to the Test

1. True or False
If a pintle hook is installed on a taxable chassis within six months of its first placement in service, the pintle hook is not taxable because the installation of pintle hooks is exempt from tax under the Six-Month Rule.

Answer: False
There is no tax exemption for pintle hooks under the Six-Month Rule. However, the installation of a pintle hook is exempted from being considered further manufacturing a vehicle. See IRC § 4052(c). Therefore, if the pintle hook is installed on a taxable chassis more than six months after the vehicle is first placed in service (and, therefore, outside the scope of the Six-Month Rule), the pintle hook likely will not be subject to FET.

2. True or False
The customer, not the installer, is solely liable for parts or accessories installed on a vehicle under the Six-Month Rule.

Answer: False
Although the customer of the vehicle is primarily liable for the installation of parts or accessories under the Six-Month Rule, the installer has *secondary* liability. *See* IRC § 4051(b)(3).

3. Fill in the Blank
In order for modifications (including repairs) of a previously taxable article to be considered "further manufacturing," the cost of the modifications must exceed ____ percent of the retail price of a new, comparable article.

Answer: 75 percent

4. True or False
If a tax-paid chassis were modified and the cost of such modifications did not exceed 75 percent of the retail price of a new chassis that is comparable to the modified chassis, the modifications do not constitute further manufacturing (and the modified chassis will not be subject to FET).

Answer: True
Under the 75 Percent Rule, the modifications to the chassis under these circumstances would not constitute further manufacturing. *See* IRC § 4052(f)(1).

5. True or False
If a *nontaxable* chassis were modified so that it becomes a *taxable chassis* and the cost of such modification did not exceed 75 percent of the retail price of a new chassis that is comparable to the modified chassis, the modifications *do* constitute further manufacturing (and the modified chassis *will* be taxable).

Answer: True
The 75 Percent Rule does not apply when the chassis was not previously subject to tax. *See* IRC § 4052(f)(2).

6. True or False
If a customer buys a new, taxable chassis with no lift-gate, and then has a modifier install a lift-gate eight months later, there is no FET imposed on the sale and installation of the lift-gate.

Answer: True
Under the Six-Month Rule, parts and accessories, like a lift-gate, may be taxable if installed within six months after the vehicle is first placed in service. If the installation takes place more than six months later, the Six-Month Rule does not apply. If the Six-Month Rule does not apply, then the installation of parts and accessories results in tax only if that installation amounts to "further manufacturing." The Internal Revenue Code specifically provides that the installation of loading and unloading devices (like a lift gate) does not constitute further manufacturing. *See* IRC § 4052(c).

7. True or False
The installation of a replacement part or accessory, within six months of the date the vehicle is first placed in service, is not subject to FET.

Answer: True
The Six-Month Rule does not apply to the installation of replacement parts or accessories. *See* IRC § 4051(b)(2)(A).

8. True or False
Under the Six-Month Rule, a replacement body is not taxable if it is installed on a chassis within six months after the date the vehicle was first placed in service.

Answer: False
Under the Six-Month Rule, the installation of replacement *parts and accessories* is not taxable. A body is not a part or accessory, and a replacement body is treated as a new body for FET purposes.

9. Fill in the Blank
The Six-Month Rule applies only if the price, in the aggregate, of parts and accessories (and installation charges) installed on a taxable article within six months after the article is placed in service, exceeds $ __________.

Answer: $1,000
(Note: Treas. Reg. § 145.4051-1(c)(3) has not been amended to reflect the increase in the Internal Revenue Code, and still refers to $200.)

10. True or False
Under the Six-Month Rule, FET applies only to the portion of the price of the parts and accessories (and installation charges) that exceed the $1,000 threshold.

Answer: False
Once you exceed the $1,000 threshold under the Six-Month Rule, the FET applies to the entire price of all the parts and accessories (including their installation), and not only that portion of the amount that exceeds $1,000.

11. Multiple Choice
The installation of which part or accessory is one of the items defined by the Internal Revenue Code as mere combination and deemed not to constitute further manufacturing, regardless of the application of the 75 Percent Rule:

a. snow and ice control equipment
b. a coupling device
c. loading and unloading equipment
d. a sleeper cab
e. all of the above

Answer: e
See IRC § 4052(c) for a complete list of these items. In addition, it is important to note that even if a part or accessory is not listed in IRC § 4052(c), it still may not constitute further manufacturing under the 75 Percent Rule.

VI. TAX-FREE SALES BASED ON THE IDENTITY OF THE PURCHASER OR THE USE OF THE ARTICLE (IRC § 4221)

There are certain circumstances in which an otherwise taxable sale can be conducted tax-free. This section discusses the types of tax-free sales available under IRC § 4221 *and their requirements*. It is important to understand that, even if a sale falls into one of the tax-free categories under section 4221, there are additional requirements that must be satisfied before the item can be sold tax-free.

A. The Basics

The section 4221 tax-free sales fall into two general categories based on: (1) the identity of the purchaser, and (2) the use or other disposition of the item.[106]

Tax-free sales under section 4221, based on the identity of the purchaser, involve certain sales to:

1. A state or local government
2. A nonprofit educational organization
3. A qualified blood collector organization

Tax-free sales under section 4221, based on the use or other disposition of the item, involve certain sales for:

1. Export
2. Further manufacturing
3. Supplies for vessels or aircraft

1. General Requirements for All Tax-Free Sales Under Section 4221

The following general requirements apply to all tax-free sales available under IRC § 4221. (*In addition to these requirements, each type of tax-free sale under section 4221 has its own special requirements that must be satisfied in order to qualify as a tax-free sale.* These special requirements are discussed in B.1, below.)

- The seller must file a Form 637 with the IRS to register under IRC § 4222.[107]
- The purchaser must be registered with the IRS, by filing a Form 637, unless the purchaser is (a) a state or local government, or (b) purchasing supplies for vessels or aircraft. In addition, a purchaser is not required to register under certain circumstances (which are discussed below in B.) if it is involved in a sale for export.[108] However, in such cases, other documentation is required. (See B., below.)
- Where the purchaser is required to be registered, the purchaser must provide the seller, in writing, the purchaser's registration number and the tax-free purpose for which the purchaser is buying the item. (This information may be written on the purchase order or on other documentation related to the sale that the purchaser provides to the taxpayer.)[109]
- The tax-free use (including exportation) of the item must be its first use.[110]
- The seller must advise the buyer that (1) the items being sold are normally taxable, and (2) the items are being furnished tax-free based on an exemption certificate or equivalent. The information the seller provides the purchaser must be sufficient so that (1) the buyer can calculate and pay the tax if the item is not first used for a tax-free purpose; (2) the seller can pay the tax if, in the case of tax-free sales for export and further manufacturing, the seller does not receive the required confirmation of tax-free use from the purchaser (as further discussed below in B.); and (3) the buyer can notify the seller that the item was not used for the tax-free purpose.[111]
- The seller must not have any reason to believe that (a) the purchaser's intent is to use the item other than for the specified tax-free purpose, or (b) the purchaser is not registered (if required).[112]
- The seller generally should retain all documentation relating to tax-free sales under IRC § 4221 for at least three years.[113]

B. A Deeper Dive

1. Additional Requirements for Each Type of Tax-Free Sale Under IRC § 4221

In addition to the general requirements listed above in

A.1, each tax-free sale described under IRC § 4221 has its own special requirements that must be satisfied in order to conduct the sale on a tax-free basis. These requirements are discussed below.

a. Sale to a State or Local Government

A state or local government includes a U.S. state or the District of Columbia, or a political subdivision of either.[114]

Additional requirements:

- The sale must be for the *exclusive* use of the state or local government. (A discussion of how the IRS has interpreted the term "exclusive" is discussed below in 2.)
- The taxpayer must sell the item *directly* to the state or local government. Tax-free treatment does not apply if the taxpayer sells to a purchaser for *resale* to a state or local government (even if, at the time of the initial sale, the taxpayer and purchaser know that the item will be resold to a qualifying governmental entity).

Special registration requirement:

- State and local governments cannot register with the IRS, so the taxpayer instead must obtain either (a) an exemption certificate signed by an authorized officer or employee of the governmental entity, or (b) a purchase order *containing all the information required to be in the exemption certificate*. The certificate must be substantially in the form set forth at Treas. Reg. § 48.4221-5(c). If the frequency of sales to the same governmental entity makes it impractical to furnish separate certificates, a single certificate may be used to cover all orders for a time period of not more than three consecutive years.

b. Sale to a Nonprofit Educational Organization

A sale to a nonprofit educational organization may be treated as tax-free only if it is an organization that (1) is exempt from federal income tax under IRC § 501(a), *and* (2) normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on (or operates a school that meets these requirements, provided that the entity is a § 501(c)(3) organization and that the primary function of the school is the presentation of formal instruction).

Additional requirements:

- The sale must be for the *exclusive* use of the nonprofit educational organization. (A discussion of how the IRS has interpreted the term "exclusive" is discussed below in 2.)
- The taxpayer must sell the item *directly* to the nonprofit educational organization. Tax-free treatment does not apply if a taxpayer sells to a purchaser for resale to the educational organization (even if, at the time of the initial sale, the taxpayer and purchaser know the item will be resold to a qualifying educational organization).

Special registration requirement:

- The general information required by registered purchasers for all section 4221 tax-free transactions, described above, must also include the office of the district director that issued the registration number. The general and specific information discussed in this paragraph may be included in a single document to cover all sales by the taxpayer to the same educational organization for a time period of not more than three consecutive years.

c. Sale to a Qualified Blood Collector Organization

A sale to a blood collector organization may qualify for tax-free treatment only if the organization (1) meets the requirements of IRC § 501(c)(3) (for example, a charitable organization) and is tax-exempt under IRC § 501(a) (federal income taxes), (2) collects human blood as its primary activity, (3) is registered with the Secretary of the Treasury for exemptions from excise tax, and (4) is registered for blood collection by the Food and Drug Administration.[115]

Additional requirement:

- The sale must be for the *exclusive* use of the blood collector organization in collecting, transporting or storing the blood.

d. Sale for Use in Further Manufacture

In general, a sale for use in further manufacture may qualify for tax-free treatment when the purchaser buys the item for use either as material to manufacture, or as a component part of, another taxable item; it does not occur if the manufacturing process (except for testing purposes) consumes the item so that it is not physically a part of the further manufactured item.[116]

NOTE: Unlike other tax-free sales under IRC § 4221, a sale for use in further manufacture may qualify for tax-free treatment when either (a) the purchaser will use the item for further manufacturing, *or* (b) the purchaser will resell the item to a second purchaser for use in further manufacturing.

Additional requirement:

- If the taxpayer sells the item to a purchaser, and the purchaser *resells* the item to a second purchaser for use in further manufacturing, the sale will not be a tax-free sale *unless* the taxpayer receives proof the item was resold for further manufacturing within six months of the taxpayer's sale or shipment of the item (whichever is earlier).[117] This proof must be either (a) a copy of the invoice of the first purchaser's sale to the second purchaser, which includes both parties' registration numbers, or (b) a statement that follows the form shown at Treas. Reg. § 48.4221-2(c)(2)(i). If the first purchaser resells more than one item for further manufacturing to the same second purchaser within this six-month period, a single statement may identify all such sales for resale.[118] *If the taxpayer does not receive such proof, the taxpayer will become responsible for paying the tax.*[119]

e. Sale for Export

The term "export" applies to sales to buyers located in possessions of the United States.[120]

Notes:

- Unlike other tax-free sales under IRC § 4221, a sale for export may qualify for tax-free treatment when either (a) the purchaser will export the item, *or* (b) the purchaser will resell the item to a second purchaser for export. (Tax-free sale treatment does not apply to a resale to a third purchaser for export.)
- If the sale for export is also a sale for resale, see B.5., below, for a discussion of which tax-free sale procedure should be used.

Additional requirements:

- A sale for export will be tax-free only if within six months of the taxpayer's sale or shipment of the item (whichever is earlier), the taxpayer receives proof the item was resold for export.[121] Proof of exportation must be in one of the following forms: (a) a copy of the export bill of lading issued by the delivering carrier; (b) a certificate by the agent or representative of the export carrier that shows the item was actually exported; (c) a certificate of lading signed by a customs officer of the foreign country to which the item is exported; (d) a statement by the foreign consignee that shows the item was received, but only if the foreign country does not have a customs administration; or (e) if a U.S. government department or agency cannot provide any of the four types of proof described above, a statement or certification by an authorized officer on department or agency stationery that the items in question were actually exported.[122] *If the taxpayer does not receive this proof within the six-month period, then the taxpayer will become responsible for paying the tax.*[123]
- If the taxpayer is not the exporter, then the taxpayer must receive a statement from the first purchaser that the item actually was

exported by either the first purchaser or the second purchaser prior to any use, further manufacturing or resale in the United States (except for export). The statement must (1) describe the evidence of exportation, which evidence must be in one of the forms described above in the previous paragraph, and must be readily available for review by government officials, and (2) be in the form provided at Treas. Reg. § 48.4221-3(d)(2). If the taxpayer sells more than one item to the same first purchaser within this six-month period, a single statement may identify all such sales for export.[124]

Special registration requirement:

- If either the first or second purchaser is located in a U.S. possession or foreign country, that purchaser need not be registered with the IRS. Instead, the taxpayer must obtain from such purchaser, at the earliest of when the title to the item shifts or when the shipment occurs, *either* (a) a written order or sales contract that shows the taxpayer will ship the item to a foreign destination, or (b) if delivery by the taxpayer will occur in the United States, a statement that shows *both* (1) the item is being purchased either to fill an existing or future order for delivery to a foreign destination or for resale to another person in the export business who will export the item, and (2) the item will be transported to the foreign destination in due course, prior to use, further manufacture or resale (other than for export).[125]

f. Sale for Use as Supplies for Vessels or Aircraft

The IRS defines "supplies for vessels and aircraft" as "fuel supplies, ships' stores, sea stores, or legitimate equipment on vessels of war of the United States or of any foreign nation, vessels employed in the fisheries or in the whaling business, or vessels actually engaged in foreign trade or trade[126] between the Atlantic and Pacific ports of the United States or between the United States and any of its possessions."[127] Most of the terms in this definition are further defined in Treas. Reg. § 48.4221-4(b).

Additional requirements:

- With respect to a taxpayer's sale of an item for a purchaser's use as supplies for civil aircraft registered in a foreign country and employed in foreign trade or trade between the United States and one of its possessions, the sale will not be tax-free *unless* the Secretary of Commerce advises the Secretary of the Treasury that the foreign country permits or will permit substantially the same reciprocal privileges for aircraft registered in the United States. If such reciprocity is discontinued, tax-free treatment will not apply after the date the Secretary of Commerce notifies the Secretary of the Treasury of such discontinuance.[128]
- Tax-free treatment for this type of sale will not apply to resales (even if, at the time of the initial sale by the taxpayer, the parties know the item will be resold for the tax-free purpose); in order to be a tax-free sale, the sale must be made directly from the taxpayer to the authorized agent (or other specified individuals) of a vessel or aircraft for use as vessel or aircraft supplies.
- A sale to passengers or crew members of a vessel or aircraft is *not* a tax-free sale.[129]

Special registration requirement:

- If the purchaser is not registered with the IRS, then tax-free treatment will apply only if, at or before the sale, the taxpayer obtains from the vessel or aircraft's owner, or chartered or authorized agent an executed exemption certificate in the form of Treas. Reg. § 48.4221-4(d)(2)(iii), and the taxpayer keeps the certificate in the taxpayer's possession.[130] If the taxpayer *regularly or frequently (as opposed to occasionally)* sells items to the same purchaser for this tax-free purpose, then one certificate may be used to cover all orders for a time period of not more than three consecutive years.[131]

2. Exclusivity Requirement

Among the requirements for a tax-free sale to a nonprofit educational organization or to a state or local government is that the sale be for the *exclusive* use of the qualifying purchaser. At least for purposes of sales to state and local governments, rulings and regulatory provisions indicate that the exclusivity requirement will not be satisfied (and a sale will not be tax-free) if, at the time of the sale, the qualifying purchaser intends to resell the item, even if (1) the sale is made to its employees in order to perform its duties within the scope of employment, and (2) the qualifying purchaser intends to first use the item prior to the resale.[132]

3. Expanded Definition of State and Local Government

Under certain circumstances, nonprofit volunteer ambulance associations[133] or fire departments may qualify for tax-free treatment under section 4221 for sales to state or local governments. (See Rev. Rul. 77-388, 1977-2 C.B. 365 (1977); Rev. Rul. 77-387, 1977-2 C.B. 364 (1977); see also Letter Ruling 200521017 (Mar. 1, 2005); Letter Ruling 200440008 (June 10, 2004).) However, the determinations in these rulings are very fact-specific, and taxpayers should consult their tax counsel prior to treating a sale to such a purchaser as a section 4221 tax-free sale. In addition, in at least two rulings, the IRS found that a state community college may be treated as a political subdivision of the state for purposes of tax-free treatment under IRC § 4221.[134]

4. Sales to the United States are Not Tax-Free

Unlike sales to state and local governments, which may be tax-free under IRC § 4221(a)(4), there is no tax-free treatment for sales to the U.S. government (or its administrative agencies). Under a different statutory section, IRC § 4293, the Secretary of the Treasury has the *authority* to issue a tax exemption if the vehicle is for the exclusive use of the United States and the Secretary determines that (1) the exemption would relieve a substantial burden or expense, and (2) the full benefit of the exemption would accrue to the United States. However, although the Secretary has the power to issue such an exemption, *it has not yet chosen to exercise this power*.[135]

5. Tax-Free Sales for Resale Versus Tax-Free Sales Under IRC § 4221

a. Sales for Resale for Exports

In Letter Ruling 200036038 (June 8, 2000), a taxpayer treated its sale of certain vehicles to a Canadian dealer as a tax-free sale for export under IRC § 4221. The IRS concluded that the tax-free sale provisions for exports did not apply to those sales, and that those sales triggered FET. The rationale used by the IRS was that a tax-free sale for export applies only to a taxable sale, and a sale for resale is not a taxable sale. This is an interesting position to take, given that tax-free sales for export under IRC § 4221 expressly apply to resales for export. Nevertheless, the IRS concluded that in order for the taxpayer to sell vehicles to a Canadian dealer tax-free, the taxpayer would need to satisfy the requirements for a tax-free sale for resale under Treas. Reg. § 48.4052-1. (For a more detailed discussion of this issue, see Section IV.B.)

b. Sales for Resale for Use in Further Manufacture

It is unclear whether a sale for resale certificate can be used if the initial sale is for use in further manufacturing. In a typical sale for resale, the same item is being sold twice, and the first seller merely passes the tax liability along to the second seller. However, when further manufacturing occurs, the modified item is treated as a new item for purposes of section 4051 tax. Thus, in a sale for further manufacturing, the first sale involves a different item than the second sale, so any tax triggered by the first sale is not merely postponed until the second sale. In light of this, the IRS may require a taxpayer to use a further manufacturing certificate rather than a resale certificate (see Section III for a discussion of resale certificates) when the original seller knows the item will be further manufactured. (However, in light of the fact that the 75 Percent Rule excludes from "further manufacturing" most modifications to taxable articles, this provision will rarely come into play.)

6. Refunds and Credits

If tax is paid on an item involved in a transaction that qualifies for a tax-free treatment under IRC § 4221, a refund or credit under certain circumstances may be available.[136]

C. Questions and Answers

1. Purchaser is Exempt from Federal Income Tax

A nonprofit 501(c)(3) corporation that is exempt from federal income tax is interested in buying trucks. Does the fact that the corporation is exempt from federal income tax mean that it also qualifies for tax-free treatment under IRC § 4221?

Answer: No

IRC § 4221 identifies particular types of sales to end-users that may be conducted tax free for purposes of the section 4051 tax. However, this list does not include sales to end-users that are exempt from federal income tax. Thus, the mere fact that a corporation is exempt from federal income tax is insufficient to confer tax-free status on the retail sale of trucks to the corporation. However, in the case of a tax-free sale to a nonprofit educational organization or to a qualified blood collector, an exemption from federal income tax is one of several requirements that must be satisfied in order to qualify for tax-free status under IRC § 4221.

2. City Agreement to Re-sell Vehicles to a Third Party

A city representative approached a seller about purchasing certain new trucks. The representative stated that the seller should contact a local utility company for the exact specifications because the utility company has agreed to buy the trucks from the city 18 months after the city purchases them. Does the city's agreement with the utility company affect the truck seller's ability to sell the city the trucks on a tax-free basis under IRC § 4221?

Answer: Yes

A seller may sell trucks tax-free to state or local governments under IRC § 4221(a)(4) if certain requirements are satisfied. One of these requirements is that the sale must be for the "exclusive use" of the governmental entity. A sale to a governmental entity for resale does not meet this exclusive use requirement (even if the resale will not occur until after the governmental entity uses the trucks). In this case, because the seller is aware of the agreement between the city and the utility company, the seller likely would not be able to sell the trucks tax-free pursuant to IRC § 4221(a)(4).

3. Sales to the United Nations and the American Red Cross

Sales of trucks to the U.S. government do not qualify for tax-free treatment under IRC § 4221, but what about sales to the U.N. or the American Red Cross?

Answer: Sales to the U.N. and the American Red Cross are not tax-free under IRC § 4221. However, they may be nontaxable pursuant to other statutory provisions or revenue rulings.

In Rev. Rul. 90-83, 1990-2 C.B. 219 (Oct. 9, 1990), the IRS determined that sales to the U.N., subject to certain conditions, would not be taxable under IRC § 4051. In that ruling the IRS explained that under the Convention on the Privileges and Immunities of the United Nations, the United States agreed to "make administrative arrangements, whenever possible, for remission or return of certain duties and taxes when the United Nations makes purchases for its official use." The IRS noted that it treats the U.N. similarly to individual states for purposes of determining whether such remissions or returns could be made for certain excise taxes, including section 4051 tax. Rev. Rul. 90-83 indicates that in order to conduct a tax-free sale to the U.N., a taxpayer must receive a signed statement from the U.N. that (1) identifies the name and title of the authorizing official, and (2) states that the trucks are purchased for the U.N.'s official use.

With respect to sales of trucks to the American Red Cross, an exemption from certain excise taxes, including the tax on heavy trucks, was enacted under IRC § 4293 in 1979. This exemption applies to sales to and for the exclusive use of the American Red Cross. Both purchaser and seller must be registered with the IRS in order for such sales to be exempt. (See Treas. Reg. § 48.4222(d)-1(b).) At the time this exemption was authorized, the tax on heavy trucks was a manufacturer's level tax under IRC § 4061. Although this exemption likely applies similarly to the current retailer's tax under IRC § 4051, taxpayers should confirm this with their tax counsel.

4. True or False

When a U.S. manufacturer sells taxable truck bodies to a Canadian dealer, the manufacturer can choose to conduct the sale on a tax-free basis either as a sale for resale or as a sale for export.

Answer: False

In a year 2000 Letter Ruling, the IRS indicated that a sale of a taxable item to a foreign dealer that will re-sell the item can be conducted on a tax-free basis only as a sale for re-sale (and not as a sale for export). Although the Internal Revenue Code does not indicate that such transactions can only be made tax-free as sales for resales, the conservative approach is to follow what the IRS apparently feels is the only correct approach. Retail sellers making sales to foreign dealers should consult with their tax advisers.

5. True or False

In order to make a tax-free sale of a taxable trailer to a state Department of Transportation, the DOT must be registered with the IRS for tax-free transactions.

Answer: False

State and local governments cannot register with the IRS for tax-free transactions. However, to sell tax-free to a state DOT, an exemption certificate must be obtained, signed by an authorized officer or employee, in the form set forth at Treas. Reg. § 48.4221-5(c).

VII. EXEMPTIONS FROM FET BASED ON THE TYPE OF ARTICLE SOLD (IRC § 4053 AND IRC § 7701(A)(48))

There are certain types of chassis, bodies, tractors, vehicles, or parts that simply are not subject to FET. IRC § 4053 describes 10 of these items. A first retail sale (or first use) of any of these ten items will not trigger FET. In addition to these ten nontaxable items, two other exclusions from FET are described in IRC § 7701(a)(48). These two exclusions are for specific vehicles Congress has categorized as non-highway vehicles. Since FET applies only to components of a so-called "highway vehicle," FET does not apply if a vehicle satisfies one of these two categories of a non-highway vehicle.

Unlike the "Identity or Use" tax-free sales under IRC § 4221 (discussed in Section VI) or the tax-free sales for resale (discussed in Section II), the non-taxable sales discussed in this section may be sold tax-free without any registration, certification, or other specific documentation requirements.[137] So long as the item the taxpayer sells or uses is the type of item described in IRC § 4053 or IRC § 7701(a)(48), that item is not subject to tax.

A. Overview

The 10 listed items under IRC § 4053 that may be sold tax-free are:

1. "Camper Coaches Bodies for Self-Propelled Mobile Homes"
2. "Feed, Seed, and Fertilizer Equipment"
3. "House Trailers"
4. "Ambulances, Hearses, Etc."
5. "Concrete Mixers"
6. "Trash Containers, Etc."
7. "Rail Trailers and Rail Vans"
8. "Mobile Machinery"
9. "Idling Reduction Devices"
10. "Advanced Insulation"

The nontaxable vehicles defined as non-highway vehicles under IRC § 7701(a)(48) are:

- "Off-highway transportation vehicles"
- "Nontransportation trailers and semitrailers"

The complete language of each of these non-taxable categories, as published in the applicable statutes, is as follows:

IRC § 4053:

1. ***Camper Coaches Bodies For Self-Propelled Mobile Homes. – Any article designed – (a) to be mounted or placed on automobile trucks, automobile truck chassis, or automobile chassis, and (b) to be used primarily as living quarters or camping accommodations.***
2. ***Feed, Seed, And Fertilizer Equipment. – Any body primarily designed – (a) to process or prepare seed, feed, or fertilizer for use on farms, (b) to haul feed, seed, or fertilizer to and on farms, (c) to spread feed, seed, or fertilizer on farms, (d) to load or unload feed, seed, or fertilizer on farms, or (e) for any combination of the foregoing.***
3. ***House Trailers. – Any house trailer.***
4. ***Ambulances, Hearses, Etc. – Any ambulance, hearse, or combination ambulance-hearse.***
5. ***Concrete Mixers. – Any article designed – (a) to be placed or mounted on an automobile truck chassis or truck trailer or semitrailer chassis, and (b) to be used to process or prepare concrete.***
6. ***Trash Containers, Etc. – Any box, container, receptacle, bin or other similar article – (a) which is designed to be used as a trash container and is not designed for the transportation of freight other than trash, and (b) which is not designed to be permanently mounted on or permanently affixed to an automobile truck chassis or body.***
7. ***Rail Trailers And Rail Vans. – Any chassis or body of a trailer or semitrailer which is designed for use both as a highway vehicle and a railroad car. For purposes of the preceding sentence, piggy-back trailer or semitrailer shall not be treated as designed for use as a railroad car.***
8. ***Mobile Machinery. – Any vehicle which consists of a chassis – (a) to which there has been permanently mounted (by welding, bolting, riveting, or other means) machinery or equipment to perform a construction,***

manufacturing, processing, farming, mining, drilling, timbering, or similar operation if the operation of the machinery or equipment is unrelated to transportation on or off the public highways, (b) which has been specially designed to serve only as a mobile carriage and mount (and a power source, where applicable) for the particular machinery or equipment involved, whether or not such machinery or equipment is in operation, and (c) which, by reason of such special design, could not, without substantial structural modification, be used as a component of a vehicle designed to perform a function of transporting any load other than that particular machinery or equipment or similar machinery or equipment requiring such a specially designed chassis.

9. *Idling Reduction Device. – Any device or system of devices which – (a) is designed to provide to a vehicle those services (such as heat, air conditioning, or electricity) that would otherwise require the operation of the main drive engine while the vehicle is temporarily parked or remains stationary using one or more devices affixed to a tractor, and (b) is determined by the Administrator of the Environmental Protection Agency, in consultation with the Secretary of Energy and the Secretary of Transportation, to reduce idling of such vehicle at a motor vehicle rest stop or other location where such vehicles are temporarily parked or remain stationary.*
10. *Advanced Insulation. – Any insulation that has an R value of not less than R35 per inch.*

IRC§7701(a)(48):

- *(A) Off-Highway Transporation Vehicles – (i) In general. – A vehicle shall not be treated as a highway vehicle if such vehicle is specially designed for the primary function of transporting a particular type of load other than over the public highway and because of this special design such vehicle's capability to transport a load over the public highway is substantially limited or impaired, (ii) Determination of vehicle's design. – For purposes of clause (i), a vehicle's design is determined solely on the basis of its physical characteristics, (iii) Determination of substantial limitation or impairment. – For purposes of clause (i), in determining whether substantial limitation or impairment exists, account may be taken of factors such as the size of the vehicle, whether such vehicle is subject to the licensing, safety, and other requirements applicable to highway vehicles, and whether such vehicle can transport a load at a sustained speed of at least 25 miles per hour. It is immaterial that a vehicle can transport a greater load off the public highway than such vehicle is permitted to transport over the public highway.*
- *(B) Nontransportation Trailers And Semitrailers. – A trailer or semitrailer shall not be treated as a highway vehicle if it is specially designed to function only as an enclosed stationary shelter for the carrying on of an off-highway function at an off-highway site.*

NOTE: The titles used in sections 4053 and 7701(a)(48) can be misleading; it is important to carefully review the complete language of these non-taxable categories in order to determine if a particular product satisfies all the necessary requirements for tax-free treatment. The IRS, in the past, generally has interpreted these categories of non-taxable items narrowly (*i.e.*, it will interpret the language of the non-taxable category in a manner that will apply to less rather than more products). Accordingly, taxpayers always should consult with their tax counsel prior to relying on any of these non-taxable categories.

The non-taxable categories that appear to be of most interest to the IRS and/or the taxpayer in recent years (or have the potential to generate the most confusion among taxpayers) are: (1) IRC § 4053(1) Camper Coaches Bodies; (2) IRC § 4053(2) Feed, Seed and Fertilizer Equipment; (3) IRC § 4053(5) Concrete Mixers; (4) IRC § 4-53(8) Mobile Machinery; (5) IRC § 4053(9) Idling Reduction Units; and (6) IRC § 7701(a)(48)(A) Off-Highway Transportation Vehicles. These six tax-free categories will be the focus of more detailed discussion below.

1. "Primary" Use

"Primary" or "primarily" are used in the description of several of the non-taxable vehicles or other items identified in the chart above. Therefore, in determining if a specific nontaxable category applies, it is important to understand the intended meaning of this term. In 2004, in the context of determining whether a vehicle was a tractor or a truck, the IRS issued a Revenue Ruling finding that the word "primary" means "principally" or "of first importance."[138] The IRS also specifically noted that the word primary does not mean "exclusive."[139]

2. The Importance of Accurate Marketing Materials

Marketing materials may serve an important role in determining whether a particular article meets the definition of the exempt article or category. When creating or using marketing materials, the understandable temptation is to focus on a product's versatility in an attempt to attract the broadest pool of potential customers. However, marketing materials that are written too broadly may undermine a taxpayer's position that a product should be treated as nontaxable.

For example, if marketing literature emphasizes a truck body's multipurpose design, it may be difficult to convince an IRS agent that the body is primarily designed for hauling feed, seed, or fertilizer on farms (and therefore the body satisfies the section 4053(2) exemption). Similarly, if marketing materials tout a vehicle's towing capabilities, it will be harder to persuade an IRS agent that the vehicle is designed primarily as living quarters (*i.e.*, that the body satisfies the 4053(1) exemption). The flip side, of course, is that when marketing materials are consistent with the requirements of a tax-free category, they can be helpful evidence in presenting your case to the IRS. In short, marketing materials should be accurate, and your tax treatment of a product should be consistent with the information in your marketing materials.

B. A Closer Look at a Few of the Exemptions

As noted above, we will now go into greater detail on several of the listed exemptions. This list is not exhaustive, and we cannot cover all of the potential issues, even for the exemptions discussed. Note also that in recent years the IRS has generally interpreted all of the categories of non-taxable vehicles and items narrowly (*i.e.*, in a manner that applies to fewer rather than more products). Taxpayers always should consult with their tax adviser prior to relying on any of the non-taxable categories.

1. IRC § 4053(1) Camper Coach Bodies

Any article designed –

- To be mounted or placed on automobile trucks, automobile truck chassis, or automobile chassis
- To be used primarily as living quarters or camping accommodations

Relatively recent rulings applying the "Camper Coach" exemption raise two important issues: (1) Whether a chassis is a conventional chassis or one built specifically to move motorhome bodies, and/or (2) Whether the primary design of a vehicle is for towing or for living accommodations.

a. Is it a Specially-Built Chassis?

First, it is important to note that under the plain language of the statute, this exemption does not appear to apply to chassis, but only to an article installed on a chassis.[140] However, a chassis designed for use with a motorhome/mobile home body still might be non-taxable because it may not be a taxable truck chassis at all (but instead a specially-designed mobile home chassis). In at least one revenue ruling, the IRS has stated that where chassis "are specifically designed, constructed, and predominantly used for the transportation of mobile home bodies and not to haul freight or cargo, the chassis are not taxable as automobile truck chassis…."[141]

As discussed above, FET on truck chassis applies only to "automobile truck chassis." Therefore, if the IRS determines that a truck chassis is not an "automobile truck chassis" (but instead is a specially designed motor home/mobile home chassis), that chassis should not be subject to FET. Obviously, this means that the determination of whether or not a chassis is a conventional chassis could have important tax consequences.

Of course, merely using a chassis with a motorhome/mobile home is not enough to render the chassis non-taxable. In other words, a conventional chassis will continue to be taxable even if it is used as a component of a motorhome/mobile home.[142] In making this determination, taxpayers should not simply rely on a manufacturer's description of the chassis. Instead, taxpayers should carefully analyze the components of the chassis to determine whether a chassis is a mobile home/motorhome chassis or a conventional chassis (and you should expect the IRS to do the same in the case of an audit).[143]

b. Is the Primary Design for Towing or Living Accommodations?

The question of whether a vehicle is primarily designed for towing or living accommodations appears to revolve around so-called toterhome vehicles. *If a vehicle is primarily designed to tow, it does not meet the "Camper Coach" exemption* (section 4053(1)). Even if the majority of the bed space is for living accommodations, the IRS still may determine that the vehicle is primarily designed for towing, based on factors such as the size and placement of a hitch and excess rear frame rail space that could accommodate a substantial hitch.[144]

On the other hand, the IRS also has determined that a vehicle can be non-taxable under IRC § 4053(1) even if it has a towing package and therefore, is presumed to be a tractor. If a taxpayer can demonstrate that, despite the towing package, the body is primarily designed for living accommodations, the tractor presumption will be rebutted and the body will be exempt from tax under IRC § 4053(1).[145]

2. IRC § 4053(2) Feed, Seed and Fertilizer Equipment

Any body primarily designed –

- To process or prepare seed, feed, or fertilizer for use on farms
- To haul feed, seed, or fertilizer to and on farms
- To spread feed, seed, or fertilizer on farms
- To load or unload feed, seed, or fertilizer on farms
- For any combination of the foregoing

First, taxpayers should understand some of the general situations in which this tax-exempt category does not apply:

- The exemption does not apply to any article other than *bodies*. Therefore, even if a body is deemed to be exempt under this category, the seller must still engage in a *separate* analysis regarding the taxability of the chassis on which that body is mounted. If that chassis would otherwise be taxable, it is still taxable even if the body is FET-exempt.
- The exemption does not apply to bodies designed for agricultural commodities, in general (such as potatoes, beets and grains), but only to those bodies designed for feed, seed, or fertilizer.
- It is not sufficient to show that a body is used for the feed, seed, or fertilizer purposes described in § 4053(2)—it must be "primarily designed" for those purposes.[146]
- It is not sufficient to show that a body is primarily designed to haul feed, seed, or fertilizer over the highway to the market, distributor, or other end-user; it must be primarily designed for transporting feed, seed, or fertilizer *to and on* farms (or for other uses *on the farms* that are specified in IRC § 4053(2)).

In addition, the IRS has issued technical advice memoranda clarifying that a conveyor belt and a powered rear discharge door are not sufficient to demonstrate a body satisfies the requirements of this exemption, noting that these design features also are useful for other purposes, such as unloading at market, and for other commodities.[147] As discussed above, the taxpayers' own marketing materials are often viewed by the IRS as important indicators whether bodies at issue meet the primary design standard of the exemption, and are often cited by the IRS.[148]

Because of the nature of these articles, the IRS will almost invariably be able to argue that the body was designed for purposes other than those listed in the exemption—if it is inclined to do so. That is because generally speaking, a body designed primarily for use with feed, seed, or fertilizer could arguably also be compatible for use with products that have physical characteristics similar to feed, seed, or fertilizer.

On the other hand, in the three rulings listed below involving the feed, seed, or fertilizer exemption, the IRS found that the body was not taxable as a result of this exemption.[149]

1. Letter Ruling 200826022 (Mar. 24, 2008) (in addition to other design features, the trailer was redesigned to replace many high-tensile steel components with extruded aluminum, rendering the trailer less strong and durable, and unable to be unloaded via a tip dumper).
2. TAM 200504034 (November 1, 2004) (the semitrailer body, designed for sticky, wet and bulky seed, feed and fertilizer, has aluminum extrusions housing a chain and belt conveyor system, as well as other characteristics such as steep side slopes, plastic liners and wide belt systems).
3. Letter Ruling 200939005 (June 23, 2009) (the taxpayer hired an engineer to design a vehicle specifically for moving corn gluten; some examples of the trailer's design features include riveted construction, sloped sidewalls made from corrugated aluminum and several anti-corrosion features including liners to the trailer's roof, a sealed door, a special tarp, and a belt floor consisting of a special grade rubber).

3. Concrete Mixers

Any article designed –

- To be placed or mounted on an automobile truck chassis or truck trailer or semitrailer chassis
- To be used to process or prepare concrete

Taxpayers need to be aware that the IRS has strictly applied this exemption only to those components of a chassis or body that actually *process or prepare* concrete (and not, for example, those components that simply transport concrete ingredients).[150] *In other words, the IRS does not necessarily apply this exemption to an entire body or an entire chassis, but on a component-by-component basis.* For example, in Technical Advice Memorandum 9509004 (November 7, 1994), the IRS determined that the compartments and hoppers of a mobile concrete dispenser were taxable, but that the components of the mixer/auger apparatus was not taxable under IRC § 4053(5). Similarly, in Technical Advice Memorandum 9306002 (October 23, 1992), the IRS determined that only specific chassis components (*i.e.*, a specially designed fender and certain in-cab controls) were nontaxable under this exemption.

NOTE: Certain concrete-related vehicles may also be exempt from FET under the so-called "mobile machinery exemption."[151] However, as discussed below, the IRS has in recent years interpreted this non-taxable category of vehicles extremely narrowly.

4. Mobile Machinery

Any vehicle which consists of a chassis –

- To which there has been permanently mounted (by welding, bolting, riveting, or other means) machinery or equipment to perform a construction, manufacturing, processing, farming, mining, drilling, timbering, or similar operation if the operation of the machinery or equipment is unrelated to transportation on or off the public highways
- Which has been specially designed to serve only as a mobile carriage and mount (and a power source, where applicable) for the particular machinery or equipment involved, whether or not such machinery or equipment is in operation
- Which, by reason of such special design, could not, without substantial structural modification, be used as a component of a vehicle designed to perform a function of transporting any load other than that particular machinery or equipment or similar machinery or equipment requiring such a specially designed chassis

This exemption focuses entirely on the chassis; however, if the chassis satisfies the three tests described above, then the *entire vehicle* (chassis and body) may be sold tax-free.[152]

Although qualifying mobile machinery vehicles are exempt from section 4051 tax, taxpayers should expect the IRS to interpret the scope of the mobile machinery exemption extremely narrowly (*i.e.*, the IRS will interpret the exemption to apply to very few vehicles).[153] In two relatively recent court cases, the Federal Claims Court supported a narrow interpretation of the mobile machinery exception.[154] As a result of these two decisions, the IRS is likely to be aggressive in determining a vehicle does not meet the mobile machinery exemption.

For example, if a chassis is capable of carrying any items other than the subject machinery (e.g., via a pintle hook, incidental storage compartments, etc.), the IRS likely will find that the vehicle does not satisfy the mobile machinery exemption because it fails the second of the three requirements (*i.e.*, the chassis is not *solely* designed to carry the mobile machinery). Similarly, if the vehicle can carry without substantial structural modification, a load other than the mobile machinery, the IRS likely would find that a vehicle does not satisfy the third requirement *even if* it would be uneconomical to carry such a load.

REMEMBER: a vehicle must satisfy all three tests listed in IRC § 4053(8) in order to be exempt from tax.

The determination of whether a vehicle will satisfy the mobile machinery exemption is highly fact-specific. Therefore, taxpayers are strongly urged to consult with their tax adviser prior to treating a vehicle as non-taxable under the mobile machinery exception.

5. **Idling Reduction Units (such as Alternative Power Units)**
   - *Idling Reduction Device. – Any device or system of devices which – (a) is designed to provide to a vehicle those services (such as heat, air conditioning, or electricity) that would otherwise require the operation of the main drive engine while the vehicle is temporarily parked or remains stationary using one or more devices affixed to a tractor, and (b) is determined by the Administrator of the Environmental Protection Agency, in consultation with the Secretary of Energy and the Secretary of Transportation, to reduce idling of such vehicle at a motor vehicle rest stop or other location where such vehicles are temporarily parked or remain stationary.*

An exemption for idling reduction units (as well as advanced insulation) was added to IRC § 4053 by the Energy Improvement and Extension Act of 2008. There are two important limitations to the application of the idling reduction unit exemption:

First, before an idling reduction unit may be sold tax-free, the Environmental Protection Agency must determine that the unit reduces vehicle idling, as described in the (b) test, above. In other words, it is not sufficient to demonstrate to the IRS, after the unit has been sold, that the unit does in fact reduce idling; the EPA must have made this determination prior to the taxpayer's sale of the unit. The EPA has published a list of units that satisfy the (b) test (have been determined to reduce idling).

See www.epa.gov/smartway/technology/excise-tax.htm#apu. This published list is effective as of August 18, 2011, and may be updated periodically.

Second, the language in this exemption applies only to idling reduction units affixed to *tractors* (*e.g.*, it does not apply to such units when they are affixed to trucks). It appears that Congress may not have intended this limitation, and may, in the future, expand the idling reduction exemption to apply to trucks and other taxable items under IRC § 4051. However, unless and until the language of the exemption is amended by Congress to reflect this change, the IRS will apply the idling reduction exception only to units affixed to tractors.

6. **Off-Highway Vehicles**
   - In general.—A vehicle shall not be treated as a highway vehicle if such vehicle is specially designed for the primary function of transporting a particular type of load other than over the public highway and because of this special design such vehicle's capability to transport a load over the public highway is substantially limited or impaired.
   - Determination of vehicle's design.—For purposes of clause (i), a vehicle's design is determined solely on the basis of its physical characteristics.
   - (iii) Determination of substantial limitation or impairment.—For purposes of clause (i), in determining whether substantial limitation or impairment exists, account may be taken of factors such as the size of the vehicle, whether such vehicle is subject to the licensing, safety, and other requirements applicable to highway vehicles, and whether such vehicle can transport a load at a sustained speed of at least 25 miles per hour. It is immaterial that a vehicle can transport a greater load off the public highway than such vehicle is permitted to transport over the public highway.

As discussed above, FET applies only to highway vehicles. Therefore, if a vehicle meets the requirements of an off-highway vehicle, as described in IRC § 7701(a)(48)(A), that vehicle is not subject to FET.[155]

There are five general principles a taxpayer should keep in mind when determining if the off-highway exception applies.

1. The off-highway exception applies to the entire vehicle, and the special design features can be on either the body or chassis, or both.

This means that if *either* the body or the chassis has special design features that satisfy the requirements, then the entire vehicle is exempt (*i.e.*, neither the body nor the chassis will be subject to FET).

2. In order for a vehicle to be considered an off-highway vehicle under IRC § 7701(a)(48)(A), it must satisfy both of the tests identified above.

In other words, the vehicle must be specially designed for the primary function of transporting a particular type of load other than over the public highway (the so-called "Special Design Test"), *and* because of this special design, such vehicle's capability to transport a load over the public highway is substantially limited or impaired (the so-called "Impairment Test").

3. The term "highway" refers to any non-private road; it does not refer only to interstate freeways.

As a result, whether a vehicle is capable, qualified, or licensed to operate on interstate highways is not determinative.

4. This exception is a design test, not a use test.

This means that the applicability of the exemption depends solely on the design features of the article. The mere fact that a customer may not ever *use* the vehicle on a highway is not sufficient to demonstrate that the vehicle satisfies the off-highway exception. This is the case *even if* the customer does not register the vehicle for highway use and/or provides the taxpayer with a certified statement that it will not use the vehicle on the highway. The exception focuses on the *design* of the vehicle, and not a customer's individual use of the vehicle.[156]

5. A vehicle designed for and used on the highway may still satisfy the off-highway exception.

Like the mobile machinery exemption, the IRS interprets the off-highway exception very narrowly. It is important to understand that, under the plain language of the exception, a vehicle can be designed for highway use and still satisfy the exception. A nontaxable off-highway vehicle need only be designed for the *primary* function of transporting a particular load off the highway; therefore, the exception permits a vehicle to have a *secondary* function of highway transportation. Note however, that the IRS has taken the position that the off-highway exception does not apply to any "dual-use" vehicle—a vehicle designed for both on- and off-road use (*e.g.*, a vehicle that satisfies Federal Motor Vehicle Safety Standards, even though it is primarily designed for off-road use).

However, in 2010, the Sixth Circuit issued a decision rejecting that position.[157] In that case, the court determined the relevant factor in applying the Special Design Test was not whether the vehicle was designed for both off-highway and on-highway use, but whether the vehicle was designed for the *primary* function of off-highway use. The court stated that "[h]ighway use that is more than incidental does not necessarily mean the truck was not designed primarily for off-highway use." In other words, a vehicle could be designed for both uses, and still satisfy the off-highway exception, *so long as* the vehicle's design features demonstrated that the vehicle's most important function was for off-highway applications. This is a significant decision, but it is too early to tell if it will change the way the IRS applies the off-highway exception (*i.e.*, it will convince the IRS that a vehicle can satisfy the Special Design Test of the off-highway exception even if it also is designed for on-highway use).[158] In any event, as noted above, in order to satisfy the off-highway exception a taxpayer also must demonstrate that the vehicle meets the Substantial Impairment Test, and the Substantial Impairment Test often is the more difficult of the two tests to satisfy.

Like the mobile machinery exemption, the application of the off-highway exception is highly fact-specific. Therefore, it is strongly recommended that taxpayers consult with their tax counsel prior to treating a vehicle as non-taxable under the off-highway exception.

C. Questions and Answers

1. Non-Highway Use and the Off-Highway Exception
A customer is willing to certify that the vehicle it purchases from a modifier will be used exclusively at job sites and will not travel over public roads. Does this type of certificate qualify the vehicle as a nontaxable "off-highway" vehicle?

Answer: No.
The Internal Revenue Service addressed this issue in technical advice memorandum 200333001. Citing Rev. Rul. 70-350, 1970-2 C.B. 262 (1970), the IRS ruled that "[t]he classification of a taxable highway vehicle is based on the design of the vehicle and not the use of the vehicle." *See* also Rev. Ruling 58-424, 1958-2 C.B. 762 (1958) (finding that a certain dump truck chassis is subject to the manufacturers excise tax, predecessor to FET, even though the purchaser uses the chassis solely underground in a mine) and Letter Ruling 8923014 (March 9, 1989) (finding that the "off-highway" exception did not apply and noting that the fact that the tractor at issue "is not operated on, or licensed for use on, public highways is not relevant").

The IRS reached a similar conclusion in TAM 200403001 (October 16, 2002), stating that "[t]he classification of an otherwise taxable highway vehicle is based on the design of the vehicle and is not affected by the use for which a particular customer purchases a vehicle."

In other words, the application of the off-highway exception to a specific truck configuration will not vary from purchaser to purchaser. If the *design* of that truck configuration does not satisfy the definition of an off-highway vehicle, then every sale of that configuration will be subject to FET (unless another tax-exemption applies), regardless of how any one purchaser intends to use the truck.

And, the certification by the purchasers does not affect the retail seller's tax liability under IRC § 4051 with respect to the subject vehicles. *See* TAM 200333001 (February 26, 2003).

Although the TAMs cited above appear to have been decided under an older definition of an off-highway vehicle, the reasoning in these rulings should equally apply under the revised definition. Accordingly, the fact that your customer is willing to certify that it will not use the vehicle on the highway is not sufficient to satisfy the off-highway exemption and *it does not relieve the modifier from FET liability*.

2. Vehicle Used to Haul Fertilizer to and on Farms
A dealer sells certain self-unloading trucks to farmers, who use them primarily to haul farm products, such as seed potatoes, sugar beets and fertilizer, both to and on farms. Each of these truck bodies contains a powered conveyor belt and powered rear discharge door, which makes these vehicles significantly more expensive than a standard truck. Are these trucks likely tax-exempt under IRC § 4053(2)?

Answer: No, not likely.
Under IRC § 4053(2), it is not sufficient that the bodies are *used* to haul feed, seed or fertilizer to and on farms; a retailer seller must be able to show that the bodies were *primarily designed* to haul such products there. (*See* Rev. Rul. 75-462, 1975-2 C.B. 419 (1975) (noting that a body "designed to haul low density farm commodities," including feed and fertilizer, on both the highway and the farm, remains taxable under IRC § 4063(a)(2)(B), the predecessor under the manufacturer's tax to IRC § 4053(2), where "the body does not have specific features that indicate it is primarily designed to haul feed, seed, or fertilizer to and on farms"). (*See* also Rev. Rul. 76-361, 1976-2 C.B. 333 (1976).)

In addition, the IRS specifically has noted that outfitting a truck body with a conveyor belt and powered rear discharge door is not sufficient to meet the "primary design" test of section 4053(2). (*See* TAM 200002006 (September 23, 1999); TAM 200002008 (September 27, 1999); and TAM 199904038 (October 8, 1998).) Therefore, the bodies in question are not automatically exempt from tax under IRC § 4053(2) simply because they haul fertilizer to and on farms, and are outfitted with a conveyor system.

In each of the three rulings cited above, the IRS determined that the bodies at issue did not satisfy the requirements for the section 4053(2) exemption, despite the fact that in two of these rulings the IRS described the subject bodies' unloading and support system as "elaborate" and noted that it would cost considerably more than a standard body's stationary bed. In determining that IRC § 4053(2) did not apply to the subject bodies in these three rulings, the IRS stated that, unlike bodies that would be bought only for the purpose of hauling feed, seed or fertilizer, the subject bodies were designed to haul a variety of farm products, such as potatoes, beets, and grain.

3. True or False

Sales to the federal government are subject to FET.

Answer: True.

Although the IRS has the authority to permit sales to the federal government to be conducted on an FET-free basis, it has not exercised that authority. As a result, retail sellers must charge FET on sales of taxable articles to the United States.

4. True or False

If a vehicle is used exclusively on a farm, and will not be registered for highway use, it can be sold tax-free under the exemption for feed, seed, and fertilizer equipment.

Answer: False.

The exemption for feed, seed, and fertilizer equipment under IRC § 4053(2) is based on the primary design of an article, not its use. The exemption, which applies only to bodies (and not to chassis), is available for articles with special features that demonstrate a primary design to (a) process or prepare feed, seed or fertilizer for use on farms; (b) haul feed or fertilizer to and on farms; (c) spread feed, seed or fertilizer on farms; (d) load or unload feed, seed or fertilizer on farms; or (e) any combination of the foregoing.

5. True or False

An alternative power unit that is on the EPA list of units that reduce idling is not subject to tax when installed on an otherwise taxable truck.

Answer: False.

Tax-free sales of idling reduction units under IRC § 4053 are limited to units that are installed on tractors. An alternative power unit is subject to tax, even if it is on the EPA list of qualifying units, when it is sold in connection with a truck.

6. True or False.

A heavy-duty vehicle is not subject to FET if it is not registered for highway use.

Answer: False.

In order to qualify as an off-highway vehicle, a vehicle must (1) be specially designed for the primary function of transporting a particular type of load off-road, and (2) because of its special design, be substantially limited or impaired in its capability to transport a load over the public highway. The fact that a vehicle is not registered for highway use in any particular case does not make the vehicle a non-highway vehicle unless the design and substantial impairment tests are met.

VIII. FIRST USE AND LEASES

FET is not only triggered by a sale of a taxable chassis, body, or tractor. It also can be triggered by that item's use or lease.

A. First Use

1. Use May Trigger Tax

If a taxable chassis, body, or tractor is used prior to its first taxable sale, the use will trigger FET. In other words, if an otherwise taxable item is used prior to being sold—whether the subsequent sale is taxable or conducted on a tax-free basis—then that first use is subject to tax. Similarly, if a body, chassis, or tractor is "further manufactured," as that term is discussed in Section V, then any use of the further manufactured item prior to a taxable (or tax-free) sale will trigger tax, unless the further manufactured item was sold in a taxable (or tax-free) sale prior to such use. The tax on use is triggered when the use begins.[159]

2. Lease May Trigger Tax

In addition to sales and use, FET also may apply to the lease of taxable chassis, bodies, and tractors. Even though a lease payment may be paid in installments (*e.g.*, on a monthly basis), the lessor's liability for the full amount of the section 4051 tax is triggered when the lease occurs.[160] Therefore, a lessor should consider its options for incorporating the amount of the section 4051 tax into the lease payments. For example, a lessor could require that a lessee pay the entire tax amount at the time of the first payment, or each installment payment could include an equal percentage of the tax amount, or the lessee could pay the entire amount of the tax with the final payment.

B. A Deeper Dive

1. Use

a. Examples of the Use of an Article Triggering FET

The following are a few examples of situations in which the use of a taxable chassis, body, or tractor could trigger FET. (Use in situations other than those described below also may trigger the tax.)

- A dealership buys a truck that it will use in its business for deliveries and for loading and unloading equipment. It modifies the truck so it is better suited for its needs, and those modifications "further manufacture" the truck. The dealership's first use of the modified truck likely would trigger FET.[161]
- A dealership either manufactures or "further manufactures" a truck and uses it as a demonstrator vehicle. After six months, it sells the truck to a customer at a discounted price. The first use of the demonstrator likely would trigger the FET.[162] The subsequent sale of the truck does not trigger tax.[163]
- A dealership purchases a truck tax-free as a sale for resale. *See* Section III. The dealership then decides not to resell the truck, but to use it in its business. The dealership's first use of the truck likely would trigger FET.
- A retail customer in the United States buys a Canadian-manufactured vehicle in Canada, because the Canadian sales price will not include a mark-up for FET. However, the customer does *not* avoid paying the FET by importing the vehicle from Canada. The customer's first use in the United States after importing the vehicle likely would trigger the tax. In such a case, the *customer* would be responsible for paying the tax directly to the IRS.
- A retail customer requests a distributor modify his used trailer and such modifications "further manufacture" the vehicle. (For example, the trailer that previously had a GVW rating of 24,000 pounds now has a GVW rating over 26,000 pounds, and otherwise meets the requirements of a taxable trailer.) The customer retains title to the trailer during and after the modifications. After the trailer has been further manufactured, the customer uses the vehicle. The *customer* may be responsible to pay the FET upon his first use of the vehicle.

b. Sales *After* First Use Irrelevant for FET Purposes

If a first use triggers FET, the good news is that any subsequent sale or use of that same body, chassis, or tractor is not taxable (assuming the body, chassis, or tractor is not further manufactured after its first use.) Of course no subsequent sale or use will alleviate the first user's responsibility to pay the tax, or reduce the amount of tax the first user must pay.[164] This is the case even if the subsequent sale or use could have been conducted as a tax-free sale. *See* Section VI for a discussion on section 4221 sales.) For example, assume a dealer's first use of a vehicle triggers FET. Subsequently, the dealer sells the vehicle to a state government, and that sale would have satisfied the requirements for a tax-free sale to a state or local government (IRC § 4221(a)(4)), if the seller had not already used the vehicle. The dealer remains responsible for the FET, even though the subsequent sale would have been tax free (and the sale to the state government would be nontaxable – even if it did not otherwise qualify as a tax-free sale).

c. Exception for Use in Further Manufacturing

If an item is first used in the process of manufacturing another article, such use generally will not trigger FET.[165]

d. Calculation of Tax on Use

The method for calculating FET that is triggered by the use of an item is discussed in Section IX.

C. Leases

1. Lease May Trigger Tax

In addition to sales, FET also may apply to the lease of taxable chassis, bodies, and tractors.

2. Classification of a Long-Term or Short-Term Lease

In applying FET to a lease, the IRS distinguishes between long-term leases and short-term leases. A long-term lease has a term of one- year or longer;[166] a short-term lease has a term less than one year.[167] In determining the term of a lease, the taxpayer should include any renewal periods. For example if the term of a lease is 9 months, but the lease contains a renewal option for an additional six-month term, the lease would be treated as a long-term lease. *See* Treas. Reg. § 145.4052-1(d)(6). In addition, if successive leases are for the same or substantially the same item and occur in a single transaction or in related transactions, then the IRS will treat those leases as a single lease. *See* Treas. Reg. § 145.4052-1(d)(6).

3. Calculation of Tax on a Lease

The method for calculating FET that is triggered by the lease of an item is discussed in Section IX.

4. Leases are Generally Taxable, but Exceptions Exist

For FET purposes, a long-term lease of a taxable chassis, body, or tractor is treated by the IRS as a retail sale.[168] As with a retail sale, a long-term lease of a taxable chassis, body, or tractor will not trigger FET if the item either were previously involved in a tax-free sale[169] or was previously involved in a prior taxable sale.[170]

For FET purposes, a short-term lease of a taxable chassis, body, or tractor is treated by the IRS as the use of such an item.[171] As noted above in A, a use (*i.e.*, a short-term lease) that occurs prior to a tax-paid or tax-exempt sale, itself will trigger tax. However, if the short-term lease occurs after a tax-paid or tax-free sale, that lease will not be taxable.

5. Sales for Long-Term Leasing

Like sales for resale, sales for long-term leasing can be done on a tax-free basis if the buyer and seller comply with the "sale for resale" certification requirements[172] (discussed in more detail in the context of sales for resale in Section III). However, the subsequent long-term lease would be taxable. For example, assume a manufacturer sells a truck to a buyer who intends to lease the truck to a third party on a long-term basis, and the manufacturer and the buyer comply with the certification requirements for a tax-free sale. In that case, the sale by the manufacturer to the buyer will not trigger FET. The subsequent long-term lease by the buyer to the lessee *will* be taxable.

The ability to conduct the sale between the manufacturer and buyer as a tax-free sale applies *only* if the subsequent lease by the buyer will be a *long-term* lease. It does not apply to sales for short-term leasing.

6. Limited Guidance

Please be aware that there are few published rulings addressing the correct application of FET to leases, especially since the regulations were changed in 1988.[173] In any event, the application of FET is very fact-specific, and taxpayers leasing chassis, bodies and tractors should consult with their tax advisor regarding the application of FET.

D. Questions and Answers

1. True or False

A dealer that uses a taxable tractor in its business and that subsequently sells the tractor will owe tax on the sale of the tractor.

Answer: False

The use of the tractor will be treated as the first retail sale of the tractor and will trigger FET. The subsequent sale of the tractor will not be subject to FET.

2. True or False

A lease with a six-month term and a renewal option for an additional six months is treated as a long-term lease for FET purposes.

Answer: True

A lease of one year or longer duration is treated as a long-term lease. When computing the duration of a lease, a renewal option is included in the calculation.

3. True or False

A manufacturer can sell a taxable tractor on a tax-free basis to a leasing company that will long-term lease the tractor.

Answer: True

The "sale for resale" provisions in Treas. Reg. §§ 48.4052-1 and 4052-1(a)(6) apply to sales for long-term leases. However, the buyer/lessor must provide the seller with a certificate similar to a resale certificate.

IX. CALCULATION OF THE TAX

This section discusses how to calculate the correct amount of section 4051 tax. In general, the section 4051 tax is 12 percent of the price for which a taxable chassis, body or tractor is sold. However, there are exceptions to this rule. The amount of money that is subject to the section 4051 tax (*i.e.*, the "taxable sales price") is not always the same amount the taxpayer actually charges the customer. This section also discusses how to calculate the tax when there is no sale price (*e.g.*, when the tax is triggered by a lease of a taxable item or by the use of a taxable item). In addition, there are some deductions and credits available to taxpayers that will affect the amount of tax ultimately owed by the taxpayer.

A. The Basics

1. Calculation of the Tax, In General

The section 4051 tax is a 12 percent tax, regardless of whether the taxable item being sold is a chassis, body, tractor or part/accessory. (Tax liability for *installing* parts/accessories under the so-called Six-Month Rule—as discussed in Section II—is 12 percent of the part/accessory price *and* installation.)

The IRS states that the taxable sale price should include "the total consideration paid for the article whether that consideration is paid in money, services, or other forms" and "any charge incident to placing the article in condition ready for use."[174] Most simply stated, a taxpayer can determine the tax owed under IRC § 4051 by multiplying 0.12 times the retail sale price it charges its customers.[175] However, there are many exceptions to this rule.

In some cases, the IRS requires that the section 4051 tax be applied to a price that is greater than the price the taxpayer charges its customer. Two common situations in which this occurs are (1) sales that require the addition of the so-called "presumed markup," and (2) sales that (a) are not conducted on an arm's length basis (such as sales between related companies) *and* (b) are conducted for less than fair market price. In other cases, tax is triggered even though there is no retail sale price, such as when tax is triggered by the use[176] or lease[177] of a taxable item. When the IRS requires that a taxpayer apply the 12 percent tax to a different or newly created sales price, that price is often referred to as a "constructive price." Also, there are a number of deductions to which a taxpayer may be entitled that will reduce the taxable sale price of an item (which, in turn, will reduce the amount of tax owed under IRC § 4051). These issues are discussed below.

It is important to be aware that this section discusses some of the common issues and deductions concerning the calculation of the section 4051 tax. However, there may be other circumstances in which a taxpayer should not use the price it charges to its customers as the taxable sale price (*i.e.*, the 12 percent tax instead will be applied to a constructive price). In addition, there may be many other deductions for which a taxpayer is eligible. Therefore, a taxpayer should discuss the specific facts related to its taxable sale with its tax adviser, prior to calculating the section 4051 tax.

2. The Presumed Markup

The presumed markup percentage generally applies to sales in which the taxpayer is the manufacturer, producer or importer of the taxable item in question. For example, a common type of sale where the presumed markup percentage would apply is a retail sale of a taxable item by a manufacturer, producer or importer directly to the retail customer (*i.e.*, the taxable item is not sold through a retail dealer or distributor). The presumed markup percentage is 4 percent, except when the sale involves trailers, semitrailers, and *remanufactured* truck chassis, bodies and tractors. In those cases, the presumed markup percentage is zero.

3. "*Non*-Arm's Length" Sales

The IRS provides that if a sale of a taxable item is not an "arm's length" sale *and* the item is sold for below fair market price, the taxable sale price of the item will not be the price for which it was sold. Instead, the tax will be applied to "the price for which similar articles are sold at retail in the ordinary course of trade, as determined by the" IRS.[178]

Generally speaking, a sale is *not* considered an "arm's length" sale if there is a special relationship or arrangement between the seller and the buyer. More specifically, the IRS defines a *non*-arm's length sale as a sale where (1) "[o]ne of the parties is controlled (in law or in fact) by the other, or there is common control, *whether or not such control is actually exercised to influence the sale price*," or (2) "the sale is made pursuant to special arrangements between a seller and a purchaser."[179]

4. Taxpayer's Use Triggers Tax

If a taxpayer triggers FET by its *use* of a taxable item, rather than its sale of such item, the taxpayer will need to determine the correct "sale" price to which the 12 percent tax applies (*i.e.*, the constructive price). The IRS provides in its regulations that, if the taxpayer's use of an item triggers FET, and the taxpayer regularly makes retail sales of the item on an arm's length basis, the constructive price will be the taxpayer's "lowest established retail price for such articles in effect at the time of the taxable use."[180] The regulations also state that if the taxpayer does not regularly make such retail sales of the item, the constructive price will be determined by the IRS, taking into account "selling practices and price structures of sellers of similar articles."[181]

5. Calculation of Tax for Leases

In a taxable lease transaction, the lessor is responsible for paying the tax. If the lessor is a manufacturer, producer or importer and enters into a taxable long-term or short-term lease, the constructive price (*i.e.*, the price to which the 12 percent tax will apply) generally will be determined by the IRS and will include the presumed markup percentage. If the lessor is not a manufacturer, producer or importer and enters into a taxable long-term or short-term lease, the constructive price, in general, will be calculated based on the price for which the lessor purchased the item, the cost of any parts/accessories added by the lessor (or its agent) and the presumed markup percentage. These constructive price calculations are discussed in more detail below.

6. Deductions and Credits

There are some charges or expenses that may be excluded from the taxable sale price (*i.e.*, the 12 percent tax does not apply to these items). This section discusses a few of the most common exclusions (as well as the tire tax credit) below in B.

B. A Deeper Dive

1. Presumed Markup

a. Why a Presumed Markup?

The presumed markup was created in an effort to equalize the tax imposed under IRC § 4051 for retail sales by both manufacturers and dealers. In other words, the presumed markup percentage was aimed at ensuring that the section 4051 tax applied to a retail price rather than a wholesale (or other discounted) price.[182] For example, if a manufacturer sells a taxable chassis, body, or tractor directly to a retail customer, the sale price generally would not include a retail markup (*i.e.*, the retail dealer's markup of the manufacturer's price, when the dealer sells the taxable item to the customer). Therefore, without a presumed markup percentage, the FET due on such a direct sale generally would be less than if the taxable vehicle had been sold through a retail dealer, even though both types of sales are retail sales. However, as discussed below, the IRS may require a manufacturer to add the presumed markup percentage to its sale price, *even when* the manufacturer's sale price already includes a standard retail markup.

b. What is the Presumed Markup Percentage?

The presumed markup percentage is defined as "the average markup percentage of retailers of articles of the type involved, as determined by" the IRS. (*See* IRC § 4052.) The IRS has determined that, in general, the presumed markup percentage will be 4 percent. However, there are certain items that are excepted from the 4 percent presumed markup percentage. For trailers, semitrailers, and *remanufactured*[183] chassis, bodies, and tractors, the presumed markup percentage is zero. (*See* Treas. Reg. § 145.4052-1(d)(7).) These items have a zero presumed markup percentage based on the IRS's belief that retail dealers do not generally play a role in the sales of such items. Therefore, the general purpose of the presumed markup percentage (*i.e.*, to have a uniform section 4051 tax on retail sales, regardless of whether such sales are sold directly to a retail customer or are sold through a retail dealer) is not served by adding this markup to the sale of those items.[184]

When the presumed markup percentage applies to a sale, the taxpayer should multiply the correct presumed markup percentage times the sale price of the taxable item, and add that amount to the sale price. This calculation generally will result in the correct taxable sales price (*i.e.*, the price to which the taxpayer will apply the 12 percent section 4051 tax.) For example, assume that a manufacturer sells a truck body directly to a retail customer for $10,000. The presumed markup percentage generally will be 4 percent. Therefore, the taxable sale price will be $10,400 (10,000, plus (.04 x 10,000)). The tax on that sale generally would be $1,248 (.12 x 10,400).

c. When Does the Presumed Markup Apply?

In general, the presumed markup percentage applies to any taxable sales where the manufacturer,[185] producer or importer (or a "related person")[186] *is the taxpayer* (*i.e.*, the party responsible for paying the section 4051 tax to the IRS).[187] It is *not* limited to sales directly to retail customers, as that term is typically used. For example, if a manufacturer sells a taxable chassis to a retail dealer for resale, but the manufacturer is liable for the tax because the sale did not meet the requirements for a tax-free sale for resale (see Section III), then the presumed markup percentage would apply to the sale by the manufacturer. This is the case, even though the retail dealer is not a typical retail customer.[188]

Taxpayers should be aware that even if a manufacturer's price to the retail customer already includes a markup equal to or greater than 4 percent, the IRS is likely still to require that the taxpayer add the presumed markup percentage to the taxable sale price. This is because the IRS has taken the position that it does not have the authority to except certain manufacturers' sales from the presumed markup percentage. (*See* TAM 9314003 (Dec. 23, 1992).) However, this position is questionable, given that the IRS, in effect, previously has excepted trailers, semitrailers, and remanufactured bodies, chassis, and tractors from the presumed markup percentage (by establishing a 0 percent presumed markup for those items). Therefore, the IRS should have the authority similarly to find that a 0 percent presumed markup applies to manufacturers' sales that already include a retail markup for customers of at least 4 percent. It should be noted that in TAM 9314003, the IRS also determined that the taxpayer did not provide sufficient evidence of a retail markup (as opposed to a markup reflecting other factors). If a manufacturer believes that the application of the presumed markup percentage to its sales will result in a double retail markup, the taxpayer should discuss this issue with its tax counsel.

Taxpayers also should be aware that the IRS has regulations to prevent using a retail dealer or other third party, in name only, as a means of avoiding the presumed markup percentage. The IRS's regulations provide that the presumed markup will apply to sales where "a person *other than* a manufacturer, producer, or importer" is the taxpayer, if, among other requirements, "[t]he principal purpose for processing the sale through such person is to avoid or evade the presumed markup…."[189]

2. *Non*-"Arm's Length" Sales

If a sale is not an "arm's length sale" as defined above in A, *and* the actual price is less than the fair market value of the article,[190] the taxpayer will need to apply the 12 percent tax to a constructive price (*i.e.*, the taxpayer cannot apply the tax to the price it charges its customer). For example, if a dealer sold a taxable item to its wholly-owned subsidiary for less than the lowest price it regularly charges unrelated customers for the same item, the IRS likely would conclude that the sale was not an "arm's length" sale. In such a case, the taxpayer would need to determine the correct taxable sales price (*i.e.*, the correct amount to which the taxpayer should apply the 12 percent tax).

In the situation described above, the IRS is likely to determine that "the lowest price at which the dealer regularly sells [a taxable item] to unrelated retail customers" is both the fair market value of the item and that item's constructive price (*i.e.*, the price that should be used in calculating the 12 percent tax).[191]

In a situation in which the taxpayer sells a taxable item only in *non*-arm's length sales (*e.g.*, the taxpayer only sells to its subsidiary; it makes no sales to unrelated buyers), the answer is less clear. The regulations generally provide that the constructive price for non-arm's length transactions will be "the price for which similar articles are sold at retail in the ordinary course of trade, *as determined by the [IRS]*."[192] There does not appear to be any ruling issued by the IRS under IRC § 4051 that addresses the calculation of a constructive price for a taxable item sold in a non-arm's length sale, if the seller does not also make arm's length sales of the same item. (Although there may be a ruling on this issue with respect to the manufacturer's excise tax under IRC § 4061, which was repealed in 1983, any such decision would be more than 35 years old.) Therefore, this situation should be discussed with tax counsel. In addition, the IRS provides that once it determines the constructive price for a non-arm's length transaction, "no further adjustment of such price shall be made."[193] This provision applies regardless of whether the taxpayer makes only non-arm's length sales of a taxable item, or whether the taxpayer also makes arm's length sales of that item. It is unclear whether this provision is intended to prevent a taxpayer from making normally permissible deductions from the constructive price. A taxpayer should discuss this issue with tax counsel prior to establishing a constructive price for a non-arm's length sale of a taxable item.

3. Taxpayer's *Use* Triggers Tax

In a situation in which a taxpayer's use of an item triggers section 4051 tax, and the taxpayer does not regularly make arm's length retail sales of that item, the IRS will determine the constructive price (*i.e.*, the price to which the 12 percent tax should be applied) based on the "selling practices and price structures of sellers of similar articles." (Unlike the IRS's regulations for non-arm's length sales, the regulations for taxable use expressly provide that certain charges may be excluded from the constructive price.)[194]

In a 1986 Revenue Ruling, the IRS established a constructive sale price for a taxpayer's use of a refurbished truck tractor.[195] In that ruling, an owner overhauled its used truck tractor for use in its business. The IRS determined the owner was a manufacturer, that its use triggered the section 4051 tax, and that the owner did not regularly make arm's length retail sales of the tractor. Therefore, the IRS established a constructive price that was equal to "the cost to the owner of all the components used by the owner in the manufacturing operation plus an amount equal to 150 percent of the owner's labor costs (including overhead) in the manufacturing operation."[196]

The ruling also noted that if the owner believed the 150 percent markup was too high under its specific facts, the owner could seek a ruling from the IRS.[197] However, taxpayers should consult with their tax advisers prior to relying on this 150 percent constructive price formulation because it is based on "selling practices and price structures of sellers of similar articles," which means (1) this calculation may not apply to items other than refurbished truck tractors,[198] and (2) "the selling practices and price structures" likely have changed since this decision was issued, more than 20 years ago.

4. Calculation of Tax for Leases

In calculating the constructive price for a lease, the Treasury Regulations provide four different possibilities—two for long-term leases, and two for short-term leases. It is important to note that the regulations on this issue do not provide clear guidance. It is recommended that taxpayers consult with their tax advisers prior to calculating a constructive lease price.

a. Constructive Lease Prices for Long-Term Leases

Possibility 1: *A manufacturer, producer, or importer* (or person related thereto) leases a taxable item in a long-term lease (*i.e.*, for one year or longer, as discussed in Section VIII). The lease triggers section 4051 tax.

Constructive Price: (1) the price, as established by the IRS, at which a manufacturer, producer, or importer would sell the item in a *non*taxable sale, such as a tax-free sale for resale or long-term lease (see Sections III and VIII) as of the lease date, *plus* (2) the applicable presumed markup percentage, multiplied by the amount of the IRS-established price ((1), directly above).[199]

Possibility 2: The lessor is *not* a manufacturer, producer or importer (or person related thereto) and leases a taxable item in a long-term lease. The lease triggers section 4051 tax.

Constructive Price: (1) the price for which the lessor purchased the item "plus the cost of any parts and accessories installed by the lessor (or an agent of the lessor) on such article before the first use by the lessee or leased in connection with such long-term lease," *plus* (2) the applicable presumed markup percentage, multiplied by the price determined in (1), directly above.[200]

Example: A manufacturer sells a truck to a dealer for $50,000. The sale to the dealer is a tax-free sale for a long-term lease. A few weeks later, the dealer leases the truck to a lessee for two years. The dealer did not install any parts or accessories on the truck. The constructive price would be $52,000 [$50,000 + ($50,000 x 4 percent)]. The section 4051 tax would be $6,240 [12 percent x $52,000].[201]

b. Constructive Lease Prices for Short-Term Leases

Possibility 1: *A manufacturer, producer, or importer* (or person related thereto) leases a taxable item in a *short*-term lease (*i.e.*, for less than one year, as discussed in Section VIII). The lease triggers tax under section 4051.

Constructive Price: "the price at which such or similar articles are generally sold in the ordinary course of trade by retailers."[202]

Possibility 2: The lessor is *not* a manufacturer, producer or importer (or person related thereto), and leases a taxable item in a *short*-term lease.

Constructive Price: (1) the price for which the lessor purchased the item "plus the cost of any parts and accessories installed by the lessor (or an agent of the lessor) on such article before the first use of lease by the lessor," *plus* (2) the applicable presumed markup percentage, multiplied by the price determined in (1), directly above.[203]

Example: A manufacturer sells a truck to a dealer for $50,000. The sale to the dealer is a tax-free sale for a long-term lease. A few weeks later, the dealer leases the truck to a lessee for six months (*i.e.*, a short-term lease). The dealer did not install any parts/accessories on the truck. The constructive price would be $52,000 [$50,000 + ($50,000 x 4 percent)]. The section 4051 tax would be $6,240 [12 percent x $52,000].[204]

5. Deductions and Credits

There are some charges or expenses that may be excluded from the taxable sale price (*i.e.*, the 12 percent tax does not apply to these items). In this section we discuss a few of the most common exclusions:

- Some specific taxes
- Certain (but not all) delivery and transportation charges
- Certain (but not all) installation charges
- Certain (but not all) warranty charges
- Certain (but not all) used components
- Machinery or equipment that does not contribute to the transportation function (so long as the taxpayer has sufficient records to support the excluded charge for such machinery/equipment)

In addition, there is a credit available to taxpayers for the amount of the tire tax under IRC § 4071.

a. Specific Taxes

The section 4051 excise tax and retail sales tax (on both the state and local level) generally may be excluded from the taxable sale price.[205] (In order to exclude the retail sales tax, that amount must be "stated as a separate charge.") Therefore, the 12 percent tax generally will not apply to the amount of the sale price attributed to these two types of taxes. The statute does not expressly provide for deductions of any other types of taxes. If other federal, state or local taxes apply to a sale that is taxable under IRC § 4051, taxpayers should consult with tax counsel prior to excluding those charges from the taxable sale price.

b. Certain Delivery/Transportation Charges

Transportation and delivery charges may be deducted from the taxable sale price only if they are incurred pursuant to a "bona fide sale."[206] For example, delivery charges incurred for stock inventory should not be deducted. In general, a taxpayer *may* deduct the transportation/delivery charges for moving the taxable item *from* the *taxpayer's* place of business *to* the *purchaser*.[207] This is true regardless of whether the taxpayer is a manufacturer or retail dealer. However, if the taxpayer is the retail dealer, delivery and transportation charges from the manufacturer to the *retail dealer* generally may *not* be deducted from the taxable sale price.

Therefore, if the retail dealer is the taxpayer, and the manufacturer ships the taxable item directly to the retail *customer*, the taxpayer may *not* exclude the entire amount of the transportation charge. Instead, the taxpayer must include in the taxable price that portion of the charges that would have resulted *if* the article had been transported from the manufacturer to the taxpayer. For example, if the actual charges to transport the item from the manufacturer to the retail customer is $150, and it would have cost $100 to transport the item from the manufacturer to the retail dealer, the taxpayer only may *exclude* from the taxable sale price $50 for the transportation charge. In other words, the taxpayer must include the $100 charge that it would have incurred if the manufacturer has shipped the item to the taxpayer instead of directly to the customer. Similarly, if the actual charges to transport the item from the manufacturer to the end user is $100 and it would have cost $125 to transport the item from the manufacturer to the taxpayer, the taxpayer is not entitled to deduct *any* of the transportation charges from the taxable price.[208]

c. Certain Installation Charges

The IRS has not published much guidance on installation charges. The common deduction for installation charges occurs when a body is installed on a *customer-owned* chassis.[209] In a 2003 Letter Ruling, the IRS held that a taxpayer could deduct from the taxable sale price "[t]he costs of attaching the body to the customer's chassis, including modifications to the chassis necessary for the installation of the body (such as for lengthening or shortening the wheel base slide)," which included "all overhead, direct and indirect, properly attributable to the installation, as well as labor and material costs."[210] However, the deduction of such costs was limited to actual expenses. Therefore, the IRS concluded that a gross margin could not be deducted.[211]

Three common situations in which installation charges may *not* be deducted are as follows: (1) the installation charges are not related to a bona fide sale (*e.g.*, a body is installed on a chassis for inventory purposes);[212] (2) the installation charges fall under the so-called Six-Month Rule (see Section II);[213] and (3) installation charges if a taxable body and a taxable chassis are sold as a unit.[214]

In order to deduct permissible installation charges, these charges are not required to be separately invoiced. However, any deducted installation charge should be supported by sufficient records.[215]

Based on older Letter Rulings under the now-repealed section 4061 tax, taxpayers also should be aware that the IRS likely will distinguish between installation charges related to installing a body on a chassis, and installation charges related solely to the manufacturing of the body itself. For example, the IRS previously determined that the attachment of a hoist to a body was not a deductible installation charge. (*See* Letter Ruling 6806208550A (June 20, 1968) (stating that "[t]he interconnection of any of the body parts, for example, the attachment of the hoist assembly to the body, front loader assembly to the subframe, and hoist and hydraulic components to the subframe and side plate, is not installation of a body on a chassis but is assembly of the body and charges for those operations are to be included in the tax base of the body," but also noting that "when such components are affixed directly to the customer-owned chassis, the cost of affixing is excludable"); Letter Ruling 7412262010A (Dec. 26, 1974) (stating that "[t]he charges you attribute to installing the body-hoist-subframe onto your customer's chassis may be excluded from the price," but "[t]he charges you attribute to combining the body, hoist, subframe and power take-off unit are not excludable").

d. Warranty Charges

In a 2003 Letter Ruling, the IRS distinguishes between two types of warranties in determining whether the related charges may be deducted from the taxable sale price. The IRS concludes that if the taxpayer requires a purchaser to pay a charge for a manufacturer's warranty as a condition to obtaining the purchased article, the warranty charge may not be deducted. However, "a charge for a warranty that is available at the purchaser's option" is deductible.[216]

e. Used Components

Section 4052(b)(1)(B)(iii) provides that a taxpayer may deduct from the taxable sale price the value of a taxable item's components if (1) "such component is furnished by the first user of such article," and (2) "such component has been used before such furnishing." For example, assume a taxpayer produces a new taxable item by using new and used components to overhaul a vehicle, and then sells the vehicle at retail. The taxpayer cannot deduct the value of the used components from the taxable sale price because the retail customer would be the first user of the new taxable item, and the retail customer did not furnish the used components.

In the early 1990s, there was some question among IRS agents as to whether the deduction should apply if the used components had never been taxed under IRC § 4051.[217] For example, if a taxable truck chassis is rebuilt with certain components that were originally used in a truck chassis rated 33,000 pounds GVW or less, should the value of those used components, which were never subject to section 4051 tax, be deductible? Although the legislative history indicated that the purpose of the deduction was to avoid double taxation, the IRS noted that the deduction language was "very simple and direct and does not lend itself to an interpretation requiring that the component need be previously taxed."[218] The IRS also noted that "[t]o require proof of such taxation would place a heavy, and administratively difficult, burden on the taxpayer."[219] The authors believe the IRS's current position continues to be that this deduction does not require that the used components previously were taxable.

Deducting the "value" of the used component refers to the component's fair market value.[220] The costs related to installing the used components are not deductible.[221]

f. Equipment or Machinery that does not Contribute to the Transportation Function

If machinery or equipment does not contribute to the transportation function, the section 4051 tax will not apply to the amounts charged for such machinery/equipment, so long as "the reasonableness of the charge…is supportable by adequate records."[222] In other words, amounts for certain machinery or equipment may be subtracted from the taxable sale price. Taxpayers should consult with their tax counsel in order to determine the correct amount that should be subtracted from the taxable sale price as a result of such machinery or equipment. For examples of machinery/equipment that do not contribute to the transportation function, see Section II.D.1.

g. Tire Tax Credit

The FET statute at IRC § 4051(d) provides "[i]f—(1) tires are sold on or in connection with the sale of any article, and (2) tax is imposed by this subsection on the sale of such tires, there shall be allowed as a credit against the tax imposed by this subsection an amount equal to the tax (if any) imposed by section 4071 on such tires." The tire tax credit became effective Jan. 1, 1998.

"Section 4071" refers to what is known as the "tire tax." The tire tax is paid by the tire manufacturer. The tires on which the tire manufacturer pays the tire tax may then be incorporated into a taxable body, chassis or tractor, and sold in a sale that triggers section 4051 tax. In such a situation, the tires will be, in effect, taxed *both* under the tire tax and under the section 4051 tax. The tire tax credit prevents the IRS from receiving tax on the tires twice.[223] As a result of the tire tax credit, the tires are effectively taxed only under IRC § 4051, because taxpayers get a credit equal to the amount of the tire tax imposed by IRC § 4071.

The taxpayer claims its tire tax credit on Form 720. Unlike deductions, the amount of the tire tax credit does *not* reduce the taxable sale price or otherwise reduce a taxpayer's section 4051 tax liability. Instead, it reduces the ultimate amount of tax a taxpayer must pay the IRS as a result of its Form 720 filing.[224]

In other words, a taxpayer should calculate its section 4051 tax, without regard to the tire tax credit, and identify its section 4051 tax liability for all sales in a calendar quarter on Line 33, Part I of Form 720. Then, separately, the taxpayer should identify the appropriate amount of tire tax credit for a calendar quarter on Schedule C, line 15a of Form 720.

Tire Tax Credit

Example:

Truck	$100,000 (selling price)
FET	$12,000
Tire Tax	$450 (tax due on tires under section 4071)
Form 720	$12,000 included on Line 33 and $450 included on Schedule C

X. IRS GUIDANCE — OPTIONS, CONSIDERATIONS AND RELIABILITY ISSUES

The IRS provides taxpayers with information, from time to time, as to the correct application of the FET. This information can come in a variety of forms, each of which has different levels of authority and significance to a taxpayer's situation, and you should discuss such information with your tax professional. This section will discuss four specific types of guidance the IRS provides to taxpayers: (1) letter rulings; (2) technical advice memoranda; (3) revenue rulings; and (4) discussions with local IRS agents.

A. The Basics

It is important to understand some of the primary differences among letter rulings, technical advice memoranda, revenue rulings, and informal IRS oral advice in terms of (1) a taxpayer's ability to request IRS guidance for a specific transaction, (2) the requirements necessary to receive IRS guidance, and (3) a taxpayer's ability to rely on such guidance.

1. Short Summary

a. Letter Rulings

A letter ruling "interprets the tax laws and applies them to the taxpayer's specific set of facts."[225] A letter ruling request generally is not an available option once the issue is under examination by the IRS.[226]

The taxpayer can choose whether to request a letter ruling, and does not need prior approval from the IRS in order to file the request. Unlike technical advice (discussed below), the IRS cannot submit a letter ruling request.

There are many informational and procedural requirements that must be satisfied (including payment of a filing fee) in order for the IRS to rule on a request. The taxpayer who requests the letter ruling generally can rely on that ruling unless and until it is revoked or modified;[227] however, no other taxpayer may rely on the letter ruling.[228]

b. Technical Advice Memoranda ("TAMs")

Technical advice is provided by the IRS to assist "on any technical or procedural question that develops *during any proceeding before the IRS*."[229] In other words, a taxpayer may request a technical advice ruling only with respect to an issue that arises during an IRS proceeding, such as an audit of the taxpayer's tax returns or an appeal of an audit.

The purpose of technical advice is to provide guidance to the *IRS officer*.[230] A taxpayer does not have a "right" to technical advice. The taxpayer can request that the IRS officer seek technical advice, but it is ultimately up to the IRS to determine whether to do so.[231] The IRS can request technical advice without the agreement of the taxpayer.[232]

There is no fee for requesting technical advice. There are procedural and informational requirements necessary in order to submit a request for technical advice.

The IRS proceeding generally must be resolved in a manner consistent with the published technical advice.[233] No other taxpayer may rely on this technical advice.[234]

c. Revenue Rulings

A revenue ruling is published in the Internal Revenue Bulletin for the purpose of providing information and guidance to the public, including taxpayers and IRS officials. Unlike letter rulings and TAMs, revenue rulings generally are designed to address issues broader than the specific facts of a single taxpayer.

There is no procedure for a taxpayer to request and receive a revenue ruling. However, the IRS will accept suggestions for revenue rulings from the public, including interested taxpayers or trade associations.

Unlike letter rulings and TAMs, *all* taxpayers generally may rely on a revenue ruling unless and until the ruling is modified or revoked.

d. Oral conversations with the IRS

A taxpayer does not have a "right" to receive oral advice from the IRS.[235]

A taxpayer is not entitled to rely on any oral advice from an examining agent (or any other IRS employee). Any oral advice a taxpayer receives from the IRS is advisory only.[236] The IRS can subsequently determine its advice was erroneous, and still assess tax against the taxpayer.

B. A Deeper Dive

1. Letter Ruling Requests

Letter ruling requests may be submitted to the IRS, at the taxpayer's option, to determine whether FET will be triggered with respect to a specific set of facts. The taxpayer does not need the IRS's prior approval to file a letter ruling request. The IRS generally will rule on all requests seeking an interpretation of a tax law, as applied to a taxpayer's specific situation. However, there are some circumstances in which the IRS has determined it will not rule on a letter ruling request. These circumstances are discussed in the first revenue procedure the IRS issues each year.[237] For example, for the year 2010, the rules for letter ruling requests can be found in Revenue Procedure 2010-1. For the year 2011, these rules are published in Revenue Procedure 2011-1. The rules concerning letter ruling requests are updated each year (although they also may be modified during the year).

It is important for taxpayers to understand upfront that requesting a letter ruling from the IRS generally is relatively expensive. In 2010, the fee to file a letter ruling request with the IRS after February 1 is $14,000, unless a taxpayer qualifies for a reduced user fee.[238] Also, a letter ruling request must satisfy numerous informational and procedural requirements. Therefore, although a letter ruling does not need to be filed by an attorney, it is likely that a taxpayer may need some assistance from an attorney or other tax professional to prepare the letter ruling request, which will add to the cost of requesting a ruling. All of these requirements are discussed in the revenue procedure for letter ruling requests. Because the rules for letter ruling requests are updated each year, a taxpayer should be sure he is following the most current version of the rules when preparing a letter ruling request.

In addition, even if an attorney or other tax adviser does not help to prepare the letter ruling request, a taxpayer always should consult with a tax advisor, as an initial matter, to determine if filing a letter ruling request is the best way to proceed. By filing a letter ruling request, a taxpayer is bringing its business (and especially the prior and current transactions for which it is seeking a letter ruling) to the attention of the IRS. Therefore, the taxpayer should understand the potential consequences of filing a letter ruling request, especially if the IRS rejects the taxpayer's position in that request. Also, letter rulings are published, which means that certain information about the taxpayer's products may become public. A taxpayer should understand the types of information that the taxpayer will be permitted to exclude from the public version of the letter ruling (*e.g.*, the taxpayer's name), and the types of information that it will not be able to exclude. Finally, the IRS is not required to issue a response to a letter ruling request within a specified amount of time. Therefore, if a taxpayer needs a quick answer, a letter ruling may not be that helpful. For all of the reasons discussed above, a letter ruling request is not always the right answer.

Letter rulings are available for review by all taxpayers on the IRS's website (and on the websites of other legal search engines). These rulings are often a good predictor of how the IRS likely will treat a transaction with similar facts. However, only the taxpayer that requested the letter ruling is entitled to *rely* on it. This means that if Taxpayer A receives a letter ruling that the sale of a certain product is not taxable, the IRS cannot assess tax against Taxpayer A for sales of that product, unless and until the letter ruling is revoked or modified. However, no taxpayer other than Taxpayer A may rely on the letter ruling. This means that if Taxpayer B does not receive his own letter ruling for sales of a product that is substantially the same as (or even identical to) Taxpayer A's product, the IRS can assess tax against Taxpayer B for those sales (*i.e.*, Taxpayer B is not protected by Taxpayer A's letter ruling).

Similarly, assume Taxpayer A received a letter ruling that a particular transaction did not trigger FET, but three years later the IRS determines the transaction should be taxable and revokes the ruling. For the 3-year period between the issuance of the letter ruling and the issuance of the revocation, Taxpayer A generally (but not always) will have no tax liability for transactions covered by the letter ruling.[239] However, assume that several other taxpayers were involved in transactions similar (or even identical) to the one addressed in Taxpayer A's letter ruling. Those other taxpayers read the letter ruling issued to Taxpayer A, and, as a result, did not charge FET on their transactions. The letter ruling to Taxpayer A would not provide those other taxpayers with any protection from tax liability during that same three-year period.

2. Technical Advice Requests

If a taxpayer is involved in an examination of its returns (*i.e.*, an audit) or an appeal of such an examination, and the taxpayer believes the IRS officer is misinterpreting a relevant provision of the tax law, then the taxpayer may want to consider requesting that the IRS officer seek technical advice on this issue. In effect, a technical advice request asks for a second opinion. If the IRS officer agrees to request technical advice, the disputed issue will be reviewed by the Office of Associate Chief Counsel (Passthroughs and Special Industries), located in Washington D.C. (There are several Offices of Associate Chief Counsel, and each one specializes in specific types of taxes.) If the IRS officer does not agree to the request for technical advice, then the taxpayer has the right to appeal that decision.[240] Ultimately, however, it is the IRS (and not the taxpayer) that has the final say as to whether a request by the taxpayer for technical advice will be submitted to the Chief Counsel's Office. Therefore, a request for technical advice is not really a filing by the taxpayer. Instead, it is a filing by the IRS, with some participation by the taxpayer.

A taxpayer also should be aware that the IRS, without any request by the taxpayer, may submit an issue for technical advice. Under such circumstances, the IRS officer will notify the taxpayer that the officer is seeking technical advice, and the taxpayer will have the opportunity to participate in the process (*e.g.*, submit a written statement of the taxpayer's position and supporting arguments, etc.).

The second revenue procedure of each year discusses in detail the rights and obligations of the taxpayer when technical advice is sought. For example, for the year 2010, the rules for technical advice are discussed at Revenue Procedure 2010-2, and for the year 2011, these rules are published in Revenue Procedure 2011-2. If the taxpayer does not follow these rules, it can lose important rights to participate in the technical advice process. Because the rules governing technical advice requests are updated each year (and may be updated during the year), the taxpayer should be sure he is following the most recent version of these rules. Consultation with tax counsel is recommended to guide the taxpayer through the process of seeking technical advice.

A taxpayer also should consult with tax counsel *prior* to making the decision to request technical advice, because different circumstances can weigh in favor or against a request for technical advice. For example, by requesting technical advice, the taxpayer can get a fresh pair of eyes on the issue, which can be very helpful if the taxpayer believes the IRS officer is being unreasonable or is mistaken as to the correct application of the law. In fact, the mere request for technical advice (which will require at least some level of review by the officer's superiors) may motivate an unreasonable IRS officer to take a more reasonable position. On the other hand, by requesting technical advice, a taxpayer may lose some of the informality of the examination or appeals process, thereby losing the best opportunity for a satisfactory settlement of the outstanding issue. As noted above in A, once the Chief Counsel's Office issues technical advice, the IRS officer generally is bound to comply with that advice.

In addition, before the taxpayer decides to request technical advice, he should discuss with his tax counsel the risk and effect of receiving unfavorable technical advice. Also, technical advice, like Letter Rulings, is available for review by all taxpayers on the IRS's website (and on the websites of other legal search engines.) Accordingly, a taxpayer should understand how the publication of the technical advice (known as a Technical Advice Memorandum or TAM) may affect the taxpayer. Whether technical advice is likely to benefit the taxpayer ultimately will depend on a variety of factors specific to the taxpayer's case.

Like letter rulings, a published TAM is a good predictor of how the IRS likely will treat a transaction with similar facts. However, if the TAM was issued to a different taxpayer, then you are not entitled to rely on it, even if the products and circumstances related to your sale are substantially the same as those in the TAM. In fact, because TAMs generally are specific to certain tax periods, there may be an argument that even the taxpayer to whom the technical advice is issued cannot technically rely on the TAM for transactions occurring in other tax periods. This issue should be discussed with your tax counsel.

3. Revenue Rulings

As noted above, there is no set procedure by which a taxpayer can request a revenue ruling. Although letter rulings and TAMs are the result of a formal request initiated either by the taxpayer or an IRS official, revenue rulings result from many different sources, such as letter rulings, TAMs, court decisions, and suggestions from the public.[241] Therefore, the IRS does not publish a detailed, annual procedure concerning revenue rulings (as it does for letter rulings and TAMs). However, interested taxpayers should review Revenue Procedure 89-14 for a brief discussion of what a revenue ruling is and how it works.

Unlike letter rulings and TAMs, a revenue ruling is not issued to a single taxpayer, but is published in the Internal Revenue Bulletin for the benefit of all taxpayers. (Although letter rulings and TAMs also are made available to the public on the IRS's website—under the heading "IRS Written Determinations," only revenue rulings are published in the Internal Revenue Bulletin). Therefore, revenue rulings generally address issues of concern on an industry-wide basis, rather than issues specific to a single taxpayer. *All* taxpayers generally may rely on a revenue ruling unless and until it is revoked or modified (*e.g.*, by subsequent statutory or regulatory provisions, court decisions or IRS publications or rulings), *so long as* the facts and circumstances of the relying taxpayer are *substantially similar* to those in the revenue ruling.[242] In addition, if a prior revenue ruling supports a taxpayer's current tax position (assuming the ruling has not been revoked or modified), that revenue ruling will be much more persuasive to the IRS or a court than a letter ruling or TAM reaching a similar conclusion.[243]

4. Oral Conversations with the IRS

Speaking informally with an IRS agent can seem like an attractive option for a taxpayer, because the taxpayer may be able to receive quick and free tax advice. However, taxpayers need to understand that even though the IRS may give you oral advice, it does not mean the advice is correct. The application of the FET tends to be very fact-specific. In an oral conversation, it is easy for both parties mistakenly to omit important facts, to make assumptions that are not correct, or simply to misunderstand what the other person is saying. Accordingly, the advice the IRS agent provides a taxpayer could be the right advice, based on the facts as understood by the agent, rather than the taxpayer's actual facts. Moreover, even if the IRS agent understands the facts perfectly, he or she may simply provide mistaken advice.

More importantly, a taxpayer who relies on IRS oral advice does so at its own risk.[244] For example, if an IRS agent incorrectly advises you that a certain sale is not taxable, the IRS still can assess the tax (and interest and penalties) against you for that transaction, even though you relied on the IRS agent's advice. Therefore, if a taxpayer seeks the oral advice of an IRS agent, the taxpayer should ask the agent if there is any statute, regulation, IRS ruling, or court case that supports the tax position the IRS agent is taking. Such information could provide the taxpayer with comfort that the agent's advice is correct, as applied to the taxpayer's facts.

As with the decision to seek a letter ruling or technical advice, a taxpayer should consult with tax counsel prior to seeking informal advice from the IRS agent. Seeking such advice may result in unwanted IRS attention with respect to the taxpayer's business (*e.g.*, an examination of the taxpayer's tax returns).

XI. PREPARING FOR AN AUDIT

A. Audit Strategy

The IRS audits excise tax returns with some frequency. The fact that one or more of your returns is scheduled for examination does not necessarily mean that the Service believes there is a problem. However, in order to maximize the likelihood of a good outcome—*i.e.*, no assessment of additional tax—there are certain steps you should consider taking.

First, contact your tax advisor immediately after you are notified that your company's returns are going to be examined. You should discuss with your advisor any areas of concern with the returns being examined. You can decide at that time whether to have your advisor be the point of contact with the examining IRS agent or whether someone in your organization will take that role. In most cases it is preferable to have the point person be someone who is knowledgeable about the tax.

Second, try to ascertain as early in the process as possible any concerns that the examining agent has with the returns. In general, the best course is to identify the concerns but hold off discussing them in detail with the agent until after you have had a chance to discuss the issue(s) with your tax advisor and get your ducks in a row.

Be aware that the IRS agents who examine returns for FET compliance typically examine returns for several other types of excise taxes as well. Because each of these taxes has its own complexities, it is not uncommon for an agent to be unfamiliar with some of the nuances of the tax. As a result, agents mistakenly identify potential problems with a return with some frequency.

Third, once you have identified the areas of concern, work with your tax advisor to develop a short, written response to any of the concerns that appear to be misplaced. The response should include appropriate citations to court cases, regulations, and rulings that support your position. Ideally, the response should be short and to the point, and not overly legalistic. You will want to get this "white paper" into the agent's hands before he or she is ready to issue a "90-day letter" assessing additional tax. If possible, you will also want to schedule a face-to-face meeting with the agent to walk him or her through your positions. It is essential that someone who is knowledgeable about FET (either someone from your organization or your retained accountant or attorney) represent your company in this meeting.

B. A Strategic Approach

When addressing potential areas of assessment, it is recommended that you use a three-pronged analysis: (1) Determine whether the article(s) in question are taxable; (2) if the articles are taxable, determine if they were sold in taxable "first retail sales"; and (3) if taxable articles were sold in taxable first retail sales, determine the proper amount of the tax due on each sale. A thorough analysis of each of these factors could either eliminate or reduce the amount of tax the agent thinks should be assessed.

It is also important to remember that, if you have some potentially taxable transactions that may be subject to assessment, you may also have charged tax on some nontaxable transactions during the period covered by the returns being examined, and the amount of tax on those sales—on which the agent is not focusing—may be available as an offset.

For example, assume that you installed 24-ft. platform bodies on a chassis rated 32,900 lbs., and on which you installed a lift-axle and a corner-mounted crane with a 28-ft. boom. Assume further that the IRS agent takes the position that the bodies, chassis, and cranes are taxable. On those facts, you likely could take the following positions that the articles in question simply are not taxable under I.R.C. § 4051: (1) the 24-ft. platform bodies are nontaxable because they are suitable for use with vehicles rated 33,000 lbs. GVW or less (and this argument, if well-supported, may well prevail); (2) the chassis are nontaxable because, when you installed the lift-axles, you did not increase the GVW of the chassis for NHTSA certification purposes (and this argument likely will fail to persuade the agent because the IRS generally does not accept this position); and (3) the corner-mounted crane is nontaxable because it has a boom in excess of 25 feet and is not designed or primarily used to load or unload the truck on which it is mounted (and this argument, if well supported, should prevail). Thus, there is a good chance of convincing the agent that the body and crane are nontaxable. The agent, however, likely will conclude the chassis are taxable, and this could result in an assessment of a significant amount of tax (and interest and penalties.

However, the inquiry should not stop there. You should next turn to whether the articles in question were sold in transactions that triggered the tax. For example, if you sold some of these vehicles to buyers who are entitled to purchase tax-free, you may be able to avoid an assessment on that basis (assuming the proper paperwork is in place). Similarly, if you imported and sold vehicles that were manufactured in the United States, you may be able to show that the vehicles were previously sold in taxable or potentially taxable transactions and thus would not be subject to further potential taxation. You will need to look carefully at each sale to determine if there is an argument available that, even if the articles in question are potentially taxable, your company's sales did not trigger FET and thus should not be subject to assessment.

After you have closely scrutinized the transactions that the agent thinks are appropriate for assessment of tax, you should look to see if you *mistakenly charged* tax on any of the other sales, covered by the subject returns. For example, if you charged tax on 8-cu.-yd. dump bodies in other transactions covered by the returns in question, then you may be able to argue successfully that you are entitled to a credit for the tax paid on those bodies, and the credit may offset all or a portion of the tax due on the transactions for which the agent will seek an assessment. This can be a painstaking process, and the review, to be effective, should be conducted by someone knowledgeable about FET who did not make the initial determination to charge the tax in the first instance. In many cases, this approach will bear fruit.

The overarching goal is to convince the examining agent to reduce or eliminate any tax assessment he or she might otherwise make as a result of the audit. However, if the agent cannot be convinced to do so, the taxpayer will still have the right (1) to an appeal at the IRS of the assessment by the examining agent (during which time the taxpayer may request that the appeals officer seek a Technical Advice Memoranda), and/or (2) to pay the tax and bring a refund action in federal court.

XII. PAYING THE TAX

This section provides a short summary of a few general guidelines for filing excise tax returns on Form 720 (a sample of which is included in the appendix of this guide), and for making semimonthly deposit payments. The requirements for filing excise tax returns change from time to time. Therefore, before filing your excise tax return, you always should review both the current Instructions for Form 720 and Publication 509, titled "Tax Calendars." Both of these documents are available on the IRS's website (www.irs.gov). Please be aware that: (1) This section generally assumes that the taxpayer is filing a Form 720 for the sole purpose of the section 4051 tax (i.e., the taxpayer is not reporting any other taxes on this form), and (2) There are other rules and requirements related to filing Form 720 and to making excise tax deposits that are not discussed in this section.

Because a variety of factors can affect the filing requirements for a specific company, it is recommended that taxpayers have their tax advisers review a return before it is filed.

A. Quarterly Tax Return Filing

You must file with the IRS a Form 720 (and pay any tax owed) each calendar quarter:

- For the quarter beginning January 1st and ending March 31st, the due date for the Form and the tax owed is April 30th
- For the quarter beginning April 1st and ending June 30th, the due date is July 31st
- For the quarter beginning July 1st and ending September 30th, the due date is October 31st
- For the quarter beginning October 1st and ending December 31st, the due date is January 31st

If the due date is a legal holiday or a weekend day, Form 720 must be filed by the *following* business day. (However, as discussed below, this is *not* the rule for deposit payments.) If a return is filed late, the taxpayer may be subject to penalties (in addition to interest charges on the late payments). Therefore, you should discuss with your tax counsel the rules for timely filing his return.

This quarterly filing is required even for quarters in which a taxpayer (*i.e.*, an entity that has previously sold articles that are subject to FET) has zero tax liability. In such a case, a taxpayer would complete its Form 720 by placing a zero on the line for section 4051 taxes of Part I of Form 720, writing "None" on line 3, Part III of Form 720, and signing and dating the return. If you are reporting a zero tax liability and you will not owe any section 4051 taxes in the future (*e.g.*, your company ceases to do business), then the taxpayer should check the "final return" box, which is located above Part I of the Form. A taxpayer should keep all documents it relied on in preparing its return for a period of four years from the date the tax is due (or, if the tax was paid later, the date the tax was paid).

B. Deposit Requirements

Part I of Form 720 lists various excise taxes (including FET). If your net liability for Part I taxes will be more than $2,500 for the quarter, you are generally required to make semi-monthly deposits of your excise tax liability. For more information about the rules governing deposits, see Treas. Reg. § 40.6302(c)-1.

1. Payment of Deposits

These deposits should never be mailed to the IRS. Instead, a taxpayer is required to make its deposits by electronic funds transfer, as that term is defined in treasury regulation section 31.6302-1(h)(4). Prior to January 1, 2011, a taxpayer, under certain circumstances, could make its deposits to an authorized financial institution, using Form 8109, "Federal Tax Deposit Coupon." That option is no longer available.[245]

An approved method of making an electronic funds transfer is through the Electronic Federal Tax Payment System (EFTPS). For information on EFTPS, call 1-800-555-4477, visit www.eftps.gov, or download Publication 966 from the IRS website.

2. Timing of Deposits

The first semi-monthly period runs from day 1 through day 15 of a given month and the second semi-monthly period runs from day 16 through the end of that month. Thus, the first semi-monthly deposit generally will be due on the 29th of that month, and the second semimonthly deposit generally will be due on the 14th of the next month.If one of these due dates falls on a weekend or legal holiday, see C, below, for the rule used to determine the actual deadline. In addition, there is a special rule for making deposits in September, which also is discussed below in C.

3. Amount of Deposits

A semimonthly deposit (if applicable) is generally required to be no less than 95 percent of the net tax liability incurred during that period (although this requirement does not apply in certain situations, see Treas. Reg. § 40.6302(c)-1(b)(2); see also the "Safe Harbor Rule" in the "Instructions for Form 720"). To determine the net tax liability incurred during a given semimonthly period, a taxpayer should subtract any claims it makes on Schedule C of Form 720 (*e.g.*, credits or refunds) for that period from its total liability for that period. A taxpayer may calculate the net tax liability incurred during a given semimonthly period by halving the net tax liability incurred during the full month. However, if this "halving method" is used, it must be applied to each semimonthly period within that calendar quarter. (The month of September has special rules, including its own safe harbor rules, as noted below in C.)

C. Special Rules

1. Deposits for the Month of September

September deposits are subject to special rules. In September, *two* deposits must be made for the *second* semimonthly period (in addition to the deposit made for the first semimonthly period). The first of these two periods runs from September 16 through September 26. Deposits for this period are due by September 29. (If these dates fall on a weekend day, there is a special rule for calculating the day on which the tax is due. This rule is discussed below in 2.) The second of these two periods runs from September27 through September 30. Deposits for this period are due by October 14. For information on calculating the amount of deposits for the month of September, see Treas. Reg. § 40.6302(c)-2.

2. Weekend and Holiday Rules

If a taxpayer fails to file Form 720 when due, or fails to make deposits on time, the IRS may assess penalties on the taxpayer *in addition to interest charges*. Therefore, it is important for taxpayers to understand the actual deadlines for filing Form 720 and for making deposits. It also is important to understand that there are different rules that apply, depending on the type of deadline. Below are some of the general rules the IRS uses to determine the actual deadline if a due date occurs on a weekend or on a legal holiday

a. Form 720

If the due date for filing Form 720 is a legal holiday[246] or a weekend day, the deadline for filing Form 720 will be the *following* business day.

b. General Deposit Rule

Unlike the rule for filing Form 720, if the due date for a deposit is a legal holiday or a weekend day, the deposit must be made by the *prior* business day (that is not also a legal holiday).[247] *In addition, deposits through EFTPS must be commenced on the business day prior to the deadline.*

c. September Deposit Rule

If September 29 is a Saturday, the deposit is due on the *prior* day (*i.e.*, Friday). If September 29 is a Sunday, the deposit is due on the *subsequent* day (*i.e.*, Monday).

Each year Publication 509 provides guidance as to the actual deadlines for filing Form 720 and for making semimonthly deposits (*i.e.*, it takes into account weekends, legal holidays[248] and the month of February, which typically has only 28 days). This publication also provides a list of the legal holidays (other than state holidays) for that year. (When using this publication, it is important to understand that there are different calendars included in the publication; deadlines for filing Form 720 and making section 4051 deposits are in the "Excise Tax Calendar.") Given that an error in calculating the appropriate deadline may result in both interest and penalty payments, taxpayers should confirm with their tax counsel that they are using the correct deadlines for their filings and deposit payments.

Appendix

Appendix A: Form 720 Quarterly Federal Excise Tax Return

The following form is interactive. You may fill it out and save a copy on your computer. You can also access this interactive form from the "Synopsis" page of this ***Driven*** guide or online (current as of October 2011) at: http://www.irs.gov/pub/irs-pdf/f720.pdf

Form **720**
(Rev. January 2011)
Department of the Treasury
Internal Revenue Service

Quarterly Federal Excise Tax Return

▶ **See the Instructions for Form 720.**

OMB No. 1545-0023

Check here if:
☐ Final return
☐ Address change

Name | Quarter ending

Number, street, and room or suite no. (If you have a P.O. box, see the instructions.) | Employer identification number

City, state, and ZIP code. (If you have a foreign address, see the instructions.)

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Part I

IRS No.	Environmental Taxes (attach Form 6627)	Tax	IRS No.
18	Domestic petroleum oil spill tax		18
21	Imported petroleum products oil spill tax		21
98	Ozone-depleting chemicals (ODCs)		98
19	ODC tax on imported products		19

IRS No.	Communications and Air Transportation Taxes (see instructions)	Tax	IRS No.
22	Local telephone service and teletypewriter exchange service		22
26	Transportation of persons by air		26
28	Transportation of property by air		28
27	Use of international air travel facilities		27

IRS No.	Fuel Taxes	Number of gallons	Rate	Tax	IRS No.
60	(a) Diesel fuel, tax on removal at terminal rack		$.244		
	(b) Diesel fuel, tax on taxable events other than removal at terminal rack		.244		60
	(c) Diesel fuel, tax on sale or removal of biodiesel mixture other than removal at terminal rack		.244		
104	Diesel-water fuel emulsion		.198		104
105	Dyed diesel fuel, LUST tax		.001		105
107	Dyed kerosene, LUST tax		.001		107
119	LUST tax, other exempt removals (see instructions)		.001		119
35	(a) Kerosene, tax on removal at terminal rack (see instructions)		.244		
	(b) Kerosene, tax on taxable events other than removal at terminal rack		.244		35
69	Kerosene for use in aviation (see instructions)		.219		69
77	Kerosene for use in commercial aviation (other than foreign trade)		.044		77
111	Kerosene for use in aviation, LUST tax on nontaxable uses		.001		111
79	Other fuels (see instructions)				79
62	(a) Gasoline, tax on removal at terminal rack		.184		
	(b) Gasoline, tax on taxable events other than removal at terminal rack		.184		62
	(c) Gasoline, tax on sale or removal of alcohol fuel mixture other than removal at terminal rack		.184		
14	Aviation gasoline		.194		14
112	Liquefied petroleum gas (LPG)		.183		112
118	"P Series" fuels		.184		118
120	Compressed natural gas (CNG) (GGE = 126.67 cu. ft.)		.183		120
121	Liquefied hydrogen		.184		121
122	Any liquid fuel derived from coal (including peat) through the Fischer-Tropsch process		.244		122
123	Liquid fuel derived from biomass		.244		123
124	Liquefied natural gas (LNG)		.243		124

IRS No.	Retail Tax	Rate	Tax	IRS No.
33	Truck, trailer, and semitrailer chassis and bodies, and tractors	12% of sales price		33

IRS No.	Ship Passenger Tax	Number of persons	Rate	Tax	IRS No.
29	Transportation by water		$3 per person		29

IRS No.	Other Excise Tax	Amount of obligations	Rate	Tax	IRS No.
31	Obligations not in registered form		$ .01		31

IRS No.	Manufacturers Taxes	Number of tons	Sales price	Rate	Tax	IRS No.
36	Coal—Underground mined			$1.10 per ton		36
37				4.4% of sales price		37
38	Coal—Surface mined			$ .55 per ton		38
39				4.4% of sales price		39

		Number of tires	Tax	IRS No.
108	Taxable tires other than bias ply or super single tires			108
109	Taxable bias ply or super single tires (other than super single tires designed for steering)			109
113	Taxable tires, super single tires designed for steering			113
40	Gas guzzler tax. Attach Form 6197. Check if one-time filing . . . . ☐			40
97	Vaccines (see instructions)			97

IRS No.	**Foreign Insurance Taxes—** Policies issued by foreign insurers	Premiums paid	Rate	Tax	IRS No.
30	Casualty insurance and indemnity bonds		$ .04		
	Life insurance, sickness and accident policies, and annuity contracts		.01		30
	Reinsurance		.01		
1	**Total.** Add all amounts in Part I. Complete Schedule A unless one-time filing ▶			$	

Part II

IRS No.		Rate	Tax	IRS No.
41	Sport fishing equipment (other than fishing rods and fishing poles)	10% of sales price		41
110	Fishing rods and fishing poles (limits apply, see instructions)	10% of sales price		110
42	Electric outboard motors	3% of sales price		42
114	Fishing tackle boxes	3% of sales price		114
44	Bows, quivers, broadheads, and points	11% of sales price		44
106	Arrow shafts	$ .45 per shaft		106
140	Indoor tanning services	10% of amount pai		140

IRS No.		Number of gallons	Rate	Tax	IRS No.
64	Inland waterways fuel use tax		$ .20		64
125	LUST tax on inland waterways fuel use (see instructions)		.001		125
51	Alcohol and cellulosic biofuel sold as but not used as fuel				51
117	Biodiesel sold as but not used as fuel				117
20	**Floor Stocks Tax—** Ozone-depleting chemicals (floor stocks). Attach Form 6627.				20
2	**Total.** Add all amounts in Part II ▶			$	

Part III

3	Total tax. Add Part I, line 1, and Part II, line 2 . . . . ▶			3
4	Claims (see instructions; complete Schedule C) . . . . ▶		4	
5	Deposits made for the quarter . . . . . ▶	5		
	☐ Check here if you used the safe harbor rule to make your deposits.			
6	Overpayment from previous quarters . . ▶	6		
7	Enter the amount from Form 720X included on line 6, if any . . . . ▶	7		
8	Add lines 5 and 6 . . . . ▶		8	
9	Add lines 4 and 8 . . . . ▶			9
10	**Balance Due.** If line 3 is greater than line 9, enter the difference. Pay the full amount with the return (see instructions) ▶			10
11	**Overpayment.** If line 9 is greater than line 3, enter the difference. Check if you want the overpayment: ☐ **Applied to your next return, or** ☐ **Refunded to you.**			11

Third Party Designee

Do you want to allow another person to discuss this return with the IRS (see instructions)? ☐ **Yes.** Complete the following. ☐ **No**

Designee name ▶ Phone no. ▶ Personal identification number (PIN) ▶

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

▶ Signature Date ▶ Title

Type or print name below signature. Telephone number

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

Schedule A Excise Tax Liability (see instructions)

Note. *You must complete Schedule A if you have a liability for any tax in Part I of Form 720. Do not complete Schedule A for Part II taxes or for a one-time filing of the gas guzzler tax.*

1 Regular method taxes

(a) Record of Net Tax Liability	Period: 1st–15th day			Period: 16th–last day		
First month	A			B		
Second month	C			D		
Third month	E			F		
Special rule for September* . . . . ▶				G		

(b) Net liability for regular method taxes. Add the amounts for each semimonthly period.

2 Alternative method taxes (IRS Nos. 22, 26, 28, and 27)

(a) Record of Taxes Considered as Collected	Period: 1st–15th day			Period: 16th–last day		
First month	M			N		
Second month	O			P		
Third month	Q			R		
Special rule for September* . . . . ▶				S		

(b) Alternative method taxes. Add the amounts for each semimonthly period.

*Complete only as instructed (see instructions).

Schedule T Two-Party Exchange Information Reporting (see instructions)

Fuel	Number of gallons
Diesel fuel, gallons received in a two-party exchange within a terminal, included on IRS No. 60(a) on Form 720	
Diesel fuel, gallons delivered in a two-party exchange within a terminal	
Kerosene, gallons received in a two-party exchange within a terminal, included on IRS No. 35(a), 69, 77, or 111 on Form 720	
Kerosene, gallons delivered in a two-party exchange within a terminal	
Gasoline, gallons received in a two-party exchange within a terminal, included on IRS No. 62(a) on Form 720	
Gasoline, gallons delivered in a two-party exchange within a terminal	
Aviation gasoline, gallons received in a two-party exchange within a terminal, included on IRS No. 14 on Form 720	
Aviation gasoline, gallons delivered in a two-party exchange within a terminal	

Schedule C **Claims** Month your income tax year ends ▶

- **Complete Schedule C for claims *only* if you are reporting liability in Part I or II of Form 720.**
- Attach a statement explaining each claim as required. Include your name and EIN on the statement (see instructions).

Caution. *Claimant has the name and address of the person(s) who sold the fuel to the claimant, the dates of purchase, and if exported, the required proof of export. For claims on lines 1a and 2b (type of use 13 and 14), 3c, 4b, and 5, claimant has not waived the right to make the claim.*

1 Nontaxable Use of Gasoline **Note:** CRN is credit reference number. Period of claim ▶

		Type of use	Rate	Gallons	Amount of claim		CRN
a	Gasoline (see **Caution** above line 1)		$.183		$		362
b	Exported (see **Caution** above line 1)		.184				411

2 Nontaxable Use of Aviation Gasoline Period of claim ▶

		Type of use	Rate	Gallons	Amount of claim		CRN
a	Used in commercial aviation (other than foreign trade)		$.15		$		354
b	Other nontaxable use (see **Caution** above line 1)		.193				324
c	Exported (see **Caution** above line 1)		.194				412
d	LUST tax on aviation fuels used in foreign trade		.001				433

3 Nontaxable Use of Undyed Diesel Fuel Period of claim ▶

Claimant certifies that the diesel fuel did not contain visible evidence of dye.
Exception. If any of the diesel fuel included in this claim **did** contain visible evidence of dye, attach a detailed explanation and check here . . . . ▶ ☐

		Type of use	Rate	Gallons	Amount of claim		CRN
a	Nontaxable use		$.243		$		360
b	Use in trains		.243				353
c	Use in certain intercity and local buses (see **Caution** above line 1)		.17				350
d	Use on a farm for farming purposes		.243				360
e	Exported (see **Caution** above line 1)		.244				413

4 Nontaxable Use of Undyed Kerosene (Other Than Kerosene Used in Aviation) Period of claim ▶

Claimant certifies that the kerosene did not contain visible evidence of dye.
Exception. If any of the kerosene included in this claim **did** contain visible evidence of dye, attach a detailed explanation and check here . . . . ▶ ☐

	Caution. *Claims cannot be made on line 4 for kerosene sales from a blocked pump.*	Type of use	Rate	Gallons	Amount of claim		CRN
a	Nontaxable use		$.243		$		346
b	Use in certain intercity and local buses (see **Caution** above line 1)		.17				347
c	Use on a farm for farming purposes		.243				346
d	Exported (see **Caution** above line 1)		.244				414
e	Nontaxable use taxed at $.044		.043				377
f	Nontaxable use taxed at $.219		.218				369

5 Kerosene Used in Aviation (see **Caution** above line 1) Period of claim ▶

		Type of use	Rate	Gallons	Amount of claim		CRN
a	Kerosene used in commercial aviation (other than foreign trade) taxed at $.244		$.200		$		417
b	Kerosene used in commercial aviation (other than foreign trade) taxed at $.219		.175				355
c	Nontaxable use (other than use by state or local government) taxed at $.244		.243				346
d	Nontaxable use (other than use by state or local government) taxed at $.219		.218				369
e	LUST tax on aviation fuels used in foreign trade		.001				433

6 Nontaxable Use of Alternative Fuel

Caution. *There is a reduced credit rate for use in certain intercity and local buses (type of use 5) (see instructions).*

		Type of use	Rate	Gallons or gasoline gallon equivalents (GGE)	Amount of claim	CRN
a	Liquefied petroleum gas (LPG)		$.183		$	419
b	"P Series" fuels		.183			420
c	Compressed natural gas (CNG) (GGE = 126.67 cu. ft.)		.183			421
d	Liquefied hydrogen		.183			422
e	Any liquid fuel derived from coal (including peat) through the Fischer-Tropsch process		.243			423
f	Liquid fuel derived from biomass		.243			424
g	Liquefied natural gas (LNG)		.243			425
h	Liquefied gas derived from biomass		.183			435

7 Sales by Registered Ultimate Vendors of Undyed Diesel Fuel

Period of claim ▶

Registration number ▶

Claimant certifies that it sold the diesel fuel at a tax-excluded price, repaid the amount of tax to the buyer, or has obtained written consent of the buyer to make the claim. Claimant certifies that the diesel fuel did not contain visible evidence of dye.

Exception. If any of the diesel fuel included in this claim **did** contain visible evidence of dye, attach a detailed explanation and check here . . . . ▶ ☐

		Rate	Gallons	Amount of claim	CRN
a	Use by a state or local government	$.243		$	360
b	Use in certain intercity and local buses	.17			350

8 Sales by Registered Ultimate Vendors of Undyed Kerosene (Other Than Kerosene For Use in Aviation)

Period of claim ▶

Registration number ▶

Claimant certifies that it sold the kerosene at a tax-excluded price, repaid the amount of tax to the buyer, or has obtained the written consent of the buyer to make the claim. Claimant certifies that the kerosene did not contain visible evidence of dye.

Exception. If any of the kerosene included in this claim **did** contain visible evidence of dye, attach a detailed explanation and check here . . . . ▶ ☐

		Rate	Gallons	Amount of claim	CRN
a	Use by a state or local government	$.243		$	346
b	Sales from a blocked pump	.243			
c	Use in certain intercity and local buses	.17			347

9 Sales by Registered Ultimate Vendors of Kerosene For Use in Aviation

Registration number ▶

Claimant sold the kerosene for use in aviation at a tax-excluded price and has not collected the amount of tax from the buyer, repaid the amount of tax to the buyer, or has obtained written consent of the buyer to make the claim. See the instructions for additional information to be submitted.

		Type of use	Rate	Gallons	Amount of claim	CRN
a	Use in commercial aviation (other than foreign trade) taxed at $.219		$.175		$	355
b	Use in commercial aviation (other than foreign trade) taxed at $.244		.200			417
c	Nonexempt use in noncommercial aviation		.025			418
d	Other nontaxable uses taxed at $.244		.243			346
e	Other nontaxable uses taxed at $.219		.218			369
f	LUST tax on aviation fuels used in foreign trade		.001			433

10 Sales by Registered Ultimate Vendors of Gasoline

Registration number ▶

Claimant sold the gasoline at a tax-excluded price and has not collected the amount of tax from the buyer, repaid the amount of tax to the buyer, or has obtained written consent of the buyer to take the claim; and obtained an unexpired certificate from the buyer and has no reason to believe any information in the certificate is false. See the instructions for additional information to be submitted.

		Rate	Gallons	Amount of claim	CRN
a	Use by a nonprofit educational organization	$.183		$	362
b	Use by a state or local government	.183			

11 Sales by Registered Ultimate Vendors of Aviation Gasoline Registration number ▶

Claimant sold the aviation gasoline at a tax-excluded price and has not collected the amount of tax from the buyer, repaid the amount of tax to the buyer, or has obtained written consent of the buyer to take the claim; and obtained an unexpired certificate from the buyer and has no reason to believe any information in the certificate is false. See the instructions for additional information to be submitted.

		Rate	Gallons	Amount of claim		CRN
a	Use by a nonprofit educational organization	$.193		$		324
b	Use by a state or local government	.193				

12 Alcohol Fuel Mixture Credit Period of claim ▶ Registration number ▶

Claimant produced an alcohol fuel mixture by mixing taxable fuel with alcohol. The alcohol fuel mixture was sold by the claimant to any person for use as a fuel or was used as a fuel by the claimant (see instructions).

		Rate	Gallons	Amount of claim		CRN
a	Alcohol fuel mixtures containing ethanol	$.45		$		393
b	Alcohol fuel mixtures containing alcohol (other than ethanol)	.60				394

13 Biodiesel or Renewable Diesel Mixture Credit Period of claim ▶ Registration number ▶

Biodiesel mixtures. Claimant produced a mixture by mixing biodiesel with diesel fuel. The biodiesel used to produce the mixture met ASTM D6751 and met EPA's registration requirements for fuels and fuel additives. The mixture was sold by the claimant to any person for use as a fuel or was used as a fuel by the claimant. Claimant has attached the Certificate for Biodiesel and, if applicable, the Statement of Biodiesel Reseller. **Renewable diesel mixtures.** Claimant produced a mixture by mixing renewable diesel with liquid fuel (other than renewable diesel). The renewable diesel used to produce the renewable diesel mixture was derived from biomass, met EPA's registration requirements for fuels and fuel additives, and met ASTM D975, D396, or other equivalent standard approved by the IRS. The mixture was sold by the claimant to any person for use as a fuel or was used as a fuel by the claimant. Claimant has attached the Certificate for Biodiesel and, if applicable, Statement of Biodiesel Reseller, both of which have been edited as discussed in the instructions for line 13. See the instructions for line 13 for information about renewable diesel used in aviation.

		Rate	Gal. of biodiesel or renewable Diesel	Amount of claim		CRN
a	Biodiesel (other than agri-biodiesel) mixtures	$1.00		$		388
b	Agri-biodiesel mixtures	1.00				390
c	Renewable diesel mixtures	1.00				307

14 Alternative Fuel Credit and Alternative Fuel Mixture Credit Registration number ▶

For the alternative fuel mixture credit, claimant produced a mixture by mixing taxable fuel with alternative fuel. Claimant certifies that it (a) produced the alternative fuel, or (b) has in its possession the name, address, and EIN of the person(s) that sold the alternative fuel to the claimant; the date of purchase; and an invoice or other documentation identifying the amount of the alternative fuel. The claimant also certifies that it made no other claim for the amount of the alternative fuel, or has repaid the amount to the government. The alternative fuel mixture was sold by the claimant to any person for use as a fuel or was used as a fuel by the claimant.

		Rate	Gallons or gasoline gallon equivalents (GGE) (see instructions)	Amount of claim		CRN
a	Liquefied petroleum gas (LPG)	$.50		$		426
b	"P" Series fuels	.50				427
c	Compressed natural gas (CNG) (GGE = 121 cu. ft.)	.50				428
d	Liquefied hydrogen	.50				429
e	Any liquid fuel derived from coal (including peat) through the Fischer-Tropsch process	.50				430
f	Liquid fuel derived from biomass	.50				431
g	Liquefied natural gas (LNG)	.50				432
h	Liquefied gas derived from biomass	.50				436
i	Compressed gas derived from biomass (GGE = 121 cu. ft.)	.50				437

15 Other claims. See the instructions. For lines 15b and 15c, see the **Caution** above line 1 on page 4.

		Amount of claim		CRN
a	Section 4051(d) tire credit (tax on vehicle reported on IRS No. 33)	$		366
b	Exported dyed diesel fuel and exported gasoline blendstocks taxed at $.001			415
c	Exported dyed kerosene			416
d	Diesel-water fuel emulsion			
e	Registered credit card issuers			

		Number of tires	Amount of claim		CRN
f	Taxable tires other than bias ply or super single tires		$		396
g	Taxable tires, bias ply or super single tires (other than super single tires designed for steering)				304
h	Taxable tires, super single tires designed for steering				305
i					
j					
k					

16 Total claims. Add amounts on lines 1 through 15. Enter the result here and on Form 720, Part III, line 4. **16**

Form 720-V, Payment Voucher

Purpose of Form

Complete Form 720-V if you are making a payment by check or money order with Form 720, Quarterly Federal Excise Tax Return. We will use the completed voucher to credit your payment more promptly and accurately, and to improve our service to you.

If you have your return prepared by a third party and a payment is required, provide this payment voucher to the return preparer.

Do not file Form 720-V if you are paying the balance due on line 10 of Form 720 using EFTPS.

Specific Instructions

Box 1. If you do not have an EIN, you may apply for one online. Go to the IRS website at *www.irs.gov/businesses/small* and click on the "Employer ID Numbers (EINs)" link. You may also apply for an EIN by calling 1-800-829-4933, or you can fax or mail Form SS-4, Application for Employer Identification Number, to the IRS. However, if you are making a one-time filing, enter your social security number.

Box 2. Enter the amount paid from line 10 of Form 720.

Box 3. Darken the circle identifying the quarter for which the payment is made. Darken only one circle.

Box 4. Enter your name and address as shown on Form 720.

- Enclose your check or money order made payable to the "United States Treasury." Be sure to enter your EIN, (SSN for one-time filing), "Form 720," and the tax period on your check or money order. Do not send cash. Do not staple this voucher or your payment to the return (or to each other).
- Detach the completed voucher and send it with your payment and Form 720. See *Where To File* on page 1 of the Instructions for Form 720.

Form **720-V** (2011)

▼ **Detach Here and Mail With Your Payment and Form 720.** ▼

720-V

Department of the Treasury
Internal Revenue Service

Payment Voucher

▶ **Do not staple or attach this voucher to your payment.**

OMB No. 1545-0023

2011

1 Enter your employer identification number (EIN) (see instructions).		**2** **Enter the amount of your payment.** ▶	Dollars	Cents
3 Tax Period		**4** Enter your business name (individual name if sole proprietor).		
○ 1st Quarter	○ 3rd Quarter	Enter your address.		
○ 2nd Quarter	○ 4th Quarter	Enter your city, state, and ZIP code.		

ENDNOTES

[1] However, Section XII reflects the new rule eliminating the deposit coupon option for making deposits, effective January 1, 2011. Please note that subsequent to December 2010, the IRS may amend its regulations or issue new rulings (or Congress may amend the statute), which may affect the accuracy of the information in this guide.

[2] Court cases also may be instructive. Although the IRS generally is free to disagree with a court ruling and take a contrary position for purposes of future audits, a court ruling that supports a taxpayer's position may persuade an IRS examining or appeals agent to adopt a similar view.

[3] A chassis or body of a passenger automobile is not subject to FET.

[4] Courts have disagreed whether a vehicle towing living accommodations (manufactured home) is a "Tractor" subject to FET. *Horton Homes Inc. v. United States,* 357 F.3d. 1209 (11th Cir. 2004) (towing a manufactured home could not be considered towing a "trailer or semitrailer" for purposes of defining a tractor; cf. *Freightliner of Grand Rapids, Inc. v. United States*, 351 F. Supp.2d 718 (W.D. Mich. 2004) ("*Freightliner*") (definition of tractor does not require the towing of a *commercial* trailer or semitrailer.)

[5] Treas. Reg. § 48.4061(a)-1(d)(1). A public highway is defined as any non-private roadway. *Id.*

[6] This was especially the case prior to October 1, 2005, when any tractor "chiefly used for highway transportation in combination with a trailer or semitrailer" was taxable, *regardless of its gross vehicle weight rating*. The 2005 Safe, Accountable, Flexible, Efficient Transportation Equality Act ("SAFETEA"), effective October 1, 2005, required that tractors exceed certain gross vehicle weight and gross combined weight levels in order to be taxable.

[7] Treas. Reg. § 145.4051-1(e)(1) (emphasis added).

[8] This presumption can be rebutted. *See* Letter Ruling 200221019. (Feb. 14, 2002) and TAM 200237002 (Apr. 26, 2002).

[9] Treas. Reg. § 145.4051-1(e)(2) (emphasis added).

[10] *See* Rev. Rul. 2004-80 (noting that "an absolute inability to carry any cargo on the vehicle's chassis" is not required in order to classify a vehicle as a tractor). *See* also TAMs, 200341003 (May 16, 2003), 200222002. (Jan. 16, 2002) and 200025006 (Mar. 2, 2000). Please note, however, that these rulings (as well as Rev. Rul. 2004-80, 2004-2 C.B. 164 (Aug. 9, 2004)) applied the law in effect prior to the enactment of SAFETEA in October 2005.

[11] Rev. Rul. 2004-80, 2004-2 C.B. 164 (Aug. 9, 2004).

[12] Rev. Rul. 2004-.80, 2004-2 C.B. 164 (Aug. 9, 2004).

[13] Letter Ruling 9013012 (Dec. 20, 1989) indicates that the IRS still might treat a chassis cab equipped with one or more of the identified equipment as a truck, if the purchaser provides the seller with a certificate that the purchaser will complete the chassis cab as a nontaxable truck and the seller receives proof from the purchaser within six months of the purchase (or delivery, if earlier) that the chassis cab was, in fact, completed as a nontaxable truck. However, be aware that this ruling appears to be contrary to the language in the regulations, so you should consult with your tax advisor on this issue.

[14] Treas. Reg. § 145.4051-1(e)(1)(ii).

[15] *Freightliner of Grand Rapids, Inc. v. United States*, 351 F. Supp.2d 718 (W.D. Mich. 2004).

[16] Treas. Reg. § 145.4051-1(e)(3)(i).

[17] Treas. Reg. § 145.4051-1(e)(3)(ii).

[18] In 2005, the IRS acknowledged that GVW rating assignments are not routinely done with respect to truck bodies because of their specialized nature, the lack of Congressional or IRS guidance and the fact that body sellers may not know the "GVW of the vehicle on which the body (or similar bodies sold by others) will be mounted." *See* Rev.Proc. 2005-19, 2005-1 C.B. 832 (Apr. 4, 2005).

[19] Rev. Rul. 85-196, 1985-2 C.B. 205 (Dec. 23, 1985), clarified by Rev. Rul. 86-143, 1986-2 C.B. 149 (Dec. 8, 1986) and Rev. Rul. 86-113, 1986-1 C.B. 177 (Sept. 22, 1986).

[20] Interestingly, Treas. Reg. § 145.4051-1(e)(3)(v) appears to contemplate the use of factors other than frame strength and axle placement and capacity in calculating a vehicle's gross vehicle weight.

[21] *See* TAM 9119001 (Oct. 3, 1990).

[22] The IRS in TAM 9119001 (Oct. 3, 1990) states that "[e]ven though Rev. Proc. 76-21 was developed for use under the now repealed manufacturer's tax imposed under section 4061 of the Code, it is equally applicable to the retailer's tax imposed under section 4051." In Rev. Proc. 76-21, 1976-1 C.B. 561 (1976), the IRS indicates that taxpayers may be able to argue for a lower GVW than the one calculated under the formula in that Revenue Procedure.

[23] *See* Treas. Reg. § 145.4051-1(e)(3)(i).

[24] *See* TAM 20060603 and TAM 9144002 (July 12, 1991)

[25] Private Letter Ruling 8412060 (Dec. 20, 1983); TAM 9717003 (Dec. 13, 1996); TAM 200606038 (Sept. 30, 2005).

[26] Treas. Reg. § 145-4051-1(e)(3)(iv).

[27] *See* TAM 9717003.

[28] The term "practical fitness" is defined as "perform[ing] its intended function up to a generally acceptable standard or efficiency." The term "commercial fitness" is defined as being "generally available for use with the vehicle at a price that is reasonably competitive with other articles that may be used for the same purpose." *See* Treas. Reg. § 145.4051-1(a)(4).

[29] *See* TAM 9752001 (Sept. 2, 1997) (applying the practical and commercial fitness standard).

[30] *See* Rev. Proc. 2005-19, 2005-1 C.B. 832 (Apr. 4, 2005) (noting that "a truck chassis which is suitable for use with a vehicle having a gross vehicle weight of 33,000 pounds or less, is not subject to the tax imposed by § 4051(a)(1) *regardless of the body actually mounted* thereon") (emphasis added); TAM 200606038 (Sept. 30, 2005) (noting that "[t]he limited capacity of the tank body does not dictate the tax status of the chassis because a body and chassis are two separate taxable items").

[31] *See* Rev. Proc. 2005-19, 2005-1 C.B. 832 (Apr. 4, 2005) (stating that "[s]ince the weight rating of the chassis and the gross vehicle weight of a complete vehicle would normally be the same, a truck chassis seller is aided in establishing a weight rating for a chassis by the guidelines set forth in Treas. Reg. § 145.4051-1(e)(3)(v)").

[32] *See* Rev. Proc. 2005-.19, 2005-1 C.B. 832 (Apr. 4, 2005). In this Revenue Procedure, the IRS notes that this is the case because "there are no federal excise tax guidelines to establish a weight rating for a truck body" and that "many truck bodies are specialized in nature."

[33] TAM 9752001 (Sept. 2, 1997) (noting that the "taxability of any particular body must always be viewed in conjunction with the weight rating of the chassis on which that particular body can *suitably* be mounted," and that the truck bodies at issue were only installed on chassis exceeding the taxable weight threshold) (emphasis added).

[34] *See* Letter Ruling 8820032 (Feb. 17, 1988). This appears to be the only letter ruling where the IRS provided specific percentage of use data. In Technical Advice Memorandum 9226995 (Feb. 27, 1992), the IRS determined that certain platform bodies in excess of 21 feet were taxable because the submitted information did not demonstrate that such bodies were suitable for use with vehicles rated 33,000 pounds GVW or less, but the IRS did not provide any specific information regarding the submitted sales data.

[35] Rev. Proc. 2005-19, 2005-1 C.B. 832 (Apr. 4, 2005).

[36] *See* Treas. Reg. § 48.4061(a)-1(a)(3). Although this regulation was issued under the now-repealed section 4061 tax, the substance of this regulation continues to apply to FET. *See* Treas. Reg. § 145.4052-1(f)(2).

[37] *See* Treas. Reg. § 48.4061(a)-1(a)(3).

[38] *See* Treas. Reg. § 48.4061(a)-1(a)(3)(ii).

[39] Treas. Reg. § 48.4061(a)-1(a)(3)(ii).

[40] Treas. Reg. § 48.4061(a)-1(a)(3)(ii). *See* also TAM 200202021 (Sept, 24, 2001) (noting that the mobile car crusher reference in Treasury Regulations does not transport cargo and is the load carried by the chassis).

[41] TAM 8610005 (Nov. 5, 1985) (but noting that the walls themselves are taxable "because they constitute an integral part of the taxable body").

[42] *See* Rev. Rul. 95-40, 1995-20 I.R.B. 5 (May 15, 1995). The following components of vacuum loaders did not contribute to the highway transportation function: "vacuum pump and hose (which perform primarily a debris retrieval function although they perform a loading and unloading function as well), filter system, material separator, silencer or muffler, control cabinet, and ladder." For the sewer cleaning vehicle, such components were: "the high pressure water pump, hose components (which perform primarily a flushing and backflushing function), and the vacuum pipe." The IRS noted that the taxpayer might be able to demonstrate that other components of the vehicles similarly did not contribute to the highway transportation function.

[43] For the vehicles removing pavement lines, the following items were not taxable because they did not contribute to the highway transportation function: "the four motors, the compressor, the vacuum fans with housing, the control panels for operation of the machinery, … the grinder and saw box carriages[,] [t]he vacuum equipment, the collector bin, the water tank, and the water spray system." For the vehicles marking the pavement, such items included "the auxiliary power plant, hydraulic pumps, hoses, paint or thermoplastic sprayer equipment, and extendable cartridges … ." *See* Letter Ruling 200031032 (May 4, 2000).

[44] Although not expressly stated in the regulations, the IRS likely would apply the flip side of this reasoning: if a part or accessory were taxable under 4061(b), then it also would be taxable under 4051(b). *See* TAM 8936004 (June 7, 1989); TAM 8752005 (Aug. 31, 1987).

[45] Treas. Reg. § 145.4051-1(c), by its terms, incorporates the prior provisions under IRC § 4061(b)(1) and (2) only with respect to the tax imposed on parts and accessories under the Six-Month Rule. *See* also TAM 200315005 (Dec. 11, 2002) (noting that a part or accessory sold on or in connection with a taxable item may be taxable, even *if* it were not taxable under 4061(b)); TAM 8936004 (June 7, 1989) (similar). In other words, the Treasury Regulation does not appear generally to apply to parts and accessories sold *on or in connection* with taxable items. *But* see endnote 50 below.

[46] Treas. Reg 48.4061(b)-2(a). Note that although this regulation was written to apply to the now-repealed section 4061(b), it still applies to parts or accessories under the Six-Month Rule.

[47] Letter Ruling 8350098 (Sept. 14, 1983).

[48] Treas. Reg. § 145.4051-1(a)(3).

[49] Treas. Reg. § 145.4051-1(a)(3). *See* also TAM 9226005 (noting that when a body and a compatible part or accessory are ordered together, the part or accessory is taxable, unless the taxpayer can show that such part or accessory is a spare or replacement). *See* also TAM 200023013 (noting that axles are truck chassis components, and rejecting argument that the sale of an axle is "in connection with" the sale of a taxable body).

[50] Revenue Ruling 75-88 (which created the 25 foot rule) was issued under IRC § 4061(b). As noted above, the Six-Month Rule, under section 4051(b), expressly incorporates the principles of section 4061(b) for purposes of determining what items are treated as taxable parts or accessories. However, the principles of section 4061(b) do not appear to have been adopted with respect to determining the taxability of parts or accessories sold on or in connection with a taxable chassis, body, or tractor, under section 4051(a). Nevertheless, the IRS appears routinely to have applied the 25-foot rule to parts and accessories sold under section 4051(a). *See* TAMs 9234001 (Jan. 27, 1992), 9332001 (Nov. 9, 1992), 9311003 (Nov. 6, 1992) and 200023015 (Feb. 29, 2000); and Letter Rulings 200032034 (May 16, 2000). This is consistent with the principle under section 4051(a) that parts or accessories are not taxable if they do not contribute to the transportation function (which includes loading and unloading) of the taxable chassis, body, or tractor.

[51] For guidance on how to calculate the taxable sales price when a nontaxable crane is installed on a taxable chassis, ad the crane and chassis are sold as a single unit, *see* Letter Ruling 200032034 (May 16, 2000) and Letter Ruling 200023015 (Feb. 29, 2000) (both citing Rev. Rul. 69-394, 1969-2 C.B. 206 (1969)).

[52] In Revenue Ruling 80-90,1980-1 C.B. 240 (Mar. 31, 1980), the IRS determined that a crane less than 25 feet long was a nontaxable part and accessory. In making such a determination, the IRS, among other factors, looked at the crane's lifting capacity, power source, winch, rotation and elevation speeds, and price.

[53] In fact, there has been at least one ruling that applied the 25-foot presumption to certain aerial devices. *See* TAM 200023015 (Feb. 29, 2000).

[54] *See* Treas. Reg. § 48.0-2(a)(4)(ii); TAM 200606038 (Sept. 30, 2005); TAM 8638002 (June 5, 1986); Rev. Rul. 83-149, 1983-2 C.B. 186 (Oct. 3, 1983), Situation 3 (decided under IRC § 4061).

[55] *See* Letter Rulings 9245003 (July 23, 1993) and 9713009 (Dec. 12, 1996); TAMs 200146024 (July 27, 2001) and 9144003 (July 22, 1991).

[56] Treas. Reg. § 145.4052-1(a)(2)(iii).

[57] Letter Ruling 9450027

[58] Treas. Reg. § 145.4052-1(a)(2)(iii)

[59] Treas. Reg. § 145.4052-1(a)(4) which states:

> (4) *Special rule for tax-paid trailer and semitrailer. In the case of a taxable sale of a trailer or semitrailer less than six months after a taxable sale of the article, the seller in the subsequent sale ("the subsequent seller") may claim a credit equal to the amount of tax previously paid by another person ("the previous taxpayer") under section 4051(a)(1) with respect to the prior taxable sale of the article. The credit for such tax will be allowed to the subsequent seller only if the form on which the credit is claimed is accompanied by a statement, signed by the subsequent seller, indicating the amount of the credit being claimed under this paragraph (a)(4) and stating that—*
>
> *(i) The subsequent seller has not been repaid any portion of such tax by the previous taxpayer,*
>
> *(ii) The subsequent seller has not provided the previous taxpayer with written consent to allow the previous taxpayer to claim a credit or refund of such tax under section 6416 (a), and*
>
> *(iii) The subsequent seller has records (e.g., invoices) substantiating the amount of tax paid by the previous taxpayer with respect to the prior taxable sale of such article.*
>
> *In no case shall the amount of the credit allowable under this paragraph (a)(4) with respect to an article exceed the tax liability of the subsequent seller with respect to the sale of such article.*

[60] *See* section 4221 and Section VI for a discussion of tax-free sales.

[61] *See* section 4053 and Section VII for a discussion of these exemptions.

[62] *See* Section II for a discussion of the types of chassis, bodies and tractors that are subject to FET.

[63] For sales after June 30, 1998, Temp. Treas. Reg. § 145.4052-1 no longer expressly refers to sales for resales as an exception in subsection (a)(2)(ii); instead, subsection (a)(2)(ii) now provides a cross reference to Treas. Reg. § 48.4052-1, which, in turn, provides that FET will not be imposed on sales for resales *if* the applicable requirements are satisfied. It is unclear why the IRS made this change in format, but it should not affect the analysis in this section. With respect to other issues, however, the subtle distinction between whether a sale for resale is (1) a taxable first retail sale, *unless* the necessary requirements are satisfied, or (2) a nontaxable sale that may become a taxable first retail sale if the necessary requirements are not satisfied, may affect whether a sale is taxable in certain contexts. For more discussion on this issue, see Section IV referring to Letter Ruling 200036038 (June 8, 2000).

[64] If the sale by a manufacturer to a distributor satisfies the requirements for a tax-free sale for resale and then the distributor sells to a *second* distributor for resale, that second sale should also be eligible for tax-free sale for resale treatment, so long as the tax-free requirements are satisfied. (However, the authors are not aware of any ruling addressing this issue.) The subsequent sale by the second distributor to the end-user would be taxable.

[65] *See* the Six-Month Rule at 26 IRC §4051(b). *See* also Section V.

[66] The pre-amendment version of Temp. Treas. Reg. § 145.4052-1(a)(1) stated that "the sale of an article to a purchaser who is not engaged in the business of leasing and who intends to resell the article *is not a first retail sale*" (emphasis added).

[67] However, even under the older regulatory framework, a narrow category of sales for resale were taxable. Under the old regulations, if a purchaser were in the business of leasing, and the purchaser intended to resell the article, then the sale was a taxable "first retail sale", unless certain certification and other requirements were satisfied. Treas. Reg. § 145.4052-1(a)(1) stated, in relevant part: "In addition, the sale of an article to a purchaser who is engaged in the business of leasing to any extent will not be considered a 'first retail sale' if the purchaser and the seller are registered under s. 48.4222(a)-1, and the seller in good faith accepts a proper certification, as provided in paragraph (a)(3) of this section, from the purchaser that the purchaser intends to resell the article." *See* 50 Fed. Reg. 37350 (Sept. 13, 1985). Therefore, older IRS rulings concerning sales for resale to purchasers in the leasing business can still provide some guidance with respect to the IRS's treatment of sales for resale.

[68] *See* Temp. Treas. Reg. § 48.4052-1.

[69] Technically, a separate "certificate" is no longer required so long as the purchaser executes a "statement" satisfying all the necessary requirements and the statement is substantially in the form of the certificate provided in the IRS's regulations. The distinction between a separate "certificate" and a "statement" presumably stems from IRC § 4052(g), which provides that a statement may be executed on the sales invoice. However, in order to avoid confusion, we will use the term "certificate" throughout this section.

[70] *See* Temp. Treas. Reg. § 145.4052-1(a)(6) as modified by Treas. Reg. § 48.4052-1.

[71] Temp. Treas. Reg. § 145.4052-1(a)(6).

[72] This choice was illustrated in TAM 200309002 (Sept. 27, 2002), in which a purchaser bought trucks from a manufacturer and then sold them to end-users. The purchaser previously had provided the manufacturer with a resale certificate, but had subsequently revoked the certificate. The local IRS office argued that the purchaser was liable for FET because the sale by the purchaser to an end-user was the first retail sale. The local IRS office supported its position by noting that the invoices by the manufacturer stated that the sales to the purchaser were for resale. The purchaser, on the other hand, argued that because it did not give the manufacturer a resale certificate, the manufacturer's sale of the trucks to the purchaser was the first retail sale.

The National Office of the IRS agreed with the purchaser and ruled that, without a resale certificate, the manufacturer was liable for its sales for resale to the purchaser. The IRS noted: *"Although a person that buys a truck for resale may purchase it tax free under the above regulatory structure, a truck retailer may elect to have the s. 4051 tax imposed on its purchase of a truck by not providing its seller with a certification of purchase for resale. If it does so, then there has been a prior taxable sale of the vehicle within the meaning of s. 145.4052-1(a)(2)(iii) and a subsequent sale of the same vehicle is not a first retail sale under these regulations."*

[73] *See Volvo Trucks North America, Inc. v. United States*, 2003 WL 223421 (M.D.N.C. 2003) ("Volvo"), aff'd, 2004 WL 952915 (4th Cir. 2004). In Volvo, a manufacturer sold certain taxable articles to three franchise dealers. At the time of these transactions, the IRS required that a resale certificate include a registration number. Two of the dealers actually provided the manufacturer with resale certificates. However, these resale certificates were incomplete. Although these resale certificates indicated that those two dealers had applied for a registration number, the certificates did not include that number. The third dealer did not provide the manufacturer with any resale certificate. However, all of the sales between the manufacturer and the dealer were governed by an agreement that indicated the sales were for resale and that required the dealer to be responsible for the excise taxes. In addition, there was some evidence that certain dealers already had paid the FET in dispute in that case. The ruling of the district court was affirmed by the Fourth Circuit. *See* 2004 WL 952915.

[74] *Freightliner of Grand Rapids, Inc. v. United States*, 351 F. Supp.2d 718 (W.D. Mich. 2004) (*Freightliner*.)

[75] That section of the Code directs the Secretary of the Treasury to issue regulations "similar to the rules of...section 4222." section 4222 of the Code requires certain manufacturers and purchasers to be registered in order to qualify for certain tax-free sales under section 4221, and certain tax-free sales under section 4221 require certificates or statements.

[76] For purposes of this section, it is assumed the chassis, bodies and tractors exceed the applicable GVW thresholds so as not to be excluded from the scope of FET. *See* Section II.A.1. Similarly, it is assumed that these chassis, bodies and tractors are not excluded from the scope of FET by virtue of an exemption at IRC § 4053. *See* Section VII.

[77] As discussed in more detail in Section III, a sale by a manufacturer to a dealer, in certain circumstances, will be treated as a "retail" sale for purposes of FET.

[78] Nothing in the IRS's regulations limits the ability of buyers and sellers to conduct a sale as a tax-free sale for resale more than once in the series of transactions that may result between the manufacture of a vehicle and its ultimate sale to an end-user. We are also aware of no IRS rulings that so limit the use of tax-free sales for resale.

[79] Rev. Rul. 85-95, 1985-2 C.B. 204 (July 8, 1985) (stating that a dealer in a foreign country sold the truck at retail in that country and ruling that the retail sale of the used truck in the U.S. following importation was the first retail sale of the truck).

[80] *See United States Truck Sales Co. v. United States*, 229 F2d 693 (6th Cir. 1956). The IRS appears to have accepted this general principle. *See* Rev. Rul. 81-97, 1981-1 C.B. 498 (March 23, 1981); Rev. Rul. 85.95, 1985-2 C.B. 204 (July 8, 1985).

[81] Letter Ruling 200036038 (June 8, 2000).

[82] Prior to March 31, 2000, the IRS regulations provided generally that all sales (including sales for resale) were taxable, unless the sale satisfied one of three exceptions. One of those exceptions was that the sale satisfied the requirements for a tax-free sale for resale. In March 2000, the IRS moved the provisions concerning sales for resale to a new section of the regulations. *See* Treas. Reg. § 48.4052-1. The new sale for resale provisions provide that such a sale will not be taxable if certain requirements are satisfied (as opposed to providing that the sale will be taxable unless those requirements are met). This is a subtle difference, but it could be construed to support the IRS position that a sale for resale is not a taxable sale for the purpose of qualifying as a tax-free sale for export. The IRS is attempting to draw a distinction between a taxable sale for export that may be conducted on a tax-free basis if certain requirements are satisfied, on the one hand, and a non-taxable sale for resale that is transformed into a taxable sale if certain requirements are not satisfied, on the other hand. Support for this IRS position would appear to rely heavily on semantics,. If you previously treated sales to dealers in foreign countries as a tax-free sale for export, and are involved in an audit in which the IRS seeks the payment of taxes for those sales, you should seek legal advice on whether to challenge the IRS's position.

[83] *See* Treas. Reg. § 48.4221-3(a)(2); Rev. Rul. 81-97, 1981-1 C.B. 498 (Mar. 23, 1981).

[84] *See* IRC § 4051(b); Temp. Treas. Reg. § 145.4051-1(c).

[85] The Treasury Regulations note that this date may be "established by the delivery ticket signed by the owner or other comparable documents indicating delivery to and acceptance by the owner." *See* Temp. Treas. Reg. § 145.4051-1(c)(2). Therefore, this date may be earlier than the date on which the owner first uses the article.

[86] Although the statute and treasury regulations expressly state that the installer is secondarily liable for FET under the Six-Month Rule, these provisions do not expressly identify the party that is primarily liable for the FET. However, Letter Ruling 200052011 (Sept. 26, 2000) states that it is the "owner, lessee, or operator of the vehicle on which the parts or accessories are installed").

[87] *See* Letter Ruling 200052011 (Sept. 26, 2000) (noting that "if the owner, lessee or operator of the vehicle on which Company installs an accessory does not file an excise tax return and pay the excise tax, Company is secondarily liable for this tax").

[88] These categories of further manufacturing are not in the statute or treasury regulations, but were identified in a 1988 Conference Committee Report and adopted by the IRS in Rev. Rul. 91-27.27, 1991-1 C.B. 192 (Apr. 15, 1991). Although Congress subsequently enacted IRC § 4052(f), which provides that a certain class of modifications will not be treated as further manufacturing, nothing in that section indicates that the exception was intended to alter the basic definition of further manufacturing.

[89] *See* IRC § 4052(f). The 75 Percent Rule became effective on January 1, 1998.

[90] *See* IRC § 4052(f)(2).

[91] The IRS takes the position that the addition of a lift-axle to a chassis increases the GVWR of that chassis. There are compelling legal and engineering reasons in some situations to argue that a lift-axle does not necessarily increase GVWR. However, in the past, the IRS has not been receptive to such arguments.

[92] *See* Treas. Reg. § 48.0-2(a)(4)(ii). *See* also TAM 200606038 (Sept. 30, 2005) and 8638002 (June 5, 1986); Rev. Rul. 83-149, 1983-2 C.B. 186 (Oct. 3, 1983), Situation 3.

[93] *See* Letter Ruling 9713009 (Dec. 12, 1996); TAM 9245003 (July 23, 1992), 9144003 (July 22, 1991) and 200146024 (July 27, 2001).

[94] *See* IRC § 4052(c).

[95] The exception, by its terms, applies only to the installation of such items, and not their removal. However, at least with respect to fifth wheels and sleeper cabs, the IRS has, in the past, treated the removal of this item as "mere combination" rather than as "further manufacturing." *See* Letter Ruling 9702018 (Oct. 9, 1996) and Letter Ruling 9731033 (May 6, 1997). This issue was of more significance prior to 1998, when the 75 percent threshold did not apply to modifications that changed the transportation function or restored a wrecked vehicle. Under the current 75 Percent Rule, the addition or removal of the items covered by the Mere Combination Rule likely would not constitute further manufacturing in any event because such modification generally would not exceed the 75 percent threshold. Under the current rules, the issue of whether the removal of certain items is covered by the Mere Combination Rule likely would be relevant only if such removal converted a nontaxable item into a taxable one (which would be unlikely to occur).

[96] *See* I.R.C. § 4052(c).

[97] For a discussion on the general taxability of parts and accessories, *see* Section II.

[98] When Congress made this increase, it also stated that this amount could be changed by the IRS regulations. However, the IRS never updated its regulations to recognize the increase by Congress or to adopt a different cost threshold. Accordingly, the IRS regulations may cause some confusion because they retain the $200 limit. We are aware of no ruling directly addressing this inconsistency. However, in Letter Ruling 200052011 (Sept. 26, 2000), the IRS referred to the $1,000 cost threshold, indicating that the IRS recognizes the higher

limit as the appropriate dollar amount in applying the Six-Month Rule.

99 *See* Revenue Ruling 91-27 (1991-1 C.B. 192 (Apr. 15, 1991). In that ruling, the IRS referred to a 1988 Conference Committee Report which was issued in connection with the Technical and Miscellaneous Revenue Act of 1988.

100 *See* Technical Advice Memorandum 9219004 (Jan. 28, 1992) ("Three categories of operations performed on a used vehicle that the Service considers to be the manufacture of a new vehicle are discussed in Rev. Rul. 91-27"). *See* also TAMs 9819001 (Oct. 29, 1998) and.9702018 (Oct. 9, 1996).

101 Examples of modifications that the IRS has previously identified as constituting further manufacturing include stretching 40-foot trailers to 45-foot trailers, converting a truck into a tractor, insulating body shells, and installing a tag or pusher axle and assembling a truck-tractor by combining a glider kit with salvaged parts from a used truck-tractor. See, respectively, Revenue Ruling 83-169, 1983-2 C.B. 13 (Nov. 14, 1983); Revenue Ruling 60-155, 1960-1 C.B. 410 (1960), Revenue Ruling 64-335, 1964-2 C.B. 413 (1964) and, Revenue Ruling 75-129 1975-1 C.B. 336 (1975) and Revenue Ruling 71-584, 1971-2 C.B. 358 (1971). However, under today's rules, these modifications would not constitute further manufacturing if the 75 Percent Rule applied and its threshold were not exceeded.

102 This narrower rule was not a statutory provision or a regulatory provision. Instead, it was derived from the 1988 Conference Committee Report referred to above and was adopted by the IRS in Revenue Ruling 91-27, 1991-1 C.B. 192 (Apr. 15, 1991).

103 *See* TAM 200146024 (July, 27, 2001).

104 For a discussion about what constitutes a nontaxable load, *see* Section II.

105 There are complex engineering issues presented with respect to the re-rating of the GVW of a truck chassis for state vehicle registration purposes or for National Highway Traffic Safety Administration certification purposes. In some instances, it would not be appropriate to increase the GVW of a chassis following the installation of a lift-axle. But, even if you do not re-rate the chassis, you still need to determine, for FET purposes, whether the addition of the lift-axle to a chassis with a GVW rating 33,000 pounds or below has increased that chassis' GVW to more than 33,000 pounds.

106 IRC § 4221(a) makes it clear that the exemptions under this section apply to sales covered by the section 4051 tax. However, the majority of the statutory and regulatory provisions assume that the tax exemption will apply to a manufacturer's level tax, rather than a retailer's level tax such as the section 4051 tax. Because section 4221 clearly applies to the section 4051 tax, references to "manufacturer," fairly read, should include "retailers." In addition, the regulations issued under each specific type of section 4221 tax-free sale (i.e., sales to state and local governments, etc.) omit any reference to FET. Nevertheless, the IRS does apply section 4221 tax-free sales to FET.

107 Treas. Reg. § 48.4221-4(d)(1) and (2), which relates to tax-free sales for vessel or aircraft supplies, indicates that any exemption certificate may be used if *both* the seller and purchaser are not registered; however, this provision appears to conflict with IRC § 4222(a) and (b).

108 Effective Aug. 5, 1997, Congress amended IRC § 4222(b)(2) to give the IRS the authority (but not the obligation) to relieve a purchaser from the requirement to register and obtain a tax-free registration number in order to qualify for a section 4221 exemption. However, the IRS has not yet exercised this discretion, so, other than as noted above, a purchaser still must satisfy the registration requirement.

109 *See* Treas. Reg. § 48.4221(c).

110 For exports and further manufacturing, tax-free treatment will apply if, prior to any use, the item is resold by the purchaser, and the second purchaser exports the item or uses it for further manufacturing.

111 *See* Treas. Reg. § 48.4221-1(b)(4).

112 *See* Treas. Reg. § 48.4221-1(b)(3). So long as this is the case (and the 4221 tax-free sale is not for export or further manufacturing), the seller generally will not be liable for the tax if the purchaser subsequently uses the item for a purpose that is not tax-free. *See* IRC § 4221(c); Treas. Reg. § 48.4221-1(b). If the tax-free sale is for export, or for certain tax-free sales for further manufacturing, the seller will be liable for the tax if it does not subsequently receive the required information documenting that the item was in fact exported or used in further manufacturing.

113 For certain section 4221 exemptions, the regulations refer to IRC § 6001 regarding the length of time a taxpayer should retain exempt sale documentation. Although this statutory cite and the regulations thereunder are not entirely clear on this issue, all taxpayers are recommended to retain documentation in support of a section 4221 exemption for at least three years, because the IRS typically will have at least three years to assess a taxpayer for past-due taxes on filed returns.

114 Treas. Reg. § 48.4221-5(b).

115 *See* IRC § 4221(a)(6); IRC § 7701(a)(49). This exemption was effective Jan. 1, 2007, and the IRS has not issued Treasury Regulations to further govern this specific tax-free sale. In addition, although the statutory language is somewhat unclear regarding whether this tax-free sale applies to section 4051 tax, the explanation of the provision by the Joint Committee on Taxation, dated Aug. 3, 2006, states that it does apply.

116 *See* IRC § 4221(d)(6); Treas. Reg. § 48.4221-2(b)(2).

117 *See* IRC § 4221(b); Treas. Reg. § 48.4221-1(a)(2).

[118] *See* Treas. Reg. § 48.4221-2(c)(2)(ii).

[119] *See* Treas. Reg. § 48.4221-2(c)(1).

[120] IRC § 4221(d)(2).

[121] *See* IRC § 4221(b).

[122] *See* Treas. Reg. § 48.4221-3(d).

[123] *See* Treas. Reg. § 48.4221-3(c).

[124] *See* Treas. Reg. § 48.4221-3(d)(3).

[125] *See* Treas. Reg. § 48.4221-3(b).

[126] Interestingly, the reference to "or trade" does not appear in the general definition of "supplies for vessels and aircraft" set forth in Treas. Reg. § 48.4221-4(b).

[127] IRC § 4221(d)(3) (footnote added).

[128] *See* IRC § 4221(e)(1); Treas. Reg. § 48.4221-4(a)(2); Treas. Reg. § 48.4221-4(c).

[129] *See* Treas. Reg. § 48.4221-4(a)(1).

[130] *See* Treas. Reg. § 48.4221-4(d)(1) and (2)(i).

[131] *See* Treas. Reg. § 48.4221-4(d)(2)(ii).

[132] *See* Treas. Reg. § 48.4221-5(a); TAM 9416007 (Jan. 7, 1994) (finding that "exclusive use" requirement not met where, at the time of purchase, the state entity intended to resell the vehicle after approximately one year of use); TAM 9219005 (Jan. 30, 1992) (finding that "exclusive use" requirement not met where, prior to purchasing vehicle, the state entity had agreement to sell the vehicle one year later for original purchase price). Although these rulings and regulatory provisions focus on tax-free sales to state and local governments, the reasoning likely also would apply to sales to nonprofit educational organizations, which also have an exclusivity requirement.

[133] Sales of ambulances are separately exempt from section 4051 tax under IRC § 4053(4). *See* Section VII for a discussion of all the section 4053 tax exemptions.

[134] *See* TAM 9219005 (Jan. 30, 1992); Letter Ruling 9002013 (Oct. 11, 1989).

[135] Interestingly, sales to the United Nations and the American Red Cross, under certain circumstances, may be conducted on a tax-free basis, but not by virtue of a section 4221 exemption.

[136] *See* IRC § 6416(b)(2) and (3) and the regulations issued thereunder.

[137] There are some conflicting statements in at least two letter rulings regarding whether registration requirements under IRC § 4222 apply to section 4053 exemptions. *See* Letter Ruling 8449056 (Sept. 5, 1984) (registration not required) and Letter Ruling 8516055 (Jan. 18, 1985) (registration requirements apply). However, in Letter Ruling 8516055, the IRS appears to rely on a reference to section 4222 in Treasury Regulation 145.4051-1(f) for the principle that registration requirements apply. That reference was deleted in the year 2000. *See* 65 Fed Reg. 17149. Similarly, another reference to 4222 in 4052(d) was deleted in 1998. And, neither the language of IRC 4222 nor its regulations provide that the registration requirement applies to IRC § 4051 (other than with respect to a section 4221 tax-free sale, as detailed in Section VI).

[138] Rev. Rul. 2004-80, 2004-2 C.B. 164 (Aug. 9, 2004) (citing Malat v. Riddle, 383 U.S. 569, 572 (1966)). *See also* Worldwide Equipment, Inc. v. United States, 605 F.3d 319 (6th Cir. 2010).

[139] Rev. Rul. 2004-80, 2004-2 C.B. 164 (Aug. 9, 2004). *See also* Rev. Rul. 77-36.

[140] *See also* TAM 200732015 (Oct. 30, 2006), noting that Senate Report Number 324, 89th Cong., 1st Sess. (1965) provides that "in the case of self-propelled mobile homes, the exemption does not extend to the chassis upon which such a body is mounted (regardless of the manner in which the entire unit is constructed)."

[141] *See* Rev. Rul. 73-197, 1973 1 C.B. 423 (1973).

[142] The IRS in TAM 200732015 (Oct. 30, 2006) recently cited to Rev. Rul. 73 197, 1973-1 C.B. 423 (1973), noting that "to consider a chassis a motorhome chassis it must be constructed specifically for the purpose of transporting motorhome bodies as described in Rev. Rul. 73-197."

[143] For example, in Rev. Rul. 73-197, 1973-1 C.B. 423 (1973), the IRS noted the following factors to support its determination that the chassis at issue were constructed for the specific purpose of moving mobile home bodies: (1) flat rail frames of the chassis (as opposed to drop frames or kick-ups); (2) engine mounted between the frame rails (as opposed to projecting above the rails); (3) different placement of water pumps, oil dip sticks, oil intakes and radiator coolant intakes to permit servicing outside the vehicle; (4) large gas tank capacity; (5) three-speed automatic transmission and power steering as standard; (6) specially-designed power brake boosters; and (7) position of steering columns and driver sears to accommodate wider mobile home bodies. The IRS also noted that "although a small fraction of these chassis are used to transport certain special automotive bodies..., it would be economically unfeasible to adapt conventional truck-type bodies fro use with these chassis, because of the increased cost of these chassis over conventional truck chassis of similar gross vehicle weight." Compare TAM 200550037 (Aug. 29, 2005). (noting that the following factors highlighted by taxpayer were not sufficient to demonstrate the chassis at issue was other than a conventional truck chassis: (a) automatic shift transmission; (b) double lad differential; (c) horsepower and torque ranges; (d) extended warranties; (e) longer wheelbase; (f) longer frame; (g) different gas tanks; and (h) sound insulation of the cab.

[144] *See* TAM 200732015 (Oct. 30, 2006).

[145] *See* Letter Rulings 200221019 (Feb. 14, 2002) and 200237002 (Apr. 26, 2002).

[146] However, evidence of use may be relevant in demonstrating the intended design purpose of a body. *See* Peerless Corp. v. United States, 185 F.3d. 922, 925 (8th Cir. 1999).

[147] *See* TAM 200126002 (Dec. 13, 2000); TAM 200002006 (Sept. 23, 1999); TAM.199904038 (Oct. 8, 1998).

[148] *See* id.

[149] Please note that the determination of whether the feed, seed or fertilizer exemption applies is highly fact-specific and may be influenced by factors described in the letter ruling submission, but not clearly detailed in the actual letter ruling. Prior to relying on the three letter rulings noted above, you should consult your tax advisor.

[150] *See* Rev. Rul. 75-244, 1975-1 C.B. 338 (1975) (finding that a trailer body designed to transport cement-making ingredients in pre-measured amounts "and to place them in the truck mixer drum that performs the function of processing or preparing the concrete at the job site" was not exempt under 4053(5)).

[151] *See* Letter Ruling 8610060 (Dec. 11, 1985) (finding that a certain concrete pumping vehicle was a nontaxable mobile machinery vehicle).

[152] Prior to 2004, there was no tax-free exemption for mobile machinery vehicles under IRC § 4053. Instead, such a vehicle was considered a non-highway vehicle under IRS regulations and, therefore, was not subject to the section 4051 tax. (*See* Treas. Reg. § 48.4061(a)-1(d)(2)(i).) In 2002, the IRS published a notice in the Federal Register (67 Fed. Reg. 38913 (June 6, 2002)) proposing to eliminate non-taxable sales of mobile machinery vehicles. However, Congress, through the American Jobs Creation Act of 2004, exempted mobile machinery vehicles from section 4051 tax under IRC § 4053(8), so the IRS can no longer eliminate the mobile machinery exception.

[153] *See* Letter Ruling 200032034 (May 16, 2000) and TAM 200023015 (noting that the "vehicles' capacities to carry any additional loads, regardless of size, weight, or frequency, disqualify the vehicles from meeting the exemption requirements, because they do not satisfy the second criteria of the exemption").

[154] *See* Florida Power & Light Co. v. U.S., 56 Fed. Cl. 328 (2003), aff'd 375 F.3d 1119 (Fed Cir. 2004) (applying mobile machinery exception language in the context of the highway use tax); Schlumberger Technology Corp. v. U.S., 55 Fed Cl. 203 (2003) (applying mobile machinery exception language in the context of fuel excise tax). Although the time periods at issue in these cases predate the existence of the statutory exemption for mobile machinery vehicles, the language of the regulatory exception and the section 4053(8) exemption is substantially identical. Accordingly, the analysis and conclusions in these decisions continue to be relevant in determining the application of the mobile machinery exemption under section 4053(8).

[155] Like the mobile machinery exception, the off-highway vehicle exception originally was a regulatory provision rather than a statutory exemption. In 2002, the IRS published a notice in the Federal Register proposing to change the language of the off-highway vehicle exception (as well to eliminate the mobile machinery exception, as discussed above in this section). In the American Jobs Creation Act of 2004, Congress codified the off-highway exception, as proposed by the IRS in the 2002 Federal Register notice, at IRC § 7701(a)(48)(A). When the IRS proposed the regulatory changes in 2002, it did not indicate an intent to substantively change the requirements for the off-highway exception. However, it could be argued that some of the changes proposed by the IRS (and subsequently adopted by Congress) narrowed the scope of this tax-free category of vehicles. Accordingly, you should consult with your tax advisor prior to relying on IRS rulings and court cases that apply the prior regulatory language of the off-highway exception.

[156] *See* TAM 200333001 (Feb. 26, 2003); TAM 20043001 (Oct. 16, 2002).

[157] *See Worldwide Equipment, Inc. v. United States*, 605 F.3d 319 (6th Cir. 2010). ("Worldwide"). Although this court case was decided under an older version of the off-highway exception, the reasoning in this case also should apply to the revised language of the exception.

[158] Please note that the Worldwide case was a court decision and not an IRS ruling; the IRS is free to take a contrary position for audit purposes and in litigation before courts not bound by the Sixth Circuit.

[159] *See* Treas. Reg. § 145.4052-1(c)(3).

[160] *See* Treas. Reg. § 145.4052-1(a)(5).

[161] *See* TAM 9146004 (Aug. 7, 1991). In this case, the taxpayer installed a readily-removable axle on its semitrailer. The taxpayer used the truck with the axle only a few times a year. The IRS held that the taxpayer had further manufactured the trailer and the taxpayer's first use of the further manufactured trailer triggered FET. The IRS stated that "it does not matter that the taxpayer only uses the booster axle occasionally or that the axle may be removed between uses. The initial installation of the axle on the semitrailer is an act of manufacture and the first use of the modified semitrailer after installation is a taxable event."

[162] *See* Letter Ruling 8447092 (Aug. 23, 1984) (citing Revenue Ruling 60-290, 1960-2 C.B. 331 (1960) and Revenue Ruling 63-256, 1963-1 C.B. 534 (1963). It is unclear what level of use as a demonstrator is sufficient to trigger FET. The conservative approach would be to treat even a single use of a vehicle for demonstration purposes as triggering FET, but taxpayers are encouraged to consult their tax advisors on this issue.

163 *See* Treas. Reg. § 145.4052-1(c)(4).

164 *See* Treas. Reg. § 145.4052-1(c)(4).

165 *See* Treas. Reg. § 145.4052-1(c)(2).

166 *See* I.R.C. § 4052(e); Treas. Reg. § 145.4052-1(d)(6). If the lease includes a service contract or similar agreement for a term longer than the lease, consult your tax advisor to determine the correct length of the lease term for FET purposes. *See* section 4052(e) (incorporating IRC § 168(i)(3)(A)).

167 *See* Treas. Reg. § 145.4052-1(d)(6).

168 *See* Treas. Reg. § 145.4052-1(b)(1). It is interesting to note that the *statutory* definition of a taxable retail sale excludes long-term leases. *See* I.R.C. § 4052(a)(1). This apparent conflict is discussed in Section III.B.

169 *See* Letter Ruling 8527042 (April 8, 1985) (stating that a long-term lease that qualifies for a tax-free sale under section IRC § 4221(a)(4) – sale to state or local government – is not taxable).

170 *See* Treas. Reg. § 145.4052-1(b)(1) (a long-term lease will be taxable "*unless one of the exceptions contained in paragraph (a)(2) of this section applies*." The exceptions in paragraph (a)(2) are (i) a tax-free sale under section 4221; (ii) a sale for resale; and (iii) a prior taxable sale. Please note the subsequent example in Treas. Reg. § 145.4052-1(b)(1) appears to contradict the previous sentence. The problem appears to be that the regulation is written a little too broadly. Although a long-term lease following a taxable or tax free sale (two of the (a)(2) exceptions) should be nontaxable, a long-term lease following a tax-free sale for long-term leasing (the third exception in paragraph (a)(2)) *would* be taxable. (*See* Section VIII.C.5 for more information on sales for long-term leasing.). This result was confirmed informally by an IRS excise tax specialist.

171 *See* Treas. Reg. § 145.4052-1(b)(2).

172 Treas. Reg. §§ 48.4052-1 and 14.4052-1(a)(6).

173 *See* 53 Fed. Reg. 16867 (May 12, 1988).

174 Treas. Reg. § 145.4052-1(d)(1).

175 This general rule applies even if the retail sales price is paid, in whole or in part, with a trade-in vehicle. For example, if the retail price of a truck were $35,000, a truck dealer might accept as payment $25,000 in cash, plus a purchaser's used vehicle, which is valued at $10,000. The FET still would be calculated on the entire $35,000 – 12 percent of the retail price – and would not be limited to the portion of the sales price paid in cash. *See* Treas. Reg. § 145.4052-1(d)(9).

176 *See* Section VIII for a discussion of how use may trigger tax.

177 *See* Section VIII for a discussion of how a lease may trigger tax.

178 Treas. Reg. § 145.4052-1(d)(10)

179 *Id.* (emphasis added).

180 Treas. Reg. § 145.4052-1(c)(5)(ii)

181 *Id.*

182 *See* Public Law 100-17, section 505 and 506 of the Highway Revenue Act of 1987; H.R. Conf. Rep. No. 100-27, at 260-261 (1987); 53 Fed. Reg. 16867, 16868 (May 12, 1988) (noting that the presumed markup sections of the statute "were added to ensure that the tax base of most transactions considered to be taxable sales subject to section 4051 includes either an actual or presumptive retail markup"); *Oshkosh Truck Corp. v. U.S.*, 123 F.3d 1477, 1479-80 (Fed. Circ. 1997).

183 A remanufactured item refers to an item that (1) is taxable under section 4051 as a result of "[t]he refurbishing, renovation or repair of the [item]" and (2) was taxable under section 4051 (or its predecessor, section 4061) prior to the remanufacturing. *See* Treas. Reg. § 145.4052-1(d)(7)(ii). *See* Section V, which discusses the concept of further manufacturing.

184 *See* 53 Fed. Reg. 16867, 16868 (May 12, 1988) (stating that "[t]he imposition of a presumed markup percentage greater than zero percent on [trailers, semitrailers, and remanufactured chassis, bodies, and tractors] is not necessary to carry out the purpose of the section 4051 retail tax because retail sales of trailers and semitrailers are generally made by trailer manufacturers" and "remanufactured trucks and tractors generally are not sold through an established retail distribution network").

185 The term "manufacturer" includes a taxpayer that "further manufactures" an item, as that term is used in Section V. *See* TAM 199946001 (Dec. 28, 1998). Please note the rules for determining when further manufacturing occurs have been modified since that ruling. *See also* TAM 9315003 (Dec. 1, 1992).

186 The IRS defines a "related person" as "any person that is a member of the same controlled group (within the meaning of section 5061(e)(3)) as the manufacturer, producer, or importer." Treas. Reg. § 145.4052-1(d)(2)(ii). For an exception to the definition of "related person," see Treas. Reg. § 145.4052-1(d)(2)(ii)(B). For a ruling applying the presumed markup percentage to a "related person," *see* TAM 9306002 (Oct. 23, 1992).

187 *See* Treas. Reg. § 145.4052-1(d)(2)(i).

188 *See* TAM 200309002 (Sept. 27, 2002); TAM 9226005 (Feb. 27, 1992).

189 Treas. Reg. § 145.4052-1(d)(3)(ii) (emphasis added).

190 Treas. Reg. § 145.4052-1(d)(10); *see also* TAM 8621001 (Jan. 31, 1986), which addresses a taxable item sold in a non-arm's length sale, *but* at a fair market price. In such a case, no constructive sale price appears necessary.

191 *See* Rev. Rul. 86-122, 1986-2 C.B. 179 (Oct. 20, 1986).

192 Treas. Reg. § 145.4052-1(d)(10) (emphasis added).

193 Treas. Reg. § 145.4052-1(d)(10).

[194] *See* Treas. Reg. § 145.4052-1(c)(5)(ii).

[195] Rev. Rul. 86-130, 1986-2 C.B. 179 (Nov. 10, 1986), Situation 2.

[196] This Revenue Ruling also addressed the constructive price if the owner takes a used tractor to an unrelated repair shop for an overhaul. After the repair shop completes the overhaul, it returns the tractor to the owner for use in the owner's business. As in the example above, the owner does not make regular arm's length retail sales of the tractors. The IRS concluded that the constructive price under such circumstances was "the amount the repair shop bills the owner for the completed overhaul operation, plus the cost of any new components furnished by the owner to the repair shop." *Id.*, Situation 3.

[197] In both Situations 2 and 3 of this ruling, the IRS notes that the taxpayer may exclude from the constructive sale price the value of certain used components, as discussed in 5.e.

[198] However, shortly after the Revenue Ruling was issued, a Letter Ruling applied this constructive price formula to tank semitrailers. *See* Letter Ruling 8707042 (Nov. 19, 1986).

[199] *See* Treas. Reg. § 145.4052-1(d)(4).

[200] *See* Treas. Reg. § 145.4052-1(d)(5).

[201] This example is based on the IRS example provided at Treas. Reg. § 145.4052-1(e), Example 4.

[202] *See* Treas. Reg. §§ 145.4052-1(c)(5)(i) and 145.4052-1(e), Example 8. Although the regulations do not expressly provide a constructive price for this situation, Example 8 indicates that the applicable constructive price in this situation is computed under Treas. Reg. § 145.4052-1(c)(5)(i).

[203] *See* Treas. Reg. §145.4052-1(c)(5)(iii).

[204] This example is based on the IRS example provided at Treas. Reg. § 145.4052-1(e), Example 5. In that example, the initial sale between the manufacturer and dealer was tax-free because it was a sale for a long-term lease. Otherwise, that sale would have been taxable and the manufacturer would have owed the tax. However, in the IRS example, the dealer ultimately leased the item only for six months (*i.e.*, not a long-term lease). The example does not explain the effect of this change, but it appears the IRS is assuming the dealer's change of plans did not affect the tax-free nature of the transaction between the manufacturer and the dealer. Therefore, the dealer's short-term lease to the lessee was taxable, and the dealer was responsible for paying the tax.

[205] *See* IRC § 4052(b)(1)(B)(i) and (ii).

[206] *See* Treas. Reg. § 145.4052-1(d)(1); Treas. Reg. § 48.4216(a)-2(b)(1).

[207] *See* TAM 200315005 (Dec. 11, 2002); TAM 200543052 (Oct. 28, 2005); Letter Ruling 200349001 (Aug. 21, 2003); Rev. Rul. 86-68. 1986-1 C.B. 318 (May 12, 1986); Treas. Reg. § 145.4052-1(d)(1).

[208] Based on the general principles discussed above – that transportation/delivery charges may be deducted only from the taxpayer's place of business to the purchaser, and that deductible transportation/delivery charges must be incurred pursuant to a bona fide sale – any delivery expenses between dealers likely would not be deductible from the taxable price.

[209] The deduction for installation charges similarly should apply to a chassis on which there is installed a customer-owned body. However, the authors are not aware of any rulings addressing this issue.

[210] Letter Ruling 200349001 (Aug. 21, 2003).

[211] *Id.*

[212] *Id.*; Treas. Reg. § 145.4052-1(d)(1) (referring to installation charges "actually incurred in connection with the delivery of an article to a purchaser pursuant to a bona fide sale"); Treas. Reg. § 48.4216(a)-2(b)(1).

[213] *See* 145.4052-1(d)(1) (noting that "installation charges to which section 4051(b) applies" are not deductible).

[214] Letter Ruling 200349001 (Aug. 21, 2003) (*citing* Rev. Rul. 76-552, 1976-2 C.B. 336 (1976)). Interestingly, Rev. Rul. 76-552, 1976-2 C.B. 336 (1976) does not appear to stand for the principle that installation charges may not be deducted from a sale of a body and chassis sold as a unit. Nevertheless, the authors believe that is the position of the IRS.

[215] Letter Ruling 200349001 (Aug. 21, 2003) (*citing* Rev. Rul. 57-253).

[216] *See* Letter Ruling 200349001 (Aug. 21, 2003).

[217] *See* Non Docketed Service Advice Review, dated Feb. 28, 1991; Field Service Advisory, dated Sept. 14, 1992. These rulings are for informal advice purposes only.

[218] *See* Non Docketed Service Advice Review, dated Feb. 28, 1991.

[219] *Id.*

[220] *See* TAM 9245003 (July 23, 1992).

[221] *Id.*; Letter Ruling 9713009 (Dec. 12, 1996) (noting that "the value of those [used] parts (not the labor incurred)" is deductible).

[222] *See* Treas. Reg. § 48.4061(a)-1(a)(3)(ii).

[223] Initially, the IRS permitted taxpayers to *deduct* the value of the tires from the taxable sale price because the tires already had been taxed separately. *See* H.R. Conf. Rep. No. 105-220, at *559, July 30, 1997. Effective Jan. 1, 1998, the deduction was replaced with the tire tax credit because of the difficulty in determining the value of the tires for purposes of the deduction. *See id*, at *560.

[224] *See* TAM 200215004 (Dec. 20, 2001) (stating that "[t]he § 4051(d) credit does not reduce the § 4051 liability; rather, credits are used to reduce the balance due" and that the tire tax credit should *not* be factored into the amount identified

on Line 33 of Form 720); Letter Ruling 201022012 (Feb. 25, 2010). These appear to be the only two IRS rulings addressing the proper application of the tire tax credit.

[225] *See* 2010-1 IRB, Jan. 4, 2010, Rev. Proc. 2010-1, Section 2.01.

[226] *See id.*, Section 6.01.

[227] *Id.*, Section 11.01,11.06, 11.09.

[228] *Id.*, Section 11.02.

[229] *See* 2010-1 IRB, Jan. 4, 2010, Rev. Proc. 2010-2, Section 3.01 (emphasis added.)

[230] *Id.*, Section 5.01

[231] *See id.*, Section 5.

[232] *Id.*, Section 3.03.

[233] *Id.*, Section 12

[234] *Id.*, Section 13.04

[235] *See Hollow v. United States*, 1998 WL 760908 (W.D. Tenn. 1998), 81 A.F.T.R.2d 98-1171 ("*Hollow*").

[236] *See* 2010-1 IRB, Jan. 4, 2010, Rev. Proc. 2010-1, Section 2.05(2); *Hollow*.

[237] *See* 2010-1 IRB, Jan. 4, 2010, Rev. Proc. 2010-1, Section 6.

[238] *Id.*, Appendix A.

[239] *Id.*, Section 11.05 through 11.10.

[240] *Id.*, Section 5.03, 5.04.

[241] Rev. Proc. 89-14, 1989-1 C.B. 814 (1989), Section 7.01.

[242] *See id.*, Section 7.01(5), (6).

[243] *Compare id*, Section 7.04 (revenue rulings are "published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for that purpose) *to* IRC § 6110(k)(3) (letter rulings and technical advice memoranda "may not be used or cited as precedent").

[244] Similarly, the court in *Hollow* indicates that the IRS has no obligation to respond to a taxpayer's request for oral advice. In other words, the fact that an IRS agent refuses to answer your tax question would *not* relieve you of your duty to pay any required tax. In the *Hollow* case, the court noted that "[i]t is well settled that a taxpayer may not rely on an IRS agent's misstatement of the law," and concluded that if the federal government is not liable for providing a taxpayer with *incorrect* advice, then it also is not liable for failing to provide a taxpayer with any advice at all.

[245] *See* 75 Fed. Reg. 75897 (Dec. 7, 2010), as corrected by 76 Fed. Reg. 708 (Jan. 6, 2011) and 76 Fed. Reg. 709 (Jan. 6, 2011).

[246] *See* IRC § 7503 for the definition of "legal holiday." *Sell also* Publication 509 (noting that "[a] statewide legal holiday delays a due date only if the IRS office where you are required to file is located in that state").

[247] The due date for a deposit that falls on a state holiday will not change the date the deposit is due, unless the state holiday is also a legal holiday in the District of Columbia. See 75 Fed. Reg. 75897, 75898 (Dec. 7, 2010). *See also* Treas. Reg. § 40.6302(c)-1(c). (For the year 2011, the IRS has indicated that, at least under certain circumstances, it would not assess penalties for treating a state holiday as a legal holiday for purposes of calculating a deposit due date. *See* 75 Fed Reg. 75897, 75899 (Dec. 7, 2010).

[248] These calendars only take into account legal holidays in the District of Columbia; they do not consider state holidays.

ACKNOWLEDGMENTS

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