

## **IRS Issues Revenue Ruling Stating That A Mixture Of Butane And Gasoline Is NOT An Alternative Fuel Mixture That Qualifies For the Alternative Fuel Mixture Credit**

The IRS Office of Chief Counsel has issued a Revenue Ruling (attached) stating that a mixture of butane (or any other enumerated gasoline blendstock) and gasoline is a mixture of two taxable fuels and not a mixture of an alternative fuel and a taxable fuel. Therefore, a mixture of butane and gasoline is not an alternative fuel mixture eligible for the \$0.50 per gallon alternative fuel mixture credit under 26 U.S.C. 6426(e).

The Ruling comes as many industry participants have sought to claim the alternative fuel mixture credit for blending butane with gasoline, arguing that butane is a form of liquefied petroleum gas and therefore qualifies as an alternative fuel under 26 U.S.C. 6426(d)(2)(A). The Ruling disagreed with the industry.

Citing 26 C.F.R. 48.4081-1(c)(3)(i) which specifically lists butane as a gasoline blendstock – and which, the Ruling notes, was promulgated in 1996, well before the alternative fuel mixture credit was enacted – Chief Counsel states that butane is a taxable fuel and that a mixture of butane and gasoline is a mixture of two taxable fuels, not a mixture of an alternative fuel and a taxable fuel which is required to meet the eligibility criteria for the alternative fuel mixture credit (this is stated clearly in IRS Notice 2006-92). Chief Counsel also points to the language in 26 C.F.R. 48.4041-8 to conclude that butane is not an alternative fuel. Section 48.4041-8(f)(1)(i) provides that the term “special motor fuel” includes LPG and that the term LPG includes butane. Section 48.4041-8(f)(2) provides that the term “special motor fuel” does not include any product that is taxable under 26 U.S.C. 4081. Butane is specifically taxable under 26 U.S.C. 4081 as an enumerated gasoline blendstock. Consequently by the language in 26 C.F.R. 48-4041-8, butane is excluded from the definition of special motor fuel to the extent it includes certain liquefied petroleum gases.

As a Revenue Ruling is an official interpretation by the IRS of the Internal Revenue Code, this Ruling may be used as precedent and cited as authority. Therefore, taxpayers that have filed claims for the alternative fuel mixture credit for blending butane with gasoline should expect the IRS to follow this Ruling when reviewing claims and should expect that such claims will be denied. The next step would be for a taxpayer who disagrees with the Ruling to file an Appeal upon denial of its claims with the ultimate intention of challenging the Ruling in the courts.

A key basis on which the Ruling could be challenged in the Courts with regards to the timing. This isn't the first time the IRS has issued a Ruling or guidance that is favorable to its position after claims or other proceedings have been initiated. In 2015, as part of guidance on how to claim the retroactively reinstated biodiesel mixture credit, the IRS issued Notice 2015-56 advising taxpayers who would otherwise have claimed the credit on IRS Form 720 how the credit should be treated for income tax purposes. Upon being challenged in the Court of Claims as part of *Sunoco, Inc. v. The United States* (No. 15-587T), the Court refused to give deference to the Notice, stating, in part, that the Notice was merely a vehicle through which the IRS conveyed its current position and should not be entitled to deference but instead should be weighed equally against the taxpayer's arguments.

In the above case, the Notice was issued after Court proceedings had begun, after the IRS had issued conflicting guidance on the tax treatment of the mixture credit and without any authority for the position cited in the Notice. With respect to the current Ruling, at this time we are not aware of pending litigation and the IRS has cited statutory support for its position. That being said, taxpayers with pending claims may opt to challenge the timing and question of deference to the Ruling in any Court proceeding.

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Section 6426.—Credit for alcohol fuel, biodiesel, and alternative fuel mixtures

26 CFR 48.4081-1(c)(3): Gasoline blendstocks (Also Sections 4041, 4081, 4083.)

Rev. Rul. 2018-2

## **ISSUE**

Is a mixture of butane and gasoline an alternative fuel mixture that qualifies for the alternative fuel mixture credit under § 6426(e) of the Internal Revenue Code (Code)?

## **FACTS**

A claimant (Producer) mixes gasoline and butane and sells it for use as a fuel.

Producer claims the alternative fuel mixture credit under § 6426(e) for an open tax period ending on or before December 31, 2016, on the premise that the gasoline in the mixture is a taxable fuel and the butane in the mixture is a form of liquefied petroleum gas (LPG), an alternative fuel. Producer indicates in its claim that the basis for its position that butane is a form of LPG is the language in Chapter One of IRS Publication 510, “Excise Taxes (Including Fuel Tax Credits and Refunds),” which provides, in the “Other Fuels (Including Alternative Fuels)” section, that “[l]iquefied petroleum gas includes propane, butane, pentane, or mixtures of those products.”

## **LAW**

Section 4081(a)(1)(A) imposes a tax on certain removals, entries, and sales of taxable fuel.

Section 4083(a)(1) provides that the term “taxable fuel” means gasoline, diesel fuel, and kerosene.

Section 4083(a)(2)(B) provides that the term “gasoline” includes, to the extent prescribed in the regulations, (i) any gasoline blend stock, and (ii) any product commonly used as an additive in gasoline (other than alcohol), and that for purposes of

§ 4083(a)(2)(B)(i), the term “gasoline blend stock” means any petroleum product component of gasoline.

Section 48.4081-1(b) of the Manufacturers and Retailers Excise Tax Regulations provides that “gasoline” means finished gasoline and gasoline blendstocks.

Section 48.4081-1(b) also provides that “finished gasoline” means all products that are commonly or commercially known or sold as gasoline and are suitable for use as a motor fuel, other than products that have an American Society for Testing and Materials (ASTM) octane number of less than 75 as determined by the motor method.

Section 48.4081-1(c)(3)(i) provides that, except as provided in § 48.4081-1(c)(3)(ii), “gasoline blendstocks” means (A) alkylate; (B) butane; (C) butene; (D) catalytically cracked gasoline; (E) coker gasoline; (F) ethyl tertiary butyl ether (ETBE);

(G) hexane; (H) hydrocrackate; (I) isomerate; (J) methyl tertiary butyl ether (MTBE); (K) mixed xylene (not including any separated isomer of xylene); (L) natural gasoline; (M) pentane; (N) pentane mixture; (O) polymer gasoline; (P) raffinate; (Q) reformat; (R) straight-run gasoline; (S) straight-run naphtha; (T) tertiary amyl methyl ether (TAME);

(U) tertiary butyl alcohol (gasoline grade) (TBA); (V) thermally cracked gasoline; (W) toluene; and (X) transmix containing gasoline.

Section 48.4081-1(c)(3)(ii) provides that the term “gasoline blendstocks” does not include any product that cannot, without further processing, be used in the production of finished gasoline.

Section 6426(a)(1) and (e)(1) allows a \$0.50 credit against a claimant’s § 4081 tax liability for each gallon of alternative fuel used by the taxpayer to produce an alternative fuel mixture for sale or use in the taxpayer’s trade or business.

Section 6426(e)(2) provides that for purposes of § 6426, the term “alternative fuel mixture” means a mixture of alternative fuel and taxable fuel (as defined in § 4083(a)(1)(A), (B), or (C)) that is sold by the taxpayer producing such mixture to any person for use as a fuel, or used as a fuel by the taxpayer producing such mixture.

Section 6426(d)(2)(A) provides that the term “alternative fuel” includes LPG.

Section 2(b) of Notice 2006-92, 2006-2 C.B. 774, provides that an alternative fuel mixture requires a mixture of alternative fuel and at least 0.1 percent (by volume) of taxable fuel.

Section 6(a)(1) of Notice 2006-92 provides that a liquid alternative fuel is a liquid other than gas oil, fuel oil, or taxable fuel and is subject to the tax imposed by

§ 4041(a)(2) when it is sold for use or used as fuel in a motor vehicle or motorboat. Section 4041(a)

generally imposes a tax on the sale or use of certain liquids, including LPG. The tax does not apply to any liquid taxed under § 4081.

Section 48.4041-8(f)(1)(i) provides that the term “special motor fuel” includes “[a]ny [LPG] (such as propane, butane, pentane, or mixtures of the same).”

Section 48.4041-8(f)(2) further provides that the term “special motor fuel” does not include any product taxable under the provisions of § 4081.

## ANALYSIS

Every gallon of gasoline sold in the United States contains butane. Gasoline contains some butane naturally from the typical refining process. Butane is also commonly blended with gasoline to achieve correct vapor pressure properties depending on where and when the gasoline will be used.

Under the facts presented, Producer blended butane with gasoline and contends that the mixture qualifies for the alternative fuel mixture credit under § 6426(e) because the gasoline in the mixture is a taxable fuel and the butane in the mixture is LPG, an alternative fuel.

Section 4083(a)(1) provides that gasoline is a taxable fuel. Section 4083(a)(2)(B) provides that, to the extent prescribed in regulations, gasoline includes any gasoline blendstock, and that for purposes of § 4083(a)(2)(B)(i), a gasoline blendstock includes any petroleum product component of gasoline. Section 48.4081-1(c)(3)(i), which was issued in 1996, states that butane is a gasoline blendstock. *See* T.D. 8659, 1996-1

C.B. 264. Accordingly, butane is and has been a taxable fuel since before the enactment of § 6426(d) and (e) in 2005 as part of the Safe, Accountable, Flexible, Efficient Transportation Equity Act. *See* 119 Stat. 1144, P.L. 109-59 (2005). A mixture of butane, a taxable fuel, with gasoline, a taxable fuel, is a mixture of two taxable fuels, not a mixture of a taxable fuel and an alternative fuel, as required by § 6426(e)(2). Therefore, Producer may not claim the alternative fuel mixture credit under § 6426(e) for the mixture of butane and gasoline. *See* Notice 2006-92.

Producer nevertheless cites to IRS Publication 510 to support its contention that the gasoline in its mixture is a taxable fuel and the butane is LPG, which is an

alternative fuel. The term “liquefied petroleum gas” as used in § 6426(d)(2)(A) is not defined in the Code or the regulations. Section 48.4041-8(f)(1)(i) provides that the term “special motor fuel” includes any LPG, “such as propane, butane, pentane, or mixtures of the same.” However, the following subsection, § 48.4041-8(f)(2), provides that the term “special motor fuel” does not include any product taxable under the provisions of

§ 4081. Thus, the language in § 48.4041-8(f) that suggests that butane is a type of LPG also contains an express exception for products taxable under § 4081. IRS Publication 510, although not authoritative guidance, is consistent with this conclusion because it lists butane as a type of LPG in the section called “Other Fuels (Including Alternative Fuels) but also provides that the term “other fuels,” which include alternative fuels, “means any liquid *except* gas oil, fuel oil, or any product taxable under § 4081” (emphasis added).

Since Producer used butane in the production of finished gasoline, the butane is a gasoline blendstock. *See* § 48.4081-1(c)(3)(i) and (ii). Because gasoline blendstocks are taxable under § 4081, Producer’s butane is a taxable fuel and not an alternative fuel. *See* Notice 2006-92; *see also* § 4041(a)(2).

Producer’s mixture is not an alternative fuel mixture for purposes of § 6426(e) because Producer blended two taxable fuels, not a taxable fuel and an alternative fuel. This conclusion is supported by §§ 6426(e), 4081(a), 4083(a), 48.4081-1(b), and 48.4081-1(c)(3), as well as the language in § 48.4041-8(f). Moreover, to view butane as an alternative fuel within the meaning of section 6426(d)(2)(A) would mean that Congress intended to allow a mixture of gasoline (a taxable fuel) and a gasoline blendstock, i.e., butane (a taxable fuel) to qualify for the alternative fuel mixture credit.

**HOLDING**

A mixture of butane (or other gasoline blendstock as defined in § 48.4081- 1(c)(3)(i)) and gasoline is a mixture of two taxable fuels. Therefore, it is not an alternative fuel mixture and does not qualify for the alternative fuel mixture credit under § 6426(e) of the Code.

**DRAFTING INFORMATION**

The principal author of this revenue ruling is Amanda F. Dunlap of the Office of the Associate Chief Counsel (Passthroughs & Special Industries). For further information about this revenue ruling, please contact Branch 7 of Passthroughs & Special Industries at (202) 317-6855 (not a toll-free call).