

ISSUES

(1) Is biodiesel taxable fuel for purposes of the tax imposed by § 4081(a)(1) of the Internal Revenue Code?

(2) If biodiesel is not taxable fuel, is tax imposed by § 4081(b)(1) on the removal or sale of blended taxable fuel produced using biodiesel?

(3) If biodiesel is not taxable fuel, is tax imposed by § 4041(a)(1) on biodiesel sold for use or used as a fuel in a diesel-powered highway vehicle or a diesel-powered train?

FACTS

Biodiesel is a liquid composed of monoalkyl esters of long chain fatty acids derived from vegetable oils or animal fats that is covered by ASTM specification D 6751. Biodiesel does not contain any paraffins.

Biodiesel is suitable for use as a fuel in a diesel-powered highway vehicle or diesel-powered train and is sometimes delivered directly into the fuel supply tank of a vehicle or train for that use. However, the most common fuel-related use of biodiesel is in the production of a mixture containing 20 percent biodiesel and 80 percent diesel fuel.

LAW

Section 4081(a)(1) imposes tax on certain removals, entries, and sales of taxable fuel. Section 4083 defines taxable fuel as diesel fuel, gasoline, and kerosene. Section 48.4081-1(c)(2)(i) of the Manufacturers and Retailers Excise Tax Regulations defines diesel fuel as any liquid that, without further processing or blending, is suitable for use as a fuel in a diesel-powered highway vehicle or diesel-powered train. However, under § 48.4081-1(c)(2)(ii), diesel fuel does not include “excluded liquid.” The definition of excluded liquid in § 48.4081-1(b) includes any liquid that contains less than four percent normal paraffins.

Section 4081(b)(1) imposes tax on taxable fuel removed or sold by the blender thereof. Section 4082 provides exemptions from this tax. Under § 48.4081-1(c), blended taxable fuel generally means any taxable fuel that is produced outside the bulk transfer/terminal system by mixing tax-

able fuel with respect to which tax has been imposed under § 4081(a) and any other liquid on which tax has not been imposed under § 4081.

Section 4041(a)(1) imposes tax on any liquid other than gasoline sold for use or used as a fuel in a diesel-powered highway vehicle or diesel-powered train unless tax was imposed on the liquid by § 4081 and not credited or refunded. Other subsections of § 4041 provide additional exemptions from this tax.

ANALYSIS

Biodiesel, although suitable for use as a fuel in a diesel-powered highway vehicle or diesel-powered train, contains less than four percent normal paraffins and, therefore, is excluded liquid for purposes of the definition of diesel fuel provided in § 48.4081-1(c)(2). Accordingly, biodiesel is not taxable fuel for purposes of § 4081(a)(1). However, subject to the exemptions in § 4082, if biodiesel is used in the production of blended taxable fuel, tax is imposed by § 4081(b)(1) on the removal or sale of the blended taxable fuel. Further, subject to the exemptions in § 4041, if biodiesel is sold for use or used as a fuel in a diesel-powered highway vehicle or a diesel-powered train, tax is imposed by § 4041(a)(1).

HOLDINGS

(1) Biodiesel is not taxable fuel for purposes of the tax imposed by § 4081(a)(1).

(2) Subject to the exemptions in § 4082, tax is imposed by § 4081(b)(1) on the removal or sale of blended taxable fuel produced using biodiesel.

(3) Subject to the exemptions in § 4041, tax is imposed by § 4041(a)(1) on biodiesel sold for use or used as a fuel in a diesel-powered highway vehicle or a diesel-powered train.

DRAFTING INFORMATION

The principal author of this revenue ruling is Susan Athy of the Office of Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue ruling, contact Susan Athy at (202) 622-3130 (not a toll-free call).