State of California

Memorandum

Board of Equalization
Legal Department-MIC: 82

To: Mr. Robert Frank, Administrator
Fuel Industry Section (MIC: 33)

Date: August 15, 2003

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State Board of Equalization
Excise Taxes Division

From: M. Judith Nelson
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Subject: Taxability of Fractional Gallons of Fuel

This is in response to your memorandum to Assistant Chief Counsel Janice Thurston dated June 6, 2003, in which you requested guidance on the issue of the taxability of fractional gallons of fuel.

Background

You indicate that the distributor[1] and supplier tax returns used for the fuel programs instruct taxpayers to report in "whole gallons only", but do not offer any instructions on how to handle fractions of gallons, (i.e. rounded up or down or truncated.) You note that in the electronic filing program, taxpayers are instructed to round gallons reported on individual transactions to the nearest whole gallon.

In your memo you explain that the position of the audit staff is that fractional gallons appearing on bills of lading must be aggregated for purposes of calculating and paying fuel tax. However, at least one taxpayer that is currently being audited by the Board, truncates the fractional gallons and bills its customers for less gallonage than is actually delivered. Subsequently, the taxpayer apparently reports on its monthly fuel tax returns the sum of the invoiced gallons as being the amount of fuel distributed or removed, instead of the actual gallons distributed or removed. The taxpayer argues that the measure of tax should be the total gallons for which a customer is billed, which amount does not include the accumulated fractions of gallons truncated from individual transactions.

[1] I note that the Motor Vehicle Fuel License Tax Distributor Motor Vehicle Fuel Tax Return does not instruct the taxpayer to report whole gallons only. Rather, that return (BOE501-MD REV. 12 (1-98)) in fact refers to "Gallonage of Motor Vehicle Fuel Distributed" with no instruction limiting the reported information to whole gallons only.

Question

The question you pose has been narrowly drawn to inquire only whether the law requires a taxpayer to include "fractional gallons" in its fuel tax returns and to pay tax on the accumulated total of fractional gallons distributed or removed from the rack during the period. In my response, I will take a different approach. Rather than answer the narrow question on fractional gallons, I will instead focus on the broader issues of identification of the taxpayer, the point of imposition of tax and the measure of tax.

Discussion

You have inquired about the application of tax under three different laws—the Motor Vehicle Fuel License Tax Law (for periods prior to January 1, 2002) the Motor Vehicle Fuel Tax Law (for periods commencing January 1, 2002 and later) and the Diesel Fuel Tax Law (for periods commencing July 1, 1995 and later.)

Motor Vehicle Fuel License Tax Law

For periods prior to January 1, 2002, the Motor Vehicle Fuel License Tax was imposed for the privilege of *distributing* motor vehicle fuel on distributors *on each gallon of fuel distributed.*[2] The law provided that a distributor owes tax on the first distribution of fuel in this state. Revenue and Taxation Code §7352 provided in pertinent part as follows:

> "For purposes of the proper administration of this part and to prevent evasion of the license tax, ...it shall be presumed that all motor vehicle fuel refined, manufactured, produced, blended, or compounded in this State or imported into this State and no longer in the possession of the distributor has been distributed...." (emphasis added)

Motor Vehicle Fuel License Tax Regulation §1116[3] provided in pertinent part as follows:

> "A 'normal' loss is that which would reasonably be expected to occur through evaporation, shrinkage, or spillage in storing, loading, unloading, transporting, and handling motor vehicle fuel.... However, when such operating loss exceeds one-half of one percent of the total gallonage[4] stored at any facility...determined on the basis of the gallonage in storage at the commencement of the month, plus the gallonage of receipts into storage during the month, less the gallonage remaining in storage at the end of the month, such excess loss shall be deemed to be a distribution." (emphasis added.)

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[2] Rev. & Tax. §7351.

[3] Repealed 7/11/2002.

[4] "Gallonage" is defined to mean the amount in gallons. This definition would include the entire amount as measured in gallons, which amount might include fractions of gallons.

No statutory provision relieves the distributor from payment of tax if it fails to reimburse itself for the proper amount of tax from its customers. Motor Vehicle Fuel License Tax Regulation §1105(b)(2)[5] provided in pertinent part as follows:

> "Any distributor who fails to invoice or collect the tax on a taxable distribution is not relieved of its liability to report and pay the tax on that distribution."

Motor Vehicle Fuel Tax Law[6] and Diesel Fuel Tax Law[7].

Both of these laws specify that the tax is imposed upon *each gallon of fuel upon removal* from a rack, upon sale or entry into the state.[8] There is a presumption of removal included in both the Motor Vehicle Fuel Tax Law and the Diesel Fuel Tax Law. For motor vehicle fuel, the presumption language is at Revenue and Taxation Code §7373 and provides in pertinent part as follows:

> "For the purpose of the proper administration of this part and to prevent evasion of the tax, ...it shall be presumed that all motor vehicle fuel received at a terminal in this state, imported into this state, or refined and placed into storage for removal at a refinery in this state ...and no longer in the possession of the supplier has been removed or sold by the supplier...."

Similarly, for diesel fuel, Revenue and Taxation Code §60064 provides in pertinent part as follows:

> "For the purpose of the proper administration of this part and to prevent evasion of the tax, ...it shall be presumed that all diesel fuel received at a terminal in this state, imported into this state, or refined and placed into storage for removal at a refinery in this state...and no longer in the possession of the supplier has been removed or sold by the supplier...."

A monthly return must be filed with the Board accompanied by tax payments payable either to the Board or to the State Controller, depending on the type of tax. Revenue and Taxation Code §7651 requires that each supplier of motor vehicle fuel must file a return with the board "...showing the total number of gallons of motor vehicle fuel removed, sold, or entered within this state during each calendar month..." The same requirement applies to suppliers of diesel fuel.[9]

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[5] In effect until 7/11/2002, when the language cited was repealed and replaced with a different (b).

[6] Effective January 1, 2002, the Motor Vehicle Fuel License Tax Law was renamed the Motor Vehicle Fuel Tax Law and the point of imposition of tax was moved from the first distribution of the fuel up to the point of removal from the rack.

[7] The Diesel Fuel Tax Law became operative July 1, 1995.

[8] For Motor Vehicle Fuel Tax Law, Revenue and Taxation Code §§7360, 7362 and 7363 so provide, and for Diesel Fuel Tax Law, Revenue and Taxation Code §§ 60050, 60051 and 60052 so provide.

[9] See Revenue and Taxation Code §60201.

The applicable tax returns and their accompanying instructions, worksheets and schedules make it clear that the only place in the process where the taxpayer is to "report whole gallons only" is on the face of the return. All other entries on the accompanying worksheets and schedules are to reflect *total gallons*. I found nothing in the laws or in the instructions to the returns or schedules to indicate that the measure of tax should be based on the sum of truncated partial gallons billed to individual purchasers instead of based on the actual metered gallons of fuel removed from the rack, sold or entered.

Conclusion

Consistent with the foregoing discussion of the various laws applicable during the audit period, tax is imposed on the distributor or supplier based on the total gallons of fuel distributed, or removed, entered or sold. Tax is *not* imposed on the customer of the distributor or supplier. Furthermore, the distributor or supplier is not relieved of its obligation to pay the tax on the total gallons distributed or removed, entered or sold just because the taxpayer failed to collect tax reimbursement from its customer.

I trust this is responsive to your inquiry. If you have any questions, or wish to discuss the matter further, please call me at (916) 324-2641.

MJN:bb

cc: Mr. Ed King (MIC: 33)
Mr. Lou Feletto (MIC: 30)
Mr. Arlo Gilbert (MIC: 33)
Mr. Frank Love (MIC: 30)