

Air Transportation Excise Tax; Amount Paid for the Right to Award Miles

Notice 2002-63

This notice provides rules relating to the application of the air transportation tax imposed by § 4261 of the Internal Revenue Code to amounts paid for the right to provide mileage awards. The notice modifies and supersedes Notice 2001-6, 2001-1 C.B. 327. The Treasury Department and the Internal Revenue Service expect to issue the substance of this notice as a regulation at a later date. Until that regulation is published, persons responsible for collecting the tax and persons responsible for paying the tax may rely on the guidance provided in this notice.

Section 4261(a) imposes a 7.5-percent excise tax on amounts paid for taxable transportation (the percentage tax). Taxable transportation means air transportation beginning and ending in the United States and certain air transportation beginning or ending in southern Canada or northern Mexico if paid for within the United States. With the exception of these Canadian and Mexican flights, the percentage tax does not apply to air transportation between the United States and a foreign country; rather, this transportation is subject to the international facilities tax imposed by § 4261(c). Entirely foreign air transportation is not subject to tax.

Section 4261(e)(3), added to the Code by § 1031(c)(2) of the Taxpayer Relief Act of 1997, 1997-4 (Vol. 1) C.B. 2, 144, provides that the percentage tax applies to any amount paid (and the value of any other benefit provided) for the right to provide mileage awards for, or other reductions in the cost of, any transportation of persons by air. Regulations under § 4261(e)(3) will provide the following rules concerning mileage awards:

(1) Amounts paid for mileage awards that cannot be redeemed for taxable transportation beginning and ending in the United States are not subject to tax. For purposes of this rule, mileage awards issued by a foreign air carrier are considered to be usable only on that foreign air carrier and thus not redeemable for taxable transportation beginning and ending in the United

States. Therefore, amounts paid to a foreign air carrier for mileage awards are not subject to tax.

(2) Amounts paid by an air carrier to a domestic air carrier for mileage awards that can be redeemed for taxable transportation are not subject to tax to the extent those miles will be awarded in connection with the purchase of taxable transportation.

(3) Amounts paid by an air carrier to a domestic air carrier for mileage awards that can be redeemed for taxable transportation are subject to tax to the extent those miles will not be awarded in connection with the purchase of taxable transportation.

An air carrier that purchases mileage awards from a domestic air carrier may use any reasonable method to allocate amounts paid (and the value of any other benefits provided) between purchased mileage that will be awarded in connection with the purchase of taxable transportation and purchased mileage that will not be so awarded.

These rules apply to amounts paid after September 30, 1997. However, any amount paid after June 11, 1997, by one member of a controlled group for a mileage award that is furnished by another member of the controlled group after September 30, 1997, is treated as paid after September 30, 1997.

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