

## Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

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### Legend

Program =

Airline =

Agreement =

Bank =

Credit Card =

Payment 1 =

Payment 2 =

Payment 3 =

Payment 4 =

Payment 5 =

Payment 6 =

Payment 7 =

Payment 8 =

Payment 9 =

Payment 10 =

Payment 11 =

Payment 12 =

Payment 13 =

Benefit =

Dear :

This document replies to a letter ruling request submitted on your behalf by your authorized representative, relating to the application of § 4261(a) of the

Internal Revenue Code to certain payments related to, and a particular benefit under, Program. Airline requests rulings regarding whether the tax imposed by § 4261(a) (the § 4261(a) tax) applies to the payments and benefit described herein, and thus whether Airline has a duty to collect the § 4261(a) tax pursuant to § 4291.

## **Facts**

Airline owns and operates a domestic commercial airline. Airline entered into Agreement with Bank, pursuant to which Bank issues co-branded affinity credit cards.

Under the terms of Agreement, Airline agrees to license its trademarks to Bank, share certain mailing lists with Bank, and make certain marketing opportunities available for individual Credit Card accounts in exchange for payments and other consideration. Agreement provides for each Credit Card to be branded with various Airline trademarks.

In addition, under the terms of Agreement, Airline agrees to create, administer, operate and maintain Program to provide rewards as prescribed by Agreement. Agreement also provides that Credit Card customers are rewarded for various Credit Card spending behaviors through the awarding of points to the customer's Program account.

Airline requests rulings on the whether the payments and benefit described below are payments for taxable transportation for purposes of § 4261(a):

Payment 1<sup>1</sup> is a payment by Bank to Airline in an amount equal to the interchange fee associated with certain customer purchases. The "interchange fee" is a transactional fee received on each credit card sale paid by a merchant, in this case, Airline. Essentially, Payment 1 is a rebate of the interchange fee.

Payment 2 is a payment by Bank to Airline to reimburse Airline for certain Program management expenses.

Payment 3 is a payment by Bank to Airline to reimburse Airline for certain Program consulting expenses.

Payment 4 is a payment by Bank to Airline to reimburse Airline for certain Program-related technology enhancements and support expenses.

Payment 5 represents the minimum amount Bank is required to spend for purposes of developing and marketing Program. No portion of Payment 5 is paid directly to Airline.

Payment 6 is a payment by Bank to Airline of a sum certain contingent upon Airline meeting in a timely fashion certain milestones with regard to Program.

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<sup>1</sup> The term "Payment" or "payment" in this letter may refer to a single payment or a series of payments. For convenience, we generally use the terms "Payment" or "payment".

Payment 7 is a payment by Bank to Airline for each new affinity credit card account opened and that remains open for a minimum period specified in Agreement.

Payment 8 is a payment by Bank to Airline for each affinity credit card account that meets certain requirements specified in Agreement.

Payment 9 is a payment by Bank to Airline for each affinity credit card account that meets certain requirements specified in Agreement.

Payment 10 is a payment by Bank to Airline based on how much customers engage in certain affinity credit card spending behaviors specified in Agreement.

Payment 11 is a payment by Bank to Airline for each affinity credit card account opened that meets certain requirements specified in Agreement.

Payment 12 is a payment by Bank to Airline for each affinity credit card account that meets certain requirements specified in Agreement.

Payment 13 is a payment by Bank to Airline of an annual bonus based on the number of affinity credit card accounts opened during a particular year that meet certain requirements specified in Agreement.

Benefit allows customers to receive a free companion ticket when a customer purchases a ticket for the customer's own use and the transaction meets certain requirements specified in Agreement.

## **Law**

Section 4261(a) imposes a tax on the amount paid for taxable transportation (as defined in § 4262). "Taxable transportation" generally includes air transportation that begins and ends in the United States.

Section 4261(d) generally provides that the taxes imposed by § 4261 are paid by the person making the payment subject to the tax. Section 4291 generally provides that any person receiving any payment for taxable air transportation must collect the amount of the tax from the person making the payment. The collector is generally required by the regulations to make deposits, file returns, and pay over the tax to the government.

Section 4261(e)(3)(A) treats any amount paid (and the value of any other benefit provided) to an air carrier for the right to provide mileage awards for any transportation of persons by air as an amount paid for taxable transportation that is taxable under § 4261(a).

Rev. Rul. 73-508, 1973-2 C.B. 366, was issued after the Civil Aeronautics Board authorized the airlines to add a charge to their existing passenger tariffs to cover the expenses involved in certain security procedures. It holds that since the described security charge is required to be paid as a condition to receiving air transportation, such charge is part of the amount paid for taxable air transportation and is subject to the § 4261 tax.

Rev. Rul. 84-12, 1984-1 C.B. 211, holds that the § 4261(a) tax does not apply to free bonus tickets issued by an airline company to customers who have already satisfied all requirements to qualify for the bonus; however, the tax applies to any amount the customer subsequently pays because of not fully qualifying for the free bonus ticket. Rev. Rul. 84-12 reasons that if no amount is paid, the tax does not apply. If payment is made at a reduced rate, however, then the reduced amount is an amount paid for air transportation within the meaning of § 4261(a), because the amount subject to tax is the actual amount paid for taxable transportation.

### **Analysis and Conclusions**

The § 4261(a) tax is imposed on amounts paid for taxable transportation. The concept of an “amount paid” for taxable transportation is addressed in published guidance. Rev. Rul. 73-508 limits the § 4261(a) tax base to amounts required to be paid as a condition to receiving air transportation; in other words, the § 4261(a) tax is imposed only on amounts that must be paid to get on an airplane.

Under § 4261(e)(3), any amount paid to an air carrier for the right to provide mileage awards is treated as an amount subject to tax under § 4261(a). The General Explanation of Tax Legislation Enacted in 1997, JCS-23-97, 230-231, clarifies that “amounts received by airlines (whether paid in cash or in kind) pursuant to joint venture credit card or other air transportation marketing arrangements as compensation for the right to air transportation” are taxable under § 4261(e)(3).

In this case, Payment 1 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 1 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 1 is not subject to the § 4261(a) tax.

Payment 2 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 2 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 2 is not subject to the § 4261(a) tax.

Payment 3 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 3 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 3 is not subject to the § 4261(a) tax.

Payment 4 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 4 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 4 is not subject to the § 4261(a) tax.

Payment 5 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 5 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 5 is not subject to the § 4261(a) tax.

Payment 6 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 6 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 6 is not subject to the § 4261(a) tax.

Payment 7 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 7 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 7 is not subject to the § 4261(a) tax.

Payment 8 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 8 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 8 is not subject to the § 4261(a) tax.



Payment 9 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 9 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 9 is not subject to the § 4261(a) tax.

Payment 10 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 10 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 10 is not subject to the § 4261(a) tax.

Payment 11 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 11 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 11 is not subject to the § 4261(a) tax.

Payment 12 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 12 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 12 is not subject to the § 4261(a) tax.

Payment 13 is not an amount required to be paid as a condition to receiving air transportation, and is not an amount received by Airline as compensation for the right to air transportation. Therefore, Payment 13 is not an amount paid for taxable transportation within the meaning of § 4261(a), or for the right to provide mileage awards within the meaning of § 4261(e)(3). Airline is not required to collect the § 4261(a) tax from Bank because Payment 13 is not subject to the § 4261(a) tax.

With respect to Benefit, no amount is paid for the companion ticket. Therefore, like the free bonus ticket described in Rev. Rul. 84-12, Benefit is not subject to the § 4261(a) tax. As a result, Airline is not required to collect the § 4261(a) tax from customers on the value of a free companion ticket that the customer receives as part of Benefit.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In addition, no opinion is expressed or implied concerning any other payments that Bank may make to Airline under, or outside of, the terms of Agreement.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

*Stephanie Bland*

Stephanie Bland  
Chief, Branch 7  
(Passthroughs & Special Industries)

Enclosures

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