IRB 2012-42
October 15, 2012

ACTION ON DECISION

Subject: L & S Industrial & Marine, Inc. v. United States
633 F.Supp.2d 727 (D. Minn. 2009)

Issue:

Whether L & S Industrial & Marine, Inc.'s (Taxpayer) vessels engaged in "commercial waterway transportation" as defined in § 4042(d)(1) of the Internal Revenue Code (Code).

Discussion:

Taxpayer contracted with the U.S. Army Corps of Engineers to dredge portions of the Mississippi River. Taxpayer's tugboats moved dredging equipment to the dredging location where Taxpayer put dredged material on barges, and transported it to a disposal site, Taxpayer then transported the empty barges back to the dredging site for refilling. The IRS audited Taxpayer's federal excise tax returns and determined that Taxpayer had failed to pay the tax imposed by § 4042 of the Code.

Section 4042(a) imposes a tax on any liquid used during any calendar quarter by any person as a fuel in a vessel in commercial waterway transportation. Section 4042(d)(1) defines the term "commercial waterway transportation" as any use of a vessel on any inland or intracoastal waterway of the United States--(A) in the business of transporting property for compensation or hire, or (B) in transporting property in the business of the owner, lessee, or operator of the vessel (*other than fish or other aquatic animal life caught on the voyage*). (Italics added).

The district court determined that the parenthetical language in § 4042(d)(1)(B) regarding fish must also exempt a vessel's fishing equipment; otherwise, the parenthetical would have no effect because fish could not be caught without fishing equipment. 633 F.Supp.2d at 731. The court then reasoned that:

> While carrying dredging equipment for use in dredging and carrying fishing equipment for use in fishing are not perfect analogues, they both appear to belong to the same general class of activities; for example both dredging equipment and fishing equipment, at least when not carried as commercial cargo, are used to complete a task during a vessel's voyage. Because of these similarities, the Court concludes that the language of the statute, though not free of ambiguity, indicates that movement of dredging equipment aboard L&S's vessels as part of L&S's dredging activities does not qualify as "transporting property" for purposes of section 4042(d)(1).

Id. Based on this rationale, the court concluded that the § 4042 tax did not apply to Taxpayer's dredging activities.

The court's extension of the § 4042(d)(1)(B) exemption for fish and other aquatic animal life to dredging equipment conflicts with the longstanding judicial principle that courts should construe exemptions from tax narrowly. United States v. Wells Fargo Bank, 485 U.S. 351, 354, 108 S.Ct. 1179, 99 L.Ed.2d 368 (1988); Bingler v. Johnson, 394 U.S. 741, 752, 89 S.Ct. 1439, 22 L.Ed.2d 695 (1969); U.S. Trust Co. v. Helvering, 307 U.S. 57, 60, 59 S.Ct. 692, 83 L.Ed. 1104 (1939); United States v. Detroit Medical Center, 557 F.3d 412, 414 (6th Cir. 2009).

When construed properly, the court's analogy between dredging equipment and fishing equipment fails. Section 4042(d)(1)(B) specifically exempts only fish and other aquatic life; it does not specifically or impliedly exempt silt or equipment used to dredge silt. Therefore, any analogy between fishing and dredging equipment for purposes of § 4042 is misplaced.

The IRS will continue to assert that the § 4042(d)(1)(B) exemption only applies to fish or other aquatic animal life, and does not apply to dredging equipment, silt, or other dredged material.

Recommendation: Nonacquiescence.

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