

Reinstatement of the Hazardous Substance Superfund Financing Rate on Crude Oil and Petroleum Products: Should We Care?

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The Inflation Reduction Act of 2022 has reinstated the Hazardous Substance Superfund Financing Rate at 16.4 cents per barrel on crude oil and petroleum products. Should chemical distributors care? The general answer is yes. This article provides background on the reinstated rate and how chemical distributors will be affected by its reinstatement, effective January 1, 2023.

Background

The Hazardous Substance Response Revenue Act of 1980 (Title II of Public Law 95-510, Comprehensive Environmental Response, Compensation & Liability Act (“CERCLA”), enacted December 11, 1980), added Sections 4611, 4612, 4661, and 4662 to the Internal Revenue Code of 1986 (“Code” or “IRC”).

IRC § 4611 imposes an excise tax on crude oil received at a United States refinery and petroleum products entered into the United States for consumption, use, or warehousing. This excise tax is referred to below as the “petroleum products tax.” The petroleum products tax also is imposed if any domestic crude oil is used in or exported from the United States, and before such use or exportation, no tax was imposed on such crude oil. [1]

The petroleum products tax applies only once with respect to any petroleum product. It is not imposed on a petroleum product if the person who would be liable establishes that the tax has already been imposed with respect to that product. IRC § 4612(b).

The petroleum products tax rate is the total of two component rates: the Hazardous Substance Superfund Financing rate; and the Oil Spill Liability Trust Fund financing rate. As originally enacted, the Hazardous Substance Superfund Financing rate was 9.7 cents a barrel. It expired in 1995.

The Oil Spill Liability Trust Fund rate was 8 cents per barrel before 2017, but was raised to 9 cents per barrel after 2016. It is scheduled to expire after 2025.

Inflation Adjustment Act of 2022

The Inflation Adjustment Act of 2022 reinstated the Hazardous Substance Superfund Financing rate at 16.4 cents per barrel effective January 1, 2023. The rate will be adjusted for inflation. Thus, through 2022, crude oil and petroleum products are taxed at only the Oil Spill Liability Trust Fund Financing rate of 9 cents per barrel. For tax years 2023 through 2025, the tax is the sum of: (1) the 9 cents-per-barrel for the Oil Spill Liability Trust Fund Financing rate; and (2) the 16.4 cents-per-barrel (for 2023, increased for inflation thereafter) for the Hazardous Substance Superfund Financing rate. After 2025, the Oil Spill Liability Trust Fund Financing rate expires (unless Congress renews it), and the tax on crude oil and petroleum products applies at only the inflation-adjusted Hazardous Substance Superfund Financing rate.

How Are Chemical Distributors Affected?

Indirect effect. Chemical distributors will be affected indirectly to the extent that the 16.4 cent-per-barrel Hazardous Substance Superfund Financing rate increases the cost of crude oil and petroleum products that are used to manufacture or produce taxable chemicals.

Direct effect on taxable chemicals. As noted below, the Internal Revenue Service (“IRS”) has determined in informal guidance that toluene, xylene, and benzene are petroleum products. Under the petroleum products tax, a chemical distributor who enters these products into the United States is subject to the petroleum products tax. These products also are listed as taxable chemicals under the Superfund Tax (IRC § 4661), which would appear to subject them to the Superfund Tax when the products are sold or used after being imported.

Direct effect on taxable substances. While there appears to be no current overlap between taxable substances and petroleum products, the IRS has not issued any guidance on this and may have a different view. It also may classify substances added to the taxable substance list as petroleum products.

What happens if a substance is both a taxable chemical or taxable substance under the Superfund Tax and a petroleum product?

Taxable substances. The petroleum products tax takes precedence over the Superfund Tax on taxable substances. IRC § 4671(c) provides that “no tax shall be imposed by this section [IRC § 4671, which imposes the Superfund Tax on taxable substances] on the sale or use of any substance if tax is imposed on such sale or use under section 4611 [the petroleum products tax] or 4661 [the Superfund Tax on taxable chemicals].” As noted above, the current list of taxable substances does not appear to include any substances that meet the definition of a petroleum product (see discussion of what are petroleum products below). Having said that, it is anticipated that many petitions will be filed with the IRS to add substances to the taxable substance list. Some of the substances added to the taxable substance list may also meet the definition of petroleum product. If this occurs, IRC § 4671(c) would provide that the taxable substance that also is a petroleum product would be taxed under petroleum products tax upon entry into the United States and not under the Superfund Tax upon sale or use. [2]

Taxable chemicals. While the Code addresses the overlap between taxable substances and petroleum products, it does not address the overlap between taxable chemicals and petroleum products. A technical reading of the Code suggests that an imported taxable chemical that is also a petroleum product would be taxed under the

petroleum products tax when entered into the United States and then taxed again under Superfund Tax when sold or used.

It is puzzling why Congress would have addressed the overlap between taxable substances and petroleum products but not the overlap between taxable chemicals and petroleum products. It may be that Congress did not think an overlap between taxable chemicals and petroleum products would occur so no rule to address the overlap was needed.

Given this state of the law, what should a chemical distributor that imports toluene, xylene, or benzene do? Before July 1, 2022, the effective date of the Superfund Tax, an importer of toluene, xylene, or benzene was taxed under the petroleum products tax when the products were entered into the United States. Only the Oil Spill Liability Trust Fund financing rate of 9 cents per barrel applied. (The Hazardous Substance Superfund Financing rate expired in 1995 and is not re-imposed until January 1, 2023.) It would seem to be a reasonable position to continue treating these chemicals as taxed only under the petroleum products tax. Congress showed its intent not to tax taxable substances twice (tax them only under the petroleum products tax), and the absence of a rule addressing the overlap with taxable chemicals was likely an oversight. Even though it seems reasonable for toluene, xylene, and benzene to be taxed only once, the IRS may take the position that it does not have the authority to tax them only once given the language of the Code. Hopefully, the IRS will clarify the tax treatment of imported toluene, xylene, and benzene and any other taxable chemicals that also are petroleum products.

What Are Petroleum Products?

The term “petroleum products” is defined to include crude oil. IRC § 4612(a)(3). The legislative history to the original Superfund Tax provides that the term “petroleum product” includes “crude oil, crude oil condensate, natural and refined gasoline, refined and residual oil, and any other hydrocarbon product derived from crude oil or natural gasoline which enters the United States in liquid form.” [Emphasis supplied.] H Rept No. 96-1016(II) Part II (PL 96-510) p. 6.

The 1983 Proposed Regulations for the original Superfund Tax followed the legislative history in providing a definition of “petroleum products.” It defined the term to include “crude oil, crude oil condensate, natural and refined gasoline, refined and residual oil, and any other hydrocarbon product derived from crude oil or natural gasoline entered into the United States in liquid form. § 52.4612(a)(5). They also provided that the term “petroleum product” does not include methane, butane, ethane, or propane. The 1983 Proposed Regulations were withdrawn and cannot be relied upon, but they are instructive.

The IRS has issued informal advice clarifying what constitutes “petroleum products” under the petroleum products tax. Although this advice is informal, it is instructive on how the IRS treats certain products.

IRS *Technical Advice Memorandum 8640005*. Imported liquid asphalt is a petroleum product taxed under the petroleum products tax (IRC § 4611(a)(2)). Because asphalt is a petroleum by-product composed of hydrocarbons, imported liquid asphalt meets the definition of a petroleum product entered into the United States for consumption, use, or warehousing.

IRS Technical Advice Memorandum 9239001. Natural gas liquids are not subject to the tax on petroleum products. In the case of a stream of natural gas liquids (“NGLs”), tax is imposed on the volume of natural gasoline contained in the mixed stream of NGLs received at the fractionator. Tax is not imposed on the entire volume of the mixed stream of NGLs. In its report accompanying Pub. L. 96-510, the House Committee on Ways and Means stated that the term “crude oil” includes crude oil condensate and natural gasoline, but not other NGLs, and thus, does not include butane, ethane, or propane recovered from a natural gas stream. H.Rep. 1016, 96th Cong., 2d Sess. (1980), 1980-2 C.B. 593, 594.

IRS Technical Advice Memorandum 9410001. The petroleum products tax applies to toluene, xylene, and benzene derived from natural gas. A company is liable for the petroleum products tax (under IRC § 4611(a)(2)) on toluene, xylene, and benzene derived from natural gas. In this ruling, the IRS rejected the company’s contention that the petroleum products tax only applies to petroleum products that are derived from crude oil — not to petroleum products derived from natural gas.

IRS Private Letter Ruling 201120019. According to IRS, the legislative history of the petroleum products tax clearly shows Congress’s intent to exclude tar sands from the definitions of crude oil and petroleum products for purposes of the petroleum products tax. So tar sands imported into the United States were not taxed. However, crude oil and/or petroleum products commingled and transported in the same pipeline with the tar sands were subject to tax.

IRS PMTA-2014-012. The petroleum products tax does not apply to the ethanol portion of an ethanol mixture (mixtures of ethanol and gasoline) in situations in which the ethanol is produced from plant matter feed stocks. In general, ethanol mixtures are composed of two distinct substances that can be readily separated and returned to their component parts. (Over time, ethanol will separate from gasoline naturally through a process known as “phase separation” when it is exposed to moisture.) As a result, for purposes of the petroleum products tax only, the IRS does not view ethanol mixtures as a “unified” petroleum product that is subject to tax. Rather, the IRS views ethanol mixtures as two distinct substances, ethanol and gasoline, that should be analyzed separately for purposes of the tax.

Key Takeaways

- The reinstatement of the Hazardous Substance Superfund Financing rate at 16.4 cents per barrel beginning in 2023 likely will work its way through the supply chain to increase the cost of chemical products.
- It is unlikely that a chemical distributor will be subject to the petroleum products tax on crude oil. Chemical distributors typically do not operate refineries nor do they typically use or export crude oil before the tax has been paid.
- Based on the IRS informal guidance that toluene, xylene, and benzene are petroleum products, a chemical distributor that imports them will be subject to the petroleum products tax upon entering these products into the United States. A chemical distributor should not be subject to the Superfund Tax when it sells or uses these products because it does not appear that Congress intended to tax these products under the petroleum products tax and the Superfund Tax. Nevertheless, the IRS may take the position that these products are taxed twice.

- A substance is a petroleum product for purposes of the petroleum products tax only if it is **in liquid form** when it is entered into the United States.
 - The petroleum products tax is imposed at the time the product is entered into the United States. The Superfund Tax on an imported taxable substance is imposed when the taxable substance is sold or used.
 - Chemical distributors will need to watch for IRS guidance on whether taxable chemicals other than toluene, xylene, and benzene are classified as petroleum products and whether any taxable substances (current or future) are classified as petroleum products.
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1. 5. The United States Court of Appeals for the Fifth Circuit, however, has held that to the extent IRC § 4611 (b) imposes a tax on crude oil exports, it violates the Export Clause of the U.S. Constitution, and is unconstitutional. The court applied the Supreme Court’s analysis in U.S. Shoe (which held imposition of the harbor maintenance excise tax on exports to be unconstitutional), in concluding that the charge imposed by IRC § 4611 (b) on exports is an impermissible tax (and not a user fee) because it is based on the volume of oil transported, and is not paid in exchange for services provided to the exporters. Instead, IRC § 4611(b) imposes the cost on crude oil exporters of anti-pollution measures that generally benefit society at large. *Trafigura Trading, LLC v. U.S.*, (2022, CA5) AFTRCOVER 2022-515 .
 2. There is a technical glitch with the language in the Code. It says no tax is imposed under IRC § 4671 (Superfund Tax) if tax was imposed on the “sale or use” under IRC § 4611 (petroleum products tax). Technically, the tax is imposed under the petroleum product tax when the petroleum product is “entered” into the United States, not when it is sold or used. This glitch was likely a technical oversight.
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