Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
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Date:
September 26, 2019

In Re:

LEGEND:

Taxpayer	=
Corporation	=
State	=
Location	=
Date 1	=
Date 2	=
Date 3	=
a	=
b	=
c	=
d	=
e	=
f	=
A	=
B	=
C	=
D	=
E	=
g	=
h	=

Dear :

This letter responds to your request, dated Date 1 and supplemented Date 2, seeking permission to aggregate separate nonoperating mineral interests under § 614 of the Internal Revenue Code (Code) and § 1.614-5(d) of the Income Tax Regulations (Regulations). The request is submitted with respect to nonoperating mineral interests held in Location.

The facts and representations submitted are summarized as follows:

Taxpayer is a U.S. limited liability company treated as a partnership, organized pursuant to the laws of State. Taxpayer is organized primarily for the purpose of making investments in assets of all types. Taxpayer is a calendar year taxpayer, utilizes an accrual method of accounting, and prepares its financial statements using the U.S. Generally Accepted Accounting Principles.

The mineral interests that are the subject of the request are located in the following areas:

1. a
2. b
3. c
4. d
5. e
6. f

For U.S. federal income tax purposes, the properties listed in this letter consist of mineral royalty interests, and each property has both currently producing and currently nonproducing portions. Taxpayer acquired the mineral royalty interest in respect of each of these properties via a lease with Corporation beginning on Date 3.

Taxpayer paid A in exchange for Corporation granting Taxpayer an irrevocable royalty on certain lands based on the sale of h that has been derived from g extracted from the lease lands. Corporation acts as the developer, producer, and marketer of g and h. As of Date 3, Taxpayer and Corporation agreed that the United States Dollar equivalent of A was B (the parties assumed an exchange rate of C to D).

Each mineral royalty interest held by Taxpayer will be referred to hereinafter as a "royalty interest." These royalty interests afford the Taxpayer the right to mineral royalties. Taxpayer does not bear the costs of exploration, development, or production on the properties. Per the royalty agreement, the royalties Corporation agreed to pay to Taxpayer are unrelated to and unaffected by the cost of production. Each of the properties at which the royalty interests are located is operated by companies unrelated to Taxpayer. Furthermore, the interests are located in tracts of land that are either contiguous, touching at one point (checker-board pattern of ownership), or reasonably close in proximity to each other. Taxpayer submitted tract descriptions and a map or maps for each property that shows the total area circumscribed by each aggregation of

nonoperating mineral interest requested by the Taxpayer. Taxpayer considers these interests to be nonoperating mineral interests and has represented that these interests are nonoperating mineral interests.

Taxpayer notes that each of the properties is currently producing or expected to be producing in the future on at least some portion of the property; however, the royalty interests acquired by the Taxpayer do not provide any royalties on production. Taxpayer indicates it uses cost depletion in respect to the royalty payment received from the Corporation and has not claimed percentage depletion in respect to any properties.

The request seeks the aggregation of nonoperating mineral interests held at each of the properties, each to be treated as one property for U.S. federal income tax purposes, to enable Taxpayer to compute its cost depletion deduction in accordance with §§ 611 and 612 and § 1.611-2. Aggregation of the royalty interests at the properties is necessary to compute the cost depletion because reserve information is not available to Taxpayer on a separate property-by-property basis. The adjusted basis for the aggregated property that will be used to calculate the Taxpayer's cost depletion will be the cost allocated to the leases with current production. Taxpayer's adjusted basis in the royalty contract is equal to the allocated portion of consideration paid to Corporation, totaling E. Granting permission to aggregate the nonoperating mineral interest at each property will reduce the administrative burden in calculating depletion and allows Taxpayer to implement consistent treatment for finical accounting and U.S. federal income tax purposes.

Taxpayer represents that a principal purpose of the submitted request for the aggregation of royalty interests held at each property is not the avoidance of tax. Taxpayer makes this representation for two reasons. First, the interests subject to this ruling do not bear the costs of exploration, development, or production at the properties. Therefore, it is highly likely that the percentage depletion deduction for each interest would be subject to the taxable income limitation contained in § 1.613-5, as only general and administrative costs plus any severance and ad valorem taxes will be allocated to each interest for the purposes of computing the taxable income limitation. Aggregating these interests at each property is not expected to alter this result, so that no additional percentage depletion deductions are expected to be allowed if permission to aggregate is granted. Second, aggregating the interests at each property will not alter the total amount of cost depletion allowed at each property over its life, as the total cost depletion deductions allowed for a property cannot exceed the depletable tax basis allocated to the interest in that property. Accordingly, no cost depletion deductions in excess of those to which Taxpayer is entitled are expected at each property.

Law and Analysis

In the case of mines, wells, and other natural deposits, § 614 and § 1.614-1(a)(1) define the term “property” to mean each separate interest owned by the taxpayer in each mineral deposit in each separate tract or parcel of land.

Section 1.614-1(a)(2) defines the term “interest” as an economic interest in a mineral deposit. It includes working interests or operating interest, royalties, overriding royalties, net profits interests, and, to the extent not treated as loans under § 636, production payments.

Section 614(e)(2) and § 1.614-5(g) define the term “nonoperating mineral interest” to include only interests described in § 614(a) that are not operating mineral interests within the meaning of § 1.614-2.

Section 1.614-2(b) defines the term “operating mineral interest” to mean a separate mineral interest as described in § 614(e), in respect of which the costs of production are required to be taken into account by the taxpayer for purposes of computing the limitation of 50 percent of taxable income from the property in determining the deduction for percentage depletion under § 613, or such costs would be so required to be taken into account if the mine, well, or other natural deposit were in the production stage. The term does not include royalty interests or similar interests, such as production payments or net profits interests.

Section 1.614-5(d) provides that upon proper showing to the Commissioner, a taxpayer who owns two or more separate nonoperating mineral interest in a single tract or parcel of land, or in two or more adjacent tracts or parcels of land, shall be permitted, under § 614(e), to form an aggregation of all such interests in each separate kind of mineral deposit and treat such aggregation as one property. Permission shall be granted by the Commissioner only if the taxpayer establishes that the principal purpose in forming the aggregation is not the avoidance of tax. The fact that the aggregation of nonoperating mineral interest will result in a substantial reduction in tax is evidence that the avoidance of tax is a principal purpose of the taxpayer. An aggregation formed under the provisions of § 1.614-5(d) shall be considered as one property for all purposes of the Internal Revenue Code. In no event may nonoperating mineral interest in tracts or parcels of land which are not adjacent be aggregated and treated as one property. The Term “two or more adjacent tracts or parcels of land” means tracts or parcels of land that are in reasonably close proximity to each other depending on the facts and circumstances of each case. Adjacent tracts or parcels of land do not necessarily have any common boundaries, and may be separated by intervening mineral rights.

Section 1.614-5(e)(1) provides that an application for permission to aggregate separate nonoperating mineral interests under § 614(e) and § 1.614-5(d) must be made

in writing to the Commissioner and must be file within 90 days after the beginning of the first taxable year beginning after December 31, 1957, for which aggregation is desired or within 90 days after the acquisition of one of the nonoperating mineral interests that is to be included in the aggregation, whichever is later.

Section 1.614-5(e)(4) provides that an application for permission to aggregate separate nonoperating mineral interests under § 614(e) and § 1.614-5(d) shall include a complete statement of the facts upon which the taxpayer relies to show that the avoidance of tax is not a principal purpose of forming the aggregation. Such application shall also include a description of the nonoperating mineral interest within the tracts or tracts of land involved. A general description, accompanied by maps appropriately marked, which accurately circumscribes the scope of the aggregation of the mineral interest in a particular mineral deposit within the tract or tracts involved will be sufficient. If the Commissioner grants permission, a copy of the letter granting permission shall be attached to the taxpayer's return for the first taxable year for which such permission applies. If the taxpayer has already filed such return, a copy of the letter of permission shall be filed with the district director for the district in which such return was filed and shall be accompanied by an amended return or returns if necessary or, if appropriate, a claim for credit or refund.

Section 1.614-5(e)(5) provides that the election to aggregate separate nonoperating mineral interests under § 614 and § 1.614-5(d) is binding on the taxpayer for the first taxable year for which the request is made and for all subsequent taxable years unless consent to make a change is obtained from the Commissioner.

Therefore, to obtain permission, the taxpayer must:

1) Apply for permission within 90 days after the beginning of the first taxable year for which aggregation is desired, or within 90 days after the acquisition of one of the properties to be included in the aggregation (§ 1.614-5(e)(1));
2) Provide maps, descriptions of the nonoperating interest, and a complete statement of facts (§ 1.614-5(e)(4)); and
3) Establish that the principal purpose for forming the aggregation is not tax avoidance. A substantial reduction in taxes is evidence that the avoidance of tax is a principal purpose (§ 1.614-5(d) and § 1.614-5(e)).

Taxpayer represents that the interests owned at each of the properties are "nonoperating mineral interests" as the term is defined in § 1.614-5(g), and that the royalty interests are interests that do not bear the cost of exploration, development, or production. Taxpayer also represents that the interests at each property are owned in two or more tracts or parcels of land that are "adjacent" or "in reasonably close proximity to each other" as provided in § 1.614-5(d). Additionally, Taxpayer represents that the maps for each property included in the ruling request demonstrate that the nonoperating interests at each property are in reasonably close proximity to each other, as these

interests are either contiguous, touch at a corner, or are separated by intervening mineral rights but included in single operating mine.

Finally, Taxpayer represents that the principal purpose of forming the requested aggregation at each property is not tax avoidance. The purpose of forming the requested aggregation is to reduce administrative burden in calculating the depletion deduction and allow Taxpayer to implement consistent treatment for financial accounting and federal income tax purposes.

Based on the representation made and consideration of the descriptions and maps submitted, we conclude that the requirements of § 614(e) and § 1.614-5 had been met. Based solely on the facts and representations submitted, we grant consent for Taxpayer to aggregate the separate nonoperating mineral interests located at a, b, c, d, e, and f, such that each of the properties is treated as one property for U.S. federal income tax purposes.

Except as specifically set forth above, we neither express nor imply any opinion concerning the federal income tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we neither express nor imply any opinion concerning Taxpayer's calculation of depletion or whether Taxpayer's interests in the properties are economic interests. This ruling is conditioned on each royalty interest qualifying as an economic interest under § 611 before the aggregation. General descriptions of the nonoperating interests accompanied by maps are to be on file with the books and other records that are necessary for examination by the Service.

The rulings contained in this letter are based upon the information and representations submitted by Taxpayer and accompanied by a "penalties 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.

In accordance with the power of attorney, we are sending copies of this letter to Taxpayer's authorized representative. We are also sending a copy of this letter to the appropriate Industry Director, LB&I. A copy of this ruling must be attached to any federal income tax return which is relevant. Alternatively, taxpayers filing their returns

electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of this letter rulings.

Sincerely,

Patrick S. Kirwan
Branch Chief, Branch 6
Office of Associate Chief Counsel
(Passthroughs & Special Industries)