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Date:
August 18, 2021

In Re: Request to aggregate nonoperating mineral interests

LEGEND

Taxpayer =
Parent =
HoldCo =
Subsidiary 1 =
Subsidiary 2 =
Date 1 =
Date 2 =
State =
Location 1 =
Location 2 =
Area =
a =
b =
Auditor =

Dear :

This letter replies to a letter dated Date 1 in which Taxpayer requests permission to form aggregations of separate nonoperating mineral interests under § 614(e) of the Internal Revenue Code (Code) and § 1.614-5(d) of the Income Tax Regulations (Regulations). The request is submitted in respect of nonoperating mineral interests held in Location 1.

The facts and representations submitted are summarized as follows:

Taxpayer is a U.S. corporation incorporated pursuant to the laws of State. Taxpayer is a calendar year taxpayer and utilizes the accrual method of accounting. Taxpayer is a wholly-owned subsidiary of Holdco, which is also incorporated pursuant to the laws of State, a calendar year taxpayer, and utilizes the accrual method of accounting. Taxpayer owns 100% of the membership interests of Subsidiary 1, which is treated as a disregarded entity for U.S. Federal tax purposes. Taxpayer wholly owns Subsidiary 2, a corporation incorporated pursuant to the laws of State. Together, Holdco, Taxpayer, Subsidiary 1, and Subsidiary 2 are an affiliated group of corporations that file a consolidated U.S. federal income tax return with Holdco serving as the common parent. Holdco is owned by Parent, a company organized in Location 2.

Parent, along with Holdco, Taxpayer, Subsidiary 1, and Subsidiary 2, is an international mineral resource and investment company that acquires mineral, oil, and natural gas royalties and other nonoperating mineral interests worldwide. Parent, Holdco, Taxpayer, Subsidiary 1, and Subsidiary 2 do not explore, develop, or operate any of the properties in which they hold interests, but instead rely on non-operating income streams, such as royalties on mineral interests, as the basis of their income. Parent prepares its financial statements based on the International Financial Reporting Standards as issued by the International Accounting Standards Board.

The mineral interests that are the subject of the request are located in Area.

For U.S. federal income tax purposes, all of the interests are treated as owned directly by Taxpayer. Taxpayer acquired the mineral royalty interests in respect of each of these properties on Date 2. Taxpayer represents that the interests consist of mineral royalty interests, nonoperating oil and gas production overriding royalty interests, non-participating royalty interests, and royalty interests. Each production royalty interest acquired by Taxpayer will be referred to as a “royalty interest.” Included in the acquisition, Taxpayer paid a in consideration for b properties.

Taxpayer represents that it does not have the ability or desire to operate any of the properties to produce oil and gas therefrom. Taxpayer further represents that the royalty interests afford Taxpayer the right to royalties, including royalties from acquired leases. Taxpayer does not bear the cost of exploration, development, nor production in respect of any of the properties. Taxpayer represents that each of the properties subject to a lease are operated by other unrelated persons, and that the leases are for 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 represents that, because Taxpayer does not incur any costs of production, all of the royalty interests are nonoperating mineral interests.

Taxpayer represents that aggregation of the nonoperating mineral interests would enable Taxpayer to compute, without undue burden, its cost depletion deduction in

accordance with §§ 611 and 612 of the Code and § 1.611-2 of the Regulations. Aggregation of the nonoperating mineral interests at the properties are necessary to compute cost depletion because reserve information is not available to Taxpayer on a separate property-by-property basis. To determine the appropriate reserves for each property, Taxpayer would generally be required to reply on publicly available information, and where possible, engage third-party experts. Taxpayer and Parent represent that they will rely on the same reserve information to compute book cost depletion in the aggregate for the property in the preparation of consolidated financial statement audited by Auditor and for regulatory filings. Taxpayer represents that granting permission to aggregate nonoperating mineral interests into a single property will reduce administrative burden in calculating depletion and allows Taxpayer to implement consistent treatment for financial accounting and U.S. federal income tax purposes.

Taxpayer represents that a principal purpose of its submitting this Request for the aggregation of nonoperating mineral interests held at Area is not the avoidance of tax. Taxpayer makes this representation supported by two bases. First, Taxpayer does not bear the costs of exploration, development, or production of oil and gas produced with respect to these nonoperating mineral interests. 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 of the Regulations, as only general and administrative costs plus any severance and ad valorem taxes will be allocated to each interest for the purpose of computing the taxable income limitation. Aggregating the nonoperating mineral interests in Area into a single property is not expected to alter this result, as no additional percentage depletion deductions would be expected to be allowed if permission to aggregate is granted. Second, aggregating the nonoperating mineral interests in the defined areas into a single property will not alter the total amount of cost depletion deductions allowed over the life of the properties, as the total cost depletion deductions allowed for the properties cannot exceed the depletable tax basis allocated to the interests in the properties. Accordingly, no cost depletion deductions in excess of those to which Taxpayer would otherwise be entitled would be expected if such nonoperating mineral interests are aggregated into a single property.

Taxpayer represents that an abandonment loss on any aggregated nonoperating mineral interests will not be taken until all of the mineral rights in the entire aggregated or combined property are proven to be worthless, or until the entire aggregated or combined property is disposed of or abandoned pursuant to § 1.614-6(d) of the Regulations.

Ruling Requested

The ruling request seeks the aggregation of the nonoperating mineral interests held at the Area, such that the separate nonoperating mineral interests is treated as one property for U.S. federal income tax purposes, pursuant to Internal Revenue Code section 614(e) and Treasury Regulation section 1.614-5(d).

Taxpayer represents the principal purpose of submitting this Request for the aggregation of nonoperating mineral interests in Area into a single property is not for the avoidance of U.S. Federal income tax.

Law and Analysis

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

Under § 614(e) and § 1.614-5(d), a taxpayer that owns two or more separate nonoperating mineral interests in a single tract or parcel of land or in two or more adjacent tracts or parcels of land, may request permission to aggregate all the interests and treat them as one property.

Section 1.614-5(e) provides that an application for permission to aggregate separate nonoperating interests under § 614(e) and § 1.614-5(d) must be made in writing to the Commissioner and must be filed 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 1.614-1(a)(2) of the Regulations defines the term "interest" as an economic interest in a mineral deposit. It includes working interests or operating interests, royalties, overriding royalties, net profits interests, and, to the extent not treated as loans under § 636 of the Code, production payments.

Section 614(e) of the Code provides that if a taxpayer owns two or more separate nonoperating mineral interests in a single tract or parcel of land or in two or more adjacent tracts or parcels of land, the Secretary shall, on a showing by the taxpayer that a principal purpose of forming the aggregation is not the avoidance of tax, permit the taxpayer to treat all such interests as one property for all subsequent taxable years unless the Secretary consents to a different treatment.

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

Section 1.614-2(b) of the Regulations defines the term "operating mineral interest" to mean a separate mineral interest as described in § 614 of the Code, in respect of with 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) of the Regulations 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) of the Code, 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 a principal purpose in forming the aggregation is not the avoidance of tax. The fact that the aggregation of nonoperating mineral interests 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 § 1.614-5(d) shall be considered as one property for all purposes of the Internal Revenue Code. In no event may nonoperating interests in tracts or parcels of land that 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) of the Regulations provides that an application for permission to aggregate separate nonoperating interests under § 614(e) of the Code and § 1.614-5(d) must be made in writing to the Commissioner and must be filed 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) of the Regulations provides that the application for permission to aggregate nonoperating mineral interests under § 614(e) of the Code 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 interests within the tract or tracts of land involved. A general description, accompanied by maps appropriately marked, which accurately circumscribes the scope of the mineral interests in a particular kind of mineral deposit within the tract or tracts of land 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) of the Regulations provides that the election to aggregate separate nonoperating mineral interests under § 614(e) of the Code and § 1.614-5(d) is binding upon 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 interests, and a complete statement of facts (§ 1.614-5(e)(4)); and
3) Establish that a principal purpose for forming the aggregation is not tax avoidance. A substantial reduction in taxes is evidence that the avoidance of taxes 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 that term is defined in § 1.614-5(g) of the Regulations, and that the royalty interests are interests that do not bear the costs of exploration, development, or production. Taxpayer also represents that the interests at each property at issue are in tracts or parcels of land that are "adjacent" or "in reasonably close proximity to each other" as provided in § 1.614-5(d) of the Regulations. Additionally, Taxpayer represents that the maps for the property included in the ruling request demonstrate that the nonoperating interests 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 a single operating mine.

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

Ruling

Taxpayer requests permission under § 614(e) and § 1.614-5(d) to aggregate the separate nonoperating mineral interests owned by Taxpayer in the Area, such that the separate nonoperating mineral interests are treated as one property.

Taxpayer has represented that it acquired multiple royalty interests in the Area. Taxpayer also has submitted descriptions and maps indicating that each of the royalty interests is adjacent to the other royalty interests within the meaning of § 1.614-5(d). Moreover, Taxpayer has represented that the avoidance of tax is not a principal purpose of forming the aggregation within the Area.

Based on the representations made and consideration of the descriptions and maps submitted, we conclude that the requirements of § 614(e) and § 1.614-5 of the Regulations have been met. Based solely on the facts and representations submitted, we grant consent for Taxpayer to aggregate the separate nonoperating mineral interests located in the Area, such that those properties are aggregated and 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. This ruling is conditioned on each royalty interest qualifying as an economic interest under § 611 of the Code 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 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 representatives. 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 to which it 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 the letter ruling.

Sincerely,

Patrick Kirwan

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

cc: