Internal Revenue Service

Number: **202044005**
Release Date: 10/30/2020

Index Number: 614.04-00

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:
CC:PSI:B06
PLR-125234-19

Date:
July 31, 2020

Re: Request to aggregate nonoperating mineral interests

LEGEND:

Taxpayer	=
Corporation	=
Holding Company	=
Company A	=
Company B	=
State A	=
State B	=
State C	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=
x	=
A	=
B	=
Director	=

Dear :

This letter responds to your request, dated Date 1, as supplemented by letter dated Date 6, seeking permission to aggregate 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 with respect to nonoperating mineral interests held in x mineral properties each separately located in State A and State B.

Taxpayer is incorporated pursuant to the laws of State C and is a wholly-owned subsidiary of Holding Company, which is also incorporated pursuant to the laws of State C. Taxpayer wholly owns Company A, a limited liability company that is treated as a disregarded entity for U.S. federal income tax purposes. Company B is a wholly-owned subsidiary of Taxpayer that was incorporated pursuant to the laws of State C. Together, Holding Company, Taxpayer (including the activities of Company A), and Company B are an affiliated group of corporations that file a consolidated U.S. federal income tax return with Holding Company serving as the common parent. Holding Company is wholly-owned by Corporation.

Corporation, along with its subsidiaries identified in this letter and its non-U.S. subsidiaries, is an international mineral resource and investment company that acquires mineral, oil, and natural gas royalties and other nonoperating mineral interests worldwide. Corporation does not explore, develop, or operate on any of the properties in which it holds interests, relying instead on passive income streams, predominantly royalties on mineral interests, as the basis of its income. Corporation prepares its financial statements based on International Financial Reporting Standards as issued by the International Accounting Standards Board.

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

1. A
2. B

The various mineral interests are distinguished and identified according to the area in which they are located; for illustration, the mineral interests located within area A are referred to as the A interests.

For U.S. federal income tax purposes, all the interests described above are treated as owned by Taxpayer.

Taxpayer acquired the A interests on Date 2. The A interests consist of overriding royalty interest in oil and gas producing wells and overriding royalty interest in acquired leases and the oil and gas from such leases (“ORRI”). Taxpayer does not have the ability to operate any of the properties in order to produce oil and gas

therefrom. The ORRI provides the Taxpayer the right to royalties from the acquired leases.

Taxpayer acquired the B interests on Date 3. The nonoperating B interests consist of gold and other mineral royalty interests including net smelter royalty interests.

Each production royalty interest held by Taxpayer will be referred to hereinafter as a "royalty interest." These royalty interests afford Taxpayer the right to mineral royalties and do not bear the costs of exploration, development, or production on the properties. Each of the properties at which the royalty interests are located are operated by unrelated parties. Furthermore, the interests at each distinct property 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 interests requested by Taxpayer. Taxpayer considers these interests to be nonoperating mineral interests and has represented that these interests are nonoperating mineral interests.

The request seeks the aggregation of the separate nonoperating mineral interests held at each of the x distinct areas such that the separate interests within each of the x distinct areas are treated as one property for U.S. federal income tax purposes, in order to enable Taxpayer to compute their cost depletion deduction in accordance with §§ 611 and 612 and § 1.611-2. Taxpayer represents the aggregation of the nonoperating interests at the x distinct areas is necessary to compute cost depletion because reserve information is not available to Taxpayer on a separate property-by-property basis. In order to determine the appropriate reserves for each property, Taxpayer will generally be required to rely on publicly available information and life of reserve reports provided by the properties' operators. Taxpayer, and its parent, Corporation, will rely on the same reserve information to compute book cost depletion in the aggregate for each of the x distinct aggregations in the preparation of Corporation's financial statements and regulatory filings. Granting permission to aggregate the nonoperating mineral interests at each of the areas into separately aggregated properties will reduce the administrative burden in calculating depletion and allow Taxpayer to implement consistent treatment for financial accounting and U.S. federal income tax purposes.

Taxpayer represents that a principal purpose of submitting the request for the aggregation of royalty interests held at each property is not the avoidance of tax. Taxpayer supports this representation with two justifications. First, the interests subject to this ruling request do not bear the costs of exploration, development, or production of the properties. Therefore, it is highly unlikely 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 purpose of computing the taxable income limitation. Aggregating the nonoperating mineral interests in the defined areas into x

single properties is not expected to alter this result, as 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 deductions 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 interests at that property. Accordingly, no cost depletion deductions in excess of those to which Taxpayer is entitled are expected at each of the x distinct aggregations.

Law and Analysis

In the case of mines, wells, and other natural deposits, § 614(a) 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 interests, royalties, overriding royalties, net profits interests, and, to the extent not treated as loans under § 636, production payments.

Section 614(e)(1) 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) and § 1.614-5(g) 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.

Section 1.614-2(b) defines the term "operating mineral interest" to mean a separate mineral interest as described in § 614, 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 interests 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 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) 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 1.614-5(e)(4) provides that the application for permission to aggregate 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 interests within the tract or tracts of land involved. A general description, accompanied by maps appropriately marked, which accurately circumscribes the scope of the aggregation and shows that the taxpayer is aggregating all the nonoperating 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 such 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(e) and § 1.614-5(d) is binding upon the taxpayer for the first taxable year for which 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 (section 1.614-5(e)(1)).

2) Provide maps, descriptions of the nonoperating interests, and a complete statement of the facts (section 1.614-5(e)(4)).

3) Establish that the principal purpose for forming the aggregation is not tax avoidance. A substantial reduction in taxes is evidence that avoidance of taxes is the principal purpose (section 1.614-5(d) and section 1.614-5(e)).

Taxpayer represents that the A interests were acquired on Date 2. Pursuant to § 1.614-5(e)(1), Taxpayer has until Date 4 to submit a timely request to aggregate the A interests. With respect to the interests located at B, Taxpayer represents the B interest were acquired on Date 3. Pursuant to § 1.614-5(e)(1), Taxpayer has until Date 5 to submit a timely application to aggregate the B interest. This request was filed on Date 1.

Taxpayer represents that to the best of Taxpayer's and its representatives' knowledge that each of the interests identified and located at each of the x distinct areas are "nonoperating mineral interests" as that term is defined in § 1.614-5(g), and that the interests are interests that do not bear the costs of exploration, development, or production. Taxpayer also represents that to the best of Taxpayer's and its representatives' knowledge 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 to the best of Taxpayer's and it representatives' knowledge that the maps for each property included with the ruling request demonstrate that the nonoperating interests at each distinct area 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 mineral interest.

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

Lastly, Taxpayer represents that to the best of Taxpayer's and its representatives' knowledge 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 depletion and allow Taxpayer to implement consistent treatment for financial accounting and federal income tax purposes

Based on the representations made and consideration of the descriptions and maps submitted, we conclude that the requirements of § 1.614-5 have been met. Based solely on the facts and representations submitted, we grant consent for Taxpayer to aggregate the separate nonoperating mineral interests located at the x distinct areas,

A and B, such that the nonoperating mineral interests located at A and B are separately treated as a single property for U.S. federal income tax purposes.

Except as specifically set forth above, we express or imply no opinion concerning the federal income tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, we express or imply no opinion concerning Taxpayers' calculation of depletion or whether Taxpayers' 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 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.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides it may not be used or cited as precedent. In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representatives. We are also sending a copy of this letter to the Director. Pursuant to § 1.614-5(e)(4), a copy of this letter must be attached to the taxpayer's federal income tax return for the first taxable year for which such permission applies. If Taxpayer has already filed such return, a copy of the letter of permission must be filed with the Director and must be accompanied by an amended return or returns if necessary or, if appropriate, a claim for credit or refund.

This letter ruling is being issued electronically in accordance with Rev. Proc. 2020-29, 2020-21 I.R.B. 859. A paper copy will not be mailed to Taxpayer.

Sincerely,

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

cc: