to geothermal wells commenced on or after that date.

(Secs. 263, 9805, Internal Revenue Code of 1954 (92 Stat. 3201, 26 U.S.C. 362; 68A Stat. 917, 26 U.S.C. 7805))

[T.D. 7806, 47 FR 4061, Jan. 28, 1982]

§ 1.613–1 Percentage depletion; general rule.

(a) *In general.* In the case of a taxpayer computing the deduction for depletion under section 611 with respect to minerals on the basis of a percentage of gross income from the property, as defined in section 613(c) and §§ 1.613–3 and 1.613–4, the deduction shall be the percentage of the gross income as specified in section 613(b) and § 1.613–2. The deduction shall not exceed 50 percent (100 percent in the case of oil and gas properties for taxable years beginning after December 31, 1990) of the taxpayer's taxable income from the property (computed without regard to the allowance for depletion). The taxable income shall be computed in accordance with § 1.613–5. In no case shall the deduction for depletion computed under this section be less than the deduction computed upon the cost or other basis of the property provided in section 612 and the regulations thereunder. The apportionment of the deduction between the several owners of economic interests in a mineral deposit will be made as provided in paragraph (c) of § 1.611–1. For rules with respect to "gross income from the property" and for definition of the term "mining," see §§ 1.613–3 and 1.613–4. For definitions of the terms "property," "mineral deposit," and "minerals," see paragraph (d) of § 1.611–1.

(b) *Denial of percentage depletion in case of oil and gas wells.* Except as otherwise provided in section 613A and the regulations thereunder, in the case of oil or gas which is produced after December 31, 1974, and to which gross income is attributable after that date, the allowance for depletion shall be computed without regard to section 613.

[T.D. 8348, 56 FR 21938, May 13, 1991, as amended by T.D. 8437, 57 FR 43899, Sept. 23, 1992]

§ 1.613–2 Percentage depletion rates.

(a) *In general.* Subject to the provisions of paragraph (b) of this section and as provided in section 613(b), in the case of mines, wells, or other natural deposits, a taxpayer may deduct as an allowance for depletion under section 611 the percentages of gross income from the property as set forth in subparagraphs (1), (2), and (3) of this paragraph.

(1) *Without regard to situs of deposits.* The following rates are applicable to the minerals listed in this subparagraph regardless of the situs of the deposits from which the minerals are produced:

(i) 27½ percent—Gas wells, oil wells.

(ii) 23 percent—Sulfur, uranium.

(iii) 15 percent—Ball clay, bentonite, china clay, metal mines,[1] sagger clay, rock asphalt, vermiculite.

(iv) 10 percent—Asbestos,[1] brucite, coal, lignite, perlite, sodium chloride, wollastonite.

(v) 5 percent—Brick and tile clay, gravel, mollusk shells (including clam shells and oyster shells), peat, pumice, sand, scoria, shale, stone (except dimension or ornamental stone). If from brine wells—Bromine, calcium chloride, magnesium chloride.

(2) *Production from United States deposits.* A rate of 23 percent is applicable to the minerals listed in this subparagraph if[2] produced from deposits within the United States:[3]

Anorthosite.[2]	Ilmenite.
Asbestos.	Kyanite.
Bauxite.	Mica.
Beryl.[3]	Olivine.
Celestite.	Quartz crystals (radio grade).
Chromite.	Rutile.
Corundum.	Block Steatite talc.
Fluorspar.	Zircon.
Graphite.	

Ores of the following metals—

[1] Not applicable if the rate prescribed in subparagraph (2) of this paragraph is applicable.

[2] The rate prescribed in this subparagraph does not apply except to the extent that alumina and aluminum compounds are extracted therefrom.

[3] Applicable only for taxable years beginning before January 1, 1964.

[4] Applicable only for taxable years beginning after December 31, 1963.

Antimony.	Platinum.
Beryllium.[4]	latinum group metals.
Bismuth.	Tantalum.
Cadmium.	Thorium.
Cobalt.	Tin.
Columbium.	Titanium.
Lead	Tungsten.
Lithium.	Vanadium.
Manganese.	Zinc.
Mercury.	
Nickel.	

(3) *Other minerals.* A rate of 15 percent is applicable to the minerals listed in this subparagraph regardless of the situs of the deposits from which the minerals are produced, provided the minerals are not used or sold for use by the mine owner or operator as rip rap, ballast, road material, rubble, concrete aggregates, or for similar purposes. If, however, such minerals are sold or used for the purposes described in the preceding sentence, a rate of 5 percent is applicable to any of such minerals unless sold on bid in direct competition with a bona fide bid to sell any of the minerals listed in subdivision (iii) of subparagraph (1) of this paragraph, in which case the rate is 15 percent. In addition, the provisions of this subparagraph are not applicable with respect to any of the minerals listed herein if the rate prescribed in subparagraph (2) of this paragraph is applicable.

Aplite.	Clay, refractory and fire.[6]
Barite.	Diatomaceous earth.
Bauxite.	Dolomite.
Beryl.[5]	Fedlspar.
Borax.	Flake Graphite.
Calcium carbonates.	

(4) For purposes of this section, the term *all other minerals* does not include (i) soil, sod, dirt, turf, water, or mosses; or (ii) minerals from sea water, the air, or similar inexhaustible sources. However, the term *all other minerals* is not limited in meaning to the minerals listed in section 613(b), but includes all other minerals (except those to which a specific percentage rate applies under subparagraphs (1), (2), (3), (4), and (5) of section 613(b)): For example, gypsum, novaculite, natural mineral pigments, quartz sand and quartz pebbles, graphite and kyanite (if section 613(b)(2)(B) does not apply), and anorthosite to the extent that alumina and aluminum compounds are not extracted therefrom. The 15–percent rate applies to such *all other minerals* when used or sold for use by the mine owner or operator for purposes other than as rip rap, ballast, road material, rubble, concrete aggregates, or for similar purposes. When any such minerals are used or sold for use by the mine owner or operator as rip rap, ballast, road material, rubble, concrete aggregates, or for similar purposes, the 5–percent rate applies except that, when sold for such use by the mine owner or operator on a bid in direct competition with a bona fide bid to sell a mineral listed in section 613(b)(3), the 15-percent rate applies. For example, limestone sold on a bid in direct competition with a bona fide bid to sell rock asphalt for road building purposes may be entitled to a 15-percent rate. In every case the taxpayer must establish to the satisfaction of the district director that there was a bona fide bid to sell a mineral listed under section 613(b)(3) by a person other than the taxpayer, and that the mineral sold by the taxpayer was sold on a bid in direct competition with such bona fide bid to sell such other material.[7]

Fluorspar	Potash.
Fullers earth.	Quartzite.
Barnet.	Slate.
Gilsonite.	Soapstone.
Granite	Spodumene.
Lepidolite.	Stone (dimension or[7] ornamental).
Limestone.	Talc (including pyrophyllite).
Magnesite.	Thernardite.
Magnesium carbonates	Tripoli.
Marble.	Trona.
Mica	All other minerals
Phosphate rock.	

(b) *Definition of terms.* (1) For purposes of this section, the minerals indicated below shall have the following meanings:

(i) Clay, brick and tile—Clay used or sold for use in the manufacture of common brick, drain and roofing tile, sewer pipe, flower pots, and kindred

[5] Applicable only for taxable years beginning before January 1, 1964.

[6] Not applicable for taxable years beginning after December 31, 1960.

[7] The 15-percent rate is applicable only to stone used or sold for use by the mine owner or operator as dimension stone or ornamental stone.

products (other than clay specifically identified as a clay for which a 15 percent rate of percentage allowance is provided).

(ii) Clay, refractory and fire—Clay which has a pyrometric cone equivalent of 19 or higher.

(iii) Pumice—All pumice including pumicite.

(iv) Scoria—Only scoria produced from natural deposits.

(2) For purposes of this section, the term *United States* means the States and the District of Columbia. See section 7701(a)(9).

(3) For purposes of this section, the term *dimension stone* means blocks and slabs of natural stone, subsequently cut to definite shapes and sizes and used or sold for such uses as building stone (excluding rubble), monumental stone, paving blocks, curbing and flagging. For purposes of this section, *ornamental stone* means blocks and slabs of natural stone, subsequently cut to definite shapes and sizes and used or sold for use for making ornaments or statues.

(c) *Rules for application of paragraph (a) of this section.* (1) In no case may the allowance for depletion computed upon the basis of a percentage of gross income from the property exceed 50 percent of the taxpayer's taxable income from the property (computed without allowance for depletion). For rules relating to the computation of such taxable income, see §1.613–5.

(2) In cases in which there are produced from a mineral property two or more minerals, each entitled to a different percentage depletion rate under section 613(b) and this section or any of which is entitled to cost depletion only, the percentage depletion allowance is the sum of the results obtained by applying the percentage applicable to each mineral (zero, if not entitled to percentage depletion) to the *gross income from the property* attributable to such mineral. The sum so computed is subject to the limitation provided in section 613(a) and §1.613–1, that is, 50 percent of the taxpayer's taxable income from the property (computed without allowance for depletion). Such taxable income (computed in accordance with §1.613–4) is the total taxable income resulting from the sale of all minerals produced from the mineral property (as defined in section 614 and the regulations thereunder). The provisions of this subparagraph may be illustrated by the following examples:

Example 1. Pyrite, an iron sulfide, may be sold for either its sulfur content or its iron content, or both. Sulfur is entitled to a percentage depletion deduction based on 23 percent of gross income from the property whereas the percentage depletion deduction for iron is based on 15 percent of such gross income. Therefore, in the case of a taxpayer who sells pyrite for both its sulfur and iron content, 23 percent of his gross income from sulfur plus 15 percent of his gross income from iron would be his maximum allowable percentage depletion deduction. However, this maximum deduction would be subject to the limitation provided for in section 613(a), *i.e.*, 50 percent of *taxable income from the property (computed without allowance for depletion)*, such taxable income being the overall taxable income resulting from the sale of both minerals contained in the deposit.

Example 2. Oil and gas are produced from a single mineral property of a taxpayer who operates a retail outlet for the sale of oil products within the meaning of section 613A(d)(2). The taxpayer is not entitled to percentage depletion on the gross income attributable to the oil, but is entitled to percentage depletion on the gross income attributable to gas which is regulated gas under section 613A(b)(2)(B). Accordingly, the taxpayer's maximum allowable percentage depletion deduction would be zero percent of gross income from the property with respect to oil, plus 22 percent (see section 613A(b)(1)) of gross income from the property with respect to gas. This maximum deduction would be subject to the limitation provided for in section 613(a), *i.e.*, 50 percent of *taxable income from the property (computed without allowance for depletion)*, such taxable income being the overall taxable income resulting from the sale of both oil and gas. However, in the case of oil or gas production which qualifies for percentage depletion under section 613A(c), see the special allocation rules contained in section 613A(c)(7) (C) and (E) and §1.613A–4.

(3) Except as provided in section 613(d) and the regulations thereunder relating to special rules for determining rates of depletion for taxable years ending after December 31, 1953, to which the Internal Revenue Code of 1939 applies:

(i) The percentage rates set forth in this section are applicable only for taxable years beginning after December 31,

1953, and ending after August 16, 1954; and

(ii) The percentage rates set forth in 26 CFR (1939) 39.23(m)–5 (Regulations 118) are applicable for taxable years beginning before January 1, 1954, or ending before August 17, 1954.

(4) Percentage depletion is not allowable with respect to the income from a disposal of coal (including lignite) or domestic iron ore (as defined in paragraph (e) of §1.631–3) with a retained economic interest to the extent that such income is treated as from a sale of coal or iron ore under section 631(c) and §1.631–3. Rents or royalties paid or incurred by a taxpayer with respect to coal (including lignite) or domestic iron ore shall be excluded by such taxpayer in determining *gross income from the property* without regard to the treatment under section 631(c) of such rents and royalties in the hands of the recipient.

(5)(i) In all cases there shall be excluded in determining the *gross income from the property* an amount equal to any rents or royalties (which are depletable income to the payee) which are paid or incurred by the taxpayer in respect of the property and are not otherwise excluded from *gross income from the property*. The following example illustrates this rule:

Example. A leases coal-bearing lands to B on condition that B will annually pay a royalty of 25 cents a ton on coal mined and sold by B. During the year 1956, B mines and sells f.o.b. mine 100,000 tons of coal for $600,000. In computing *gross income from the property* for the year 1956, B will exclude $25,000 (100,000 tons×$0.25) in computing his allowable percentage depletion deduction. B's allowable percentage depletion deduction (without reference to the limitation based on taxable income from the property) for the year 1956 will be $57,500 (($600,000 − $25,000)×10 percent).

(ii) If bonus payments have been paid in respect of the property in any taxable year or any prior taxable years, there shall be excluded in determining the *gross income from the property*, an amount equal to that part of such payments which is allocable to the product sold (or otherwise giving rise to gross income) for the taxable year. For purposes of the preceding sentence, bonus payments include payments by the lessee with respect to a production payment which is treated as a bonus under section 636(c). Such a production payment is equally allocable to all mineral from the mineral property burdened thereby. The following examples illustrate the provisions of this subdivision:

Example 1. In 1956, A leases oil bearing lands to B, receiving $200,000 as a bonus and reserving a royalty of one-eighth of the proceeds of all oil produced and sold. It is estimated at the time the lease is entered into that there are 1,000,000 barrels of oil recoverable. In 1956, B produces and sells 100,000 barrels for $240,000. In computing his *gross income from the property* for the year 1956, B will exclude $30,000 (⅛ of $240,000), the royalty paid to A, and $20,000 (100,000 bbls. sold/1,000,000 bbls. estimated to be available × $200,000 bonus), the portion of the bonus allocable to the oil produced and sold during the year. However, in computing B's taxable income under section 63, the $20,000 attributable to the bonus payment shall not be either excluded or deducted from B's gross income computed under section 61. (See paragraph (a)(3) of §1.612–3.)

Example 2. In 1971, C leases to D oil bearing lands estimated to contain 1,000,000 barrels of oil, reserving a royalty of one-eighth of the proceeds of all oil produced and sold and a $500,000 production payment payable out of 50 percent of the first oil produced and sold attributable to the seven-eighths operating interest. In 1972, D produces and sells 100,000 barrels of oil. In computing his *gross income from the property* for the year 1972, D will exclude, in addition to the royalty paid to C, $50,000 (100,000 bbls. sold/1,000,000 bbls. estimated to be available × $500,000 treated under section 636(c) as a bonus), the portion of the production payment allocable to the oil produced and sold during the taxable year. However, in computing D's taxable income under section 63, the $50,000 attributable to the retained production payment shall not be either excluded or deducted from D's gross income computed under section 61.

(iii) If advanced royalties have been paid in respect of the property in any taxable year, the amount excluded from *gross income from the property* of the payor for the current taxable year on account of such payment, shall be an amount equal to the deduction for such taxable year taken on account of such payment pursuant to paragraph (b)(3) of §1.612–3.

Example. If B in example 2 in paragraph (b)(4) of §1.612–3, elects to deduct in 1956 the $10,000 paid to A in that year, he must exclude the same amount from *gross income from the property* in 1956; however, if B elects to defer the deduction until 1957 when he mined and sold the mineral, he must exclude

the $10,000 from *gross income from the property* in 1957.

[T.D. 6500, 25 FR 11737, Nov. 26, 1960, as amended by T.D. 6841, 30 FR 9306, July 27, 1965; T.D. 7170, 37 FR 5374, Mar. 15, 1972; T.D. 7261, 38 FR 5467, Mar. 1, 1973; T.D. 7487, 42 FR 24263, May 13, 1977]

§ 1.613–3 Gross income from the property.

Oil and gas wells. In the case of oil and gas wells, *gross income from the property*, as used in section 613(c)(1), means the amount for which the taxpayer sells the oil or gas in the immediate vicinity of the well. If the oil or gas is not sold on the premises but is manufactured or converted into a refined product prior to sale, or is transported from the premises prior to sale, the gross income from the property shall be assumed to be equivalent to the representative market or filed price of the oil or gas before conversion or transportation.

[T.D. 6500, 25 FR 11737, Nov. 26, 1960, as amended by T.D. 6965, 33 FR 10692, July 26, 1968; T.D. 8474, 58 FR 25557, Apr. 27, 1993]

§ 1.613–4 Gross income from the property in the case of minerals other than oil and gas.

(a) *In general.* The rules contained in this section are applicable to the determination of gross income from the property in the case of minerals other than oil and gas and the rules contained in § 1.613–3 are not applicable to such determination, notwithstanding provisions to the contrary in § 1.613–3. The term *gross income from the property*, as used in section 613(c)(1), means, in the case of a mineral property other than an oil or gas property, gross income from mining. *Gross income from mining* is that amount of income which is attributable to the extraction of the ores or minerals from the ground and the application of mining processes, including mining transportation. For the purpose of this section, *ordinary treatment processes* (applicable to the taxable years beginning before January 1, 1961) and *treatment processes considered as mining* (applicable to the taxable years beginning after December 31, 1960) will be referred to as *mining processes*. Processes, including packaging and transportation, which do not qualify as mining will be referred to as *nonmining processes*. Also for the purpose of this section, transportation which qualifies as *mining* will be referred to as *mining transportation* and transportation which does not qualify as *mining* will be referred to as *nonmining transportation*. See paragraph (f) of this section for the definition of the term *mining* and paragraph (g) of this section for rules relating to nonmining processes.

(b) *Sales prior to the application of nonmining processes including nonmining transportation.* (1) Subject to the adjustments required by paragraph (e)(1) of this section, gross income from mining means (except as provided in subparagraph (2) of this paragraph) the actual amount for which the ore or mineral is sold if the taxpayer sells the ore or mineral:

(i) As it emerges from the mine, prior to the application of any process other than a mining process or any transportation, or

(ii) After application of only mining processes, including mining transportation, and before any nonmining transportation

If the taxpayer sells his ore or mineral in more than one form, and if only mining processes are applied to the ore or mineral, gross income from mining is the actual amount for which the various forms of the ore or mineral are sold, after any adjustments required by paragraph (e)(1) of this section. For example, if, at his mine or quarry, a taxpayer sells several sizes of crushed gypsum and also sells gypsum fines produced as an incidental byproduct of his crushing operations, without applying any nonmining processes, gross income from mining will ordinarily be the total amount for which such crushed gypsum and fines are actually sold. See paragraphs (f) and (g) of this section for provisions defining mining and nonmining processes for various minerals.

(2) In the case of sales between members of a controlled group (including sales as to which the district director exercises his authority under section 482 and the regulations thereunder), the prices for such sales (which shall be deemed to be the actual amount for which the ore or mineral is sold) shall be determined, if possible, by use of the representative market or field price