11 T.C. 495 (1948)

An oil payment contract, even without formal assignment language, constitutes a depletable interest in oil in place.

Summary

The case concerns a partnership, X and Y, engaged in drilling oil wells, which contracted with Z to drill wells in exchange for an oil payment of $52,000. The cost to X and Y was $27,000, including $14,000 for materials and equipment. The contract stipulated that the materials and equipment remained the property of the partnership until fully paid for. The Tax Court addressed whether this constituted a depletable interest in oil in place. The court held that the partnership held a depletable interest, following the precedent set in *T.W. Lee, 42 B.T.A. 1217*. Other tax issues related to partnership deductions were also addressed based on the specific facts presented.

Facts

The partnership of Richards, Holloway & Myers was formed in 1939 to drill oil wells with Richards and Holloway as experienced drillers and Myers providing capital. In 1941, the partnership contracted with Swindler, et al., to drill four wells for a total payment of $52,000, payable out of 76.5625% of the gross production. The contract stipulated that the title to the materials and equipment furnished by the partnership remained its property until fully paid. The partnership reported a loss on its 1941 tax return. The Commissioner adjusted the partnership income, treating the Swindler contract as an oil payment and determining a depletable interest.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the petitioners' income tax for 1941, increasing their community income based on adjustments to partnership income. The petitioners contested these adjustments, leading to a case before the Tax Court. The Tax Court consolidated the cases and addressed several issues related to partnership deductions and the treatment of income from the drilling contracts.

Issue(s)

1. Whether the partnership of Richards, Holloway & Myers held a depletable interest in oil in place under the Swindler contract.

Holding

1. Yes, because the oil payment contract, even with a reservation of title to materials, constituted a depletable interest in oil in place.

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Court’s Reasoning

The court relied on *T.W. Lee, 42 B.T.A. 1217*, which established that an interest held under an oil payment contract is a depletable interest in oil in place,

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