20 T.C. 398 (1953)

A taxpayer must consistently treat multiple mineral properties as either separate or a single property for calculating depletion allowances under Section 114(b)(4) of the Internal Revenue Code.

Summary

Buffalo Chilton Coal Company mined coal from three different mines located on contiguous properties. To maintain market standards for its coal, it blended coal from the high-sulfur No. 1 mine with lower-sulfur coal from the No. 2 and No. 3 mines. The company sought to calculate its depletion allowance as if it were operating a single property. The Tax Court held that the Commissioner of Internal Revenue properly computed the depletion allowance by treating the coal mining operation as three separate properties because the taxpayer had not consistently treated the mines as a single property in prior years.

Facts

Buffalo Chilton Coal Company operated three coal mines (No. 1, No. 2, and No. 3) on contiguous properties under various leases. No. 1 mine produced coal with a high sulfur content, which, over time, made it unsuitable for its primary market. To maintain its market share, the company opened No. 2 and No. 3 mines, which produced coal with a low sulfur content. The coal from all three mines was blended before being sold under the trade name "Buffalo Chilton Coal." The taxpayer owned leaseholds in all tracts under which it operates. All of the lands were contiguous and contained within a single boundary line.

Procedural History

The Commissioner of Internal Revenue determined a deficiency in Buffalo Chilton Coal Company's income tax for 1948. The Commissioner computed the depletion allowance by treating the company's operations as three separate properties, while the company argued that it should be treated as a single property. The Tax Court upheld the Commissioner's determination.

Issue(s)

Whether the Commissioner erred in computing depletion allowable to petitioner for 1948 by treating petitioner's operation as three separate properties within the meaning of section 114 (b) (4) of the Internal Revenue Code, as amended.

Holding

No, because the taxpayer did not consistently treat its properties as a single property for depletion purposes as required by the regulations.

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Court’s Reasoning

The court relied on Treasury Regulations 111, Section 29.23(m)-1(i), which defines “the property” as the interest owned by the taxpayer in any mineral property. The regulation states that a taxpayer’s interest in each separate mineral property is a separate “property,” but where two or more mineral properties are included in a single tract or parcel of land, the taxpayer’s interest in such mineral properties may be considered a single “property,” provided such treatment is consistently followed. The court emphasized that the taxpayer had not consistently treated its properties as a single property. In some years, the company claimed percentage depletion on the combined sales of coal from multiple mines, while in other years, it claimed cost depletion for some mines and percentage depletion for others. The court cited *Helvering v. Jewel Mining Co.*, 126 F.2d 1011, *Black Mountain Corporation*, 5 T.C. 1117, and *Amherst Coal Co.*, 11 T.C. 209 to support the validity of the regulations as a valid interpretation of the revenue acts, emphasizing that consistency of treatment of the properties was a material factor.

Practical Implications

This case highlights the importance of consistent treatment of mineral properties for depletion allowance calculations. Taxpayers with multiple mineral properties located on a single tract of land must elect whether to treat those properties as a single unit or as separate units for depletion purposes. This election is binding for all subsequent years. Failure to consistently treat the properties as a single unit will result in the IRS calculating depletion allowances on a property-by-property basis. This can impact the overall tax liability of the mining company. The case reinforces the Commissioner’s authority to enforce regulations requiring consistent accounting methods for depletion, providing clarity for both taxpayers and the IRS in managing mineral property taxation.

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