***Santa Fe Pacific Gold Company and Subsidiaries, By and Through Its Successor in Interest, Newmont USA Limited v. Commissioner of Internal Revenue, 130 T. C. 299 (U. S. Tax Court 2008)***

In a significant ruling on alternative minimum tax (AMT) calculations, the U. S. Tax Court held that depletion deductions for mines placed in service before December 31, 1989, must be adjusted under the Adjusted Current Earnings (ACE) method if the deductions exceed the property's adjusted basis. This decision impacts how mining companies calculate their tax liabilities, affirming the IRS's position on the applicability of Section 56(g)(4)(C)(i) to depletion deductions, while clarifying the treatment of unamortized development costs under AMT.

## Parties

The petitioner was Santa Fe Pacific Gold Company and its subsidiaries, through its successor in interest, Newmont USA Limited. The respondent was the Commissioner of Internal Revenue. At the trial level, Santa Fe Pacific Gold was the plaintiff, and the Commissioner was the defendant. On appeal, Newmont USA Limited maintained the petitioner status, while the Commissioner remained the respondent.

## Facts

Santa Fe Pacific Gold Company and its subsidiaries (collectively referred to as Santa Fe) owned several gold mines, including the Mesquite Mine placed in service in September 1981, and two Twin Creeks Mines placed in service in December 1987 and March 1989, respectively. For the taxable years ending December 31, 1994, 1995, 1996, and May 5, 1997, Santa Fe calculated its depletion deductions using the percentage depletion method under Section 613, which resulted in deductions higher than those allowed under the cost depletion method of Section 612. Santa Fe was subject to the alternative minimum tax (AMT) and did not make Adjusted Current Earnings (ACE) adjustments for the depletion deductions of its mines placed in service before December 31, 1989, despite these deductions exceeding the adjusted basis of the mines for cost depletion purposes. The Commissioner issued a notice of deficiency on November 13, 2006, adjusting Santa Fe's ACE calculations to include these adjustments.

## Procedural History

The Commissioner issued a notice of deficiency to Santa Fe on November 13, 2006, for the taxable years ending December 31, 1994, 1995, 1996, and May 5, 1997. Santa Fe timely filed a petition in the U. S. Tax Court to contest the Commissioner's adjustments. The parties filed cross-motions for partial summary judgment on the issue of whether Section 56(g)(4)(C)(i) required ACE adjustments for depletion deductions of mines placed in service before December 31, 1989. The Tax Court granted the Commissioner's motion for partial summary judgment on this issue, holding that Section 56(g)(4)(C)(i) applied to depletion deductions for such mines.

**Issue(s)**

Whether Section 56(g)(4)(C)(i) of the Internal Revenue Code requires an Adjusted Current Earnings (ACE) adjustment for depletion deductions for mines placed in service on or before December 31, 1989, when such deductions exceed the adjusted basis of the property for cost depletion purposes?

**Rule(s) of Law**

Section 56(g)(4)(C)(i) of the Internal Revenue Code states that in determining ACE, no deduction is allowed for any item that would not be deductible for any taxable year for purposes of computing earnings and profits. Section 1. 312-6(c)(1) of the Income Tax Regulations specifies that percentage depletion under all revenue acts for mines and oil and gas wells is not to be taken into account in computing earnings and profits. Section 56(g)(4)(F)(i) applies only to property placed in service after December 31, 1989, and requires the use of the cost depletion method under Section 611 for AMT purposes.

**Holding**

The U. S. Tax Court held that Section 56(g)(4)(C)(i) applies to depletion deductions for mines placed in service on or before December 31, 1989, requiring an ACE adjustment for the amount by which the depletion deduction exceeds the adjusted basis of the property, except to the extent that the same amount is also treated as a preference under Section 57(a)(1).

**Reasoning**

The Tax Court's reasoning was based on the plain language and statutory scheme of the Internal Revenue Code. The court rejected Santa Fe's argument that Section 56(g)(4)(C)(i) did not apply to depletion deductions because Section 56(g)(4)(F)(i) was the only provision governing ACE adjustments for depletion. The court noted that while Section 56(g)(4)(F)(i) applies only to property placed in service after December 31, 1989, Section 56(g)(4)(C)(i) applies to all property regardless of when it was placed in service. The court further reasoned that the two sections are not in conflict, as Section 56(g)(4)(F)(i) only limits the temporary benefits of the percentage depletion method, while Section 56(g)(4)(C)(i) offsets the permanent benefits when the deduction exceeds the adjusted basis. The court also addressed the treatment of unamortized development costs under Section 56(a)(2), holding that such costs are not included in the adjusted basis of depletable property for purposes of calculating ACE adjustments under Section 56(g)(4)(C)(i) or preferences under Section 57(a)(1). However, the court allowed Santa Fe to include these costs in the adjusted basis of the Mesquite Mine for calculating Section 57(a)(1) preferences due to the Commissioner's concession on this point.

**Disposition**

 

The U. S. Tax Court granted the Commissioner's motion for partial summary judgment, holding that Santa Fe must make ACE adjustments under Section 56(g)(4)(C)(i) for depletion deductions of the Mesquite Mine that exceed its adjusted basis for the years at issue.

**Significance/Impact**

This decision clarifies the application of Section 56(g)(4)(C)(i) to depletion deductions for mines placed in service before December 31, 1989, under the AMT. It reaffirms the IRS's position that such deductions must be adjusted to prevent permanent tax benefits when they exceed the adjusted basis of the property. The ruling also highlights the importance of the adjusted basis in determining AMT liability and the treatment of unamortized development costs. The decision may impact how mining companies calculate their AMT liabilities and could lead to increased tax liabilities for those with mines placed in service before the specified date.

 