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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

method, as described in paragraph (c) of this section; otherwise such prices shall be determined by the appropriate pricing method as provided in paragraph (d)(1) of this section. For the definitions of the terms *controlled* and *group,* see paragraph (j) (1) and (2) of this section.

(c) *Cases where a representative market or field price for the taxpayer's ore or mineral can be ascertained*—(1) *General rule.* If the taxpayer processes the ore or mineral before sale by the application of nonmining processes (including nonmining transportation), or uses it in his operations, gross income from mining shall be computed by use of the representative market or field price of an ore or mineral of like kind and grade as the taxpayer's ore or mineral after the application of the mining processes actually applied (if any), including mining transportation (if any), and before any nonmining transportation, subject to any adjustments required by paragraph (e)(1) of this section. See paragraph (e)(2)(i) of this section for certain other situations in which this paragraph shall apply. The objective in computing gross income from mining by the representative market or field price method is to ascertain, on the basis of an analysis of actual competitive sales by the taxpayer or others, the dollar figure or amount which most nearly represents the approximate price at which the taxpayer, in light of market conditions, could have sold his ores or minerals if, prior to the application of nonmining processes, the taxpayer had sold the quantities and types of ores and minerals to which he applied nonmining processes. If it is possible to determine a market or field price under the provisions of this paragraph, and if that price is determined to be representative, the taxpayer's gross income from mining shall be determined on the basis of that price and not under the provisions of paragraph (d) of this section. The taxpayer's own actual sales prices for ores or minerals of like kind and grade shall be taken into account when establishing market or field prices, provided that those sales are determined to be representative.

(2) *Criteria for determining whether an ore or mineral is of like kind and grade as the taxpayer's ore or mineral.* An ore or mineral will be considered to be of like kind and grade as the taxpayer's ore or mineral if, in common commercial practice, it is sufficiently similar in chemical, mineralogical, or physical characteristics to the taxpayer's ore or mineral that it is used, or is commercially suitable for use, for essentially the same purposes as the uses to which the taxpayer's ore or mineral is put. Whether an ore or mineral is of like kind and grade as the taxpayer's ore or mineral will generally be determined by reference to industrial or commercial specifications and by consideration of chemical and physical data relating to the minerals and deposits in question. The fact that the taxpayer applies slightly different size reduction processes, or the fact that the taxpayer uses slightly different benefication processes, or the fact that the taxpayer sells his ore or mineral for different purposes, will not, in itself, prevent another person's ore or mineral from being considered to be of like kind and grade as the taxpayer's ore or mineral. On the other hand, the fact that the taxpayer's ore or mineral is suitable for the same general commercial use as another person's ore or mineral will not cause the two ores or minerals to be considered to be of like kind and grade if the desirable natural constituents of the two ores or minerals are markedly different substances. For example, anthracite coal will not be considered to be of like kind as bituminous coal merely because both types of coal can be used as fuel. Similarly, bituminous coal which does not possess coking qualities will not be considered to be of like grade as bituminous coking coal. However, in the case of a taxpayer who mines and uses his bituminous coal in the production of coke, all bituminous coals in the same marketing area will be considered to be of like kind, and all such bituminous coals having the same or similar coking quality suitable for commercial use by coke producers will be considered to be of like grade as the coal mined and used by the taxpayer

Fine distinctions between various grades of minerals are to be avoided unless those distinctions are clearly

shown to have genuine commercial significance.

(3) *Factors to be considered in determining the representative market or field price for the taxpayer's ore or mineral.* In determining the representative market or field price for the taxpayer's ore or mineral, consideration shall be given only to prices of ores or minerals of like kind and grade as the taxpayer's ore or mineral and with which, under commercially accepted standards, the taxpayer's ore or mineral would be considered to be in competition if it were sold under the conditions described in paragraph (b)(1) of this section. A weighted average of the competitive selling prices of ores or minerals of like kind and grade as the taxpayer's, beneficiated only by mining processes, if any, in the relevant markets, although not determinative of the representative market or field price, is an important factor in the determination of that price. The taxpayer's own competitive sales prices for minerals which have been subjected only to mining processes shall be taken into account in computing such a weighted average. For purposes of the preceding sentence, if the district director has exercised his authority under section 482 and the regulations thereunder and has determined the appropriate price with respect to specific sales transactions by the taxpayer, that price shall be deemed to be a competitive sales price for those transactions. Sales or purchases, including the taxpayer's, of ores or minerals of like kind and grade as the taxpayer's, will be taken into consideration in determining the representative market or field price for the taxpayer's ore or mineral only if those sales or purchases are the result of competitive transactions. The identity of the taxpayer's relevant markets (including their accessibility to the taxpayer), and the representative market or field price within those markets, are necessarily factual determinations to be made on the basis of the facts and circumstances of each individual case. For the purpose of determining the representative market or field price for the taxpayer's ore or mineral, exceptional, insignificant, unusual, tie-in, or accommodation sales shall be disregarded. Except as provided above, representative market or field prices shall not be determined by reference to prices established between members of a controlled group. See paragraph (j) of this section for the definitions of the terms *controlled* and *group*.

(4) *Use of prices of mineral of different grade.* If there is no representative market or field price for a mineral of like kind and grade as the taxpayer's, representative market or field prices for an ore or mineral which is of like kind but which is not of like grade as his ore or mineral may be used, with appropriate adjustments for differences in mineral content. Representative market or field prices of an ore or mineral of like kind but not of like grade may be used only if such adjustments are readily ascertainable. For example, it may be appropriate in a particular case to establish the representative market or field price for an ore having 50 percent X mineral content by reference to the representative market or field price for the same kind of ore having 60 percent X mineral content with an appropriate adjustment for the differences in the valuable mineral content of the two ores, any differences in processing costs attributable to impurities, and any other relevant factors.

(5) *Information to be furnished by a taxpayer computing gross income from mining by use of a representative market or field price.* A taxpayer who computes his gross income from mining pursuant to the provisions of this paragraph shall attach to his return a summary statement indicating the prices used by him in computing gross income from mining under this paragraph and the source of his information as to those prices, and the relevant supporting data shall be assembled, segregated, and made readily available at the taxpayer's principal place of business.

(6) *Limitation on gross income from mining computed under the provisions of this paragraph.* It shall be presumed that a price is not a representative market or field price for the taxpayer's ore or mineral if the sum of such price plus the total of all costs of the nonmining processes (including nonmining transportation) which the taxpayer applies to his ore or mineral regularly exceeds the taxpayer's actual sales price

of his product. For example, if on a regular basis the total of all costs of nonmining processes applied by the taxpayer to coal for the purpose of making coke is $12 per ton, and if the taxpayer's actual sale price for such coke is $18 per ton, a price of $7 per ton would not be a representative market or field price for the taxpayer's coal which is used for making coke. In order to rebut the presumption set forth in the first sentence of this subparagraph, it must be established that the loss on nonmining operations is directly attributable to unusual, peculiar and nonrecurring factors rather than to the use of a market or field price which is not representative. For example, the first sentence of this subparagraph shall not apply if the taxpayer establishes in an appropriate case that the loss on nonmining operations is directly attributable to an event such as a fire, flood, explosion, earthquake, or strike.

(d) *Cases where a representative market or field price cannot be ascertained*—(1) *General rule.* (i) If it is impossible to determine a representative market or field price as described in paragraph (c) of this section then, except as provided in subdivision (ii) of this subparagraph, gross income from mining shall be computed by use of the proportionate profits method as set forth in subparagraph (4) of this paragraph. A method of computing gross income from mining under the provisions of this paragraph shall not be deemed to be a method of accounting for purposes of paragraph (e) of § 1.446–1.

(ii)(*a*) The Office of the Assistant Commissioner (Technical) may determine that a method of computation is more appropriate than the proportionate profits method or the method being used by the taxpayer. The taxpayer may request such a determination (see (*d*) of this subdivision (ii)). If the taxpayer is using a method of computation which has been determined by the Office of Assistant Commissioner (Technical) to be more appropriate than the proportionate profits method, such method shall continue to be used until it is determined by the Office of Assistant Commissioner (Technical) that either the proportionate profits method or another method is more appropriate.

(*b*) The proportionate profits method is more appropriate than the method being used under (*a*) if, under the particular facts and circumstances, the method being used under (*a*) consistently fails to clearly reflect gross income from mining and the proportionate profits method more clearly reflects gross income from mining for the taxable year.

(*c*) An alternative method (a method other than the method being used under (*a*) (if any) and the proportionate profits method) is more appropriate than the method being used under (*a*) (if any) and the proportionate profits method if, under the particular facts and circumstances, the latter methods consistently fail to clearly reflect gross income from mining, and the alternative method being considered more clearly reflects gross income from mining on a consistent basis than the method being used under (*a*) (if any) and the proportionate profits method. When determining whether a method of computation clearly reflects gross income from mining, it is relevant to compare the gross income from mining produced by such method with the gross income from mining, on an equivalent amount of production, which results from the computation methods used by competitors. When determining the acceptability of proposed alternative methods, primary consideration will be given to computation methods based upon representative charges for ores, minerals, products, or services. See paragraph (c) of this section for principles determining the representative character of a charge.

(*d*) Application for permission to compute gross income from mining by use of an alternative method shall be made by submitting a request to the Commissioner of Internal Revenue, Attention: Assistant Commissioner (Technical), Washington, DC 20224.

(*e*) Among the alternative methods of computation to which consideration will be given, provided that the requirements of this subdivision (ii) are

met, are the methods listed in subparagraphs (5), (6), and (7) of this paragraph. The order in which these methods are listed is not significant, and the listing of these methods does not preclude a request to make use of a method which is not listed.

(iii) Approval and continued use of any method of computation under this paragraph depends upon all the facts and circumstances in each case, and shall be subject to such terms and conditions as may be necessary in the opinion of the Commissioner to reflect clearly the gross income from mining. Accordingly, the use of such a method for any taxable year shall be subject to review and change.

(2) *Costs to be used in computing gross income from mining by use of methods based on the taxpayer's costs.* In determining the taxpayer's gross income from mining by use of methods based on the taxpayer's costs, only costs actually paid or incurred shall be taken into consideration. In general, if the taxpayer has consistently employed a reasonable method of determining the costs of the various individual phases of his mining and nonmining processes (such as extraction, loading for shipment, calcining, packaging, etc.), such method shall not be disturbed. The amount of any particular item to be taken into account shall, for taxable years beginning after November 30, 1968, be the amount used in determining the taxpayer's income for tax purposes. For example, the depreciation lives, methods, and records used for tax purposes, if different from those used for book purposes, shall be the basis for determining the amount of depreciation to be used. However, a taxpayer may continue to use a reasonable method for determining those costs on the basis of the amounts computed for cost control or similar financial or accounting books and records if that method has been used consistently and is applied to the determination of all those costs.

(3) *Treatment of particular items in computing gross income from the mining by use of methods based on the taxpayer's costs.* (i) Except as specifically provided elsewhere in this section, when determining gross income from mining by use of methods based on the taxpayer's costs, the costs attributable to mining transportation shall be treated as mining costs, and the costs attributable to nonmining transportation shall be treated as nonmining costs. Accordingly, except as specifically provided elsewhere in this section, all profits attributable to mining transportation shall be treated as mining profits, and all profits attributable to nonmining transportation shall be treated as nonmining profits. For this purpose, mining transportation means so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to plants or mills in which other mining processes are applied thereto as is not in excess of 50 miles or, if the taxpayer files an application pursuant to paragraph (h) of this section and the Commissioner finds that both the physical and other requirements are such that the ores or minerals must be transported a greater distance to such plants or mills, the transportation over the greater distance. Further, for this purpose, nonmining transportation includes the transportation (whether or not by common carrier) of ores, minerals, or the products produced therefrom, from the point of extraction from the ground to nonmining facilities, or from a mining facility to a nonmining facility, or from one nonmining facility to another, or from a nonmining facility to the customers who purchase the taxpayer's first marketable product or group of products. See paragraph (e)(2) of this section for provisions relating to purchased transportation to the customer and paragraph (g)(3) of this section for provisions relating to transportation the primary purpose of which is marketing or distribution. In the absence of other methods which clearly reflect the costs of the various phases of transportation, the cost attributable to nonmining transportation shall be an amount which is in the same ratio to the costs incurred for the total transportation as the distance of the nonmining transportation is to the distance of the total transportation. As an example, where the plants or mills in which mining processes are applied to ores or minerals are in excess of 50 miles from the point of extraction from

the ground (or in excess of a greater distance approved by the Commissioner), the costs incurred for transportation to those plants or mills in excess of 50 miles (or of that greater distance) shall be treated as nonmining costs in determining gross income from mining. Accordingly, all profits attributable to that excess transportation are treated as nonmining profits. However, except in the case of transportation performed in conveyances owned or leased by the taxpayer, the preceding sentence shall apply only to taxable years beginning after November 30, 1968.

(ii) In determining gross income from mining by use of methods based on the taxpayer's costs, a process shall not be considered as a mining process to the extent it is applied to ores, minerals, or other materials with respect to which the taxpayer is not entitled to a deduction for depletion under section 611. The costs of such nondepletable ores, minerals, or materials; the costs of the processes (including blending, size reduction, etc.) applied thereto; and the transportation costs thereof, if any, shall be considered as nominating costs in determining gross income from mining. If a mining process is applied to an admixture of depletable and nondepletable material, the cost of the process and the cost of transportation, if any, attributable to the nondepletable material shall be considered as nonmining costs in determining gross income from mining. Accordingly, all profits attributable thereto are treated as nonmining profits. In the absence of other methods which clearly reflect the cost attributable to the processing and transportation, if any, of the nondepletable admixed material, that cost shall be deemed to be that proportion of the costs which the tonnage of nondepletable material bears to the total tonnage of both depletable and nondepletable material.

(iii) In determining gross income from mining by use of methods based on the taxpayer's costs:

(*a*) The costs attributable to containers, bags, packages, pallets, and similar items as well as the costs of materials and labor attributable to bagging, packaging, palletizing, or similar operations shall be considered as nonmining costs.

(*b*) The costs attributable to the bulk loading of manufactured products shall be considered as nonmining costs.

(*c*) The costs attributable to the operation of warehouses or distribution terminals for manufactured products shall be considered as nonmining costs

Accordingly, all profits attributable thereto are treated as nonmining profits.

(iv) In computing gross income from mining by the use of methods based on the taxpayer's costs, the principles set forth in paragraph (c) of §1.613–5 shall apply when determining whether selling expenses and trade association dues are to be treated, in whole or in part, as mining costs or as nonmining costs. To the extent that selling expenses and trade association dues are treated as nonmining costs, all profits attributable thereto are treated as nonmining profits.

(v) See paragraph (e)(1) of this section for provisions excluding certain allowances from the taxpayer's gross sales and costs of his first marketable product or group of products.

(4) *Proportionate profits method.* (i) The objective of the *proportionate profits method* of computation is to ascertain gross income from mining by applying the principle that each dollar of the total costs paid or incurred to produce, sell, and transport the first marketable product or group of products (as defined in subdivision (iv) of this subparagraph) earns the same percentage of profit. Accordingly, in the proportionate profits method no ranking of costs is permissible which results in excluding or minimizing the effect of any costs incurred to produce, sell, and transport the first marketable product or group of products. For purposes of this subparagraph, members of a controlled group shall be treated as divisions of a single taxpayer. See paragraph (j) of this section for the definitions of the terms *controlled* and *group*.

(ii) The proportionate profits method of computation is applied by multiplying the taxpayer's gross sales (actual or constructive) of his first marketable product or group of products (after making the adjustments required

by paragraph (e) of this section) by a fraction whose numerator is the sum of all the costs allocable to those mining processes which are applied to produce, sell, and transport the first marketable product or group of products, and whose denominator is the total of all the mining and nonmining costs paid or incurred to produce, sell, and transport the first marketable product or group of products (after making the adjustments required by this paragraph and paragraph (e) of this section). The method as described herein is merely a restatement of the method formerly set forth in the second sentence of Regulations 118, section 39.23(m)–1 (e)(3) (1939 Code). The proportionate profits method of computation may be illustrated by the following equation:

$$\frac{\text{Mining costs}}{\text{Total costs}} \times \text{Gross sales} = \text{Gross income from mining}$$

(iii) Those costs which are paid or incurred by the taxpayer to produce, sell, and transport the first marketable product or group of products, and which are not directly identifiable with either a particular mining process or a particular nonmining process shall, in the absence of a specific provision of this section providing an apportionment method, be apportioned to mining and to nonmining by use of a method which is reasonable under the circumstances. One method which may be reasonable in a particular case is an allocation based on the proportion that the direct costs of mining processes and the direct costs of nonmining processes bear to each other. For example, the salary of a corporate officer engaged in overseeing all of the taxpayer's processes is an expense which may reasonably be apportioned on the basis of the ratio between the direct costs of mining and nonmining processes. On the other hand, an expense such as workmen's compensation premiums would normally be apportioned on the basis of direct labor costs. For the rule relating to selling expenses, see paragraph (c)(4) of § 1.613–5.

(iv) As used in this section, the term *first marketable product or group of products* means the product (or group of essentially the same products) produced by the taxpayer as a result of the application of nonmining processes, in the form or condition in which such product or products are first marketed in significant quantities by the taxpayer or by others in the taxpayer's marketing area. For this purpose, bulk and packaged products are considered to be essentially the same product. Sales between members of a controlled group (as defined in paragraph (j) of this section) shall not be considered in making a determination under this subdivision. The first marketable product or group of products does not include any product which results from additional manufacturing or other nonmining processes applied to the product or products first marketed in significant quantities by the taxpayer or others in the taxpayer's marketing area. For example, if a cement manufacturer sells his own finished cement in bulk and bags and also sells concrete blocks or dry ready-mix aggregates containing additives, the finished cement, in bulk and bags, constitutes the first marketable product or group of products produced by him. Similarly, if an integrated iron ore and steel producer sells both pig iron in various sizes and rolled sheet iron or shapes, his first marketable product is the pig iron in its various sizes. Further, if an integrated clay and brick producer sells both unglazed bricks and tiles of various shapes and sizes and additionally manufactured bricks and tiles which are specially glazed, the unglazed products, both packaged and unpackaged, constitute his first marketable product or group of products.

(v)(*a*) As used in this subparagraph, the term *gross sales (actual or constructive)* means the total of the taxpayer's actual competitive sales to others of the first marketable product or group of products, plus the taxpayer's constructive sales of the first marketable product or group of products used or

retained for use in his own subsequent operations, subject to the adjustments required by paragraph (e) of this section. See (*b*) of this subdivision in the case of actual sales between members of controlled groups and in the case of constructive sales. A *constructive sale* occurs when a miner-manufacturer is deemed, for percentage depletion purposes, to be selling the first marketable product or group of products to himself.

(*b*) In the case of sales between members of a controlled group as to which the district director has exercised his authority under section 482 and the regulations thereunder and has determined the appropriate price with respect to specific sales transactions, that price shall be deemed, for those transactions, to be the actual amount for which the first marketable product or group of products is sold for purposes of this subdivision (v). In the case of all other sales between members of a controlled group, and in the case of constructive sales, the prices for such sales shall be determined by use of the principles set forth in paragraph (c) of this section, subject to the adjustments required by paragraph (e) of this section. In the case of constructive sales, see paragraph (c)(4) of this section for rules relating to information to be furnished by the taxpayer.

(vi) The provisions of this subparagraph may be illustrated by the following examples:

Example 1. (a) Facts. A is engaged in the mining of a mineral to which section 613 applies and in the application thereto of nonmining processes. During 1968, A incurred extraction costs of $35,000; other mining costs of $56,000; $150,000 for manufacturing costs; $46,000 for other nonmining processes; and $14,000 for the company president's salary and similiar costs resulting from both nonmining and mining processes. During that year, A produced and sold 70,000 tons of his first marketable product for an actual gross sales price of $420,000, after the adjustments required by paragraph (e) of this section. A representative market or field price for A's mineral before the application of nonmining processes cannot be established.

(*b*) *Computation.* (*1*) The computation of A's gross income from mining by use of the proportionate profits method involves two steps. The first step is to apportion A's costs to mining and to nonmining. A apportions the company president's salary and similiar costs to mining and to nonmining in the manner described in the second and third sentences of subdivision (iii) of this subparagraph, and apportions his remaining costs as follows:

Cost	Mining	Nonmining	Total
Extraction	$35,000	.....	$35,000
Other mining processes	56,000	.....	56,000
Manufacturing	.....	$150,000	150,000
Other nonmining processes	.....	46,000	46,000
Subtotal	91,000	196,000	287,000
President's salary and similar costs	4,439	9,561	14,000
Total costs	95,439	205,561	301,000

(*2*) The second step is to apply the proportionate profits fraction so as to compute A's gross income from mining. To do this, A first computes his gross sales of his first marketable group of products, in this case $420,000. A multiplies his actual gross sales of $420,000 by the proportionate profits fraction, whose numerator consists of his total mining costs ($95,439) and whose denominator consists of his total costs ($301,000). Thus, A's gross income from mining is $133,170 (*i.e.,* 95,439/301,000ths of A's actual gross sales of $420,000).

Example 2. B, who leases a mineral property from C, is engaged in the mining of a mineral to which section 613 applies and in the application thereto of nonmining processes. Pursuant to the terms of the lease, B is required to pay C 10 cents for each ton of mineral which B mines. During 1971, B extracted 100,000 tons of mineral. He sold his first marketable product for an actual gross sales price of $225,000 after the adjustments required by paragraph (e) of this section. A representative market or field price for B's mineral before the application of nonmining processes cannot be established. During 1971, with respect to the 100,000 tons of mineral extracted, B incurred mining costs of $50,000 and nonmining costs of $100,000, and paid $10,000 to C as C's royalty. Since the royalty payment is considered to be C's share of the gross income from mining under section 613(a), it is not considered to be either a mining cost or a nonmining cost of B. B's gross income from mining is $65,000 under the proportionate profits method, determined as follows: The $225,000 gross receipts must be multiplied by the proportionate profits fraction which is $50,000 mining costs over $150,000 total costs ($50,000+$100,000 nonmining costs). Since the resulting $75,000 is the total gross income from mining with respect to the property, it must be allocated between B's lease interest and C's royalty interest. The $10,000 paid to C must be subtracted from the $75,000 leaving $65,000 which represents B's gross income from mining. C's

gross income from mining is the royalty he received or $10,000.

(5) *Representative schedule method.* The *representative schedule method* is a pricing formula which uses representative finished product prices, penalties, charges and adjustments, established in arms-length transactions between unrelated parties, to determine the market or field price for a crude mineral product. The representative character of a price, penalty, charge, or adjustment shall be determined by applying the principles set forth in paragraph (c) of this section. The representative schedule method is principally intended for use in those industries in which such a schedule-type pricing method is in general use to determine the price paid to unintegrated mineral producers for their crude mineral product. For example, if unintegrated producers of copper concentrate in a particular field or market customarily sell their product at prices which are determined in accordance with a schedule-type pricing formula, consideration will be given to the determination of concentrate prices for integrated copper producers in accordance with the same pricing formula. The representative schedule method shall not be used if it is impossible to determine one or more of the elements in the representative schedule formula by reference to prices, penalties, charges, or adjustments established in representative transactions between unrelated parties. See paragraph (c) of this section for principles determining the representative character of a charge.

(6) *Method using prices outside the taxpayer's market.* Under the *other market method* the taxpayer uses representative market or field prices established outside his markets, provided that conditions there are substantially the same as in his markets. For example, it may be appropriate in a particular case to establish the representative market or field price for pellets containing 60 percent iron which are produced and used in market area X by reference to the representative market or field price for pellets containing 60 percent iron which are produced and sold in adjacent market area Y, provided that conditions in the two marketing areas are shown to be substantially the same.

(7) *Rate of return on investment method.* [Reserved]

(e) *Reductions of sales price in computing gross income from mining*—(1) *Discounts.* If a taxpayer computes gross income from mining under the provisions of paragraph (b)(1) of this section, trade discounts and, for taxable years beginning after November 30, 1968, cash discounts actually allowed by the taxpayer shall be subtracted from the sale price of the taxpayer's ore or mineral. If a taxpayer computes gross income from mining under the provisions of paragraph (c) of this section, any such discounts actually allowed (if not otherwise taken into account) by the person or persons making the sales on the basis of which the representative market or field price for the taxpayer's ore or mineral is to be determined shall be subtracted from the sale price in computing such representative market or field price. If a taxpayer computes gross income from mining under the provisions of paragraph (d) of this section, such discounts actually allowed (if not otherwise taken into account) shall be subtracted from the gross sales (actual or constructive), and shall not be considered a cost, of the first marketable product or group of products. The provisions of this subparagraph shall apply to arrangements which have the same effect as trade or cash discounts, regardless of the form of the arrangements.

(2) *Purchased transportation to the customer.* (i) A taxpayer who computes gross income from mining under the provisions of paragraph (c) of this section and who sells his ore or mineral after the application of only mining processes but after nonmining transportation shall use as the representative market or field price his delivered price (if otherwise representative) reduced by costs paid or incurred by him for purchased transportation to the customer as defined in subdivision (iii) of this subparagraph. If the transportation by the taxpayer is not purchased transportation to the customer, or if the taxpayer does not sell the ore or mineral until after the application of nonmining processes, and if other producers in the taxpayer's marketing

area sell significant quantities of an ore or mineral of like kind and grade after the application of only mining processes but after purchased transportation to the customer, the representative delivered price at which the ore or mineral is sold by those other producers reduced by representative costs of purchased transportation to the customer paid or incurred by those producers shall be used by the taxpayer as the representative market or field price for his ore or mineral in applying paragraph (c) of this section. Furthermore, appropriate adjustments shall be made to take into account differences in mode of transportation and distance. When applying this subdivision, the representative market or field price so computed shall not exceed the taxpayer's delivered price less his actual costs of transportation to the customer. For purposes of this subdivision, any delivered price shall be adjusted as provided in subparagraph (1) of this paragraph.

(ii) If a taxpayer computes gross income from mining under the provisions of paragraph (d) of this section, the cost of purchased transportation to the customer (as defined in subdivision (iii) of this subparagraph) shall be excluded from the gross sales of his first marketable product or group of products (after any adjustments required by subparagraph (1) of this paragraph), and from the denominator of the proportionate profits fraction, so as not to attribute profits to the cost of that transportation. Similar transportation cost adjustments may be made, if appropriate, in the case of other methods of computation which are based on the taxpayer's costs. For the treatment of costs and profits attributable to transportation which is not purchased transportation to the customer as defined in subdivision (iii) of this subparagraph, see paragraph (d)(3)(i) of this section.

(iii) For purposes of this section, the term *purchased transportation to the customer* means, in general, nonmining transportation of the taxpayer's minerals or mineral products to the customer:

(*a*) Which is not performed in conveyances owned or leased directly or indirectly, in whole or in part, by the taxpayer,

(*b*) Which is performed solely to deliver the taxpayer's minerals or mineral products to the customer, rather than to transport such minerals or products for packaging or other additional processing by the taxpayer (other than incidental storage or handling), and

(*c*) With respect to which the taxpayer ordinarily does not earn any profit

For purposes of the preceding sentence, transportation which is performed by a person controlling or controlled by the taxpayer (within the meaning of paragraph (j)(1) of this section) shall be deemed to have been performed in conveyances owned or leased by the taxpayer unless it is established by the taxpayer that the price charged by the controlling or controlled person for such transportation constitutes an arm's-length charge (under the standard described in paragraph (b)(1) of § 1.482–1). The term *purchased transportation to the customer* includes transportation to a warehouse, terminal, or distribution facility owned or operated by the taxpayer, provided that such transportation is performed under the conditions described in the first sentence of this subdivision. A taxpayer will not be deemed ordinarily to earn a profit on transportation merely because charges for the transportation are included in the stated selling price, rather than being separately stated or segregated from other billing. A taxpayer will not be deemed ordinarily to earn a profit on transportation if the rates for the transportation constitute an arm's-length charge ordinarily paid by shippers of the same product in similar circumstances. If a taxpayer computes gross income from mining under the provisions of paragraph (d) of this section, the term *purchased transportation to the customer* refers to transportation which conforms to the other requirements of this subdivision and which is performed to transport the taxpayer's first marketable product or group of products (as defined in paragraph (d)(4)(iv) of this section) rather than to transport minerals or mineral products which do not yet constitute the taxpayer's first marketable product or group of products.

(iv) The provisions of this subparagraph may be illustrated by the following examples:

Example 1. A is engaged in the mining of an ore of mineral M and in the production and sale of M concentrate. A retains a portion of his concentrate for use in his own nonmining operations. During 1968, A sold 100,000 tons of M concentrate of ore mined and processed by him, which sales constituted a significant portion of his total production. Eighty thousand tons of that concentrate were sold by A on the basis of a representative price (after adjustments required by subparagraph (1) of this paragraph) of $30 per ton f.o.b. mine or plant, resulting in gross income from mining of $2,400,000. The remaining 20,000 tons were sold by A, both directly and through terminals, on the basis of a delivered price (after adjustments required by subparagraph (1) of this paragraph) at City X of $40 per ton. The delivered price included $15 per ton cost of purchased transportation from the mine or plant to customers in City X. The representative market or field price of the concentrate sold by A on the basis of a delivered price is $25 per ton, determined by subtracting the cost of the purchased transportation to the customer ($15 per ton) from the delivered price for the concentrate ($40 per ton). Accordingly, A's gross income from mining with respect to the 20,000 tons of M concentrate sold on a delivered basis is $500,000. The representative market or field price for the concentrate retained by A and used in his own nonmining operations may be computed by reference to the weighted average price for both A's f.o.b. mine and A's delivered sales of concentrate, with the delivered sales prices reduced in the manner described above. On this basis, the representative market or field price for the retained concentrate is $29 per ton.

Example 2. B is engaged in the mining of an ore of mineral N and in the production of N concentrate. B retained all but an insignificant amount of his concentrate for use in his own nonmining operations. Other producers in B's marketing area sell significant amounts of N concentrate of like kind and grade, both on an f.o.b. mine or plant basis and on a delivered basis. In this case, the prices for both the f.o.b. and the delivered sales made by other producers (after any adjustments required by subparagraph (1) of this paragraph), after reduction of the delivered prices by the cost of purchased transportation to the customer, shall, if such prices are otherwise representative, be taken into account in establishing the representative market or field price for the N concentrate produced and used by B.

(f) *Definition of mining*—(1) *In general.* The term *mining* includes only:

(i) The extraction of ores or minerals from the ground;

(ii) Mining processes, as described in subparagraphs (2) through (6) of this paragraph; and

(iii) So much of the transportation (whether or not by common carrier) of ores or minerals from the point of extraction of the ores or minerals from the ground to the plants or mills in which the processes referred to in subdivision (ii) of this subparagraph are applied thereto as is not in excess of 50 miles, and, if the Commissioner finds that both the physical and other requirements are such that the ores or minerals must be transported a greater distance to such plants or mills, the transportation over such greater distance as the Commissioner authorizes. See paragraph (h) of this section for rules relating to the filing of applications to treat as mining any transportation in excess of 50 miles.

(2) *Definition of mining processes.* (i) As used in subparagraph (1)(ii) of this paragraph, the term *mining processes* means, for taxable years beginning before January 1, 1961, the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, including the following processes (and the processes necessary or incidental thereto), and, for taxable years beginning after December 31, 1960, the following processes (and the processes necessary or incidental thereto):

(*a*) In the case of coal—cleaning, breaking, sizing, dust allaying, treating to prevent freezing, and loading for shipment;

(*b*) In the case of sulfur recovered by the Frasch process—cleaning, pumping to vats, cooling, breaking, and loading for shipment;

(*c*) In the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and ores or minerals which are customarily sold in the form of a crude mineral product (as defined in subparagraph (3)(iv) of this paragraph):

(*1*) Where applied for the purpose of bringing to shipping grade and form (as defined in subparagraph (3)(iii) of this paragraph)—sorting, concentrating, sintering, and substantially equivalent processes, and

(*2*) Loading for shipment.

(*d*) In the case of lead, zinc, copper, gold, silver, uranium, or fluorspar ores, potash, and ores or minerals which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore or the mineral or minerals from other material from the mine or other natural deposit; and

(*e*) In the case of the following ores or minerals:

(*1*) The furnacing of quicksilver ores,

(*2*) The pulverization of talc,

(*3*) The burning of magnesite, and

(*4*) The sintering and nodulizing of phosphate rock.

(ii) The term *mining processes* also includes the following processes (and, except as otherwise provided in this subdivision, the processes necessary or incidental thereto):

(*a*) For taxable years beginning after December 31, 1960, in the case of calcium carbonates and other minerals when used in making cement—all processes (other than preheating the kiln feed) applied prior to the introduction of the kiln feed into the kiln, but not including any subsequent process;

(*b*) For taxable years beginning after December 31, 1960, and before November 14, 1966, in the case of clay to which former section 613(b)(5)(B) applied, and for taxable years beginning after November 13, 1966, in the case of clay to which section 613(b) (5) or (6) (B) applies—crushing, grinding, and separating the clay from waste, but not including any subsequent process;

(*c*) For taxable years beginning after October 9, 1969, in the case of minerals (other than sodium chloride) extracted from brines pumped from a saline perennial lake (as defined in paragraph (b) of §1.613–2)—the extraction of such minerals from the brines, but in no case including any further processing or refining of such extracted minerals; and

(*d*) For taxable years beginning after December 30, 1969, in the case of oil shale (as defined in paragraph (b) of §1.613–2)—extraction from the ground, crushing, loading into the retort, and retorting, but in no case hydrogenation, refining, or any other process subsequent to retorting.

(iii) A process is *necessary* to another related process if it is prerequisite to the performance of the other process. For example, if the concentrating of low-grade iron ores to bring to shipping grade and form cannot be effectively accomplished without fine pulverization, such pulverization shall be treated as a process which is *necessary* to the concentration process. Accordingly, because concentration is a mining process, such pulverization is also a mining process. Furthermore, if mining processes cannot be effectively applied to a mineral without storage of the mineral while awaiting the application of such processes, such storage shall be treated as a process which is *necessary* to the accomplishment of such mining processes. A process is *incidental* to another related process if the cost thereof is insubstantial in relation to the cost of the other process, or if the process is merely the coincidental result of the application of the other process. For example, the sprinkling of coal, prior to loading for shipment, with dots of paper to identify the coal for tradename purposes will be considered incidental to the loading where the cost of that sprinkling is insubstantial in relation to the cost of the loading process. Also, where crushing of a crude mineral is treated as a mining process, the production of fines as a byproduct is ordinarily the coincidental result of the application of a mining process. If a taxpayer demonstrates that, as a factual matter, a particular process is necessary or incidental to a process named as a mining process in section 613(c)(4) of this paragraph, the necessary or incidental process will also be considered a mining process.

(iv) The term *mining* does not include purchasing minerals from another. Accordingly, the processes listed in this paragraph shall be considered as mining processes only to the extent that they are applied by a mine owner or operator to an ore or mineral in respect

of which he is entitled to a deduction for depletion under section 611. The application of these processes to purchased ores, minerals, or materials does not constitute mining.

(3) *Processes recognized as mining for ores or minerals covered by section 613(c)(4)(C).* (i) As used in section 613(c)(4)(C) and subparagraph (2)(i) (*c*) of this paragraph, the terms *sorting* and *concentrating* mean the process of eliminating substantial amounts of the impurities or foreign matter associated with the ores or minerals in their natural state, or of separating two or more valuable minerals or ores, without changing the physical or chemical identity of the ores or minerals. Examples of sorting and concentrating processes are hand or mechanical sorting, magnetic separation, gravity concentration, jigging, the use of shaking or concentrating tables, the use of spiral concentrators, the use of sluices or sluice boxes, sink-and-float processes, classifiers, hydrotators and flotation processes. Under section 613(c)(4)(C), sorting and concentration will be considered mining processes only where they are applied to bring an ore or mineral to shipping grade and form.

(ii) As used in section 613(c)(4)(C) and subparagraph (2)(i)(*c*) of this paragraph, the term *sintering* means the agglomeration of fine particles by heating to a temperature at which incipient, but not complete, fusion occurs. Sintering will be considered a mining process only where it is applied to an ore or mineral, or a concentrate of an ore or mineral, as an auxiliary process necessary to bring the ore or mineral to shipping form. A thermal action which is applied in the manufacture of a finished product will not be considered to be a mining process even though such thermal action may cause the agglomeration of fine particles by incipient fusion, and even though such action does not cause a chemical change in the agglomerated particles. For example, the sintering of finely ground iron ore concentrate, prior to shipment from the concentration plant, for the purpose of preventing the risk of loss of the finely divided particles during shipment is considered a mining process. On the other hand, for example, a heating process applied to expand or harden clay, shale, perlite, vermiculite, or other materials in the course of the manufacture of lightweight aggregate or other building materials is not considered to be a mining process.

(iii) As used in section 613(c)(4)(C) and this section, to *bring to shipping grade and form* means, with respect to taxable years beginning after December 31, 1960, to bring (by the application of mining processes at the mine or concentration plant) the quality or size of an ore or mineral to the stage or stages at which the ore or mineral is shipped to customers or used in nonmining processes (as defined in paragraph (g) of this section) by the taxpayer.

(iv) An ore or mineral is *customarily sold in the form of a crude mineral product,* within the meaning of section 613 (c)(4)(C), if a significant portion of the production thereof is sold or used in a nonmining process prior to the alteration of its inherent mineral content by some form of beneficiation, concentration, or ore dressing. An ore or mineral does not lose its classification as a crude mineral product by reason of the fact that, before sale or use in a nonmining process, the ore or mineral may be crushed or subjected to other processes which do not alter its inherent mineral content. Whether the portion of production sold or used in the form of a crude mineral product is a significant portion of the total production of an ore or mineral is a question of fact.

(4) *Type of processes recognized as mining for ores or minerals covered by section 613(c)(4)(D).* Cyanidation, leaching, crystallization, and precipitation, which are listed in section 613(c)(4)(D) as treatment processes considered as mining, and the processes (or combination of processes) which are substantially equivalent thereto, will be recognized as mining only to the extent that they are applied to the taxpayer's ore or mineral for the purpose of separation or extraction of the valuable mineral product or products from the ore, or for the purpose of separation or extraction of the mineral or minerals from other material extracted from the mine or other natural deposit. A process, no matter how denominated, will not be recognized as mining if the process beneficiates the ore or mineral to

the degree that such process, in effect, constitutes smelting, refining, or any other nonmining process within the meaning of paragraph (g) of this section. As used in section 613(c)(4)(D) and subparagraph (2)(i) (*d*) of this paragraph, the term *concentration* has the meaning set forth in the first two sentences of subparagraph (3)(i) of this paragraph.

(5) *Processes recognized as mining under section 613(c)(4)(I)*. Under the authority granted the Secretary or his delegate in section 613(c)(4)(I), the processes which are described in subdivisions (i) through (iv) of this subparagraph, and the processes necessary or incidental thereto, are recognized as mining processes for taxable years beginning after December 31, 1960. The processes described in subdivisions (i) through (iv) of this subparagraph are in addition to the specific processes recognized as mining under section 613(c)(4). Such additional processes are:

(i) Crushing and grinding, but not fine pulverization (as defined in paragraph (g) (6) (v) of this section);

(ii) Size classification processes applied to the products of an allowable mining process;

(iii) Drying to remove free water, provided that such drying does not change the physical or chemical identity or composition of the mineral; and

(iv) Washing or cleaning the surface of mineral particles (including the washing of sand and gravel and the treatment of kaolin particles to remove surface stains), provided that such washing or cleaning does not activate or otherwise change the physical or chemical structure of the mineral particles.

(6) In the case of a process applied subsequent to a nonmining process, see paragraph (g)(2) of this section.

(g) *Nonmining processes*—(1) *General rule*. Unless they are otherwise provided for in paragraph (f) of this section as mining processes (or are necessary or incidental to processes listed therein), the following processes are not considered to be mining processes—electrolytic deposition, roasting, calcining, thermal or electric smelting, refining, polishing, fine pulverization, blending with other materials, treatment effecting a chemical change, thermal action, and molding or shaping. See subparagraph (6) of this paragraph for definitions of certain of these terms.

(2) *Processes subsequent to nonmining processes*. Notwithstanding any other provision of this section, a process applied subsequent to a nonmining process (other than nonmining transportation) shall also be considered to be a nonmining process. Exceptions to this rule shall be made, however, in those instances in which the rule would discriminate between similarly situated producers of the same mineral. For example, roasting is specifically designated in subparagraph (1) of this paragraph as a nonmining process, but in the case of minerals referred to in section 613(c)(4)(C) sintering is recognized as a mining process. If certain impurities in an ore can only be removed by roasting in order to bring it to the same shipping grade and form as a competitive sintered ore of the same kind which requires no roasting, the subsequent sintering of the roasted ore will be treated as a mining process. In that case, however, the roasting of the ore will nonetheless continue to be treated as a nonmining process.

(3) *Transportation for the purpose of marketing or distribution; storage*. Transportation the primary purpose of which is marketing, distribution, or delivery for the application of only nonmining processes shall not be considered as mining. Nor shall transportation be considered as mining merely because, during the course of such transportation, some extraneous matter is removed from the ore or mineral by the operation of forces of nature, such as evaporation, drainage, or gravity flow. Similarly, storage or warehousing of manufactured products shall not be considered as mining. The preceding sentence shall apply even though, during the course of such storage or warehousing, some extraneous matter is removed from the ore or mineral by the operation of forces of nature, such as evaporation, drainage, or gravity flow.

(4) *Manufacturing, etc*. The production, packaging, distribution, and marketing of manufactured products, and the processes necessary or incidental thereto, are nonmining processes.

(5) *Transformation processes*. Processes which effect a substantial physical or chemical change in a crude mineral product, or which transform a crude mineral product into new or different mineral products, or into refined or manufactured products, are nonmining processes except to the extent that such processes are allowed as mining processes under section 613(c) or under paragraph (f) of this section.

(6) *Definitions*. As used in section 613(c)(5) and this section:

(i) The term *calcining* refers to processes used to expel the volatile portions of a mineral by the application of heat, as, for example, the burning of carbonate rock to produce lime, the heating of gypsum to produce calcined gypsum or plaster of Paris, or the heating of clays to reduce water of crystallization.

(ii) The term *thermal smelting* refers to processes which reduce, separate, or remove impurities from ores or minerals by the application of heat, as, for example, the furnacing of copper concentrates, the heating of iron ores, concentrates, or pellets in a blast furnace to produce pig iron, or the heating of iron ores or concentrates in a direct reduction kiln to produce a feed for direct conversion into steel.

(iii) The term *refining* refers to processes (other than mining processes designated in section 613(c)(4) or this section) used to eliminate impurities or foreign matter from smelted or partially processed metallic and nonmetallic ores and minerals, as, for example, the refining of blister copper. In general, a refining process is designed to achieve a high degree of purity by removing relatively small amounts of impurities or foreign matter from smelted or partially processed ores or minerals.

(iv) The term *polishing* refers to processes used to smooth the surface of minerals, as, for example, sawing applied to finish rough cut blocks of stone, sand finishing, buffing, or otherwise smoothing blocks of stone.

(v) The term *fine pulverization* refers to any grinding or other size reduction process applied to reduce the normal topsize of a mineral product to less than .0331 inches, which is the size opening in a No. 20 Screen (U.S. Standard Sieve Series). A mineral product will be considered to have a normal topsize of .0331 inches if at least 98 percent of the product will pass through a No. 20 Screen (U.S. Standard Sieve Series), provided that at least 5 percent of the product is retained on a No. 45 Screen (U.S. Standard Sieve Series). Compliance with the normal topsize test may also be demonstrated by other tests which are shown to be reasonable in the circumstances. The normal topsize test shall be applied to the product of the operation of each separate and distinct piece of size reduction equipment utilized (such as a roller mill), rather than to the final products for sale. Fine pulverization includes the repeated recirculation of material through crushing or grinding equipment to accomplish fine pulverization. Separating or screening the product of a fine pulverization process (including separation by air or water flotation) shall be treated as a nonmining process.

(vi) The term *blending with other materials* refers to processes used to blend different kinds of minerals with one another, as, for example, blending iodine with common salt for the purpose of producing iodized table salt.

(vii) The term *treatment effecting a chemical change* refers to processes which transform or modify the chemical composition of a crude mineral, as, for example, the coking of coal. The term does not include the use of chemicals to clean the surface of mineral particles provided that such cleaning does not make any change in the physical or chemical structure of the mineral particles.

(viii) The term *thermal action* refers to processes which involve the application of artificial heat to ores or minerals, such as, for example, the burning of bricks, the coking of coal, the expansion or popping of perlite, the exfoliation of vermiculite, the heat treatment of garnet, and the heating of shale, clay, or slate to produce lightweight aggregates. The term does not include drying to remove free water.

(h) *Application to treat, as mining, transportation in excess of 50 miles*. If a taxpayer desires to include in the computation of his gross income from mining transportation in excess of 50 miles

from the point of extraction of the minerals from the ground, he shall file an original and one copy of an application for the inclusion of such greater distance with the Commissioner of Internal Revenue, Washington, DC 20224. The application must include a statement setting forth in detail the facts concerning the physical and other requirements which prevented the construction and operation of the plant (in which mining processes, as defined in paragraph (f) of this section, are applied) at a place nearer to the point of extraction from the ground. These facts must be sufficient to apprise the Commissioner of the exact basis of the application. If the taxpayer's return is filed prior to receipt of notice of the Commissioner's action upon the application, a copy of such application shall be attached to the return. If, after an application is approved by the Commissioner, there is a material change in any of the facts relied upon in such application, a new application must be submitted by the taxpayer.

(i) *Extraction from waste or residue. Extraction of ores or minerals from the ground* means not only the extraction of ores or minerals from a deposit, but also the extraction by mine owners or operators of ores or minerals from waste or residue of their prior mining. It is immaterial whether the waste or residue results from the process of extraction from the ground or from application of mining processes as defined in paragraph (f) of this section. However, extraction of ores or minerals from waste or residue which results from processes which are not allowable as mining processes is not treated as mining. *Extraction of ores or minerals from the ground* does not include extraction of ores or minerals by the purchaser of waste or residue or the purchaser of the rights to extract ores or minerals from waste or residue. The term *purchaser* does not apply to any person who acquires a mineral property, including waste or residue, in a tax-free exchange, such as a corporate reorganization, from a person who was entitled to a depletion allowance upon ores or minerals produced from such waste or residue, or from a person who would have been entitled to such depletion allowance had section 613(c)(3) been in effect at the time of the transfer. The term *purchaser* also does not apply to a lessee who has renewed a mineral lease if the lessee was entitled to a depletion allowance (or would have been so entitled had section 613(c)(3) been in effect at the time of the renewal) upon ores or minerals produced from waste or residue before renewal of the lease. It is not necessary, for purposes of the preceding sentence, that the mineral lease contain an option for renewal. The term *purchaser* does include a person who acquires waste or residue in a taxable transaction, even though such waste or residue is acquired merely as an incidental part of the entire mineral enterprise. For special rules with respect to certain corporate acquisitions referred to in section 381(a), see section 381(c)(18) and the regulations thereunder.

(j) *Definition of controlled group.* When used in this section:

(1) The term *controlled* includes any kind of control, direct or indirect, whether or not legally enforceable, and however exercisable or exercised. It is the reality of the control which is decisive, not its form or the mode of its exercise. A presumption of control arises if income or deductions have been arbitrarily shifted.

(2) The term *group* means the organizations, trades, or businesses owned or controlled by the same interests.

[T.D. 7170, 37 FR 5374, Mar. 15, 1972]

§ 1.613–5 Taxable income from the property.

(a) *General rule.* The term *taxable income from the property (computed without allowance for depletion*), as used in section 613 and this part, means *gross income from the property* as defined in section 613(c) and §§ 1.613–3 and 1.613–4, less all allowable deductions (excluding any deduction for depletion) which are attributable to mining processes, including mining transportation, with respect to which depletion is claimed. These deductible items include operating expenses, certain selling expenses, administrative and financial overhead, depreciation, taxes deductible under section 162 or 164, losses sustained, intangible drilling and development costs, exploration and development expenditures, etc. See paragraph