



Comparison of Percentage Depletion Tax Provisions

Federal tax policy allowing for percentage depletion applies to mineral assets¹, including oil and natural gas. Percentage depletion of mineral assets allows the taxpayer to deduct a fixed percent of its income to reflect its production of a depleting asset.

Federal tax law has always recognized the validity of a deduction for depleting mineral assets. Initially, the only deduction was based on the cost of the project. In 1918, Congress recognized the strategic importance of petroleum and it sought to increase petroleum development. It also recognized that cost depletion alone might not be sufficient to enable mineral producers to replace exhausted reserves and could result in abandoning mineral assets before they were fully produced. Consequently, it created a depletion option based on the value of the assets. It recognized that value depletion could exceed cost depletion because it is impossible to fully value mineral assets based on the initial development costs. The initial value depletion approach was too cumbersome and in 1926 Congress created percentage depletion for oil and natural gas because it is straightforward to calculate and audit. Subsequently, Congress applied percentage depletion to other minerals. Similarly, percentage depletion applies to royalty owners of the mineral assets where it is particularly useful because of the challenges to royalty owners to acquire accurate and current cost depletion information.

Both cost depletion and percentage depletion must be calculated and the higher value used as a deduction.

Tax Provision	Section 613 – Percentage Depletion for Oil and Natural Gas Wells	Section 613 – Percentage Depletion for Coal	Section 613 – Percentage Depletion for Sulfur	Section 613 – Percentage Depletion
Basic Provision	Deduction of 15 percent of gross income, excluding rents and royalties paid	Deduction of 23 percent of income, excluding rents and royalties paid	Deduction of 10 percent of income, excluding rents and royalties paid	Deductions of various percentages of income, excluding rents and royalties paid, for other minerals listed in footnote
Presence in Tax Code	Added to the tax code in 1926	Added to the tax code in 1932	Added to the tax code in 1932	Added to the tax code from 1932 to 1954
Limitations	Applies only to US production Available only to independent producers and royalty owners Limited to the first 1000 barrel/day of oil (6000 mcf/day of natural gas) Limited to net income of the producing property, computed without allowance for depletion and without the deduction under the manufacturers tax deduction Limited to 65 percent of the taxpayers net income Applies to both regular and alternative minimum tax	Limited to 50 percent net income of the producing property, computed without allowance for depletion and without the deduction under the manufacturers tax deduction	Limited to 50 percent net income of the producing property, computed without allowance for depletion and without the deduction under the manufacturers tax deduction	Limited to 50 percent net income of the producing property, computed without allowance for depletion and without the deduction under the manufacturers tax deduction Limited for some minerals to US production

¹ Sulfur, uranium, asbestos, brucite, coal, lignite, perlite, sodium chloride, wollastonite, gravel, peat, pumice, sand, scoria, shale, stone, clay, metal mines, rock asphalt, vermiculite and all other minerals (including, but not limited to, apatite, barite, borax, calcium carbonates, diatomaceous earth, dolomite, feldspar, fullers earth, garnet, gilsonite, granite, limestone, magnesite, magnesium carbonates, marble, mollusk shells (including clam shells and oyster shells), phosphate rock, potash, quartzite, slate, soapstone, stone (used or sold for use by the mine owner or operator as dimension stone or ornamental stone), thenardite, tripoli, trona, bauxite, flake graphite, fluorspar, lepidolite, mica, spodumene, and talc (including pyrophyllite)). If from deposits in the United States— oil and natural gas, geothermal energy, gold, silver, copper, iron ore, anorthosite, clay, laterite, and nephelite syenite (to the extent that alumina and aluminum compounds are extracted therefrom), bauxite, celestite, chromite, corundum, fluorspar, graphite, ilmenite, kyanite, mica, olivine, quartz crystals (radio grade), rutile, block steatite talc, and zircon, and ores of the following metals: antimony, beryllium, bismuth, cadmium, cobalt, columbium, lead, lithium, manganese, mercury, molybdenum, nickel, platinum and platinum group metals, tantalum, thorium, tin, titanium, tungsten, vanadium, and zinc.