NOTE: Where it is feasible, a syllabus (headnote) will be released, as is being done in connection with this case, at the time the opinion is issued. The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States* v. *Detroit Lumber Co.,* 200 U. S. 321, 337.

SUPREME COURT OF THE UNITED STATES

Syllabus

UNITED STATES *v.* HILL ET UX.

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

No. 91–1421. Argued November 2, 1992—Decided January 25, 1993

Under §57(a)(8) of the Internal Revenue Code of 1954, 26 U. S. C. §57(a)(8) (1976 ed.), ``the excess of the deduction for depletion . . . over the adjusted basis of'' ``property (as defined in [§]614)'' is an ``ite[m] of tax preference'' on which a taxpayer must pay a ``minimum tax'' for the tax year in question. See §56(a). In computing the minimum taxes due on their interests in oil and gas deposits for tax years 1981 and 1982, respondents Hill calculated their depletion allowances according to the ``percentage depletion'' method, and included in the interests' adjusted bases the unrecovered costs of certain depreciable tangible items used in drilling and development (machinery, tools, pipes, etc.), as identified in §1.612–4(c)(1) of the applicable Treasury Department regulations. The Commissioner of Internal Revenue disputed that inclusion, and assessed larger minimum taxes based on the exclusion of the tangible costs from the mineral interests' adjusted bases. The Hills paid the resulting deficiencies and filed a refund claim, which the Commissioner denied. The Claims Court granted summary judgment for the Hills in their ensuing refund suit, and the Court of Appeals affirmed.

Held: The term ``adjusted basis,'' as used in §57(a)(8), does not include the depreciable drilling and development costs identified in Treas. Reg. §1.612–4(c)(1). Pp. 6–17.

(a) The definitional scheme established by the Code and accompanying regulations suggests strongly that the ``property'' with which §57(a)(8) is concerned excludes just those improvements that the Hills wish to include in adjusted basis. Section 614(a) defines ``property'' for §57(a)(8)'s purposes as ``each separate interest owned by the taxpayer in each mineral deposit.'' Treasury Reg. §1.611–1(d)(4) defines

``mineral deposit'' as ``minerals in place,'' while Treas. Reg. §1.611–1(d)(3) defines ``mineral enterprise'' to include ``the mineral deposit or deposits *and improvements, if any, used in . . . the production of oil and gas.*'' (Emphasis added.) Because these regulatory definitions were well-established when Congress passed §57(a)(8), it is reasonable to assume that Congress relied on the accepted distinction between them in its reference to "mineral deposit" in §614. This conclusion is confirmed by Treas. Reg. §1.57–1(h)(3)'s incorporation into §57(a)(8) of §1016 of the Code, 26 U. S. C. §1016 (1976 ed. and Supp. V), which provides the rules for making ``[a]djustments to basis'' in determining the amount of gain or loss a taxpayer must recognize when he sells or otherwise disposes of property. To follow §1016(a)(2)'s directive that the taxpayer subtract from his original basis in the property ``not less than the amount allowable'' for exhaustion, wear and tear, obsolescence, amortization, and depletion, a taxpayer must determine whether parts of the item sold are subject to different tax treatments, and must treat those parts as different properties under the section. Depletion and depreciation are two of the major categories of tax treatment, and a review of pertinent Code and regulation provisions reveals that the boundaries between the two are virtually impassable. Thus, if a depletable mineral deposit and depreciable associated equipment are sold together, §1016 requires the seller to separate them. In light of the incorporation of this rule into §57(a)(8), and the Hills' failure to identify any exception to the rule, it may be inferred that their tangible costs may not be included in the basis of their depletable mineral deposits. Pp. 6–13.

(b) This conclusion is confirmed by the astonishing results of reading §57(a)(8) in the manner urged by the Hills, whereby the tangible costs at issue here would shelter, over the years a taxpayer owned the capital item they represented, an amount of percentage depletion many times that of the costs themselves. It is hard to believe that Congress would enact a minimum tax to limit the benefit that taxpayers could realize from ``items of tax preference,'' only to define one of those items in a way that would create an even greater proportional tax benefit from investing in tangible items, and to do so in an oblique fashion that, as far as appears, has no precedent in federal income tax history. Pp. 13–14.

(c) Contrary to the Hills' contention, two other Treasury Department regulations do not foreclose the foregoing conclusion. First, Treas. Reg. §1.612–1(b)(1)'s reference, in its title, to a ``[s]pecial rul[e]'' excluding amounts recoverable through depreciation deductions from the basis for ``cost'' depletion of mineral property cannot have been intended to indicate that such amounts should, as a general rule, be included in the calculation of basis for percentage depletion, since that would allow the title of one subsection of a regulation to defeat the entire Code framework for determining basis, and since §1.612–1(b)(1) was issued long before the minimum tax was enacted. Second, excluding tangible costs from the adjusted basis of mineral deposit interests would not run counter to Treas. Reg. §1.612–4(b)(1), which specifies that certain intangible drilling and development costs are recoverable through depletion, as adjustments to the bases of the mineral deposit interests to which they relate. There is no reason why this regulation's deviation from general principles of basis allocation, if such it be, should force the Government, or this Court, to create another deviation. Pp. 14–17.

945 F. 2d 1529, reversed.

SOUTER, J., delivered the opinion for a unanimous Court.