















































The reporting period runs from September 1 thru September 1 of the following year, requiring the need to review 2 years of affidavits.

Often, the reports will reveal that the owner of the claim did not actually do the physical labor of working the claim. This standing alone would not immediately make the activity passive to the owner. Management of the activities, hiring the laborers, and filing the necessary documentation pertaining to the claim all must be considered in the determination of the participation by the owner. (Note: Treas. Reg. sections 1.469-5T(b)(2)(ii) and (f)(2) exclude certain types of participation from consideration.) This may be difficult to ascertain as there are no strict record-keeping requirements. Thus, obtaining information at the initial interview is critical. Third-party contacts with those individuals identified on the labor reports may also be helpful in determining the amount of participation on the part of the owner.

Remember, the Affidavits of Annual Labor are NOT verified by the Department of Natural Resources. This information must be used only as reference information. Audit comments should be made regarding the extent of reliance on the information.

The mining season for the small scale miner can be a short period during the spring and summer. This is due to the extreme weather conditions and the need for heavy duty equipment to work in the winter months. Larger operations have more resources and are better able to extend the period of operations. However, for the individual, this relatively shorter working season should be considered when making an analysis of the numbers of hours worked.

## **Chapter 6**

### **Non-Filers**

Through examination of DNR documentation and research of the information available through internal resources, the identity and filing status of an individual can be ascertained. Investigation of these records will allow for determination of compliance by this population.

Affidavits of Annual Labor on file with DNR are a good place to start. The documents will reveal the owner of a claim and the current address. It is the owner's responsibility that the Division of Mining have a current address. The Affidavit further reports the names and current addresses of the persons who actually performed the work.

When examining the DNR documents, the names and addresses of the individuals on the report should be noted and subsequently verified through IDRS for their filing status. If research reveals that an individual has failed to file a return, contact should be made and they should be encouraged to come into compliance.

An IRP document should be obtained and checked for information regarding wages or non-employee compensation. Employers can then be contacted for copies of documents or any other information concerning the individual which would be helpful in supporting an income issue. The DNR files can also be examined for activity regarding this individual. This includes any property transfers, production reports, etc.

The Affidavit of Annual Labor gives the names of individuals who actually worked the claim in any given year. It does not detail the capacity of the laborer, that is, as an employee or an independent contractor. If the SSN or the EIN can be ascertained for the owner, a PMFOLS (summary) can be run to determine if Forms W-2 or 1099 have been filed. If it is found that information documents have been filed, a PMFOLD (detail) can then be run to further define what has been filed.

If it is found that an individual laborer has not filed an income tax return but information reports were filed, the information should be obtained to properly document the file. Initially, this information should be sought from the individual who actually filed the form. If the documents are not obtainable, an explanation as to why and what procedures were taken to procure a copy should be included in the file.

Upon confirmation of an individual's non-filer status, an IRP document should be ordered. An IRP document will be considered evidence of income, as it is an internal IRS document whose source and authenticity is within the Service's ability to confirm. However, copies of actual documents are preferable over internal documentation.

The Bureau of Labor Statistics (BLS) for non-filers should be considered when a taxpayer can be located but is uncooperative. The BLS statistics can be used, if it appears that a taxpayer is gainfully employed or self-employed, based upon the individual's standard of living.

## **Chapter 7**

### **Employee versus Independent Contractor Status**

If individuals work a claim as employees or independent contractors, they are performing a service for the owner and not conducting exploration or development for themselves. Thus, they are not entitled to deduct expenses with regards to that claim.

However, an employee or independent contractor would be allowed to deduct unreimbursed expenses under IRC section 162. It is advisable to find out what the individual's status is in relationship to the owner or lessee of the claim. This information can be obtained through interviewing the individual, the claim owner, or from the information available at the Department of Natural Resources.

If the individual is working as an employee, there should be a Form W-4 filed with the employer and Forms W-2 & W-3 filed by the employer, as well as the appropriate employment tax returns. The documents should be examined for possible employment tax issues when completing the Required Filing Checks as part of an examination of the employer's income tax return. Employee returns should include Form 2106 to claim expenses in connection with the employment. Since the employee is working for the owner, no Schedule C should be filed.

If the individual is working as an independent contractor, a Form 1099 should be issued by the owner. The income and associated expenses of the contractor should be reported on Schedule C. In most cases, the independent contractor does not have an interest in the claim or mine. Thus, the contractor cannot deduct exploration or development expenses for the particular claim. If there are expenses, determine the type and if the taxpayer is deducting them under IRC section 162 as ordinary and necessary business expenses or as exploration or development expenses. In the case of the independent contractor, an IRC section 183 issue can be considered.

In either case, whether an employee or independent contractor, a determination of employment tax issues should be considered. Consult the employment tax coordinator if there are any questions or issues regarding the classification of workers or employment taxes.

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## **Chapter 8**

### **Depletion**

Depletion, like depreciation, is a form of cost recovery. Just as the owner of a business asset is allowed to recover the cost of an asset over its useful life, a miner is allowed to recover the cost of mineral property. Depletion is taken over the period of time that mineral is being extracted. Two forms of depletion are allowed: cost depletion and percentage depletion. The taxpayer is required to use the method which will result in the greatest deduction.

#### **Cost Depletion**

The general method used for the calculation of depletion is the cost method. The first step of this method is to determine the number of units which comprise the deposit. The units can be tons of ore, barrels of oil, board feet of timber, etc. The taxpayer must be consistent from year to year in the type of unit being calculated to insure uniformity. The second step takes the cost or adjusted basis of the property which pertains to the deposit and divides this basis by the total number of units to obtain the depletion cost per unit. Once the total number of units extracted is determined for the tax year, it is multiplied by the cost per unit to obtain the amount of depletion available.

It is possible that during the course of the operation or from examination, the estimate of the number of units which comprise the deposit may change. If this happens, the calculation can change. While the number of units can be recalculated, the basis cannot be adjusted. It is advisable to discuss with the taxpayer as early as possible how they estimated the number of units used in the depletion calculation. It is also helpful to determine if the taxpayer has adjusted this estimate over the course of production. Check to see if the taxpayer is being consistent with the measure of units and what method was used to develop the new estimate.

The following example covers depletion using constant estimates.

The taxpayer purchases a claim for \$50,000, with known mineral reserves in mineable quantities. He states that he is in the production phase and is selling product. The taxpayer estimates that there is 100,000 tons of ore to be extracted. For purposes of the computation for depletion, the basis of the mine is \$50,000. During the tax year, the taxpayer mines and sells 3,500 tons of ore. The first year depletion would be calculated as follows:

Rate of Depletion per ton (\$50,000/100,000) .....	\$	.50
Depletion for year (3,500 x \$.50) .....	\$	1,750.00
 Purchase price .....	\$	50,000
First year depletion .....		<u>1,750</u>
First year basis of the property .....	\$	48,250

If estimates of the amount of reserves were never adjusted, the above calculation for depletion would remain constant. The basis would be reduced each year by the amount of depletion until it is totally consumed and the taxpayer has no basis left in the property. At this time, cost depletion is no longer allowed. While this scenario would certainly not be out of the ordinary, a revision in the estimate of reserves will affect the depletion calculation, and should be thoroughly examined. The following example covers depletion using revised estimates.

In tax year 2, the miner sells 7,000 tons. At the end of the year, the estimate of the ore changes to 130,000 tons. The calculation for depletion for year 2 would be as follows:

Revised estimate of unextracted ore .....	130,000	
Ore sold during the year .....	<u>7,000</u>	
Total tonnage used to compute new rate .....	137,000	
Remaining Adjusted Basis of property .....	\$48,250	
 Rate of Depletion per ton (\$48,250 / 137,000) .....	\$	.35
Depletion for year 2 (7,000 x .35) .....	\$	2,450
 First year basis of the property .....	\$48,250	
Second year depletion .....	<u>-2,450</u>	
Second year basis of the property .....	\$45,800	

## **Percentage Depletion**

Under the percentage depletion method, a flat percentage of gross income from the activity is used to calculate the depletion allowance. The deduction for depletion cannot exceed 50 percent of the taxable income from the activity. This limitation is computed without regard to the depletion allowance. Depletion percentages are found in IRC section 613(b) and Treas. Reg. section 1.613-2. The amount of the deduction allowable under percentage depletion is not limited by the basis of the property. Thus, even though the basis of the property is reduced by the amount of depletion taken, if the basis becomes zero, the depletion based on the percentage of gross income may continue. However, if cost depletion will yield a higher deduction, it must be used to calculate the amount deducted.

In using percentage depletion the concepts of gross income, taxable income, and different percentages based on the type of material extracted all come into play in the computation. The Code and Regulations are specific regarding the percentages to be used for the various types of materials which can be mined. Particular attention should be paid to the type of arrangement the taxpayer is involved in, that is, is the property being leased, are there royalties involved, are there prepayments of any kind, etc. This information should be discussed in the initial interview in order to clearly establish the nature of the mining activity.

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## **Chapter 9**

### **Sale of Claims**

Information on sales and other transfers of mining claims can be obtained from the files maintained at the Department of Natural Resources. All transfers must be recorded and a copy of the recorded document supplied to the state. These documents include quitclaim deeds, warranty deeds, and contracts of sale. They provide the names of the seller, buyer, which property is transferred, and the terms of the transfer.

The documents may not contain the true sales price. Usually the documents indicate that the property was transferred for \$10.00 and/or other good and valuable consideration. After the information derived from these documents is obtained, an RTVUE of the sellers return can be requested and examined to verify if the sale has been reported. If there is no sale apparent on the return, further research is warranted. This can be achieved by a third-party contact with the buyer. However, it may be advisable to probe further to guarantee that there is no collusion between the buyer and seller or to verify that the transaction was at arms length.

Since the purchase price or fair market value establishes the basis for the buyer in the majority of transactions, there is some incentive for the buyer to give correct information. Research of sales of property may also reveal a non-filer, so it is advisable to review both the seller's and the buyer's returns.

IRC section 617(d)(1) states:

Except as otherwise provided in this subsection, if mining property is disposed of, the lower of—

- A. the adjusted exploration expenditures with respect to such property, or
- B. the excess of
  - (i) the amount realized (in the case of a sale, exchange, or involuntary conversion), or the fair market value (in the case of any other disposition), over
  - (ii) the adjusted basis of such property,

shall be treated as ordinary income. Such gain shall be recognized notwithstanding any other provision of this subtitle.

Treas. Reg. section 1.617-4(a)(2) states:

In the case of a sale, exchange, or involuntary conversion of mining property, the gain to which [IRC] section 617(d)(1) applies is the lower of the adjusted exploration expenditures with respect to such property or the excess of the amount realized upon the disposition of the property over the adjusted basis of the property. In the case of a disposition of mining property other than by a manner described in the preceding sentence, the gain to which [IRC] section 617(d)(1) applies is the lower of the adjusted exploration expenditures with respect to such property \* \* \* on the date of disposition over the adjusted basis of the property.

IRC section 617(f)(1) states:

- \* \* \* The term "adjusted exploration expenditures" means, with respect to any property or mine—
- A. the amount of the expenditures allowed for the taxable year and all preceding taxable years as deductions under subsection (a) to the taxpayer or any other person which are properly chargeable to such property or mine and which (but for the election under subsection (a)) would be reflected in the adjusted basis of such property or mine, reduced by
  - B. for the taxable year and for each preceding taxable year, the amount (if any) by which
    - (i) the amount which would have been allowable for percentage depletion under [IRC] section 613 but for the deduction of such expenditures, exceeds
    - (ii) the amount allowable for depletion under [IRC] section 611, properly adjusted for any amounts included in gross income under subsection (b) or (c) and for any amounts of gain to which subsection (d) applied.

Because a large percentage of Schedule C gold mines never claim to reach the production stage, depletion is rarely claimed. It is unlikely that there will be any recapture of exploration and development expenses. The computation described by IRC section 617(f)(1), regarding adjusted exploration expenditures, will generally not be a consideration when determining the gain on the sale of a particular claim; however, it must be considered.

It is important to determine the amount of exploration and development expenditures previously deducted pertaining to a particular claim or group of claims. The taxpayer is required to supply copies of all returns which include exploration or development expenditures pertaining to the claim or claims sold and be able to segregate the expenses by claim. This information can then be used to determine if a gain exists.

The basis of the claim must also be determined in order to ascertain if there is any excess basis. Once determined, the formula per IRC section 617(d)(1) can be applied. Also see IRC section 1254 for property placed in service after 1986.

## Chapter 10

### Alternative Minimum Tax

For purposes of determining Alternative Minimum Taxable Income (AMTI), mining development and exploration costs paid or incurred after December 31, 1986, which were allowable as a current deduction under IRC section 616(a) or 617(a), must be capitalized and amortized ratably over the 10-year period beginning with the taxable year in which the expenditures were made. This amount is shown as an Alternative Minimum Tax adjustment item and is the difference between the recomputed Alternative Minimum Tax expense and the expense claimed on the return. This adjustment is subject to an election under IRC section 59(e) which could eliminate the adjustment for AMTI purposes.

A taxpayer pays or incurs expenditures of \$50,000 in the current taxable year for mining exploration and development costs. This amount was deducted on the Schedule C. Had the taxpayer elected to amortize the expenses over a 10-year period, the deduction in the current year would have been \$5,000. The Alternative Minimum Tax adjustment would be calculated as follows:

Current Year Deduction .....	\$50,000
Amortized Deduction .....	<u>-5,000</u>
Total Adjustment to AMT .....	\$45,000

In years 2 through 10, the unamortized amount becomes a negative adjustment in computing AMTI. That is, the unamortized amount reduces AMTI in years 2 through 10 as shown below:

Current Year Deduction .....	\$70,000
Current Year Amortized Deduction .....	-7,000
Prior Year Amortized Deduction .....	<u>-5,000</u>
Total Adjustment to AMT .....	\$58,000

Exploration and development expenditures can effect the Alternative Minimum Tax calculation. Consider also the calculation for Depreciation and Depletion. Most miners tend to have some heavy equipment with sizable basis. The recalculation of the depreciation or depletion and subsequent changes can have an effect on the Alternative Minimum Tax.

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## **Chapter 11**

### **Corporate Exploration and Development Costs**

Per IRC section 291(b), the amount allowable as a deduction for exploration expenses (IRC section 617(a)) and development expenses (IRC section 616(a)) must be reduced by 30 percent. The unallowed expenses are deducted ratably over a 60-month period beginning with the month the costs are paid or incurred. Thus the corporation must prorate the expenses in the first year. The expenses are not taken into account for purposes of determining depletion under IRC section 611. If a corporation subsequently abandons or declares the property worthless and is still carrying unamortized expenses, they may be deducted in full in the tax year the properties are deemed worthless. If there are indications that a corporation is deducting exploration or development expenses, there should be an amount for amortization somewhere on the return. If there is not, it may indicate the corporation is deducting the exploration or development expenses in full.

Per IRC section 617(h), exploration expenses incurred outside of the United States may not be deducted in full in the year paid or incurred. These expenses must either be included in the adjusted basis of the property and recovered through depletion or be deducted ratably over a 10-year period beginning in the year the expenses were paid or incurred. The same rules pertain to development expenditures per IRC section 616(d).

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## **Chapter 12**

### **Fuel Excise Tax**

Taxpayers may be eligible to claim a credit or refund of excise tax included in the price of fuel if it was for off-highway use. Publication 378 defines off-highway business use as any use of fuel in a trade or business other than as a fuel in a registered highway vehicle. A highway vehicle is "any self-propelled vehicle designed to carry a load over public highways, whether or not also designed to perform other functions."

These are vehicles not considered highway vehicles:

1. Specially designed mobile machinery for non-transportation functions. A self-propelled vehicle is not a highway vehicle if it consists of a chassis that:
  - a. has permanently mounted to it machinery or equipment used to perform certain operations if the operation of the machinery or equipment is unrelated to transportation on or off the public highways;
  - b. has been specially designed to serve only as a mobile carriage and mount for the machinery or equipment, whether or not the machinery or equipment is in operation; and
  - c. could not be used, because of its special design, as part of a vehicle designed to carry any other load without substantial structural modification.
2. Vehicles designed for off-highway transportation. A self-propelled vehicle is not a highway vehicle if:
  - a. the vehicle is designed primarily to carry a specific kind of load other than over the public highway for certain operations; and
  - b. the vehicle's use of carrying this load over public highways is substantially limited or impaired because of its design.

Fuels used in off-highway business use include fuels for stationary machines such as generators, compressors, power saws, and similar equipment; for cleaning purposes; forklift trucks and bulldozers; and cars and trucks operating off the highway in construction, mining, or timbering activities, if the vehicles are neither registered nor required to be registered.

A credit or refund is allowable only if tax has been imposed on the fuel. All gasoline and undyed (clear) diesel fuel have been taxed by the time these fuels are used at the mine. Dyed diesel fuels generally do not qualify for a credit or refund. Other types of fuel (such as propane) generally are bought tax free and are not eligible for a credit or refund.

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## **Chapter 13**

### **Inventories and Uniform Capitalization**

It is the Government's position that, under IRC section 471(a), in order to achieve the matching of income to expenses, the taxpayer is required to maintain in inventory the gold extracted from the mining operation. This is necessary in order to determine the income of the taxpayer. The matching of expense to income follows the generally accepted accounting principal. A matching principal issue generally arises when the taxpayer is in the production stage deducting expenses related to the production phase of mining with little or no income. It is not uncommon to examine a return where the taxpayer claims to be in production yet keeps no inventory. Since the gold recovered must eventually be recognized as income, inventories must be maintained.

The initial interview should establish when the taxpayer first went into production and if any gold was on hand, either obtained with the claim or produced in the exploration or development stages. The general rules of inventory apply here, that is, how much gold was on hand at the beginning of the year, how much was produced during the year, how much was sold, and how much was on hand at the end of the year. This will provide the physical amounts used in computing the cost-of-goods sold.

IRC section 471 establishes that an inventory must be kept. Treas. Reg. section 1.446-1(a)(4)(i) recognizes the need for inventories and makes reference to IRC sections 263A and 471. Treas. Reg. section 1.471-7 establishes the need for inventories of miners and manufacturers and is supported by Treas. Reg. section 1.61-3 which provides that in a manufacturing, merchandising, or mining business, gross income means total sales less cost-of-goods sold. Cost-of-goods sold should be determined in accordance with the method of accounting consistently used by the taxpayer.

Treas. Reg. section 1.471-11(a) states that:

\* \* \* In order to conform as nearly as possible to the best accounting practices and to clearly reflect income (as required by section 471 of the Code), both direct and indirect production costs must be taken into account in the computation of inventoriable costs in accordance with the "full absorption" method of inventory costing.

The Uniform Capitalization rules require the capitalization of the costs of producing real and tangible personal property. See IRC section 263A(b)(1). Mining operations involve the production of both real and tangible personal property. Until the gold is extracted from the land, the taxpayer is engaged in the production of tangible personal property. The gold is inventory in the hands of the taxpayer.

The costs that must be capitalized are: (1) the direct costs, and (2) a properly allocable share of the indirect costs that benefit or are incurred by reason of the production of the mineral property.

See IRC section 263A(2) and Treas. Reg. section 1.263A-1(e)(3)(i). Treas. Reg. section 1.263A-1(e)(ii) provides an illustrative list of indirect costs required to be capitalized. In addition, IRC section 263A(f) requires the capitalization of interest incurred with respect to the production of real property.

IRC section 263A(c)(3) provides that the general rules of IRC section 263A do not require the capitalization of any cost that is allowable as a deduction under IRC sections 263(c), 263(i), 291(b)(2), 616, or 617.

The direct and indirect costs that benefit or that are incurred by reason of the production of the mineral property must be capitalized to that property. See IRC section 263A(a)(1)(B). The direct and indirect costs that directly benefit or are incurred by reason of the gold must be included in the inventoriable cost of the gold. See IRC section 263A(a)(1)(A).

# Appendix A

## References

### Applicable Code Sections

43 CFR Ch.11 Treas. Reg. section 1865.0-5(c)	Patents and Conveyance of Land
IRC section 263A	Capitalization and inclusion in inventory costs of certain expenses
IRC section 291	Special rules relating to corporate preference items
IRC section 611	Allowance for deduction of depletion
IRC section 612	Basis for cost depletion
IRC section 613	Percentage Depletion
IRC section 614	Definition of property
IRC section 616	Development expenditures
IRC section 617	Deduction and recapture of certain mining exploration expenditures.

## Revenue Rulings by Code and Treasury Regulation Sections

<b><u>Revenue Ruling Number and Description</u></b>	<b><u>IRC Sections</u></b>	<b><u>Treasury Regulations</u></b>
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**70-287, 1970-1 C.B. 146**

**617**

**1.617-1**

Expenditures paid or incurred by a mining company in connection with core drilling to ascertain the existence of commercially marketable ore are "exploration expenditures" within the meaning of IRC section 617.

**70-288, 1970-1 C.B. 146**

**616**

**1.616-1**

Expenditures paid or incurred by a mining company in connection with core drilling to further delineate the extent and location of existing commercially marketable ore to facilitate its development are "development expenditures" within the meaning of IRC section 616.

**70-289, 1970-1 C.B. 147**

**617**

**1.617-1**

Expenditures paid or incurred by a mining company in connection with core drilling from within an existing mine to ascertain the existence of a new ore deposit are "exploration expenditures" within the meaning of IRC section 617.

**74-282, 1974-1 C.B. 150**

**167  
616**

**1.167(a)-1  
1.616-1**

Strip mining; land purchased as dumping area for overburden. The cost of a tract of land containing an exhausted open pit mine, purchased for use as a dumping area for overburden removed from an adjacent strip mine at a price greater than the going price of similar tracts containing no open pit mine, is not deductible as a development expenditure. The entire cost must be capitalized, but the portion attributable to the exhausted open pit mine is an expenditure for an asset that is depreciable over its useful life based on the capacity of the open pit and the rate of dumping overburden into it.

**74-67, 1974-1 C.B. 63**

**174  
617**

**1.174-1  
1.617-1**

Research and experiments; mining exploration; core and non-core drill holes. Expenditures paid or incurred before January 1, 1970, by a domestic corporation under a mining lease agreement involving the drilling of core and non-core holes in connection with the production of minerals are mining exploration expenditures subject to the provisions of IRC section 617. Additional expenditures required to use the drill holes for designing and testing a new mining method are research and experimental expenditures and are subject to the provisions of IRC section 174.

**75-122, 1975-1 C.B. 87**

**174  
616  
617**

**1.174-2  
1.616-1  
1.617-1**

Mining; research and experimental expenditures. A domestic mining corporation's expenditures incurred directly in the development of prototype mining equipment and in perfecting a new metallurgical process, including the cost of shipping mineral samples to the research laboratory, are research and experimental expenditures deductible under IRC section 174(a). However, the expenses for driving shafts, drifts, cross-cuts, and for other production facilities that are not limited to the research activities are mine development expenses within the meaning of IRC section 616.

**77-188, 1977-1 C.B. 76**

**165  
263  
614  
617**

**1.165-1  
1.263(a)-1  
1.614-1  
1.617-1**

Geological and geophysical exploration expenditures. The tax treatment of geological and geophysical expenditures, for the purpose of obtaining data that will serve as a basis for the acquisition or retention of a mineral property by a taxpayer engaged in exploring for minerals is discussed; I.T. 4006 superseded.

**90-20, 1990-1 C.B. 117**

**616  
617**

**1.616-1  
1.617-1**

Carrying party's costs to explore, develop, and operate a mineral property; deductibility. The taxpayer may deduct all amounts it paid or incurred prior to payout that qualify as exploration expenditures under IRC section 617(a) if it has made a proper election under that section. The taxpayer may also deduct all amounts it paid or incurred prior to payout that qualify as development expenditures under IRC section 616(a).

## Government Agencies

### FEDERAL

U.S. Department of the Interior  
Office of the Secretary  
1689 C St, Ste 100  
Anchorage AK 99501-5151  
Telephone: (907) 271-5485

U.S. Department of the Interior  
Bureau of Land Management  
Alaska State Office  
222 W 7th Ave #13  
Anchorage AK 99513-7599  
Telephone: (907) 271-3323

Arctic Office  
1150 University Ave  
Fairbanks AK 99709-3844  
Telephone: (907) 474-2302

Bureau of Mines  
Alaska Field Operations Center  
3301 C St, Ste 525  
Anchorage AK 99503-3935  
Telephone: (907) 271-2455

Mine Safety and Health Administration  
Juneau Field Office  
Federal Building  
107 W 9th  
PO Box 22049  
Juneau AK 99802  
Telephone: (907) 586-7165

### STATE (ALASKA)

Department of Natural Resources  
Division of Mining  
3601 C St, Ste 800  
PO Box 107016  
Anchorage AK 99510-7016  
Telephone: (907) 762-2165

Northern Regional Office  
3700 Airport Way  
Fairbanks AK 99709-4699  
Telephone: (907) 451-2790

Department of Environmental Conservation  
South Central Regional Office  
3601 C St, Ste 1334  
Anchorage AK 99503  
Telephone: (907) 563-6529

Northern Regional Office  
1001 Noble St, Ste 350  
Fairbanks AK 99701  
Telephone: (907) 451-2101

Alaska Minerals Commission  
PO Box 80148  
Fairbanks AK 99708  
Telephone: (907) 479-6240

## Non-Governmental Groups and Associations

Alaska Miners Association, Inc.  
Statewide Office  
501 W Northern Lights Blvd, Ste 203  
Anchorage AK 99503  
Telephone: (907) 276-0347

Fairbanks Branch  
PO Box 82524  
Fairbanks AK 99708  
Telephone: (907) 455-6739

American Institute of Professional  
Geologists  
Alaska Section  
PO Box 9-2082  
Anchorage AK 99509  
Telephone: (907) 562-3279

Society of Mining Engineers  
PO Box 625002  
Littleton CO 80162-5002  
Telephone: (303) 973-9550

Placer Miners of Alaska  
PO Box 83151  
Fairbanks AK 99708

Miners Advocacy Council  
PO Box 73824  
Fairbanks AK 99707  
Telephone: (907) 479-0471

Northwest Mining Association  
414 Peyton Bldg  
Spokane WA 99201  
Telephone: (509) 624-1158

Western Mining Council  
Kenai Peninsula Chapter  
Old Nash Rd  
Seward AK 99664  
Telephone: (907) 224-5963

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## **Appendix C**

### **Examination Checklist for Mining**

An examination checklist covering mining activity is included as part of this audit technique guide for Placer Mining to assist the user with pre-examination planning, the initial interview, and with the recognition of potential issues. This checklist is not intended to be all inclusive but only to serve as a guide.

## EXAMINATION CHECKLIST - MINING

- \_\_\_\_\_ Location of Mine
- \_\_\_\_\_ Ownership of Mine
- \_\_\_\_\_ Years of Operation
- \_\_\_\_\_ Status of Mining Activity
- \_\_\_\_\_ Type of Minerals Mined
- \_\_\_\_\_ Type of Mining / Placer
- \_\_\_\_\_ History of Activity and Operations
- \_\_\_\_\_ History of Income and/or Losses
- \_\_\_\_\_ RTVUE of Prior and Subsequent Years
- \_\_\_\_\_ Other Mines or Miners in Area
- \_\_\_\_\_ Permits Required and Obtained
- \_\_\_\_\_ Governmental Agencies Regulating the Activity
- \_\_\_\_\_ Mining Forms Filed
- \_\_\_\_\_ State or Federal Claim Number
- \_\_\_\_\_ Affidavits of Annual Labor
- \_\_\_\_\_ Mining Activity on Privately Owned Property
- \_\_\_\_\_ CTR's
- \_\_\_\_\_ Review IRP Documents
- \_\_\_\_\_ Inspect Mining Agencies' Files
- \_\_\_\_\_ Sources of Mining Income
- \_\_\_\_\_ Types of Sales
- \_\_\_\_\_ Sales of Minerals
- \_\_\_\_\_ Amount of Gold Sold and Dates of Sales
- \_\_\_\_\_ Sales of Raw or Refined Gold
- \_\_\_\_\_ Sales of Nuggets

## EXAMINATION CHECKLIST - MINING

- \_\_\_\_\_ Records Kept
- \_\_\_\_\_ Mining Partners/employees
- \_\_\_\_\_ Mining Stage for Years under Exam
- \_\_\_\_\_ Type of Mining Activity
- \_\_\_\_\_ Plan of Development for the Mine
- \_\_\_\_\_ Mining Season
- \_\_\_\_\_ Mining Equipment Used
- \_\_\_\_\_ Assets
- \_\_\_\_\_ Mining Assets
- \_\_\_\_\_ Acquisition of Assets
- \_\_\_\_\_ Bank Accounts
- \_\_\_\_\_ Source of Funds for Purchases
- \_\_\_\_\_ Loans and Collateral for Loans
- \_\_\_\_\_ Name and Location of Buyers of Inventory
- \_\_\_\_\_ Cash Transactions
- \_\_\_\_\_ Cash Hoard
- \_\_\_\_\_ Cash Expenditures
- \_\_\_\_\_ Bartering
- \_\_\_\_\_ Inventory of Gold or Other Minerals Maintained
- \_\_\_\_\_ Beginning and Ending Inventories
- \_\_\_\_\_ Payments of Labor or Expenses in Kind
- \_\_\_\_\_ Prospecting Activity
- \_\_\_\_\_ Exploration Stage and Expenses
- \_\_\_\_\_ Development Stage and Expenses
- \_\_\_\_\_ Producing Stage

## EXAMINATION CHECKLIST - MINING

- \_\_\_\_\_ Mineral Discoveries
- \_\_\_\_\_ Recapture of Exploration or Development Expenses
- \_\_\_\_\_ Claims Sold
- \_\_\_\_\_ Trade or Business versus Hobby
- \_\_\_\_\_ Activity Not for Profit Factors - IRC section 183
- \_\_\_\_\_ Economic Feasibility of the Operation
- \_\_\_\_\_ Passive Activity
- \_\_\_\_\_ Material Participation
- \_\_\_\_\_ Mining Lease or Royalty Income
- \_\_\_\_\_ Who Runs Day-to-Day Operations
- \_\_\_\_\_ Location of Residence of Owners
- \_\_\_\_\_ Hours Worked
- \_\_\_\_\_ Employees
- \_\_\_\_\_ Forms W-4, W-3, W-2, and 1099
- \_\_\_\_\_ Employment and Excise Tax Returns Filed
- \_\_\_\_\_ Employee versus Independent Contractor
- \_\_\_\_\_ Method of Depletion
- \_\_\_\_\_ Basis or Adjusted Basis of the Mineral Property
- \_\_\_\_\_ Estimated Reserves in Units
- \_\_\_\_\_ Fuel Costs and Type of Use
- \_\_\_\_\_ Environmental Permits and Restrictions

## **Appendix D**

### **Glossary of Mining Definitions**

**ABANDONED** Given up with the intent of never again claiming a right or interest in the mineral interest.

**ACRE** A measure of land, 160 square rods (4,840 square yards, 43,560 square feet).

**ACTIVE PARTICIPATION** Involvement in a rental real estate activity making management decisions. Requires no specific number of hours.

**ACTIVITY** A trade or business. Two or more operations within a trade or business could be deemed separate activities.

**ADIT** A nearly horizontal gallery or passage driven from the surface of the ground to the ore body. The term "tunnel" is frequently used in place of adit, but technically a tunnel is open to the surface on both ends.

**ADJUSTED GROSS INCOME** For purposes of IRC section 469(i)(3)(E), adjusted gross income shall be determined without regard to:

- social security and tier 1 railroad benefits included in income;
- the amount of income from savings bonds used for higher education fees excluded from income;
- the deduction allowed for qualified retirement contributions, and
- any passive activity loss or any loss from rental real estate activities allowed under IRC section 469(c)(7).

**AGGREGATE** Natural particles, crushed and broken rock, and man-made materials that are graded by size into categories to meet specifications for particular construction uses.

**AGGREGATION** Combining two or more passive activities in which the taxpayer works 100 to 500 hours.

**ALLUVIAL** Adjective used to identify particular types of, or minerals found associated with, deposits made by flowing water as, alluvial fan, alluvial terrace, alluvial told, alluvial tin.

**ALLUVIAL DEPOSIT** Generally pertains to loose gravel, soil, or mud which have been transported and deposited by flowing water.

**ALLUVIUM** Clay silt, sand, gravel, or other rock materials transported by flowing water and deposited in comparatively recent geologic time as sorted or semi-sorted sediments in river beds,

estuaries, and floor plains, in lakes, on shores and in fans at the base of mountain slopes. The term is not applied to subaqueous sediments deposited in seas or lakes or to non-sorted sediments carried or deposited by glaciers.

**ANALYSIS** A separation of compound substances by chemical means.

**ANGLE OF REST** The maximum slope at which a heap of any loose or fragmented solid material will stand without sliding or will come to rest when poured or dumped in a pile or on a slope.

**ANGLE OF SLIDE** The slope, measured in degrees of deviation from the horizontal, on which loose or fragmented solid materials will start to slide; it is a slightly greater angle than the angle of rest.

**ARMOR ROCK** Stone resulting from blasting, cutting, or other methods to obtain pieces heavy enough (generally 1 to 3 tons) to require handling two individual pieces by mechanical means. Used to protect beds, bank, shores, and embankments against intense erosion and scour by running water, tidal currents, and wave action.

**ASPHALT SAND AND GRAVEL** Sized and broken sand and gravel mixed with asphalt in batch plants to form asphalt concrete and road pavements. Dry, clean, fractured particle faces adhere well to bitumen and pack (interlock) efficiently to provide increased concrete and pavement strength.

**ASSAY** The determination of the valuable minerals in a sample. A wet assay is determined by the use of chemicals. A fire assay is determined by both chemicals and fire. Gold and silver are usually assayed by fire.

**AVULSION** Removal of land from one owner to another when a stream suddenly changes its channel.

**BANK** A steeply sloping mass of any earthy or rock material rising above the digging level from which the soil or rock is to be dug from its natural or blasted position in an open pit mine or quarry.

**BANK HEIGHT** The vertical height of a bank as measured between its highest point or crest and its toe at the digging level or bench.

**BANK SLOPE** The angle, measured in degrees of deviation from the horizontal, at which the earthy or rock material will stand in an excavated cut in an open-pit mine or quarry.

**BARITE** Barium sulfate, which has a specific gravity of 4.3 to 4.6.

**BEDROCK** Any solid rock underlying gold-bearing gravels.

**BENCH** A former wave-cut shore of a sea or lake or flood plain of a river.

**BLACK SAND** Grains of heavy, dark minerals such as magnetite, limonite, chromite, etc., found in streams which commonly collect in sluice boxes and which may carry gold and platinum.

**BULK** Not divided into parts.

**BY-PRODUCTS** Placer metals, garnet, limonite, chromite, rare-earth elements, zircon, cassiterite, and other minerals concentrated during the mechanical processing of natural aggregates.

**CHUTE** An opening in the ground where ore is allowed to pass from one level to another. It is the structure built to load cars from a stope.

**CLAIM** A land area claimed by a prospector and marked out by stakes.

**CLOSELY HELD CORPORATION** A corporation with five or fewer shareholders owning more than 50 percent in value of the stock at any time during the last half of the taxable year.

**COLOR** A term referring to small grains or flakes of gold.

**COMMODITIES** Economic goods, for example, products of agriculture or mining.

**CONTRACTOR** One that contracts to perform work or provide supplies on a large scale.

**CONTOUR** Lines connecting points of equal elevation on a contour map.

**CRUSHER** A machine used to squeeze or force by pressure so as to alter or destroy structure.

**DEMARCATÉ** To mark the limits of.

**DEPLETION** The process by which the cost or other basis of a natural resource is recovered upon extraction and sale of the resource. For tax purposes, the two ways to determine the depletion allowance are the cost and percentage methods.

**DEPOSIT** Something laid down; such as matter deposited by a natural process.

**DIP** The maximum angle of inclination downward that a vein or bed makes with a horizontal plane.

**DYNAMITE** An explosive mixture of glycerin, sodium or ammonium nitrate, and a filler of combustible pulp such as a wood meal.

**ELECTRIC CAP** A small metallic cap containing fulminating powder which is detonated by an electric current.

**EMPLOYEE** One employed by another usually for wages or salary and in a position below the executive level.

**ENTITY** Any corporation, partnership, trust, association, or estate formed for carrying on a business activity.

**EXCAVATION** A cavity formed by cutting, digging, or scooping.

**EXPOSURE** Any part of a vein or rock outcrop that can easily be seen.

**FAULT** A fracture in the earth's crust accompanied by a displacement of one side of the fracture with respect to the other and in a direction parallel to the fracture.

**FISSURE** An opening or crack in the rock. A fissure vein is a fissure filled with mineral matter.

**FLOAT** The loose and scattered pieces of ore which have been broken off from an outcrop.

**FOOTWALL** The bottom or lower enclosing wall of a vein.

**FUSE** A tube or cord filled or impregnated with combustible matter for igniting an explosive charge after a predetermined interval, as in blasting.

**GRANTEE** A person to whom real estate is conveyed; the buyer.

**GRANTOR** A person who conveys real estate by deed; the seller.

**HANGING WALL** The down thrown side of fault block in normal faulting.

**HEAD FRAME** A structure erected over a shaft to support the sheave wheel for hoisting purposes.

**HEADING** Any part of a mine where work is under way. Usually confined to development workings only.

**HECTARE** A metric measure of surface area (2.471 acres).

**HEDGING** Entering into the purchase of commodity futures contracts to reduce the risk of an unfavorable price fluctuation.

**HIGH GRADING** Stealing of high grade ore or nuggets from workings of a hard rock or placer mine by employees or others.

**HORIZONTAL** Parallel to, in the plane of, or operating in a plane parallel to the horizon or to a base line.

**IGNEOUS ROCK** Rock formed from molten lava.

**K-1** The form attached to Forms 1065, 1120-S, and 1041 returns which reports the flow-through of income and losses to an investor's individual return.

**KILOGRAM (kg)** The basic metric unit of mass and weight equal to the mass of a platinum-iridium cylinder kept at the International Bureau of Weights and Measures near Paris and nearly equal to 1000 cubic centimeters of water at the temperature of its maximum density.

**KILOMETER** 1,000 meters; approximate equivalent equals 0.62 mile.

**LATERAL** A horizontal mine working. A drift in the footwall of a vein is often called a lateral.

**LEASE** A contract by which the owner of operating rights assigns all or a portion of such rights to another person whether for no immediate consideration or for cash and its equivalent, and retains a continuing nonoperating interest in production.

**LESSEE** A person who obtains a lease on mining land.

**LESSOR** The grantor of a lease.

**LEVEL** All the connected horizontal mine openings at a certain elevation.

**LIMITED PARTNER** An investor in a partnership whose personal liability is limited. Presumed to be not materially participating (passive) according to the passive activity rules.

**LOCATING** The marking of the boundaries and staking of a mining claim.

**LODE** A tabular deposit between definite walls.

**LONG TOM** An inclined trough used to concentrate gold from auriferous earth.

**MATERIAL PARTICIPATION** Regular, substantial, and continuous involvement in a business. Allows losses to be deducted in full and not limited by the passive activity rules.

**MILL** A machine for crushing or comminuting.

**MILLING ORE** Ore that must be concentrated at or near the mine before it is shipped.

**MINE** A pit or excavation in the earth from which mineral substances are taken.

**MINERAL** A solid homogenous crystalline chemical element or compound that results from the inorganic processes of nature.

**MODIFIED ADJUSTED GROSS INCOME (AGI)** See definition for Adjusted Gross Income.

**MUCK** To move or load muck.

**MUCK** Broken underground rock removed in the process of excavating or mining.

**MUCKER** A shoveler, or one who handles muck.

**NITRO** Short for nitroglycerin, which is any nitrate of glycerol, a colorless, heavy, oily, explosive liquid used in making dynamite.

**NONPASSIVE ACTIVITY** A trade or business in which the taxpayer materially participates, that is, on a regular, continuous, and substantial basis. Losses can be deducted in full.

**NUGGET** A piece of gold of any shape or size larger than a flake, usually rounded by stream or water action.

**OPTION** The right to purchase at a stated price.

**ORE** A source from which valuable matter is extracted.

**ORE** A mineral aggregate containing a valuable constituent (as metal) for which it is mined and worked for a profit.

**ORE BODY** The part of a vein that carries ore. Generally, all parts of a vein are not ore. Ore shoot has the same meaning.

**OUTCROP** The edge or surface of a mineral deposit or sedimentary bed which appears on the surface.

**OVERBURDEN** The valueless material overlaying the pay zone in a placer deposit or the waste or valueless material of a solid outcrop.

**OXIDE** A compound of a metal and oxygen.

**OZ.** Ounce.

**PASSIVE ACTIVITY** Any activity which involves the conduct of a trade or business which the taxpayer does not materially participate.

**PASSIVE INCOME** Income from a passive activity.

**PASSIVE LOSS** Loss from a passive activity.

**PATENT** Conveyance of title to government land.

**PAY** Ore or a natural situation that yields metal and/or gold in profitable amounts.

**PIT** A hole, shaft, or cavity in the ground.

**PLACER** An alluvial or glacial deposit containing particles of valuable mineral-bearing gravel or gold.

**PLANE** An even surface. A horizontal plane is a flat, even, level surface.

**PORTFOLIO INCOME** All gross income, other than income derived in the ordinary course of a trade or business, that is attributable to interest, dividends, royalties, and gains from the sale of stocks and bonds as well as other investment activities.

**PRECIOUS** Of great value or high price.

**PRECIPICE** A very steep or overhanging place.

**PROXIMITY** The quality or state of being proximate.

**QUADRANGLE** A tract of the land in the U.S. Governmental Survey System measuring 24 miles on each side of the square, sometimes referred to as a "check".

**QUARRY** An open excavation usually for obtaining building stone, slate, or limestone.

**QUITCLAIM DEED** A deed given when the grantee already has, or claims, complete or partial title to the premises and the grantor has a possible interest that otherwise would constitute a cloud upon the title.

**RAISE** An excavation of restricted cross-section, driven upwards either vertically or at an angle from a level in the mine.

**RAKE** The trend of the ore body within the vein.

**RECHARACTERIZATION RULES** Rules which recharacterize passive income as nonpassive.

**REFINE** To reduce to a pure state.

**RIFFLES** Obstacles placed along the bottom of a sluice or rocker that form pockets to catch gold by concentrating heavier materials.

**RIPARIAN** Pertaining to the banks of a river, stream, waterway, and so forth.

**RIPARIAN OWNER** One who owns lands bounding upon a river or water course.

**RIPRAP ROCK** Selected hard, angular, quarried stone generally weighing between 25 and 5,400 pounds individually and placed to protect beds, banks, shores, and embankments against wave action, tidal forces, and stream currents.

**ROCK** Naturally occurring, consolidated materials composed of one or more minerals of the earth's crust. Any hard, consolidated materials derived from the earth and usually of relatively small size.

**ROCKER** A mechanical panning device comprised of three parts: a body or sluice box, a screen, and an apron.

**SAND** Particles of rock that pass a No.4 (4.75 mm) U.S. Standard sieve and are retained on a No. 200 (.075 mm) U.S. Standard sieve.

**SECTION** A section of land established by government survey and containing 640 acres or 1 square mile.

**SELF-RENTED PROPERTY** Personal or real property rented to an entity which the taxpayer personally controls. Stated in different terms, property rented to a nonpassive activity of the taxpayer.

**SHAFT** A vertical or inclined opening of a uniform and limited cross section made for finding or mining ore, raising water, or ventilating underground workings (as in a cave).

**SIGNIFICANT PARTICIPATION** An individual is treated as significantly participating in an activity if the individual participates in the activity for more than 100 hours during such taxable year and in which the taxpayer did not materially participate under any of the material participation tests, other than this test.

**SLIP** A small fault.

**SLUICE BOX** A sloping trough, having riffles on the bottom, through which gravel and wash from placer mining operations pass to catch and save the gold and other valuable minerals.

**SPECIAL WARRANTY DEED** A deed wherein the grantor limits his liability to the grantee to anyone claiming, by, from, through, or under him.

**SPECIFIC GRAVITY** The ratio of the weight of any substance to the weight of an equal volume of water.

**STONE** Natural rock material of adequate integrity and quality that can be quarried and then sawed, cut, split, or otherwise sized, shaped, or finished for specific purposes. Natural building stone includes granitic rocks, greenstones, limestones, marbles, massive serpentinite (antigorite), and sandstones.

**STOPE** A step-like excavation underground for the removal of ore. It is formed as the ore is mined in successive layers.

**STRIKE** The bearing of a horizontal line in the plane of a vein, bed, or fault in respect to the cardinal points of the compass.

**STRIPPING** Removal of the overburden from a placer deposit or the barren outcrop from an ore deposit.

**STULL** A timber used to support loose rocks or slabs. It may also be used to support a platform in a working area.

**SUMP** The lowest part of a mine shaft into which water drains.

**SURVEY** The process by which a parcel of land is measured and its area ascertained.

**SUSPENDED LOSSES** Passive losses which are carried forward indefinitely until the taxpayer has passive income or there is an entire disposition of the activity.

**TAILINGS** Residue separated in the preparation of various products (as grains or ores).

**TIERED ENTITIES** Partnerships or trusts or corporations invested in other partnerships or trusts or corporations.

**TOPOGRAPHY** The contour and slope of land, hills, valleys, streams, etc.

**TRAVERTINE** A variety of layered or banded, porous to dense, crystalline to microcrystalline limestone that is deposited by springs, seeps, or running water.

**TREND** The general direction or bearing of a vein, fault, or rock outcrop.

**UNDERCURRENT** A wide, flat sluice box placed beneath the main sluice box used to save fine gold.

**VALUE** Refers to the mineral substance sought. In the case of gold, the term is synonymous with color.

**VEIN** A well-defined, tabular, mineralized zone which may or may not have valuable ore bodies.

**VERTICAL** Perpendicular to the plane of the horizon or to a primary axis.

**WALL** The waste or country rock on either side of a vein.

**WARRANTY DEED** One that contains a covenant that the grantor will protect the grantee against any claimant.

**WASTE** Barren rock or mineralized material which does not have enough value to be classified as an ore.

**WELL** An issue of water from the earth. A shaft or hole sunk to obtain oil, brine, or gas.

**WINZE** A steeply inclined passageway connecting a mine working place with a lower one.

**WORKING FACE** Any portion of the mine where work is under way, such as the face of a drift or the face of a raise.

