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Person To Contact:
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Telephone Number:

Refer Reply To:
CC:PSI:B01
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Date:
April 18, 2013

LEGEND

X =

Y =

State =

b =

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Dear :

This letter responds to a letter from X's authorized representatives dated November 20, 2012, submitted on behalf of X, requesting a ruling concerning the qualifying income exception to the publicly traded partnership rules of § 7704 of the Internal Revenue Code (the Code).

FACTS

According to the information submitted and representations made, X is a limited liability company organized under the laws of State. X intends to contribute all or a portion of its assets to a new limited partnership, Y. After the consummation of an initial public offering, interests in Y are expected to be listed and traded on a nationally recognized exchange. Thus, Y will be a publicly traded partnership within the meaning of § 7704(b). Y's employer identification number will be applied for at the time of its organization.

To start, Y will own and develop kaolin reserves. Y will mine sedimentary kaolin from its deposits via a third party contractor. It will then process the kaolin into ceramic pellets. Finally, it will market the pellets for use as proppants by oilfield service companies in hydraulic fracturing operations.

Ceramic pellets are well suited to serve as proppants in the fracturing of oil and gas deposits. Fracturing is a technique in which fluids, primarily water, are pumped into an oil or gas well as high pressure to fracture the geologic formations and open up pathways for the oil or gas to flow to the well. The wings of the fracture extend away from the wellbore in opposing directions according to the natural stresses within the particular formation. The pellets, serving as a propping agent, or proppant, will be mixed with fluid and pumped into the fractures to keep them from closing when the pumping pressure is released. Fracturing allows oil and natural gas that could not otherwise be produced in an economical manner to move freely through the rock pores to a producing well that can bring the oil and gas to the surface.

Lightweight ceramic proppants, such as the ones that Y will produce, have similar or slightly higher density than sand proppants, but greater strength and flow capacity. The increased strength of ceramic proppants allows better resistance to down-well closure stresses. Y's lightweight ceramic proppants will primarily be utilized in wells with down-well closure stresses of b to c psi. Under this intense pressure, typical sand-based proppants are crushed or dislodged, causing rock fractures to become less productive or close altogether.

As part of a contemplated expansion of its business, Y may also utilize bauxite ore, acquired from third parties, for the base mineral of the ceramic proppant. Bauxite-based ceramic proppants are well suited for use in ultra-high-pressure hydraulic fracturing operations, such as offshore oil and gas wells.

LAW AND ANALYSIS

Section 7704(a) provides that, except as provided in § 7704(c), a publicly traded partnership shall be treated as a corporation.

Section 7704(b) provides that, for the purposes of § 7704, the term "publicly traded partnership" means any partnership if (1) interests in the partnership are traded on an established securities market, or (2) interests in the partnership are readily tradable on a secondary market (or substantial equivalent thereof).

Section 7704(c)(1) provides that § 7701(a) shall not apply to any publicly traded partnership for any taxable year if such partnership met the gross income requirements of § 7704(c)(2) for such taxable year and each preceding taxable year beginning after December 31, 1987, during which the partnership (or any predecessor) was in existence. Section 7704(c)(2) explains that a partnership meets the gross income requirements of § 7704(c)(2) for any taxable year if 90 percent or more of the gross income of such partnership for such taxable year is qualifying income.

Section 7704(d)(1)(E) provides that the term "qualifying income" means income or gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resource (including fertilizer, geothermal energy, or timber).

Based solely on the facts submitted and representations made, we conclude that income derived by Y from the mining, processing, and marketing of sedimentary kaolin and bauxite for sale to oilfield service companies for use as a ceramic proppant in the production of crude oil and natural gas constitutes qualifying income within the meaning of § 7704(d)(1)(E).

Except as expressly provided herein, we express or imply no opinion concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed as to whether Y meets the 90 percent gross income requirement of § 7704(c) in any taxable year.

This ruling is directed only to the taxpayer requesting it. However, in the event of a technical termination of Y under § 708(b)(1)(B), the resulting partnership may continue to rely on this ruling in determining its qualifying income under § 7704(d)(1)(E). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to X's authorized representative.

Sincerely,

David R. Haglund
David R. Haglund
Chief, Branch 1
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter
Copy of this letter for section 6110 purposes

cc: