



AMERICAN COUNCIL OF ENGINEERING COMPANIES

August 31, 2005

Attn: Comments on the *Tax Technical Corrections Act of 2005*  
U.S. Senate Committee on Finance  
219 Dirksen Senate Office Building  
Washington, D.C. 20515

**Re:** The Tax Technical Corrections Act of 2005

The American Council of Engineering Companies (ACEC) submits these comments in regard to the Tax Technical Corrections Act of 2005. ACEC is the business association of America's engineering industry, representing approximately 5,500 independent engineering companies throughout the United States engaged in the development of America's transportation, environmental, industrial, and other infrastructure. ACEC thanks the Ways and Means Committee for their work to ensure that the implementation of the American Jobs Creation Act (P.L. 108- 357) is carried out smoothly and to solicit the input of the regulated community on this process.

### **Definition of Engineering**

The proposed definition in the Notice for "engineering and architectural services" is consistent with IRS Regulation Section 1.924(a)-1T(e)(5) and -1T(e)(6):

*(b) Engineering services. Engineering services in connection with any construction project include any professional services requiring engineering education, training, and experience and the application of special knowledge of the mathematical, physical, or engineering sciences to those professional services such as consultation, investigation, evaluation, planning, design, or*

*responsible supervision of construction for the purpose of assuring compliance with plans, specifications, and design.*

While this definition is consistent with previous relevant IRS definitions, it could be interpreted to exclude engineering services that are related to a construction project, but occur after construction is completed. ACEC suggests Congress include in the Tax Technical Correction Act language to amend the definition to:

*(b) Engineering services. Engineering services in connection with any construction project include any professional services requiring engineering education, training, and experience and the application of special knowledge of the mathematical, physical, or engineering sciences to those professional services such as consultation, investigation, evaluation, planning, design, ~~or~~ responsible supervision of construction for the purpose of assuring compliance with plans, specifications, and design **or the inspection of the constructed facilities after construction.***

This amended definition would clarify that projects like bridge inspections and other post-construction engineering studies, evaluations and audits would qualify for the deduction. These engineering services are crucial to ensuring the safety of construction projects.

### **Accounting Burden**

Engineering firms undertake an enormous volume of projects in a given year. For our larger firms, the contracts associated with engineering and construction/construction management annually number in the thousands, and the projects associated with the those contracts would be more than ten-thousand for any given year. Additionally, projects are further broken down into task and sub-tasks, significantly expanding the level of detail. These facts are consistent throughout the architectural and engineering industry.

The IRS Notice on Section 199 requires that the determination of Qualified Production Activities Income be:

*“On an item-by-item basis (and not, for example, on a division-by-division, product line-by-product line, or transaction-by-transaction basis) and is the sum of QPAI derived by the taxpayer from each item.”*

The Notice also states that (**emphasis added**):

*“The Engineering or architectural services must relate to real property, must be performed in the United States, and the taxpayer providing these services must be able to **substantiate** that the services relate to a construction project within the United States.”*

ACEC believes that the rigorous requirements for determining QPAI “*on an item-by-item basis*” will impose a substantial and unreasonable burden to taxpayers which will overwhelm tax departments and result in firms not taking advantage of the tax treatment that they are entitled to. The “item-by-item basis” could result in each invoice and job scope needing to be reviewed in order to determine whether the Section 199 requirements are met.

ACEC requests that Congress include in the Tax Technical Corrections Act an instruction to the IRS and the Treasury to examine methods that would reduce the accounting burden for engineering firms who are affected by the item-by-item provision. These methods should include the allowance of statistical sampling as already provided in Rev Procs 2004-29, 2004-34 and Rev Proc 81-70.

### **Real Property Restriction**

ACEC is concerned about troubling and restrictive language that requires that “engineering or architectural services must relate to real property...” which was contained in the Tax Technical Corrections Act and also in Treasury Notice 2005-14, the Interim Guidance on Income Attributable to Domestic Production Activities [*hereinafter*, Notice]. The Notice defined real property as “residential and commercial buildings (including items that are structural components of such buildings), inherently permanent structures other than tangible property in the nature of machinery, inherently permanent land improvements, and infrastructure.” Also, the Notice defines construction to mean “the construction of real property ....” Section 4.04(11). The Notice also states that “tangible personal property (as defined under section 4.04(8)(b)) (for

example, appliances, furniture and fixtures) that is sold as part of a construction project is not considered real property for this purpose.”

ACEC recommends that the provision requiring that engineering services “must relate to real property” in order to qualify for the tax relief included in the American Jobs Creation Act (P.L. 108-357) should be removed from the Tax Technical Corrections Act and that Congress should instruct the Treasury Department to provide a more inclusive definition for “real property” as related to construction projects. This language, as written, will result in the non-applicability of the provision to engineering work that Congress intended the provision to apply to and will create an undue compliance burden for engineering firms.

The real property restriction in its current form will create difficulties for engineering firms in determining whether they qualify for the benefit. In many cases, an engineering and/or architectural design firm or a construction firm may design or build a project that contains both real and personal property elements. With the many projects that engineering firms undertake each year, the task of determining what percentage of the project fee related to real property and what percentage related to personal property will be extremely complex and will require the firm to expend considerable resources. This may result in many firms not taking advantage of the tax treatment that Congress intended.

In addition to the compliance aspect, certain work that qualified for the export tax deduction under Domestic International Sales Corporation (DISC), the Foreign Sales Corporation (FSC), and the Extraterritorial Income (ETI) would not qualify for the Domestic Production Activities benefit if the proposed real property restriction is included in the final regulation. For example, the design and construction of clean rooms, power plants, steam generating units, and oil refineries would not benefit for the deduction, which was not Congress’ intent. Congress intended for this legislation to provide much needed tax relief and to ensure that U.S. business can remain competitive in the global marketplace. The restriction for real property would not fulfill those goals.

ACEC strongly recommends the current language relating to real property should be removed from the Tax Technical Corrections Act and that Congress should instruct the Treasury

Department to reconsider their definition of “real property” as related to construction projects in any regulations that are promulgated.

ACEC and our member organizations stand ready to provide you with any additional information necessary to help you implement the American Jobs Creation Act. In addition, we realize that other issues of concern may arise during the implementation of H.R. 4520 and look forward to continuing this dialogue as needed.

Thank you in advance for your consideration of these matters. Please do not hesitate to contact us with any questions.

Sincerely,

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