

June 3, 2005

Tax Break For The Construction Industry

The American Jobs Creation Act of 2004 established a new Internal Revenue Code section 199, which permits qualifying taxpayers to claim a deduction from taxable income attributable to certain domestic production activities, including construction performed in the United States. In general, for 2005 new section 199 provides for a 3% deduction, increasing to 6% for tax years beginning in 2007, 2008, and 2009, and 9% for tax years beginning in 2010 and thereafter.

Construction Services

To qualify, the taxpayer's construction activities must:

- **Relate to real property**, such as residential and commercial buildings (including the structural components of such buildings); inherently permanent structures other than tangible personal property in the nature of machinery; inherently permanent land improvements; and infrastructure (roads, power lines, water systems, railroad spurs, communications facilities, sewers, sidewalks, cable, and wiring).
- **Be performed by a taxpayer engaged in a construction trade or business**, such as land development, land subdivision, general contracting, infrastructure construction, and certain specialty subcontracting trades.
- **Be performed in connection with "construction activities,"** such as a project to erect or substantially renovate real property. Tangential services, such as hauling trash and debris and delivering materials, do not qualify as a construction activity unless the taxpayer performing construction is also performing those tangential services in connection with the construction project. Activities, such as improving land (for example, grading and landscaping) and painting, will constitute construction only if those activities are performed in connection with other activities (whether or not by the same taxpayer) that constitute the erection or substantial renovation of real property.

CAUTION: the deduction only applies to gross receipts derived from (1) a sale, exchange, or other disposition of the property constructed or (2) the performance of construction services. Lease or rental income is excluded.

Engineering and Architectural Services

Engineering or architectural services performed in the United States for construction projects in the United States may also qualify for the deduction.

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.

Architectural services in connection with any construction project include the offering or furnishing of any professional services, such as consultation, planning, aesthetic and structural design, and drawings and specifications, or responsible supervision of construction (for the purpose of assuring compliance with plans, specifications, and design) or erection, in connection with any construction project.

If you have any questions concerning section 199 and whether it applies to you or your company, please contact the Seyfarth Shaw LLP Construction or Tax attorney with whom you work or any construction or tax attorney on the website at www.seyfarth.com.



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