CC:PA:LPD:PR (REG-132634-14)
Room 5203
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Comments on REG-132634-14, Qualifying Income from Activities of Publicly Traded Partnerships With Respect to Minerals or Natural Resources

Vulcan Materials Company ("***Vulcan***" or "***we***") is pleased to submit comments to the Internal Revenue Service regarding the proposed Treasury regulations (REG 132634-14) (the "***Proposed Regulations***") regarding "qualifying income" under section 7704(d)(1)(E)[1] of the Internal Revenue Code of 1986, as amended (the "***Code***").

I. Executive Summary

Vulcan is the nation's largest producer of construction aggregates (crushed stone, gravel, and sand) and a major producer of aggregates-based construction materials, primarily asphalt mix and ready-mixed concrete. We believe that our asphalt mix activities and our ready-mixed concrete activities produce qualifying income from the "processing" of natural resources under section 7704.

However, the Proposed Regulations limit qualifying processing activities to those that "purify, separate or eliminate impurities" by conflating "processing" and "refining". In so doing, the Proposed Regulations effectively limit qualified processing activities to the "mining processes" that are a part of "mining" under section 613(c)(2) and Treas. Reg. § 1.613-4(f). Such construction is (a) contrary to the plain language of section 7704, (b) ignores the non-mining processes defined in Treas. Reg. § 1.613-4(g)(1), and (c) violates rules of statutory construction. Instead, the final regulations should conform to the construction of section 7704, with "processing" a distinct qualifying activity, and define processing to include all of the non-mining processes described in Treas. Reg. § 1.613-4(g)(1).[2]

The Proposed Regulations also require that "the partnership's position that an activity is processing or refining be consistent with the Modified Accelerated Cost Recovery System ("***MACRS***") class life" for the assets used in that activity. The MACRS classifications were never intended, and are not suited, to be used to determine section 7704 qualifying activities. The final regulations should eliminate this requirement.

[1] For simplicity, throughout the remainder of the document, we use "section 7704" to refer to section 7704(d)(1)(E).
[2] We note that the list of processes in Treas. Reg. § 1.613-4(g)(1) does not include the manufacturing processes listed in Treas. Reg. § 1.613-4(g)(4), which describes "[t]he production, packaging, distribution, and marketing of manufactured products, and the processes necessary or incidental thereto[.]"

Finally, the Proposed Regulations exclude from qualifying activities "activities that cause a substantial physical or chemical change in a mineral or natural resource, or that transform the extracted mineral or natural resource into new or different mineral products, including manufactured products" (the "***Transformation Exclusions***"). There is no support in section 7704, Treas. Reg. § 1.613-4, or the legislative history for any such limitations, and they should be eliminated from the final regulations.

II. Vulcan's Business Summary

Vulcan (NYSE: VMC) is the nation's largest producer of construction aggregates (crushed stone, gravel, and sand) and a major producer of aggregates-based construction materials, primarily asphalt mix ("***AM***") and ready-mixed concrete ("***RMC***"). As of December 31, 2014, we operated 315 aggregates facilities, 38 AM plants, and 65 RMC plants across 20 states. In 2014, revenue was approximately $3.0 billion, and year-end assets were approximately $8.0 billion.

We mine aggregates from natural mineral deposits, such as granite, limestone, dolomite, and trap rock. The mined aggregates are either sold for use in a wide variety of construction applications (including the production of AM and RMC), or used in our own production of AM and RMC (both of which are then sold to contractors for use in finished products such as road pavement). Our aggregates mining activities produce qualifying income under section 7704, and we believe that our AM and RMC activities do so as well.

AM and RMC are composite materials[3] made via similar processes. In each process, aggregates are blended with a matrix material that binds the aggregates, and each input material remains distinct in the composite material. [4] AM's matrix material is liquid asphalt[5], and RMC's matrix material is cement (activated by water)[6]. In each of AM and RMC, minor amounts of performance additives (which, for example, accelerate or retard hardening) may be added.

In both cases, the activities are "non-mining processes" under Treas. Reg. § 1.613-4(g)(1) since we are "blending" natural resources "with other materials". As such, our AM and RMC activities should be qualifying activities under section 7704.[7]

III. Analysis of the Proposed Regulations

A. *The Definition of "Processing or Refining" Is Inconsistent With the Plain Language of Section 7704, Ignores the Non-Mining Definitions in Treas. Reg. § 1.613-4(g)(1), and Violates Rules of Statutory Construction.*

Section 7704 defines "qualifying income" as:

> Income and 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…

[3] Composite materials are materials made from two or more constituent materials which remain separate and distinct within the finished composite.
[4] See Exhibit 1.
[5] AM is generally, by weight, approximately 95% aggregates and 5% liquid asphalt.
[6] RMC is generally, by weight, approximately 78% aggregates and 22% 'paste' (cement and water).
[7] We note that the production of AM and RMC do not result in physical or chemical changes to the natural resources.

"Processing" and "Refining" are Separate Activities Under Section 7704

The preamble to the Proposed Regulations (the "***Preamble***") and Prop. Reg. § 1.7704-4(c)(1) reference the "exploration, development, mining or production, processing, refining, transportation, or marketing of any mineral or natural resource." Mirroring the construction in section 7704, each qualifying activity is separated by a comma, with the exception of "mining" and "production" which are separated by the word "or."[8] The Proposed Regulations thereafter, inexplicably, conflate the separate activities of "processing" and "refining" into a single category titled "processing or refining". Specifically, Prop. Reg. § 1.7704-4(c)(5) states that "processing or refining" is an activity "done to purify, separate or eliminate impurities."

The separation by commas in section 7704 of the qualifying activities other than "mining" and "production" indicates that such activities are separate and distinct qualifying activities. The conflation of "processing" and "refining" into "processing or refining" in Prop. Reg. § 1.7704-4(c)(5) is (a) arbitrary and inconsistent with the treatment accorded the other qualifying activities listed in section 7704,[9] (b) inconsistent with Prop. Reg. § 1.7704-4(c)(1), and (c) in contrast with the plain language of section 7704.

The Proposed Regulations Write "Processing" Out of Section 7704

As mentioned above, Prop. Reg. § 1.7704-4(c)(5) states that "processing or refining" is an activity "done to purify, separate or eliminate impurities." This language is drawn directly from the definition of "refining" in Treas. Reg. § 1.613-4(g)(6)(iii)[10], and ignores Treas. Reg. §1.613-4(g)(1).

Treas. Reg. § 1.613-4 divides "processes" into "mining processes" described in Treas. Reg. 1.613-4(f) and "non-mining processes."[11] Section 613(c)(2) and Treas. Reg. § 1.613-4(f)(1) define "mining" to include "mining processes" (which have been part of the definition of "mining" since 1943[12]). Treas. Reg. § 1.613-4(g)(1) identifies the non-mining processes (which are distinct from mining processes) to include the following processes: "electrolytic deposition, roasting, calcining, thermal or electric smelting, refining, polishing, fine pulverization, blending with other materials, treatment effecting a chemical change, thermal action, and molding or shaping."

Prop. Reg. § 1.7704-4(c)(5) effectively writes the word "processing" out of section 7704. In so doing, the Proposed Regulations limit qualifying processing activities to those that constitute either (i) mining under Treas. Reg. § 1.613-4(f)(1)(ii)[13] or (ii) refining under Treas. Reg. § 1.613-4(g)(6)(iii).

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[8] The separation of "mining" and "production" by the word "or" makes sense, because "mining" and "production" describe the same qualifying activity in different industries …specifically, ores and minerals are "mined" while oil and gas are "produced."

[9] Each of the other qualifying activities separated by a comma in section 7704 is treated as a separate activity in Prop. Reg. § 1.7704-4(c).

[10] Treas. Reg. § 1.613-4(g)(6)(iii) states that refining refers to processes that eliminate impurities or foreign matter from partially processed ores and minerals.

[11] *See* Treas. Reg. § 1.613-4(f)(2)-(6), -4(g).

[12] *See* Revenue Act of 1943, § 124 ("(c) Definition of gross income from the property. Section 114(b)(4) is amended by adding at the end thereof the following: (B) Definition of gross income from property. As used in this paragraph the term 'gross income from the property' means the gross income from mining. *The term 'mining', as used herein, shall be considered to include* not merely the extraction of the ores or minerals from the ground but also *the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products*....") Emphasis added. The Act then described mining processes and non-mining processes.

[13] In addition, the proposed regulations erroneously define mining of ores and minerals to mean only activities "performed to extract minerals or natural resources from the ground" and exclude the mining processes that are part of the definition of mining in Treas. Reg. § 1.613-4(f)(1).

The Proposed Regulations Violate the Rules of Statutory Construction

By effectively eliminating the word "processing" from section 7704, the Proposed Regulations also violate at least two rules of statutory construction affirmed by the Supreme Court.

Under the rule against surplusage, courts must "give effect, if possible, to every clause and word of a statute."[14] The rule that "a statute ought, upon the whole, to be construed so that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant,"[15] is a "cardinal principle of statutory construction."[16] The Proposed Regulations treat "processing" and "refining" as the same activity, notwithstanding the separation of such words in section 7704 by a comma, rendering one of those terms superfluous, void, or insignificant.

Under another well-settled principle in construing the Code, similar words and phrases used by Congress in different provisions of the Code have the same meaning in each provision.[17] As the Supreme Court has frequently stated, "the Code must be given 'as great an internal symmetry and consistency as its words permit."[18]

When Congress enacted section 7704 in 1987, and each time it subsequently amended section 7704, it did so against the backdrop of the definitions in section 613, the regulations thereunder, and court case precedent.[19] Given such backdrop, and the specific construction of section 7704 (i.e., separation of activities via comma), it's clear that Congress did not intend to restrict "processing" activities to those that are either mining processes or refining processes.

The Proposed Regulations' conflated definition of "processing or refining" violates judicial precedent regarding statutory construction.

B. ***The MACRS Consistency Requirement is Unsupported in Section 7704, Treas. Reg. § 1.613-4(f)-(g), and the Legislative History; It's Also Impractical.***

Prop. Reg. § 1.7704-4(c)(5)(i) reads:

> For an activity to be treated as processing or refining for purposes of this section, the partnership's position that an activity is processing or refining for purposes of this section must be consistent with the partnership's designation of an appropriate Modified Accelerated Cost Recovery System (MACRS) class life for assets used in the activity in accordance with Rev. [Proc.] 87-56, 1987-2 CB [674] [(the "***MACRS Consistency Requirement***")]…. For example, for an activity to be processing or refining of crude oil under paragraph (c)(5)(iii) of this section, the assets used in that process must also have a MACRS class life of 13.3, Petroleum Refining.

There is no basis in section 7704 or its legislative history for the use of MACRS asset classifications (the "***Classifications***") as part of the test for determining whether an activity is processing or refining. The Classifications were not intended, and most classifications are not even helpful, to distinguish between qualifying activities and non-qualifying activities under section 7704. Furthermore, the Classifications neither align with the

[14] *Duncan v. Walker*, 533 U.S. 167, 174 (2001) (quoting *United States v. Menasche*, 348 U.S. 528, 538-39 (1955) (quoting *Montclair v. Ramsell*, 107 U.S. 147, 152 (1883))).
[15] *Market Co v. Hoffman*, 101 U.S. 112, 115 (1879).
[16] *Williams v. Taylor*, 529 U.S. 362, 404 (2000).
[17] *See, e.g., Commissioner v. Keystone Consol. Indus.*, 508 U.S. 152, 159 (1993) (quoting *Atlantic Cleaners & Dryers, Inc. v. United States*, 286 U.S. 427, 433 (1932)); *Seaman v. Commissioner*, 29 T.C.M. 1331, 1333 (1970).
[18] *Commissioner v. Lester*, 366 U.S. 299, 304 (1961) (quoting *United States v. Olympic Radio & Television, 1955*, 349 U.S. 232, 236 (1955)).
[19] *See* T.D. 6446, 1960-1 C.B. 208.

definitions of qualifying activities in section 7704 and Treas. Reg. § 1.613-4(f)-(g), nor cover all types of business activities.[20] The MACRS Consistency Requirement can be read to further restrict qualifying processing and refining activities to those that fall into Classifications that use the words "processing" or "refining."[21] Such further limitation could conflict with other definitions of "processing or refining" in the Proposed Regulations (not to mention the conflict with the plain language of section 7704 and Treas. Reg. § 1.613-4(f)-(g) discussed previously).

The MACRS Consistency Requirement is unsupported in the language and legislative history of section 7704, and impractical in application.

C. The Transformation Exclusions Are Unsupported in Section 7704 and Treas. Reg. § 1.613-4(g).

Prop. Reg. § 1.7704-4(c)(5)(i) states that, except as specifically provided otherwise, an activity would not qualify as processing or refining if the activity "causes a substantial physical or chemical change in a mineral or natural resource, or transforms the extracted mineral or natural resource into new or different mineral products or into manufactured products."

The Preamble suggests that the Transformation Exclusions are consistent with Treas. Reg. § 1.613-4(g)(5) which defines "transformation processes". Treas. Reg. § 1.613-4(g)(5) defines "transformation processes" to identify the non-mining processes that cannot be used in the determination of percentage depletion deduction. Just because an activity cannot be used to determine the percentage depletion deduction does not mean that such activity is not "processing" or "refining" under section 7704. And, as importantly, the fact that Treas. Reg. § 1.613-4(g)(5) defines "transformation processes" as separate from "mining processes" for purposes of calculating percentage depletion actually supports the view that there are activities beyond those defined in Prop. Reg. § 1.7704-4(c)(5)(i) that qualify as "processing" and "refining" under section 7704.

As previously discussed, Treas. Reg. § 1.613-4(g)(1) identifies non-mining processes as: "electrolytic deposition, roasting, calcining, thermal or electric smelting, refining, polishing, fine pulverization, blending with other materials, treatment effecting a chemical change, thermal action, and molding or shaping." The Transformation Exclusions are in direct contradiction with Treas. Reg. § 1.613-4(g)(1) which specifically allows for chemical (e.g., "treatment effecting a chemical change") and physical (e.g., "pulverization", "molding or shaping") changes.

Further, the Transformation Exclusions are irreconcilably at odds with established understandings of the terms "processing" and "refining." The Oxford Dictionary defines "to process" as "to perform a series of mechanical or chemical operations on (something) in order to change or preserve it." "To refine" is defined as "to remove impurities or unwanted elements from (a substance), typically as part of an industrial process." Both "processing" and "refining" contemplate, by their very definitions, physical and/or chemical changes to the input material.

There is no support in section 7704, Treas. Reg. § 1.613-4(g), nor the common understanding of the terms "processing" and "refining" for the Transformation Exclusions.

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[20] For example, Vulcan's AM and RMC assets are classified under 32.3 Manufacture of Other Stone and Clay Products. Some Classifications combine refining activities and manufacturing. *See, e.g.*, Rev. Proc. 87-56, 1987-2 C.B. 674, classes 33.2 and 33.4 (refining of iron and nonferrous metals).

[21] The requirement that a classification be "consistent with" an asset class must mean, at a minimum, that the asset class includes the word "processing" or "refining." Otherwise, taxpayers like Vulcan would have no way of knowing whether their position was "consistent with" the MACRS asset class.

IV. Recommendations

We believe that the following revisions to the Proposed Regulations would align the definition of "processing" with the plain meaning of section 7704 and with Supreme Court affirmed rules of statutory construction:

1. Prop. Reg. § 1.7704-4(c)(5) should be revised to provide separate definitions for "processing" and "refining." The definition of "processing" should not refer to the mining processes in Treas. Reg. § 1.613-4(f)(1)(ii), as these processes have been a part of the definition of "mining" since 1943.[22] Rather, at a minimum, the final regulations should include the non-mining processes listed in Treas. Reg. § 1.613-4(g)(1).

2. The definition of mining in Prop. Reg. § 1.7704-4(c)(4) should be amended to include the mining processes described in Treas. Reg. § 1.613-4(f)(1).

3. Prop. Reg. § 1.7704-4(c)(5)(i) should be revised to strike the MACRS Consistency Requirement.

4. Prop. Reg. § 1.7704-4(c)(5)(i) should be revised to strike the Additional Exclusions.

V. Policy Considerations

In addition to the clear legal reasons for revising the Proposed Regulations, we believe there are compelling policy reasons for doing so. It is well known, generally, that our nation's transportation infrastructure (shape, size/capacity and condition) is not keeping pace with population growth and use. Specifically, according to the U.S. Department of Transportation[23]:

- The U.S. population is expected to grow by 30 million between 2015 and 2045 (more than the current populations of NY, TX and FL combined)
- We each spend an average of 40 hours each year sitting in traffic
- The annual cost of traffic congestion is $120 billion
- The U.S. 'energy boom' is placing unprecedented demand on our transportation system; by 2040, the volume of freight moved will grow 45%
- 65% of U.S. roads are in less than good condition
- 25% of U.S. bridges need significant repair or can't handle today's traffic
- Overall infrastructure grade is D+; quality of roads is 16th worldwide
- Improving the condition and performance of highways and bridges will cost approximately $120 billion annually between 2015 and 2020…current spending at all levels of government is approximately $83 billion

Private capital is likely to be a meaningful part of the funding solution for the necessary investments in our transportation system. The Proposed Regulations will make it harder to attract private investment capital to a critical area for our economy, and should be revised as recommended above.

[22] *See* Revenue Act of 1943, §124, *supra* note 3.
[23] U.S. Department of Transportation "Beyond Traffic 2045".

EXHIBIT 1

AM Cross Section View

RMC Cross Section View