NATIONAL ASSOCIATION OF Manufacturers

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Vice President,
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The Honorable Jason Smith
Chairman
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Richard Neal
Ranking Member
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Ron Wyden
Chairman
Committee on Finance
U.S. Senate
Washington, D.C. 20510

The Honorable Mike Crapo
Ranking Member
Committee on Finance
U.S. Senate
Washington, D.C. 20510

Dear Chairman Smith, Ranking Member Neal, Chairman Wyden and Ranking Member Crapo:

On behalf of the National Association of Manufacturers and the 13 million people who make things in America, I write to you today as you begin your work to prevent the devastating tax increases that will take effect for manufacturers and manufacturing families at the end of next year.

The 2017 Tax Cuts and Jobs Act was revolutionary for the manufacturing sector. Tax reform kickstarted years of economic growth throughout the industry, providing a new foundation for the manufacturing economy to thrive:

- In 2018, manufacturers added 263,000 new jobs, the best year for job creation in manufacturing in 21 years.[1]
- In 2018, manufacturing wages increased 3% and continued going up—by 2.8% in 2019 and by 3% in 2020. Those were the fastest rates of annual growth since 2003.[2]
- Manufacturing capital spending grew 4.5% and 5.7% in 2018 and 2019, respectively.[3]
- Overall, manufacturing production grew 2.7% in 2018, with December 2018 being the best month for manufacturing output since May 2008.[4]

Manufacturers have used the savings from tax reform to grow their businesses, create jobs, raise wages, add new benefits for employees, fund research and development, purchase new equipment, expand their facilities and give back to their communities.

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[1] Bureau of Labor Statistics, Current Employment Statistics, Manufacturing Employment, Seasonally Adjusted. *Available at* https://www.bls.gov/ces/data/.
[2] Bureau of Labor Statistics, Current Employment Statistics, Average Hourly Earnings for Production and Nonsupervisory Employees, Manufacturing, Seasonally Adjusted. *Available at* https://www.bls.gov/ces/data/.
[3] U.S. Census Bureau, Annual Survey of Capital Expenditures, Table 2A, Manufacturing. *Available at* https://www.census.gov/data/tables/2019/econ/aces/2019-aces-summary.html.
[4] Federal Reserve Board of Governors, Industrial Production, Manufacturing, Seasonally Adjusted. *Available at:* https://www.federalreserve.gov/releases/g17/Current/default.htm .

However, critical tax reform provisions are set to expire at the end of 2025, resulting in significant tax increases for virtually all manufacturers. Congress and the president *must act* to prevent tax hikes from stunting manufacturing job creation, growth and innovation.

Ensuring that the U.S. tax system supports manufacturers' ability to invest for growth will strengthen our country's supply chain, encourage domestic investment and enable manufacturers to compete on the world stage. As the tax-writing committees investigate how the 2017 reforms set the stage for manufacturers' success, we encourage you to take proactive steps to prevent the drastic consequences for the manufacturing economy that will ensue if these reforms expire. The following policies are of critical importance to protecting manufacturers from harmful tax increases.

Pass-Through Deduction

Small and medium manufacturers, which are often organized as pass-through entities, are the backbone of the American supply chain. Tax reform created a 20% deduction to allow these businesses to compete on a level playing field with their peers organized as corporations. This deduction allows pass-through manufacturers to deduct up to 20% of their business income on their personal returns. The lower tax burden provides manufacturers with additional capital to hire workers, increase wages and expand operations. Pass-throughs pay tax at individual income tax rates, and because the vast majority of domestic manufacturers are small and organized as pass-through entities, allowing the deduction to expire would overwhelmingly hurt the men and women who make things in America.

A recent NAM survey found that 93% of pass-through manufacturers reported that the loss of this deduction will harm their ability to grow, create jobs and invest in their business. Congress should make the pass-through deduction permanent to prevent damaging tax increases on small businesses and to ensure that small business owners have certainty that they will not have to contend with unpredictable changes to the tax code year after year.

Corporate Tax Rate

Congress must ensure that America is one of the most desirable places in the world for companies to conduct business. Prior to tax reform, the U.S. had one of the highest corporate tax rates in the entire world—and the single highest rate among our peers in the OECD. Tax reform reduced the corporate rate from 35% to 21%, stimulating economic activity here at home and bolstering America's competitiveness on the world stage. Since then, manufacturers have made significant domestic investments, working to secure our manufacturing base here at home.

The 21% corporate rate is not scheduled to expire; however, President Biden's FY 2025 budget proposed a 28% corporate rate—which would once again subject manufacturers in the U.S. to one of the highest rates of tax in the developed world. A lower corporate rate directly translates to well-paying jobs and more job opportunities for workers across the economy. The U.S. simply cannot afford to return to a corporate tax system that punishes manufacturers for investing and creating jobs here in America.

Individual Tax Rates

Tax reform significantly reduced income taxes for every American making more than $10,000 per year. Cutting taxes for American families bolstered spending power and financial security for manufacturers across the country. These reforms also eased the tax burden on pass-through manufacturers, who generally pay tax at the top individual tax rate. The combination of the reduction in the top rate and the 20% pass-through deduction resulted in significant tax savings for these small businesses—enabling them to invest in new equipment, machinery, facilities and job creation.

Individual tax rates are scheduled to increase to pre-2017 levels at the end of 2025, meaning that almost every American will face a higher tax bill the following year. Manufacturers organized as pass-throughs will be especially impacted by the combined effect of the expiration of the 20% pass-through deduction and rising individual tax rates. Congress must prevent these damaging tax hikes on manufacturers and manufacturing families.

Research and Development

For nearly 70 years, the U.S. tax code recognized the vital importance of R&D for businesses trying to compete and innovate. Until recently, manufacturers in the U.S. were able to fully deduct their R&D expenses in the year incurred. However, immediate R&D expensing expired in 2022, and manufacturers are now required to amortize their R&D expenses over several years. This harmful change increases the cost of conducting R&D in the U.S. at a time when our global competitors are offering robust R&D incentives—like China's 200% super deduction. Now, the U.S. tax code puts American manufacturers who invest in R&D at a severe disadvantage, drastically reducing the tax savings associated with R&D expensing and thus reducing the additional capital manufacturers have available to invest for the future:

	R&D Spending	Year 1 Tax Deduction	Corporate Rate	Year 1 Tax Savings
Immediate R&D Expensing (U.S., pre-2022)	$1,000	$1,000	21%	***$210***
R&D Amortization (U.S., 2022-present)	$1,000	$100	21%	***$21***
200% Super Deduction (China)	$1,000	$2,000	25%	***$500***

The private sector accounts for more than 75% of total R&D spending in the U.S.,[5] with small businesses spending more than $90 billion on R&D each year.[6] Manufacturers perform more than half of all private-sector R&D—across the industry, manufacturers spend more than $350 billion annually on groundbreaking research, including payroll expenses relating to R&D. Meanwhile, countries around the world are implementing more favorable R&D policies than in

[5] National Center for Science and Engineering Statistics, National Science Foundation, National Patterns of R&D Resources: 2020-21 Data Update, NSF 23-321 (Jan. 4, 2023), *Available at* https://ncses.nsf.gov/pubs/nsf23321.
[6] National Center for Science and Engineering Statistics, National Science Foundation, InfoBrief, NSF 22-343 (Oct. 4, 2022), *Available at* https://ncses.nsf.gov/pubs/nsf22343 and InfoBrief, NSF 23-305 (Dec. 14, 2022), *Available at* https://ncses.nsf.gov/pubs/nsf23305.

the U.S. Congress must act to restore immediate R&D expensing and preserve America's leadership in R&D and innovation—and the economic growth that comes with it.

Full Expensing

Companies' ability deduct all or a portion of capital equipment purchases has been a staple of the U.S. tax code for decades. Tax reform allowed manufacturers to immediately expense 100% of the cost of capital equipment purchases in the year incurred, spurring unprecedented growth in the manufacturing sector and positioned the U.S. to attract capital in a competitive global market. However, full expensing began phasing out in 2023 and will completely expire in 2027. This phase-down comes at a time when many of the United States' global competitors, including China, have instituted permanent full expensing polices to attract foreign investment.

Capital-intensive industries like manufacturing are the primary beneficiaries of full expensing; according to the non-partisan Joint Committee on Taxation, the manufacturing sector, and specifically small manufacturers, overwhelmingly utilize accelerated depreciation more than any other sector.[7] If Congress does not act, accelerated depreciation will be entirely absent from the U.S. tax code for the first time in decades—limiting manufacturers' tax savings from capital equipment expensing and thus harming the sector's ability to invest in job-creating and job-sustaining equipment and machinery:

	Capital Equipment Purchases	**Year 1 Tax Deduction**	**Corporate Rate**	**Year 1 Tax Savings**
Full Expensing (U.S., 2018-2022)	$1,000	$1,000	21%	***$210***
20% Immediate Expensing (U.S., 2026)	$1,000	$200	21%	***$42***

Interest Deductibility

Many manufacturers borrow funds to finance long-term investments in equipment and facilities, which in turn help create jobs and enable manufacturers to compete effectively in today's global economy. Tax reform allowed manufacturers to deduct interest on business loans, up to a cap: 30% of a business's earnings before interest, tax, depreciation and amortization (EBITDA). But this pro-growth EBITDA standard expired in 2022, and the cap is now 30% of a business's earnings before interest and tax (EBIT).

By excluding depreciation and amortization expenses from the interest deduction calculation, the EBIT standard makes debt financing more expensive—punishing manufacturers with significant investments in depreciable assets like equipment and machinery as well as valuable intellectual property subject to amortization. Increasing the cost of debt financing makes it more costly for manufacturers to invest in growth and expansion.

[7] Joint Committee on Taxation, "Tax Incentives for Domestic Manufacturing," JCX-15-21 (March 2021), *Available at* https://www.jct.gov/publications/2021/jcx-15-21/.

An NAM study found that limiting manufacturers' ability to deduct interest on debt-financed investments will cost the U.S. economy more than 860,000 jobs.[8] Congress should support manufacturers' efforts to get job-creating projects off the ground by returning the U.S. to an EBITDA standard for interest deductibility.

Estate Tax

Manufacturers believe that the U.S. tax code should protect and promote the hard work that goes into the 90% of American businesses that are family-owned. However, the estate tax unfairly taxes families during the most difficult time in their lives. The estate tax harms family-owned manufacturers by forcing the next generation to pay tax on a business and its assets when a loved one passes away. Tax reform increased the value of assets that can be passed on without incurring the estate tax. This increase in the estate tax exemption threshold made a crucial difference for family-owned manufacturers, given that manufacturing businesses consist largely of assets like equipment and machinery that would have to be sold to pay the tax.

The estate tax exemption threshold is scheduled to be reduced by half at the end of 2025, subjecting more family business assets to taxation and threatening the viability of these businesses when the owner passes away. Congress should protect family-owned manufacturers by preserving the increased exemption threshold or by eliminating the estate tax altogether, providing confidence to small manufacturers that they will be able to continue to operate in the event of losing a loved one.

Further, Congress should fully preserve stepped-up basis, which prevents a business owner's heirs from being forced to pay a capital gains tax on the asset appreciation that occurred during the owner's lifetime. Ending stepped-up basis would cost the U.S. economy 80,000 jobs per year over the course of a decade and 100,000 jobs per year thereafter.[9] Congress should preserve both the increased estate tax exemption threshold and stepped-up basis so family-owned manufacturers do not face costly and damaging tax bills that threaten their ability to keep the business in their family.

International Tax

Tax reform implemented a competitive, pro-growth hybrid territorial system, anchored by the newly lowered corporate income tax rate, that supports manufacturers' efforts to invest and create jobs here at home. These reforms changed the way foreign-sourced income earned by U.S. companies and their foreign subsidiaries are taxed, creating a far more competitive and desirable market in the U.S. Tax increases on globally engaged manufacturers are scheduled to take effect at the end of 2025 that will make the U.S. a less competitive place to invest.

Tax reform's international provisions were designed to make it easier and more cost-effective for manufacturers to locate their headquarters, assets and intellectual property here in the United States. The scheduled changes to these provisions will undermine the U.S.'s leadership on the world stage and make America a less attractive, more expensive home for manufacturing investment. Congress must preserve an international system that bolsters, rather than undermines, America's global competitiveness.

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[8] "Economic impact of a stricter 163(j) interest expense limitation," EY (September 2022). *Available at* https://documents.nam.org/COMM/EY_NAM_Economic_Analysis_163j_Limitation_FINAL_10_06_2023.pdf
[9] "Repealing step-up of basis on inherited assets: Macroeconomic impacts and effects on illustrative family businesses," EY (April 2021), *Available at* https://documents.nam.org/tax/ey-fbetc-stepupreport.pdf.

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Manufacturing employs 13 million Americans, contributes $2.81 trillion to the U.S. economy annually, pays workers 18% more than the average for all businesses and has one of the largest multipliers in the economy. Taken alone, manufacturing in the United States would be the eighth-largest economy in the world. But that economic leadership, and therefore the economic security of American families, is in jeopardy if Congress fails to preserve tax reform in its entirety before the end of next year.

Manufacturers appreciate the thoughtful consideration that the committees are giving to how the tax code impacts our sector. Failing to act in 2025 will cost millions of jobs and put the American manufacturing sector at a severe disadvantage globally. Congress should pursue tax policies that strengthen manufacturing in the U.S., ensuring that America remains a globally competitive home for manufacturing investment.

Sincerely,

Charles Crain
Vice President, Domestic Policy
National Association of Manufacturers