NATIONAL ASSOCIATION OF Manufacturers

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

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

The Honorable Jason Smith
Chairman
Committee on Ways and Means
U.S. House of Representatives
Washington, DC 20515

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

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

Manufacturers' ability to create jobs in the United States, invest in communities and effectively compete against China and others in the global economy is threatened by recent harmful tax changes that make it more costly to perform research, buy machinery and finance important investments. These damaging changes come at time when 62% of manufacturing leaders already expect a recession in 2023, according to the most recent National Association of Manufacturers' Outlook Survey.

Manufacturing employs nearly 13 million Americans, contributes $2.81 trillion to the U.S. economy annually, pays workers over 18% more than the average for all businesses and has one of the largest sectoral 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.

As the largest manufacturing association in the United States, the NAM represents small and large manufacturers in every industrial sector and in all 50 states, and for all manufacturers in the U.S., it is critical that Congress act without delay to reverse these harmful tax changes to help ensure a strong and competitive manufacturing economy here in the U.S.

1. Ensure the tax code continues to support innovation.

Manufacturers in the United States drive more innovation than any other sector, performing 55% of private-sector research and development in the U.S. In 2021 alone, manufacturers spent nearly $350 billion on R&D. Research is the lifeblood of manufacturing: new products, new materials and new processes help propel manufacturing in America forward. Unless Congress acts, manufacturers' ability to innovate and create new products, technologies and lifesaving medicines will be harmed.

Since 1954, the tax code has recognized the important role of R&D in creating jobs and spurring innovation by providing a critical incentive for investments in R&D. Specifically, the tax code has allowed businesses to immediately deduct 100% of their R&D expenses in the same year in which they are incurred. However, as of Jan. 1, 2022, businesses have been required to amortize, or deduct over a period of years, these expenses—making R&D more costly to conduct in the U.S.

Coming at a time of increasingly fierce global competition for research dollars, this policy—if not reversed—will hurt jobs, innovation and competitiveness. According to a recent economic analysis, the U.S. economy would lose 263,382 jobs and experience a GDP reduction of $82.39 billion in 2023, with the manufacturing industry projected to lose nearly 60,000 jobs, if the harmful R&D amortization policy is not reversed quickly.[1]

Unless Congress acts, the U.S. will continue to be just one of two developed countries with an amortization requirement for R&D expensing (the other being Belgium). Meanwhile, China, which has made no secret of its ambition to become the world leader in advanced manufacturing, currently provides a 200% deduction for R&D expenses for manufacturers.

For these reasons, the NAM strongly encourages Congress to act without delay to pass legislation reversing the R&D amortization provision so that manufacturers in the U.S. can continue leading the world in innovation, growing the economy and creating well-paying jobs.

2. <u>Enable manufacturers to continue to finance growth</u>.

Debt financing plays an important role in supporting manufacturing growth. 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. At the beginning of 2022, a stricter limitation on the deductibility of the interest payments on business loans went into effect, increasing the cost of financing critical investments in machinery and equipment.

The maximum interest deduction under section 163(j) is now limited to 30% of a company's earnings before interest and tax ("EBIT")—a substantial change from the standard in place prior to 2022, which was based on earnings before interest, tax, depreciation and amortization. ("EBITDA"). By excluding depreciation and amortization, the EBIT-based limitation makes it more expensive for capital-intensive companies to finance critical purchases, grow their businesses and hire new workers. This stricter limitation effectively acts as a tax on investment, and it makes the U.S. a global outlier. Of the more than 30 OECD countries with an earnings-based interest limitation, the U.S. is the only one that employs an EBIT standard.

According to a recent study, failing to reverse this harmful change could cost the U.S. economy 467,000 jobs and reduce U.S. GDP by $43.8 billion.[2] The NAM encourages Congress to support job-creating manufacturing investments here in the U.S. by acting expeditiously to protect interest deductibility.

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[1] *New Data: Taxing R&D Will Cost U.S. More Than 260,000 Jobs Next Year If Congress Doesn't Act*. National Association of Manufacturers (Dec. 16, 2022). *Available at* https://www.nam.org/new-data-taxing-rd-will-cost-u-s-more-than-260000-jobs-next-year-if-congress-doesnt-act-19948/.

[2] *Economic Impact of Not Addressing the More Stringent 163(j) Interest Expense Limitation*. EY (September 2022). *Available at* https://documents.nam.org/tax/nam_interest_deductibility_study.pdf.

3. <u>Make permanent a key incentive for capital equipment purchases</u>.

For the past several decades, the tax code has provided businesses with varying degrees of first-year expensing (i.e., bonus deprecation). A 100% deduction for the purchase of equipment and machinery in the tax year purchased has been in place since 2017. This critical incentive for capital-intensive industries like manufacturing reduces the after-tax cost of capital equipment purchases and increases the return on investments. These projects in turn support job creation and retention. According to recent analysis by the nonpartisan Joint Committee on Taxation, manufacturers led all sectors in the use of expensing by a wide margin.[3] Unfortunately, the 100% level of full expensing began to phase out this year and will be eliminated completely by 2027. If this occurs, it will be much more expensive for manufacturers to undertake job-creating investments and effectively compete on a global scale. As such, the NAM encourages Congress to protect full expensing.

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Competitive tax policies are critical to supporting growth and long-term investment in manufacturing in the U.S. Those investments create jobs and opportunity and family-supporting careers. They help communities grow and strengthen the supply chains that determine whether the products Americans need reach their stores and their homes.

By reversing the harmful change to the tax treatment of R&D, returning to an EBITDA-based standard for interest deductibility and restoring full expensing, Congress can help ensure that manufacturers, especially small manufacturers, can continue to invest in their operations, their workers and America's future.

Sincerely,

Aric Newhouse
Senior Vice President, Policy and Government Relations
National Association of Manufacturers

cc: Members of the Senate Finance Committee
Members of the House Ways and Means Committee

[3] *Tax Incentives for Domestic Manufacturing*. Joint Committee on Taxation (March 12, 2021). *Available at* https://www.jct.gov/publications/2021/jcx-15-21/.