

STATEMENT OF THE R&D CREDIT COALITION
ON
RESEARCH AND DEVELOPMENT INCENTIVES IN THE U.S. AND ABROAD
SUBMITTED FOR THE RECORD OF THE HEARING
ON
“TAX REFORM OPTIONS: INCENTIVES FOR INNOVATION”
BEFORE
UNITED STATES SENATE COMMITTEE ON FINANCE
ON
SEPTEMBER 20, 2011

Introduction

The R&D Credit Coalition welcomes the opportunity to provide comments for the record of the September 20, 2011, Senate Committee on Finance (“Committee”) hearing to examine tax reform options: incentives for innovation.

The R&D Credit Coalition would like to thank Chairman Baucus and Ranking Member Hatch for their leadership in sponsoring legislation that would provide for a strengthened and permanent R&D tax credit. We look forward to working with them this year to advance their proposal to ensure that U.S. businesses have the certainty and incentives they need to maintain and increase their R&D jobs here in the U.S.

The R&D Credit Coalition is a group of more than 100 trade and professional associations along with hundreds of small, medium and large companies that collectively represent millions of American workers engaged in U.S.-based research throughout major sectors of the U.S.

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economy, including aerospace, agriculture, biotechnology, chemicals, electronics, energy, information technology, manufacturing, medical technology, pharmaceuticals, software and telecommunications.

Although the make-up of the R&D Credit Coalition is diverse, the member companies share a major characteristic— they collectively spend billions of dollars annually on research and development (“R&D”), which provides for high-wage and highly-skilled, domestic jobs. Companies must decide where they are going to invest their research dollars— here in the U.S. or abroad. The high U.S. corporate tax rate and the temporary nature of the U.S. R&D tax credit, compared to the lower corporate tax rates and more attractive, often permanent, research incentives in most industrialized countries, are key factors that companies consider in determining where they are going to create R&D jobs. Today, a company claiming the U.S. R&D credit on average only realizes an effective credit rate of six percent. In addition, the U.S. requires that any deduction for R&D expenses may not also be claimed for the R&D credit.

Thus, corporate tax reform proposals limiting or eliminating research and development tax incentives could have a dramatic impact on both the number and location of R&D jobs in the U.S., as well as the ability of our companies to compete effectively in the global marketplace. Given the Committee’s focus on how the tax code can encourage job creation in the United States, the R&D Credit Coalition would like to share our preliminary views regarding tax reform options and incentives for innovation. It is important for Congress to recognize that even in the context of tax reform, maintaining a permanent, strengthened R&D tax credit is critically important to ensure that U.S. companies keep jobs here in America.

Discussion

The R&D tax credit was originally enacted in 1981 and has provided an important incentive to spur private sector investment in innovative research by companies of all sizes and in a variety of industries. The enactment of this incentive helped establish the U.S. as a leader in cutting-edge research. In fact, during the 1980s, the U.S. was the leader among OECD countries in providing the best R&D incentives for companies. However, many of our foreign competitors have since instituted more generous R&D incentives in the decades following, causing the U.S. to drop below the top 10, and today ranks 24th in research incentives among industrialized countries. The temporary nature of U.S. R&D incentives is a strain on U.S. companies, causing uncertainty that negatively influences future company R&D budgets. Providing the certainty of a permanent credit, especially in a tax reform environment, is critical to maintaining U.S. leadership in global advanced research and ensuring that U.S. companies will continue to do their R&D here in the U.S.

Many other countries offer *both* lower tax rates and more attractive R&D incentives, proving that the U.S. should not engage in an “either/or” debate with respect to lower marginal rates and boosting U.S. job creation through R&D incentives when looking at options to reform the corporate tax code.

The R&D credit is a *jobs* credit—with seventy percent of credit dollars used for salaries of high skilled R&D workers in the United States. A study by the Information Technology and

Innovation Foundation (ITIF), “estimates that expanding the Alternative Simplified Credit (ASC) from 14 percent to 20 percent would spur the creation of 162,000 jobs in the short term and an additional, but unspecified, number of jobs in the longer run.”¹ The U.S. must ensure that our tax system supports high-skilled, high-paying jobs, here in the U.S. We cannot let our tax system put these jobs at risk of moving abroad.

A newly-published study by Ernst & Young² finds that the R&D credit has a significant effect on R&D spending:

- The existing credit is estimated to have increased annual private research spending \$10 billion in the short-term and by \$22 billion in the long-term (beyond the first several years), substantially higher than the credit’s roughly \$6 billion to \$8 billion revenue cost.
- Strengthening the credit by increasing the simplified credit from 14% to 20% is estimated to increase annual private research spending by an additional \$5 billion in the short-term and an additional \$11 billion in the long-term.
- In total, the overall policy – the existing credit plus strengthening the alternative simplified credit – is estimated to increase annual private research spending by \$15 billion in the short-term and \$33 billion in the long-term.

The study also finds that the R&D credit has significant effects on U.S. wages and employment.

Higher wages:

- In the short-term, wages are estimated to rise by \$10 billion from the overall policy, with an additional \$7 billion due to the existing credit and \$3 billion due to strengthening.
- In the long-term, wages are estimated to rise by \$23 billion from the overall policy, with an additional \$15 billion due to the existing credit and \$8 billion due to its strengthening.

Higher employment:

- Research-orientated employment in the U.S. would be 130,000 higher in the short-term and 300,000 higher in the long-term because of the combination of the existing credit and the strengthening of the alternative simplified credit.

These and other study results demonstrate the effectiveness of the R&D credit in terms of encouraging additional research spending, employment and higher wages. A permanent enhanced R&D credit will help to ensure that our tax system supports high-skilled, high-paying jobs, here in the U.S. We cannot let our tax system put these jobs at risk of moving abroad.

International R&D Tax Incentives

The number of OECD countries offering some sort of incentive for research has grown dramatically in recent years as countries attempt to become leaders in research. The U.S. share of

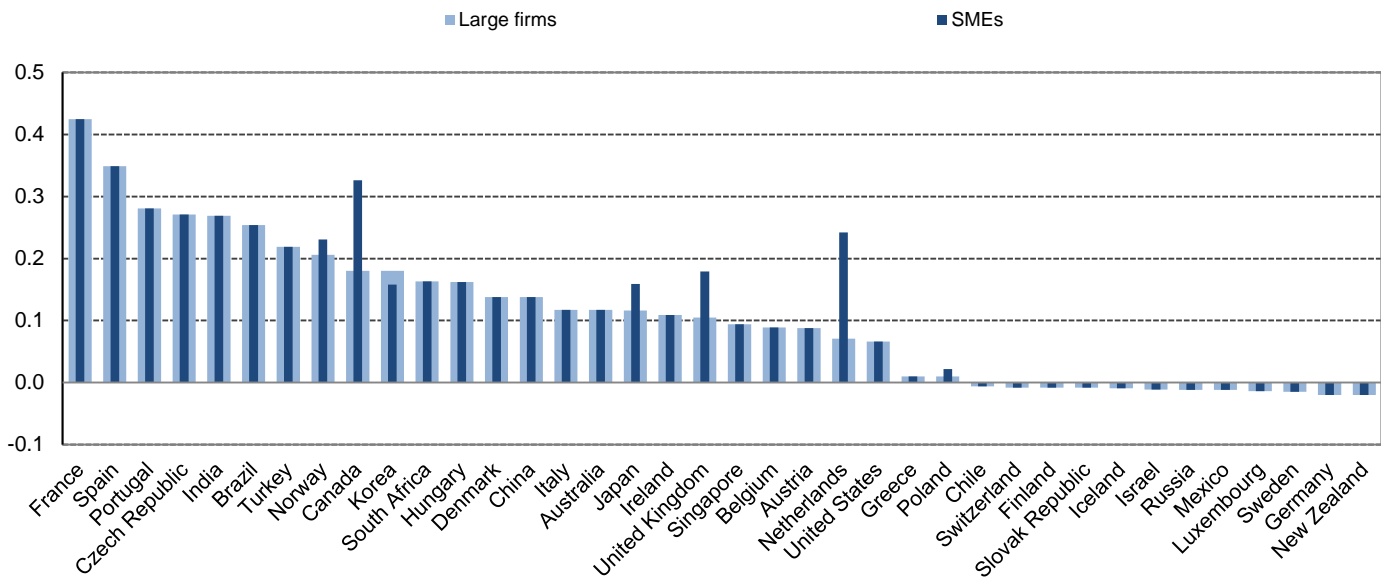
¹ Information and Technology Innovation Foundation, “*Create Jobs by Expanding the R&D Tax Credit*,” by Robert D. Atkinson. January 26, 2010 (page 1)

² Ernst & Young, LLP, “*The R&D Credit: An effective policy for promoting research spending*,” by Drs. Robert Carroll, Gerald Prante and Robin Quek, September 16, 2011.

global R&D fell from 39 percent in 1999 to 33 percent in 2007.³ In addition, the following OECD chart shows that in 2009, the United States ranked 24 among 38 industrialized countries offering R&D tax incentives.⁴

[OECD Science, Technology and Industry Scoreboard 2009 - OECD © 2009 - ISBN 9789264063716](#)

Tax subsidy rate for USD 1 of R&D, large firms and SMEs, 2008



Bipartisan Support for a Strengthened, Permanent Research & Development Incentive

Every Administration has supported the R&D tax credit since its enactment. More recently, a March 25, 2011, Treasury Department study stated, “Two years ago, the President set an ambitious goal of achieving a level of research and development that is the highest share of the economy since the space race of the 1960’s – 3 percent of GDP – a commitment he re-emphasized in his State of the Union address in 2011. The R&D tax credit is a vital component of achieving this goal and helping us out-innovate our competition. This is why, in addition to making it permanent, the President proposed on September 8, 2010, to expand and simplify the credit, making it easier and more attractive for businesses to claim this credit for their research

³ OECD, Ministerial Report on the OECD Innovation Strategy, May 2010, p. 8.

⁴ OECD, “Science, Technology and Industry Scorecard,” December 2009, p 79.

investments. This proposal was subsequently included in the President's FY 2012 Budget and should be part of the reform of our corporate tax system currently under consideration."⁵

Moreover, Congress has extended the credit 14 times since it was first adopted in 1981. Finance Committee Chairman Baucus and Ranking Member Hatch and a bipartisan group of senators have introduced S. 1577, the Greater Research Opportunities with Tax Help Act of 2011, to simplify and make permanent the R&D tax credit. In addition, earlier this year, Ways and Means Committee members Kevin Brady (R-TX), John Larson (D-CT) and many others introduced H.R. 942, The American Research and Competitiveness Act of 2011. This legislation would provide important certainty for U.S.-based research spending by making the R&D tax credit permanent as well as simplifying and strengthening it, thereby increasing its effectiveness. We urge Congress to pass this legislation before the credit expires on December 31, 2011.

Conclusion

It is vitally important that U.S. policy makers support a strengthened and permanent research and development incentive as part of any tax reform measure. A robust and permanent research and development tax credit is critical to competitiveness, innovation and U.S. jobs. Congress must recognize, that in the global economy, many companies have a choice as to where they are going to do their research—and with many other countries offering *both* lower corporate income tax rates and more robust R&D incentives, the U.S. must ensure that R&D incentives are included as part of any tax reform package. The R&D Credit Coalition looks forward to assisting members of the Committee and their staffs to gain a more detailed understanding of the research and development tax credit and its impact on U.S. jobs.

⁵ *“Investing in U.S. Competitiveness: The benefits of Enhancing the Research and Experimentation (R&E) Tax Credit,”* U.S. Department of the Treasury, March 25, 2011, page 1.